EXECUTIVE BUSINESS MEETING TO REVIEW AND MAKE RECOMMENDATIONS ON PROPOSED LEGISLATION IMPLEMENTING THE U.S.-PERU TRADE PROMOTION AGREEMENT, AS WELL AS THE ASSOCIATED PROPOSED STATEMENT OF ADMINISTRATIVE ACTION; AND TO CONSIDER THE AMERICAN INFRASTRUCTURE INVESTMENT AND IMPROVEMENT ACT; AND THE HABITAT AND LAND CONSERVATION ACT OF 2007

FRIDAY, SEPTEMBER 21, 2007

U.S. Senate,

Committee on Finance,

Washington, DC.

The hearing was convened, pursuant to recess, at 8:00 a.m., in room 215, Dirksen Senate Office Building, Hon. Max Baucus (chairman of the committee) presiding.

Present: Senators Rockefeller, Conrad, Bingaman, Kerry, Lincoln, Schumer, Stabenow, Cantwell, Salazar, Grassley, Hatch, Snowe, Kyl, Crapo, Roberts, and Ensign.

Also present: Russ Sullivan, Democratic Staff Director; Bill Dauster, Deputy Staff Director and Chief Counsel; Kolan Davis, Republican Staff Director and Chief Counsel; Dean Zerbe, Tax Counsel and Senior Counsel to the Ranking Member; Carla Martin, Chief Clerk; Mark Blair, Deputy Clerk; and Jewel Harper, Hearing Clerk.

Also present: Edward D. Kleinbard, Chief of Staff, Joint Committee on Taxation; Thomas Barthold, Deputy

Chief of Staff, Joint Committee on Taxation; Everett Eissenstat, Assistant U.S. Trade Representative for the Americas; Michael Desmond, Tax Legislative Counsel, Department of the Treasury; Amber Cottle, International Trade Counsel; David Johanson, International Trade Counsel; Elizabeth Paris, Tax Counsel; Warren Maruyamma, General Counsel; Pat Bousliman, Natural Resource Advisor; Jo-Ellen Darcy, Senior Environment Advisor.

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OPENING STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA, CHAIRMAN, COMMITTEE ON FINANCE

The Chairman. The committee will come to order.

We are here to resume our mark-up of the Peru, Transportation, and Habitat legislation, and we are here at this hour because a Senator--which is certainly within his rights--has exercised that right under the Standing Rules of the Senate to object to this committee meeting while the Senate is in session. Under the rules of the Senate, again, any Senator has that right, and I fully respect it.

But to avoid such as disruption today, we will move expeditiously to conclude our mark-up before 11:15 this morning, because the Senate comes in at 9:15, and after the expiration of two hours it is possible that the Senator might again exercise his or her right to object to this mark-up. So we will conclude, certainly, before 11:15.

In fact, I would like to conclude at least by 10:00, because there is a vote at 10:00. I have a hunch that some Senators might be disinclined to return back to the committee after that vote. So we are trying to finish, certainly, by 10:00.

I might remind the committee that we experienced a

similar instance of obstruction, or at least delay, exactly two months ago. At that time we were working on the Children's Health Insurance Program bill, and we responded by expediting the mark-up when we next met and we reported our bill, and we will do so again today.

So all Senators' full statements will be printed in the record, and I will shortly recognize Senator Grassley for any remarks that he may wish to make. Right after, we will do our walk-through and have questions on the mark.

If Senators insist in asking questions or making statements, they certainly may do so at that point, but I will limit all Senators to four minutes and I will strictly enforce that limit because we do have to conclude this mark-up on all three bills today before 10:00.

Senator Grassley?

OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA

Senator Grassley. Yes. I have got a lot that I would like to say, but I think if it is all right with you and every other member, if you would let us go immediately to the walk-through, I would appreciate it very much because I think statements can be put in the record.

Most of these bills that we have before us have been before us for a long time. I might say I am particularly glad that we were able to get Senator Crapo's bill out, because he has been working on that for such a long period of time as well. So, that is all I have to say for now.

[The prepared statement of Senator Grassley appears in the appendix.]

The Chairman. Any other statements?

[No response]

The Chairman. I see no Senators seeking recognition.

The next order of business before the committee is to walk through the Peru mark. Ms. Cottle, would you briefly describe its main features?

Ms. Cottle. Yes. Thank you, Chairman Baucus.

The committee is considering two documents today relating to the U.S.-Peru Trade Promotion Agreement. The first document is the Statement of Administrative Action, which provides the administration's views on the proper interpretation of the agreement.

The second document is the implementing bill, which makes the changes to U.S. law that are necessary to implement the agreement. The implementing bill is divided into six titles, which I will briefly summarize.

Title 1 provides for congressional approval of the agreement and the accompanying Statement of Administrative Action.

Title 2 authorizes the President to modify tariffs in accordance with the agreement, and establishes rules of origin that define which goods are eligible for preferential treatment under the agreement.

Title 3 creates safeguard mechanisms to remedy any import surges that may result from the tariff modifications.

Title 4 gives eligible Peruvian goods and services access to U.S. Government procurement bidding procedures.

Title 5 implements the new illegal logging annex added to the agreement as a result of the May 10 bipartisan trade deal. It also requires the administration to provide periodic reports to Congress on

the steps that Peru has taken to comply with the logging annex. These new illegal logging provisions are the only aspect of the May 10 deal that requires changes to U.S. law.

And finally, Title 6 provides offsets for the bill's projected revenue losses.

Mr. Chairman, that concludes my summary of the implementing bill.

The Chairman. Thank you.

Any questions? If not, we will go straight to amendments. Senator Salazar?

Senator Salazar. Thank you, Chairman Baucus. I want to just make a quick comment about the Peru Free Trade Agreement. It is the first free trade agreement that I have an opportunity to vote on in this committee. As Senator Conrad said yesterday, I had the privilege of traveling with him and with Senators Reid and Gregg to Bolivia, Ecuador and Peru in January.

I believe this is an important free trade agreement, and I believe that part of what Senator Reid was trying to do by taking that CODEL into South America was to try to put a spotlight on the importance of the western hemispheric north/south relationship.

It is something that I very much agree with because I think too often our focus has been across the ocean,

the transatlantic relationship, which is appropriate and important, but it is also important for us to understand the geopolitical realities that we live in in the western hemisphere.

So, I intend to be supportive of this free trade agreement for that reason. I think it is in keeping with the vision that President John Kennedy laid out in 1961 when he announced the Alliance for Progress, and I think we have a lot of work to do in terms of the north/south relationship. It is for that reason, among a whole host of other reasons, that I will be supporting this free trade agreement.

The Chairman. Thank you, Senator.

Mr. Johanson, do you have any comments with respect to the mark that you would like to make?

Mr. Johanson. No, Chairman Baucus, I do not.

The Chairman. All right. Thank you.

I will proceed to amendments. Do any Senators have amendments? Senator Bingaman?

Senator Bingaman. Yes, Mr. Chairman. Let me raise an amendment here. I intend to support the agreement and I congratulate you and others for the provisions that have been included with regard to labor rights. But I have an amendment that authorizes $30 million over five years for the State Department to assist the

International Labor Organization in expanding its Better Factories Program to Peru. This is a program under which the ILO would directly monitor Peru's export-oriented workplaces for compliance with Peru's labor laws.

The concern I have had is that we get agreement by these various countries to go ahead and apply and implement and enforce their own labor laws, but we do not have any way to really verify that that is happening. The ILO has this Better Factories program that they have had in place in Cambodia where they directly do some of that monitoring themselves and it has been very effective. I would very much like to see us use that same model for this Peru Free Trade Agreement, and later when we do Panama and Colombia, if those free trade agreements do come before the committee and are considered.

So that is my amendment, Mr. Chairman. I know that there is some concern about whether or not is in order, but I raise it at this point to get any reaction that you have to it.

The Chairman. Thank you, Senator. Frankly, I think it is not a bad amendment. I support the substance of it, and I certainly commend your work on CAFTA to ensure that the United States has the necessary funds for technical capacity building.

Under the Trade Act of 2002, provisions included in the implementing bill must be required by the agreement and necessary and appropriate to implement the language of the amendment. Unfortunately, at this point it does not appear to meet that test.

Senator Bingaman. Well, unfortunately I have to agree with you that it does not meet the test of being required in order to implement the agreement. I do think it is an appropriate amendment to implement the agreement.

I guess my thought is that -- well, two thoughts. One, is if we are not able to do it as an amendment here because of that restriction in the Trade Act of 2002 because it would not be in order, I would hope we could find another place to do that, to put this same provision in, to authorize this funding and to provide that the ILO will do this direct monitoring.

The other point that seems to me pretty straightforward, is we ought to revisit this Trade Act of 2002 because, in my view, the language is unduly restrictive. This is an entirely appropriate amendment, as I would see it, to this kind of an agreement. I think we made a big mistake by putting language in the Trade Act saying that it has to be a required provision in order to be in order. So, those are the two points that

I would make.

The Chairman. Well, I will certainly work with you. You make very good points. Very good points. There will be many opportunities later this year to improve fast track, is one opportunity, or other FTAs where we will have opportunities. But I really hear what you are saying. This is a longstanding interest of yours for which I have great respect, and many others do, too. You have put a lot of work into it, and I have a hunch we are going to find a way to deal with it.

Senator Bingaman. Well, I appreciate your assurances in that regard and I will not press the amendment at this time, since, as you point out, under the language of this Act it would not be in order.

But I do think, particularly the experience we have had with CAFTA, requires me or causes me to want to pursue this. I think in the case of CAFTA, we have several of these countries that have signed up to enforce their own labor laws, and the truth is, they do not have the capacity in their own governments to do that. We need someone to do independent monitoring of those laws, and that is what I would hope we could accomplish. But I appreciate your comments and I will not press the amendment.

The Chairman. Thank you, Senator. The amendment

is withdrawn.

Any other amendments? Senator Stabenow?

Senator Stabenow. Thank you, Mr. Chairman.

Concerning the Peru agreement, first of all I want to applaud the new provisions that are in this trade agreement. We have come a long way in reflecting our values for our country as it relates to labor and the environment.

I particularly want to thank my friend and colleague in the House, Congressman Sander Levin, for his work, and Charlie Rangel, and the Chairman of this committee, and Ranking Member, for moving this in the right direction. It has good intentions. I think it has the right words on paper.

For me, however, this is not enough to just have the right words on paper when we are not yet fulfilling our enforcement responsibilities or funding the training programs that were promised for displaced workers, and so on. I have 33,000 people in Michigan on a waiting list for training that are waiting for the new TAA to be developed. Mr. Chairman, I am very hopeful, and it is very positive, what you are developing there and I am pleased to be working with you.

But for me, this is a matter of principle. When I listened to former Secretary Kantor say we have the

smallest funded trade enforcement agency of any developed country and that it is an issue of credibility for our country in terms of businesses, workers, and communities, I think it is time to stop and get that right before we go ahead with any new trade agreement.

I feel strongly. I met with a group of small manufacturers this week, small businesses, hiring 40, 50, 60 people who are competing with Chinese companies, who, by the way, are part of the country. Our businesses are competing with countries, not just companies. But they see a 20 or 30 percent price differential solely as a result of currency manipulation. They are losing bids, laying off people, and we are losing jobs. It is a matter of jobs.

So, Mr. Chairman, I appreciate very much the work that has been done, but for me -- and I do have an amendment. I will not proceed with it. My preference would be to indicate that neither this agreement, or any agreement, takes place until we have in place a new and improved TAA system for our workers, businesses, and communities, until we have a tough currency bill actually passed, and that we have a trade enforcement bill in place, all of which I know are being worked on. But we do not have the credibility. Too many people are impacted by trade right now because we have not put those

things in place.

So, Mr. Chairman, I cannot support this agreement, or any trade agreement, until we get those things in place that affect our people.

The Chairman. I appreciate that, Senator. Just for clarification here, what is the number of your amendment?

Senator Stabenow. The number of the amendment is #2. It is called New Priorities amendment. I will not ask for a vote at this time, but it is my preference that we, in fact, put in place TAA, a currency bill, and a strong trade enforcement bill before we proceed with any other trade agreements.

The Chairman. Thank you very much. I, frankly, agree with all of the measures that you have mentioned, Senator, trade enforcement, TAA, and currency. It is just a question of which comes first. We cannot do it all at once. But I intend very much to move those three issues this year, the trade enforcement provision which you have sponsored which is very much needed in my view, and, second, trade adjustment assistance, which needs to be beefed up. It is very important for America.

And then the currency legislation that passed out of this committee. We are working now with the Banking Committee to find the right way to advance that

legislation. But it is my intention, my full intention, to move all three of those issues this year, and I thank you, Senator.

Senator Stabenow. Thank you.

The Chairman. Any more amendments?

Senator Hatch. Are you through?

The Chairman. Yes, I am through.

Senator Hatch. Well, thank you, Mr. Chairman. I do have a couple of amendments that I would like voted on, regardless of which way the vote goes. I hope that my colleagues will listen to me.

I would like to offer amendment #2. Now, this amendment deals with intellectual property laws. For years I have been a steadfast supporter of the intellectual property laws and the appropriate enforcement thereof. The Constitution itself provides for the creation of intellectual property and it has been the processed used by brilliant U.S. innovators to develop, market, and sell groundbreaking new products for years. In the sea of red trade deficits we have faced for so many years now, IP and the innovative U.S. products that use its protection have been one of the few areas where the United States has a real trade surplus.

Now, my amendment is simple. I applaud the USTR and her staff for their hard work in negotiating this

agreement, especially in the area of intellectual property rights. My amendment does nothing more than clarify that it is the intent of this committee that the Government of Peru adopt rigorous intellectual property rights protections similar to those that we have right here in the United States.

In fact, it is such a simple amendment that it might benefit my colleagues if I just simply read it: "Nothing in this Act or in the agreement prevents the Government of Peru from imposing strong and rigorous intellectual property rights protections across all sectors of the economy of Peru that are similar to the intellectual property rights protections available in the United States."

Now, I know that there are several Senators on this committee who represents States that contain numerous innovative companies that benefit from strong intellectual property laws and their enforcement. May 24, 2007, I, along with four other members of this committee, and one former member, Senator Thomas, who lamentably passed on, sent a letter outlining our concerns over the future direction of international trade. I would like to enter a copy of that letter into the record at this time, Mr. Chairman.

The Chairman. Without objection.

[The letter appears in the appendix.]

Senator Hatch. Now, millions of jobs in this country depend on these laws. I know firsthand that many countries around the world would like nothing more than to see the U.S. intellectual property laws and enforcement diminished. Why? Because they want to exploit us. They want to be able to steal our inventions. And they are stealing them. They want to be able to rip off our best and brightest ideas.

They want our taxpayers to fund billions of dollars of extremely important research and then take it from us for free. That is why we must ensure that the Peruvian government recognizes that it has the obligation under this agreement to adopt and maintain stringent intellectual property rights protections.

Now, I realize that no one on this committee wants to weaken our intellectual property rights. However, the one way that we can, I think, help to secure our rights, is by accepting my amendment, and I hope everybody will vote in favor of the amendment.

But let me just make this point. This first amendment involves intellectual property rights and sets a standard. It says, look, we are not going to be fools with regard to our trade and treaty agreements. I know this, that if this treaty is adopted in its current form

without a caveat like this, and on the second point, and I will get into that on the labor matters, I guarantee you, these provisions are going to be in every treaty from here on in.

I can tell you right now, we live up to our obligations but others do not. We are just undermining our businesses and our country if we start doing this across the board. And I do not see how you are going to avoid doing it. So I am very concerned about it and I hope my colleagues will support this. It is very simple, and I think a pretty much unobtrusive amendment. But I hope you can support.

The Chairman. Is there any discussion?

Senator Grassley. Mr. Chairman?

The Chairman. Senator Grassley.

Senator Grassley. I would ask my colleagues to vote against Senator Hatch's amendment, well intended that it is, because I have to have some sympathy for what he says, I have to have some sympathy for what Senator Stabenow said about her opposition to this amendment. But the perfect world is not very often present in Senate debate, and this is one of those instances.

We have this May 10th compromise between the administration and the new Democrat Majority of the Senate, trying to strike a balance with regard to

intellectual property rights that is different from the original balance that this committee considered last year.

The May 10th compromise may not strike the balance that I would like to see in intellectual property rights, but I think you have to consider the trade agreement in its entirety. I would say that same thing for comments that Senator Stabenow made.

On the whole, even with these revisions, our trade agreement with Peru is a very good trade agreement. Article 16 of the agreement states that "either party may implement stronger protections for intellectual property rights as long as they do not conflict with the agreement." That is very broad.

So I do not see how this amendment is necessary to implement our trade agreements, so I ask Senator Hatch to consider, overall, the good that this amendment is going to do, as I asked Senator Stabenow to look at the good it does. What she says needs to be done in trade needs to be, but in the process we have got to think of the good that this would do for business in Utah, the good that it would do for business, farmers, and services in Michigan.

We heard these same arguments on the Central American Free Trade Agreement. Prior to our adopting that agreement, we had a trade imbalance with those

Central American countries. Today, just two years later, we have a trade surplus with those nations. We have got a situation where Peruvian products have been coming into this country duty-free for decades.

Now we have got a chance to get our products, whether it is corn grown in Michigan, or services from Michigan, or manufactured products in Michigan, and get them into Peru. So you ought to try to help what you can along the way, everybody you can help. And this is going to help Americans because it is a non-level playing field for us today.

The Chairman. Any further discussion?

[No response]

The Chairman. I would also hope that Senators vote against this amendment. Essentially, the amendment is a restatement of provisions already in the agreement, therefore it is not required by the agreement. This amendment is not necessary and appropriate. Also, I would remind Senators that if we go down this road and start adding extraneous provisions in that are not necessary or appropriate and not required, the other body is going to do the same, probably in an offsetting way, and those authors of the amendment may end up with the situation being much worse than they contemplated in the first place.

So I would advise us not to adopt this amendment. It is not required by the agreement. It is not necessary. It is not appropriate. It is a restatement. It is extraneous. I understand the intent of the author of the amendment, but I just do not think, all things considered, it is wise.

Senator Hatch. Well, Mr. Chairman, let me just add one or two more thoughts. I realize where the votes are on this, but I have got to tell you, I am very concerned about. I have gone all around this world arguing for intellectual property rights protections for our intellectual property and for theirs, and we have seen this, year after year, being taken advantage of.

I do not think Peru is going to take advantage of us. I do not have any problem with that. I do not think any of the three are going to be big problems to us. I just see big problems on the horizon with this kind of language, and especially the labor language as well, in this treaty.

My amendment is simple. It does not nullify the treaty, does not really hurt the treaty, but it does set a standard and says, look, we are concerned about our own intellectual property rights. Now, I am prepared to vote. I understand where the votes are, but I think we should vote.

The Chairman. The Clerk will call the roll.
The Clerk. Mr. Rockefeller?
The Chairman. No by proxy.
The Clerk. Mr. Conrad?
Senator Conrad. No.
The Clerk. Mr. Bingaman?
Senator Bingaman. No.
The Clerk. Mr. Kerry?
Senator Kerry. No.
The Clerk. Mrs. Lincoln?
Senator Lincoln. No.
The Clerk. Mr. Wyden?
The Chairman. No by proxy.
The Clerk. Mr. Schumer?
The Chairman. No by proxy.
The Clerk. Ms. Stabenow?
Senator Stabenow. No.
The Clerk. Ms. Cantwell?
The Chairman. No by proxy.
The Clerk. Mr. Salazar?
Senator Salazar. No.
The Clerk. Mr. Grassley?
Senator Grassley. No.
The Clerk. Mr. Hatch?
Senator Hatch. Aye.

The Clerk. Mr. Lott?

Senator Grassley. I do not have a vote for him, so he will have to pass.

The Clerk. Ms. Snowe?

Senator Snowe. Aye.

The Clerk. Mr. Kyl?

Senator Grassley. Aye by proxy.

The Clerk. Mr. Smith?

Senator Grassley. Aye by proxy.

The Clerk. Mr. Bunning?

Senator Grassley. Aye by proxy.

The Clerk. Mr. Crapo?

Senator Crapo. No.

The Clerk. Mr. Roberts?

Senator Roberts. No.

The Clerk. Mr. Ensign?

Senator Ensign. No.

The Clerk. Mr. Chairman?

The Chairman. No. I assume Senator Rockefeller would like to vote in person.

Senator Rockefeller. Yes, I would, Mr. Chairman. Thank you. I vote "no".

The Chairman. The Clerk will announce the results of the vote.

The Clerk. Mr. Chairman, the tally is 6 ayes, 14

nays.

The Chairman. The nays have it. The amendment fails.

Any further amendments?

Senator Hatch. Mr. Chairman?

The Chairman. Senator Hatch?

Senator Hatch. Mr. Chairman, I call up Hatch amendment #1. This is the labor chapter of the U.S.-Peru Free Trade Agreement, which puts us at risk in both our Federal and our State labor laws. It is significant risk without an explicit safe harbor provision.

Now, several provisions of the labor chapter of the U.S.-Peru trade agreement create an unacceptable risk that the United States will be required to change important provisions of U.S. Federal and State labor laws or be subject to trade sanctions. Given that the purpose of the May 10 trade deal was to ensure that Peru adopted strong labor provisions, not the United States, Congress' implementation of this agreement should provide an explicit safe harbor for U.S. labor law.

Now, the Peru FTA requirement to adopt "fundamental labor rights" puts Right to Work, and there are some 20 States in this country that have Right to Work laws, Freedom of Association, and other major U.S. labor provisions at significant risk.

Article 17.2 of the Peru Free Trade Agreement requires both Peru and the United States to adopt and maintain in its statutes and regulations and practices there under the following rights, as stated in the ILO Declaration on Fundamental Principles and Rights At Work and its follow-up--that is the 1998 ILO Declaration--where it affects trade between the countries.

Now, these rights are freedom of association, recognition of collective bargaining, eliminate of forced, compulsory labor, effective abolition of child labor, prohibition of the worst forms of child labor, and elimination of employment discrimination.

Now, the Peru Free Trade Agreement does not provide any definition of these fundamental rights, leaving the interpretation of what constitutes "freedom of association" or "collective bargaining" to a dispute resolution panel appointed by the U.S. and Peruvian governments. That panel can change, the way I understand it, at the whim of whoever is President.

Given the agreement's reference to the ILO Declaration, it is widely expected that such a dispute settlement panel would, in fact, look at, and rely at least partially on, the standards of the relevant ILO--International Labor Organization--core conventions associated with these rights, much as the ILO does each

year in its follow-up reports required by the ILO Declaration itself.

Now, the recent push by House Democrats to have Peru enact very detailed changes to its treatment of contract laborers as part of its implementation of this agreement, an issue not specifically addressed in the Peru Free Trade Agreement, confirms the wide range of issues subject to this chapter.

The United States, which has only ratified two of the eight ILO core conventions, faces substantial risk that a panel will find that the U.S. labor law violates the Peru FTA, requiring the United States, and even the States themselves, to change their laws or face trade sanctions. Key U.S. laws subject to the risk include -- let me just go through some of them.

State Right to Work rules. Which standard labor market analysis in several other countries, such as Canada, find imposes improper restraint on the ability of workers to bargain collectively or to strike as non-union workers, have the authority to vote on whether to strike?

Take this one. U.S. prohibitions on the admission to unions of persons connected with the Communist Party or the Klu Klux Klan. These are now prohibited by unions, given that ILO standards require the admission of all applicants.

How about this one? U.S. prohibitions in the National Labor Relations Act on the inclusion of supervisors in a union, which is required by ILO conventions? In other words, the ILO conventions require that supervisors be union. I cannot tell you how that would disrupt American labor law.

How about exclusive bargaining rights provided under the National Labor Relations Act which are in conflict with ILO standards requiring minority unions to be allowed to function?

How about various Federal and State laws that place reasonable and balanced limits on the right to strike which are in conflict with the ILO conventions' prohibition on virtually all restrictions on the right to strike?

The Chairman. I am going to have to ask you to summarize, Senator. Your four minutes has expired.

Senator Hatch. I am trying to. This is pretty important. I am going to finish it. I will try to be quicker.

How about this one? U.S. law is permitting the permanent replacement of striking workers, which the ILO has indicated may pose a risk to the effective enforcement of the right of collective bargaining when it occurs on an extensive basis?

How about the Fair Labor Standards Act minimum age of 14, and State laws where there are no minimum ages for children working in agricultural, contravenes the ILO minimum age convention?

How about the lack of equal remuneration of comparable worth rules? These are all problems that would interfere with our laws as they currently exist.

Now, I have to make this point. The Peru Free Trade Act will also require State labor law changes, too. By requiring the adoption of these rights at the Federal level, the Peru FTA, in combination with the U.S. Constitution Supremacy Clause in Article 6, Section 2, is also expected to require any changes made at the Federal level to preempt conflicting State law.

As a result, State Right to Work rules or lower minimum age standards would face the significant risk of being overturned by dispute settlement panels. These are really important things. And, yes, I do not know that we are going to have trouble with Peru, but these agreements, these stipulated terms, will be in every trade agreement from here on in. Let us start with China.

The Chairman. Any further discussion?

Senator Hatch. Two paragraphs and I will be through.

The next, 17.6 requires the United States and Peru to engage in a wide range of capacity-building work. While much of it could be useful, its obligation to promote migrant rights, without regard to the legal status of the migrant, creates a troubling requirement that the United States would be promoting rights for illegal immigrants, at odds with Congress' direction.

For all of these reasons--and I am only mentioning a few of them--it is critical for this committee to ensure, through an explicit clarification in the Peru FTA, to create a safe harbor for U.S. Federal and State labor laws and adopt this amendment.

The Chairman. Any further discussion?

Senator Hatch. I will end with that. I can see the Chairman is getting upset. But that is all right. I am just beginning to upset you. [Laughter].

The Chairman. We do not want to upset you, Senator.

Senator Hatch. I understand. No, you do not. This is going to be a battle.

The Chairman. Exactly. All right.

Senator Grassley?

Senator Grassley. Mr. Chairman, if all of these things that Senator Hatch is talking are a problem, I would not be here supporting this either. If you want

Mr. Maruyamma to back me up on that, I will call on him. But I think that there is nothing in this implementing legislation or the trade agreement itself that requires amendments to our Federal or State labor laws. In fact, that is one of the main reasons why I accepted the May 10th compromise, because it does not require any changes in our labor laws.

But there is already a provision in implementing legislation that clearly makes this. Section 102(a) of the proposed legislation states that the Act cannot be construed to amend any U.S. laws unless the Act specifically provides for the amendment. It is clear the implementing legislation does not contain any amendments to our labor laws, whether State or Federal. So this amendment is simply not necessary for implementing our trade agreement with Peru.

Under trade promotion authority and the implementing bill, it should contain only the provisions that are necessary to implement the trade agreement itself. And when I was Chairman of the committee, I defended bills to implement trade agreements against amendments that failed to meet that standard, so I would ask that we would oppose the Hatch amendment.

Senator Hatch. Mr. Chairman, just one --

The Chairman. We are going to have to vote,

Senator.

Senator Hatch. I understand. One short comment. Seventeen pages. And you do not think it is in there? I can make that argument, too. But I have also been to the ILO. I have actually made arguments over there. Frankly, I can tell you right now, there are 17 pages in this treaty that I think are going to come back to haunt us in this country on labor law. I have to say, I have been in these fights for 31 years, and I am sure Mr. Maruyamma can make arguments against what I have said, but they would not, in my opinion, be valid.

The Chairman. The Clerk will call the roll.

The Clerk. Mr. Chairman, I would like to clarify the recorded vote on committee amendment #5, Hatch #2. The recorded vote is 5 ayes, 15 nays.

The Chairman. Thank you. The amendment still does not pass. That was Hatch #2. Excuse me. It was the second one he has offered, but it is #1. Hatch #1.

The Clerk. Mr. Rockefeller?

Senator Rockefeller. No.

The Clerk. Mr. Conrad?

Senator Conrad. No.

The Clerk. Mr. Bingaman?

Senator Bingaman. No.

The Clerk. Mr. Kerry?

Senator Kerry. No.

The Clerk. Mrs. Lincoln?

Senator Lincoln. No.

The Clerk. Mr. Wyden?

The Chairman. No by proxy.

The Clerk. Mr. Schumer?

Senator Schumer. No.

The Clerk. Ms. Stabenow?

Senator Stabenow. No.

The Clerk. Ms. Cantwell?

Senator Cantwell. No.

The Clerk. Mr. Salazar?

Senator Salazar. No.

The Clerk. Mr. Grassley?

Senator Grassley. No.

The Clerk. Mr. Hatch?

Senator Hatch. Aye.

The Clerk. Mr. Lott?

Senator Grassley. I have no proxy for Senator Lott.

The Clerk. Ms. Snowe?

Senator Snowe. No.

The Clerk. Mr. Kyl?

Senator Grassley. Aye by proxy.

The Clerk. Mr. Smith?

Senator Grassley. Aye by proxy.

The Clerk. Mr. Bunning?

Senator Grassley. Aye by proxy.

The Clerk. Mr. Crapo?

Senator Crapo. No.

The Clerk. Mr. Roberts?

Senator Roberts. No.

The Clerk. Mr. Ensign?

Senator Ensign. No.

The Clerk. Mr. Chairman?

The Chairman. No. The Clerk will announce the results of the vote.

The Clerk. Mr. Chairman, the tally is 4 ayes, 16 nays.

The Chairman. The nays have it. The amendment is not agreed to.

Any further amendments?

[No response]

The Chairman. If there are no further amendments, I would entertain a motion that the committee report the Chairman's mark on the Peru agreement.

Senator Rockefeller. So moved.

The Chairman. A recorded vote has been requested. At least, I requested it. The Clerk will call the roll.

The Clerk. Mr. Rockefeller?

Senator Rockefeller. Aye.
The Clerk. Mr. Conrad?
Senator Conrad. Aye.
The Clerk. Mr. Bingaman?
The Chairman. Pass for now.
The Clerk. Mr. Kerry?
Senator Kerry. Aye.
The Clerk. Mrs. Lincoln?
Senator Lincoln. Aye.
The Clerk. Mr. Wyden?
The Chairman. Aye by proxy.
The Clerk. Mr. Schumer?
Senator Schumer. Aye.
The Clerk. Ms. Stabenow?
Senator Stabenow. No.
The Clerk. Ms. Cantwell?
Senator Cantwell. Aye.
The Clerk. Mr. Salazar?
Senator Salazar. Aye.
The Clerk. Mr. Grassley?
Senator Grassley. Aye.
The Clerk. Mr. Hatch?
Senator Hatch. No.
The Clerk. Mr. Lott?
Senator Grassley. Lott is "aye". I have his

proxy. That is "aye".

The Clerk. Ms. Snowe?

Senator Snowe. Aye.

The Clerk. Mr. Kyl?

Senator Grassley. That is no by proxy.

The Clerk. Mr. Smith?

Senator Grassley. Smith would be aye by proxy.

The Clerk. Mr. Bunning?

Senator Grassley. Aye by proxy.

The Clerk. Mr. Crapo?

Senator Crapo. Aye.

The Clerk. Mr. Roberts?

Senator Roberts. Aye.

The Clerk. Mr. Ensign?

Senator Ensign. Aye.

The Clerk. Mr. Chairman?

The Chairman. Aye.

Senator Bingaman?

Senator Bingaman. Mr. Chairman, am I recorded aye?

The Clerk. Mr. Bingaman, aye.

Mr. Chairman, the tally of members present is 14 ayes, 2 nays. The final tally, including proxies, is 18 ayes, 3 nays.

The Chairman. The ayes have it. The committee will report that the mark on the Peru agreement is agreed

to.

The next order of business is the Airways mark. There is a modification before the committee in connection with the Airways mark. The mark is so modified.

The next order of business before the committee is walk through the Airways mark and modification. We have the new Chief of Staff of the Joint Committee on Taxation here to do so. Welcome, Mr. Kleinbard. We are very honored to have you here and very thankful for all of the service that you are performing for this committee, for Ways and Means, and for the whole Congress. Thank you for your service.

Mr. Kleinbard. Thank you, Mr. Chairman.

The Chairman. I also want to acknowledge the very significant contributions of the Joint Committee's Deputy Chief of Staff, Tom Barthold. Mr. Barthold is sitting right over here in the front row. Thank you very much, Tom, for your work. You have been very, very helpful. Many members have told me how hard you worked, and we appreciate your service. Thank you very much.

Do Senators have any questions regarding the mark or modification?

Senator Stabenow. Mr. Chairman?

The Chairman. Or Mr. Kleinbard, if you could

briefly just --

Senator Stabenow. Mr. Chairman, if I might just say, because I need to step out --

The Chairman. Sure. Sure.

Senator Stabenow. I just want to thank you. This has been a tremendous amount of hard work. I know there are still issues to be negotiated and we have to strike, I believe, a better balance. But I believe it is important to move the bill forward, and in leaving, will leave my vote to do that. Thank you.

The Chairman. Thank you. Thank you, Senator.

It would be helpful if we had order in the room so we could all hear Mr. Kleinbard, give him the courtesy, the new Director of the Joint Committee on Taxation. Mr. Kleinbard?

Mr. Kleinbard. Thank you, Mr. Chairman.

You have before you the following documents describing the American Infrastructure Investment and Improvement Act of 2007. You have the staff of Joint Committee on Taxation's explanation of the Chairman's mark, our number JCX-4207, our revenue table for the Chairman's mark, and then the corresponding items for the Chairman's modification, JCX-8307, and the revenue table, 8407.

What I propose to do, Mr. Chairman, if this is

satisfactory to you, is to identify those points in the modification that differ from the original Chairman's mark and briefly describe those.

The Chairman. If you would, please.

Mr. Kleinbard. The Chairman's modification makes the following changes to the mark previously distributed. First, it increases the international departure and arrival tax to $16.65, and indexes that for inflation. Current law provides a departure tax of $15.10.

Second, the modification drops a provision that was in the Chairman's mark to tax the domestic segment of an international flight, to impose a fuel tax on those domestic segments.

Third, the Chairman's mark imposes a new requirement of transparency in the tax disclosures that airline passengers will see when they look at their tickets. Some airlines have been putting fuel surcharges payable to the airline in the tax line, and this provision requires that only governmental charges be reflected in the tax line on the ticket.

Fourth, the Chairman's modification makes an important modification to the pension funding rules for certain plans. Essentially, though the provision itself is complex, what it in essence does is require that those airlines that take advantage of a special relief rule in

the Pension Protection Act of 2006 make current contributions to their pension plans that would be no less than the accrual of current liabilities for the current year.

In respect of the Highway Trust Fund provisions of the Chairman's modification, there are a number of new proposals. The first, is to impose a tax liability on certain inversion transactions. These are the transactions in which U.S. corporations re-domicile themselves in foreign jurisdictions.

The next, is to deny a deduction for punitive damages. The provision would require that taxpayers not be able to deduct punitive damages paid in the context of civil litigation.

Finally, the proposal makes a cluster of clerical and conforming amendments to various fuel tax provisions. It clarifies some aspects of the Motor Fuel Tax Enforcement Advisory Commission, and it makes some conforming amendments with respect to the Highway Trust Fund.

The Chairman. Are there any questions regarding the mark or the modification?

Senator Schumer. Mr. Chairman?

The Chairman. Senator Schumer?

Senator Schumer. I do not have any questions, but

I would like to join in the welcome of Mr. Kleinbard. He is from not only New York and not only Brooklyn, but Park Slope, Brooklyn, a neighborhood in which I have lived 27 years. I welcome him with open arms.

The Chairman. Thank you, Senator. That is quite a welcome.

Mr. Kleinbard. We think we are going to reconsider now. [Laughter].

The Chairman. Any further questions?

Mr. Kleinbard. Mr. Chairman?

The Chairman. Mr. Kleinbard?

Mr. Kleinbard. I apologize. But in going through the modification, I did not cover the additional infrastructure modifications, including Senator Schumer's Liberty Zone amendment and a couple of others, which I could go through if you would like.

Senator Conrad. Could we move to eliminate that then?

Mr. Kleinbard. Yes. We can eliminate my description.

Senator Conrad. No. I mean, just Schumer's amendment. [Laughter].

The Chairman. Are there amendments to the mark? Does any Senator wish to be recognized to offer an amendment?

Senator Kerry. To the whole mark.

The Chairman. The whole mark. Senator Kerry?

Senator Kerry. Mr. Chairman, I call up amendment 20, which is actually Senator Lott's and my amendment, and Senator Smith has asked to be a co-sponsor of this also.

Just very quickly, this week the Texas Transportation Institute released its annual study that shows that highway congested is costing us $78 billion annually, and 2.9 billion gallons of wasted fuel. As we all know, fuel costs are now up to over $80 a barrel.

States across the country have all cited about $12.7 billion needed over the next 6 years for developing passenger rail corridors and systems, so this is an amendment which Senator Lott, I, and others have worked on for a period of time.

Modifications have been made to the amendment to meet some of the issues that were raised. It is an amendment to provide $900 million of qualified rail infrastructure bonds for 2008, 2009, and 2010. The Joint Committee on Taxation has estimated this amendment: it raises $24 million over 10 years. It is offset fully. I would ask my colleagues to support it, It is an important infrastructure investment for many parts of the country.

The Chairman. Any further discussion on the amendment?

[No response]

The Chairman. Senator, I think you have got a good idea here. You have carefully thought through your amendment. It is fully offset with proposals that have passed this committee already, with slight modification, but very slight, and I recommend that the committee adopt your amendment.

Senator Kerry. Thank you, Mr. Chairman.

The Chairman. If a recorded vote has not been requested, all those in favor of the amendment say "aye".

[Chorus of ayes]

The Chairman. Those opposed, "no".

[No response]

The Chairman. The ayes have it. The amendment is agreed to.

Senator Kerry. Thank you very much, Mr. Chairman.

The Chairman. You are welcome.

Any further amendments?

Senator Kerry. Mr. Chairman? I wanted to just raise an issue that is not an amendment, but as I understand the mark, we developed a new tax regime for flights that are flown under fractional ownership programs.

The Chairman. Correct.

Senator Kerry. And this new regime is taxed as general aviation, and the fractional management company is subject to this $58 departure fee, I believe.

This new regime raises funding that is needed from the sector. We want to make sure the details of it are consistent with the business model that these fractional companies have pioneered, and there is some concern about that. I would like to just indicate to you that I think we need to commit to work with the sector to address several issues related to this new tax structure. Some of the details that were put together very quickly and I think could benefit from a little more scrutiny before this finally becomes law.

The Chairman. I appreciate that, Senator. As the Senator well knows, actually the fractional jet industry wanted these changes. They wanted to be treated and taxed as general aviation rather than commercial planes. In fact, they have generally agreed to the provisions in this bill, from my understanding. I am certain you are correct, that they will tell us of little wrinkles we have to work on. We will, clearly, work with you to make sure that happens. Thank you.

Senator Roberts. Mr. Chairman?

The Chairman. Senator Rockefeller, earlier, wanted

to be recognized.

Senator Roberts. I would just like to agree with Senator Bingaman and I share his concern, and I would like to be part of that working group to address these concerns.

The Chairman. Absolutely.

Senator Roberts. Thank you.

The Chairman. Senator Rockefeller?

Senator Rockefeller. Thank you, Mr. Chairman.

I call up Trent Lott's and my amendment, #6. I would ask to explain it, and then also, in view of our conversation, that I might at some point make some remarks generally because I think I know what is going to happen here.

The Chairman. Sure. Not too long.

Senator Rockefeller. Yes. But I want to make it -- all right.

You have something now called the departure segment tax for passengers leaving from small airports, rural airports across the country. Our amendment would eliminate that departure tax, except all but one aspect of it, and we increased the tax on general aviation jet fuel. It is all about jets. We include King Airs in our amendment, but per an agreement with Kent Conrad we were going to try to eliminate that on the floor so that they

would be gone. But for the purposes of this amendment, they are in.

The amendment would save American consumers about $248 million a year. You have a very interesting thing here. We all know passengers departing from small communities pay much higher airfares. We should not be further penalizing them by imposing higher taxes on the airlines that will be passed on to our constituents, because when you do that to commercial airlines the service in the rural communities declines.

For the information of those, the gas/fuel tax that we have added on will be 60 cents per gallon. No, it would be 52 cents per gallon for general aviation. The average motorist, if he is driving, pays 60 cents a gallon, so that puts it in some perspective.

Let me point out that the commercial airline passengers pay--not just the airlines, but the passengers--97 percent of the total revenues of the Aviation Trust Fund to keep the analog Aviation Trust Fund operating. They pay 97 percent, despite only imposing 70 percent of the cost of operating the system. This is not fair.

Corporate users are deducting the cost of their aircraft, a generous tax break that the vast majority of American owners do not get to use. I know for the time

for debate is limited, but we view this as a critical amendment, and I think it is a fair amendment.

The Chairman. Is there any further debate on the amendment?

Senator Roberts. Mr. Chairman?

The Chairman. Senator Roberts?

Senator Roberts. I think this amendment aims to decrease the fares on rural airline service, but I do not think it is going to accomplish that goal. I know the authors of the bill say the fuel tax increase only hits the business jets, but it is not that simple. Turbo props use the same fuel, and I do not know how you can separate that out. I have a whole series of graphs here on the various general aviation airplanes where you have the turbo prop and then the other plane that is very similar.

This amendment works out to an additional 16-cent increase upon general aviation fuel. The underlying bill that we have all agreed to, or we had hoped to agree to, increases the general aviation fuel tax by roughly 65 percent. This amendment would bring that fuel tax increase to 237 percent.

Now, the airlines pay a fuel tax as well, 4.3 cents. The underlying bill does nothing to their rate. I support that in the mark. I thought that was part of the

agreement. All this amendment will do is allow the airlines to increase their profits, and thank goodness they are doing that five straight quarters. They deserve an outstanding round of applause and everybody's admiration to do that, some $15 billion we have invested in that regard. When they are setting records, it puts the entire cost of the modernization on the general aviation business, and I do not think that is right.

According to the GAO, when ticket taxes and fees lapsed in 1996, Congress suspended the security fees in 2003. When carriers raised their airfares, making up the difference, passengers saw no decrease in ticket prices.

I respect the Senator greatly, but I would hope that my colleagues would oppose this amendment.

Senator Rockefeller. Would the Senator yield?

Senator Roberts. I think it would break the mark.

Senator Rockefeller. Would the Senator yield?

Senator Roberts. Certainly.

Senator Rockefeller. You do agree, however, that the tax on general aviation fuel that we are proposing is substantially lower than what it is that American motorists pay at the gasoline tank?

Senator Roberts. If you would like to drive from Wichita to Dodge City, that is your business. I would like to fly, and I would like to at least get there from

here.

Senator Rockefeller. But if you could answer the question.

Senator Roberts. I think I have.

The Chairman. Any further discussion?

Senator Bingaman. Mr. Chairman?

The Chairman. Senator Bingaman?

Senator Bingaman. Mr. Chairman, I reluctantly have to oppose the amendment also. As I understand current law, today we exempt ticket tax for domestic passengers who begin or end their flights at airports with fewer than 100,000 passenger enplanements per year. That is all the airports in my State, except Albuquerque. So that, to me, is small and rural.

As I understand this exemption, I think it is too broad. It extends well beyond rural communities. For example, departure from airports such as Louisville, El Paso, or Oklahoma City would be exempt under the amendment.

In my view, these airports are not rural. They had more than 1.6 million enplanements in fiscal year 2006. Louisville is currently served by 10 commercial airlines, Oklahoma City has 11 commercial airlines, El Paso has 8 airlines. I think it would be a mistake for us to raise this exemption from this tax to these very large

airports.

Senator Grassley. Mr. Chairman?

The Chairman. Senator Grassley?

Senator Grassley. I think this tax increase is outrageous. Most of us in the Senate are representing rural communities, we have been working for rural development. I think this is going to bring about rural destruction. The Federal Government collects tax on fuel when it leaves the pipeline. That is long before it is ever in an airplane. So that means that every airport in my State, and almost every State represented by Senators here in this committee, is going to see an increase.

Every regional airline, cargo, or charter will have to pay 52 cents, and then wait for a refund, because when the jet fuel is sold out of the pipeline the tax is collected. No one knows what kind of plane is going to use that particular fuel. Every flight into your State will have to file for a 48-cent-a-gallon refund.

You think that this is not economical to fly into rural America now? Just wait until you see this sort of a tax increase. Every rural airport will have $4,680 of excise tax tied up in every tanker truck of jet fuel that they buy just waiting for a decision whether this jet fuel will feed a regional commercial plane, a jet, or a turbo prop. Then they have to keep records, subject to

an audit of course, and they have to file them for a refund on a different tax rate.

So I think we need to get very real. This is all over a $3.10 segment tax per flight that our constituents will probably never see. Do you think that this ticket price will ever go down? The local airports lose the time value of money that could buy over 1,500 segments.

Now, that just does not make economic sense, to my point of view. I am against this amendment.

Senator Hatch. Mr. Chairman?

The Chairman. Senator Hatch?

Senator Hatch. Look, I do not think it is a bad amendment. I mean, all he is saying is, we are going to have $400 million in increases no matter what way this goes. This is not a tax increase in that sense, except one way or the other it is going to increase the $400 million. But it is the allocation of the $400 million that Senator Rockefeller is advocating, and that is that -- what is it? They pay 3 cents out of 16 cents?

Senator Rockefeller. It is 3.5 percent.

Senator Hatch. Yes. And these are, for the most part, corporate jets that many feel are not paying their fair share. Now, I do not think anybody is arguing they should pay the actual amount, but there would be a slight shift here, as I understand it, which seems to me

equitable and fair. But it is going to be a tax increase no matter which way you go on this thing. If you do not approve the Rockefeller amendment, there is still a tax increase. In the sense that we feel we have to do this -- well, I just wanted to make that point.

The Chairman. I appreciate that. I urge Senators not to support the amendment. Frankly, there already is a sufficient exemption from the segment fee for rural airports, as pointed out by the Senator from New Mexico. Second, this is, I think, too much of an increase in jet fuel. It is not just the persons mentioned by the Senator, but as has been indicated from the Senator from Iowa and the Senator from Kansas, it has other detrimental effects as well.

All those in favor of the amendment say aye.

[Chorus of ayes]

The Chairman. Those opposed, no.

[Chorus of nays]

The Chairman. The nays have it. The amendment is not agreed to.

Senator Rockefeller?

Senator Rockefeller. I want to thank the Chairman and the Ranking Member for allowing me to make some comments. I understood what the outcome was going to be. I just want to spend a minute or so, a couple of minutes,

explaining our deal here, because we still have the Commerce Committee bill which was passed easily, and we have the Finance Committee bill which was passed. They are going to have to be reconciled and we are going to have to get together. So, I wanted to just give this background. Senator Baucus graciously agreed to let me do this.

Now, every member of our committee knows that we must authorize the expiring aviation taxes. That is not debatable. These taxes generate over $12 billion in revenue for the Aviation Trust Fund, which funds the vast majority of the Federal aviation operations, the air traffic control system, and other things.

Ten years ago, we had a long and brutal debate over how to reauthorize aviation taxes and who should pay these taxes. Today, in essence, we are not having that and we just voted as we did.

I believe that Senator Lott and I had crafted a strong, and have crafted a strong, FAA reauthorization bill that lays modernization before us. I cannot support the Chairman's proposal as introduced. I know the Chairman worked hard. They have produced a reauthorization bill that shares our goals, but we believe that it is inadequate to the bill's equitable financing.

We believe that the Commerce Committee bill absolutely guarantees funding for modernization of the air traffic control system--remember, we have to build a digital one while maintaining the analog system that we have--because of the revenue stream generated by what we have in our bill, and that is 25-cent surcharge on general aviation.

The surcharge does not create any budgetary issues and allows the Appropriations Committee the ability to spend $400 million more on FAA authorization, if they choose to do that, without sacrificing other priorities.

Now, I know that this mark included mandatory spending on modernization as well, but we know that the Appropriations Committee has already voiced its serious concerns about this provision. I think that we have to realize that they are unlikely to yield their position. So we do not have a fenced in $400 million, we do not have a fenced in way of building digitalization unless they will change their views, and I do not think they will.

The second issue, frankly, is financial equity. For far too long, the high-end corporate GAs have gotten a free ride on the backs of commercial airliners. Now, you can say airliners, if you choose, or you can say the vast majority of people who fly in this country. If airlines

have made profits recently, that is nice, but they sure have not for a long time and might not again. There are going to be a billion people flying in another 10 years, and you have got to keep this in mind.

I have heard endlessly how corporate jets are only marginal users of the system. If this is truly the case, then I think that they should have only marginal access to the system. So I would just highlight a few facts, Mr. Chairman.

Airline passengers, commercial, pay for 97 percent of the cost of the air traffic control system, but they only use 73 percent of the system. General aviation traffic accounts for 16 percent of air traffic control, but they only pay 3 percent.

Now, the Finance Committee's plan equity shifts amounts to all users, and any move towards equity would be slight. Airline passengers would still contribute nearly 95.5 percent of all funding for the system. Airline passengers would contribute that, and then be expected to pay more for its use. High-performance GA jet aircraft would contribute, under this system, approximately 4.5 percent of the total. I do not think that is fair.

The Chairman's mark, of course, would index new taxes on airline passengers--there has been no indexing

since 1991--but not on personal-use GA jets. They are excluded. They are excluded, leading to even less equity in the long term. This will make the problem worse. The total number of GA aircraft has tripled over the past decade.

Now, just imagine when you are sitting on the tarmac waiting to get a take-off to some city, and you are sitting there. The reason, probably, is because two-thirds of all the aviation in the air at any one moment are general aviation planes. Two-thirds, although they are paying almost nothing and getting a free ride and getting to write off their costs.

So again, if you say, as the FAA does, that business jet growth will be twice the rate of commercial aircraft over the next 14 years, you have got to think about that. You have just got to think about it.

The average American pays 61 cents a gallon in State and Federal excise fuel taxes to run a car. The CEO flying up in his Lear jet pays a whopping 36 cents a gallon; 61 cents driving a car, 36 doing your Lear jet. That does not seem very fair to me. I think it is wrong.

Business jets also have very generous tax breaks for owning aircraft. They can, and they do, deduct the cost of operation of the aircraft. They can do that, commercial airlines cannot. One amendment Senator Lott

and I had filed that I am not bringing up--and just understand this number--was to adjust the depreciation of corporate aircraft to match that of commercial aviation. If we had done that, we would have raised $3 billion, so that gives you some sense of the inequity that we are talking about.

So the American taxpayer is subsidizing CEOs flying around the country in their private jets. This is a little bit direct, but there is an example of a CEO of one of the major companies in this country, and he flies his daughter back and forth from Denver in his GA to California so she can attend high school there. All right. That is fine. But is it fair to the average taxpayer unless there is some equity in the paying system?

I do not understand why we are not making this segment of the community pay what they should and can afford to pay. Now, I know that some of my colleagues are concerned about the effect of the King Air, and we were going to try to work it out on the floor, and we may still. According to the AV Buyer website which lists aircraft for sale, a 2005 King Air is listed at $4.295 million, which is not an inconsequential amount.

A King Air costs over $1,500 to operate an hour. A lot of West Virginians do not make $1,500 a month. My

main objection is that this mark does not go far enough to address the critical issue of equity among the users of this system. I am not asking for complete, but we are asking for a reasonable contribution on the part of GA.

Everybody in the world, every corporate jet owner, has called up everybody in the Senate and they have lobbied very hard and very effectively. So we have to realize that the air space, which is going to be increasingly crowded, due mostly to corporate jets and the taxi jets which are coming, is very limited. The public space is limited, so the problem is going to get much worse. We cannot allow one segment of the industry access to it without asking them to pay for the use of it.

So airlines barely cover their costs serving small communities, in spite of what the Senator from Kansas has indicated. Small communities. Not overall, but small communities. I am interested in small communities, and so is the Senator from Kansas. We do not want to make this service so costly, because we know exactly what happens. If they do not make a profit, they pull out. That is the history of West Virginia. I am scrambling all the time to try and keep some kind of flights. We are worse off than we were in 2001 in terms of service in our State, in our small communities, and I am sure that

is true for others, too.

So, in conclusion, I know that the Chairman and Ranking Member are committed to continue working on this issue, and we will need to because we have two bills of jurisdiction, so to speak, that have to be reconciled. Neither has, I think, universal support. I think we are all here to understand that we have to make something pass.

What I would actually prefer to do is to extend the aviation taxes 90 days as part of a continuing resolution. We will see what happens with that. So here we are, trying to build a digital air control system that is a huge impact. If you have a digital system, it does not take you three minutes to land a plane after the previous one, but takes you two. You can land airplanes on parallel runways at the same time, where you cannot now. And if there is wind shear, it does not matter. Digital will take care of that.

So I just think general aviation is not paying its fair share. I think it is sort of a Jay Leno/David Letterman type of thing. I do not understand why they have not taken it up. I think it is subject of some ridicule. It is not fair and it makes me angry, upset, makes my people angry and upset. But fortunately we have time to work on this, and I look forward, Senator Baucus

and Senator Grassley, to working with you, Senator Lott, and others, and with Patty Murray.

The Chairman. Thank you, Senator. I think I can speak for the committee in saying we all--and certainly I--are deeply indebted for all your work, especially in the Commerce Committee, trying to address the basic issue, namely, how do we prepare for the next generation, move to digitization, move to NextGen, and so forth. It is so critically necessary, as you stated so eloquently, far better than any of us here. We are far behind in this country and we have got to get moving, and you are trying to address that.

Second, we deeply appreciate--I do, anyway--your efforts to get some balance here. Balance is a little bit in the eyes of the beholder, but you sure worked at it and you moved us in the direction that you wanted to go. I deeply appreciate that effort as well.

This is a work in progress. I do believe that it is important to move. The deadline is very close. The world is run by deadlines. If we do not move here and keep postponing it, I am not sure we are ever going to totally resolve it. But at least by referring this bill out of committee today and as we go to the floor, we can keep working on ways to try to make some of the improvements that you have mentioned. Other Senators on

the committee have made the same recommendations.

Senator Rockefeller. And we do have two bills on the floor.

The Chairman. That is correct.

Senator Rockefeller. On this subject.

The Chairman. That is correct. But I thank you very much for your efforts.

Senator Rockefeller. Thank you.

Senator Roberts. Mr. Chairman?

The Chairman. The Senator from Kansas.

Senator Roberts. I am going to submit a statement for the record in answer to Senator Rockefeller's comments, which I think would be helpful in regards to this debate and in response to his question to me. Perhaps I misunderstood, but that was the earlier comment. I just want to make the record clear. The Federal gasoline tax is 18.4 percent. In this bill, the Federal tax is 36 cents. I think you included the State tax. So I just wanted to clear that up. But I thank the Senator for his comments, and I am going to submit my statement for the record.

Senator Rockefeller. Thank you.

[The prepared statement of Senator Roberts appears in the appendix.]

The Chairman. Are there other amendments?

Senator Kyl. Mr. Chairman?

The Chairman. Yes, Senator Kyl?

Senator Kyl. I would just like to ask a couple of questions, if I could. And I apologize. I had a previous engagement that was scheduled before this meeting, so I could not be here at the very beginning.

I will just address this to you. This has to do with the New York rail provision. I wonder if you could explain. There has been a lot of criticism of it on the grounds that the committee should not be setting a precedent to create a tax credit for an entity that does not pay taxes. This could set a precedent for this kind of, in effect, a back door appropriation.

Also, a question about -- and either you, or perhaps the Budget Committee chairman, since he is here, could perhaps answer the question of whether this might violate the rule against tax earmarks, since it only benefits New York City, as I understand it. And either Joint Tax, or perhaps you could tell us whether this has ever been done before. Has our committee ever provided a tax credit to an entity that does not pay taxes, to a city?

The Chairman. This provision does not limit other entities from the same treatment, so it is not designed for New York City alone.

Senator Kyl. So it could be used by other cities.

It does set a precedent, then?

The Chairman. That is my understanding. I am sorry. I think the Senator from New York wants to address that question.

Senator Schumer. Let me just say what this is. Six years ago, in the wake of 9/11, the President supported, and I think just about everybody who was here, voted for $20 billion for New York City. This is the last piece of that promise, and it is supported by the White House and just about by everybody else.

This has been in previous bills, supported both by Senator Baucus, and Senator Grassley when the Majority was on the other side. It had to be taken out--that is why it has taken as long as it has--because of other extraneous reasons, nothing to do with objection to the provision. And the identical language was passed by the House on previous occasions as well.

I would say to my friend from Arizona, this was a promise made. It is the last phase of the $20 billion. Thank God, downtown New York is on the way to recovery. If there were ever a disaster or an attack somewhere else and the country made a promise to them, I know all of us would want to stand by that, and I think we should stand by this. We can quibble about the means of doing it, but that is what has held this up for, now, six years. Not

six, four probably, because it did not really come to fruition. We negotiated these terms with Mitch Daniels when he was the OMB Director, I guess, three or four years ago and it was acceptable to everybody then. I do not think it would be right to hold this up now because of a specific-type objection to the way it is being done. So I would ask my colleague from Arizona to join us in moving this forward.

Senator Kyl. Mr. Chairman, if I could, I appreciate the explanation and I was certainly, along with all of our colleagues, very willing to respond with every need that New York City presented after the tragedy of 9/11, no question about that.

When you have good news that things do not use up all of the money that you have allocated, though, I am not sure that it was the $20 billion as much as it was, we need money to do things. It is not just a quibble about how you do it. This is over $600 million, as I understand it, with a new, unprecedented kind of funding, a tax credit for an entity that does not pay taxes. As the Chairman noted, it will establish a precedent for any other city to request funding in the same way. So, in effect, we are opening an new chapter in fundraising.

When our constituents are very concerned about wasteful Washington spending and want us to get a handle

on it, and we have had a hard enough time in the appropriation process with earmarks, to be opening up a new -- and the *Wall Street Journal* editorialized about this a few months ago.

I have forgotten whether they used the term "back door", but a new back door way of getting money to cities that is not an appropriation and a lot harder to follow, right after we have made rules about how we have to disclose earmarks, and the appropriations process is going to be transparent.

Now we come in with a new method of financing that is not covered by these new rules and that does set a precedent, and I think it sets a very bad precedent. I am troubled that this committee, now, will be the target of tax preferences for non-taxpayers as a way to fund public works. I think it is more than a quibble.

I appreciate that the project itself may be very desirable. That, I am not contesting. But in any other context, I suspect the Senator from New York would also agree that this is a big step for this committee to take, and it sets up a very troublesome precedent.

The Chairman. I might say, Senator, essentially this measure has already passed in this committee. It was in the reconciliation bill. It passed the Senate and it was taken out in conference, this same provision. In

addition, it was the final, major piece of the congressional support for New York post-9/11. It was just an extra part that was not yet --

Senator Kyl. I understand. I understand. Of all the committees in the Senate, this committee is a really professional committee. It has got a very professional staff. The staff is always coming back to me saying, granted, people want to do this, but the reason we have not done it is because this is bad policy.

This committee is kind of the backstop, kind of the conscience of making sure we do not do things wrong. I just really understand it has passed before. There is a lot of emotional support for it. But I think at the end of the day we will rue the day that we opened up this new financing mechanism. It is now in this committee, not just the Appropriations Committee.

The Chairman. Yes. I do not think this new financing mechanism is going to go very much further in many other instances, and I say that because this is a very specific case with a very unique history. Because New York is a nonprofit, does not pay taxes, we have come up with this new --

Senator Kyl. I have already been approached.

The Chairman. [Continuing]. This new mechanism.

Senator Kyl. I have been approached by a city, but

I will not disclose who it was.

The Chairman. You may have been approached, but I do not know how far that is going to go.

Senator Kyl. So this will be a special deal then for New York?

The Chairman. Well, this is part of the post-9/11 commitment.

Senator Ensign. Mr. Chairman? Mr. Chairman?

The Chairman. Senator Ensign? Sorry.

Senator Ensign. I share some of the same concerns that Senator Kyl has on the precedent that it has set, because the tragedy of 9/11, there are other tragedies. I mean, Katrina was certainly a terrible tragedy. There are other tragedies that can hit. Obviously we had the tornadoes that hit.

Senator Schumer. Would the gentleman yield?

Senator Ensign. No, I will not yield. I want to make my point. The point that Senator Kyl is making, is that we all made a tremendous commitment to New York City and I think that that was appropriate. What we are talking about here, though, is setting the type of precedent on the financing of it to where we are basically taking money from one pot in the Federal Government through the tax laws and back-filing that.

And the amount of money that we are talking about

here is setting a precedent that other entities will want to take advantage of in the future. As a matter of fact, the tragedy of 9/11 did set certain precedents, and we have used those. People will argue, well, you did it for New York City, you should do it for other places.

I think that is the point that Senator Kyl is making here, is that we are setting a precedent that will be used in the future. I think that you can almost guarantee, other cities will make the argument in the future that this should be done. That is why we should go cautiously forward when we are doing that.

Senator Schumer. Mr. Chairman?

The Chairman. The Senator from New York.

Senator Schumer. Mr. Chairman, I have to say in all due respect, not to the argument made by the Senator from Arizona that Mr. Ensign is echoing, but to say that the attack on 9/11, and compare it to other tragedies like tornadoes, it is not fair to New York, it is not fair to America. It is not even fair to the war on terrorism. This was an unprecedented attack.

It was not a natural decision of God. It was an evil attack, which our city is still suffering from. And to say that there will be other attacks, other issues like tornadoes and compare them to this, I think is unfair and wrong, and I hope my friend from Nevada will

re-think that part of his remarks.

As for the specifics here, which is a legitimate argument, I can tell you that we thought this through thoroughly, that there has always been a reason to say, we will do it a different way, and then it never happens.

We have waited two, three, four years for this. It has been approved before. It has been approved by the administration. And, sure, my friend from Arizona and I have no doubts about his integrity and desire to help. But my friend from Arizona, I would say this was unique, the attack, unprecedented. More American civilians died that day than any day in our history.

And yes, this may be unique, but I do not think any city applying for this for another purpose will be able to cite this as a precedent, and I would urge my colleagues, in the spirit that America pulled together after the day, after 9/11, on 9/12, 9/13, led by President Bush, who fully supports this provision, and his administration is not known willy-nilly for supporting new kinds of tax provisions, to join and move this forward.

Senator Ensign. Mr. Chairman, I need to respond.

The Chairman. We are going to have to move forward.

Senator Ensign. No. I need to respond because --

The Chairman. This is the last comment, then we are going to move.

Senator Ensign. Because I think that all Americans -- I mean, we all did. I mean, people cried. It was an absolutely terrible day in the history of America, and I think that all of our hearts went out to those who were affected by 9/11. I was just making the point that tragedies do happen. You cannot ever compare one tragedy to another. Everybody has different feelings about tragedies.

The point I was making was, and echoing Senator Kyl's points, is that I think that we have to be very cautious in setting precedents in how we do things around here because they can be taken advantage of in the future. This may be very worthwhile to do, but I think he is raising a cautionary note and I think that we should heed that cautionary note.

The Chairman. Senator Salazar?

Senator Salazar. Thank you very much.

The Chairman. I urge my colleagues, this is the last comment on this measure, because we do have another bill to go to.

Senator Salazar. Thank you very much, Chairman Baucus and Ranking Member Grassley. I want to just say two things. First, I hope that we can continue to try to

work with Senator Rockefeller and Senator Lott to make some accommodations on some legitimate issues that they have raised. It seemed to me, over the last several weeks we have been close to getting the battles of the Titans resolved here between commercial aviation and general aviation.

I thought we were going to get there last week, but we did not. But there are still some remaining issues and I would hope that our committee staffs and our Senators can continue to work together to try to address some of the issues that Senator Rockefeller and Senator Lott have legitimately raised.

Second, I did want to make a comment specifically to the increase in the international rates here. Frankly, the international flights that we currently do have are flights that impose a lesser burden on the system than domestic flights, and that is because of the size of the airplanes that we have doing those international flights.

So it is those kinds of issues that we might be able to resolve as we move forward in getting this bill through to the floor, and I look forward to working with all of you in getting that done.

The Chairman. All right. You bet. Thank you, Senator.

If there are no further amendments, I would

entertain a motion that the committee report on the Chairman's mark on the Airways bill be reported.

Senator Grassley. So moved.

The Chairman. Is there a request for a recorded vote?

[No response]

The Chairman. I see no request. A recorded vote is requested.

The Clerk. Mr. Rockefeller?

Senator Rockefeller. No.

The Clerk. Mr. Conrad?

Senator Conrad. Aye.

The Clerk. Mr. Bingaman?

Senator Bingaman. Aye.

The Clerk. Mr. Kerry?

Senator Kerry. Aye.

The Clerk. Mrs. Lincoln?

Senator Lincoln. Aye.

The Clerk. Mr. Wyden?

The Chairman. Aye by proxy.

The Clerk. Mr. Schumer?

Senator Schumer. Aye.

The Clerk. Ms. Stabenow?

The Chairman. Aye by proxy.

The Clerk. Ms. Cantwell?

Senator Cantwell. Aye.

The Clerk. Mr. Salazar?

Senator Salazar. Aye.

The Clerk. Mr. Grassley?

Senator Grassley. Aye.

The Clerk. Mr. Hatch?

Senator Grassley. Aye by proxy.

The Clerk. Mr. Lott?

Senator Grassley. No by proxy.

The Clerk. Ms. Snowe?

Senator Snowe. Aye.

The Clerk. Mr. Kyl?

Senator Grassley. No by proxy.

The Clerk. Mr. Smith?

Senator Grassley. No by proxy.

The Clerk. Mr. Bunning?

Senator Grassley. No by proxy.

The Clerk. Mr. Crapo?

Senator Crapo. Aye.

The Clerk. Mr. Roberts?

Senator Roberts. Aye.

The Clerk. Mr. Ensign?

Senator Grassley. No by proxy.

The Clerk. Mr. Chairman?

The Chairman. I vote aye.

Senator Rockefeller. Mr. Chairman?

The Chairman. Senator Rockefeller?

Senator Rockefeller. In view of the discussion that was just held with respect to New York, I would change my vote from a "no" to an "aye".

The Clerk. Mr. Rockefeller changes his vote to "aye".

Senator Grassley. I hope everybody will stay here so we can get Senator Crapo's bill out.

Senator Conrad. Mr. Chairman?

The Chairman. Senator Conrad?

Senator Conrad. Might I just say in response to questions Senator Lott has raised and Senator Kyl has raised, there are no budget points of order against the bill that was just passed.

The Chairman. The Clerk will announce the vote.

The Clerk. Mr. Chairman, the tally of members present is 13 ayes, zero nays. The final tally, including proxies, is 16 ayes, 5 nays.

The Chairman. The ayes have it. The mark is reported. I might say, just for the curious, that under the committee rules only votes present are counted on measures reported out of the committee, and that is why the Clerk is announcing two tallies. The tally that counts is the first tally of the Senators present.

Proxies do not count on reporting measures out of this committee. Proxies do count for amendments, but do not count to report a bill out of this committee. All right.

The next order of business is for Mr. Kleinbard, if you could briefly walk through the next measure before the committee.

Mr. Kleinbard. Thank you, Mr. Chairman.

You have before you the following documents that describe the Chairman's mark of The Habitat and Land Conservation Act of 2007. You have the staff of the Joint Committee's description of the bill, JCX-7507, and our revenue table, JCX-7607. I will describe the bill.

The Chairman. Mr. Kleinbard, could you please suspend? I urge those Senators present to stay present. This measure should not take long. We need 11 Senators present.

Senator Grassley. In other words, what he means is, there is just the right number here. Don't anybody go.

Senator Crapo. Mr. Chairman, could we ask unanimous consent to forego the explanation?

The Chairman. Absolutely. Thank you, Senator.

Senator Crapo. I ask such unanimous consent.

The Chairman. All those in favor of the mark, say aye.

[Chorus of ayes]

The Chairman. Those opposed?

[No response]

The Chairman. The mark is agreed to.

Senator Crapo. Mr. Chairman, may I engage with you in a brief --

The Chairman. Absolutely.

Senator Crapo. Mr. Chairman, as you know, I am very interested in this bill and I appreciate you bringing it forward and helping us to move it forward, and Senator Grassley's assistance as well. You were both original co-sponsors and have been very helpful to work with me.

I would like to bring to the attention of the committee my concern with the approach taken in the pay-for in terms of modifying the effective date of leasing provisions in the American Jobs Creation Act of 2004, the so-called "silo" provision to provide the revenue offset for this important legislation.

It is my understanding that the provision, as drafted, would have an effect on some of the Nation's largest financial institutions.

The Chairman. Those in the hearing room, if you wish to converse, I urge you to leave, go out in the hallway. I think we owe the Senator from Idaho the

courtesy of not engaging in conversation while he is speaking, and I thank everyone.

Senator Crapo. Thank you, Mr. Chairman.

As I was saying, I think this provision, as drafted, would have an effect on some of the Nation's largest financial institutions, but extends beyond tax policy. They would be required to restate the way they account for their leasing transactions to their shareholders.

Since the American Jobs Creation Act of 2004 was enacted, major accounting rule changes for financial institutions under FASBE 13-2 significantly changed how banks must account for changes in their lease economics. This result may have a negative effect on the regulatory capital of banks, and this comes at a time when the financial services industry is facing enormous pressure and our economy is facing uncertainty.

With that in mind, I have been working with the banking industry to develop a silo compromise that would resolve this issue satisfactorily without requiring financial institutions to restate their leasing economics. Mr. Chairman, it is my understanding that you have been considering a similar proposal.

As we consider this mark and move forward, I would like to establish that we have a mutual interest in arriving at an equitable outcome on the tax treatment of

silos that considers the lease accounting concerns of the financial institutions that I have mentioned.

Mr. Chairman, I would like to work with you to resolve this issue in a fair and responsible way in the future.

The Chairman. Thank you, Senator. As you state, there has been significant tax non-compliance using leasing transactions. In this case, we are talking about silos. In fact, the IRS has identified these as "listed" tax shelter transactions, and that is a designation reserved for the most questionable tax arrangements.

The IRS has informed me that they intend to audit every siloed investor that was not covered by the 2004 change in the tax treatment of silos. That requires a large commitment of IRS resources that are unavailable for other work.

I am committed to resolving this issue in a fair and responsible manner, and I want to eliminate the tax abuse--I very much mean that--and help IRS save on resources without having to audit each silo investor. I understand and appreciate your concerns about on lease accounting effects for financial investors. I understand that. It is not my intention or desire to create unintended burdens or disadvantages for these taxpayers.

I have asked my staff to consider the alternative I

mentioned, and any other viable options to resolve the silo issue. As this process moves forward, I look forward to working with you to achieve a fair and equitable result. But the main bottom line is, these silos are not a good deal and we have got to make sure that they are not continued. But I certainly understand the financial concerns that you are making.

Senator Lincoln. Mr. Chairman?

Senator Crapo. Thank you, Mr. Chairman.

The Chairman. Thank you, Senator.

Yes. The Senator from Arkansas?

Senator Lincoln. Thank you, Mr. Chairman. I just want to thank you, the Ranking Member, and all of your staff for working with myself and Senator Crapo on this bill. Senator Crapo and I started working on this issue in a broader way early in the 109th Congress, and I think the bill that we are passing today represents a great deal of hard work and compromise that has resulted in a piece of legislation that I believe can really have a profound effect on the recovery of efforts around the country.

The Endangered Species Act has played such a crucial role in protecting threatened and endangered species and habitat, and really promoting species recovery. But we also know that on private lands, which are relied upon by

the majority of threatened species for their survival and recovery, the Act does not have all of those necessary tools and that is what we provide in this. We really fill the gap by this legislation.

The bill will encourage greater involvement of private landowners in the ESA process, something that will only help to help to achieve greater recovery of species. We really appreciate you and Senator Grassley, and all of your support throughout this process, of coming up with a good compromise and something that will move us forward. I especially thank my colleague from Idaho, because Senator Crapo has been great to work with and I feel good about what we have been able to do.

Thank you, Mr. Chairman.

The Chairman. Thank you, Senator. You are absolutely right. In fact, maybe we were a little bit quick in moving on his measure. I want to thank you, Senator, very much.

Senator Crapo. Thank you.

The Chairman. You have been a leader on this in trying to figure out a way that landowners can deal with the requirements in the Endangered Species Act, and it is very creative work that you have come up with, and it has been a pleasure for all of us to work with you.

Senator Crapo. Thank you, Mr. Chairman. May I

just also say, as we were moving so fast at the end there to avoid losing a quorum, I did omit to take the opportunity to thank Senator Lincoln. Without her help, this would not have happened. She has been a tremendous partner with me not only on this, but on a number of pieces of legislation. I just want to publicly thank her for the tremendous work that she does in this area.

The Chairman. Thank you. We have seven members. I ask consent that staff have authority to make changes for technical, conforming, and budgetary reasons to all measures that the committee has considered today. Without objection, so ordered.

[No response]

The Chairman. Once again, I thank all Senators. I thank all who have worked on all of this legislation, especially the staff. They have worked long, hard hours and worked hard to get compromises. WE are very grateful for your work. Thank you.

The committee is adjourned.

[Whereupon, at 9:38 a.m. the meeting was concluded.]

UNITED STATES SENATE
COMMITTEE ON FINANCE

Max Baucus, Chairman

Friday, September 21, 2007

219 Dirksen Senate Office Building

Agenda for Business Meeting

I. To review and make recommendations on proposed legislation implementing the U.S.-Peru Trade Promotion Agreement, as well as the associated proposed Statement of Administrative Action.

II. To consider an original bill entitled "American Infrastructure Investment and Improvement Act."

III. To consider an original bill entitled, "The Habitat and Land Conservation Act of 2007."

THE UNITED STATES – PERU TRADE PROMOTION AGREEMENT IMPLEMENTATION ACT

STATEMENT OF ADMINISTRATIVE ACTION

This Statement of Administrative Action ("Statement") is submitted to the Congress in compliance with section 2105(a)(1)(C)(ii) of the Bipartisan Trade Promotion Authority Act of 2002 ("TPA Act") and accompanies the implementing bill for the free trade agreement that the United States has concluded with Peru. The bill approves and makes statutory changes necessary or appropriate to implement the Agreement, which the United States Trade Representative signed on April 12, 2006, and amended through a Protocol signed in Washington, D.C. on June 24, 2007 and Lima on June 25, 2007.

As is the case with earlier Statements of Administrative Action submitted to the Congress in connection with fast-track bills, this Statement represents an authoritative expression by the Administration concerning its views regarding the interpretation and application of the Agreement, both for purposes of U.S. international obligations and domestic law. The Administration understands that it is the expectation of the Congress that future administrations will observe and apply the interpretations and commitments set out in this Statement. In addition, since this Statement will be approved by the Congress at the time it approves the implementing bill for this Agreement, the interpretation of the Agreement included in this Statement carries particular authority.

This Statement describes significant administrative actions proposed to implement U.S. obligations under the Agreement.

In addition, incorporated into this Statement are two other statements required under section 2105(a) of the TPA Act: (1) an explanation of how the implementing bill and proposed administrative action will change or affect existing law; and (2) a statement setting forth the reasons why the implementing bill and proposed administrative action are necessary or appropriate to carry out the Agreement. The Agreement does not change the provisions of any agreement the United States has previously negotiated with Peru.

For ease of reference, this Statement generally follows the organization of the Agreement, with the exception of grouping the general provisions of the Agreement (Chapters One and Nineteen through Twenty-Three) at the beginning of the discussion.

For each chapter of the Agreement, the Statement describes the pertinent provisions of the implementing bill, explaining how the bill changes or affects existing law, and stating why those provisions are necessary or appropriate to implement the Agreement. The Statement then describes the administrative action proposed to implement the particular chapter of the Agreement, explaining how the proposed action changes existing administrative practice or authorizes further action and stating why such actions are necessary or appropriate to implement

the Agreement.

It should be noted that this Statement does not, for the most part, discuss those many instances in which U.S. law or administrative practice will remain unchanged under the Agreement. In many cases, U.S. laws and regulations are already in conformity with the obligations assumed under the Agreement.

Finally, references in this Statement to particular sections of U.S. statutes are based on those statutes in effect as of the date this Statement was submitted to the Congress.

Chapters:
One (Initial Provisions and General Definitions)
Nineteen (Transparency)
Twenty (Administration of the Agreement and Trade Capacity Building)
Twenty-One (Dispute Settlement)
Twenty-Two (Exceptions)
Twenty-Three (Final Provisions)

1. Implementing Bill

a. Congressional Approval

Section 101(a) of the implementing bill provides Congressional approval for the Agreement and this Statement, as required by sections 2103(b)(3) and 2105(a)(1) of the TPA Act.

b. Entry into Force

Article 23.4 requires the United States and Peru to exchange written notifications that their respective legal requirements for the entry into force of the Agreement have been fulfilled. The exchange of notifications is a necessary condition for the Agreement's entry into force. Section 101(b) of the implementing bill authorizes the President to exchange notes with Peru to provide for the Agreement to enter into force for the United States on or after January 1, 2008. The exchange of notes is conditioned on a determination by the President that Peru has taken measures necessary to comply with those of its obligations that are to take effect at the time the Agreement enters into force.

Certain provisions of the Agreement become effective after the Agreement enters into force. For example, the Agreement provides Peru up to three years to comply with certain provisions relating to customs administration. Likewise, the Agreement allots Peru 18 months to begin carrying out certain transparency provisions governing financial services measures. In addition, the Agreement's obligations regarding intellectual property rights, specifically those governing the ratification of certain international agreements, patent restoration, and the enforcement of certain copyright protections apply to Peru at prescribed times after the Agreement enters into force.

c. Relationship to Federal Law

Section 102(a) of the bill establishes the relationship between the Agreement and U.S. law. The implementing bill, including the authority granted to federal agencies to promulgate implementing regulations, is intended to bring U.S. law fully into compliance with U.S. obligations under the Agreement. The bill accomplishes that objective with respect to federal legislation by amending existing federal statutes that would otherwise be inconsistent with the Agreement and, in certain instances, by creating entirely new provisions of law.

Section 102(a) clarifies that no provision of the Agreement will be given effect under domestic law if it is inconsistent with federal law, including provisions of federal law enacted or amended by the bill. Section 102(a) will not prevent implementation of federal statutes consistent with the Agreement, where permissible under the terms of such statutes. Rather, the section reflects the Congressional view that necessary changes in federal statutes should be specifically enacted rather than provided for in a blanket preemption of federal statutes by the Agreement.

The Administration has made every effort to include all laws in the implementing bill and to identify all administrative actions in this Statement that must be changed in order to conform with the new U.S. rights and obligations arising from the Agreement. Those include both regulations resulting from statutory changes in the bill itself and changes in laws, regulations, rules, and orders that can be implemented without a change in the underlying U.S. statute.

Accordingly, at this time it is the expectation of the Administration that no changes in existing federal law, rules, regulations, or orders other than those specifically indicated in the implementing bill and this Statement will be required to implement the new international obligations that the United States will assume under the Agreement. This is without prejudice to the President's continuing responsibility and authority to carry out U.S. law and agreements. As experience under the Agreement is gained over time, other or different administrative actions may be taken in accordance with applicable law to implement the Agreement. If additional action is called for, the Administration will seek legislation from Congress or, if a change in regulation is required, follow normal agency procedures for amending regulations.

d. Relationship to State Law

The Agreement's rules generally cover state and local laws and regulations, as well as those at the federal level. There are a number of exceptions to, or limitations on, this general rule, however, particularly in the areas of government procurement, labor and environment, investment, and cross-border trade in services and financial services.

The Agreement does not automatically "preempt" or invalidate state laws that do not conform to the Agreement's rules, even if a dispute settlement panel were to find a state measure inconsistent with the Agreement. The United States is free under the Agreement to determine how it will conform with the Agreement's rules at the federal and non-federal level. The

Administration is committed to carrying out U.S. obligations under the Agreement, as they apply to the states, through the greatest possible degree of state-federal consultation and cooperation.

Section 102(b)(1) of the bill makes clear that only the United States is entitled to bring an action in court in the event that there is an unresolved conflict between a state law, or the application of a state law, and the Agreement. The authority conferred on the United States under this paragraph is intended to be used only as a "last resort," in the unlikely event that efforts to achieve consistency through consultations have not succeeded.

The reference in section 102(b)(2) of the bill to the business of insurance is required by virtue of section 2 of the McCarran-Ferguson Act (15 U.S.C. 1012). That section states that no federal statute shall be construed to supersede any state law regulating or taxing the business of insurance unless the federal statute "specifically relates to the business of insurance." Certain provisions of the Agreement (for example, Chapter Twelve, relating to financial services) do apply to state measures regulating the insurance business, although "grandfathering" provisions in Chapter Twelve exempt existing inconsistent (*i.e.*, "non-conforming") measures.

Given the provision of the McCarran-Ferguson Act, the implementing act must make specific reference to the business of insurance in order for the Agreement's provisions covering the insurance business to be given effect with respect to state insurance law. Insurance is otherwise treated in the same manner under the Agreement and the implementing bill as other financial services under the Agreement.

e. Private Lawsuits

Section 102(c) of the implementing bill precludes any private right of action or remedy against a federal, state, or local government, or against a private party, based on the provisions of the Agreement. A private party thus could not sue (or defend a suit against) the United States, a state, or a private party on grounds of consistency (or inconsistency) with the Agreement. The provision also precludes a private right of action attempting to require, preclude, or modify federal or state action on grounds such as an allegation that the government is required to exercise discretionary authority or general "public interest" authority under other provisions of law in conformity with the Agreement.

With respect to the states, section 102(c) represents a determination by the Congress and the Administration that private lawsuits are not an appropriate means for ensuring state compliance with the Agreement. Suits of this nature may interfere with the Administration's conduct of trade and foreign relations and with suitable resolution of disagreements or disputes under the Agreement.

Section 102(c) does not preclude a private party from submitting a claim against the United States to arbitration under Chapter Ten (Investment) of the Agreement or seeking to enforce an award against the United States issued pursuant to such arbitration. The provision also would not preclude any agency of government from considering, or entertaining argument

on, whether its action or proposed action is consistent with the Agreement, although any change in agency action would have to be consistent with domestic law.

f. Implementing Regulations

Section 103(a) of the bill provides the authority for new or amended regulations to be issued, and for the President to proclaim actions implementing the provisions of the Agreement, as of the date the Agreement enters into force. Section 103(b) of the bill requires that, whenever possible, all federal regulations required or authorized under the bill and those proposed in this Statement as necessary or appropriate to implement immediately applicable U.S. obligations under the Agreement are to be developed and promulgated within one year of the Agreement's entry into force. In practice, the Administration intends, wherever possible, to amend or issue the other regulations required to implement U.S. obligations under the Agreement at the time the Agreement enters into force. The process for issuing regulations pursuant to this authority will comply with the requirements of the Administrative Procedures Act, including requirements to provide notice of and an opportunity for public comment on such regulations. If issuance of any regulation will occur more than one year after the date provided in section 103(b), the officer responsible for issuing such regulation will notify the relevant committees of both Houses of Congress of the delay, the reasons for such delay, and the expected date for issuance of the regulation. Such notice will be provided at least 30 days prior to the end of the one-year period.

g. Dispute Settlement

Section 105(a) of the bill authorizes the President to establish within the Department of Commerce an office responsible for providing administrative assistance to dispute settlement panels established under Chapter Twenty-One of the Agreement. This provision enables the United States to implement its obligations under Article 20.3.1 of the Agreement. This office will not be an "agency" within the meaning of 5 U.S.C. 552, consistent with treatment provided under other U.S. free trade agreements, including the North American Free Trade Agreement ("NAFTA") and free trade agreements with Australia, Chile, and Singapore, Morocco, Bahrain, and Oman. Thus, for example, the office will not be subject to the Freedom of Information Act or the Government in the Sunshine Act. Since they are international bodies, panels established under Chapter Twenty-One are not subject to those acts.

Section 105(b) of the bill authorizes the appropriation of funds to support the office established pursuant to section 105(a).

h. Effective Dates

Section 107(b) of the bill provides that the first three sections of the bill as well as Title I of the bill go into effect when the bill is enacted into law.

Section 107(a) provides that the other provisions of the bill and the amendments to other statutes made by the bill take effect on the date on which the Agreement enters into force.

Section 107(c) provides that the provisions of the bill (other than section 107(c) itself) and the amendments to other statutes made by the bill will cease to have effect on the date on which the Agreement terminates.

2. Administrative Action

No administrative changes will be necessary to implement Chapters One, Twenty, Twenty-Two, and Twenty-Three.

Article 19.1.1 of the Agreement requires each government to designate a contact point to facilitate communications regarding the Agreement. The Office of the United States Trade Representative ("USTR") will serve as the U.S. contact point for this purpose.

The Agreement calls for the United States and Peru to develop rosters of independent experts willing to serve as panelists to settle disputes between the parties that may arise under the Agreement. One roster will be available for most types of disputes, while a specialized roster will be established to address disputes regarding the Agreement's financial services provisions. USTR will consult with the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate ("Trade Committees") as it develops rosters of panelists. USTR will provide the Trade Committees with the names of the experts it is considering, and detailed background information on each, at least 30 days before submitting the names of any nominees to Peru.

Chapter Two (National Treatment and Market Access for Goods)

1. Implementing Bill

a. Proclamation Authority

Section 201(a)(1) of the bill grants the President authority to implement by proclamation U.S. rights and obligations under Chapter Two of the Agreement through the application or elimination of customs duties and tariff-rate quotas ("TRQs"). Section 201(a)(1) authorizes the President to:

- modify or continue any duty;
- keep in place duty-free or excise treatment; or
- impose any duty

that the President determines to be necessary or appropriate to carry out or apply Articles 2.3, 2.5, 2.6, 3.3.13, and Annex 2.3 of the Agreement.

The proclamation authority with respect to Article 2.3 authorizes the President to provide for the continuation, phase-out, and elimination, according to the Schedule of the United States to Annex 2.3 of the Agreement, of customs duties on imports from Peru that meet the Agreement's rules of origin.

The proclamation authority with respect to Articles 2.5 and 2.6 authorizes the President to provide for the elimination of duties on particular categories of imports from the other Agreement countries. Article 2.5 pertains to the temporary admission of certain goods, such as commercial samples, goods intended for display at an exhibition, and goods necessary for carrying out the business activity of a person who qualifies for temporary entry into the United States. Article 2.6 pertains to the importation of goods: (i) returned to the United States after undergoing repair or alteration in Peru; or (ii) sent from Peru for repair or alteration in the United States.

Sections 201(a)(2) of the bill address the status of Peru as a designated beneficiary country under the Generalized System of Preferences.

Section 201(a)(2) of the bill requires the President to withdraw beneficiary country status under the Generalized System of Preferences from Peru on the date the Agreement takes effect.

Section 201(b) of the bill authorizes the President, subject to the consultation and layover provisions of section 104 of the bill, to:

- modify or continue any duty;
- modify the staging of any duty elimination set out in Annex 2.3, pursuant to an agreement with Peru under Article 2.3.4;
- keep in place duty-free or excise treatment; or
- impose any duty

by proclamation whenever the President determines it to be necessary or appropriate to maintain the general level of reciprocal and mutually advantageous concessions with respect to Peru provided by the Agreement.

Section 104 of the bill sets forth consultation and layover steps that must precede the President's implementation of any duty modification by proclamation. This would include, for example, modifications of duties under section 201(b) of the bill. Under the consultation and layover provisions, the President must obtain the advice of the appropriate private sector advisory committees (pursuant to section 135 of the Trade Act of 1974) and the ITC on the proposed action. The President must submit a report to the Trade Committees setting forth the action proposed, the reasons for the proposed action, and the advice of the private sector and the ITC. The bill sets aside a 60-day period following the date of transmittal of the report for the

President to consult with the Trade Committees on the action. Following the expiration of the 60-day period, the President may proclaim the action.

The President may initiate the consultation and layover process under section 104 of the bill on enactment of the bill. However, under section 103(a), any modifying proclamation cannot take effect until the Agreement enters into force. In addition to modifications of customs duties, these provisions apply to other Presidential proclamation authority provided in the bill that is subject to consultation and layover, such as authority to implement a proposal to modify the Agreement's specific rules of origin pursuant to an agreement with Peru under Article 4.14 of the Agreement.

Section 201(c) of the bill provides for the conversion of existing specific or compound rates of duty for various goods to *ad valorem* rates for purposes of implementing the Agreement's customs duty reductions. (A compound rate of duty for a good would be a rate of duty stated, for example, as the sum of X dollars per kilogram plus Y percent of the value of the good.)

Section 201(d) of the bill directs the President to take such action as may be necessary to ensure that imports of goods subject to TRQs do not disrupt the orderly marketing of commodities in the United States. This provision will be implemented consistent with Article 2.15 of the Agreement. Any agency action pursuant to this provision will be taken in accordance with regulations promulgated after providing notice and opportunity for public comment.

b. Agricultural Safeguard

Section 202 of the bill implements the agricultural safeguard provisions of Article 2.18 and Annex 2.18 of the Agreement. Article 2.18 permits the United States to impose an "agricultural safeguard measure," in the form of additional duties, on imports of certain goods of Peru specified in the Schedule of the United States to Annex 2.18 of the Agreement that exceed the volume thresholds set out in that annex.

Section 202(a) of the bill provides the overall contour of the agricultural safeguard rules, including definitions of terms used in the agricultural safeguard provisions. Section 202(a)(1) defines the applicable normal trade relations (most-favored-nation) ("NTR (MFN)") rate of duty for purposes of the agricultural safeguard. Under the Agreement, the sum of the duties assessed under an agricultural safeguard and the applicable rate of duty in the Schedule of the United States to Annex 2.3 of the Agreement may not exceed the general NTR (MFN) rate of duty.

Section 202(a)(2) of the bill defines the "schedule rate of duty" for purposes of the agricultural safeguard as the rate of duty for a good set out in the Schedule of the United States to Annex 2.3 of the Agreement.

Section 202(a)(3) of the bill specifies the products that may be subject to an agricultural safeguard measure. These goods must qualify as originating goods under section 203, except

that operations performed in or material obtained from the United States will be considered as if the operations were performed in, and the material was obtained from, a country that is not a party to the Agreement.

Section 202(b) of the bill provides for the Secretary to impose agricultural safeguard duties and explains how the additional duties are to be calculated. The additional duties are triggered in any year when the volume of imports of the good from an Agreement country exceeds 130 percent of the in-quota quantity allocated to Peru for the good in that calendar year in the Schedule of the United States to Annex 2.3 of the Agreement. (The in-quota quantities for goods are set out in the Schedule of the United States to Annex 2.3 of the Agreement on a calendar-year basis beginning with "year one." Year one refers to the calendar year in which the Agreement enters into force.) The additional duties remain in effect only until the end of the calendar year in which they are imposed.

Section 202(b)(3) of the bill implements Article 2.18.6 of the Agreement by directing the Secretary of the Treasury (the "Secretary") within 60 days of the date on which the Secretary first assesses an agricultural safeguard duty on a good to notify Peru and provide it with supporting data.

Section 202(c) of the bill implements Article 2.18.4 of the Agreement by establishing that no additional duty may be applied on a good if, at the time of entry, the good is subject to a safeguard measure under the procedures set out in Subtitle A of Title III of the bill or under the safeguard procedures set out in chapter 1 of Title II of the Trade Act of 1974.

Section 202(d) of the bill provides that the agricultural safeguard provision ceases to apply with respect to a good on the date on which duty-free treatment must be provided to that good under the Schedule of the United States to Annex 2.3 of the Agreement.

c. Customs User Fees

Section 204 of the bill implements U.S. commitments under Article 2.10.4 of the Agreement, regarding customs user fees on originating goods, by amending section 13031(b) of the Consolidated Omnibus Budget Reconciliation Act of 1985 (19 U.S.C. 58c(b)). The amendment provides for the immediate elimination of the merchandise processing fee for goods qualifying as originating goods under Article 3.3, Annex 3-A or Chapter Four of the Agreement. Customs processing of goods qualifying as originating goods under the Agreement will be financed by money from the General Fund of the Treasury. This is necessary to ensure that the United States complies with obligations under the General Agreement on Tariffs and Trade 1994 by limiting fees charged for the processing of non-originating imports to amounts commensurate with the processing services provided. That is, fees charged on such non-originating imports will not be used to finance the processing of originating imports.

2. Administrative Action

a. Temporary Admission of Goods and Goods Entered After Repair or Alteration

As discussed above, section 201(a)(1) of the bill authorizes the President to proclaim duty-free treatment for certain goods to carry out Article 2.5 (temporary admission of certain goods) and Article 2.6 (repair or alteration of certain goods) of the Agreement. The Secretary will issue regulations to carry out this portion of the proclamation.

b. Agricultural Safeguard

The Secretary will issue regulations implementing the agricultural safeguard provisions of section 202. It is the Administration's intent that agricultural safeguard measures will be applied whenever the volume thresholds specified in the Agreement have been met.

Chapter Three (Textiles and Apparel)

1. Implementing Bill

a. Handloomed, Handmade, or Folklore Articles

The proclamation authority granted to the President under section 201(a)(1) includes authority to implement Article 3.3.13 of the Agreement by providing duty-free treatment for Peruvian textile or apparel articles that the United States and Peru agree are handloomed, handmade, or folklore articles, and are certified as such by Peru's competent authority.

b. Textile or Apparel Safeguard

Article 3.1 of the Agreement makes remedies available to domestic textile and apparel industries that have sustained or are threatened by serious damage from imports of textile or apparel goods for which duties have been reduced or eliminated under the Agreement. It also sets forth procedures for obtaining such remedies. The Administration does not anticipate that the Agreement will result in injurious increases in textile or apparel imports from the other Agreement countries. Nevertheless, the Agreement's textile or apparel safeguard procedure will ensure that relief is available if needed.

The safeguard mechanism applies when, as a result of the reduction or elimination of a customs duty under the Agreement, textile or apparel goods of Peru are being imported into the United States in such increased quantities, in absolute or relative terms, and under such conditions as to cause serious damage or actual threat thereof to a U.S. industry producing like or directly competitive goods. In these circumstances, Article 3.1 permits the United States to increase duties on the imported goods to a level that does not exceed the lesser of the prevailing

U.S. NTR (MFN) duty rate for the good or the U.S. NTR (MFN) duty rate in effect at the time the Agreement entered into force.

Subtitle B of Title III of the bill (sections 321 through 328) implements the Agreement's textile and apparel safeguard.

Section 321(a) establishes that an interested party may file a request for a textile or apparel safeguard measure with the President, who must review the request to determine whether to commence consideration of the request on its merits. Under section 321(b), if the President determines that the request contains information necessary to warrant consideration on the merits, the President must provide notice in the *Federal Register* stating that the request will be considered and seeking public comments on the request. The notice will contain a summary of the request itself and the dates by which comments and rebuttals must be received. Subject to protection of confidential business information, if any, the full text of the request will be made available on the Department of Commerce, International Trade Administration's website.

Section 322 sets out the procedures to be followed in considering the request. Section 322(a)(1) of the bill provides for the President to determine whether, as a result of the reduction or elimination of a duty provided for under the Agreement, a "Peruvian textile or apparel article" is being imported into the United States in such increased quantities, in absolute terms or relative to the domestic market for that article, and under such conditions that imports of the article cause serious damage, or actual threat thereof, to a domestic industry producing an article that is like, or directly competitive with, the imported article. Section 301(2) of the bill defines "Peruvian textile or apparel article" to mean an article listed in the Annex to the World Trade Organization ("WTO") Agreement on Textiles and Clothing (other than a good listed in Annex 3-C of the Agreement) that qualifies as an originating good under section 203(b) of the bill. The President's determination corresponds to the determination required under Article 3.1.1 of the Agreement. Section 322(a)(2) of the bill includes criteria for determining serious damage or actual threat thereof, consistent with Article 3.1.2 of the Agreement.

Section 322(b) of the bill identifies the relief that the President may provide to a U.S. industry that the President determines is facing serious damage or actual threat thereof. Such relief may consist of an increase in tariffs to the lesser of: (i) the NTR (MFN) duty rate in place for the textile or apparel article at the time the relief is granted; or (ii) the NTR (MFN) duty rate for that article on the day before the Agreement entered into force.

Section 323 of the bill provides that the maximum period of relief under the textile or apparel safeguard shall be three years in the aggregate. The initial period of import relief may be up to two years. The President may extend the relief for up to one year, however, if he determines that continuation is necessary to remedy or prevent serious damage and to facilitate adjustment, and that the domestic industry is, in fact, adjusting to import competition.

Section 324 of the bill provides that relief may not be granted to an article under the textile and apparel safeguard if: (i) relief previously has been granted to that article under the

textile and apparel safeguard; or (ii) the article is subject, or becomes subject, to a safeguard measure under (a) Chapter Eight of the Agreement (corresponding to Subtitle A of Title III of the bill), or (b) chapter 1 of Title II of the Trade Act of 1974.

Section 325 of the bill provides that on the date import relief terminates, imports of the textile or apparel article that was subject to the safeguard action will be subject to the rate of duty that would have been in effect on that date in the absence of the relief.

Section 326 of the bill provides that authority to provide relief under the textile and apparel safeguard will expire five years after the date on which the Agreement enters into force.

Under Article 3.1.7 of the Agreement, if the United States provides relief to a domestic industry under the textile and apparel safeguard, it must provide Peru "mutually agreed trade liberalizing compensation in the form of concessions having substantially equivalent trade effects or equivalent to the value of the additional duties expected to result from the [safeguard]." If the United States and Peru are unable to agree on trade liberalizing compensation, that country may increase tariffs equivalently on U.S. goods. The obligation to provide compensation (and the right to increase tariffs absent agreement on compensation) terminates when the safeguard relief ends.

Section 123 of the Trade Act of 1974 (19 U.S.C. 2133), as amended, authorizes the President to provide trade compensation for global safeguard measures taken pursuant to chapter 1 of title II of the Trade Act of 1974. Section 327 of the implementing bill extends that authority to measures taken pursuant to the Agreement's textile or apparel safeguard provisions.

Finally, section 328 of the bill provides that confidential business information submitted in the course of consideration of a request for a textile or apparel safeguard may not be released absent the consent of the party providing the information. It also provides that a party submitting confidential business information in a textile or apparel safeguard proceeding must submit a non-confidential version of the information or a summary of the information.

c. Enforcement of Textile and Apparel Rules of Origin

In addition to lowering barriers to trade in textile and apparel goods, the Agreement includes anti-circumvention provisions designed to ensure the accuracy of claims of origin and to prevent circumvention of laws, regulations, and procedures affecting such trade. Article 3.2 of the Agreement provides for verifications to determine the accuracy of claims of origin for textile or apparel goods, and to determine that exporters and producers are complying with applicable laws, regulations, and procedures regarding trade in textile or apparel goods.

Under Articles 3.2.3 and 3.2.4 of the Agreement, at the request of the United States, the government of Peru must conduct a verification. The object of a verification under Article 3.2.3(a)(i) is to determine whether a claim of origin for a textile or apparel good is accurate. The object of a verification under Article 3.2.3(a)(ii) is to determine whether an exporter or producer

is complying with applicable customs laws, regulations, and procedures regarding trade in textile or apparel goods, including those implementing international agreements. The United States may assist in the verification or, at the request of the government of Peru, conduct the verification itself. A verification may entail visits by officials of Peru and the United States to the premises of a textile or apparel exporter or producer in Peru.

Pursuant to Article 3.2.7 of the Agreement, the United States may take appropriate action during and after a verification, including, depending on the nature of the verification, by suspending or denying preferential tariff treatment for textile or apparel goods exported or produced by the person subject to the verification, detaining the goods, or denying them entry into the United States.

Section 208 of the bill implements Article 3.2 of the Agreement. Under section 208(a), the President may direct the Secretary to take "appropriate action" while a verification that the Secretary has requested is being conducted. Section 208(b) provides that, depending on the nature of the verification, the action may include: (i) suspending preferential tariff treatment for textile or apparel goods that the person subject to the verification has produced or exported if the Secretary believes there is insufficient information to sustain a claim for such treatment; (ii) denying preferential tariff treatment to such goods if the Secretary decides that a person has provided incorrect information to support a claim for such treatment; (iii) detaining such goods if the Secretary considers there is not enough information to determine their country of origin; and (iv) denying entry to such goods if the Secretary determines that a person has provided incorrect information on their origin.

Under section 208(c), the President may also direct the Secretary to take "appropriate action" after a verification has been completed. Under section 208(d), depending on the nature of the verification, the action may include: (i) denying preferential tariff treatment under the Agreement to textile or apparel goods that the person subject to the verification has exported or produced if the Secretary considers there is insufficient information to support a claim for such treatment or determines that a person has provided incorrect information to support a claim for such treatment; and (ii) denying entry to such goods if the Secretary decides that a person has provided incorrect information regarding their origin or that there is insufficient information to determine their origin. Unless the President sets an earlier date, any such action may remain in place until the Secretary obtains enough information to decide whether the exporter or producer that was subject to the verification is complying with applicable customs rules or whether a claim that the goods qualify for preferential tariff treatment or originate in an Agreement country is accurate.

Under section 208(e), the Secretary may publish the name of person that the Secretary has determined: (i) is engaged in circumvention of applicable laws, regulations, or procedures affecting trade in textile or apparel goods; or (ii) has failed to demonstrate that it produces, or is capable of producing, textile or apparel goods.

d. Fabrics, Yarns, or Fibers Not Available in Commercial Quantities

Under the specific rules of origin for textile and apparel goods set out in Annex 3-A of the Agreement, fabrics, yarns, or fibers that are not available in commercial quantities in a timely manner in the United States and Peru are treated as if they originate in the United States or Peru, regardless of their actual origin, when used as inputs in the production of textile or apparel goods. Annex 3-B lists certain fabrics, yarns, and fibers that the governments of the United States and Peru have collectively agreed are unavailable in the region.

In addition, Article 3.3.5 of the Agreement provides that the United States may add fabrics, yarns, or fibers to the list in certain circumstances. First, Article 3.3.5(e) of the Agreement provides that the United States may, after consultations with Peru add any fabrics or yarns that it has determined under its regional trade preference programs before the Agreement enters into force to be unavailable in the United States in commercial quantities in a timely manner. These regional trade preference program provisions are set out in: section 112(b)(5)(B) of the African Growth and Opportunity Act (19 U.S.C. § 3721(b)), section 204(b)(3)(B)(ii) of the Andean Trade Preference Act (19 U.S.C. § 3203(b)(3)(B)(ii)), and section 213(b)(2)(A)(v)(II) of the Caribbean Basin Economic Recovery Act (19 U.S.C. § 2703(b)(2)(A)(v)(II)).

Second, if the United States determines, at the request of an "interested entity" (a potential or actual purchaser or seller, or the government of Peru), that a fabric, yarn, or fiber is unavailable in commercial quantities in a timely manner in Peru and the United States, or if it determines that no interested entity objects to the request, the United States will add the material to the list – in a restricted or unrestricted quantity. In addition, within six months of adding a material to the list in Annex 3-B, the United States may remove any restriction it has imposed on the product.

Article 3.3.6 authorizes the United States, in response to a request from an interested entity, either to remove a material from the list or impose a restriction on any material it has added to the list in an unrestricted quantity. The United States may take this action beginning six months after it determines, in response to a request, that the material has become commercially available in Peru or the United States.

Section 203(o)(2) of the bill provides authority for the President to carry out the provision in Article 3.3.5(e) of the Agreement pursuant to which the United States may, after consultations with Peru, add materials to the list that it has determined are unavailable in commercial quantities in a timely manner in the United States under its regional trade preference programs (the African Growth and Opportunity Act, the Andean Trade Preference Act, and the Caribbean Basin Economic Recovery Act) before the Agreement enters into force.

Section 203(o)(4) of the bill implements those provisions of Article 3.3 that provide for the United States to modify the list of materials in Annex 3-B after the Agreement enters into force.

Specifically, subparagraph (C)(i) provides that an interested entity may request the

President to determine that a fabric, yarn, or fiber is not available in commercial quantities in Peru and the United States and to proclaim that the material is included in the list in Annex 3-B.

Subparagraph (C)(ii) authorizes the President to determine whether the material is commercially available in a timely manner in Peru or the United States. Subparagraph (C)(iii) provides that if the President determines that the material is not commercially available in a timely manner in Peru and the United States, or if no interested entity has objected, he may issue a proclamation adding the fabric, yarn, or fiber to the Annex 3-B list in a restricted or unrestricted quantity. The President normally must issue the proclamation within 30 business days of receiving a request. However, subparagraph (C)(iv)(II) provides that the President may take up to 44 business days if the President decides he lacks sufficient information to make the determination within 30 business days. Subparagraph (C)(v) provides for proclamations to take effect when published in the *Federal Register.*

Subparagraph (C)(vi) provides that within six months after adding a fabric, yarn, or fiber to the list in Annex 3-B in a restricted quantity, the President may eliminate the restriction if he determines that the fabric, yarn, or fiber is not available in commercial quantities in a timely manner in the territory of Peru and the United States.

Subparagraph (D) implements Article 3.3.5(c) of the Agreement. It provides that in the unlikely event that the President takes no action in response to a request to add a material to the list, the material is automatically added in an unrestricted quantity beginning 45 business days after the request was submitted, or 60 days after the request was submitted if the President has determined under subparagraph (C)(iv) that he lacks sufficient information to make the determination within 30 business days.

Under subparagraph (E)(i), an interested entity may request the President to limit the amount of any fabric, yarn, or fiber that the United States has included on the list in Annex 3-B in an unrestricted quantity, or to remove such a material from the list entirely. Under subparagraph (E)(ii), an interested entity may submit such a request beginning six months after the product was placed on the list in an unrestricted amount. Subparagraph (E)(iii) provides for the President to issue a proclamation carrying out a request if he determines within 30 business days after the request is submitted that the material is available in commercial quantities in a timely manner in Peru or the United States. Subparagraph (E)(iv) provides that this type of proclamation may take effect no earlier than six months after it is published in the *Federal Register.*

Subparagraph (F) calls for the President to establish procedures for interested entities to submit requests for changes in the Annex 3-B list and to submit comments and supporting evidence before the President determines whether to change the list.

2. Administrative Action

a. Handloomed, Handmade, or Folklore Articles

The President will authorize the Committee for the Implementation of Textile Agreements ("CITA") to consult with Peru to determine which, if any, textile or apparel goods from Peru will be treated as handloomed, handmade, or folklore articles. CITA is an interagency entity created by Executive Order 11651 that carries out U.S. textile trade policies, as directed by the President. The President will delegate to CITA his authority under the bill to provide duty-free treatment for these articles.

b. Textile and Apparel Safeguard

CITA will perform the function of receiving requests for textile or apparel safeguard measures under section 321 of the bill, making determinations of serious damage or actual threat thereof under section 322(a), and providing relief under section 322(b). CITA will issue procedures for requesting such safeguard measures, for making its determinations under section 322(a), and for providing relief under section 322(b). CITA will perform these functions pursuant to a delegation of the President's authority under the bill.

c. Enforcement of Textile and Apparel Rules of Origin

Section 208 of the bill provides that the Secretary may request Peru to initiate verifications in order to determine whether claims of origin for textile or apparel goods are accurate or whether exporters and producers are complying with applicable laws, regulations, and procedures regarding trade in textile or apparel goods. The President will delegate to CITA his authority under the bill to direct appropriate U.S. officials to take an action described in section 208(b) of the bill while such a verification is being conducted. The President will also authorize CITA to direct pertinent U.S. officials to take an action described in section 208(d) after a verification is completed. If CITA decides that it is appropriate to deny preferential tariff treatment or deny entry to particular goods, CITA will issue an appropriate directive to U.S. Customs and Border Protection (CBP).

Section 208 of the bill provides the exclusive basis in U.S. law for CITA to direct appropriate action implementing Article 3.2 of the Agreement.

d. Fabrics, Yarns, or Fibers Not Available in Commercial Quantities

The President will delegate to CITA his authority under section 203(o)(4) of the bill, which establishes procedures for changing the list of fabrics, yarns, or fibers not available in commercial quantities in a timely manner in Agreement countries set out in Annex 3-B of the Agreement.

CITA will publish procedures under which interested entities may request that CITA: (i) add a fabric, yarn, or fiber to the list in Annex 3-B; (ii) eliminate a restriction on a fabric, yarn, or fiber within six months after the item was added to the list in a restricted quantity; (iii) remove a fabric, yarn, or fiber from the list; or (iv) restrict the quantity of a fabric, yarn, or fiber that was added to the list in an unrestricted quantity or with respect to which CITA previously eliminated a restriction. These procedures will set out the information required to be submitted with a request. CITA will publish notice of requests that meet these requirements. CITA will provide an opportunity for interested entities to submit comments and evidence regarding a request, and to rebut evidence that other interested entities have submitted, before CITA makes a determination.

CITA will make determinations under section 203(o)(4) on a case-by-case basis taking into account factors relevant to the request. Such factors ordinarily would include the physical and technical specifications of the fabric, yarn, or fiber that is the subject of the request, as well as evidence demonstrating the extent to which manufacturers in Peru or the United States are able to supply the item in commercial quantities in a timely manner. CITA will provide public notice of its determinations.

Chapter Four (Rules of Origin)

1. Implementing Bill

a. General

Section 203 of the implementing bill codifies the general rules of origin set forth in Chapter Four of the Agreement. These rules apply only for the purposes of this bill and for the purposes of implementing the customs duty treatment provided under the Agreement. An originating good for the purposes of this bill would not necessarily be a good of or import from Peru for the purposes of other U.S. laws or regulations.

Under the general rules, there are three basic ways for a good of Peru to qualify as an "originating" good, and therefore be eligible for preferential treatment when it is imported into the United States. First, a good is originating if it is "wholly obtained or produced entirely in the territory of Peru, the United States, or both." The term "good wholly obtained or produced entirely in the territory of Peru, the United States, or both" is defined in section 203(n)(5) of the bill and includes, for example, minerals extracted from the territory of Peru, the United States, or

both, animals born and raised in the territory of Peru, the United States, or both, and waste and scrap derived from production of goods that takes place in the territory of Peru, the United States, or both.

The term "good wholly obtained or produced entirely in the territory of Peru, the United States, or both" includes "recovered goods." These are parts resulting from the disassembly of used goods that are brought into good working condition in order to be combined with other recovered goods and other materials to form a "remanufactured good." The term "remanufactured good" is separately defined in section 203(n)(20) to mean an industrial good assembled in the territory of Peru or the United States, or both, and falling within Chapter 84, 85, 87 or 90 of the HTS or heading 9402 (with the exception of goods under heading 8418 or 8516) that: (i) is entirely or partially comprised of recovered goods; and (ii) has a similar life expectancy and enjoys a factory warranty similar to such a good that is new.

Second, the general rules of origin provide that a good is "originating" if the good is produced in the territory of Peru, the United States, or both, and the materials used to produce the good that are not themselves originating goods are transformed in such a way as to cause their tariff classification to change and to meet other requirements, as specified in Annex 3-A or Annex 4.1 of the Agreement. Such additional requirements include, for example, performing certain processes or operations related to textile or apparel goods in the territory of Peru, the United States, or both, or meeting regional value content requirements, sometimes in conjunction with changes in tariff classification.

Third, the general rules of origin provide that a good is "originating" if the good is produced entirely in the territory of Peru, the United States, or both, exclusively from materials that themselves qualify as originating goods.

The remainder of section 203 of the implementing bill sets forth specific rules related to determining whether a good meets the Agreement's specific requirements to qualify as an originating good. For example, section 203(c) implements provisions in Annex 4.1 of the Agreement that require certain goods to have at least a specified percentage of "regional value content" to qualify as originating goods. It prescribes alternative methods for calculating regional value content, as well as a specific method that may be used in the case of certain automotive goods. Section 203(f) provides that a good is not disqualified as an originating good if it contains *de minimis* quantities of non-originating materials that do not undergo a change in tariff classification. Other provisions in section 203 address how materials are to be valued, how to determine whether fungible goods and materials qualify as originating or non-originating, as well as a variety of other matters.

Section 203(l) allows a good to be shipped through a third country without losing its status as an originating good, provided certain conditions are met. While in a third country, the good may not be further produced, except that it may be unloaded, reloaded, or preserved, if necessary. Whether the good is unloaded, reloaded, or preserved in a third country, or is simply

shipped through the third country, the good must, while in that country, remain under customs control.

Section 203(l) recognizes that, in modern commerce, a good may not be directly shipped from Peru to the United States, or vice versa; for example, shipments may be consolidated at an interim port. At the same time, in order to ensure that the preferential tariff treatment under the Agreement inures to producers in Peru and the United States, rather than producers in third countries, an originating good may not be further produced in a country that is not a party to the Agreement. Requiring the good to remain under customs control provides greater traceability of the good to ensure that no further production occurred.

b. Proclamation Authority

Section 203(o)(1) of the bill authorizes the President to proclaim the specific rules of origin in Annex 3-A and Annex 4.1 of the Agreement, as well as any additional subordinate rules necessary to carry out the customs duty provisions of the bill consistent with the Agreement. In addition, section 203(o)(3) gives authority to the President to modify certain of the Agreement's specific origin rules by proclamation, subject to the consultation and layover provisions of section 104 of the bill. (See item 1.a of Chapter Two, above.)

Various provisions of the Agreement expressly contemplate that Peru and the United States may agree to modify the Agreement's rules of origin. Article 4.14 calls for two governments to consult regularly after the Agreement's entry into force to discuss proposed modifications to Annex 4.1. Article 20.1.3(b) of the Agreement authorizes the Free Trade Commission to approve proposed modifications to any of the Agreement's origin rules. Such modifications are to be implemented in accordance with each country's applicable legal procedures. In addition, Article 3.3.2 of the Agreement calls for the Parties to consult at either Party's request to consider whether rules of origin for particular textile or apparel goods should be modified.

Section 203(o)(3) of the bill expressly limits the President's authority to modify by proclamation specific rules of origin pertaining to textile or apparel goods (listed in Chapters 50 through 63 of the HTS and identified in Annex 3-A of the Agreement). Those rules of origin may be modified by proclamation within one year of enactment of the implementing bill, to correct typographical, clerical, or other non-substantive technical errors. However, Section 203(o)(4), discussed above, provides the President with authority to proclaim modifications to the rules of origin for textile or apparel articles that are not available in commercial quantities in the United States and Peru.

c. Disclosure of Incorrect Information and Denial of Preferential Treatment

Article 4.19.3 of the Agreement provides that a Party may not impose a penalty on an importer who makes an invalid claim for preferential tariff treatment under the Agreement if the importer did not engage in negligence, gross negligence, or fraud in making the claim or, after

discovering that the claim is invalid, promptly and voluntarily corrects the claim and pays any customs duty owing. Article 4.18.5 of the Agreement provides if an importing country determines through verification that an importer, exporter, or producer has engaged in a pattern of conduct in providing false or unsupported certifications or other representations that a good qualifies as originating, it may suspend preferential tariff treatment under the Agreement for identical goods covered by any subsequent certifications or other representations that that person may make. The suspension may continue until the importing country determines that the importer, exporter, or producer is in compliance with applicable laws and regulations governing claims for preferential tariff treatment under the Agreement.

Section 205(a) of the bill implements Article 4.19.3 for the United States by amending section 592(c) of the Tariff Act of 1930 (19 U.S.C. 1592(c)). Section 205(b) of the bill implements Article 4.18.5 for the United States by amending section 514 of the Tariff Act of 1930 (19 U.S.C. 1514).

d. Claims for Preferential Tariff Treatment

Article 4.19.5 of the Agreement provides that an importer may claim preferential tariff treatment for an originating good within one year of importation, even if no such claim was made at the time of importation. In seeking a refund for excess duties paid, the importer must provide to the customs authorities information substantiating that the good was in fact an originating good at the time of importation.

Section 206 of the bill implements U.S. obligations under Article 4.19.5 of the Agreement by amending section 520(d) of the Tariff Act of 1930 (19 U.S.C. 1520(d)) to allow an importer to claim preferential tariff treatment for originating goods within one year of their importation.

e. Exporter and Producer Certifications

Article 4.15 of the Agreement provides that an importer may base a claim for preferential tariff treatment on either (i) a written or electronic certification by the importer, exporter, or producer, or (ii) the importer's knowledge that the good is an originating good, including through reasonable reliance on information in the importer's possession that the good is an originating good. (The Agreement allows certain exceptions, for example, for goods with a customs value less than or equal to $1,500.) If an exporter issues a certification, it must either be based on the person's knowledge that the good is originating or supported by a separate certification issued by the producer.

Article 4.20 of the Agreement sets out rules governing incorrect certifications of origin issued by exporters or producers. Where an exporter or producer becomes aware that a certification of origin contains or is based on incorrect information, it must promptly and voluntarily notify in writing every person to whom the exporter or producer issued the

certification of any change that could affect the accuracy or validity of the certification. If it does so, the United States may not impose a penalty.

Section 205(a) of the bill implements U.S. obligations under Article 4.20 by amending section 592 of the Tariff Act of 1930 (19 U.S.C. 1592). New subsection (i) of section 592, as added by section 205(a), imposes penalties on exporters and producers that issue false PTPA certifications of origin through fraud, gross negligence, or negligence. These penalties do not apply where an exporter or producer corrects an error in the manner described above.

f. Recordkeeping Requirements

Article 4.17 of the Agreement sets forth record keeping requirements that each government must apply to its importers. U.S. obligations under Article 4.17 regarding importers are satisfied by current law, including the record keeping provisions in section 508 of the Tariff Act of 1930 (19 U.S.C. 1508).

Article 4.17 also sets forth record keeping requirements that each government must apply to exporters and producers issuing certifications of origin for goods exported under the Agreement. Section 207 of the bill implements Article 4.17 for the United States by amending the customs record keeping statute (section 508 of the Tariff Act of 1930).

As added by section 207 of the bill, subsection (h) of section 508 of the Tariff Act of 1930 defines the terms "PTPA certification of origin" and "records and supporting documents." It then provides that a U.S. exporter or producer that issues a PTPA certification of origin must make, keep, and, if requested pursuant to rules and regulations promulgated by the Secretary, render for examination and inspection a copy of the certification and such records and supporting documents. The exporter or producer must keep these records and supporting documents for five years from the date it issues the certification. New subsection (h) of section 508 of the Tariff Act of 1930 sets forth penalties for violations of this record keeping requirement.

2. Administrative Action

The rules of origin in Chapter Four of the Agreement are intended to direct the benefits of customs duty elimination under the Agreement principally to firms producing or manufacturing goods in Peru and the United States. For this reason, the rules ensure that, in general, a good is eligible for benefits under the Agreement only if it is: (i) wholly produced or obtained in the territory of Peru, the United States, or both; or (ii) undergoes substantial processing in the territory of Peru, the United States, or both.

a. Claims for Preferential Treatment

Section 209 of the bill authorizes the Secretary to prescribe regulations necessary to carry out the tariff-related provisions of the bill, including the rules of origin and customs user fee provisions. The Secretary will use this authority in part to promulgate any regulations necessary

to implement the Agreement's provisions governing claims for preferential treatment. Under Article 4.15 of the Agreement, an importer may claim preferential treatment for a good based on either (i) a written or electronic certification by the importer, exporter, or producer, or (ii) the importer's knowledge, including through reasonable reliance on information in the importer's possession, that the good is originating. A certification need not be in a prescribed format, but must include the elements set out in Article 4.15.2 of the Agreement. Under Article 4.19 of the Agreement, an importing Party must grant a claim for preferential tariff treatment unless its customs officials issue a written determination that the claim is invalid as a matter of law or fact.

b. Verification

Under Article 4.18 of the Agreement, customs officials may use a variety of methods to verify claims that goods imported from the other Party satisfy the Agreement's rules of origin. Article 3.2 sets out special procedures for verifying claims that textile or apparel goods imported from the other Party meet the Agreement's origin rules. (See item 1.c of Chapter Three, above.) U.S. officials will carry out verifications under Articles 4.18 and 3.2 of the Agreement pursuant to authorities under current law. For example, section 509 of the Tariff Act of 1930 (19 U.S.C. 1509) provides authority to examine records and issue summonses to determine liability for duty and ensure compliance with U.S. customs laws.

Chapter Five (Customs Administration and Trade Facilitation)

1. Implementing Bill

No statutory changes will be required to implement Chapter Five.

2. Administrative Action

a. Inquiry Point

Article 5.1.2 of the Agreement requires each government to designate an inquiry point for inquiries from interested persons on customs matters. CBP will serve as the U.S. inquiry point for this purpose. Consistent with Article 5.1.2, CBP will post information on the Internet at "www.cbp.gov" on how interested persons can make customs-related inquiries.

b. Advance Rulings

Treasury regulations for advance rulings under Article 5.10 of the Agreement (including on classification, valuation, origin, and qualification as an originating good) will parallel in most respects existing regulations in Part 177 of the Customs Regulations for obtaining advance rulings. For example, a ruling may be relied on provided that the facts and circumstances represented in the ruling are complete and do not change. The regulations will make provision for modifications and revocations as well as for delaying the effective date of a modification

where the firm in question has relied on an existing ruling. Advance rulings under the Agreement will be issued within 150 days of receipt of all information reasonably required to process the application for the ruling.

Chapter Six (Sanitary and Phytosanitary Measures)

No statutory or administrative changes will be required to implement Chapter Six.

Chapter Seven (Technical Barriers to Trade)

1. Implementing Bill

No statutory changes will be required to implement Chapter Seven.

2. Administrative Action

Article 7.7 of the Agreement establishes an inter-governmental Committee on Technical Barriers to Trade ("TBT"). A USTR official responsible for TBT matters or trade relations with Peru will serve as the U.S. coordinator for the committee.

Chapter Eight (Trade Remedies)

1. Implementing Bill

Subtitle A of Title III of the bill implements in U.S. law the safeguard provisions set out in Chapter Eight of the Agreement. Subtitle C of Title III of the bill implements the global safeguard provisions set out in Chapter Eight of the Agreement. (As discussed under Chapter Three, above, Subtitle B of Title III of the bill implements the textile or apparel safeguard provisions of the Agreement.)

a. Safeguard Measures

Subtitle A of Title III of the bill, Sections 311 through 316, authorizes the President, after an investigation and affirmative determination by the ITC (or a determination that the President may consider to be an affirmative determination), to suspend duty reductions or impose duties temporarily up to NTR (MFN) rates on a "Peruvian article" when, as a result of the reduction or elimination of a duty under the Agreement, the article is being imported into the United States in such increased quantities and under such conditions as to be a substantial cause of serious injury or threat of serious injury to a domestic industry that produces a like or directly competitive good. The standards and procedures set out in these provisions closely parallel the procedures set forth in sections 201 through 204 of the Trade Act of 1974 (19 U.S.C. 2251 – 2254).

Section 301(1) defines the term "Peruvian article" to mean a good that qualifies as an originating good under section 203(b) of the bill.

Section 311 of the bill provides for the filing of petitions with the ITC and for the ITC to conduct safeguard investigations initiated under Subtitle A. Section 311(a) provides that a petition requesting a safeguard action may be filed with the ITC by an entity that is "representative of an industry." As under section 202(a)(1) of the Trade Act of 1974, the term "entity" is defined to include a trade association, firm, certified or recognized union, or a group of workers.

Section 311(b) sets out the standard to be used by the ITC in undertaking an investigation and making a determination in Subtitle A safeguard proceedings.

Section 311(c) makes applicable by reference several provisions of the Trade Act of 1974. These are the definition of "substantial cause" in section 202(b)(1)(B), the factors listed in section 202(c) applied in making determinations, the hearing requirement of section 202(b)(3), and the provisions of section 202(i) permitting confidential business information to be made available under protective order to authorized representatives of parties to a safeguard investigation.

Section 311(d) exempts from investigation under this section Peruvian articles that have previously been the basis for according relief under Subtitle A to a domestic industry.

Section 312(a) establishes deadlines for ITC determinations following an investigation under section 311(b). The ITC must make its injury determination within 120 days of the date on which it initiates an investigation.

Section 312(b) makes applicable the provisions of section 330(d) of the Tariff Act of 1930, which will apply when the ITC Commissioners are equally divided on the question of injury or remedy.

Under section 312(c), if the ITC makes an affirmative determination, or a determination that the President may consider to be an affirmative determination, under section 312(a), it must find and recommend to the President the amount of import relief that is necessary to remedy or prevent the serious injury and to facilitate the efforts of the domestic industry to make a positive adjustment to import competition. The relief that the ITC may recommend is limited to that authorized in section 313(c). Similar to procedures under the global safeguards provisions in current law, section 312(c) of the bill provides that only those members of the ITC who agreed to the affirmative determination under section 312(a) may vote on the recommendation of relief under section 312(c).

Under section 312(d), the ITC is required to transmit a report to the President not later than 30 days after making its injury determination. The ITC's report must include: (i) the ITC's

determination(s) under section 312(a) and the reasons supporting the determination(s); (ii) if the determination under section 312(a) is affirmative or may be considered to be affirmative by the President, any findings and recommendations for import relief and an explanation of the basis for each recommendation; and (iii) any dissenting or separate views of ITC Commissioners. Section 312(e) requires the ITC to publish its report promptly and to publish a summary of the report in the *Federal Register*.

Section 313(a) of the bill directs the President, subject to section 313(b), to take action not later than 30 days after receiving a report from the ITC containing an affirmative determination or a determination that the President may consider to be an affirmative determination. The President must provide import relief to the extent that the President determines is necessary to remedy or prevent the injury the ITC has found and to facilitate the efforts of the domestic industry to make a positive adjustment to import competition. Under section 313(b), the President is not required to provide import relief if the President determines that the relief will not provide greater economic and social benefits than costs.

Section 313(c)(1) sets forth the nature of the relief that the President may provide. In general, the President may take action in the form of:

- a suspension of further reductions in the rate of duty to be applied to the articles in question; or

- an increase in the rate of duty on the articles in question to a level that does not exceed the lesser of the existing NTR (MFN) rate or the NTR (MFN) rate of duty imposed on the day before the Agreement entered into force.

Under section 313(c)(2), if the relief the President provides has a duration greater than one year, the relief must be subject to progressive liberalization at regular intervals over the course of its application.

Section 313(d) provides that the period for import relief under a Subtitle A safeguard may not exceed four years in the aggregate. The initial period of import relief may be of up to two years. The President may extend the period of import relief provided by up to two years, however, if he determines that continuation of relief is necessary to remedy or prevent serious injury and to facilitate adjustment to import competition, and that there is evidence that the industry is making a positive adjustment to import competition. That determination must follow an affirmative determination (or a determination that the President may consider to be an affirmative determination) by the ITC to the same effect.

Section 313(e) specifies the duty rate to be applied to Peruvian articles after termination of a safeguard action. On the termination of relief, the rate of duty for the remainder of the calendar year is to be the rate that was scheduled to have been in effect one year after the initial

provision of import relief. For the rest of the duty phase-out period, the President may set the duty:

- at the rate called for under the Schedule of the United States to Annex 2.3 of the Agreement; or
- in a manner that eliminates the duty in equal annual stages ending on the date set out in that Schedule.

Section 313(f) exempts from relief any article that is: (i) subject to import relief under the global safeguard provisions in U.S. law (chapter 1 of Title II of the Trade Act of 1974); (ii) subject to import relief under subtitle B; or (iii) subject to an assessment of additional duty under subsection (b) of section 202.

Section 314 provides that the President's authority to take action under Subtitle A expires ten years after the date on which the Agreement enters into force, unless the period for elimination of duties on a good exceeds ten years. In such case, relief may be provided until the expiration of the period for elimination of duties.

Section 315 allows the President to provide trade compensation to Peru, as required under Article 8.5 of the Agreement, when the United States imposes relief through a Subtitle A safeguard action. Section 315 provides that for purposes of section 123 of the Trade Act of 1974, which allows the President to provide compensation for global safeguards, any relief provided under section 313 will be treated as an action taken under the global safeguard provisions of U.S. law (sections 201 through 204 of the Trade Act of 1974).

Section 316 amends section 202(a) of the Trade Act of 1974 to provide that the procedures in section 332(g) of the Tariff Act of 1930 with respect to the release of confidential business information are to apply to Subtitle A safeguard investigations.

The Administration has not provided classified information to the ITC in past safeguard proceedings and does not expect to provide such information in future proceedings. In the unlikely event that the Administration provides classified information to the ITC in such proceedings, that information would be protected from publication in accordance with Executive Order 12958.

b. Global Safeguard Measures

Section 331 of the bill implements the global safeguard provisions of Article 8.6.2 of the Agreement. It authorizes the President, in granting global import relief under sections 201 through 204 of the Trade Act of 1974, to exclude imports of originating articles from the relief when certain conditions are present.

Specifically, section 331(a) provides that if the ITC makes an affirmative determination, or a determination that the President may consider to be an affirmative determination, in a global safeguard investigation under section 202(b) of the Trade Act of 1974, the ITC must find and report to the President whether imports of the article from Peru considered individually that qualify as originating goods under section 203(b) are a substantial cause of serious injury or threat thereof. Under section 331(b), if the ITC makes a negative finding under section 331(a) the President may exclude any imports that are covered by the ITC's finding from the global safeguard action.

2. Administrative Action

No administrative changes will be required to implement Chapter Eight.

Chapter Nine (Government Procurement)

1. Implementing Bill

Chapter Nine of the Agreement establishes rules that certain government entities, listed in Annex 9.1 of the Agreement, must follow in procuring goods and services. The Chapter's rules will apply whenever these entities undertake procurements valued above thresholds specified in Annex 9.1.

In order to comply with its obligations under Chapter Nine, the United States must waive the application of certain federal laws, regulations, procedures and practices that ordinarily treat foreign goods and services and suppliers of such goods and services less favorably than U.S. goods, services, and suppliers. Section 301(a) of the Trade Agreements Act of 1979 (19 U.S.C. 2511(a)) authorizes the President to waive the application of such laws, regulations, procedures, and practices with respect to "eligible products" of a foreign country designated under section 301(b) of that Act. By virtue of taking on the procurement-related obligations in Chapter Nine, Peru is eligible to be designated under section 301(b) of the Trade Agreements Act and will be so designated.

The term "eligible product" in section 301(a) of the Trade Agreements Act is defined in section 308(4)(A) of that Act for goods and services of countries and instrumentalities that are parties to the WTO Agreement on Government Procurement and countries that are parties to the NAFTA and other recent free trade agreements. Section 401 of the bill amends the definition of "eligible product" in section 308(4)(A) of the Trade Agreements Act. As amended, section 308(4)(A) will provide that, for Peru, an "eligible product" means a product or service of Peru that is covered under the Agreement for procurement by the United States. This amended definition, coupled with the President's exercise of his authority under section 301(a) of the Trade Agreements Act, will allow U.S. government entities covered by the Agreement to purchase products and services from Peru.

2. Administrative Action

As noted above, Annex 9.1 of the Agreement provides that U.S. government entities subject to Chapter Nine must apply the Chapter's rules to goods and services from Peru when they make purchases valued above certain dollar thresholds. USTR will notify the Federal Acquisition Regulatory Council ("FAR Council") of the thresholds that pertain to Peru under the Agreement. The FAR Council will then incorporate those thresholds into the Federal Acquisition Regulation in accordance with applicable procedures under the Office of Federal Procurement Policy Act.

Article 9.6.7 clarifies that a procuring entity is not precluded from preparing, adopting, or applying "technical specifications" to promote the conservation of natural resources and the environment, or to require a supplier to comply with generally applicable laws regarding fundamental principles and rights at work and acceptable conditions of work with respect to minimum wages, hours of work, and occupational safety and health, in the territory in which the good is produced or the service is performed. Thus, for example, a procuring entity is permitted to require a foreign producer to comply with laws guaranteeing freedom of association and protecting collective bargaining rights that generally apply in the territory in which the good is produced, even if that law does not apply to that foreign producer based on its location in an export processing zone.

Finally, neither this provision nor any other provision of Chapter Nine will affect application of the Davis-Bacon Act and related Acts (40 U.S.C. 3141 - 48 and 29 C.F.R. 5.1).

Chapter Ten (Investment)

1. Implementing Bill

Section 106 of the bill authorizes the United States to use binding arbitration to resolve claims by investors of Peru under Article 10.16.1(a)(i)(C) or Article 10.16.1(b)(i)(C) of the Agreement. Those articles concern disputes over certain types of government contracts, and section 106 of the bill clarifies that the United States consents to the arbitration of such disputes. No statutory authorization is required for the United States to engage in binding arbitration for other claims covered by Article 10.16. Provisions allowing arbitration of certain contract claims have regularly been included in U.S. bilateral investment treaties over recent decades, and were included in the free trade agreements with Chile, Singapore, Morocco, CAFTA-DR, and Oman.

2. Administrative Action

No administrative changes will be required to implement Chapter Ten.

Chapter Eleven (Cross-Border Trade in Services)

No statutory or administrative changes will be required to implement Chapter Eleven.

Chapter Twelve (Financial Services)

No statutory or administrative changes will be required to implement Chapter Twelve.

Chapter Thirteen (Competition Policy, Designated Monopolies, and State Enterprises)

No statutory or administrative changes will be required to implement Chapter Thirteen.

Chapter Fourteen (Telecommunications)

No statutory or administrative changes will be required to implement Chapter Fourteen.

Chapter Fifteen (Electronic Commerce)

No statutory or administrative changes will be required to implement Chapter Fifteen.

Chapter Sixteen (Intellectual Property Rights)

No statutory or administrative changes will be required to implement Chapter Sixteen.

For pharmaceutical products, Article 16.10.2(e)(i) provides an exception to the data exclusivity obligations for measures to protect public health in accordance with the Declaration on the TRIPS Agreement and Public Health (WT/MIN(01)/DEC/2) (the "Doha Declaration"). Thus, where a Party issues a compulsory license in accordance with Article 31 of the TRIPS Agreement and the Doha Declaration, the data exclusivity obligations in Chapter Sixteen will not prevent the adoption or implementation of such a public health measure. In addition, in a case in which there is no patent on the pharmaceutical product, and, therefore, no need to issue a compulsory license, the data exclusivity obligations in Chapter Sixteen will not prevent the adoption or implementation of such a measure.

Chapter Seventeen (Labor)

1. Implementing Bill

No statutory changes will be required to implement Chapter Seventeen.

2. Administrative Action

Article 17.4.1 of the Agreement establishes a Labor Affairs Council comprising cabinet-level officials from each Party. Article 17.4.5 of the Agreement calls for each government to designate an office to serve as a contact point with the other country and the public and to assist the Council in carrying out the Agreement's Labor Cooperation and Capacity Building Mechanism. The Department of Labor's Bureau of International Labor Affairs (ILAB) will serve as the U.S. contact point for this purpose.

Chapter Eighteen (Environment)

1. Implementing Bill

Annex 18.3.4 of the Agreement calls on Peru to take certain actions to enhance its forest sector governance and promote legal trade in timber products. In addition, the Annex authorizes the United States to take steps to ensure that timber products of Peru that are exported to the United States comply with Peruvian law governing harvest of, and trade in, those products. Among other things, the United States may request Peruvian officials to conduct audits or on-site inspections of harvesting operations and timber producers in Peru and to permit U.S. compliance officers to accompany them on the inspections. The Annex authorizes the United States to detain or bar imports from a Peruvian producer under certain circumstances, such as when a producer knowingly provides false information to Peruvian or U.S. officials.

Section 501 of the bill establishes an interagency committee to oversee implementation of Annex 18.3.4. In particular, section 501 describes requests and determinations the committee may make relating to audits and verifications pursuant to the Annex. Section 501 also provides authority to the committee to request verifications and take appropriate enforcement measures, including directing CBP to apply import measures of the type and in the circumstances contemplated under the Annex.

Section 502 of the bill provides that no later than the beginning of the second and third years after the Agreement enters into force, and periodically thereafter, USTR will report to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives on steps the United States and Peru have taken to carry out Annex 18.3.4 and on activities related to forest sector governance carried out under the Environmental Cooperation Agreement entered into between the United States and Peru.

2. Administrative Action

USTR and other agencies will monitor progress of Peru in implementing the broad range of obligations contained in Annex 18.3.4, including those designed to further improve Peru's governance in the forest sector over the period of 18 months from the date of entry-into-force of the Agreement. In particular, USTR will work with the State Department, and other appropriate agencies, to identify specific areas in which Peru requires assistance, through capacity building, in pursuing the improvements specified in the Annex. The State Department will coordinate the interagency effort to address these specific areas under the Environmental Cooperation Agreement, as provided for in Article 18.10. Areas already identified in the Annex for possible capacity-building initiatives include: strengthening the legal, policy, and institutional framework governing the forest estate and the international trade in forest products; building institutional capacity for forest law enforcement and the international trade in forest products; improving the performance of the forest concession system in meeting economic, social, and ecological objectives; and increasing public participation and improving transparency in forest resource planning and management decision-making.

No later than 90 days after the Agreement enters into force, the President will establish the interagency committee provided for in section 501(a) and will direct the appropriate authorities in the executive branch, in consultation with USTR, to issue those measures, including agency regulations, that may be necessary to implement Annex 18.3.4. The committee, which USTR will coordinate, will comprise agencies with relevant authorities or expertise, including the Forest Service, the Animal and Plant Health Inspection Service (APHIS), the Fish and Wildlife Service (FWS), CBP, the Department of State, and other agencies, as appropriate.

Especially in the context of verifications, the Forest Service will bring to the committee, its long history of developing and implementing policies to protect and manage forest resources, particularly on government-owned and -managed lands, in a manner that enhances both resource productivity and sound environmental stewardship. The experience of APHIS and FWS in ensuring compliance with the Endangered Species Act and the Lacey Act, and in particular in making use of the enforcement tools available under those statutes, will serve to inform the committee as it determines whether particular producers or exporters are complying with Peru's laws governing its forest sector and what compliance measures, if any, may be appropriate. The State Department, through its Bureau of Oceans and International Environmental and Scientific Affairs, has worked extensively with other governments, including Peru, to address concerns relating to local and cross-border wildlife and forest issues. It is also the lead agency for administering the Environmental Cooperation Agreement with Peru, which calls for the two governments to undertake capacity-building initiatives, including in the area of sustainable management of forest resources. Finally, because the Annex contemplates enforcement measures that may include actions relating to U.S. imports, CBP's participation in the committee will be critical.

USTR will coordinate with the Forest Service, APHIS, FWS, CBP, the Department of State, and other agencies, as appropriate, in developing the report required under section 502 of the bill.

Article 18.5.1 of the Agreement establishes an Environmental Affairs Council, comprising senior-level officials with environmental responsibilities from each Party, and provides that each government will designate a contact point for carrying out the Council's work. The Department of State (Bureau of Oceans and International Environmental and Scientific Affairs), in consultation with USTR, will serve as the U.S. contact point.

DESCRIPTION OF THE REVENUE RAISING PROVISIONS OF PROPOSED LEGISLATION IMPLEMENTING THE UNITED STATES - PERU TRADE PROMOTION AGREEMENT

Scheduled for Markup
by the
SENATE COMMITTEE ON FINANCE
on September 20, 2007

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION

September 19, 2007
JCX-77-07

CONTENTS

INTRODUCTION

The Senate Committee on Finance has scheduled a markup on September 20, 2007. This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of the revenue raising provisions of proposed legislation implementing the United States - Peru trade promotion agreement.

[1] This document may be cited as follows: Joint Committee on Taxation, *Description of the Revenue Raising Provisions of Proposed Legislation Implementing the United States - Peru Trade Promotion Agreement,* (JCX-77-07), September 19, 2007. This document can also be found on the web at www.house.gov/jct.

A. Extension of Customs User Fees

Present Law

Section 13031 of the Consolidated Omnibus Budget Reconciliation Act of 1985 ("COBRA")[2] authorized the Secretary of the Treasury to collect certain service fees. Section 412 of the Homeland Security Act of 2002[3] authorized the Secretary of the Treasury to delegate such authority to the Secretary of Homeland Security. Provided for under 19 U.S.C. 58c, these fees include: processing fees for air and sea passengers, commercial trucks, rail cars, private aircraft and vessels, commercial vessels, dutiable mail packages, barges and bulk carriers, merchandise, and Customs broker permits. COBRA was amended on several occasions. The current authorization for the collection of the passenger and conveyance processing fees is through September 30, 2014. The current authorization for the collection of the merchandise processing fees is through October 21, 2014.[4]

Description of Proposal

The proposal extends the passenger and conveyance processing fees and the merchandise processing fees authorized under COBRA through December 13, 2014.

Effective Date

The proposal is effective on the date of enactment.

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[2] Pub. L. No. 99-272.

[3] Pub. L No. 107-296.

[4] For fiscal years after September 30, 2005, the Secretary is to charge fees in amounts that are reasonably related to the costs of providing customs services in connection with the activity or item for which the fee is charged.

B. Modifications to Corporate Estimated Tax Payments

Present Law

In general, corporations are required to make quarterly estimated tax payments of their income tax liability. For a corporation whose taxable year is a calendar year, these estimated tax payments must be made by April 15, June 15, September 15, and December 15.

Under present law, in the case of a corporation with assets of at least $1 billion, the payments due in July, August, and September, 2012, shall be increased to 114.75 percent of the payment otherwise due and the next required payment shall be reduced accordingly.

Description of Proposal

The proposal increases the percentage from 114.75 percent to 115.50 percent.

Effective Date

The proposal is effective on the date of enactment.

JOINT COMMITTEE ON TAXATION
September 19, 2007
JCX-78-07

ESTIMATED REVENUE EFFECTS OF PROPOSED LEGISLATION IMPLEMENTING THE UNITED STATES - PERU TRADE PROMOTION AGREEMENT SCHEDULED FOR MARKUP BY THE SENATE COMMITTEE ON FINANCE ON SEPTEMBER 20, 2007

Fiscal Years 2008 - 2017

[Millions of Dollars]

Provision	Effective	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2008-12	2008-17
1. Extend Customs User Fees (sunset 12/13/14) [1]	DOE	---	---	---	---	---	---	---	495	---	---	---	495
2. Increase the Required Corporate Estimated Tax Payments Due in July, August, and September 2012 from 114.75 to 115.50 Percent of the Payment Otherwise Due for Corporations With Assets of at Least $1 Billion	DOE	---	---	---	---	465	-465	---	---	---	---	465	---
NET TOTAL		---	---	---	---	**465**	**-465**	---	**495**	---	---	**465**	**495**

Joint Committee on Taxation

NOTE: Details may not add to totals due to rounding. The date of enactment is assumed to be October 1, 2007.

Legend for "Effective" column: DOE = date of enactment

[1] Estimate provided by the Congressional Budget Office.

DESCRIPTION OF THE "AMERICAN INFRASTRUCTURE INVESTMENT AND IMPROVEMENT ACT"

Scheduled for Markup
By the
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CONTENTS

INTRODUCTION

The Airport and Airway Trust Fund ("AATF") provides funding for capital improvements to the U.S. airport and airway system and funding for Federal Aviation Administration ("FAA") operations and programs, among other purposes. The Internal Revenue Code (the "Code") contains the provisions that dedicate revenues from certain excise taxes to the AATF, provide the relevant expenditure provisions governing the purposes for which AATF monies may be spent, and set the period for when those expenditures may occur. The excise taxes imposed to finance the AATF are:[1]

- ticket taxes imposed on commercial, domestic passenger transportation by air;
- a use of international air facilities tax;
- a cargo tax imposed on freight transportation by air;
- fuels taxes imposed on gasoline used in commercial aviation and noncommercial aviation; and
- fuels taxes imposed on (kerosene) jet fuel and other aviation fuels used in commercial aviation and noncommercial aviation.

Domestic commercial aviation (the use of an aircraft in a business of transporting persons or property for compensation) is subject to the ticket tax and air cargo tax, as well as a 4.4-cent-per-gallon fuel tax.[2] Noncommercial aviation is subject only to the fuel taxes, but at higher rates.

With the exception of 4.4 cents per gallon of the fuel tax rates, the taxes imposed and dedicated to the AATF do not apply after September 30, 2007. The AATF expenditure authority expires on October 1, 2007. The purposes for which AATF funds may be expended are fixed as of the date of enactment of the Vision 100—Century of Aviation Reauthorization Act (Pub. L. No. 108-176, December 12, 2003). As a result, the Code provisions must be amended to permit the expenditure of AATF monies for those purposes as provided for in any new reauthorization bill, as well as to authorize the imposition of the dedicated taxes beyond September 30, 2007.

The Senate Committee on Commerce, Science, and Transportation has considered and reported favorably with amendments S. 1300, the "Aviation Investment and Modernization Act

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[1] Sec. 9502(b)(1). The AATF also is credited with interest under sec. 9602(b). Unless otherwise stated, all section references are to the Internal Revenue Code of 1986, as amended.

[2] As described below, the fuel tax consists of two components: 4.3 cents per gallon dedicated to the AATF and 0.1 cent per gallon dedicated to the Leaking Underground Storage Tank Trust Fund. The higher fuel tax imposed on noncommercial aviation similarly consists of an AATF component (21.8 cents per gallon for jet fuel, 19.3 cents for aviation gasoline) plus 0.1 cent per gallon for the Leaking Underground Storage Tank Trust Fund.

of 2007." That bill authorizes appropriations for the FAA for fiscal years 2008 through 2011, among other provisions.[3]

The Senate Committee on Finance has scheduled a markup of a bill relating to the AATF reauthorization for September 20, 2007. This document,[4] prepared by the staff of the Joint Committee on Taxation, provides a description of the present-law taxes dedicated to the AATF, a summary of the AATF expenditure purposes, and a description of the bill. That bill reauthorizes the taxes and amends the purposes for which AATF funds may be expended to include the reauthorization bill, increases the taxes on aviation-grade kerosene for use in noncommercial aviation, imposes a tax at the domestic commercial aviation rate to fuel consumed during wholly domestic segments of international flights, increases the tax on the use of international air facilities, creates a new sub-account within the AATF for air traffic control modernization, creates a new tax regime for fractional ownership aircraft programs, and repeals the exemption for small aircraft operating on nonestablished lines (other than exclusively for sightseeing). The bill also provides for increased funding for the Highway Trust Fund.

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[3] A complete description of S.1300 can be found in S. Rept. 110-144 (110th Cong. 1st Sess.)(August 3, 2007).

[4] This document may be cited as follows: Joint Committee on Taxation, *Description of the "American Infrastructure Investment and Improvement Act"* (JCX-79-07), September 18, 2007. This document can be found on our website at www.house.gov/jct.

I. AVIATION TRUST FUND EXTENSION

A. Extension of Airport and Airway Trust Fund Tax and Expenditure Provisions

Present Law

Taxes on transportation of persons by air

The Code imposes an excise tax on both domestic and certain international transportation of passengers by air. The AATF is credited with amounts equivalent to these taxes. The taxes do not apply after September 30, 2007.[5]

Domestic air passenger excise tax

Domestic air passenger transportation generally is subject to a two-part excise tax. The first component is an *ad valorem* tax imposed at the rate of 7.5 percent of the amount paid for the transportation. The second component is a flight segment tax. For 2007, the flight segment tax rate is $3.40.[6] A flight segment is defined as transportation involving a single take-off and a single landing. For example, travel from New York to San Francisco, with an intermediate stop in Chicago, consists of two flight segments (without regard to whether the passenger changes aircraft in Chicago).

The flight segment component of the tax does not apply to segments to or from qualified "rural airports." For any calendar year, a rural airport is defined as an airport that in the second preceding calendar year had fewer than 100,000 commercial passenger departures, and meets one of the following three additional requirements (1) the airport is not located within 75 miles of another airport that had more than 100,000 such departures in that year, (2) the airport is receiving payments under the Federal "essential air service" program, or (3) the airport is not connected by paved roads to another airport.[7]

The domestic air passenger excise tax applies to "taxable transportation." Taxable transportation means transportation by air that begins in the United States or in the portion of Canada or Mexico that is not more than 225 miles from the nearest point in the continental United States and ends in the United States or in such 225-mile zone. If the domestic

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[5] Sec. 4261(j)(1)(A)(ii). The person making the payment (generally the passenger) is liable for the tax; airlines and others receiving payments are liable for remitting tax and are primarily liable if they fail to collect the tax. Secs. 4261(d) and 4263(c).

[6] Sec. 4261(b)(1) and 4261(d)(4). The Code provides for a $3 tax indexed annually for inflation, effective each January 1st, resulting in the current rate of $3.40.

[7] In the case of an airport qualifying as "rural" because it is not connected by paved roads to another airport, only departures for flight segments of 100 miles or more are considered in calculating whether the airport has fewer than 100,000 commercial passenger departures. The Department of Transportation has published a list of airports that meet the definition of rural airports. See Rev. Proc. 2005-45.

transportation is paid for outside of the United States, it is taxable only if it begins and ends in the United States.

For purposes of the domestic air passenger excise tax, taxable transportation does not include "uninterrupted international air transportation." Uninterrupted international air transportation is any transportation that does not both begin and end in the United States or in the 225-mile zone and does not have a layover time of more than 12 hours. The tax on international air passenger transportation is discussed below.

Use of international air facilities

For 2007, international air passenger transportation is subject to a tax of $15.10 per arrival or departure in lieu of the taxes imposed on domestic air passenger transportation if the transportation begins or ends in the United States.[8] The definition of international transportation includes certain purely domestic transportation that is associated with an international journey. Under these rules, a passenger traveling on separate domestic segments integral to international travel is exempt from the domestic passenger taxes on those segments if the stopover time at any point within the United States does not exceed 12 hours.

In the case of a domestic segment beginning or ending in Alaska or Hawaii, the tax applies to departures only and is $7.50 for calendar year 2007.

"Free" travel

Both the domestic air passenger tax and the use of international air facilities tax apply only to transportation for which an amount is paid. Thus, free travel, such as that awarded in "frequent flyer" programs and nonrevenue travel by airline industry employees, is not subject to tax. However, amounts paid to air carriers (in cash or in kind) for the right to award free or reduced-fare transportation are treated as amounts paid for taxable air transportation and are subject to the 7.5 percent *ad valorem* tax (but not the flight segment tax or the use of international air facilities tax). Examples of such payments are purchases of miles by credit card companies and affiliates (including airline affiliates) for use as "rewards" to cardholders.

Disclosure of air passenger transportation taxes on tickets and in advertising

Transportation providers are subject to special penalties if they do not separately disclose the amount of the passenger taxes on tickets and in advertising. Failure to satisfy these disclosure requirements is a misdemeanor, upon conviction of which the guilty party is fined not more than $100 per violation.[9]

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[8] Secs. 4261(c) and 4261(d)(4). The international air facilities tax rate of $12 is indexed annually for inflation, effective each January 1, resulting in the current rate of $15.10.

[9] Sec. 7275.

Tax on transportation of property (cargo) by air

The AATF is credited with amounts equivalent to the taxes received from the transportation of property by air. Domestic air cargo transportation is subject to a 6.25 percent *ad valorem* excise tax on the amount paid for the transportation.[10] The tax applies only to transportation that both begins and ends in the United States. Unlike the air passenger taxes, only shippers (the persons paying for the transportation) are liable for payment of the air cargo tax. There is no disclosure requirement for the air cargo tax. This tax does not apply after September 30, 2007.[11]

Aviation fuel taxes

The Code imposes excise taxes on gasoline used in commercial aviation and noncommercial aviation, and on jet fuel (kerosene) and other aviation fuels used in commercial aviation and noncommercial aviation. Amounts equivalent to these taxes are credited to the AATF. With the exception of 4.4 cents per gallon, the fuel taxes will not apply after September 30, 2007. Table 1 below summarizes the taxes on fuel used in aviation:

Table 1.–Taxes on Fuel Used in Aviation

Fuel Type	Tax Rate (including 0.1 cent for Leaking Underground Storage Tank Trust Fund Tax)
Jet fuel and liquids other than aviation gasoline	
Commercial aviation	4.4 cents per gallon
Noncommercial aviation	21.9 cents per gallon
Exempt use	0.1 cent per gallon
Aviation gasoline	
Commercial	4.4 cents per gallon
Noncommercial	19.4 cents per gallon
Exempt use	0.1 cent per gallon

Trust Fund expenditure provisions

In general

The AATF was created in 1970 to finance a major portion of the Federal expenditures on national aviation programs. Prior to that time, these expenditures had been financed with

[10] Sec. 4271.

[11] Sec. 4271(d).

General Fund monies. The statutory provisions relating to the AATF were placed in the Code in 1982.[12]

Expenditures from the fund support the FAA and the majority of the FAA's programs and activities. The FAA budget has four major components: (1) operations and maintenance; (2) facilities and equipment; (3) research, engineering, and development; and (4) the airport improvement program.[13] Operations and maintenance are the only segments of the FAA budget that are funded by both a trust fund contribution and a General Fund contribution.[14] The remaining three items receive all their funding from the AATF.

The current expenditure purposes for the AATF are:

1. obligations incurred under provisions of previous aviation authorizing legislation enacted since 1970, as those provisions were in effect on the date of enactment of the Vision 100–Century of Aviation Reauthorization Act (December 12, 2003);[15]

2. obligations incurred under part A of subtitle VII of Title 49, United States Code (generally, FAA programmatic provisions), which are attributable to planning, research and development, construction, or operation and maintenance of–

   (a) air traffic control,

   (b) air navigation,

   (c) communications, or

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[12] Sec. 9502.

[13] Congressional Research Service, *Aviation Taxes and the Airport and Airway Trust Fund,* CRS Report 97-657E at CRS-2 (1997). The airport improvement program is only for airports in the National Plan of Integrated Airport Systems.

[14] *Id.*

[15] The Acts (or provisions of Acts) pursuant to which aviation trust fund expenditures are allowed are Title I of the Airport and Airway Development Act of 1970; the Airport and Airway Development Act Amendments of 1976; the Aviation Safety and Noise Abatement Act of 1979; the Fiscal Year 1981 Airport Development Authorization Act; the provisions of the Airport and Airway Improvement Act of 1982; the Airport and Airway Safety and Capacity Expansion Act of 1987; the Federal Aviation Administration Research, Engineering, and Development Authorization Act of 1990; the Aviation Safety and Capacity Expansion Act of 1990; the Airport and Airway Safety, Capacity, Noise Improvement, and Intermodal Transportation Act of 1992; the Airport Improvement Program Temporary Extension Act of 1994; Federal Aviation Administration Authorization Act of 1994; Federal Aviation Reauthorization Act of 1996; the provisions of the Omnibus Consolidated and Emergency Supplemental Appropriations Act, 1999 providing for payments from the Airport and Airway Trust Fund; the Interim Federal Aviation Administration Authorization Act; section 6002 of the 1999 Emergency Supplemental Appropriations Act; Public Law 106-59; the Wendell H. Ford Aviation Investment and Reform Act for the 21st Century; the Aviation and Transportation Security Act; and the Vision 100–Century of Aviation Reauthorization Act.

(d) supporting services for the airway system; and

3. obligations incurred for administrative expenses of the Department of Transportation that are attributable to activities described in items (1) and (2).

No expenditures are permitted to be made from the AATF after September 30, 2007. Because the purposes for which AATF funds are permitted to be expended are fixed as of the date of enactment of the Vision 100—Century of Aviation Reauthorization Act (December 12, 2003), the Code must be amended in order to accommodate new purposes. In addition, the Code contains a special enforcement provision to prevent expenditure of AATF monies for purposes not authorized in section 9502.[16] This provision provides that, should such unapproved expenditures occur, no further excise tax receipts will be transferred to the AATF. Rather, the taxes will continue to be imposed but the receipts will be retained in the General Fund. This enforcement provision provides specifically that it applies not only to unauthorized expenditures under the current Code provisions, but also to expenditures pursuant to future legislation that may provide for them unless either the legislation providing for the expenditure amends section 9502's expenditure authorization provisions or otherwise authorizes the expenditure as part of a revenue Act.

Specific AATF expenditure programs

Authorized expenditures for the following airport and airway programs are included under the general purposes described above.

1. Airport Improvement Program (AIP).–

(a) Airport planning.–Planning for airport systems for airport master plans; also, airport noise compatibility planning for air carrier airports eligible for terminal development costs.

(b) Airport construction.–Construction, improvement, or repair of a public airport (includes removal of airport hazards and construction of physical barriers and landscaping to diminish noise).[17]

(c) Airport terminal facilities.–Non-revenue-producing public-use areas that are directly related to movement of passengers and baggage at certified air carrier airports; also, development of revenue-producing areas and construction of non-revenue-producing parking lots for nonhub airports (subject to certification that the grant will not defer needed development with respect to safety, security, or capacity).

[16] Sec. 9502(f)(1).

[17] Airport construction is usually limited to construction or improvements related to aircraft operations, such as runways, taxiways, etc.

(d) Land acquisition.–Includes land or property interests for airport noise control purposes; also includes acquisition of land for, or work necessary to construct, pads suitable for aircraft deicing (subject to certain limitations).

(e) Airport-related equipment.–Airport security equipment required by Department of Transportation regulations, snow removal equipment, noise suppressing equipment, firefighting equipment, navigation aids, and safety equipment required for airport certification; also includes construction or purchase of capital equipment necessary for compliance by an airport with the Americans with Disabilities Act, the Clean Air Act, or the Federal Water Pollution Control Act, other than capital equipment that would primarily benefit a revenue-producing area of the airport used by a nonaeronautical business.

(f) Airport noise compatibility programs.–Includes sound-proofing of public buildings; local governmental units are eligible for project grants as well as airports.

2. Facilities and Equipment Program (F&E).–Costs of acquiring, establishing, and improving air navigation facilities.

3. Research, Engineering, Development, and Demonstration Program (R&D).–Projects in connection with FAA research and development activities.

4. Operations and Maintenance Programs (O&M).–Operations and maintenance of air navigation facilities, including air traffic control and flight checks; services provided under international agreements relating to the U.S. share of joint provision of air navigation services; weather reporting services provided to the FAA by the National Oceanic and Atmospheric Administration.

5. Small Community Air Service Development Pilot Program.–For payments to ensure that eligible localities receiving airline service at the time of deregulation continue to have airline service.

6. Vocational Technical Institutions.–Grants to up to four vocational technical institutions for the acquisition of facilities for the advanced training of maintenance technicians for air carrier aircraft.

7. Airway Science Curriculum Grants.–Grants for higher education airway science study programs, including equipment, buildings, and associated facilities.

8. Civil Aircraft Security Research and Development.–Grants relating to technologies and procedures to counteract terrorist activities against civil aviation.

Description of Proposal

The proposal extends the taxes imposed on the transportation of persons by air and on the transportation of property by air through September 30, 2011. The proposal extends the taxes imposed on aviation fuels through September 30, 2011. The proposal extends the expenditure

authority for the AATF through September 30, 2011, and conforms the purposes for which AATF funds are permitted to be expended to include those obligations authorized by S. 1300.

Effective Date

The proposal is effective on the date of enactment.

B. Taxation of Kerosene for Use in Aviation

Present Law

In general

Under section 4081, an excise tax is imposed upon (1) the removal of any taxable fuel from a refinery or terminal,[18] (2) the entry of any taxable fuel into the United States, or (3) the sale of any taxable fuel to any person who is not registered with the IRS to receive untaxed fuel, unless there was a prior taxable removal or entry.[19] The tax does not apply to any removal or entry of taxable fuel transferred in bulk by pipeline or vessel to a terminal or refinery if the person removing or entering the taxable fuel, the operator of such pipeline or vessel (excluding deep draft vessels), and the operator of such terminal or refinery are registered with the Secretary.[20] If the bulk transfer exception applies, tax is not imposed until the fuel "breaks bulk," i.e., when it is removed from the terminal, typically by rail car or truck, for delivery to a smaller wholesale facility or retail outlet, or removed directly from the terminal into the fuel tank of an aircraft.[21]

The term "taxable fuel" means gasoline, diesel fuel (including any liquid, other than gasoline, that is suitable for use as a fuel in a diesel-powered highway vehicle or train), and kerosene.[22] The term includes kerosene used in aviation (jet fuel) as well as aviation gasoline.

Section 4041(c) provides a back-up tax for liquids (other than aviation gasoline) that are sold for use as a fuel in aircraft and that have not been previously taxed under section 4081.[23]

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[18] A "terminal" is a taxable fuel storage and distribution facility that is supplied by pipeline or vessel and from which taxable fuel may be removed at a rack. A "rack" is a mechanism capable of delivering taxable fuel into a means of transport other than a pipeline or vessel. A terminal can be located at an airport, or fuel may be delivered to the airport from a terminal located off the airport grounds.

[19] Sec. 4081(a)(1).

[20] Sec. 4081(a)(1)(B).

[21] In general, the party liable for payment of the taxes when the fuel breaks bulk at the terminal is the "position holder," the person shown on the records of the terminal facility as holding the inventory position in the fuel. However, when fuel is removed directly into the fuel tank of an aircraft for use in commercial aviation, the person who uses the fuel is liable for the tax. The fuel is treated as used when such fuel is removed into the fuel tank. Sec. 4081(a)(4).

[22] Sec. 4083(a).

[23] Sec. 4041(c).

Kerosene for use in aviation

In general

Present law generally imposes a tax of 24.4 cents per gallon on kerosene. However, reduced rates apply for kerosene removed directly from a terminal into the fuel tank of an aircraft.[24] For kerosene removed directly from a terminal into the fuel tank of an aircraft for use in commercial aviation, the tax rate is 4.4 cents per gallon.[25] For kerosene removed directly from a terminal into the fuel tank of an aircraft for use in noncommercial aviation, the tax rate is 21.9 cents per gallon. All of these tax rates include a 0.1 cent per gallon component for the Leaking Underground Storage Tank Trust Fund. For kerosene removed directly from a terminal into the fuel tank of an aircraft for an exempt use (such as foreign trade or for the exclusive use of a State or local government), only the Leaking Underground Storage Tank Trust Fund tax of 0.1 cent per gallon applies.

"Commercial aviation" generally means any use of an aircraft in the business of transporting by air persons or property for compensation or hire.[26] Commercial aviation does not include transportation exempt from the ticket taxes and air cargo taxes by reason of sections 4281 or 4282 or by reason of section 4261(h) or 4261(i). Thus, small aircraft operating on nonestablished lines (sec. 4281), air transportation for affiliated group members (sec. 4282), air transportation for skydiving (sec. 4261(h)), and certain air transportation by seaplane (sec. 4261(i)) are excluded from the definition of commercial aviation, and accordingly are subject to the tax regime applicable to noncommercial aviation.

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[24] If certain conditions are met, present law permits the removal of kerosene from a refueler truck, tanker, or tank wagon to be treated as a removal from a terminal for purposes of determining whether kerosene is removed directly into the fuel tank of an aircraft. A refueler truck, tanker, or tank wagon is treated as part of a terminal if: (1) the terminal is located within an airport, (2) any kerosene which is loaded in such truck, tanker, or wagon at such terminal is for delivery only into aircraft at the airport in which such terminal is located, and (3) no vehicle licensed for highway use is loaded with kerosene at such terminal, except in exigent circumstances identified by the Secretary in regulations. In order to qualify for the special rule, a refueler truck, tanker, or tank wagon must: (1) have storage tanks, hose, and coupling equipment designed and used for the purposes of fueling aircraft; (2) not be registered for highway use; and (3) be operated by the terminal operator (who operates the terminal rack from which the fuel is unloaded) or by a person that makes a daily accounting to such terminal operator of each delivery of fuel from such truck, tanker, or tank wagon. Sec. 4081(a)(3).

[25] Tax is imposed at this rate if the commercial aircraft operator is registered with the IRS, and the fuel terminal is located within a secured area of an airport. The IRS has published a list of airports with secured areas in which a terminal is located. See Notice 2005-4, 2005-1 C.B. 289, at sec. 4(d)(2)(ii) (2005) (adopting the list from H.R. Conf. Rep. No. 755, 108th Cong., 2d Sess. 692 n. 718 (2004) with modifications) and Notice 2005-80, 2005-2 C.B. 953, at sec. 3(c)(2) (2005). If the fuel terminal is located at an unsecured airport, the fuel is taxed at 21.9 cents per gallon if the fuel is removed directly from the terminal into the fuel tank of an aircraft.

[26] Sec. 4083(b).

Refunds and credits to obtain the appropriate aviation tax rate

If the kerosene is not removed directly into the fuel tank of an aircraft, the fuel is taxed at 24.4 cents per gallon. (This is generally the rate applied to diesel fuel and kerosene used in highway vehicles). A claim for credit or payment may be made for the difference between the tax paid and the appropriate aviation rate (21.9 cents per gallon for noncommercial aviation, 4.4 cents per gallon for commercial aviation, and 0.1 cent per gallon for an exempt use).[27]

For noncommercial aviation, other than for exempt use, only the registered ultimate vendor may make the claim for the 2.5-cent-per-gallon difference between the 24.4 cents per gallon rate and the noncommercial aviation rate of 21.9 cents per gallon.[28] For commercial aviation and exempt use (other than State and local government use), the ultimate purchaser may make a claim for the difference in tax rates, or the ultimate purchaser may waive the right to make the claim for payment to the ultimate vendor.[29] For State and local government use, the registered ultimate vendor is the proper claimant.[30]

Commercial aviation claimants are permitted to credit their fuel tax claims against their other excise tax liabilities, thereby reducing the amount of excise tax to be paid with the excise tax return.

Transfers between the Highway Trust Fund and the AATF to account for aviation use

Kerosene that is not removed directly from the terminal into an airplane (e.g., the jet fuel is transferred from the terminal by highway vehicle to the airport) is taxed at the highway fuel rate of 24.4 cents per gallon. The Highway Trust Fund is credited with 24.3 cents per gallon of the 24.4 cents per gallon imposed. The remaining 0.1 cent is credited to the Leaking Underground Storage Tank Trust Fund. If a claim for payment is later made indicating that the fuel was used in aviation, the Secretary then transfers to the AATF 4.3 cents per gallon for commercial aviation use and 21.8 cents per gallon for noncommercial aviation use. These transfers initially are based on estimates, and proper adjustments are made in amounts subsequently transferred to the extent prior estimates were in excess of or less than the amounts required to be transferred. Thus, to the extent claims for credit or payment are not made for the difference between the highway rate and the aviation rate, the AATF will not be credited for fuel used in aviation that was taxed at the 24.4 cents per gallon rate.

Aviation gasoline

The tax on aviation gasoline is 19.4 cents per gallon (including 0.1 cent per gallon Leaking Underground Storage Tank Trust Fund component). If aviation gasoline is used in

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[27] Sec. 6427(l)(4).

[28] Sec. 6427(l)(4)(C)(ii).

[29] Sec. 6427(l)(4)(C)(i).

[30] See secs. 6427(l)(5). Special rules apply if the kerosene is purchased with a credit card issued to a State or local government.

commercial aviation, the ultimate purchaser may obtain a credit or payment in the amount of 15 cents per gallon, such that the tax rate on such gasoline is 4.4 cents per gallon.[31] If aviation gasoline is sold for an exempt use, a credit or refund is allowable for all but the Leaking Underground Storage Tank Trust Fund tax (0.1 cent per gallon).[32]

Description of Proposal

The proposal creates a separate category of kerosene for tax purposes: aviation-grade kerosene.[33] Aviation-grade kerosene is taxed at 35.9 cents per gallon plus 0.1 cent per gallon for the Leaking Underground Storage Tank Trust Fund. Under the proposal, aviation-grade kerosene used in noncommercial aviation will bear the full rate of tax. The rate of tax for aviation-grade kerosene used in commercial aviation and exempt use remains unchanged.[34]

Because the tax on aviation-grade kerosene used in noncommercial aviation is equal to the applicable rate of tax collected, the proposal repeals the ultimate vendor refund provisions for noncommercial aviation. In addition, the proposal eliminates the inter-fund transfers from the Highway Trust Fund to the AATF for kerosene used in aviation. Instead, the taxes imposed on aviation-grade kerosene will be credited to the AATF only. As a result, the AATF, rather than the Highway Trust Fund, will reimburse the General Fund for any amounts paid with respect to the use of aviation-grade kerosene for a nontaxable use. The proposal also provides a refund mechanism for aviation-grade kerosene used for a taxable purpose other than in an aircraft and the related-trust fund accounting.

In the case of aviation-grade kerosene held on January 1, 2008, by any person, a floor stocks tax is imposed equal to the tax that would have been imposed if the increased rates had been in effect before such date, less (1) the tax actually imposed on such fuel and (2) for fuel held by a person for his own use, the amount that such person would reasonably expect to be paid as a refund. The tax is to be paid at such time and in such manner as the Secretary shall prescribe.

The floor stocks tax does not apply to fuel held in the fuel tank of an aircraft on January 1, 2008. Nor does it apply to fuel held exclusively for any use to the extent a refund or credit of tax is allowable under the Code. The floor stocks tax does not apply if the amount of fuel held by a person does not exceed 2,000 gallons.

For purposes of the floor stocks tax, a controlled group is treated as one person. "Controlled group" for these purposes means a parent-subsidiary, brother-sister, or combined

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[31] Sec. 6421(f)(2).

[32] Sec. 6416(a); sec. 6420 (farming purposes); sec. 6421(c); and sec. 6430.

[33] Aviation-grade kerosene means, as defined by the Internal Revenue Service, kerosene-type jet fuel covered by ASTM specification D1655, or military specification MIL-DTL-5624 (Grade JP-5) or MIL-DTL-83133E (Grade JP-8). See section 4(b) of Notice 2005-4.

[34] Accordingly, commercial aviation use will continue to be subject to a tax of 4.4 cents per gallon and exempt use will be subject to 0.1 cent per gallon.

corporate group with more than 50-percent ownership with respect to either combined voting power or total value. Under regulations, similar principles may apply to a group of persons under common control where one or more persons are not a corporation.

All provisions of law, including penalties, applicable with respect to the taxes imposed by section 4081 also apply to the floor stocks taxes to the extent not inconsistent with the provisions of the proposal. For purposes of determining receipts to the AATF, the floor stocks tax is treated as if it were a tax listed in section 9502(b)(1) (governing transfers to the AATF).

Effective Date

The proposal is generally effective for fuel removed, entered, or sold after December 31, 2007. The floor stocks tax is effective January 1, 2008.

C. Subject Fuel Consumed During Wholly Domestic Segments of International Flights to Tax at the Domestic Commercial Aviation Rate

Present Law

Aviation fuel that is sold for use or used as "supplies for vessels or aircraft" is a nontaxable use for purposes of the fuel taxes (other than the Leaking Underground Storage Tank Trust Fund tax). Under section 4221(d)(3) of the Code, the term "supplies for vessels and aircraft" includes fuel supplies, ships' stores, sea stores, or legitimate equipment on vessels actually engaged in foreign trade or trade between the United States and any of its possessions. For purposes of the preceding sentence, the term "vessels" includes civil aircraft employed in foreign trade or trade between the United States any of its possessions.[35] The term "trade" includes the transportation of persons or property for hire and the making of the necessary preparations for the transportation.[36]

An aircraft that flies a person for hire between the United States and a foreign country is actually engaged in foreign trade within the meaning of section 4221(d)(3). Once an aircraft is actually engaged in foreign trade the aircraft remains so engaged even though it makes intermediate stops in the United States.[37] Under Revenue Ruling 2002-50, that aircraft is also actually engaged in foreign trade when flying a person from a city in the United States to another city in the United States as part of the transportation between the United States and the foreign country. Therefore, only the Leaking Underground Storage Tank Trust Fund tax applies to fuel used in such flights, including fuel consumed between domestic intermediate stops. For example, if an airline carries at least one passenger from Los Angeles to London, with an intermediate stop in New York, the entire flight including the Los Angeles to New York segment, is treated as an international flight subject only Leaking Underground Storage Tank Trust Fund tax even if all the other passengers are flying only from Los Angeles to New York. If the flight were purely domestic, i.e., Los Angeles to New York, the fuel would be taxed at the commercial aviation rate of 4.3 cents per gallon plus 0.1 cent per gallon for Leaking Underground Storage Tank Trust Fund, for a total of 4.4 cents per gallon.

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[35] In the case of civil aircraft employed in foreign trade or trade between the U.S. and its possessions and registered in a foreign country, the exemption from tax is allowed only if the Secretary has been advised by the Secretary of Commerce that such foreign country allows, or will allow, substantially reciprocal privileges in respect of aircraft registered in the United States. If the Secretary has been advised that a foreign country has discontinued or will discontinue the allowance of such privileges, the exemption will not apply thereafter in respect of civil aircraft registered in that foreign country and employed in foreign trade or trade between the United States and any of its possessions. Sec. 4221(e).

[36] Treas. Reg. sec. 48.4221-4(b)(8).

[37] Treas. Reg. sec. 48.4221-4(b)(2).

Description of Proposal

The proposal taxes the fuel consumed during the wholly domestic segments of an international flight at the commercial aviation rate of 4.4 cents per gallon.

Effective Date

The proposal is effective on January 1, 2008.

D. Use of International Air Facilities Tax

Present Law

For 2007, international air passenger transportation is subject to a tax of $15.10 per arrival or departure in lieu of the taxes imposed on domestic air passenger transportation if the transportation begins or ends in the United States.[38] The definition of international transportation includes certain purely domestic transportation that is associated with an international journey. Under these rules, a passenger traveling on separate domestic segments integral to international travel is exempt from the domestic passenger taxes on those segments if the stopover time at any point within the United States does not exceed 12 hours.

In the case of a domestic segment beginning or ending in Alaska or Hawaii, the tax applies to departures only and is $7.50 for calendar year 2007.

Description of Proposal

Beginning January 1, 2008, the proposal increases the tax on the use of international facilities to $16.50. This amount is indexed as under present law. The special rule for Alaska and Hawaii is unchanged by the proposal.

Effective Date

The proposal is effective on January 1, 2008.

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[38] Sec. 4261(c) and 4261(d)(4). The international air facilities tax rate of $12 is indexed annually for inflation, effective each January 1, resulting in the current rate of $15.10.

E. Air Traffic Control System Modernization Sub-Account

Present Law

Under present law, there is no special sub-account of the AATF to which funds are dedicated for air traffic control systems modernization.

Description of Proposal

The proposal creates an Air Traffic Modernization Sub-Account within the AATF to ensure sufficient funding is provided for modernization of the air traffic control system. The Modernization Sub-Account is supported through annual transfers of approximately $400 million from the parent Trust Fund. The funds are made available to the FAA through mandatory spending specifically dedicated to modernization costs approved by the Air Traffic Control Modernization Oversight Board. Use of the funds also may include FAA's Facility and Equipment account expenditures.

Effective Date

The proposal is effective on the date of enactment.

F. Treatment of Fractional Aircraft Ownership Programs

Present Law

For excise tax purposes, fractional ownership flights are treated as commercial aviation. As commercial aviation, such flights are subject to the *ad valorem* tax of 7.5 percent of the amount paid for the transportation, a $3.40 segment tax, and tax of 4.4 cents per gallon on fuel. For international flights, fractional ownership flights pay the $15.10 international travel facilities use tax and a fuel tax of 0.1 cents per gallon.

For purposes of the FAA safety regulations, fractional aircraft ownership programs are treated as a special category of general aviation.[39]

Description of Proposal

Under the proposal, special rules apply to flights on aircraft that are part of a "fractional ownership aircraft program." For this purpose, fractional ownership aircraft program is defined as a program in which:

- A single fractional ownership program manager provides fractional ownership program management services on behalf of the fractional owners;
- Two or more airworthy aircraft are part of the program;
- There are one or more fractional owners per program aircraft, with at least one program aircraft having more than one owner;
- Each fractional owner possesses at least a minimum fractional ownership interest in one or more program aircraft;[40]
- There exists a dry-lease exchange arrangement among all of the fractional owners;[41]
- There are multi-year program agreements covering the fractional ownership, fractional ownership program management services, and dry-lease aircraft exchange aspects of the program.

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[39] 14 C.F.R. Part 91, subpart k.

[40] A minimum fractional ownership interest means: (1) A fractional ownership interest equal to or greater than one-sixteenth of at least one subsonic, fixed wing or powered lift program aircraft; [or (2) a fractional ownership interest equal to, or greater than one-thirty-second of a least one rotorcraft program aircraft.]

[41] A "dry-lease aircraft exchange" means an agreement, documented by the written program agreements, under which the program aircraft are available, on an as needed basis without crew, to each fractional owner.

Under the proposal, in lieu of the present-law taxes on domestic commercial aviation and international flights, every flight on an aircraft that is part of a fractional ownership aircraft program is subject to a $58 departure tax and a fuel tax of 36 cents per gallon. The presence or absence of the fractional owner during the flight has no bearing on the amount of tax imposed on the flight. Thus, positioning the aircraft for the owner, as well as charter flights for non-owners are subject to the new tax regime.

Effective Date

The proposal is effective for transportation beginning after, and fuel sold or used after, December 31, 2007.

G. Repeal Exemption for Small Aircraft Operating on Nonestablished Lines

Present Law

Under present law, transportation by aircraft with a certificated maximum takeoff weight of 6,000 pounds or less is exempt from the excise taxes imposed on the transportation of persons by air and the transportation of cargo by air when operating on a nonestablished line. Similarly, when such aircraft are operating on a flight for the sole purpose of sightseeing, the taxes imposed on the transportation or persons or cargo by air do not apply.

Description of Proposal

The proposal repeals the exemption for transportation by small aircraft operating on nonestablished lines. The present-law exemption for flights operated for the sole purposes of sightseeing is unchanged by the proposal.

Effective Date

The proposal is effective for transportation beginning after December 31, 2007.

II. INCREASED FUNDING FOR THE HIGHWAY TRUST FUND

A. Replenish Emergency Spending From the Highway Trust Fund

Present Law

Certain trust funds defined under the Code receive amounts equivalent to the receipts from taxes dedicated to such trust funds, e.g., the Airports and Airways Trust Fund and the Highway Trust Fund. Receipts from undedicated taxes are deposited in the General Fund of the Treasury.

The Safe, Accountable, Flexible, and Efficient Transportation Equity Act: A Legacy for Users ("SAFETEA") and previous legislation specifically allowed emergency relief to be paid out of the Highway Trust Fund. Since 1998, there have been six emergency appropriations (excluding regular annual appropriations of $100 million for emergencies) from the Highway Trust Fund including responses to disaster relief from terrorism and from natural disasters.[42] Infrastructure otherwise benefited by trust funds has previously received its disaster relief from the General Fund.

Description of Proposal

The proposal would replenish the Highway Trust Fund for emergency appropriations since 1998, through the previous reauthorization period by transferring $3.4 billion from the General Fund of the Treasury to the Highway Trust Fund.

Effective Date

The proposal is effective on the date of enactment.

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[42] See Pub. L. No. 105-174 ($259 million), Pub. L. No. 106-346 ($720 million), Pub. L. No. 107-117 ($175 million), Pub. L. No. 107-206 ($265 million), Pub. L. No. 324 ($1.2 billion), and Pub. L. No. 108-447 ($741 million).

B. Suspension of Transfers from Highway Trust Fund for Certain Repayments and Credit

Present Law

Under sec. 9503(c)(2), certain transfers are made from the Highway Trust Fund to reimburse the General Fund for amounts paid in respect of gasoline used on farms[43], amounts paid in respect of gasoline used for certain nonhighway purposes or by local transit systems[44], amounts relating to fuels not used for taxable purposes[45], and income tax credits allowed with respect to the nontaxable uses of fuels.[46]

Description of Proposal

Section 9503(c)(2), relating to certain transfers from the Highway Trust Fund to the General Fund, is suspended on the date of enactment and for six months thereafter.

Effective Date

The proposal applies to amounts paid for which no transfer has been made before the date of enactment.

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[43] Sec. 6420.

[44] Sec. 6421.

[45] Sec. 6427.

[46] Sec. 34.

C. Impose Excise Tax on Certain Removals of Taxable Fuel from Foreign Trade Zones

Present Law

In general

Generally, excise taxes are imposed on gasoline, diesel fuel and kerosene (collectively referred to as "taxable fuel") when taxable fuel is removed from a refinery or terminal or upon its entry into the United States.[47] The tax does not apply to any removal or entry of taxable fuel transferred in bulk by pipeline or vessel to a terminal or refinery, if the person removing or entering the fuel, the pipeline or vessel operator, and the terminal or refinery operator are all registered with the IRS.[48]

The Code generally permits the Secretary of the Treasury to require persons to register with respect to taxable fuel.[49] The American Jobs Creation Act of 2004 requires persons that operate a terminal or refinery within a foreign trade zone or within a customs bonded storage facility, or that hold an inventory position with respect to taxable fuel in such a terminal, to register with the Secretary of the Treasury.[50] Treasury Regulations require blenders, enterers, pipeline operators, position holders, refiners, terminal operators, and vessel operators, among others, to register.[51]

The Code also provides that the Secretary may require information reporting from any registered person.[52] A Department of Treasury fuel information reporting program, the Excise Summary Terminal Activity Reporting System ("ExSTARS"), requires terminal operators and bulk transport carriers to report monthly on the movement of any liquid product into or out of an approved terminal. Terminal operators file Form 720-TO - Terminal Operator Report, which shows the monthly receipts and disbursements of all liquid products to and from an approved terminal.[53] Bulk transport carriers (vessels and pipelines) that receive liquid product from an approved terminal or deliver liquid product to an approved terminal file Form 720-CS - Carrier Summary Report, which details such receipts and disbursements.

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[47] Sec. 4081(a)(1)(A).

[48] Sec. 4081(a)(1)(B)(i). A vessel operator is not required to be registered with respect to certain deep draft ocean-going vessels. Sec. 4081(a)(1)(B)(ii).

[49] Sec. 4101(a).

[50] See Sec. 4101(a)(2), added by the American Jobs Creation Act of 2004, Pub. L. 108-357, sec. 861(a)(2).

[51] Treas. Reg. sec. 48.4101-1(c)(1).

[52] Sec. 4101(d)(1). See also Treas. Reg. sec. 48.4101-2. The reports are required to be filed by the end of the month following the month to which the report relates.

[53] See Announcement 2001-48, 2001 C.B. An approved terminal is a terminal that is operated by a taxable fuel registrant that is a terminal operator. Treas. Reg. sec. 48.4081-1(b).

Foreign trade zones

Foreign trade zones are established under chapter 1A of title 19 of the United States Code. Customs regulations issued pursuant to title 19 provide that merchandise taken into a foreign trade zone for the sole purpose of exportation or storage will be given "zone restricted" status on proper application and be considered exported for purposes of customs law. If merchandise is to be considered exported for the purpose of any Federal law other than customs laws, the port director shall be satisfied that all pertinent laws, regulations, and rules administered by the Federal agency concerned have been complied with before the application is approved. In general, zone restricted merchandise may not be returned to the customs territory of the United States for domestic consumption.[54]

Rev. Rul. 59-318 holds that an article subject to a manufacturers excise tax is "exported" when it is shipped to a foreign trade zone for the sole purpose of exportation.[55] Consequently, any later removal from such a refinery or terminal in a foreign trade zone for "actual" export is not considered a taxable event.[56] In contrast, if the terminal is located outside of a foreign trade zone, the removal for export is a taxable event unless certain conditions are met.[57]

Many petroleum refineries and terminals are located within foreign trade zones or subzones[58] or bonded warehouses. When taxable fuel is removed by truck or rail from such refinery or terminal, excise taxes may or may not be due at the rack, depending on the mode of removal, as follows. If the taxable fuel is entered into the United States upon such removal, excise taxes and duties are generally due at that point. However, the fuel may be removed under bonded transport without immediate tax or duties. Such transported fuel can be destined for export, for entry into another foreign trade zone (or subzone) or bonded warehouse, or may be entered into the United States at its destination. Excise tax only applies if and when the fuel is entered into the United States. No tax is due if the fuel is exported or re-entered into a foreign trade zone or subzone or bonded warehouse.

U.S. Customs enforcement procedures, which may include forfeiture of the full value of the goods, are triggered if fuel removed under bonded transport is not reported within 30 days as exported, entered into another foreign trade zone or subzone or bonded warehouse, or entered

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[54] 19 C.F.R. sec. 146.44.

[55] 1959-2 C.B. 310. Under Rev. Rul. 59-318, a bill of lading containing the statement "Shipped into Foreign-Trade Zone for Export" is acceptable as proof of exportation.

[56] See, e.g., Priv. Ltr. Rul. 9351006 (Sept. 17, 1993), Transaction 4.

[57] For example, regulations provide that the tax does not apply if the buyer is outside the United States, the sale occurs as the fuel is delivered into a vessel with a capacity of at least 20,000 barrels, the seller is registered and is the exporter of record, and the fuel is exported in due course. Treas. Reg. sec. 48.4081-3(f)(2).

[58] A subzone is a special-purpose zone established as an adjunct to a zone project for a limited purpose. The rules and regulations applicable to foreign trade zones apply equally to subzones. 15 C.F.R. sec. 400.2(n)-(o).

into the United States.[59] Customs also tracks all entries and removals from foreign trade zones and subzones.

Refineries in general, and terminals within foreign trade zones or subzones or bonded warehouses, are not currently required to report under Ex-STARS.

Description of Proposal

Under the proposal, excise tax is generally due on the non-bulk removal (i.e., removal by truck or train) of taxable fuel from terminals or refineries within a foreign trade zone or subzone or bonded warehouse at the same time and in the same manner as if such terminal or refinery were not located in such foreign trade zone or subzone or bonded warehouse, notwithstanding any Customs statute, rule, or regulation. Tax is due upon such removal even if the fuel is entered into another foreign trade zone or subzone or bonded warehouse or is eventually exported. If such taxable fuel is later exported, a credit or refund may be claimed. No interest shall be due on such credits or refunds.

Under the proposal, a removal from a refinery or terminal in a foreign trade zone or subzone or bonded warehouse is not treated any worse than would be the case if the refinery or terminal were not in such a foreign trade zone or subzone or bonded warehouse. Consequently, any removal that would be exempt if the refinery or terminal were not in a foreign trade zone or subzone or bonded warehouse will be exempt where the refinery or terminal is in a foreign trade zone or subzone or bonded warehouse.

The present-law rules continue to apply to any removal by pipeline or vessel of taxable fuel from a terminal or refinery located in a foreign trade zone or subzone or bonded warehouse.

It is intended that the Secretary of the Treasury will require owners and operators of terminals within a foreign trade zone or subzone or bonded warehouse to electronically report monthly all removals of taxable fuel, to the same extent as if such terminal were not located in a foreign trade zone or subzone or bonded warehouse, and it is anticipated that such reporting will be required to be done through Ex-STARS or in some other reasonable form.

Effective Date

The proposal is effective for removals and entries after December 31, 2007.

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[59] See, e.g., 19 C.F.R. secs. 18.25 and 18.26.

D. Clarification of Penalty for Sale of Fuel Failing to Meet EPA Regulations

Present Law

Under the present law, any person other than a retailer who knowingly transfers for resale, sells for resale, or holds out for resale for use in a diesel-powered highway vehicle (or train) any liquid that does not meet applicable Environmental Protection Agency ("EPA") regulations (as defined in section 45H(c)(3)) is subject to a penalty of $10,000 for each such transfer, sale, or holding out for resale, in addition to the tax on such liquid, if any.[60] Any retailer who knowingly holds out for sale (other than for resale) any such liquid, is subject to a $10,000 penalty for each such holding out for sale, in addition to the tax on such liquid, if any.

Description of Proposal

The proposal expands the penalty to include any fuel which does not meet EPA standards for distribution to the public. The proposal reaffirms that the Secretary is authorized to make the determination that the fuel does not comply with the applicable EPA regulations and standards for purposes of asserting the penalty.

Effective Date

The proposal is effective on the date of enactment.

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[60] Sec. 6720A.

E. Clarification of Eligibility for Certain Fuel Credits for Fuel With Insufficient Nexus to the United States

Present Law

The Code provides per-gallon incentives relating to the following qualified fuels: alcohol (including ethanol), biodiesel (including agri-biodiesel), renewable diesel, and certain alternative fuels.[61] The incentives may be taken as an income tax credit, excise tax credit or payment. The provisions are coordinated so that a gallon of qualified fuel is only taken into account once. If the qualified fuel is part of a qualified fuel mixture, the incentives apply only to the amount of qualified fuel in the mixture.

For alcohol, other than ethanol, the amount of the credit is 60 cents per gallon. For ethanol, the credit is 51 cents per gallon. The alcohol incentives expire after December 31, 2010. The amount of the credit for biodiesel is 50 cents. For agri-biodiesel and renewable diesel, the credit amount is $1.00 per gallon. The biodiesel, agri-biodiesel and renewable diesel incentives expire after December 31, 2008. The credit amount for alternative fuels is 50 cents per gallon. The incentives for alternative fuels expire after September 30, 2009 (after September 30, 2014, in the case of liquefied hydrogen). Present law also provides a separate 10-cents-per-gallon incentive to small producers of ethanol and to small producers of agri-biodiesel for up to 15 million gallons.

The Code is silent as to the geographic limitations on where the fuel must be produced, used, or sold. For imported ethanol, there is an offsetting tariff of 54 cents per gallon. This tariff expires January 1, 2009.

Description of Proposal

On a prospective basis, the proposal limits the per-gallon tax incentives for alcohol fuels, biodiesel (including agri-biodiesel), renewable diesel, and alternative fuels to fuels that are consumed or sold for consumption in the United States. Thus, foreign-produced fuel must be entered into the United States for consumption in the United States. Similarly, domestically produced fuel sold for export will not qualify for the credit. However, these restrictions do not apply to the small ethanol producer credit or the small agri-biodiesel producer credit.

Effective Date

The proposal is effective for fuels sold or used after the date of enactment.

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[61] See secs. 40, 40A, 6426, and paragraph (e) of section 6427.

F. Treatment of Qualified Alcohol Fuel Mixtures and Qualified Biodiesel Fuel Mixtures as Taxable Fuel

Present Law

An excise tax is imposed upon (1) the removal of any taxable fuel from a refinery or terminal, (2) the entry of any taxable fuel into the United States, or (3) the sale of any taxable fuel to any person who is not registered with the IRS to receive untaxed fuel, unless there was a prior taxable removal or entry.[62] The tax does not apply to any removal or entry of taxable fuel transferred in bulk by pipeline or vessel to a terminal or refinery if the person removing or entering the taxable fuel, the operator of such pipeline or vessel (excluding deep draft vessels) and the operator of such terminal or refinery are registered with the Secretary.[63] The term "taxable fuel" means gasoline, diesel fuel, and kerosene.[64]

Diesel fuel is (1) any liquid suitable for use in a diesel powered highway vehicle or diesel powered train, (2) transmix, and (3) diesel fuel blendstocks identified by the Secretary.[65] By regulation, diesel fuel does not include kerosene, gasoline, No. 5 and No. 6 fuel oils (as described in ASTM Specification D 396), or F-76 (Fuel Naval Distillates MIL-F-16884) any liquid that contains less than four percent normal parafins, or any liquid that has a distillation range of 125 degrees Fahrenheit or less, sulfur content of 10 ppm or less and minimum color of +27 Saybolt.[66]

Biodiesel is not a taxable fuel because it has less than four percent paraffin content. Ethanol and other fuel alcohols also are not treated as taxable fuel. However, such fuels are subject to the backup tax under section 4041 if sold for use or used as a fuel in a diesel powered highway vehicle or diesel powered train and not for a nontaxable use.

In addition, such fuels are taxable if used in the production of a blended taxable fuel.[67]

The Code provides per-gallon tax incentives relating to biodiesel fuel used in a qualified mixture. The taxpayer has the option of taking the credit amount as an income tax credit, excise tax credit against the tax imposed on taxable fuels ("section 4081 liability") or as a payment from the Secretary in the amount of the credit. The credit is 50 cents for each gallon of biodiesel used

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[62] Sec. 4081(a)(1).

[63] Sec. 4081(a)(1)(B).

[64] Sec. 4083(a).

[65] Sec. 4083(a)(3).

[66] Treas. Reg. sec. 48.4081-1(c)(2)(ii).

[67] Under Treas. Reg. sec. 48.4081-1(c), blended taxable fuel generally means any taxable fuel that (1) is produced outside the bulk transfer/terminal system and (2) by mixing taxable fuel with respect to which tax has been imposed under sec. 4081(a) (gasoline, diesel fuel or kersosene) with any other liquid on which tax has not been imposed under sec. 4081.

by the taxpayer in producing a biodiesel mixture for sale or use in a trade or business of the taxpayer. In the case of agri-biodiesel, the credit is $1.00 per gallon.

A qualified biodiesel mixture is a mixture of biodiesel and diesel fuel that is (1) sold by the taxpayer producing such mixture to any person for use as a fuel, or (2) is used as a fuel by the taxpayer producing such mixture. Pursuant to Treasury Notice, a mixture of 99.9 percent biodiesel and diesel fuel is considered a mixture but such mixture is not a blended taxable fuel because it contains less than four percent paraffin content. Thus, while eligible for the biodiesel fuel mixture tax credit and payment provisions, such fuel would not be subject to tax until put in a motor vehicle for a taxable use.

The Code also provides per-gallon tax incentives relating to alcohol used in a qualified mixture. A qualified mixture means a mixture of alcohol and gasoline, (or of alcohol and a special fuel) sold by the taxpayer as fuel, or used as fuel by the taxpayer producing such mixture. The credit is 51 cents if the alcohol is ethanol (60 cents in the case of other alcohols).

Description of Proposal

The proposal adds qualified alcohol fuel mixtures and qualified biodiesel fuel mixtures to the definition of taxable fuel as a type of diesel fuel.

Effective Date

The proposal is effective for fuels removed, entered, or sold after December 31, 2007.

G. Excluding Volume of Denaturants from the Alcohol Fuels Credit

Present Law

The Code provides a per-gallon credit for the volume of alcohol used as a fuel or in a qualified mixture. For purposes of determining the number of gallons of alcohol with respect to which the credit is allowable, the volume of alcohol includes any denaturant, including gasoline.[68] The denaturant must be added under a formula approved by the Secretary and the denaturant cannot exceed five percent of the volume of such alcohol (including denaturants).

Description of Proposal

The proposal provides that the volume of alcohol eligible for the credit does not include the volume of any denaturant.

Effective Date

The proposal is effective January 1, 2008.

[68] Sec. 40(d)(4).

H. Tax Finished Gasoline at the Refinery Gate

Present Law

An excise tax is imposed upon (1) the removal of any taxable fuel from a refinery or terminal, (2) the entry of any taxable fuel into the United States, or (3) the sale of any taxable fuel to any person who is not registered with the IRS to receive untaxed fuel, unless there was a prior taxable removal or entry.[69] The tax does not apply to any removal or entry of taxable fuel transferred in bulk by pipeline or vessel to a terminal or refinery if the person removing or entering the taxable fuel, the operator of such pipeline or vessel (excluding deep draft vessels), and the operator of such terminal or refinery are registered with the Secretary.[70] The term "taxable fuel" means gasoline, diesel fuel (including any liquid, other than gasoline, which is suitable for use as a fuel in a diesel-powered highway vehicle or train), and kerosene.[71]

Description of Proposal

The proposal imposes a tax on finished gasoline upon removal from the refinery or entry into the United States. The bulk transfer exception would not apply. Only the increased volume resulting from the addition of oxygenates, detergents and other untaxed liquids after the gasoline leaves the refinery would be subject to a subsequent tax.

Effective Date

The proposal is effective for fuel removed, entered, or sold after December 31, 2007.

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[69] Sec. 4081(a)(1).

[70] Sec. 4081(a)(1)(B).

[71] Sec. 4083(a).

I. Oil Spill Liability Trust Fund Tax

Present Law

The Oil Spill Liability Trust Fund financing rate ("oil spill tax") was reinstated effective April 1, 2006.[72] The oil spill tax rate is five cents per barrel and generally applies to crude oil received at a U.S. refinery and to petroleum products entered into the United States for consumption, use, or warehousing.[73]

The oil spill tax also applies to certain uses and the exportation of domestic crude oil.[74] If any domestic crude oil is used in or exported from the United States, and before such use or exportation no oil spill tax was imposed on such crude oil, then the oil spill tax is imposed on such crude oil. The tax does not apply to any use of crude oil for extracting oil or natural gas on the premises where such crude oil was produced.

For crude oil received at a refinery, the operator of the United States refinery is liable for the tax. For imported petroleum products, the person entering the product for consumption, use or warehousing is liable for the tax. For certain uses and exports, the person using or exporting the crude oil is liable for the tax. No tax is imposed with respect to any petroleum product if the person who would be liable for such tax establishes that a prior oil spill tax has been imposed with respect to such product.

The imposition of the tax is dependent in part on the balance of the Oil Spill Liability Trust Fund. The oil spill tax does not apply during a calendar quarter if the Secretary estimates that, as of the close of the preceding calendar quarter, the unobligated balance of the Oil Spill Liability Trust Fund exceeds $2.7 billion. If the Secretary estimates the unobligated balance in the Oil Spill Liability Trust Fund is less than $2 billion at close of any calendar quarter, the oil spill tax will apply on the date that is 30 days from the last day of that quarter. The tax does not apply to any periods after December 31, 2014.

Description of Proposal

The proposal extends the oil spill tax through December 31, 2017. The proposal increases the tax rate from five cents to 10 cents per barrel. The proposal also repeals the requirement that the tax be suspended when the unobligated balance exceeds $2.7 billion.

Effective Date

The proposal is effective beginning the first quarter that is more than 60 days after the date of enactment.

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[72] Sec. 4611(f)

[73] The term "crude oil" includes crude oil condensates and natural gasoline. The term "petroleum product" includes crude oil.

[74] The term "domestic crude oil" means any crude oil produced from a well located in the United States.

J. Tax Treatment of Certain Inverted Corporate Entities

Present Law

Determination of corporate residence

The U.S. tax treatment of a multinational corporate group depends significantly on whether the parent corporation of the group is domestic or foreign. For purposes of U.S. tax law, a corporation is treated as domestic if it is incorporated under the law of the United States or of any State. Other corporations (i.e., those incorporated under the laws of foreign countries or U.S. possessions) generally are treated as foreign.

U.S. taxation of domestic corporations

The United States employs a "worldwide" tax system under which domestic corporations generally are taxed on all income, whether derived in the United States or abroad. In order to mitigate the double taxation that may arise from taxing the foreign-source income of a domestic corporation, a foreign tax credit for income taxes paid to foreign countries is provided to reduce or eliminate the U.S. tax owed on such income, subject to certain limitations.

Income earned by a domestic parent corporation from foreign operations conducted by foreign corporate subsidiaries generally is subject to U.S. tax when the income is distributed as a dividend to the domestic corporation. Until such repatriation, the U.S. tax on such income generally is deferred, and U.S. tax is imposed on such income when repatriated. However, certain anti-deferral regimes may cause the domestic parent corporation to be taxed on a current basis in the United States with respect to certain categories of passive or highly mobile income earned by its foreign subsidiaries, regardless of whether the income has been distributed as a dividend to the domestic parent corporation. The main anti-deferral regimes in this context are the controlled foreign corporation rules of subpart F[75] and the passive foreign investment company rules.[76] A foreign tax credit is generally available to offset, in whole or in part, the U.S. tax owed on this foreign-source income, whether such income is repatriated as an actual dividend or included under one of the anti-deferral regimes.

U.S. taxation of foreign corporations

The United States taxes foreign corporations only on income that has a sufficient nexus to the United States. Thus, a foreign corporation is generally subject to U.S. tax only on income that is "effectively connected" with the conduct of a trade or business in the United States. Such "effectively connected income" generally is taxed in the same manner and at the same rates as the income of a U.S. corporation. An applicable tax treaty may limit the imposition of U.S. tax on business operations of a foreign corporation to cases in which the business is conducted through a "permanent establishment" in the United States.

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[75] Secs. 951-964.

[76] Secs. 1291-1298.

In addition, foreign corporations generally are subject to a gross-basis U.S. tax at a flat 30-percent rate on the receipt of interest, dividends, rents, royalties, and certain similar types of income derived from U.S. sources, subject to certain exceptions. The tax generally is collected by means of withholding by the person making the payment. This tax may be reduced or eliminated under an applicable tax treaty.

U.S. tax treatment of inversion transactions prior to the AJCA

Prior to the AJCA, a U.S. corporation could reincorporate in a foreign jurisdiction and thereby replace the U.S. parent corporation of a multinational corporate group with a foreign parent corporation. These transactions were commonly referred to as inversion transactions. Inversion transactions could take many different forms, including stock inversions, asset inversions, and various combinations of and variations on the two. Most of the known transactions were stock inversions. In one example of a stock inversion, a U.S. corporation forms a foreign corporation, which in turn forms a domestic merger subsidiary. The domestic merger subsidiary then merges into the U.S. corporation, with the U.S. corporation surviving, now as a subsidiary of the new foreign corporation. The U.S. corporation's shareholders receive shares of the foreign corporation and are treated as having exchanged their U.S. corporation shares for the foreign corporation shares. An asset inversion could be used to reach a similar result, but through a direct merger of the top-tier U.S. corporation into a new foreign corporation, among other possible forms. An inversion transaction could be accompanied or followed by further restructuring of the corporate group. For example, in the case of a stock inversion, in order to remove income from foreign operations from the U.S. taxing jurisdiction, the U.S. corporation could transfer some or all of its foreign subsidiaries directly to the new foreign parent corporation or other related foreign corporations.

In addition to removing foreign operations from U.S. taxing jurisdiction, the corporate group could seek to derive further advantage from the inverted structure by reducing U.S. tax on U.S.-source income through various earnings stripping or other transactions. For example, the corporate group could engage in earnings stripping through payment by a U.S. corporation of deductible amounts such as interest, royalties, rents, or management service fees to the new foreign parent or other foreign affiliates. In this respect, the post-inversion structure could enable the group to employ the same tax-reduction strategies that are available to other multinational corporate groups with foreign parents and U.S. subsidiaries, subject to the same limitations (e.g., sections 163(j) and 482).

Inversion transactions could give rise to immediate U.S. tax consequences at the shareholder and/or the corporate level, depending on the type of inversion. In stock inversions, the U.S. shareholders generally recognized gain (but not loss) under section 367(a), based on the difference between the fair market value of the foreign corporation shares received and the adjusted basis of the domestic corporation stock exchanged. To the extent that a corporation's share value had declined, and/or it had many foreign or tax-exempt shareholders, the impact of this section 367(a) "toll charge" was reduced. The transfer of foreign subsidiaries or other assets to the foreign parent corporation also could give rise to U.S. tax consequences at the corporate level (e.g., gain recognition and earnings and profits inclusions under sections 1001, 311(b), 304, 367, 1248, or other provisions). The tax on any income recognized as a result of these

restructurings could be reduced or eliminated through the use of net operating losses, foreign tax credits, and other tax attributes.

In asset inversions, the U.S. corporation generally recognized gain (but not loss) under section 367(a) as though it had sold all of its assets, but the shareholders generally did not recognize gain or loss, assuming the transaction met the requirements of a reorganization under section 368.

U.S. tax treatment of inversion transactions under AJCA

In general

AJCA added new section 7874 to the Code, which defines two different types of corporate inversion transactions and establishes a different set of consequences for each type. Certain partnership transactions also are covered.

Transactions involving at least 80 percent identity of stock ownership

The first type of inversion is a transaction in which, pursuant to a plan[77] or a series of related transactions: (1) a U.S. corporation becomes a subsidiary of a foreign-incorporated entity or otherwise transfers substantially all of its properties to such an entity in a transaction completed after March 4, 2003; (2) the former shareholders of the U.S. corporation hold (by reason of holding stock in the U.S. corporation) 80 percent or more (by vote or value) of the stock of the foreign-incorporated entity after the transaction; and (3) the foreign-incorporated entity, considered together with all companies connected to it by a chain of greater than 50 percent ownership (i.e., the "expanded affiliated group"), does not have substantial business activities in the entity's country of incorporation, compared to the total worldwide business activities of the expanded affiliated group. The provision denies the intended tax benefits of this type of inversion ("80-percent inversion") by deeming the top-tier foreign corporation to be a domestic corporation for all purposes of the Code.[78]

In determining whether a transaction meets the definition of an inversion under the provision, stock held by members of the expanded affiliated group that includes the foreign incorporated entity is disregarded. For example, if the former top-tier U.S. corporation receives stock of the foreign incorporated entity (e.g., so-called "hook" stock), the stock would not be considered in determining whether the transaction meets the definition. Similarly, if a U.S. parent corporation converts an existing wholly owned U.S. subsidiary into a new wholly owned controlled foreign corporation, the stock of the new foreign corporation would be disregarded, with the result that the transaction would not meet the definition of an inversion under the

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[77] Acquisitions with respect to a domestic corporation or partnership are deemed to be "pursuant to a plan" if they occur within the four-year period beginning on the date that is two years before the ownership threshold under the provision is met with respect to such corporation or partnership.

[78] Since the top-tier foreign corporation is treated for all purposes of the Code as domestic, the shareholder-level "toll charge" of section 367(a) does not apply to these inversion transactions.

provision. Stock sold in a public offering related to the transaction also is disregarded for these purposes.

Transfers of properties or liabilities as part of a plan a principal purpose of which is to avoid the purposes of the provision are disregarded. In addition, the Treasury Secretary is to provide regulations to carry out the provision, including regulations to prevent the avoidance of the purposes of the provision, including avoidance through the use of related persons, pass-through or other noncorporate entities, or other intermediaries, and through transactions designed to qualify or disqualify a person as a related person or a member of an expanded affiliated group. Similarly, the Treasury Secretary has the authority to treat certain nonstock instruments as stock, and certain stock as not stock, where necessary to carry out the purposes of the provision.

Transactions involving at least 60 percent but less than 80 percent identity of stock ownership

The second type of inversion is a transaction that would meet the definition of an inversion transaction described above, except that the 80-percent ownership threshold is not met. In such a case, if at least a 60-percent ownership threshold is met, then a second set of rules applies to the inversion. Under these rules, the inversion transaction is respected (i.e., the foreign corporation is treated as foreign), but any applicable corporate-level "toll charges" for establishing the inverted structure are not offset by tax attributes such as net operating losses or foreign tax credits. Specifically, any applicable corporate-level income or gain required to be recognized under sections 304, 311(b), 367, 1001, 1248, or any other provision with respect to the transfer of controlled foreign corporation stock or the transfer or license of other assets by a U.S. corporation as part of the inversion transaction or after such transaction to a related foreign person is taxable, without offset by any tax attributes (e.g., net operating losses or foreign tax credits). This rule does not apply to certain transfers of inventory and similar property. These measures generally apply for a 10-year period following the inversion transaction.

Other rules

Under section 7874, inversion transactions include certain partnership transactions. Specifically, the provision applies to transactions in which a foreign-incorporated entity acquires substantially all of the properties constituting a trade or business of a domestic partnership, if after the acquisition at least 60 percent (or 80 percent, as the case may be) of the stock of the entity is held by former partners of the partnership (by reason of holding their partnership interests), provided that the other terms of the basic definition are met. For purposes of applying this test, all partnerships that are under common control within the meaning of section 482 are treated as one partnership, except as provided otherwise in regulations. In addition, the modified "toll charge" rules apply at the partner level.

A transaction otherwise meeting the definition of an inversion transaction is not treated as an inversion transaction if, on or before March 4, 2003, the foreign-incorporated entity had acquired directly or indirectly more than half of the properties held directly or indirectly by the domestic corporation, or more than half of the properties constituting the partnership trade or business, as the case may be.

Description of Proposal

The proposal generally extends the 80-percent inversion regime of section 7874 to 80-percent inversions completed after March 20, 2002, but on or before March 4, 2003, with certain modifications as described below. A transaction otherwise meeting the definition of an 80-percent inversion under the proposal (i.e., one completed after March 20, 2002, but on or before March 4, 2003) is not treated as an 80-percent inversion if, on or before March 20, 2002, the foreign-incorporated entity had acquired directly or indirectly more than half the properties held directly or indirectly by the domestic corporation, or more than half the properties constituting the partnership trade or business, as the case may be.

Under the proposal, an 80-percent inversion that is completed after March 20, 2002, but on or before March 4, 2003, is respected until the end of the last day of the foreign-incorporated entity's first taxable year ending after the date of enactment. At the end of that day, the inverted foreign-incorporated entity that completed the 80-percent inversion (or, if relevant, any successor entity) is deemed to have transferred all of its assets and liabilities to a domestic corporation in a transaction that is generally treated as a nontaxable inbound reorganization ("repatriation"). The basis of the assets of the foreign-incorporated entity generally remains the same in the hands of the domestic corporation, subject to any special adjustments for importing built-in losses (e.g., section 362(e)). Shareholders of the domestic corporation inherit the respective bases of their shares of the foreign-incorporated entity.

On the day of the repatriation, the earnings and profits of the inverted foreign-incorporated entity transfer over to the domestic corporation. The transfer of such earnings and profits is not a deemed dividend and does not result in a tax upon the domestic corporation or its shareholders. In addition, any foreign taxes attributable to such earnings and profits are not creditable. However, shareholders may be subject to tax on distributions of such earnings and profits.

Beginning on the day after the repatriation, the inverted foreign-incorporated entity is treated for all tax purposes as a domestic corporation. Thus, any income earned by the inverted foreign-incorporated entity after the date of repatriation is deemed to be earned by a domestic corporation, and, therefore, is fully taxable at U.S. corporate income tax rates. As a further consequence of the repatriation of the inverted foreign-incorporated entity, foreign subsidiaries become controlled foreign corporations, subject to the rules of subpart F.

It is intended that the Treasury Secretary will prescribe regulations that are necessary or appropriate to carry out the proposal, including, but not limited to, regulations to prevent the avoidance of the purposes of the proposal.

Effective Date

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

JOINT COMMITTEE ON TAXATION
September 18, 2007
JCX-80-07

ESTIMATED REVENUE, GENERAL FUND, AND TRUST FUND EFFECTS OF THE "AMERICAN INFRASTRUCTURE INVESTMENT AND IMPROVEMENT ACT," [1] SCHEDULED FOR MARKUP BY THE COMMITTEE ON FINANCE ON SEPTEMBER 20, 2007

[Millions of Dollars]

Provision	Effective	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2008-12	2008-17
I. Airport and Airway Trust Fund Provisions and Related Taxes													
A. Revenue Effects													
1. Extension of Airport and Airway Trust Fund Tax and Expenditure Provisions (sunset 9/30/11)	DOE	*No Revenue Effect*											
2. Increase the 21.9 cents per gallon tax on non-commercial aviation-grade kerosene (jet fuel) to 36.0 cents per gallon, including floor stocks	[2]	112	161	166	170	174	179	184	189	195	200	782	1,729
3. Increase international departure and arrival tax to $16.50 and index for inflation	ttpa 12/31/07	84	120	128	136	145	154	164	174	184	196	613	1,485
4. 4.3 cents per gallon tax on fuel consumed during domestic segments of international passenger flights	fsoua 12/31/07	19	29	30	32	33	35	37	38	40	42	143	335
5. Air traffic control system modernization sub-account	---	*Estimate to be Provided by the Congressional Budget Office*											
6. For fractional ownership arrangements - increase the fuel tax from 4.4 cents per gallon to 36.0 cents per gallon, repeal the ad valorem tax, repeal the segment tax, and assess a $58.00 flight departure fee (unindexed)	fsoua 12/31/07 & ttpa 12/31/07	43	76	29	15	19	21	25	35	44	53	182	360
7. Repeal section 4281 (relating to the exemption for small aircraft operating on nonestablished lines) for all except sightseeing aircraft	ttpa 12/31/07	4	7	7	7	7	8	8	9	9	9	32	75
Total of Revenue Effects		262	393	360	360	378	397	418	445	472	500	1,752	3,984
B. General Fund and Trust Fund Effects													
1. General Fund	DOE	-68	-110	-96	-97	-100	-107	-111	-119	-125	-133	-472	-1,066
2. Airport and Airway Trust Fund	DOE	330	503	457	457	478	505	529	564	596	633	2,225	5,051
3. Leaking Underground Storage Tank Trust Fund	DOE	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	-1
Total of General Fund and Trust Fund Effects		262	393	360	360	378	397	418	445	472	500	1,752	3,984
II. Increased Funding for the Highway Trust Fund													
A. Revenue Effects													
1. Replenish emergency spending from the Highway Trust Fund [4]	DOE	*No Revenue Effect*											
2. Suspension of transfers from Highway Trust Fund for certain repayments and credits for six months	DOE	*No Revenue Effect*											
3. Fuel Fraud:													
a. Impose excise tax on certain removals of taxable fuel from foreign trade zones	1/1/08	8	2	2	2	2	2	2	2	2	2	16	26
b. Clarification of penalty for sale of fuel failing to meet EPA regulations	fsoua DOE	[5]	[5]	[5]	[5]	[5]	[5]	[5]	[5]	[5]	[5]	[5]	[5]
c. Clarification of eligibility for certain fuel credits for fuel with insufficient nexus to the United States (various sunsets)	fsoua DOE	17	18	18	5	---	---	---	---	---	---	58	58

Provision	Effective	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2008-12	2008-17
d. Treatment of qualified alcohol fuel mixtures and qualified biodiesel fuel mixtures as taxable fuel	fsoua 12/31/07	4	1	1	1	1	1	1	1	2	2	8	15
e. Exclude volume of denaturants from the alcohol fuels credit	fsoua 12/31/07	59	91	102	32	---	---	---	---	---	---	284	284
f. Tax finished gasoline at the refinery gate	freosa 12/31/07	636	18	18	20	22	22	22	22	22	22	714	824
4. Increase excise tax rate to $0.10 for the Oil Spill Liability Trust Fund (sunset 12/31/17)	[6]	148	250	269	273	276	279	280	283	286	287	1,215	2,630
5. Tax treatment of certain inversion transactions	[7]	109	92	100	108	116	116	136	146	155	163	525	1,241
Total of Revenue Effects		981	472	510	441	417	420	441	454	467	476	2,820	5,078
B. General Fund and Trust Fund Effects													
1. General Fund	DOE	-3,480	-1,388	123	46	16	15	34	44	51	58	-4,683	-4,482
2. Highway Trust Fund	DOE	4,264	1,527	28	31	33	33	33	33	35	35	5,883	6,053
3. Oil Spill Liability Trust Fund	DOE	196	333	359	364	368	372	373	377	381	383	1,620	3,506
Total of General Fund and Trust Fund Effects		981	472	510	441	417	420	441	454	467	476	2,820	5,078
NET TOTAL OF REVENUE EFFECTS		**1,243**	**865**	**870**	**801**	**795**	**817**	**859**	**899**	**939**	**976**	**4,572**	**9,062**
General Fund		**-3,548**	**-1,498**	**27**	**-51**	**-84**	**-92**	**-77**	**-75**	**-74**	**-75**	**-5,155**	**-5,548**
Airport and Airway Trust Fund		**330**	**503**	**457**	**457**	**478**	**505**	**529**	**564**	**596**	**633**	**2,225**	**5,051**
Leaking Underground Storage Tank Trust Fund		**[3]**	**[3]**	**[3]**	**[3]**	**[3]**	**[3]**	**[3]**	**[3]**	**[3]**	**[3]**	**[3]**	**-1**
Highway Trust Fund		**4,264**	**1,527**	**28**	**31**	**33**	**33**	**33**	**33**	**35**	**35**	**5,883**	**6,053**
Oil Spill Liability Trust Fund		**196**	**333**	**359**	**364**	**368**	**372**	**373**	**377**	**381**	**383**	**1,620**	**3,506**
NET TOTAL OF GENERAL FUND AND TRUST FUND EFFECTS		**1,243**	**865**	**870**	**801**	**795**	**817**	**859**	**899**	**939**	**976**	**4,572**	**9,062**

Joint Committee on Taxation

NOTE: Details may not add to totals due to rounding. Date of enactment is assumed to be October 1, 2007.
Changes to revenues credited to the Highway Account of the Highway Trust Fund would affect the calculation of Revenue Aligned Budget Authority ("RABA"), a type of Contract Authority, a mandatory form of budget authority.

Legend for "Effective" column:
DOE = date of enactment
fsoua = fuel sold or used after
ttpa = taxable transportation provided after
freosa = fuel removed, entered, or sold after

[1] The estimates do not include potential effects on direct spending that would be estimated by the Congressional Budget Office
[2] The provision is generally effective for fuel removed, entered, or sold after December 31, 2007. The floor stocks tax provision is effective January 1, 2008.
[3] Loss of less than $500,000.
[4] Estimate provided by the Congressional Budget Office and should be considered preliminary.
[5] Gain of less than $500,000.
[6] Effective for the first quarter that begins more than 60 days after the date of enactment.
[7] Effective for taxable years beginning after the date of enactment, with respect to certain transactions substantially completed after March 20, 2002.

DESCRIPTION OF THE CHAIRMAN'S MARK OF THE "HABITAT AND LAND CONSERVATION ACT OF 2007"

Scheduled for Markup
by the
SENATE COMMITTEE ON FINANCE
on September 20, 2007

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION

September 18, 2007
JCX-75-07

CONTENTS

INTRODUCTION

The Senate Committee on Finance has scheduled a markup of the "Habitat and Land Conservation Act of 2007." This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of the Chairman's Mark.

[1] This document may be cited as follows: Joint Committee on Taxation, *"Description of the Chairman's Mark of the "Habitat and Land Conservation Act of 2007,"* September 18, 2007, (JCX-75-07). This document can also be found on our website at www.house.gov/jct.

A. Make Permanent the Special Rule Encouraging Contribution of Capital Gain Real Property for Conservation Purposes

Present Law

Charitable contributions generally

In general, a deduction is permitted for charitable contributions, subject to certain limitations that depend on the type of taxpayer, the property contributed, and the donee organization. The amount of deduction generally equals the fair market value of the contributed property on the date of the contribution. Charitable deductions are provided for income, estate, and gift tax purposes.[2]

In general, in any taxable year, charitable contributions by a corporation are not deductible to the extent the aggregate contributions exceed 10 percent of the corporation's taxable income computed without regard to net operating or capital loss carrybacks. For individuals, the amount deductible is a percentage of the taxpayer's contribution base, which is the taxpayer's adjusted gross income computed without regard to any net operating loss carryback. The applicable percentage of the contribution base varies depending on the type of donee organization and property contributed. Cash contributions of an individual taxpayer to public charities, private operating foundations, and certain types of private nonoperating foundations may not exceed 50 percent of the taxpayer's contribution base. Cash contributions to private foundations and certain other organizations generally may be deducted up to 30 percent of the taxpayer's contribution base.

In general, a charitable deduction is not allowed for income, estate, or gift tax purposes if the donor transfers an interest in property to a charity while also either retaining an interest in that property or transferring an interest in that property to a noncharity for less than full and adequate consideration. Exceptions to this general rule are provided for, among other interests, remainder interests in charitable remainder annuity trusts, charitable remainder unitrusts, and pooled income funds, present interests in the form of a guaranteed annuity or a fixed percentage of the annual value of the property, and qualified conservation contributions.

Capital gain property

Capital gain property means any capital asset or property used in the taxpayer's trade or business the sale of which at its fair market value, at the time of contribution, would have resulted in gain that would have been long-term capital gain. Contributions of capital gain property to a qualified charity are deductible at fair market value within certain limitations. Contributions of capital gain property to charitable organizations described in section 170(b)(1)(A) (e.g., public charities, private foundations other than private non-operating foundations, and certain governmental units) generally are deductible up to 30 percent of the taxpayer's contribution base. An individual may elect, however, to bring all these contributions

[2] Secs. 170, 2055, and 2522, respectively. Unless otherwise provided, all section references are to the Internal Revenue Code of 1986, as amended (the "Code").

of capital gain property for a taxable year within the 50-percent limitation category by reducing the amount of the contribution deduction by the amount of the appreciation in the capital gain property. Contributions of capital gain property to charitable organizations described in section 170(b)(1)(B) (e.g., private non-operating foundations) are deductible up to 20 percent of the taxpayer's contribution base.

For purposes of determining whether a taxpayer's aggregate charitable contributions in a taxable year exceed the applicable percentage limitation, contributions of capital gain property are taken into account after other charitable contributions. Contributions of capital gain property that exceed the percentage limitation may be carried forward for five years.

Qualified conservation contributions

Qualified conservation contributions are not subject to the "partial interest" rule, which generally bars deductions for charitable contributions of partial interests in property. A qualified conservation contribution is a contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes. A qualified real property interest is defined as: (1) the entire interest of the donor other than a qualified mineral interest; (2) a remainder interest; or (3) a restriction (granted in perpetuity) on the use that may be made of the real property. Qualified organizations include certain governmental units, public charities that meet certain public support tests, and certain supporting organizations. Conservation purposes include: (1) the preservation of land areas for outdoor recreation by, or for the education of, the general public; (2) the protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem; (3) the preservation of open space (including farmland and forest land) where such preservation will yield a significant public benefit and is either for the scenic enjoyment of the general public or pursuant to a clearly delineated Federal, State, or local governmental conservation policy; and (4) the preservation of an historically important land area or a certified historic structure.

Qualified conservation contributions of capital gain property are subject to the same limitations and carryover rules of other charitable contributions of capital gain property.

Special rule regarding contributions of capital gain real property for conservation purposes

In general

Under a temporary provision that is effective for contributions made in taxable years beginning after December 31, 2005,[3] the 30-percent contribution base limitation on contributions of capital gain property by individuals does not apply to qualified conservation contributions (as defined under present law). Instead, individuals may deduct the fair market value of any qualified conservation contribution to an organization described in section 170(b)(1)(A) to the extent of the excess of 50 percent of the contribution base over the amount of all other allowable

[3] Sec. 170(b)(1)(E).

charitable contributions. These contributions are not taken into account in determining the amount of other allowable charitable contributions.

Individuals are allowed to carryover any qualified conservation contributions that exceed the 50-percent limitation for up to 15 years.

For example, assume an individual with a contribution base of $100 makes a qualified conservation contribution of property with a fair market value of $80 and makes other charitable contributions subject to the 50-percent limitation of $60. The individual is allowed a deduction of $50 in the current taxable year for the non-conservation contributions (50 percent of the $100 contribution base) and is allowed to carryover the excess $10 for up to 5 years. No current deduction is allowed for the qualified conservation contribution, but the entire $80 qualified conservation contribution may be carried forward for up to 15 years.

Farmers and ranchers

In the case of an individual who is a qualified farmer or rancher for the taxable year in which the contribution is made, a qualified conservation contribution is allowable up to 100 percent of the excess of the taxpayer's contribution base over the amount of all other allowable charitable contributions.

In the above example, if the individual is a qualified farmer or rancher, in addition to the $50 deduction for non-conservation contributions, an additional $50 for the qualified conservation contribution is allowed and $30 may be carried forward for up to 15 years as a contribution subject to the 100-percent limitation.

In the case of a corporation (other than a publicly traded corporation) that is a qualified farmer or rancher for the taxable year in which the contribution is made, any qualified conservation contribution is allowable up to 100 percent of the excess of the corporation's taxable income (as computed under section 170(b)(2)) over the amount of all other allowable charitable contributions. Any excess may be carried forward for up to 15 years as a contribution subject to the 100-percent limitation.[4]

As an additional condition of eligibility for the 100 percent limitation, with respect to any contribution of property in agriculture or livestock production, or that is available for such production, by a qualified farmer or rancher, the qualified real property interest must include a restriction that the property remain generally available for such production. (There is no requirement as to any specific use in agriculture or farming, or necessarily that the property be used for such purposes, merely that the property remain available for such purposes.) Such additional condition does not apply to contributions made on or before August 17, 2006.

A qualified farmer or rancher means a taxpayer whose gross income from the trade or business of farming (within the meaning of section 2032A(e)(5)) is greater than 50 percent of the taxpayer's gross income for the taxable year.

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[4] Sec. 170(b)(2)(B).

Termination

The special rule regarding contributions of capital gain real property for conservation purposes does not apply to contributions made in taxable years beginning after December 31, 2007.

Description of Proposal

The proposal makes permanent the special rule regarding contributions of capital gain real property for conservation purposes.

Effective Date

The proposal is effective for contributions made in taxable years beginning after December 31, 2007.

B. Provide Tax Credit for Recovery and Restoration of Endangered Species

Present Law

Present law does not provide an income tax credit for endangered species recovery expenditures.

Description of Proposal

In general

For eligible taxpayers, the proposal establishes a credit against income taxes for: (1) costs paid or incurred by an eligible taxpayer for the taxable year (reduced by the amount of government financing for conservation of a qualified species, and not including costs required by a Federal, State, or local government) pursuant to a habitat management plan entered into under certain qualified habitat protection agreements ("habitat restoration credit") and (2) a percentage of the loss in value to real property attributable to an easement placed on the property pursuant to such agreements (less any amount received in connection with the easement) ("habitat protection easement credit"). The allowable credit amount is 100 percent of costs paid or incurred and the loss in value to property pursuant to qualified perpetual habitat protection agreements; 75 percent of costs paid or incurred and the loss in value to property pursuant to qualified 30-year habitat protection agreements; and 50 percent of costs paid or incurred pursuant to a qualified habitat protection agreement.

For purposes of the habitat protection easement credit, the loss in value is the difference between the fair market value of the real property subject to the agreement determined on the day before the agreement is entered into less the fair market value of such property determined one day after the agreement is entered into. To claim such credit, the eligible taxpayer must include on the tax return for the taxable year a qualified appraisal (within the meaning of section 170(f)(11)(E)) of the real property. The taxpayer's basis in such property is reduced by the amount of the credit allowed.

The habitat restoration credit is taken into account after other credits (sections 27, 30, 30B, and 30C) and may not offset the alternative minimum tax. The habitat protection easement credit is taken into account after other credits (sections 27, 30, 30B, and 30C) and such credit may offset the alternative minimum tax. Amounts allowed but in excess of either limitation may be carried forward to the succeeding taxable year. No deduction is allowed for any amount with respect to which a credit is allowed. The Secretary of the Treasury shall by regulations provide for the recapture of the credit if such Secretary, in consultation with the appropriate Secretary, determines that the eligible taxpayer has failed to carry out the duties required by the qualified agreement and there are no other available means to remediate such failure.

The sum of the two credits may not exceed the amount allocated to the eligible taxpayer by the Secretary of the Treasury, in consultation with the Secretary of the Interior and the Secretary of Commerce, for the calendar year in which the taxpayer's taxable year ends. If the amount allowed as a credit exceeds the amount allocated for such year, the excess may be carried forward to the next taxable year for which the taxpayer has received an allocation. If the amount allocated to a taxpayer for a calendar year exceeds the amount allowed as a credit for such year,

the difference may be carried forward to the next taxable year and treated as allocated to the taxpayer for use in such year. No credit is allowed unless the appropriate Secretary certifies that a qualified agreement will contribute to the recovery of a qualified species.

The aggregate amount allocated by the Secretary of the Treasury may not exceed in each year 2008 through 2012: $290,000,000 with respect to qualified perpetual habitat protection agreements, $55,000,000 with respect to qualified 30-year habitat protection agreements, and $35,000,000 with respect to qualified habitat protection agreements. No allocation is allowed after 2012, except that unallocated amounts with respect to any calendar year are carried forward to the allowable allocation for the next calendar year.

Not later than 180 days after the date of enactment, the Secretary of the Treasury, in consultation with the Secretary of the Interior and the Secretary of Commerce, shall by regulation establish a program to process applications from eligible taxpayers and to determine how best to allocate the credit. In allocating the credit, priority shall be given to taxpayers with agreements (1) relating to habitats that will significantly increase the likelihood of recovering and delisting a species as an endangered species or a threatened species (as defined under section 2 of the Endangered Species Act of 1973), (2) that are cost-effective and maximize the benefits to a qualified species per dollar expended, (3) relating to habitats of species that have a Federally approved recovery plan pursuant to section 4 of the Endangered Species Act of 1973, (4) relating to habitats with the potential to contribute significantly to the improvement of the status of a qualified species, (5) relating to habitats with the potential to contribute significantly to the eradication or control of invasive species that are imperiling a qualified species, (6) with habitat management plans that will manage multiple qualified species, (7) with habitat management plans that will create adjacent or proximate habitat for the recovery of a qualified species, (8) relating to habitats for qualified species with an urgent need for protection, (9) with habitat management plans that assist in preventing the listing of a species as endangered or threatened under the Endangered Species Act of 1973 or a similar State law, (10) with habitat management plans that may resolve conflicts between the protection of qualified species and otherwise lawful human activities, and (11) with habitat management plans that may resolve conflicts between the protection of a qualified species and military training or other military operation.

The Secretary of the Treasury shall request that the appropriate Secretary consider whether to authorize under the Endangered Species Act of 1973 takings by an eligible taxpayer of a qualified species to which a qualified agreement relates if the takings are incidental to (1) the restoration, enhancement, or management of the habitat pursuant to the habitat management plan under the agreement or (2) the use of the property to which the agreement pertains at any time after the expiration of the easement (or specified period of time pursuant to a qualified habitat protection agreement), but only if such use will leave the qualified species at least as well off on the property as it was before the agreement was made.

The Comptroller General of the United States shall undertake a study on the effectiveness of the credits. Such study shall evaluate the effectiveness of the credits in encouraging landowners to enter into agreements for the protection of the habitats of endangered and threatened species, and the degree to which such agreements are effective in preserving the habitats of such species and assisting in the recovery of such species, and shall include recommendations for improving the effectiveness of the credits. The Comptroller General shall

issue an interim report based on such study within three years of the date of enactment and a final report within five years of such date.

Definitions

Eligible taxpayer

An eligible taxpayer is (1) a taxpayer who owns real property that contains habitat of a qualified species and enters into a qualified perpetual habitat protection agreement, a qualified 30-year habitat protection agreement, or a qualified habitat protection agreement with the appropriate Secretary with respect to such real property, and (2) a taxpayer who is a party to a qualified perpetual habitat protection agreement, a qualified 30-year habitat protection agreement, or a qualified habitat protection agreement and, as part of any such agreement, agrees to assume responsibility for costs paid or incurred as a result of implementing such agreement.

Qualified agreements

A qualified perpetual habitat protection agreement is an agreement under which an easement is granted to the appropriate Secretary, the Secretary of Agriculture, the Secretary of Defense, or a State to protect the habitat of a qualified species in perpetuity. A qualified 30-year habitat protection agreement is an agreement under which an easement is granted to the appropriate Secretary, the Secretary of Agriculture, the Secretary of Defense, or a State to protect the habitat of a qualified species for a period of not less than 30 years and less than perpetuity. A qualified habitat protection agreement requires agreement with the appropriate Secretary, the Secretary of Agriculture, the Secretary of Defense, or a State to protect the habitat of a qualified species for a specified period of time.

In addition, each of the three types of qualified agreement must meet the following requirements: (1) the agreement must be consistent with any recovery plan that is applicable and that has been approved for a qualified species under section 4 of the Endangered Species Act of 1973; (2) the appropriate Secretary and the eligible taxpayer must enter into a habitat management plan that is designed to restore or enhance the habitat of a qualified species or reduce threats to a qualified species through the management of the habitat; and (3) the appropriate Secretary must ensure that the eligible taxpayer is provided with technical assistance in carrying out the duties of the taxpayer under the terms of the agreement.

Habitat management plan

A habitat management plan means, with respect to any habitat, a plan that identifies one or more qualified species to which the plan applies, describes the management practices to be undertaken by the taxpayer, describes the technical assistance to be provided to the taxpayer and identifies the entity that will provide such assistance, provides a schedule of deadlines for undertaking such management practices, and requires monitoring of the management practices and the status of the qualified species.

Qualified species

A qualified species is any species listed as an endangered species or threatened species under the Endangered Species Act of 1973 or any species for which a finding has been made under section 4(b)(3) of the Endangered Species Act of 1973 that listing under such Act may be warranted.

Taking

A taking has the meaning given to such term under the Endangered Species Act of 1973.

Appropriate Secretary

Appropriate Secretary has the meaning given to the term "Secretary" under section 3(15) of the Endangered Species Act of 1973.

Effective Date

The proposal is effective for taxable years beginning after December 31, 2007.

C. Allow Deduction for Endangered Species Recovery Expenditures

Present Law

Under present law, a taxpayer engaged in the business of farming may treat expenditures that are paid or incurred by him during the taxable year for the purpose of soil or water conservation in respect of land used in farming, or for the prevention or erosion of land used in farming, as expenses that are not chargeable to capital account. Such expenditures are allowed as a deduction, not to exceed 25 percent of the gross income derived from farming during the taxable year.[5] Any excess above such percentage is deductible for succeeding taxable years, not to exceed 25 percent of the gross income derived from farming during such succeeding taxable year.

Description of Proposal

The proposal provides that expenditures paid or incurred by a taxpayer engaged in the business of farming for the purpose of achieving site-specific management actions pursuant to the Endangered Species Act of 1973[6] to be treated the same as expenditures for the purpose of soil or water conservation in respect of land used in farming, or for the prevention or erosion of land used in farming, i.e., such expenditures are treated as not chargeable to capital account and are deductible subject to the limitation that the deduction may not exceed 25 percent of the farmer's gross income derived from farming during the taxable year.

Effective Date

The proposal is effective for expenditures paid or incurred after the date of enactment.

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[5] Sec. 175.

[6] 16 U.S.C. 1533(f)(B).

D. Provide Exclusion for Certain Payments and Programs Relating to Fish and Wildlife

Present Law

Under present law, gross income does not include the excludable portion of payments made to taxpayers by the Federal and State governments for a share of the cost of improvements to property under certain conservation programs.[7]

The excludable portion is the portion (or all) of a payment made under such programs that is determined by the Secretary of Agriculture to be made primarily for the purpose of conserving soil and water resources, protecting or restoring the environment, improving forests, or providing a habitat for wildlife, and is determined by the Secretary of the Treasury as not increasing substantially the annual income derived from the property. The excludable portion does not include that portion of any payment that is properly associated with an amount that is allowable as a deduction for the taxable year in which such amount is paid or incurred.

Applicable conservation programs include (1) the rural clean water program authorized by section 208(j) of the Federal Water Pollution Control Act, (2) the rural abandoned mine program authorized by section 406 of the Surface Mining Control and Reclamation Act of 1977, (3) the water bank program authorized by the Water Bank Act, (4) the emergency conservation measures program authorized by title IV of the Agricultural Credit Act of 1978, (5) the agriculture conservation program authorized by the Soil Conservation and Domestic Allotment Act, (6) the great plains conservation program authorized by section 16 of the Soil Conservation and Domestic Policy Act, (7) the resource conservation and development program authorized by the Bankhead-Jones Farm Tenant Act and by the Soil Conservation and Domestic Allotment Act, (8) the forestry incentives program authorized by section 4 of the Cooperative Forestry Assistance Act of 1978, (9) any small watershed program administered by the Secretary of Agriculture which is determined by the Secretary of the Treasury or his delegate to be substantially similar to the type of programs described in items (1) through (8), and (10) any program of a State, possession of the United States, a political subdivision of any of the foregoing, or the District of Columbia under which payments are made to individuals primarily for the purpose of conserving soil, protecting or restoring the environment, improving forests, or providing a habitat for wildlife.

Description of Proposal

The proposal expands the exclusion for the excludable portion of certain payments to include the excludable portion of payments made under the Partners for Fish and Wildlife Program authorized by the Partners for Fish and Wildlife Act, the Landowner Incentive Program, the State Wildlife Grants Program, and the Private Stewardship Grants Program authorized by the Fish and Wildlife Act of 1956.

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[7] Sec. 126.

Effective Date

The proposal is effective for payments received after the date of enactment.

E. Extend Expensing of Brownfields Remediation Costs

Present Law

Present law allows a deduction for ordinary and necessary expenses paid or incurred in carrying on any trade or business.[8] Treasury regulations provide that the cost of incidental repairs that neither materially add to the value of property nor appreciably prolong its life, but keep it in an ordinarily efficient operating condition, may be deducted currently as a business expense. Section 263(a)(1) limits the scope of section 162 by prohibiting a current deduction for certain capital expenditures. Treasury regulations define "capital expenditures" as amounts paid or incurred to materially add to the value, or substantially prolong the useful life, of property owned by the taxpayer, or to adapt property to a new or different use. Amounts paid for repairs and maintenance do not constitute capital expenditures. The determination of whether an expense is deductible or capitalizable is based on the facts and circumstances of each case.

Taxpayers may elect to treat certain environmental remediation expenditures that would otherwise be chargeable to capital account as deductible in the year paid or incurred.[9] The deduction applies for both regular and alternative minimum tax purposes. The expenditure must be incurred in connection with the abatement or control of hazardous substances at a qualified contaminated site. In general, any expenditure for the acquisition of depreciable property used in connection with the abatement or control of hazardous substances at a qualified contaminated site does not constitute a qualified environmental remediation expenditure. However, depreciation deductions allowable for such property, which would otherwise be allocated to the site under the principles set forth in Commissioner v. Idaho Power Co.[10] and section 263A, are treated as qualified environmental remediation expenditures.

A "qualified contaminated site" (a so-called "brownfield") generally is any property that is held for use in a trade or business, for the production of income, or as inventory and is certified by the appropriate State environmental agency to be an area at or on which there has been a release (or threat of release) or disposal of a hazardous substance. Both urban and rural property may qualify. However, sites that are identified on the national priorities list under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 ("CERCLA")[11] cannot qualify as targeted areas. Hazardous substances generally are defined by reference to sections 101(14) and 102 of CERCLA, subject to additional limitations applicable to asbestos and similar substances within buildings, certain naturally occurring substances such as radon, and certain other substances released into drinking water supplies due to deterioration through ordinary use, as well as petroleum products defined in section 4612(a)(3) of the Code.

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[8] Sec. 162.

[9] Sec. 198.

[10] 418 U.S. 1 (1974).

[11] Pub. L. No. 96-510 (1980).

In the case of property to which a qualified environmental remediation expenditure otherwise would have been capitalized, any deduction allowed under section 198 is treated as a depreciation deduction and the property is treated as section 1245 property. Thus, deductions for qualified environmental remediation expenditures are subject to recapture as ordinary income upon a sale or other disposition of the property. In addition, sections 280B (demolition of structures) and 468 (special rules for mining and solid waste reclamation and closing costs) do not apply to amounts that are treated as expenses under this provision.

Eligible expenditures are those paid or incurred before January 1, 2008.

The Gulf Opportunity Zone Act of 2005[12] added section 1400N(g) to the Code, which extended for two years (through December 31, 2007) the expensing of environmental remediation expenditures paid or incurred to abate contamination at qualified contaminated sites located in the Gulf Opportunity Zone. As a result of the extension of section 198 contained in the Tax Relief and Health Care Act of 2006,[13] eligible expenditures covered under both section 1400N(g) and section 198 must be paid or incurred prior to January 1, 2008.

Description of Proposal

The proposal extends the present law expensing provision under section 198 for three years through December 31, 2010.

Effective Date

The proposal is effective for expenditures paid or incurred after December 31, 2007.

[12] Pub. L. No. 109-135 (2005).

[13] Pub. L. No. 109-432 (2006).

F. Allowance of Section 1031 Treatment for Exchanges Involving Certain Mutual Ditch, Reservoir, or Irrigation Company Stock

Present Law

An exchange of property, like a sale, generally is a taxable event. However, no gain or loss is recognized if property held for productive use in a trade or business or for investment is exchanged for property of a "like-kind" which is to be held for productive use in a trade or business or for investment.[14] If section 1031 applies to an exchange of properties, the basis of the property received in the exchange is equal to the basis of the property transferred, decreased by any money received by the taxpayer, and further adjusted for any gain or loss recognized on the exchange. In general, section 1031 does not apply to any exchange of stock in trade or other property held primarily for sale; stocks, bonds or notes; other securities or evidences of indebtedness or interest; interests in a partnership; certificates of trust or beneficial interests; or choses in action.[15]

Description of Proposal

The proposal provides that the general exclusion from section 1031 treatment for stocks shall not apply to shares in a mutual ditch, reservoir, or irrigation company, if at the time of the exchange: (1) the company is an organization described in section 501(c)(12)(A) (determined without regard to the percentage of its income that is collected from its members for the purpose of meeting losses and expenses); and (2) the shares in the company have been recognized by the highest court of the State in which such company was organized or by applicable State statute as constituting or representing real property or an interest in real property.

Effective Date

The proposal is effective for transfers after the date of enactment.

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[14] Sec. 1031(a)(1).

[15] Sec. 1031(a)(2).

G. Modification of Effective Date of Leasing Provisions of the American Jobs Creation Act of 2004

Present Law

Present law provides for the deferral of losses attributable to certain tax exempt use property, generally effective for leases entered into after March 12, 2004. The deferral provision does not apply to property located in the United States that is subject to a lease with respect to which a formal application: (1) was submitted for approval to the Federal Transit Administration (an agency of the Department of Transportation) after June 30, 2003, and before March 13, 2004; (2) is approved by the Federal Transit Administration before January 1, 2006; and (3) includes a description and the fair market value of such property (the "qualified transportation property exception").

Description of Proposal

The proposal changes the effective date of the loss deferral rules with respect to certain leases. Under the proposal, the loss deferral rules also apply to leases entered into on or before March 12, 2004, if the lessee is a foreign person or entity. With respect to such leases, losses are deferred starting in taxable years beginning after December 31, 2006.

No inference is intended regarding the appropriate present-law tax treatment of transactions entered into prior to March 12, 2004, if the lessee is not a foreign person or entity. In addition, it is intended that the proposal shall not be construed as altering or supplanting the present-law tax rules providing that a taxpayer is treated as the owner of leased property only if the taxpayer acquires and retains significant and genuine attributes of an owner of the property, including the benefits and burdens of ownership. The proposal also is not intended to affect the scope of any other present-law tax rules or doctrines applicable to purported leasing transactions.

Effective Date

The proposal is effective as if included in the provisions of the American Jobs Creation Act of 2004 to which it relates.

JOINT COMMITTEE ON TAXATION
September 18, 2007
JCX-76-07

ESTIMATED REVENUE EFFECTS OF
THE "HABITAT AND LAND CONSERVATION ACT OF 2007,"
SCHEDULED FOR MARKUP BY THE COMMITTEE ON FINANCE ON SEPTEMBER 20, 2007

Fiscal Years 2008 - 2017

[Millions of Dollars]

Provision	Effective	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2008-12	2008-17
1. Make permanent the special rule for contributions of qualified conservation contributions	cmi tyba 12/31/07	-36	-46	-57	-69	-83	-86	-90	-94	-98	-102	-291	-761
2. Provide a tax credit for recovery and restoration of endangered species	tyba 12/31/07	-12	-75	-117	-196	-244	-257	-201	-135	-66	-33	-644	-1,335
3. Allow a deduction for endangered species recovery expenditures	epoia DOE	-14	-21	-24	-29	-35	-40	-47	-54	-63	-73	-122	-399
4. Provide an exclusion for certain payments and programs relating to fish and wildlife	pra DOE	-3	-5	-6	-6	-6	-6	-6	-6	-6	-6	-26	-55
5. Extend expensing of Brownfields remediation costs (sunset 12/31/10)	epoia 12/31/07	-227	-368	-353	-98	76	80	78	70	61	52	-971	-630
6. Allowance of section 1031 treatment for exchanges involving certain mutual ditch, reservoir, or irrigation company stock	tyba DOE	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	-1	-2
7. Modify the effective date for the application of the AJCA 2004 leasing (SILO) provision - apply loss limitation to leases with foreign entities regardless of when the lease was entered into	tyba 12/31/06	2,680	896	407	290	288	260	135	-239	-629	-854	4,561	3,235
NET TOTAL		**2,388**	**381**	**-150**	**-108**	**-4**	**-49**	**-131**	**-458**	**-801**	**-1,016**	**2,506**	**53**

Joint Committee on Taxation

NOTE: Details may not add to totals due to rounding. Date of enactment is assumed to be October 1, 2007.

Legend for "Effective" column:
cmi = contributions made in
DOE = date of enactment
epoia = expenditures paid or incurred after
pra = payments received after
tyba = taxable years beginning after

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

COLLOQUY – CONSERVATION EASEMENT

Mr. Chairman:

I appreciate your bringing forward this legislation regarding land conservation. It includes legislation that you and I worked on to encourage farmers and ranchers to contribute conservation easements. I was pleased to have this legislation be part of the charitable package that was signed into law last Congress and am pleased to have it being made permanent here today.

However, I am very concerned that we have not done more at this time to deal with the ongoing abuses the IRS is seeing in the area of donations of easements. We have all talked a great deal about the tax gap in this committee – and that certainly important. As we all know, the tax gap is made of many little items and there is no question that problems with conservation easements is a part of the tax gap problem.

The IRS Commissioners in two letters to you and me, Mr. Chairman, have highlighted the problems of conservation easements as one of the top problems the IRS faces in the tax-exempt area. In addition, the IRS has placed conservation easement abuses on its annual dirty dozen list of notorious tax scams in recent years.

While we passed reform legislation that took a good bite at the apple in dealing with these problems, the fact that the IRS continues to see this as a problem tells me more work is needed. The IRS is doing what it can having opened 900 examinations of easements – but this is extraordinarily time intensive and burdensome work for the IRS. Dealing with the tax gap means dealing with problems other than with a hammer and an anvil.

I offer an amendment today that is a fair compromise to the abuses we see out there. I had earlier looked at simply doing away with certain types of easements that are highly suspect – such as those for golf courses As a compromise, I proposed an amendment that provided that in those cases where the Secretary found a likelihood of possible abuse, the donor needed to first get approval from the IRS. I would remind my colleagues that is was only a little over three years ago that we had to read headline after headline in the Washington Post about abuses in easement donations involving The Nature Conservancy and other organizations.

Mr. Chairman, I want to move this conservation bill forward today and hope that we can work together, as we always have, to deal with this problem of the tax gap.

Chairman Baucus:

I appreciate the concerns you've raised and agree we need to make certain that we address abuses in this area. I will have our staffs continue to work on balanced reforms that deal with the problems at hand while providing that the intended benefits of encouraging conservation easements can be realized.

Senator Grassley:

I thank the Chairman.

Statement of Senator Jon Kyl
Senate Finance Committee Consideration of Proposed Legislation Implementing
the U.S.-Peru Trade Promotion Agreement
September 21, 2007

Mr. Chairman, before I address the Peru Free Trade Agreement (FTA), I would like to encourage the Finance Committee to take up and approve the U.S-Colombia FTA as soon as possible. Of all of the FTAs that are pending in one form or another before the Committee, I believe Colombia is the most important, from a geo-political standpoint.

While the Colombia FTA has the exact same labor, environment, and intellectual property problems as the Peru agreement, I am willing to set aside my concerns for that one agreement only because it is simply too important to our country, our citizens, and the world that Colombia, which has taken many difficult and dangerous steps in combating drug traffickers, continue on its path as a responsible state.

I have never opposed a free trade agreement, although I have sometimes had reservations or concerns about different elements of the agreements. I take my vote against the Peru FTA today extremely seriously. I have decided to oppose the Peru FTA not because I have any quarrel with Peru. In fact, I strongly support the original Peru FTA.

My opposition to the FTA is caused by the agreement reached by the U.S. Trade Representative with Representatives Rangel and Levin in May of this year. That agreement forced the U.S. to renegotiate the Peru, Panama, and Colombia FTAs to add new requirements for labor and environmental protections and weakened traditional trade agreement protections for certain U.S. intellectual property related to pharmaceutical products.

I am concerned about the labor and environment provisions, but I am simply puzzled by the intellectual property changes. I am not sure what my colleagues hoped to gain by weakening standard protections for U.S. intellectual property through this trade agreement. I see no reason why U.S. legislators would want to weaken the ordinary protections that are normally accorded to pharmaceutical intellectual property in our bilateral trade agreements. Peru did not, in the course of negotiations, ask us to weaken the IP requirements. Peru was perfectly willing to abide by the greater protections of the original FTA.

If Representatives Rangel and Levin hoped to provide better access to life-saving medicines in Peru, I worry that their action could have the exact opposite result. Countries with weaker IP protections will have a difficult time encouraging U.S. companies to do business there.

And why should we expect that those who want to weaken protections for U.S.-owned intellectual property will stop at pharmaceuticals? Are computers, movies, music, and other products that involve valuable U.S. intellectual property next? U.S. intellectual property is one of our most valuable exports; we should not unilaterally weaken protections for it.

I cannot imagine that Chairman Baucus would agree to a trade agreement that treated Montana wheat in a manner that was worse than other, prior trade agreements. The Chairman may be interested to know that, according to the State of Montana, pharmaceutical product exports increased threefold in Montana from 2005 to 2006. I hope the Chairman will reconsider his support for weakening the IP protections for pharmaceuticals in future trade agreements.

I would like to share some statistics that underscore my concern for protecting U.S. intellectual property. First, employees in IP-related industries earn on average significantly more than employees in non-IP related industries—according to some studies as much as 40 to 50 percent more. That means that devaluing U.S. intellectual property will hurt U.S. workers. Further, economists estimate that over 50 percent of U.S. exports depend upon intellectual property protection of some sort, up from below 10 percent 50 years ago. My colleagues know that theft of U.S. intellectual property is rampant overseas, costing U.S. companies many billions of dollars annually and costing the U.S. economy high-paying jobs. We should use FTAs to enhance protection for U.S. intellectual property, not weaken it.

As I said, I also have concerns about the labor and environment provisions, and I encourage the Chairman and Ranking Member to reconsider their support for these types of provisions, just as I urge them to give additional thought to whether it is wise to unilaterally weaken the intellectual property protections we normally include in FTAs.

Again, in closing, I urge you, Mr. Chairman, to bring the Colombia agreement before this committee as soon as possible. And I urge you to insist upon our prior, stronger IP protections in all future trade agreements.

Statement of Senator Jon Kyl for the Record
"American Infrastructure Investment and Improvement Act"
September 21, 2007

Mr. Chairman, I want to express my disappointment that the Finance Committee moved forward today with consideration of the "American Infrastructure Investment and Improvement Act." I am disappointed because I had hoped that the differences between the general aviation interests and the commercial aviation interests would have been resolved before the committee considered this bill. I voted against the bill to express my view that the committee mark-up was premature.

Rather than force Senators to vote "for" one interest and "against" another interest, I believe the Chairman and Ranking Member should have continued their discussions with Senators Lott and Rockefeller. The issues that were under debate – how to finance the necessary modernization of the air traffic control system and whether it is possible to better allocate the funding burden between commercial air passengers and business jets – will still need to be resolved before the legislation can be brought before the full Senate for consideration. I believe it would have been more responsible for the Committee to resolve those issues before proceeding with the mark-up.

As is typical of most states, Arizona has very strong interests in both general aviation and commercial aviation, and I have always strived to lend strong support to both segments of the aviation industry. Arizona is a large state with widely-spread rural communities and smaller towns. That makes general aviation essential to many business-owners in Arizona. But at the same time, Arizona has a fast-growing population that travels on the commercial airlines for its business and vacation needs. Moreover, Arizona, with its mild winter climate, beautiful resorts, and spectacular natural beauty, is a top vacation destination. In 2006, nearly 34 million domestic and international air travelers visited Arizona. The commercial air carriers that bring these millions of visitors to our state are an essential component of Arizona's economy.

While today's mark-up advances a simple four-year extension and increase of existing taxes, I urge the Chairman and Ranking Member to make another attempt to reach an agreement about how to pay for modernizing the air traffic control system and consider ways to better allocate the burdens of the system.

Senator Olympia J. Snowe
Senate Finance Committee Mark-up
Statement on the U.S.-Peru Trade Promotion Agreement
September 21, 2007

Thank you, Mr. Chairman, for holding this mark-up. I voted against an earlier version of the agreement before the committee today, after an amendment to add binding, internationally-recognized labor standards failed by one vote at the July 2006 mock mark-up. The standards which nine of my colleagues on this committee and I sought to make enforceable under this agreement included the following five fundamental labor rights set forth in the *International Labor Organization Declaration on Fundamental Principles and Rights at Work*:

- **The freedom of workers to associate;**
- **The effective recognition of the right to collective bargaining;**
- **The elimination of all forms of forced or compulsory labor;**
- **The abolition of child labor; and**
- **The elimination of employment discrimination.**

Despite this committee's failure to recommend the protection of these common-sense rights—as well as the right to acceptable conditions of work with respect to minimum wages, hours of work, and occupational safety and health--as binding obligations in the agreement, the administration subsequently—albeit reluctantly— included them after further consultations with Congress.

The inclusion of these binding labor standards potentially marks the beginning of a new chapter in U.S. trade policy. Whereas previous Free Trade Agreements have made reference to these standards, the agreement before us today represents the first instance in which they are treated as fully enforceable obligations of the parties, no different from any other provision of the agreement.

Some of my esteemed colleagues on this committee oppose this new approach, and feel that a trade agreement is not an appropriate document in which to include an enforceable obligation to adhere to these standards. Let me explain precisely why this trade agreement, and those that will be modeled on it, are in fact the *most* appropriate mechanism for ensuring compliance with fundamental labor rights.

I know that many if not all of my colleagues will agree that American companies and workers can successfully compete in the global economy, so long as other countries are not free to stack the deck against U.S. firms by engaging in unfair practices which artificially lower production costs and therefore the prices of foreign goods. Among the most reprehensible and egregious of these is the exploitation of labor.

Appalling on moral grounds alone, the use of child, forced or exploited labor continues in major trade partners of the United States, including China. It has been estimated that in 2006 only 20 percent of Chinese suppliers of manufactured goods met China's own wage laws, while a mere 5 percent complied with that country's working hours requirements. Similarly objectionable were reports that emerged in May 2006 of labor abuses in Jordanian factories that made goods destined for the U.S. market. These claims of forced labor and human trafficking would be horrifying no matter where they took place– but in this case, such inhumane practices were taking place in a country with which the United States already has a Free Trade Agreement!

In fact, the Jordanian FTA specifically listed out four of the five fundamental labor standards I mentioned, but obligated Jordan only to "strive to ensure that such... labor rights... are recognized and protected by domestic law." Thus, when an actual violation of those rights occurred, the U.S. had no means to enforce those obligations as it could the other non-labor provisions of the FTA. That is why it is not only appropriate but essential to demand that

these labor standards be binding and enforceable in the agreement before us today, and in all trade agreements going forward.

The people of my home state of Maine are all too familiar with the consequences of our Government's failure to enforce the trade obligations of our trade partners. Besides the obvious human rights concerns these despicable practices raise, they also put U.S. workers and businesses– which must adhere to our robust labor laws– at risk from unfair competition by foreign producers who willfully exploit workers in their facilities. Since 2000, the U.S. has lost approximately 3 million, or 17%, of its manufacturing jobs. Maine has lost over 21,000 jobs, representing over 26 percent of our manufacturing workforce!

That is also why I carefully consider the impact on Maine jobs of each trade agreement presented to this committee. Constituting less than 1% of total U.S. trade, the U.S.-Peru trade relationship is a relatively small one. To the Maine industries involved in that trade, however, every sale counts. For example, Maine's paper industry-- which in the past few months saw the devastating closure of two production facilities run by manufacturers Domtar and Fraser— exported over one million dollars of its product to Peru last year. Similarly, Maine's chemical, machinery and electronics manufacturers each benefit from modest but critical sales to the Peruvian market.

Because of the ongoing and potential benefit to these key industries in Maine, and because of the critical need to ensure that the binding labor provisions included for the first time are not abandoned to appease their critics, I have decided not to oppose this particular trade agreement. As we move forward in considering other agreements that come before the Senate, I will remain vigilant in my efforts to see that the concerns of manufacturers in Maine and elsewhere are adequately addressed. Because when it comes to protecting the livelihood of America's workers– no threat is too small.

Thank you, Mr. Chairman.

Senator Pat Roberts
Statement for the Record
Senate Finance Committee
Executive Session
September 21, 2007

Mr. Chairman, Mr. Grassley, thank you for your leadership on these matters today. You've had a tremendous task before you and I appreciate you and your staff's attention to detail and efforts to listen to all involved.

It's no secret that this committee is passionate about aviation. Thankfully we all agree that modernization of our Air Traffic Control (ATC) system is necessary. The committee's mark recognizes the importance of modernization and recognizes what many of us said during hearings on this matter: everyone will have to pay more.

Under this proposal the general aviation (GA) community bears the largest brunt of the increase. The vast majority of this community is made up of personal pilots who fly and own their own planes. They are small business owners and operators in rural America, often in areas not served by commercial airlines.

Yet these folks understand the need for modernization and have offered an increase in their taxes to help pay for it. Mr. Chairman, I don't know if I've ever had an industry approach me volunteering to pay more taxes. The underlying mark we're discussing today pins about two-thirds of the new money on general aviation.

According to the Department of Transportation's recent analysis, commercial airline profits are up again for the quarter and for the first time since 2000, the airline industry has had five consecutive profitable quarters. We've spent a lot of taxpayer dollars helping the airline industry since the September 11th attacks. I believe it was a shade over $5 billion in direct funding and $10 billion in loan guarantees in one bill alone. We've paid insurance premiums, and helped with pensions.

The airlines were back flying two days after September 11, 2001, while general aviation was grounded for months. 25 percent of the workforce was let go and the economy of Kansas, where over 70 percent of the worlds GA planes are built, suffered greatly. Thankfully those days are behind us. Airline profits are up and general aviation is making a comeback.

With these positive market signals, now is the time to modernize our aviation system to ensure its longevity and maximize its efficiency. Let me just point out, the reason all parties are calling for modernization, including the FAA, is to reduce airline congestion. While some blame general aviation for congestion, this simply isn't true. Congestion is the result of weather and the airlines' decisions regarding flight schedules. Modernization will help, but the airlines also will have to make decisions about their operations. Because of this, modernization should not be paid entirely by general aviation.

The underlying mark sets the general aviation contribution at 65 percent of the new money for modernization. That's quite a load to bear. A few members of this committee want to shift more of the financial burden on to general aviation. Several statements were made in an attempt to justify increasing GA's financial burden beyond the committee's mark. I'd like to clarify some misconceptions that I believe formed the basis of those statements.

Senator Rockefeller cited FAA's recent Cost Allocation Study which assigned 16 percent of Air Traffic Control (ATC) costs to the general aviation community as a reason to increase their taxes even further. While the airlines like to tout this study because it benefits their needs, they are not as quick to respond to the growing concerns over this study's methodology and results.

The FAA study divided ATC users merely into two groups; high-performance aircraft and piston engine aircraft. The high-performance group includes all turbine powered fixed wing aircraft. This puts a small turbine powered Cessna in the same category as an Airbus A380. GAO questioned this methodology in their testimony before the Subcommittee on Aviation in the House Committee on Transportation and Infrastructure. GAO's testimony went on to state that had FAA undergone a more accurate methodology, the effect would likely have decreased general aviation's allocation under that study.

Outside analysis of FAA's Cost Allocation study confirms GAO's criticisms. Furthermore, if a more appropriate approach to the cost allocation study had been taken, general aviation's allocation would likely be reduced from 16 percent to between 7.5 and 9.5 percent.

Another misconception the airlines like to perpetuate is that commercial carriers currently pay 97 percent of the taxes used to fill the Airport and Airway Trust Fund. This is another attempt to unfairly paint the general aviation community as not paying their fair share. According to the 2005 IRS Certified Airport and Airway Trust Fund data, U.S. Commercial Passenger Carriers paid 64 percent of the fund. If you include Regional Airlines, their share increases to 77 percent. According to the same data, general aviation's share totaled 8 percent.

When you add the estimated $250 million in increased taxes paid by general aviation in the underlying mark, GA's contribution to the total trust fund mirrors what an accurate cost allocation study would attribute to GA, about 10 percent. It appears to me the underlying mark does provide an equitable distribution of taxes on users.

Next, Senator Rockefeller and Lott proposed an amendment that would increase the general aviation jet fuel tax by an additional 16 cents per gallon, this is above the 36 cent rate in the underlying mark. The authors claim this tax would only apply to GA jet aircraft and would keep smaller GA aircraft taxed at the underlying mark's level. What my colleagues may not realize is that many of general aviation's small aircraft are propeller powered that use jet fuel.

I'd like to submit for the record a comparison of small general aviation planes that use jet

fuel and would have to pay this additional fuel tax increase should the amendment be adopted. What you can't see in the pictures is a measurable difference between a piston powered plane and its turbine powered counterpart.

Senators Rockefeller and Lott have also argued that the taxes imposed on commercial airlines, paid by passengers, should be reduced in order to lower passenger airfares. Twice before the federal government has allowed either the carrier taxes or fees to lapse. According to GAO, when the fees and taxes were reduced, passengers saw no savings in ticket prices. Commercial airlines increased their fares to make up the difference between the lapsed taxes/fees and what the passengers paid when they were in affect.

Commercial airline representatives admit that reducing airline taxes won't translate into savings for passengers. I'd like to quote an article from *The Politico* which ran on September 19th, 2007. "Whichever side wins, don't expect ticket prices to drop. '[User fees] mean that there is less tax demand on carriers,' says May. 'Whether it results in lower prices, no one can predict."

If we look back on history to provide us a glimpse of the future, we see that lessening the tax burden on commercial airlines will not lead to lower ticket prices for passengers. But it certainly will lead to increased profits for the airlines at a time when they are enjoying records profits.

Another claim Senator Rockefeller made was that highway users pay about 61 cents per gallon in taxes and that this is a higher rate than general aviation users. This too is a mis-characterization of facts. The federal excise tax on gasoline is 18.4 cents per gallon. Senator Rockefeller took the liberty of adding state gasoline taxes in his number. The underlying mark increases the federal aviation jet fuel tax to 36 cents per gallon, nearly twice as much as the federal tax on gasoline.

If we add state and local taxes on fuel to meet Senator Rockefeller's 61 cent per gallon figure, we find that general aviation users again pay much higher fuel taxes. Take for example Illinois. The state imposes a 6.25 percent sales tax on jet fuel. Local governments also have authority to charge additional taxes. Customers at Chicago Midway pay a total of 9 percent in sales tax. Based on recent fuel prices and including the 36 cent per gallon tax in the underlying mark, GA customers would pay about 80 cents in federal, state and local jet fuel taxes.

The result is similar in California. California imposes a 7.25 percent sales tax plus a 2 cent excise tax on non-commercial aviation jet fuel. In Van Nuys, again taking into account recent fuel prices and the underlying mark, GA customers would pay 73 cents per gallon on GA jet fuel taxes.

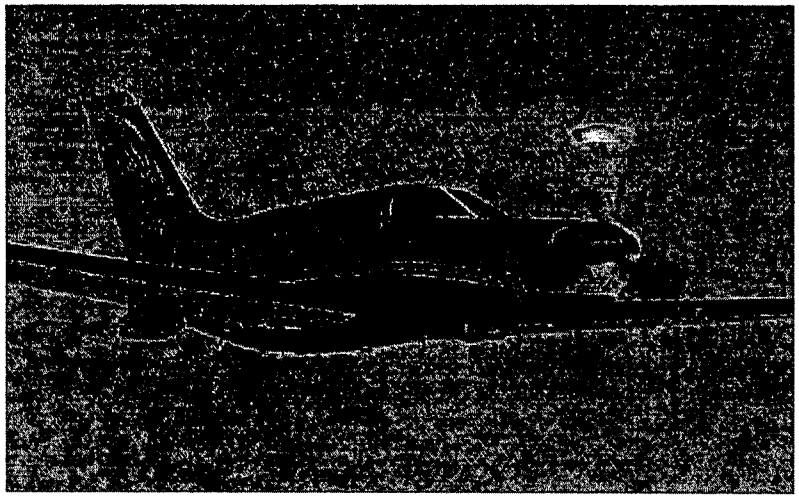
I appreciate Senator Rockefeller's concern for highway users; however, we must compare apples with apples. If his highway tax figure includes federal, state and local taxes, it's only fair

to apply the same taxes to the general aviation tax figure.

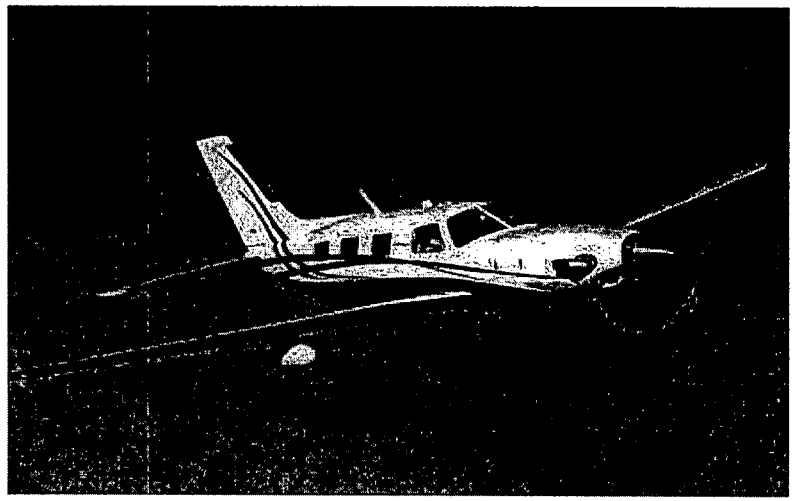
The final comment by Senator Rockefeller that I'll respond to addresses his example of a businessman using his or his company's plane to transport his daughter to school. While I do not know all of the details of this particular case and am not a tax attorney, I will say that if that businessman is deducting that trip on his tax returns, it sounds like tax fraud to me. That case shows the need for strong law enforcement, not a new law.

Mr. Chairman and Mr. Grassley, again I appreciate the opportunity to respond to the comments of my colleagues. I also thank you for moving this important piece of legislation forward. The underlying mark is a true example of compromise and bipartisanship. While I do have concerns over the treatment of fractionally owned aircraft in the mark, I understand the Chairman and Ranking Member are willing to keep working on this as the bill progresses.

“Small” GA is also turbine-powered

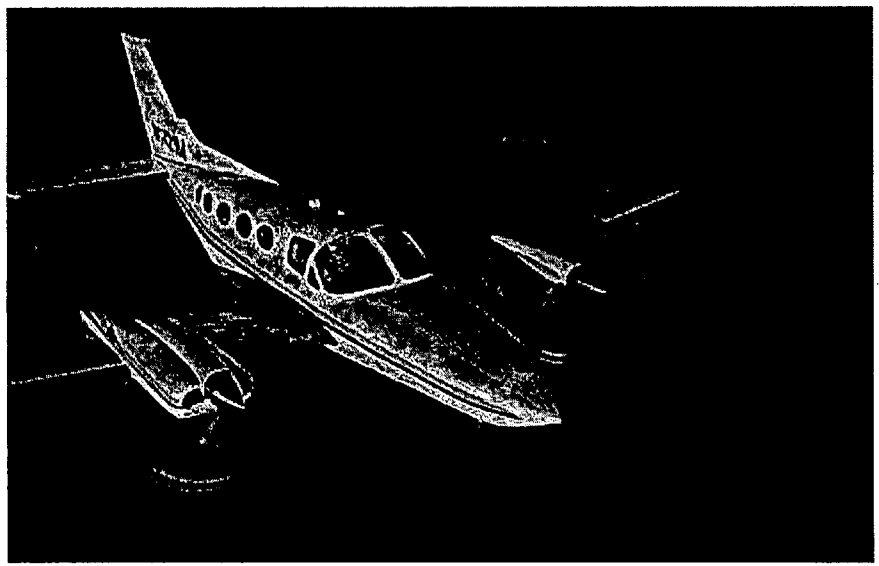


Piper Meridian - piston

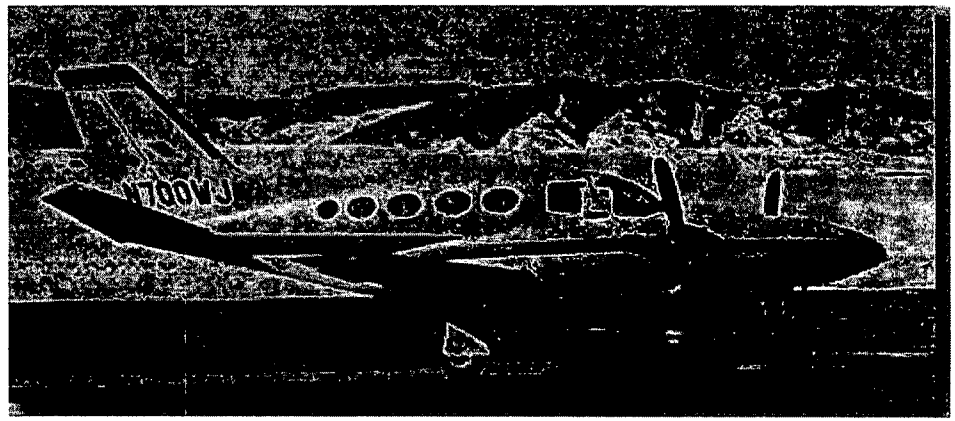


Piper Mirage - turbine

“Small” GA is also turbine-powered

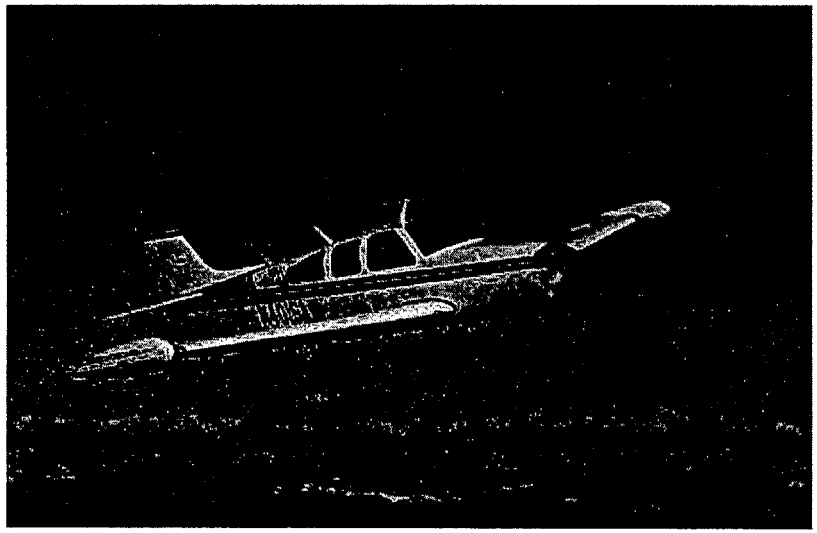


Cessna 421 - piston

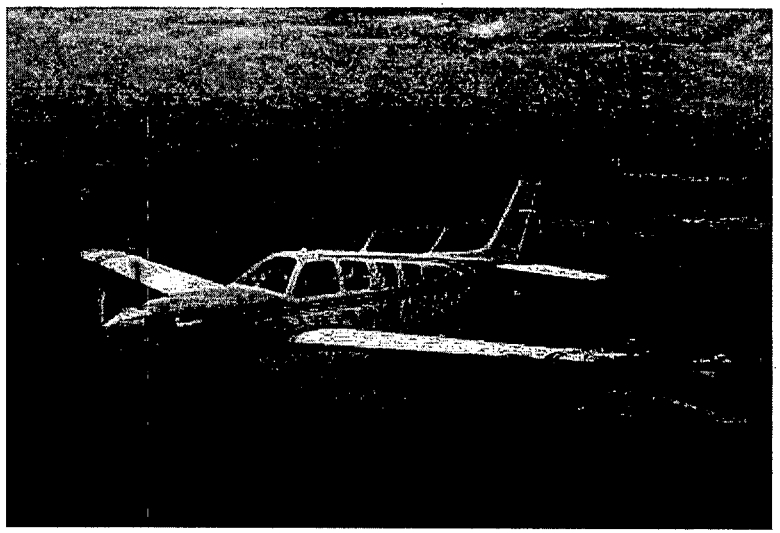


Cessna 425 - turbine

“Small” GA is also turbine-powered

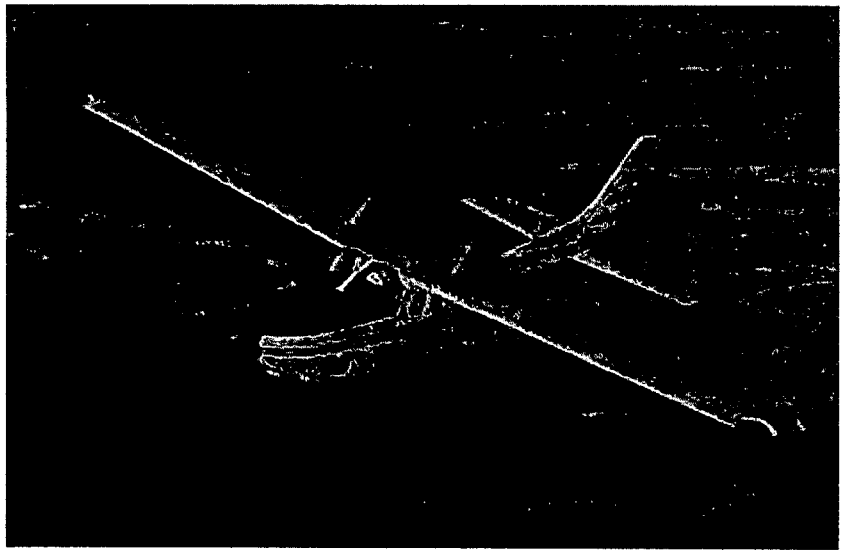


Beechcraft Bonanza - piston

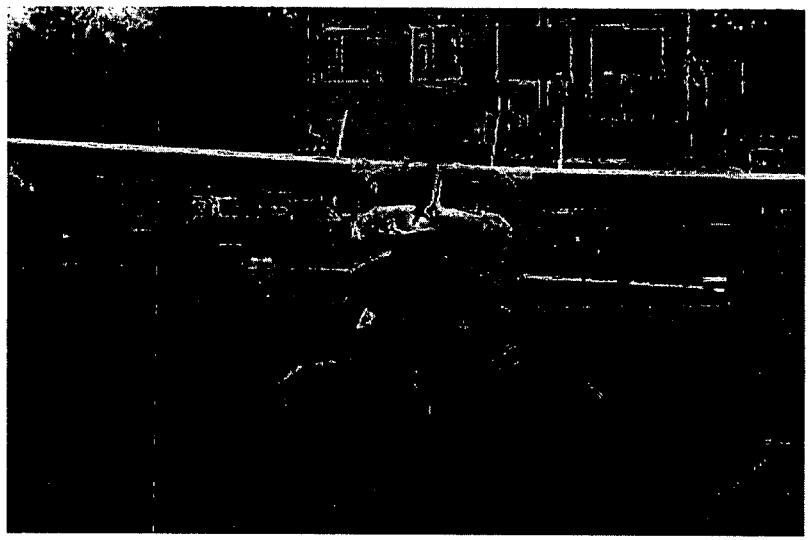


Beechcraft Bonanza - turbine

"Small" GA is also turbine-powered



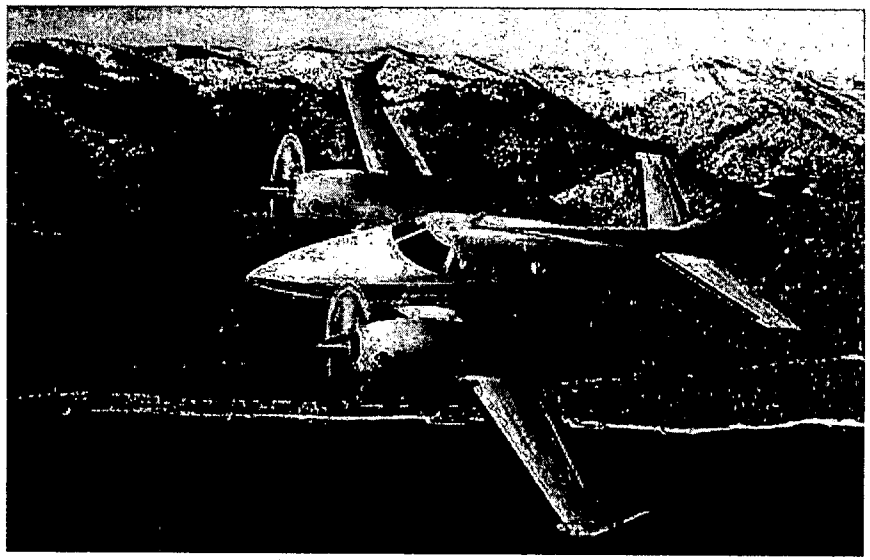
Cessna 210 - piston



Cessna 210 - turbine

“Small” GA is also turbine-powered

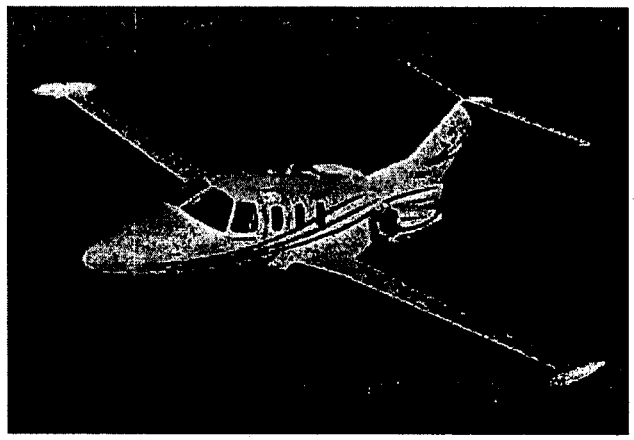
Beechcraft Duke - piston

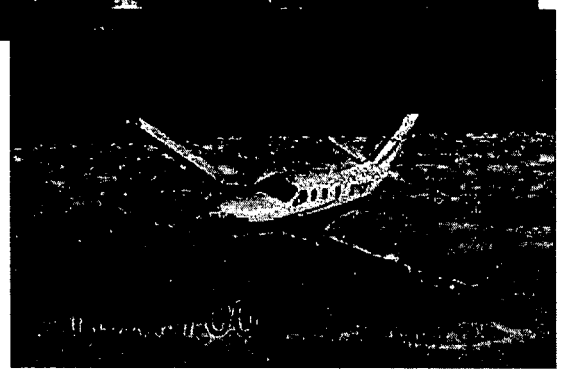


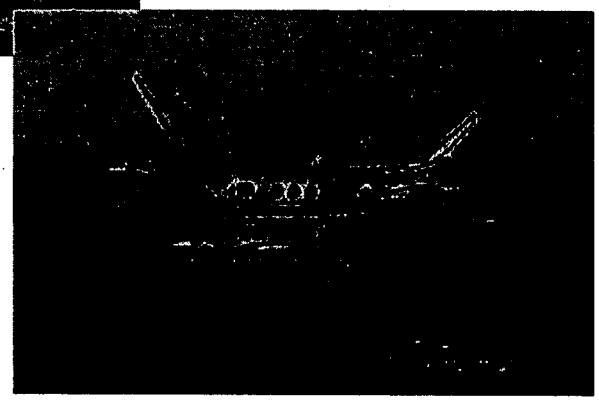
Beechcraft Duke - turbine

Owner-flown turbo-props and jets

- 4 – 6 seats
- Small, fuel efficient
- Turbine-powered







United States Senate
COMMITTEE ON ENVIRONMENT AND PUBLIC WORKS
WASHINGTON, DC 20510–6175

September 19, 2007

The Honorable Max Baucus
Chairman
Committee on Finance
219 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Charles Grassley
Ranking Member
Committee on Finance
219 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Baucus and Ranking Member Grassley:

We write to support your efforts to ensure the solvency of the Highway Trust Fund through 2009.

The Congressional Budget Office has projected we will face a shortfall of $4.3 billion in 2009 and further shortfalls in subsequent years unless additional revenues can be generated. As the Chairman and Ranking Member of the Committee which has jurisdiction over the Federal-Aid Highway program funded by the Highway Trust Fund, we are particularly interested in maintaining its solvency so that funding levels set in the Safe Accountable Flexible Efficient Transportation Equity Act: a Legacy for Users (P.L. 109-59) can continue to be met. We cannot afford to cut back on investment in our nation's infrastructure.

Thank you for your efforts in securing America's transportation programs.

Sincerely,

Barbara Boxer
Chairman

James M. Inhofe
Ranking Member