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REVENUE ACT OF 1978

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REVENUE ACT OF 1978

OCTOBER 15 (legislative day, OCTOBER 14), 1978.—Ordered to be printed

Mr. ULLMAN, from the committee of conference, submitted the following

CONFERENCE REPORT

[To accompany H.R. 13511]

The committee of conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill (H.R. 13511) to amend the Internal Revenue Code of 1954 to reduce income taxes, and for other purposes, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the House recede from its disagreement to the amendment of the Senate and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

SECTION 1. SHORT TITLE; TABLE OF CONTENTS

(*a*) *SHORT TITLE.—This Act may be cited as the "Revenue Act of 1978"*

(*b*) *TABLE OF CONTENTS.—*

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SEC. 2. AMENDMENT OF 1954 CODE.

Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1954.

SEC. 3. POLICY WITH RESPECT TO ADDITIONAL TAX REDUCTIONS.

As a matter of national policy the rate of growth in Federal outlays, adjusted for inflation, should not exceed one percent per year between fiscal year 1979 and fiscal year 1983; Federal outlays as a percentage of gross national product should decline to below 21 percent in fiscal year 1980, 20.5 percent in fiscal year 1981, 20 percent in fiscal year 1982 and 19.5 percent in fiscal year 1983; and the Federal budget should be balanced in fiscal years 1982 and 1983. If these conditions are met, it is the intention that the tax-writing committees of Congress will report legislation providing significant tax reductions for individuals to the extent that these tax reductions are justified in the light of prevailing and expected economic conditions.

TITLE I—PROVISIONS PRIMARILY AFFECTING INDIVIDUAL INCOME TAX

Subtitle A—Tax Reductions and Extensions

SEC. 101. WIDENING OF BRACKETS; RATE CUTS IN CERTAIN BRACKETS; INCREASE IN ZERO BRACKET AMOUNTS.

(a) RATE REDUCTION.—Section 1 (relating to tax imposed) is amended to read as follows:

"SECTION 1. TAX IMPOSED.

"(a) MARRIED INDIVIDUALS FILING JOINT RETURNS AND SURVIVING SPOUSES.—There is hereby imposed on the taxable income of—

"(1) every married individual (as defined in section 143) who makes a single return jointly with his spouse under section 6013, and

"(2) *every surviving spouse (as defined in section 2(a)), a tax determined in accordance with the following table:*

"If taxable income is:	*The tax is:*
Not over $3,400	*No Tax.*
Over $3,400 but not over $5,500	*14% of excess over $3,400.*
Over $5,500 but not over $7,600	*$294, plus 16% of excess over $5,500.*
Over $7,600 but not over $11,900	*$630, plus 18% of excess over $7,600.*
Over $11,900 but not over $16,000	*$1,404, plus 21% of excess over $11,900.*
Over $16,000 but not over $20,200	*$2,265, plus 24% of excess over $16,000.*
Over $20,200 but not over $24,600	*$3,273 plus 28% of excess over $20,200.*
Over $24,600 but not over $29,900	*$4,505, plus 32% of excess over $24,600.*
Over $29,900 but not over $35,200	*$6,201 plus 37% of excess over $29,900.*
Over $35,200 but not over $45,800	*$8,162, plus 43% of excess over $35,200.*
Over $45,800 but not over $60,000	*$12,720 plus 49% of excess over $45,800.*
Over $60,000 but not over $85,600	*$19,678, plus 54% of excess over $60,000.*
Over $85,600 but not over $109,400	*$33,502, plus 59% of excess over $85,600.*
Over $109,400 but not over $162,400	*$47,544, plus 64% of excess over $109,400.*
Over $162,400 but not over $215,400	*$81,464, plus 68% of excess over $162,400.*
Over $215,400	*$117,504, plus 70% of excess over $215,400.*

"(b) HEADS OF HOUSEHOLDS.—*There is hereby imposed on the taxable income of every individual who is the head of a household (as defined in section 2(b)) a tax determined in accordance with the following table:*

"If taxable income is:	*The tax is:*
Not over $2,300	*No tax.*
Over $2,300 but not over $4,400	*14% of excess over $2,300.*
Over $4,400 but not over $6,500	*$294, plus 16% of excess over $4,400.*
Over $6,500 but not over $8,700	*$630, plus 18% of excess over $6,500.*
Over $8,700 but not over $11,800	*$1,026, plus 22% of excess over $8,700.*
Over $11,800 but not over $15,000	*$1,708 plus 24% of excess over $11,800.*
Over $15,000 but not over $18,200	*$2,476, plus 26% of excess over $15,000.*
Over $18,200 but not over $23,500	*$3,308, plus 31% of excess over $18,200.*
Over $23,500 but not over $28,800	*$4,951, plus 36% of excess over $23,500.*
Over $28,800 but not over $34,100	*$6,859, plus 42% of excess over $28,800.*
Over $34,100 but not over $44,700	*$9,085, plus 46% of excess over $34,100.*
Over $44,700 but not over $60,600	*$13,961, plus 54% of excess over $44,700.*
Over $60,600 but not over $81,800	*$22,547, plus 59% of excess over $60,600.*
Over $81,800 but not over $108,300	*$35,055, plus 63% of excess over $81,800.*
Over $108,300 but not over $161,300	*$51,750, plus 68% of excess over $108,300.*
Over $161,300	*$87,790, plus 70% of excess over $161,300.*

"(c) UNMARRIED INDIVIDUALS (OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLDS).—*There is hereby imposed on the taxable income of every individual (other than a surviving spouse as defined in section 2(a) or the head of a household as defined in section 2(b)) who is not a married individual (as defined in section 143) a tax determined in accordance with the following table:*

"If taxable income is:	*The tax is:*
Not over $2,300	*No tax.*
Over $2,300 but not over $3,400	*14% of excess over $2,300.*
Over $3,400 but not over $4,400	*$154, plus 16% of excess over $3,400.*
Over $4,400 but not over $6,500	*$314, plus 18% of excess over $4,400.*
Over $6,500 but not over $8,500	*$692, plus 19% of excess over $6,500.*
Over $8,500 but not over $10,800	*$1,072, plus 21% of excess over $8,500.*
Over $10,800 but not over $12,900	*$1,555, plus 24% of excess over $10,800.*
Over $12,900 but not over $15,000	*$2,059, plus 26% of excess over $12,900.*
Over $15,000 but not over $18,200	*$2,605, plus 30% of excess over $15,000.*
Over $18,200 but not over $23,500	*$3,565, plus 34% of excess over $18,200.*
Over $23,500 but not over $28,800	*$5,367, plus 39% of excess over $23,500.*
Over $28,800 but not over $34,100	*$7,434, plus 44% of excess over $28,800.*
Over $34,100 but not over $41,500	*$9,766, plus 49% of excess over $34,100.*
Over $41,500 but not over $55,300	*$13,392, plus 55% of excess over $41,500.*
Over $55,300 but not over $81,800	*$20,982, plus 63% of excess over $55,300.*
Over $81,800 but not over $108,300	*$37,677, plus 68% of excess over $81,800.*
Over $108,300	*$55,697, plus 70% of excess over $108,300.*

"(d) MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—*There is hereby imposed on the taxable income of every married individual (as defined in section 143) who does not make a single return jointly with his spouse under section 6013 a tax determined in accordance with the following table:*

"If taxable income is:	*The tax is:*
Not over $1,700	*No tax.*
Over $1,700 but not over $2,750	*14% of excess over $1,700.*
Over $2,750 but not over $3,800	*$147, plus 16% of excess over $2,750.*
Over $3,800 but not over $5,950	*$315, plus 18% of excess over $3,800.*
Over $5,950 but not over $8,000	*$702, plus 21% of excess over $5,950.*
Over $8,000 but not over $10,100	*$1,132.50, plus 24% of excess over $8,000.*
Over $10,100 but not over $12,300	*$1,636.50, plus 28% of excess over $10,100.*
Over $12,300 but not over $14,950	*$2,252.50, plus 32% of excess over $12,300.*
Over $14,950 but not over $17,600	*$3,100.50, plus 37% of excess over $14,950.*
Over $17,600 but not over $22,900	*$4,081, plus 43% of excess over $17,600.*
Over $22,900 but not over $30,000	*$6,360, plus 49% of excess over $22,900.*
Over $30,000 but not over $42,800	*$9,839, plus 54% of excess over $30,000.*
Over $42,800 but not over $54,700	*$16,751, plus 59% of excess over $42,800.*
Over $54,700 but not over $81,200	*$23,772, plus 64% of excess over $54,700.*
Over $81,200 but not over $107,700	*$40,732, plus 68% of excess over $81,200.*
Over $107,700	*$58,752, plus 70% of excess over $107,700.*

"(e) ESTATES AND TRUSTS.—There is hereby imposed on the taxable income of every estate and trust taxable under this subsection a tax determined in accordance with the following table:

"If taxable income is:	The tax is:
Not over $1,050	14% of taxable income.
Over $1,050 but not over $2,100	$147, plus 16% of excess over $1,050.
Over $2,100 but not over $4,250	$315, plus 18% of excess over $2,100.
Over $4,250 but not over $6,300	$702, plus 21% of excess over $4,250.
Over $6,300 but not over $8,400	$1,132.50, plus 24% of excess over $6,300.
Over $8,400 but not over $10,600	$1,636.50, plus 28% of excess over $8,400.
Over $10,600 but not over $13,250	$2,252.50 plus 32% of excess over $10,600.
Over $13,250 but not over $15,900	$3,100.50, plus 37% of excess over $13,250.
Over $15,900 but not over $21,200	$4,081, plus 43% of excess over $15,900.
Over $21,200 but not over $28,300	$6,360, plus 49% of excess over $21,200.
Over $28,300 but not over $41,100	$9,839, plus 54% of excess over $28,300.
Over $41,100 but not over $53,000	$16,751, plus 59% of excess over $41,100.
Over $53,000 but not over $79,500	$23,772 plus 64% of excess over $53,000.
Over $79,500 but not over $106,000	$40,732, plus 68% of excess over $79,500.
Over $106,000	$58,752, plus 70% of excess over $106,000."

(b) INCREASE IN ZERO BRACKET AMOUNT.—Subsection (d) of section 63 (defining zero bracket amount) is amended—

(1) by striking out "$3,200" and inserting in lieu thereof "$3,400",

(2) by striking out "$2,200" and inserting in lieu thereof "$2,300", and

(3) by striking out "$1,600" and inserting in lieu thereof "$1,700".

(c) FILING REQUIREMENTS.—Paragraph (1) of section 6012(a) (relating to persons required to make returns of income) is amended—

(1) by striking out "$2,950" and inserting in lieu thereof "$3,050",

(2) by striking out "$3,950" and inserting in lieu thereof "$4,150", and

(3) by striking out "$4,700" and inserting in lieu thereof "$4,900".

(d) TECHNICAL AMENDMENTS.—

(1) Subparagraph (C) of section 402(e)(1) (relating to tax on lump sum distributions) is amended by striking out "$2,200" and inserting in lieu thereof "$2,300".

(2) Paragraph (3) of section 1302(b) (relating to transitional rule for determining base period income) is amended to read as follows:

"(3) TRANSITIONAL RULE FOR DETERMINING BASE PERIOD INCOME.—The base period income (determined under paragraph (2)) for any taxable year beginning before January 1, 1977, shall be increased by—

"(A) $3,200 in the case of a joint return or a surviving spouse, (as defined in section 2(a)),

"(B) $2,200 in the case of an individual who is not married (within the meaning of section 143) and is not a surviving spouse (as so defined), or

"(C) $1,600 in the case of a married individual (within the meaning of section 143) filing a separate return.

For purposes of this paragraph, filing status shall be determined as of the computation year."

(e) WITHHOLDING AMENDMENTS.—

(1) WITHHOLDING TABLES.—Subsection (a) of section 3402 (relating to requirement of withholding) is amended by striking out the second and third sentences and inserting in lieu thereof the following new sentence: "With respect to wages paid after December 31, 1978, the tables so prescribed shall be the same as the tables prescribed under this subsection which were in effect on January 1, 1975, except that such tables shall be modified to the extent necessary to reflect the amendments made by sections 101 and 102 of the Tax Reduction and Simplification Act of 1977 and the amendments made by section 101 of the Revenue Act of 1978."

(2) WITHHOLDING ALLOWANCES BASED ON ITEMIZED DEDUCTIONS.—Subparagraph (B) of section 3402(m)(1) (relating to withholding allowances based on itemized deductions) is amended—

(A) by striking out "$3,200" and inserting in lieu thereof "$3,400", and

(B) by striking out "$2,200" and inserting in lieu thereof "$2,300".

(f) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by subsections (a), (b), (c), and (d) shall apply to taxable years beginning after December 31, 1978.

(2) WITHHOLDING AMENDMENTS.—The amendments made by subsection (e) shall apply to remuneration paid after December 31, 1978.

SEC. 102. PERSONAL EXEMPTIONS INCREASED TO $1,000.

(a) GENERAL RULE.—Section 151 (relating to allowance of deductions for personal exemptions) is amended by striking out "$750" each place it appears and inserting in lieu thereof "$1,000".

(b) FILING REQUIREMENTS.—

(1) Paragraph (1) of section 6012(a) (relating to persons required to make returns of income), as amended by section 101(c) of this Act, is amended by striking out "$750", "$3,050", "$4,150", and "$4,900" each place they appear and inserting in lieu thereof "$1,000", "$3,300", "$4,400", and "$5,400", respectively.

(2) Subparagraph (A) of section 6013(b)(3) (relating to assessment and collection in the case of certain returns of husband and wife) is amended by striking out "$750" and "$1,500" each place they appear and inserting in lieu thereof "$1,000" and "$2,000", respectively.

(c) WITHHOLDING REQUIREMENTS.—

(1) Paragraph (1) of section 3402(b) (relating to percentage method of withholding income tax at source) is amended by striking out the table and inserting in lieu thereof the following:

"Percentage Method Withholding Table

Payroll period	Amount of one withholding exemption
Weekly	$19.23
Biweekly	38.46
Semimonthly	41.66
Monthly	83.33
Quarterly	250.00
Semiannual	500.00
Annual	1,000.00
Daily or miscellaneous (per day of such period)	2.74".

(2) Paragraph (1) of section 3402(m) (relating to withholding allowances based on itemized deductions) is amended by striking out "$750" and inserting in lieu thereof "$1,000".

(d) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by subsections (a) and (b) shall apply to taxable years beginning after December 31, 1978.

(2) WITHHOLDING AMENDMENTS.—The amendments made by subsection (c) shall apply with respect to remuneration paid after December 31, 1978.

SEC. 103. EARNED INCOME CREDIT MADE PERMANENT.

(a) GENERAL RULE.—Subsection (b) of section 209 of the Tax Reduction Act of 1975 is amended by striking out ", and before January 1, 1979".

(b) TECHNICAL AMENDMENT.—The second sentence of section 401(e) of the Tax Reform Act of 1976 (as added by section 103 of the Tax Reduction and Simplification Act of 1977) is amended by striking out ", and shall cease to apply to taxable years beginning after December 31, 1978".

SEC. 104. INCREASE IN AND SIMPLIFICATION OF THE EARNED INCOME TAX CREDIT.

(a) INCREASE IN CREDIT.—Subsection (a) of section 43 (relating to earned income credit) is amended—

(1) by striking out "chapter" and inserting in lieu thereof "subtitle", and

(2) by striking out "$4,000" and inserting in lieu thereof "$5,000".

(b) REVISION OF THE LIMITATION.—Subsection (b) of section 43 is amended to read as follows;

"(b) LIMITATION.—The amount of the credit allowable to a taxpayer under subsection (a) for any taxable year shall not exceed the excess (if any) of—

"(1) $600, over

"(2) 12.5 percent of so much of the adjusted gross income (or, if greater, the earned income) of the taxapyer for the taxable year as exceeds $6,000."

(c) AMOUNT OF CREDIT TO BE DETERMINED UNDER TABLES.—Section 43 is amended by adding at the end thereof the following new subsection:

"(f) AMOUNT OF CREDIT TO BE DETERMINED UNDER TABLES.—

"(1) IN GENERAL.—The amount of the credit allowed by this section shall be determined under tables prescribed by the Secretary.

"(2) REQUIREMENTS FOR TABLES.—The tables prescribed under paragraph (1) shall reflect the provisions of subsections (a) and (b) and shall have income brackets of not greater than $50 each—

"(A) for earned income between $0 and $10,000, and

"(B) for adjusted gross income between $6,000 and $10,000.".

(d) EXCLUDABLE EARNED INCOME TAKEN INTO ACCOUNT.—Subparagraph (B) of section 43(c)(2) (defining earned income) is amended by striking out clause (i) and by redesignating clauses (ii), (iii), and (iv) as clauses (i), (ii), and (iii), respectively.

(e) DEFINITION OF ELIGIBLE INDIVIDUAL.—Paragraph (1) of section 43(c) (defining eligible individual) is amended to read as follows:

"(1) ELIGIBLE INDIVIDUAL.—

"(A) IN GENERAL.—The term 'eligible individual' means an individual who, for the taxable year—

"(i) is married (within the meaning of section 143) and is entitled to a deduction under section 151 for a child (within the meaning of section 151(e)(3)),

"(ii) is a surviving spouse (as determined under section 2(a)), or

"(iii) is a head of a household (as determined under subsection (b) of section 2 without regard to subparagraphs (A)(ii) and (B) of paragraph (1) of such subsection).

"(B) CHILD MUST RESIDE WITH TAXPAYER IN THE UNITED STATES.—An individual shall be treated as satisfying clause (i) of subparagraph (A) only if the child has the same principal place of abode as the individual and such abode is in the United States. An individual shall be treated as satisfying clause (ii) or (iii) of subparagraph (A) only if the household in question is in the United States.

"(C) INDIVIDUAL ENTITLED TO EXCLUDE INCOME UNDER SECTION 911 NOT ELIGIBLE INDIVIDUAL.—The term 'eligible individual' does not include an individual who, for the taxable year, is entitled to exclude any amount from gross income under section 911 (relating to earned income from sources without the United States) or section 931 (relating to income from sources within the possessions of the United States)."

(f) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1978.

SEC. 105. ADVANCE PAYMENT OF EARNED INCOME CREDIT.

(a) COORDINATION OF CREDIT WITH ADVANCE PAYMENTS.—Section 43 (relating to earned income credit) is amended by adding at the end thereof the following new subsection:

"(h) COORDINATION WITH ADVANCE PAYMENTS OF EARNED INCOME CREDIT.—

"(1) RECAPTURE OF EXCESS ADVANCE PAYMENTS.—If any payment is made to the individual by an employer under section 3507 during any calendar year, then the tax imposed by this chapter for the individual's last taxable year beginning in such calendar year shall be increased by the aggregate amount of such payments.

"(2) RECONCILIATION OF PAYMENTS ADVANCED AND CREDIT ALLOWED.—Any increase in tax under paragraph (1) shall not be treated as tax imposed by this chapter for purposes of determining the amount of any credit (other than the credit allowed by subsection (a)) allowable under this subpart.".

(b) ADVANCE PAYMENT OF EARNED INCOME CREDIT.—

(1) IN GENERAL.—Chapter 25 (general provisions relating to employment taxes) is amended by adding at the end thereof the following new section:

"SEC. 3507. ADVANCE PAYMENT OF EARNED INCOME CREDIT.

"(a) GENERAL RULE.—Except as otherwise provided in this section, every employer making payment of wages to an employee with respect to whom an earned income eligibility certificate is in effect shall, at the time of paying such wages, make an additional payment to such employee equal to such employee's earned income advance amount.

"(b) EARNED INCOME ELIGIBILITY CERTIFICATE.—For purposes of this title, an earned income eligibility certificate is a statement furnished by an employee to the employer which—

"(1) certifies that the employee will be eligible to receive the credit provided by section 43 for the taxable year;

"(2) certifies that the employee does not have an earned income eligibility certificate in effect for the calendar year with respect to the payment of wages by another employer, and

"(3) states whether or not the employee's spouse has an earned income eligibility certificate in effect.

For purposes of this section, a certificate shall be treated as being in effect with respect to a spouse if such a certificate will be in effect on the first status determination date following the date on which the employee furnishes the statement in question.

"(c) EARNED INCOME ADVANCE AMOUNT.—

"(1) IN GENERAL.—For purposes of this title, the term 'earned income advance amount' means, with respect to any payroll period, the amount determined—

"(A) on the basis of the employee's wages from the employer for such period, and

"(B) in accordance with tables prescribed by the Secretary.

"(2) ADVANCE AMOUNT TABLES.—The tables referred to in paragraph (1)(B)—

"(A) shall be similar in form to the tables prescribed under section 3402 and, to the maximum extent feasible, shall be coordinated with such tables, and

"(B) if the employee is not married, or if no earned income eligibility certificate is in effect with respect to the spouse of the employee, shall treat the credit provided by section 43 as if it were a credit—

"(i) of not more than 10 percent of the first $5,000 of earned income, which

"(ii) *phases out between $6,000 and $11,000 of earned income, or*

"(C) *if an earned income eligibility certificate is in effect with respect to the spouse of the employee, shall treat the credit provided by section 43 as if it were a credit—*

"(i) *of not more than 10 percent of the first $2,500 of of earned income, which*

"(ii) *phases out between $3,000 and $5,000 of earned income.*

"(d) PAYMENTS TO BE TREATED AS PAYMENTS OF WITHHOLDING AND FICA TAXES.—

"(1) IN GENERAL.—*For purposes of this title, payments made by an employer under subsection (a) to his employees for any payroll period—*

"(A) *shall not be treated as the payment of compensation, and*

"(B) *shall be treated as made out of—*

"(i) *amounts required to be deducted and withheld for the payroll period under section 3401 (relating to wage withholding), and*

"(ii) *amounts required to be deducted for the payroll period under section 3102 (relating to FICA employee taxes), and*

"(iii) *amounts of the taxes imposed for the payroll period under section 3111 (relating to FICA employer taxes),*

as if the employer had paid to the Secretary, on the day on which the wages are paid to the employees, an amount equal to such payments.

"(2) ADVANCE PAYMENTS EXCEED TAXES DUE.—*In the case of any employer, if for any payroll period the aggregate amount of earned income advance payments exceeds the sum of the amounts referred to in paragraph (1)(B), each such advance payment shall be reduced by an amount which bears the same ratio to such excess as such advance payment bears to the aggregate amount of all such advance payments.*

"(3) EMPLOYER MAY MAKE FULL ADVANCE PAYMENTS.—*The Secretary shall prescribe regulations under which an employer may elect (in lieu of any application of paragraph (2))—*

"(A) *to pay in full all earned income advance amounts, and*

"(B) *to have additional amounts paid by reason of this paragraph treated as the advance payment of taxes imposed by this title.*

"(4) FAILURE TO MAKE ADVANCE PAYMENTS.—*For purposes of this title (including penalties), failure to make any advance payment under this section at the time provided therefor shall be treated as the failure at such time to deduct and withhold under chapter 24 an amount equal to the amount of such advance payment.*

"(e) FURNISHING AND TAKING EFFECT OF CERTIFICATES.—*For purposes of this section—*

"(1) WHEN CERTIFICATE TAKES EFFECT.—

"(A) FIRST CERTIFICATE FURNISHED.—*An earned income eligibility certificate furnished the employer in cases in which no previous such certificate had been in effect for the calendar year*

shall take effect as of the beginning of the first payroll period ending, or the first payment of wages made without regard to a payroll period, on or after the date on which such certificate is so furnished (or if later, the first day of the calendar year for which furnished).

"(B) LATER CERTIFICATE.—An earned income eligibility certificate furnished the employer in cases in which a previous such certificate had been in effect for the calendar year shall take effect with respect to the first payment of wages made on or after the first status determination date which occurs at least 30 days after the date on which such certificate is so furnished, except that at the election of the employer such certificate may be made effective with respect to any payment of wages made on or after the date on which such certificate is so furnished. For purposes of this section, the term 'status determination date' means January 1, May 1, July 1, and October 1 of each year.

"(2) PERIOD DURING WHICH CERTIFICATE REMAINS IN EFFECT.—An earned income eligibility certificate which takes effect under this section for any calendar year shall continue in effect with respect to the employee during such calendar year until revoked by the employee or until another such certificate takes effect under this section.

"(3) CHANGE OF STATUS.—

"(A) REQUIREMENT TO REVOKE OR FURNISH NEW CERTIFICATE.—If, after an employee has furnished an earned income eligibility certificate under this section, there has been a change of circumstances which has the effect of—

"(i) making the employee ineligible for the credit provided by section 43 for the taxable year, or

"(ii) causing an earned income eligibility certificate to be in effect with respect to the spouse of the employee,

the employee shall, within 10 days after such change in circumstances, furnish the employer with a revocation of such certificate or with a new certificate (as the case may be). Such a revocation (or such a new certificate) shall take effect under the rules provided by paragraph (1)(B) for a later certificate and shall be made in such form as the Secretary shall by regulations prescribe.

"(B) CERTIFICATE NO LONGER IN EFFECT.—If, after an employee has furnished an earned income eligibility certificate under this section which certifies that such a certificate is in effect with respect to the spouse of the employee, such a certificate is no longer in effect with respect to such spouse, then the employee may furnish the employer with a new earned income eligibility certificate.

"(4) FORM AND CONTENTS OF CERTIFICATE.—Earned income eligibility certificates shall be in such form and contain such other information as the Secretary may by regulations prescribe.

"(5) TAXABLE YEAR DEFINED.—The term 'taxable year' means the last taxable year of the employee under subtitle A beginning in the calendar year in which the wages are paid.".

(2) CLERICAL AMENDMENT.—The table of sections for chapter 25 is amended by adding at the end thereof the following new item:

"Sec. 3507. Advance payment of earned income credit.".

(c) INFORMATION SHOWN ON W–2.—The first sentence of section 6051(a) (relating to receipts for employees) is amended—

(1) by striking out "and" at the end of paragraph (5),

(2) by striking out the period at the end of paragraph (6) and inserting in lieu thereof ", and", and

(3) by adding at the end thereof the following new paragraph:

"(7) the total amount paid to the employee under section 3507 (relating to advance payment of earned income credit).".

(d) REQUIREMENT OF RETURN.—Subsection (a) of section 6012 (relating to persons required to make returns of income) is amended by adding at the end thereof the following new paragraph:

"(8) Every individual who receives payments during the calendar year in which the taxable year begins under section 3507 (relating to advance payment of earned income credit).".

(e) CROSS REFERENCE.—Section 6302 (relating to mode or time of collection) is amended by adding at the end thereof the following new subsection:

"(d) CROSS REFERENCE.—

"For treatment of payment of earned income advance amounts as payment of withholding and FICA taxes, see section 3507(d).".

(f) DISREGARD TO TERMINATE IN 1980.—Section 2(d) of the Revenue Adjustment Act of 1975 (relating to disregard of refund) is amended—

(1) by inserting before "shall not be taken into account" the following: ", and any payment made by an employer under section 3507 of such Code (relating to advance payment of earned income credit)", and

(2) by inserting after "shall not be taken into account" the following: "in any year ending before 1980".

(g) EFFECTIVE DATE.—

(1) The amendments made by subsections (a) and (d) shall apply to taxable years beginning after December 31, 1978.

(2) The amendments made by subsections (b), (c), and (e) shall apply to remuneration paid after June 30, 1978.

(3) Subsection (f) shall take effect on the date of the enactment of this Act.

SEC. 106. APPLICATION OF CERTAIN CHANGES IN THE CASE OF FISCAL YEAR TAXPAYERS.

Section 21 (relating to effects of changes in rate of tax) is amended by adding at the end thereof the following new subsection:

"(f) CHANGES MADE BY REVENUE ACT OF 1978.—In applying subsection (a) to a taxable year which is not a calendar year—

"(1) the amendments made by sections 101, 102, and 301 of the Revenue Act of 1978 (and no other amendments made by such Act), and

"(2) the expiration of section 42 (relating to general tax credit), shall be treated as a change in a rate of tax."

Subtitle B—Itemized Deductions; Etc.

SEC. 111. REPEAL OF DEDUCTION FOR STATE AND LOCAL TAXES ON GASOLINE AND OTHER MOTOR FUELS.

(a) REPEAL.—Paragraph (5) of section 164(a) (relating to deduction for taxes) is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) The heading of paragraph (5) of section 164(b) is amended by striking out "AND GASOLINE TAXES".

(2) The text of such paragraph (5) is amended by striking out "or of any tax on the sale of gasoline, diesel fuel, or other motor fuel".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1978.

SEC. 112. TAXATION OF UNEMPLOYMENT COMPENSATION BENEFITS AT CERTAIN INCOME LEVELS.

(a) INCLUSION IN GROSS INCOME.—Part II of subchapter B of chapter 1 (relating to amounts specifically included in gross income) is amended by adding at the end thereof the following new section:

"SEC. 85. UNEMPLOYMENT COMPENSATION.

"(a) IN GENERAL.—If the sum for the taxable year of the adjusted gross income of the taxpayer (determined without regard to this section and without regard to section 105(d)) and the unemployment compensation exceeds the base amount, gross income for the taxable year included unemployment compensation in an amount equal to the lesser of—

"(1) one-half of the amount of the excess of such sum over the base amount, or

"(2) the amount of the unemployment compensation.

"(b) BASE AMOUNT DEFINED.—For purposes of this section, the term 'base amount' means—

"(1) except as provided in paragraphs (2) and (3), $20,000,

"(2) $25,000, in the case of a joint return under section 6013, or

"(3) zero, in the case of a taxpayer who—

"(A) is married at the close of the taxable year (within the meaning of section 143) but does not file a joint return for such for such year, and

"(B) does not live apart from his spouse at all times during the taxable year.

"(c) UNEMPLOYMENT COMPENSATION DEFINED.—For purposes of this section, the term 'unemployment compensation' means any amount received under a law of the United States or of a State which is in the nature of unemployment compensation."

(b) REPORTING OF UNEMPLOYMENT COMPENSATION PAYMENTS.—Subpart B of part III of subchapter A of chapter 61 (relating to information concerning transactions with other persons) is amended by adding at the end thereof the following new section:

"SEC. 6050B. RETURNS RELATING TO UNEMPLOYMENT COMPENSATION.

"(a) REQUIREMENT OF REPORTING.—Every person who makes payments of unemployment compensation aggregating $10 or more to any individual during any calendar year shall make a return according to the forms or regulations prescribed by the Secretary, setting forth the aggregate amounts of such payments and the name and address of the individual to whom paid.

"(b) STATEMENTS TO BE FURNISHED TO INDIVIDUALS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—Every person making a return under subsection (a) shall furnish to each individual whose name is set forth in such return a written statement showing—

"(1) the name and address of the person making such return, and

"(2) the aagregate amount of payments to the individuals as shown on such return.

The written statement required under the preceding sentence shall be furnished to the individual on or before January 31 of the year following

the calendar year for which the return under subsection (a) was made. No statement shall be required to be furnished to any individual under this subsection if the aggregate amount of payments to such individual shown on the return made under subsection (a) is less than $10.

"(c) DEFINITIONS.—For purposes of this section—

"(1) UNEMPLOYMENT COMPENSATION.—The term 'unemployment compensation' has the meaning given to such term by section 85(c).

"(2) PERSON.—The term 'person' means the officer or employee having control of the payment of the unemployment compensation, or the person appropriately designated for purposes of this section."

(c) CLERICAL AMENDMENTS.—

(1) The table of sections for part II of subchapter B of chapter 1 is amended by adding at the end thereof the following new item:

"Sec. 85. Unemployment compensation."

(2) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by adding at the end thereof the following new item:

"Sec. 6050B. Returns relating to unemployment compensation."

(d) EFFECTIVE DATE.—The amendments made by this section shal apply to payments of unemployment compensation made after December 31, 1978, in taxable years ending after such date.

SEC. 113. REPEAL OF DEDUCTION FOR POLITICAL CONTRIBUTIONS; INCREASE IN CREDIT.

(a) REPEAL OF DEDUCTION.—

(1) REPEAL.—Section 218 (relating to deduction for contributions to candidates for public office and newsletter funds) is hereby repealed.

(2) CONFORMING AMENDMENTS.—

(A) The table of sections for part VII of subchapter B of chapter 1 (relating to additional itemized deductions for individuals) is amended by striking out the item relating to section 218.

(B) Section 642 (relating to special rules for credits and deductions of estates and trusts) is amended by striking out subsection (i) and by redesignating subsections (j) and (k) as subsections (i) and (j), respectively.

(c) INCREASE IN AMOUNT OF CREDIT.—Paragraph (1) of section 41(b) (relating to maximum credit) is amended by striking out "$25" and "$50" and inserting in lieu thereof "$50" and "$100", respectively.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to contributions the payment of which is made after December 31, 1978, in taxable years beginning after such date.

Subtitle C—Credits

SEC. 121. PAYMENTS TO RELATED INDIVIDUALS UNDER CHILD CARE CREDIT.

(a) IN GENERAL.—Paragraph (6) of section 44A(f) (relating to payments to related individuals) is amended to read as follows:

(6) PAYMENTS TO RELATED INDIVIDUALS.—No credit shall be allowed under subsection (a) for any amount paid by the taxpayer to an individual—

"(A) with respect to whom, for the taxable year, a deduction under section 151(e) (relating to deduction for personal exemp-

tions for dependents) is allowable either to the taxpayer or his spouse, or

"(B) who is a child of the taxpayer (within the meaning of section 151(e)(3)) who has not attained the age of 19 at the close of the taxable year.

For purposes of this paragraph, the term 'taxable year' means the taxable year of the taxpayer in which the service is performed."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1978.

Subtitle D—Deferred Compensation

PART I—DEFERRED COMPENSATION PROVISIONS

SEC. 131. DEFERRED COMPENSATION PLANS WITH RESPECT TO SERVICE FOR STATE AND LOCAL GOVERNMENTS.

(a) IN GENERAL.—Subpart B of part II of subchapter E of chapter 1 (relating to taxable years for which gross income included) is amended by adding at the end thereof the following new section:

"SEC. 457. DEFERRED COMPENSATION PLANS WITH RESPECT TO SERVICE FOR STATE AND LOCAL GOVERNMENTS.

"(a) YEAR OF INCLUSION IN GROSS INCOME.—In the case of a participant in an eligible State deferred compensation plan, any amount of compensation deferred under the plan, and any income attributable to the amounts so deferred, shall be includible in gross income only for the taxable year in which such compensation or other income is paid or otherwise made available to the participant or other beneficiary.

"(b) ELIGIBLE STATE DEFERRED COMPENSATION PLAN DEFINED.—For purposes of this section, the term 'eligible State deferred compensation plan' means a plan established and maintained by a State—

"(1) in which only individuals who perform service for the State may be participants,

"(2) which provides that (except as provided in paragraph (3)) the maximum that may be deferred under the plan for the taxable year shall not exceed the lesser of—

"(A) $7,500, or

"(B) 33⅓ percent of the participant's includible compensation,

"(3) which may provide that, for 1 or more of the participant's last 3 taxable years ending before he attains normal retirement age under the plan, the ceiling set forth in paragraph (2) shall be the lesser of—

"(A) $15,000, or

"(B) the sum of—

"(i) the plan ceiling established for purposes of paragraph (2) for the taxable year (determined without regard to this paragraph), plus

"(ii) so much of the plan ceiling established for purposes of paragraph (2) for taxable years before the taxable year as has not theretofore been used under paragraph (2) or this paragraph,

"(4) which provides that compensation will be deferred for any calendar month only if an agreement providing for such deferral has been entered into before the beginning of such month,

"(5) which does not provide that amounts payable under the plan will be made available to participants or other beneficiaries earlier than when the participant is separated from service with the State or is faced with an unforeseeable emergency (determined in the manner prescribed by the Secretary by regulation), and

"(6) which provides that—

"(A) all amounts of compensation deferred under the plan,

"(B) all property and rights purchased with such amounts, and

"(C) all income attributable to such amounts, property, or rights,

shall remain (until made available to the particpant or other beneficiary) solely the property and rights of the State (without being restricted to the provision of benefits under the plan) subject only to the claims of the State's general creditors.

A plan which is administered in a manner which is inconsistent with the requirements of any of the preceding paragraphs shall be treated as not meeting the requirements of such paragraph as of the first plan year beginning more than 180 days after the date of notification by the Secretary of the inconsistency unless the State corrects the inconsistency before the first day of such plan year.

"(c) INDIVIDUALS WHO ARE PARTICIPANTS IN MORE THAN ONE PLAN.—

"(1) IN GENERAL.—The maximum amount of the compensation of any one individual which may be deferred under subsection (a) during any taxable year shall not exceed $7,500 (as modified by any adjustment provided under subsection (b)(3)).

"(2) COORDINATION WITH SECTION 403(b).—In applying paragraph (1) of this subsection and paragraphs (2) and (3) of subsection (b), an amount excluded during a taxable year under section 403(b) shall be treated as an amount deferred under subsection (a). In applying clause (ii) of section 403(b)(2)(A), an amount deferred under subsection (a) for any year of service shall be taken into account as if described in such clause.

"(d) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) STATE.—The term 'State' means a State, a political subdivision of a State, and an agency or instrumentality of a State or political subdivision of a State.

"(2) PERFORMANCE OF SERVICE.—The performance of service includes performance of service as an independent contractor.

"(3) PARTICIPANT.—The term 'participant' means an individual who is eligible to defer compensation under the plan.

"(4) BENEFICIARY.—The term 'beneficiary' means a beneficiary of the participant, his estate, or any other person whose interest in the plan is derived from the participant.

"(5) INCLUDIBLE COMPENSATION.—The term 'includible compensation' means compensation for service performed for the State which (taking into account the provisions of this section and section 403(b)) is currently includible in gross income.

"(6) COMPENSATION TAKEN INTO ACCOUNT AT PRESENT VALUE.—Compensation shall be taken into account at its present value.

"(7) COMMUNITY PROPERTY LAWS.—The amount of includible compensation shall be determined without regard to any community property laws.

"(8) INCOME ATTRIBUTABLE.—Gains from the disposition of property shall be treated as income attributable to such property.

"(9) SECTION TO APPLY TO RURAL ELECTRIC COOPERATIVES.—

"(A) IN GENERAL.—This section shall apply with respect to any participant in a plan of a rural electric cooperative in the same manner and to the same extent as if such plan were a plan of a State.

"(B) RURAL ELECTRIC COOPERATIVE DEFINED.—For purposes of subparagraph (A), the term 'rural electric cooperative' means—

"(i) any organization described in section 501(c)(12) which is exempt from tax under section 501(a) and which is engaged primarily in providing electric service, and

"(ii) any organization described in section 501(c)(6) which is exempt from tax under section 501(a) and all the members of which are organizations described in clause (i).

"(e) TAX TREATMENT OF PARTICIPANTS WHERE PLAN OR ARRANGEMENT OF STATE IS NOT ELIGIBLE.—

"(1) IN GENERAL.—In the case of a plan of a State providing for a deferral of compensation, if such plan is not an eligible State deferred compensation plan, then—

"(A) the compensation shall be included in the gross income of the participant or beneficiary for the first taxable year in which there is no substantial risk of forfeiture of the rights to such compensation, and

"(B) the tax treatment of any amount made available under the plan to a participant or beneficiary shall be determined under section 72 (relating to annuities, etc.).

"(2) EXCEPTIONS.—Paragraph (1) shall not apply to—

"(A) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a).

"(B) an annuity plan or contract described in section 403,

"(C) a qualified bond purchase plan described in section 405(a),

"(D) that portion of any plan which consists of a transfer of property described in section 83, and

"(E) that portion of any plan which consists of a trust to which section 402(b) applies.

"(3) DEFINITIONS.—For purposes of this subsection—

"(A) PLAN INCLUDES ARRANGEMENTS, ETC.—The term 'plan' includes any agreement or arrangement.

"(B) SUBSTANTIAL RISK OF FORFEITURE.—The rights of a person to compensation are subject to a substantial risk of forfeiture if such person's rights to such compensation are conditioned upon the future performance of substantial services by any individual."

(b) CLERICAL AMENDMENT.—The table of sections for such subpart B is amended by adding at the end thereof the following:

"Sec. 457. Deferred compensation plans with respect to service for State and local governments."

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1978.

(2) TRANSITIONAL RULES.—

(A) IN GENERAL.—In the case of any taxable year beginning after December 31, 1978, and before January 1, 1982—

(i) any amount of compensation deferred under a plan of a State providing for a deferral of compensation (other than a plan described in section 457(e)(2) of the Internal Revenue Code of 1954), and any income attributable to the amounts so deferred, shall be includible in gross income only for the taxable year in which such compensation or other income is paid or otherwise made available to the participant or other beneficiary, but

(ii) the maximum amount of the compensation of any one individual which may be excluded from gross income by reason of clause (i) and by reason of section 457(a) of such Code during any such taxable year shall not exceed the lesser of—

(I) $7,500, or

(II) 33⅓ percent of the participant's includible compensation.

(B) APPLICATION OF CATCH-UP PROVISIONS IN CERTAIN CASES.—If, in the case of any participant for any taxable year, all of the plans are eligible State deferred compensation plans, then clause (ii) of subparagraph (A) of this paragraph shall be applied with the modification provided by paragraph (3) of section 457(b) of such Code.

(C) APPLICATIONS OF CERTAIN COORDINATION PROVISIONS.—In applying clause (ii) of subparagraph (A) of this paragraph and section 403(b)(2)(A)(ii) of such Code, rules similar to the rules of section 457(c)(2) of such Code shall apply.

(D) MEANING OF TERMS.—Except as otherwise provided in this paragraph, terms used in this paragraph shall have the same meaning as when used in section 457 of such Code.

SEC. 132. CERTAIN PRIVATE DEFERRED COMPENSATION PLANS.

(a) GENERAL RULE.—The taxable year of inclusion in gross income of any amount covered by a private deferred compensation plan shall be determined in accordance with the principles set forth in regulations, rulings, and judicial decisions relating to deferred compensation which were in effect on February 1, 1978.

(b) PRIVATE DEFERRED COMPENSATION PLAN DEFINED.—

(1) IN GENERAL.—For purposes of this section, the term "private deferred compensation plan" means a plan, agreement, or arrangement—

(A) where the person for whom the service is performed is not a State (within the meaning of paragraph (1) of section 457(d) of the Internal Revenue Code of 1954) and not an organization which is exempt from tax under section 501 of such Code, and

(B) under which the payment or otherwise making available of compensation is deferred.

(2) CERTAIN PLANS EXCLUDED.—Paragraph (1) shall not apply to—

(A) a plan described in section 401(a) of the Internal Revenue Code of 1954 which includes a trust exempt from tax under section 501(a) of such Code,

(B) an annuity plan or contract described in section 403 of such Code,

(C) a qualified bond purchase plan described in section 405(a) of such Code,

(D) that portion of any plan which consists of a transfer of property described in section 83 (determined without regard to subsection (e) thereof) of such Code, and

(E) that portion of any plan which consists of a trust to which section 402(b) of such Code applies.

(c) EFFECTIVE DATE.—This section shall apply to taxable years ending on or after February 1, 1978.

SEC. 133. CLARIFICATION OF DEDUCTIBILITY OF PAYMENTS OF DEFERRED COMPENSATION, ETC., TO INDEPENDENT CONTRACTORS.

(a) IN GENERAL.—Section 404 (relating to deduction for contributions of an employer to an employees' trust or annuity plan and compensation under a deferred-payment plan) is amended by inserting after subsection (c) the following new subsection:

"(d) DEDUCTIBILITY OF PAYMENTS OF DEFERRED COMPENSATION, ETC., TO INDEPENDENT CONTRACTORS.—If a plan would be described in so much of subsection (a) as precedes paragraph (1) thereof (as modified by subsection (b)) but for the fact that there is no employer-employee relationship, the contributions or compensation—

"(1) shall not be deductible by the payor thereof under section 162 or 212, but

"(2) shall (if they would be deductible under section 162 or 212 but for paragraph (1)) be deductible under this susection for the taxable year in which an amount attributable to the contribution or compensation is includible in the gross income of the persons participating in the plan."

(b) CLARIFICATION OF SECTION 404(b).—Subsection (b) of section 404 (relating to method of contributions, etc., having the effect of a plan) is amended by striking out "similar plan" and inserting in lieu thereof "other plan".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to deductions for taxable years beginning after December 31, 1978.

SEC. 134. TAX TREATMENT OF CAFETERIA PLANS.

(a) IN GENERAL.—Part III of subchapter B of chapter 1 (relating to items specifically excluded from gross income) is amended by redesignating section 125 as section 126 and by inserting after section 124 the following new section:

"SEC. 125. CAFETERIA PLANS.

"(a) IN GENERAL.—Except as provided in subsection (b), no amount shall be included in the gross income of a participant in a cafeteria plan solely because, under the plan, the participant may choose among the benefits of the plan.

"(b) EXCEPTION FOR HIGHLY COMPENSATED PARTICIPANTS WHERE PLAN IS DISCRIMINATORY.—

"(1) IN GENERAL.—In the case of a highly compensated participant, subsection (a) shall not apply to any benefit attributable to a plan year for which the plan discriminates in favor of—

"(A) highly compensated individuals as to eligibility to participate, or

"(B) highly compensated participants as to contributions and benefits.

"(2) YEAR OF INCLUSION.—For purposes of determining the taxable year of inclusion, any benefit described in paragraph (1) shall be treated as received or accrued in the participant's taxable year in which the plan year ends.

"(c) DISCRIMINATION AS TO BENEFITS OR CONTRIBUTIONS.—For purposes of subparagraph (B) of subsection (b)(1), a cafeteria plan does not discriminate where nontaxable benefits and total benefits (or employer contributions allocable to nontaxable benefits and employer contributions for total benefits) do not discriminate in favor of highly compensated participants.

"(d) CAFETERIA PLAN DEFINED.—For purposes of this section—

"(1) IN GENERAL.—The term 'cafeteria plan' means a written plan under which—

"(A) all participants are employees, and

"(B) the participants may choose among two or more benefits. The benefits which may be chosen may be nontaxable benefits, or cash, property, or other taxable benefits.

"(2) DEFERRED COMPENSATION PLANS EXCLUDED.—The term 'cafeteria plan' does not include any plan which provides for deferred compensation.

"(e) HIGHLY COMPENSATED PARTICIPANT AND INDIVIDUAL DEFINED.—For purposes of this section—

"(1) HIGHLY COMPENSATED PARTICIPANT.—The term 'highly compensated participant' means a participant who is—

"(A) an officer,

"(B) a shareholder owning more than 5 percent of the voting power or value of all classes of stock of the employer,

"(C) highly compensated, or

"(D) a spouse or dependent (within the meaning of section 152) of an individual described in subparagraph (A), (B), or (C).

"(2) HIGHLY COMPENSATED INDIVIDUAL.—The term 'highly compensated individual' means an individual who is described in subparagraph (A), (B), (C), or (D) of paragraph (1).

"(f) NONTAXABLE BENEFIT DEFINED.—For purposes of this section, the term 'nontaxable benefit' means any benefit which, with the application of subsection (a), is not includible in the gross income of the employee.

"(g) SPECIAL RULES.—

"(1) COLLECTIVELY BARGAINED PLAN NOT CONSIDERED DISCRIMINATORY.—For purposes of this section, a plan shall not be treated as discriminatory if the plan is maintained under an agreement which the Secretary finds to be a collective bargaining agreement between employee representatives and one or more employers.

"(2) HEALTH BENEFITS. —For purposes of subparagraph (B) of subsection (b)(1), a cafeteria plan which provides health benefits shall not be treated as discriminatory if—

"(A) contributions under the plan on behalf of each participant include an amount which—

"(i) equals 100 percent of the cost of the health benefit coverage under the plan of the majority of the highly compensated participants similarly situated, or

"(ii) equals or exceeds 75 percent of the cost of the health benefit coverage of the participant (similarly situated) having the highest cost health benefit coverage under the plan, and

"(B) contributions or benefits under the plan in excess of those described in subparagraph (A) bear a uniform relationship to compensation.

"(3) CERTAIN PARTICIPATION ELIGIBILITY RULES NOT TREATED AS DISCRIMINATORY.—For purposes of subparagraph (A) of subsection (b)(1), a classification shall not be treated as discriminatory if the plan—

"(A) benefits a group of employees described in subparagraph (B) of section 410(b)(1), and

"(B) meets the requirements of clauses (i) and (ii):

"(i) No employee is required to complete more than 3 years of employment with the employer or employers maintaining the plan as a condition of participation in the plan, and the service requirement for each employee is the same.

"(ii) Any employee who has satisfied the employment requirement of clause (i) and who is otherwise entitled to participate in the plan commences participation no later than the first day of the first plan year beginning after the date the service requirement was satisfied unless the employee was separated from service before the first day of that plan year.

"(4) CERTAIN CONTROLLED GROUPS.—All employees who are treated as employed by a single employer under subsection (b) or (c) of section 414 shall be treated as employed by a single employer for purposes of this section.

"(h) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this section."

(b) CLERICAL AMENDMENT.—The table of sections for part III of subchapter B of chapter 1 is amended by striking out the item relating to section 124 and inserting in lieu thereof the following:

"Sec. 125. Cafeteria plans.
"Sec. 126. Cross references to other Acts."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1978.

SEC. 135. CERTAIN CASH OR DEFERRED ARRANGEMENTS.

(a) IN GENERAL.—Section 401 (relating to qualified pension, profit-sharing, and stock bonus plans) is amended by redesignating subsection (k) as (l) and by inserting after subsection (j) the following new subsection:

"(k) CASH OR DEFERRED ARRANGEMENTS.—

"(1) GENERAL RULE.—A profit-sharing or stock bonus plan shall not be considered as not satisfying the requirements of subsection (a) merely because the plan includes a qualified cash or deferred arrangement.

"(2) QUALIFIED CASH OR DEFERRED ARRANGEMENT.—A qualified cash or deferred arrangement is any arrangement which is part of a profit-sharing or stock bonus plan which meets the requirements of subsection (a)—

"(A) under which a covered employee may elect to have the employer make payments as contributions to a trust under the plan on behalf of the employee, or to the employee directly in cash;

"(B) under which amounts held by the trust which are attributable to employer contributions made pursuant to the employee's election may not be distributable to participants or other beneficiaries earlier than upon retirement, death, disability, or separation from service, hardship or the attainment of age 59½, and will not be distributable merely by reason of the completion of a stated period of participation or the lapse of a fixed number of years; and

"(C) which provides that an employee's right to his accrued benefit derived from employer contributions made to the trust pursuant to his election are nonforfeitable.

"(3) APPLICATION OF PARTICIPATION AND DISCRIMINATION STANDARDS.—

"(A) A qualified cash or deferred arrangement shall be considered to satisfy the requirements of subsection (a)(4), with respect to the amount of contributions, and of subparagraph (B) of section 410(b)(1) for a plan year if those employees eligible to benefit under the plan satisfy the provisions of subparagraph (A) or (B) of section 410(b)(1) and if the actual deferral percentage for highly compensated employees (as defined in paragraph (4)) for such plan year bears a relationship to the actual deferral percentage for all other eligible employees for such plan year which meets either of the following tests:

"(i) The actual deferral percentage for the group of highly compensated employees is not more than the actual deferral percentage of all other eligible employees multiplied by 1.5.

"(ii) The excess of the actual deferral percentage for the group of highly compensated employees over that of all other eligible employees is not more than 3 percentage points, and the actual deferral percentage for the group of highly compensated employees is not more than the actual deferral percentage of all other eligible employees multiplied by 2.5.

"(B) For purposes of subparagraph (A), the actual deferral percentage for a specified group of employees for a plan year shall be the average of the ratios (calculated separately for each employee in such group) of—

"(i) the amount of employer contributions actually paid over to the trust on behalf of each such employee for such plan year, to

"(ii) the employee's compensation for such plan year.

For purposes of the preceding sentence, the compensation of any employee for a plan year shall be the amount of his compensation which is taken into account under the plan in calculating the contribution which may be made on his behalf for such plan year.

"(4) HIGHLY COMPENSATED EMPLOYEE.—For purposes of this subsection, the term 'highly compensated employee' means any

employee who is more highly compensated than two-thirds of all eligible employees, taking into account only compensation which is considered in applying paragraph (3).''

(b) TAXABILITY OF BENEFICIARIES.—Subsection (a) of section 402 is amended by adding at the end thereof the following new paragraph:

''(8) CASH OR DEFERRED ARRANGEMENTS.—For purposes of this title, contributions made by an employer on behalf of an employee to a trust which is a part of a qualified cash or deferred arrangement (as defined in section 401(k)(2)) shall not be treated as distributed or made available to the employee nor as contributions made to the trust by the employee merely because the arrangement includes provisions under which the employee has an election whether the contribution will be made to the trust or received by the employee in cash.''

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to plan years beginning after December 31, 1979.

(2) TRANSITIONAL RULE.—In the case of cash or deferred arrangements in existence on June 27, 1974—

(A) the qualification of the plan and the trust under section 401 of the Internal Revenue Code of 1954;

(B) the exemption of the trust under section 501(a) of such Code;

(C) the taxable year of inclusion in gross income of the employee of any amount so contributed by the employer to the trust; and

(D) the excludability of the interest of the employee in the trust under sections 2039 and 2517 of such Code,

shall be determined for plan years beginning before January 1, 1980 in a manner consistent with Revenue Ruling 56–497 (1956–2 C.B. 284), Revenue Ruling 63–180 (1963–2 C.B. 189), and Revenue Ruling 68–89 (1968–1 C.B. 402).

PART II—EMPLOYEE STOCK OWNERSHIP PLANS

SEC. 141. ESOPS.

(a) IN GENERAL.—Subpart A of part I of subchapter D of chapter 1 (relating to general rule for pension, profit-sharing, stock bonus plans, etc.) is amended by adding at the end thereof the following new section:

''SEC. 409A. QUALIFICATIONS FOR ESOPS.

''(a) ESOP DEFINED.—Except as otherwise provided in this title, for purposes of this title, the term 'ESOP' means a defined contribution plan which—

''(1) meets the requirements of section 401(a),

''(2) is designed to invest primarily in employer securities, and

''(3) meets the requirements of subsections (b), (c), (d), (e), (f), (g), and (h) of this section.

''(b) REQUIRED ALLOCATION OF EMPLOYER SECURITIES.—

''(1) IN GENERAL.—A plan meets the requirements of this subsection if—

''(A) the plan provides for the allocation for the plan year of all employer securities transferred to it or purchased by it (because of the requirements of section 48(n)(1)(A)) to the accounts of all participants who are entitled to share in such allocation, and

"(B) for the plan year the allocation to each participant so entitled is an amount which bears substantially the same proportion to the amount of all such securities allocated to all such participants in the plan for that year as the amount of compensation paid to such participant during that year bears to the compensation paid to all such participants during that year.

"(2) COMPENSATION IN EXCESS OF $100,000 DISREGARDED.—For purposes of paragraph (1), compensation of any participant in excess of the first $100,000 per year shall be disregarded.

"(3) DETERMINATION OF COMPENSATION.—For purposes of this subsection, the amount of compensation paid to a participant for any period is the amount of such participant's compensation (within the meaning of section 415(c)(3)) for such period.

"(4) SUSPENSION OF ALLOCATION IN CERTAIN CASES.—Notwithstanding paragraph (1), the allocation to the account of any participant which is attributable to the basic ESOP credit may be extended over whatever period may be necessary to comply with the requirements of section 415.

"(c) PARTICIPANTS MUST HAVE NONFORFEITABLE RIGHTS.—A plan meets the requirements of this subsection only if it provides that each participant has a nonforfeitable right to any employer security allocated to his account.

"(d) EMPLOYER SECURITIES MUST STAY IN THE PLAN.—A plan meets the requirements of this subsection only if it provides that no employer security allocated to a participant's account under subsection (b) may be distributed from that account before the end of the 84th month beginning after the month in which the security is allocated to the account. To the extent provided in the plan, the preceding sentence shall not apply in the case of separation from service, death, or disability.

"(e) VOTING RIGHTS.—

"(1) IN GENERAL.—A plan meets the requirements of this subsection if it meets the requirements of paragraph (2) or (3), whichever is applicable.

"(2) REQUIREMENTS WHERE EMPLOYER HAS A REGISTRATION-TYPE CLASS OF SECURITIES.—If the employer has a registration-type class of securities, the plan meets the requirements of this paragraph only if each participant in the plan is entitled to direct the plan as to the manner in which employer securities which are entitled to vote and are allocated to the account of such participant are to be voted.

"(3) REQUIREMENT FOR OTHER EMPLOYERS.—If the employer does not have a registration-type class of securities, the plan meets the requirements of this paragraph only if each participant in the plan is entitled to direct the plan as to the manner in which voting rights under employer securities which are allocated to the account of such participant are to be exercised with respect to a corporate matter which (by law or charter) must be decided by more than a majority vote of outstanding common shares voted.

"(4) REGISTRATION-TYPE CLASS OF SECURITIES DEFINED.—For purposes of this subsection, the term 'registration-type class of securities' means—

"(A) a class of securities required to be registered under section 12 of the Securities Exchange Act of 1934, and

"(B) a class of securities which would be required to be so registered except for the exemption from registration provided in subsection (g)(2)(H) of such section 12.

"(f) PLAN MUST BE ESTABLISHED BEFORE EMPLOYER'S DUE DATE.—

"(1) IN GENERAL.—A plan meets the requirements of this subsection for a plan year only if it is established on or before the due date for the filing of the employer's tax return for the taxable year (including any extensions of such date) in which or with which the plan year ends.

"(2) SPECIAL RULE FOR FIRST YEAR.—A plan which otherwise meets the requirements of this section shall not be considered to have failed to meet the requirements of section 401(a) merely because it was not established by the close of the first taxable year of the employer for which an ESOP credit is claimed by the employer.

"(g) TRANSFERRED AMOUNTS MUST STAY IN PLAN EVEN THOUGH INVESTMENT CREDIT IS REDETERMINED OR RECAPTURED.—A plan meets the requirement of this subsection only if it provides that amounts which are transferred to the plan (because of the requirements of section 48(n)(1)) shall remain in the plan (and, if allocated under the plan, shall remain so allocated) even though part or all of the ESOP credit is recaptured or redetermined.

"(h) RIGHT TO DEMAND EMPLOYER SECURITIES; PUT OPTION.—

"(1) IN GENERAL.—A plan meets the requirements of this subsection if a participant who is entitled to a distribution from the plan—

"(A) has a right to demand that his benefits be distributed in the form of employer securities, and

"(B) if the employer securities are not readily tradable on an established market, has a right to require that the employer repurchase employer securities under a fair valuation formula.

"(2) PLAN MAY DISTRIBUTE CASH IN CERTAIN CASES.—A plan which otherwise meets the requirements of this section shall not be considered to have failed to meet the requirements of section 401(a) merely because under the plan the benefits may be distributed in cash or in the form of employer securities.

"(i) REIMBURSEMENT FOR EXPENSES OF ESTABLISHING AND ADMINISTERING PLAN.—A plan which otherwise meets the requirements of this section shall not be treated as failing to meet such requirements merely because it provides that—

"(1) EXPENSES OF ESTABLISHING PLAN.—As reimbursement for the expenses of establishing the plan, the employer may withhold from amounts due the plan for the taxable year for which the plan is established (or the plan may pay) so much of the amounts paid or incurred in connection with the establishment of the plan as does not exceed the sum of—

"(A) 10 percent of the first $100,000 which the employer is required to transfer to the plan for that taxable year under section 48(n)(1), and

"(B) 5 percent of any amount so required to be transferred in excess of the first $100,000; and

"(2) ADMINISTRATIVE EXPENSES.—As reimbursement for the expenses of administering the plan, the employer may withhold from amounts due the plan (or the plan may pay) so much of the amounts paid or incurred during the taxable year as expenses of administering the plan as does not exceed the lesser of—

"(A) the sum of—

"(i) 10 percent of the first $100,000 of the dividends paid to the plan with respect to stock of the employer during the plan year ending with or within the employer's taxable year, and

"(ii) 5 percent of the amount of such dividends in excess of $100,000 or

"(B) $100,000.

"(j) CONDITIONAL CONTRIBUTIONS TO THE PLAN.—A plan which otherwise meets the requirements of this section shall not be treated as failing to satisfy such requirements (or as failing to satisfy the requirements of section 401(a) of this title or of section 403(c)(1) of the Employee Retirement Income Security Act of 1974) merely because of the return of a contribution (or a provision permitting such a return) if—

"(1) the contribution to the plan is conditioned on a determination by the Secretary that such plan meets the requirements of this section,

"(2) the application for a determination described in paragraph (1) is filed with the Secretary not later than 90 days after the date on which an ESOP credit is claimed, and

"(3) the contribution is returned within 1 year after the date on which the Secretary issues notice to the employer that such plan does not satisfy the requirements of this section.

"(k) REQUIREMENTS RELATING TO CERTAIN WITHDRAWALS.—Notwithstanding any other law or rule of law—

"(1) the withdrawal from a plan which otherwise meets the requirements of this section by the employer of an amount contributed for purposes of the matching ESOP credit shall not be considered to make the benefits forfeitable, and

"(2) the plan shall not, by reason of such withdrawal, fail to be for the exclusive benefit of participants or their beneficiaries,

if the withdrawn amounts were not matched by employee contributions or were in excess of the limitations of section 415. Any withdrawal described in the preceding sentence shall not be considered to violate the provisons of section 403(c)(1) of the Employee Retirement Income Security Act of 1974.

"(l) EMPLOYER SECURITIES DEFINED.—For purposes of this section—

"(1) IN GENERAL.—The term 'employer securities' means common stock issued by the employer (or by a corporation which is a member of the controlled group) which is readily tradable on an established securities market.

"(2) SPECIAL RULE WHERE THERE IS NO READILY TRADABLE COMMON STOCK.—If there is no common stock which meets the requirements of paragraph (1), the term 'employer securities' means common stock issued by the employer (or by a corporation which is a member of the same controlled group) having a combination of voting power and dividend rights equal to or in excess of—

"(A) that class of common stock of the employer (or of any other such corporation) having the greatest voting power, and

"(B) that class of stock of the employer (or of any other such corporation) having the greatest dividend rights.

"(3) PREFERRED STOCK MAY BE ISSUED IN CERTAIN CASES — Noncallable preferred stock shall be treated as meeting the requirements of paragraph (1) if such stock is convertible at any time into stock which meets the requirements of paragraph (1) and if such conversion is at a conversion price which (as of the date of the acquisition by the ESOP) is reasonable.

"(4) CONTROLLED GROUP OF CORPORATIONS DEFINED.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'controlled group of corporations' has the meaning given to such term of by section 1563(a) (determined without regard to subsection (a)(4) and (e)(3)(C) of section 1563).

"(B) COMMON PARENT MAY OWN ONLY 50 PERCENT OF FIRST TIER SUBSIDIARY.—For purposes of subparagraph (A), if the common parent owns directly stock possessing at least 50 percent of the voting power of all classes of stock and at least 50 percent of each class of nonvoting stock in a first tier subsidiary, such subsidiary (and all other corporations below it in the chain which would meet the 80 percent test of section 1563(a) if the first tier subsidiary were the common parent) shall be treated as includible corporations.

"(m) CONTRIBUTIONS OF STOCK OF CONTROLLING CORPORATIONS.—If the stock of a corporation which controls another corporation or which controls a corporation controlled by such other corporation is contributed to an ESOP of the controlled corporation, then no gain or loss shall be recognized, because of that contribution, to the controlled corporation. For purposes of this subsection, the term 'control' has the same meaning as that term has in section 368(c).

"(n) CROSS REFERENCES.—

"(1) For requirements for allowance of ESOP credit, see section 48(n).

"(2) For assessable penalties for failure to meet requirements of this section, or for failure to make contributions required with respect to the allowance of an ESOP credit, see section 6699."

(b) AMENDMENT OF INVESTMENT CREDIT RULES.—Section 48 (relating to definitions and special rules) is amended by redesignating subsection (n) as subsection (p) and by inserting after subsection (m) the following new subsections:

"(n) REQUIREMENTS FOR ALLOWANCE OF ESOP PERCENTAGE.—

"(1) IN GENERAL.—

"(A) BASIC ESOP PERCENTAGE.—The basic ESOP percentage shall not apply to any taxpayer for any taxable year unless the taxpayer on his return for such taxable year agrees, as a condition for the allowance of such percentage—

"(i) to make transfers of employer securities to an ESOP maintained by the taxpayer having an aggregate value equal to 1 percent of the amount of the qualified investment (as determined under subsections (c) and (d) of section 46) for the taxable year, and

"(ii) to make such transfers at the times prescribed in subparagraph (C).

"(B) MATCHING ESOP PERCENTAGE.—The matching ESOP percentage shall not apply to any taxpayer for any taxable year unless the basic ESOP percentage applies to such taxpayer for such taxable year, and the taxpayer on his return for such taxable year agrees, as a condition for the allowance of the matching ESOP percentage—

"(i) to make transfers of employer securities to an ESOP maintained by the taxpayer having an aggregate value equal to the sum of the qualified matching employee contributions made to such ESOP for the taxable year, and

"(ii) to make such transfers at the times prescribed in subparagraph (C).

"(C) TIMES FOR MAKING TRANSFERS.—The aggregate of the transfers required under subparagraphs (A) and (B) shall be made—

"(i) to the extent allocable to that portion of the ESOP credit allowed for the taxable year or allowed as a carryback to a preceding taxable year, not later than 30 days after the due date (including extensions) for filing the return for the taxable year, or

"(ii) to the extent allocable to that portion of the ESOP credit which is allowed as a carryover in a succeeding taxable year, not later than 30 days after the due date (including extensions) for filing the return for such succeeding taxable year.

The Secretary may by regulations provide that transfers may be made later than the times prescribed in the preceding sentence where the amount of any credit or carryover or carryback for any taxable year exceeds the amount shown on the return for the taxable year.

"(D) ORDERING RULES.—For purposes of subparagraph (C), the portion of the ESOP credit allowed for the current year or as a carryover or carryback shall be determined—

"(i) first by treating the credit or carryover or carryback as attributable to the regular percentage,

"(ii) second by treating the portion (not allocated under clause (i)) of such credit or carryover or carryback as attributable to the basic ESOP percentage, and

"(iii) finally by treating the portion (not allocated under clause (i) or (ii)) as attributable to the matching ESOP percentage.

"(2) QUALIFIED MATCHING EMPLOYEE CONTRIBUTION DEFINED.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'qualified matching employee contribution' means, with respect to any taxable year, any contribution made by an employee to an ESOP maintained by the taxpayer if—

"(i) each employee who is entitled to an allocation of employer securities transferred to the ESOP under paragraph (1)(A) is entitled to make such a contribution,

"(ii) the contribution is designated by the employee as a contribution intended to be taken into account under this subparagraph for the taxable year,

"(iii) the contribution is paid in cash to the employer or plan administrator not later than 24 months after the close of the taxable year, and is invested forthwith in employer securities, and

"(iv) the ESOP meets the requirements of subparagraph (B).

"(B) PLAN REQUIREMENTS.—For purposes of subparagraph (A), an ESOP meets the requirements of this subparagraph if—

"(i) participation in the ESOP is not required as a condition of employment and the ESOP does not require matching employee contributions as a condition of participation in the ESOP,

"(ii) employee contributions under the ESOP meet the requirements of section 401(a)(4), and

"(iii) the ESOP provides for allocation of all employer securities transferred to it or purchased by it (because of the requirements of paragraph (1)(B)) to the account of each participant in an amount equal to such participant's matching employee contributions for the year.

"(3) CERTAIN CONTRIBUTIONS OF CASH TREATED AS CONTRIBUTIONS OF EMPLOYER SECURITIES.—For purposes of this subsection, a transfer of cash shall be treated as a transfer of employer securities if the cash is, under the ESOP, used within 30 days to purchase employer securities.

"(4) ADJUSTMENTS IF ESOP CREDIT RECAPTURED.—If any portion of the ESOP credit is recaptured under section 47 or the ESOP credit is reduced by a final determination—

"(A) the employer may reduce the amount required to be transferred to the ESOP under paragraph (1) for the current taxable year or any succeeding taxable year by an amount equal to such portion (or reduction), or

"(B) notwithstanding the provisions of paragraph (5) and to the extent not taken into account under subparagraph (A), the employer may deduct an amount equal to such portion (or reduction), subject to the limitations of section 404.

"(5) DISALLOWANCE OF DEDUCTION.—No deduction shall be allowed under section 162, 212, or 404 for amounts required to be transferred to an ESOP under this subsection.

"(6) DEFINITIONS.—For purposes of this subsection—

"(A) EMPLOYER SECURITIES.—The term 'employer securities' has the meaning given to such term by section 409A(l).

"(B) VALUE.—The term 'value' means—

"(i) in the case of securities listed on a national exchange, the average of closing prices of such securities for the 20 consecutive trading days immediately preceding the due date for filing the return for the taxable year (determined with regard to extensions), or

"(ii) in the case of securities not listed on a national exchange, the fair market value as determined in good faith and in accordance with regulations prescribed by the Secretary.

"(o) CERTAIN CREDITS DEFINED.—For purpose of this title—

"(1) REGULAR INVESTMENT CREDIT.—The term 'regular investment credit' means that portion of the credit allowable by section 38 which is attributable to the regular percentage.

"(2) ENERGY INVESTMENT CREDIT.—The term 'energy investment credit' means that portion of the credit allowable by section 38 which is attributable to the energy percentage.

"(3) ESOP CREDIT.—The term 'ESOP credit' means the sum of—

"(A) the basic ESOP credit, and

"(B) the matching ESOP credit.

"(4) BASIC ESOP CREDIT.—The term 'basic ESOP credit' means that portion of the credit allowable by section 38 which is attributable to the basic ESOP percentage.

"(5) MATCHING ESOP CREDIT.—The term 'matching ESOP credit' means that portion of the credit allowable by section 38 which is attributable to the matching ESOP.

"(6) BASIC ESOP PERCENTAGE.—The term 'basic ESOP percentage' means the 1-percent ESOP percentage set forth in section 46(a)(2)(E)(i).

"(7) MATCHING ESOP PERCENTAGE.—The term 'matching ESOP percentage' means the additional ESOP percentage (not to exceed ½ of 1 percent) set forth in section 46(a)(2)(E)(ii)."

(c) ASSESSABLE PENALTIES.—

(1) IN GENERAL.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding at the end thereof the following new section:

"SEC. 6699. ASSESSABLE PENALTIES RELATING TO ESOP.

"(a) IN GENERAL.—If a taxpayer who has claimed an ESOP credit for any taxable year—

"(1) fails to satisfy any requirement provided by section 409A, or

"(2) fails to make any contribution which is required under section 48(n) within the period required for making such contribution,

the taxpayer shall pay a penalty in an amount equal to the amount involved in such failure.

"(b) NO PENALTY WHERE THERE IS TIMELY CORRECTION OF FAILURE.—Subsection (a) shall not apply with respect to any failure if the employer corrects such failure (as determined by the Secretary) within 90 days after the Secretary notifies him of such failure.

"(c) AMOUNT INVOLVED DEFINED.—

"(1) IN GENERAL.—For purposes of this section, the term 'amount involved' means an amount determined by the Secretary.

"(2) MAXIMUM AND MINIMUM AMOUNT.—The amount determined under paragraph (1)—

"(A) shall not exceed the amount determined by multiplying the qualified investment of the employer for the taxable year to which the failure relates by the ESOP percentage claimed by the employer for such year, and

"(B) shall not be less than the product of one-half of 1 percent of the amount referred to in subparagraph (A), multiplied by the number of months (or parts thereof) during which such failure continues."

(2) CLERICAL AMENDMENT.—The table of sections for such subchapter B is amended by adding at the end thereof the following new item:

Sec. 6699. Assessable penalties relating to ESOP."

(d) REGULAR TAX DEDUCTION FOR PURPOSES OF THE MINIMUM TAX DETERMINED WITHOUT REGARD TO ESOP PERCENTAGE.—Subsection (c) of section 56 (defining regular tax deduction) is amended by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, the amount of the credit allowable under section 38 shall be determined without regard to the ESOP percentage set forth in section 46(a)(2)(E)."

(e) ESOP CREDIT EXTENDED FOR 3 YEARS.—Subparagraph (E) of section 46(a)(2) (relating to amount of business investment credit for current taxable year) is amended by striking out "and ending on December 31, 1980," each place it appears and inserting in lieu thereof "December 31, 1983."

(f) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) Subsections (d), (e), and (f) of section 301 of the Tax Reduction Act of 1975 are hereby repealed.

(2) Subparagraph (E) of section 46(a)(2) is amended—

(A) by striking out "section 301(e) of the Tax Reduction Act of 1975" and inserting in lieu thereof "section 48(n)(1)(B)", and

(B) by striking out "section 301(d) of the Tax Reduction Act of 1975" and inserting in lieu thereof "section 409A".

(3) Paragraph (21) of section 401(a) is amended to read as follows:

"(21) A trust forming part of an ESOP shall not fail to be considered a permanent program merely because employer contributions under the plan are determined solely by reference to the amount of credit which would be allowable under section 46(a) if the employer made the transfer described in section 48(n)(1)."

(4) The last sentence of section 1504(a) (defining affiliated group) is amended to read as follows:

"As used in this subsection, the term 'stock' does not include nonvoting stock which is limited and preferred as to dividends, employer securities (within the meaning for section 409A(l)) while such securities are held under an ESOP, or qualifying employer securities (within the meaning of section 4975(e)(8)) while such securities are held under a leveraged employee stock ownership plan which meets the requirements of section 4975(e)(7)."

(5) Paragraph (7) of section 4975(e) (defining employee stock ownership plan) is amended—

(A) by striking out "EMPLOYEE" in the paragraph heading and inserting in lieu thereof "LEVERAGED EMPLOYEE", and

(B) by striking out "employee" in the text and inserting in lieu thereof "leveraged employee", and

(C) by adding at the end thereof the following new sentence: "A plan shall not be treated as a leveraged employee stock ownership plan unless it meets the requirements of subsections (e) and (h) of section 409A."

(6) Paragraph (3) of section 4975(d) is amended by striking out "employee" and inserting in lieu thereof "leveraged employee".

(7) Subparagraph (B) of section 415(c)(6) is amended by striking out clauses (i) and (ii) and inserting in lieu thereof the following:

"(i) the term 'employee stock ownership plan' means a leveraged employee stock ownership plan (within the meaning of section 4975(e)(7)) or an ESOP,

"(ii) the term 'employer securities' has the meaning given to such term by section 409A,".

(8) The table of sections for part I of subchapter D of chapter 1 is amended by inserting after the item relating to section 409 the following new item:

"Sec. 409A. Qualification for ESOP's."

(9) Section 404(a)(2) and section 805(d) are each amended by striking out "and (20)" and inserting in lieu thereof "(20), and (22)".

(g) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section (other than by subsection (f)(3) shall apply with respect to qualified investment for taxable years beginning after December 31, 1978. The amendment made by subsection (f)(7) shall apply to years beginning after December 31, 1978.

(2) RETROACTIVE APPLICATION OF AMENDMENT MADE BY SUBSECTION (d).—In determining the regular tax deduction under section 6 of the Internal Revenue Code of 1954 for any taxable year beginning before January 1, 1979, the amount of the credit allowable under section 38 shall be determined without regard to section 46(a)(2)(B) of such Code (as in effect before the enactment of the Energy Tax Act of 1978).

SEC. 142. CERTAIN LUMP SUM DISTRIBUTIONS EXCLUDED FROM GROSS ESTATE WHERE RECIPIENT ELECTS NOT TO APPLY 10-YEAR AVERAGING.

(a) IN GENERAL.—Subsection (c) of section 2039 (relating to exemption of annuities under certain trusts and plans) is amended by striking out "(other than a lump sum distribution described in section 402(e)(4), determined without regard to the next to the last sentence of section 402(e)(4)(A))" and inserting in lieu thereof "(other than an amount described in subsection (f))".

(b) DEFINITIONS.—Section 2039 is amended by adding at the end thereof the following new subsection:

"(f) LUMP SUM DISTRIBUTIONS.—

"(1) IN GENERAL.—An amount is described in this subsection if it is a lump sum distribution described in section 402(e)(4)(determined without regard to the next to the last sentence of section 402(e)(4)(A))

"(2) EXCEPTION WHERE RECIPIENT ELECTS NOT TO TAKE 10-YEAR AVERAGING.—A lump sum distribution described in paragraph (1) shall be treated as not described in this subsection if the recipient elects irrevocably (at such time and in such manner as the Secretary may by regulations prescribe) to treat the distribution as taxable under section 402 (a) without the application of paragraph (2) thereof."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to the estates of decedents dying after December 31, 1978.

SEC. 143. QUALIFIED PLANS REQUIRED TO PASS THROUGH VOTING RIGHTS ON EMPLOYER SECURITIES.

(a) IN GENERAL.—Subsection (a) of section 401 (relating to qualified pension, profit-sharing, and stock bonus plans) is amended by inserting after paragraph (21) the following new paragraph;

"(A) is established by an employer whose stock is not publicly traded, and

"(B) after acquiring securities of the employer, more than 10 percent of the total assets of the plan was securities of the employer,

any trust forming part of such plan shall not constitute a qualified trust under this section unless the plan meets the requirements of subsection (e) of section 409A."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to acquisitions of securities after December 31, 1979.

Subtitle E—Retirement Plans

SEC. 152. SIMPLIFIED EMPLOYEE PENSIONS.

(a) INCREASE IN MAXIMUM LIMITATION UNDER SECTION 408 TO $7,500.—Section 408 (relating to individual retirement account) is amended by redesignating subsection (j) as subsection (m) and by inserting after subsection (i) the following new subsection:

"(j) INCREASE IN MAXIMUM LIMITATIONS FOR SIMPLIFIED EMPLOYEE PENSIONS.—In the case of a simplified employee pension, this section shall be applied by substituting '$7,500' for '$1,500' in the following provisions:

"(1) paragraph (1) of subsection (a),

"(2) paragraph (2) of subsection (b), and

"(3) paragraph (5) of subsection (b)."

(b) SIMPLIFIED EMPLOYEE PENSION DEFINED.—Section 408 is amended by inserting after subsection (j) the following new subsection:

"(k) SIMPLIFIED EMPLOYEE PENSION DEFINED.—

"(1) IN GENERAL.—For purposes of this title, the term 'simplified employee pension' means an individual retirement account or individual retirement annuity with respect to which the requirements of paragraphs (2), (3), (4), and (5) of this subsection are met.

"(2) PARTICIPATION REQUIREMENTS.—This paragraph is satisfied with respect to a simplified employee pension for a calendar year only if for such year the employer contributes to the simplified employee pension of each employee who—

"(A) has attained age 25, and

"(B) has performed service for the employer during at least 3 of the immediately preceding 5 calendar years.

"(3) CONTRIBUTIONS MAY NOT DISCRIMINATE IN FAVOR OF THE HIGHLY COMPENSATED, ETC.—

"(A) IN GENERAL.—The requirements of this paragraph are met with respect to a simplified employee pension for a calendar year if for such year the contributions made by the employer to simplified employee pensions for his employees do not discriminate in favor of any employee who is—

"(i) an officer,

"(ii) a shareholder,

"(iii) a self-employed individual, or

"(iv) highly compensated.

"(B) SPECIAL RULES.—For purposes of subparagraph (A)—

"(i) there shall be excluded from consideration employees described in subparagraph (A) or (C) of section 410(b)(2), and

"(ii) an individual shall be considered a shareholder if he owns (with the application of section 318) more than 10 percent of the value of the stock of the employer.

"(C) CONTRIBUTIONS MUST BEAR A UNIFORM RELATIONSHIP TO TOTAL COMPENSATION.—For purposes of subparagraph (A), employer contributions to simplified employee pensions shall be considered discriminatory unless contributions thereto bear a uniform relationship to the total compensation (not in excess of the first $100,000) of each employee maintaining a simplified employee pension.

"(D) TREATMENT OF CERTAIN CONTRIBUTIONS AND TAXES.—Except as provided in this subparagraph, employer contributions do not meet the requirements of this paragraph unless such contributions meet the requirements of this paragraph without taking into account contributions or benefits under chapter 2 (relating to tax on self-employment income), chapter 21 (relating to Federal Insurance Contribution Act), title II of the Social Security Act, or any other Federal or State law. Taxes paid under section 3111 (relating to tax on employers) with respect to an employee may, for purposes of this paragraph, be taken into account as a contribution by the employer to an employee's simplified employee pension. If contributions are made to the simplified employee pension of an owner-employee, the preceding sentence shall not apply unless taxes paid by all such owner-employees under chapter 2, and the taxes which would be payable under chapter 2 by such owner-employees but for paragraphs (4) and (5) of section 1402(c), are taken into account as contributions by the employer on behalf of such owner-employees.

"(4) WITHDRAWALS MUST BE PERMITTED.—A simplified employee pension meets the requirements of this paragraph only if—

"(A) employer contributions thereto are not conditioned on the retention in such pension of any portion of the amount contributed, and

"(B) there is no prohibition imposed by the employer on withdrawals from the simplified employee pension.

"(5) CONTRIBUTIONS MUST BE MADE UNDER WRITTEN ALLOCATION FORMULA.—The requirements of this paragraph are met with respect to a simplified employee pension only if employer contributions to such pension are determined under a definite written allocation formula which specifies—

"(A) the requirements which an employee must satisfy to share in an allocation, and

"(B) the manner in which the amount allocated is computed.

"(6) DEFINITIONS.—For purposes of this subsection and subsection (l)—

"(A) EMPLOYEE, EMPLOYER, OR OWNER-EMPLOYEE.—The terms 'employee', 'employer', and 'owner-employee' shall have the respective meanings given such terms by section 401(c).

"(B) COMPENSATION.—The term 'compensation' means, in the case of an employee within the meaning of section 401(c)(1), earned income within the meaning of section 401(c)(2).

"(l) SIMPLIFIED EMPLOYER REPORTS.—An employer who makes a contribution on behalf of an employee to a simplified employee pension shall provide such simplified reports with respect to such contributions

as the Secretary may require by regulations. The reports required by this subsection shall be filed at such time and in such manner, and information with respect to such contributions shall be furnished to the employee at such time and in such manner, as may be required by regulations."

(c) MAXIMUM DEDUCTION UNDER SECTION 219.—Subsection (b) of section 219 (relating to maximum deduction in the case of retirement savings) is amended by adding at the end thereof the following new paragraph:

"(7) SIMPLIFIED EMPLOYEE PENSIONS.—In the case of an employer contribution on behalf of the employee to a simplified employee pension, paragraph (2) shall not apply with respect to the employer contribution and the limitation under paragraph (1) shall be the lesser of—

"(A) 15 percent of compensation includible in the employee's gross income for the taxable year (determined without regard to the employer contribution to the simplified employee pension), or

"(B) the sum of—

"(i) the amount contributed by the employer to the simplified employee pension and included in gross income (but not in excess of $7,500), and

"(ii) $1,500, reduced (but not below zero) by the amount described in clause (i).

In the case of an employee who is an officer, shareholder, or owner-employee described in section 408(k)(3), the amount referred to in subparagraph (B) shall be reduced by the amount of tax taken into account with respect to such individual under subparagraph (D) of section 408(k)(3)."

(d) EMPLOYEES OF ENTERPRISES UNDER COMMON CONTROL.—Subsections (b) and (c) of section 414 are each amended by inserting "408(k)," after "401,".

(e) SIMPLIFIED EMPLOYEE PENSION MAY BE TAKEN INTO ACCOUNT IN DETERMINING WHETHER EMPLOYER MEETS CERTAIN OTHER NONDISCRIMINATION PROVISIONS.—Paragraph (5) of section 401(a) is amended by adding at the end thereof the following new sentence: "For purposes of determining whether one or more plans of an employer satisfy the requirements of paragraph (4) and of section 410(b), an employer may take into account all simplified employee pensions to which only the employer contributes."

(f) EMPLOYEE DEDUCTIONS.—Section 404 (relating to deduction for contributions of an employer) is amended by adding the following new subsection at the end thereof:

"(h) SPECIAL RULES FOR SIMPLIFIED EMPLOYEE PENSIONS.—

"(1) IN GENERAL.—Employer contributions to a simplified employee pension shall be treated as if they are made to a plan subject to the requirements of this section. Employer contributions to a simplified employee pension are subject to the following limitations:

"(A) Contributions made for a calendar year are deductible for the taxable year with which or within which the calendar year ends.

"(B) Contributions made within 3½ months after the close of a calendar year are treated as if they were made on the last day of such calendar year if they are made on account of such calendar year.

"(C) The amount deductible in a taxable year for a simplified employee pension shall not exceed 15 percent of the compensation paid to the employees during the calendar year ending with or within the taxable year. The excess of the amount contributed over the amount deductible for a taxable year shall be deductible in the succeeding taxable years in order of time, subject to the 15 percent limit of the preceding sentence.

"(2) EFFECT ON STOCK BONUS AND PROFIT-SHARING TRUST.—For any taxable year for which the employer has a deduction under subparagraph (1), the otherwise applicable limitations in subsection (a)(3)(A) shall be reduced by the amount of the allowable deductions under subparagraph (1) with respect to participants in the stock bonus or profit-sharing trust.

"(3) EFFECT ON LIMIT ON DEDUCTIONS.—For any taxable year for which the employer has a deduction under subparagraph (1), the otherwise applicable 25 percent limitations in subsection (a)(7) shall be reduced by the amount of the allowable deductions under subparagraph (1) with respect to participants in the stock bonus or profit-sharing trust.

"(4) EFFECT ON SELF-EMPLOYED INDIVIDUALS.—The limitations described in paragraphs (1), (2)(A), and (4) of subsection (e) for any taxable year shall be reduced by the amount of the allowable deductions under subparagraph (1) with respect to an employee within the meaning of section 401(c)(1)."

(g) AMENDMENTS TO SECTION 415.—Section 415 (relating to limitations on benefits and contributions under certain plans) is amended—

(1) by redesignating subparagraphs (E) and (F) of subsection (a)(2) and subparagraphs (F) and (G) and by inserting after subparagraph (D) the following new subparagraph:

"(E) a simplified employee pension,";

(2) by inserting "408(k)," after "408(b)," in the material immediately following subparagraph (G) of section 415(b)(2);

(3) by inserting "any simplified employee pension," after "section 408(b)," in section 415(e)(5); and

(4) by striking out "or" in section 415(k)(1)(F), by redesignating subparagraph (G) of section 415(k)(1) as subparagraph (H), and by inserting after section 415(k)(1)(F) the following new subparagraph:

"(G) a simplified employee pension, or".

(h) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1978.

SEC. 153. DEFINED BENEFIT PLAN LIMITS.

(a) IN GENERAL.—Subsection (b) of section 415 (relating to limitation for defined benefit plans) is amended by adding at the end thereof the following new paragraph:

"(7) BENEFITS UNDER CERTAIN COLLECTIVELY BARGAINED PLANS.—For a year, the limitation referred to in paragraph (1)(B) shall not apply to benefits with respect to a participant under a defined benefit plan—

"(A) which is maintained for such year pursuant to a collective bargaining agreement between employee representatives and one or more employers,

"(B) which, at all times during such year, has at least 100 participants,

"(C) benefits under which are determined by multiplying a specified amount (which is the same amount for each participant) by the number of the participant's years of service,

"(D) which provides that an employee who has at least 4 years of service has a nonforfeitable right to 100 percent of his accrued benefit dreived from employer contributions, and

"(E) which requires, as a condition of participation in the plan, that an employee complete a period of not more than 60 consecutive days of service with the employer or employers maintaining the plan.

This paragraph shall not apply to a participant whose compensation for any 3 years during the 10-year period immediately preceding the year in which he separates from service exceeded the average compensation for such 3 years of all participants in such plan. For any year for which the paragraph applies to benefits with respect to a participant, paragraph (1)(A) and subsection (d)(1)(A) shall be applied with respect to such participant by substituting '37,500' for '75,000'."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to years beginning after December 31, 1978.

SEC. 154. CUSTODIAL ACCOUNTS FOR REGULATED INVESTMENT COMPANY STOCK.

(a) AMENDMENT OF SECTION 403.—Subparagraph (A) of section 403(b)(7) (relating to custodial accounts for regulated investment company stock) is amended to read as follows:

"(A) AMOUNTS PAID TREATED AS CONTRIBUTIONS.—For purposes of this title, amounts paid by an employer described in paragraph (1)(A) to a custodial account which satisfied the requirements of section 401(f)(2) shall be treated as amounts contributed by him for an annuity contract for his employee if—

(i) the amounts are to be invested in regulated investment company stock to be held in that custodial account, and

(ii) under the custodial account no such amounts may be paid or made available to any distributee before the employee dies, attains age 59½, separates from service, becomes disabled (within the meaning of section 72(m)(7)), or encounters financial hardship."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 1978.

SEC. 155. PENSION PLAN RESERVES.

(a) IN GENERAL.—Subsection (d) of section 805 (relating to pension plan reserves) is amended—

(1) by striking out "or" at the end of paragraph (4);

(2) by striking out the period at the end of paragraph (5) and inserting in lieu thereof "; or"; and

(3) by adding at the end thereof the following new paragraph:

"(6) purchased by—

"(A) a governmental plan (within the meaning of section 414(d)), or

"(B) the Government of the United States, the government of any State or political subdivision thereof, or by any agency or

instrumentality of the foregoing, for use in satisfying an obligation of such government, political subdivision, or agency or instrumentality to provide a benefit under a plan described in subparagraph (A)."

(*b*) *EFFECTIVE DATE.—The amendments made by this section apply to taxable years beginning after December 31, 1978.*

SEC. 156. ROLLOVER OF SECTION 403(b) ANNUITIES PERMITTED.

(*a*) *GENERAL RULE.—Subsection (b) of section 403 (relating to taxability of beneficiary under annuity purchased by section 501(c)(3) organization or public school) is amended by adding at the end thereof the following new paragraph:*

"(*8*) *ROLLOVER AMOUNTS.—*

"(*A*) *GENERAL RULE.—If—*

"(*i*) *the balance to the credit of an employee is paid to him in a qualifying distribution,*

"(*ii*) *the employee transfers any portion of the property he receives in such distribution to an individual retirement plan or to an annuity contract described in paragraph (1), and*

"(*iii*) *in the case of a distribution of property other than money, the property so transferred consists of the property distributed,*

then such distribution (to the extent so transferred) shall not be includible in gross income for the taxable year in which paid.

"(*B*) *QUALIFYING DISTRIBUTION DEFINED.—*

"(*i*) *IN GENERAL.—For purposes of subparagraph (A), the term 'qualifying distribution' means 1 or more distributions from an annuity contract described in paragraph (1) which would constitute a lump sum distribution within the meaning of section 402(e)(4)(A) (determined without regard to subparagraphs (B) and (H) of section 402(e)(4)) if such annuity contract were described in subsection (a).*

"(*ii*) *AGGREGATION OF ANNUITY CONTRACTS.—For purposes of this paragraph, all annuity contracts described in paragraph (1) purchased by an employer shall be treated as a single contract, and section 402(e)(4)(C) shall not apply.*

"(*C*) *CERTAIN RULES MADE APPLICABLE.—Rules similar to the rules of subparagraphs (B), (C), and (E)(i) of section 402(a)(5) and of paragraphs (6) and (7) of section 402(a) shall apply for purposes of subparagraph (A).*"

(*b*) *TREATMENT OF ROLLOVER CONTRIBUTIONS.—Section 403(b)(1) (relating to annuities purchased by certain exempt organizations and public schools) is amended by adding at the end thereof the following new sentence: "For purposes of applying the rules of this subsection to amounts contributed by an employer for a taxable year, amounts transferred to a contract described in this paragraph by reason of a rollover contribution described in paragraph (8) of this subsection or section 408(d)(3)(A)(iii) or 409(d)(3)(C) shall not be considered contributed by such employer.*"

(*c*) *TECHNICAL AND CONFORMING AMENDMENTS.—*

(*1*) *Subparagraph (A) of section 408(d)(3) is amended by striking out "or" at the end of clause (i), by striking out the period at the*

end of clause (ii) and inserting in lieu thereof "; or", and by adding at the end thereof the following new clause:

"(iii)(I) the entire amount received (including money and other property) represents the entire interest in the account or the entire value of the annuity,

"(II) no amount in the account and no part of the value of the annuity is attributable to any source other than a rollover contribution from an annuity contract described in section 403(b) and any earnings on such rollover, and

"(III) the entire amount thereof is paid into another annuity contract described in section 403(b) (for the benefit of such individual) not later than the 60th day after he receives the payment or distribution."

(2) Subparagraph (C) of section 409(b)(3) is amended—

(A) by striking out "or an annuity plan described in section 403(a)" in the first sentence and inserting in lieu thereof "an annuity plan described in section 403(a), or an annuity contract described in section 403(b)", and

(B) by adding at the end thereof the following new sentence: "This subparagraph does not apply in the case of a transfer to an annuity contract described in section 403(b) unless no part of the value of such proceeds is attributable to any source other than a rollover contribution from such an annuity contract."

(3) Sections 219(b)(4), 220(b)(5), 408(a)(1), 409(a)(4), and 4973(b)(1)(A) are each amended by inserting "403(b)(8)," after "403(a)(4)," each place it appears.

(4) Section 2039(e) is amended by inserting after "403(a)(4)," the following: "section 403(b)(8) (but only to the extent such contribution is attributable to a distribution from a contract described in subsection (c)(3)),".

(5) Section 4973(c)(1) is amended by inserting after "account" the following: "(other than a rollover contribution described in section 403(b)(8), 408(d)(3)(A)(iii), or 409(d)(3)(C))".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to distributions or transfers made after December 31, 1978, in taxable years beginning after such date.

SEC. 157. INDIVIDUAL RETIREMENT ACCOUNT TECHNICAL CHANGES.

(a) EXTENSION OF PERIOD FOR MAKING INDIVIDUAL RETIREMENT PLAN CONTRIBUTIONS.—

(1) AMENDMENT OF SECTION 219(c)(3).—Paragraph (3) of section 219(c) (relating to time when contributions deemed made in the case of retirement savings) is amended by striking out "not later than 45 days after the end of such taxable year" and inserting in lieu thereof "not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof)".

(2) AMENDMENT OF SECTION 220(c)(4).—Paragraph (4) of section 220(c) (relating to time when contributions deemed made in the case of retirement savings for certain married individuals) is amended by striking out "not later than 45 days after the end of such taxable year" and inserting in lieu thereof "not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof)".

(3) EFFECTIVE DATE.—*The amendments made by this subsection shall apply to taxable years beginning after December 31, 1977.*

(b) EXCESS CONTRIBUTIONS MAY BE DEDUCTED IN SUBSEQUENT YEAR FOR WHICH THERE IS AN UNUSED LIMITATION.—

(1) AMENDMENT OF SECTION 219.—*Subsection (c) of section 219 (relating to definitions and special rules for retirement savings) is amended by adding at the end thereof the following new paragraph:*

"(5) EXCESS CONTRIBUTIONS TREATED AS CONTRIBUTION MADE DURING SUBSEQUENT YEAR FOR WHICH THERE IS AN UNUSED LIMITATION.—

"(A) IN GENERAL.—*If for the taxable year the maximum amount allowable as a deduction under this section exceeds the amount contributed, then the taxpayer shall be treated as having made an additional contribution for the taxable year in an amount equal to the lesser of—*

"(i) *the amount of such excess, or*

"(ii) *the amount of the excess contributions for such taxable year (determined under section 4973(b)(2) without regard to subparagraph (C) thereof).*

"(B) AMOUNT CONTRIBUTED.—*For purposes of this paragraph, the amount contributed—*

"(i) *shall be determined without regard to this paragraph, and*

"(ii) *shall not include any rollover contribution.*

"(C) SPECIAL RULE WHERE EXCESS DEDUCTION WAS ALLOWED FOR CLOSED YEAR.—*Proper reduction shall be made in the amount allowable as a deduction by reason of this paragraph for any amount allowed as a deduction under this section or section 220 for a prior taxable year for which the period for assessing deficiency has expired if the amount so allowed exceeds the amount which should have been allowed for such prior taxable year.*"

(2) AMENDMENT OF SECTION 220.—*Subsection (c) of section 220 (relating to definitions and special rules for retirement savings for certain married individuals) is amended by adding at the end thereof the following new paragraph:*

"(6) EXCESS CONTRIBUTIONS TREATED AS CONTRIBUTION MADE DURING SUBSEQUENT YEAR FOR WHICH THERE IS AN UNUSED LIMITATION.—

"(A) IN GENERAL.—*If for the taxable year the maximum amount allowable as a deduction under this section exceeds the amount contributed, then the taxpayer shall be treated as having made an additional contribution for the taxable year in an amount equal to the lesser of—*

"(i) *the amount of such excess, or*

"(ii) *the amount of the excess contributions for such taxable year (determined under section 4973(b)(2) without regard to subparagraph (C) thereof).*

"(B) AMOUNT CONTRIBUTED.—*For purposes of this paragraph, the amount contributed—*

"(i) *shall be determined without regard to this paragraph, and*

"(ii) *shall not include any rollover contribution.*

"(C) SPECIAL RULE WHERE EXCESS DEDUCTION WAS ALLOWED FOR CLOSED YEAR.—Proper reduction shall be made in the amount allowable as a deduction by reason of this paragraph for any amount allowed as a deduction under this section or section 219 for a prior taxable year for which the period for assessing a deficiency has expired if the amount so allowed exceeds the amount which should have been allowed for such prior taxable year."

(3) AMENDMENT OF SECTION 4973.—Paragraph (2) of section 4973(b) (defining excess contributions) is amended to read as follows:

"(2) the amount determined under this subsection for the preceding taxable year reduced by the sum of—

"(A) the distributions out of the account for the taxable year which were included in the gross income of the payee under section 408(d)(1),

"(B) the distributions out of the account for the taxable year to which section 408(d)(5) applies, and

"(C) the excess (if any) of the maximum amount allowable as a deduction under section 219 or 220 for the taxable year over the amount contributed (determined without regard to sections 219(c)(5) and 220(c)(6)) to the accounts or for the annuities or bonds for the taxable year."

(4) EFFECTIVE DATE.—

(A) IN GENERAL.—The amendments made by this subsection shall apply to the determination of deductions for taxable years beginning after December 31, 1975.

(B) TRANSITIONAL RULE.—If, but for this subparagraph, an amount would be allowable as a deduction by reason of section 219(c)(5) or 220(c)(6) of the Internal Revenue Code of 1954 for a taxable year beginning before January 1, 1978, such amount shall be allowable only for the taxpayer's first taxable year beginning in 1978.

(c) ADDITIONAL PERIOD TO RECTIFY CERTAIN EXCESS CONTRIBUTIONS.—

(1) GENERAL RULE.—Subsection (d) of section 408 (relating to tax treatment of distributions) is amended by redesignating paragraph (5) as paragraph (6) and by inserting after paragraph (4) the following new paragraph:

"(5) CERTAIN DISTRIBUTIONS OF EXCESS CONTRIBUTIONS AFTER DUE DATE FOR TAXABLE YEAR.—

"(A) IN GENERAL.—In the case of any individual, if the aggregate contributions (other than rollover contributions) paid for any taxable year to an individual retirement account or for an individual retirement annuity do not exceed $1,750, paragraph (1) shall not apply to the distribution of any such contribution to the extent that such contribution exceeds the amount allowable as a deduction under section 219 or 220 for the taxable year for which the contribution was paid—

"(i) if such distribution is received after the date described in paragraph (4),

"(ii) but only to the extent that no deduction has been allowed under section 219 or 220 with respect to such excess contribution.

"(B) EXCESS ROLLOVER CONTRIBUTIONS ATTRIBUTABLE TO ERRONEOUS INFORMATION.—If—

"(i) the taxpayer reasonably relies on information supplied pursuant to subtitle F for determining the amount of a rollover contribution, but

"(ii) such information was erroneous, subparagraph (A) shall be applied by increasing the dollar limit set forth therein by that portion of the excess contribution which was attributable to such information."

(2) EFFECTIVE DATE.—

(A) IN GENERAL.—The amendments made by paragraph (1) shall apply to distributions in taxable years beginning after December 31, 1975.

(B) TRANSITIONAL RULE.—In the case of contributions for taxable years beginning before January 1, 1978, paragraph (5) of section 408(d) of the Internal Revenue Code of 1954 shall be applied as if such paragraph did not contain any dollar limitation.

(d) REQUIREMENT THAT ANNUITY CONTRACTS WILL QUALIFY AS INDIVIDUAL RETIREMENT ANNUITY ONLY IF THE PREMIUMS ARE FLEXIBLE.—

(1) IN GENERAL.—Paragraph (2) of section 408(b) (defining individual retirement annuity) is amended to read as follows:

"(2) Under the contract—

"(A) the premiums are not fixed,

"(B) the annual premium will not exceed $1,500, and

"(C) any refund of premiums will be applied before the close of the calendar year following the year of the refund toward the payment of future premiums or the purchase of additional benefits."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to contracts issued after the date of the enactment of this Act.

(3) TAX RELIEF FOR FIXED PREMIUM CONTRACTS HERETOFORE ISSUED.—In the case of any annuity or endowment contract issued on or before the date of the enactment of this Act which would be an individual retirement annuity within the meaning of section 408(b) of the Internal Revenue Code of 1954 (as amended by paragraph (1)) but for the fact that the premiums under the contract are fixed, at the election of the taxpayer an exchange before January 1, 1981, of that contract for an individual retirement annuity within the meaning of such section 408(b) (as amended by paragraph (1)) shall be treated as a nontaxable exchange which does not constitute a distribution.

(e) CLARIFICATION OF DOLLAR LIMIT IN THE CASE OF INDIVIDUAL RETIREMENT ANNUITIES AND RETIREMENT BONDS.—

(1) IN GENERAL.—

(A) AMENDMENT OF SECTION 408(b)(2).—Subparagraph (B) of section 408(b)(2) (as amended by paragraph (1) of subsection (d)) is amended by inserting "on behalf of any individual" after "annual premium".

(B) AMENDMENT OF SECTION 409(a)(4).—Paragraph (4) of section 409(a) (relating to retirement bonds) is amended by inserting "on behalf of any individual" after "May not contribute".

(2) EFFECTIVE DATE.—*The amendments made by paragraph (1) shall apply to taxable years beginning after December 31, 1976.*

(f) ROLLOVER OF PROCEEDS FROM SALE OF PROPERTY PERMITTED.—

(1) ROLLOVERS FROM QUALIFIED EMPLOYEES' TRUSTS AND ANNUITIES.—*Paragraph (6) of section 402(a) (relating to special rollover rules) is amended by adding at the end thereof the following new subparagraph:*

"(D) SALES OF DISTRIBUTED PROPERTY.—*For purposes of subparagraphs (5) and (7)—*

"(i) TRANSFER OF PROCEEDS FROM SALE OF DISTRIBUTED PROPERTY TREATED AS TRANSFER OF DISTRIBUTED PROPERTY.—*The transfer of an amount equal to any portion of the proceeds from the sale of property received in the distribution shall be treated as the transfer of property received in the distribution.*

"(ii) PROCEEDS ATTRIBUTABLE TO INCREASE IN VALUE.—*The excess of fair market value of property on sale over its fair market value on distribution shall be treated as property received in the distribution.*

"(iii) DESIGNATION WHERE AMOUNT OF DISTRIBUTION EXCEEDS ROLLOVER CONTRIBUTION.—*In any case where part or all of the distribution consists of property other than money, the taxpayer may designate—*

"(I) *the portion of the money or other property which is to be treated as attributable to employee contributions, and*

"(II) *the portion of the money or other property which is to be treated as included in the rollover contribution.*

Any designation under this clause for a taxable year shall be made not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof). Any such designation, once made, shall be irrevocable.

"(iv) TREATMENT WHERE NO DESIGNATION.—*In any case where part or all of the distribution consists of property other than money and the taxpayer fails to make a designation under clause (iii) within the time provided therein, then—*

"(I) *the portion of the money or other property which is to be treated as attributable to employee contributions, and*

"(II) *the portion of the money or other property which is to be treated as included in the rollover contribution*

shall be determined on a ratable basis.

"(v) NONRECOGNITION OF GAIN OR LOSS.—*In the case of any sale described in clause (i), to the extent that an amount equal to the proceeds is transferred pursuant to paragraph (5)(B) or (7)(B) (as the case may be), neither gain nor loss on such sale shall be recognized.*"

(2) EFFECTIVE DATE.—*The amendment made by paragraph (1) shall apply to qualifying rollover distributions (as defined in section*

402(a)(5)(D)(i) of the Internal Revenue Code of 1954) completed after December 31, 1978, in taxable years ending after such date.

(g) DISTRIBUTION FROM EMPLOYEES' QUALIFIED PLAN OR ANNUITY TO SPOUSE MAY BE ROLLOVER CONTRIBUTION TO AN INDIVIDUAL RETIREMENT PLAN.—

(1) ROLLOVERS FROM QUALIFIED EMPLOYEES' TRUST.—Subsection (a) of section 402 (relating to taxability of beneficiary of exempt trust) is amended by adding at the end thereof the following new paragraph:

"(7) ROLLOVER WHERE SPOUSE RECEIVES LUMP-SUM DISTRIBUTION AT DEATH OF EMPLOYEE.—

"(A) GENERAL RULE.—If—

"(i) any portion of a lump-sum distribution from a qualified trust is paid to the spouse of the employee on account of the employee's death,

"(ii) the spouse transfers any portion of the property which the spouse receives in such distribution to an individual retirement plan, and

"(iii) in the case of a distribution of property other than money, the amount so transferred consists of the property distributed,

then such distribution (to the extent so transferred) shall not be includible in gross income for the taxable year in which paid.

"(B) CERTAIN RULES MADE APPLICABLE.—Rules similar to the rules of subparagraphs (B) through (E) of paragraph (5) and of paragraph (6) shall apply for purposes of this paragraph."

(2) ROLLOVER FROM QUALIFIED ANNUITY PLANS.—Subparagraph (B) of section 403(a)(4), as amended by section 21(b), is amended by striking out "paragraph (6)" and inserting lieu thereof "paragraphs (6) and (7)".

(3) NO ROLLOVER TO QUALIFIED PLAN OR ANNUITY FROM IRA TO WHICH SPOUSE MADE ROLLOVER CONTRIBUTION.—Subparagraph (B) of section 408(d)(3) is amended by adding at the end thereof the following: "Clause (ii) of subparagraph (A) shall not apply to any amount paid or distributed out of an individual retirement account or an individual retirement annuity to which an amount was contributed which was treated as a rollover contribution by section 402(a)(7) (or in the case of an individual retirement annuity, such section as made applicable by section 403(a)(4)(B))."

(4) EFFECTIVE DATE.—The amendments made by this subsection shall apply to lump-sum distributions completed after December 31, 1978, in taxable years ending after such date.

(h) REMOVAL OF CERTAIN REQUIREMENTS.—

(1) DISREGARD OF 5-YEAR MINIMUM PARTICIPATION RULE FOR PURPOSES OF ROLLOVERS.—Subclause (II) of section 402(a)(5)(D)(i) is amended by striking out "subsection (e)(4)(B)" and inserting in lieu thereof "subparagraphs (B) and (H) of subsection (e)(4)".

(2) REDUCTION OF REQUIRED PERIOD BETWEEN ROLLOVER CONTRIBUTIONS FROM 3 YEARS TO 1 YEAR.—The first sentence of subparagraph (B) of section 408(d)(3) is amended by striking out "3-year period" and inserting in lieu thereof "1-year period".

(3) EFFECTIVE DATE.—

(A) IN GENERAL.—*The amendments made by this section shall apply to payments made in taxable years beginning after December 31, 1977.*

(B) TRANSITIONAL RULE.—*In the case of any payment which is described in section 402(a)(5)(A) of 403(a)(4)(A) of the Internal Revenue Code of 1954 by reason of the amendments made by this section, the applicable period specified in section 402(a)(5)(C) of such Code (or in the case of an individual retirement annuity, such section as made applicable by section 403(a)(4)(B) of such Code) shall not expire before the close of December 31, 1978.*

(i) WAIVER OF EXCISE TAX ON CERTAIN ACCUMULATIONS IN INDIVIDUAL RETIREMENT ACCOUNTS OR ANNUITIES.—

(1) GENERAL RULE.—*Section 4974 (relating to excise tax on certain accumulations in individual retirement accounts or annuities) is amended by adding at the end thereof the following new subsection:*

"(c) WAIVER OF TAX IN CERTAIN CASES.—*If the taxpayer establishes to the satisfaction of the Secretary that—*

"(1) *the shortfall described in subsection (a) in the amount distributed during any taxable year was due to reasonable error, and*

"(2) *reasonable steps are being taken to remedy the shortfall,*

the Secretary may waive the tax imposed by subsection (a) for the taxable year."

(2) EFFECTIVE DATE.—*The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1975.*

(j) REMOVAL OF CERTAIN LIMITATIONS ON PROVISION ALLOWING CORRECTION OF EXCESS CONTRIBUTIONS.—

(1) GENERAL RULE.—*The last sentence of section 4973(b) (defining excess contributions) is amended to read as follows: "For purposes of this subsection, any contribution which is distributed from the individual retirement account, individual retirement annuity, or bond in a distribution to which section 408(d)(4) applies shall be treated as an amount not contributed."*

(2) EFFECTIVE DATE.—*The amendment made by paragraph (1) shall apply to contributions made for taxable years beginning after December 31, 1977.*

(k) SIMPLIFICATION OF RETURN REQUIREMENTS WITH RESPECT TO INDIVIDUAL RETIREMENT PLANS.—

(1) IN GENERAL.—*Section 6058 (relating to information required in connection with certain plans of deferred compensation) is amended by redesignating subsection (d) as subsection (f) and by striking out subsection (c) and inserting in lieu thereof the following new subsections:*

"(c) EMPLOYER.—*For purposes of this section, the term 'employer' includes a person described in section 401(c)(4) and an individual who establishes an individual retirement plan.*

"(d) COORDINATION WITH INCOME TAX RETURNS, ETC.—*An individual who establishes an individual retirement plan shall not be required to file a return under this section with respect to such plan for any taxable year for which there is—*

"(1) *no special IRP tax, and*

"(2) *no plan activity other than—*

"(A) the making of contributions (other than rollover contributions), and

"(B) the making of distributions.

"(e) SPECIAL IRP TAX DEFINED.—For purposes of this section, the term 'special IRP tax' means a tax imposed by—

"(1) section 408(f),

"(2) section 409(c),

"(3) section 4973, or

"(4) section 4974.".

(2) INDIVIDUAL RETIREMENT PLAN DEFINED.—Subsection (a) of section 7701 (relating to definitions of general application throughout the Code) is amended by adding at the end thereof the following new paragraph:

"(37) INDIVIDUAL RETIREMENT PLAN.—The term 'individual retirement plan' means—

"(A) an individual retirement account described in section 408(a),

"(B) an individual retirement annuity described in section 408(b), and

"(C) a retirement bond described in section 409."

(3) EFFECTIVE DATE.—The amendments made by paragraph (1) shall apply to returns for taxable years beginning after December 31, 1977. The amendment made by paragraph (2) shall apply to taxable years beginning after December 31, 1974.

Subtitle F—Other Individual Items

SEC. 161. CERTAIN GOVERNMENT SCHOLARSHIP AND AWARD PROGRAMS.

(a) GOVERNMENT HEALTH PROFESSION SCHOLARSHIP PROGRAMS.—Subsection (c) of section 4 of the Act entitled "An Act to suspend until the close of June 30, 1975, the duty on certain carboxymethyl cellulose salts, and for other purposes" (Public Law 93-483; 88 Stat. 1457) approved October 26, 1974, is amended—

(1) by striking out "1979" and inserting in lieu thereof "1980", and

(2) by striking out "1983" and inserting in lieu thereof "1984".

(b) NATIONAL RESEARCH SERVICE AWARDS.—

(1) GENERAL RULE.—Any amount paid to, or on behalf of, an individual from appropriated funds as a national research service award under section 472 of the Public Health Service Act shall be treated as a scholarship or fellowship grant under section 117 of the Internal Revenue Code of 1954.

(2) EFFECTIVE DATE.—The provisions of subsection (b) shall apply to awards made during calendar years 1974 through 1979.

SEC. 162. CANCELLATION OF STUDENT LOANS.

Subsection (c) of section 2117 of the Tax Reform Act of 1976 (relating to cancellation of certain student loans) is amended by striking out "January 1, 1979" and inserting in lieu thereof "January 1, 1983".

SEC. 163. TAX COUNSELING FOR THE ELDERLY.

(a) TRAINING AND TECHNICAL ASSISTANCE.—

(1) AGREEMENTS.—The Secretary, through the Internal Revenue Service, is authorized to enter into agreements with private or public

nonprofit agencies or organizations for the purpose of providing training and technical assistance to prepare volunteers to provide tax counseling assistance for elderly individuals in the preparation of their Federal income tax returns.

(2) OTHER ASSISTANCE.—In addition to any other forms of technical assistance provided under this section, the Secretary may provide—

(A) preferential access to Internal Revenue Service taxpayer service representatives for the purpose of making available technical information needed during the course of the volunteers' work;

(B) material to be used in making elderly persons aware of the availability of assistance under volunteer taxpayer assistance programs under this section; and

(C) technical materials and publications to be used by such volunteers.

(b) POWERS OF THE SECRETARY.—In carrying out his responsibilities under this section, the Secretary is authorized—

(1) to provide assistance to organizations which demonstrate, to the satisfaction of the Secretary, that their volunteers are adequately trained and competent to render effective tax counseling to the elderly;

(2) to provide for the training of such volunteers, and to assist in such training, to insure that such volunteers are qualified to provide tax counseling assistance to elderly individuals;

(3) to provide reimbursement to volunteers through such organizations for transportation, meals, and other expenses incurred by them in training or providing tax counseling assistance under this section, and such other support and assistance as he determines to be appropriate in carrying out the provisions of this section;

(4) to provide for the use of services, personnel, and facilities of Federal executive agencies and of State and local public agencies with their consent, with or without reimbursement therefor; and

(5) to prescribe such rules and regulations as he deems necessary to carry out the provisions of this section.

(c) EMPLOYMENT OF VOLUNTEERS.—

(1) IN GENERAL.—Service as a volunteer in any program carried out under this section shall not be considered service as an employee of the United States. Volunteers under such a program shall not be considered Federal employees and shall not be subject to the provisions of law relating to Federal employment, except that the provisions of section 1905 of title 18, United States Code, shall apply to volunteers as if they were employees of the United States.

(2) EXPENSES.—Amounts received by volunteers serving in any program carried out under this section as reimbursement for expenses are exempt from taxation under chapters 1 and 21 of the Internal Revenue Code of 1954.

(d) PUBLICITY RELATING TO INCOME TAX PROVISIONS PARTICULARLY IMPORTANT TO THE ELDERLY.—The Secretary shall, from time to time, undertake to direct the attention of elderly individuals to those provisions of the Internal Revenue Code of 1954 which are particularly important to taxpayers who are elderly individuals, such as the provisions of section 37 (relating to credit for the elderly) and section 121 (relating

to one-time exclusion of gain from sale of principal residence) of the Internal Revenue Code of 1954.

(e) DEFINITIONS.—For purposes of this section—

(1) The term "Secretary" means the Secretary of the Treasury or his delegate.

(2) The term "elderly individual" means an individual who has attained the age of 60 years as of the close of his taxable year.

(3) The term "Federal income tax return" means any return required under chapter 61 of the Internal Revenue Code of 1954 with respect to the tax imposed on an individual under chapter 1 of such Code.

(f) AUTHORIZATION OF APPROPRIATIONS.—There are authorized to be appropriated for the purpose of carrying out the provisions of this section $2,500,000 for the fiscal year ending September 30, 1979, and $3,500,000 for the fiscal year ending September 30, 1980.

SEC. 164. EXCLUSION OF VALUE OF CERTAIN EDUCATIONAL ASSISTANCE PROGRAMS.

(a) IN GENERAL.—Part III of subchapter B of chapter 1 (relating to items specifically excluded from gross income) is amended by redesignating section 127 as 128 and by inserting after section 126 the following new section:

"SEC. 127. EDUCATIONAL ASSISTANCE PROGRAMS.

"(a) GENERAL RULE.—Gross income of an employee does not include amounts paid or expenses incurred by the employer for educational assistance to the employee if the assistance is furnished pursuant to a program which is described in subsection (b).

"(b) EDUCATIONAL ASSISTANCE PROGRAM.—

"(1) IN GENERAL.—For purposes of this section an educational assistance program is a separate written plan of an employer for the exclusive benefit of his employees to provide such employees with educational assistance. The program must meet the requirements of paragraphs (2) through (6) of this subsection.

"(2) ELIGIBILITY.—The program shall benefit employees who qualify under a classification set up by the employer and found by the Secretary not be to discriminatory in favor of employees who are officers, owners, or highly compensated, or their dependents. For purposes of this paragraph, there shall be excluded from consideration employees not included in the program who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, if there is evidence that educational assistance benefits were the subject of good faith bargaining between such employee representatives and such employer or employers.

"(3) PRINCIPAL SHAREHOLDERS OR OWNERS.—Not more than 5 percent of the amounts paid or incurred by the employer for educational assistance during the year may be provided for the class of individuals who are shareholders or owners (or their spouses or dependents), each of whom (on any day of the year) owns more than 5 percent of the stock or of the capital or profits interest in the employer.

"(4) OTHER BENEFITS AS AN ALTERNATIVE.—A program must not provide eligible employees with a choice between educational

assistance and other remuneration includible in gross income. For purposes of this section, the business practices of the employer (as well as the written program) will be taken into account.

"(5) NO FUNDING REQUIRED.—A program referred to in paragraph (1) is not required to be funded.

"(6) NOTIFICATION OF EMPLOYEES.—Reasonable notification of the availability and terms of the program must be provided to eligible employees.

"(c) DEFINITIONS; SPECAL RULES.—For purposes of this section—

"(1) EDUCATIONAL ASSISTANCE.—The term 'educational assistance' means—

"(A) the payment, by an employer, of expenses incurred by or on behalf of an employee for education of the employee (including, but not limited to, tuition, fees, and similar payments, books, supplies, and equipment), and

"(B) the provision, by an employer, of courses of instruction for such employee (including books, supplies, and equipment), but does not include payment for, or the provision of, tools or supplies which may be retained by the employee after completion of a course of instruction, or meals, lodging, or transportation. The term 'educational assistance' also does not include any payment for, or the provision of any benefits with respect to, any course or other education involving svorts, games, or hobbies.

"(2) EMPLOYEE.—The term 'employee' includes, for any year, an individual who is an employee within the meaning of section 401(c)(1) (relating to self-employed individuals).

"(3) EMPLOYER.—An individual who owns the entire interest in an unincorporated trade or business shall be treated as his own employer. A partnership shall be treated as the employer of each partner who is an employee within the meaning of paragraph (2).

"(4) ATTRIBUTION RULES.—

"(A) OWNERSHIP OF STOCK.—Ownership of stock in a corporation shall be determined in accordance with the rules provided under subsections (d) and (e) of section 1563 (without regard to section 1563(e)(3)(C)).

"(B) INTEREST IN UNINCORPORATED TRADE OR BUSINESS.—The interest of an employee in a trade or business which is not incorporated shall be determined in accordance with regulations prescribed by the Secretary, which shall be based on principles similar to the principles which apply in the case of subparagraph (A).

"(5) CERTAIN TESTS NOT APPLICABLE.—An educational assistance program shall not be held or considered to fail to meet any requirements of subsection (b) merely because—

"(A) of utilization rates for the different types of educational assistance made available under the program; or

"(B) successful completion, or attaining a particular course grade is required for or considered in determining reimbursement under the program.

"(6) RELATIONSHIP TO CURRENT LAW.—This section shall not be construed to affect the deduction or inclusion in income of amounts (not within the exclusion under this section) which are paid or in-

curred, or received as reimbursement, for educational expenses under section 117, 162 or 212.

"(7) DISALLOWANCE OF EXCLUDED AMOUNTS AS CREDIT OR DEDUCTION.—No deduction or credit shall be allowed under any other section of this chapter for any amount excluded from income by reason of this section.

"(d) TERMINATION.—This section shall not apply to taxable years beginning after December 31, 1983."

(b) TREATMENT OF EMPLOYER EDUCATIONAL ASSISTANCE BENEFITS FOR PURPOSES OF WITHHOLDING, UNEMPLOYMENT TAXES, AND SOCIAL SECURITY TAXES.—

(1) Section 3401(a) (relating to the definition of wages for purposes of collection of income tax at the source) is amended—

(A) by striking out "or" at the end of paragraph (16);

(B) by striking out the period at the end of paragraph (17); and

(C) by adding at the end thereof the following new paragraph:

"(18) for any payment made, or benefit furnished, to or for the benefit of an employee if at the time of such payment or such furnishing it is reasonable to believe that the employee will be able to exclude such payment or benefit from income under section 127.".

(2) Section 3306(b) (relating to the definition of wages for purposes of the Federal Unemployment Tax Act) is amended—

(A) by striking out "or" at the end of paragraph (11);

(B) by striking out the period at the end of paragraph (12) and inserting in lieu thereof "; or"; and

(C) by adding at the end thereof the following new paragraph:

"(13) any payment made, or benefit furnished, to or for the benefit of an employee if at the time of such payment or such furnishing it is reasonable to believe that the employee will be able to exclude such payment or benefit from income under section 127.".

(3) Section 3121(a) (relating to the definition of wages for purposes of the Federal Insurance Contributions Act) is amended—

(A) by striking out "or" at the end of paragraph (16);

(B) by striking out the period at the end of subparagraph (17) and inserting in lieu thereof; "or"; and

(C) by adding at the end thereof the following new paragraph:

"(18) any payment made, or benefit furnished, to or for the benefit of an employee if at the time of such payment or such furnishing it is reasonable to believe that the employee will be able to exclude such payment or benefit from income under section 127.".

(4) Section 209 of the Social Security Act is amended—

(A) by striking out "or" at the end of subsection (o);

(B) by striking out the period at the end of subsection (p) and inserting in lieu thereof "; or"; and

(C) by inserting after subsection (p) and before the sentence beginning with "For purposes of this title, in the case of domestic service" the following new subsection:

"(q) Any payment made, or benefit furnished, to or for the benefit of an employee at the time of such payment or such furnishing it is reasonable to believe that the employee will be able to exclude such payment or benefit from income under section 127 of the Internal Revenue Code of 1954.".

(c) CLERICAL AMENDMENT.—The table of sections for such part is amended by striking out the item relating to section 124 and inserting in lieu thereof the following:

"Sec. 124. Educational assistance programs.
"Sec. 125. Cross references to other Acts.".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years beginning after December 31, 1978.

TITLE II—TAX SHELTER PROVISIONS

Subtitle A—Provisions Related To At Risk Rules

SEC. 201. EXTENSION OF SECTION 465 AT RISK RULES TO ALL ACTIVITIES OTHER THAN REAL ESTATE.

(a) EXTENSION.—Subsection (c) of section 465 (relating to activities to which section applies) is amended by adding at the end thereof the following new paragraph:

"(3) EXTENSION TO OTHER ACTIVITIES.—

"(A) IN GENERAL.—In the case of taxable years beginning after December 31, 1978, this section also applies to each activity—

"(i) engaged in by the taxpayer in carrying on a trade or business or for the production of income, and

"(ii) which is not described in paragraph (1).

"(B) AGGREGATION OF ACTIVITIES WHERE TAXPAYER ACTIVELY PARTICIPATES IN MANAGEMENT OF TRADE OR BUSINESS.—Except as provided in subparagraph (C), for purposes of this section, activities described in subparagraph (A) which constitute a trade or business shall be treated as 1 activity if—

"(i) the taxpayer actively participates in the management of such trade or business, or

"(ii) such trade or business is carried on by a partnership or electing small business corporation (as defined in section 1371(b)) and 65 percent or more of the losses for the taxable year is allocable to persons who actively participate in the management of the trade or business.

"(C) AGGREGATION OR SEPARATION OF ACTIVITIES UNDER REGULATIONS.—The Secretary shall prescribe regulations under which activities described in subparagraph (A) shall be aggregated or treated as separate activities.

"(D) EXCLUSIONS.—

"(i) REAL PROPERTY.—In the case of activities described in subparagraph (A), the holding of real property (other than mineral property) shall be treated as a separate activity, and subsection (a) shall not apply to losses from such activity. For purposes of the preceding sentence, personal property and services which are incidental to making real property available as living accommodations shall be treated as part of the activity of holding such real property.

"(ii) EQUIPMENT LEASING BY CLOSELY-HELD CORPORATIONS.—

"(I) *In the case of a corporation described in subsection (a)(1)(C) actively engaged in leasing equipment which is section 1245 property, the activity of leasing such equipment shall be treated, for purposes of subsection (a), as a separate activity and subsection (a) shall not apply to losses from such activity.*

"(II) *A corporation described in subsection (a)(1)(C) shall not be considered to be actively engaged in leasing such equipment unless 50 percent or more of the gross receipts of the corporation for the taxable year are attributable, under regulations prescribed by the Secretary, to leasing and selling such equipment.*

"(III) *For purposes of this paragraph, the leasing of master sound recordings, and other similar contractual arrangements with respect to tangible or intangible assets associated with literary, artistic, or musical properties shall not be treated as leasing equipment which is section 1245 property.*

"(IV) *In the case of a controlled group of corporations (within the meaning of section 1563(a)), this paragraph shall be applied by treating the controlled group as a single corporation.*

"(E) APPLICATION OF SUBSECTION (b)(3).—*In the case of an activity described in subparagraph (A), subsection (b)(3) shall apply only to the extent provided in regulations prescribed by the Secretary.*"

(b) REPEAL OF SECTION 704(d) AT RISK RULES.—

(1) IN GENERAL.—*Subsection (d) of section 704 is amended by striking out the last 2 sentences.*

(2) TRANSITIONAL RULE.—*In the case of a loss which was not allowed for any taxable year by reason of the last 2 sentences of section 704(d) of the Internal Revenue Code of 1954 (as in effect before the date of the enactment of this Act), such loss shall be treated as a deduction (subject to section 465(a) of such Code) for the first taxable year beginning after December 31, 1978. Section 465(a) of such Code (as amended by this section) shall not apply with respect to partnership liabilities to which the last 2 sentences of section 704(d) of such Code (as in effect on the day before the date of enactment of this Act) did not apply because of the provisions of section 213(f)(2) of the Tax Reform Act of 1976.*

(c) CLERICAL AMENDMENTS.—

(1) *The heading of section 465 is amended to read as follows:*

"SEC. 465. DEDUCTIONS LIMITED TO AMOUNT AT RISK."

(2) *The table of sections for subpart C of part II of subchapter E of chapter 1 is amended by striking out "in case of certain activities" in the item relating to section 465.*

SEC. 202. EXTENSION OF AT RISK PROVISIONS TO CLOSELY HELD CORPORATIONS.

Subsection (a) of section 465 (relating to deductions limited to amount at risk) is amended to read as follows:

"(a) LIMITATION TO AMOUNT AT RISK.—

"(1) IN GENERAL.—In the case of—

"(A) an individual,

"(B) an electing small business corporation (as defined in section 1371(b)), and

"(C) a corporation with respect to which the stock ownership requirement of paragraph (2) of section 542(a) (determined by reference to the rules contained in section 318 rather than under section 544) is met,

engaged in an activity to which this section applies, any loss from such activity for the taxable year shall be allowed only to the extent of the aggregate amount with respect to which the taxpayer is at risk (within the meaning of subsection (b)) for such activity at the close of the taxable year.

"(2) DEDUCTION IN SUCCEEDING YEAR.—Any loss from an activity to which this section applies not allowed under this section for the taxable year shall be treated as a deduction allocable to such activity in the first succeeding taxable year."

SEC. 203. RECAPTURE OF LOSSES WHERE AMOUNT AT RISK IS LESS THAN ZERO.

Section 465 (relating to deductions limited to amount at risk) is amended by adding at the end thereof the following new subsection:

"(e) RECAPTURE OF LOSSES WHERE AMOUNT AT RISK IS LESS THAN ZERO.—

"(1) IN GENERAL.—If zero exceeds the amount for which the taxpayer is at risk in any activity at the close of any taxable year—

"(A) the taxpayer shall include in his gross income for such taxable year (as income from such activity) an amount equal to such excess, and

"(B) an amount equal to the amount so included in gross income shall be treated as a deduction allocable to such activity for the first succeeding taxable year.

"(2) LIMITATION.—The excess referred to in paragraph (1) shall not exceed—

"(A) the aggregate amount of the reductions required by subsection (b)(5) with respect to the activity for all prior taxable years beginning after December 31, 1978, reduced by

"(B) the amounts previously included in gross income with respect to such activity under this subsection."

SEC. 204. EFFECTIVE DATES.

(a) IN GENERAL.—The amendments made by this subtitle shall apply to taxable years beginning after December 31, 1978.

(b) TRANSITIONAL RULES.—

(1) RECAPTURE PROVISIONS.—If the amount for which the taxpayer is at risk in any activity as of the close of the taxpayer's last taxable year beginning before January 1, 1979, is less than zero, section 465(e)(1) of the Internal Revenue Code of 1954 (as added by section 203 of this Act) shall be applied with respect to such activity of the taxpayer by substituting such negative amount for zero.

(2) SPECIAL TRANSITIONAL RULES FOR LEASING ACTIVITIES.—

(A) RULE FOR LEASES.—In the case of any activity described in section 465(c)(1)(C) of such Code in which a corporation

described in section 465(a)(1)(C) of such Code is engaged, the amendments made by this section shall not apply with respect to—

(i) leases entered into before November 1, 1978, and

(ii) leases where the property was ordered by the lessor or lessee before November 1, 1978.

(B) HOLDING OF INTERESTS FOR PURPOSES OF SUBPARAGRAPH (A).—Subparagraph (A) shall apply only to taxpayers who held their interests in the property on October 31, 1978.

Subtitle B—Partnership Provisions

SEC. 211. PENALTY FOR FAILURE TO FILE PARTNERSHIP RETURN.

(a) GENERAL RULE.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding at the end thereof the following new section:

"SEC. 6698. FAILURE TO FILE PARTNERSHIP RETURN.

"(a) GENERAL RULE.—In addition to the penalty imposed by section 7203 (relating to willful failure to file return, supply information, or pay tax), if any partnership required to file a return under section 6031 for any taxable year—

"(1) fails to file such return at the time prescribed therefor (determined with regard to any extension of time for filing), or

"(2) files a return which fails to show the information required under section 6031,

such partnership shall be liable for a penalty determined under subsection (b) for each month (or fraction thereof) during which such failure continues (but not to exceed 5 months), unless it is shown that such failure is due to reasonable cause.

"(b) AMOUNT PER MONTH.—For purposes of subsection (a), the amount determined under this subsection for any month is the product of—

"(1) $50, multiplied by

"(2) the number of persons who were partners in the partnership during any part of the taxable year.

"(c) ASSESSMENT OF PENALTY.—The penalty imposed by subsection (a) shall be assessed against the partnership.

"(d) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a)."

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 68 is amended by adding at the end thereof the following new item:

"Sec. 6698. Failure to file partnership return."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to returns for taxable years beginning after December 31, 1978.

SEC. 212. EXTENSION OF STATUTE OF LIMITATIONS IN THE CASE OF PARTNERSHIP ITEMS.

(a) ASSESSMENT OF DEFICIENCIES.—Section 6501 (relating to limitations on assessment and collection) is amended by adding at the end thereof the following new subsection:

"(q) SPECIAL RULES FOR PARTNERSHIP ITEMS OF FEDERALLY REGISTERED PARTNERSHIPS.—

"(1) IN GENERAL.—In the case of any tax imposed by subtitle A with respect to any person, the period for assessing a deficiency attributable to any partnership item of a federally registered partnership shall not expire before the later of—

"(A) the date which is 4 years after the date on which the partnership return of the federally registered partnership for the partnership taxable year in which the item arose was filed (or, later, if the date prescribed for filing the return), or

"(B) if the name or address of such person does not appear on the partnership return, the date which is 1 year after the date on which such information is furnished to the Secretary in such manner and at such place as he may prescribe by regulations.

"(2) PARTNERSHIP ITEM DEFINED.—For purposes of this subsection, the term 'partnership item' means—

"(A) any item required to be taken into account for the partnership taxable year under any provision of subchapter K of chapter 1 to the extent that regulations prescribed by the Secretary provide that for purposes of this subtitle such item is more appropriately determined at the partnership level than at the partner level, and

"(B) any other item to the extent affected by an item described in subparagraph (A).

"(3) EXTENSION BY AGREEMENT.—The extensions referred to in subsection (c)(4), insofar as they relate to partnership items, may, with respect to any person, be consented to—

"(A) except to the extent the Secretary is otherwise notified by the partnership, by a general partner of the partnership, or

"(B) by any person authorized to do so by the partnership in writing.

"(4) FEDERALLY REGISTERED PARTNERSHIP.—For purposes of this subsection, the term 'federally registered partnership' means, with respect to any partnership taxable year, any partnership—

"(A) interests in which have been offered for sale at any time during such taxable year or a prior taxable year in any offering required to be registered with the Securities and Exchange Commission, or

"(B) which, at any time during such taxable year or a prior taxable year, was subject to the annual reporting requirements of the Securities and Exchange Commission which relate to the protection of investors in the partnership."

(b) CREDITS AND REFUNDS.—

(1) IN GENERAL.—Section 6511 (relating to limitations on credit or refund) is amended by redesignating subsection (g) as subsection (h) and by inserting after subsection (f) the following new subsection:

"(g) SPECIAL RULE FOR PARTNERSHIP ITEMS OF FEDERALLY REGISTERED PARTNERSHIPS.—

"(1) IN GENERAL.—In the case of any tax imposed by subtitle A with respect to any person, the period for filing a claim for credit or refund of any overpayment attributable to any partnership item of a federally registered partnership shall not expire before the later of—

"(A) the date which is 4 years after the date prescribed by law (including extensions thereof) for filing the partnership return for the partnership taxable year in which the item arose, or

"(B) if an agreement under the provisions of section 6501 (c)(4) extending the period for the assessment of any deficiency attributable to such partnership item is made before the date specified in subparagraph (A), the date 6 months after the expiration of such extension.

In any case to which the preceding sentence applies, the amount of the credit or refund may exceed the portion of the tax paid within the period provided in subsection (b)(2) or (c), whichever is applicable.

"(2) DEFINITIONS.—For purposes of this subsection, the terms 'partnership item' and 'federally registered partnership' have the same meanings as such terms have when used in section 6501(q)."

(2) TECHNICAL AMENDMENT.—Paragraph (2) of section 6512(b) (relating to overpayment determined by Tax Court) is amended by striking out "(c), or (d)" each place it appears and inserting in lieu thereof "(c), (d), or (g)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to partnership items arising in partnership taxable years beginning after December 31, 1978.

TITLE III—PROVISIONS PRIMARILY AFFECTING BUSINESS INCOME TAX

Subtitle A—Corporate Rate Reductions

SEC. 301. CORPORATE RATE REDUCTIONS.

(a) IN GENERAL.—Section 11 (relating to the tax imposed on corporations) is amended to read as follows:

"SEC. 11. TAX IMPOSED.

"(a) CORPORATIONS IN GENERAL.—A tax is hereby imposed for each taxable year on the taxable income of every corporation.

"(b) AMOUNT OF TAX.—The amount of the tax imposed by subsection (a) shall be the sum of—

"(1) 17 percent of so much of the taxable income as does not exceed $25,000;

"(2) 20 percent of so much of the taxable income as exceeds $25,000 but does not exceed $50,000;

"(3) 30 percent of so much of the taxable income as exceeds $50,000 but does not exceed $75,000;

"(4) 40 percent of so much of the taxable income as exceeds $75,000 but does not exceed $100,000; plus

"(5) 46 percent of so much of the taxable income as exceeds $100,000.

"(c) EXCEPTIONS.—Subsection (a) shall not apply to a corporation subject to a tax imposed by—

"(1) section 594 (relating to mutual savings banks conducting life insurance business),

"(2) subchapter L (sec. 801 and following, relating to insurance companies), or

"(3) subchapter M (sec. 851 and following, relating to regulated investment companies and real estate investment trusts).

"(d) FOREIGN CORPORATIONS.—In the case of a foreign corporation, the tax imposed by subsection (a) shall apply only as provided by section 882."

(b) CONFORMING AMENDMENTS.

(1) CROSS REFERENCES RELATING TO CORPORATIONS.—Paragraph (7) of section 12 (relating to cross references relating to tax on corporations) is amended to read as follows:

"(7) For limitation on benefits of graduated rate schedule provided in section 11(b), see section 1551."

(2) MINIMUM TAX.—Subparagraph (B) of section 57(a)(9) (relating to capital gains preference for corporations) is amended by striking out "the sum of the normal tax rate and the surtax rate under section 11" each place it appears and inserting in lieu thereof "the highest rate of tax specified in section 11(b)".

(3) DIVIDENDS RECEIVED ON CERTAIN PREFERRED STOCK.—Subparagraph (B) of section 244(a)(2) (relating to dividends received on certain preferred stock) is amended by striking out "the sum of the normal tax rate and the surtax rate for the taxable year prescribed by section 11" and inserting in lieu thereof "the highest rate of tax specified in section 11(b)".

(4) DIVIDENDS PAID ON CERTAIN PREFERRED STOCK OF PUBLIC UTILITIES.—Subparagraph (B) of section 247(a)(2) (relating to dividends paid on certain preferred stock of public utilities) is amended by striking out "the sum of the normal tax rate and the surtax rate for the taxable year specified in section 11" and inserting in lieu thereof "the highest rate of tax specified in section 11(b)".

(5) TAX ON UNRELATED BUSINESS INCOME OF CHARITABLE, ETC., ORGANIZATIONS.—

(A) IMPOSITION OF TAX.—Paragraph (1) of section 511(a) (relating to charitable, etc., organizations taxable at corporation rates) is amended by striking out "a normal tax and a surtax" and inserting in lieu thereof "a tax".

(B) ORGANIZATIONS SUBJECT TO TAX.—Paragraph (2) of section 511(a) is amended by striking out "taxes" each place it appears and inserting in lieu thereof "tax".

(6) POLITICAL ORGANIZATIONS.—Paragraph (1) of section 527(b) (relating to tax imposed) is amended to read as follows:

"(1) IN GENERAL.—A tax is hereby imposed for each taxable year on the political organization taxable income of every political organization. Such tax shall be computed by multiplying the political organization taxable income by the highest rate of tax specified in section 11(b)."

(7) HOMEOWNERS ASSOCIATIONS.—Paragraph (1) of section 528(b) (relating to tax imposed) is amended to read as follows:

"(1) IN GENERAL.—A tax is hereby imposed for each taxable year on the homeowners association taxable income of every homeowners association. Such tax shall be computed by multiplying the homeowners association taxable income by the highest rate of tax specified in section 11 (b)."

(8) LIFE INSURANCE COMPANIES.—Paragraph (1) of section 802(a) (relating to tax imposed) is amended by striking out "a normal tax and surtax" and inserting in lieu thereof "a tax".

(9) MUTUAL INSURANCE COMPANIES.—

(A) IN GENERAL.—Subsection (a) of section 821 (relating to tax on mutual insurance companies to which part II applies) is amended to read as follows:

"(a) IMPOSITION OF TAX.—

"(1) IN GENERAL.—A tax is hereby imposed for each taxable year on the mutual insurance company taxable income of every mutual insurance company (other than a life insurance company and other than a fire, flood, or marine insurance company subject to the tax imposed by section 831). Such tax shall be computed by multiplying the mutual insurance company taxable income by the rates provided in section 11(b).

"(2) CAP ON TAX WHERE INCOME IS LESS THAN $12,000.—The tax imposed by paragraph (1) shall not exceed 34 percent of the amount by which the mutual insurance company taxable income exceeds $6,000."

(B) SMALL COMPANIES.—Paragraph (1) of section 821(c) (relating to alternative tax for certain small companies) is amended to read as follows:

"(1) IMPOSITION OF TAX.—

"(A) IN GENERAL.—There is hereby imposed for each taxable year on the income of every mutual insurance company to which this subsection applies a tax (which shall be in lieu of the tax imposed by subsection (a)). Such tax shall be computed by multiplying the taxable investment income by the rates provided in section 11(b).

"(B) CAP WHERE INCOME IS LESS THAN $6,000.—The tax imposed by subparagraph (A) shall not exceed 34 percent of the amount by which the taxable investment income exceeds $3,000."

(10) ELECTION BY MUTUAL INSURANCE COMPANY WHICH IS A RECIPROCAL.—Paragraph (1) of section 826(c) (relating to exception) is amended to read as follows:

"(1) is subject to the tax imposed by section 11;".

(11) REGULATED INVESTMENT COMPANIES.—Paragraph (1) of section 852(b) (relating to method of taxation of companies and shareholders) is amended to read as follows:

"(1) IMPOSITION OF TAX ON REGULATED INVESTMENT COMPANIES.—There is hereby imposed for each taxable year upon the investment company taxable income of every regulated investment company a tax computed as provided in section 11, as though the investment company taxable income were the taxable income referred to in section 11."

(12) REAL ESTATE INVESTMENT TRUSTS.—Paragraph (1) of section 857(b) (relating to imposition of normal tax and surtax on real estate invetment trusts) is amended to read as follows:

"(1) IMPOSITION OF TAX ON REAL ESTATE INVESTMENT TRUSTS.—There is hereby imposed for each taxable year on the real estate investment trust taxable income of every real estate investment trust a tax computed as provided in section, 11, as though the real estate investment trust taxable income were the taxable income referred to in section 11."

(13) TAX ON INCOME OF FOREIGN CORPORATIONS CONNECTED WITH UNITED STATES BUSINESS.—The heading of subsection (a) of section 882 (relating to tax on income of foreign corporations connected with United States business) and the heading of paragraph (1) of such subsection are amended to read as follows:

"(a) IMPOSITION OF TAX.—

"(1) IN GENERAL.—".

(14) FOREIGN TAX CREDIT.—Paragraph (2) of section 907(a) (relating to reduction in amount allowed as foreign tax under section 901) is amended to read as follows:

"(2) the percentage which is equal to the highest rate of tax specified in section 11(b)."

(15) SPECIAL DEDUCTION FOR WESTERN HEMISPHERE TRADE CORPORATION.—Subparagraph (B) of section 922(a)(2) (relating to general rule) is amended by striking out "the sum of the normal tax rate and the surtax rate for the taxable year prescribed by section 11" and inserting in lieu thereof "the highest rate of tax specified in section 11(b)."

(16) ELECTION BY INDIVIDUALS TO BE SUBJECT TO TAX AT CORPORATE RATES.—Subsection (c) of section 962 (relating to surtax exemption with respect to individuals subject to tax at corporate rates) is amended to read as follows:

"(c) PRO RATION OF EACH SECTION 11 BRACKET AMOUNT.—For purposes of applying subsection (a)(1), the amount in each taxable income bracket in the tax table in section 11(b) shall not exceed an amount which bears the same ratio to such bracket amount as the amount included in the gross income of the United States shareholder under section 951(a) for the taxable year bears to such shareholder's pro rata share of the earnings and profits for the taxable year of all controlled foreign corporations with respect to which such shareholder includes any amount in gross income under section 951(a)."

(17) TREATMENT OF RECOVERIES OF FOREIGN EXPROPRIATION LOSSES.—Paragraph (4) of section 1351(d) (relating to adjustment for prior tax benefits) is amended to read as follows:

"(4) SUBSTITUTION OF CURRENT TAX RATE.—For purposes of this subsection, the rates of tax specified in section 11(b) for the taxable year of the recovery shall be treated as having been in effect for all prior taxable years."

(18) AMENDMENTS OF SECTION 1551.—

(A) Subsection (a) of section 1551 (relating to disallowance of surtax exemption and accumulated earnings credit) is amended—

(i) by striking out "disallow the surtax exemption (as defined in section 11(d))" and inserting in lieu thereof

"disallow the benefits of the rates contained in section 11 (b) which are lower than the highest rate specified in such section", and

(ii) by striking out "such exemption or" and inserting in lieu thereof "such benefits or".

(B) The section heading of section 1551 is amended to read as follows:

"SEC. 1551. DISALLOWANCE OF THE BENEFITS OF THE GRADUATED CORPORATE RATES AND ACCUMULATED EARNINGS CREDIT."

(C) The table of sections for part I of subchapter B of chapter 6 is amended by striking out the item relating to section 1551 and inserting in lieu thereof the following new item:

"Sec. 1551. Disallowance of the benefits of the graduated corporate rates and accumulated earnings credit."

(19) LIMITATIONS ON CERTAIN MULTIPLE TAX BENEFITS IN THE CASE OF CERTAIN CONTROLLED CORPORATIONS.—

(A) IN GENERAL.—Subsection (a) of section 1561 (relating to limitations on certain multiple tax benefits in the case of certain controlled corporations) is amended—

(i) by striking out paragraph (1) and inserting in lieu thereof the following:

"(1) amounts in each taxable income bracket in the tax table in section 11(b) which do not aggregate more than the maximum amount in such bracket to which a corporation which is not a component member of a controlled group is entitled,",

(ii) by striking out "amount" each place it appears in the second sentence and inserting in lieu thereof "amounts", and

(iii) by striking out the last sentence.

(B) CERTAIN SHORT TAXABLE YEARS.—Paragraph (1) of section 1561(b) (relating to certain short taxable years) is amended to read as follows:

"(1) the amount in each taxable income bracket in the tax table in section 11(b),",

(20) REPEAL OF CERTAIN OBSOLETE PROVISIONS.—

(A) Subsection (c) of section 6154 (defining estimated tax) is amended to read as follows:

"(c) ESTIMATED TAX DEFINED.—For purposes of this title, in the case of a corporation the term 'estimated tax' means the excess of—

"(1) the amount which the corporation estimates as the amount of the income tax imposed by section 11 or 1201(a), or subchapter L of chapter 1, whichever is applicable, over

"(2) the amount which the corporation estimates as the sum of the credits against tax provided by part IV of subchapter A of chapter 1."

(B) Subsection (e) of section 6655 (defining tax) is amended to read as follows:

"(e) DEFINITION OF TAX.—For purposes of subsections (b) and (d), the term 'tax' means the excess of—

"(1) the tax imposed by section 11 or 1201(a), or subchapter L of chapter 1, whichever is applicable, over

"(2) the credits against tax provided by part IV of subchapter A of chapter 1."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1978.

Subtitle B—Credits

SEC. 311. 10-PERCENT INVESTMENT TAX CREDIT AND $100,000 LIMITATION ON USED PROPERTY MADE PERMANENT.

(a) 10-PERCENT INVESTMENT CREDIT.—Subparagraph (B) of section 46(a)(2) (defining regular percentage) is amended to read as follows:

"(B) REGULAR PERCENTAGE.—For purposes of this paragraph, the regular percentage is 10 percent."

(b) $100,000 LIMITATION ON USED PROPERTY.—Paragraph (2) of section 301(c) of the Tax Reduction Act of 1975 (relating to effective date or increase of dollar limitation on used property) is amended by striking out ", and before January 1, 1981".

(c) TECHNICAL AMENDMENTS.—

(1) Subparagraph (A) of section 46(c)(3) (relating to public utility property) is amended by striking out "For the period beginning on January 1, 1981" and inserting in lieu thereof "To the extent that the credit allowed by section 38 with respect to any public utility property is determined at the rate of 7 percent".

(2) The first sentence of section 46(f)(8) (relating to prohibition of immediate flow through) is amended by striking out "and the Energy Tax Act of 1978" and inserting in lieu thereof "the Energy Tax Act of 1978, and the Revenue Act of 1978".

SEC. 312. INCREASE IN LIMITATION ON INVESTMENT CREDIT TO 90 PERCENT OF TAX LIABILITY.

(a) INCREASE IN GENERAL LIMITATION.—Paragraph (3) of section 46(a) (relating to amount of credit) is amended to read as follows:

"(3) LIMITATION BASED ON AMOUNT OF TAX.—Notwithstanding paragraph (1), the credit allowed by section 38 for the taxable year shall not exceed—

"(A) so much of the liability for tax for the taxable year as does not exceed $25,000, plus

"(B) the following percentage of so much of the liability for tax for the taxable year as exceeds $25,000:

"If the taxable year ends in:	The percentage is:
1979	60
1980	70
1981	80
1982 or thereafter	90."

(b) SPECIAL RULES FOR CERTAIN UTILITIES, RAILROADS, AND AIRLINES.—

(1) UTILITIES.—Paragraph (7) of section 46(a) (relating to alternative limitation in the case of certain utilities) is amended to read as follows:

"(7) ALTERNATIVE LIMITATION IN THE CASE OF CERTAIN UTILITIES.—

"(A) IN GENERAL.—If, for the taxable year ending in 1979—

"(i) the amount of the qualified investment of the taxpayer which is attributable to public utility property is 25 percent or more of his aggregate qualified investment, and

"(ii) the application of this paragraph results in a percentage higher than 60 percent,

then subparagraph (B) of paragraph (3) of this subsection shall be applied by substituting for '60 percent' the taxpayer's applicable percentage for such year.

"(B) APPLICABLE PERCENTAGE.—The applicable percentage for any taxpayer for any taxable year ending in 1979 is—

"(i) 50 percent, plus

"(ii) that portion of 20 percent which the taxpayer's amount of qualified investment which is public utility property bears to his aggregate qualified investment.

If the proportion referred to in clause (ii) is 75 percent or more, the applicable percentage of the taxpayer for the year shall be 70 percent.

"(C) PUBLIC UTILITY PROPERTY DEFINED.—For purposes of this paragraph, the term 'public utility property' has the meaning given to such term by the first sentence of subsection (c)(3)(B)."

(2) ALTERNATIVE LIMITATION IN THE CASE OF CERTAIN RAILROADS AND AIRLINES.—Subsection (a) of section 46 is amended by striking out paragraphs (8) and (9) and by inserting in lieu thereof the following new paragraph:

"(8) ALTERNATIVE LIMITATION IN THE CASE OF CERTAIN RAILROADS AND AIRLINES.—

"(A) IN GENERAL.—If, for a taxable year ending in 1979 or 1980—

"(i) the amount of the qualified investment of the taxpayer which is attributable to railroad property or to airline property, as the case may be, is 25 percent or more of his aggregate qualified investment, and

"(ii) the application of this paragraph results in a percentage higher than 60 percent (70 percent in the case of a taxable year ending in 1980),

then subparagraph (B) of paragraph (3) of this subsection shall be applied by substituting for '60 percent' ('70 percent' in the case of a taxable year ending in 1980) the taxpayer's applicable percentage for such year.

"(B) APPLICABLE PERCENTAGE.—The applicable percentage of any taxpayer for any taxable year under this paragraph is—

"(i) 50 percent, plus

"(ii) that portion of the tenative percentage for the taxable year which the taxpayer's amount of qualified investment which is railroad property or airline property (as the case may be) bears to his aggregate qualified investment.

If the proportion referred to in clause (ii) is 75 percent or more, the applicable percentage of the taxpayer for the taxable

year shall be 90 percent (80 percent in the case of a taxable year ending in 1980).

"(C) TENTATIVE PERCENTAGE.—For purposes of subparagraph (B), the tentative percentage shall be determined under the following table:

"If the taxable year ends in:	*The tentative percentage is:*
1979	*40*
1980	*30*

"(D) RAILROAD PROPERTY DEFINED.—For purposes of this paragraph, the term 'railroad property' means section 38 property used by the taxpayer directly in connection with the trade or business carried on by the taxpayer of operating a railroad (including a railroad switching or terminal company).

"(E) AIRLINE PROPERTY DEFINED.—For purposes of this paragraph, the term 'airline property' means section 38 property used by the taxpayer directly in connection with the trade or business carried on by the taxpayer of the furnishing or sale of transportation as a common carrier by air subject to the jurisdiction of the Civil Aeronautics Board or the Federal Aviation Administration."

(c) REPEAL OF CERTAIN OBSOLETE PROVISIONS.—

(1) Subsections (h), (i), and (j) of section 48 and sections 49 and 50 are hereby repealed.

(2) Paragraphs (1) and (2) of section 46(f) and subparagraph (B) of section 48(a)(7) are each amended by striking out "described in section 50".

(3) Subparagraph (A) of section 48(a)(7) is amended by striking out "(other than pre-termination property)".

(4) Subsection (i) of section 167 is hereby repealed.

(5) The table of sections for subpart B of part IV of subchapter A of chapter 1 is amended by striking out the items relating to sections 49 and 50.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years ending after December 31, 1978.

SEC. 313. INVESTMENT CREDIT FOR POLLUTION CONTROL FACILITIES.

(a) IN GENERAL.—Paragraph (5) of section 46(c) (relating to applicable percentage in the case of certain pollution control facilities) is amended to read as follows:

"(5) APPLICABLE PERCENTAGE IN THE CASE OF CERTAIN POLLUTION CONTROL FACILITIES.—

"(A) IN GENERAL.—Notwithstanding paragraph (2), in the case of property—

"(i) with respect to which an election under section 169 applies, and

"(ii) the useful life of which (determined without regard to section 169) is not less than 5 years,

100 percent shall be the applicable percentage for purposes of applying paragraph (1) with respect to so much of the adjusted basis of the property as (after the application of section 169(f)) constitutes the amortizable basis for purposes of section 169.

"(B) SPECIAL RULE WHERE PROPERTY IS FINANCED BY INDUSTRIAL DEVELOPMENT BONDS.—To the extent that any

property is financed by the proceeds of an industrial development bond (within the meaning of section 103(b)(2)) the interest on which is exempt from tax under section 103, subparagraph (A) shall be applied by substituting '50 percent' for '100 percent'."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to—

(1) property acquired by the taxpayer after December 31, 1978, and

(2) property the construction, reconstruction, or erection of which was completed by the taxpayer after December 31, 1978 (but only to the extent of the basis thereof attributable to construction, reconstruction, or erection after such date).

SEC. 314. INVESTMENT CREDIT FOR CERTAIN SINGLE PURPOSE AGRICULTURAL OR HORTICULTURAL STRUCTURES.

(a) GENERAL RULE.—Paragraph (1) of section 48(a) (defining section 38 property) is amended by striking out the period at the end of subparagraph (C) and inserting in lieu thereof ", or" and by inserting after subparagraph (C) the following new subparagraph:

"(D) single purpose agricultural or horticultural structures."

(b) DEFINITION OF SINGLE PURPOSE AGRICULTURAL OR HORTICULTURAL STRUCTURES.—Section 48 is amended by redesignating subsection (p) as subsection (q) and by inserting after subsection (o) the following new subsection:

"(p) SINGLE PURPOSE AGRICULTURAL OR HORTICULTURAL STRUCTURE DEFINED.—For purposes of this section—

"(1) IN GENERAL.—The term 'single purpose agricultural or horticultural structure' means—

"(A) a single purpose livestock structure, and

"(B) a single purpose horticultural structure.

"(2) SINGLE PURPOSE LIVESTOCK STRUCTURE.—The term 'single purpose livestock structure' means any enclosure or structure specifically designed, constructed, and used—

"(A) for housing, raising, and feeding a particular type of livestock and their produce, and

"(B) for housing the equipment (including any replacements) necessary for the housing, raising, and feeding referred to in subparagraph (A).

"(3) SINGLE PURPOSE HORTICULTURAL STRUCTURE.—The term 'single purpose horticultural structure' means—

"(A) a greenhouse specifically designed, constructed, and used for the commercial production of plants, and

"(B) a structure specifically designed constructed and used for the commercial production of mushrooms.

"(4) STRUCTURES WHICH INCLUDE WORK SPACE.—An enclosure or structure which provides work space shall be treated as a single purpose agricultural or horticultural structure only if such work space is solely for—

"(A) the stocking, caring for, or collecting of livestock or plants (as the case may be) or their produce,

"(B) the maintenance of the enclosure or structure, and

"(C) the maintenance or replacement of the equipment or stock enclosed or housed therein.

"(5) SPECIAL RULE FOR APPLYING SECTION 47.—For purposes of section 47, any single purpose agricultural or horticultural structure shall be treated as meeting the requirements of this subsection for any period during which such structure is held for the use under which it qualified inder this subsection.

"(6) LIVESTOCK.—The term 'livestock' includes poultry."

(c) EFFECTIVE DATE.—The amendments made by subsections (a) and (b) shall apply to taxable years ending after August 15, 1971.

SEC. 315. INVESTMENT CREDIT ALLOWED FOR CERTAIN REHABILITATED BUILDINGS.

(a) IN GENERAL.—Paragraph (1) of section 48(a) (defining section 38 property) is amended by striking out the period at the end of subparagraph (D) and by inserting in lieu thereof "; or" and the following new subparagraph:

"(E) in the case of a qualified rehabilitated building, that portion of the basis which is attributable to qualified rehabilitation expenditures (within the meaning of subsection (g))."

(b) QUALIFIED REHABILITATED BUILDINGS DEFINED.—Section 48 is amended by inserting after subsection (f) the following new subsection:

"(g) SPECIAL RULES FOR QUALIFIED REHABILITATED BUILDINGS.—For purposes of this subpart—

"(1) QUALIFIED REHABILITATED BUILDING DEFINED.—

"(A) IN GENERAL.—The term 'qualified rehabilitated building' means any building (and its structural components)—

"(i) which has been rehabilitated,

"(ii) which was placed in service before the beginning of the rehabilitation, and

"(iii) 75 percent or more of the existing external walls of which are retained in place as external walls in the rehabilitation process.

"(B) 20 YEARS MUST HAVE ELAPSED SINCE CONSTRUCTION OR PRIOR REHABILITATION.—A building shall not be a qualified rehabilitated building unless there is a period of at least 20 years between—

"(i) the date the physical work on this rehabilitation of the building began, and

"(ii) the later of—

"(I) the date such building was first placed in service, or

"(II) the date such building was placed in service in connection with a prior rehabilitation with respect to which a credit was allowed by reason of subsection (a)(1)(E).

"(C) MAJOR PORTION TREATED AS SEPARATE BUILDING IN CERTAIN CASES.—Where there is a separate rehabilitation of a major portion of a building, such major portion shall be treated as a separate building.

"(D) REHABILITATION INCLUDES RECONSTRUCTION.—Rehabilitation includes reconstruction.

"(2) QUALIFIED REHABILITATION EXPENDITURE DEFINED.—

"(A) IN GENERAL.—The term 'qualified rehabilitation expenditure' means any amount properly chargeable to capital account which is incurred after October 31, 1978—

"(i) for property (or additions or improvements to property) with a useful life of 5 years or more, and

"(ii) in connection with the rehabilitation of a qualified rehabilitated building.

"(B) CERTAIN EXPENDITURES NOT INCLUDED.—The term 'qualified rehabilitation expenditure' does not include—

"(i) PROPERTY OTHERWISE SECTION 38 PROPERTY.—Any expenditure for property which constitutes section 38 property (determined without regard to subsection (a)(1)(E)).

"(ii) COST OF ACQUISITION.—The cost of acquiring any building or any interest therein.

"(iii) ENLARGEMENTS.—Any expenditure attributable to the enlargement of the existing building.

"(iv) CERTIFIED HISTORIC STRUCTURES.—Any expenditure attributable to the rehabilitation of a certified historic structure (within the meaning of section 191(d)(1)), unless the rehabilitation is a certified rehabilitation (within the meaning of section 191(d)(4)).

"(3) PROPERTY TREATED AS NEW SECTION 38 PROPERTY.—Property which is treated as section 38 property by reason of subsection (a)(1)(E) shall be treated as new section 38 property."

(c) TECHNICAL AMENDMENT.—Paragraph (8) of section 48(a) (relating to amortized property) is amended by striking out "or 188" and inserting in lieu thereof "188, or 191".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years ending after October 31, 1978; except that the amendment made by subsection (c) shall only apply with respect to property placed in service after such date.

SEC. 316. TAX TREATMENT OF THE INVESTMENT CREDIT IN THE CASE OF COOPERATIVE ORGANIZATIONS.

(a) IN GENERAL.—Section 46 (relating to amount of credit) is amended by adding at the end thereof the following new subsection:

"(h) SPECIAL RULES FOR COOPERATIVES.—In the case of a cooperative organization described in section 1381(a)—

"(1) that portion of the credit allowable to the organization under section 38 which the organization cannot use for the taxable year to which the qualified investment is attributable because of the limitation contained in subsection (a)(3) shall be allocated to the patrons of the organization,

"(2) section 47 (relating to certain dispositions, etc., of section 38 property) shall be applied as if any allocated portion of the credit had been retained by the organization, and

"(3) the rules necessary to carry out the purposes of this subsection shall be determined under regulations prescribed by the Secretary."

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 46(e) (relating to limitations in case of certain persons) is amended—

(A) by adding "and" at the end of subparagraph (A),

(B) by striking out "and" at the end of subparagraph (B), and

(C) by striking out subparagraph (C).

(2) Paragraph (2) of section 46(e) is amended—

(A) by adding "and" at the end of subparagraph (A),

(B) by striking out ", and" at the end of subparagraph (B) and inserting in lieu thereof a period, and

(C) by striking out subparagraph (C).

(3) Section 1388 (relating to definitions and special rules for cooperative organizations) is amended by adding at the end thereof the following new subsection:

"(j) Cross Reference.—

"For provisions relating to the apportionment of the investment credit between cooperative organizations and their patrons, see section 46(h)."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years ending after October 31, 1978.

SEC. 317. TRANSFERS TO CONRAIL NOT TREATED AS DISPOSITIONS FOR PURPOSES OF THE INVESTMENT CREDIT.

(a) IN GENERAL.—Subsection (b) of section 47 (relating to certain dispositions, etc., of section 38 property) is amended by striking out "or" at the end of paragraph (1), by striking out the period at the end of paragraph (2) and inserting in lieu thereof ", or", and by inserting after paragraph (2) the following new paragraph:

"(3) a transfer to which subsection (c) of section 374 (relating to exchanges under the final system plan for ConRail) applies."

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to taxable years ending after March 31, 1976.

Subtitle C—Targeted Jobs Credit; WIN Credit

SEC. 321. TARGETED JOBS CREDIT.

(a) IN GENERAL.—Section 51. (relating to amount of credit) is amended to read as follows:

"SEC. 51. AMOUNT OF CREDIT.

"(a) DETERMINATION OF AMOUNT.—The amount of the credit allowable by section 44B for the taxable year shall be the sum of—

"(1) 50 percent of the qualified first-year wages for such year, and

"(2) 25 percent of the qualified second-year wages for such year.

"(b) QUALIFIED WAGES DEFINED.—For purposes of this subpart—

"(1) IN GENERAL.—The term 'qualified wages' means the wages paid or incurred by the employer during the taxable year to individuals who are members of a targeted group.

"(2) QUALIFIED FIRST-YEAR WAGES.—The term 'qualified first-year wages' means, with respect to any individual, qualified wages attributable to service rendered during the 1-year period beginning with the day the individual begins work for the employer (or, in the case of a vocational rehabilitation referral, the day the individual begins work for the employer on or after the beginning of such individual's rehabilitation plan).

"(3) QUALIFIED SECOND-YEAR WAGES.—The term 'qualified second-year wages' means, with respect to any individual, the qualified wages attributable to service rendered during the 1-year

period beginning on the day after the last day of the 1-year period with respect to such individual determined under paragraph (2).

"(4) ONLY FIRST $6,000 OF WAGES PER YEAR TAKEN INTO ACCOUNT.—The amount of the qualified first-year wages, and the amount of the qualified second-year wages, which may be taken into account with respect to any individual shall not exceed $6,000 per year.

"(c) WAGES DEFINED.—For purposes of this subpart—

"(1) IN GENERAL.—Except as otherwise provided in this subsection and subsection (h)(2), the term 'wages' has the meaning given to such term by subsection (b) of section 3306 (determined without regard to any dollar limitation contained in such section).

"(2) EXCLUSION FOR EMPLOYERS RECEIVING ON-THE-JOB TRAINING PAYMENTS.—The term 'wages' shall not include any amounts paid by an employer for any period to any individual for whom the employer receives federally funded payments for on-the-job training of such individual for such period.

"(3) INDIVIDUALS FOR WHOM WIN CREDIT CLAIMED.—The term 'wages' does not include any amount paid or incurred by the employer to an individual with respect to whom the employer claims credit under section 40.

"(4) TERMINATION.—The term 'wages' shall not include any amount paid or incurred after December 31, 1980.

"(d) MEMBERS OF TARGETED GROUPS.—For purposes of this subpart—

"(1) IN GENERAL.—An individual is a member of a targeted group if such individual is—

"(A) a vocational rehabilitation referral,

"(B) an economically disadvantaged youth,

"(C) an economically disadvantaged Vietnam-era veteran,

"(D) an SSI recipient,

"(E) a general assistance recipient, or

"(F) a youth participating in a cooperative education program, or

"(G) an economically disadvantaged convict.

"(2) VOCATIONAL REHABILITATION REFERRAL.—The term 'vocational rehabilitation referral' means any individual who is certified by the designated local agency as—

"(A) having a physical or mental disability which, for such individual, constitutes or results in a substantial handicap to employment, and

"(B) having been referred to the employer upon completion of (or while receiving) rehabilitative services pursuant to—

"(i) an individualized written rehabilitation plan under a State plan for vocational rehabilitation services approved under the Rehabilitation Act of 1973, or

"(ii) a program of vocational rehabilitation carried out under chapter 31 of title 38, United States Code.

"(3) ECONOMICALLY DISADVANTAGED YOUTH.—

"(A) IN GENERAL.—The term 'economically disadvantaged youth' means any individual who is certified by the designated local agency as—

"(i) meeting the age requirements of subparagraph (B), and

"(ii) being a member of an economically disadvantaged family (as determined under paragraph (9)).

"(B) AGE REQUIREMENTS.—An individual meets the age requirements of this subparagraph if such individual has attained age 18 but not age 25 on the hiring date.

"(4) VIETNAM VETERAN WHO IS A MEMBER OF AN ECONOMICALLY DISADVANTAGED FAMILY.—The term 'Vietnam veteran who is a member of an economically disadvantaged family' means any individual who is certified by the designated local agency as—

"(A)(i) having served on active duty (other than active duty for training) in the Armed Forces of the United States for a period of more than 180 days, any part of which occurred after August 4, 1964, and before May 8, 1975, or

"(ii) having been discharged or released from active duty in the Armed Forces of the United States for a service-connected disability if any part of such active duty was performed after August 4, 1964, and before May 8, 1975,

"(B) not having any day during the preemployment period which was a day of extended active duty in the Armed Forces of the United States,

"(C) being a member of an economically disadvantaged family (determined under paragraph (9)), and

"(D) not having attained the age of 35 on the hiring date.

For purposes of subparagraph (B), the term 'extended active duty' means a period of more than 90 days during which the individual was on active duty (other than active duty for training).

"(5) SSI RECIPIENTS.—The term 'SSI recipient' means any individual who is certified by the designated local agency as receiving supplemental security income benefits under title XVI of the Social Security Act (including supplemental security income benefits of the type described in section 1616 of such Act or section 212 of Public Law 93–66) for any month ending in the preemployment period.

(6) GENERAL ASSISTANCE RECIPIENTS.—

"(A) IN GENERAL.—The term 'general assistance recipient' means any individual who is certified by the designated local agency as receiving assistance under a qualified general assistance program for any period of not less than 30 days ending within the preemployment period.

"(B) QUALIFIED GENERAL ASSISTANCE PROGRAM.—The term 'qualified general assistance program' means any program of a State or a political subdivision of a State—

"(i) which provides general assistance or similar assistance which—

"(I) is based on need, and

"(II) consists of money payments,

and

"(ii) which is designated by the Secretary (after consultation with the Secretary of Health, Education, and Welfare) as meeting the requirements of clause (i).

"(7) ECONOMICALLY DISADVANTAGED EX-CONVICT.—The term 'economically disadvantaged ex-convict' means any individual who is certified by the designated local agency—

"(A) as having been convicted of a felony under any statute of the United States or any State,

"(B) as being a member of an economically disadvantaged family (as determined under paragraph (9)), and

"(C) as having a hiring date which is not more than 5 years after the last date on which such individual was so convicted or was released from prison.

"(8) YOUTH PARTICIPATING IN A QUALIFIED COOPERATIVE EDUCATION PROGRAM —

"(A) IN GENERAL.—The term 'youth participating in a qualified cooperative education program' means any individual who is certified by the school participating in the program as—

"(i) having attained age 16 and not having attained age 19,

"(ii) not having graduated from a high school or vocational school, and

"(iii) being enrolled in and actively pursuing a qualified cooperative education program.

"(B) QUALIFIED COOPERATIVE EDUCATION PROGRAM DEFINED.—The term 'qualified cooperative education program' means a program of vocational education for individuals who (through written cooperative arrangements between a qualified school and 1 or more employers) receive instruction (including required academic instruction) by alternation of study and school with a job in any occupational field (but only if these 2 experiences are planned by the school and employer so that each contributes to the student's education and employability).

"(C) QUALIFIED SCHOOL DEFINED.—The term 'qualified school' means—

"(i) a specialized high school used exclusively or principally for the provision of vocational education to individuals who are available for study in preparation for entering the labor market,

"(ii) the department of a high school exclusively or principally used for providing vocational education to persons who are available for study in preparation for entering the labor market, or

"(iii) a technical or vocational school used exclusively or principally for the provision of vocational education to persons who have completed or left high school and who are available for study in preparation for entering the labor market.

A school which is not a public school shall be treated as a qualified school only if it is exempt from tax under section 501(a).

"(D) INDIVIDUAL MUST BE CURRENTLY PURSUING PROGRAM.—Wages shall be taken into account with respect to a qualified cooperative education program only if the wages are attributable to services performed while the individual meets the requirements of subparagraph (A).

"(9) MEMBERS OF ECONOMICALLY DISADVANTAGED FAMILIES.—An individual is a member of an economically disadvantaged family if the designated local agency determines that such individual was a

member of a family which had an income during the 6 months immediately preceding the month in which the hiring date occurs, which, on an annual basis would be less than 70 percent of the Bureau of Labor Statistics lower living standard.

"(10) PREEMPLOYMENT PERIOD.—The term 'preemployment period' means the 60-day period ending on the hiring date.

"(11) HIRING DATE.—The term 'hiring date' means the day the individual is hired by the employer.

"(12) DESIGNATED LOCAL AGENCY.—The term 'designated local agency' means the agency for any locality designated jointly by the Secretary and the Secretary of Labor to perform certification of employees for employers in that locality.

"(e) QUALIFIED FIRST-YEAR WAGES CANNOT EXCEED 30 PERCENT OF FUTA WAGES FOR ALL EMPLOYEES.—The amount of the qualified first-year wages which may be taken into account under subsection (a)(1) or any taxable year shall not exceed 30 percent of the aggregate unemployment insurance wages paid by the employer during the calendar year ending in such taxable year. For purposes of the preceding sentence, the term 'unemployment insurance wages' has the meaning given to the term 'wages' by section 3306(b).

"(f) REMUNERATION MUST BE FOR TRADE OR BUSINESS EMPLOYMENT.—

"(1) IN GENERAL.—For purposes of this subpart, remuneration paid by an employer to an employee during any year shall be taken into account only if more than one-half of the remuneration so paid is for services performed in a trade or business of the employer.

"(2) SPECIAL RULE FOR CERTAIN DETERMINATION.—Any determination as to whether paragraph (1), or subparagraph (A) or (B) of subsection (h)(1), applies with respect to any employee for any year shall be made without regard to subsections (a) and (b) of section 52.

"(3) YEAR DEFINED.—For purposes of this subsection and subsection (h), the term 'year' means the taxable year; except that, for purposes of applying so much of such subsections as relates to subsection (e), such term means the calendar year.

"(g) SECRETARY OF LABOR TO NOTIFY EMPLOYERS OF AVAILABILITY OF CREDIT.—The Secretary of Labor, in consultation with the Internal Revenue Service, shall take such steps as may be necessary or appropriate to keep employers apprised of the availability of the credit provided by section 44B.

"(h) SPECIAL RULES FOR AGRICULTURAL LABOR AND RAILWAY LABOR.—For purposes of this subpart—

"(1) UNEMPLOYMENT INSURANCE WAGES.—

"(A) AGRICULTURAL LABOR.—If the services performed by any employee for an employer during more than one-half of any pay period (within the meaning of section 3306(d)) taken into account with respect to any year constitute agricultural labor (within the meaning of section 3306(k)), the term 'unemployment insurance wages' means, with respect to the remuneration paid by the employer to such employee for such year, an amount equal to so much of such remuneration as constitutes 'wages' within the meaning of section 3121(a), except that the contribution and benefit base for each calendar year shall be deemed to be $6,000.

"(B) RAILWAY LABOR.—If more than one-half of remuneration paid by an employer to an employee during any year is remuneration for service described in section 3306(c)(9), the term 'unemployment insurance wages' means, with respect to such employee for such year, an amount equal to so much of the remuneration paid to such employee during such year which would be subject to contributions under section 8(a) of the Railroad Unemployment Insurance Act (45 U.S.C. 358(a)) if the maximum amount subject to such contributions were $500 per month..

"(2) WAGES.—In any case to which subparagraph (A) or (B) of paragraph (1) applies, the term 'wages' means unemployment insurance wages (determined without regard to any dollar limitation)."

(b) JOBS CREDIT MADE ELECTIVE.—

(1) Section 44B (relating to credit for employment of certain new employees) is amended—

(A) by striking out "There shall be allowed" in subsection (a) and inserting in lieu thereof "At the election at the taxpayer, there shall be allowed", and

(B) by adding at the end thereof the following new subsection:

"(c) ELECTION.—

"(1) TIME FOR MAKING ELECTION.—An election under subsection (a) for any taxable year may be made (or revoked) at any time before the expiration of the 3-year period beginning on the last date prescribed by law for filing the return for such taxable year (determined without regard to extensions).

"(2) MANNER OF MAKING ELECTION.—Any election under subsection (a) (or revocation thereof) shall be made in such manner as the Secretary may by regulations prescribe."

(2) Section 6501 (relating to limitations on assessment and collection) is amended by adding at the end thereof the following new subsection:

"(q) DEFICIENCY ATTRIBUTABLE TO ELECTION UNDER SECTION 44B.—The period for assessing a deficiency attributable to any election under section 44B (or any revocation thereof) shall not expire before the date 1 year after the date on which the Secretary is notified of such election (or revocation)."

(c) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) AMENDMENTS OF SECTION 52.—

(A) Section 52 (relating to special rules for computing credit for employment of certain new employees) is amended—

(i) by striking out subsections (c), (e), (i), and (j), and

(ii) by redesignating subsections (d), (f), (g), and (h) as subsections (c), (d), (e), and (f), respectively.

(B) Subsections (a) and (b) of section 52 are each amended by striking out "proportionate contribution to the increase in unemployment insurance wages" and inserting in lieu thereof "proportionate share of the wages".

(C) Subsection (e) of section 52 (as redesignated by subparagraph (A)) is amended—

(i) by adding "and" at the end of paragraph (1);

(ii) by striking out ", and " at the end of paragraph (2) and inserting a period; and

(iii) by striking out paragraph (3).

(2) AMENDMENTS OF SECTION 53.—

(A) Subsection (a) of section 53 is amended by striking out "the amount of the tax imposed by this chapter for the taxable year, reduced by" and inserting in lieu thereof "90 percent of the excess of the tax imposed by this chapter for the taxable year over the sum of".

(B) Section 53 (relating to limitation based on amount of tax is amended by striking out subsection (b) and by redesignating subsection (c) as subsection (b).

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall apply to amounts paid or incurred after December 31, 1978, in taxable years ending after such date.

(2) SPECIAL RULES FOR NEWLY TARGETED GROUPS.—

(A) INDIVIDUAL MUST BE HIRED AFTER SEPTEMBER 26, 1978.—In the case of a member of a newly targeted group—

(i) such individual shall be taken into account for purposes of the credit allowable by section 44B of the Internal Revenue Code of 1954 only if such individual is first hired by the employer after September 26, 1978, and

(ii) such individual shall be treated for purposes of such credit as having first begun work for the employer not earlier than January 1, 1979.

(B) MEMBER OF NEWLY TARGETED GROUP DEFINED.—For purposes of subparagraph (A), an individual is a member of a newly targeted group if—

(i) such individual meets the requirements of subparagraph (A), (C), (D), (E), (F) or (G) of section 51(d)(1) of such Code, and

(ii) in the case of an individual meeting the requirements of subparagraph (A) of such section 51(d)(1), a credit was not claimed for such individual by the taxpayer for a taxable year beginning before January 1, 1979.

(3) TRANSITIONAL RULE.—In the case of a taxable year which begins in 1978 and ends after December 31, 1978, the amount of the credit allowable by section 44B of the Internal Revenue Code of 1954 (determined without regard to section 53 of such Code) shall be the sum of—

(A) the amount of the credit which would be so allowable without regard to the amendments made by this section, plus

(B) the amount which would be so allowable by reason of the amendments made by this section.

(4) SUBSECTION (c)(2).—The amendments made by subsection (b)(2) shall apply to taxable years beginning after December 31, 1978.

SEC. 322. WORK INCENTIVE PROGRAM CREDIT CHANGES.

(a) CHANGES IN AMOUNT OF CREDIT.—Section 50A(a) (relating to amount of credit) is amended by striking out paragraphs (1) and (2) and inserting in lieu thereof the following:

"(1) GENERAL RULE.—The amount of the credit allowed by section 40 for the taxable year shall be equal to the sum or—

"(A) 50 percent of the first-year work incentive program expenses, and

"(B) 25 percent of the second-year work incentive program expenses.

"(2) LIMITATION BASED ON AMOUNT OF TAX.—Notwithstanding paragraph (1), the amount of credit allowed by section 40 for the taxable year shall not exceed the liability for tax for the taxable year."

(b) CHANGES IN LIMITATIONS.—Subsection (a) of section 50A is amended by striking out paragraphs (4), (5), and (6) and by inserting immediately after paragraph (3) the following new paragraph:

"(4) LIMITATION WITH RESPECT TO NONBUSINESS ELIGIBLE EMPLOYEES.—

"(A) IN GENERAL.—In the case of any work incentive program expenses paid or incurred by the taxpayer during the taxable year to eligible employees whose services are not performed in connection with a trade or business of the taxpayer—

"(i) paragraph (1)(A) shall be applied by substituting 35 percent for 50 percent,

"(ii) subparagraph (B) of paragraph (1) shall not apply, and

"(iii) the aggregate amount of such work incentive program expenses which may be taken into account under paragraph (1) for such taxable year may not exceed $12,000.

"(B) DEPENDENT CARE CREDIT MAY NOT BE CLAIMED.—No credit shall be allowed under section 44A with respect to any amounts paid or incurred by the taxpayer with respect to which the taxpayer is allowed a credit under section 40.

"(C) MARRIED INDIVIDUALS.—In the case of a husband or wife who files a separate return, subparagraph (A) shall be applied by substituting $6,000 and $12,000. The preceding sentence shall not apply if the spouse of the taxpayer has no work incentive program expenses described in such subparagraph for the taxable year."

(c) REPEAL OF PROVISIONS PERMITTING RECOVERY OF CREDIT.—Section 50A is amended by striking out subsections (c) and (d).

(d) CHANGES IN DEFINITIONS AND SPECIAL RULES.—

(1) Subsection (a) of section 50B (relating to work incentive program expenses) is amended to read as follows:

"(a) WORK INCENTIVE PROGRAM EXPENSES.—For purposes of this subpart—

"(1) IN GENERAL.—The term 'work incentive program expenses' means the amount of wages paid or incurred by the taxpayer for services rendered by eligible employees.

"(2) FIRST-YEAR WORK INCENTIVE PROGRAM EXPENSES.—The term 'first-year work incentive program expenses' means, with respect to any eligible employee, work incentive program expenses attributable to service rendered during the one-year period which begins on the day the eligible employee begins work for the taxpayer.

"(3) SECOND-YEAR WORK INCENTIVE PROGRAM EXPENSES.—The term 'second-year work incentive program expenses' means, with respect to any eligible employee, work incentive program expenses attributable to service rendered during the one-year period which begins on the day after the last day of the one-year period described in paragraph (2).

"(4) LIMITATION ON AMOUNT OF WORK INCENTIVE PROGRAM EXPENSES.—The amount of the work incentive program expenses

taken into account with respect to any eligible employee for any one-year period described in paragraph (2) or (3) (as the case may be) shall not exceed $6,000."

(2) Subsection (c) of section 50B is amended by striking out paragraphs (1) and (4) and by redesignating paragraphs (2), (3), and (5) as paragraphs (1), (2), and (3), respectively.

(3) Subsection (e) of section 50B (relating to estates and trusts) is amended—

(A) by inserting "and" at the end of paragraph (1),

(B) by striking out ", and" at the end of paragraph (2) and inserting in lieu thereof a period, and

(C) by striking out paragraph (3).

(4) Section 50B is amended by redesignating subsections (g) and (h) as subsections (h) and (i), respectively, and by inserting after subsection (f) the following new subsection:

"(g) SPECIAL RULES FOR CONTROLLED GROUPS.—

"(1) CONTROLLED GROUP OF CORPORATIONS.—For purposes of this subpart, all employees of all corporations which are members of the same controlled group of corporations shall be treated as employed by a single employer. In any such case, the credit (if any) allowable by section 40 to each such member shall be its proportionate share of the work incentive program expenses giving rise to such credit. For purposes of this subsection, the term 'controlled group of corporations' has the meaning given to such term by section 1563(a), except that—

"(A) 'more than 50 percent' shall be substituted for 'at least 80 percent' each place it appears in section 1563(a)(1), and

"(B) the determination shall be made without regard to subsections (a)(4) and (e)(3)(C) of section 1563.

"(2) EMPLOYEES OF PARTNERSHIPS, PROPRIETORSHIPS, ETC., WHICH ARE UNDER COMMON CONTROL.—For purposes of this subpart under regulations prescribed by the Secretary—

"(A) all employees of trades or business (whether or not incorporated) which are under common control shall be treated as employed by a single employer, and

"(B) the credit (if any) allowable by section 40 with respect to each trade or business shall be its proportionate share of the work incentive program expenses giving rise to such credit.

The regulations prescribed under this paragraph shall be based on principles similar to the principles which apply in the case of paragraph (1).".

(5) Paragraph (1) of subsection (h) (as redesignated by paragraph (4)) of section 50B (relating to eligible employee) is amended to read as follows:

"(1) ELIGIBLE EMPLOYEE.—For purposes of this subpart the term 'eligible employee' means an individual—

"(A) who has been certified by the Secretary of Labor or by the appropriate agency of State or local government as—

"(i) being eligible for financial assistance under part A of title IV of the Social Security Act and as having continually received such financial assistance during the 90-day period which immediately precedes the date on which such individual is hired by the employer, or

"(ii) having been placed in employment under a work incentive program established under section 432(b)(1) of the Social Security Act,

"(B) who has been employed by the taxpayer for a period in excess of 30 consecutive days on a substantially full-time basis,

"(C) who has not displaced any other individual from employment by the taxpayer, and

"(D) who is not a migrant worker.

The term 'eligible employee' includes an employee of the taxpayer whose services are not performed in connection with a trade or business of the taxpayer.".

(d) DEDUCTION FOR WAGES REDUCED BY AMOUNT OF CREDIT.—

(1) Section 280C (relating to portion of wages for which credit is claimed under section 44B) is amended—

(A) by striking out "SECTION 44B" in the caption and inserting in lieu thereof "SECTION 40 OR 44B",

(B) by inserting "(b) RULE FOR SECTION 44B CREDIT.—" immediately before "No deduction",

(C) by striking out "this section shall be applied" and inserting in lieu thereof "this subsection shall be applied" in the second sentence, and

(D) by inserting immediately after the caption of such section the following new subsection:

"(a) RULE FOR SECTION 40 CREDIT.—No deduction shall be allowed for that portion of the work incentive program expenses paid or incurred for the taxable year which is equal to the amount of the credit allowable for the taxable year under section 40 (relating to credit for expenses of work incentive programs) determined without regard to the provisions of section 50A(a)(2) (relating to limitation based on amount of tax). In the case of a corporation which is a member of a controlled group of corporations (within the meaning of section 50B(g)(1)) or a trade or business which is treated as being under common control with other trades or businesses (within the meaning of section 50B(g)(2)), this subsection shall be applied under rules prescribed by the Secretary similar to the rules applicable under paragraphs (1) and (2) of section 50B(g).".

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall apply to work incentive program expenses paid or incurred after December 31, 1978, in taxable years ending after such date; except that so much of the amendment made by subsection (a) as affects section 50A(a)(2) of the Internal Revenue Code of 1954 shall apply to taxable years beginning after December 31, 1978.

(2) SPECIAL RULES FOR CERTAIN ELIGIBLE EMPLOYEES.—

(A) ELIGIBLE EMPLOYEES HIRED BEFORE SEPTEMBER 27, 1978.—In the case of any eligible employee (as defined in section 50B(h)) hired before September 27, 1978, no credit shall be allowed under section 40 with respect to second-year work incentive program expenses (as defined in section 50B(a)) attributable to service performed by such employee.

(B) ELIGIBLE EMPLOYEES HIRED AFTER SEPTEMBER 26, 1978.—*In the case of any eligible employee (as defined in section 50B(h)) hired after September 27, 1978, such individual shall be treated for purposes of the credit allowed by section 40 as having first begun work for the taxpayer not earlier than January 1, 1979.*

Subtitle D—Tax-Exempt Bonds

PART I—INDUSTRIAL DEVELOPMENT BONDS

SEC. 331. INCREASE IN LIMIT ON SMALL ISSUES OF INDUSTRIAL DEVELOPMENT BONDS.

(a) GENERAL RULE.—*Subparagraph (D) of section 103(b)(6) (relating to $5,000,000 limit in certain cases) is amended by striking out "$5,000,000" in the heading and in the text and inserting in lieu thereof $10,000,000".*

(b) TREATMENT OF CERTAIN URBAN DEVELOPMENT ACTION GRANTS.—*Paragraph (6) of section 103(c) (relating to exemption for certain small issues) is amended by adding at the end thereof the following new subparagraph:*

"(I) AGGREGATE AMOUNT OF CAPITAL EXPENDITURES WHERE THERE IS URBAN DEVELOPMENT ACTION GRANT.—*In the case of any issue substantially all of the proceeds of which are to be used to provide facilities with respect to which an urban development action grant has been made under section 119 of the Housing and Community Development Act of 1974, capital expenditures of not to exceed $10,000,000 shall not be taken into account for purposes of applying subparagraph (D)(ii).*"

(c) EFFECTIVE DATES.—

(1) *The amendments made by subsection (a) shall apply to—*

(A) *obligations issued after December 31, 1978, in taxable years ending after such date, and*

(B) *capital expenditures made after December 31, 1978, with respect to obligations issued before January 1, 1979.*

(2) *The amendment made by subsection (b) shall apply to—*

(A) *obligations issued after September 30, 1979, in taxable years ending after such date, and*

(B) *capital expenditures made after September 30, 1979, with respect to obligations issued after such date.*

SEC. 332. LOCAL FURNISHING OF ELECTRIC ENERGY.

(a) IN GENERAL.—*Paragraph (4) of section 103(b) (relating to certain exempt activities) is amended by adding at the end thereof the following new sentence:*

"*For purposes of subparagraph (E), the local furnishing of electric energy from a facility shall include furnishing solely within the area consisting of a city and 1 contiguous county.*"

(b) EFFECTIVE DATE.—*The amendment made by subsection (a) shall apply to taxable years ending after April 30, 1968, but only with respect to obligations issued after such date.*

SEC. 333. INDUSTRIAL DEVELOPMENT BONDS FOR WATER FACILITIES.

(a) IN GENERAL.—Subparagraph (G) of section 103(b)(4) (relating to industrial development bonds) is amended to read as follows:

"(G) facilities for the furnishing of water for any purpose if—

"(i) the water is or will be made available to members of the general public (including electric utility, industrial, agricultural, or commercial users), and

"(ii) either the facilities are operated by a governmental unit or the rates for the furnishing or sale of the water have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to obligations issued after the date of the enactment of this Act in taxable years ending after such date.

PART II—OTHER TAX-EXEMPT BOND PROVISIONS

SEC. 336. DECLARATORY JUDGMENT PROCEDURE FOR JUDICIAL REVIEW OF DETERMINATIONS RELATING TO GOVERNMENTAL OBLIGATIONS.

(a) IN GENERAL.—Part IV of subchapter C of chapter 76 (relating to declaratory judgments) is amended by adding at the end thereof the following new section:

"SEC. 7478. DECLARATORY JUDGMENTS RELATING TO STATUS OF CERTAIN GOVERNMENTAL OBLIGATIONS.

"(a) CREATION OF REMEDY.—In a case of actual controversy involving—

"(1) a determination by the Secretary whether prospective obligations are described in section 103(a), or

"(2) a failure by the Secretary to make a determination with respect to any matter referred to in paragraph (1),

upon the filing of an appropriate pleading, the Tax Court may make a declaration whether such prospective obligations are described in section 103(a). Any such declaration shall have the force and effect of a decision of the Tax Court and shall be reviewable as such.

"(b) LIMITATIONS.—

"(1) PETITIONER.—A pleading may be filed under this section only by the prospective issuer.

"(2) EXHAUSTION OF ADMINISTRATIVE REMEDIES.—The court shall not issue a declaratory judgment or decree under this section in any proceeding unless it determines that the petitioner has exhausted all available administrative remedies within the Internal Revenue Service. A petitioner shall be deemed to have exhausted its administrative remedies with respect to a failure of the Secretary to make a determination with respect to an issue of obligations at the expiration of 180 days after the date on which the request for such determination was made if the petitioner has taken, in a timely manner, all reasonable steps to secure such determination.

"(3) TIME FOR BRINGING ACTION.—If the Secretary sends by certified or registered mail notice of his determination as described in subsection (a)(1) to the petitioner, no proceeding may be initiated under this section unless the pleading is filed before the 91st day after the date of such mailing."

(b) AUTHORITY OF TAX COURT TO ASSIGN PROCEEDINGS TO COMMISSIONERS.—

(1) IN GENERAL.—Subsection (c) of section 7456 (relating to commissioners of the Tax Court) is amended by adding at the end thereof the following new sentence: "The chief judge may assign proceedings under sections 7428, 7476, 7477, and 7478 to be heard by the commissioners of the court, and the court may authorize a commissioner to make the decision of the court with respect to such proceeding subject to such conditions and review as the court may by rule provide."

(2) TECHNICAL AMENDMENTS.—

(A) Section 7476 is amended by striking out subsection (c) and by redesignating subsections (d) and (e) as subsections (c) and (d), respectively.

(B) Section 7477 is amended by striking out subsection (c).

(c) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 7482(b) (relating to venue for appeal of decision of Tax Court) is amended—

(A) by striking out "provided in paragraph (2)" in paragraph (1) and inserting in lieu thereof "provided in paragraphs (2) and (3)", and

(B) by adding at the end thereof the following new paragraph:

"(3) DECLARATORY JUDGMENT ACTIONS RELATING TO STATUS OF CERTAIN GOVERNMENTAL OBLIGATIONS.—In the case of any decision of the Tax Court in a proceeding under section 7478, such decision may only be reviewed by the Court of Appeals for the District of Columbia."

(2) The table of sections for part IV of subchapter C of chapter 76 is amended by adding at the end thereof the following new item:

"Sec. 7478. Declaratory judgments relating to status of certain governmental obligations."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to requests for determinations made after December 31, 1978.

SEC. 337. DISPOSITION OF AMOUNTS GENERATED BY ADVANCE REFUNDING OF CERTAIN GOVERNMENTAL OBLIGATIONS.

(a) GENERAL RULE.—The payment to a charitable organization of a refund profit held in a trust fund or escrow arrangement, or held by an underwriter or other person under a qualified agreement in accordance with that agreement—

(1) shall not cause the refunding obligations out of which the refund profit arose to be treated as arbitrage bonds (within the meaning of section 103(c) of the Internal Revenue Code of 1954) and

(2) may be paid without penalty imposed on the issuer of such obligations.

(b) RULE FOR GOVERNMENTS WHICH HAVE ALREADY PAID ARBITRAGE PROFITS TO THE UNITED STATES.—In the case of a State or local government which, before January 1, 1977—

(1) requested in writing a ruling by the Internal Revenue Service with respect to the tax consequences of paying refund profit to charitable organizations,

(2) failed to receive a favorable ruling and did not pay the refund profit to a charitable organization, and

which accounted to the United States for refund profit by direct payment to the United States, or by the purchase of low-interest United States obligations, the Secretary of the Treasury shall pay, out of any amounts in the Treasury not otherwise appropriated, an amount equal to the refund profit for which the State or local government has accounted to the United States. Amounts paid to a State or local government under this subsection shall be distributed to such charitable organizations within 90 days after the date on which the payment is received by the State or local government in the same manner as if the refund profit had not been paid to the United States and met the requirements of subsection (a).

(c) DEFINITIONS.—For purposes of this section—

(1) REFUND PROFIT.—The term "refund profit" means interest, profit, or other amounts generated by, or arising out of, the advance refunding, before September 24, 1976, of an obligation of a State or local government described in section 103 of such Code.

(2) CHARITABLE ORGANIZATION.—The term "charitable organization" means an organization described in section 501(c)(3) of such Code and exempt from taxation under section 501(a) of such Code other than an organization described in section 509(a) of such Code.

(3) QUALIFIED AGREEMENT.—The term "qualified agreement" means an agreement (whether or not enforceable) which provides for, or contemplates, the payment of refund profit to one or more charitable organizations.

(4) LOW-INTEREST UNITED STATES OBLIGATIONS.—The term "low-interest United States obligations" means United States obligations which bear an interest rate lower than the highest rate of interest borne by public debt securities generally available for purchase at the time such obligations were purchased.

Subtitle E—Small Business Provisions

PART I—PROVISIONS RELATING TO SUBCHAPTER S

SEC. 341. SUBCHAPTER S CORPORATIONS ALLOWED 15 SHAREHOLDERS.

(a) GENERAL RULE.—Paragraph (1) of section 1371(a) (defining small business corporation) is amended to read as follows:

"(1) have more than 15 shareholders;".

(b) TECHNICAL AMENDMENTS.—

(1) Section 1371 is amended by striking out subsection (e) and by redesignating subsection (f) as subsection (e).

(2) Paragraph (2) of section 1371(a) is amended by striking out "subsection (f)" and inserting in lieu thereof "subsection (e)".

SEC. 342. PERMITTED SHAREHOLDERS OF SUBCHAPTER S CORPORATIONS.

(a) HUSBAND AND WIFE TREATED AS ONE INDIVIDUAL.—Subsection (c) of section 1371 (relating to stock owned by husband and wife) is amended to read as follows:

"(c) STOCK OWNED BY HUSBAND AND WIFE.—For purposes of subsection (a)(1), a husband and wife (and their estates) shall be treated as one shareholder."

(b) GRANTOR OF GRANTOR TRUST TREATED AS THE SHAREHOLDER.—Subsection (e) of section 1371 (as redesignated by section 331(b)(1) of this Act) is amended by inserting after the first sentence the following new sentence: "In the case of a trust described in paragraph (1), the grantor shall be treated as the shareholder."

SEC. 343. EXTENSION OF PERIOD FOR MAKING SUBCHAPTER S ELECTIONS.

(a) GENERAL RULE.—Subsection (c) of section 1372 (relating to when and how subchapter S election may be made) is amended to read as follows:

"(c) WHEN AND HOW MADE.—

"(1) IN GENERAL.—An election under subsection (a) may be made by a small business corporation for any taxable year—

"(A) at any time during the preceding taxable year, or

"(B) at any time during the first 75 days of the taxable year.

"(2) TREATMENT OF CERTAIN LATE ELECTIONS.—If—

"(A) a small business corporation makes an election under subsection (a) for any taxable year, and

"(B) such election is made after the first 75 days of the taxable year and on or before the last day of such taxable year,

then such election shall be treated as made for the following taxable year.

"(3) MANNER OF MAKING ELECTION.—An election under subsection (a) shall be made in such manner as the Secretary shall prescribe by regulations."

(b) TECHNICAL AMENDMENTS.—

(1) The second sentence of section 1372(a) is amended to read as follows: "Such election shall be valid only if all persons who are shareholders in such corporation on the day on which such election is made consent to such election."

(2) Supbaragraph (A) of section 1372(e)(1) is amended to read as follows:

"(A) An election under subsection (a) made by a small business corporation shall terminate if any person who was not a shareholder in such corporation on the day on which the election is made becomes a shareholder in such corporation and affirmatively refuses (in such manner as the Secretary may by regulations prescribe) to consent to such election on or before the 60th day after the day on which he acquires the stock."

(3) Subparagraph (C) of section 1372(e)(1) is amended by inserting "(or, if later, the first taxable year for which such election would otherwise have been effective)" after "in the corporation".

SEC. 344. EFFECTIVE DATE.

The amendments made by this part shall apply to taxable years beginning after December 31, 1978.

PART II—OTHER PROVISIONS

SEC. 345. SMALL BUSINESS CORPORATION STOCK.

(a) INCREASE TO $1,000,000 AMOUNT OF STOCK POTENTIALLY SUBJECT TO ORDINARY LOSS TREATMENT; REMOVAL OF EQUITY CAPITAL TEST.—Subsection (c) of section 1244 (relating to losses on small business stock) is amended by striking out paragraph (2) and inserting in lieu thereof the following:

"(3) SMALL BUSINESS CORPORATION DEFINED.—

"(A) IN GENERAL.—For purposes of this section, a corporation shall be treated as a small business corporation if the aggregate amount of money and other property received by the corporation for stock, as a contribution to capital, and as paid-in surplus, does not exceed $1,000,000. The determination under the preceding sentence shall be made as of the time of the issuance of the stock in question but shall include amounts received for such stock and for all stock theretofore issued.

"(B) AMOUNT TAKEN INTO ACCOUNT WITH RESPECT TO PROPERTY.—For purposes of subparagraph (A), the amount taken into account with respect to any property other than money shall be the amount equal to the adjusted basis to the corporation of such property for determining gain, reduced by any liability to which the property was subject or which was assumed by the corporation. The determination under the preceding sentence shall be made as of the time the property was received by the corporation."

(b) INCREASE IN MAXIMUM AMOUNT TREATED AS ORDINARY LOSS FOR ANY TAXABLE YEAR.—Subsection (b) of section 1244 is amended—

(1) by striking out "$25,000" in paragraph (1) and inserting in lieu thereof "$50,000", and

(2) by striking out "$50,000" in paragraph (2) and inserting in lieu thereof "$100,000".

(c) REMOVAL OF REQUIREMENT THAT STOCK ISSUANCE BE PURSUANT TO PLAN.—Subsection (c) of section 1244 (defining section 1244 stock) is amended by striking out paragraph (1) and inserting in lieu thereof the following new paragraphs:

"(1) IN GENERAL.—For purposes of this section, the term 'section 1244 stock' means common stock in a domestic corporation if—

"(A) at the time such stock is issued, such corporation was a small business corporation,

"(B) such stock was issued by such corporation for money or other property (other than stock and securities), and

"(C) such corporation, during the period of its 5 most recent taxable years ending before the date the loss on such stock was sustained, derived more than 50 percent of its aggregate gross receipts from sources other than royalties, rents, dividends, interests, annuitities, and sales or exchanges of stocks or securities.

"(2) RULES FOR APPLICATION OF PARAGRAPH (1)(C).—

"(A) PERIOD TAKEN INTO ACCOUNT WITH RESPECT TO NEW CORPORATIONS.—For purposes of paragraph (1)(C), if the corporation has not been in existence for 5 taxable years ending before the date the loss on the stock was sustained, there shall be substituted for such 5-year period—

"(i) the period of the corporation's taxable years ending ending before such date, or

"(ii) if the corporation has not been in existence for 1 taxable year ending before such date, the period such corporation has been in existence before such date.

"(B) GROSS RECEIPTS FROM SALES OF SECURITIES.—For purposes of paragraph (1)(C), gross receipts from the sales or exchanges of stock or securities shall be taken into account only to the extent of gains therefrom.

"(C) NONAPPLICATION WHERE DEDUCTIONS EXCEED GROSS INCOME.—Paragraph (1)(C) shall not apply with respect to any corporation if, for the period taken into account for purposes of paragraph (1)(C), the amount of the deductions allowed by this chapter (other than by sections 172, 243, 244, and 245) exceeds the amount of gross income."

(d) TECHNICAL AMENDMENTS.—Paragraph (2) of section 1244(d) (relating to special rules) is amended—

(1) by striking out "subparagraph (E)" and inserting in lieu thereof "subparagraph (C)", and

(2) by striking out "paragraphs (1)(E) and (2)(A)" and inserting in lieu thereof "paragraphs (1)(C) and (3)(A)".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to stock issued after the date of the enactment of this Act.

Subtitle F—Accounting Provisions

SEC. 351. TREATMENT OF CERTAIN CLOSELY HELD FARM CORPORATIONS FOR PURPOSES OF RULE REQUIRING ACCRUAL ACCOUNTING.

(a) GENERAL RULE.—Section 447 (relating to method of accounting for corporations engaged in farming) is amended by adding at the end thereof the following new subsection:

"(h) EXCEPTION FOR CERTAIN CLOSELY HELD CORPORATIONS.—

"(1) IN GENERAL.—This section shall not apply to any corporation if, on October 4, 1976, and at all times thereafter—

"(A) members of 2 families (within the meaning of subsection (d)(1)) have owned (directly or through the application of subsection (d)) at least 65 percent of the total combined voting power of all classes of stock of such corporation entitled to vote, and at least 65 percent of the total number of shares of all other classes of stock of such corporation; or

"(B)(i) members of 3 families (within the meaning of subsection (d)(1)) have owned (directly or through the application of subsection (d)) at least 50 percent of the total combined voting power of all classes of stock of such corporation entitled to vote, and at least 50 percent of the total number of shares of all other classes of stock of such corporation; and

"(ii) substantially all of the stock of such corporation which is not so owned (directly or through the application of subsection (d)) by members of such 3 families is owned directly—

"(I) by employees of the corporation or members of their families (within the meaning of section 267(c)(4)), or

"(II) by a trust for the benefit of the employees of such corporation which is described in section 401(a) and which is exempt from taxation under section 501(a).

"(2) STOCK HELD BY EMPLOYEES, ETC.—For purposes of this subsection, stock which—

"(A) is owned directly by employees of the corporation or members of their families (within the meaing of section 267(c)(4)) or by a trust described in paragraph (1)(B)(ii)(II), and

"(B) was acquired on or after October 4, 1976, from the corporation or from a member of a family which, on October 4, 1976, was described in subparagraph (A) or (B)(i) of paragraph (1),

shall be treated as owned by a member of a family which, on October 4, 1976, was described in subparagraph (A) or (B)(i) of paragraph (1).

"(3) CORPORATION MUST BE ENGAGED IN FARMING.—This subsection shall apply only in the case of a corporation which was, on October 4, 1976, and at all times thereafter, engaged in the trade or business of farming."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1977.

SEC. 352. ACCOUNTING FOR GROWING CROPS.

(a) APPLICATION OF SECTION.—This section shall apply to a taxpayer who—

(1) is a farmer, nurseryman, or florist,

(2) is on an accrual method of accounting, and

(3) is not required by section 447 of the Internal Revenue Code of 1954 to capitalize preproductive period expenses.

(b) TAXPAYER MAY NOT BE REQUIRED TO INVENTORY GROWING CROPS.—A taxpayer to whom this section applies may not be required to inventory growing crops for any taxable year beginning after December 31, 1977.

(c) TAXPAYER MAY ELECT TO CHANGE TO CASH METHOD.—A taxpayer to whom this section applies may, for any taxable year beginning after December 31, 1977, and before January 1, 1981, change to the cash receipts and disbursements method of accounting with respect to any trade or business in which the principal activity is growing crops.

(d) SECTION 481 OF CODE TO APPLY.—Any change in the way in which a taxpayer accounts for the costs of growing crops resulting from the application of subsection (b) or (c)—

(1) shall not require the consent of the Secretary of the Treasury or his delegate, and

(2) shall be treated, for purposes of section 481 of the Internal Revenue Code of 1954, as a change in the method of accounting initiated by the taxpayer.

(e) GROWING CROPS.—For purposes of this section, the term "growing crops" does not include trees grown for lumber, pulp, or other nonlife purposes.

SEC. 353. TREATMENT OF CERTAIN FARMS FOR PURPOSES OF RULE REQUIRING ACCRUAL ACCOUNTING.

(a) GENERAL RULE.—Section 447 (relating to method of accounting for corporations engaged in farming) is amended by striking out "nursery" in subsection (a) thereof and adding in lieu thereof "nursery or sod farm".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1976.

Subtitle G—Other Business Provisions

SEC. 361. DISALLOWANCE OF CERTAIN DEDUCTIONS FOR YACHTS, HUNTING LODGES, ETC.

(a) EXTENSION OF RULE DISALLOWING DEDUCTIONS FOR FACILITIES.—So much of paragraph (1) of section 274(a) (relating to disallowance of certain entertainment, etc., expenses) as follows subparagraph (A) is amended to read as follows:

"(B) FACILITY.—With respect to a facility used in connection with an activity referred to in subparagraph (A).

In the case of an item described in subparagraph (A), the deduction shall in no event exceed the portion of such item which meets the requirements of subparagraph (A).".

(b) COUNTRY CLUBS.—Paragraph (2) of section 274(a) (relating to special rules) is amended by adding at the end thereof the following new subparagraph:

"(C) In the case of a country club, paragraph (1)(B) shall apply unless the taxpayer establishes that the facility was used primarily for the furtherance of the taxpayer's trade or business and that the item was directly related to the active conduct of such trade or business."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to items paid or incurred after December 31, 1978, in taxable years ending after such date.

SEC. 362. DEFICIENCY DIVIDEND PROCEDURE FOR REGULATED INVESTMENT COMPANIES.

(a) GENERAL RULE.—Subchapter M of chapter 1 (relating to regulated investment companies and real estate investment trusts) is amended by adding at the end thereof the following new part:

"PART III—PROVISIONS WHICH APPLY TO BOTH REGULATED INVESTMENT COMPANIES AND REAL ESTATE INVESTMENT TRUSTS

"SEC. 860. DEDUCTION FOR DEFICIENCY DIVIDENDS.

"(a) GENERAL RULE.—If a determination with respect to any qualified investment entity results in any adjustment for any taxable year, a deduction shall be allowed to such entity for the amount of deficiency dividends for purposes of determining the deduction for dividends paid (for purposes of section 852 or 857, whichever applies) for such year.

"(b) QUALIFIED INVESTMENT ENTITY DEFINED.—For purposes of this section, the term 'qualified investment entity' means—

"(1) a regulated investment company, and

"(2) a real estate investment trust.

"(c) RULES FOR APPLICATION OF SECTION.—

"(1) INTEREST AND ADDITIONS TO TAX DETERMINED WITH RESPECT TO THE AMOUNT OF DEFICIENCY DIVIDEND DEDUCTION ALLOWED.—For purposes of determining interest, additions to tax, and additional amounts—

"(A) the tax imposed by this chapter (after taking into account the deduction allowed by subsection (a)) on the qualified investment entity for the taxable year with respect to which the determination is made shall be deemed to be increased by an amount equal to the deduction allowed by subsection (a) with respect to such taxable year,

"(B) the last date prescribed for payment of such increase in tax shall be deemed to have been the last date prescribed for the payment of tax (determined in the manner provided by section 6601(b)) for the taxable year with respect to which the determination is made, and

"(C) such increase in tax shall be deemed to be paid as of the date the claim for the deficiency dividend deduction is filed.

"(2) CREDIT OR REFUND.—If the allowance of a deficiency dividend deduction results in an overpayment of tax for any taxable year, credit or refund with respect to such overpayment shall be made as if on the date of the determination 2 years remained before the expiration of the period of limitations on the filing of claim for refund for the taxable year to which the overpayment relates.

"(d) ADJUSTMENT.—For purposes of this section—

"(1) ADJUSTMENT IN THE CASE OF REGULATED INVESTMENT COMPANY.—In the case of any regulated investment company, the term 'adjustment' means—

"(A) any increase in the investment company taxable income of the regulated investment company (determined without regard to the deduction for dividends paid (as defined in section 561)),

"(B) any increase in the amount of the excess described in section 852(b)(3)(A) (relating to the excess of the net capital gain over the deduction for capital gain dividends paid), and

"(C) any decrease in the deduction for dividends paid (as defined in section 561) determined without regard to capital gains dividends.

"(2) ADJUSTMENT IN THE CASE OF REAL ESTATE INVESTMENT TRUST.—In the case of any real estate investment trust, the term 'adjustment' means—

"(A) any increase in the sum of—

"(i) the real estate investment trust taxable income of the real estate investment trust (determined without regard to the deduction for dividends paid (as defined in section 561) and by excluding any net capital gain), and

"(ii) the excess of the net income from foreclosure property (as defined in section 857(b)(4)(B)) over the tax on such income imposed by section 857(b)(4)(A),

"(B) any increase in the amount of the excess described in section 857(b)(3)(A)(ii) (relating to the excess of the net capital gain over the deduction for capital gains dividends paid), and

"(C) any decrease in the deduction for dividends paid (as defined in section 561) determined without regard to capital gains dividends.

"(e) DETERMINATION.—For purposes of this section, the term 'determination' means—

"(1) a decision by the Tax Court, or a judgment, decree, or other order by any court of competent jurisdiction, which has become final;

"(2) a closing agreement made under section 7121; or

"(3) under regulations prescribed by the Secretary, an agreement signed by the Secretary and by, or on behalf of, the qualified investment entity relating to the liability of such entity for tax.

"(f) DEFICIENCY DIVIDENDS.—

"(1) DEFINITION.—For purposes of this section, the term 'deficiency dividends' means a distribution of property made by the qualified investment entity on or after the date of the determination and before filing claim under subsection (g), which would have been includible in the computation of the deduction for divldends paid under section 561 for the taxable year with respect to which the liability for tax resulting from the determination exists if distributed during such

taxable year. No distribution of property shall be considered as deficiency dividends for purposes of subsection (a) unless distributed within 90 days after the determination, and unless a claim for a deficiency dividend deduction with respect to such distribution is filed pursuant to subsection (g).

"(2) LIMITATIONS.—

"(A) ORDINARY DIVIDENDS.—The amount of deficiency dividends (other than deficiency dividends qualifying as capital gain dividends) paid by a qualified investment entity for the taxable year with respect to which the liability for tax resulting from the determination exists shall not exceed the sum of—

"(i) the excess of the amount of increase referred to in subparagraph (A) of paragraph (1) or (2) of subsection (d) (whichever applies) over the amount of any increase in the deduction for dividends paid computed without regard to capital gain dividends) for such taxable year which results from such determination, and

"(ii) the amount of decrease referred to in subparagraph (C) of paragraph (1) or (2) of subsection (d) (whichever applies).

"(B) CAPITAL GAIN DIVIDENDS.—The amount of deficiency dividends qualifying as capital gain dividends paid by a qualified investment entity for the taxable year with respect to which the liability for tax resulting from the determination exists shall not exceed the amount by which (i) the increase referred to in subparagraph (B) of paragraph (1) or (2) of subsection (d) (whichever applies), exceeds (ii) the amount of any dividends paid during such taxable year which are designated as capital gain dividends after such determination.

"(3) EFFECT ON DIVIDENDS PAID DEDUCTION.—

"(A) FOR TAXABLE YEAR IN WHICH PAID.—Deficiency dividends paid in any taxable year shall not be included in the amount of dividends paid for such year for purposes of computing the dividends paid deduction for such year.

"(B) FOR PRIOR TAXABLE YEAR.—Deficiency dividends paid in any taxable year shall not be allowed for purposes of section 855(a) or 858(a) in the computation of the dividends paid deduction for the taxable year preceding the taxable year in which paid.

"(g) CLAIM REQUIRED.—No deficiency dividend deduction shall be allowed under subsection (a) unless (under regulations prescribed by the Secretary) claim therefor is filed within 120 days after the date of the determination.

"(h) SUSPENSION OF STATUTE OF LIMITATIONS AND STAY OF COLLECTION.—

"(1) SUSPENSION OF RUNNING OF STATUTE.—If the qualified investment entity files a claim as provided in subsection (g), the running of the statute of limitations provided in section 6501 on the making of assessments, and the bringing of distraint or a proceeding in court for collection, in respect of the deficiency established by a determination under this section, and all interest, additions to tax, additional amounts, or assessable penalties in respect thereof, shall be suspended for a period of 2 years after the date of the determination.

"(2) STAY OF COLLECTION.—In the case of any deficiency established by a determination under this section—

"(A) the collection of the deficiency, and all interest, additions to tax, additional amounts, and assessable penalties in respect thereof, shall, except in cases of jeopardy, be stayed until the expiration of 120 days after the date of the determination, and

"(B) if claim for a deficiency dividend deduction is filed under subsection (g), the collection of such part of the deficiency as is not reduced by the deduction for deficiency dividends provided in subsection (a) shall be stayed until the date the claim is disallowed (in whole or in part), and if disallowed in part collection shall be made only with respect to the part disallowed.

No distraint or proceeding in court shall be begun for the collection of an amount the collection of which is stayed under subparagraph (A) or (B) during the period for which the collection of such amount is stayed.

"(i) DEDUCTION DENIED IN CASE OF FRAUD.—No deficiency dividend deduction shall be allowed under subsection (a) if the determination contains a finding that any part of any deficiency attributable to an adjustment with respect to the taxable year is due to fraud with intent to evade tax or to willfull failure to file an income tax return within the time prescribed by law or prescribed by the Secretary in pursuance of law.

"(j) PENALTY.—

"For assessable penalty with respect to liability for tax of a qualified investment entity which is allowed a deduction under subsection (a), see section 6697."

(b) ASSESSABLE PENALTIES.—Section 6697 (relating to assessable penalties with respect to liability for tax of real estate investment trusts) is amended to read as follows:

"SEC. 6697. ASSESSABLE PENALTIES WITH RESPECT TO LIABILITY FOR TAX OF QUALIFIED INVESTMENT ENTITIES.

"(a) CIVIL PENALTY.—In addition to any other penalty provided by law, any qualified investment entity (as defined in section 860(b)) whose tax liability for any taxable year is deemed to be increased pursuant to section 860(c)(1)(A) (relating to interest and additions to tax determined with respect to the amount of the deduction for deficiency dividends allowed) shall pay a penalty in an amount equal to the amount of interest (for which such entity is liable) which is attributable solely to such increase.

"(b) 50-PERCENT LIMITATION.—The penalty payable under this section with respect to any determination shall not exceed one-half of the amount of the deduction allowed by section 860(a) for such taxable year.

"(c) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedure for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a)."

(c) LATE DESIGNATION AND PAYMENT OF CAPITAL GAIN DIVIDEND.—The first sentence of subparagraph (C) of section 852(b)(3) (defining capital gain dividend) is amended by inserting before the period at the end thereof the following: "; except that, if there is an increase in the excess described in subparagraph (A) of this paragraph for such year which results from a determination (as defined in section 860(e)), such designation may be made with respect to such increase at any time before the expiration of 120 days after the date of such determination".

(d) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) Paragraph (3) of section 316(b) (relating to deficiency dividend distributions by a real estate investment trust) is amended—

(A) by striking out "section 859(d)" and inserting in lieu thereof "section 860(f)", and

(B) by striking out "REAL ESTATE INVESTMENT TRUST" in the paragraph heading and inserting in lieu thereof "REGULATED INVESTMENT COMPANY OR REAL ESTATE INVESTMENT TRUST".

(2) Paragraph (25) of section 381(c) is amended—

(A) by striking out "section 859(d)" and inserting in lieu thereof "section 860(f)",

(B) by striking out "section 859" and inserting in lieu thereof "section 860", and

(C) by striking out "REAL ESTATE INVESTMENT TRUST" in the paragraph heading and inserting in lieu thereof "REGULATED INVESTMENT COMPANY OR REAL ESTATE INVESTMENT TRUST".

(3) Subparagraph (C) of section 857(b)(3) is amended by striking out "section 859(c)" and inserting in lieu thereof "section 860(e)".

(4) Sections 6422(14) and 6515(5) are each amended—

(A) by inserting "regulated investment company or" before "real estate investment trust", and

(B) by striking out "859" and inserting in lieu thereof "860".

(5) Paragraph (5) of section 6503(i) is amended to read as follows:

"(5) Deficiency dividends in the case of a regulated investment company or a real estate investment trust, see section 860(h)."

(6) Part II of subchapter M of chapter 1 is amended by striking out section 859 and redesignating section 860 as section 859.

(7) The table of sections for part II of subchapter M of chapter 1 is amended by striking out the items relating to sections 859 and 860 and inserting in lieu thereof the following:

"Sec. 859. Adoption of annual accounting period."

(8) The table of parts for subchapter M of chapter 1 is amended by adding at the end thereof the following new item:

"Part III. Provisions which apply to both regulated investment companies and real estate investment trusts."

(9) The table of sections for subchapter B of chapter 68 is amended by striking out the item relating to section 6697 and inserting in lieu thereof the following:

"Sec. 6697. Assessable penalties with respect to liability for tax of qualified investment entities."

(e) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to determinations (as defined in section 860(d) of the Internal Revenue Code of 1954) after the date of the enactment of this Act.

SEC. 363. REAL ESTATE INVESTMENT TRUST PROVISIONS.

(a) LIMITATIONS.—

(1) Section 856(c)(2) (relating to limitations) is amended by striking out the word "and" at the end of subparagraph (F), by inserting the word "and" at the end of subparagraph (G), and by adding the following new subparagraph at the end thereof:

"(H) gain from the sale or other disposition of a real estate asset which is not a prohibited transaction solely by reason of section 857(b)(6);".

(2) Section 856(c)(3) (relating to limitations) is amended by striking out the word "and" at the end of subparagraph (F), by inserting the word "and" at the end of subparagraph (G), and by adding the following new subparagraph at the end thereof:

"(H) gain from the sale or other disposition of a real estate asset which is not a prohibited transaction solely by reason of section 857(b)(6);".

(3) Subparagraph (B) of section 856(c)(4) (relating to limitations) is amended to read as follows:

"(B) property in a transaction which is a prohibited transaction; and".

(b) PROHIBITED TRANSACTIONS.—Paragraph (6) of section 857(b) (relating to income from prohibited transactions) is amended by adding the following subparagraphs at the end thereof:

"(C) CERTAIN SALES NOT TO CONSTITUTE PROHIBITED TRANSACTIONS.—For purposes of this part, the term 'prohibited transaction' does not include a sale of property which is a real estate asset as defined in section 856(c)(6)(B) if—

"(i) the trust has held the property for not less than 4 years;

"(ii) aggregate expenditures made by the trust, or any partner of the trust, during the 4-year period preceding the date of sale which are includible in the basis of the property do not exceed 20 percent of the net selling price of the property;

"(iii) during the taxable year the trust does not make more than 5 sales of property (other than foreclosure property); and

"(iv) in the case of property, which consists of land or improvements, not acquired through foreclosure (or deed in lieu of foreclosure), or lease termination, the trust has held the property for not less than 4 years for production of rental income.

"(D) SPECIAL RULES.—In applying subparagraph (C) the following special rules apply:

"(i) The holding period of property acquired through foreclosure (or deed in lieu of foreclosure), or termination of the lease, includes the period for which the trust held the loan which such property secured, or the lease of such property.

"(ii) In the case of a property acquired through foreclosure (or deed in lieu of foreclosure), or termination of a lease, expenditures made by, or for the account of, the mortgagor or lessee after default became imminent will be regarded as made by the trust.

"(iii) Expenditures (including expenditures regarded as made directly by the trust, or indirectly by any partner of the trust, under clause (ii)) will not be taken into account if they relate to foreclosure property and did not cause the property to lose its status as foreclosure property.

"(iv) Expenditures will not be taken into account if they are made solely to comply with standards or requirements of any government or governmental authority having relevant jurisdiction, or if they are made to restore the property as a result of losses arising from fire, storm or other casualty.

"(v) *The term 'expenditures' does not include advances on a loan made by the trust.*

"(vi) *The sale of more than one property to one buyer as part of one transaction constitutes one sale.*

"(vii) *The term 'sale' does not include any transaction in which the net selling price is less than $10,000.*

"(E) SALES NOT MEETING REQUIREMENTS.—*In determining whether or not any sale constitutes a 'prohibited transaction' for purposes of subparagraph (A), the fact that such sale does not meet the requirements of subparagraph (C) of this paragraph shall not be taken into account; and such determination, in the case of a sale not meeting such requirements, shall be made as if subparagraphs (C) and (D) had not been enacted.*"

(c) EXTENSIONS.—*Paragraph (3) of section 856(e) (relating to extensions) is amended to read as follows:*

"(3) EXTENSIONS.—*If the real estate investment trust establishes to the satisfaction of the Secretary that an extension of the grace period is necessary for the orderly liquidation of the trust's interests in such property, the Secretary may grant one or more extensions of the grace period for such property. Any such extension shall not extend the grace period beyond the date which is 6 years after the date such trust acquired such property.*"

(d) EFFECTIVE DATE.—*The amendments made by subsections (a) and (b) shall apply to taxable years ending after the date of the enactment of this Act. The amendment made by subsection (c) shall apply to extensions granted after the date of the enactment of this Act with respect to periods beginning after December 31, 1977.*

SEC. 364. CONTRIBUTIONS IN AID OF CONSTRUCTION.

(a) IN GENERAL.—*Section 118(b) (relating to contributions in aid of construction) is amended—*

(1) *by striking out "water" in the portion of paragraph (1) preceding subparagraph (A) thereof and inserting in lieu thereof "electric energy, gas (through a local distribution system or transportation by pipeline), water,";*

(2) *by striking out "water" in paragraph (1)(B) and inserting in lieu thereof "electric energy, gas, steam, water,";*

(3) *by striking out "water" in paragraph (2)(A)(ii) and by inserting in lieu thereof "electric energy, gas, steam, water,";*

(4) *by striking out "property" in paragraph (3)(A) and by inserting in lieu thereof "line" and by striking out "a main water or sewer line" in paragraph (3)(A) and by inserting in lieu thereof "an electric line, a gas main, a steam line, or a main water or sewer line"; and*

(5) *by amending paragraph (3)(C) to read as follows:*

"(C) REGULATED PUBLIC UTILITY.—*The term 'regulated public utility has the meaning given such term by section 7701 (a)(33); except that such term shall not include any such utility which is not required to provide electric energy, gas, water, or sewerage disposal services to members of the general public (including in the case of a gas transmission utility, the provision of gas services by sale for resale to the general public) in its service area.*"

(b) EFFECTIVE DATE.—*The amendments made by this section shall apply to contributions made after January 31, 1976.*

SEC. 365. LIABILITIES OF CONTROLLED CORPORATIONS.

(a) IN GENERAL.—Subsection (c) of section 357 (relating to assumption of liability) is amended by adding at the end thereof the following new paragraph:

"(3) CERTAIN LIABILITIES EXCLUDED.—

"(A) IN GENERAL.—If—

"(i) the taxpayer's taxable income is computed under the cash receipts and disbursements method of accounting, and

"(ii) such taxpayer transfers, in an exchange to which section 351 applies, a liability which is either—

"(I) an account payable payment of which would give rise to a deduction, or

"(II) an amount payable which is described in section 736(a),

then, for purposes of paragraph (1), the amount of such liability shall be excluded in determining the amount of liabilities assumed or to which the property transferred is subject.

"(B) EXCEPTION.—Subparagraph (A) shall not apply to any liability to the extent that the incurrence of the liability resulted in the creation of, or an increase in, the basis of any property."

(b) BASIS OF DISTRIBUTEES.—Subsection (d) of section 358 (relating to basis to distributees) is amended to read as follows:

"(d) ASSUMPTION OF LIABILITY.—

"(1) IN GENERAL.—Where, as part of the consideration to the taxpayer, another party to the exchange assumed a liability of the taxpayer or acquired from the taxpayer property subject to a liability, such assumption or acquisition (in the amount of the liability) shall, for purposes of this section, be treated as money received by the taxpayer on the exchange.

"(2) EXCEPTION.—Paragraph (1) shall not apply to the amount of any liability excluded under section 357(c)(3)."

(c) EFFECTIVE DATE.—The amendments made by subsections (a) and (b) shall apply to transfers occurring on or after the date of the enactment of this Act.

SEC. 366. MEDICAL EXPENSE REIMBURSEMENT PLANS.

(a) GENERAL RULE.—Section 105 (relating to accident and health plans) is amended by adding at the end thereof the following:

"(h) AMOUNT PAID TO HIGHLY COMPENSATED INDIVIDUALS UNDER A DISCRIMINATORY SELF-INSURED MEDICAL EXPENSE REIMBURSEMENT PLAN.—

"(1) IN GENERAL.—In the case of amounts paid to a highly compensated individual under a self-insured medical reimbursement plan which does not satisfy the requirements of paragraph (2) for a plan year, subsection (b) shall not apply to such amounts to the extent they constitute an excess reimbursement of such highly compensated individual.

"(2) PROHIBITION OF DISCRIMINATION.—A self-insured medical reimbursement plan satisfies the requirements of this paragraph only if—

"(A) the plan does not discriminate in favor of highly compensated individuals as to eligibility to participate; and

"(B) the benefits provided under the plan do not discriminate in favor of participants who are highly compensated individuals.

"(3) NONDISCRIMINATORY ELIGIBILITY CLASSIFICATIONS.—

"(A) IN GENERAL.—A self-insured medical reimbursement plan does not satisfy the requirements of subparagraph (A) of paragraph (2) unless such plan benefits—

"(i) 70 percent or more of all employees, or 80 percent or more of all the employees who are eligible to benefit under the plan if 70 percent or more of all employees are eligible to benefit under the plan; or

"(ii) such employees as qualify under a classification set up by the employer and found by the Secretary not to be discriminatory in favor of highly compensated participants.

"(B) EXCLUSION OF CERTAIN EMPLOYEES.—For purposes of subparagraph (A), there may be excluded from consideration—

"(i) employees who have not completed 3 years of service;

"(ii) employees who have not attained age 25;

"(iii) part-time or seasonal employees;

"(iv) employees not included in the plan who are included in a unit of employees covered by an agreement between employee representatives and one or more employers which the Secretary finds to be a collective bargaining agreement, if accident and health benefits were the subject of good faith bargaining between such employee representatives and such employer or employers; and

"(v) employees who are nonresident aliens and who receive no earned income (within the meaning of section 911(b)) from the employer which constitutes income from sources within the United States (within the meaning of section 861(a)(3)).

"(4) NONDISCRIMINATORY BENEFITS.—A self-insured medical reimbursement plan does not meet the requirements of subparagraph (B) of paragraph (2) unless all benefits provided for participants who are highly compensated individuals are provided for all other participants.

"(5) HIGHLY COMPENSATED INDIVIDUAL DEFINED.—For purposes of this subsection, the term 'highly compensated individual' means an individual who is—

"(A) one of the 5 highest paid officers,

"(B) a shareholder who owns (with the application of section 318) more than 10 percent in value of the stock of the employer, or

"(C) among the highest paid 25 percent of all employees (other than employees described in paragraph (3)(B) who are not participants).

"(6) SELF-INSURED MEDICAL REIMBURSEMENT PLAN.—The term 'self-insured medical reimbursement plan' means a plan of an employer to reimburse employees for expenses referred to in subsection (b) for which reimbursement is not provided under a policy of accident and health insurance.

"(7) EXCESS REIMBURSEMENT OF HIGHLY COMPENSATED INDIVIDUAL.—For purposes of this section, the excess reimbursement of a highly compensated individual which is attributable to a self-insured medical reimbursement plan is—

"(A) in the case of a benefit available to a highly compensated individual but not to a broad cross-section of employees, the amount reimbursed under the plan to the employee with respect to such benefit, and

"(B) in the case of benefits (other than benefits described in subparagraph (A) paid to a highly compensated individual by a plan which fails to satisfy the requirements of paragraph (2), the total amount reimbursed to the highly compensated individual for the plan year multiplied by a fraction—

"(i) the numerator of which is the total amount reimbursed to all participants who are highly compensated individuals under the plan for the plan year, and

"(ii) the denominator of which is the total amount reimbursed to all employees under the plan for such plan year.

In determining the fraction under subparagraph (B), there shall not be taken into account any reimbursement which is attributable to a benefit described in subparagraph (A).

"(8) CERTAIN CONTROLLED GROUPS.—All employees who are treated as employed by a single employer under subsection (b) or (c) of section 414 shall be treated as employed by a single employer for purposes of this section.

"(9) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this section.

"(10) TIME OF INCLUSION.—Any amount paid for a plan year that is included in income by reason of this subsection shall be treated as received or accrued in the taxable year of the participant in which the plan year ends."

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1979.

SEC. 367. THREE-YEAR EXTENSION OF PROVISION FOR 60-MONTH DEPRECIATION OF EXPENDITURES TO REHABILITATE LOW-INCOME RENTAL HOUSING.

Subsection (k) of section 167 (relating to depreciation of expenditures to rehabilitate low-income rental housing) is amended by striking out "January 1, 1979" each place it appears and inserting in lieu thereof "January 1, 1982".

SEC. 368. DELAY IN APPLICATION OF NEW NET OPERATING LOSS RULES.

(a) IN GENERAL.—Except as provided in subsection (b), paragraphs (2) and (3) of section 806(g) of the Tax Reform Act of 1976 (relating to effective dates for the amendments to sections 382 and 383 of the Code) are amended by striking out "1978" each place it appears and inserting in lieu thereof "1980".

(b) ELECTION OF PRIOR LAW.—

(1) A taxpayer may elect not to have the amendment made by subsection (a) apply with respect to any acquisition or reorganization occurring before the end of the taxpayer's first taxable year beginning after June 30, 1978, where such acquisition or reorganization occurs pursuant to a written binding contract or option to acquire stock or assets which was entered into before September 27, 1978.

(2) An election under this subsection shall be filed with a taxpayer's timely filed return for the first taxable year in which a reorganization or acquisition described in paragraph (1) occurs, or, if later, within 90 days after the date of enactment of this Act. Such election shall apply to all acquisitions and reorganizations to which, but for such election, subsection (a) would apply.

SEC. 369. USE OF CERTAIN EXPIRED NET OPERATING LOSS CARRYOVERS.

(a) IN GENERAL.—Clause (iv) of section 374(e)(1)(A) (relating to use of expired net operating loss carryovers to offset income arising from certain railroad reorganization proceedings) is amended to read as follows:

> *"(iv) a redemption of a certificate of value of the United States Railway Association issued under section 306 of such Act to such corporation (or issued to another member of the same affiliated group (within the meaning of section 1504) as such corporation for their taxable years which included March 31, 1967),".*

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years ending after March 31, 1976.

SEC. 370. INCOME FROM CERTAIN RAILROAD ROLLING STOCK TREATED AS INCOME FROM SOURCES WITHIN THE UNITED STATES.

(a) GENERAL RULE.—Section 861 (relating to income from sources within the United States) is amended by adding at the end thereof the following new subsection:

"(f) INCOME FROM CERTAIN RAILROAD ROLLING STOCK TREATED AS INCOME FROM SOURCES WITHIN THE UNITED STATES.

"(1) GENERAL RULE.—For purposes of subsection (a) and section 862(a), if—

"(A) a taxpayer leases railroad rolling stock which is section 38 property (or would be section 38 property but for section 48(a)(5)) to a domestic common carrier by railroad or a corporation which is controlled, directly or indirectly, by one or more such common carriers, and

"(B) the use under such lease is expected to be use within the United States,

all amounts includible in gross income by the taxpayer with respect to such railroad rolling stock (including gain from sale or other disposition of such railroad rolling stock) shall be treated as income from sources within the United States. The requirements of subparagraph (B) of the preceding sentence shall be treated as satisfied if the only expected use outside the United States is use by a person (whether or not a United States person) in Canada or Mexico on a temporary basis which is not expected to exceed a total of 90 days in any taxable year.

"(2) PARAGRAPH (1) NOT TO APPLY WHERE LESSOR IS A MEMBER OF CONTROLLED GROUP WHICH INCLUDES A RAILROAD.—Paragraph (1) shall not apply to a lease between two members of the same controlled group of corporations (as defined in section 1563) if any member of such group is a domestic common carrier by railroad or a switching or terminal company referred to in subparagraph (B) of section 184(d)(1).

"(3) DENIAL OF FOREIGN TAX CREDIT.—No credit shall be allowed under section 901 for any payments to foreign countries with respect to any amount received by the taxpayer with respect to railroad rolling stock which is subject to paragraph (1).".

(b) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendment made by subsection (a) shall apply to all railroad rolling stock placed in service with respect to the taxpayer after the date of the enactment of this Act.

(2) ELECTION TO EXTEND SECTION 861 (f) TO RAILROAD ROLLING STOCK PLACED IN SERVICE BEFORE DATE OF ENACTMENT.

(A) IN GENERAL.—At the election of the taxpayer, the amendment made by subsection (a) shall also apply, for taxable years beginning after the date of the enactment of this Act, to all railroad rolling stock placed in service with respect to the taxpayer on or before such date of enactment. Such an election may not be revoked except with the consent of the Secretary of the Treasury or his delegate.

(B) MANNER AND TIME OF ELECTION AND REVOCATION.—An election under subparagraph (A), and any revocation of such an election, shall be made in such manner and at such time as the Secretary of the Treasury or his delegate may by regulations prescribe.

SEC. 371. NET OPERATING LOSSES ATTRIBUTABLE TO PRODUCT LIABILITY LOSSES.

(a) 10-YEAR CARRYBACK.—

(1) IN GENERAL.—Paragraph (1) of section 172(b) (relating to years to which loss may be carried) is amended by adding at the end thereof the following new subparagraph:

"(H) PRODUCT LIABILITY LOSSES.—In the case of a taxpayer which has a product liability loss (as defined in subsection (i)) for a taxable year beginning after September 30, 1979 (referred to in this subparagraph as the 'loss year'), the product liability loss shall be a net operating loss carryback to each of the 10 taxable years preceding the loss year."

(2) CONFORMING AMENDMENT.—Clause (i) of section 172(b)(1)(A) is amended by striking out "and (G)" and inserting in lieu thereof "(G), and (H)".

(b) RULES RELATING TO PRODUCT LIABILITY LOSSES.—Section 172 is amended by redesignating subsection (i) as subsection (j) and by inserting after subsection (h) the following new subsection:

"(i) RULES RELATING TO PRODUCT LIABILITY LOSSES.—For purposes of subsection (b)—

"(1) PRODUCT LIABILITY LOSS.—The term 'product liability loss' means, for any taxable year, the lesser of—

"(A) the net operating loss for such year reduced by any portion thereof which is attributable to a foreign expropriation loss, or

"(B) the sum of the amounts allowable as deductions under sections 162 and 165 which are attributable to—

"(i) product liability, or

"(ii) expenses incurred in the investigation or settlement of, or opposition to, claims against the taxpayer on account of product liability.

"(2) PRODUCT LIABILITY.—The term 'product liability' means—

"(A) liability of the taxpayer for damages on account of physical injury or emotional harm to individuals, or damage to or loss of the use of property, on account of any defect in any product which is manufactured, leased, or sold by the taxpayer, but only if

"(B) such injury, harm, or damage arises after the taxpayer has completed or terminated operations with respect to, and has relinquished possession of, such product.

"(3) ELECTION.—Any taxpayer entitled to a 10-year carryback under subsection (b)(1)(H) from any loss year may elect to have the carryback period with respect to such loss year determined without regard to subsection (b)(1)(H). Such election shall be made in such manner as may be prescribed by the Secretary and shall be made by the due date (including extensions of time) for filing the taxpayer's return for the taxable year of the net operating loss. Such election, once made for any taxable year, shall be irrevocable for that taxable year."

(c) APPLICATION OF ACCUMULATED EARNINGS TAX TO PRODUCT LIABILITY LOSS RESERVES.—Subsection (b) of section 537 (relating to special rules) is amended by redesignating paragraph (4) as paragraph (5) and by inserting after paragraph (3) the following new paragraph:

"(4) PRODUCT LIABILITY LOSS RESERVES.—The accumulation of reasonable amounts for the payment of reasonably anticipated product liability losses (as defined in section 172(i)), as determined under regulations prescribed by the Secretary, shall be treated as accumulated for the reasonably anticipated needs of the business."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxable years beginning after September 30, 1979.

SEC. 372. EXCLUSION FROM GROSS INCOME WITH RESPECT TO MAGAZINES, PAPERBACKS, AND RECORDS RETURNED AFTER THE CLOSE OF THE TAXABLE YEAR.

(a) IN GENERAL.—Subpart B of part II of subchapter E of chapter 1 (relating to taxable year for which items of gross income included) is amended by adding at the end thereof the following new section:

"SEC. 458. MAGAZINES, PAPERBACKS, AND RECORDS RETURNED AFTER THE CLOSE OF THE TAXABLE YEAR.

"(a) EXCLUSION FROM GROSS INCOME.—A taxpayer who is on an accrual method of accounting may elect not to include in the gross income for the taxable year the income attributable to the qualified sale of any magazine, paperback, or record which is returned to the taxpayer before the close of the merchandise return period.

"(b) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) MAGAZINE.—The term 'magazine' includes any other periodical.

"(2) PAPERBACK.—The term 'paperback' means any book which has a flexible outer cover and the pages of which are affixed directly to such outer cover. Such term does not include a magazine.

"(3) RECORD.—The term 'record' means a disc, tape, or similar object on which musical, spoken, or other sounds are recorded.

"(4) SEPARATE APPLICATION WITH RESPECT TO MAGAZINES, PAPERBACKS, AND RECORDS.—If a taxpayer makes qualified sales of more than one category of merchandise in connection with the same

trade or business, this section shall be applied as if the qualified sales of each such category were made in connection with a separate trade or business. For purposes of the preceding sentence, magazines, paperbacks, and records shall each be treated as a separate category of merchandise.

"(5) QUALIFIED SALE.—A sale of a magazine, paperback, or record is a qualified sale if—

"(A) at the time of sale, the taxpayer has a legal obligation to adjust the sales price of such magazine, paperback, or record if it is not resold, and

"(B) the sales price of such magazine, paperback, or record is adjusted by the taxpayer because of a failure to resell it.

"(6) AMOUNT EXCLUDED.—The amount excluded under this section with respect to any qualified sale shall be the lesser of—

"(A) the amount covered by the legal obligation described in paragraph (5)(A), or

"(B) the amount of the adjustment agreed to by the taxpayer before the close of the merchandise return period.

"(7) MERCHANDISE RETURN PERIOD.—

"(A) Except as provided in subparagraph (B), the term 'merchandise return period' means, with respect to any taxable year—

"(i) in the case of magazines, the period of 2 months and 15 days first occurring after the close of taxable year, or

"(ii) in the case of paperbacks and records, the period of 4 months and 15 days first occurring after the close of the taxable year.

"(B) The taxpayer may select a shorter period than the applicable period set forth in subparagraph (A).

"(C) Any change in the merchandise return period shall be treated as a change in the method of accounting.

"(8) CERTAIN EVIDENCE MAY BE SUBSTITUTED FOR PHYSICAL RETURN OF MERCHANDISE.—Under regulations prescribed by the Secretary, the taxpayer may substitute, for the physical return of magazines, paperbacks, or records required by subsection (a), certification or other evidence that the magazine, paperback, or record has not been resold and will not be resold if such evidence—

"(A) is in the possession of the taxpayer at the close of the merchandise return period, and

"(B) is satisfactory to the Secretary.

"(9) REPURCHASE BY THE TAXPAYER NOT TREATED AS RESALE.—A repurchase by the taxpayer shall be treated as an adjustment of the sales price rather than as a resale.

"(c) QUALIFIED SALES TO WHICH SECTION APPLIES.—

"(1) ELECTION OF BENEFITS.—This section shall apply to qualified sales of magazines, paperbacks, or records, as the case may be, if and only if the taxpayer makes an election under this section with respect to the trade or business in connection with which such sales are made. An election under this section may be made without the consent of the Secretary. The election shall be made in such manner as the Secretary may by regulations prescribe and shall be made for any taxable year not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof).

"(2) SCOPE OF ELECTION.—An election made under this section shall apply to all qualified sales of magazines, paperbacks, or records,

as the case may be, made in connection with the trade or business with respect to which the taxpayer has made the election.

"(3) PERIOD TO WHICH ELECTION APPLIES.—An election under this section shall be effective for the taxable year for which it is made and for all subsequent taxable years, unless the taxpayer secures the consent of the Secretary to the revocation of such election.

"(4) TREATMENT AS METHOD OF ACCOUNTING.—Except to the extent inconsistent with the provisions of this section, for purposes of this subtitle, the computation of taxable income under an election made under this section shall be treated as a method of accounting.

"(d) 5-YEAR SPREAD OF TRANSITIONAL ADJUSTMENTS FOR MAGAZINES.—In applying section 481(c) with respect to any election under this section which applies to magazines, the period for taking into account any decrease in taxable income resulting from the application of section 481(a)(2) shall be the taxable year for which the election is made and the 4 succeeding taxable years.

"(e) SUSPENSE ACCOUNT FOR PAPERBACKS AND RECORDS.—

"(1) IN GENERAL.—In the case of any election under this section which applies to paperbacks or records, in lieu of applying section 481, the taxpayer shall establish a suspense account for the trade or business for the taxable year for which the election is made.

"(2) INITIAL OPENING BALANCE.—The opening balance of the account described in paragraph (1) for the first taxable year to which the election applies shall be the largest dollar amount of returned merchandise which would have been taken into account under this section for any of the 3 immediately preceding taxable years if this section had applied to such preceding 3 taxable years. This paragraph and paragraph (3) shall be applied by taking into account only amounts attributable to the trade or business for which such account is established.

"(3) ADJUSTMENTS IN SUSPENSE ACCOUNT.—At the close of each taxable year the suspense account shall be—

"(A) reduced by the excess (if any) of—

"(i) the opening balance of the suspense account for the taxable year, over

"(ii) the amount excluded from gross income for the taxable year under subsection (a), or

"(B) increased (but not in excess of the initial opening balance) by the excess (if any) of—

"(i) the amount excluded from gross income for the taxable year under subsection (a), over

"(ii) the opening balance of the account for the taxable year.

"(4) GROSS INCOME ADJUSTMENTS.—

"(A) REDUCTIONS EXCLUDED FROM GROSS INCOME.—In the case of any reduction under paragraph (3)(A) in the account for the taxable year, an amount equal to such reduction shall be excluded from gross income for such taxable year.

"(B) INCREASES ADDED TO GROSS INCOME.—In the case of any increase under paragraph (3)(B) in the account for the taxable year, an amount equal to such increase shall be included in gross income for such taxable year.

If the initial opening balance exceeds the dollar amount of returned merchandise which would have been taken into account under

subsection (a) for the taxable year preceding the first taxable year for which the election is effective if this section had applied to such preceding taxable year, then an amount equal to the amount of such excess shall be included in gross income for such first taxable year.

"(5) SUBCHAPTER C TRANSACTIONS.—The application of this subsection with respect to a taxpayer which is a party to any transaction with respect to which there is nonrecognition of gain or loss to any party to the transaction by reason of subchapter C shall be determined under regulations prescribed by the Secretary."

(b) CLERICAL AMENDMENTS.—The table of sections for such subpart B is amended by adding at the end thereof the following:

"Sec. 458. Magazines, paperbacks, and records returned after the close of the taxable year."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after September 30, 1979.

SEC. 373. QUALIFIED DISCOUNT COUPONS REDEEMED AFTER CLOSE OF TAXABLE YEAR.

(a) GENERAL RULE.—Subpart C of part II of subchapter E of chapter 1 of the Internal Revenue Code of 1954 (relating to taxable year for which deductions taken) is amended by adding at the end thereof the following new section:

"SEC. 466. QUALIFIED DISCOUNT COUPONS REDEEMED AFTER CLOSE OF TAXABLE YEAR.

"(a) ALLOWANCE OF DEDUCTION.—At the election of a taxpayer whose taxable income is computed under an accural method of accounting, the deduction allowable under this chapter for the redemption costs of qualified discount coupons shall be an amount equal to the sum of—

"(1) such costs incurred by the taxpayer with respect to coupons—

"(A) which were outstanding at the close of the taxable year, and

"(B) which were received by the taxpayer before the close of the redemption period for the taxable year, plus

"(2) such costs (other than costs properly taken into account under paragraph (1) for a prior taxable year) incurred by the taxpayer during the taxable year.

"(b) QUALIFIED DISCOUNT COUPONS.—For purposes of this section—

"(1) IN GENERAL.—The term 'qualified discount coupon' means a discount coupon which—

"(A) was issued by the taxpayer,

"(B) is redeemable by the taxpayer, and

"(C) allows a discount on the purchase price of merchandise or other tangible personal property.

"(2) METHOD OF ISSUANCE NOT TAKEN INTO ACCOUNT.—The determination of whether or not a discount coupon is a qualified discount coupon shall be made without regard to whether the coupon was issued through a newspaper, magazine, or other publication, by mail, on the pack or in the pack of merchandise, or otherwise.

"(3) DISCOUNT ON ITEM CANNOT EXCEED $5.—A coupon shall not be a qualified discount coupon if—

"(A) the face amount of such coupon is more than $5, or

"(B) such coupon may be used with other coupons to bring about a price discount of more than $5 with respect to any item.

"(4) THERE MUST BE REDEMPTION CHAIN.—A coupon shall not be a qualified discount coupon if the issuer directly redeems such coupon from the person using the coupon to receive a price discount. For purposes of the preceding sentence, corporations which are members of the same controlled group of corporations (within the meaning of section 1563(a) as the issurer shall be treated as the issuer.

"(5) REDEEMABLE BY TAXPAYER.—A coupon is redeemable by the taxpayer if the terms of the coupon require the taxpayer to redeem the coupon when presented for redemption in accordance with its terms.

"(c) REDEMPTION COSTS; REDEMPTION PERIOD.—For purposes of this section—

"(1) REDEMPTION COSTS.—The term 'redemption cost' means, with respect to any coupon—

"(A) the lesser of—

"(i) the amount of the discount provided by the terms of the coupon, or

"(ii) the amount incurred by the taxpayer for paying such discount, plus

"(B) the amount incurred by the taxpayer for a payment to the retailer (or other person redeeming the coupon from the person receiving the price discount), but only if the amount so payable is stated on the coupon.

"(2) REDEMPTION PERIOD.—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the redemption period for any taxable year is the 6-month period immediately following the close of the taxable year.

"(B) TAXPAYER MAY SELECT SHORTER PERIOD.— The taxpayer may select a redemption period which is shorter than 6 months.

"(C) CHANGE IN REDEMPTION PERIOD.—Any change in the redemption period shall be treated as a change in the method of accounting.

"(d) QUALIFIED DISCOUNT COUPONS TO WHICH SECTION APPLIES.—

"(1) ELECTION OF BENEFITS.—This section shall apply to qualified discount coupons if and only if the taxpayer makes an election under this section with respect to the trade or business in connection with which such coupons are issued. An election under this section may be made without the consent of the Secretary. The election shall be made in such manner as the Secretary may by regulations prescribe and shall be made for any taxable year not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof).

"(2) SCOPE OF ELECTION.—An election made under this section shall apply to all qualified discount coupons issued in connection with the trade or business with respect to which the taxpayer has made the election.

"(3) PERIOD TO WHICH ELECTION APPLIES.—An election under this section shall apply to the taxable year for which it is made and for all subsequent taxable years, unless the taxpayer secures the consent of the Secretary to the revocation of such election.

"(4) TREATMENT AS METHOD OF ACCOUNTING.—Except to the extent inconsistent with the provisions of this section, for purposes of this subtitle, the computation of taxable income under an election made under this section shall be treated as a method of accounting.

"(e) SUSPENSE ACCOUNT.—

"(1) IN GENERAL.—In the case of any election under this section which (but for this subsection) would result in a net decrease in taxable income under section 481(a)(2), in lieu of applying section 481, the taxpayer shall establish a suspense account for the trade or business for the taxable year for which the election is made.

"(2) INITIAL OPENING BALANCE.—The initial opening balance of the account described in paragraph (1) for the first taxable year to which the election applies shall be the amount by which—

"(A) the largest dollar amount which would have been taken into account under subsection (a)(1) for any of the 3 immediately preceding taxable years if this section had applied to such 3 preceding taxable years, exceeds

"(B) the sum of the increases in income (and the decreases in deductions) which (but for this subsection) would result under section 481(a)(2) for such first taxable years.

This subsection shall be applied by taking into account only amounts attributal to the trade or business for which such account is established.

"(3) ADJUSTMENTS IN SUSPENSE ACCOUNT.—At the close of each taxable year, the suspense account shall be—

"(A) reduced by the excess (if any) of—

"(i) the opening balance of the suspense account for the taxable year, over

"(ii) the amount deducted for the taxable year under subsection (a)(1), or

"(B) increased (but not in excess of the initial opening balance) by the excess (if any) of—

"(i) the amount deducted for the taxable year under subsection (a)(1), over

"(ii) the opening balance of the suspense account for the taxable year.

"(4) INCOME ADJUSTMENTS.—

"(A) REDUCTIONS ALLOWED AS DEDUCTION.—In the case of any reduction under paragraph (3)(A) in the account for the taxable year, an amount equal to such reduction shall be allowed as a deduction for such taxable year.

"(B) INCREASES ADDED TO GROSS INCOME.—In the case of any increase under paragraph (3)(B) in the account for the taxable year, an amount equal to such increase shall be included in gross income for such taxable year.

If the amount described in paragraph (2)(A) exceeds the dollar amount which would have been taken into account under subsection (a)(1) for the taxable year preceding the first taxable year for which thr election is effective if this section had applied to such preceding taxable year, then an amount equal to the amount of such excess shall be included in gross income for such first taxable year.

"(5) SUBCHAPTER C TRANSACTIONS.—The application of this subsection with respect to a taxpayer which is a party to any transaction with respect to which there is nonrecognition of gain or loss to any party to the transaction by reason of subchapter C shall be determined under regulations prescribed by the Secretary.

"(f) 10-YEAR SPREAD OF ANY NET INCREASE IN TAXABLE INCOME UNDER SECTION 481(a)(2).—In the case of any election under this section

which results in a net increase in taxable income under section 481(a)(2), under regulations prescribed by the Secretary, such net increase shall (except as otherwise provided in such regulations) be taken into account by the taxpayer in computing taxable income in each of the 10 taxable years beginning with the year for which the election is made."

(b) CLERICAL AMENDMENT.—The table of sections for such subpart C is amended by adding at the end thereof the following new item:

"Sec. 466. Qualified discount coupons redeemed after close of taxable year."

(C) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by subsections (a) and (b) shall apply to taxable years ending after December 31, 1978.

(2) APPLICATION TO CERTAIN PRIOR TAXABLE YEARS.—

(A) IN GENERAL.—If—

(i) the taxpayer makes an election under section 466 of the Internal Revenue Code of 1954 for his first taxable year ending after December 31, 1978, and

(ii) for a continuous period of 1 or more taxable years each of which ends on or before December 31, 1978, the taxpayer used a method of accounting with respect to any type of discount coupons which was reasonably similar to the method of accounting provided by section 1.451–4 of the Income Tax Regulations,

then the taxpayer may make an election under this paragraph to have the method of accounting which he used for such continuous period treated as a valid method of accounting with respect to each such type of discount coupons for such period for purposes of the Internal Revenue Code of 1954. A taxpayer may make an election under this paragraph with respect to only one such continuous period.

(B) CERTAIN AMOUNTS TO WHICH METHOD OF ACCOUNTING APPLIES.—An accounting method which the taxpayer used for the period described in subparagraph (A) may include—

(i) costs of the type permitted by section 1.451–4 of the Income Tax Regulations to be included in the estimated average cost of redeeming coupons, plus

(ii) any amount designated or referred to on the coupon payable by the taxpayer to the person who allowed the discount on a sale by such person to the user of the coupon.

(C) SUSPENSE ACCOUNT NOT REQUIRED IN CERTAIN CASES.—A taxpayer whose election under this paragraph applies to all types of discount coupons which he issued during the continuous period referred to in subparagraph (A)(ii) shall not be required to establish a suspense account under section 466(e) of the Internal Revenue Code of 1954.

(D) RULES RELATING TO ELECTION UNDER THIS SUBSECTION.—An election under this paragraph may be made only before the expiration of the period for making an election under section 466 of the Internal Revenue Code of 1954 for the taxpayer's first taxable year ending after December 31, 1978. An election under this paragraph shall be made in such a manner and form as the Secretary of the Treasury or his delegate may by regulations prescribe. For purposes of the Internal Revenue Code of 1954, such an election shall be treated as a method of accounting, except that the approval of the Secretary of the Treasury or his delegate to the making of the election may not be required.

TITLE IV—CAPITAL GAINS; MINIMUM TAX; MAXIMUM TAX

Subtitle A—Capital Gains

SEC. 401. REPEAL OF ALTERNATIVE TAX ON CAPITAL GAINS OF INDIVIDUALS.

(a) GENERAL RULE.—Section 1201 (relating to alternative tax) is amended—

(1) by striking out subsections (b) and (c),

(2) by redesignating subsection (d) as subsection (b), and

(3) by amending the section heading to read as follows:

"SEC. 1201. ALTERNATIVE TAX FOR CORPORATIONS.".

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 3(b) is amended by striking out subparagraph (B) and by redesignating subparagraphs (C) and (D) as subparagraphs (B) and (C), respectively.

(2) Subsection (a) of section 5 is amended by striking out paragraph (3) and by redesignating paragraphs (4) and (5) as paragraphs (3) and (4), respectively.

(3) Paragraph (1) of section 871(b) is amended by striking out "section 1, 402(e)(1), or 1201(b)" and inserting in lieu thereof "section 1 or 402(e)(1)".

(4) Paragraph (1) of section 911(d) is amended—

(A) by striking out "section 1 or section 1201" each place it appears and inserting in lieu thereof "section 1", and

(B) by striking out "(whichever is applicable)" each place it appears.

(5) Subsection (b) of section 1304 is amended—

(A) by adding "and" at the end of paragraph (2),

(B) by striking out parargraph (3), and

(C) by redesignating paragraph (4) as paragraph (3).

(6) The table of sections for part I of subchapter P of chapter 1 is amended by striking out the item relating to section 1201 and inserting in lieu thereof the following:

"Sec. 1201. Alternative tax for corporations."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1978.

SEC. 402. INCREASED CAPITAL GAINS DEDUCTION FOR INDIVIDUALS.

(a) GENERAL RULE.— Section 1202 (relating to deduction for capital gains) is amended to read as follows:

"SEC. 1202. DEDUCTION FOR CAPITAL GAINS.

"(a) IN GENERAL.—If for any taxable year a taxpayer other than a corporation has a net capital gain, 60 percent of the amount of the net capital gain shall be a deduction from gross income.

"(b) ESTATES AND TRUSTS.—In the case of an estate or trust, the deduction shall be computed by excluding the portion (if any) of the gains for the taxable year from sales or exchanges of capital assets which, under sections 652 and 662 (relating to inclusions of amounts in gross income of beneficiaries of trusts), is includible by the income beneficiaries as gain derived from the sale or exchange of capital assets.

"(c) TAXABLE YEARS WHICH INCLUDE NOVEMBER 1, 1978.—If for any taxable year beginning before November 1, 1978, and ending after October 31, 1978, a taxpayer other than a corporation has a net capital gain, the deduction under subsection (a) shall be the sum of—

"(1) 60 percent of the lesser of—

"(A) the net capital gain for the taxable year, or

"(B) the net capital gain taking into account only sales and exchanges after October 31, 1978, plus

"(2) 50 percent of the excess of—

"(A) the net capital gain for the taxable year, over

"(B) the amount of net capital gain taken into account under paragraph (1)."

(b) TECHNICAL AMENDMENTS.—

(1) Subparagraph (A) of section 57(a)(9) (relating to treatment of capital gains for purposes of the minimum tax) is amended to read as follows:

"(A) INDIVIDUALS.—In the case of a taxpayer other than a corporation, an amount equal to the net capital gain deduction for the taxable year determined under section 1202."

(2) Subparagraph (B) of section 170(e)(1) (relating to charitable deduction for contributions of capital gain property) is amended by striking out "50 percent" and inserting in lieu thereof "40 percent".

(c) EFFECTIVE DATES.—

(1) The amendments made by subsections (a) and (b)(1) shall apply to taxable years ending after October 31, 1978.

(2) The amendment made by subsection (b)(2) shall apply to contributions made after October 31, 1978.

SEC. 403. REDUCTION OF ALTERNATIVE CAPITAL GAINS TAX FOR CORPORATIONS.

(a) GENERAL RULE.—Paragraph (2) of section 1201(a) (relating to alternative tax for corporations) is amended by striking out "30 percent" and inserting in lieu thereof "28 percent".

(b) TRANSITIONAL RULE.—Section 1201 is amended by adding at the end thereof the following new subsection:

"(c) TAXABLE YEARS WHICH INCLUDE JANAURY 1, 1979.—If for any taxable year beginning before January 1, 1979, and ending after December 31, 1978, a corporation has a net capital gain, then subsection (a) shall be applied by substituting for the language of paragraph (2) the following:

"(2)(A) a tax of 28 percent of the lesser of—

"(i) the net capital gain for the taxable year, or

"(ii) the net capital gain taking into account only sales and exchanges after December 31, 1978, plus

"(B) a tax of 30 percent of the excess of—

"(i) the net capital gains for the taxable year, over

"(ii) the amount of net capital gain taken into account under subparagraph (A)."

(c) CONFORMING AMENDMENTS.—

(1) Subparagraph (B) of section 170(e)(1) (relating to charitable deduction for contributions of capital gain property) is amended by striking out "62½ percent" and inserting in lieu thereof "28/46".

(2) Subparagraph (B) of section 528(b)(2) (relating to tax imposed on certain homeowners associations) is amended to read as follows:

"(B) an amount determined as provided in section 1201(a) on such gain."

(3) Clause (ii) of section 857(b)(3)(A) (relating to tax on real estate investment trusts) is amended by striking out "a tax of 30 percent of" and inserting in lieu thereof "a tax determined at the rate provided in section 1201(a) on".

(4) Subsection (b) of section 904 (relating to taxable income for computing the limitation on foreign tax credits) is amended—

(A) by striking out "three-eights" wherever it appears and inserting in lieu thereof "the rate differential portion"; and

(B) by striking the period at the end of subparagraph (D) of paragraph (3), inserting in lieu thereof a comma, and inserting immediately thereafter the following new paragraph to read as follows:

"(E) RATE DIFFERENTIAL PORTION.—The 'rate differential portion' of foreign source net capital gain, net capital gain, or the excess of net capital gain from sources within the United States over net capital gain, as the case may be, is the same proportion of such amount as the excess of the highest rate of rate of tax specified in section 11(b) over the alternative rate of tax under section 1201(a) bears to the highest rate of tax specified in section 11(b)."

(d) EFFECTIVE DATES.—

(1) The amendments made by subsections (a) and (b) shall apply to taxable years ending after December 31, 1978.

(2) The amendment made by paragraph (1) of subsection (c) shall apply to gifts made after December 31, 1978.

(3) The amendments made by paragraphs (2), (3), and (4) of subsection (c) shall take effect on the date of the enactment of this Act.

SEC. 404. ONE-TIME EXCLUSION OF GAIN FROM SALE OF PRINCIPAL RESIDENCE BY INDIVIDUAL WHO HAS ATTAINED AGE 55.

(a) GENERAL RULE.—The section heading and subsections (a) and (b) of section 121 are amended to read as follows:

"SEC. 121. ONE-TIME EXCLUSION OF GAIN FROM SALE OF PRINCIPAL RESIDENCE BY INDIVIDUAL WHO HAS ATTAINED AGE 55.

"(a) GENERAL RULE.—At the election of the taxpayer, gross income does not include gain from the sale or exchange of property if—

"(1) the taxpayer has attained the age of 55 before the date of such sale or exchange, and

"(2) during the 5-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer as his principal residence for periods aggregating 3 years or more.

"(b) LIMITATIONS.—

"(1) DOLLAR LIMITATION.—The amount of the gain excluded from gross income under subsection (a) shall not exceed $100,000 ($50,000 in the case of a separate return by a married individual).

"(2) APPLICATION TO ONLY 1 SALE OR EXCHANGE.—Subsection (a) shall not apply to any sale or exchange by the taxpayer if an election by the taxpayer or his spouse under subsection (a) with respect to any other sale or exchange is in effect.

"(3) ADDITIONAL ELECTION IF PRIOR SALE WAS MADE ON OR BEFORE JULY 26, 1978.—In the case of any sale or exchange after July 26, 1978, this section shall be applied by not taking into account any election made with respect to a sale or exchange on or before such date."

(b) TACKING OF HOLDING PERIOD IN CASE OF INVOLUNTARY CONVERSIONS.—Subsection (d) of section 121 (relating to special rules) is amended by adding at the end thereof the following new paragraph:

"(8) PROPERTY ACQUIRED AFTER INVOLUNTARY CONVERSION.—If the basis of the property sold or exchanged is determined (in whole or in part) under subsection (b) of section 1033 (relating to basis of property acquired through involuntary conversion), then the holding and use by the taxpayer of the converted property shall be treated as holding and use by the taxpayer of the property sold or exchanged."

(c) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) Paragraph (2) of section 121(d) is amended by striking out "8-year period" and inserting in lieu thereof "5-year period".

(2) Paragraph (5) of section 121(d) is amended—

(A) by striking out "8-year period" and inserting in lieu thereof "5-year period", and

(B) by striking out "5 years" and inserting in lieu thereof "3 years".

(3) The table of sections for part III of subchapter B of chapter 1 is amended by striking out the item relating to section 121 and inserting in lieu thereof the following:

"Sec. 121. One-time exclusion of gain from sale of principal residence by individual who has attained age 55."

(4) Paragraph (3) of section 1033(g) (relating to cross references) is amended to read as follows:

"(3) For one-time exclusion from gross income of gain from involuntary conversion of principal residence by individual who has attained age 55, see section 121."

(5) Subsection (k) of section 1034 (relating to cross references) is amended to read as follows:

"(k) CROSS REFERENCE.—

"For one-time exclusion from gross income of gain from sale of principal residence by individual who has attained age 55, see section 121."

(6) Section 1038(e)(1)(A) is amended by striking out "relating to gain from sale or exchange of residence of an individual who has attained age 65" and inserting in lieu thereof "relating to one-time exclusion of gain from sale of principal residence by individual who has attained age 55".

(7) Section 1250(d)(7)(B) is amended by striking out "relating to gains from sale or exchange of residence of individual who has attained the age of 65" and inserting in lieu thereof "relating to one-time exclusion of gain from sale of principal residence by individual who has attained age 55".

(8) Section 6012(c) is amended by striking out "relating to sale of residence by individual who has attained age 65" and inserting in lieu thereof "relating to one-time exclusion of gain from sale of principal residence by individual who has attained age 55".

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to sales or exchanges after July 26, 1978, in taxable years ending after such date.

(2) TRANSITIONAL RULE.—In the case of a sale or exchange of a residence before July 26, 1981, a taxpayer who has attained age 65 on the date of such sale or exchange may elect to have section 121 of the Internal Revenue Code of 1954 applied by substituting "8-year period" for "5-year period" and "5 years" for "3 years" in subsections (a), (d)(2), and (d)(5) of such section.

SEC. 405. WAIVER OF CERTAIN 18-MONTH RULES OF SECTION 1034 WHEN SALE OF RESIDENCE IS CONNECTED WITH COMMENCING WORK AT NEW PLACE.

(a) IN GENERAL.—Subsection (d) of section 1034 (relating to sale or exchange of residence) is amended to read as follows:

"(d) LIMITATION.—

"(1) IN GENERAL.—Subsection (a) shall not apply with respect to the sale of the taxpayer's residence if within 18 months before the date of such sale the taxpayer sold at a gain other property used by him as his principal residence, and any part of such gain was not recognized by reason of subsection (a).

"(2) SUBSEQUENT SALE CONNECTED WITH COMMENCING WORK AT NEW PLACE.—Paragraph (1) shall not apply with respect to the sale of the taxpayer's residence if—

"(A) such sale was in connection with the commencement of work by the taxpayer as an employee or as a self-employed individual at a new principal place of work, and

"(B) if the residence so sold is treated as the former residence for purposes of section 217 (relating to moving expenses), the taxpayer would satisfy the conditions of subsection (c) of section 217 (as modified by the other subsections of such section)."

(b) RELATED TECHNICAL AMENDMENT.—Paragraph (4) of section 1034(c) is amended by adding at the end thereof the following new sentence: "If a principal residence is sold in a sale to which subsection (d)(2) applies within 18 months after the sale of the old residence, for purposes of applying the preceding sentence with respect to the old residence, the principal residence so sold shall be treated as the last residence used during such 18-month period."

(c) CLERICAL AMENDMENTS.—

(1) The section heading of section 1034 is amended to read as follows:

"SEC. 1034. ROLLOVER OF GAIN ON SALE OF PRINCIPAL RESIDENCE."

(2) The table of sections for part III of subchapter O of chapter 1 is amended by striking out the item relating to section 1034 and inserting in lieu thereof the following new item:

"Sec. 1034. Rollover of gain on sale of principal residence."

(3) Subparagraph (B) of section 1038(e)(1) (relating to certain acquisitions of real property) is amended by striking out "(relating to sale or exchange of residence)" and inserting in lieu thereof "(relating to rollover of gain on sale of principal residence)".

(4) Subparagraph (A) of section 1250(d)(7) (relating to gain from dispositions of certain depreciable realty) is amended by striking out "relating to sale or exchange of residence" and inserting in lieu thereof "relating to rollover of gain on sale of principal residence".

(5) Subparagraph (C) of section 6212(c)(2) (relating to cross references) is amended by striking out "**personal residence**" and inserting in lieu thereof "**principal residence**".

(6) Paragraph (4) of section 6504 (relating to cross references) is amended by striking out "**residence**" and inserting in lieu thereof "**principal residence**".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to sales and exchanges of residences after July 26, 1978, in taxable years ending after such date.

Subtitle B—Minimum Tax Provisions

SEC. 421. ALTERNATIVE MINIMUM TAX FOR TAXPAYERS OTHER THAN CORPORATIONS.

(a) IN GENERAL.—Part VI of subchapter A of chapter 1 (relating to minimum tax for tax preferences) is amended by inserting immediately before section 56 the following new section:

"SEC. 55. ALTERNATIVE MINIMUM TAX FOR TAXPAYERS OTHER THAN CORPORATIONS.

"(a) ALTERNATIVE MINIMUM TAX IMPOSED.—In the case of a taxpayer other than a corporation, if—

"(1) an amount equal to the sum of—

"(A) 10 percent of so much of the alternative minimum taxable income as exceeds $20,000 but does not exceed $60,000, plus

"(B) 20 percent of so much of the alternative minimum taxable income as exceeds $60,000 but does not exceed $100,000, plus

"(C) 25 percent of so much of the alternative minimum taxable income as exceeds $100,000, exceeds

"(2) the regular tax for the taxable year, then there is imposed (in addition to all other taxes imposed by this title) a tax equal to the amount of such excess.

"(b) DEFINITIONS.—For purposes of this section—

"(1) ALTERNATIVE MINIMUM TAXABLE INCOME.—The term 'alternative minimum taxable income' means gross income—

"(A) reduced by the sum of the deductions allowed for the taxable year,

"(B) reduced by the sum of any amounts included in income under section 667, and

"(C) increased by an amount equal to the sum of the tax preference items for—

"(i) adjusted itemized deductions (within the meaning of section 57(a)(1)), and

"(ii) capital gains (within the meaning of section 57(a)(9)).

"(2) REGULAR TAX.—The term 'regular tax' means the taxes imposed by this chapter for the taxable year (computed without regard to this section and without regard to the taxes imposed by sections 72(m)(5)(B), 402(e), 408(f), and 667(b)) reduced by the sum of the credits allowable under subpart A of part IV of this subchapter (other than under sections 31, 39 and 43).

"(c) CREDITS.—

"(1) CREDITS OTHER THAN THE FOREIGN TAX CREDIT NOT ALLOWABLE.—For purposes of determining the amount of any credit allowable under subpart A of part IV of this subchapter (other than the foreign tax credit allowed under section 33(a)), the tax imposed by this section shall not be treated as a tax imposed by this chapter.

"(2) FOREIGN TAX CREDIT ALLOWED AGAINST ALTERNATIVE MINIMUM TAX.—The total amount of the foreign tax credit which can be taken against the tax imposed by subsection (a) shall be determined under section 901 and sections 903 through 908. For purposes of this determination—

"(A) the amount of taxes paid or accrued to foreign countries or possessions of the United States in the taxable year shall be deemed to include an amount equal to the lesser of (i) the foreign tax credit allowed under section 33(a) in computing the regular tax for the taxable year, or (ii) the tax imposed under subsection (a);

"(B) the limitation of section 904(a) shall be an amount equal to the same proportion of the sum of the tax imposed by this section against which such credit is taken and the regular tax (excluding the tax imposed by section 56) which the taxpayer's alternative minimum taxable income from sources without the United States (but not in excess of the taxpayer's entire alternative minimum taxable income) bears to his entire alternative minimum taxable income for the same taxable year. For purposes of the preceding sentence, the entire alternative minimum taxable income shall be reduced by an amount equal to the zero bracket amount;

"(C) the term 'alternative minimum taxable income from sources without United States' means the excess of the items of gross income from sources without the United States over that portion of the deductions taken into account in computing alternative minimum taxable income which are deducted from those items of gross income in computing taxable income from sources without the United States; for purposes of this subparagraph, and except as provided in section 904, gross and taxable income from sources without the United States shall be determined under part I of subchapter N of chapter 1; and

"(D) the amount of foreign taxes paid during the taxable year which may be deemed to be paid in a preceding or succeeding year under section 904 (c), the limitation of section 904 (a) shall be increased by the lesser of (i) the amount described in subparagraph (B) or (ii) the tax imposed under subsection (a).

"(3) CARRYOVER AND CARRYBACK OF CERTAIN CREDITS.—In any taxable year in which a tax is imposed by this section (referred to as the current taxable year)—

"(A) EMPLOYMENT CREDIT.—For purposes of determining under section 53(c) the amount of any jobs credit carryback or carryover to any other taxable year, the amount of the limitation under section 53(a) for the current taxable year shall be deemed to be—

"(i) the amount of the credit allowable under section 44B for the current taxable year without regard to this subparagraph, reduced by

"(ii) the amount equal to the lesser of (I) the amount of the credit allowable under section 44B for the current taxable year without regard to this subparagraph, or (II) the net tax imposed by this section for the current taxable year.

"(B) WORK INCENTIVE PROGRAM CREDIT.—For purposes of determining under section 50A(b) the amount of any work incentive program credit carryback or carryover to any other taxable year, the amount of the limitation under section 50A(a)(2) for the current taxable year shall be deemed to be—

"(i) the amount of the credit allowable under section 40 for the current taxable year without regard to this subparagraph, reduced by

"(ii) the amount equal to the lesser of (I) the amount of the credit allowable under section 40 for the current taxable year without regard to this subparagraph, or, (II) the net tax imposed by this section for the current taxable year reduced by the amount of reduction described in clause (ii) of subparagraph (A).

"(C) INVESTMENT CREDIT.—For purposes of determining under section 46(b) the amount of any investment credit carryback or carryover to any other taxable year, the amount of the limitation under section 46(a)(3) for the current taxable year shall be deemed to be

"(i) the amount of the credit allowable under section 38 for the current taxable year without regard to this subparagraph, reduced by

"(ii) the amount equal to the lesser of (I) the amount of the credit allowable under section 38 for the current taxable year without regard to this subparagraph, or (II) the net tax imposed by this section for the current taxable year reduced by the sum of the amounts of reduction described in clause (ii) of subparagraphs (A) and (B).

"(D) NET TAX IMPOSED BY THIS SECTION.—For purposes of this paragraph, the term 'net tax imposed by this section' means the tax imposed by this section reduced by the foreign tax credit allowed under section 33(a), as modified by paragraph (2).

(b) AMENDMENT OF SECTION 57.—Section 57 (relating to items of tax preference) is amended—

(1) by adding the following at the end of paragraph (9) of subsection (a):

"(D) PRINCIPAL RESIDENCE.—For purposes of subparagraph (A), gain from the sale or exchange of a principal residence (within the meaning of section 1034) shall not be taken into account.",

(2) by striking out the last sentence of subsection (a) and inserting in lieu thereof the following: "Paragraphs (3) and (11) shall not apply to a corporation other than an electing small business corporation (as defined in section 1371(b)) and a personal holding company (as defined in section 542). For purposes of section 56, in the case of a taxpayer other than a corporation, the adjusted itemized deductions described in paragraph (1) and capital gains described in paragraph (9) shall not be treated as items of tax preference."

(3) by striking out subsection (b)(1) and inserting the following in lieu thereof:

"(1) IN GENERAL.—For purposes of paragraph (1) of subsection (a), the amount of the adjusted itemized deductions for any taxable year is the amount by which the sum of the itemized deductions (as defined in section 63(f)) other than—

"(A) the deduction for State and local taxes provided by section 164(a),

"(B) the deduction for medical, dental, etc., expenses provided by section 213,

"(C) the deduction for casualty losses described in section 165(c)(3), and

"(D) the deduction allowable under section 691(c),

exceeds 60 percent of the taxpayer's adjusted gross income reduced by the items in subparagraphs (A) through (D) for the taxable year.", and

(4) by striking out subparagraph (A) of subsection (b)(2), as amended by section 701 of this Act, and inserting in lieu thereof the following:

"(A) IN GENERAL.—In the case of an estate or trust, for purposes of paragraph (1) of subsection (a), the amount of the adjusted itemized deductions for any taxable year is the amount by which the sum of the deductions for the taxable year other than—

"(i) the deductions allowable in arriving at adjusted gross income,

"(ii) the deduction for personal exemption provided by section 642(b),

"(iii) the deduction for casualty losses described in section 165(c)(3),

"(iv) the deductions allowable under section 651(a), 661(a), or 691(c),

"(v) the deduction for State and local taxes provided by section 164(a), and

"(vi) the deductions allowable to a trust under section 642(c) to the extent that a corresponding amount is included in the gross income of the beneficiary under section 662(a)(1) for the taxable year of the beneficiary with which or within which the taxable year of the trust ends,

exceeds 60 percent of the adjusted gross income reduced by the items in clauses (i) through (vi) for the taxable year."

(c) AMENDMENTS OF SECTION 58.—Section 58 (relating to rules for application of part) is amended—

(1) by adding at the end of subsection (a) the following new sentence: "In the case of a married individual who files a separate return for the taxable year, the amount determined under paragraph (1) of section 55(a) shall be an amount equal to one-half of the amount which would be determined under such paragraph if the amount of the individual's alternative minimum taxable income were multiplied by 2.";

(2) by amending subsection (c) to read as follows:

"(c) ESTATES AND TRUSTS.—In the case of an estate or trust—

"(1) the sum of the items of tax preference for any taxable year of the estate or trust shall be apportioned between the estate or trust and the beneficiaries on the basis of the income of the estate or trust allocable to each,

"(2) the $10,000 amount specified in section 56 applicable to such estate or trust shall be reduced to an amount which bears the same ratio to $10,000 as the portion of the sum of the items of tax preference allocated to the estate or trust under paragraph (1) bears to such sum, and

"(3) the liability for the tax imposed by section 55 (a) shall be determined as in the case of a married individual filing separately.", and

(3) by deleting subsection (i) (relating to the definition of corporation).

(d) TAXES TAKEN INTO ACCOUNT IN CASE OF ACCUMULATION DISTRIBUTIONS BY TRUSTS.—The second sentence of section 666(b) (relating to total taxes deemed distributed) is amended by striking out "taxes" and inserting in lieu thereof "taxes (other than the tax imposed by section 55)".

(e) TECHNICAL AMENDMENTS.—

(1) Paragraph (4) of section (5)(a) (as redesignated by section 401 to this Act) (relating to cross references relating to tax on individuals) is amended to read as follows:

"(4) For minimum tax for taxpayers other than corporations, see section 55.".

(2) Subsection (d) of section 443 (relating to adjustment in computing minimum tax for short periods) is amended to read as follows:

"(d) ADJUSTMENT IN COMPUTING MINIMUM TAX FOR TAX PREFERENCES.—If a return is made for a short period by reason of subsection (a), then—

"(1) in the case of a taxpayer other than a corporation, the alternative minimum taxable income for the short period shall be placed on an annual basis by multiplying that amount by 12 and dividing the result by the number of months in the short period, and the amount computed under paragraph (1) of section 55(a) shall be the same part of the tax computed on the annual basis as the number of months in the short period is of 12 months; and

"(2) in the case of a corporation, the $10,000 amount specified in section 56 (relating to minimum tax for tax preferences), modified as provided by section 58, shall be reduced to the amount which bears the same ratio to such specified amount as the number of days in the short period bears to 365.".

(3) Subsection (d) of section 511 (relating to tax preferences) is amended to read as follows:

"(d) TAX PREFERENCES. —

"(1) ORGANIZATIONS TAXABLE AT CORPORATE RATES.—If an organization is subject to tax on unrelated business taxable income pursuant to subsection (a), the tax imposed by section 56 shall apply to such organizations with respect to items of tax preference which enter into the computation of unrelated business taxable income in the same manner as section 56 applies to corporations.

"(2) ORGANIZATIONS TAXABLE AS TRUSTS —If an organization is subject to tax on unrelated business taxable income pursuant to subsection (b), the taxes imposed by section 55 and section 56 (as the case may be) shall apply to such organization with respect to items of tax preference which enter into the computation of unrelated business taxable income."

(4) Paragraph (1) of section 871(b) (relating to tax on nonresident alien individuals) is amended by inserting ", section 55," after "section 1".

(5) Subsection (b) of section 877 (relating to expatriation to avoid tax) is amended by inserting ", section 55," after "section 1".

(6) Section 904(h) (relating to cross references) is amended to read as follows:

"(h) CROSS REFERENCES.—

"(1) For increase of limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States shareholder with respect to a controlled foreign corporation, see section 960(b).

"(2) For modification of limitation under subsection (a) for purposes of determining the amount of credit which can be taken by an individual against the alternative minimum tax, see section 55(c).".

(7) Paragraph (1) of section 6015(c) (defining estimated tax) is amended by striking out "section 56" and inserting in lieu thereof "section 55 or 56".

(8) Subparagraph (A) of section 6362(b) (relating to qualified individual income taxes) is amended by striking out "section 56" and inserting in lieu thereof "section 55 or 56".

(f) CLERICAL AMENDMENT.—The table of sections for part VI of subchapter A of chapter 1 is amended by adding at the beginning thereof the following new item:

(9) Paragraph (1) of section 6654(f) (relating to tax computed after applications of credit against tax) is amended by striking out "section 56" and inserting in lieu thereof "section 55 or 56".

"SEC. 55. Alternative Minimum Tax for Taxpayers other than Corporations."

(g) EFFECTIVE DATE.—The amendments made by this section shal apply to taxable years beginning after December 31, 1978, except that the amendment made by paragraph (1) of subsection (b) shall apply to sales and exchanges made after July 26, 1978, in taxable years ending after such date.

SEC. 422. TREATMENT OF INTANGIBLE DRILLING COSTS FOR PURPOSES OF THE MINIMUM TAX.

Subsection (b) of section 308 of the Tax Reduction and Simplification Act of 1977 is amended by striking out ", and before January 1, 1978".

SEC. 423. AMENDMENT TO DEFINITION OF FOREIGN SOURCE CAPITAL GAIN TAX PREFERENCES.

(a) GENERAL RULE.—Section 58(g)(2) (relating to capital gains and stock options) is amended by striking out the period at the end of the last sentence thereof, and inserting the following:

"; except that, for purposes of subparagraph (B), preferential treatment shall be deemed not to be accorded to capital gain recognized on the receipt of property (other than money) in exchange for stock of a corporation which is engaged in the active conduct of a trade or business within one or more foreign countries or possessions if (i) such exchange is described in section 332, 351, 354, 355, 356 or 361, (ii) such exchange is made in the foreign country or possession in which such corporation's business is primarily carried

on, (iii) such exchange is not subject to tax by such foreign country or possession because it is regarded under the laws of such country or possession as a transaction in which gain or loss is either not realized or not recognized, and (iv) such gain, if it had been realized and recognized under the laws of such country or possession, would not have been accorded preferential treatment and would have been subject to tax at a rate of at least 28 percent (30 percent if the exchange occurs before January 1, 1979). For purposes of computing the minimum tax, if any, which may be payable on a subsequent transaction involving any property received upon the exchange of stock described in the preceding sentence, the property received shall be treated as having the same basis in the taxpayer's hands immediately after such exchange as such stock had immediately before such exchange."

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act.

Subtitle C—Maximum Tax Provisions

SEC. 441. TREATMENT OF CAPITAL GAINS FOR PURPOSES OF THE MAXIMUM TAX.

(a) GENERAL RULE.—Subparagraph (B) of section 1348(b)(2) (relating to definition of personal service income) is amended by striking out "items of tax preference (as defined in section 57)" and inserting in lieu thereof "items of tax preference described in subsection (a) (other than paragraph (9)) of section 57".

(b) EFFECTIVE DATE.—

(1) GENERAL RULE.—The amendment made by subsection (a) shall apply with respect to taxable years beginning after October 31, 1978.

(2) TRANSITIONAL RULES.—In the case of a taxable year which begins before November 1, 1978, and ends after October 31, 1978, the amendment made by subsection (a) shall apply with respect to so much of the net capital gain of the taxpayer for the taxable year as is attributed to sales or exchanges after October 31, 1978

SEC. 442. DETERMINATION OF PERSONAL SERVICE INCOME FROM NONSALARIED TRADE OR BUSINESS ACTIVITIES.

(a) IN GENERAL.—Subparagraph (A) of section 1348(b)(1) (relating to personal service income) is amended by adding at the end thereof the following: "For purposes of this subparagraph, section 911(b) shall be applied without regard to the phrase ', not in excess of 30 percent of his share of the net profits of such trade or business,'."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1978.

TITLE V—OTHER TAX PROVISIONS

Subtitle A—Administrative Provisions

SEC. 501. REPORTING REQUIREMENTS WITH RESPECT TO CHARGED TIPS.

(a) RECORDS.—Section 6001 (relating to notice or regulations requiring records, statements, and special returns) is amended by adding at the end thereof the following: "The only records which an employer shall be

required to keep under this section in connection with charged tips shall be charge receipts and copies of statements furnished by employees under section 6053(a).''

(b) RETURNS.—Section 6041 (relating to information at source) is amended by redesignating subsection (d) as subsection (c) and by adding at the end thereof the following new subsection:

''(d) SECTION DOES NOT APPLY TO CERTAIN TIPS.—This section shall not apply to tips with respect to which section 6053(a) (relating to reporting of tips) applies.''

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to payments made after December 31, 1978.

SEC. 502. EXTENSION OF OPTIONAL SMALL TAX CASE PROCEDURES AND EXPANSION OF AUTHORITY OF COMMISSIONERS OF TAX COURT.

(a) EXTENDING THE OPTIONAL SMALL TAX CASE PROCEDURES TO ADDITIONAL TAXPAYERS.—

(1) IN GENERAL.—Subsection (a) of section 7463 (relating to small tax cases) is amended by striking out paragraphs (1) and (2) and inserting in lieu thereof the following:

''(1) $5,000 for any one taxable year, in the case of the taxes imposed by subtitle A,

''(2) $5,000, in the case of the tax imposed by chapter 11, or

''(3) $5,000 for any one calendar year, in the case of the tax imposed by chapter 12,''.

(2) CONFORMING AMENDMENTS.—

*(A) The heading of section 7463 is amended by striking out **''$1,500''** and inserting in lieu thereof **''$5,000.''***

*(B) The table of sections for part II of subchapter C of chapter 76 is amended by striking out **''$1,500''** in the item relating to section 7463 and inserting in lieu thereof ''$5,000''.*

(b) AUTHORITY TO ASSIGN SMALL TAX CASES TO COMMISSIONERS.—Section 7463 (relating to small tax cases) is amended by adding at the end thereof the following new subsection:

''(g) COMMISSIONERS.—The chief judge of the Tax Court may assign proceedings conducted under this section to be heard by the commissioners of the court, and the court may authorize a commissioner to make the decision of the court with respect to any such proceeding, subject to such conditions and review as the court may by rule provide.''

(c) AUTHORITY OF TAX COURT COMMISSIONERS TO ADMINISTER OATHS, PROCURE TESTIMONY, ETC.—Subsection (a) of section 7456 (relating to the administration of oaths and testimony) is amended—

(1) by striking out ''any judge of the Tax Court'' each place it appears and inserting in lieu thereof ''any judge or commissioner of the Tax Court''; and

(2) by striking out ''by the judge'' and inserting in lieu thereof ''by the judge or commissioner''.

(d) EFFECTIVE DATES.—

(1) SUBSECTION (a).—The amendments made by subsection (a) shall take effect on the first day of the first calendar month beginning more than 180 days after the date of the enactment of this Act.

(2) SUBSECTIONS (b) AND (c).—The amendments made by subsection (b) and (c) shall take effect on the date of the enactment of this Act.

SEC. 503. DISCLOSURE OF RETURN INFORMATION TO CERTAIN FEDERAL OFFICERS AND EMPLOYEES FOR PURPOSES OF TAX ADMINISTRATION, ETC.

(a) IN GENERAL.—Paragraph (2) of section 6103(h) (relating to Department of Justice) is amended—

(1) by striking out "A" after the heading, and inserting in lieu thereof "In a matter involving tax administration, a",

(2) by striking out "attorneys" after "open to inspection by or disclosure to", in paragraph (2) and inserting in lieu thereof "officers and employees",

(3) by inserting "any proceeding before a Federal grand jury or" before "preparation for any proceeding" in paragraph (2).

(4) by striking out "in a matter involving tax administration" after "or any Federal or State court".

(b) APPLICATION TO TAXPAYER.—

(1) Section 6103(h)(2) is amended by striking out subparagraph (A) and inserting in lieu thereof the following:

"(A) the taxpayer is or may be a party to the proceeding, or the proceeding arose out of, or in connection with, determining the taxpayer's civil or criminal liability, or the collection of such civil liability in respect of any tax imposed under this title;".

(2) Section 6103(h)(4) is amended by striking out subparagraph (A) and inserting in lieu thereof the following:

"(A) the taxpayer is a party to the proceeding, or the proceeding arose out of, or in connection with, determining the taxpayer's civil or criminal liability, or the collection of such civil liability, in respect of any tax imposed under this title;".

SEC. 504. REFUND ADJUSTMENTS FOR AMOUNTS HELD UNDER CLAIM OF RIGHT.

(a) IN GENERAL.—Section 6411 (relating to application for adjustment) is amended by adding at the end thereof the following new subsection:

"(d) TENTATIVE REFUND OF TAX UNDER CLAIM OF RIGHT ADJUSTMENT.—

"(1) APPLICATION.—A taxpayer may file an application for a tentative refund of any amount treated as an overpayment of tax for the taxable year under section 1341(b)(1). Such application shall be in such manner and form as the Secretary may prescribe by regulation and shall—

"(A) be verified in the same manner as an application under subsection (a),

"(B) be filed during the period beginning on the date of filing the return for such taxable year and ending on the date 12 months from the last day of such taxable year, and

"(C) set forth in such detail and with such supporting data as such regulations prescribe—

"(i) the amount of the tax for such taxable year computed without regard to the deduction described in section 1341(a)(2).

"(ii) the amount of the tax for all prior taxable years for which the decrease in tax provided in section 1341(a)(5)(B) was computed,

"(iii) the amount determined under section 1341(a)(5)(B),

"(iv) the amount of the overpayment determined under section 1341(b)(1); and

"(v) such other information as the Secretary may require.

"(2) ALLOWANCE OF ADJUSTMENTS.—Within a period of 90 days from the date on which an application is filed under paragraph (1), or from the last day of the month in which falls the last date prescribed by law (including any extension of time granted the taxpayer) for filing the return for taxable year in which the overpayment occurs, whichever is later, the Secretary shall—

"(A) review the application,

"(B) determine the amount of the overpayment, and

"(C) apply, credit, or refund such overpayment in a manner similar to the manner provided in subsection (b).

"(3) CONSOLIDATED RETURNS.—The provisions of subsection (c) shall apply to an adjustment under this subsection to the same extent and manner as the Secretary may by regulations provide.".

(b) TECHNICAL AND CONFORMING AMENDMENTS.—

(1)(A) The heading for section 6411 is amended by inserting "AND REFUND" after "CARRYBACK".

(B) The table of sections for subchapter B of chapter 65 is amended by inserting "and refund" after "carryback" in the item relating to section 6411.

(2) Paragraph (3) of section 6213(b) (relating to assessments arising out of tentative carryback adjustments) is amended—

(A) by inserting "or refund" after "carryback" in the heading; and

(B) by inserting "or the amount described in section 1341(b)(1)" after "carryback".

(3) Subsection (m) of section 6501 (relating to tentative carryback adjustment period) is amended by inserting "and refund" after "carryback" the first place it appears.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to tentative refund claims filed on and after the date of the enactment of this Act.

Subtitle B—Estate and Gift Tax Provisions

SEC. 511. REDUCTION OF VALUE TAKEN INTO ACCOUNT FOR ESTATE TAX PURPOSES WHERE SPOUSE OF DECEDENT MATERIALLY PARTICIPATED IN FARM OR OTHER BUSINESS.

(a) IN GENERAL.—Section 2040 (relating to joint interests) is amended by adding at the end thereof the following new subsection:

"(c) VALUE WHERE SPOUSE OF DECEDENT MATERIALLY PARTICIPATED IN FARM OR OTHER BUSINESS.—

"(1) IN GENERAL.—Notwithstanding subsection (a), in the case of an eligible joint interest in section 2040(c) property, the value included in the gross estate with respect to such interest by reason of this section shall be—

"(A) the value of such interest, reduced by

"(B) the sum of—

"(i) the section 2040(c) value of such interest, and

"(ii) the adjusted consideration furnished by the decedent's spouse.

"(2) LIMITATIONS.—

"(A) AT LEAST 50 PERCENT OF VALUE TO BE INCLUDED.—Paragraph (1) shall in no event result in the inclusion in the decedent's gross estate of less than 50 percent of the value of the eligible joint interest.

"(B) AGGREGATE REDUCTION.—The aggregate decrease in the value of the decedent's gross estate resulting from the application of this subsection shall not exceed $500,000.

"(3) ELIGIBLE JOINT INTEREST DEFINED.—For purposes of paragraph (1), the term 'eligible joint interest' means any interest in property held by the decedent and the decedent's spouse as joint tenants or as tenants by the entirety, but only if—

"(A) such joint interest was created by the decedent, the decedent's spouse, or both, and

"(B) in the case of a joint tenancy, only the decedent and the decedent's spouse are joint tenants.

"(4) SECTION 2040(c) PROPERTY DEFINED.—For purposes of paragraph (1), the term 'section 2040(c) property' means any interest in any real or tangible personal property which is devoted to use as a farm or used for farming purposes (within the meaning of paragraphs (4) and (5) of section 2032A(e)) or is used in any other trade or business.

"(5) SECTION 2040(c) VALUE.—For purposes of paragraph (1), the term 'section 2040(c) value' means—

"(A) the excess of the value of the eligible joint interest over the adjusted consideration furnished by the decedent, the decedent's spouse, or both, multiplied by

"(B) 2 percent for each taxable year in which the spouse materially participated in the operation of the farm or other trade or business but not to exceed 50 percent.

"(6) ADJUSTED CONSIDERATION.—For purposes of this subsection, the term 'adjusted consideration' means—

"(A) the consideration furnished by the individual concerned (not taking into account any consideration in the form of income or gain from the business of which the section 2040(c) property is a part) determined under rules similar to the rules set forth in subsection (a), and

"(B) an amount equal to the amount of interest which the consideration referred to in subparagraph (A) would have earned over the period in which it was invested in the farm or other business if it had been earning interest throughout such period at 6 percent simple interest.

"(7) MATERIAL PARTICIPATION.—For purposes of paragraph (1), material participation shall be determined in a manner similar to the manner used for purposes of paragraph (1) of section 1402(a) (relating to net earnings from self-employment).

"(8) VALUE.—For purposes of this subsection, except where the context clearly indicates otherwise, the term 'value' means value determined without regard to this subsection.

"(9) ELECTION TO HAVE SUBSECTION APPLY.—This subsection shall apply with respect to a joint interest only if the estate of the decedent elects to have this subsection apply to such interest. Such an election shall be made not later than the time prescribed by section

6075(a) for filing the return of tax imposed by section 2001 (including extensions thereof), and shall be made in such manner as the Secretary shall by regulations prescribe."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to estates of decedents dying after December 31, 1978.

SEC. 512. TREATMENT OF CERTAIN INTERESTS HELD BY DECEDENT'S FAMILY FOR PURPOSES OF THE EXTENSION OF TIME FOR PAYMENT OF ESTATE TAX PROVIDED BY SECTION 6166.

(a) INTEREST HELD BY MEMBER OF DECEDENT'S FAMILY TREATED AS HELD BY DECEDENT.—Paragraph (2) of section 6166(b) (relating to definitions and special rules) is amended by adding at the end thereof the following new subparagraph:

"(D) CERTAIN INTERESTS HELD BY MEMBERS OF DECEDENT'S FAMILY.—All stock and all partnership interests held by the decedent or by any member of his family (within the meaning of section 267(c)(4)) shall be treated as owned by the decedent."

(b) ELECTION FOR PURPOSES OF THE 20-PERCENT REQUIREMENTS WITH RESPECT TO PARTNERSHIP INTERESTS AND STOCK WHICH IS NOT READILY TRADABLE.—Subsection (b) of section 6166 (relating to definitions and special rules) is amended by adding at the end thereof the following new paragraph:

"(7) PARTNERSHIP INTERESTS AND STOCK WHICH IS NOT READILY TRADABLE.—

"(A) IN GENERAL.—If the executor elects the benefits of this paragraph (at such time and in such manner as the Secretary shall by regulations prescribe), then—

"(i) for purposes of paragraph (1)(B)(i) or (1)(C)(i) (whichever is appropriate) and for purposes of subsection (c), any capital interest in a partnership and any non-readily-tradable stock which (after the application of paragraph (2)) is treated as owned by the decedent shall be treated as included in determining the value of the decedent's gross estate,

"(ii) the executor shall be treated as having selected under subsection (a)(3) the date prescribed by section 6151(a), and

"(iii) section 6601(j) (relating to 4-percent rate of interest) shall not apply.

"(B) NON-READILY-TRADABLE STOCK DEFINED.—For purposes of this paragraph, the term 'non-readily-tradable stock' means stock for which, at the time of the decedent's death, there was no market on a stock exchange or in an over-the-counter market."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to the estates of decedents dying after the date of the enactment of this Act.

SEC. 513. SUBORDINATION OF SPECIAL LIENS FOR ADDITIONAL ESTATE TAX ATTRIBUTABLE TO FARM, ETC., VALUATION.

(a) GENERAL RULE.—Subsection (d) of section 6325 (relating to subordination of lien) is amended by striking out "or" at the end of paragraph (1), by striking out the period at the end of paragraph (2) and in-

serting in lieu thereof ", or", and by adding at the end thereof the following new paragraph:

"(3) in the case of any lien imposed by section 6324B, if the Secretary determines that the United States will be adequately secured after such subordination."

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply with respect to the estates of decedents dying after December 31, 1976.

SEC. 514. AMENDMENT OF GOVERNING INSTRUMENTS TO MEET REQUIREMENTS FOR GIFTS OF SPLIT INTEREST TO CHARITY.

(a) CHARITABLE LEAD TRUSTS AND CHARITABLE REMAINDER TRUSTS IN THE CASE OF ESTATE TAX.—The first sentence of paragraph (3) of section 2055(e) is amended to read as follows: "In the case of a will executed before December 31, 1977, or a trust created before such date, if a deduction is not allowable at the time of the decedent's death because of the failure of an interest in property which passes from the decedent to a person, or for a use, described in subsection (a) to meet the requirements of subparagraph (A) or (B) of paragraph (2) of this subsection, and if the governing instrument is amended or conformed on or before December 31, 1978, or, if later, on or before the 30th day after the date on which judicial proceedings begun on or before December 31, 1978 (which are required to amend or conform the governing instrument), become final, so that interest is in a trust which meets the requirements of such subparagraph (a) of (B) (as the case may be), a deduction shall nevertheless be allowed."

(b) CHARITABLE LEAD TRUSTS AND CHARITABLE REMAINDER TRUSTS IN THE CASE OF INCOME AND GIFT TAXES.—Under regulations prescribed by the Secretary of the Treasury or his delegate, in the case of trusts created before December 31, 1977, provisions comparable to section 2055(e)(3) of the Internal Revenue Code of 1954 (as amended by subsecsection (a)) shall be deemed to be included in sections 170 and 2522 of the Internal Revenue Code of 1954.

SEC. 515. DEFERRAL OF CARRYOVER BASIS RULES.

The following provisions are each amended by striking out "December 31, 1976" and inserting in lieu thereof "December 31, 1979":

(1) the caption and text of section 1014(d) (relating to basis of property acquired from the decedent);

(2) section 1016(a)(23) (relating to adjustments to basis);

(3) the heading of section 1023 (relating to carryover basis for certain property);

(4) section 1023(a) (relating to general rule for carryover basis);

(5) the item relating to section 1023 in the table of sections for part II of subchapter O of chapter I; and

(6) section 2005(f)(1) of the Tax Reform Act of 1976 (relating to effective dates for carryover basis provisions).

Subtitle C—Other Excise Tax Provisions

SEC. 520. REDUCTION OF ADMINISTRATION TAX ON PRIVATE FOUNDATIONS.

(a) IN GENERAL.—Subsection (a) of section 4940 (relating to excise tax based on investment income) is amended by striking out "4 percent" and inserting in lieu thereof "2 percent".

(b) EFFECTIVE DATE.—The amendment made by the first section of this Act shall apply to taxable years beginning after September 30, 1977.

SEC. 521. EXCISE TAX ON CERTAIN GAMING DEVICES.

(a) INCREASE IN CREDIT FOR STATE TAX.—Paragraph (2) of section 4464(b) (relating to limitations on the credit for State-imposed taxes) is amended by striking out "80 percent" in the heading and text thereof and inserting in lieu thereof "95 percent".

(b) REPEAL OF OCCUPATIONAL TAX.—Subchapter B of chapter 36 is repealed.

(c) CONFORMING AMENDMENTS.—

(1) Section 4402(2) (relating to exemptions from taxes on wagering) is amended to read as follows:

"(2) COIN-OPERATED DEVICES.—On any wager placed in a coin-operated device (as defined in section 4462 as in effect for years beginning before July 1, 1980), or on any amount paid, in lieu of inserting a coin, token, or similar object, to operate a device described in section 4462(a)(2) (as so in effect), or".

(2) Subsection (a) of section 4901 (relating to payment of occupational tax) is amended by striking out "or 4461(a)(1) (coin-operated gaming devices)".

(d) EFFECTIVE DATES.—

(1) The amendment made by subsection (a) shall apply with respect to years ending June 30, 1979, and June 30, 1980.

(2) The amendments made by subsections (b) and (c) shall apply with respect to years beginning after June 30, 1980.

SEC. 522. TREATMENT OF CERTAIN PRIVATE FOUNDATIONS FOR PURPOSES OF SECTION 4942.

(a) GENERAL RULE.—Subsection (j) of section 4942 (relating to other definitions) is amended by adding at the end thereof the following new paragraph:

"(6) CERTAIN ELDERLY CARE FACILITIES.—For purposes of this section (but no other provision of this title), the term 'operating foundation' includes any organization which, on May 26, 1969, and at all times thereafter before the close of the taxable year, operated and maintained as its principal functional purpose facilities for the long-term care, comfort, maintenance, or education of permanently and totally disabled persons, elderly persons, needy widows, or children, but only if such organization meets the requirements of paragraph (3)(B)(ii)."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1969.

Subtitle D—Income Tax Provisions

SEC. 530. CONTROVERSIES INVOLVING WHETHER INDIVIDUALS ARE EMPLOYEES FOR PURPOSES OF THE EMPLOYMENT TAXES.

(a) TERMINATION OF CERTAIN EMPLOYMENT TAX LIABILITY FOR PERIODS BEFORE 1980.—

(1) IN GENERAL.—If—

(A) for purposes of employment taxes, the taxpayer did not treat an individual as an employee for any period ending before January 1, 1980, and

(B) in the case of periods after December 31, 1978, all Federal tax returns (including information returns) required to be filed by the taxpayer with respect to such individual for such period are filed on a basis consistent with the taxpayer's treatment of such individual as not being an employee,

then, for purposes of applying such taxes for such period with respect to the taxpayer, the individual shall be deemed not to be an employee unless the taxpayer had no reasonable basis for not treating such individual as an employee.

(2) STATUTORY STANDARDS PROVIDING ONE METHOD OF SATISFYING THE REQUIREMENTS OF PARAGRAPH (1).—For purposes of paragraph (1), a taxpayer shall in any case be treated as having a reasonable basis for not treating an individual as an employee for a period if the tax payer's treatment of such individual for such period was in reasonable reliance on any of the following:

(A) judicial precedent, published rulings, technical advice with respect to the taxpayer, or a letter ruling to the taxpayer;

(B) a past Internal Revenue Service audit of the taxpayer in which there was no assessment attributable to the treatment (for employment tax purposes) of the individuals holding positions substantially similar to the position held by this individual; or

(C) long-standing recognized practice of a significant segment of the industry in which such individual was engaged.

(3) CONSISTENCY REQUIRED IN THE CASE OF 1979 TAX TREATMENT.—Paragraph (1) shall not apply with respect to the treatment of any individual for employment tax purposes for any period ending after December 31, 1978, and before January 1, 1980, if the taxpayer (or a predecessor) has treated any individual holding a substantially similar position as an employee for purposes of the employment taxes for any period beginning after December 31, 1977.

(4) REFUND OR CREDIT OF OVERPAYMENT.—If refund or credit of any overpayment of an employment tax resulting from the application of paragraph (1) is not barred on the date of the enactment of this Act by any law or rule of law, the period for filing a claim for refund or credit of such overpayment (to the extent attributable to the application of paragraph (1)) shall not expire before the date 1 year after the date of the enactment of this Act.

(b) PROHIBITION AGAINST REGULATIONS AND RULINGS ON EMPLOYMENT STATUS.—No regulation or Revenue Ruling shall be published on or after the date of the enactment of this Act and before January 1, 1980 (or, if earlier, the effective date of any law hereafter enacted clarifying the employment status of individuals for purposes of the employment taxes) by the Department of the Treasury (including the Internal Revenue Service) with respect to the employment status of any individual for purposes of the employment taxes.

(c) DEFINITIONS.—For purposes of this section—

(1) EMPLOYMENT TAX.—The term "employment tax" means any tax imposed by subtitle C of the Internal Revenue Code of 1954.

(2) EMPLOYMENT STATUS.—The term "employment status" means the status of an individual, under the usual common law rules applicable in determining the employer-employee relationship, as an employee or as an independent contractor (or other individual who is not an employee).

SEC. 531. CERTAIN ORIGINAL STOCKHOLDERS OF COOPERATIVE HOUSING CORPORATIONS.

(a) IN GENERAL.—Subsection (b) of section 216 (relating to deduction of taxes, interest, and business depreciation by cooperative housing corporation tenant-stockholder) is amended by adding at the end thereof the following new paragraph:

"(6) STOCK OWNED BY PERSON FROM WHOM THE CORPORATION ACQUIRED ITS PROPERTY.—

"(A) IN GENERAL.—If the original seller acquires any stock of the corporation—

"(i) from the corporation by purchase, or

"(ii) by foreclosure (or by instrument in lieu of foreclosure) of any purchase-money security interest in such stock held by the original seller,

the original seller shall be treated as a tenant-stock holder for a period not to exceed 3 years from the date of acquisition.

"(B) ORIGINAL SELLER MUST HAVE RIGHT TO OCCUPY APARTMENT OR HOUSE.—Subparagraph (A) shall apply with respect to any acquisition of stock only if, together with such acquisition, the original seller acquires the right to occupy an apartment or house to which such stock is appurtenant. For purposes of the preceding sentence, there shall not be taken into account the fact that, by agreement with the corporation, the original seller or its nominee may not occupy the house or apartment without the prior approval of the corporation.

"(C) ORIGINAL SELLER DEFINED.—For purposes of this paragraph, the term 'original seller' means the person from whom the corporation has acquired the apartments or houses (or leaseholds therein)."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to stock acquired after the date of the enactment of this Act.

Subtitle E—Other Income Tax Provisions

SEC. 540. DEPOSITS IN CERTAIN BRANCHES OF PUERTO RICAN SAVINGS AND LOAN ASSOCIATIONS.

(a) IN GENERAL.—Subparagraph (F) of section 861(a)(1) (relating to income from sources within the United States) is amended to read as follows:

"(F) interest—

"(i) on deposits with a foreign branch of a domestic corporation or a domestic partnership if such branch is engaged in the commercial banking business, and

"(ii) on amounts satisfying the requirements of paragraph (2) of subsection (c) which are paid by a foreign branch of a domestic corporation or a domestic partnership,".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after the date of the enactment of this Act.

SEC. 541. TAXATION OF ALASKA NATIVE CLAIMS SETTLEMENT ACT CORPORATIONS.

Section 21 of the Alaska Native Claims Settlement Act (43 U.S.C. 1620) is amended by adding three new subsections at the end thereof, as follows:

"(g) In the case of any Native Corporation established pursuant to this Act, income for purposes of any form of Federal, State, or local taxation shall not be deemed to include the value of—

"(1) the receipt, acquisition, or use of any resource information or analysis (including the receipt of any right of access to such information or analysis) relating to lands or interests therein conveyed, selected but not conveyed, or available for selection pursuant to this Act;

"(2) the promise or performance by any person or by any Federal, State, or local government agency of any professional or technical services relating to the resources of lands or interests therein conveyed, selected but not conveyed, or available for selection pursuant to this Act, including, but not limited to, services in connection with exploration on such lands for oil, gas, or other minerals; and

"(3) the expenditure of funds, incurring of costs, or the use of any equipment or supplies by any person or any Federal, State, or local government agency, or any promise, agreement, or other arrangement by such person or agency to expend funds or use any equipment or supplies for the purpose of creating, developing, or acquiring the resource information or analysis described in paragraph (1) or for the purpose of performing or otherwise furnishing the services described in paragraph (2): Provided, That this paragraph shall not apply to any funds paid to a Native Corporation established pursuant to this Act or to any subsidiary thereof.

This subsection shall be effective as of December 18, 1971, and, with respect to each Native Corporation, shall remain in full force and effect for a period of twenty years thereafter or until the Corporation has received conveyance of its full land entitlement, whichever first occurs. Except as set forth in this subsection and in subsection (d) hereof, all rents, royalties, profits, and other revenues or proceeds derived from real property interests selected and conveyed pursuant to sections 12 and 14 shall be taxable to the same extent as such revenues or proceeds are taxable when received by a non-Native individual or corporation.

"(h)(1) Notwithstanding any other provision of law, each Native Corporation established pursuant to this Act shall be deemed to have become engaged in carrying on a trade or business as of the date it was incorporated for purposes of any form of Federal, State, or local taxation.

"(2) All expenses heretofore or hereafter paid or incurred by a Native Corporation established pursuant to this Act in connection with the selection or conveyance of lands pursuant to this Act, or in assisting another Native Corporation within or for the same region in the selection or conveyance of lands under this Act, shall be deemed to be or to have been ordinary and necessary expenses of such Corporation, paid or incurred in carrying on a trade or business for purposes of any form of Federal, State, or local taxation."

"(i) PERSONAL HOLDING COMPANY ACT EXEMPTION.—No Corporation created pursuant to the Alaska Native Claims Settlement Act shall be considered to be a personal holding company within the meaning of section 542(a) of the Internal Revenue Code of 1954 prior to January 1, 1992."

SEC. 542. REPLACEMENT OF LIVESTOCK WITH OTHER FARM PROPERTY WHERE THERE HAS BEEN ENVIRONMENTAL CONTAMINATION.

(a) IN GENERAL.—Section 1033 (relating to involuntary conversions) is amended by redesignating subsections (f) and (g) as subsections (g) and (h), respectively, and by inserting after subsection (e) the following new subsection:

"(f) REPLACEMENT OF LIVESTOCK WITH OTHER FARM PROPERTY WHERE THERE HAS BEEN ENVIRONMENTAL CONTAMINATION.—For

purposes of subsection (a), if, because of soil contamination or other environmental contamination, it is not feasible for the taxpayer to reinvest the proceeds from compulsorily or involuntarily converted livestock in property similar or related in use to the livestock so converted, other property (including real property) used for farming purposes shall be treated as property similar or related in service or use to the livestock so converted."

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1974.

SEC. 543. CERTAIN PAYMENTS NOT INCLUDED IN GROSS INCOME.

(a) IN GENERAL.—Part III of subchapter B of chapter 1 (relating to items specifically excluded from gross income) is amended by redesignating section 126 as 127 and by inserting immediately after section 125 the following new section:

"SEC. 126. CERTAIN COST-SHARING PAYMENTS.

"(a) GENERAL RULE.—Gross income does not include the excludable portion of payments received under—

"(1) The rural clean water program authorized by section 208(j) of the Federal Water Pollution Control Act (33 U.S.C. 1288(j)).

"(2) The rural abandoned mine program authorized by section 406 of the Surface Mining Control and Reclamation Act of 1977 (30 U.S.C. 1236).

"(3) The water bank program authorized by the Water Bank Act (16 U.S.C. 1301 et seq.).

"(4) The emergency conservation measures program authorized by title IV of the Agricultural Credit Act of 1978.

"(5) The agricultural conservation program authorized by the Soil Conservation and Domestic Allotment Act (16 U.S.C. 590a).

"(6) The great plains conservation program authorized by section 16 of the Soil Conservation and Domestic Policy Act (16 U.S.C. 590p (b)).

"(7) The resource conservation and development program authorized by the Bankhead-Jones Farm Tenant Act and by the Soil Conservation and Domestic Allotment Act (7 U.S.C. 1010; 16 U.S.C. 590a et seq.).

"(8) The forestry incentives program authorized by section 4 of the Cooperative Forestry Assistance Act of 1978 (16 U.S.C. 2103).

"(9) Any small watershed program administered by the Secretary of Agriculture which is determined by the Secretary of the Treasury to be substantially similar to the type of programs described in paragraphs (1) through (8).

"(10) Any State program 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.

"(b) EXCLUDABLE PORTION.—For purposes of this section, the term 'excludable portion' means that portion (or all) of a payment made to any person under any program described in subsection (a) which—

"(1) 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

"(2) is determined by the Secretary of the Treasury as not increasing substantially the annual income derived from the property.

"(c) APPLICATION WITH OTHER SECTIONS.—No deduction or credit allowable under any other provision of this chapter shall be allowed with respect to any expenditure made with the use of payments described in subsection (a) or with respect to any property acquired with any payment described in subsection (a) (to the extent that the basis is allocable to the use of such payments). Notwithstanding any provision of section 1016 to the contrary, no adjustment to basis shall be made with respect to property acquired through the use of such payments, to the extent that such adjustment would reflect the amount of such payment."

(b) CLERICAL AMENDMENT.—The table of sections for such part is amended by striking out the last item and inserting in lieu thereof the following:

"Sec. 126. Certain cost-sharing payments.
"Sec. 127. Cross references to other Acts."

(c) RECAPTURE OF GAIN FROM DISPOSITION OF PROPERTY.—

(1) Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by adding at the end thereof the following:

"SEC. 1255. GAIN FORM DISPOSITION OF SECTION 126 PROPERTY.

"(a) GENERAL RULE.—

"(1) ORDINARY INCOME.—Except as otherwise provided in this section, if section 126 property is disposed of, the lower of—

"(A) the applicable percentage of the aggregate payments, with respect to such property, excluded from gross income under section 126, or

"(B) the excess of—

"(i) the amount realized (in the case of a sale, exchange, or involuntary conversion), or the fair market value of such section 126 property (in the case of any other disposition), over

"(ii) the adjusted basis of such property, shall be treated as ordinary income.

"(2) SECTION 126 PROPERTY.—For purposes of this section, 'section 126 property' means any property acquired, improved, or otherwise modified by the application of payments excluded from gross income under section 126.

"(3) APPLICABLE PERCENTAGE.—For purposes of this section, if section 126 property is disposed of less than 10 years after the date of receipt of payments excluded from gross income under section 126, the applicable percentage is 100 percent. If section 126 property is disposed of more than 10 years after such date, the applicable percentage is 100 percent reduced (but not below zero) by 10 percent for each year or part thereof in excess of 10 years such property was held after the date of receipt of the payments.

"(b) SPECIAL RULES.—Under regulations prescribed by the Secretary—

"(1) rules similar to the rules applicable under section 1245 shall be applied for purposes of this section, and

"(2) amounts treated as ordinary income under this section shall be treated in the same manner as amounts treated as ordinary income under section 1245."

(2) The table of sections for such part is amended by adding at the end thereof the following new item:

"Sec. 1255. Gain from disposition of section 126 property."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to grants made under the programs after September 30, 1979.

Subtitle F—Studies

SEC. 551. STUDY OF SIMPLIFICATION OF TAX RETURNS.

(a) STUDY.—The Secretary of the Treasury shall conduct a full and complete study and investigation with respect to—

(1) provisions of the Internal Revenue Code of 1954 which, due to their complexity, may hamper the ability of individuals to prepare accurate and complete Federal income tax returns, and

(2) methods of simplifying Federal income tax return forms and instructions accompanying such forms.

(b) TASK FORCE.—

(1) IN GENERAL.—The Secretary of the Treasury shall establish a task force to assist him in the conduct of the study and investigation under subsection (a).

(2) REPORTS OF TASK FORCE.—The task force shall report from time to time on its progress directly to the Secretary and shall submit a final report to the Secretary which includes its findings with respect to such study and investigation and any recommendations with respect thereto. Such final report shall be submitted by such time as is necessary to enable the Secretary to file the report called for in subsection (c) of this section.

(3) AUTHORITY TO HIRE.—The Secretary is authorized to appoint such employees, not in excess of 10, as may be necessary to carry out the functions of the task force without regard to the provisions of chapter 51 and subchapter III of chapter 53 of title 5, United States Code, except that such employees shall not be paid at a rate in excess of the annual rate of pay under grade GS–18 of the General Schedule under section 5332 of such title 5.

(c) REPORT.—The Secretary, after studying the reports and recommendations of the task force under subsection (b), shall, not later than 2 years after the date of the enactment of this Act, submit to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives a final report on the study and investigation conducted under this section, together with such recommendations for legislation as he finds necessary.

SEC. 552. STUDY OF TAX INCENTIVES FOR EXPENDITURES REQUIRED BY OCCUPATIONAL SAFETY AND HEALTH ADMINISTRATION AND MINING HEALTH AND SAFETY ADMINISTRATION.

(a) STUDY.—The Secretary of the Treasury shall make a full and complete study and investigation with respect to the appropriateness of providing additional tax incentives for expenditures required by the Occupational Safety and Health Act (OSHA) and the Mining Safety and Health Administration (MSHA) of the Department of Labor.

(b) REPORT.—Before April 1, 1979, the Secretary of the Treasury shall submit to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives a report of its study and investigation together with its recommendations for legislation.

SEC. 553. STUDY OF TAXATION OF NONRESIDENT ALIEN REAL ESTATE TRANSACTIONS IN THE UNITED STATES.

(a) STUDY.—The Secretary of the Treasury shall make a full and complete study and analysis of the appropriate tax treatment to be given to income derived from, or gain realized on, the sale of interests in United States property held by nonresident aliens or foreign corporations.

(b) REPORT.—The Secretary of the Treasury shall submit to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives a final report of its study, together with its recommendations, no later than 6 months from the date of enactment of this Act.

SEC. 554. REPORT ON EFFECTIVENESS OF JOBS CREDIT.

(a) REPORT ON TARGETED JOBS CREDIT.—Not later than June 30, 1981, the Secretary of the Treasury and the Secretary of Labor shall jointly submit to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate a report on—

(1) the effectiveness of the targeted jobs credit provided by the amendments made by this section in improving the employment situation of the targeted groups, and

(2) the types of employers claiming such credit.

(b) GENERAL JOBS CREDIT.—The report required under paragraph (1) shall also include an evaluation of—

(1) the effectiveness of the general jobs credit provided by section 44B of the Internal Revenue Code of 1954 for 1977 and 1978 in stimulating employment and enhancing economic growth, and

(2) the types of employers claiming such credit.

SEC. 555. STUDY OF EFFECTS OF CHANGES IN THE TAX TREATMENT OF CAPITAL GAINS ON STIMULATING INVESTMENT AND ECONOMIC GROWTH.

Not later than September 30, 1981, the Secretary of the Treasury shall submit to the Committee on Ways and Means of the House of Representatives and to the Committee on Finance of the Senate a report on the effectiveness of the changes made by this title in the tax treatment of capital gains of individuals and corporations in stimulating investment and increasing the rate of economic growth. The report shall also include an analysis of the effects these changes had on employment growth and on income tax revenues.

TITLE VI—GENERAL STOCK OWNERSHIP CORPORATIONS

SEC. 601. ESTABLISHMENT AND TAXATION OF GENERAL STOCK OWNERSHIP CORPORATIONS AND THEIR SHAREHOLDERS.

(a) IN GENERAL.—Chapter 1 (relating to normal taxes and surtaxes) is amended by adding at the end thereof the following new subchapter:

"Subchapter U—General Stock Ownership Corporations

"SEC. 1391. DEFINITIONS.

"(a) GENERAL STOCK OWNERSHIP CORPORATION.—For purposes of this subchapter, the term 'general stock ownership corporation' (hereinafter referred to as a 'GSOC') means a domestic corporation which—

"(1) is not a member of an affiliated group (as defined in section 1504), and

"(2) is chartered and organized after December 31, 1978, and before January 1, 1984;

"(3) is chartered by an act of a State legislature or as a result of a State-wide referendum;

"(4) has a charter providing—

"(A) for the issuance of only 1 class of stock,

"(B) for the issuance of shares only to eligible individuals (as defined in subsection (c));

"(C) for the issuance of at least one share to each eligible individual, unless such eligible individual elects within one year after the date of issuance not to receive such share;

"(D) that no share of stock shall be tranferable—

"(i) by a shareholder other than by will or the laws of descent and distribution until after the expiration of 5 years from the date such stock is issued by the GSOC except where the shareholder ceases to be a resident of the State;

"(ii) to any person other than a resident individual of the chartering State;

"(iii) to any individual who, after the transfer, would own more than 10 shares of the GSOC;

"(E) that such corporation shall qualify as a GSOC under the Internal Revenue Code;

"(5) is empowered to invest in properties (but not in properties acquired by it or for its benefit through the right of eminent domain). For purposes of this subsection, section 1504(a) shall be applied by substituting '20 percent' for '80 percent' wherever it appears.

"(b) ELECTING GSOC.—For purposes of this subchapter, the term 'electing GSOC' means a GSOC which files an election under section 1392 which, under section 1392, is in effect for such taxable year.

"(c) ELIGIBLE INDIVIDUALS.—For purposes of subsection (a), the term 'eligible individual' means an individual who is, as of a date specified in the State's enabling legislation for the GSOC, a resident of the chartering State and who remains a resident of such State between that date and the date of issuance.

"(d) TREATED AS PRIVATE CORPORATION.—For purposes of this title, a GSOC shall be treated as a private corporation and not as a governmental unit.

"(e) STUDY OF GENERAL STOCK OWNERSHIP CORPORATIONS.—The staff of the Joint Committee on Taxation shall prepare a report on the operation and effects of this subchapter relating to GSOC's. An interim report shall be filed within two years after the first GSOC is formed and a final report shall be filed by September 30, 1983.

"SEC. 1392. ELECTION BY GSOC.

"(a) ELIGIBILITY.—Except as provided in section 1393, any GSOC may elect, in accordance with the provisions of this section, not to be subject to the taxes imposed by this chapter.

"(b) EFFECT.—If a GSOC makes an election under subsection (a) then—

"(1) with respect to the taxable years of the GSOC for which such election is in effect, such corporation shall not be subject to the taxes imposed by this chapter and, with respect to such taxable years and all succeeding taxable years, the provisions of section 1396 shall apply to such GSOC, and

"(2) with respect to each such taxable year, the provisions of sections 1393, 1394, and 1395 shall apply to the shareholders of such GSOC.

"(c) WHERE AND HOW MADE.—An election under subsection (a) may be made by a GSOC at such time and in such manner as the Secretary shall prescribe by regulations.

"(d) YEARS FOR WHICH EFFECTIVE.—An election under subsection (a) shall be effective for the taxable year of the GSOC for which it is made and for all succeeding taxable years of the GSOC, unless it is terminated under subsection (f).

"(e) TAXABLE YEAR.—The taxable year of a GSOC shall end on October 31 unless the Secretary consents to a different taxable year.".

"(f) TERMINATION.—The election of a GSOC under subsection (a) shall terminate for any taxable year during which it ceases to be a GSOC and for all succeeding taxable years. The election of a GSOC under subsection (a) may be terminated at any other time with the consent of the Secretary, effective for the first taxable year with respect to which the Secretary consents and for all succeeding taxable years.

"SEC. 1393. GSOC TAXABLE INCOME TAXED TO SHAREHOLDERS.

"(a) GENERAL RULE.—The taxable income of an electing GSOC for any taxable year shall be included in the gross income of the shareholders of such GSOC in the manner and to the extent set forth in this subsection.

"(1) AMOUNT INCLUDED IN GROSS INCOME.—Each shareholder of an electing GSOC on any day of a taxable year of such GSOC shall include in his gross income for the taxable year with or within which the taxable year of the GSOC ends the amount he would have received if, on each day of such taxable year, there had been distributed pro rata to its shareholders by such GSOC an amount equal to the taxable income of the GSOC for its taxable year divided by the number of days in the GSOC's taxable year.

"(2) TAXABLE INCOME DEFINED.—For purposes of this section, the term 'taxable income' of a GSOC shall be determined without regard to the deductions allowed by part VIII of subchapter B (other than deductions allowed by section 248, relating to organizational expenditures).

"(b) SPECIAL RULE FOR INVESTMENT CREDIT.—The investment credit of an electing GSOC for any taxable year shall be allowed as a credit to the shareholders of such corporation in the manner and to the extent set forth in this subsection.

"(1) CREDIT.—There shall be apportioned among the shareholders a credit equal to the amount each shareholder would have received if, on each day of such taxable year, there had been distributed pro rata to the shareholders the electing GSOC's net investment credit divided by the number of days in the GSOC's taxable year.

"(2) NET INVESTMENT CREDIT.—For purposes of this paragraph the term 'net investment credit' means the investment credit of the electing GSOC for its taxable year less any tax from recomputing a prior year's investment credit in accordance with section 47.

"(3) RECAPTURE.—There shall be apportioned among the shareholders of a GSOC, in the manner described in paragraph (1), an additional tax equal to the excess of any tax resulting from recomputing a prior year's investment credit in accordance with section 47 over the investment credit of the GSOC for it's taxable year.

'SEC. 1394. RULES APPLICABLE TO DISTRIBUTIONS OF AN ELECTING GSOCs.

"(a) SHAREHOLDER INCOME ACCOUNT.—An electing GSOC shall establish and maintain a shareholder income account which account shall be—

"(1) increased at the close of the GSOC's taxable year by an amount equal to the GSOC's taxable income for such year, and

"(2) Decreased, but not below zero, on the first day of the GSOC's taxable year by the amount of any GSOC distribution to the shareholders of such GSOC made or treated as made during the prior taxable year.

"(b) TAXATION OF DISTRIBUTIONS.—Distributions by an electing GSOC shall be treated as—

"(1) a distribution of previously taxed income to the extent such distribution does not exceed the balance of the shareholder income account as of the close of the taxable year of the GSOC, and

"(2) a distribution to which section 301(a) applies but only to the extent such distribution exceeds the balance of the shareholder income account as of the close of the taxable year of the GSOC.

"(c) DISTRIBUTIONS NOT TREATED AS A DIVIDEND.—Any amounts includible in the gross income of any individual by reason of ownership of stock in a GSOC shall not be considered as a dividend for purposes of section 116.

"(d) REGULATIONS.—The Secretary shall have authority to prescribe by regulation, rules for treatment of distributions in respect of shares of stock of the GSOC that have been transferred during the taxable year.

"SEC. 1395. ADJUSTMENT TO BASIS OF STOCK OF SHAREHOLDERS.

"The basis of a shareholder's stock in an electing GSOC shall be increased by the amount includible in the gross income of such shareholder under section 1393, but only to the extent to which such amount is actually included in the gross income of such shareholder.

"SEC. 1396. MINIMUM DISTRIBUTIONS.

"(a) GENERAL RULE.—A GSOC shall distribute at least 90 percent of its taxable income for any taxable year by January 31 following the close of such taxable year. Any distribution made on or before January 31 shall be treated as made as of the close of the preceding taxable year.

"(b) IMPOSITION OF TAX IN CASE OF FAILURE TO MAKE MINIMUM DISTRIBUTIONS.—If a GSOC fails to make the minimum distribution requirements described in subsection (a), there is hereby imposed on the GSOC tax equal to 20 percent of the excess of the amount required to be distributed over the amount actually distributed.

"SEC. 1397. SPECIAL RULES APPLICABLE TO AN ELECTING GSOC.

"(a) GENERAL RULE.—The current earnings and profits of an electing GSOC as of the close of its taxable year shall not include the amount of taxable income for such year which is required to be included in the gross income of the shareholders of such GSOC under section 1393(a).

"(b) SPECIAL RULE FOR AUDIT ADJUSTMENTS.—

"(1) TAXABLE INCOME.—*Taxable income of an electing GSOC shall, in the year of final determination, be increased or decreased, as the case might be, by any adjustment to taxable income for a prior taxable year.*

"(2) INVESTMENT CREDIT.—*The net investment credit of an electing GSOC shall, in the year of final determination, be increased or decreased, as the case might be, by any adjustment to the net investment credit for a prior taxable year.*

"(3) METHOD OF MAKING ADJUSTMENTS.—*An electing GSOC shall include in gross income for the year of an adjustment the amount described in paragraph (1) and shall take into account the adjustment described in paragraph (2), and shall be liable for payment of interest in the amount that would have been payable by the GSOC under section 6601 (relating to interest on underpayment, nonpayment or extensions of time for payment, of tax) or receivable by the GSOC under section 6611 (relating to interest on overpayments) if such GSOC had been a corporation other than an electing GSOC.*"

(b) TECHNICAL AMENDMENTS.—

(1) NET OPERATING LOSS DEDUCTION.—*Paragraph (1) of section 172(b) (relating to net operating loss carrybacks and carryovers) is amended by adding at the end thereof the following new subparagraph:*

"(H) *In the case of an electing GSOC which has a net operating loss for any taxable year such loss shall not be a net operating loss carryback to any taxable year preceding the year of such loss, but shall be a net operating loss carryover to each of the 10 taxable years following the year of such loss.*"

(2) INCOME TAX COLLECTED AT SOURCE.—*Section 3402 (relating to income collected at source) is amended by adding at the end thereof the following new subsection:*

"(r) EXTENSION OF WITHHOLDING TO GSOC DISTRIBUTIONS.—

"(1) GENERAL RULE.—*An electing GSOC making any distribution to its shareholders shall deduct and withhold from such payment a tax in an amount equal to 25 percent of such payment.*

"(2) COORDINATION WITH OTHER SECTIONS.—*For purposes of sections 3403 and 3404 and for purposes of so much of subtitle F (except section 7205) as relates to this chapter, distributions of an electing GSOC to any shareholder which are subject to withholding shall be treated as if they were wages paid by an employer to an employee.*"

(3) ADJUSTMENTS TO BASIS.—*Section 1016(a) (relating to adjustments of basis) is amended by redesignating paragraph (23) as (22) and by inserting after paragraph (20) the following new paragraph:*

"(21) *to the extent provided in section 1395 in the case of stock of shareholders of a general stock ownership corporation (as defined in section 1391) which makes the election provided by section 1392; and*".

(4) RETURN OF GENERAL STOCK OWNERSHIP CORPORATION.—*Subpart A of part III of subchapter A of Chapter 61 (relating to information returns) is amended by adding at the end thereof the following new section:*

"SEC. 6039B. RETURN OF GENERAL STOCK OWNERSHIP CORPORATION.

"Every general stock ownership corporation (as defined in section 1391) which makes the election provided by section 1392 shall make a return for each taxable year, stating specifically the items of its gross income and the deductions allowable by subtitle A, the amount of investment credit or additional tax, as the case may be, the names and addresses of all persons owning stock in the corporation at any time during the taxable year, the number of shares of stock owned by each shareholder at all times during the taxable year, the amount of money and other property distributed by the corporation during the taxable year to each shareholder, the date of each such distribution, and such other information, for the purpose of carrying out the provisions of subchapter U of chapter 1, as the Secretary may by regulation prescribe. Any return filed pursuant to this section shall, for purposes of chapter 66 (relating to limitations), be treated as a return filed by the corporation under section 6012. Every GSOC shall file an annual report with the Secretary summarizing its operations for such year."

(c) CLERICAL AMENDMENTS.—

(1) The table of subchapters for chapter 1 is amended by adding at the end thereof the following:

"SUBCHAPTER U.—General stock ownership plans."

(2) The table of sections for subpart A of part III of subchapter A of chapter 61 is amended by adding at the end thereof the following:

"Sec. 6039B. Return of general stock ownership corporation."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to corporations chartered after December 31, 1978, and before January 1, 1984.

TITLE VII—TECHNICAL CORRECTIONS OF THE TAX REFORM ACT OF 1976

SEC. 701. TECHNICAL AMENDMENTS TO INCOME TAX PROVISIONS AND ADMINISTRATIVE PROVISIONS.

(a) AMENDMENTS RELATING TO RETENTION OF PRIOR LAW FOR RETIREMENT INCOME CREDIT UNDER SECTION 37(e).—

(1) CLARIFICATION THAT SPOUSE UNDER AGE 65 MUST HAVE PUBLIC RETIREMENT SYSTEM INCOME.—Paragraph (2) of section 37(e) (relating to election of prior law with respect to public retirement system income) is amended by striking out "who has not attained age 65 before the close of the taxable year" and inserting in lieu thereof "who has not attained age 65 before the close of the taxable year (and whose gross income includes income described in paragraph (4)(B))".

(2) CLARIFICATION THAT QUALIFYING SERVICES MUST HAVE BEEN PEFFORMED BY TAXPAYER OR SPOUSE.—Subparagraph (B) of section 37(e)(4) (defining retirement income) is amended by inserting "and who performed the services giving rise to the pension or annuity (or is the spouse of the individual who performed the services)" after "before the close of the taxable year".

(3) DISREGARD OF COMMUNITY PROPERTY LAWS.—Subsection (c) of section 37 (relating to election of prior law with respect to public retirement system income) is amended—

(A) by redesignating paragraph (8) as paragraph (9) and by inserting after paragraph (7) the following new paragraph:

"(8) COMMUNITY PROPERTY LAWS NOT APPLICABLE.—In the case of a joint return, this subsection shall be applied without regard to community property laws.",

(B) by striking out "paragraph (8)(A)" in paragraph (4)(B) and inserting in lieu thereof "paragraph (9)(A)"; and

(C) by striking out "paragraph (8)(B)" in paragraph (5)(B) and inserting in lieu thereof "paragraph (9)(B)".

(4) EFFECTIVE DATES.—

(A) The amendments made by paragraphs (1) and (2) shall apply to taxable years beginning after December 31, 1975.

(B) The amendments made by paragraph (3) shall apply to taxable years beginning after December 31, 1977.

(b) AMENDMENTS RELATING TO THE MINIMUM TAX.—

(1) SPECIAL RULES FOR MINIMUM TAX IN THE CASE OF SUBCHAPTERS CORPORATIONS AND PERSONAL HOLDING COMPANIES.—

(A) Paragraph (1) of section 57(a) (relating to adjusted itemized deductions) is amended by striking out "An amount" and inserting in lieu thereof "In the case of an individual, an amount".

(B) The last sentence of section 57(a) (relating to items of tax preference) is amended by striking out "Paragraphs (1), (3), and" and inserting in lieu thereof "Paragraphs (3) and".

(2) DIVISION OF $10,000 AMOUNT AMONG MEMBERS OF CONTROLLED GROUPS.—Subsection (b) of section 58 (relating to members of controlled groups) is amended to read as follows:

"(b) MEMBERS OF CONTROLLED GROUPS.—In the case of a controlled group of corporations (as defined in section 1563(a)), the $10,000 amount specified in section 56 shall be divided among the component members of such group in proportion to their respective regular tax deductions (within the meaning of section 56(c)) for the taxable year."

(3) COMPUTATION OF ADJUSTED ITEMIZED DEDUCTIONS IN THE CASE OF ESTATES AND TRUSTS.—Paragraph (2) of section 57(b) (relating to computation of adjusted itemized deductions in the case of estates and trusts) is amended to read as follows:

"(2) SPECIAL RULES FOR ESTATES AND TRUSTS.—

"(A) IN GENERAL.—In the case of an estate or trust, for purposes of paragraph (1) of subsection (a), the amount of the adjusted itemized deductions for any taxable year is the amount by which the sum of the deductions for the taxable year other than—

"(i) the deductions allowable in arriving at adjusted gross income,

"(ii) the deduction for personal exemption provided by section 642(b),

"(iii) the deduction for casualty losses described in section 165(c)(3),

"(iv) the deductions allowable under section 651(a), 661(a), or 691(c), and

"(v) the deductions allowable to a trust under section 642(c) to the extent that a corresponding amount is included in the gross income of the beneficiary under section 662(a)(1) for the taxable year of the beneficiary with which or within which the taxable year of the trusts ends,

exceeds 60 percent (but does not exceed 100 percent) of the adjusted gross income of the estate or trust for the taxable year.

"(B) DETERMINATION OF ADJUSTED GROSS INCOME.—For purposes of this paragraph, the adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual, except that—

"(i) the deductions for costs paid or incurred in connection with the administration of the estate or trust, and

"(ii) to the extent provided in subparagraph (C), the deductions under section 642(c),

shall be treated as allowable in arriving at adjusted gross income.

"(C) TREATMENT OF CERTAIN CHARITABLE CONTRIBUTIONS.—For purposes of this paragraph, the following deductions under section 642(c) (relating to deductions for amounts paid or permanently set aside for charitable purposes) shall be treated as deductions allowable in arriving at adjusted gross income:

"(i) deductions allowable to an estate,

"(ii) deductions allowable to a trust all of the unexpired interests in which are devoted to one or more of the purposes described in section 170(c)(2)(B),

"(iii) deductions allowable to a trust which is a pooled income fund within the meaning of section 642(c)(5),

"(iv) deductions allowable to a trust which are attributable to transfers to the trust before January 1, 1977, and

"(v) deductions allowable to a trust, all of the income interest of which is devoted solely to one or more of the purposes described in section 170(c)(2)(B), which are attributable to transfers pursuant to a will or pursuant to an inter vivos trust in which the grantor had the power to revoke at the date of his death."

(4) SECTION 691(c) DEDUCTION NOT TAKEN INTO ACCOUNT FOR DETERMINING ADJUSTED ITEMIZED DEDUCTIONS.—Paragraph (1) of section 57(b) is amended by striking out "and" at the end of subparagraph (C), by inserting "and" at the end of subparagraph (D), and by inserting after subparagraph (D) the following new subparagraph:

"(E) the deduction allowable under section 691(c),".

(5) EFFECTIVE DATE.—The amendments made by this subsection shall take effect as if included in the amendments made by section 301 of the Tax Reform Act of 1976.

(c) SICK PAY.—

(1) IN GENERAL.—Section 105(d) is amended by striking out paragraphs (4) and (6), by redesignating paragraph (5) as paragraph (4) and paragraph (7) as paragraph (6), and by inserting after paragraph (4) the following new paragraph:

"(5) SPECIAL RULES FOR MARRIED COUPLES.—

"(A) MARRIED COUPLE MUST FILE JOINT RETURN.—Except in the case of a husband and wife who live apart at all times during the taxable year, if the taxpayer is married at the close of the taxable year, the exclusion provided by this subsection shall be allowed only if the taxpayer and his spouse file a joint return for the taxable year.

"(B) APPLICATION OF PARAGRAPHS (2) AND (3).—In the case of a joint return—

"(i) paragraph (2) shall be applied separately with respect to each spouse, but

"(ii) paragraph (3) shall be applied with respect to their combined adjusted gross income.

"(C) DETERMINATION OF MARITAL STATUS.—For purposes of this subsection, marital status shall be determined under section 143(a).

"(D) JOINT RETURN DEFINED.—For purposes of this subsection, the term 'joint return' means the joint return of a husband and wife made under section 6013."

(2) CONFORMING AMENDMENTS.—

(A) Subsection (c)(3) of section 505 of the Tax Reform Act of 1976 (relating to disability retirement) is amended by striking out "section 105(d)(5)" and inserting in lieu thereof "section 105(d)(4)".

(B) Subsections (c) and (e)(1) of section 301 of the Tax Reduction and Simplification Act of 1977 (relating to effective date of changes in the exclusion for sick pay) are each amended by striking out "section 105(d)(7)" and inserting in lieu thereof "section 105(d)(6)".

(3) EFFECTIVE DATE.—

(A) The amendments made by paragraphs (1) and (2)(A) shall take effect as if included in section 105(d) of the Internal Revenue Code of 1954 as such section was amended by section 505(a) of the Tax Reform Act of 1976.

(B) The amendments made by paragraph (2)(B) shall take effect as if included in section 301 of the Tax Reduction and Simplification Act of 1977.

(d) NET OPERATING LOSSES.—

(1) AMENDMENT OF SECTION 172 (b)(1)(B).—The second sentence of subparagraph (B) of section 172(b)(1) (relating to years to which net operating losses may be carried) is amended by striking out "and (F)" and inserting in lieu thereof "(F), and (G)".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to losses incurred in taxable years ending after December 31, 1975.

(e) EFFECTIVE DATE FOR FISCAL YEAR TAXPAYERS FOR CONSTRUCTION PERIOD INTEREST AND TAXES.—Paragraph (1) of section 201(c) of the Tax Reform Act of 1976 is amended to read as follows:

"(1) in the case of nonresidential real property, if the construction period begins on or after the first day of the first taxable year beginning after December 31, 1975,".

(f) CLARIFICATION OF PROVISIONS PROVIDING TAX INCENTIVES TO ENCOURAGE THE PRESERVATION OF HISTORIC STRUCTURES.—

(1) DEFINITION OF CERTIFIED HISTORIC STRUCTURES.—Subsection (d) of section 191 (relating to amortization of certain rehabilitation expenditures for certified historic structures) is amended by redesignating paragraphs (2) and (3) as paragraphs (3) and (4), respectively, and by striking out paragraph (1) and inserting in lieu thereof the following new paragraphs:

"(1) CERTIFIED HISTORIC STRUCTURE.—The term 'certified historic structure' means a building or structure which is of a character subject to the allowance for depreciation provided in section 167 and which—

"(A) is listed in the National Register, or

(B) is located in a registered historic district and is certified by the Secretary of the Interior to the Secretary as being of historic significance to the district.

"(2) REGISTERED HISTORIC DISTRICT.—The term 'registered historic district' means—

"(A) any district listed in the National Register, and

"(B) any district—

"(i) which is designated under a statute of the appropriate State or local government, if such statute is certified by the Secretary of the Interior to the Secretary as containing criteria which will substantially achieve the purpose of preserving and rehabilitating buildings of historic significance to the district, and

"(ii) which is certified by the Secretary of the Interior to the Secretary as meeting substantially all of the requirements for the listing of districts in the National Register."

(2) AMENDMENT OF CROSS REFERENCES.—Subsection (g) of section 191 (relating to cross references) is amended to read as follows:

"(g) CROSS REFERENCES.—

"(1) For rules relating to the listing of buildings, structures, and historic districts in the National Register, see the Act entitled 'An Act to establish a program for the preservation of additional historic properties throughout the Nation, and for other purposes, approved October 15, 1966 (16 U.S.C. 470 et seq.).

"(2) For special rules with respect to certain gain derived from the disposition of property the adjusted basis of which is determined with regard to this section, see sections 1245 and 1250."

(3) SPECIAL RULES FOR RECAPTURE OF AMORTIZATION DEDUCTION.—

(A) Paragraph (2) of section 1245(a) (relating to gain from dispositions of certain depreciable property) is amended—

(i) by striking out "190, or 191" the first place it appears and inserting in lieu thereof "or 190" and

(ii) by striking out "190, or 191" the second and third place it appears and inserting in lieu thereof "190, or (in the case of property described in paragraph (3)(C)) 191".

(B) Subparagraph (D) of section 1245(a)(3) (relating to gain from dispositions of certain depreciable property) is amended by striking out "190, or 191" and inserting in lieu thereof "or 190".

(C) Paragraph (3) of section 1250(b) (relating to depreciation adjustments) is amended by striking out "190 or 191" and inserting in lieu thereof "or 190".

(D) Paragraph (2) of section 57(a) (relating to items of tax preference) is amended by inserting "or 191" after "167(k)".

(E) Paragraph (4) of section 1250(b) (relating to definition of additional depreciation) is amended—

(i) by inserting "or amortization" after "depreciation" the second and third places it appears, and

(ii) by inserting "or 191" after "167(k)" each place it appears.

(4) STRAIGHT LINE METHOD IN CERTAIN CASES.—Subsection (n) of section 167 is amended to read as follows:

"(n) STRAIGHT LINE METHOD IN CERTAIN CASES.—

"(1) IN GENERAL.—In the case of any property in whole or in part constructed, reconstructed, erected, or used on a site which was, on or after June 30, 1976, occupied by a certified historic structure (or by any structure in a registered historic district) which is demolished or substantially altered after such date—

"(A) subsections (b), (j), (k), and (l) shall not apply, and

"(B) the term 'reasonable allowance' as used in subsection (a) means only an allowance computed under the straight line method.

The preceding sentences shall not apply if the last substantial alteration of the structure is a certified rehabilitation.

"(2) EXCEPTIONS.—The limitations imposed by this subsection shall not apply—

"(A) to personal property, and

"(B) in the case of demolition or substantial alteration of a structure located in a registered historic district, if—

"(i) such structure was not a certified historic structure,

"(ii) the Secretary of the Interior certified to the Secretary that such structure is not of historic significance to the district, and

"(iii) if the certification referred to in clause (ii) occurs after the beginning of the demolition or substantial alteration of such structure, the taxpayer certifies to the Secretary that, at the beginning of such demolition or substantial alteration, he in good faith was not aware of the requirements of clause (ii).

"(3) DEFINITIONS.—For purposes of this subsection, the terms 'certified historic structure', 'registered historic district', and 'certified rehabilitation' have the respective meanings given such terms by section 191(d)."

(5) DEMOLITION OF CERTAIN HISTORIC STRUCTURES.—Subsection (b) of section 280B (relating to special rule for registered historic districts) is amended to read as follows:

"(b) SPECIAL RULE FOR REGISTERED HISTORIC DISTRICTS.—For purposes of this section, any building or other structure located in a registered historic district (as defined in section 191(d)(2)) shall be treated as a certified historic structure unless the Secretary of the Interior has certified that such structure is not a certified historic structure, and that such structure is not of historic significance to the district, and if such certification occurs after the beginning of the demolition of such structure, the taxpayer has certified to the Secretary that, at the time of such demolition, he in good faith was not aware of the certification requirement by the Secretary of the Interior.".

(6) SUBSTANTIALLY REHABILITATED HISTORIC PROPERTY.—

(A) Paragraph (1) of section 167(o) (relating to substantially rehabilitated historic property) is amended by inserting "(other than property with respect to which an amortization deduction has been allowed to the taxpayer under section 191)" after "substantially rehabilitated historic property".

(B) Paragraph (2) of section 167(o) is amended by striking out "section 191(d)(3)" and inserting in lieu thereof "section 191(d)(4)".

(7) AMORTIZATION ALLOWABLE TO PERSONS WITH CERTAIN LEASE INTERESTS.—Section 191(f) (relating to treatment of life tenants and remaindermen) is amended to read as follows:

"(f) SPECIAL RULES FOR CERTAIN INTERESTS.—

"(1) LIFE TENANT AND REMAINDERMAN.—In the case of property held by one person for life with remainder to another person, the deduction under this section shall be computed as if the life tenant were the absolute owner of the property and shall be allowable to the life tenant.

"(2) CERTAIN LESSEES.—

"(A) IN GENERAL.—In the case of a lessee of a certified historic structure who has expended amounts in connection with the certified rehabilitation of such structure which are properly chargeable to capital account, the deduction under this section shall be allowable to such lessee with respect to such amounts.

"(B) AMORTIZABLE BASIS.—For purposes of subsection (a), the amortizable basis of such lessee shall not exceed the sum of the amounts described in subparagraph (A).

"(C) LIMITATION.—Subparagraph (A) shall apply only if on the date of the certified rehabilitation is completed, the remaining term of the lease (determined without regard to any renewal periods) extends—

"(i) beyond the last day of the useful life (determined without regard to this section) of the improvements for which the amounts described in subparagraph (A) were expended, and

"(ii) for not less than 30 years.".

(8) EFFECTIVE DATE.—The amendments made by this subsection shall take effect as if included in the respective provisions of the Internal Revenue Code of 1954 to which such amendments relate, as such provision were added to such Code, or amended, by section 2124 of the Tax Reform Act of 1976.

(g) FOREIGN CONVENTIONS.—

(1) DEDUCTIONS NOT DISALLOWED TO EMPLOYER WHERE EMPLOYEE INCLUDES AMOUNTS IN GROSS INCOME.—Subparagraph (D) of section 274(h)(6) (relating to application of subsection to employer as well as to traveler) is amended to read as follows:

"(D) SUBSECTION TO APPLY TO EMPLOYER AS WELL AS TO TRAVELER.—

"(i) Except as provided in clause (ii), this subsection shall apply to deductions otherwise allowable under section 162 or 212 to any person, whether or not such person is the individual attending the foreign convention. For the purposes of the preceding sentence such person shall be treated, with respect to each individual, as having selected the same 2 foreign conventions as were selected by such individual.

"(ii) *This subsection shall not deny a deduction to any person other than the individual attending the foreign convention with respect to any amount paid by such person to or on behalf of another person if includible in the gross income of such other person. The preceding sentence shall not apply if such amount is required to be included in any information return filed by such person under part III of subchapter A of chapter 61 and is not so included.*".

(2) INDIVIDUALS RESIDING IN FOREIGN COUNTRIES.—*Section 274(h)(6) is amended by adding at the end thereof the following new subparagraph:*

"(E) INDIVIDUALS RESIDING IN FOREIGN COUNTRIES.—*For purposes of this subsection, in the case of an individual citizen of the United States who establishes to the satisfaction of the Secretary that he was a bona fide resident of a foreign country at the time that he attended a convention in such foreign country, such individual's attendance at such convention shall not be considered as attendance at a foreign convention.*".

(3) TECHNICAL AMENDMENT.—*The first sentence of section 274(h)(3) is amended by striking out "more than one-half" and inserting in lieu thereof "at least one-half".*

(4) EFFECTIVE DATE.—*The amendments made by this subsection shall apply to conventions beginning after December 31, 1976.*

(h) RENTAL OF FORMER PRINCIPAL RESIDENCE.—

(1) IN GENERAL.—*Subsection (d) of section 280A (relating to use of residence for personal purposes) is amended by adding at the end thereof the following new paragraph:*

"(3) RENTAL OF PRINCIPAL RESIDENCE.—

"(A) IN GENERAL.—*For purposes of applying subsection (c)(5) to deductions allocable to a qualified rental period, a taxpayer shall not be considered to have used a dwelling unit for personal purposes for any day during the taxable year which occurs before or after a qualified rental period described in subparagraph (B)(i), or before a qualified rental period described in subparagraph (B)(ii), if with respect to such day such unit constitutes the principal residence (within the meaning of section 1034) of the taxpayer.*

"(B) QUALIFIED RENTAL PERIOD.—*For purposes of subparagraph (A), the term 'qualified rental period' means a consecutive period of—*

"(i) *12 or more months which begins or ends in such taxable year, or*

"(ii) *less than 12 months which begins in such taxable year and at the end of which such dwelling unit is sold or exchanged, and*

for which such unit is rented to a person other than a member of the family (as defined in section 267(c)(4)) of the taxpayer, or is held for rental, at a fair rental."

(2) EFFECTIVE DATE.—*The amendment made by paragraph (1) shall take effect as if included in section 280A of the Internal Revenue Code of 1954, as such provision was added to such Code by section 601(a) of the Tax Reform Act of 1976.*

(i) CLARIFICATION OF LAST SENTENCE OF SECTION 337(c)(2).—

(1) IN GENERAL.—Subsection (c) of section 337 (relating to limitations on application of section 337) is amended by striking out the last sentence of paragraph (2) and by adding at the end of such subsection the following new paragraph:

"(3) SPECIAL RULE FOR AFFILIATED GROUP.—

"(A) IN GENERAL.—Paragraph (2) shall not apply to a sale or exchange by a corporation (hereinafter in this paragraph referred to as the 'selling corporation') if—

"(i) within the 12-month period beginning on the date of the adoption of a plan of complete liquidation by the selling corporation, the selling corporation and each distributee corporation is completely liquidated, and

"(ii) none of the complete liquidations referred to in clause (i) is a liquidation with respect to which section 333 applies.

"(B) DEFINITIONS.—For purposes of subparagraph (A)—

"(i) The term 'distributee corporation' means a corporation in the chain of includible corporations to which the selling corporation or a corporation above the selling corporation in such chain makes a distribution in complete liquidation within the 12-month period referred to in subparagraph (A)(i).

"(ii) The term 'chain of includible corporation' includes, in the case of any distribution, any corporation which (at the time of such distribution) is in a chain of includible corporations for purposes of section 1504(a) (determined without regard to the exceptions contained in section 1504(b)). Such term includes, where appropriate, the common parent corporation."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to sales or exchanges made pursuant to a plan of complete liquidation adopted after December 31, 1975.

(j) CERTAIN TRANSACTIONS INVOLVING 2 OR MORE INVESTMENT COMPANIES.—

(1) AMENDMENTS OF SECTION 368(a)(2)(F).—

(A) The first sentence of clause (iii) of section 368(a)(2)(F) is amended—

(i) by striking out "more than 50 percent" and inserting in lieu thereof "50 percent or more", and

(ii) by striking out "more than 80 percent" and inserting in lieu thereof "80 percent or more."

(B) The first sentence of clause (vi) of section 368(a)(2)(F) is amended by striking out "is not diversified within the meaning" and inserting in lieu thereof "does not meet the requirements".

(C) The second sentence of such clause (vi) is amended to read as follows: "If such investment company acquires stock of another corporation in a reorganization described in section 368(a)(1)(B), clause (i) shall be applied to the shareholders of such investment company as though they had exchanged with such other corporation all of their stock in such company for stock having a fair market value equal to the fair market value of their stock of such investment company immediately after the exchange."

(D) Subparagraph (F) of section 368(a)(2) is amended by adding at the end thereof the following new clauses:

"(vii) For purposes of clauses (ii) and (iii), the term 'securities' includes obligations of State and local governments, commodity futures contracts, shares of regulated investment companies and real estate investment trusts, and other investments constituting a security within the meaning of the Investment Company Act of 1940 (15 U.S.C. 80a–2(36)).

"(viii) In applying paragraph (3) of section 267(b) in respect of any transaction to which this subparagraph applies, the reference to a personal holding company in such paragraph (3) shall be treated as including a reference to an investment company and the determination of whether a corporation is an investment company shall be made as of the time immediately before the transaction instead of with respect to the taxable year referred to in such paragraph (3)."

(2) EFFECTIVE DATES.—

(A) Except as provided in subparagraphs (B) and (C), the amendments made by paragraph (1) shall apply as if included in section 368(a)(2)(F) of the Internal Revenue Code of 1954 as added by section 2131(a) of the Tax Reform Act of 1976.

(B) Clause (viii) of section 368(a)(2)(F) of the Internal Revenue Code of 1954 (as added by paragraph (1)) shall apply only with respect to losses sustained after September 26, 1977.

(C) Clause (vii) of section 368(a)(2)(F) of the Internal Revenue Code of 1954 (as added by paragraph (1)) shall apply only with respect to transfers made after September 26, 1977.

(k) AT RISK PROVISIONS.—

(1) CLERICAL AMENDMENT TO EFFECTIVE DATE.—Subparagraph (A) of section 204(c)(3) of the Tax Reform Act of 1976 is amended by striking out "section 465(c)(1)(B)" and inserting in lieu thereof "section 465(c)(1)(C)".

(2) CLARIFICATION OF SECTION 465(d).—Subsection (d) of section 465 (defining loss for purposes of the at risk provisions) is amended by striking out "(determined without regard to this section)" and inserting in lieu thereof "(determined without regard to the first sentence of subsection (a))".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall take effect on October 4, 1976.

(l) AMENDMENTS RELATING TO USE OF ACCRUAL ACCOUNTING FOR FARMING.—

(1) AUTOMATIC 10-YEAR ADJUSTMENT PERIOD FOR FARMING CORPORATIONS REQUIRED TO USE ACCRUAL ACCOUNTING.—Paragraph (3) of section 447(f) (relating to coordination with section 481) is amended—

(A) by striking out "(except as otherwise provided in such regulations)", and

(B) by inserting "(or the remaining taxable years where there is a stated future life of less than 10 taxable years)" after "10 taxable years".

(2) AUTOMATIC 10-YEAR ADJUSTMENT FOR FARMING SYNDICATES CHANGING TO ACCRUAL ACCOUNTING.—If—

(A) a farming syndicate (within the meaning of section 464(c) of the Internal Revenue Code of 1954) was in existence on December 31, 1975, and

(B) such syndicate elects an accrual method of accounting (including the capitalization of preproductive period expenses described in section 447(b) of such Code) for a taxable year beginning before January 1, 1979,

then such election shall be treated as having been made with the consent of the Secretary of the Treasury or his delegate and, under regulations prescribed by the Secretary of the Treasury or his delegate, the net amount of the adjustments required by section 481(a) of such Code to be taken into account by the taxpayer in computing taxable income shall be taken into account in each of the 10 taxable years (or the remaining taxable years where there is a stated future life of less than 10 taxable years) beginning with the year of change.

(3) EXTENDING FAMILY ATTRIBUTION TO SPOUSE IN THE FARMING SYNDICATE RULES.—

(A) Subparagraph (E) of section 464(c)(2) (defining farming syndicate) is amended by striking out "(within the meaning of section 267(c)(4))" and inserting in lieu thereof "(or a spouse of any such member)".

(B) Paragraph (2) of section 464(c) is amended by adding at the end thereof the following new sentence: "For purposes of subparagraph (E), the term 'family' has the meaning given to such term by section 267(c)(4)."

(4) EFFECTIVE DATE.—The amendment made by paragraphs (1) and (3) shall take effect as if included in section 447 or 464 (as the case may be) of the Internal Revenue Code of 1954 at the time of the enactment of such sections.

(m) EXTENSION OF CERTAIN PROVISIONS TO FOREIGN PERSONAL HOLDING COMPANIES.—

(1) SECTION 189.—Subsection (a) of section 189 (relating to amortization of real property construction period interest and taxes) is amended—

(A) by striking out "an electing small business corporation (within the meaning of section 1371(b)), or personal holding company (within the meaning of section 542),"; and

(B) by adding at the end thereof the following new sentence: "For purposes of this section, an electing small business corporation (as defined in section 1371(b)), a personal holding company (as defined in section 542), and a foreign personal holding company (as defined in section 552) shall be treated as an individual."

(2) SECTION 280.—Subsection (a) of section 280 (relating to certain expenditures incurred in production of films, books, records, or similar property) is amended—

(A) by striking out "Except in the case of a corporation (other than an electing small business corporation (as defined in section 1371(b)) or a personal holding company (as defined in section 542) and except" and inserting in lieu thereof "In the case of an individual, except"; and

(B) by adding at the end thereof the following new sentence: "For purposes of this section, an electing small business corporation (as defined in section 1371(b)), a personal holding company (as defined in section 542), and a foreign personal holding company (as defined in section 552) shall be treated as an individual."

(3) EFFECTIVE DATES.—

(A) The amendments made by paragraph (1) shall take effect as if included in the amendment made by section 201(a) of the Tax Reform Act of 1976.

(B) The amendments made by paragraph (2) shall take effect as if included in the amendment made by section 210(a) of the Tax Reform Act of 1976.

(n) DEFINITION OF CONDOMINIUM MANAGEMENT ASSOCIATION.—

(1) IN GENERAL.—Paragraph (2) of section 528(c) (defining condominium management association) is amended by striking out "as residences" and inserting in lieu thereof "by individuals for residences".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1973.

(o) DEFINITION OF PERSONAL HOLDING COMPANY.—

(1) IN GENERAL.—The last sentence of section 542(a)(2) of the Internal Revenue Code of 1954 (relating to stock ownership requirement) shall not apply in the case of an organization or trust organized or created before July 1, 1950, if at all times on or after July 1, 1950, and before the close of the taxable year such orgranization or trust has owned all of the common stock and at least 80 percent of the total number of shares of all other classes of stock of the corporation.

(2) EFFECTIVE DATE.—The provisions of paragraph (1) shall apply with respect to taxable years beginning after December 31, 1976.

(p) SPECIAL RULE FOR GAIN ON PROPERTY TRANSFERRED TO TRUST AT LESS THAN FAIR MARKET VALUE.—

(1) ADDITIONAL TAX TO APPLY ONLY TO RECOGNIZED GAINS.—

(A) IN GENERAL.—Subsections (a)(1), (a)(2), and (b)(1) of section 644 (relating to special rule for gain on property transferred to trust at less than fair market value) are each amended by striking out "gain realized" each place it appears and inserting in lieu thereof "gain recognized".

(B) SPECIAL RULE FOR SUBSTITUTED BASIS PROPERTY.—Subsection (d) of section 644 (relating to special rule for short sales) is amended to read as follows:

"(d) SPECIAL RULES.—

"(1) SHORT SALES.—If the trust sells the property referred to in subsection (a) in a short sale within the 2-year period referred to in such subsection, such 2-year period shall be extended to the date of the closing of such short sale.

"(2) SUBSTITUTED BASIS PROPERTY.—For purposes of this section, in the case of any property held by the trust which has a basis determined in whole or in part by reference to the basis of any other property which was transferred to the trust—

"(A) the initial transfer of such property in trust by the transfer shall be treated as having occurred on the date of the initial transfer in trust of such other property,

"(B) subsections (a)(1)(B) and (b)(2) shall be applied by taking into account the fair market value and the adjusted basis of such other property, and

"(C) the amount determined under subsection (b)(2) with respect to such other property shall be allocated (under regulations prescribed by the Secretary) among such other property and all properties held by the trust which have a basis determined in whole or in part by reference to the basis of such other property."

(2) TREATMENT OF NET OPERATING LOSSES, CAPITAL LOSSES, ETC., WHICH MAY AFFECT TRANSFEROR'S TAX IN OTHER YEARS.—Section 644(a)(2) (relating to additional tax on gain on property transferred to trust at less than fair market value) is amended by adding at the end thereof the following new sentence: "The determination of tax under clause (i) of subparagraph (A) shall be made by not taking into account any carryback, and by not taking into account any loss or deduction to the extent that such loss or deduction may be carried by the transferor to any other taxable year."

(3) TECHNICAL AMENDMENT.—Paragraph (1) of section 644(f) is amended by striking out "subsection (a)" and inserting in lieu thereof "subsection (a) (other than the 2-year requirement of paragraph (1)(A) thereof)".

(4) CONFORMING AMENDMENT TO REVISION OF SECTION 644.—Section 1402(b)(1) of the Tax Reform Act of 1976 (relating to holding period for long-term capital gains treatment) is amended by striking out subparagraph (K) thereof.

(5) EFFECTIVE DATES.—

(A) Except as provided in subparagraph (B), the amendment made by this subsection shall apply to transfers in trust made after May 21, 1976.

(B) The amendment made by paragraph (4) shall take effect on October 4, 1976.

(q) ALLOWANCE OF FOREIGN TAX CREDIT FOR ACCUMULATION DISTRIBUTIONS.—

(1) SPECIAL RULES FOR FOREIGN TRUST.—

(A) Subsection (d) of section 665 is amended to read as follows:

"(d) TAXES IMPOSED ON THE TRUST.—For purposes of this subpart—

"(1) IN GENERAL.—The term 'taxes imposed on the trust' means the amount of the taxes which are imposed for any taxable year of the trust under this chapter (without regard to this subpart or subpart A of part IV of subchapter A) and which, under regulations prescribed by the Secretary, are properly allocable to the undistributed portions of distributable net income and gains in excess of losses from sales or exchanges of capital assets. The amount determined in the preceding sentence shall be reduced by any amount of such taxes deemed distributed under section 666 (b) and (c) or 669 (d) and (e) to any beneficiary.

"(2) FOREIGN TRUSTS.—In the case of any foreign trust, the term 'taxes imposed on the trust' includes the amount, reduced as provided in the last sentence of paragraph (1), of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on such foreign trust which, as determined under paragraph (1), are so properly allocable."

(B) Section 667 is amended by adding at the end thereof the following new subsection:

"(d) SPECIAL RULES FOR FOREIGN TRUST.—

"(1) FOREIGN TAX DEEMED PAID BY BENEFICIARY.—

"(A) IN GENERAL.—In determining the increase in tax under subsection (b)(1)(D) for any computation year, the taxes described in section 665(d)(2) which are deemed distributed under section 666(b) or (c) and added under subsection (b)(1)(C) to the taxable income of the beneficiary for any computation year shall, except as provided in subparagraphs (B) and (C), be treated as a credit against the increase in tax for such computation year under subsection (b)(1)(D).

"(B) DEDUCTION IN LIEU OF CREDIT.—If the beneficiary did not choose the benefits of subpart A of part III of subchapter N with respect to the computation year, the beneficiary may in lieu of treating the amounts described in subparagraph (A) (without regard to subparagraph (C)) as a credit may treat such amounts as a deduction in computing the beneficiary's taxable income under subsection (b)(1)(C) for the computation year.

"(C) LIMITATION ON CREDIT; RETENTION OF CHARACTER.—

"(i) LIMITATION ON CREDIT.—For purposes of determining under subparagraph (A) the amount treated as a credit for any computation year, the limitations under subpart A of part III of subchapter N shall be applied separately with respect to amounts added under subsection (b)(1)(C) to the taxable income of the beneficiary for such computation year. For purposes of computing the increase in tax under subsection (b)(1)(D) for any computation year for which the beneficiary did not choose the benefits of subpart A of part III of subchapter N, the beneficiary shall be treated as having chosen such benefits for such computation year.

"(ii) RETENTION OF CHARACTER.—The items of income, deduction, and credit of the Trust shall retain their character (subject to the application of section 904(f)(5)) to the extent necessary to apply this paragraph.

"(D) COMPUTATION YEAR.—For purposes of this paragraph, the term 'computation year' means any of the three taxable years remaining after application of subsection (b)(1)(B)."

(C) The last sentence of section 667(b)(1) is amended by inserting "(other than the amount of taxes described in section 665(d)(2))" after "taxes".

(2) RECAPTURE OF OVERALL FOREIGN LOSS.—Section 904(f) is amended by adding at the end thereof the following new paragraph:

"(5) ACCUMULATION DISTRIBUTIONS OF FOREIGN TRUST.—For purposes of this chapter, in the case of amounts of income from sources without the United States which are treated under section 666 (without regard to subsections (b) and (c) thereof if the taxpayer chose to take a deduction with respect to the amounts described in such subsections under section 667(d)(1)(B)) as having been distributed by a foreign trust in a preceding taxable year, that portion of such amounts equal to the amount of any overall foreign loss sustained by the beneficiary in a year prior to the taxable year of the beneficiary in which

such distribution is received from the trust shall be treated as income from sources within the United States (and not income from sources without the United States) to the extent that such loss was not used under this subsection in prior taxable years, or in the current taxable year, against other income of the beneficiary.".

(3) EFFECTIVE DATES.—

(A) The amendments made by paragraph (1) shall apply to distributions made in taxable years beginning after December 31, 1975.

(B) The amendments made by paragraph (2) shall take effect as if included in section 904(f) of the Internal Revenue Code of 1954, as such provision was added to such Code by section 1032(a) of the Tax Reform Act of 1976.

(r) RETENTION OF CHARACTER OF AMOUNTS DISTRIBUTED FROM ACCUMULATION TRUST TO NONRESIDENT ALIENS AND FOREIGN CORPORATIONS.—

(1) IN GENERAL.—Section 667 (relating to treatment of amounts deemed distributed by trust in preceding years) is amended by adding at the end thereof the following new subsection:

"(e) RETENTION OF CHARACTER OF AMOUNTS DISTRIBUTED FROM ACCUMULATION TRUST TO NONRESIDENT ALIENS AND FOREIGN CORPORATIONS.—In the case of a distribution from a trust to a nonresident alien individual or to a foreign corporation, the first sentence of subsection (a) shall be applied as if the reference to the determination of character under section 662(b) applied to all amounts instead of just to tax-exempt interest."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to distributions made in taxable years beginning after December 31, 1975.

(s) EXEMPT INTEREST DIVIDENDS OF REGULATED INVESTMENT COMPANIES.—

(1) TREATMENT OF TAX-EXEMPT INTEREST FOR PURPOSES OF THE 90-PERCENT AND 30-PERCENT TESTS.—Subsection (b) of section 851 (relating to limitations on the definition of regulated investment company) is amended by adding at the end thereof the following new sentence: "For purposes of paragraphs (2) and (3), amounts excludable from gross income under section 103(a)(1) shall be treated as included in gross income."

(2) LOSSES ATTRIBUTABLE TO TAX-EXEMPT INTEREST WHERE STOCK IS HELD LESS THAN 31 DAYS.—Paragraph (4) of section 852(b) (relating to loss on sale or exchange of stock held less than 31 days) is amended to read as follows:

"(4) LOSS ON SALE OR EXCHANGE OF STOCK HELD LESS THAN 31 DAYS.—

"(A) LOSS ATTRIBUTABLE TO CAPITAL GAIN DIVIDEND.—If—

"(i) under subparagraph (B) or (D) of paragraph (3) a shareholder of a regulated investment company is required, with respect to any share, to treat any amount as a long-term capital gain, and

"(ii) such share is held by the taxpayer for less than 31 days,

then any loss (to the extent not disallowed under subparagraph (B)) on the sale or exchange of such share shall, to the extent of the amount described in clause (i), be treated as a long-term capital loss.

"(B) LOSS ATTRIBUTABLE TO EXEMPT INTEREST DIVIDEND.—If—

"(i) a shareholder of a regulated investment company receives an exempt-interest dividend with respect to any share, and

"(ii) such share is held by the taxpayer for less than 31 days,

then any loss on the sale or exchange of such share shall, to the extent of the amount of such exempt-interest dividend, be disallowed.

"(C) DETERMINATION OF HOLDING PERIODS.—For purposes of this paragraph, the rules of section 246(c)(3) shall apply in determining whether any share of stock has been held for less than 31 days; except that '30 days' shall be substituted for the number of days specified in subparagraph (B) of section 246 (C)(3)."

(3) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1975.

(t) AMENDMENTS RELATING TO REAL ESTATE INVESTMENT TRUSTS.—

(1) ANNUAL ACCOUNTING PERIOD.—Section 859 (relating to adoption of annual accounting period), as redesignated by the Act, is further amended to read as follows:

"SEC. 859. ADOPTION OF ANNUAL ACCOUNTING PERIOD.

"For purposes of this subtitle—

"(1) a real estate investment trust shall not change to any accounting period other than the calendar year, and

"(2) a corporation, trust, or association may not elect to be a real estate investment trust for any taxable year beginning after October 4, 1976, unless its accounting period is the calendar year.

Paragraph (2) shall not apply to a corporation, trust, or association which was considered to be a real estate investment trust for any taxable year beginning on or before October 4, 1976."

(2) AMENDMENT OF SECTION 856(C)(3)(D).—Subparagraph (D) of section 856(c)(3) is amended by inserting "(other than gain from prohibited transactions)" after "and gain".

(3) EXCISE TAX ON REIT UNDISTRIBUTED INCOME.—

(A) Paragraph (3) of section 6501(e) (relating to limitations on assessment and collection) is amended by striking out "or 43" and inserting in lieu thereof "43, or 44".

(B) Subsection (b) of section 1605 of the Tax Reform Act of 1976 (relating to technical amendments) is amended by striking out paragraph (1) thereof.

(C) Subparagraph (D) of section 1605(b)(5) of the Tax Reform Act of 1976 is amended to read as follows:

"(D) by striking out 'of chapter 43 tax for the same taxable years,' in subsection (c)(1) and inserting in lieu thereof 'of chapter 43 tax for the same taxable year, of chapter 44 tax for the same taxable year,'."

(4) CORRECTION OF CROSS REFERENCE.—Subparagraph (B) of section 859(b)(2) is amended by striking out "**section 6601(c)**" and inserting in lieu thereof "**section 6601(b)**".

(5) EFFECTIVE DATE.—The amendments made by this subsection shall take effect on October 4, 1976.

(u) AMENDMENTS RELATING TO TREATMENT OF FOREIGN INCOME.—

(1) FOREIGN TAX CREDITS NOT DISALLOWED ON CERTAIN DISTRIBUTIONS MADE BY POSSESSIONS CORPORATIONS.—

(A) IN GENERAL.—Paragraph (1) of section 901(g) (relating to certain taxes paid with respect to distributions from possessions corporations) is amended to read as follows:

"(1) IN GENERAL.—For purposes of this chapter, any tax of a foreign country or possession of the United States which is paid or accrued with respect to any distribution from a corporation—

"(A) to the extent that such distribution is attributable to periods during which such corporation is a possessions corporation, and

"(B)(i) if a dividends received deduction is allowable with respect to such distribution under part VIII of subchapter B, or

"(ii) to the extent that such distribution is received in connection with a liquidation or other transaction with respect to which gain or loss is not recognized,

shall not be treated as income, war profits, or excess profits taxes paid or accrued to a foreign country or possession of the United States, and no deduction shall be allowed under this title with respect to any amount so paid or accrued."

(B) DEFINITION OF POSSESSIONS CORPORATION.—Paragraph (2) of section 901(g) (defining possessions corporation) is amended—

(i) by striking out "or during which section 931" and inserting in lieu thereof ", during which section 931", and

(ii) by inserting before the period at the end thereof the following: ", or during which section 957(c) applied to such corporation".

(C) EFFECTIVE DATES.—The amendment made by subparagraph (A) shall apply as if included in section 901(g) of the Internal Revenue Code of 1954 as added by section 1051(d)(2) of the Tax Reform Act of 1976. The amendments made by subparagraph (B) shall apply to distributions made after the date of the enactment of this Act in taxable years ending after such date.

(2) FOREIGN TAX CREDIT ADJUSTMENTS FOR CAPITAL GAINS.—

(A) IN GENERAL.—Paragraph (2) of section 904(b) (relating to treatment of capital gains for purposes of the foreign tax credit limitation) is amended by striking out "For purposes of subsection (a)—" and inserting in lieu thereof "For purposes of this section—".

(B) SOURCE RULE.—Subparagraph (C) of section 904(b)(3) is amended by striking out "For purposes of this paragraph, there" and inserting in lieu thereof "There".

(C) SOURCE RULE FOR LIQUIDATIONS OF CERTAIN FOREIGN CORPORATIONS.—Paragraph (3) of section 904(b) (relating to source rules for gain from the sale of certain personal property) is

amended by redesignating subparagraph (D) as subparagraph (E) and by inserting after subparagraph (C) the following new subparagraph:

"(D) GAIN FROM LIQUIDATION OF CERTAIN FOREIGN CORPORATIONS.—Subparagraph (C) shall not apply with respect to a distribution in liquidation of a foreign corporation to which part II of subchapter C applies if such corporation derived less than 50 percent of its gross income from sources within the United States for the 3-year period ending with the close of such corporation's taxable year immediately preceding the year during which the distribution occurred."

(D) EFFECTIVE DATE.—The amendments made by this paragraph shall apply to taxable years beginning after December 31, 1975.

(3) TREATMENT OF CERTAIN CAPITAL LOSS CARRYOVERS AND CARRYBACKS FOR PURPOSES OF THE LIMITATION ON CREDIT FOR FOREIGN TAXES.—

(A) IN GENERAL.—Clause (iii) of section 904(b)(2)(A) (relating to treatment of capital gains of corporations for purposes of the foreign tax credit limitation) is amended by striking out "any net capital loss" and inserting in lieu thereof "for purposes of determining taxable income from sources without the United States, any net capital loss (and any amount which is a short-term capital loss under section 1212(a))".

(B) EFFECTIVE DATE.—The amendment made by subparagraph (A) shall apply to taxable years beginning after December 31, 1975.

(4) TREATMENT OF CAPITAL LOSS CARRYOVERS FOR PURPOSES OF FOREIGN LOSS RECAPTURE.—

(A) IN GENERAL.—Subparagraph (a) of section 904(f)(2) (defining overall foreign loss) is amended by striking out "or any capital loss carrybacks and carryovers to such year under section 1212".

(B) FOREIGN OIL RELATED LOSSES.—Subparagraph (A) of section 904(f)(4) (relating to determination of foreign oil related loss where section 907 applies) is amended by striking out "or any capital loss carrybacks and carryovers to such year under section 1212".

(C) EFFECTIVE DATE.—The amendments made by this paragraph shall apply—

(i) to overall foreign losses sustained in taxable years beginning after December 31, 1975, and

(ii) to foreign oil related losses sustained in taxable years ending after December 31, 1975.

(5) EFFECTIVE DATE FOR RECAPTURE OF FOREIGN OIL RELATED LOSSES.—

(A) IN GENERAL.—Paragraph (1) of section 1032(c) of the Tax Reform Act of 1976 is amended to read as follows:

"(1) IN GENERAL.—Except as provided in paragraphs (2), (3), and (5), the amendment made by subsection (a) shall apply to losses sustained in taxable years beginning after December 31, 1975. The amendment made by subsection (b)(1) shall apply to taxable years beginning after December 31, 1975. The amendment made by subsection (b)(2) shall apply to losses sustained in taxable years ending after December 31, 1975."

(B) FOREIGN OIL RELATED LOSSES.—Subsection (c) of section 1032 of the Tax Reform Act of 1976 is amended by adding at the end thereof the following new paragraph:

"(5) FOREIGN OIL RELATED LOSSES.—The amendment made by subsection (a) shall apply to foreign oil related losses sustained in taxable years ending after December 31, 1975."

(6) TRANSITIONAL RULES FOR CERTAIN MINING OPERATIONS.—The second sentence of paragraph (2) of section 1031(c) of the Tax Reform Act of 1976 is amended to read as follows: "In the case of a loss sustained in a taxable year beginning before January 1, 1979, by any corporation to which this paragraph applies, if section 904 (a)(1) of such Code (as in effect before the enactment of this Act) applies with respect to such taxable year, the provisions of section 904(f) of such Code shall be applied with respect to such loss under the principles of such section 904(a)(1)."

(7) TRANSITIONAL RULES FOR RECAPTURE OF CERTAIN FOREIGN LOSSES.—

(A) COMPUTATION OF DEFICIT IN EARNINGS AND PROFITS FOR PURPOSES OF THE RECAPTURE OF CERTAIN FOREIGN LOSSES.—Paragraph (4) of section 1032(c) of the Tax Reform Act of 1976 (relating to limitation based on deficit in earnings and profits for purposes of the recapture of foreign losses) is amended by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, there shall be taken into account only earnings and profits of the corporation which (A) were accumulated in taxable years of the corporation beginning after December 31, 1962, and during the period in which the stock of such corporation from which the loss arose was held by the taxpayer and (B) are attributable to such stock."

(B) RECAPTURE OF POSSESSION LOSSES DURING TRANSITIONAL PERIOD WHERE TAXPAYER IS ON A PER-COUNTRY BASIS.—

(i) Subsection (c) of section 1032 of the Tax Reform Act of 1976 (relating to effective dates for recapture of foreign losses) is amended by adding at the end thereof the following new paragraph:

"(6) RECAPTURE OF POSSESSION LOSSES DURING TRANSITIONAL PERIOD WHERE TAXPAYER IS ON A PER-COUNTRY BASIS.—

"(A) APPLICATION OF PARAGRAPH.—This paragraph shall apply if—

"(i) the taxpayer sustained a loss in a possession of the United States in a taxable year beginning after December 31, 1975, and before January 1, 1979,

"(ii) such loss is attributable to a trade or business engaged in by the taxpayer in such possession on January 1, 1976, and

"(iii) the taxpayer chooses to have the benefits of subpart A of part III of subchapter N apply for such taxable year and section 904(a)(1) of the Internal Revenue Code of 1954 (as in effect before the enactment of this Act) applies with respect to such taxable year.

"(B) NO RECAPTURE DURING TRANSITION PERIOD.—In any case to which this paragraph applies, for purposes of determining the liability for tax of the taxpayer for taxable years beginning

before January 1, 1979, section 904(f) of the Internal Revenue Code of 1954 shall not apply with respect to the loss described in subparagraph (A)(i).

"(C) RECAPTURE OF LOSS AFTER THE TRANSITION PERIOD.—In any case to which this paragraph applies—

"(i) for purposes of determining the liability for tax of the taxpayer for taxable years beginning after December 31, 1978, section 904(f) of the Internal Revenue Code of 1954 shall be applied with respect to the loss described in subparagraph (A)(i) under the principles of section 904(a)(1) of such Code (as in effect before the enactment of this Act); but

"(ii) in the case of any taxpayer and any possession, the aggregate amount to which such section 904(f) applies by reason of clause (i) shall not exceed the sum of the net incomes of all affiliated corporations from such possession for taxable years of such affiliated corporations beginning after December 31, 1975, and before January 1, 1979.

"(D) TAXPAYERS NOT ENGAGED IN TRADE ON BUSINESS ON JANUARY 1, 1976.—In any case to which this paragraph applies but for the fact that the taxpayer was not engaged in a trade or business in such possession on January 1, 1976, for purposes of determining the liability for tax of the taxpayer for taxable years beginning before January 1, 1979; if section 904(a)(1) of such Code (as in effect before the enactment of this Act) applies with respect to such taxable year, the provisions of section 904(f) of such Code shall be applied with respect to the loss described in subparagraph (A)(i) under the principles of such section 904(a)(1).

"(E) AFFILIATED CORPORATION DEFINED.—For purposes of subparagraph (C)(ii), the term 'affiliated corporation' means a corporation which, for the taxable year for which the net income is being determined, was not a member of the same affiliated group (within the meaning of section 1504 of the Internal Revenue Code of 1954) as the taxpayer but would have been a member of such group but for the application of subsection (b) of such section 1504."

(ii) Paragraph (3) of section 1031(c) of the Tax Reform Act of 1976 is amended by striking out the last sentence.

(8) LIMITATIONS ON FOREIGN TAX CREDIT WHERE INDIVIDUAL HAS FOREIGN OIL AND GAS EXTRACTION INCOME.—

(A) REDUCTION IN FOREIGN TAX CREDIT FOR CERTAIN INDIVIDUALS HAVING FOREIGN OIL AND GAS EXTRACTION INCOME.—Subsection (a) (as amended by this Act) of section 907 (relating to special rules in case of foreign oil and gas income) is further amended to read as follows:

"(a) REDUCTION IN AMOUNT ALLOWED AS FOREIGN TAX UNDER SECTION 901.—In applying section 901, the amount of any oil and gas extraction taxes paid or accrued (or deemed to have been paid) during the taxable year which would (but for this subsection) be taken into account for purposes of section 901 shall be reduced by the amount (if any) by which the amount of such taxes exceeds the product of—

"(1) the amount of the foreign oil and gas extraction income for the taxable year,

"(2) multiplied by—

"(A) in the case of a corporation, the percentage which is equal to the highest rate of tax specified under section 11(b), or

"(B) in the case of an individual, a fraction the numerator of which is the tax against which the credit under section 901(a) is taken and the denominator of which is the taxpayer's entire taxable income."

(B) APPLICATION OF SECTION 904 SEPARATELY TO FOREIGN OIL RELATED INCOME OF INDIVIDUALS.—Subsection (b) of section 907 (relating to application of section 904 limitation) is amended to read as follows:

"(b) APPLICATION OF SECTION 904 LIMITATION.—The provisions of section 904 shall be applied separately with respect to—

"(1) foreign oil related income, and

"(2) other taxable income."

(C) TECHNICAL AMENDMENT.—Paragraph (4) of section 904(f) (relating to recapture of overall foreign loss) is amended by striking out "In the case of a corporation to which section 907(b)(1) applies" and inserting in lieu thereof "In making the separate computation under this subsection with respect to foreign oil related income which is required by section 907(b)".

(D) EFFECTIVE DATES.—

(i) The amendments made by this paragraph shall apply, in the case of individuals, to taxable years ending after December 31, 1974, and, in the case of corporations, to taxable years ending after December 31, 1976.

(ii) In the case of any taxable year ending after December 31, 1975, with respect to foreign oil related income (within the meaning of section 907(c) of the Internal Revenue Code of 1954), the overall limitation provided by section 904(a)(2) of such Code shall apply and the per-country limitation provided by section 904(a)(1) of such Code shall not apply.

(9) EFFECTIVE DATE FOR DISALLOWANCE OF FOREIGN TAX CREDIT FOR CERTAIN PRODUCTION-SHARING CONTRACTS.—The second sentence of paragraph (3) of section 1035(c) of the Tax Reform Act of 1976 (relating to tax credit for production-sharing contracts) is amended to read as follows: "A contract described in the preceding sentence shall be taken into account under paragraph (1) only with respect to amounts (A) paid or accrued to the foreign government before January 1, 1978, and (B) attributable to income earned before such date."

(10) FOREIGN TAXES ATTRIBUTABLE TO SECTION 911 EXCLUSION.—

(A) IN GENERAL.—The last sentence of section 911(a) (relating to earned income from sources without the United States) is amended to read as follows:

"An individual shall not be allowed as a deduction from his gross income any deductions (other than those allowed by section 151, relating to personal exemptions), to the extent that such deductions are properly allocable to or chargeable against amounts excluded from gross income under this subsection. For purposes of this title, the amount of the income, war profits, and excess profits taxes paid or accrued by any individual to a foreign country or possession of the United States for any taxable year shall be reduced by an amount determined by multiplying the amount of such taxes by a fraction—

"(A) the numerator of which is the tax determined under subsection (d)(1)(B), and

"(B) the denominator of which is the sum of the amount referred to in subparagraph (A), plus the limitation imposed for the taxable year by section 904(a).".

(B) EFFECTIVE DATE.—The amendment made by subparagraph (A) shall apply to taxable years beginning after December 31, 1976.

(11) SALE OF ASSETS BY A POSSESSIONS CORPORATION.—

(A) IN GENERAL.—Subsection (a) of section 936 (relating to Puerto Rico and possession tax credit) is amended by redesignating paragraph (2) as paragraph (3) and by amending so much of paragraph (1) as precedes subparagraph (A) thereof to read as follows:

"(1) IN GENERAL.—Except as provided in paragraph (3), if a domestic corporation elects the application of this section and if the conditions of both subparagraph (A) and subparagraph (B) of paragraph (2) are satisfied, there shall be allowed as a credit against the tax imposed by this chapter an amount equal to the portion of the tax which is attributable to the sum of—

"(A) the taxable income, from sources without the United States, from—

"(i) the active conduct of a trade or business within a possession of the United States, or

"(ii) the sale or exchange of substantially all of the assets used by the taxpayer in the active conduct of such trade or business, and

"(B) the qualified possession source investment income.

"(2) CONDITIONS WHICH MUST BE SATISFIED.—The conditions referred to in paragraph (1) are:".

(B) INCOME FROM SALE OF CARRYOVER BASIS PROPERTY NOT TAKEN INTO ACCOUNT.—

(i) Subsection (d) of section 936 (relating to definitions) is amended by adding at the end thereof the following new paragraph:

"(3) CARRYOVER BASIS PROPERTY.—

"(A) IN GENERAL.—Income from the sale or exchange of any asset the basis of which is determined in whole or in part by reference to its basis in the hands of another person shall not be treated as income described in subparagraph (A) or (B) of subsection (a)(1).

"(B) EXCEPTION FOR POSSESSIONS CORPORATIONS, ETC.—For purposes of subparagraph (A), the holding of any asset by another person shall not be taken into account if throughout the period for which such asset was held by such person section 931, this section, or section 957(c) applied to such person.".

(ii) The heading of such subsection (d) is amended to read as follows:

"(d) DEFINITIONS AND SPECIAL RULES.—".

(C) EFFECTIVE DATE.—The amendments made by this paragraph shall apply as if included in section 936 of the Internal Revenue Code of 1954 at the time of its addition by section 1051(b) of the Tax Reform Act of 1976.

(12) GAIN ON DISPOSITION OF STOCK IN A DISC.—

(A) DELAY IN EFFECTIVE DATE.—Paragraph (4) of section 1101(g) of the Tax Reform Act of 1976 (relating to effective date for amendment relating to gain or disposition of DISC stock) is amended by striking out "December 31, 1975" snd inserting in lieu thereof "December 31, 1976".

(B) TECHNICAL AMENDMENT.—Paragraph (1) of section 995(c) (relating to gain on disposition of stock in a DISC) is amended by adding st the end thereof the following new sentence: "Subparagraph (C) shall not apply if the person receiving the stock in the disposition has a holding period for the stock which includes the period for which the stock was held by the shareholder disposing of such stock."

(C) EFFECTIVE DATE.—The amendment made by subparagraph (B) shall apply to dispositions made after December 31, 1976, in taxable years ending after such date.

(13) LIMITATION ON PARTNER'S TAX WHERE PARTNER RECEIVES AMOUNT TREATED AS SALE OF SECTION 1248 STOCK.—

(A) IN GENERAL.—Section 751 (relating to unrealized receivables and inventory items) is amended by adding at the end thereof the following new subsection:

"(e) LIMITATION ON TAX ATTRIBUTABLE TO DEEMED SALES OF SECTION 1248 STOCK.—For purposes of applying this section and sections 731, 736, and 741 to any amount resulting from the reference to section 1248 (a) in the second sentence of subsection (c), in the case of an individual, the tax attributable to such amount shall be limited in the manner provided by subsection (b) of section 1248 (relating to gain from certain sales or exchanges of stock in certain foreign corporation)."

(B) CROSS REFERENCE.—Section 736 (relating to payments to a retiring partner or a deceased partner's successor in interest) is amended by adding at the end thereof the following new subsection:

"(c) CROSS REFERENCE.—

"For limitation on the tax attributable to certain gain connected with section 1248 stock, see section 751(e)."

(C) EFFECTIVE DATE.—The amendments made by this paragraph shall apply to transfers beginning after October 9, 1975, and to sales, exchanges, and distributions taking place after such date.

(14) EXCISE TAX ON TRANSFERS OF PROPERTY TO FOREIGN PERSONS TO AVOID FEDERAL INCOME TAX.—

(A) TRANSFERS INVOLVING ESTATES.—Section 1491 (relating to tax on transfsrs to avoid income tax) is amended by striking out "trust" each place it appears therein and inserting in lieu thereof "estate or trust".

(B) CLARIFICATION OF PARAGRAPH (3) OF SECTION 1492.—Paragraph (3) of section 1492 (relating to nontaxable transfers) is amended to read as follows:

"(3) To a transfer described in section 367; or".

(C) EFFECTIVE DATE.—The amendments made by this paragraph shall apply to transfers after October 2, 1975.

(15) ELECTION TO TREAT NONRESIDENT ALIEN INDIVIDUAL AS RESIDENT OF THE UNITED STATES.—

(A) PROVISIONS AFFECTED BY ELECTION.—Paragraph (1) of section 6013(g) (relating to election to treat nonresident alien individual as resident of the United States) is amended to read as follows:

"(1) IN GENERAL.—A nonresident alien individual with respect to whom this subsection is in effect for the taxable year shall be treated as a resident of the United States—

"(A) for purposes of chapters 1 and 5 for all of such taxable year, and

"(B) for purposes of chapter 24 (relating to wage withholding) for payments of wages made during such taxable year."

(B) CONFORMING AMENDMENT.—Paragraph (5) of section 6013(g) (relating to termination of election by Secretary) is amended by striking out "chapter 1" and inserting in lieu thereof "chapters 1 and 5".

(C) YEAR OF RESIDENCY.—Paragraph (1) of section 6013(h) (relating to return for year nonresident alien becomes resident) amended—

(i) by striking out "chapter 1" and inserting in lieu thereof "chapters 1 and 5", and

(ii) by inserting before the period at the end thereof the following: ", and for purposes of chapter 24 (relating to wage withholding) for payments of wages made during such taxable year".

(D) CERTAIN AMOUNTS WITHHELD UNDER CHAPTER 3 TREATED AS OVERPAYMENTS OF TAX.—Subsection (b) of section 6401 (relating to excessive credits) is amended by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, any credit allowed under paragraph (1) of section 32 (relating to withholding of tax on nonresident aliens and on foreign corporations) to a nonresident alien individual for a taxable year with respect to which an election under section 6013 (g) or (h) is in effect shall be treated as an amount allowable as a credit under section 31."

(E) EFFECTIVE DATES.—The amendments made by this paragraph—

(i) to the extent that they relate to chapter 1 or 5 of the Internal Revenue Code of 1954, shall apply to taxable years ending on or after December 31, 1975, and

(ii) to the extent that they relate to wage withholding under chapter 24 of such Code, shall apply to remuneration paid on or after the first day of the first month which begins more than 90 days after the date of the enactment of this Act.

(16) NONRESIDENT ALIEN INDIVIDUAL ALLOWED TO BE TREATED AS RESIDENT OF THE UNITED STATES.—

(A) IN GENERAL.—Paragraph (2) of section 6013(g) (relating to election to treat nonresident alien individual as resident of the United States) is amended by striking out "who, at the time an election was made under this subsection," and inserting in lieu thereof "who, at the close of the taxable year for which an election under this subsection was made,".

(B) EFFECTIVE DATE.—The amendment made by subparagraph (A) shall apply to taxable years beginning after December 31, 1975.

(v) AMENDMENT OF SECTION 1239(a).—

(1) IN GENERAL.—Subsection (a) of section 1239 (relating to gain form sale of depreciable propery between certain relate taxpayers) is amended by striking out "subject to the allowance for depreciation provided in section 167" and inserting in lieu thereof "of a character which is subject to the allowance for depreciation provided in section 167".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply as if included in the amendment made to section 1239 of the Internal Revenue Code of 1954 by section 2129(a) of the Tax Reform Act of 1976.

(w) RECAPTURE OF DEPRECIATION ON PLAYER CONTRACTS.—

(1) IN GENERAL.—Subparagraph (C) of section 1245(a)(4) (defining previously unrecaptured depreciation with respect to contracts transferred) is amended to read as follows:

"(C) PREVIOUSLY UNRECAPTURED DEPRECIATION WITH RESPECT TO CONTRACTS TRANSFERRED.—For purposes of subparagrpah (A)(ii), the term 'previously unrecaptured depreciation' means the amount of any deduction allowed or allowable to the taxapyer transferor for the depreciation of any contracts involved in such transfer."

(2) RECAPTURE OF DEPRECIATION WITH RESPECT TO INITIAL CONTRACTS.—Subparagraph (B) of section 1245(a)(4) (defining previously unrecaptured depreciation with respect to initial contracts) is amended—

(A) by inserting "attributable to periods after December 31, 1975," after "depreciation" in clause (i),

(B) by inserting "incurred after December 31, 1975," after "losses" in clause (i), and

(C) by inserting "described in clause (i)" after "amounts" in clause (ii).

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to transfers of player contracts in connection with any sale or exchange of a franchise after December 31, 1975.

(x) TREATMENT OF PENSIONS AND ANNUITIES FOR 50-PERCENT MAXIMUM RATE ON PERSONAL SERVICE INCOME.—

(1) IN GENERAL.—Subparagraph (A) of section 1348(b)(1) (defining personal service income) is amended by striking out "pension or annuity" and inserting in lieu thereof "pension or annuity which arises from employer-employee relationship or from tax-deductible contributions to a retirement plan".

(2) TECHNICAL AMENDMENT.—The last sentence of section 1348(b) is amended by striking out "earned income" and inserting in lieu thereof "personal service income".

(3) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1976.

(y) CHANGES IN THE SUBCHAPTER S PROVISIONS.—

(1) GRANTOR TRUST MAY BE TREATED AS PERMITTED SHAREHOLDER AFTER DECEDENT'S DEATH; GRANTOR OE GRANTOR TRUST MUST BE INDIVIDUAL.—Paragraph (1) of subsection (e) of section 1371 (as redesignated by this Act) is amended to read as follows:

"(1)(A) A trust all of which is treated as owned by the grantor (who is an individual who is a citizen or resident of the United States) under subpart E of part I of subchapter J of this chapter.

"(B) A trust which was described in subparagraph (A) immediately before the death of the grantor and which continues in existence after such death, but only for the 60-day period beginning on the day of the grantor's death. If a trust is described in the preceding sentence and if the entire corpus of the trust is includible in the gross estate of the grantor, the preceding sentence shall be applied by substituting '2-year period' for '60-day period'."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1976.

(z) WITHHOLDING OF FEDERAL TAXES ON CERTAIN INDIVIDUALS ENGAGED IN FISHING.—

(1) IN GENERAL.—Section 1207(f)(4) of the Tax Reform Act of 1976 (relating to effective date of provisions relating to withholding on certain individuals engaged in fishing) is amended by striking out "December 31, 1971" each place it appears and inserting in lieu thereof "December 31, 1954".

(2) EFFECTIVE DATE.—The amendments made by paragraph (1) shall take effect on October 4, 1976.

(aa) WITHDRAWALS FROM INDIVIDUAL RETIREMENT ACCOUNTS, ETC.—

(1) IN GENERAL.—The last sentence of section 4973(b) (relating to excess contributions to individual retirement accounts, etc.) is amended by striking out "solely because of employer contributions to a plan or contract described in section 219(b)(2)" and inserting in lieu thereof "solely because of ineligibility under section 219(b)(2) or section 220(b)(3)".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply as if included in section 1501 of the Tax Reform Act of 1976 at the time of the enactment of such Act.

(bb) AMENDMENTS RELATING TO DISCLOSURE OF TAX RETURNS.—

(1) DISCLOSURE OF MAILING ADDRESS FOR PURPOSES OF COLLECTING CERTAIN STUDENT LOANS.—

(A) Subsection (m) of section 6103 (relating to disclosure of taxpayer identity information) is amended to read as follows:

"(m) DISCLOSURE OF TAXPAYER IDENITTY INFORMATION.—

"(1) TAX REFUNDS.—The Secretary may disclose taxpayer identity information to the press and other media for purposes of notifying persons entitled to tax refunds when the Secretary, after reasonable effort and lapse of time, has been unable to locate such persons.

"(2) FEDERAL CLAIMS.—Upon written request, the Secretary may disclose the mailing address of a taxpayer to officers and employees of an agency personally and directly engaged in, and solely for their use in, preparation for any administrative or judicial proceeding (or investigation which may result in such a proceeding) pertaining to the collection or compromise of a Federal claim against such taxpayer in accordance with the provisions of section 3 of the Federal Claims Collection Act of 1966.

"(3) NATIONAL INSTITUTE FOR OCCUPATIONAL SAFETY AND HEALTH.—Upon written request, the Secretary may disclose the mailing address if taxpayers to officers and employees of the National Institute for Occupational Safety and Health solely for the purpose of locating individuals who are, or may have been, exposed to occupational hazards in order to determine the status of their health or to inform them of the possible need for medical care and treatment.

"(4) INDIVIDUALS WHO HAVE DEFAULTED ON STUDENT LOANS.—

"(A) IN GENERAL.—Upon written request by the Commissioner of Education, the Secretary may disclose the mailing address of any taxpayer who has defaulted on a loan made from the student loan fund established under part E of title IV of the Higher Education Act of 1965 for use only for purposes of locating such taxpayer for purposes of collecting such loan.

"(B) DISCLOSURE TO INSTITUTIONS.—Any mailing address disclosed under subparagraph (A) may be disclosed by the Commissioner of Education to any educational institution with which he has an agreement under part E of title IV of the Higher Education Act of 1965 only for use by officers, employees or agents of such institution whose duties relate to the collection of student loans for purposes of locating individuals who have defaulted on student loans made by such institution pursuant to such agreement for purposes of collecting such loans."

(B) Paragraph (3) of section 6103(a) is amended by inserting ", subsection (m)(4)(B)," after "subsection (e)(1)(D)(iii)".

(C) Paragraph (2) of section 7213(a) (relating to penalties for unauthorized disclosure of information) is amended—

(i) by striking out "or any local" and inserting in lieu thereof ", any local";

(ii) by inserting ", or any educational institution" after "enforcement agency"; and

(iii) by striking out "section 6103(d) or (l)(6)" and inserting in lieu thereof "subsection (d), (l)(6), or (m)(4)(B) of section 6103".

(2) DISCLOSURE OF TAX RETURN INFORMATION REGARDING SPECIAL FUEL EXCISE TAXES.—Subsection (d) of section 6103 (relating to disclosure to State tax officials) is amended by inserting "31," after "24,".

(3) RETURN INFORMATION OTHER THAN TAXPAYER RETURN INFORMATION.—Paragraph (2) of section 6103(i) (relating to return information other than taxpayer return information) is amended by adding at the end thereof the following new sentence: "For purposes of this paragraph, the name and address of the taxpayer shall not be treated as taxpayer return information."

(4) DISCLOSURE OF RETURN INFORMATION CONCERNING POSSIBLE CRIMINAL ACTIVITIES.—Paragraph (3) of section 6103(i) (relating to disclosure of return information concerning possible criminal activities) is amended by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, the name and address of the taxpayer shall not be treated as taxpayer return information if there is return information (other than taxpayer return information) which may constitute evidence of a violation of Federal criminal laws."

(5) DISCLOSURE UNDER TAX CONVENTIONS.—Section 6103(k)(4) (relating to disclosure of return information under income tax conventions) is amended—

(A) by striking out "income" in the caption thereof,

(B) by inserting "or gift and estate tax" after "income tax", and

(C) by inserting ", or other convention relating to the exchange of tax information," after "convention" the first place it appears.

(6) CRIMINAL PENALTY FOR UNAUTHORIZED DISCLOSURE OF INFORMATION.—Section 7213(a) (relating to unauthorized disclosure of information) is amended—

(A) by strkiing out "to disclose" in paragraphs (1), (2), and (5) and inserting in lieu thereof "willfully to disclose",

(B) by striking out "to thereafter print or publish" in paragraph (3) and inserting in lieu thereof "therafter willfully to print or publish", and

(C) by striking out "to offer" in paragraph (4) and inserting in lieu thereof "willfully to offer".

(7) NO CIVIL LIABILITY FOR GOOD FAITH BUT ERRONEOUS INTERPRETATION OF DICSLOSURE REQUIREMENTS.—Section 7217 (relating to civil damages for unauthorized disclosure of return and return information) is amended—

(A) by redesignating subsections (b) and (c) as subsections (c) and (d), respectively;

(B) by inserting after subsection (a) the following new subsection:

"(b) NO LIABILITY FOR GOOD FAITH BUT ERRONEOUS INTERPRETATION.—No liability shall arise under this section with respect to any disclosure which results from a good faith, but erroneous, interpretation of section 6103."; and

(C) by striking out "An action" in subsection (d) (as so redesignated) and inserting in lieu thereof "PERIOD FOR BRINGING ACTION.—An action".

(8) EFFECTIVE DATES.—

(A) Except as provided in subparagraph (B), the amendments made by this subsection shall take effect January 1, 1977.

(B) The amendments made by paragraph (7) shall apply with respect to disclosures made after the date of the enactment of this Act.

(cc) AMENDMENTS RELATING TO INCOME TAX RETURN PREPARERS.—

(1) NEGOTIATION OF CHECKS BY BANK.—Subsection (f) of section 6695 (relating to negotiation of check) is amended by adding at the end thereof the following new sentence: "The preceding sentence shall not apply with respect to the deposit by a bank (within the meaning of section 581) of the full amount of the check in the taxpayer's account in such bank for the benefit of the taxpayer."

(2) DEFINITION.—Clause (iii) of section 7701(a)(36)(B) (relating to exceptions form the definition of income tax return prepr~r) is amended to read as follows:

"(iii) prepares as a fiduciary a return or claim for refund for any person, or".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to documents prepared after December 31, 1976.

(dd) CLARIFICATION OF DECLARATORY JUDGMENT PROVISIONS WITH RESPECT TO REVOCATIONS OF OR OTHER CHANGES IN THE QUALIFICATIONS OF CERTAIN ORGANIZATIONS.—

(1) QUALIFICATION OF CERTAIN RETIREMENT PLANS.—Subsection (a) of section 7476 (relating to declaratory judgments relating to qualification of certain retirement plans) is amended by adding at the end thereof the following new sentence: "For purposes of this section, a determination with respect to a continuing qualification includes any revocation of or other change in a qualification."

(2) CLASSIFICATION OF ORGANIZATIONS UNDER SECTION 501(c)(3), ETC.—Subsection (a) of section 7428 (relating to declaratory judgments relating to status and classification of organizations under section 501(c)(3), etc.) is amended by adding at the end thereof the following new sentence: "For purposes of this section, a determination with respect to a continuing qualification or continuing classification includes any revocation of or other change in a qualification or classification."

(3) EFFECTIVE DATE.—The amendments made by paragraphs (1) and (2) shall take effect as if included in section 7476 or 7428 of the Internal Revenue Code of 1954 (as the case may be) at the respective times such sections were added to such Code.

(ee) CONTRIBUTIONS OF CERTAIN GOVERNMENT PUBLICATIONS.—

(1) IN GENERAL.—Paragraph (1) of section 1231(b) (relating to definition of property used in trade or business) is amended—

(A) by striking out "or" at the end of subparagraph (B),

(B) by striking out the period at the end of subparagraph (C) and inserting in lieu thereof a comma and "or", and

(C) by adding at the end thereof the following new subparagraph:

"(D) a publication of the United States Government (including the Congressional Record) which is received from the United States Government, or any agency thereof, other than by purchase at the price at which it is offered for sale to the public, and which is held by a taxpayer described in paragraph (6) of section 1221.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply with respect to sales, exchanges, and contributions made after October 4, 1976.

(ff) EXEMPTION FOR LIGHT-DUTY TRUCK PARTS.—

(1) IN GENERAL.—Section 4063 (relating to exemption of motor vehicles and parts) is amended by adding at the end thereof the following new subsection:

"(e) PARTS FOR LIGHT-DUTY TRUCKS.—The tax imposed by section 4061(b) shall not apply to the sale by the manufacturer, producer, or importer of any article which is to be resold by the purchaser on or in connection with the first retail sale of a light-duty truck, as described in section 4061(a)(2), or which is to be resold by the purchaser to a second purchaser for resale by such second purchaser on or in connection with the first retail sale of a light-duty truck."

(2) CONFORMING AMENDMENTS.—

(A) Section 4221(c) (relating to manufacturer relieved from liability in certain cases) is amended by inserting "4063(e)" after "4063(b),".

(B) Section 4222(d) (relating to registration in the case of tax-free sales) is amended by inserting "4063(e)," after "4063(b),".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall take effect on the first day of the first calendar month beginning more than 20 days after the date of the enactment of this Act.

SEC. 702. TECHNICAL, CLERICAL, AND CONFORMING AMENDMENTS TO ESTATE AND GIFT TAX PROVISIONS.

(a) AMENDMENTS RELATING TO TREATMENT OF SECTION 306 STOCK.—

(1) APPLICATION OF "FRESH START" TO SECTION 306 STOCK.—

Subsection (a) of section 306 (relating to disposition of certain stock) is amended by adding at the end thereof the following new paragraph:

"(3) ORDINARY INCOME FROM SALE OR REDEMPTION OF SECTION 306 STOCK WHICH IS CARRYOVER BASIS PROPERTY ADJUSTED FOR 1976 VALUE.—

"(A) IN GENERAL.—If any section 306 stock was distributed before January 1, 1977, and if the adjusted basis of such stock in the hands of the person disposing of it is determined under section 1023 (relating to carryover basis), then the amount treated as ordinary income under paragraph (1)(A) of this subsection (or the amount treated as a dividend under section 301(c)(1)) shall not exceed the excess of the amount realized over the sum of—

"(i) the adjusted basis of such stock on December 31, 1976, and

"(ii) any increase in basis under section 1023(h).

"(B) REDEMPTION MUST BE DESCRIBED IN SECTION 302(b).—Subparagraph (A) shall apply to a redemption only if such redemption is described in paragraph (1), (2), or (4) of section 302(b)."

(2) CLARIFICATION THAT SECTION 303 OVERRIDES SECTION 306.—Subsection (b) of section 306 (relating to exceptions) is amended by adding at the end thereof the following new paragraph:

"(5) SECTION 303 REDEMPTIONS.—To the extent that section 303 applies to a distribution in redemption of section 306 stock.".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to the estates of decedents dying after December 31, 1979.

(b) COORDINATION OF DEDUCTION FOR ESTATE TAXES ATTRIBUTABLE TO INCOME IN RESPECT OF A DECEDENT WITH THE CAPITAL GAIN DEDUCTION, ETC.—

(1) IN GENERAL.—Subsection (c) of section 691 (relating to deduction for estate taxes in the case of income in respect of decedents) is amended by adding at the end thereof the following new paragraph:

"(4) COORDINATION WITH CAPITAL GAIN DEDUCTION, ETC.—For purposes of sections 1201, 1202, and 1211, and for purposes of section 57(a)(9), the amount of any gain taken into account with respect to any item described in subsection (a)(1) shall be reduced (but not below zero) by the amount of the deduction allowable under paragraph (1) of this subsection with respect to such item."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply with respect to decedents dying after the date of the enactment of this Act.

(c) AMENDMENTS RELATING TO CARRYOVER BASIS.—

(1) AMENDMENTS RELATING TO THE POSTPONEMENT OF THE EFFECTIVE DATE OF CARRYOVER BASIS PROVISIONS.—

(A) FAIR MARKET VALUE WHERE FARM VALUATION ELECTED.—Subsection (a) of section 1014 (relating to basis of property acquired from a decedent) is amended to read as follows:

"(a) IN GENERAL.—Except as otherwise provided in this section, the basis of property in the hands of a person acquiring the property from a

decedent or to whom the property passed from a decedent shall, if not sold, exchanged, or otherwise disposed of before the decedent's death by such person, be—

"(1) the fair market value of the property at the date of the decedent's death, or

"(2) in the case of an election under either section 2032 or section 811(j) of the Internal Revenue Code of 1939 where the decedent died after October 21, 1942, its value at the applicable valuation date prescribed by those sections, or

"(3) in the case of an election under section 2032.1, its value determined under such section."

(B) GENERATION-SKIPPING TRANSFERS.—The second sentence of section 2614(a) (relating to basis adjustments in connection with generation-skipping transfers) is amended to read as follows: "If property is transferred in a generation-skipping transfer subject to tax under this chapter which occurs at the same time as, or after, the death of the deemed transferor, the basis of such property shall be adjusted—

"(1) in the case of such a transfer occurring after June 11, 1976, and before January 1, 1980, in a manner similar to the manner provided under section 1014(a), and

"(2) in the case of such a transfer occurring after December 31, 1979, in a manner similar to the manner provided by section 1023 without regard to subsection (d) thereof (relating to basis of property passing from a decedent dying after December 31, 1979)."

(2) MINIMUM CARRYOVER BASIS FOR TANGIBLE PERSONAL PROPERTY.—

(A) IN GENERAL.—Subsection (h) of section 1023 (relating to adjustment to basis for December 31, 1976, fair market value) is amended by adding at the end thereof the following new paragraph:

"(3) MINIMUM BASIS FOR TANGIBLE PERSONAL PROPERTY.—

"(A) IN GENERAL.—If the holding period for any carryover basis property which is tangible personal property includes December 31, 1976, then, for purposes of determining gain and applying this section, the adjusted basis of such property immediately before the death of the decedent shall be treated as being not less than the amount determined under subparagraph (B).

"(B) AMOUNT.—The amount determined under this subparagraph for any property is—

"(i) the value of such property (as determined with respect to the estate of the decedent without regard to section 2032), divided by

"(ii) 1.0066 to the nth power where n equals the number of full calendar months which have elapsed between December 31, 1976, and the date of the decedent's death."

(B) CONFORMING AMENDMENT.—Paragraph (3) of section 1023(g) (relating to decedent's basis unknown) is amended by striking out "to the person acquiring such property from the decedent" and inserting in lieu thereof "and cannot be reasonably ascertained".

(3) TREATMENT OF INDEBTEDNESS.—

(A) IN GENERAL.—Paragraph (1) of section 1023(g) (defining fair market value) is amended by inserting "(without regard to whether there is a mortgage in, or indebtedness in reepect of, the property)" after "chapter 11".

(B) TECHNICAL AMENDMENT.—Subsection (g) of section 1023 (relating to other special rules and definitions) is amended by striking out paragraph (4).

(4) ONLY ONE FRESH START WITH RESPECT TO CARRYOVER BASIS PROPERTY HELD ON DECEMBER 31, 1976.—Subsection (h) of section 1023 (relating to adjustment to basis for December 31, 1976, fair market value) is amended by adding at the end thereof the following new paragraph:

"(4) ONLY ONE FRESH START.—There shall be no increase in basis under this subsection by reason of the death of any decedent if the adjusted basis of the property in the hands of such decedent reflects the adjusted basis of property which was carryover basis property with respect to a prior decedent."

(5) AUTOMATIC LONG-TERM STATUS FOR GAINS AND LOSSES ON CARRYOVER BASIS PROPERTY.—Subparagraph (A) of section 1223(11) is amended by inserting "or 1023" after "section 1014".

(6) CLARIFICATION THAT ADJUSTED BASIS IS INCREASED FOR STATE ESTATE TAXES.—

(A) Subsection (c) of section 1023 (relating to increase in basis for Federal and State estate taxes attributable to appreciation) is amended to read as follows:

"(c) INCREASE IN BASIS FOR FEDERAL AND STATE ESTATE TAXES ATTRIBUTABLE TO APPRECIATION.—

"(1) FEDERAL ESTATE TAXES.—The basis of appreciated carryover basis property (determined after any adjustment under subsection (h)) which is subject to the tax imposed by section 2001 or 2101 in the hands of the person acquiring it from the decedent shall be increased by an amount which bears the same ratio to the Federal estate taxes as—

"(A) the net appreciation in value of such property, bears to

"(B) the fair market value of all property which is subject to the tax imposed by section 2001 or 2101.

"(2) STATE ESTATE TAXES.—The basis of appreciated carryover basis property (determined after any adjustment under subsection (h)) which is subject to State estate taxes in the hands of the person acquiring it from the decedent shall be increased by an amount which bears the same ratio to the State estate taxes as—

"(A) the net appreciation in value of such property, bears to

"(B) the fair market value of all property which is subject to the State estate taxes."

(B) The second sentence of paragraph (2) of section 1023(f) (defining net appreciation) is amended by striking out "For purposes of subsection (d)," and inserting in lieu thereof "For purposes of paragraph (2) of subsection (c), such adjusted basis shall be increased by the amount of any adjustment under paragraph (1) of subsection (c), for purposes of subsection (d).".

(C) Paragraph (3) of section 1023(f) (defining Federal and State estate taxes) is amended to read as follows:

"(3) FEDERAL AND STATE ESTATE TAXES.—For purposes of subsection (c)—

"(A) FEDERAL ESTATE TAXES.—The term 'Federal estate taxes' means the tax imposed by section 2001 or 2101, reduced by the credits against such tax.

"(B) STATE ESTATE TAXES.—The term 'State estate taxes' means any estate, inheritance, legacy, or succession taxes, for which the estate is liable, actually paid by the estate to any State or the District of Columbia.

(7) CLARIFICATION OF INCREASE IN BASIS FOR CERTAIN STATE SUCCESSION TAXES.—Paragraph (2) of section 1023(e) (relating to further increase in basis for certain State succession tax paid by transferee of property) is amended by striking out "for which the estate is not liable".

(8) CLARIFICATION OF APPLICATION OF FRESH START.—Paragraphs (1) and (2)(A) of section 1023(h) (relating to adjustment to basis for December 31, 1976, fair market value) are each amended by striking out "for purposes of determining gain" and inserting in lieu thereof "for purposes of determining gain and applying this section".

(9) TECHNICAL AMENDMENT WITH RESPECT TO CERTAIN TERM INTERESTS.—Paragraph (1) of section 1001(e) (relating to certain term interests) is amended by striking out "section 1014 or 1015" and inserting in lieu thereof "section 1014, 1015, or 1023".

(10) EFFECTIVE DATE.—The amendments made by this subsection shall take effect as if included in the amendments and additions made by, and the appropriate provisions of the Tax Reform Act of 1976.

(d) AMENDMENTS RELATING TO VALUATION OF CERTAIN FORM, ETC., REAL PROPERTY.—

(1) CLARIFICATION THAT SPECIAL VALUATION APPLIES ONLY TO INTERESTS PASSING TO QUALIFIED HEIRS.—Paragraph (1) of section 2032A(b) (defining qualified real property) is amended by striking out "real property located in the United States" and inserting in lieu thereof "real property located in the United States which was acquired from or passed from the decedent to a qualified heir of the decedent and".

(2) PROPERTY RECEIVED IN SATISFACTION OF PECUNIARY BEQUEST.—Subsection (e) of section 2032A (relating to definitions and special rules for farm valuation property) is amended by adding at the end thereof the following new paragraph:

"(9) PROPERTY ACQUIRED FROM DECEDENT.—Property shall be considered to have been acquired from or to have passed from the decedent if—

"(A) such property is so considered under section 1014(b) (relating to basis of property acquired from a decedent),

"(B) such property is acquired by any person from the estate in satisfaction of the right of such person to a pecuniary bequest, or

"(C) such property is acquired by any person from a trust in satisfaction of a right (which such person has by reason of the death of the decedent) to receive from the trust a specific dollar amount which is the equivalent of a pecuniary bequest."

(3) USE OF FARM VALUATION PROPERTY TO SATISFY PECUNIARY BEQUEST.—Subsection (a) of section 1040 (relating to use of certain appreciated carryover basis property to satisfy pecuniary bequest) is amended by inserting "(determined without regard to section 2032A)" after "chapter 11".

(4) TREATMENT OF CERTAIN COMMUNITY PROPERTY.—Subsection (e) of section 2032A is amended by adding at the end thereof the following new paragraph:

"(10) COMMUNITY PROPERTY.—If the decedent and his surviving spouse at any time held qualified real property as community property, the interest of the surviving spouse in such property shall be taken into account under this section to the extent necessary to provide a result under this section with respect to such property which is consistent with the result which would have obtained under this section if such property had not been community property."

(5) SUBSTITUTION OF BOND FOR PERSONAL LIABILITY OF QUALIFIED HEIR FOR THE RECAPTURE TAX WITH RESPECT TO FARM VALUATION PROPERTY.—

(A) IN GENERAL.—Paragraph (6) of section 2032A(c) is amended to read as follows:

"(6) LIABILITY FOR TAX; FURNISHING OF BOND.—The qualified heir shall be personally liable for the additional tax imposed by this subsection with respect to his interest unless the heir has furnished bond which meets the requirements of subsection (e)(11)."

(B) BOND REQUIREMENTS.—Subsection (e) of section 2032A is amended by adding at the end thereof the following new paragraph:

"(11) BOND IN LIEU OF PERSONAL LIABILITY.—If the qualified heir makes written application to the Secretary for determination of the maximum amount of the additional tax which may be imposed by subsection (c) with respect to the qualified heir's interest, the Secretary (as soon as possible, and in any event within 1 year after the making of such application) shall notify the heir of such maximum amount. The qualified heir, on furnishing a bond in such amount and for such period as may be required, shall be discharged from personal liability for any additional tax imposed by subsection (c) and shall be entitled to a receipt or writing showing such discharge."

(6) EFFECTIVE DATE.—The amendments made by this subsection shall apply to the estates of decedents dying after December 31, 1976.

(e) AMOUNT OF SECURITY REQUIRED FOR EXTENDED PAYMENT PROVISIONS FOR CLOSELY HELD BUSINESSES.—

(1) IN GENERAL.—

(A) Paragraph (2) of section 6324A(e) (defining aggregate interest amount) is amended to read as follows:

"(2) REQUIRED INTEREST AMOUNT.—The term 'required interest amount' means the aggregate amount of interest which will be payable over the first 4 years of the deferral period with respect to the deferred amount (determined as of the date prescribed by section 6151(a) for the payment of the tax imposed by chapter 11)."

(B) Subparagraph (B) of section 6324A(b)(2) (relating to maximum value of required property) is amended by striking out "aggregate interest amount" and inserting in lieu thereof "required interest amount".

(C) Paragraph (5) of section 6324A(d) (relating to special rules) is amended by striking out "aggregate interest amount" and inserting in lieu thereof "required interest amount".

(D) Paragraph (4) of section 6324A(e) (relating to application of definitions in case of deficiencies) is amended by striking out "aggregate interest amount" and inserting in lieu thereof "required interest amount".

(2) EFFECTIVE DATE.—The amendments made by this section shall apply to the estates of decedents dying after December 31, 1976.

(f) CLARIFICATION OF THE $3,000 ANNUAL EXCLUSION FROM THE RULE INCLUDING IN GROSS ESTATE TRANSFERS WITHIN 3 YEARS OF DEATH.—

(1) AMENDMENT OF SECTION 2035(b).—Subsection (b) of section 2035 (relating to adjustments for gifts made within 3 years of decedent's death) is amended to read as follows:

"(b) EXCEPTIONS.—Subsection (a) shall not apply—

"(1) to any bona fide sale for an adequate and full consideration in money or money's worth, and

"(2) to any gift to a donee made during a calendar year if the decedent was not required by section 6019 to file any gift tax return for such year with respect to gifts to such donee.

Paragraph (2) shall not apply to any transfer with respect to a life insurance policy."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to the estates of decedents dying after December 31, 1976, except that it shall not apply to transfers made before January 1, 1977.

(g) AMENDMENTS RELATING TO ESTATE TAX MARITAL DEDUCTION.—

(1) DEDUCTION NOT REDUCED FOR GIFT TO SPOUSE WHICH IS INCLUDED IN DONOR'S ESTATE BY REASON OF SECTION 2035.—Subparagraph (B) of section 2056(c)(1) (relating to adjustment to estate tax marital deduction for certain gifts to spouse) is amended by adding at the end thereof the following new sentence:

"For purposes of this subparagraph, a gift which is includible in the gross estate of the donor by reason of section 2035 shall not be taken into account."

(2) REDUCTION FOR GIFT TAX MARITAL DEDUCTION IN EXCESS OF 50 PERCENT OF THE VALUE OF GIFTS TO A SPOUSE.—Clause (ii) of section 2056(c)(1)(B) (relating to adjustment to estate tax marital deduction for certain gifts to spouse) is amended by inserting "required to be included in a gift tax return" after "with respect to any gift".

(3) EFFECTIVE DATE.—The amendment made by this subsection shall apply to the estates of decedents dying after December 31, 1976.

(h) COORDINATION OF SECTIONS 2513 AND 2035.—

(1) IN GENERAL.—Section 2001 (relating to imposition and rate of estate tax) is amended by adding at the end thereof the following new subsection:

"(e) COORDINATION OF SECTIONS 2513 AND 2035.—If—

"(1) the decedent's spouse was the donor of any gift one-half of which was considered under section 2513 as made by the decedent, and

"(2) the amount of such gift is includible in the gross estate of the decedent's spouse by reason of section 2035, such gift shall not be included in the adjusted taxable gifts of the decedent for purposes of subsection (b)(1)(B), and the aggregate amount determined under subsection (b)(2) shall be reduced by the amount (if any) determined under subsection (d) which was treated as a tax payable by the decedent's spouse with respect to such gift."

(2) CONFORMING AMENDMENT.—Subparagraph (C) of section 2602(a)(1) (relating to amount of tax on generation-skipping trans-

fers) is amended by striking out "section 2001(b))" and inserting in lieu thereof "section 2001(b), as modified by section 2001(e))".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply with respect to the estates of decedents dying after December 31, 1976, except that such amendments shall not apply to transfers made before January 1, 1977.

(i) INCLUSION IN GROSS ESTATE OF STOCK TRANSFERRED BY THE DECEDENT WHERE THE DECEDENT RETAINS OR ACQUIRES VOTING RIGHTS.—

(1) IN GENERAL.—Section 2036 (relating to transfers with retained life estate) is amended by redesignating subsection (b) as subsection (c) and by inserting after subsection (a) the following new subsection:

"(b) VOTING RIGHTS.—

"(1) IN GENERAL.—For purposes of subsection (a)(1), the retention of the right to vote (directly or indirectly) shares of stock of a controlled corporation shall be considered to be a retention of the enjoyment of transferred property.

"(2) CONTROLLED CORPORATION.—For purposes of paragraph (1), a corporation shall be treated as a controlled corporation if, at any time after the transfer of the property and during the 3-year period ending on the date of the decedent's death, the decedent owned (with the application of section 318), or had the right (either alone or in conjunction with any person) to vote, stock possessing at least 20 percent of the total combined voting power of all classes of stock.

"(3) COORDINATION WITH SECTION 2035.—For purposes of applying section 2035 with respect to paragraph (1), the relinquishment or cessation of voting rights shall be treated as a transfer of property made by the decedent."

(2) CONFORMING AMENDMENT.—Subsection (a) of section 2036 is amended by striking out the last sentence thereof.

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to transfers made after June 22, 1976.

(j) AMENDMENTS RELATING TO INDIVIDUAL RETIREMENT ACCOUNTS, ETC., FOR SPOUSE.—

(1) APPLICATION OF ESTATE TAX EXCLUSION TO INDIVIDUAL RETIREMENT ACCOUNTS, ETC., FOR SPOUSE.—Subsection (e) of section 2039 (relating to exclusion of individual retirement accounts, etc.) is amended by striking out "section 219" each place it appears and inserting in lieu thereof "section 219 or 220".

(2) TRANSFERS TO INDIVIDUAL RETIREMENT ACCOUNTS, ETC., FOR SPOUSE TREATED AS TRANSFERS OF PRESENT INTERESTS.—Section 2503 (relating to taxable gifts) is amended by adding at the end thereof the following new subsection:

"(d) INDIVIDUAL RETIREMENT ACCOUNTS, ETC., FOR SPOUSE.—For purposes of subsection (b), any payment made by an individual for the benefit of his spouse—

"(1) to an individual retirement account described in section 408(a),

"(2) for an individual retirement annuity described in section 408(b), or

"(3) for a retirement bond described in section 409,

shall not be considered a gift of a future interest in property to the extent that such payment is allowable as a deduction under section 220".

(3) EFFECTIVE DATES.—

(A) *The amendment made by paragraph (1) shall apply to the estates of decedents dying after December 31, 1976.*

(B) *The amendment made by paragraph (2) shall apply to transfers made after December 31, 1976.*

(k) PROVISIONS RELATING TO TREATMENT OF JOINT INTERESTS.—

(1) REMOVAL OF REQUIREMENT OF ACTUARIAL COMPUTATIONS FOR JOINT INTERESTS IN PERSONAL PROPERTY.—

(A) IN GENERAL.—*Subchapter (B) of chapter 12 (relating to transfers for purposes of the gift tax) is amended by inserting after section 2515 the following new section:*

"SEC. 2515A. TENANCIES BY THE ENTIRETY IN PERSONAL PROPERTY.

"(a) CERTAIN ACTUARIAL COMPUTATIONS NOT REQUIRED.—In the case of—

"(1) the creation (either by one spouse alone or by both spouses) of a joint interest of a husband and wife in personal property with right of survivorship, or

"(2) additions to the value thereof in the form of improvements, reductions in the indebtedness thereof, or otherwise,

the retained interest of each spouse shall be treated as one-half of the value of their joint interest.

"(b) EXCEPTION.—Subsection (a) shall not apply with respect to any joint interest in property if the fair market value of the interest or of the property (determined as if each spouse had a right to sever) cannot reasonably be ascertained except by reference to the life expectancy of one or both spouses."

(B) CHANGE IN SECTION 2515 HEADING.—*The heading for section 2515 is amended to read as follows:*

"SEC. 2515. TENANCIES BY THE ENTIRETY IN REAL PROPERTY."

(C) CLERICAL AMENDMENTS.—*The table of sections for subchapter B of chapter 12 is amended by striking out the item relating to section 2515 and inserting in lieu thereof the following:*

"Sec. 2515. Tenancies by the entirety in real property.
"Sec. 2515A. Tenancies by the entirety in personal property."

(D) EFFECTIVE DATE.—*The amendments made by this paragraph shall apply to joint interests created after December 31, 1976.*

(2) EXTENSION OF FRACTIONAL INTEREST RULE TO CERTAIN JOINT INTERESTS IN REAL OR PERSONAL PROPERTY CREATED BEFORE 1977.—*Section 2040 (relating to joint interests) as amended by this Act, is further amended by adding at the end thereof the following new subsections:*

"(d) JOINT INTEREST OF HUSBAND AND WIFE CREATED BEFORE 1977.—Under regulations prescribed by the Secretary—

"(1) IN GENERAL.—In the case of any joint interest created before January 1, 1977, which (if created after December 31, 1976) would have constituted a qualified joint interest under subsection (b)(2) (determined without regard to clause (ii) of subsection (b)(2)(B)), the donor may make an election under this subsection to have paragraph (1) of subsection (b) apply with respect to such joint interest.

"(2) TIME FOR MAKING ELECTION.—An election under this subsection with respect to any property shall be made for the calendar quarter in 1977, 1978, or 1979 selected by the donor in a gift tax return filed within the time prescribed by law for filing a gift tax

return for such quarter. Such an election may be made irrespective of whether or not the amount involved exceeds the exclusion provided by section 2503(b); but no election may be made under this subsection after the death of the donor.

"(3) TAX EFFECTS OF ELECTION.—In the case of any property with respect to which an election has been made under this subsection, for purposes of this title—

"(A) the donor shall be treated as having made a gift at the close of the calendar quarter selected under paragraph (2), and

"(B) the amount of the gift shall be determined under paragraph (4).

"(4) AMOUNT OF GIFT.—For purposes of paragraph (3)(B), the amount of any gift is one-half of the amount—

"(A) which bears the same ratio to the excess of (i) the value of the property on the date of the deemed making of the gift under paragraph (3)(A), over (ii) the value of such property on the date of the creation of the joint interest, as

"(B) the excess of (i) the consideration furnished by the donor at the time of the creation of the joint interest, over (ii) the consideration furnished at such time by the donor's spouse, bears to the total consideration furnished by both spouses at such time.

"(5) SPECIAL RULE FOR PARAGRAPH (4)(A).—For purposes of paragraph (4)(A)—

"(A) in the case of real property, if the creation was not treated as a gift at the time of the creation, or

"(B) in the case of personal property, if the gift was required to be included on a gift tax return but was not so included, and the period of limitations on assessment under section 6501 has expired with respect to the tax (if any) on such gift, then the value of the property on the date of the creation of the joint interest shall be treated as zero.

"(6) SUBSTANTIAL IMPROVEMENTS.—For purposes of this subsection, a substantial improvement of any property shall be treated as the creation of a separate joint interest.

"(e) TREATMENT OF CERTAIN POST-1976 TERMINATIONS.—

"(1) IN GENERAL.—If—

"(A) before January 1, 1977, a husband and wife had a joint interest in property with right of survivorship,

"(B) after December 31, 1976, such joint interest was terminated, and

"(C) after December 31, 1976, a joint interest of such husband and wife in such property (or in property the basis of which in whole or in part reflects the basis of such property) was created. then paragraph (1) of subsection (b) shall apply to the joint interest described in subparagraph (C) only if an election is made under subsection (d).

"(2) SPECIAL RULES.—For purposes of applying subsection (d) to property described in paragraph (1) of this subsection—

"(A) if the creation described in paragraph (1)(C) occurs after December 31, 1979, the election may be made only with respect to the calendar quarter in which such creation occurs, and

"(B) *the creation of the joint interest described in paragraphs (4) and (5) of subsection (d) is the creation of the joint interest described in paragraph (1)(A) of this subsection.*"

(l) AMENDMENTS RELATING TO ORPHANS' EXCLUSION.—

(1) ORPHANS' EXCLUSION WHERE THERE IS A TRUST FOR MINOR CHILDREN.—*Section 2057 (relating to bequests, etc., to certain minor children) is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:*

"(d) QUALIFIED MINORS' TRUST.—

"(1) IN GENERAL.—*For purposes of subsection (a), the interest of a minor child in a qualified minors' trust shall be treated as an interest in property which passes or has passed from the decedent to such child.*

"(2) QUALIFIED MINORS' TRUST.—*For purposes of paragraph (1), the term 'qualified minors' trust' means a trust—*

"(A) *except as provided in subparagraph (D), all of the beneficiaries of which are minor children of the decedent,*

"(B) *the corpus of which is property which passes or has passed from the decedent to such trust,*

"(C) *except as provided in paragraph (3), all distributions from which to the beneficiaries of the trust before the termination of their interests will be pro rata,*

"(D) *on the death of any beneficiary of which before the termination of the trust, the beneficiary's pro rata share of the corpus and accumulated income remains in the trust for the benefit of the minor children of the decedent who survive the beneficiary or vests in any person, and*

"(E) *on the termination of which, each beneficiary will receive a pro rata share of the corpus and accumulated income.*

"(3) CERTAIN DISPROPORTIONATE DISTRIBUTIONS PERMITTED.—*A trust shall not be treated as failing to meet the requirements of paragraph (2)(C) solely by reason of the fact that the governing instrument of the trust permits the making of disproportionate distributions which are limited by an ascertainable standard relating to the health, education, support, or maintenance of the beneficiaries.*

"(4) TRUSTEE MAY ACCUMULATE INCOME.—*A trust which otherwise qualifies as a qualified minors' trust shall not be disqualified solely by reason of the fact that the trustee has power to accumulate income.*

"(5) COORDINATION WITH SUBSECTION (c).—*In applying subsection (c) to a qualified minors' trust, those provisions of section 2056(b) which are inconsistent with paragraph (3) or (4) of this subsection shall not apply.*

"(6) DEATH OF BENEFICIARY BEFORE YOUNGEST CHILD REACHES AGE 23.—*Nothing in this subsection shall be treated as disqualifying an interest of a minor child in a trust solely because such interest will pass to another person if the child dies before the youngest child of the decedent attains age 23.*"

(2) AGE 23 FOR TERMINABLE INTEREST RULE IN THE CASE OF ORPHANS' EXCLUSION.—*The second sentence of subsection (c) of section 2057 (relating to limitation in the case of life estate or other terminable interest) is amended by striking out "21" and inserting in lieu thereof "23".*

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to the estates of decedents dying after December 31, 1976.

(m) DISCLAIMER BY SURVIVING SPOUSE WHERE INTEREST PASSES TO SUCH SPOUSE.—

(1) IN GENERAL.—Paragraph (4) of section 2518(b) (defining qualified disclaimer) is amended to read as follows:

"(4) as a result of such refusal, the interest passes without any direction on the part of the person making the disclaimer and passes either—

"(A) to the spouse of the decedent, or

"(B) to a person other than the person making the disclaimer."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to transfers creating an interest in the person disclaiming made after December 31, 1976.

(n) AMENDMENTS RELATING TO TAX ON GENERATION-SKIPPING TRANSFERS.—

(1) EFFECTIVE DATE OF GENERATION-SKIPPING TRANSFER PROVISIONS.—Section 2006(c) of the Tax Reform Act of 1976 (relating to effective date of generation-skipping transfer provisions) is amended by striking out "April 30, 1976" each place it appears and inserting in lieu thereof "June 11, 1976".

(2) CERTAIN POWERS OF INDEPENDENT TRUSTEES NOT TREATED AS POWERS.—Subsection (e) of section 2613 (relating to definitions for purposes of the tax on generation-skipping transfers) is amended to read as follows:

"(e) CERTAIN POWERS NOT TAKEN INTO ACCOUNT.—

"(1) LIMITED POWER TO APPOINT AMONG LINEAL DESCENDANTS OF THE GRANTOR.—For purposes of this chapter, an individual shall be treated as not having any power in a trust if such individual does not have any present or future power in the trust other than a power to dispose of the corpus of the trust or the income therefrom to a beneficiary or a class of beneficiaries who are lineal descendants of the grantor assigned to a generation younger than the generation assignment of such individual.

"(2) POWERS OF INDEPENDENT TRUSTEES.—

"(A) IN GENERAL.—For purposes of this chapter, an individual shall be treated as not having any power in a trust if such individual—

"(i) is a trustee who has no interest in the trust,

"(ii) is not a related or subordinate trustee, and

"(iii) does not have any present or future power in the trust other than a power to dispose of the corpus of the trust or the income therefrom to a beneficiary or a class of beneficiaries designated in the trust instrument.

"(B) RELATED OR SUBORDINATE TRUSTEE DEFINED.—For purposes of subparagraph (A), the term 'related or subordinate trustee' means any trustee who is assigned to a younger generation than the grantor's generation and who is—

"(i) the spouse of the grantor or of any beneficiary,

"(ii) the father, mother, lineal descendant, brother, or sister of the grantor or of any beneficiary,

"(iii) an employee of a corporation in which the stockholdings of the grantor, the trust, and the beneficiaries of the trust are significant from the viewpoint of voting control,

"(iv) an employee of a corporation in which the grantor or any beneficiary of the trust is an executive."

"(v) a partner of a partnership in which the interest of the grantor, the trust, and the beneficiaries of the trust are significant from the viewpoint of operating control or distributive share of partnership income,".

"(vi) an employee of a corporation in which the grantor or any beneficiary of the trust is an executive, or

"(vii) an employee of a partnership in which the grantor or any beneficiary of the trust is a partner.".

(3) CLARIFICATION OF SECTION 2613(b)(2)(B).—Subparagraph (B) of section 2613(b)(2) (defining taxable termination for purposes of the tax on generation-skipping transfer) is amended—

(A) by striking out "an interest and a power" and inserting in lieu thereof "a present interest and a present power", and

(B) by striking out "interest or power" and inserting in lieu thereof "present interest or present power".

(4) ALTERNATE VALUATION IN CERTAIN CASES WHERE THERE IS A TAXABLE TERMINATION AT DEATH OF OLDER GENERATION BENEFICIARY.—

(A) IN GENERAL.—Subparagraph (A) of section 2602(d)(1) (relating to alternate valuation) is amended by inserting "(or at the same time as the death of a beneficiary of the trust assigned to a higher generation than such deemed transferor)" after "such deemed transferor".

(B) SPECIAL RULES.—Subparagraph (A) of section 2602(d)(2) (relating to special rules for alternate valuation) is amended by inserting "(or beneficiary)" after "the deemed transferor".

(5) EFFECTIVE DATE.—

(A) Except as provided in subparagraph (B), the amendments made by this subsection shall take effect as if included in chapter 13 of the Internal Revenue Code of 1954 as added by section 2006 of the Tax Reform Act of 1976.

(B) The amendment made by paragraph (1) shall take effect on October 4, 1976.

(o) ADJUSTMENT IN INCOME TAX ON ACCUMULATION DISTRIBUTIONS FOR PORTION OF ESTATE AND GENERATION-SKIPPING TRANSFER TAXES.—

(1) IN GENERAL.—Subsection (b) of section 667 (relating to tax on accumulation distribution) is amended by adding at the end thereof the following new paragraph:

"(6) ADJUSTMENT IN PARTIAL TAX FOR ESTATE AND GENERATION-SKIPPING TRANSFER TAXES ATTRIBUTABLE TO PARTIAL TAX.—

"(A) IN GENERAL.—The partial tax shall be reduced by an amount which is equal to the predeath portion of the partial tax multiplied by a fraction—

"(i) the numerator of which is that portion of the tax imposed by chapter 11 or 13, as the case may be, which is attributable (on a proportionate basis) to amounts included in the accumulation distribution, and

"(ii) the denominator of which is the amount of the accumulation distribution which is subject to the tax imposed by chapter 11 or 13, as the case may be.

"(B) PARTIAL TAX DETERMINED WITHOUT REGARD TO THIS PARAGRAPH.—For purposes of this paragraph, the term 'partial tax' means the partial tax imposed by subsection (a)(2) determined under this subsection without regard to this paragraph.

"(C) PRE-DEATH PORTION.—For purposes of this paragraph, the pre-death portion of the partial tax shall be an amount which bears the same ratio to the partial tax as the portion of the accumulation distribution which is attributable to the period before the date of the death of the decedent or the date of the generation-skipping transfer bears to the total accumulation distribution."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply—

(A) in the case of the tax imposed by chapter 11 of the Internal Revenue Code of 1954, to the estates of decedents dying after December 31, 1979, and

(B) in the case of the tax imposed by chapter 13, to any generation-skipping transfer (within the meaning of section 2611(a) of such Code) made after June 11, 1976.

(p) RELIEF OF EXECUTOR FROM PERSONAL LIABILITY IN THE CASE OF RELIANCE ON GIFT TAX RETURNS.—

(1) IN GENERAL.—Section 2204 (relating to discharge of fiduciary from personal liability) is amended by adding at the end thereof the following new subsection:

"(d) GOOD FAITH RELIANCE ON GIFT TAX RETURNS.—If the executor in good faith relies on gift tax returns furnished under section 6103(e)(3) for determining the decedent's adjusted taxable gifts, the executor shall be discharged from personal liability with respect to any deficiency of the tax imposed by this chapter which is attributable to adjusted taxable gifts which—

"(1) are made more than 3 years before the date of the decedent's death, and

"(2) are not shown on such returns.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply with respect to the estates of decedents dying after December 31, 1976.

(q) INDEXING OF FEDERAL TAX LIENS.—

(1) IN GENERAL.—Paragraph (4) of section 6323(f) (relating to indexing of tax liens) is amended to read as follows:

"(4) INDEXING REQUIRED WITH RESPECT TO CERTAIN REAL PROPERTY.—In the case of real property, if—

"(A) under the laws of the State in which the real property is located, a deed is not valid as against a purchaser of the property who (at the time of purchase) does not have actual notice or knowledge of the existence of such deed unless the fact of filing of such deed has been entered and recorded in a public index at the place of filing in such a manner that a reasonable inspection of the index will reveal the existence of the deed, and

"(B) there is maintained (at the applicable office under paragraph (1)) an adequate system for the public indexing of Federal tax liens,

then the notice of lien referred to in subsection (a) shall not be treated as meeting the filing requirements under paragraph (1) unless the fact of filing is entered and recorded in the index referred to in subparagraph (B) in such a manner that a reasonable inspection of the index will reveal the existence of the lien."

(2) REFILING OF NOTICE OF LIEN.—Section 6323(g)(2)(A) (relating to refiling of notice of lien) is amended to read as follows:

"(A) if—

"(i) such notice of lien is refiled in the office in which the prior notice of lien was filed, and

"(ii) in the case of real property, the fact of refiling is entered and recorded in an index to the extent required by subsection (f)(4); and".

(3) EFFECTIVE DATE.—

(A) The amendments made by this subsection shall apply with respect to liens, other security interests, and other interests in real property acquired after the date of the enactment of this Act.

(B) If, after the date of the enactment of this Act, there is a change in the application (or nonapplication) of section 6323 (f)(4) of the Internal Revenue Code of 1954 (as amended by paragraph (1)) with respect to any filing jurisdiction, such change shall apply only with respect to liens, other security interests, and other interests in real property acquired after the date of such change.

(r) CLERICAL AMENDMENTS.—

(1) CLERICAL AMENDMENTS WITH RESPECT TO SECTION 6694.—

(A) IN GENERAL.—Section 6694 (relating to failure to file information with respect to carryover basis property) which was added by section 2005(d)(2) of the Tax Reform Act of 1976 is redesignated as section 6698

(B) DEFICIENCY PROCEDURES NOT TO APPLY.—Section 6698 (as redesignated by subparagraph (A)) is amended by adding at the end thereof the following new subsection:

"(c) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a)."

(C) TABLE OF SECTIONS.—The table of sections for subchapter B of chapter 68 is amended by striking out

"Sec. 6694. Failure to file information with respect to carryover basis property."

and inserting in lieu thereof the following:

"Sec. 6698. Failure to file information with respect to carryover basis property."

(2) CLERICAL AMENDMENT TO SECTION 2051.—Section 2051 (defining taxable estate) is amended by striking out "exemption and".

(3) CLERICAL AMENDMENT TO SECTION 1016(a).—Subsection (a) of section 1016 (relating to adjustments to basis) is amended by redesignating paragraph (23) as paragraph (21).

(4) CLERICAL AMENDMENT TO SECTION 6324B(b).—Subsection (b) of section 6324B (relating to period of lien for additional estate tax attributable to farm, etc, valuation) is amended by striking out "qualified farm real property" and inserting in lieu thereof "qualified real property".

(5) EFFECTIVE DATE.—The amendments made by this subsection shall apply to estates of decedents dying after December 31, 1976.

SEC. 703. CORRECTIONS OF PUNCTUATION, SPELLING, INCORRECT CROSS REFERENCES, ETC.

(a) ERRONEOUS CROSS REFERENCE IN INVESTMENT CREDIT.—

(1) AMENDMENT OF SECTION 46(f)(8).—The first sentence of paragraph (8) of section 46(f) is amended by striking out "subsection (a)(6)(D)" and inserting in lieu thereof "subsection (a)(7)(D)".

(2) AMENDMENT OF SECTION 46(g)(5).—Paragraph (5) of section 46(g) (relating to definitions) is amended by striking out "Merchant Marine Act, 1970" and inserting in lieu thereof "Merchant Marine Act, 1936".

(3) AMENDMENT OF SECTION 48(d)(1)(B).—Subparagraph (B) of section 48(d)(1) is amended by striking out "section 46(a)(5) and inserting in lieu thereof "section 46(a)(6)".

(4) AMENDMENT OF SECTION 48(d)(4)(D).—Subparagraph (D) of section 48(d)(4) is amended by striking out "section 57(c)(2)" and inserting in lieu thereof "section 57(c)(1)(B)".

(b) PREPAID LEGAL SERVICES.—

(1) Paragraph (2) of section 213(e) of the Tax Reform Act of 1976 is amended by striking out "section 120(d)(6)" and inserting in lieu thereof "section 120(d)(7)".

(2) Paragraph (20) of section 501(c) is amended by striking out "section 501(c)(20)" and inserting in lieu thereof "this paragraph".

(c) AMENDMENTS RELATING TO SECTIONS 219 AND 220.—

(1) AMENDMENT OF SECTION 219(c)(4).—Paragraph (4) of section 219(c) (relating to participation in governmental plans by certain individuals) is amended by striking out "subsection (b)(3)(A)(iv)" each place it appears and inserting in lieu thereof "subsection (b)(2)(A)(iv)".

(2) AMENDMENT OF SECTION 220(b)(1)(A).—Subparagraph (A) of section 220(b)(1) (relating to retirement savings for certain married individuals) is amended by striking out "amount paid to the account or annuity, or for the bond" and inserting in lieu thereof "amount paid to the account, for the annuity, or for the bond".

(3) AMENDMENT OF SECTION 220(b)(4).—Paragraph (4) of section 220(b) is amended by inserting "described in subsection (a)" after "any payment".

(4) AMENDMENT OF SECTION 408(d)(4).—Subparagraph (A) of section 1501(b)(5) of the Tax Reform Act of 1976 is amended to read as follows;

"(A) by inserting 'or 220' after '219' each place it appears, and".

(5) EFFECTIVE DATE.—The amendments made by this subsection shall apply to taxable years beginning after December 31, 1976.

(d) ACCRUAL ACCOUNTING FOR FARM CORPORATIONS.—Subsections (a) and (g)(2) of section 447 are each amended by striking out "preproductive expenses" and inserting in lieu thereof "preporductive period expenses".

(e) AMENDMENT OF SECTION 911.—Subsection (c) of section 911 is amended by redesignating paragraph (8) as paragraph (7).

(f) TRANSITION RULE FOR PRIVATE FOUNDATIONS.—Subparagraph (F) of section 101(l)(2) of the Tax Reform Act of 1969 (relating to private foundations savings provisions) is amended by striking out the period at the end of clause (i) and inserting in lieu thereof a comma.

(g) LOBBYING BY PUBLIC CHARITIES.—

(1) LOBBYING NONTAXABLE AMOUNT.—Paragraph (2) of section 4911(c) (defining lobbying nontaxable amount) is amended by striking out "proposed expenditures" in the heading of the table contained in such paragraph and inserting in lieu thereof "exempt purpose expenditures".

(2) TECHNICAL AMENDMENTS RELATING TO SECTION 501.—

(A) Section 2(a) of Public Law 94–568 is amended by striking out "subsection (h) as subsection (i) and by inserting after subsection (g)" and inserting in lieu thereof "subsection (i) as subsection (j) and by inserting after subsection (h)".

(B) Subsection (g) of section 501 of the Internal Revenue Code of 1954 (as inserted by section 2(a) of Public Law 94–568) is redesignated as subsection (i).

(C) The amendments made by this paragraph shall take effect on October 20, 1976, as if included in Public Law 94–568.

(h) AMENDMENTS TO FOREIGN TAX PROVISIONS.—

(1) Paragraph (2) of section 1035(c) of the Tax Reform Act of 1976 (relating to tax credit for production-sharing contracts) is amended—

(A) by inserting "(as defined in section 907 (c) of such Code)" after "gas extraction income" in subparagraph (A), and

(B) by striking out "(as defined in section 907(c)(1) of such Code)" in subparagraph (B) and inserting in lieu thereof "(as so defined)".

(2) Paragraph (1) of section 999(c), (relating to international boycott factor) is amended by striking out "995(b)(3)" and inserting in lieu thereof "995(b)(1)(F)(ii)".

(3) Paragraph (2) of section 999(c) is amended by striking out "995(b)(1)(D)(ii)" and inserting in lieu thereof "995(b)(1)(F)(ii)".

(i) AMENDMENTS TO DISC PROVISIONS.—

(1) The last two sentences of section 995(b)(1) (relating to deemed distributions to shareholders of a DISC) are amended—

(A) by striking out "gross income (taxable income in the case of subparagraph (D))" and inserting in lieu thereof "income"; and

(B) by striking out "subparagraph (E)" and inserting in lieu thereof "subparagraph (G)".

(2) Subparagraph (G) of section 995(b)(1) is amended by striking out "subsection (D)" and inserting in lieu thereof "subsection (d)".

(3) Paragraph (2) of section 996(a) (relating to qualifying distributions) is amended by striking out "section 995(b)(1)(E)" and inserting in lieu thereof "section 995(b)(1)(G)".

(4) Paragraph (5) of section 1101(g) of the Tax Reform Act of 1976 is amended by striking out "section 993(e)(3)" and inserting in lieu thereof "section 995(e)(3)".

(j) AMENDMENTS RELATING TO DEADWOOD PROVISIONS.—

(1) TAX EXEMPT GOVERNMENTAL OBLIGATIONS.—

(A) The heading of paragraph (1) of section 103(b) is amended to read as follows:

"(1) SUBSECTION (a) (1) OR (2) NOT TO APPLY.—

(B) Paragraph (1) of section 103(c) is amended by striking out "(a) (1) or (4)" each place it appears (including in the paragraph heading) and inserting in lieu thereof "(a) (1) or (2)".

(C) Subparagraph (A) of section 103(c)(2) is amended by striking out "subsection (a) (1) or (2) or (4)" and inserting in lieu thereof "subsection (a) (1) or (2)".

(D) Paragraph (5) of section 103(c) is amended by striking out "subsection (d)(2)(A)" and inserting in lieu thereof "paragraph (2)(A)".

(E) Subsection (d) of section 103 is amended by striking out "subsection (c)(4)(G)" and inserting in lieu thereof "subsection (b)(4)(G)".

(2) AMENDMENTS RELATING TO SECTION 311(d)(2).—

(A) Subsection (b) of section 2 of the Bank Holding Company Tax Act of 1976 is amended—

(i) by striking out "subparagraph (F)" and inserting in lieu thereof "subparagraph (E)", and

(ii) by striking out "subparagraph (G)" and inserting in lieu thereof "subparagraph (F)".

(B) Subparagraph (H) of section 311(d)(2) is redesignated as subparagraph (G).

(C) The amendments made by this paragraph shall take effect as if included in section 2(b) of the Bank Holding Company Tax Act of 1976.

(3) AMENDMENT TO SECTION 453(c).—Paragraph (3) of section 453(c) is amended—

(A) by striking out "(or by the corresponding provisions of prior revenue laws)" in the first sentence, and

(B) by striking out the last sentence.

(4) AMENDMENT OF SECTION 801(g).—Paragraphs (1)(B)(ii) and (7) of section 801(g) are each amended by striking out "subparagraph (A), (B), (C), (D), or (E) of section 805(d)(1)" and inserting in lieu thereof "any paragraph of section 805(d)".

(5) AMENDMENT OF SECTION 1033(a)(2).—Clause (ii) of section 103(a)(2)(A) is amended by striking out "subsection (c)" and inserting in lieu thereof "subsection (b)".

(6) AMENDMENT OF SECTION 1375(a).—Paragraph (2) of section 1375(a) is amended by striking out "such excess" each place it appears and inserting in lieu thereof "such gain".

(7) AMENDMENT OF SECTION 1561(b)(3).—Paragraph (3) of section 1561(b) is amended by striking out "804(a)(4)" and inserting in lieu thereof "804(a)(3)".

(8) AMENDMENTS OF SECTION 1402.—

(A) The last paragraph of section 1402(a) of the Internal Revenue Code of 1954 (definition of net earnings from self-employment) is amended by striking out "subsection (i)" each place it appears and inserting in lieu thereof "subsection (h)".

(B) Section 1402(c)(6) of such Code (definition of trade or business) is amended by striking out "subsection (h)" and inserting in lieu thereof "subsection (g)".

(9) AMENDMENT TO SECTION 46(a).—Subparagraph (C) of section 1901(b)(1) of the Tax Reform Act of 1976 is amended by striking out "Section 46(a)(3)" and inserting in lieu thereof "Section 46(a)(4)".

(10) AMENDMENT RELATING TO SECTION 6504.—Subparagraph (D) of section 1901(b)(37) of the Tax Reform Act of 1976 is amended by striking out "6515" and inserting in lieu thereof "6504".

(11) TERRITORIES.—Subsection (c) of section 1901 of the Tax Reform Act of 1976 (relating to Territories) is amended by striking out paragraph (1) thereof.

(12) ESTATE AND GIFT TAXES EFFECTIVE DATE.—Subsection (c) of section 1902 of the Tax Reform Act of 1976 is amended to read as follows:

"(c) EFFECTIVE DATES.—

"(1) ESTATE TAX AMENDMENTS.—The amendments made by paragraphs (1) through (8), and paragraphs (12) (A), (B), and (C), of subsection (a) and by subsection (b) shall apply in the case of estates of decedents dying after the date of the enactment of this Act, and the amendment made by paragraph (9) of subsection (a) shall apply in the case of estates of decedents dying after December 31, 1970.

"(2) GIFT TAX AMENDMENTS.—The amendments made by paragraphs (10), (11), and (12) (D) and (E) of subsection (a) shall apply with respect to gifts made after December 31, 1976."

(13) EFFECTIVE DATE FOR AMENDMENT MADE BY SECTION 1904(a)(22)(A).—Notwithstanding section 1904(d) of the Tax Reform Act of 1976, the amendment made by section 1904(a)(22)(A) of such Act shall take effect on the date of the enactment of such Act.

(14) AMENDMENTS TO SOCIAL SECURITY ACT.—

(A) Section 202(v) of the Social Security Act is amended by striking out "section 1402(h)" each place it appears and inserting in lieu thereof "section 1402(g)".

(B) Section 205(p)(3) of such Act is amended by striking out "Secretary of the Treasury" and inserting in lieu thereof "Secretary of Transportation".

(C) Section 210(a)(6)(B)(v) of such Act is amended by striking out "Secretary of the Treasury" and inserting in lieu thereof "Secretary of Transportation".

(D) Section 211(a)(2) of such Act is amended by striking out "(other than interest described in section 35 of the Internal Revenue Code of 1954)".

(E) Section 211(c)(6) of such Act is amended by striking out "section 1402(h)" and inserting in lieu thereof "section 1402(g)".

(k) CAPITAL LOSS CARRYOVERS.—Clause (ii) of section 1212(a)(1)(C) (relating to capital loss carryovers for foreign expropriation losses) is amended by striking out "exceeding the loss year" and inserting in lieu thereof "succeeding the loss year".

(l) AMENDMENTS RELATING TO CERTAIN AIRCRAFT MUSEUMS.—

(1) Paragraph (2) of section 4041(h) (defining aircraft museum) is amended by striking out "term 'aircraft' means" and inserting in lieu thereof "term 'aircraft museum' means".

(2) Subsection (i) of section 4041 (as added by section 1904 (a)(1)(C) of the Tax Reform Act of 1976) is redesignated as subsection (j).

(3) Subsection (d) of section 6427 (relating to repayment of tax on fuels used by certain aircraft museums) is amended by striking out "Secretary or his delegate" and inserting in lieu thereof "Secretary".

(4) Paragraph (1) of section 7609(c) (defining summons to which section applies) is amended by striking out "6427(e)(2)" and inserting in lieu thereof "6427(f)(2)".

(m) INSPECTION BY COMMITTEE OF CONGRESS.—Paragraph (2) of section 6104(a) (relating to inspection by committee of Congress) is amended by striking out "Section 6103(d)" and inserting in lieu thereof "Section 6103(f)".

(n) AMENDMENT OF SECTION 6501.—Subsections (h), (j), and (o) of section 6501 are each amended by striking out "section 6213(b)(2)" and inserting in lieu thereof "section 6213(b)(3)".

(o) CONFORMING AMENDMENTS TO NEW DEFINITION OF TAXABLE INCOME.—

(1) Subparagraph (A) of section 443(b)(2) (relating to computation based on 12-month period) is amended—

(A) by striking out "taxable income" the second and third places it appears in clause (i) and inserting in lieu thereof "modified taxable income", and

(B) by amending clause (ii) to read as follows:

"(ii) the tax computed on the sum of the modified taxable income for the short period plus the zero bracket amount."

(2) Paragraph (1) of section 443(b) is amended by striking out "gross income for such short period (minus the deductions allowed by this chapter for the short period, but only the adjusted amount of the deductions for personal exemptions)" and inserting in lieu thereof "modified taxable income for such short period".

(3) Subsection (b) of section 443 is amended by adding at the end thereof the following new paragraph:

"(3) MODIFIED TAXABLE INCOME DEFINED.—For purposes of this subsection the term 'modified taxable income' means, with respect to any period, the gross income for such period minus the deductions allowed by this chapter for such period (but, in the case of a short period, only the adjusted amount of the deductions for personal exemptions)."

(4) The amendments made by this subsection shall apply to taxable years beginning after December 31, 1976.

(p) CONFORMING AMENDMENTS TO REPEAL OF SECTION 317 OF TRADE EXPANSION ACT OF 1962.—

(1) AMENDMENTS OF SECTION 172.—

(A) Subparagraph (A) of section 172(b)(1) (relating to years to which loss may be carried) is amended to read as follows:

"(A) Except as provided in subparagraphs (D), (E), (F), and (G), a net operating loss for any taxable year shall be a net operating loss carryback to each of the 3 taxable years preceding the taxable year of such loss."

(B) Paragraph (3) of section 172(b) (relating to special rules) is amended by striking out subparagraph (A) and (B) and by redesignating subparagraphs (C), (D), and (E) as subparagraphs (A), (B), and (C), respectively.

(C) Subparagraph (B) of section 172(b)(3) (as redesignated by subparagraph (B)) is amended by striking out "subparagraph (C)(iii)" each place it appears and inserting in lieu thereof "subparagraph (A)(iii)".

(2) AMENDMENT OF SECTION 6501(h).—Subsection (h) of section 6501 (relating to net operating loss or capital loss carryback) is amended by striking out the last sentence.

(3) AMENDMENT OF SECTION 6511(d)(2).—The first sentence of section 6511(d)(2)(A) (relating to special period of limitation for net operating loss or capital loss carrybacks) is amended by striking out "except that—" and all that follows down through the period at the end of such sentence and inserting in lieu thereof the following: "except that with respect to any overpayment attributable to the creation of, or an increase in a net operating loss carryback as a result of the elimination of excessive profits by a renegotiation (as defined in section 1481(a)(1)(A)), the period shall not expire before the expiration of the 12th month following the month in which the agreement or order for the elimination of such excessive profits becomes final."

(4) EFFECTIVE DATE.—The amendments made by this subsection shall apply with respect to losses sustained in taxable years ending after the date of the enactment of this Act.

(q) CONFORMING AMENDMENT TO REPEAL OF SECTION 2 OF THE EMERGENCY INSURED STUDENT LOAN ACT OF 1969.—

(1) IN GENERAL.—Paragraph (5) of section 103(d) (relating to arbitrage bonds) is amended by striking out "section 2 of the Emergency Insured Student Loan Act of 1969" and inserting in lieu thereof "section 438 of the Higher Education Act of 1965".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply with respect to payments made by the Commissioner of Education after December 31, 1976.

(r) EFFECTIVE DATE.—Except as otherwise provided, the amendments made by this section shall take effect on October 4, 1976.

TITLE VIII—AMENDMENTS RELATING TO SOCIAL SECURITY ACT

SEC. 801. GRANTS TO STATES FOR SOCIAL SERVICES.

(a) AMOUNT TO BE ALLOCATED TO STATES.—Section 2020(a)(2)(A) of the Social Security Act is amended—

(1) by striking out "$2,500,000,000" and inserting in lieu thereof "the amount specified in clause (ii)":

(2) by inserting "(i)" after "(2)(A)"; and

(3) by adding the following clause at the end thereof:

"(ii) The amount specified for purposes of clause (i) is $2,500,000,000 for fiscal years prior to fiscal year 1979, $2,700,000,000 for fiscal year 1979 and $2,500,000,000 for fiscal years after fiscal 1979.".

(b) ADDITIONAL AMOUNT FOR CHILD DAY CARE SERVICES IN FISCAL YEAR 1979.—Section 3 of Public Law 94-401 is amended—

(1) in the matter preceding paragraph (1) of subsection (a)—

(A) by striking out the word "and" which appears after "1977,", and

(B) by inserting after "1978," the following: "and the fiscal year ending September 30, 1979,":

(2) in subsection (a)(1), by adding after and below subparagraph (B) the following new subparagraph:

"(C) 107.407 per centum of the amount of the limitation so imposed (as determined without regard to this section) in the case of such fiscal year ending September 30, 1979, or",

(3) in subsection (a)(2), by striking out "or either such fiscal year" and inserting in lieu thereof "or any such fiscal year",

(4) in subsection (b), by striking out "or either fiscal year" and inserting in lieu thereof "or and fiscal year",

(5) in subsections (c)(1) and (c)(2)(A), by striking out "or either fiscal year" and inserting in lieu thereof "or any fiscal year (other than the fiscal year ending September 30, 1979)",

(6) in subsection (d)(1)—

(A) by striking out the word "or" which appears after "1977,", and

(B) by inserting after "1978" the following: ", or the fiscal year ending September 30, 1979", and

(7) in subsection (d)(2), by striking out "for either such fiscal year" and inserting in lieu thereof "for any such fiscal year".

SEC. 802. CHANGES IN PUBLIC ASSISTANCE MATCHING FORMULA, AND INCREASE IN AMOUNT OF PUBLIC ASSISTANCE DOLLAR LIMITATIONS, FOR PUERTO RICO, THE VIRGIN ISLANDS, AND GUAM IN FISCAL YEAR 1979.

(a) PUBLIC ASSISTANCE MATCHING FORMULA.—Section 1118 of the Social Security Act is amended by adding at the end thereof the following new sentence. "For purposes of the preceding sentence, the term 'Federal medical assistance percentage' shall, in the case of Puerto Rico, the Virgin Islands, and Guam, mean 75 per centum when applied to quarters in the fiscal year ending September 30, 1979.".

(b) DOLLAR LIMITATIONS.—Subsection (a) of section 1108 of such Act is amended—

(1) in paragraph (1)—

(A) by striking out "or" at the end of clause (D),

(B) by striking out the semicolon at the end of clause (E) and inserting in lieu thereof "other than the fiscal year 1979, or"; and

(C) by adding at the end thereof the following new subparagraph.

"(F) $72,000,000 with respect to the fiscal year 1979;",

(2) in paragraph (2)—

(A) by striking out "or" at the end of clause (D),

(B) by striking out "; and" at the end of clause (E) and inserting in lieu thereof "other than the fiscal year 1979, or"; and

(C) by adding at the end thereof the following new subparagraph:

"(F) $2,400,000 with respect to the fiscal year 1979;", and

(3) in paragraph (3)—

(A) by striking out "or" at the end of clause (D),

(B) by striking out the period at the end of clause (E) and inserting in lieu thereof "other than the fiscal year 1979, or"; and

(C) by adding at the end thereof the following new subparagraph:

"(F) $3,300,000 with respect to the fiscal year 1979.".

And the Senate agree to the same.

AL ULLMAN,
DAN ROSTENKOWSKI,
CHARLES A. VANIK,
JAMES C. CORMAN,
OMAR BURLESON,
SAM GIBBONS,
JOE D. WAGGONNER, JR.,
JOHN J. DUNCAN,
BILL ARCHER,
Managers on the Part of the House.

RUSSELL B. LONG,
HERMAN TALMADGE,
ABRAHAM RIBICOFF,
HARRY F. BYRD, JR.,
GAYLORD NELSON,
MIKE GRAVEL,
LLOYD BENTSEN,
SPARK M. MATSUNAGA,
DANIEL P. MOYNIHAN,
CARL T. CURTIS,
CLIFFORD P. HANSEN,
BOB PACKWOOD,
Managers on the Part of the Senate.

JOINT EXPLANATORY STATEMENT OF THE COMMITTEE OF THE CONFERENCE

The Managers on the part of the House and Senate at the conference on the disagreeing votes of the two houses on the amendments of the Senate to the bill (H.R. 13511) to amend the Internal Revenue Code of 1954 to reduce income taxes, and for other purposes, submit the following joint statement to the House and the Senate as an explanation of the effect of the action agreed upon by the Managers and recommended in the accompanying conference report:

Contents

I. INDIVIDUAL TAX REDUCTIONS AND REVISIONS

A. Individual Tax Reductions and Extensions

1. Widening tax brackets, rate cuts in certain brackets, and increase in zero bracket amount

House bill.—Under present law, individual income tax rates begin at 14 percent on taxable income in excess of $3,200 on a joint return and $2,200 on a single return, and a head of household return. There is no tax on the first tax bracket, referred to as the "zero bracket amount." This amount is also a floor under itemized deductions.

Individual tax rates range up to 70 percent on taxable income in excess of $203,200 for joint returns and $102,200 for single returns. Present law also provides different rate schedules for heads of households, married couples filing separately, and estates and trusts. There are 25 tax brackets.

Increase in zero bracket amount.—The House bill increases the zero bracket amount from $3,200 to 3,400 for joint returns and from $2,200 to $2,300 for single persons. For heads of households, the increase is also $100 to $2,300. For married persons filing separate returns, the increase is from $1,600 to $1,700.

Widening of tax brackets.—The second rate schedule change is that the size of the tax brackets (in excess of the zero bracket) are increased by 6 percent. For example, under present law, the zero bracket amount is $3,200 and the first tax bracket is from $3,200 to $4,200, or $1,000 wide. Under the bill, the zero bracket amount is $3,400 and the bracket width is increased by 6 percent of $1,000 (or $60) to $1,060, so that the first income bracket range is from $3,400 to $4,460. The same principle applies throughout the rate schedule.

Reduction in certain tax rates.—The House bill also reduces, for married individuals filing jointly, the present 19, 22 and 25 percent rates one point to 18, 21 and 24 percent, respectively, for the present law taxable income range $7,200 to $19,200, The change in the tax rate schedule, including the higher zero bracket amount, is effective for taxable years beginning after December 31, 1978.

Senate amendment.—Increase in zero bracket amount.—Same as the House bill, except that the increase for heads of households is to $3,000, not $2,300.

Widening of tax brackets.—A new tax rate schedule is provided with 15 instead of 25 tax brackets for married individuals filing jointly, and 16 brackets for single individuals, with wider brackets, particularly the top brackets.

Reduction in certain tax rates.—The rate reductions are directed more toward the lower- and middle-income tax brackets than in the House bill. Six tax rates are reduced compared to present law (joint return schedule): the 14-percent rate to 13, the 15, 16 and 17 percent rate to 14, the 9 percent rate to 16 and the 22 percent rate to 21—this covers the first $15,000 of taxable income under present law.

One tax rate is increased: the 28 percent rate to 29 which covers the present law taxable income range $19,200 to $23,200. These changes are effective for taxable years beginning after December 31, 1978.

Conference agreement.—The conference agreement retains the tax brackets of the Senate amendment, but the zero bracket amount for heads of households is the $2,300 of the House bill rather than the $3,000 of the Senate amendment. The conference agreement modifies the Senate bill rate reductions so that they yield a tax reduction $1 billion more than the House bill rather than the $2 billion more to the Senate amendment.

2. Increase in the personal exemption

House bill.—Under present law, the amount of the personal exemption is $750 for the taxpayer, his or her spouse, and each dependent whose gross income is less than $750 (unless the dependent is the taxpayer's child and is either under age 19 or a student). An additional exemption is provided for a taxpayer who is blind or age 65 or over. Present law also provides a general tax credit, which is the larger of $35 per exemption or 2 percent of the first $9,000 of taxable income (in excess of the zero bracket amount), with a maximum credit of $180. The credit is scheduled to expire at the end of 1978.

The House bill provides a permanent increase in the personal exemption from $750 to $1,000, and increases the gross income limit for a dependent from $750 to $1,000. The general tax credit is allowed to expire at the end of 1978. The increase in the personal exemption is effective for taxable years beginning after December 31, 1978. The general tax credit will no longer apply for taxable years ending after December 31, 1978.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement follows the House bill and the Senate amendment.

3. Additional personal exemption for the handicapped

House bill.—No provision.

Senate amendment.—Under present law, there is no extra personal exemption provided for handicapped persons (as there is in the case of those who are blind or age 65 and over).

The Senate amendment provides an additional personal exemption to a handicapped taxpayer. Handicapped means permanently and totally disabled.

The additional exemption would not be available to an individual, however, if he or she received benefits as a disabled veteran, a disabled civil service employee, or receives cash benefits as a disabled person under the Social Security Act or other Federal, State or local government program, In addition, the extra exemption would not be available with respect to anyone age 65 or over.

The additional personal exemption is to be $500 for 1979 and 1980 and is to be increased to $1,000 for 1981 and thereafter.

Conference agreement.—The conference agreement does not contain this provision.

4. Changes in filing requirements and withholding changes

House bill.—Under present law, a tax return must be filed by a single person and a head of household if his or her income is $2,950 or more a year and by a married couple under age 65 filing a joint return if their income is $4,700 or more. The House bill increases the filing levels for a single person and a head of household to $3,300 and to $4,500 for a married couple (under age 65).

The withholding tax rates reflect the present law tax rates, the zero bracket amount, and the amount of the personal exemption. Under the House bill, the withholding rates and tables are to be changed by the Secretary of the Treasury to reflect the increase in the zero bracket amount and the personal exemption.

The change in the filing requirement is effective for taxable years beginning after December 31, 1978, and the withholding changes apply to wages paid after December 31, 1978.

Senate amendment.—The Senate amendment is the same as the House bill, except the filing requirement for heads of households is increased to $4,000.

The withholding changes are to be the same as the House bill except to reflect the higher zero bracket amount for heads of households and the different tax rate reductions.

The date for the filing requirement change is the same as the House bill, but the withholding changes are to apply to wages paid after July 31, 1978.

Conference agreement.—The conference agreement is the same as the House bill except the withholding changes are to reflect the larger rate reductions than in the House bill.

5. Earned income credit

House bill.—Under present law, a refundable credit is allowed against income tax equal to 10 percent of the first $4,000 of earned income (a maximum of $400). The credit phases out between $4,000 and $8,000 of adjusted gross income (or, if higher, earned income). The credit generally is allowed to taxpayers who live with children, and is due to expire at the end of 1978.

The House bill makes the earned income credit permanent, and modifies the credit in several respects to make it easier for taxpayers to compute the credit and to enable the Internal Revenue Service to allow the credit to taxpayers who qualify but neglect to claim the credit on their tax return. Generally, under the House bill, any individual who is considered to be married and who is entitled to a dependency exemption, under section 151 of the Code, for a child living with the individual and surviving spouse, and any head of household will be eligible for the earned income credit.

Senate amendment.—The Senate amendment makes the credit permanent, and simplifies the determination of the amount of, and eligibility for, the credit in a manner similar to the House bill. In addition, the Senate amendment increases the amount of the credit to 12 percent of the first $5,000 of earned income (a maximum of $600) phased out between $6,000 and $11,000 of adjusted gross income (or, if higher, earned income), These dollar amounts are adjusted upward by the ratio of the poverty line for any noncontiguous State to the poverty line for the 48 contiguous States, if this ratio is 15 percent or greater.

Under the Senate amendment, employees could elect to have advance payments of the earned income credit added to their paychecks each pay period. The amount of the payment would be determined from tables which take into account the amount of wages paid and whether or not an employee's spouse was also claiming advance payments. Employers would reduce their liability for income tax withholding and FICA taxes for the aggregate amount of advance payments made to employees in any pay period.

Also, under the Senate amendment, the credit would be taken into account for purposes of Federal or Federally aided assistance programs. In addition, the Social Security Act would be amended to provide specifically that the earned income credit, and advance payments of the credit, be treated as earned income for purposes of the aid to families with dependent children program (AFDC) and supplemental security income (SSI) programs.

Conference agreement.—The conference agreement makes the earned income credit permanent, and simplifies the determination of the amount of, and eligibility for, the credit in a manner similar to both the House bill and the Senate amendment. Under the conference agreement, the credit is 10 percent of the first $5,000 of earned income (a maximum of $500) and is phased out between $6,000 and $10,000 of adjusted gross income (or, if higher, earned income).

The conference agreement provides that, as of July 1, 1979, employees may elect to have advance payments of the earned income credit added to their paychecks each pay period. The amount of advance payment would be determined from tables which take into account the amount of wages paid and whether or not an employee's spouse was also claiming advance payments. Employers would reduce their liability for income tax withholding and FICA taxes for the aggregate amount of advance payments made to employees in any pay period.

In addition, the conference agreement requires the credit to be taken into account for purposes of Federal or Federally aided assistance programs, effective January 1, 1980. Further, the Social Security Act will be amended, effective January 1, 1980, to provide specifically that the earned income credit, and advance payments of the credit, be treated as earned income for purposes of the aid to families with dependent children program (AFDC) and supplemental security income (SSI) programs.

B. Itemized Deductions and Individual Tax Credits

6. Repeal of deduction for State and local nonbusiness gasoline and other motor fuel taxes

House bill.—Under present law, an individual who itemizes deductions can deduct State and local taxes imposed on gasoline, diesel, and other motor fuels not used in business or investment activities.

The House bill repeals the itemized deduction for State and local taxes on gasoline, diesel, and other motor fuels not used by the taxpayer in business or investment activities.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement follows the House bill and the Senate amendment.

7. Revision of deduction for medical, dental, etc., expenses

House bill.—Under present law, an individual who itemizes deductions generally can deduct unreimbursed medical and dental expenses paid for the medical care of the individual, and his or her spouse and dependents, to the extent that the total of such expenses exceeds 3 percent of adjusted gross income. Amounts paid for medicine and drugs may be counted toward the deductible amount only to the extent they exceed one percent of adjusted gross income. In addition, one-half of the amount of medical insurance premiums (up to $150) can be deducted by itemizers without regard to the 3-percent limitation. The balance of medical insurance premiums is added to other medical expenses and is subject to the 3-percent limitation.

The House bill repeals the itemized deduction for one-half of the amount of medical insurance premiums (up to $150) without regard to the 3-percent limitation. In addition, the House bill repeals the special limitation in present law which permits deduction of prescription and nonprescription medicine and drug costs only to the extent they exceed one percent of adjusted gross income, and provides that only "prescribed drugs" and insulin are eligible for the medical expense deduction.

Senate amendment.—No provision.

Conference agreement.—The conference agreement retains the provisions of present law.

8. Political contributions

House bill.—Under present law, an individual who itemizes deductions can deduct political or newsletter fund contributions of up to $100 per year ($200 in the case of a joint return). Contributions eligible for the deduction may be made to (1) candidates for nomination or election to Federal, State, or local office in general, primary, or special elections; (2) committees sponsoring such candidates; (3) national, State, or local committees of a national political party; and (4) newsletter funds of an official or candidate.

Alternatively, a taxpayer can elect an income tax credit equal to one-half of such political and newsletter fund contribution, but not more than $25 ($50 in the case of a joint return).

The House bill repeals the itemized deduction for political or newsletter fund contributions. The income tax credit for such contributions, however, would remain available to taxpayers as under present law.

Senate amendment.—The Senate amendment, which is effective for taxable years beginning after December 31, 1978, increases the maximum amount of the income tax credit for political contributions from $25 to $50 ($100 in the case of a joint return). In all other respects, the amendment retains the limitations of present law on the credit's availability, and does not modify the alternative deduction for political contributions,

Conference agreement.—The conference agreement follows the provisions of the House bill and the Senate amendment. It repeals the deduction for political contributions, and increases the maximum amount of the income tax credit from $25 to $50 ($100 in the case of a joint return), In all other respects, the conference agreement retains the limitations of present law on the credit's availability.

9. Increase in tax credit for the elderly

House bill.—No provision.

Senate amendment.—Under present law, an individual taxpayer age 65 or older is entitled to a tax credit equal to 15 percent of the credit base minus certain offsets. Currently, the credit base is:

$2,500—Single individual or joint return where only one spouse is eligible;

$3,750—Joint return where both the spouses are eligible; or

$1,875—Married individuals filing a separate return.

This credit base is reduced by certain amounts received as a tax-free pension or annuity (for example, under Social Security or the Railroad Retirement System). The credit base also is reduced by one-half of the adjusted gross income in excess of certain limitations. These limitations are:

$7,500—Single individuals;

$10,000—Joint returns; or

$5,000—Married individuals filing separate returns.

The Senate amendment increases the credit base to $3,000 for a single person, $4,500 for a married couple where both spouses are age 65 or over, and to $2,250 for married individuals filing a separate return.

The Senate amendment also increases the income limitation to $15,000 for a single person and $17,500 for a married couple where both spouses are age 65 or over and to $8,750 for a married individual filing separately. The provision is effective for taxable years beginning after December 31, 1978.

Conference agreement.—The conference agreement does not contain this provision.

10. Credit for child care services

House bill.—No provision.

Senate amendment.—Under present law, payments for child care services by a taxpayer to certain relatives qualify for the child care credit only if the services constitute "employment," as defined for

Social Security purposes. Under the Social Security definition, child care services rendered by a grandparent generally do not constitute employment.

The Senate amendment provides generally that payments to grandparents for care of their grandchildren may qualify for the child care credit. This provision is effective for taxable years beginning after December 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment.

11. Tuition tax credit

House bill.—No provision.

Senate amendment.—Under present law, there is no tax credit for personal educational expenses.

The Senate amendment provides a nonrefundable tax credit equal to 35 percent of the tuition paid to one or more institutions of higher education or postsecondary vocational schools by an individual for himself, his spouse, or his dependents.

The maximum allowable credit for tuition paid to any one institution is:

(1) $100 for calendar year 1978;
(2) $150 for calendar year 1979, and
(3) $250 for calendar years 1980 and 1981.

The credit applies to amounts paid for education on or after August 1, 1978, for education furnished on or after that date. Expenses of half-time students are eligible for the credit as of January 1, 1980. The credit will remain in effect through calendar year 1981.

Conference agreement.—The conference agreement omits this provision.

C. Deferred Compensation Plans

12. State and local government deferred compensation plans

House bill.—Under present law, a cash method taxpayer generally is not required to include compensation in income until it is actually received or otherwise made available. Compensation generally is considered made available to the taxpayer if there are no substantial restrictions on the right to receive it.

If a taxpayer enters into an agreement with a payor to receive compensation on a deferred basis, rather than currently, the taxpayer generally will not be in constructive receipt of that compensation (i.e., it is not considered to be made available) so long as the agreement is made before the taxpayer obtains an unqualified and unconditional right to the compensation.

On February 3, 1978, the Internal Revenue Service issued proposed regulations which provided generally that, if payment of an amount of a taxpayer's fixed basic or regular compensation is deferred at the taxpayer's individual election to a taxable year later than that in which the amount would have been payable but for the election, the deferred amount would be treated as received in the earlier taxable year. These proposed regulations would apply to plans maintained by States and local governments and tax-exempt organizations as well as plans maintained by taxable employers.

The House bill provides that amounts of compensation deferred by a participant in an eligible deferred compensation plan maintained by a State or local government unit or a tax-exempt rural electric cooperative (and certain tax-exempt affiliates), plus any income attributable to the investment of such deferred amounts, will be includible in the income of the participant or his beneficiary only when such amounts are paid or otherwise made available. This rule will apply whether the participants are employees of the State or are independent contractors performing services for the State.

To qualify as an eligible deferred compensation plan, the plan must not allow the deferral of more than $7,500, or 33⅓ percent of the participant's includible compensation for the taxable year, whichever is less. Participants in these plans must reduce the $7,500 and 33⅓ percent limitations by the amounts deferred under any tax-sheltered annuity program which is excludable from income under section 403(b). In addition, the plan must satisfy other requirements relating to (1) the time an election to defer must be made (except in the case of new employees or newly implemented plans, the election to defer compensation must be made before the beginning of the plan year for which the deferral election is to be effective), (2) the time distributions can be made under the plan, and (3) the ownership of investments made with deferred amounts. The plan can provide an increased limitation in the 3 years before a participant retires.

All plans to which this provision applies will have until January 1, 1982, to satisfy the plan requirements for classification as an eligible State deferred compensation plan. However, the limitations on amounts that can be deferred under such a plan will apply for all taxable years beginning after December 31, 1978.

Senate amendment.—The Senate amendment would provide the same limitations on deferral as the House bill for employees or independent contractors who are participants in an unfunded deferred compensation arrangement maintained by a State or local government unit. However, the Senate amendment would not apply to participants in a plan maintained by a tax-exempt rural electric cooperative or any of its tax-exempt affiliates. In addition, the Senate amendment would permit plan participants to make monthly, rather than annual, elections to defer compensation.

Conference agreement.—The conference agreement generally follows the House bill except that it permits monthly, rather than annual, elections to defer compensation.

13. Private nonqualified plans

House bill.—The present law tax treatment of participants in unfunded deferred compensation arrangements maintained by taxable entities is the same as the tax treatment of participants in such arrangements maintained by States and local government units.

The House bill provides that the taxable year for including compensation deferred under a deferred compensation plan maintained by a taxable entity is to be determined in accordance with the principles set forth in regulations, rulings, and judicial decisions relating to deferred compensation which were in effect on February 1, 1978.

Senate amendment.—The Senate amendment is the same as the House bill, except that it applies also to participants in plans maintained by tax-exempt organizations.

Conference agreement.—The conference agreement follows the House bill.

14. Payments to independent contractors

House bill.—Under present law, an employer generally is permitted a deduction for deferred compensation provided under a nonqaulified plan in the year that such compensation is includible in the employee's gross income, even though the employer is on the accrual basis and normally would be entitled to a current deduction. This rule applies to any method of contributions or compensation having the effect of a plan deferring the receipt of compensation.

Under present law, the rule permitting a deduction for deferred compensation only when there is a corresponding income inclusion by a plan participant applies only where there is an employer-employee relationship. Thus, an accrual basis taxpayer generally is able to establish an unfunded deferred compensation plan for a cash basis independent contractor and obtain a deduction for such liability in accordance with the usual accrual accounting rules.

The House bill adds a new provision, effective for taxable years beginning after December 31, 1978, which denies a deduction for deferred compensation provided under a nonqualified plan to nonemployee participants until that compensation is includible in the gross income of the participants.

The House bill also clarifies current law by providing that a method of compensation or employer contributions having the effect of a plan deferring the receipt of compensation does not have to be similar to a stock bonus, pension, profit-sharing, or annuity plan to be subject to the deferred compensation deduction-timing rules.

Senate amendment.—The Senate amendment is the same as the House bill with minor technical changes.

Conference agreement.—The conference agreement is the same as the Senate amendment.

15. Tax treatment of "cafeteria plans"

House bill.—Under a "cafeteria" or "flexible benefit" plan an employee may choose from a package of employer-provided fringe benefits, some of which may be taxable and some of which may be nontaxable. Under a provision of the Employee Retirement Income Security Act of 1974 (ERISA), an employer contribution made before January 1, 1977, to a cafeteria plan in existence on June 27, 1974, is required to be included in an employee's gross income only to the extent that the employee actually elects taxable benefits. In the case of a plan not in existence on June 27, 1974, the employer contribution is required to be included in income to the extent the employee could have elected taxable benefits. Under the Tax Reform Act of 1976, these rules apply with respect to employer contributions made before January 1, 1978.

The House bill provides that employer contributions under a cafeteria plan generally are excluded from the employer's gross income to the extent that nontaxable benefits are elected. However, in the case of a highly compensated employee, amounts contributed under a cafeteria plan will be included in gross income for the taxable year in which the plan year ends, to the extent the individual could have elected taxable benefits unless the plan meets specified antidiscrimination standards with respect to coverage and eligibility and with respect to contributions or benefits. These rules apply for taxable years beginning after December 31, 1978.

Senate amendment.—The Senate amendment is the same as the House bill except for changes adding clarifying language, and making it clear that a plan must be in writing to be subject to the cafeteria plan rules. Thus, this provision will apply only when there is a written plan which provides employees a choice between taxable and nontaxable benefits. The taxation of benefits provided under other types of arrangements will be determined under existing law.

Conference agreement.—The conference agreement follows the Senate amendment.

16. Tax treatment of cash or deferred profit-sharing plans

House bill.—Under present law, the tax treatment of amounts contributed by an employer, to a cash or deferred profit-sharing plan, at the election of an employee, depends upon when the plan was established. Under a provision of the Employee Retirement Income Security Act of 1974 (ERISA), as amended by the Tax Reform Act of 1976, the tax treatment of contributions to cash or deferred profit-sharing plans in existence on June 27, 1974, is governed (until January 1, 1978) under the law as it was applied prior to 1972. (Under the rules in effect then, an employee was not taxed currently on amounts

he chose to have contributed to a tax-qualified cash or deferred profit-sharing plan.) In the case of plans not in existence on June 27, 1974, contributions to a cash or deferred profit-sharing plan are treated as employee contributions (until January 1, 1978, or until new regulations are prescribed in this area.)

The House bill changes present law with respect to new cash or deferred profit-sharing plans by permitting those plans to be tax-qualified (for taxable years beginning after December 31, 1977) provided the plans satisfy the law with respect to cash or deferred profit-sharing plans as it was administered before January 1, 1972.

Senate amendment.—The Senate amendment provides that a participant in a qualified cash or deferred arrangement will not have to include in income any employer contribution to the plan merely because he could have elected to receive such amount in cash instead. For the cash or deferred arrangement to be a tax-qualified plan, it must satisfy the normal pension plan qualification rules. In addition, it must satisfy the following requirements: (1) it must not permit the distribution of amounts attributable to employer contributions merely because of the completion of a stated period of plan participation or the passage of a fixed period of time, and (2) all amounts contributed by the employer pursuant to an employee's election must be nonforfeitable at all times.

Special nondiscrimination rules are provided for these arrangements to test for discrimination as to actual plan participation or as to the amount of contributions to the plan. Under these rules, a cash or deferred arrangement will meet the nondiscrimination requirements for qualification for a plan year if (1) the actual deferral percentage for the highest paid one-third of all eligible employees does not exceed the actual deferral percentage for the other eligible employees by more than 50 percent, or)2) the actual deferral percentage for the highest paid one-third of all eligible employees does not exceed the actual deferral percentage of the other eligible employees by more than three percentage points. (If this latter test is used, the actual percentage for the highest paid one-third cannot exceed the actual deferral percentage of all other eligible employees by more than 150 percent.)

The Senate amendment is effective for taxable years beginning after December 31, 1979; however, a transitional rule is provided for those cash or deferred arrangements in existence on January 27, 1974 under which their qualified status for plan years beginning before January 1, 1980 shall be determined in a manner consistent with Rev. Rul. 56–497 (1956–2 C.B. 284), Rev. Rul. 63–180 (1963–2 C.B. 189), and Rev. Rul. 68–89 (1968–1 C.B. 402).

Conference agreement.—The conference agreement follows the Senate amendment.

D. Employee Stock Ownership Plans

17. Employee stock ownership plans

House bill.—No provision.

Senate amendment.—(a) *Expiration date of TRASOP provisions.*—The Senate amendment makes the TRASOP provisions, as amended, part of the Code for the first time and makes them permanent by repealing the present law December 31, 1980, expiration date.

(b) *Qualification requirements for TRASOPs.*—The Senate amendment requires that all TRASOPs are to be tax-qualified plans if contributions are made for plan years beginning after December 31, 1978.

(c) *Date by which a TRASOP must be established for a plan year.*—The Senate amendment provides that a TRASOP may be treated as tax-qualified from its effective date even though the TRASOP is not actually established until the date for filing the employer's tax return for its taxable year (including extensions) in which the effective date falls.

(d) *Allocation of TRASOP contributions.*—Under present law, an employee who participates in a TRASOP at any time during the year for which an employer contribution is made is entitled to an allocation of the contribution. Under the Senate amendment, employer contributions to a TRASOP for a plan year generally are to be allocated in accordance with the rules governing the allocation of contributions to tax-qualified plans. In addition, the Senate amendment retains the present law requirement that the allocation of employer contributions to a TRASOP for a year must be made in proportion to total compensation of all participants sharing in the allocation for the plan year, taking into account only the first $100,000 of compensation for an employee.

(e) *Provisions relating to voting of employer securities by plan.*—The Senate amendment provides that if an ESOP or TRASOP holds employer stock issued by a corporation whose stock is "publicly traded," the plan must provide that the stock is to be voted by the plan participants. In addition, under the Senate amendment, the plan must provide for voting and dividend rights equivalent to rights possessed by shareholders of the highest class of stock of the issuing corporation which is "readily available" on a public market. The Senate amendment provides that a tax qualified defined contribution plan which, following any acquisition of employer securities after December 31, 1979, holds more than 10 percent of its assets in employer securities must provide that the plan participants are entitled to exercise voting rights with respect to any of such acquired stock which is issued by a corporation which is closely held on any corporate issue which must by law (or charter) be decided by more than a majority vote of common shareholders voting on the issue. The Senate amendment also provides that a TRASOP which holds employer stock issued by a corporation which is closely held must

provide that the plan participants are entitled to exercise voting rights with respect to the stock on the same types of corporate issues.

(f) *Treasury Department study with respect to voting rights by participants in ESOPs and TRASOPs.*—The Senate amendment requires the Treasury Department (working with representatives of private businesses, Congressional staffs and the Department of Labor) to institute a one-year study and to report to the Senate Finance Committee on the extent to which voting rights and different forms of financial disclosure should be given to participants in ESOPs and TRASOPs which hold employer stock issued by closely held corporations, and on the resale rights which should be available to a participant (or a beneficiary) who receives a distribution of employer stock from an ESOP, TRASOP, or stock bonus plan.

(g) *Definition of employer securities for leveraged ESOPs and TRASOPs.*—The Senate amendment provides that, in the case of a TRASOP or a leveraged ESOP, the only types of employer securities which may be acquired and held by the plan are common stock of the issuing corporation and preferred stock of the issuing corporation which is readily convertible into its common stock. In addition, in the case of a TRASOP, the Senate amendment applied a 50-percent test in lieu of the present law 80-percent test is determining whether a parent corporation is a member of the same parent-subsidiary controlled group of corporations as a subsidiary corporation.

(h) *Nonrecognition of gain or loss on contribution of stock of parent to TRASOP.*—The Senate amendment provides that where a parent corporation and a subsidiary corporation (including a second-tier subsidiary) are members of an affiliated group of corporations, the subsidiary corporation will not recognize gain or loss on a contribution to a TRASOP maintained by it of stock in the parent corporation.

(i) *Minimum tax.*—The Senate amendment provides that additional investment tax credit attributable to a TRASOP contribution will not result in the imposition of any additional minimum tax on the employer.

(j) *Special rule for contributions attributable to one-half percent TRASOP credit.*—The Senate amendment requires that the employer TRASOP contribution attributable to extra additional investment tax credit (up to one-half of one percent) for a qualified investment must be made to the extent that matching employee contributions are made, and must be made for the period in which the employee contributions are made.

(k) *Deduction of TRASOP contributions.*—The Senate amendment provides that, where the credit for a TRASOP contribution expires, a deduction is allowed for the amount of the expired credit in the year in which the credit expires.

(l) *Prohibition of withdrawal of TRASOP contributions on recapture.*—The Senate amendment provides that a TRASOP contribution made with respect to a particular qualified investment may not be withdrawn if all or a portion of the credit is later recaptured due to an early disposition of the qualified investment.

(m) *Distribution from ESOPs and TRASOPs.*—The Senate amendment provides that a participant in an ESOP or TRASOP who is entitled to a distribution under the plan must be given the right to

require that the distribution be made in the form of employer securities. Subject to such right, the plan may elect to distribute the participant's interest to him in cash, in employer securities, or partially in cash and partially in employer securities.

(n) *Put option on ESOP or TRASOP stock.*—The Senate amendment requires that participants or beneficiaries receiving a distribution of employer stock from a leveraged ESOP or TRASOP must generally be given a "put option," for the stock which meets specified requirements, in the case of an employer whose stock is subject to a trading limitation or is not publicly traded at the time of the distribution.

(o) *Estate tax exclusion for qualified plan distributions not subject to 10-year averaging.*—The Senate amendment provides that a death benefit under a qualified plan, which is eligible to be treated as a lump sum distribution, is excludible from the estate of the deceased plan participant if the recipient of the distribution agrees in writing not to elect to treat the distribution as a lump sum distribution eligible for special, favorable income tax treatment.

(p) *Rollover of proceeds from the sale of employer securities distributed rom a qualified plan.*—The Senate amendment permits an employee who receives employer securities as part of a lump sum distribution from a qualified plan, or as part of a complete distribution upon termination of a qualified plan, to sell the employer securities and receive tax-free rollover treatment by contributing all of the proceeds from the sale, plus any other assets received as part of the distribution to an IRA, within 60 days from the date of the distribution.

Conference agreement.—The conference agreement follows the Senate amendment except that (1) the TRASOP provisions are not made permanent, but rather, the expiration date of those provisions is extended for three years until December 31, 1983, and (2) the provision for rollover of proceeds from the sale of distributed employer securities is omitted from the ESOP provisions because the substance of the provision is covered elsewhere in the conference agreement.

E. Retirement Plan Provisions

18. Deduction for certain employee retirement savings contributions

House bill.—No provision.

Senate amendment.—Present law allows a deduction for a contribution to an IRA (an individual retirement account, annuity, or bond) for the lesser of 15 percent of earned income or $1,500 ($1,750 in the case of spousal IRAs). The deduction is not allowed to an active participant in a tax-qualified pension plan, a tax-sheltered annuity, or a governmental plan. No deduction is allowed for employee contributions to a qualified plan or a group retirement trust (a pre-1974 private annuity program under which benefits are fully vested and which is financed solely by employee contributions). Amounts held in an IRA are subject to an additional 10 percent income tax if distributed before age 59½, death, or disability.

The Senate amendment allows a deduction to an active participant in a private qualified pension plan, a group retirement trust, or an IRA of the lesser of 10 percent of earned income or $1,000. No more than $100 is allowed as a deduction for mandatory contributions to a pension plan. Employers would be required to accept employee contributions to a plan. The deductible employee contributions could not discriminate in favor of officer, shareholders, or highly compensated employees. Deductible employee contributions would be tested for discrimination as if they were employer contributions. The Senate amendment applies for taxable year beginning after December 31, 1978.

Conference agreement.—The Conference agreement omits this provision.

19. Simplified pension plan

House bill.—No provision.

Senate amendment.—Under present law, the requirements that must be met by a qualified pension plan are considerably more complex and burdensome than the requirements applicable to individual retirement accounts or individual retirement annuities.

The Senate amendment raises the usual deduction limit for contributions to an individual retirement account or annuity to $7,500 or 15 percent of compensation, whichever is less, if the account or annuity qualifies as a simplified employee pension. The $7,500 limit applies only with respect to employer contributions to an individual retirement account or annuity maintained by an employee and only if the employer contributions are made under a written allocation formula which is not discriminatory in favor of employees who are officers, shareholders, self-employed, or highly compensated. Also, each employee who has attained age 25 and has performed service for the employer for the current calendar year and at least 3 of the 5 preceding calendar years must be entitled to employer contributions. The conferees do not intend the $7,500 limitation as a precedent for establishing reduced limitations on contributions under qualified plans of small businesses employers or other employers.

An amount contributed to a simplified employee pension by an employer would be fully nonforfeitable (vested), and would be subject to the usual rules for individual retirements accounts or annuities. Also, an employee's right to withdraw amounts held in the account or annuity cannot be restricted by the employer. Reporting and disclosure requirements would be reduced.

If the employer contribution is a simplified employee pension is less than the amount the employee could deduct for a contribution under the usual IRA rules, the employee could make up the difference.

Employer contributions to simplified employee pensions could be taken into account in determining whether an employer's pension plan meets the nondiscrimination requirements for tax qualification. The Senate amendment applies for taxable years beginning after December 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment.

20. Defined benefit plan limits

House bill.—No provision.

Senate amendment.—Under present law, benefits under a qualified defined pension plan are limited to the lesser of 100 percent of pay or $75,000 per year, adjusted for inflation since 1974 ($90,150 for 1978).

The Senate amendment provides that the 100-percent-of-pay limit is disregarded in the case of an employee under a collectively bargained plan with at least 100 participants where (1) benefits for a particular of an employee's service are the same for all participants regardless of the participant's other compensation, (2) benefits are fully nonforfeitable after not more than 4 years of service, (3) employees participate in the plan after not more than 60 days of service, and (4) the employee is not a participant in any other plan of a sponsoring employer. The $75,000 limit on annual benefits is reduced to $37,500 (adjusted for inflation) for an employee if the 100-percent-of-pay limit is disregarded. The Senate amendment applies for years beginning after December 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment.

21. Custodial accounts for regulated investment companies

House bill.—No provision.

Senate amendment.—Under present law, amounts paid by a tax-exempt charitable organization or an educational institution to purchase an annuity contract or stock in a regulated investment company (a mutual fund or a closed-end investment company) for an employee can be excluded from the employee's income under the tax-sheltered annuity rules. To qualify under the tax-sheltered annuity rules, an annuity contract or stock must be purchased to provide a retirement benefit. Because State law generally requires that the cash value of an annuity contract must be payable in the event the contract is surrendered before annuity payments begin, employees are able to use annuity contracts to save for purposes other than retirement. However, under proposed Treasury regulations stock of a regulated investment company cannot be distributed before the employee attains age 65 unless the employee dies or becomes disabled and can be distributed on account of a separation from service only if the employee has attained age 55.

The Senate amendment permits distributions of stock of a regulated investment company after an employee dies, becomes disabled, separates from service, attains age 59½, or encounters financial hardship. Under the "finanical hardship" rule, stock in a regulated investment company could be distributed to an employee if the hardship is such that it would permit a distribution from a qualified profit-sharing plan which provides for distributions in the event of financial hardship. In some cases the "financial hardship" rule for stock would permit distributions to an employee for the purpose of purchasing a residence or to provide higher education for the employee's children. The Senate amendment applies for taxable years beginning after December 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment. The conferees are concerned, however that if a financial hardship standard is applied under tax-favored retirement arrangements, the Congressional purpose for providing favorable tax treatment can be frustrated. Accordingly, the conferees believe that consideration should be given to provisions which withdraw the favorable tax treatment where funds are distributed for purposes other than retirement, to an employee who has not become disabled or died.

22. Pension plan reserves

House bill.—No provision.

Senate amendment.—Present law provides that the income of a life insurance company from its reserves for annuity contracts sold a qualified pension plan, or sold for use as individual retirement annuities or tax-sheltered annuities is subject to more favorable tax treatment than income from reserves for other annuity contracts.

Under the Senate amendment, income of a life insurance company from reserves for an annuity contract sold to a governmental pension plan (whether or not qualified) or to a government for use under an unfunded plan of deferred compensation plan would be accorded the same tax treatment as income from its reserves for annuities sold to a qualified plan. The Senate amendment applies for taxable years beginning after December 31, 1979.

Conference agreement.—The conference agreement follows the Senate amendment.

23. Rollover of distribution from a tax-sheltered annuity

House bill.—No provision.

Senate amendment.—Under present law, the recipient of a "lump-sum distribution" from a tax-qualified pension, profit-sharing, stock bonus, or annuity plan may defer tax on the receipt of such distribution by rolling over the proceeds (net of any employee contributions) within 60 days of receipt to an individual retirement arrangement or to another employer-sponsored qualified retirement plan. In lieu of rolling over the distribution to an individual retirement arrangement, the recipient of a lump-sum distribution (other than a lump-sum distribution caused by plan termination) may elect to compute his tax on the distribution by using special 10-year income averaging.

Recipients of distributions under a tax-sheltered annuity purchased by an employer that is a tax-exempt organization or a public school are taxed under the usual annuity rules (section 72). They are not eligible for special 10-year averaging, and they are not eligible to roll distributions over to an individual retirement arrangement or to another tax-sheltered annuity.

The Senate amendment permits recipients of a "lump-sum distribution" from a tax-sheltered annuity to defer tax on the distribution by rolling it over within 60 days of receipt to an individual retirement arrangement or to another tax-sheltered annuity. This provision will apply to distributions or transfers made after December 31, 1977, in taxable years beginning after that date.

Conference agreement.—The conference agreement follows the Senate amendment but makes technical changes to coordinate the Senate amendment with the technical changes to the individual retirement account provisions made by another provision of the bill. Thus, under the conference agreement, the recipient of a lump-sum distribution from an annuity contract described in section 403(b)(1) or a custodial account which meets the requirements of section 403(b)(7) will be eligible to completely or partially roll over the otherwise taxable portion of such distribution to an individual retirement plan. Subsequently, the amount rolled over to the individual retirement plan plus earnings, could be rolled over to another annuity contract or custodial account, but could not be rolled into a tax-qualified retirement plan.

F. Unemployment Compensation

24. Taxation of unemployment compensation

House bill.—Under present law, based upon a series of Internal Revenue Service rulings, unemployment compensation is excluded from adjusted gross income.

The House bill phases out the current exclusion from adjusted gross income for unemployment compensation paid pursuant to government programs at higher levels of income. The amount of unemployment compensation excluded would be reduced by one-half of the excess of gross income (including unemployment compensation) over $20,000 for single taxpayers, over $25,000 for married taxpayers filing jointly, and over zero for married taxpayers filing separately.

Senate amendment.—No provision.

Conference agreement.—The conference agreement follows the House bill, with a technical amendment providing that any person who makes unemployment compensation payments, pursuant to a government program, to any individual during any calendar year will be required to provide the Secretary of the Treasury with a return setting forth the amount of such payments and the name and address of the individual to whom paid. Any individual who has received such payments also must be furnished with a written statement setting forth the name and address of the person who made the unemployment compensation payments and the total amount of such payments.

G. Other Individual Income Tax Provisions

25. Uniformed services health professions scholarship programs

House bill.—No provision.

Senate amendments.—Under present law, participants in the Uniformed Services Health Professions Scholarship Program (including the Armed Forces and Public Health Services programs) entering before 1979 may exclude from their income amounts received under these programs through 1982.

The Senate amendment extends the exclusion for 1 year to cover scholarships received by students entering these programs in 1979 and to apply for amounts received by such students under these programs through 1983. This provision is effective with respect to students entering programs in 1979, and applies for amounts received through 1983.

Conference agreement.—The conference agreement follows the Senate amendment.

26. National research service awards

House bill.—No provision.

Senate amendments.—Certain amounts received in connection with education may be excluded from income as scholarship or fellowships. In Rev. Rul 77–319, the Service ruled that amounts received as National Research Services Awards under the Public Health Services Awards under the Public Health Service Act of 1974 (42 U.S.C. section 2891), which have no specific statutory exemption, are not excludible scholarships or fellowship grants.

The Senate amendment provides tax-exempt scholarship treatment for National Research Services Awards made through 1979. The exemption applies to amounts received under awards made during calendar years 1974 through 1979.

Conference agreement.—The conference agreement follows the Senate amendment.

27. Cancellation of certain student loans

House bill.—No provision.

Senate amendment.—The Tax Reform Act of 1976 provided that no amount is to be included in gross income by reason of the discharge of all or part of a student loan if, pursuant to the loan agreement, such discharge is made if the individual works for a certain period of time in certain geographical areas, or for certain classes of employers. This exclusion applies only to loans made by a governmental agency and is effective for discharge of such indebtedness if made before January 1, 1979.

The Senate amendment extends the exclusion provided in present law to the discharge of such student loan indebtedness made before January 1, 1983. The amendment applies with respect to loans forgiven prior to January 1, 1983.

Conference agreement.—The conference agreement follows the Senate amendment.

28. Employer educational assistance programs

House bill.—No provision.

Senate amendment.—Under present law, employer-provided educational assistance is includible in an employee's income and is subject to tax unless the education is "job-related." Educational expenditures generally are deductible if they are for education that (1) maintains or improves skill required by the individual's employment or other trade or business, or (2) meets the express requirements of the individual's employer or the requirements of applicable law or regulations imposed as a condition to the retention of an established employment relationship, status or rate of compensation.

The Senate amendment excludes from an employee's income educational assistance provided by an employer under a qualified program. Excludible "educational assistance" includes tuition, fees, books, course supplies and similar items, but does not include personal living expenses nor any benefits for instruction involving sports, games, or hobbies.

A qualified program must be—

(1) a separate written plan of an employer;

(2) for the exclusive benefit of his employees; and

(3) nondiscriminatory with respect to eligibility and participation.

No more than 5 percent of an employer's annual costs for a program may benefit officers, highly compensated individuals, or owners of more than 5 percent of the employer's stock capital, or profits interests. Employees may not elect taxable compensation in lieu of educational assistance. No deduction or credit can be claimed with respect to any amount excluded under this provision.

Excludible assistance also is exempt from employment taxes.

This provision applies to taxable years beginning after December 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment except that the provision is temporary. The exclusion applies to taxable years beginning after December 31, 1978, and ending before January 1, 1984.

29. Tax counseling for the elderly

House bill.—No provision.

Senate amendment.—Present law contains no provision specifically authorizing tax counseling for the elderly. However, the Internal Revenue Service has established a Volunteer Income Tax Assistance Program, which is designed specifically to provide assistance to low-income taxpayers and others.

The Senate amendment authorizes the Secretary of the Treasury, through the Internal Revenue Service, to enter into training and technical assistance agreements with private or public non-profit agencies and organizations to prepare volunteers to provide tax counseling assistance for elderly individuals in the preparation of their Federal income tax returns. Under the amendment, an "elderly individual" is defined as a person who has attained the age of 60.

The amendment authorizes the Service to provide reimbursement to volunteers for transportation, meals, and other expenses incurred

by the volunteers during the course of trainiug or in providing counseling assistance. The amendment also authorizes the appropriation of $2.5 million for fiscal year 1979, and $3.5 million for fiscal year 1980 to implement this provision, This provision is to be effective from the date of enactment.

Conference agreement.—The conference agreement adopts the Senate amendment.

30. Study by the Treasury Department of simplifying the filing of Federal income tax returns

House bill.—No provision.

Senate amendment.—The Senate amendment requires the Treasury Department to study methods by which the process of filing Federal income tax returns could be made simpler and requires the Secretary of the Treasury to submit to the Senate Finance Committee and the House Ways and Means Committee a final report of its study, together with its recommendations, no later than six months from the date of enactment of this Act.

Conference agreement.—The conference agreement follows the Senate amendment.

II. Tax Shelter and Partnership Provisions

31. Modifications of at risk provisions

House bill.—Present law contains two "at risk" rules which are designed to prevent a taxpayer from deducting losses in excess of his actual economic investment in the activity involved. The specific at risk rule applies to four specified activities: (1) farming; (2) exploring for, or exploiting, oil and natural gas resources; (3) holding, producing, or distributing motion picture films or video tapes; and (4) leasing of personal property. The specific at risk rule applies to all types of taxpayers other than regular corporations (that is, corporations which are not subchapter S corporations or personal holding companies). Losses which may not be deducted for any taxable year because of the specific at risk rule are deferred and may be deducted in any subsequent year in which this at risk limitation does not prevent the deduction. The partnership at risk rule applies generally to activities engaged in through partnerships. This rule provides that, for purposes of the limitation on allowance of partnership losses, the adjusted basis of a partner's interest does not include any portion of any partnership liability with respect to which the partner has no personal liability. However, the rule does not apply (1) to any activity to the extent that the specific at risk rule applies, or (2) to any partnership the principal activity of which is investing in real property (other than mineral property).

The House bill extends the specific at risk rule to all activities except real estate and repeals the partnership at risk rule. Separate rules for aggregation and separation of activities are provided for the activities to which the at risk rule is extended. The House bill also extends the at risk rule to all corporations in which five or fewer individuals own more than 50 percent of the stock and requires the recapture of previously allowed losses when the at risk amount is reduced below zero. However, the amount recaptured is limited to the excess of the losses previously allowed in that activity over any amounts previously recaptured. The provision applies to taxable years beginning after December 31, 1978.

Senate amendment.—No provision.

Conference agreement.—The conference agreement follows the House bill, with certain modifications.

First, the at risk rule is not to apply to closely held corporations (i.e., where five or fewer individuals own 50 percent or more of the stock of the corporation) to the extent they are actively engaged in leasing equipment which is section 1245 property. A closely held corporation will not be considered to be actively engaged in equipment leasing unless 50 percent or more of its gross receipts for the taxable year are attributable to equipment leasing. For purposes of this test, gross receipts are to include gross receipts from the sale or the servicing of the same type of equipment leased by the corporation.[1]

[1] For example, the gross receipts from the sale of computers would be included if the corporation also leased computers, notwithstanding that the computers involved had different functional capacities. The gross receipts from the sale and lease of office equipment would be combined for purposes of this test, as would the gross receipts from the sale and lease of automobiles.

"Equipment leasing" includes the leasing of such tangible personal property as computers,[2] copiers, calculators, airplanes, automobiles, tractors, cranes, railroad cars, and furniture. "Equipment leasing" does not include the leasing of master recordings and other similar contractual arrangements made with respect to tangible or intangible assets associated with literary, artistic, or musical properties (such as books, lithographs of works of art, or musical tapes). Equipment leasing would also not include any lease activity which is described in section 465(c)(1) (A), (B), or (D) (relating to motion picture films or video tapes, farming, and oil and gas property). Thus, for example, the lease of a video tape (which is described in section 465(c)(1)(A)) would not be considered equipment leasing.

Losses attributable to an equipment leasing activity which were suspended as a result of the application of the at risk rule, are to become fully deductible for the first taxable year in which the corporation meets the 50 percent or more gross receipts requirement. For the first taxable year in which a corporation fails to meet the 50 percent or more gross receipts requirement, the at risk basis in the equipment leasing activity is to be computed in accordance with the rules (including transitional rules[3]) normally applicable to computing at risk basis for the first year that an activity is subject to the at risk rule.

Second, in determing whether 5 or fewer individuals own 50 percent or more of the stock or a corporation (thus, making the corporation subject to the at risk rule), the attribution rules of section 318, not section 544, are to apply.

Third, the at risk rule is not to apply to partnership liabilities which were not subject to section 704(d) (as in effect before the date of the enactment of this Act) by reason of section 213(f)(2) of the Tax Reform Act of 1976 (P.L. 94–455).

Fourth, with respect to leasing activities conducted by a closely held corporation which are subject to the at risk rule, the at risk rule will not apply to any type of leasing transaction where the property was either leased or ordered (by the lessor or lessee) before November 1, 1978, but only for those taxpayers who owned their interests in the property on October 31, 1978. For purposes of these transitional rules, an order, a lease, and the acquisition of an interest in the property will not be considered to have occured until they are evidenced by binding and legally enforceable agreements which are complete as to all relevant terms. However, a lease agreement will be considered binding on the relevant dates under the above provisions even though it is later modified to increase (but not decrease) the lease term.

Fifth, the loss recapture provision is to apply only to losses which were allowed and reduced the taxpayer's at risk basis in the activity involved for taxable years beginning after December 31, 1978.

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[2] For the purposes of this provision, computer software is to be considered equipment.

[3] Thus, amounts paid or incurred with respect to the equipment leasing activity for taxable years beginning prior to the year of disqualification, and deducted in such taxable years, will, generally be treated as reducing first that portion of the taxpayer's basis which is attributable to amounts not at risk. On the other hand, withdrawals made in taxable years beginning before the year of disqualification will be treated as reducing the amount which the taxpayer is at risk.

32a. Penalty for failure to file return

House bill.—The House bill imposes a penalty on partnerships for failure to timely file a complete partnership information return. The penalty is $50 per month (or fraction of a month) that the return is late or incomplete, multiplied by the number of partners in the partnership. The penalty is assessed agianst the partnership, and the partners are individually liable to the extent they are liable for partnership debts generally. The penalty will not be imposed if the partnership can show reasonable cause for failure to file a complete or timely return. Smaller partnerships (those with 10 or fewer partners) will not be subject to the penalty under this reasonable cause test so long as each partner fully reports his share of the income, deductions and credits of the partnership. The House bill is effective for partnership returns due for taxable years beginning after December 31, 1978.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement follows the House bill and the Senate amendment.

32.b. Extension of statute of limitations for partnership items

House bill.—Under present law, the Internal Revenue Service may assess an additional tax, or a taxpayer may claim a refund, generally within 3 years from the date the tax return is filed. Items of partnership income, deduction and credit are treated the same under these rules as other items on a taxpayer return. This period of limitations begins to run on the due date (or date filed, if later) of the partner's own income tax return. The due date of the partnership information return does not affect the statutory period. In order to extend the period of limitations, the Service must obtain the consent of the individual taxpayer involved. The consent to extend generally relates to all items on the taxpayer's return.

The House bill extends generally to 4 years the period of time in which assessments of deficiencies and claims for refund of tax attributable to partnership items may be made. This rule applies only to partnership items attributable to a "federally registered partnership." A federally registered partnership means any partnership the interests in which have been offered for sale prior to the close of the taxable year in an offering required to be registered with the Securities and Exchange Commission, or any partnership that is or has been subject to the annual reporting requirements of the Security and Exchange Commission.

The 4-year period of limitations under the House bill begins to run on the due date (or date filed, if later) of the partnership information return for the federally registered partnership in which the item arose. However, this special period of limitations does not expire in any event until at least 1 year after the partner's name and address is provided to the Service in the manner prescribed by regulations.

This special period of limitations may be extended as to all partners by any general partner of the partnership or by any other person authorized to do so by the partnership in writing.

This provision is effective for partnership items arising in partnership taxable years beginning after December 31, 1978.

Senate amendment.—No provision.

Conference agreement.—The conference agreement follows the House bill, with a minor change. The conferees intend that only the annual reporting requirements of the SEC relating to protection of investors in the partnership will cause the partnership to be a federally registered partnership. For example, the reports required to be filed with the SEC by a brokerage firm (organized as a partnership) for regulatory purposes do not make the brokerage firm a federally registered partnership under this provision.

III. GENERAL STOCK OWNERSHIP PLANS

33. General stock ownership corporations

House bill.—No provision.

Senate amendment.—Under present law, there are no special provisions relating to the establishment of a private corporation for the benefit of the residents of a State. The Senate amendment authorizes a State to establish a General Stock Ownership Corporation ("GSOC") for the benefit of its citizens. In order to qualify for the special treatment accorded GSOC's, its charter must meet certain statutory provisions and make an irrevocable election. If a GSOC meets these requirements, it is not subject to Federal income tax. Instead, the shareholders of the GSOC are taxable on their daily pro rate share of the GSOP's taxable income. The GSOC computes its taxable income in the same manner as a regular corporation; but is not eligible for the dividends received deduction, Also, the GSOC's losses do not flow through to its shareholders. However, such losses are allowed as a 10-year net operating loss carryforward.

The GSOC is also required to distribute to its shareholders 90 percent of its taxable income. Such distributions are tax-free when received by the GSOC shareholders to the extent they have been previously taxed to them. The GSOC is required to withhold 30 percent of every shareholder distribution which has been made from such previously taxed income.

Conference agreement.—The conference agreement follows the Senate amendment.

IV. BUSINESS TAX REDUCTIONS AND EXTENSIONS

A. Corporate Rate Reductions

34. Corporate rate reductions

House bill.—Under present law, corporate income is subject to a normal tax of 20 percent on the first $25,000 of taxable income and 22 percent on taxable income in excess of $25,000. In addition, a surtax of 26 percent is imposed on corporate taxable income in excess of $50,000. For taxable years ending after December 31, 1978, the normal tax will be 22 percent on all corporate income and the surtax will be 26 percent on taxable income in excess of $25,000. The House bill replaces the present normal tax and surtax with the following rate schedule:

Taxable income:	*Percent*
$0 to $25,000	17
$25,000 to $50,000	20
$50,000 to $75,000	30
$75,000 to $100,000	40
Over $100,000	46

The rates would be effective for taxable years beginning after December 31, 1978.

Senate amendment.—The Senate amendment is the same as the House bill except the top rate would be reduced to 45 percent in 1980, and to 44 percent beginning in 1981.

Conference agreement.—The conference agreement follows the House bill.

B. Investment Tax Credit Provisions

35. Permanent extension of 10-percent rate and $100,000 used property limitation for investment credit

House bill.—Present law provides a permanent investment credit of 7 percent (4 percent for certain utility property) for qualified investment. This rate was temporarily increased to 10 percent for all taxpayers in 1975. The annual limitation on used property was also temporarily increased from $50,000 to $100,000 in 1975. These temporary increases are scheduled to expire in 1981.

The House bill makes permanent the 10-percent investment credit rate and the $100,000 used property limitation.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement follows the House bill and Senate amendment.

36. Increase in tax liability limitation for investment credit

House bill.—Under present law, taxpayers generally may use investment credits to apply against the first $25,000 of tax liability, plus 50 percent of tax liability in excess of $25,000. Special temporary increases in the 50 percent limitation are presently provided for taxpayers with utility property, airline property and railroad property.

The House bill increases the 50-percent limitation to 90 percent, to be phased-in at 10 additional percentage points per year beginning with taxable years which end in 1979. The limitation will reach the permanent 90-percent level beginning with taxable years which end in 1982.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement follows the House bill and Senate amendment.

37. Increased investment credit for pollution control facilities

House bill.—Under present law, the investment credit is allowed for only one-half of a taxpayer's investment in a pollution control facility where the taxpayer has elected 5-year amortization for the facility.

The House bill generally allows the credit for the full investment in a pollution control facility where 5-year amortization has been elected. However, where the facility has also been financed by tax-exempt industrial development bonds, the credit is available for only one-half of the investment to the extent it is subject to 5-year amortization. These provisions would be effective after December 31, 1978.

Senate amendment.—Same as the House bill, except the Senate amendment eliminates the limitation of one-half of the credit where a facility is both amortized and financed with industrial development bonds.

Conference agreement.—The conference agreement follows the House bill.

38. Investment credit for rehabilitation expenditures for certain structures

House bill.—Under present law, buildings and their structural components are not eligible for the investment credit, nor are expenditures for rehabilitating or renovating existing structures.

The House bill extends the investment credit to rehabilitation expenditures for all types of business and productive buildings, except those, such as apartments, which are used for residential purposes. Eligible buildings include factories, warehouses, hotels, and retail and wholesale stores. Qualifying expenditures are depreciable rehabilitation costs incurred after July 26, 1978, in connection with a building which has been in use for at least five years, for the interior or exterior renovation, restoration or reconstruction of the building. Costs for acquiring or completing a building, or for the replacement or enlargement of a building, are excluded. If more than 25 percent of the exterior walls are replaced, the costs will not qualify. The costs must have useful lives of at least five years and the credit will be determined using the present limitations applicable to useful lives. In addition, the costs must be incurred at least five years after the last prior qualifying rehabilitation (if any) was completed. The credit is not available where 5-year amortization has been elected for rehabilitation costs on a certified historic structure. This provision is effective for qualifying expenditures incurred after July 26, 1978.

Senate amendment.—The Senate amendment is the same as the House bill except that the expenditures must be incurred after September 1, 1979, and the building must have been in use for at least 20 years before rehabilitation costs will qualify for the investment credit. In addition, the costs must be incurred at least 20 years after the last qualifying rehabilitation was completed. The Senate amendment will apply to qualifying expenditures incurred after September 1, 1979.

Conference agreement.—The conference agreement modifies and follows the House bill. Under the conference agreement, a building must have been in use for at least 20 years, and the costs must be incurred at least 20 years after the last rehabilitation was completed, in order to qualify for the credit. In addition, under the conference agreement, rehabilitation expenditures in connection with a certified historic structure must themselves be certified as appropriate by the Secretary of the Interior in order to qualify for the investment credit in those situations where the taxpayer elects to claim the credit rather than 5-year amortization. These provisions will be effective for qualifying expenditures incurred after October 31, 1978.

39. Investment credit for single purpose agricultural structures

House bill.—No provision.

Senate amendment.—Under present law, buildings and their structural components are not eligible for the investment credit. However, certain tangible property (which may be categorized as buildings under local law) is eligible for the credit if used for productive purposes, including farming. The Internal Revenue Service has disallowed the credit for certain special purpose poultry, hog and greenhouse structures which are specifically designed and constructed for the purpose for which they are used. Generally, the tests applied by the Service are whether the structure is so integrally related to the equipment

that it will be abandoned or destroyed when the equipment is worn out and whether the structure provides regular working space for employees. Taxpayers have successfully litigated this issue in some cases.

The Senate amendment makes specifically eligible for the investment credit those structures, including poultry and livestock structures and greenhouses, which are specifically designed, constructed and used for single purpose food and plant production. The amendment clarifies how the law was intended to be interpreted when the credit was restored on August 15, 1971, and applies to taxable years ending after that date.

Conference agreement.—The conference agreement modifies the Senate amendment to specifically extend the investment credit to special purpose structures used for livestock and horticultural products and to adopt the general conditions and requirements of H.R. 12846, as passed by the House of Representatives on October 13, 1978.

In order to be included under this provision, a livestock structure must be specifically designed, constructed, and used for the housing, raising and feeding of livestock and their produce. The term "livestock" for this purpose includes poultry. The full range of livestock breeding, raising and production activities is intended to be included so that special purpose structures will qualify for credit if used, for example, to breed chickens or hogs to produce milk from dairy cattle, or to produce feeder cattle or pigs, broiler chickens, or eggs. In addition, the structure or enclosure must be designed and used to house equipment necessary to feed and care for the livestock. As a result, such facilities must include, as an integral part of the structure or enclosure, equipment to contain the livestock and to provide water, feed and temperature control, if necessary.

Similarly a horticultural structure is made specifically eligible for the credit under this provision if it has been designed, constructed, and used for the commercial production of plants, including mushrooms.

The issues which have arisen concerning allowance of the credit under present law are also resolved by providing that the life of the structure need not be contemporaneous with the equipment it houses. In addition, working space is permitted within an eligible structure. Under this latter rule, the property will be eligible for the credit even if working space is provided for caring for the livestock or plants or for gathering their produce (such as eggs, tomatoes or flowers). In addition, working space may be provided to maintain the structure and to maintain or replace the equipment within the structure.

It should be emphasized that the structure must be used exclusively for the purpose for which it was specifically designed and constructed. As a result of this requirement, a hog structure will not be eligible property, for example, if it is used for the housing and feeding of poultry or cattle or if more than incidental use of a structure is made to store feed or machinery. (However, mere vacancy of the facility will not violate this usage test.) Similarly, the use of part of a greenhouse for the purpose of selling plants or their produce, such as by

installation of a check-out stand, will make the greenhouse ineligible for the credit. If a single purpose structure becomes ineligible because of this usage test within seven years from the time it was placed in service, investment credits claimed on the structure may be partially or entirely recaptured under the investment credit recapture rules in present law. In addition, the conferees wish to emphasize that the specific provisions concerning the eligibility of these structures for the investment credit are not to create a negative inference regarding the eligibility of other special purpose agricultural and productive structures for the credit under existing law.

40. Investment credit for cooperatives

House bill.—No provision.

Senate amendment.—Under present law, cooperatives are generally taxed like corporations, but are allowed to deduct certain payments made to patrons and shareholders. The amount of investment credit available for cooperatives is reduced proportionate to the reduction in taxable income because of the special deductions. These otherwise allowable credits expire and are not passed through to the patrons or shareholders.

The Senate amendment allows taxable cooperatives (those defined in Code section 1381(a)) the full investment credit for taxable years ending after December 31, 1978. The credit is not reduced proportionate to the reduction in taxable income because of deductions for payments made to patrons and shareholders. In addition, these cooperatives are allowed an irrevocable annual election to apportion all or part of the credit they have earned each taxable year to their patrons proportionate to patronage business done with the patron during the year.

Conference agreement.—Under the conference agreement, the special limitations on the use of the investment credit by cooperatives are eliminated. Cooperatives will be permitted to use the investment credit in the year property is placed in service to the same extent as corporations generally. To the extent a cooperative cannot use an investment credit in the current year, the credit will not be carried back or carried forward but will be allocated to the patrons of the cooperative. Any recapture of investment credits including credits allocated to patrons, will be effected at the level of the cooperative. These rules will apply for taxable years ending after October 31, 1978. The Secretary is authorized to promulgate regulations to effect the purposes of this section. For this purpose, it is anticipated that the allocation of the credit to patrons will be on a basis similar to that used for patronage dividends under section 1388(a)(1). The rules will provide for the treatment of carryovers of investment credits from years prior to the effective date of this provision which are not to be allocated to patrons of the cooperative.

41. Investment credit for horses

House bill.—No provision.

Senate amendment.—Under present law, livestock is specifically eligible for the investment credit if it otherwise qualifies as eligible property. Horses, however, are not considered livestock for this purpose and, as a result, are not eligible for the credit.

The Senate amendment extends the investment credit to horses used for working or breeding purposes. Horses used for sporting purposes (such as race or show horses) would not be eligible for the credit. These provisions would apply to horses which become qualifying property after December 31, 1978.

Conference agreement.—The conference agreement omits the Senate amendment.

42. Additional carryover year for investment credits expiring in 1977

House bill.—No provision.

Senate amendment.—Under present law, the investment tax credit for any year generally cannot exceed the first $25,000 of tax liability plus 50 percent of the tax liability in excess of $25,000. If the amount of investment tax credit for any year exceeds the applicable limitation based on the amount of tax liability for that year, the excess is generally an investment credit carryback to each of the 3 preceding taxable years and an investment credit carryover to each of the seven following taxable years and, subject to certain limitations, is included in the amount allowable as a credit for those years (sec. 46(b)). However, pre-1971 investment credits are allowed a 10-year carryover. Carryover credits from prior taxable years—beginning with the earliest eligible preceding year—are to be used first in the current year before any credits arising in the current year—or any carryback from future years. If any portion of a credit remains unused after application of the carryback and carryover periods, the unused portion expires and cannot be used subsequently by the taxpayer.

Under the Senate amendment, one additional carryover year is allowed for investment credits which could be carried to a taxable year ending in 1977, but which expire unused after that taxable year.

Conference agreement.—The conference agreement omits the Senate amendment.

43. Investment credit for manufacturer-lessors of railroad property

House bill.—No provision.

Senate amendment.—Under present law, special tax liability limitations apply with respect to the investment tax credit for railroads. Taxpayers with railroad property are allowed, under provisions enacted in the Tax Reform Act of 1976, to take credits up to 100 percent of tax liability for 1977 and 1978 with annual reductions of 10 percentage points thereafter until the limitition returns to 50 percent of tax liability in excess of $25,000 in 1983. Only the operator of a railroad, and not a lessor of railroad property, is eligible for the special increased limitation.

The Senate amendment provides that the tax liability limitation applicable to taxpayers with railroad property would also apply to investment tax credits applicable to railroad rolling stock placed in service by a taxpayer who manufactured the rolling stock and leases it out to others. Manufacturer-lessors would be eligible for the increase to the same extent as operators of railroads.

Conference agreement.—The conference agreement omits this provision.

44. Investment credit recapture under the ConRail reorganization

House bill.—No provision.

Senate amendment.—Present law includes provisions which deal with the tax consequences of the April 1, 1976, ConRail reorganization under which the railroad properties of eleven bankrupt railroads were transferred to ConRail for ConRail stock and certain "certificates of value." The rules applicable to this special reorganization provide that the transfer of rail properties to ConRail is treated like reorganizations in general (and other bankrupt railroad reorganizations in particular) so that the transferor companies and their shareholders and security holders do not recognize gain or loss on the transfer and ConRail receives a carryover basis in the properties it acquired. However, these rules do not deal with investment credit recapture which may arise to the transferor railroads because of the ConRail reorganization. In contrast, present law generally provides an exemption from investment credit recapture where assets are transferred in a tax-free reorganization.

The Senate amendment adds an exception to the investment credit recapture rules so that a transferor railroad will not be subject to additional tax on its transfer of rail properties to ConRail. This amendment applies to taxable years ending after March 31, 1976.

Conference agreement.—The conference agreement follows the Senate amendment. The conferees intend that investment credits which are not subject to recapture because of this provision shall be treated as "other benefits" to the same extent that any other tax benefits are so treated for purposes of the special court's determination of compensation to the transferor railroads under sections 303 and 306 of the Regional Rail Reorganization Act of 1973.

C. Jobs Tax Credit and WIN Tax Credit

45. Targeted jobs credit

House bill.—Present law contains a general jobs credit, due to expire at the end of 1978, equal to 50 percent of the increase in each employer's FUTA base above 102 percent of that wage base in the previous year. This amount is subjcet to certain limitations. The present law jobs credit also contains an additional credit equal to 10 percent of the first $4,200 of FUTA wages paid to handicapped individuals who receive vocational rehabilitation.

Under the House bill, a permanent tax credit of 50 percent of the first $6,000 of wages per employee for the first year of employment and 16⅔ percent of such wages for the second year of employment would be provided for hiring: (1) AFDC recipients who register for the WIN program, (2) recipients of Supplemental Security Income (SSI), (3) handicapped individuals, (4) individuals of ages 18 through 24 who are members of households receiving food stamps, (5) Vietnam veterans who are members of households receiving food stamps, (6) recipients of general assistance for 30 or more days, and (7) individuals of ages 16 through 18 who are participants in a high school or vocational school sponsored or cooperative education program. Wages eligible for the credit would be limited to 30 percent of the total FUTA wages paid by an employer.

The House bill further provides that certification of eligible employees is to be performed by an agency designated by the Secretary of Labor. The amount of the credit would be limited to 100 percent of tax liability, and an employer's deduction for wages would be reduced by the amount of the credit.

The current general jobs tax credit would be allowed to expire at the end of 1978.

The Secretaries of Treasury and Labor would be required to submit a report to Congress by June 30, 1981, on the effectiveness of the general jobs credit in stimulating employment in 1977 and 1978 and of the targeted jobs credit, as provided in the bill, in improving the employment situation of the targeted groups.

Senate amendment.—The Senate amendment provides a tax credit of 50 percent of the first $6,000 of wages per employee for the first year of employment, 33⅓ percent of such wages for the second year of employment, and 25 percent of such wages for the third year of employment. The credit would be provided for hiring: (1) disabled recipients of Supplemental Security Income (SSI), (2) handicapped individuals undergoing vocational rehabilitation, (3) economically disadvantaged youths, (4) Vietnam-era veterans under the age of 35 who are members of economically disadvantaged families, (5) recipients of general assistance for 30 or more days, and (6) convicts who are members of economically disadvantaged families. Wages eligible for the credit would be limited to 20 percent of the total FUTA wages paid by an employer.

Under the Senate amendment, the credit would not be claimed with respect to employees for whom the employers receive on-the-job training payments. In addition, the credit would not be available with respect to employees who work for the employer less than 75 days in the first year of employment.

The Senate amendment further provides that certification of eligible employees is to be performed by one certification agency in each locality jointly designated by the Secretaries of Labor and Treasury. The amount of the credit would be limited to 90 percent of tax liability, and an employer's deduction for wages would be limited by the amount of the credit.

The credit provided by the Senate amendment would be effective for taxible years beginning after December 31, 1978, and before January 1, 1982 generally for employees hired after September 26, 1978.

Conference agreement.—The conference agreement replaces the present law general jobs credit with a targeted jobs credit, equal to 50 percent of the first $6,000 of wages for the first year of employment and 25 percent of such wages for the second year of employment, for hiring: (1) recipients of Supplemental Security Income (SSI), (2) handicapped individuals undergoing vocational rehabilitation, (3) individuals at least 18 but not over age 25, who are members of economically disadvantaged families (defined as families with income during the preceding 6 months which on an annual basis was less than 70 percent of the Bureau of Labor Statistics lower living standard), (4) Vietnam-era veterans under the age of 35 who are members of economically disadvantaged families, (5) recipients of general assistance for 30 or more days, (6) individuals of ages 16 through 18 who are participants in a qualified cooperative education program, and (7) convicts who are members of economically disadvantaged families (if they are hired within 5 years of the later of release from prison or date of conviction).

Under the conference agreement, the credit is not allowed with respect to employees for whom employers receive on-the-job training payments. Certification of eligible employees is to be performed by one certification agency in each location jointly designated by the Secretaries of Labor and Treasury.

Qualified wages of first-year employees is limited to 30 percent of aggregate FUTA wages for all employees. In addition, an employer's deduction for wages is reduced by the amount of the credit, and the credit is limited to 90 percent of tax liability.

The Secretaries of Labor and Treasury are required to submit a report to the Congress by June 30, 1981, on the effectiveness of the general and targeted jobs credit.

The credit will apply to taxable years beginning after December 31, 1978, and before January 1, 1982, generally for employees hired after September 26, 1978.

46. WIN-welfare recipient tax credit

House bill.—Present law provides a 20-percent credit, plus full deduction, for wages paid in the first year of employment to AFDC recipients who receive assistance for at least 90 days or who register for

the WIN program. The amount of credit is limited to $50,000 of tax liability plus one-half ot tax liability in excess of $50,000. Generally, up to $5,000 of wages paid for nonbusiness employment are eligible for the credit.

The House bill terminates the separate WIN-welfare recipient tax credit. However, AFDC recipients who register for the WIN program are an eligible group under the targeted jobs credit provided in the House bill.

Senate amendment.—The Senate amendment modifies the present law WIN-welfare recipient tax credit so that employers who hire AFDC recipients who register for the WIN program, or who receive assistance for at least 90 days, are entitled to a credit equal to 75 percent of up to $6,000 of wages for the first year of employment, 65 percent of such wages for the second year of employment, and 55 percent of such wages for the third year of employment. An employer's deduction for wages is reduced by the amount of the credit. The $6,000 wage base of the Senate amendment would be increased to $7,000 for years of employment beginning in 1981 and thereafter.

In addition, the Senate amendment provides that, for employment not in a trade or business, the credit is to be 50 percent of the first $6,000 of wages for the first year of employment ($7,000 for years of employment beginning in 1981 and thereafter). Eligible nonbusiness wages are limited to $12,000 for any employer ($14,000 for 1981 and thereafter).

The Senate amendment would not allow the credit for (1) expenses reimbursed by a grant, (2) employees who work for the employer less than 30 days on a substantially full-time basis, (3) employees who displace other employees from employment, (4) migrant workers, or (5) employees who are close relatives, dependents, or major stockholders of the employer.

The WIN-welfare recipient tax credit would be nonrefundable.

Conference agreement.—The conference agreement generally follows the Senate amendment. Under the conference agreement, employers who hire AFDC recipients who register for the WIN program, or who receive assistance for at least 90 days, are entitled to a credit equal to 50 percent of up to $6,000 of wages for the first year of employment and 25 percent of such wages for the second year of employment. An employer's deduction for wages is reduced by the amount of the credit.

For employment not in a trade or business, the credit is 35 percent of the first $6,000 of wages for the first year of employment. Eligible nonbusiness wages are limited to $12,000 for any employer.

No credit would be allowed for: (1) expenses reimbursed by a grant; (2) employees who work for the employer less than 30 days on a substantially full-time basis, (3) employees who displace other employees from employment, (4) migrant workers, or (5) employees who are close relatives, dependents, or major stockholders of the employer.

The WIN-Welfare recipient tax credit is limited to 100 percent of tax liability.

47. Extension of general jobs credit

House bill.—No provision.

Senate bill.—Present law contains a general jobs credit equal to 50 percent of the increase in each employer's wage base under the Federal Unemployment Tax Act (FUTA) above 102 percent of

that wage base in the previous year. The FUTA base for 1977 consisted of wages paid of up to $4,200 per employee. The credit for 1978 uses a similar base. The employer's deduction for wages is reduced by the amount of the credit.

The total amount of the credit has four limitations: (1) the credit cannot be more than 50 percent of the increase in total wages paid by the employer for the year above 105 percent of total wages paid by the employer in the previous year, (2) the base of the credit must be no more than 50 percent of the current year's FUTA wages, (3) the credit for a year cannot exceed $100,000, and (4) the credit cannot exceed the taxpayer's tax liability. Credits which exceed tax liability for a year may be carried back for 3 years and carried forward for 7 years.

Present law also provides an additional nonincremental credit equal to 10 percent of the first $4,200 of FUTA wages paid to handicapped individuals (including handicapped veterans) who receive vocational rehabilitation. The credit for handicapped workers cannot be greater than one-fifth of the regular 50-percent new jobs credit which would have been allowable without regard to the $100,000 limitation. However, the special 10-percent credit is not itself subject to any specific dollar limitation.

The Senate amendment would extend the general jobs credit for two years and would make several changes. The amount of the credit would be equal to 35 percent of up to $6,000 of wages per employee. Unlike the present law general jobs credit, the total amount of the credit would not be limited to a percentage of the increase in an employer's total wages over total wages in the previous year. Further, the credit for an employer would be reduced by the amount of targeted jobs credit allowed that employer.

In addition, the Senate amendment would make the credit elective and extend the credit to employment on American vessels.

Conference agreement.—The conference agreement follows the House bill, except that the credit is made elective for taxable years beginning after December 31, 1976.

D. Industrial Development Bond Provisions

48. Small issues exception to industrial development bond tax treatment

House bill.—Under present law, interest on industrial development bonds is, in general, taxable. However, interest on certain small issues of industrial development bonds is tax-exempt. Small issues are issues of $1 million or less the proceeds of which are used for the acquisition or construction of depreciable property or land. At the election of the issuer, the $1 million limitation can be increased to $5 million. If this election is made, capital expenditures and the total of a series of small issues for a project cannot exceed $5 million.

Under the House bill the $5 million elective limitation is increased to $10 million, and applies only to bonds issued after December 31, 1978.

Senate amendment.—The amendment increases both the $1 million and $5 million limitation to $2 million and $12 million respectively. In addition, the amendment is in general effective for bonds issued after December 31, 1978. It also specifies that the higher limitation is to apply to capital expenditures made after December 31, 1978, with respect to bonds that were issued prior to December 31, 1978. Finally, with respect to bonds issued after December 31, 1978, the $12 million limitation is to apply by taking bonds issued prior to December 31, 1978, into account in determining the amount of bonds that can be issued after December 31, 1978.

Conference agreement.—The conference agreement follows the House bill with the Senate amendment effective date.

49. Advance refunding of industrial development bonds for certain public projects

House bill.—No provision.

Senate amendment.—Under present law, certain industrial development bonds qualify for tax-exemption where substantially all the proceeds of the bonds are used to provide certain "exempt activities" facilities. Such facilities include convention and trade show facilities (sec. 103(b)(4)(C)) airports, docks, wharves, and facilities for mass commuting, parking, or storage and training directly related to those installations (sec. 103(b)(4)(D)).

However, under present law, it is unclear whether a refunding issue of an exempt activity industrial development bond also qualifies for tax-exemption. The Senate amendment provides that a refunding issue of a tax-exempt industrial development bond will qualify for tax-exemption where substantially all the proceeds of the refunded issue were used to provide a qualified public facility. Qualified public facilities are defined as (1) public airports, (2) public docks, or wharves, (3) public mass commuting facilities, (4) public convention or trade show facilities, or (5) public facilities for parking, storage or training that are related to any of the facilities described in (1), (2), or (3).

Moreover, under the amendment a refunding issue of bonds used to provide property functionally related and subordinate to a qualified public facility will not qualify for tax-exemption unless the property itself is generally available to use by the general public. On the other hand, where the bonds for the qualified public facility are redeemed and the bonds for the subordinate facility are also redeemed in a multi-issue redemption, then, in general, the entire refunding issue will qualify for tax-exemption.

The amendment applies to refunding bonds issued after the date of enactment.

Conference agreement.—The conference agreement generally follows the Senate amendment. However, it places a further requirement that a facility will constitute a qualified public facility only if it is generally available for use by the general public. Thus, an advance refunding issue of bonds used to provide facilities such as hangers will not meet the requirements of this provision if the hanger is only available for use by a non-exempt person. In addition, a multi-issue advance refunding issue will not be tax-exempt under the conference agreement unless substantially all the proceeds of the refunded issues (taken as a whole) were used to provide qualified public facilities.

The conference agreement further provides that a substantial user is prohibited from holding any advance refunding issues issued under this provision.

50. Advance refunding of certain other industrial development bonds

House bill.—No provision.

Senate amendment.—Prior to 1968 interest on industrial development bonds was tax-exempt. In 1968 the interest on most industrial development bonds was made taxable. However, a transitional rule provided that interest on industrial development bonds issued prior to May 1, 1968, was to remain tax-exempt.

Prior to November 4, 1977, it was unclear under the then existing proposed Treasury regulations whether a refunding issue with respect to pre-1968 industrial development bonds qualified for tax-exemption where it had the effect of extending the maturity date of the refunded pre-1968 issue.

On November 4, 1977, the Treasury announced that it would propose amendments to the regulation which would substantially restrict current and advance refunding of pre-1968 and post-1968 industrial development bonds. The proposed regulations were published December 6, 1977, and were made effective as of November 4, 1977.

The Senate amendment provides transitional rules for the refunding of pre-1968 industrial development bonds.

The amendment would not apply in a case where the refunding bonds are held by a substantial user of the facility financed by the refunded bonds (or by a related person).

The amendment also provides a general rule with respect to refunding issues of post-1968 industrial development bonds. Under the amendment a bond issue that refunds a previously issued industrial development bond will qualify for tax-exempt status if it satisfies conditions prescribed or proposed to be prescribed by the Secretary of the Treasury prior to the date on which the refunding obligation is

issued. This provision of the amendment applies to any refunding obligation issued to refund any obligation with respect to which paragraph (4), (5), or (6) of section 103(b) of the Code applied.

Conference agreement.—The conference agreement omits the Senate amendment.

51. Income tax exemption for bonds for water facilities

House bill.—No provision.

Senate amendment.—Under present law, an industrial development bond will qualify for tax-exemption where substantially all the proceeds of the bond are used to provide facilities for the furnishing of water if available on reasonable demand to members of the general public. In recent years the Internal Revenue Service has been reluctant to rule that business and commercial users of water constitute members of the general public. In addition, under present law considerable uncertainty exists over whether bonds used to finance a portion of a water facility (such as water lines) qualify for tax-exemption unless the segment to be financed itself serves the general public, not-withstanding that the segment may be part of an overall facility serving the general public.

The amendment provides that an industrial development bond the proceeds of which are used to provide government operated facilities for the furnishing of water to the general public for any purpose will qualify for tax-exemption.

The amendment imposes three requirements which the facility must satisfy in order for the bonds to qualify for tax-exemption. First, the facility must be for the furnishing of water. Thus, a facility cannot be one that uses water in the production process, such as a cooling pond. Second, the facility must be operated by a governmental unit. In general, this requirement will be satisfied if a governmental unit is responsible for maintenance and repair of the facility. Finally, the facility must make or will make water available to members of the general public. For purposes of this provision the general public includes agricultural, industrial, commercial and electric utility users. Under the amendment a facility cannot deny access to water to members of the general public in its service area. However, a portion of the water of a facility may be committed to a limited number of users, provided other members of the general public in the service area (including residential users and municipal water districts) are granted access to a substantial portion of the water.

The amendment applies to obligations issued after the date of enactment.

Conference agreement.—The conference agreement generally follows the Senate amendment with certain technical changes.

The Senate amendment provides tax-exempt status for bonds used to provide facilities for the furnishing of water to the general public only if the facilities are government operated. Under present law, in certain instances, bonds used to provide facilities for furnishing water to the general public which are operated by an investor-owned regulated public water utility may qualify as tax-exempt bonds. The conference agreement provides that facilities operated by investor-owned regulated public utilities are to be granted the same treatment as government operated water facilities.

In addition, the conferees make it clear that in order to satisfy the first requirement of the Senate amendment, that a facility be a facility for the furnishing of water, it must be a component of a system or project which furnishes water. Ordinarily, such a system or project would include only those components necessary for the collection, treatment and distribution of water to a service area, and any other functionally related and subordinate components. For example, a reservoir and its functionally related and subordinate components will constitute a single system. Thus, if a governmental unit operates such a system, an individual water line, canal, or the like for transportation of water from the main system to a single industrial user will constitute a facility for the furnishing of water.

On the other hand, a series of dams will not, in general, constitute a single system, but rather a series of individual systems. In order for any one of these individual systems to qualify under the provision, it must individually satisfy the requirements of the provision.

Further, the fact that an electric utility is a customer of a governmental unit which operates facilities for the furnishing of water does not, in general, transform those water facilities into facilities for the furnishing of electric energy. Thus, a reservoir or dam would not be denied tax-exempt financing merely because one of the uses of the water is for the production of hydroelectricity. Tax exempt financing will be allowed if substantially all of the water is used for other purposes in addition to the production of hydroelectricity. However, in no event will tax-exempt financing be allowed for the hydroelectric facility itself, such as for the generators and turbines, unless the local furnishing test is satisfied.

Finally, a reservoir does not have to provide water to *all* segments of the public to qualify for tax-exempt financing. For example, a reservoir that provides water to residential or industrial users is not ineligible for tax-exempt financing merely because the reservoir does not also furnish water for agricultural or irrigation purposes. In addition, the water does not have to be made available to *all* residential users in the service area.

52. Income tax exemption for bonds for facilities for furnishing electric energy

House bill.—No provision.

Senate amendment.—Under present law, interest earned on obligations of a State or local government generally is exempt from Federal income tax. This rule does not extend to industrial development bonds, the proceeds of which are used by a taxpaying enterprise in its trade or business, except where the proceeds of the bonds are used for specified exempt purposes, and except for certain small issues.

Although the use of facilities for the local furnishing of electric energy is one specified exempt purpose for industrial development bonds (sec. 103(b)(4)(E)), many bond issues for electric energy facilities cannot qualify for the exemption under current Treasury Department regulations (§ 1.103–8(f)(2)(iii)(d)), which interpret the term "local furnishing" to mean, in general, furnishing electric energy to no more than two contiguous counties (or political equivalents). This bars exempt status for bonds issued for facilities serving a larger area.

The amendment provides that industrial development bonds substantially all the proceeds of which are used to provide certain electric energy facilities will qualify for tax-exemption where certain requirements are met. The first requirement is that the energy from the facilities be sold to a regulated public utility having a customer service area with a territory no greater than one city and one contiguous county. Under this requirement the energy from the facility must also be sold within the one city-one county area.

The second requirement provides that with respect to pumped storage, other hydroelectric facilities or electrical transmission facilities construction of which is completed after October 1, 1977, that they be operated by a State agency which was in existence prior to January 1, 1935, whose governing body was appointed by the governor of such state and which was authorized prior to October 1, 1977, to develop such projects.

The amendment also provides tax-exemption for bonds substantially all the proceeds of which were used to provide certain other facilities for the furnishing of electric energy. This provision imposes the one city and one county requirement and also imposes a second requirement that a Federal or State agency license or certification authorizing construction be issued or first applied for prior to October 1, 1977, by a State agency which was in existence prior to January 1, 1935, whose governing body was appointed by the governor of such state and which was authorized prior to October 1, 1977, to develop such projects.

Finally, under the amendment an issuer may elect to have the provisions apply to obligations issued prior to the date of enactment provided that the facility with respect to which the obligations were issued meet the requirements for pumped storage facilities or meet the requirements for other facilities.

Conference agreement.—The conference agreement generally follows the Senate amendment. However, under the conference agreement, the one city and one contiguous county definition of "local furnishing" would apply generally for facilities for the local furnishing of electric energy, without regard to the date of authorization or completion of the facility, and without regard to the histrionics of the agency operating the facility.

The conferees wish to make it clear that their agreement that local furnishing includes a city and a contiguous county provides an exception from the general rule that local furnishing means a service area comprising no more than two contiguous counties (or a political equivalent). Thus, under the conference agreement local furnishing includes an area comprising no more than two contiguous counties, or one city and a contiguous county.

The conference agreement also modifies the effective date of the Senate amendment. Under the conference agreement, the provision applies to taxable years ending after April 30, 1968, but only with respect to obligations issued after that date.

E. Other Tax-Exempt Bond Provisions

53. Declaratory judgments relating to the status of State and local government obligations

House bill.—No Provision.

Senate amendment.—Present law provides that interest on State and local government obligations is, in general, tax-exempt. However, tax-exempt status is denied to arbitrage bonds and certain industrial development bonds. Moreover, in order for an obligation to be tax-exempt it must have been issued by a State or local government or issued by an authority "in behalf of" a State or local government.

As a practical matter, an issuer has no appeal from a Service private letter ruling (or failure to issue a private letter ruling) that a proposed issue of municipal bonds is taxable. In addition, it is impossible for an issuer to question the Service's rulings and regulations directly.

The amendment authorizes the Tax Court, Court of Claims and U.S. district courts to issue declaratory judgments with respect to the tax-exempt status of proposed bond issues. However, relief under the amendment is available only to the proposed bond issuer and only if: (1) the proposed issuer has requested a private letter ruling from the IRS (2) the IRS has acted adversely on the request or has failed to act within 60 days (3) and the proposed issuer has otherwise exhausted all administrative remedies.

The amendment applies to requests for determinations (private ruling requests) filed with the Internal Revenue Service after December 31, 1978.

Conference agreement.—The conference agreement generally follows the Senate amendment. However, the agreement provides that (1) jurisdiction under this provision is to lie exclusively with the United States Tax Court; (2) a proposed issuer will not be deemed to have exhausted its administrative remedies before the expiration of 180 days where a request for a determination has been made and the Service has failed to act; (3) appeal of the decision of the Tax Court will lie exclusively with the United States Court of Appeals for the District of Columbia Circuit; and (4) the Tax Court determination is to be based on any facts or arguments which the Service and/or the proposed issuer wish to introduce at the time of trial.

Further, the conferees wish to make it clear that while it is anticipated the Tax Court will expedite resolution of these cases, such treatment will be at the discretion of the Tax Court so as not to restrict the Court's flexibility in handling the remainder of its already heavy caseload.

54. Treatment of certain arbitrage profits from advance refunding of State and local government obligations

House bill.—No provision.

Senate amendment.—Prior to 1969 State and local governments were able to earn arbitrage profits through investing the proceeds of their tax-exempt bonds in higher yielding Treasury obligations. In 1969

tax-exempt status was denied to State and local government obligations (arbitrage bonds) the proceeds of which are invested in materially higher yielding securities or the proceeds of which are used to replace funds which were used to acquire materially higher yielding obligations.

These yield restrictions which were placed on State and local government obligations created a situation where some State and local governments attempted to divert arbitrage profits to third parties which in some instances were charities.

On September 24, 1976, the Treasury announced regulations which would effect bonds issued after that date. These regulations in general were designed to prevent issuers from diverting arbitrage profits to underwriters and third parties.

The amendment, in general, prohibits the Treasury from applying the position taken by the regulations retroactively to prevent arbitrage profits from being donated to an exempt organization described in section 501(c). In addition, where arbitrage profits were put into escrow pending donation and then were paid over to the Treasury Department because of the Internal Revenue Service rulings policy, the provision directs the Treasury to return the profits so that it can be given within 90 days to the intended beneficiary.

The amendment is effective on the date of enactment.

Conference agreement.—The conference agreement follows the Senate amendment with certain technical modifications.

Under the conference agreement payment of a refund profit in accordance with a qualified agreement shall not cause the refunding obligation (which gave rise to the refund profit) to be treated as an arbitrage bond or cause the issuer to be "blacklisted" if pursuant to the qualified agreement the refund profit is held (1) in a trust fund, (2) in an escrow account, or (3) by an underwriter or other person.

The conference agreement further provides that in certain instances in which a State or local government accounts to the United States for the refund profit by direct payment or by purchase of low-interest United States obligations, that the Treasury shall repay such accounted for refund profits to the designated charitable organizations. The repayment shall be paid out of unappropriated Treasury funds. In addition, only charitable organizations described in sec. 501(c)(3) other than an organization described in sec. 509(a) shall be eligible to receive such refund profits.

Repayment by the Treasury shall be required under the conference agreement only if on or before January 1, 1977, the State or local government which entered into a qualified agreement requested, in writing, a ruling from the Internal Revenue Service on the tax consequences of paying refund profits to charitable organizations and failed to receive a favorable ruling, and did not pay the refund profit to a charitable organization.

F. Small Business Corporations

55. Subchapter S corporations allowed 15 shareholders

House bill.—Under present law, a subchapter S corporation may have 10 shareholders, and after 5 years the number of shareholders may be increased by inheritance to 15. The House bill would allow subchapter S corporations to have 15 shareholders initially.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement is the same as the House bill and the Senate amendment.

56. Permitted shareholder of subchapter S corporations

House bill.—Under present law, a husband and wife owning stock jointly are counted as one shareholder for purposes of determining the number of shareholders of the corporation for purposes of subchapter S eligibility. The House bill counts a husband and wife (and their estates) as one shareholder in all situations for purposes of determining the number of shareholders.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement is the same as the House bill and the Senate amendment.

57. Time for making a subchapter S election

House bill.—Under present law, a subchapter S election may be made at any time during a 2-month period beginning one month before the start of the taxable year. Under the House bill, the period for making an election would be extended to the entire previous taxable year and the first 75 days of the current taxable year.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement is the same as the House bill and the Senate amendment.

58. "Simple" trusts permitted as subchapter S shareholders

House bill.—No provision.

Senate amendment.—Under present law, a trust (with limited exceptions) may not be a shareholder in a subchapter S corporation. The Senate amendment allows domestic trusts required to currently distribute all their income (including all income passed through from the subchapter S corporation) to be shareholders in a subchapter S corporation.

Conference agreement.—The conference agreement omits this provision.

59. Small business corporation stock

House bill.—Under present law, ordinary loss, rather than capital loss, treatment is provided in certain cases for small business corporation stock (section 1244 stock) which is disposed of at a loss by indi-

vidual shareholders to whom the stock was issued. The maximum amount of ordinary loss from the disposition of section 1244 stock that may be claimed in any taxable year is $25,000 ($50,000 in the case of a joint return). Excess losses are treated as capital losses.

Under present law, in addition to certain other requirements, the following requirements must be met for stock to qualify as section 1244 stock: (1) The corporation issuing the stock must adopt a written plan under which the stock will be issued; (2) the amount of section 1244 stock issued by the corporation may not exceed $500,000, and the total stock issued plus the equity capital of the corporation may not exceed $1,000,000; (3) no prior offering of stock of the corporation or any portion of a prior offering of stock may be unissued.

The House bill increases the maximum amount an individual may treat as an ordinary loss on section 1244 stock for any taxable year from $25,000 to $50,000 ($100,000 in the case of a joint return) and also increases the amount of section 1244 stock that a qualified small business corporation may issue from $500,000 to $1,000,000. Additionally, the House bill repeals the: (1) written plan requirement, (2) equity capital limitation, and (3) no prior stock offering limitation. The provision applies to common stock issued after the date of enactment of this Act.

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement follows the House bill and the Senate amendment.

G. Farm Accounting Rules

60. Accrual accounting for farming corporations

House bill.—With certain exceptions, the Tax Reform Act of 1976, required corporations (and partnerships in which nonexcepted corporations are partners) engaged in farming to use an accrual method of accounting and to capitalize preproductive period expenses. However, subchapter S corporations, family corporations (in which one family owns at least 50 percent of the stock), corporations with annual gross receipts of $1 million or less, and nurseries are not required to use the accrual method of accounting or to capitalize preproductive period expenses.

The 1976 Act provisions generally are effective for taxable years beginning after December 31, 1976. However, the Tax Reduction and Simplification Act of 1977 postponed the effective date of the required accrual accounting provision until taxable years beginning after December 31, 1977, for certain farming corporations controlled by two or three families.

The House bill provides exceptions to the required accrual accounting and capitalization of preproductive period expenses rules for certain corporations which are controlled by two or three families. The provisions requiring accrual accounting and the capitalization of preproductive period expenses will not apply to any farm corporation if, as of October 4, 1976, and at all times thereafter, either (1) two families own (directly or through attribution) at least 65 percent of the total combined voting power of all classes of stock of the corporation entitled to vote and at least 65 percent of the total number of shares of all other classes of stock of the corporation or (2) (a) members of three families own (directly or through attribution) at least 50 percent of the total combined voting power of all classes of stock entitled to vote and at least 50 percent of the total number of shares of all other classes of stock and (b) substantially all of the remaining stock is owned by corporate employees or by their family members or by a tax-exempt employees' trust for the benefit of the corporation's employees.

The House bill provides that, with respect to corporations described in the preceding paragraph, stock acquired after October 4, 1976, by the corporation's employees, their families, or a tax-exempt trust for their benefit will be treated as owned by one of the two or three families whose combined stock ownership was used to establish the initial qualification for this provision (as of October 4, 1976). The provision requires that corporations must have been engaged in the trade or business of farming on October 4, 1976, and at all times thereafter, to qualify for this exception.

Senate amendment.—The Senate amendment provides the same exception for corporations which are controlled by two or three families.

In addition, the Senate amendment excepts sod farms from the provisions requiring accrual accounting and capitalization of preproductive period expenses.

Conference agreement.—The conference agreement follows the Senate amendment.

61. Accounting for costs of growing crops

House bill.—Prior to 1976, farmers, nurserymen, and florists were not required to inventory growing crops regardless of the method of accounting they used for income tax purposes. However, in 1976 the Internal Revenue Service ruled that an accrual method farmer, nurseryman, or florist would be required to inventory growing crops. The changes made by this ruling are to be for taxable years beginning on or after January 1, 1978.

Under present law, corporations and partnerships (in which non-excepted corporations are partners) engaged in farming are required to use the accrual method of accounting and to capitalize preproductive period expenses (sec. 447). However, subchapter S corporations, family corporations (in which one family owns at least 50 percent of the stock), corporations with annual gross receipts of $1 million or less, and nurseries are not required to use the accrual method of accounting or to capitalize preproductive period expenses. In general, the requirement that preproductive period expenses be capitalized would have the effect of requiring taxpayers to inventory (or capitalize) the costs of growing crops.

The House bill permits a farmer, nurseryman, or florist who is on an accrual method of accounting and is not required by section 447 of the Code to capitalize preproductive period expenses to be exempt from the requirement that growing crops be inventoried.

The House bill also allows those farmers, nurserymen, or florists who are eligible to use an accrual method of accounting without inventorying growing crops to elect, without the prior approval of the IRS, to change to the cash receipts and disbursements method of accounting with respect to any trade or business in which the principal activity is growing crops. This election may be initiated only with respect to a taxable year beginning after December 31, 1977, and before January 1, 1981.

Senate amendment.—The Senate amendment is identical to the House bill.

Conference agreement.—The conference agreement is the same as the House bill and the Senate amendment.

H. Depreciation Provisions

62. Depreciation for small business

House bill.—Under present law, there are no special provisions exclusively applicable to the depreciation of assets by a small business. Although not limited to small businesses, the provision for additional first-year depreciation (sec. 179) was enacted to provide a special incentive for small businesses to make investments in depreciable property. Under this provision, a deduction is allowed for additional first-year depreciation in an amount not exceeding 20 percent of the cost of eligible property. In general, depreciable property placed in service during a taxable year is eligible under the provision if it is tangible personal property with a useful life of 6 years or more. The cost of the property which may be taken into account may not exceed $10,000 ($20,000 for individuals who file a joint return). Thus, the maximum additional first-year depreciation deduction is limited to $2,000 ($4,000 for individuals filing a joint return).

The House bill increases the allowable additional first-year depreciation percentage from 20 to 25 percent and increases the limitation on eligible property from $10,000 to $20,000 ($20,000 to $40,000 for individuals filing joint returns). Also, the additional first-year depreciation is limited to small businesses by providing that additional first-year depreciation is to be available only for taxpayers (including a controlled group of corporations) with depreciable assets whose adjusted basis as of the beginning of the taxable year is less than $1 million.

Senate amendment.—The Senate amendment would permit a taxpayer to elect to depreciate up to $25,000 in annual acquisitions of depreciable property over a 3 year period under the straight-line method and to obtain the benefit of the full investment tax credit (based on the regular useful life of the property) with respect to property for which an elction is made. Property which is depreciated under this provision is not eligible for additional first-year depreciation under section 179, but no other changes affecting section 179 are made.

Conference agreement.—The conference agreement omits both the provision of the House bill and the provision of the Senate amendment.

63. Treasury study of tax treatment of certain Government-mandated equipment

House bill.—No provision.

Senate amendment.—The Treasury Department is required to conduct a study to determine the tax treatment of various expenditures incurred by a taxpayer to comply with rules and regulations of the Occupational Safety and Health Act (OSHA) and the Mining Safety and Health Administration (MSHA) of the Department of Labor. The study is to focus on the feasibility of providing rapid 5-year amortization and special tax credit provisions. The report is to be submitted to Congress before April 1, 1979.

Conference agreement.—The conference agreement adopts the Senate amendment.

64. Five-year amortization for low-income housing

House bill.—Under present law, special 5-year amortization is provided for certain expenditures to rehabilitate low-income housing. These special rules are scheduled to expire on December 31, 1978. The House bill extends the provision for 3 years (until January 1, 1982).

Senate amendment.—The Senate amendment is the same as the House bill.

Conference agreement.—The conference agreement follows the House bill and the Senate amendment.

I. Other Business Provisions

65. Entertainment facility expenses

House bill.—No provision.

Senate amendment.—Under present law, deductions are allowable for ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business or for the production of income (secs. 162 and 212). Whether an expense is ordinary and necessary depends largely upon the particular facts and circumstances involved in each case. Ordinary and necessary business expenses which are deductible may include the cost of club dues or fees, and certain other expenditures relating to facilities. However, these expenses are deductible only if they both satisfy certain substantiation requirements (sec. 274(d)), and met the other prerequisites for deductibility.

Generally, no deduction is allowed for entertainment expenses unless the taxpayer substantiates by adequate records, or by sufficiently corroborative evidence, (1) the amount of the expense, (2) the time and place of its occurrence, (3) its business purpose, and (4) the business relationship to the taxpayer of the person or persons entertained (sec. 274(d)). In addition, ordinary and necessary expenses are deductible only if the expenses are allocable to the taxpayer's business, and are reasonable in amount, i.e., not lavish or extravagant.

Expenses with respect to entertainment "facilities" may be deductible if (1) they are ordinary and necessary, (2) the facility is used primarily for the furtherance of the taxpayer's business (i.e., more than 50 percent of the time that it is used), and (3) the expense in question is "directly related" to the active conduct of the taxpayer's business.

For this purpose, an entertainment facility is any item of personal or real property owned, rented, or used by a taxpayer during the taxable year for, or in connection with, any activity which is of a type generally considered to constitute entertainment, amusement, or recreation. For example, entertainment facilities include yachts, hunting lodges, fishing camps, swimming pools, tennis courts, bowling alleys, automobiles, airplanes, apartments, hotel suites, and vacation homes. However, a facility is not considered to be an "entertainment facility" if it is used only incidentally during a taxable year in connection with entertainment, and that use is insubstantial in relation to its business use. In the case of individuals and subchapter S corporations, apartments, hotel suites, vacation homes, and boats also may be subject to "vacation home" special disallowance rules if there is a certain amount of personal use of the facility, i.e., the personal use exceeds the greater of 14 days or 10 percent of rental days (sec. 280A).

If an item of property is considered to be an entertainment facility, the expenditure subject to the special entertainment facility rules include depreciation, rent, utility charges, maintenance and repair expenses, insurance premiums, salaries for caretakers and watchmen, and losses realized on the sale of other disposition of the property.

These expenditures also include dues and fees paid to any social, athletic, or sporting club or organization.[1] However, expenditures are not treated as being made with respect to a facility if they are out-of-pocket expenses, e.g., nonoperating costs such as expenditures for food and beverages. In addition, expenses attributable to a nonentertainment use of a facility are not treated as being expenses with respect to an "entertainment" facility, e.g., the use of an automobile or airplane for business travel purposes. Finally, expenses which are deductible without regard to their connection with a taxpayer's trade or business are not considered to be expenditures with respect to an entertainment facility, e.g., taxes, interest, and casualty losses.

In determining whether an entertainment facility is used primarily for business purposes, all the ordinary and necessary business use of the facility may be taken into account even though the use is not "directly related to" or "associated with" the active conduct of the taxpayer's profit-seeking activities. (Rev. Rul. 63–144, 1963–2 CB 129, 137). However, only the portion of the expenses which are "directly related" to the active conduct of the taxpayer's trade or business are deductible. Thus, the use of the facility in providing entertainment "associated with" the active conduct of a trade or business is taken into account in determining if the facility is used primarily for business purposes, but only those expenses attributable to a use which is "directly related" to the active conduct of a trade or business deductible.

The amendment, which is effective for expenditures paid or incurred after December 31, 1978, in taxable years ending after that date, provides that no deduction is allowed for any expenses paid or incurred with respect to a facility which is used in conjunction with an activity which is of a type generally considered to constitute entertainment, amusement, or recreation.[2]

Generally, the term "facility" includes any item of real or personal property which is owned, rented, or used by a taxpayer in conjunction or connection with an entertainment activity. Thus, expenses incurred with regard to entertainment facilities which are disallowed, include yachts, hunting lodges, fishing camps, swimming pools, tennis courts, and bowling alleys. Facilities also may include airplanes, automobiles, hotel suites, apartments, and houses (such as beach cottages and ski lodges) located in recreational areas. However, the deduction is not affected unless the property is used in connection with entertainment

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[1] While dues or fees paid to any social, athletic, or sporting club or organization are considered to be expenses incurred with respect to an entertainment facility, clubs operated solely to provide lunches under circumstances generally considered to be conducive to business discussions are exempted. Treas. Regs. § 1.274–2 (e)(3)(ii). In addition, dues paid to professional associations and civil organizations generally are exempt. Rev. Rul. 63–144, 1963–2 C.B. 129, 138–139. An initiation or similar fee which is payable only upon joining a club, and the useful life of which extends over more than one year, is a nondeductible capital expenditure. *Kenneth D. Smith*, 24 TCM 899 (1965).

[2] Such a facility would be considered to be an asset which is used for personal, living, or family purposes, and not as an asset used in the taxpayer's trade or business, or in a profit-seeking endeavor. As such, the investment tax credit would not be available upon the acquisition of such a facility.

Expenses of an automobile or an airplane used on business trips will continue to be allowed. In addition, as under present law, the term "facility" includes dues or fees paid to any social, athletic, or sporting club or organization.

If otherwise deductible, the amendment would not apply to dues or fees which are paid to civic or professional organizations, or to those which are paid to business luncheon clubs. Nevertheless, the bill would not preclude an otherwise allowable deduction for business meals merely because the expense was incurred in the dining room of a club or organization with respect to which no deduction is allowed for dues or fees.

Similarly, the amendment would disallow and otherwise allowable deduction for items relating to bona fide business expenses incurred while away from home overnight. For example, the amendment generally would not apply to expenses incurred by an individual away from home at a bona fide business, trade, or professional organization meeting or convention. These expenses, however, would continue to be subject to the generally applicable rules relating to the deductibility of business travel, convention, and entertainment activity expenses.

The provisions of the amendment also would be inapplicable to expenditures for tickets to sporting and theatrical events, regardless of whether the tickets are purchased individually, in a series or by the season, or by an equivalent fee which entitles the taxpayer to use a seat, sky-box, lounge, box, or other similar facility which provides a viewing area for such an event. Ticket costs generally would be subject either to the provisions of present law relating to entertainment activities, or to those which govern the deductibility of business gifts.

In addition, the amendment would continue a number of the present statutory exceptions to the facility expense rules. Thus, for example, otherwise allowable deductions for expenditures relating to the following items would not be covered by the amendment: (1) facilities, located on the taxpayer's business premises and used in connection with furnishing food, (2) certain employee recreational facilities, (3) facility expenses treated as employee compensation, (4) facilities made available to the general public, (5) facilities used in connection with a taxpayer's trade or business of selling entertainment for adequate and full consideration in bona fide transactions, and (6) facilities actively used in the taxpayer's business of selling such facilities. The amendment, however, also continues any applicable present law limitations on these exceptions, including those pertaining to allocation of expenses.

In addition to the above-enumerated expenses, the disallowance rule would not apply to the extent that a portion of the facility otherwise qualified as one which was not an entertainment facility, or to the extent that a facility with respect to which expenses ordinarily would be denied as deductions, qualifies under one of the above exceptions. Similarly, expenses incurred with respect to certain transportation facilities, for example automobiles and airplanes, would be allowed provided that the taxpayer establishes that the facility was used primarily for the furtherance of a trade or business, and that the expenses otherwise met the ordinarily applicable rules with respect to business deductions.

Although the amendment disallows deductions which are predicated upon a profit-seeking intent, it does not apply to any deduction allowable without regard to the taxpayer's trade or business or income producing activity, e.g., interest (sec. 163), taxes (sec. 164), or casualty losses (sec. 165).

In addition, the generally applicable investment credit and depreciation recapture rules are not to apply simply due to the characterization of a facility as a nontrade or business asset. These rules, however, remain effective with respect to all other events which ordinarily would require recapture.

Conference agreement.—The conference agreement follows the Senate amendment, but excludes dues or fees paid to country clubs from the disallowance rules.

Moreover, the deductions for otherwise allowable business entertainment activities and business meals are not affected by this legislation. For example, if a salesman took a customer hunting for a day at a commercial shooting preserve, the expenses of the hunt (such as hunting rights, dogs, a guide, etc.) would be deductible provided that the current law requirements of substantiation, adequate records, ordinary and necessary, directly related, etc. are met. However, if the hunters stayed overnight at a hunting lodge on the shooting preserve, the cost attributable to the lodging would be non-deductible but expenses for any meals would be deductible if they satisfied the requirements of current law. The shooting preserve should provide the taxpayer with an allocation of charges attributable to the overnight lodging for the taxpayer and guests.

The provisions of the bill also would be inapplicable to expenditures for tickets to sporting and theatrical events, regardless of whether the tickets are purchased individually, in a series or by the season, or by an equivalent fee which entitles the taxpayer to use a seat, sky-boxes, lounges, boxes or other similar facilities which provide a viewing area for such an event. These costs generally would be subject either to the provisions of present law relating to entertainment activities, or to those which govern the deductibility of business gifts.

66. Deficiency dividend procedure for regulated investment companies

House bill.—No provision.

Senate amendment.—The Senate amendment provides a deficiency dividend procedure for regulated investment companies under which the corporation could make qualifying distributions after the normal period for making distributions when an adjustment by the Internal Revenue Service occurs that either increases the amount which the corporation is required to distribute to meet the distribution requirement or decreases the amount of dividends previously distributed for that year.

Conference agreement.—The conference agreement follows the Senate amendment.

67. Safe Harbor rule for real estate investment trusts

House bill.—No provision.

Senate amendment.—Under present law, a 100-percent penalty tax is imposed on the gain of a real estate investment trust (commonly called a "REIT") from certain property primarily held for sale to customers

in the ordinary course of the REIT's trade or business. In addition, in lieu of the 100 percent tax, the normal corporate income tax is imposed upon certain income from property acquired by foreclosure for a period of two years (with permissible extensions by the IRS for another two years.)

The Senate amendment provides a safe harbor rule for real estate investment trusts which would exempt from the 100-percent tax on prohibited transactions any gain from the sale of a real estate asset where (1) the property was held by the real estate investment trust for a minimum of four years, (2) the real estate investment trust made no more than five sales of property in the taxable year, (3) the real estate investment trust did not make improvements to the property during the four-year period prior to sale in excess of 20 percent of the net selling price, and (4) the property generally was held for rent by the real estate investment trust for at least four years. In addition, the Senate amendment would increase the additional period that the IRS may grant to a REIT to hold foreclosure property from two years to four years (for a total of six years that foreclosure property may be held).

Conference agreement.—The conference agreement follows the Senate amendment with minor technical changes.

68. Contributions in aid of construction

House bill.—No provision.

Senate amendment.—Under present law, contributions to the capital of a corporation, whether or not contributed by a shareholder, are not includible in the gross income of the corporation (sec. 118). Nonshareholder contributions of property to the capital of a corporation have a zero basis to the corporation. If money is contributed by a nonshareholder, the basis of any property acquired with the money during the 12-month period beginning on the date the contribution is received, or of certain other property, is reduced by the amount of the contribution (sec. 362 (c)).

Generally, the Tax Reform Act of 1976 provided that contributions in aid of constructions (other than customer connection fees) to regulated public water and sewerage utilities are to be treated as nontaxable contributions to capital by nonshareholders. The 1976 Act did not affect the treatment of contributions to utilities other than water and sewerage utilities. The treatment of contributions in aid of construction to such other utilities is unclear under present law.

The Senate amendment extends the present law provision on contributions in aid of construction to water and sewerage utilities (sec. 118 (b)) to regulated public gas and electric utilities. Under that provision, contributions in aid of construction to regulated public gas and electric utilities are treated as nontaxable contributions to capital by nonshareholders.

Conference agreement.—The conference agreement follows the Senate amendment.

69. Treatment of certain liabilities on incorporation of a trade or business

House bill.—No provision.

Senate amendment.—Under present law, upon incorporation of a business no gain or loss is generally recognized as a result of the

transfer of property to the corporation provided the transferors own 80 percent of the stock of the corporation immediately following the transfer. An exception applies where the corporation assumes a liability or acquires property subject to a liability, and the total amount of these liabilities exceeds the adjusted basis of the property transferred to the corporation. In this situation, the difference between the liabilities over the adjusted basis of the assets is considered as taxable gain to the transferor.

This provision has caused unintended tax difficulties for certain cash-basis businesses. The problem is caused by the fact that these businesses may have large amounts of trade accounts payable and trade accounts receivable. The trade accounts receivable have a zero adjusted basis in tha hands of the transferor, and the accounts payable are not deductible until paid and are thus carried on the taxpayers books until payment. Upon incorporation, if the trade accounts payable are treated as liabilities then the transferor may have taxable gain if the total liabilities transferred to the corporation exceeds the total of the adjusted basis of the assets transferred to the corporation.

Under the amendment, in determining (for purposes of section 357(c)) the amount of liabilities assumed or to which the property transferred is subject, the amount of a liability would be excluded for a cash basis transferor to the extent payment thereof by the transferor would have given rise to a deduction or would have constituted certain payments to partners under section 736(a). However, the amount of any liability excluded under this general rule would be included for purposes of section 357(c) computation to the extent that the incurrence of such obligation resulted in the creation of, or an increase in, the basis of any property.

Finally, under the amendment the amount of such excluded liabilities would not reduce the transferor's basis in stock received in the exchange.

The amendment applies to transfers of property to corporations made on or after the date of enactment.

Conference agreement.—The conference agreement follows the Senate amendment.

70. Medical expense reimbursement plans

House bill.—No provision.

Senate amendment.—Under present law, gross income does not include amounts received under a self-insured accident or health plan for employees as reimbursement for employee medical expenses, unless the expenses were deducted in a prior taxable year.

Under the Senate amendment, self-insured medical reimbursement plans would be subject to rules forbidding discrimination in favor of employees who are officers, shareholders, or highly paid. Part-time and seasonal employees, as well as certain employees in a collective bargaining unit and employees who are nonresident aliens with no U.S. earned income from the employer would be excluded from a plan.

Plan benefits would be required to extend to a nondiscriminatory group of employees. Also benefits provided by a plan would be subject to a nondiscrimination test. Amounts paid under a discriminatory benefit to an officer, etc., would be includible in income. Also, benefits

paid to an officer, etc., under a plan which does not cover a nondiscriminatory group of employees would be partially includible in income. The Senate amendment would apply for taxable years beginning after December 31, 1979.

Conference agreement.—The conference agreement generally follows the Senate amendment.

Under the conference agreement, an employee who qualifies for benefits under a medical reimbursement plan on the date of enactment of the Act and who is not employed by the employer after that date would not be considered in testing a plan for prohibited discrimination. Also, under the conference agreement, employees whose customary weekly employment is for less than 35 hours would be considered part-time and employees whose customary annual employment is for less than 9 months would be considered seasonal.

In addition, the conference agreement provides that amounts reimbursed under a medical reimbursement plan would not be subject to withholding tax or social security tax.

Although no advance rulings from the Internal Revenue Service would be required, the conferees expect that, in a typical case, advance rulings will be available. The conferees also expect that a determination by the Service that a plan is discriminatory will not be applied retroactively where the plan has made reasonable efforts to comply with tax discrimination rules.

The conference agreement authorizes the Secretary of the Treasury to prescribe necessary regulations. The conferees expect that these regulations will provide that reimbursement for diagnostic procedures (medical examinations, X-rays, etc.) need not be considered by an employer to be a part of a medical reimbursement plan. However, this exception is to apply only for diagnostic procedures performed at a facility which provides no services other than medical services and ancillary services and applies to travel expenses only to the extent such expenses are ordinary and necessary.

Under the conference agreement, an employer's plan will not violate the discrimination rules merely because benefits under the plan are offset by benefits paid under a self-insured or insured plan of the employer or another employer, or by benefits paid under Medicare or other Federal or State law.

Under the conference agreement, if a self-insured medical reimbursement plan is included in a "cafeteria plan", the medical reimbursement plan rules would determine the status of a benefit as a taxable or nontaxable fringe benefit and the cafeteria plan rules would determine whether an employee would be taxed as though he elected all available taxable benefits (including taxable benefits under a discriminatory medical reimbursement plan). The conference agreement applies to claims filed and paid in taxable years beginning after December 31, 1979.

71. Postponement of effective date for special limitations on net loss carryovers

House bill.—No provision.

Senate amendment.—Under present law, the 1976 Act extensively revised the Code provisions dealing with the carryover of net operating losses in cases of acquisitions of loss corporations. The limitations on

loss carryover attributes apply to acquisitions made by purchase or through corporate reorganizations. The new provisions changed the basic concept underlying the rules by deleting continuity of business requirements for purchases and establishing a new continuity of ownership test applicable to both purchases and reorganizations. These new provisions apply to plans of reorganization adopted on or after January 1, 1978, and to sales or exchanges in taxable years beginning after June 30, 1978.

The Senate amendment delays the effective date of the 1976 change until January 1, 1980, with respect to plans of reorganization adopted on or after that date, or until June 30, 1980, with respect to sales or exchanges occurring in taxable years beginning after that date. It also permits taxpayers to elect to have the 1976 changes apply to any acquisition or reorganization occurring before the close of the taxpayer's first taxable year beginning after June 30, 1978. This election applies only if the acquisition or reorganization occurs pursuant to a contract or option to acquire stock or assets entered into before September 30, 1978.

Conference agreement.—The conference agreement follows the Senate amendment.

72. Redemptions of United States railway certificates of value

House bill.—No provision.

Senate amendment.—Under present law, tax attributes (including net operating losses) of a predecessor corporation generally carry over to a successor corporation in a tax-free reorganization. Special net operating loss rules apply to railroads which transfer property under the ConRail reorganization (i.e., otherwise expired net operating losses are revived to the extent any income is realized eventually from certificates of value issued for the transfer of property). Present law does not deal specifically with the effect of the tax-free reorganization on the special net operating loss rule for ConRail transfer or corporations.

The Senate amendment provides that the special treatment of net operating losses of transferor railroads and redemptions of certificates of value is not to be affected by a tax-free reorganization of a transferor railroad and another member of its affiliated group of corporations. This provision is effective for taxable years ending after March 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment.

73. Source of income from rental of railroad rolling stock

House bill.—No provision. (However, the House has passed a bill, H.R. 12352, which is substantially the same as the Senate amendment.)

Senate amendment.—Under present law, a lessor of railroad rolling stock may lose foreign tax credits if the lease produces a tax loss for the year and the cars are used outside the United States, because the loss is treated as a foreign source loss in proportion to the time during the year that the car is used outside the United States. Some lessors have required railroads which lease the cars from them to agree to indemnify them for these adverse tax consequences. The potential liability under these indemnity agreements has deterred the railroads from allowing the lease-financed rolling stock to be used outside the United States and therefore has resulted in inefficient utilization and routing of the rolling stock.

The Senate amendment provides that the income or loss from the rental of rolling stock to railroads is to be U.S. source income or loss if the rolling stock is not used outside the United States except on a temporary basis not expected to exceed 90 days. This modification of the source rules for income and loss from the rental of rolling stock would prevent the potential loss of lessors' foreign tax credits.

The amendment is effective with respect to rolling stock placed in service after the date of enactment. At the election of the lessor, the provision also applies to railroad rolling stock placed in service on or before the date of enactment.

Conference agreement.—The conference agreement follows the Senate amendment.

V. CAPITAL GAINS PROVISIONS

74. Capital gains deduction for individuals

House bill.—No provision.

Senate amendment.—Under present law, a noncorporate taxpayer deducts from gross income 50 percent of the amount of any net capital gain for the taxable year, and the balance is included in income and taxed at the regular rates.

The Senate amendment provides that a noncorporate taxpayer may deduct from gross income 70 percent of the amount of any net capital gain for the taxable year, and that the remaining 30 percent is includible in income and subject to the regular tax rates.

The provision is effective for taxable transactions occurring, and installment payments received, after October 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment, but increases the amount of any net capital gain which a noncorporate taxpayer may deduct from gross income from 50 to 60 percent. The remaining 40 percent of the net capital gain is includible in gross income and subject to tax at the otherwise applicable rates. The deducted gain is classified as a tax preference item for minimum tax purposes (*see below*), but not for purposes of reducing the amount of personal service income which is eligible for the maximum tax (*see below*). The provisions of the conference agreement are effective for taxable transactions occurring, and installment payments received, after October 31, 1978.

The conference agreement also coordinates the increased capital gains deduction with the rules applicable to charitable contributions of property. It provides that the amount of certain charitable contributions of capital gains property is to be reduced by 40, rather than 50, percent of the gain which would have been long-term capital gain if the property contributed had been sold by the taxpayer at its fair market value.

The conference agreement does not change the present law treatment of a noncorporate taxpayer's capital losses.

As a transition rule for 1978, the conference agreement generally provides that a noncorporate taxpayer may deduct from gross income 60 percent of the post-October, and one-half of the pre-November, capital gains. Under this rule, the 60 percent deduction will apply to the net capital gains in excess of any pre-November capital losses taking into account only sales or exchanges (including short-term transactions) after October 31, 1978. In computing the post-October net gain, no capital loss carryover is taken into account. These rules are intended so make the appropriate differentiation between pre-and post-effective date gains and losses.

75. Alternative tax for capital gains of individuals

House bill.—Under present law, a noncorporate taxpayer deducts from gross income 50 percent of the amount of any net capital gain for the taxable year, and the balance is includible in gross income and

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taxed at the regular rates. In lieu of taxing 50 percent on net capital gains at the regular rates, a partial alternative tax of 25 percent of the first $50,000 of net capital gains applies if it results in lower tax rates than that produced by the regular method.

The House bill repeals the alternative tax for taxable years beginning after December 31, 1978.

Senate amendment.—Same as the House bill, except that the alternative tax would be repealed for taxable years beginning after October 31, 1978.

Conference agreement.—The conference agreement adopts the House bill and the Senate amendment, effective for taxable years beginning after December 31, 1978.

76. Corporate alternative capital gains tax

House bill.—No provision.

Senate amendment.—Under present law, an alternative tax of 30 percent applies to corporate net capital gains if that rate is less than its regular tax rates. No special deduction for corporate capital gains is available.

The Senate amendment reduces the corporate alternative tax rate from 30 percent to 28 percent.

This change is effective with respect to sales occurring, and installment payments received, after December 31, 1978.

Conference agreement.—The conference agreement adopts the provisions of the Senate amendment.

77. Indexing of capital assets for purposes of gain on sale

House bill.—The House bill provides for the indexing for inflation on the basis of common stock, real estate and tangible personal property for purposes of determining gain (or loss) on sale.

Senate amendment.—No provision.

Conference agreement.—The conference agreement does not contain this provision.

78. Exclusion of gain on residential sales

House bill.—Under present law, the entire amount of gain or loss realized on the sale or exchange of property generally is recognized. However, under a "rollover" provision of the Code, gain is not recognized on the sale or exchange of a taxpayer's principal residence if a new principal residence, at least equal in cost to the adjusted sales price of the old residence, is purchased and used by the taxpayer as his or her principal residence within a period beginning 18 months before, and ending 18 months after, the date of the sale of the old residence. The basis of the new residence then is reduced by the amount of gain not recognized on the sale of the old residence. When the purchase price of the new residence is less than the adjusted sales price of the old residence, gain is recognized only to the extent that the adjusted sales price of the old residence exceeds the taxpayer's cost of purchasing the new residence.

If, however, an individual realizes gain on the sale or exchange of a residence and fails to satisfy the rollover requirements, then the gain generally is taxable pursuant to the usual rules of the Code to the extent the exclusion for sales of residences by elderly taxpayers does not apply.

In addition, under present law, an individual who has attained the age of 65 may elect to exclude from gross income, on a one-time basis, the entire gain realized on the sale of his or her principal residence if the adjusted sales price is $35,000 or less. If the adjusted sales price exceeds $35,000 the amount excludable is that portion of the gain which is determined by multiplying the total gain by a fraction, the numerator of which is $35,000, and the denominator of which is the adjusted sales price of the residence. The exclusion is not available unless the property was owned and used by the taxpayer as his or her principal residence for 5 years or more during the 8-year period preceding the sale. Due to this actual use and occupancy requirement the holding period of condemned or involuntarily converted residence is not added to that of a replacement residence for purposes of having gain on the sale of the latter property qualify for the exclusion.

A taxpayer who has attained the age of 65 may utilize the special exclusion and then use the generally available rollover provision with respect to the balance of any gain.

The House bill repeals the provision of present law relating to gain realized on the sale of a principal residence by a taxpayer 65 and over. It provides that an individual, regardless of age, may elect to exclude from gross income up to $100,000 ($50,000 in the case of married individuals who file separate returns) of any gain realized on the sale or exchange of his or her principal residence. The exclusion applies only once in a taxpayer's lifetime, and the provisions relating to rollover of gain on the sale of a principal residence would not apply to any sale or exchange of the principal residence with respect to which this election is made. The exclusion applies only with respect to gain realized on the sale or exchange of a residence which the taxpayer has owned and occupied as his or her principal residence for periods aggregating two years out of the three-year period which immediately precedes the sale. The definition of a taxpayer's principal residence is that presently used for the rollover provision.

There is to be only one lifetime election with respect to married taxpayers, i.e., the election does not apply separately to each spouse. If, however, each of two parties have made elections independently prior to becoming married, there is to be no recapture of the taxes attributable to the gain excluded with respect to the sale of one of the residences. If spouses make an election during marriage, and subsequently become divorced, no further elections are available to either of them or to their spouses should they marry.

Gain realized on the sale of a taxpayer's principal residence is not a tax preference item.

Senate amendment.—The amendment modifies the provision of present law relating to the exclusion of gain realized on the sale of a principal residence by an individual 65 and over. Generally, the amendment extends the availability of the special exclusion provision to all taxpayers who either have attained the age of 55 or who are totally and permanently disabled (within the meaning of Code section 105(d)(5)), and increases the numerator of the ratio formula from $35,000 to $100,000. It also removes all gain recognized on the sale of a principal residence from the minimum tax. In addition, the amendment provides that the holding period of a condemned or involuntarily converted residence may be tacked to that of a replacement residence for purposes of having gain on the sale of the latter property qualify for the exclusion.

The amendment's exclusion applies only with respect to gain realized on the sale or exchange of a principal residence (including condominiums and stock of a tenant-shareholder of a cooperative housing corporation) which the taxpayer has owned and occupied as his or her principal residence for a period aggregating two years out of the three-year period which immediately precedes the sale. However, the amendment provides two exceptions to the generally applicable ownership and occupancy rule. The first exception is a limited transition rule which provides that individuals who can, or could have, satisfied the age, ownership and use requirements of present law (5 years or more out of the 8-year period which precedes the sale) will have until July 27, 1981, to qualify for the exclusion either under the new ownership and occupancy test or that of the present law. The second exception provides that the holding period of a condemned or involuntarily converted resdience may be tacked to that of a replacement residence for purposes of having gain on the sale of the latter property qualify for the exclusion.

If a taxpayer makes an election to exclude gain realized on the sale of his or her principal residence, and subsequently purchases a new residence, the amount of any gain exlcuded on the prior sale will not reduce his or her basis for the new residence.

The amendment also provides that no amount of gain realized on the sale or exchange of an individual's principal residence, whether or not excludable under the amendment, is a tax preference subject to the minimum tax, or to the alternative minimum tax. Gain recognized on the sale of a residence which is not the taxpayer's principal residence remains an item of tax preference.

The election is allowed only once, and must be made in accordance with regulations prescribed by the Secretary.

This provision is effective for sales and exchanges after July 26, 1978.

Conference agreement.—The conference agreement repeals the provision of present law which relates to the exclusion of gain on the sale of a residence by an individual who has attained the age of 65. The agreement provides that an individual who has attained the age of 55 may exclude from gross income, on a one-time elective basis, up to $100,000 of gain from the sale of his or her principal residence. The exclusion would be available only in the case of gain from the sale of a principal residence which the individual owned and occupied as his or her principal residence for a period aggregating 3 out of the 5 years which precede the sale. (However, a special transition rule is provided by the conference agreement for individuals eligible under the present law test.) Consequently, except in the case of a principal residence which has been involuntarily converted, no tacking of holding periods is allowed with respect to the exclusion.

There is to be only one lifetime election with respect to married individuals, i.e., the election does not apply separately to each spouse. However, if each of two parties have made the election independently prior to becoming married, there is to be no recapture of the taxes attributable to the gain excluded with respect to the sale of one of the residences.

Gain realized on the sale of a taxpayer's principal residence is not an item of tax preference.

As under the present law applicable to residential sales by individuals who have attained the age of 65, taxpayers eligible for the election contained in the conference agreement may use it in conjunction with the residential rollover provision.

The election, which is effective for sales and exchanges after July 26, 1978, must be made in accordance with regulations prescribed by the Secretary.

79. Rollover of gain of residential sales

House bill.—Under present law, gain realized from the sale of a taxpayer's principal residence generally is not recognized where the taxpayer purchases and uses a new principal residence, at least equal in cost to the sales price of the old residence, within a period beginning 18 months before, and ending 18 months after, the sale. Only the last principal residence purchased and used during this replacement period constitutes the new residence for purposes of the rollover provision.

The bill generally provides for the rollover of gain realized on the sale of more than one principal residence where an individual relocates for employment purposes more than once within a period beginning 18 months from the time that his or her first principal residence is sold. Taxpayers generally will be allowed the benefits of this multiple rollover provision where there was a reasonable expectation at the time of the relocation that the taxpayer would be employed, or remain, at the new location for a substantial period of time.

Thus, where the taxpayer is entitled to deduct moving expenses with respect to a relocation falling within the 18-month period, the multiple rollover provision would be available so as to allow the nonrecognition of gain on the sale of a principal residence occupied by the taxpayer of, in fact, the taxpayer subsequently relocated within the 18-month period for employment purposes and acquired a new principal residence. However, in order to qualify for such treatment, a sale must be in connection with the commencement of work by the taxpayer as an employee or as a self-employed individual at a new principal place of work and the taxpayer must satisfy both the geographic and length of employment requirements for deductibility of moving expenses.

The provision is effective for sales and exchanges of principal residences after July 26, 1978.

Senate amendment.—Same as the House bill.

Conference agreement.—The conference agreement adopts the provisions of the House bill and the Senate amendment.

80. Capital gains study

House bill.—Under present law, the Treasury Department is not required to submit reports to Congress on the effectiveness of specific tax provisions in accomplishing the purposes for which they were enacted.

The House bill requires the Treasury Department to prepare, and submit to Congress, a report on the effectiveness of the reductions of both the individual and corporate capital gains tax rates in stimulating investment, increasing the rate of economic growth, increasing employment, and of the effects of these reductions on income tax revenues.

The report is to be made by September 30, 1981.

Senate amendment.—No provision.

Conference agreement.—The conference agreement follows the House bill.

VI. MINIMUM AND MAXIMUM TAX PROVISIONS

A. Minimum Tax Provisions

81a. Minimum tax for individuals

House bill.—Present law (sec. 56 of the Code) provides a minimum tax on certain tax preferences of individuals and corporations. The minimum tax for individuals amounts to 15 percent of the sum of an individual's (or estate or trusts's) tax preferences in excess of one-half of regular income taxes paid or, if greater, $10,000.

The tax preference items included in this base of the minimum tax for individuals are:

(1) Accelerated depreciation on real property in excess of straight-line depreciation;

(2) Accelerated depreciation on personal property subject to a lease in excess of straight-line depreciation;

(3) Amortization of certified pollution control facilities (the excess of 60-month amortization (sec. 169) over depreciation otherwise allowable (sec. 167));

(4) Amortization of railroad rolling stock (the excess of 60-month amortization (sec. 184) over depreciation otherwise allowable (sec. 167));

(5) Qualified stock options (the excess of the fair market value at the time of exercise over the option price);

(6) Percentage depletion in excess of the adjusted basis of the property;

(7) The deduction for long-term capital gains;

(8) Amortization of child care facilities (the excess of 60-month amortization (sec. 188) over depreciation otherwise allowable (sec. 167));

(9) Itemized deductions (other than medical and casualty loss deductions) in excess of 60 percent of adjusted gross income; and

(10) Intangible drilling costs on oil and gas wells in excess of the amount amortizable with respect to those costs and, for 1977, in excess of net income from oil and gas production.

The House bill removes capital gains as an item of tax preference subject to the existing 15-percent minimum tax. However, the bill provides for the imposition of an alternative minimum tax at a rate of 10 percent on one-half of a noncorporate taxpayer's net capital gains (not including any gain recognized on the sale of the taxpayer's principal residence), reduced by a $10,000 exemption, if this amount exceeds the taxpayer's regular tax liability as computed after the application of tax credits. The tax applies to individuals, estates and trusts.

Under the bill, noncorporate taxpayers who realize capital gains would compute their regular tax liability, and compare this amount with that calculated under the alternative minimum tax. These amounts would be compared prior to being increased by the amount,

if any, of the existing 15-percent minimum tax. For this purpose, regular tax liability is computed before subtraction of the credit for withheld tax (sec. 31), the credit for refunds of taxes on gasoline, etc. (sec. 39), and the earned income credit (sec. 43), but after the subtraction of other credits.

Where the alternative minimum tax exceeds the regular tax, no credits generally will be allowable against the alternative minimum tax liability. However, certain refundable credits will be allowed against the alternative minimum tax (i.e., the credit for withheld taxes, the credit for refunds of gasoline and other fuel taxes, and the earned income credit), because the amounts involved would be available as refunds to the taxpayer in any event.

Senate amendment.—The Senate amendment repeals the present law minimum tax for individuals beginning in 1979 and establishes an alternative minimum tax, under which a taxpayer pays the alternative minimum tax only where it exceeds the taxpayer's regular income tax.

Generally, the tax base for the alternative minimum tax is taxable income plus the taxpayer's preferences items for the year. This amount then is reduced by a $20,000 exemption and subject to the following minimum tax rates:

	Percent
0–$40,000	10
$40–$80,000	20
Over $80,000	25

The amount of minimum tax is the amount by which the tax computed under this rate schedule exceeds the taxpayer's regular tax. Thus, although the tax is in effect a true alternative tax, in the sense that it is paid only when the amount of tax computed under the above schedule exceeds regular tax, technically the taxpayer's regular tax continues to be imposed and the amount of alternative minimum tax is the excess of the amount computed under the minimum tax rate table over the amount of the regular tax.

The provision then allows a foreign tax credit and the refundable credits against this tax is the amount in excess of the taxpayer's regular tax.

In general the preferences for purposes of the new alternative minimum tax are the same as under present law. The preference for excluded gain from the sale or exchange of a capital asset is increased, however, to conform to the higher capital gains deduction. (This change in the capital gains preference also is made with respect to the increased deduction provided for gains from sales or exchanges occurring in November and December 1978, which is treated as a preference under the present law minimum tax.) Also, gain from the sale of principal residences is not included as a preference under the alternative minimum tax (or under the add-on minimum tax for sales in November or December 1978).

In addition, the amendment makes permanent the preference for intangible drilling costs in excess of oil income as modified by the Tax Reduction and Simplification Act of 1977 and as agreed to by both the House and Senate in their versions of the energy tax legislation of this Congress. Under the amendment, intangible drilling cost deductions for oil and gas wells would be included in the minimum

tax base of individuals only to the extent that intangible drilling and development costs, over the amount of those costs amortizable on the basis of a 10-year life or under cost depletion, exceed the net taxpayer's income from oil and gas properties.

In addition, the amendment significantly modifies the preference for adjusted itemized deductions. Under the amendment, itemized deductions (as under present law) plus State and local tax deductions and, in the case of income in respect of decedents, amounts deducted (under sec. 691(c)) for estate taxes. The remaining itemized deductions are preferences to the extent they exceed sixty percent of adjusted gross income minus the medical and casualty deductions, State and local taxes and the estate tax described above.

The provision contains two special elections to allow taxpayers to avoid claiming an item of tax preference to reduce their regular tax. First, the amendment allows a taxpayer, in the manner prescribed by the Secretary, to elect to capitalize intangible drilling costs with respect to any oil and gas property. This property by property election replaces the election under present law which once made by a taxpayer applies for all oil and gas properties for all years of that taxpayer. Second, the amendment includes a provision allowing any recipient of a stock option which continues to meet the requirements for preferential treatment provided in secs. 422 or 424 of the Code) under transitional rules provided in the 1976 Tax Reform Act to be treated as nonqualified options and taxed under section 83 of the Code.

Finally, the amendment provides that certain charitable lead trusts which received transfers of property prior to January 1, 1977, would not be subject to the preference for adjusted itemized deduction for contributions attributed to that property.

The amount of income subject to the alternative minimum tax is gross income reduced by all deductions (other than any net operating loss deduction) and by any nonpreferential net operating loss and increased by the amount of tax preferences. This net amount, reduced by a $20,000 exemption is subject to the alternative minimum tax rates described above.

The alternative minimum tax is paid only to the extent that it exceeds an individual's regular tax. A taxpayer's regular tax means the taxes imposed by chapter 1 of the Code other than the alternative minimum tax and the penalty taxes applicable in certain circumstances. These taxes are to be reduced by all nonrefundable credits including the foreign tax credit (sec. 33). Thus, taxpayers paying the alternative minimum tax are not to obtain the benefit of nonrefundable credits other than the foreign tax credit to the extent of that taxpayer's alternative minimum tax. However, the amendment provides that in the case of certain credits, any credit carryovers to future years from a year in which the taxpayer is liable for some amount of alternative minimum tax are not to be reduced to the extent of the taxpayer's alternative minimum tax liability.

The foreign tax credit is to be allowed against the alternative minimum tax. Under the provision the amount of credit allowed is to be determined under the normal foreign tax credit limitation rules (sec. 904), but the computation of the limit is to be modified to include preference items which are added back in computing income

subject to minimum tax. Thus, a taxpayer's foreign source income on which foreign tax credits are allowed is to be increased by any preference attributable to foreign sources (or, in the case of deduction preferences, those properly allocated or apportioned to foreign source income) and a taxpayer's entire taxable income is to be increased by all preferences.

Under special rules for net operating losses, a taxpayer's income for alternative minimum tax purposes is to be reduced by net operating loss deductions only to the extent of the taxpayer's "nonpreferential net operating loss deduction," which is defined as the net operating loss deduction computed without regard to items preference included in that deduction. Thus, a taxpayer is allowed to reduce income subject to the new alternative minimum tax only by any net operating loss deduction to the extent of nonpreference losses making up the deduction.

The provision also includes special rules for the application of the alternative minimum tax in the case of trusts. First, the $20,000 exemption from the tax is to be allocated in the case of trusts. Second, in the case of a trust making current distributions of tax preferences which are items of deductions other than depletion and depreciation (e.g., intangible drilling costs) are to be allocated to beneficiaries where appropriate under regulations prescribed by the Secretary. (Of course, a trust is to receive the same deduction for alternative minimum tax purposes for the amount of income currently distributed as is received for regular tax purposes.)

Finally, in the case of accumulation distributions from a trust, the amount of taxes deemed imposed on the trust is not to be increased by any alternative minimum tax in excess of the trust's regular tax liability. Thus, no credit is available to pay any beneficiary of an accumulation distribution for any minimum tax paid by the trust with respect to that distribution; however, under the normal trust rules, no amount received by that beneficiary is treated as an item of tax preference to the beneficiary.

In general, the provision is effective for taxable years beginning after 1978. In addition, the provision is not to be treated as a change of the rate of tax (under sec. 21 of the Code). Thus, fiscal year taxpayers are to first be subject to the new minimum tax for their taxable year beginning in 1979.

However, the provisions changing the effective date for the preferences for capital gains (to 60 percent of net capital gain) for purposes of the present law minimum tax is to apply for all sales or exchanges taking place after October 31, 1978.

For purposes of both effective dates payments received after the effective date with respect to pre-effective date installment sales are to be taxed under the new provisions applicable generally to sales made after the effective date.

Conference agreement.—The conference agreement adopts a modified form of the provisions contained in the House bill and the Senate amendment. It retains the present law minimum tax with respect to all preference items except the deducted amount of capital gains and excess itemized deductions. In addition, it provides for an alternative minimum tax which is paid by an individual only to the extent that it

exceeds regular tax paid as increased by the present add-on minimum tax. Under the conference agreement, noncorporate taxpayers would compute regular tax liability and increase it by the amount of any add-on minimum tax liability. This sum then would be compared to the amount of tax computed under the alternative minimum tax formula. The alternative minimum tax, the computation of which generally follows that contained in the Senate amendment, is based on the sum of an individual's taxable income (as computed under present law), adjusted itemized deductions, and the amount of any capital gains deduction. This total would be subject to the tax rates contained in the Senate amendment. If liability computed under the alternative minimum tax exceeds that calculated under the present regular income tax, as increased by the present add-on minimum tax, the individual would pay the greater amount.

For the alternative minimum tax the conference agreement adopts the exemption, rates, and computation methods contained in the Senate amendment. In addition, it follows the Senate amendment's definition of adjusted itemized deductions. Thus, under the conference agreement, itemized deductions subject to the preference would exclude medical and casualty deductions (as under present law) plus State and local tax deductions, and, in the case of income in respect of decedents, amounts deducted (under section 691(c)) as estate taxes. The remaining itemized deductions are preferences only to the extent that they exceed 60 percent of adjusted gross income reduced by the medical and casualty deductions, State and local taxes, and the estate tax deduction previously described.

The conference agreement also retains those provisions of the Senate amendment which relate to certain charitable lead trusts and tax credits. Thus, the foreign tax credit is to be allowed against the alternative minimum tax. However, individuals paying the alternative minimum tax are not to obtain the benefit of nonrefundable credits other than the foreign tax credit to the extent of that individual's alternative minimum tax. Investment credit and jobs credit carryovers to future years, from a year in which the taxpayer is liable for some amount of alternative minimum tax, are not to be reduced to the extent the alternative minimum to the extent the alternative minimum tax liability reduced the benefit of these credits.

In the case of trusts and estates, the conference agreement provides special rules for the reduction of the exemption and the treatment of preference items.

Because the conference agreement retains the present add-on minimum tax with respect to deferral preferences, the agreement does not adopt that part of the Senate amendment which would allow new elections in the case of intangible drilling costs and stock options.

The conference agreement makes permanent the preference for intangible drilling costs in excess of oil income which was adopted for 1977 by the Tax Reduction and Simplification Act of 1977. Under the conference agreement, intangible drilling costs deductions would be included in the minimum tax base of individuals only to the extent that those costs, over the portion of those costs amortizable on the basis of a 10-year life or under cost depletion, exceed the taxpayer's income from oil and gas properties. Income from oil and gas properties

is to be determined first with regard to the rules for determining gross income from oil and gas properties for purposes of percentage depletion (sec. 613(a) of the Code, without regard to the limitations under sec. 613A). Net income from oil and gas properties is gross income from those properties reduced by the amount of deductions (other than intangible drilling costs subject to the preference) properly attributable to that gross income. The conferees also clarified that under the provision deductions attributable to properties with no gross income are not to be taken into account for purposes of computing net income from oil and gas properties.

The conference agreement follows the House bill and the Senate amendment in providing that no amount of gain from the sale of principal residence is included as a preference item under the alternative minimum tax (or under the present minimum tax for sales in November and December, 1978).

The capital gains preference is conformed to the increased capital gains deduction provided in the conference agreement. (This change in the capital gains preference also is made with respect to the increased deduction allowed for gains from sales or exchanges occurring in November and December 1978, which is treated as a preference under the present law minimum tax.)

In general, the conference agreement is effective for taxable years beginning after 1978. In addition, the provision is not to be treated as a change of the tax rate (under sec. 21 of the Code). Consequently, fiscal year taxpayers are to be subject first to the alternative minimum tax for their taxable years beginning in 1979. The conference agreement provisions changing the effective date for the capital gains preference (to 60 percent of net capital gain) for purposes of the present minimum tax is to apply for all sales and exchanges taking place after October 31, 1978.

For purposes of both effective dates, payments received after the effective date with respect to pre-effective date installment sales are to be taxed under the new provisions applicable generally to sales made after the effective date.

81b. Corporate minimum tax

House bill.—Under present law, a 15 percent minimum tax is imposed on the sum of a corporation's tax preferences less the greater of $10,000 or the full amount of the corporation's regular tax. Generally, the tax preference items are the same for corporations as they are for individuals. However, corporate minimum tax preference items differ in the following respect: (1) the capital gains preference is 18/48th of net capital gains, (2) certain reserves for losses on bad debts of financial institutions are preference items, and (3) the individual preferences for itemized deductions, accelerated depreciation on leased personal property, and intangible drilling costs do not apply to corporations,

The House bill, for taxable years beginning after December 31, 1978, eliminates corporate capital gains as an item of tax preference.

Senate amendment.—No provision.

Conference agreement.—The conference agreement does not contain this provision, and thus corporate capital gains remain an item of tax preference.

B. Maximum Tax Provisions

82a. Limitation on personal service incomes

House bill.—No provision.

Senate amendment.—Under present law the maximum marginal tax rate on taxable income for personal services is 50 percent. Income from personal services includes wages, salaries, professional fees and other compensation for personal services. In the case of an individual engaged in a trade or business where both personal services and capital are material income producing factors, a reasonable allowance for personal services is treated as personal service income but the amount cannot exceed 30 percent of the income from the business.

The Senate amendment, effective for taxable years beginning after December 31, 1978, removes the 30-percent limitation on the amount of income from a trade or business that can be treated as personal services income where capital is an income-producing factor. Instead, individual taxpayers would receive the benefits of the 50-percent maximum tax on earned income only for income that constitutes a reasonable compensation for the services they actually render whether or not they conduct their businesses in corporate form. In making this determination, the reasonable compensation paid for personal services actually rendered would be allowed. However, an individual would not be permitted to convert into personal service income passive income on investments or assets held or used in a trade or business. Whether there has been such a conversion of passive income to personal service income must be determined by reference to all the facts of each case. For example, a sole proprietor of a small manufacturing business cannot treat dividend and interest income received on investments held by him as personal service income. If passive income is derived from investments held by a trade or business, expenses of the trade or business must be allocated between such passive income and the income available for payment as personal service income.

Conference agreement.—The conference agreement adopts the provisions of the Senate amendment.

82b. Tax preference offset

House bill.—Under present law the highest marginal tax rate of personal service income is 50 percent. However, the amount eligible for this maximum tax rate is reduced dollar-for-dollar by the individual's items of tax preference, including capital gains, for the year.

The House bill removes the capital gains tax preference offset of the amount eligible for the maximum tax. This provision is effective for taxable years beginning after December 31, 1978.

Senate amendment.—Same as the House bill, except that the provision is effective with respect to sales and exchanges after October 31, 1978 in taxable years ending after that date.

Conference agreement.—The conference agreement adopts the provisions of the House bill and the Senate amendment, effective with respect to sales and exchanges after October 31, 1978 in taxable years ending after that date.

VIII. OTHER TAX PROVISIONS

83. Employment status of independent contractors and employees

House bill.—No provision.

Senate amendment.—Under present law, the classification of particular workers or classes of workers as employees or independent contractors for purposes of Federal income tax withholding, social security (FICA) taxes and unemployment (FUTA) taxes is made under the common law test of control.

The Senate amendment prohibits the IRS from applying any new or changed position with respect to an individual's status for employment tax purposes, if the position is inconsistent with a pre-1976 general audit position, ruling, or regulation. The amendment also prohibits IRS reclassifications of individuals whom taxpayers in good faith treated as independent contractors provided the taxpayers fulfilled tax filing requirements. These provisions apply for all calendar quarters, for which as of date of enactment, an assessment or refund with respect to employment taxes is not barred.

Conference agreement.—The conference agreement is substantially the same as the Senate amendment. However, for technical reasons, the agreement generally follows the text of H.R. 14159, reported by the Committee on Ways and Means on October 10, 1978 (H. Rep. No. 95–1748). The agreement terminates pre-1979 employment tax liabilities of taxpayers who had a reasonable basis for treating workers other than as employees and who file all required federal tax returns for periods after December 31, 1978; (2) extends relief prospectively through 1979 for taxpayers having a reasonable basis for their classification of workers; and (3) prohibits the issuance of regulations and Revenue Rulings on common law employment status before 1980. The provision becomes effective upon enactment.

84. Employer reporting requirements with respect to charged tips

House bill.—No provision.

Senate amendment.—Present law requires an employee to report tips, including charged tips, to his or her employer. The employer must report to the IRS tips actually reported to the employer by the employee and, under IRS rulings issued in 1975 and 1976, any charge account tips not reported to the employer by the employee. In the Tax Reform Act of 1976, the Congress prohibited the IRS from following, prior to 1979, these rulings.

The Senate amendment provides that the only employee tips which an employer must report to the IRS are those reported to the employer by employees. Also, the amendment provides that, with respect to the amount of tips paid to a particular employee, the only records of charged tips which an employer may be required to keep are charge receipts and copies of tip statements furnished by employees.

Conference agreement.—The conference agreement follows the Senate amendment.

85. Deferral of carryover basis rules

House bill.—No provision.

Senate amendment.—Under the Tax Reform Act of 1976, the basis of property passing from a decedent is "carried over" from the decedent to the estate or heir. Adjustments to basis are made for death taxes, pre-1977 appreciation, and a $60,000 minimum basis. The provision applies with respect to property passing from decedents dying after December 31, 1976. The Senate amendment postpones the effective date of the carryover basis provisions so that they will only apply to property passing from decedents dying after December 31, 1979.

For estates of decedents dying after 1976 and before the date of enactment of the bill, an executor is permitted to elect the carryover basis rules. If elected, the basis of all property passing from the decedent would be determined under the carryover rules (including property that is not sold or distributed before the date of enactment of the bill). The election is to be irrevocably made within 120 days following the date of enactment of the bill and in the manner prescribed by the Secretary of the Treasury.

Conference agreement.—The conference agreement follows the Senate amendment for the postponement of the carryover basis provisions but eliminates the election.

86. Jointly-owned farms and closely held businesses

House bill.—No provision.

Senate amendment.—Under present estate tax law, the value of a joint tenancy with rights of survivorship is included in the joint tenant's gross estate except for the portion of the value shown to be attributable to consideration furnished by the surviving joint tenant. The Senate amendment provides a special rule for excluding a portion of the value of jointly owned property used in a farm or other business. The exclusion is based on the number of years the surviving joint tenant martially participated in the business. The provision applies only to a joint interest in property held by a husband and wife.

The amount excludible would be determined by applying a percentage rate of 2 percent for each year the surviving spouse materially participated in the business (not to exceed 50 percent) to the excess of the value of the joint interest over the amount attributable to the original consideration furnished. For this purpose, the amount attributable to the original consideration would consist of the amount of that consideration plus assumed appreciation at the rate of 6 percent simple interest for the period of investment of the consideration.

The amount by which the value of a joint interest includible in the gross estate may be reduced under the Senate amendment is limited to $500,000.

The provision is to apply if elected by the executor of the estate not later than the time for filing the estate tax return (including extensions) and in the manner prescribed under Treasury regulations.

The provision is to apply with respect to estates of decedents dying after December 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment.

87. Source of interest income on Puerto Rican branches of U.S. savings and loan associations.

House bill.—No provision. (However, the House has passed H.R. 13758, the same as the Senate provision.)

Senate amendment.—U.S. citizens and resident aliens residing in Puerto Rico generally are subject to U.S. tax on all of their income other than Puerto Rican source income. U.S. corporations qualifying under section 936 are entitled to a "possessions" credit against any U.S. tax on foreign source income of their U.S. possessions businesses, and on certain investment income from U.S. possession sources.

Generally, interest received from a U.S. corporation is treated entirely (or, in some cases, partially) as U.S. source income and thus does not qualify for the special tax treatment described above. However, interest on deposits with a foreign branch of a U.S. commercial bank, including a branch located in Puerto Rico, is treated as income from sources within that foreign locality. As a result, interest paid by Puerto Rico branches of a U.S. commercial bank generally qualifies for the special treatment provided Puerto Rican residents and possessions corporations. This exception for foreign branches of U.S. banks does not extend to similar branches of U.S. savings and loan associations.

The Senate amendment extends the special source rule for interest on deposits in foreign branches of U.S. commercial banks to interest on deposits in similar branches of U.S. savings and loan associations. As a result, interest from Puerto Rican branches of U.S. savings and loan associations will be treated as Puerto Rican source income, and thus will qualify for special treatment afforded Puerto Rican source income. The amendment is effective for taxable years of recipients of the interest beginning after the date of enactment.

Conference agreement.—The conference agreement follows the Senate amendment.

88. Reduction in excise tax on investment income of private foundations

House bill.—No provision. (However, H.R. 112, as passed by the House, would reduce the rate of the excise tax on the net investment income of domestic private foundations from 4 percent to 2 percent.)

Senate amendment.—The Senate amendment reduces the rate of the excise tax on the net investment income of domestic private foundations from 4 percent to 2 percent.

Conference agreement.—The conference agreement follows the Senate amendment.

89. State tax credit against Federal slot machine tax

House bill.—No provision.

Senate amendment.—Under present law, there is an annual Federal excise tax of $250 on each slot machine or other coin-operated gaming device. Up to 80 percent of the Federal tax can be offset by similar State taxes. The Senate amendment increases the Senate credit against the Federal slot machine excise tax from 80 to 95 percent for years ending June 30, 1979, and June 30, 1980. The Federal excise tax is repealed after June 30, 1980.

Conference agreement.—The conference agreement follows the Senate amendment.

90. Study of taxation of foreign owners of U.S. real estate

House bill.—No provision.

Senate amendment.—Under the Code, nonresident aliens and foreign corporations are subject to a flat 30-percent tax on their gross current income from U.S. real estate investments not connected with an active business in the United States. However, they are exempt from capital gains tax on the sale of capital assets generally, and nonbusiness U.S. real estate in particular. They may elect to be taxed on a net basis on their current income from nonbusiness real estate in the same manner as U.S. persons but, as a condition, must agree to be taxable on any gains from the sale of that real estate. Foreign investors can generally avoid most or all U.S. taxes on U.S. real estate, including both taxes on current income and gain on the sale, by utilizing U.S. tax treaties.

The Senate amendment directs the Treasury Department to submit a study to Congress within 6 months of the date of enactment on the taxation of foreign owners of U.S. property for the purpose of determining the appropriate tax treatment of income or gain from U.S. property.

Conference agreement.—The conference agreement follows the Senate amendment.

91. Excessive Government spending surtax

House bill.—No provision.

Senate amendment.—Under present law, tax changes generally are not related directly to government spending levels, except that certain trust fund taxes have been changed when related expenditures have been increased or decreased.

The Senate amendment imposes an income tax surcharge if Federal spending, except in the case of war or recession, exceeds specified limits. The surtax is to be the rate necessary to finance the Federal spending in excess of the limit, after adjustment for inflation. The provision is to be effective upon enactment, but no surtax could apply prior to calendar year 1980.

Conference agreement.—The conference agreement does not contain this provision.

92. Charitable split interest trusts

House bill.—No provision.

Senate amendment.—The Tax Reform Act of 1969 imposed new requirements that must be met in order for a charitable deduction to be allowed for income, gift, and estate tax purposes for the transfer of a split interest to charity (i.e., part charitable and part noncharitable). In the case of a remainder interest in trust, the interest passing to charity must be in either a charitable remainder annuity trust, a charitable remainder unitrust, or a pooled income fund. In the case of an "income" interest passing to charity (i.e., a charitable lead trust), the "income" interest must be either a guaranteed annuity or a fixed percentage of the fair market value of the trust (determined at least annually).

Many persons have created instruments that do not comply with these new requirements. As a result, Congress provided, as early as

1974, that the governing instruments of charitable remainder trusts could be amended to meet the new rules within certain time limitations for estate tax purposes. The latest extension of these time limitations was made by the Tax Reform Act of 1976 which permitted amendment of charitable remainder trusts until December 31, 1977, in order to qualify the trust for the charitable estate tax deduction. However, it provided this relief only in the case of the charitable deduction for estate tax purposes and only for remainder interests passing to charity. No relief was provided for the charitable deduction for income or gift tax purposes or for "income" interests passing to charity for income, gift or estate tax purposes.

The Senate amendment would extend until December 31, 1978, the time to amend (or to commence judicial proceedings to amend) instruments establishing charitable remainder trusts which were enacted before December 31, 1977, to comply with the requirements of the Tax Reform Act of 1969 in order for a charitable deduction to be allowed for estate tax purposes. The amendment would also provide that instruments establishing charitable lead trusts and charitable remainder trusts in the case of income and gift taxes, which were created before December 31, 1977, could be amended to comply with the requirements of the 1969 Act if the instrument is amended (or judicial proceedings to amend are commenced) by December 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment.

93. Attribution rules for extension of time to pay estate tax

House bill.—No provision.

Senate amendment.—Under present law, an executor can elect a 15-year period for the payment of the estate tax attributable to the decedent's interest in a closely held business if the value of that interest exceeds 65 percent of the value of the gross estate. Pursuant to such an election, principal (but not interest) payments may be deferred for up to 5 years from the date of the estate tax return, and a special 4-percent interest rate is allowed on the estate tax attributable to the first $1 million of the business interest. For this purpose, a closely held business means an interest as (1) a sole proprietorship, (2) a partner in a partnership (a) having 15 or fewer partners, or (b) in which the decedent owned 20 percent or more of the capital, or (3) stock in a corporation (a) having 15 or fewer shareholders, or (b) in which the decedent owned 20 percent or more of the voting stock.

In determining the number of partners or shareholders, each individual is counted once without regard to any attribution rules.

In addition, if the value of the business is in excess of either 35 percent of the value of the gross estate or 50 percent of the value of the taxable estate, a 10-year extended payment period may be used.

Moreover, where reasonable cause for an extension exists, the Service has the discretion to extend the payment period for up to 10 years.

The Senate amendment provides that stock or partnership interests held by the decedent's family is to be treated as being held by a single shareholder or partner for purposes of determining eligibility for the extended estate tax payment provisions.

This provision applies to the estates of decedents dying after the date of enactment.

Conference agreement.—The conference agreement adopts the provisions of the Senate amendment.

94. Exemption from private foundation tax for failure to distribute income

House bill.—No provision.

Senate amendment.—Under present law the term "private foundation" means any charitable, educational, religious, or other organization described in section 501(c)(3), *other than* certain specified categories of organizations (sec. 509(a) of the Code). These categories (known as "public charities") include churches, schools, hospitals or certain medical research organizations, certain other organizations which receive specified "public" support, and organizations which are "supporting" organizations to other public charities. For this purpose, under Treasury regulations, the term "hospital" does not include "convalescent homes or homes for children or the aged, nor does the term include institutions whose principal purpose or function is to train handicapped individuals to pursue some vocation" (Reg. sec. 1.170A–9(c)(1)).

In addition to other restrictions on private foundations, a private foundation is required to make annual expenditures or distributions for exempt purposes generally equal to the net income of the private foundation. However, an exception to this rule is provided for certain private foundations known as "operating foundations." A private foundation may qualify as an "operating" foundation if it spends directly for the active conduct of its exempt-purpose activities amounts which are at least equal to 85 percent of its adjusted net income, and which are at least equal to 3⅓ percent of its net endowment assets, or if the foundation meets certain other tests (sec. 4942(j)(3)).

In general, the rules relating to income tax deductions by individuals for contributions to public charities or to private operating foundations are more favorable to the donor than the rules relating to the deductibility of contributions to private non-operating foundations (sec. 170).

The Senate amendment provides that certain private foundations which provide long-term care facilities are not subject to the general requirement that a private foundation spend its net income for exempt purposes (sec. 4942). However, all of the other rules governing private foundations (including rules governing deductibility of contributions) will continue to apply. In order to qualify for this exception the private foundation must, on or before May 26, 1969, and continuously thereafter to the close of the taxable year, operate and maintain as its principal functional purpose facilities for the loug-term care, comfort, maintenance, or education of permanently and totally disabled persons, elderly persons, needy widows, or children.

Conference agreement.—The conference agreement basically adopts the Senate amendment. Under the conference agreement, only for purposes of the distribution requirements of section 4942, an "operating foundation" includes a private foundation which, on or before May 26, 1969, and continuously thereafter to the the close of the taxable year, operates and maintains as its principal functional purpose facilities for the long-term care, comfort, maintenance, or education of permanently and totally disabled persons, elderly persons, needy widows, or children if the foundation meets the distribution requirements applicable to operating foundations (sec. 4942(j)(3)(B)(ii)). Since this rule applies only for purposes of the distribution require-

ment, the rules for deductibility of contributions to such an organization will be determined as if the organization is a nonoperating private foundation (unless it meets the regular definition of a public charity or operating foundation).

95. Small tax case procedures before the Tax Court

House bill.—No provision.

Senate amendment.—Under present law, taxpayers who file a petition with the Tax Court for a redetermination of income, estate, or gift tax deficiencies or overpayments have the option of having their cases heard as small tax cases under an expedited and simplified procedure (sec. 7463). The option, however, is available only where the amount of the deficiency, or claimed overpayment, does not exceed $1,500, and where the cases are approved by the Tax Court. Trials of these cases are conducted informally. The rules of evidence are relaxed and neither party is required to file a brief. In addition, neither party may appeal, and decisions in these cases are not treated as precedents for any other case or purpose.

Typically, small tax cases are heard by commissioners appointed by the chief judge of the Tax Court (sec. 7456(c)). However, the law which provides for the appointment of commissioners does not specifically authorize them to administer oaths, issue subponeas or examine witnesses. Under present law, judges and certain other employees, are authorized to administer oaths and issue subpoeneas, but only judges are authorized to examine witnesses (sec. 7456(a)).

Following the hearing in small tax cases, the commissioners file reports which, upon review by the chief judge, may be adopted as reports of the Court. After a report is filed by the Court, a decision will be entered. The decision is based on the report and is comprised of a computational determination of the deficiency or overpayment.

Under present law, the decision in a small tax case must be entered by a judge, rather than by a commissioner, in accordance with the report of the Tax Court (sec. 7459(a)).

The amendment, in general, increases the jurisdictional amount for election of the small case procedure from $1,500 to $5,000. In the case of a deficiency or overpayment in income taxes, the jurisdictional amount is applicable to each taxable year in dispute. In the case of a gift tax deficiency or overpayment, the jurisdictional amount is applicable with respect to each calendar year. Finally, in the case of an estate tax deficiency or overpayment, the jurisdictional amount is applicable to the total amount of deficiency or overpayment in dispute.

Use of this procedure would continue to be optional with the taxpayer unless the Tax Court decided before the hearing that the case should be heard under normal procedures and should be subject to appeal. Presently, the Tax Court rules provide that the Commissioner of Internal Revenue may file a motion requesting that a small tax case be removed from that category. In view of the proposed increase in the small case jurisdictional amount to $5,000 it is contemplated that, the Tax Court will give careful consideration to a request by the Commissioner of Internal Revenue to remove a case from the small case procedures when the orderly conduct of the work of the Court or the administration of the tax laws would be better served by a regular trial of the case. Thus, in some situations, proper

Court management may require the removal of a case from the small case procedures so that it can be consolidated with a regular case involving common facts or a common issue of law. Similarly, removal of the case from the small case category may be appropriate where a decision in the case will provide a precedent for the disposition of a substantial number of other cases or where an appellate court decision is needed on a significant issue.

Most of the small tax cases are handled by commissioners. It is contemplated that such cases will, in general, continue to be tried before the commissioners, with the Court continuing to have the power to authorize the commissioners to hear other cases (e.g., small tax cases where the taxpayers have not elected the simplified procedures), as was the situation after the enactment of the Tax Reform Act of 1969.

In order to alleviate any uncertainity which exists under present law as to the authority of commissioners to administer oaths, issue subpoenas and to prepare reports of small tax cases proceedings that they conduct, the amendment expressely authorizes commissioners to perform such functions and duties. In addition, in order to further clarify the law with respect to the authority of commissioners, the amendment authorizes commissioners to examine witnesses. Finally, under the amendment, the Tax Court may authorize a commissioner to enter a decision in a small tax case proceeding subject to such conditions of review as the Court may impose by an appropriate rule, directive or order, whether or not published.

The provision of the amendment increasing the jurisdictional amount in small tax cases from $1,500 to $5,000 will be effective on the first day of the first calendar month beginning more than 180 days after the date of the enactment of the bill. The provisions of the bill relating to the powers of commissioners will be effective on the date of enactment.

Conferenec agreement.—The conference agreement follows the Senate amendment.

96. Tax treatment of cooperative housing corporations

House bill.—No provision.

Senate amendment.—Under present law, a tenant-stockholder in a cooperative housing corporation is entitled to deduct amounts paid to the corporation which represents his or her proportionate share of allowable real estate taxes and interest relating to the corporation's land and buildings. (In addition, to the extent a tenant-stockholder uses depreciable property leased from the cooperative housing corporation in a trade or business or for the production of income, the tenant-shareholder is allowed to take depreciation deductions with respect to the stock the ownership of which gives the tenant-stockholder the right to lease such property.) In general, for an organization to qualify to pass through these deductions to tenant-stockholders, 80 percent or more of the gross income of the cooperative housing corporation must have been derived from individual tenant-stockholders. However, for purposes of determining whether the 80 percent test has been satisfied, stock owned and dwelling units leased by governmental entities for the purpose of providing housing facilities are not taken

into account. Further, banks and other lending institutions which which obtain stock in a cooperative housing corporation through foreclosures are treated as tenant-stockholders for up to three years after the date of acquisition.

The Senate amendment provides that if a person (including a corporation) who conveys the houses, apartment building or leasehold thereof to a cooperative housing corporation acquires stock in the corporation by purchase or foreclosure, together with a lease or right to occupy the house or apartment, such person would be treated as a tenant-stockholder for up to three years from the date of acquisition. This provision would apply even though such person or any purchaser from such person could not occupy the apartment or house without prior approval of the corporation or its managing agent.

Conference agreement.—The conference agreement follows the Senate amendment.

97. Tax exemption for certain mutual deposit guaranty organizations

House bill.— No provision.

Senate amendment.—Present law provides an exemption from Federal income taxation for State-chartered, nonprofit mutual corporations or associations organized before September 1, 1957, which provide reserve funds for, and insurance of shares or deposits in, State-chartered (1) domestic building and loan associations ("savings and loan associations"), (2) certain cooperative banks, or (3) mutual savings banks (section 501(c)(14)(B)). The Senate amendment extends Federal income tax exemption retroactively (to 1969) to any State-chartered organization created before January 1, 1969, which provides reserve funds for, and insurance of shares or deposits, in State-chartered savings and loan associations, cooperative banks, or mutual savings banks. The Senate amendment prospectively provides Federal income tax exemption for certain State-chartered organizations created before January 1, 1969, which provide reserve funds for, and insurance of shares or deposits in, both State-chartered credit unions and State-chartered savings and loan associations.

Conference agreement.—The conference agreement omits this provision of the Senate amendment.

98. Tax treatment of magazines, etc., returned after the close of the accounting year

House bill.—No provision.

Senate amendment.—Under present law, sellers of merchandise who use an accrual method of accounting generally must include sales proceeds in income for the taxable year when all events have occurred that fix the right to receive the income and the amount can be determined with reasonable accuracy. The Internal Revenue Service has taken the position that accrual-basis publishers and distributors of magazines, paperbacks, or records must include the sales proceeds of these items in income when they are shipped to purchasers, and may reduce income for returns only in the year the items are returned unsold by the purchaser.

The Senate amendment permits an accrual-basis publisher or distributor of magazines, paperbacks, or records to elect to exclude from income amounts attributable to qualifying items returned within the merchandise return period, which is 2 months and 15 days in the

case of magazines, and 4 months and 15 days in the case of paperbacks and records, after the close of the taxable year in which the sales of the items were made. The taxpayer may initially select a shorter merchandise return period, but is required to consistently use the shorter period.

Also under present law, when a taxpayer changes a method of accounting, certain adjustments (called transitional adjustments) are often required to prevent the duplication or omission of an item of income or deduction. These transitional adjustments are subject to special rules that generally prescribe that the amount of adjustment is to be taken into income (or claimed as a deduction) ratably over 10 years, beginning with the year in which the change in method of accounting occurs.

The election of the method of accounting provided in the Senate amendment is a change in method of accounting that gives rise to a transitional adjustment. However, instead of applying the rules of present law regarding the treatment of transitional adjustments, the Senate amendment provides special rules. Under the amendment, the transitional adjustment (usually a deduction under this election) attributable to magazines is amortized over 5 years and the transitional adjustment attributable to paperbacks and records is placed in a suspense account. The effect of the suspense account is to defer the deduction of the transitional adjustment until the taxpayer is no longer in the trade or business of publishing or distributing paperbacks or records. The purpose of the suspense account is to reduce the revenue loss on provisions that allow taxpayers to more nearly conform their tax and financial accounting.

The Senate amendment is effective for taxable years beginning after September 30, 1979. The amendment is identical to a House passed bill (H.R. 3050), except for the effective date and a minor change that allows taxpayers to initially select a shorter merchandise return period, even though regulations have not been issued.

Conference agreement.—The conference agreement follows the Senate amendment.

99. Accounting treatment for discount coupons redeemed after the close of the taxable year

House bill.—No provision.

Senate amendment.—Under present Treasury regulations specifying the appropriate taxable year for inclusion of income items, accrual-basis issuers of premium coupons with sales may reduce gross receipts by the estimated cost of redeeming such coupons outstanding at the close of the taxable year (plus the cost of redeeming coupons during the taxable year that have not previously been taken into account.) The term "premium coupon" is not defined in the regulations, and the courts have not directly addressed the question of what constitutes a premium coupon. The Internal Revenue Service has issued two revenue rulings that deny the application of the regulation to two types of coupons that give consumers "cents off" or other discounts on the purchase price of specified merchandise.

The Senate amendment provides a special accounting rule that allows certain issuers of qualified discount coupons to elect to deduct for a taxable year the cost of redeeming qualified discount coupons

that are (1) outstanding at the close of the taxable year, and (2) redeemed within 6 months after the close of the taxable year, plus the cost (if not previously taken into account) of redeeming discount coupons received during the year. This rule only applies to discount coupons and does not affect the tax treatment of premium coupons.

Also under present law, when a taxpayer changes a method of accounting, certain adjustments (called transitional adjustments) are often required to prevent the duplication or omission of an item of income or deduction. These transitional adjustments are subject to special rules that generally prescribe that the amount of adjustment is to be taken into income (or claimed as a deduction) ratably over 10 years, beginning with the year in which the change in method of accounting occurs.

The election of the method of accounting provided in the Senate amendment is a change in method of accounting that gives rise to a transitional adjustment. However, instead of applying the rules of present law regarding the treatment of transitional adjustments, the Senate amendment provides special rules. Under the amendment a transitional adjustment that would increase taxable income is taken into income ratably over a period of 10 years, beginning with the year in which the change in method of accounting occurs. A transitional adjustment that would decrease taxable income is placed in a suspense account. The effect of the suspense account is to defer the deduction of the transitional adjustment until the taxpayer no longer issues discount coupons in connection with his trade or business. The purpose of the suspense account is to reduce the revenue loss on provisions that allow taxpayers to more nearly conform their tax and financial accounting.

The Senate amendment also allows taxpayers who, in prior years, have accounted for discount coupons under the existing premium coupon regulations to elect to treat their method of accounting as a proper method for those years. If a taxpayer makes this second election within a specified period of time, and it covers all discount coupons issued in those prior years, then he will not be required to establish the suspense account. Instead, the present law rules relating to transitional adjustments would apply to the transitional adjustment.

The Senate amendment is effective for taxable years ending after December 31, 1978. The amendment is identical to a House passed bill (H.R. 13047).

Conference agreement.—The conference agreement follows the Senate amendment.

100. Exemption from highway use tax for certain farm and soil and water conservation trucks

House bill.—No provision.

Senate amendment.—Under present law, an annual highway use tax of $3 per 1,000 pounds is imposed on the use of highway motor vehicles having a group weight in excess of 26,000.

The Senate amendment exempts certain farm and soil and water conservation trucks from the highway use tax. The exemption would not apply to any vehicle registered in the name of a corporation the gross receipts of which for the last taxable year exceeded $950,000,

or which derived more than 50 percent of its gross receipts for the year from activities other than farming or soil and water conservation.

This provision applies to uses after the first day of the first month which begins more than 30 days after the date of enactment.

Conference agreement.—The conference agreement does not contain this provision.

101. Taxation of foreign investors on sale of certain U.S. real estate

House bill.—No provision.

Senate amendment.—Under the Code, nonresident aliens and foreign corporations are subject to a flat 30-percent tax on their gross current income from U.S. real estate investments not connected with an active business in the United States. However, they are exempt from capital gains tax on the sale of capital assets generally, and nonbusiness U.S. real estate in particular. They may elect to be taxed on a net basis on their current income from nonbusiness real estate in the same manner as U.S. persons but, as a condition, must agree to be taxable on any gains from the sale of that real estate. Foreign investors can generally avoid most or all U.S. taxes on U.S. real estate, including both taxes on current income and gain on the sale, by utilizing U.S. tax treaties.

The Senate amendment provides that nonresident aliens and foreign corporations would be taxed on gains from the sale of farmland and other rural land (as defined in the Consolidated Farm and Rural Development Act) which is not connected with an active business in the United States. These changes would apply to sales of stock in a corporation formed or availed of to acquire, hold, or sell such land.

The amendment generally is effective for sales in taxable years beginning after December 31, 1978. However, there is a 5-year delay for sales of property acquired prior to enactment if there is a contrary U.S. tax treaty obligation.

Conference agreement.—The conference agreement omits the Senate amendment.

102. Alaska Native Claims Settlement Act corporations

House bill.—No provision.

Senate amendment.—Corporations formed pursuant to the Alaska Native Claims Settlement Act (ANCSA) received money from the United States and the right to select Alaskan land. The shareholders are Alaska Natives. The IRS has held that (1) the value of surveys of the land made by oil companies to assist the corporations in making their selections is income to the corporations; (2) land selection costs incurred by the corporations are not deductible but must be added to the basis for the land; and (3) other expenses of the corporations are nondeductible "start-up" costs because the corporations have not yet begun business. Because many Native shareholders are related to one another, some corporations may meet the definition of personal holding companies.

The Senate amendment provides that ANSCA corporations (1) do not include in income the value of outside surveys; (2) may deduct land selection costs; (3) are deemed to have begun business; and (4) are not personal holding companies.

The amendment is effective as of December 18, 1971. The survey income provision would remain in effect until the earlier of 1991 or the date the corporation has received all its land under ANSCA. The personal holding company provision would remain in effect until 1991.

Conference agreement.—The conference agreement follows the Senate amendment.

103. Technical corrections to the Tax Reform Act of 1976

House bill.—No provision.

Senate amendment.—The Tax Reform Act of 1976 made numerous changes to the Internal Revenue Code of 1954. H.R. 6715, the Technical Corrections bill, which has passed the House, would make technical, clerical, conforming, and clarifying amendments to the provisions enacted by the Tax Reform Act of 1976. The Senate amendment includes the provisions of H.R. 6715, as passed by the House, with a number of modifications. The principal modifications are as follows:

The effective date for the provision under which community property laws are to be disregarded for purposes of determining eligibility for, and the amount of, the elderly credit would be postponed for one year so that it would apply to taxable years beginning after 1977 (rather than 1976).

The exemption from minimum tax preference treatment of excess itemized deductions for charitable deductions from a trust would be changed to apply to deductions attributable to transfers before 1977 (rather than before 1976).

Charitable distributions by certain testamentary trusts would not be treated as an itemized deduction for purposes of the minimum tax preference for excess itemized deductions.

In certain limited circumstances, retroactive decertification of buildings without historic significance would be permitted so that disallowance of deductions for the demolition of a historic structure would not apply.

Rapid amortization would be allowed with respect to rehabilitation expenditures incurred by certain long-term lessees of historic structures.

A U.S. citizen residing abroad would not be subject to the foreign convention rules with respect to a convention held in the country in which the citizen resides.

An exception to the vacation home disallowance rules would be provided so that personal use of a residence would not be taken into account for a taxable year in which the residence is converted to rental property.

The real estate exception from the partnership at risk rules would be clarified to make it clear that the exception applies where services are rendered in connection with providing living accommodations, i.e., to hotels, motels, and similar establishments.

The provision of the House bill which would have restricted the 6-month long-term capital gain holding period to agricultural commodities futures contracts is deleted so that all commodities futures contracts are eligible for the 6-month holding period rule.

The amount recaptured as ordinary income under the special rules for depreciable player contracts sold by a sports franchise would be limited to depreciation allowable after 1975.

The treatment of certain members of a fishing boat crew as self-employed individuals would be extended to cover services performed prior to 1972.

The penalty imposed upon income tax return preparers for the intentional disregard of rules and regulations would not apply with respect to an Internal Revenue Service ruling.

A technical change would be made to make it clear that capital asset treatment would not apply to U.S. Government publications which are received by a taxpayer free of charge or at a reduced rate.

The amendment would permit the tax-free sale of a truck part if it is to be resold by the purchaser in connection with the first retail sale of a light-duty truck.

Conforming changes would be made to reflect the postponement of the carryover basis provisions under another provision of the Senate amendment.

The effective date of the generation-skipping provisions of the 1976 Act would be changed to apply to transfers made after June 11, 1976 (rather than April 30, 1976).

Technical changes are made to the definition of a "subordinate trustee" for purposes of excepting a power held by an independent trustee under the generation-skipping transfer provision.

The time for conforming governing instruments for split-interest trusts for charitable deduction purposes would be extended until the end of 1978 (rather than 1977). The provision would not apply to charitable remainder trusts with respect to the estate tax charitable deduction. (However, another Senate amendment provides a similar extension for these trusts and for charitable remainder trusts.)

The effective dates of the amendment generally are the same as the respective effective dates of the Tax Reform Act of 1976.

Conference agreement.—The conference agreement follows the Senate amendment but for two exceptions. Since the date for conforming governing instruments for charitable split-interest trusts is extended through 1978 under another provision of the bill, the similar provision under the technical corrections title is deleted.

In addition, the Senate amendment provision relating to tax return preparers is deleted. It is intended that if a preparer in good faith and with reasonable basis takes the position that a rule or regulation does not accurately reflect the Code and does not follow it, the preparer has not negligently or intentionally disregarded the rule or regulation. This test shall be applied in the same manner as it is applied under section 6653(a) and the regulations thereunder (relating to disregard of rules and regulations by taxpayers). For example, if a preparer reasonably takes the position in good faith that a revenue ruling does not accurately reflect the Code, the preparation of a return or claim for refund by the preparer in conflict with the revenue ruling is not a negligent or intentional disregard of the revenue ruling. For purposes of section 6694(a), the view of the taxpayer concerning a rule or regulation is not material.

The conferees further direct that the Internal Revenue Service shall reasonably interpret section 6694(a) according to the standards of section 6653(a) and in light of all the facts and circumstances of each case, taking into account any and all mitigating factors.

104. Industrial development bonds for urban development action grant (UDAG) facilities

House bill.—No provision.

Senate amendment.—Under present law, interest on industrial development bonds is, in general, taxable. However, interest on certain small issues of industrial development bonds is tax-exempt. Small issues are issues of $1 million or less the proceeds of which are used for the acquisition, construction of land, or depreciable property. At the election of the issuer the $1 million limitation can be increased to $5 million. If this election is made, capital expenditures and the total of a series of small issues for a project cannot exceed $5 million.

Section 321 of the House bill increases the amount of the elective small issues limitation from $5 million to $10 million. Senate Amendment Number 48 increases the amount of this limitation for $5 million to $12 million. This Senate amendment provides that the total amount of capital expenditures with respect to certain facilities financed with tax-exempt "small issue" industrial development bonds shall be $20 million. However, the limitation on elective small issues would continue to apply to limit the amount of these capital expenditures which could be financed with tax-exempt bonds.

However, the amendment would apply only with respect to a small issue substantially all the proceeds of which are to be used to provide facilities with respect to which an urban development action grant has been made.

The amendment applies to taxable years ending after October 1, 1979, but only with respect to obligations issued after such date.

It also specifies that the higher limitation is to apply to capital expenditures made after October 1, 1979, with respect to bonds that were issued prior to October 1, 1979.

Conference agreement.—The conference agreement follows the Senate amendment under which the capital expenditure limitation test for urban development action grant facilities is $20 million. As incidated under Senate Amendment No. 48, the conferees agreed to increase the elective small issue limitation to $10 million. Under that $10 million limitation up to $10 million of tax-exempt small issue industrial development bonds could be issued to finance an urban facility action grant facility. In addition to this $10 million exempt bond financing the principal user of the facility could also make capital expenditures of $10 million financed with funds received from sources other than tax-exempt bonds.

105. Subordination of special liens for additional estate tax attributable to special valuation property

House bill.—No provision.

Senate amendment.—Present law provides an estate tax election pursuant to which certain qualifying property may be valued at actual use rather than at its fair market value (sec. 2032A). Where this election is made, a special lien arises on the property (sec. 6324B), and continues until the earlier of the recapture of the tax benefit, or the termination of potential liability for recapture (*i.e.*, the death of a qualified heir, or the expiration of a 15-year period from the decedent's death). The Treasury Department is to issue regulations under which other security could be substituted for the real property.

The Senate amendment, effective with respect to estates of decedents who die after December 31, 1976, permits the subordination of the special lien for additional estate tax attributable to the special valuation of a farm or other qualified real property where the Secretary of the Treasury is satisfied that the interests of the U.S. are protected adequately after the subordination.

Conference agreement.—The conference agreement adopts the Senate amendment.

106. 10-year carryback of product liability net operating losses

House bill.—No provision.

Senate amendment.—Under present law, net operating losses incurred in a taxable year generally may be "carried back" and offset against taxable income of the 3 years first preceding the year of loss and, if not fully absorbed, "carried forward" and offset against taxable income of the 7 years next succeeding the year of loss. Losses offset against taxable income in carryback years generally result in tax refunds, and losses offset against taxable income in future years generally result in decreases in tax liabilities for those years.

Under the Senate amendment, the amount of a net operating loss that is attributable to a product liability loss could be carried back an additional 7 years. Thus, in total, the product liability loss could be carried back to the 10 years first preceding the loss year and carried forward to the 7 years next succeeding the loss year. A taxpayer could elect not to apply this special carryback rule and, instead to carry the entire net operating loss back 3 years and forward 7 years as under present law. The amount of a net operating loss that is attributable to a product liability loss is the lesser of (1) the sum of the product liability losses deductible for the taxable year, or (2) the net operating loss (reduced by any portion thereof that is attributable to a foreign expropriation loss) for the taxable year.[1]

Product liability losses include not only the liability for damages under product liability claims, but also the expenses incurred in the investigation or settlement of, or opposition to, product liability claims. Indirect corporate expense, or overhead, is not to be allocated to product liability claims so as to become a product liability loss. Only expenses directly incurred in connection with the product liability claim are to be included in determining the amount of the product liability losses for the year.

The definition of product liability under the Senate amendment is intended to include the kinds of damages that are recoverable under prevalent theories of product liability. The laws of the several states regarding product liability are not uniform, but it is believed that the

[1] The operation of this rule is illustrated as follows: Assume a taxpayer incurs a net operating loss for the taxable year of $80,000, of which $60,000 is attributable to a product liability loss. Assume further that taxable income for each of the 10 years immediately preceding the loss year is $5,000. The product liability loss of $60,000 may first be carried back to the 10th through the 4th preceding years, thus absorbing $35,000 of the loss. The remaining $25,000 of product liability loss is added to the "regular" net operating loss of $20,000 (for a total of $45,000) and is carried to the 3rd through 1st preceding years, which utilizes $15,000 of the loss. The remaining loss ($30,000) is carried forward to future years under present law rules, without regard to the source of the loss. Of course, in computing the amount of loss that may be carried from one preceding year to another, the normal adjustments under section 172 (such as the adjustment for the capital gain exclusion or excess of nonbusiness deductions over nonbusiness income) would continue to be applicable even in the extended carryback years.

definition of product liability provided in the amendment is sufficiently broad to encompass the kinds of damages that may be recovered under product liability theories in most states. If a type of injury or damage included within the definition of the amendment (such as emotional harm without physical injury) it is to be considered a product liability loss (assuming it otherwise qualifies) even though it may not be recoverable under State law. Thus, if a taxpayer settles out of court on such a claim, the payment may be classified as a product liability loss even though the law of the State would not then have allowed recovery.

The definition of product liability in the amendment does not include liabilities arising under warranty, which essentially are contract liabilities. Nor does the definition include liabilities based on services performed by the taxpayer. For example, medical or legal malpractice is not a product liability under the definition. Where both product and services are an integral part of the transaction, such as in the sale and installation of a boiler by the taxpayer, no product liability arises under the definition until all operations have been completed (or terminated) and the taxpayer has relinquished possession of the product. If the loss occurs prior to that point in time, it is not a product liability loss under the definition.

The Senate amendment also makes it clear that self-insurance of product liability risks is a business need for which earnings and profits may be accumulated to a reasonable extent without imposition of the tax on unreasonable accumulation of earnings. This amendment is consistent with, and merely clarifies, present law. Under the amendment, the Secretary of the Treasury will prescribe regulations regarding the determination of the amount that may reasonably be accumulated to meet product liability self-insurance needs. It is expected that the regulations will provide that in determining what is a reasonable accumulation, it is appropriate to take into account the taxpayer's product liability experience, the extent of its commercial coverage for product liability, and the tax consequences of the taxpayer's ability to deduct product liability losses and related expenses for income tax purposes. Estimates of product liability claims that may be made against the taxpayer in the future must be reasonable both as to probability of occurrence and amount.

The Senate amendment would be effective for product liability losses deductible in taxable years beginning after September 30, 1979.

Conference agreement.—The conference agreement follows the Senate amendment.

107. Certain cost sharing payments

House bill.—No provision.

Senate amendment.—Under the Senate amendment, an exclusion from gross income would be provided for certain payments received under a number of Federal and State cost-sharing conservation programs. The exclusion would apply to the extent that the Secretary of Agriculture determines that the payment is made primarily for conservation, etc., purposes and only to the extent the Secretary of the Treasury determines that the payment does not increase substantially the annual income of the recipient. Neither a current deduction, depreciation, amortization, depletion, nor the investment credit may be claimed with respect to amounts excluded under this provision.

The basis of any property acquired or improved with such payments would not reflect the amount of such payments. Ordinary income recapture is provided (to the extent of the lesser of the income recognized or the excluded payments) where the property or improvements purchased with such payments are disposed of before the expiration of 20 years. The amount recaptured is reduced 10 percent per year after the first ten years.

Conference agreement.—The conference agreement generally follows the Senate amendment with certain technical changes. The most significant of these changes provides that a payment (or a portion of a payment) will be excluded from income if the Secretary of the Treasury determines that the payment will not increase substantially the annual income from the property with respect to which the payment is made.[1]

108. Claim of right carryback

House bill.—No provision.

Senate amendment.—If a taxpayer includes in income for a prior year an amount received or accrued under a "claim of right," and it subsequently is determined that no such "claim of right" existed then a deduction is allowed for the amount restored to another. This situation may arise, for example, when a utility bills customers based on a temporary rate schedule, and after the rates are finalized by a utility commission in a subsequent year must make rebates to its customers.

The tax benefit (i.e., reduction in current year taxes) that is attributable to this deduction is the greater of the tax reduction that would be realized by treating the item as a deduction in (1) the year it originally was included in income, or (2) the subsequent year in which it was discovered that the claim of right did not exist.

If the greater tax benefit is realized by treating the item as a deduction in the prior year, it may result in a tax benefit greater than the entire tax liability otherwise due in the current year. In this case, the excess benefit is treated as an overpayment of tax in the current year and is refundable. Under present law, however, this refund may not be received for several years, since it is treated as an overpayment of tax for the current year and payment may be postponed until the return for the year is audited.

The Senate amendment provides that a taxpayer may apply for a tentative refund of the amount of an overpayment for a taxable year that is attributable to a claim of right adjustment. The application for tentative refund may not be filed before the taxpayer has filed its income tax return for the taxable year, and must be filed within 12 months after the close of the taxable year. The amendment specifies certain information that must be provided in connection with the application.

Within 90 days after the application is filed (or, if later, within 90 days after the last day of the month in which the tax return for the year in which the overpayment occurs must be filed, including extensions) the Secretary of the Treasury must review the application, determine the amount of the overpayment and apply credit or refund the overpayment to the taxpayer.

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[1] The comparable restriction in the Senate amendment indicated that a payment would be excludible only if the Secretary of the Treasury determines that the payment would not increase substantially the annual income of the recipient.

This application for tentative refund will be administered in a manner similar to the manner prescribed under present law for tentative refunds due to carryback of net operating losses, investment tax credit, etc. Thus, special rules may need to be prescribed by the Secretary of the Treasury to take into account special problems involving consolidated returns.

The amendment applies to tentative refund claims filed on and after the date of enactment.

Conference agreement.—The conference agreement follows the Senate amendment.

109. Revision of disability income exclusion for married taxpayers

House bill.—No provision.

Senate amendment.—Under present law, a disability income exclusion generally is available to taxpayers who have not attained age 65 before the close of the taxable year and who have retired because of permanent and total disability. This exclusion is limited to $100 per week (a maximum of $5,200 a year). The amount of the exclusion is phased out on a dollar-for-dollar basis for taxpayers with adjusted gross incomes greater than $15,000. Thus, a taxpayer with $20,200 or more of adjusted gross income is not entitled to an exclusion.

In order to claim the disability income exclusion, a taxpayer who is married at the close of a taxable year must file a joint return with his or her spouse, unless they have lived apart at all times during that year.

The Senate amendment eliminates the requirement under present law that married taxpayers claiming the disability income exclusion must file a joint return. Thus, under the Senate amendment, if a married taxpayer filed a separate return, the phase-out of the exclusion for adjusted gross income over $15,000 would be computed without regard to any income of the other spouse.

Conference agreement.—The conference agreement does not contain this provision.

110. Conditional tax reductions based on limited Federal spending

House bill.—No provision

Senate amendment.—Under present law, individual income tax rate reductions are not linked directly to Federal spending.

The Senate amendment provides individual income tax reductions for 1980–1983 if: (1) total Federal outlays, as agreed to in the appropriate fiscal year budget resolution, do not exceed the following percentages of the projected gross national product:

Fiscal year:	*Percent*
1980	21.0
1981	20.3
1982	19.6
1983	19.0

(2) the increase in Federal outlays specified in the budget resolution for a fiscal year does not exceed the previous year's outlays by more than the percentage increase in prices plus one percent; (3) for fiscal year 1982 only total Federal outlays do not exceed total revenues, as specified in the Second Concurrent Budget Resolution

Conference agreement.—The conference agreement provides that as a matter of national policy the rate of growth in Federal outlays, adjusted for inflation, should not exceed one percent per year between fiscal year 1979 and fiscal year 1983; Federal outlays as a percentage of gross national product should decline to below 21 percent in fiscal year 1980, 20.5 percent in fiscal year 1981, 20 percent in fiscal year 1982 and 19.5 percent in fiscal year 1983; and the Federal budget should be balanced in fiscal years 1982 and 1983. If these conditions are met, it is the intention that the tax-writing committees of Congress will report legislation providing significant tax reductions for individuals to the extent that these tax reductions are justified in the light of prevailing and expected economic conditions.

111. Sense of the Senate regarding revenue loss for fiscal years after 1979

House bill.—No provision

Senate amendment.—The Senate amendment expresses the sense of the Senate that the conferees on the part of the Senate shall limit, to an extent that is practical and reasonable, the revenue loss for the fiscal years following 1979.

Conference agreement.—The conferees agreed to the principles contained in the sense of the Senate regarding limiting the revenue loss for the fiscal years following 1979.

112. Study by the Treasury on ways to simplify Federal individual income tax return forms and instructions

House bill.—No provision.

Senate amendment.—The Senate amendment provides for the establishment of a Treasury Department task force to study the simplification of individual income tax returns and related instructions. Graphic and communication experts would be used in this study Interim reports would be made to the Secretary, and a final report, with recommendations, would be made to the Congress not later than 2 years after date of enactment.

Conference agreement.—The conference agreement follows the Senate amendment

113. Involuntary conversion of livestock

House bill.—No provision.

Senate amendment.—Under present law, taxpayers may elect not to recognize gain realized on the involuntary conversion of certain property if property similar or related in service or use to the property converted is acquired by the taxpayer within the replacement period. In such a situation, gain is recognized only to the extent that the amount realized exceeds the cost of the replacement property. The basis of the replacement property is that of the converted property, decreased by any gain not recognized.

In the case of involuntarily converted livestock, the replacement property satisfies the "similar or related in service or use" requirements for nonrecognition only if the new livestock is functionally the same as that converted.

The Senate amendment provides that gain realized on the involuntary conversion of livestock will qualify for nonrecognition if property,

which is to be used for farming purposes (including farm land), is acquired by the taxpayer. All other rules of present law would continue to apply. The provision is effective for taxable years beginning after December 31, 1974.

Conference agreement.—The conference agreement follows the Senate amendment, except that gain realized from the involuntary conversion of livestock can be rolled over into other farming property only if the conversion of the livestock was due to environmental contamination. In all other cases. the provisions of present law would continue to apply with respect to gain realized on the involuntary conversion of livestock.

114. Tax credit for 1976 minimum tax on intangible drilling costs

House bill.—No provision.

Senate amendment.—The 1976 Tax Reform Act made certain excess intangible drilling costs an item of preference subject to the minimum tax for individuals. The 1977 Tax Reduction and Simplification Act modified the formulation of the tax preference for 1977 so that it would apply only to the extent that excess intangible drilling costs exceeded oil income. This modification would be continued under both the House and the Senate versions of the energy tax cut, and also is contained in the Sentate amendment to the House bill.

The Senate amendment provides a tax credit for individuals whose regular tax, increased by their 1976 minimum tax on intangible drilling costs, exceeded their taxable income. The credit generally would be equal to the 1976 minimum tax on intangible drilling costs. However, no credit would be available unless the taxpayer's intangible drilling costs for the year in question are at least equal to 110 percent of his or her 1976 intangible drilling costs. This provision is effective for taxable years beginning after December 31, 1977, and before January 1, 1982.

Conference agreement.—The conference agreement does not contain this provision.

115. Minimum tax on 5-year amortization of low-income housing

House bill.—No provision.

Senate amendment.—Under present law, special depreciation rules for certain low-income rental property allow taxpayers to elect to compute depreciation on eligible rehabilitation expenditures under a straight-line method over a period of 60 months.

For purposes of the minimum tax, excess derpreciation on real porperty is an item of tax preference. Excess depreciation generally is that amount by which the deduction allowable for the taxable year exceeds the depreciation deduction which would have been allowable for that year had the taxpayer depreciated the property under the straight-line method for each taxable year of its useful life. The amount of any excess depreciation is determined without regard to the special election allowed for low-income rental property.

The Senate amendment provides that in a case of an election to depreciate certain low-income rental housing under the special depreciation rules, the amount treated as an item of tax preference will not exceed the amount which would have been treated as an item of tax preference if the taxpayer had claimed as a depreciation deduction an allowance computed under the declining balance method using a rate

not in excess of twice the rate which would have been used had the allowance been computed under the straight-line method. Thus, only the excess depreciation over that which would have been allowed had the double declining balance method been used would be a tax preference item. This provision is effective for taxable years ending after December 31, 1978.

Conference agreement.—The conference agreement does not contain this provision.

116. Individual retirement accounts technical corrections

House bill.—No provision.

Senate amendment.—The Senate amendment makes several changes to the provisions of the Code dealing with IRAs (individual retirement accounts, individual retirement annuities, and retirement bonds.) These changes generally affect (1) the timing of IRA contributions, (2) IRA penalty tax liability, and, (3) rollovers of plan and IRA distributions to IRAs and to other qualified plans. The Senate amendment is essentially the same as the bill reported from the House Ways and Means Committee on October 6, 1978, H.R. 13619. The provisions generally apply to taxable years beginning after December 31, 1978 however, some provisions contain retroactive amendment dates.

Conference agreement.—The conference agreement follows the Senate amendment except that the effective dates of the provisions were changed to conform with those set forth in H.R. 13619. The conferees agree with the interpretation of the provisions as set forth in the House Ways and Means Committee report, 95–1739.

The only clarification made by the conferees concerns the portion of money or other property to be treated as attributable to the employee contributions where property received in the distribution is sold and a partial rollover of the distribution is made. The conferees have agreed that employee contributions should come first from the ordinary income portion of the amount of the distribution retained.

117. Disclosure of tax return information to the Department of Justice in tax administration matters

House bill.—No provision.

Senate amendment.—Under present law, in tax administration matters, returns and return information are generally made available to attorneys of the Department of Justice (including United States attorneys) in preparation for any proceeding (or investigation which may result in such a proceeding) before a Federal grand jury or any Federal or State court. One of the requirements to be met before the return is made available in these situations is that the taxpayer whose return is the subject of disclosure either be or may be a party to the proceeding involved. The return of a third party could also be made available to the Department of Justice in preparation for a tax proceeding where the third party's return or return information relates or may relate to a transaction between the third party and the taxpayer whose tax liability is or may be at issue, and the return information pertaining to the transaction may affect the resolution of an issue of the taxpayer's liability. The disclosure of a third party return in a tax proceeding is subject to the same transactional tests, described above, except that the transactions must have a direct

relationship to the resolution of an issue of the taxpayer's liability.

The Senate amendment modifies present law in three respects. First, the return of a taxpayer who is not a party to the proceeding may be made available to the Department of Justice if the proceeding arose out of, or in connection with, determining the taxpayers' civil or criminal tax liability or the collection of civil tax liability. This provision would apply in such situations as where the taxpayer's liability may have given rise to transferee liability or where the taxpayer did not (or was unable to) intervene in a summons enforcement case.

The second modification makes it clear that disclosures of third party returns made to the grand jury in tax cases are investigative disclosures and, thus, not subject to the more restrictive requirements applicable to disclosures of third party returns in tax proceedings.

The third modification allows disclosure of returns to officers and employees of the Department of Justice, rather than just the attorneys of the Department of Justice.

This provision applies to disclosures made after December 31, 1978.

Conference agreement.—The conference agreement follows the Senate amendment.

VIII. PROVISIONS RELATING TO SOCIAL SECURITY ACT PROGRAMS

118. Title XX Social Services Programs

a. Ceiling on Federal title XX funds

House bill.—No provision.

Senate amendment.—Under existing law there is a permanent annual ceiling of $2.5 billion on Federal matching funds for the state Title XX social services programs. Since October 1, 1976 an additional $200 million of Federal Title XX funds has been available to states on a non-matching basis. To qualify for their portion of the $200 million states have to spend for day care under Title XX an amount equal to their additional allotment under the temporary $200 million. Authority for this $200 million expired September 30, 1978.

The Senate amendment increases the permanent ceiling to $2.9 billion beginning with fiscal year 1979. $200 million of the Title XX funds would be designated for child care services with no state matching requirement in Fiscal year 1979.

Conference agreement.—The conference agreement follows the Senate amendment except that the increase in the ceiling to $2.9 billion is for one year only (fiscal year 1979). After 1979, the ceiling reverts to $2.5 billion.

b. Multiyear planning program

House bill.—No provision.

Senate amendment.—Present law requires states to develop an annual services plan for the title XX program in the state. The Senate amendment provides the option for a state to establish either a one, two or three year Title XX program period.

Conference agreement.—The conference agreement does not include this provision.

c. Program year used by States

House bill.—No provision.

Senate amendment.—Under present law states must use either the Federal or state fiscal year as their program year for their Title XX social services program year. The Senate amendment would also give states the option to establish their social services program plans according to the fiscal year which applies to counties in the state.

Conference agreement.—The conference agreement does not include this provision.

119. AFDC management information system

House bill.—No provision.

Senate amendment.—Present law provides that states receive 50 percent Federal matching for the cost of administering their AFDC programs. The Senate amendment provides 90 percent Federal matching to states for the costs of developing and implementing computerized AFDC management information systems and 75 percent for the

cost of their operation. HEW would be required to approve state systems as a condition of Federal matching (both initially and on a continuing basis). A state system would have to include certain specified characteristics, including ability to provide data on AFDC eligibility factors, capacity for verification of factors with other agencies, capability for notifying child support, food stamps, social services and Medicaid programs of changes in AFDC eligibility and benefit amount, compatibility with systems in other jurisdictions, and security against unauthorized access to or use of data in the system. HEW would be required to provide technical assistance to the states. Increased matching would be payable for quarters beginning January 1, 1979.

Conference agreement.—The conference agreement does not include this provision.

120. Amendments to AFDC employment requirements under WIN program

a. Employment search requirement

House bill.—No provision.

Senate amendment.—Present law provides that AFDC recipients who are not specifically exempt are required to register for manpower services, training and employment as a condition of AFDC eligibility. The Senate amendment adds "other employment related activities" to the types of activities for which recipients must register. Requires that necessary social and supportive services be provided during employment search.

Conference agreement.—The conference agreement does not include this provision.

b. Termination of assistance

House bill.—No provision.

Senate amendment.—Present law provides assistance is to be terminated for so long as an individual (who has been certified by the welfare agency as ready for employment or training) refuses without good cause to participate in WIN. There is a 60 day counseling period during which assistance may not be terminated despite an individual's refusal to participate in WIN so long as the individual accepts counseling and other services aimed at persuading the individual to participate in a WIN program.

The Senate amendment eliminates provision for the 60 day counseling period. It also authorizes the Secretaries of Labor and HEW to establish by regulation the period of time during which an individual will not be eligible for assistance in the case of refusal without good cause to participate in a WIN program.

Conference agreement.—The conference agreement does not include this provision.

c. Support units

House bill.—No provision.

Senate amendment.—Present law requires states to have special units to provide social and supportive services to enable WIN registrants to engage in seeking and retaining employment.

The Senate amendment requires that these special units be colocated with the WIN manpower units to the maximum extent feasible.

Conference agreement.—The conference agreement does not include this provision.

d. State matching funds

House bill.—No provision.

Senate amendment.—Present law provides that states must provide 10% of the cost of the WIN program. Matching for manpower activities may be in cash or in-kind, but matching for the supportive services must be in cash.

The Senate amendment would allow state matching for the supportive services to be in cash or in-kind.

Conference agreement.—The conference agreement does not include this provision.

e. Treatment of public service employment earnings

House bill.—No provision.

Senate amendment.—Current law makes it unclear whether income from public service employment is excluded in determining AFDC benefits.

The Senate amendment clarifies that income from public service employment is not excluded in determining AFDC benefits.

Conference agreement.—The conference agreement does not include this provision.

f. Individuals exempt from WIN

House bill.—No provision.

Senate amendment.—Present law provides that certain categories of AFDC recipients are exempted from the WIN registration requirement, including children under 16; persons caring for a child under 6; persons who are ill or needed as caretaker of someone in the home who is ill; or persons who are remote from a WIN project.

The Sentate amendment adds to the individuals who are exempted from registration for WIN individuals who are working at least 30 hours a week.

Conference agreement.—The conference agreement does not include this provision.

121. Incentive for AFDC recipients to report earnings

House bill.—No provision.

Senate amendment.—Present law requires AFDC recipients to report earnings to the welfare agency. There is provision for disregarding portions of earned income in determining eligibility for and amount of the AFDC payment. When unreported earnings resulting in overpayments are discovered, the earned income disregards are applied to the unreported earnings in calculating the amount of the overpayment.

The Senate amendment provides that, if a recipient fails without good cause to make a timely report of earnings, the recipient would not have the benefit of having the earned income disregards applied to such unreported earnings.

Conference agreement.—The conference agreement does not include this provision.

122. Matching for child support costs of court personnel

House bill.—No provision.

Senate amendment.—Under present law State plans under the Title IV-D child support enforcement program must provide for entering into cooperative arrangements with appropriate courts and law enforcement officials to assist the child support agency in administering the program. The law provides or entering into financial arrangements with courts and officials. HEW regulations prohibit Federal matching for salaries of judges and their support staff.

The Senate amendment authorizes matching for compensation for judges and other support and administrative personnel of courts who performed Title IV-D functions, but only for those functions, specifically identifiable as IV-D functions. Matching would be provided only for expenditures in excess of levels of spending in the state for these activities in 1976.

Conference agreement.—The conference agreement does not include this provision.

123. Increase in Federal funding for territorial assistance programs

House bill.—No provision.

Senate amendment.—Under present law, public assistance programs in Puerto Rico, Guam and the Virgin Islands qualify for Federal matching at a 50 percent rate and are subject to dollar limits on the amount of Federal funding available. The annual limit is $24 million for Puerto Rico, $800,000 for the Virgin Islands and $1.1 million for Guam.

The Senate amendment would increase the Federal matching rate for public assistance programs (aid to the aged, blind and disabled and AFDC) to 75 percent and would triple the maximum annual amount of Federal funding to $72 million for Puerto Rico, $2.4 million for the Virgin Islands, and $3.3 million for Guam.

Conference agreement.—The conference agreement follows the Senate amendment, except that the increase in the matching rate and ceilings is effective only for one year—fiscal year 1979.

124. Northern Mariana Island provisions

House bill.—No provision.

Senate amendment.—In present law, the covenant establishing the Commonwealth of the Northern Marianas specifically extended the supplemental security income (SSI) program to that jurisdiction and implicitly extends other public assistance programs. Statutory provisions do not specifically include the Marianas under any Social Security Act programs.

The Senate amendment provides for bringing the Mariana Commonwealth under the Social Security Act public assistance programs in a manner compatible to the other territories. This would allow the Commonwealth to provide assistance and social services under state plan programs of the aged, blind and disabled and aid to families with dependent children. Coverage under the medical assistance (Medicaid) program would also be provided. Under the Senate amendment, the SSI program would no longer be applicable in the Marianas.

Conference agreement.—The conference agreement does not include this provision.

125. Foster care, adoption assistance and child welfare services

a. Ceiling on Federal AFDC foster care funds

House bill.—No provision.

Senate amendment.—Under present law Title IV–A authorized open-ended Federal matching for use by states to provide foster care payments for the care of children who (1) meet the state AFDC eligibility requiremens and (2) have been removed from their homes as the result of judicial determination. Federal matching rate is the same as for AFDC income maintenance payments.

The Senate amendment creates a new Part E of Title IV "Federal Payments for Adoption Assistance and Foster Care" and amends the child welfare services program. It also establishes a ceiling on Federal foster care funding. The state's fiscal year 1978 expenditures of Federal funds for foster care would be the base and the allotment for each state could not exceed an additional 20 percent in 1979 and 10 percent per year in each of the next 4 years. To provide room for growth in states with small programs an alternative ceiling would be provided equal to each state's share of $100 million based on state population under age 21. States that did not use their full allotment for foster care could use excess funds for IV–B child welfare services.

Conference agreement.—The conference agreement does not include this provision.

b. Foster care provided in institutions

House bill.—No provision.

Senate amendment.—Present law provides that Federal foster care matching funds are available for foster care provided in institutions only in the case of nonprofit private institutions.

The Senate amendment allows funding of foster care maintenance payments for children in public facilities, but only if the public institution serves no more than 25 children. Funding would not be available for children in such institutions prior to enactment of these provisions.

Conference agreement.—The conference agreement does not include this provision.

c. Adoption assistance

House bill.—No provision.

Senate amendment.—Under present law Federal AFDC matching funds are not available for adoption subsidies.

The Senate amendment authorizes states to make assistance payments to parents who adopt "hard-to-place" children. The matching rate would be the same as under the AFDC program. States would have to find that the child would have been receiving AFDC but for the child's removal from the home of his relatives; that the child cannot be returned to that home; and that after making a reasonable effort consistent with the child's needs, the child has not been adopted without offering of financial assistance. The determination of whether a child is difficult to place would have to be made by the state based on a specific fact or condition because of which it is reasonable to conclude that the child cannot be adopted without adoption assistance.

Families would be eligible for an adoption subsidy so long as their income does not exceed 115 percent of the median family income for a family of four in the state, adjusted to reflect family size. The amount of the subsidy would be agreed on by the family and the agency but could not exceed the amount paid for foster care (in a foster family home) and would be terminated when the child reached 18 or the family's income exceeded the specified limits. A child with a medical disability that existed at the time of adoption would continue to be covered under medicaid for treatment related to that medical disability. States would be permitted to make an adopted child with a pre-existing medical condition eligible for treatment under medicaid for other medical conditions as well. Matching for adoption subsidies would not be provided for adoption agreements entered into after January 1, 1983.

Conference agreement.—The conference agreement does not include this provision.

d. Federal funds for child welfare services

House bill.—No provision.

Senate amendment.—Present law authorizes $266 million (of which $56.5 million was appropriated for fiscal year 1978) in Federal matching funds to be alloted to the States for a wide range of child welfare services and for foster care payments. The theoretical Federal matching rate ranges from 33⅓ to 66⅔ percent. There are no prohibitions on the use of funds for foster care maintenance payments.

The Senate amendment retains the present law authorization of up to $266 million for child welfare services, but increases the Federal matching to 75 percent, and provides that funds appropriated in future years that are above the amount appropriated for fiscal year 1978 ($56.5 million) may not be used for foster care maintenance payments.

Conference agreement.—The conference agreement does not include this provision.

e. Foster care protections

House bill.—No provision.

Senate amendment.—There is no provision in present law. The Senate amendment permits States to use child welfare service funds for State tracking and information systems, individual case review systems, services to reunite families or place children in adoption, and procedures to protect the rights of natural parents, children and foster parents. The amendment allows the Congress to designate that any new funding be specifically used for these purposes. In the first year for which a State receives funds for these purposes it would be allowed to use them to conduct an inventory of children who have been in foster care for 6 months preceding the inventory, and to design and develop a statewide information system for children in foster care, a case review system for each child, and a service program designed to help children remain with their families.

Conference agreement.—The conference agreement does not include this provision.

126. AFDC earned income disregard

House bill.—No provision.

Senate amendment.—Under present law, in determining the amount of benefits to be paid to an AFDC recipient with earnings the following formula is used: Disregard (1) $30 a month in earnings, (2) one-third of remaining earnings, and (3) the amount of work related expenses.

The Senate amendment provides for disregarding from earned income (1) an amount equal to reasonable child care expenses (subject to limitation prescribed by HEW), (2) from the remaining income $60 a month in the case of an individual working full time and $30 in the case of an individual working part-time (3) one-third of the next $300 of monthly earnings, and (4) one-fifth of the remaining earnings.

Conference agreement.—The conference agreement does not include this provision.

APPENDIX

APPENDIX

BUDGET EFFECTS OF HOUSE, SENATE AND CONFERENCE VERSIONS OF H.R. 13511

Part A.—Tax Reductions and Revisions

[In millions of dollars]

Item	House					Senate					Conference				
	1979	1980	1981	1982	1983	1979	1980	1981	1982	1983	1979	1980	1981	1982	1983
Individual Tax Reduction and Revisions															
Bracket widening, rate cuts, and increase zero bracket amount	−6,549	−11,608	−13,440	−15,587	−18,104	−8,571	−22,049	−23,453	−27,842	−33,099	−7,317	−13,057	−15,453	−18,317	−21,742
Exemption related provisions:															
Repeal general tax credit	7,278	10,809	11,428	12,097	12,818	7,278	10,809	11,428	12,097	12,818	7,278	10,809	11,428	12,097	12,818
$1,000 personal exemption	−8,177	−12,171	−12,902	−13,677	−14,497	−8,177	−12,171	−12,902	−13,677	−14,497	−8,177	−12,171	−12,902	−13,677	−14,497
Additional exemption for disabled						−121	−248	−379	−519	−546					
Earned income credit provisions:															
Simplify earned income credit		−17	−16	−16	−15		−17	−16	−16	−15		−17	−16	−16	−15
Increase earned income credit						−110	−1,969	−1,624	−1,497	−1,588	−82	−1,210	−960	−921	−885
Itemized deductions and tax credits:															
Repeal gasoline tax deduction	471	1,237	1,458	1,720	2,029	471	1,237	1,458	1,720	2,029	471	1,237	1,458	1,720	2,029
Revise medical expense deduction	16	43	51	60	71										
Disability income exclusion						−26	−14	−15	−16	−17					
Repeal political contributions deduction	2	6	7	8	10							−20	−33	−20	−20
Increase political contribution credit							−16	−26	−16	−16					
Increase elderly credit						−104	−278	−278	−278	−278					
Credit for child care services						−5	−38	−39	−40	−39	−5	−38	−39	−40	−39
Tuition tax credit						−330	−539	−968	−845						
Tax certain unemployment benefits		251	261	259	263							251	261	259	263

Deferred compensation provisions						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Pension plan provisions:															
Additional contributions to pension plans						−144	−352	−425	−487	−536					
IRA pension plans						−6	−18	−29	−39	−49	−6	−18	−29	−39	−49
Rollover of annuities						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
IRA technical provisions						−25	−12	−12	−12	−12	−25	−12	−12	−12	−12
Total, individual	−6, 959	−11, 450	−13, 153	−15, 136	−17, 425	−9, 870	−25, 675	−27, 280	−31, 558	−35, 754	−7, 863	−14, 246	−16, 297	−18, 966	−22, 149
Business Tax Reductions and Revisions															
Tax rates on corporate income	−2, 281	−5, 286	−5, 788	−6, 338	−6, 940	−2, 281	−6, 109	−8, 616	−10, 558	−11, 561	−2, 281	−5, 286	−5, 788	−6, 338	−6, 940
Investment tax credit provisions:															
Increase limitation to 90%	−129	−441	−872	−1, 015	−782	−129	−441	−872	−1, 015	−782	−129	−441	−872	−1, 015	−782
Investment credit for pollution control facilities	−6	−18	−42	−76	−104	−10	−34	−85	−156	−211	−6	−18	−42	−76	−104
Investment credit for certain food and plant production						[3] −53	−33	−22	−24	−26	[3] −53	−33	−22	−24	−26
Investment credit for farm cooperatives						−15	−33	−35	−37	−39	−20	−33	−35	−37	−39
Investment credit for breeding and draft horses						−6	−16	−17	−19	−21					
Extend 1-yr carryover period for unused credit						(2)	(2)	(2)	(2)	(2)					
Modify credit limitation for lessors of railroad cars						−4	−5	(1)	2	2	−4	−5	(1)	2	2
Credit recapture on property transfers to Con-Rail						−3					−3				
Investment credit for rehabilitated structures	−84	−259	−292	−318	−340	−9	−52	−190	−215	−234	−67	−181	−205	−222	−238
Jobs credit provisions:															
Repeal general jobs credit	689	2, 458	2, 458	2, 458	2, 458	689	2, 458	2, 458	2, 458	2, 458	689	2, 458	2, 458	2, 458	2, 458
Targeted jobs credit	−189	−602	−745	−825	−875	−129	−455	−601	−560	−85	−141	−483	−651	−426	−86
WIN credit						−58	−223	−314	−370	−422	−39	−136	−197	−234	−264
Extend general jobs credit in modified form						−360	−1, 350	−990							
Industrial development bond provisions:															
Small issues exception to IDB tax treatment	(1)	−3	−13	−22	−30	(1)	−4	−17	−29	−39	(1)	−3	−13	−22	−30

See footnotes at end of table.

APPENDIX—Continued

BUDGET EFFECTS OF HOUSE, SENATE AND CONFERENCE VERSIONS OF H.R. 13511—Con.

Part A.—Tax Reductions and Revisions—Continued

[In millions of dollars]

Item	House					Senate					Conference				
	1979	1980	1981	1982	1983	1979	1980	1981	1982	1983	1979	1980	1981	1982	1983
Industrial development bond provisions—continued															
Bonds for certain qualified public facilities						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Advance refundings of certain other IDB's						(1)	−8	−9	−9	−9					
Bonds for water projects						(1)	−6	−26	−49	−65	(1)	−7	−31	−59	−78
Industrial development bonds for facilities involving urban grants							(1)	−1	−5	−9		(1)	−1	−4	−7
IDB use for local furnishing of electricity by State power authority						(1)	−3	−10	−18	−23	(1)	−3	−10	−18	−23
Subchapter S corporations	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Small business corporation stock	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Accrual accounting for farm corporations	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Accounting for costs of growing crops	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Small business depreciation	−148	−357	−305	−263	−232	−37	−421	−1,439	−2,374	−2,376					
Denial of deduction for expenditures on entertainment facilities						51	116	126	138	151	13	29	31	34	38
Deficiency dividend procedure for regulated investment companies						(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Safe harbor rule for REIT's						(4)	(4)	(4)	(4)	(4)	(4)	(4)	(4)	(4)	(4)
Contributions in aid of construction [5]						(2)	−50	−100	−100	−100	(2)	−50	−100	−100	−100
Treatment of certain liabilities on incorporation of trade or business						(3)	(3)	(3)	(3)	(3)	(3)	(3)	(3)	(3)	(3)
Medical reimbursement plan							(3)	(3)	(3)	(3)		(3)	(3)	(3)	(3)

Postponement of effective date for special limitations on NOL's						[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]	[2]
Redemptions of U.S. Fairway certificates of value						[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]
Railroad rolling stock (Sec. 861)						[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]	[1]
Tax shelter provisions	2	14	10	8	5						2	13	9	7	5
Total, business	−2,146	−4,494	−5,589	−6,390	−6,840	−2,354	−6,669	−10,760	−12,940	−13,391	−2,039	−4,179	−5,469	−6,074	−6,214
Capital Gains Reductions and Revisions															
Individuals revisions:															
Repeal alternative tax	[1]	133	143	154	166	20	133	143	154	166	20	133	143	154	166
Remove capital gains from preferences	[1]	−1,327	−1,459	−1,605	−1,766										
Capital gains exclusion						−250	−3,394	−3,648	−3,922	−4,214	−131	−1,763	−1,895	−2,037	−2,190
Exclude gains from sale of personal residence	−282	−745	−820	−901	−992	−161	−322	−354	−388	−426	−165	−415	−457	−502	−552
Sale of personal residence within 18 mo	−2	−3	−3	−3	−3	−2	−3	−3	−3	−3	−3	−4	−4	−4	−4
Postponement of carryover basis						−36	−93	−162	−185	−190	−36	−93	−162	−185	−190
Index the basis of certain capital assets		[1]	−409	−1,396	−2,082										
Corporate provisions:															
Remove capital gains from preferences		−95	−104	−114	−125										
Index basis of certain capital assets		−58	−263	−583	−977										
Reduce alternative tax rate on capital gains						−53	−125	−141	−155	−170	−53	−125	−141	−155	−170
Tax increase from induced capital gains realizations						85	1,092	1,173	1,261	1,356	37	738	799	864	1,011
Total, capital gains	−284	−2,095	−2,915	−4,448	−5,779	−397	−2,712	−2,992	−3,238	−3,483	−331	−1,529	−1,717	−1,865	−1,929
Minimum and Maximum Tax Provisions															
Repeal existing minimum tax							−1,566	−1,722	−1,894	−2,083		−1,274	−1,401	−1,541	−1,695
Alternative minimum tax							1,603	1,763	1,939	2,133		739	813	894	984
Alternative minimum tax on capital gains	[1]	172	190	209	230										
Intangible drilling costs in minimum tax						−51	−61	−73	−84	−97	−51	−61	−73	−84	97−

See footnotes at the end of the table.

APPENDIX—Continued

BUDGET EFFECTS OF HOUSE, SENATE AND CONFERENCE VERSIONS OF H.R. 13511—Con.

Part A.—Tax Reductions and Revisions—Continued

[In millions of dollars]

Item	House					Senate					Conference				
	1979	1980	1981	1982	1983	1979	1980	1981	1982	1983	1979	1980	1981	1982	1983
Intangible drilling cost tax credit from 1976 liability						−15	−5	−3							
Maximum tax provisions															
Limitation on personal service income						−21	−59	−69	−79	−91	−21	−59	−69	−79	−91
Tax preference offset						−6	−52	−57	−63	−69	−6	−52	−57	−63	−69
Total, minimum and maximum tax	(1)	172	190	209	230	−93	−140	−161	−181	−207	−78	−707	−787	−873	−968
Other Tax Provisions															
Independent contractor status [6]						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)		
Reporting of tips [7]						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Revised estate tax for joint farm and business						(1)	−41	−43	−46	−48	(1)	−41	−43	−46	−48
Puerto Rico S & L associations						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Reduce excise tax on foundation investment income						−40	−40	−40	−40	−40	−40	−40	−40	−40	−40
Excise tax on gaming machines phased out						−5	−6	−7	−7	−7	−5	−6	−7	−7	−7
Excessive Government spending surtax						(4)	(4)	(4)	(4)	(4)					
Charitable lead trusts						[3] −15					[3] −15				
Attribution rules for extension of time to pay estate tax						(4)	(4)	(4)	(4)	(4)	(4)	(4)	(4)	(4)	(4)
Exemption from private foundation tax for failure to distribute						(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Small tax case procedures before tax court						(5)	(5)	(5)	(5)	(5)	(5)	(5)	(5)	(5)	(5)

Tax treatment of cooperative housing corporations						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Tax exemption for certain mutual guaranty organizations						[3] −5	(1)	(1)	(1)	(1)	[3] −5	(1)	(1)	(1)	(1)
Tax accounting rules for magazines, etc							−5	−11	−12	−13		−5	−11	−12	−13
Tax accounting rules for discount coupons							[9] −103	−10	−10	−10		[9] −103	−10	−10	−10
Exempts farm and soil and water conservation trucks from use tax						−12	−20	−20	−20	−20					
Taxes foreign investors on sale of farmland						(2)	(2)	(2)	(2)	(2)					
Alaskan Native Claims Settlement Act						(8)	(8)	(8)	(8)	(8)	(8)	(8)	(8)	(8)	(8)
Conditional tax reductions						(4)	(4)	(4)	(4)	(4)					
Technical corrections to the Tax Reform Act of 1976						[3] −8		(1)	−7	−10	[3] −8		(1)	−7	−10
Certain cost sharing payments							−28	−77	−78	−79		−28	−77	−78	−79
Involuntary conversion of livestock						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Claim of right						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Product liability carryovers						(1)	(2)	−7	−8	−9	(1)	(2)	−7	−8	−9
Uniformed services scholarship exclusion						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
National research service awards						[3] −52	−18	−10	(2)		−52	−18	−10	(2)	
Cancellation of student loans						(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)	(2)
Employer educational assistance						−18	−28	−31	−35	−39	−18	−28	−31	−35	−39
Total, other tax provisions						−155	−289	−256	−263	−275	−143	−269	−236	−243	−255
Total, tax reductions and revisions	−9, 387	−17, 867	−21, 465	−25, 765	−29, 814	−12, 869	−35, 485	−41, 449	−48, 180	−53, 110	−10, 454	−20, 930	−24, 506	−28, 021	−31, 515

[1] Less than $1,000,000.
[2] Less than $5,000,000.
[3] Includes liabilities of prior years.
[4] No direct revenue effect is expected.
[5] The estimates were derived assuming that the position taken by the IRS is the correct one. The figures do not allow for revenue effects of additional charges the utilities may make in order to get reimbursement for the additional taxes payable under IRS ruling.
[6] The revenue effect cannot be estimated because the provision affects liabilities being contested by taxpayers in administrative and judicial proceedings.
[7] This provision has the effect of overturning Revenue Rulings 75–400 and 76–231. If the employer reporting requirements contained in these rulings were to take effect, increases in budget receipts could be substantial. This revenue is not being collected at the present time, therefore no change in budget receipts is estimated.
[8] Settlement of the contested issues is not expected to result in a significant impact on budget receipts through 1983.
[9] It is assumed the Service's position will be upheld by the courts in 1980.

Part B.—Estimated Revenue Effect of Extending or Making Permanent Existing Temporary Income Tax Reduction Provisions, Fiscal Years 1979–1983

[In millions of dollars]

Provision	House					Senate					Conference				
	1979	1980	1981	1982	1983	1979	1980	1981	1982	1983	1979	1980	1981	1982	1983
Individual income taxes:															
Per capita credit [1]	−4,514	−6,853	−6,780	−6,984	−7,194	−4,514	−6,583	−6,780	−6,984	−7,194	−4,514	−6,583	−6,780	−6,984	−7,194
Optional taxable income credit [1]	−2,764	−4,226	−4,648	−5,113	−5,624	−2,764	−4,226	−4,648	−5,113	−5,624	−2,764	−4,226	−4,648	−5,113	−5,624
Earned income credit		−1,061	−1,019	−978	−938		−1,061	−1,019	−978	−938		−1,061	−1,019	−978	−938
Investment tax credit at 10-percent rate			−271	−741	−794			−271	−741	−794			−271	−741	−794
Amortization for low-income rate	(2)	−2	−6	−11	−14	(2)	−2	−6	−11	−14	(2)	−2	−6	−11	−14
Jobs tax credit [3]	−125	−983	−983	−983	−983	−125	−983	−983	−983	−983	−125	−983	−983	−983	−983
Total, individual income taxes	−7,403	−12,855	−13,707	−14,810	−15,547	−7,403	−12,855	−13,707	−14,810	−15,547	−7,403	−12,855	−13,707	−14,810	−15,547
Corporation income taxes:															
Rate reductions	−927	−2,148	−2,352	−2,575	−2,819	−927	−2,148	−2,352	−2,575	−2,819	−927	−2,148	−2,352	−2,575	−2,819
Investment tax credit at 10-percent rate			−1,800	−4,460	−5,489			−1,800	−4,460	−5,489			−1,800	−4,460	−5,489
TRASOP investment credit at 1½-percent rate								−178	−446	−545			−178	−446	−545
Amortization for low-income housing	(2)	−2	−5	−8	−10	(2)	−2	−5	−8	−10	(2)	−2	−5	−8	−10
Jobs tax credit [3]	−564	−1,475	−1,475	−1,475	−1,475	−564	−1,475	−1,475	−1,475	−1,475	−564	−1,475	−1,475	−1,475	−1,475
Total, corporation income taxes	−1,491	−3,625	−5,632	−8,518	−9,793	−1,491	−3,625	−5,810	−8,964	−10,338	−1,491	−3,625	−5,810	−8,964	−10,338
Total, temporary tax reduction extensions	−8,894	−16,480	−19,339	−23,328	−25,340	−8,894	−16,480	−19,517	−23,774	−25,885	−8,894	−16,480	−19,517	−23,774	−25,885
Grand total, tax reductions, revisions, and extensions	−18,283	−34,347	−40,804	−49,095	−55,154	−21,763	−51,965	−60,966	−71,954	−78,995	−19,348	−37,410	−44,023	−51,795	−57,400

[1] These items are not extended by H.R. 13511, but are allowed to expire after 1978 and are replaced by an increase in the personal exemption from $750 to $1,000.

[2] Less than $500,000.

[3] The expiring general jobs tax credit is not extended and an offsetting entry is shown in part A of this table.

4. Changes in filing requirements and withholding changes

House bill.—Under present law, a tax return must be filed by a single person and a head of household if his or her income is $2,950 or more a year and by a married couple under age 65 filing a joint return if their income is $4,700 or more. The House bill increases the filing levels for single person and a head of household to $3,300 and to $4,500 for a married couple (under age 65).

The withholding tax rates reflect the present law tax rates, the zero bracket amount, and the amount of the personal exemption. Under the House bill, the withholding rates and tables are to be changed by the Secretary of the Treasury to reflect the increase in the zero bracket amount and the personal exemption.

The change in the filing requirement is effective for taxable years beginning after December 31, 1978, and the withholding changes apply to wages paid after December 31, 1978.

Senate amendment.—The Senate amendment is the same as the House bill, except the filing requirement for heasd of households is increased to $4,000.

The withholding changes are to be the same as the House bill except to reflect the higher zero bracket amount for heads of households and the different tax rate reductions.

The date for the filing requirement change is the same as the House bill, but the withholding changes are to apply to wages paid after July 31, 1978.

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