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EXPLANATION OF COMMITTEE AMENDMENT TO H.R. 2973

I. INTEREST AND DIVIDEND COMPLIANCE
II. CARIBBEAN BASIN ECONOMIC RECOVERY ACT
III. ENTERPRISE ZONE TAX ACT
IV. INTERNATIONAL TRADE AND INVESTMENT ACT
V. PERMANENT EXTENSION OF TAX EXEMPTION FOR INTEREST ON QUALIFIED MORTGAGE BONDS

COMMITTEE ON FINANCE
UNITED STATES SENATE

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CONTENTS

	Page
Introduction	1
Summary	1
Explanation of Committee Amendment	8
Title I—Interest and Dividend Tax Compliance	8
1. Withholding repeal	8
2. Compliance study by the General Accounting Office	9
3. Backup withholding	9
4. Information returns filed on magnetic media	18
5. Payor penalties	18
6. Attachment of Form 1099s	18
7. Payee penalties for failure to report income	18
8. Acceleration of information matching programs	18
Title II—Caribbean Basin Economic Recovery Act	22
A. Summary	22
B. Background—The Caribbean Basin Initiative	22
C. Explanation of Trade and Tariff Provisions	26
D. Explanation of Tax Provisions	44
E. Sense of the Senate on Sugar Imports	49
F. Budgetary Impact	50
G. Vote of the Committee	51
Title III—Enterprise Zone Tax Act	52
1. Designation of enterprise zones	57
2. Tax credit for zone employers	62
3. Tax credit for zone employees	65
4. Investment tax credit for zone property	66
5. Elimination of capital gains taxation	67
6. Industrial development bonds	69
7. Tax simplification	69
8. Regulatory flexibility	69
9. Establishment of foreign trade zones in enterprise zones	70
Title IV—International Trade and Investment Act	72
A. Summary	72
B. General Explanation	72
C. Budgetary Impact	82
D. Vote of the Committee	82
Title V—Permanent Extension of Tax Exemption for Interest on Qualified Mortgage Bonds	83

INTRODUCTION

On May 26, 1983, the Committee on Finance approved a committee amendment to H.R. 2973. This document is an explanation of that committee amendment, whch includes five titles: (1) repeal of mandatory withholding on interest and dividends together with a compliance package designed to increase tax collections from interest and dividend income; (2) the Caribbean Basin Economic Recovery Act (the provisions of S. 544 as amended by the Committee on May 12, 1983, with an additional modification); (3) enterprise zone incentive provisions (provisions of the Enterprise Zone Tax Act of 1983, as agreed to by the Committee on May 17); (4) trade reciprocity provisions (previously reported in S. 144, the International Trade and Investment Act, and as passed by the Senate on April 2, 1983; and (5) permanent extension of tax exemption for interest on qualified mortgage bonds.

This document is intended to be the equivalent of a committee report explaining the legislative provisions of the committee amendment. The committee amendment is to be offered as an amendment to H.R. 2973, upon Senate consideration of that bill. H.R. 2973 as passed by the House would repeal the mandatory withholding on interest and dividends (which otherwise would go into effect on July 1, 1983).

SUMMARY

The committee amendment to H.R. 2973 contains five titles.

First, withholding on interest and dividends, which is scheduled to take effect on July 1, 1983, is repealed. In its place, the committee amendment adopts a number of provisions designed to improve the effectiveness of the information reporting system and authorizes increased appropriations for the Internal Revenue Service.

Second, the committee amendment includes the Caribbean Basin Economic Recovery Act, which, under specific conditions, provides for a waiver of duties on certain products imported from 27 Caribbean and Central American countries, allows for reasonable deductions of business expenses incurred in attending conventions in those countries, and provides certain benefits for Puerto Rico and the Virgin Islands.

Third, the committee amendment provides for the establishment of no more than 75 urban enterprise zones in which employers and investors will have specific tax benefits designed to encourage economic development within the zones.

Fourth, the committee amendment includes the International Trade and Investment Act (previously reported by the Committee in S. 144), which among other things: (1) establishes new specific negotiating objectives with respect to trade in services, advanced technology products, and investment restraints; (2) clarifies the President's retaliatory authority with respect to unfair trade practices; and (3) authorizes tariff negotiations with respect to certain advanced technology products.

Fifth, the committee amendment provides for a permanent extension of the tax-exemption presently provided for interest on qualified mortgage bonds.

EXPLANATION OF COMMITTEE AMENDMENT

TITLE I—INTEREST AND DIVIDEND TAX COMPLIANCE

Present Law

Legislative history

During consideration of the Revenue Act of 1962, the House of Representatives adopted an Administration proposal to require withholding on most interest, dividend and patronage dividend payments, at a 20-percent rate. The House Ways and Means Committee report explained that withholding was expected to collect over 80 percent of an estimated $800 million annual revenue loss attributable to unreported interest and dividend income.

Instead of the House-passed withholding provisions, the Revenue Act of 1962 enacted the provisions of the Senate bill which required expanded information reporting. The Report of the Senate Finance Committee explaining the Senate provisions stated:

> Your committee strongly endorses the concept that everyone must pay his full share of the income tax liability. Moreover, it recognizes that the underreporting of dividends and interest on tax returns is a serious problem which needs correction. However, it has concluded that an improved reporting system is preferable to a provision for withholding.
>
> Your committee believes that the matching of information returns and tax returns by the Government can provide essentially the same check on dividend and interest reporting as a withholding system, except that the effectiveness of the information returns is not limited to collecting the tax at the first bracket rate. While it may be difficult initially to provide a full matching of information and tax returns, the extended use of automatic data processing, together with the accounting number system provided for in legislation enacted last year should quite soon make it possible to provide for a full matching of these information and tax returns.
>
> It is recognized that improving the collection of tax with respect to dividend, interest and patronage dividend payments by an expanded use of information returns may involve some increase in the personnel of the Internal Revenue Service. It is believed, however, that this is preferable to the complications and hardships which would be involved under a withholding system.

By 1981, the annual revenue loss from unreported interest and dividends was estimated by the Internal Revenue Service to be in excess of $8 billion despite the existence of the information reporting system adopted in 1962. In 1982, the Administration proposed withholding on interest and dividends, at a 5-percent rate, to close this compliance gap. In addition to the Administration's withholding proposal, other legislation was proposed to improve compliance by improving the accuracy and reliability of information returns and extending information reporting requirements to Treasury obligations and corporate bearer obligations.

In the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA"), Congress enacted the Administration's withholding proposal, at a 10-percent rate, together with provisions improving and expanding the information reporting system. These and other provisions of TEFRA were enacted to satisfy the requirements of the First Concurrent Resolution on the Budget for fiscal year 1983 that Federal Revenues be increased by $98.3 billion through fiscal year 1985.

The TEFRA withholding provisions, which were enacted to take effect on July 1, 1983, became the subject of controversy, and in April 1983, the Senate voted to delay implementation of withholding during a period in which a strengthened information reporting and backup withholding system is in effect.

Withholding

Generally, present law (enacted in TEFRA) provides for a system of withholding on payments of interest, dividends, and patronage dividends to individuals (other than certain low-income and elderly individuals) at a rate of 10 percent to take effect on July 1, 1983. Withholding is also required on payments to unincorporated entities, such as partnerships and estates, which are not themselves required to withhold on payments to individuals.

Exemptions from withholding are specifically provided for various types of payments, including: (1) payments to individuals who had tax liability in the preceding year of $600 or less ($1,000 in the case of a joint return); (2) payments to persons age 65 or older whose tax liability in the preceding year was $1,500 or less ($2,500 in the case of a joint return); (3) at the payor's election, payments of interest which do not exceed $150 and which would not exceed $150 on an annual basis; (4) payments to corporations, governments, security dealers, money market funds, exempt organizations, and nominees or custodians; (5) payments to trusts that must distribute all of their income currently, if all the beneficiaries are individuals who could qualify as exempt individuals on the basis of their prior year's tax liability, or exempt organizations, or individu~~al retirement plans; (6) payments to exempt organizations or indi~~vidual retirement plans; and (7) certain payments by consumer cooperatives. In addition, subject to Treasury Department regulations, banking institutions and money market funds are permitted to elect to defer withholding to the end of the year with respect to payments of interest on most deposit and transaction accounts. Persons required to withhold tax also are authorized to withhold from alternative sources.

In implementing the withholding deposit requirements, the Treasury Department is required to take into account the costs incurred by payors in instituting withholding. The Treasury Department's regulations provide an extended period of generally 19 banking days for making otherwise required deposits. Thus, payors may generally retain withheld amounts for an average of one calendar month before depositing them. This extended period is available to all payors through June 1984. After June 1984, medium and small banking organizations will have the extended deposit period for an additional one and two years, respectively. Further, the Secretary may exempt any payor from the withholding requirement, but not beyond 1983, if complying with the requirement prior to January 1, 1984, would impose an undue hardship on the payor.

Other compliance provisions

Present law also contains a number of provisions which were designed to encourage compliance in reporting and paying tax on payments that are not subject to withholding. Thus, for certain payments that are not otherwise subject to withholding, backup withholding is required starting on January 1, 1984. Under these rules, withholding is required at the rate of 15 percent on certain payments to taxpayers who fail to furnish the payor with a taxpayer identification number or who fail to supply the correct identification number. Thus, if the Internal Revenue Service cannot verify that income has been reported because the correct taxpayer identification number has not been provided, the law assures the collection of at least 15 percent of the payment through backup withholding.

Under present law, penalties are imposed on payors of items subject to information reporting for failure either to file required information returns or to include taxpayer identification numbers on those returns. Specifically, the penalty for failure to file a required information return is $50 for each failure up to a maximum of $50,000 per payor, unless the failure is due to reasonable cause and not due to willful neglect. If the failure is due to intentional disregard, the $50,000 limitation does not apply and the penalty generally will be at least 10 percent of the aggregate amount required to be reported (5 percent of the gross proceeds required to be reported in the case of broker returns). The penalty for failure to provide a taxpayer identification number to a payor or to include in any return or other document made with respect to another person the taxpayer identification number of such person is $50 per failure up to $50,000 per year unless the failure is due to reasonable cause and not due to willful neglect. These penalties were raised to the present law levels from the prior law level of $5 per offense (not to exceed $10,000 per year) by TEFRA.

Under present law, if any part of an underpayment is attributable to fraud, a civil penalty is imposed equal to 50 percent of the entire underpayment and 50 percent of the interest on the portion of the underpayment attributable to the fraud. This 50 percent of interest portion of the fraud penalty was also enacted in the 1982 tax legislation.

Reasons for Change

The House bill would repeal withholding without enacting any improvements in information reporting beyond those provided by TEFRA. In light of the large current and projected Federal budget-

21-334 O - 83 - 2

ary deficits, and the serious fiscal and social problems posed by tax noncompliance, the committee believes that repeal of withholding requires a careful strenghtening of other compliance provisions of the Internal Revenue Code, a thorough review of Internal Revenue Service enforcement practices, and increases in the level of Internal Revenue Service funding.

According to Treasury Department and Internal Revenue Service estimates, in the absence of the compliance provisions enacted in TEFRA, $25 billion of interest and dividend income required to be reported on 1983 tax returns would not be reported (excluding interest and dividends exempt from the TEFRA withholding and reporting rules, such as interest paid by individuals). This annual reporting gap has been estimated by the Internal Revenue Service to result in lost tax revenues in excess of $8 billion. The committee does not believe that such levels of noncompliance are acceptable.

The TEFRA withholding provisions were controversial because of a number of concerns, including the perception that withholding might impose undue burdens on conscientious taxpayers. This concern was aggravated by uncertainty as to whether the Congress had enabled and directed the Internal Revenue Service to pursue diligently alternative approaches to closing the compliance gap. In addition, it was recognized that even under the 10-percent mandatory withholding provisions, the law continued to rely on the information reporting system to collect taxes on unreported income earned by taxpayers with tax rates higher than 10 percent. Although the committee has no reason to question the estimates of noncompliance of the Internal Revenue Service, the committee recognizes that such estimates were not uncontroversial. The payor institutions have urged the Congress that they can cooperate with the Internal Revenue Service to secure a compliance rate of 95 percent or higher without the burden or cost of withholding. Accordingly, measures to improve the ability of the Internal Revenue Service to pursue underreported income were increasingly viewed as an appropriate response to the compliance problem. The committee has identified several problem areas in the current information reporting and enforcement system, and recommends provisions to address these problems.

In particular, the committee is concerned that the information reporting system which must be relied on to achieve compliance in the absence of withholding should operate as effectively as possible. In the past, the efficiency of the Internal Revenue Service in using the information reporting process has been hampered by missing or erroneous taxpayer identification numbers, large volumes of paper information returns, and significant failures to file information returns. In addition, the Internal Revenue Service has not had the resources to pursue all nonfilers and underreporters. Further, even after the amendments made by TEFRA increased the penalties, the payor penalties continued to be subject to aggregate limitations and certain defenses. These factors may have led some payors to conclude that it was more economical to risk imposition of the penalty than to implement an effective information reporting system.

The committee amendment generally provides (1) for imposition of backup withholding at a 20-percent rate on interest, dividend, and patronage dividend payments for any periods during which identification numbers are not present beginning 45 days after the date of enactment, and (2) for backup withholding at a rate of 20 percent on payments to taxpayers who the Secretary determines failed to properly report and pay tax on interest, dividend, and patronage dividend income. In addition, there are increases in the penalties relating to information reporting and provisions designed to accelerate the matching of information returns and income tax returns so that appropriate compliance action may be taken.

Although the Internal Revenue Service receives information returns on most interest and dividend payments, it does not currently match by computer all the information returns it receives against individual tax returns. The committee understands that this problem is attributable to the absence of correct taxpayer identification numbers or other necessary information on many information returns, to the Internal Revenue Service's inability to process many of the paper information returns it receives, and to other factors, including budgetary constraints.

Even when processing is feasible, the committee understands that computerized matching cannot disclose apparent discrepancies until 17 months after the end of a calendar year. Moreover, in the case of taxpayers who file returns with underreported income, additional time (up to 9 months) is required to process returns manually, to insure that apparently unreported interest or dividends have not simply been reported in the incorrect place on an individual tax return.

The committee amendment addresses these problems by requiring substantially all interest and dividend returns to be filed in machine readable form, and imposing strict penalties for payors who negligently fail to obtain correct taxpayer identification numbers. In addition, the committee amendment requires the Internal Revenue Service to complete its matching program and to begin to notify all taxpayers identified by the matching program as having underreported more than $50 of interest, dividends, or patronage dividend income (or such lessor amount as the Secretary may determine) within 15½ months of the end of the calendar year.

The committee also understands that current Internal Revenue Service enforcement procedures collect only a small fraction of the more than $8 billion in taxes due on unreported interest and dividend income. The committee is concerned, as it was in the enactment of TEFRA, that the Internal Revenue Service has not employed the information reporting system as effectively as is desirable. In the main, this failure may be due to resource limitations and inefficiencies inherent in the collection tools provided to the Internal Revenue Service under the Code. The new 20-percent backup withholding system will provide the Internal Revenue Service with an important new tool to reduce noncompliance.

The committee amendment requires the Secretary to identify and notify all taxpayers with more than $50 of the underreported interest, dividend, or patronage dividend income disclosed by the matching program. After notification and a reasonable opportunity to correct or explain the discrepancy, the Secretary must notify payors of interest and dividends to such taxpayers to begin withholding on interest and dividends at a 20-percent rate. Generally, this backup withholding will continue until the taxes, interest, and penalties due with respect to the underreported income have been paid or otherwise collected. The committee expects to monitor the operation of the new system carefully over the next several years to insure that the Internal Revenue Service makes full use of its new tools.

The committee amendment authorizes and anticipates the enactment of the appropriations necessary to accelerate and expand the matching program and to provide for backup withholding and requires the Secretary to report to the Congress on the level of annual appropriations required for these programs.

The Secretary is excused from compliance with the directive to complete the matching and notification program within 15½ months and to begin backup withholding only if the Congress fails to appropriate expressly the amount specified in the Secretary's report, or the Secretary determines that, in the absence of such a specific appropriation, it would not be cost-effective to devote resources to interest and dividend matching and backup withholding at the expense of other enforcement activities. An annual report to the Congress is required if the Secretary determines, on these grounds, that he will not comply with the accelerated matching requirement, or that he will not follow-up all interest and dividend discrepancies above the $50 threshhold with backup withholding. The committee anticipates that any such report will disclose the reasons for the Secretary's determination and possible legislative options to facilitate backup withholding or to improve the matching program without additional appropriations. The Comptroller General is required to report to the Congress on the compliance rate for the tax year 1985. If the compliance rate is not at least 95 percent, the Committee believes that it will probably be appropriate for the Congress to review alternative compliance measures.

Explanation of Provisions

1. Withholding repeal

Under the committee amendment, mandatory withholding on interest, dividends, and patronage dividends (enacted as part of TEFRA) is repealed, effective as if never enacted.

To protect from estimated tax penalties any individual who underpaid pre-July 1983 estimated tax installments on the assumption that withholding would be effective, the committee amendment provides an estimated tax penalty exception. For purposes of computing any penalty for underpayment of estimated tax by individuals with respect to installments required to be paid before July 1, 1983, an amount equal to 10 percent of any amount of interest, dividends, and patronage dividends received after June 30, 1983, and before January 1, 1984, which would have been subject to mandatory withholding, shall be treated as a payment of tax. This determination is made without regard to whether individuals would have been exempt from withholding. Thus, if a taxpayer reduced any pre-July 1, 1983, estimated tax payment in anticipation of mandatory withholding, the taxpayer will not be subject to estimated tax payment penalties by reason of that action with respect to installments required to be paid before July 1, 1983. To the extent estimated taxes for the pre-July period would have been underpaid even if withholding had taken effect, a penalty will be imposed.

This relief provision does not extend to post-June 1983 installments. Taxpayers are required to meet their estimated tax payment obligations for the second half of 1983 without claiming any benefit that would have arisen from withholding. In addition, this relief provision does not apply unless the individual pays in full any underpayment of estimated taxes with respect to the first half of the year with the first installment paid in the second half of the year.

2. Compliance study by the General Accounting Office

The committee amendment requires that the Comptroller General of the United States (the GAO) conduct a study of interest, dividend and patronage dividend compliance and report to the Congress not later than January 1, 1988. This study will include an analysis of the existing efforts of the Internal Revenue Service to collect income tax with respect to interest, dividends, and patronage dividends and of alternative methods of improving such collections including mandatory withholding. The GAO will also determine the compliance rate for interest, dividends, and patronage dividends by dividing a reasonable estimate of the amounts of such income shown on 1985 individual returns filed by August 15, 1986, by the aggregate amount of such income reasonably estimated to have been required to be reported on those returns. It is intended that this percentage, in conjunction with the rest of the study, will be useful to Congress in connection with future deliberations with respect to tax compliance.

In making its study and report, the GAO will rely on the work of the Internal Revenue Service in matching information and tax returns, in identifying nonfilers, and in auditing taxpayers. The GAO will, in effect, supervise a compliance study of the sort that the Internal Revenue Service would otherwise conduct. Consistent with present law restrictions, the GAO will not engage in the processing of returns or the auditing of returns.

3. Backup withholding

Under present law, backup withholding on payments that are not otherwise subject to withholding is scheduled to take effect on January 1, 1984. Under these rules, withholding is required at the rate of 15 percent on certain payments to taxpayers who fail to furnish the payor with a taxpayer identification number or who refuse, after notice, to correct an incorrect number.

Incorrect or missing identification numbers

The committee amendment provides for the imposition of the backup withholding requirements of present law with respect to interest, dividends, and patronage dividends so that backup withholding will apply with respect to payments made after 45 days after the date of enactment unless the Secretary (on a case-by-case basis) delays the requirement for an additional 45 days. In addition, the backup withholding rate for interest, dividend, and patronage dividend payments is increased to 20 percent.

The committee understands that the Internal Revenue Service does not expect to commence notification of taxpayers and payors regarding incorrect identification numbers until 1984. Thus, backup withholding will commence 45 days after enactment only for new accounts or investments for which the taxpayers have provided no taxpayer identification number (or one with an incorrect number of digits). These accounts are easily identified; moreover, payors have been required to make efforts to obtain taxpayer identification numbers since 1962. To improve the reliability of information furnished to payors, statements by taxpayers making corrections of their identification numbers of providing numbers on new investments must be made under penalties of perjury.

Underreporting or failure to file

The committee amendment also imposes backup withholding, after notice, at a 20-percent rate on payments of interest, dividends, or patronage dividends to taxpayers who the Internal Revenue Service determines have either underreported interest, dividend, and patronage dividend income by an amount in excess of $50 (or any lesser amount which may be specified by the Secretary) or failed to file a Federal income tax return which was required to show any amount of interest and dividend income in excess of $50 (or any lesser amount which may be specified by the Secretary). However, the requirement that the Secretary identify and pursue every discrepancy of more than $50 applies only if adequate funding is available. In determining whether the $50 amount applies to any taxpayer, the Secretary is not obligated to take into account any amounts not reported to the Secretary on an information return.

Before backup withholding with respect to payments of interest, dividends, and patronage dividends to nonfilers or underreporters may be imposed, the Internal Revenue Service must provide at least 90 days written notice to the taxpayer. This notice must inform the taxpayer of the Secretary's determination and of the requirement that, if notified, the taxpayer's payors must institute backup withholding. The 90-day period will enable the taxpayer to respond, under procedures prescribed by the Secretary, to the notice and correct the errant condition. If the taxpayer fails to establish (to the satisfaction of the Secretary) grounds which would prevent commencement of backup withholding, notice may be sent (beginning on the 91st day after the taxpayer was notified of the determination of underreporting or failure to file), to persons known to have made interest, dividend, or patronage dividend payments to the taxpayer. The committee anticipates that such payors will be identified by comparing the names and identification numbers of delinquent taxpayers against the most recently filed information returns available. Subsequent payor notifications will be based on later filed information returns. If, during this 90-day period, the taxpayer establishes the grounds which are necessary to prevent backup withholding from commencing, the Secretary will not notify the taxpayer's payors to begin withholding.

Once notice is given, the payor has the same 15-day grace period to implement withholding that is provided in present law. Any payor required to withhold because of a taxpayer's failure to report interest, dividend, or patronage dividends, must notify the payee of such withholding at the time withholding begins.

The committee amendment provides that backup withholding will not be required if the Secretary determines to his satisfaction that (1) the failure to report income did not occur, (2) the failure (including payment of tax, penalties, or interest) has been corrected, (3) the imposition of backup withholding (because of a failure to report or an underreporting of interest, dividend, or patronage dividend income), would cause an undue hardship on the payee and that it is unlikely that any such failure will occur again, or (4) there is a bona fide dispute as to whether that failure to report or file exists. The Secretary might relieve a payee of backup withholding under the undue hardship provision if, for example, the taxpayer is unable to pay the past-due tax immediately and withholding at the 20-percent rate would result in significant overwithholding of current taxes. In determining whether a failure has been corrected, the Secretary is to take into account payments made after the statute of limitations has run on the year for which the failure occurred.

When the Secretary determines that backup withholding is no longer required with respect to a particular taxpayer, he is required (1) to promptly notify any payors who received notice to commence backup withholding and (2) to promptly provide the taxpayer with a written certification that he or she is not subject to backup withholding.

Certification of backup withholding statement

The committee amendment contains three provisions to assure that all of a taxpayer's payors receive notice of required backup withholding and that taxpayers do not avoid backup withholding by shifting their investments to new payors. Although no similar provision is included in the backup withholding system approved by the Congress in TEFRA, the committee believes that further safeguards are necessary and appropriate. First, with respect to any interest-bearing, dividend-paying, or patronage dividend-paying account, stock or other instrument established, acquired, or entered into after December 31, 1983, a payee who is not subject to backup withholding due to a failure to report an underreporting of interest, dividend, or patronage dividend income, may certify to the payor (i.e., generally, anyone required to file an information return with respect to payments of interest, dividends, or patronage dividends) under penalties of perjury if he or she is not subject to back withholding. In the case of the sale, exchange, or other disposition of any readily tradeable instrument which involves a retail broker, the purchaser may certify under penalties of perjury to the retail broker if he or she is not subject to such backup withholding. If the purchaser so certifies, the retail broker must notify the payor of such certificate within 15 days of the disposition of a readily tradeable instrument or, in the case of a sale or exchange, the settlement date. Where the purchased stock or debt instrument is held in street name (i.e., the broker is a nominee for the purchaser), the retail broker need not transmit notice to the issuer of the shares since the broker is treated as the payor for reporting purposes. In either case, however, failure to certify that backup withholding does not apply will result in backup withholding.

Generally, backup witholding will apply to any backup withholding payment made after the failure to certify. Where backup withholding is imposed because of a notification to withhold from the Secretary, backup withholding applies to any payment made after the close of the 15th day after the date of notification by the Secretary to the payor and before the payee furnishes a taxpayer identification number certificate, or corrects the errant condition and the Secretary gives notice, etc. Backup withholding applies to any payment made after the close of that period.

Any retail broker (or other person involved in the sale or exchange of a readily tradeable instrument) who intentionally disregards this requirement to notify a payor with respect to backup withholding (or taxpayer identification number) is subject to an assessable penalty of $500.

Second, the Secretary may be regulation establish a system requiring payees to submit the names of all payors from which the payee receives payments of interest, dividends, or patronage dividends.

The Committee intends the Internal Revenue Service to use its data processing resources to identify those who commit perjury, and the Justice Department to prosecute such perjury. As an adjunct to existing criminal penalties for such perjury, the committee amendment creates a new civil penalty.Finally, the Secretary may by regulation establish a computerized, confidential notification system and require payors to submit taxpayer identification numbers and names of payees to the Secretary to determine whether backup withholding is required with respect to any payee. If such a system is adopted, the Secretary may eliminate the requirement that payees certify that they are not subject to backup withholding.

To prevent improper use of information about which persons are subject to backup withholding, the committee amendment provides that any person receiving backup withholding information (including payors, payor's agents and payor's independent contractors) may use such information solely for the purpose of satisfying the backup withholding requirement. Thus, for example, a payor could not use this information, including a payee's inability to certify that he is not subject to backup withholding, in deciding whether to extend credit to the payee, to surcharge an account, to close an account, or to refuse to open an account. Use of this information for any purpose other than implementing backup withholding is a misuse of confidential taxpayer information subject to civil damages.

Under present law, the penalty for failure to withhold tax is equal to the amount of tax not withheld. Thus, in the case of small payments this penalty is small. To assure implementation of backup withholding, the committee amendment provides an additional $100 penalty for failure to deduct and withhold under the backup withholding provisions unless the failure is due to reasonable cause and not to willful neglect.

The committee amendment provides general authority under which the Secretary may prescribe regulations necessary or appropriate to implement backup withholding.

4. Information returns filed on magnetic media

Under present law, any taxpayer may request permission to file returns on magnetic media or other machine readable form. In addition, present law requires the Secretary to provide regulatory standards under which returns, other than those filed by individuals, estates, or trusts, must be filed in machine-readable form. Such a filing requirement may be imposed, however, only after the Secretary takes into account the ability of the taxpayer to comply at a reasonable cost. At present, the Secretary has required returns to be made on magnetic media only in the case of certain returns by brokers.

The committee amendment requires that taxpayers filing more than 50 information returns with the Secretary for any calendar year with respect to payments of interest, dividends, or patronage dividends must file these returns on magnetic media or other machine readable form. This requirement applies with respect to returns the due date for which, without regard to extensions, is after December 31, 1983. However, if the Secretary determines that application of this provision would cause undue hardship, he may extend the application of this provision no later than returns the due date for which (without regard to extensions) is after December 31, 1984. Granting undue hardship relief could be appropriate, for example, with respect to returns filed prior to enactment but due after the effective date or with respect to returns by payors who manually process all of their own account information. Returns due under this provision must be filed no later than January 31 of the year following the calendar year to which they relate.

The committee understands that a substantial part of the delay in matching tax returns and information returns arises out of the inability of the Social Security Administration to deliver W-2 information on magnetic tape to the Internal Revenue Service until 13 months after the end of the taxable year. The committee amendment also requires the Secretary of the Treasury, in consultation with the Secretary of Health and Human Services, to study and report to the Congress by January 1, 1984, on the feasibility of requiring wage statements (W-2's) to be filed on magnetic media.

5. Payor penalities

Failure to report identification numbers

Under the committee amendment, the present law penalty of $50 per failure by the taxpayer to furnish his taxpayer indentification number to another person, or to include the taxpayer identification number of another person in any return or other document filed with respect to that person (up to $50,000 per calendar year), is modified with respect to failures to include correct taxpayer identification numbers on information returns for interest, dividends, and patronage dividends. First, the $50,000 limitation on the amount of penalties on a payor for any year is eliminated. Second, the $50 penalty is increased to $100 in the case of substantial noncompliance. Substantial noncompliance exists with respect to any payor if the total number of failures to include correct identification numbers or to file information returns or statements with respect to interest, dividends, and patronage dividends exceeds the lesser of 10,000 failures or 5 percent of the total number of such returns or statements required to be filed by the payor for any calendar year. Third, a specific set of statutory exceptions is substituted for the general reasonable cause exception of present law. Under these exceptions, no penalty is imposed if

(a) the payor reports an identification number which was provided by the payee under penalties of perjury, unless the number provided contained an incorrect number of digits;

(b) in the case of any failure to obtain a correct taxpayer identification number on the sale, exchange or disposition of a readily tradeable instrument, the payor includes a number provided by a retail broker or (under regulations) another party to the exchange;

(c) under regulations, the payee is awaiting receipt of an identification number; and

(d) with respect to existing accounts (as defined below), and certain new investments in readily tradeable instruments, the payor establishes to the satisfaction of the Secretary that the payor exercised due diligence in attempting to obtain the correct identification number.

In addition, this penalty may be abated if the Secretary determines that the failure could not have been prevented without undue hardship. Undue hardship would be determined under principles analogous to those described under the new information return or statement penalty (below).

In general, an "existing account" is, in general, any investment resulting in the payment of interest, dividends, or patronage dividends made on or before the thirty-first day after the date of enactment. In particular, in the case of interest the account, deposit, obligation, certificate or similar instrument must have been established or acquired before the thirty-first day after the date of enactment to be eligible for the due diligence exception. In the case of dividends, stocks or other instruments acquired before such thirty-first day are existing accounts. In the case of patronage dividends, accounts are existing memberships acquired and contracts entered into before the thirty-first day after the date of enactment.

A readily tradeable instrument is any instrument which is part of an issue any portion of which is traded on an established securities market (within the meaning of section 453(f)(5)), or is regularly quoted by brokers or dealers making a market. In general, a retail broker is any person who deals directly with the purchaser of a readily tradable instrument and participates in the purchase of such instrument, or maintains an inventory of such instruments for sale to others, in the ordinary course of the trade or business.

To satisfy the requirement for due diligence and thus avoid any penalty for erroneous or missing taxpayer identification numbers on existing accounts, etc., the payor must furnish various written notices to the payee. These notices must notify the payee of (1) what a taxpayer identification number is, (2) the requirement that correct numbers be provided, (3) the nature and amount of penalties for failure to provide correct identification numbers, (4) the possibility of backup withholding where an erroneous number (or no number) is provided, and (5) how to provide a correct number. This type of notification constitutes due diligence if given annually except that in 1983 it must be given more frequently. Of course, in all years, more frequent notice is permitted.

For 1983, if a payee has not provided an identification number or has provided an obviously incorrect number, notice must be provided on three different occasions. In other cases, notice must be provided twice in 1983 (unless the payee has more than one regular mailing to the payee in 1983 beginning 31 days after the date of enactment in which case three mailings are required). The first required mailing in 1983 and the mailing required in 1984 must be sent in a separate first-class mailing and contain a prepaid postage reply envelope and a form for certifying the correct number under penalties of perjury. After 1984, the annual mailing need not be sent separately or include a postage prepaid envelope, but it must include a form for certifying the correct number under penalties of perjury.

If, in the case of a sale, exchange, or other disposition of a readily tradeable instrument involving a retail broker (other than a retail broker who is the payor with respect to such instrument), the broker fails to obtain a taxpayer identification number certificate under penalty perjury, or fails to pass a number to the payor, the payor is subject to a penalty unless he exercises due diligence to obtain a correct number from the payee. In this case, due diligence will consist of (1) the payor deducting and withholding backup withholding tax on payments to such payee, (2) the payor mailing to the payee within 60 days of the date of the sale, exchange, or other disposition (by a separate first-class mailing) a notice containing the five items described above and, (3) the payor including in such notice the penalty of perjury form on which the payee may include his correct taxpayer identification number, and a postage prepaid envelope in which the payee may return this form to the payor.

If there is an obviously incorrect number or no taxpayor identification number, the due deligence defenses are not available with respect to the return for any particular account unless the payor deducts and withholds from the account under the backup withholding rules. Thus, the absence of a taxpayer identification number will always result in backup withholding or a payor penalty, or both.

It is anticipated that notice with substantially the following content will be adequate if presented in a legible manner in 12-point leaded type; however, other forms of notice may also be adequate:

IMPORTANT TAX INFORMATION

Under the law, you are subject to penalties and withholding at a 20-percent rate if you have not provided us with your correct social security or other tax identification number. Please read this notice carefully.

The law requires that we maintain accurate taxpayer identifcation numbers for all accounts of individuals, corporations, estates, trusts and partnerships. For individuals, this number is the nine digit social security number. For other taxpayers, it is their employer identification number. These numbers are used by the Internal Revenue Service to associate and verify payments to income recipients with corresponding amounts on tax returns.

The penalty for failure to provide a correct number is $50 which may be asserted by the Internal Revenue Service. If you have not provided any number or the Internal Revenue Service notifies us that your number is incorrect, we will withhold 20 percent of income payments to you and deposit this amount with the Internal Revenue Service. Once tax is withheld, you will have to apply to the Internal Revenue Service to receive a credit or refund of that amount.

If the taxpayer identification number we have for you is incorrect or if you have not provided us with a number, you may satisfy your legal obligations by signing the enclosed certification and returning it to us.

Failure to file information returns or statements

Under the committee amendment, the present law penalty for failure to file information returns or statements with respect to interest, dividends, and patronage dividends ($50 per failure, up to $50,000 per year), is modified by eliminating the $50,000 limitation and increasing the penalty to $100. In the case of substantial noncompliance (as defined in the case of failure to supply correct taxpayer identification numbers), the penalty is increased to $200. The reasonable cause defense and increase in cases of intentional disregard provided for in present law are eliminated for interest, dividend, and patronage dividend payments. However, the Secretary is authorized to abate any portion of the failure-to-file penalty (and any related interest or penalties for failure to self-assess), if the Secretary determines that the failure could not have been prevented without undue hardship. Both penalties must be self-assessed under the rules described below. For this purpose, undue hardship would exist when, because of a supervening event or physical constraint (e.g. an earthquake, flood, or civil disturbance), the taxpayer is unable to comply without incurring costs that would be disproportionately high when compared to the costs that otherwise would be incurred complying with the law, or is prevented from complying.

Special rules for dispositions of readily tradeable instruments

In the case of any disposition of a readily tradeable instrument the settlement date for which is more than 30 days after the date of enactment, the retail broker must obtain a taxpayer identification number from the purchaser under penalty of perjury. Failure to do so will result in a $50 penalty per failure. This special rule does not apply in the case of an instrument held in street name, since the retail broker is treated as a payor with respect to that instrument.

The retail broker must then provide this certified number to the payor, if the stock or debt instrument purchased will be issued in the name of the purchaser, i.e., not held in street name by the broker. The penalty for failure to obtain a correct identification number does not apply to payors who rely on numbers furnished by a retail broker (or other person). This rule reflects the fact that the payor may not have the opportunity to insist on a sworn certificate from the payee since the payor is not a party to the payee's purchase transaction. Payors may, of course, seek to obtain a sworn certificate to avoid further obligation to exercise due diligence.

If the payor receives no identification number from the broker (or an obviously incorrect number) and fails to provide a correct tax identification number on the return, then the payor is subject to the penalty for failure to provide an identification number unless the payor deducts and withholds under the backup withholding rules, and the payor exercizes due diligence to obtain a correct number. This rule does not apply in the case of an instrument held in street name, since the retail broker is treated as a payor with respect to that instrument.

This rule may be illustrated as follows: Assume individual A purchases two blocks of stock a year after enactment through a long-established brokerage relationship. If A provides a sworn statement of his identification number to the broker and the broker provides it to each of the payors who use it, no penalty will apply to the payors or brokers even if the number or statement is wrong (in which case backup withholding could be imposed by the Secretary). If the broker neglects to demand an identification number certificate, he or she is liable for the penalty once with respect to each purchase of stock even if he provides a number to the payors (out of pre-existing but unsworn records) No penalty is imposed on a payor relying on that number, even if it is incorrect. But if the number is incorrect, backup withholding could be imposed. If the payors received no number from the broker, they must apply backup withholding and notify the payee within 60 days (and annually thereafter) that backup withholding is required by the absence of the identification number.

Assessment of penalties

The committee amendment provides that the penalties for failure to supply correct identification numbers or to file information returns or statements with respect to interest, dividends, or patronage dividends shall be treated as an addition to tax on the first return of income of the payor due after the calendar year with respect to which the information returns are filed. However, if the return is due (without regard to extensions), less than 30 days after the returns or statements are required to be filed, the penalty is payable with the first succeeding income tax return. For example, if a calendar year taxpayer fails to file information returns for calendar year 1984, the tax return which is due on March 15, 1985, should include the penalty for that failure. If the payor is not required to file a return of income tax, the Secretary will prescribe the form for self-assessment of the penalty. The Secretary may by regulations provide that taxpayers may make application for abatement. The Internal Revenue Service could be authorized under such regulations, where appropriate, to suspend the requirement to pay the penalty until the Secretary had determined whether to grant the abatement request. However, if the request was not approved, interest would be owing from the due date of the return.

6. Attachment of information returns to individual tax returns

The committee amendment requires that payees be furnished (in person or by first-class mail) a statement in duplicate of any interest, dividend, or patronage dividend information return filed with respect to them. Statements and copies must be in the form required by the Secretary and must be attached to the payee's income tax return for the relevant taxable year. Failure to attach these statements will be subject to a penalty of $50 for each statement that is not attached to the return with no cap, unless the failure was due to reasonable cause and not willful neglect. It is anticipated that the Secretary will require information return statements provided to payees to be in a form similar to the form currently used for wage statements in order to ensure that the taxpayer is apprised of the importance of the form and of the penalty for failing to attach the statement to his income tax return.

7. Payee penalties for failure to report income

The committee amendment imposes a civil penalty of $1,000 on taxpayers who fail to include on a return any amount of interest, dividend, or patronage dividend income as the result of a willful attempt to evade or avoid any Federal income tax on such income. This penalty is an addition to tax to which the deficiency procedures will apply and is in addition to all other penalties.

The committee amendment also imposes a penalty of $1,000 for each false certification or affirmation with respect to a taxpayer identification number or backup withholding status which the Secretary establishes any individual willfully made. While the deficiency procedures do not apply to this penalty, procedures are provided under which the taxpayer may obtain pre-enforcement review of the Secretary's determination that the penalty is owing on payment of 15 percent of the demanded amount and filing a claim for refund, and under which the burden of proof is on the Secretary.

The Committee understands that this penalty will provide even greater assurance that intentional noncompliance through filing false certificates will not permit evasion of the backup withholding system than existed for mandatory withholding.

8. Acceleration of information matching programs

The committee amendment requires the Internal Revenue Service to undertake the matching of information returns with respect to interest, dividends and patronage dividends so that inquiries with respect to discrepancies may be made to taxpayers by 15½ months of the close of the calendar year with respect to which the information returns are filed. But such matching and inquiry is required only if such action is justified by a cost-benefit analysis or specific appropriations are made for that purpose. It is anticipated that compliance with this requirement may require an acceleration of the time for filing information returns, a shortening of the standard period of extension of the time for filing individual tax returns, two computer runs of the Internal Revenue Service master file rather than the one presently needed at the beginning of the calendar year following the year for which returns are filed and changes in return formats to require separate listing of interest, dividends, and patronage dividends subject to information reporting. In addition, a significant increase in Internal Revenue Service staffing may be necessary. If the 15½-month matching program is not implemented, the Secretary must report this to the Congress.

The committee amendment requires the Secretary of the Treasury to report to the Congress on the additional appropriations necessary to improve interest and dividends information processing in accordance with the committee amendment. The committee anticipates that the Secretary's initial report to the Congress on needed appropriations, and any annual report that may be filed thereafter, will include information on relevant IRS managerial decisions, and discussion of legislative options to improve the matching and notification program and to implement backup withholding without substantial additional appropriations.

For example, the committee would be interested in knowing whether redesign of the individual tax return to include separate line items for interest or dividends reported on information documents, or a complete listing of all interest and dividend payments, could substantially reduce or eliminate the need to allocate time and resources for manual processing of returns. Information of this nature is already required to be reported to the Congress by June 30, 1983 (sec. 353 of TEFRA). The committee would also be interested in an evaluation of the costs and benefits of notifying taxpayers whenever a discrepancy was disclosed, without manual processing of an individual tax return. Among the benefits to be evaluated in this regard would be preventing recurring errors by taxpayers who improperly report amounts of income without underreporting such amount. Similarly, the committee would be interested in learning the extent to which information return discrepancies are generated inappropriately in the case of informal trust, co-ownership, and joint accounts, where it turns out that ostensibly unreported income is properly reported by an individual other than the taxpayer identified by the payor on an information return. In this regard, the committee understands that the Secretary currently has the authority to require payees to disclose, and to require payors to report on information returns, the name and identification numbers of the individuals whom the payees believe are required to report payments of interest and dividends on their individual tax returns. The committee would be interested in learning whether adoption of such a requirement by regulation would facilitate compliance by the Secretary with the requirement to accelerate and expand the information returns matching program.

For example, the committee would be interested in learning how many notices the Internal Revenue Service currently furnishes to underreporters and nonfilers, and what pattern of voluntary response is experienced. To the extent the rate of nonfrivolous voluntary responses is high, the committee would be interested in learning what level of resources are needed to process responses. In addition, the committee would be interested in learning what resources are needed to notify payors of backup withholding requirements, and to process corrections, disputed cases, and exemptions after withholding has commenced. The committee would be interested in an evaluation of the costs and benefits of establishing the computerized notification system authorized to be implemented by regulations, especially if the Secretary determines that account shifting to avoid backup withholding is a potential problem.

Finally, the committee would be interested in learning whether the penalty provisions of this committee amendment, and the backup withholding provisions of TEFRA, are effective in improving the accuracy of identification numbers furnished on information returns.

The committee amendment authorizes and anticipates the enactment of the appropriations necessary to accelerate and expand the matching program and to provide for backup withholding and requires the Secretary to report to the Congress on the level of annual appropriations required for these programs.

The Secretary is excused from compliance with the directive to complete the matching and notification program within 15½-months and to begin backup withholding above the $50 level, only if the Congress fails to expressly appropriate the amount specified in the Secretary's report, or the Secretary determines that, in the absence of such a specific appropriation, it would not be cost-effective to devote resources to interest and dividend matching and backup withholding at the expense of other enforcement activities. An annual report to the Congress is required if the Secretary determines, on these grounds, that he will not comply with the accelerated matching requirement, or that he will not follow-up all interest and dividend discrepancies above the $50 threshold with backup withholding. The committee anticipates that any such report will disclose the reasons for the Secretary's determination and possible legislative options to facilitate backup withholding or to improve the matching program without additional appropriations.

Effective Dates

In general, the provisions of the committee amendment are effective for taxable years beginning after 1982. Thus, mandatory withholding on interest, dividends, and patronage dividends is repealed as if never enacted.

The backup withholding provisions are generally effective 45 days after the date of enactment, except that the Secretary may extend the effective date for up to an additional 45 days if compliance by any payor would cause undue hardship. In addition, the effective date of present-law backup withholding is conformed to match the effective date of these amendments.

The magnetic requirement is effective for returns the due date of which (without extensions) is after 1983, except that the Secretary may extend the effective date for individual payors to such returns the due date of which (without extensions) is after 1984, to prevent undue hardship.

The new payor penalties and requirement to attach 1099s to returns generally apply to returns due (without regard to extensions) after 1983. However, if no interest, dividend, or patronage dividend income was paid or credited after 30 days after the date of enactment, these amendments do not apply.

Revenue Effect

It is anticipated that the repeal of withholding on interest and dividends will reduce fiscal year budget receipts by $0.3 billion in 1983, $2.5 billion in 1984, $2.5 billion in 1985, $2.5 billion in 1986, $2.7 billion in 1987, $2.9 billion in 1988, with a total of $13.4 billion for years 1983 through 1988.

It is anticipated that if adequate funding is provided to the Internal Revenue Service, the compliance portions of the committee amendment would increase fiscal year budget receipts by $0.3 billion in 1985, $0.9 billion in 1986, $1.7 billion in 1987, $2.0 billion in 1988, with a total of $4.9 billion for years 1983 through 1988.

21-334 O - 83 - 4

TITLE II—CARIBBEAN BASIN ECONOMIC RECOVERY ACT

A. SUMMARY

Subtitle A of title II provides for the waiver of duties until September 30, 1995, on products imported from 27 Caribbean and Central American countries. Beneficiary countries must meet several criteria before the President is authorized to designate them as eligible for this program. Further, several products cannot be declared duty free, and pursuant to current law, duty-free treatment may be withdrawn for articles imported in such quantities as to threaten injury to a competing U.S. industry. A rule of origin specifies under what conditions articles will be considered products of a beneficiary country, and therefore entitled to duty-free entry.

Subtitle B would allow the deduction of reasonable business expenses for attending conventions held in an eligible beneficiary country, if that country (1) agrees to exchange information to enforce tax laws, and (2) does not discriminate against U.S. convention sites in its tax law.

Title II also provides certain benefits for Puerto Rico and the Virgin Islands. These include: (1) an increase in the amount of alcoholic beverages that may be brought back free of duty into the United States from an insular possession by a returning resident; (2) the transfer to them of excise tax revenues from foreign rum brought into the United States; (3) the exemption of a Virgin Islands rum production plant from certain requirements of the Federal Water Pollution Control Act; and (4) the inclusion of insular possessions' producers among those entitled to seek import relief under section 201 of the Trade Act of 1974.

B. BACKGROUND—THE CARIBBEAN BASIN INITIATIVE

Title II of the Committee amendment embodies the substance of S. 544, which was approved with amendments by the Committee on May 12 and May 26, 1983. It implements the "Caribbean Basin Initiative" (CBI), an economic recovery program for nations of the Caribbean Sea and Central America announced by President Reagan on February 24, 1982, in an address to the Organization of American States. The President's announcement outlined the U.S. contribution to an agreement by the governments of Canada, Mexico, Venezuela, and Colombia to join in a multilateral effort to foster economic development in the region. As described further below, U.S. efforts will require authorizing legislation only in part. Title II, by creating a program of trade preferences, forms a principal part of the U.S. effort but cannot be implemented under existing authority.

The donor countries agreed to a regional rescue plan because critically dangerous circumstances, rooted in economic difficulties, threaten the stability of the entire region. The United States in particular has a large stake in participating in such cooperative assistance efforts. The seven countries of Central America and twenty island nations of the Caribbean Sea that are the potential beneficiaries of the CBI comprise a broad southern border of this country.

Together with the other donor nations and Puerto Rico and the Virgin Islands, these lands increasingly share economic and political ties commensurate with their geographical proximity. But historically only limited integration has occurred, either among any groups of these nations or with the United States, and this has inhibited cooperative efforts to address common problems. This lack of close association arises from a wide divergence among the countries in origin, language, culture, economies, and democratic traditions.

The countries now grouped in the "Caribbean Basin" are generally small geographically and in population. Many were, until relatively recently, European colonies. More than a dozen of these countries attained independence only in the last two decades, and many remain tied to their former rulers (France, Spain, the Netherlands, or the United Kingdom) through commonwealth or trade preference arrangements. As these colonial ties have dissolved, however, the countries have attempted to augment their traditional trading patterns with intra-Caribbean and intra-Central American common market arrangements. Neither arrangement currently offers significant growth potential, and ties between the isthmus and the island nations never have developed to a substantial degree. Testimony to the Committee attributed the current economic malaise in the region at least in part to this rupture of traditional markets combined with the inability--due to lack of size, resources, and cooperation—of the countries to build new ones.

Besides these changes in trading patterns, the countries in recent years have suffered a damaging combination of declining prices for principal export commodities (sugar, coffee, bananas, and bauxite) and fast-rising costs for energy and other essential imports. The Basin countries as a whole now suffer serious balance-of-payments difficulties, high inflation rates, high unemployment, and low or negative growth rates. The World Bank estimates that the balance-of-payments gap for these countries reached $1 billion in 1982.

Immigration increasingly links the United States and the countries of the Caribbean Basin. The region's population doubled between 1950 and 1980, and may redouble before the turn of the century. Seeking political or economic emancipation, increasing numbers of this growing population have emigrated legally or illegally to the United States. Some estimate that over 10 percent of the population of several Caribbean nations now reside in the United States. Current U.S. aid to Haiti already is dwarfed by the $150 million in basic medical services extended by the State of Florida alone to illegal Haitian immigrants. The Administration estimates that over $1 billion has been spent on operations and services related to the 135,000 Cuban and Haitian refugees that arrived in this country in recent years.

More importantly, the United States has critical security and economic interests in the region. These nations bracket vital U.S. sea lanes and the Panama Canal. Economically, the Basin is a demonstrated and growing market. The United States already accounts for a large share of the imports of the Caribbean Basin countries; total U.S. exports there in 1982 exceeded $6.3 billion and U.S. direct investment approximated $5.65 billion. Total U.S. imports from the Basin in 1982 exceeded $8 billion. Over 2.5 million U.S. tourists in 1980 spent in excess of a billion dollars in the region.

The following trade data for the region show that in 1982, U.S. exports declined after several growth years. Further, the data reveal that absent petroleum imports, this country exports nearly twice what it imports from the region. By a large margin, the United States is the principal supplier in the region, but this market is in danger of serious contraction without economic development assistance.

U.S. EXPORTS TO AND IMPORTS FROM CBI COUNTRIES—1979-82

[Dollars in millions]

	1982		1981		1980		1979	
	U.S. Exports	U.S. Imports	U.S. Exports	U.S. Imports	U.S. Exports	U.S. Imports	U.S. Exports	U.S. Imports
Country:								
Bahamas	585	1,045	435	1,243	391	1,373	330	1,602
Barbados	152	107	146	81	134	96	118	57
Belize	60	38	65	42	52	58	54	31
Cayman Island	72	15	58	5	54	3	34	2
Costa Rica	327	358	370	365	493	357	410	392
Dominican Republic	649	623	762	922	786	790	603	664
El Salvador	264	310	302	259	267	426	345	443
Guatemala	385	330	550	347	546	431	458	409
Guyana	55	71	105	104	96	120	73	65
Haiti	293	310	296	276	303	253	238	222
Honduras	261	360	338	431	369	418	318	412
Jamaica	460	278	468	357	302	379	290	369
Netherlands Antilles	648	2,107	485	2,599	438	2,537	404	1,810
Nicaragua	118	87	182	140	247	214	100	234
Panama	825	251	833	297	688	324	519	190
Suriname	127	60	137	179	134	109	112	106
Trinidad and Tobago	880	1,628	681	2,215	673	2,385	456	1,553
Turks and Caiman	8	4	5	4	3	3	3	2
Windward and Leeward Islands [1]	169	27	275	32	149	34	96	33
Total	6,339	8,008	6,493	9,899	6,124	10,309	4,960	8,597
Total excluding petroleum imports	6,339	3,416	6,493	4,085	6,124	4,269	4,960	3,873

[1] Anguilla, British Virgin Islands, St. Christopher-Nevis, Antigua and Barbuda, Montserrat, Dominica, St. Lucia, St. Vincent and the Grenadines, Grenada.

In announcing the CBI, President Reagan offered an integrated package of aid, trade, and investment measures designed to spur long-term, market-oriented development in the beneficiary countries. Not all of the measures required legislative action. For example, the Administration encouraged the Overseas Private Investment Corporation to expand its political risk insurance program and its financing efforts; expanded Ex-Im Bank protection for short-term credit; commenced negotiating bilateral investment treaties with beneficiary countries expressing an interest in such agreements; and negotiated more favorable treatment for textile and apparel imports within overall U.S. textiles policy. These measures have been initiated.

The President further sought legislative authority to create for 12 years a one-way free trade zone with the countries; to expend $350 million in supplemental fiscal year 1982 aid funds; and to extend certain tax incentives for investment in the countries. In the 97th Congress, the House of Representatives and the Finance Committee approved an amended version of the one-way free trade area, excepting certain products from it. These bodies also rejected the proposed extension of the domestic investment tax credit to investments in the beneficiary countries. Substituted instead was authority to extend North American convention tax status to countries that agree to exchange-of-information agreements regarding enforcement of the tax laws. The Senate did not act on the bill as reported by the Committee on Finance.

The Congress did approve fully the supplemental aid request. Secretary of State Shultz testified to the Committee, at hearings on S. 544 held April 13, 1983, that these funds were obligated for balance-of-payments support and infrastructure development in the least developed countries, and for private sector assistance in countries with serious financial problems. Further, a portion of the funds was obligated to support 1,300 training and education scholarships for individuals from the region. The administration increased significantly its requests for fiscal years 1983 and 1984 to continue and to improve these programs. As a percentage of the overall economic assistance budget, assistance to the Caribbean region will double in fiscal years 1983 and 1984 compared to 1980; it will constitute 13.6 percent of the total assistance proposed for fiscal year 1984.

The other donor countries also have initiated their contributions to the multilateral effort. Canada provides duty-free or preferential treatment for 98 percent of its Caribbean Basin imports, and has implemented a $500 million, 5-year assistance program. Mexico and Venezuela have maintained a program of concessional financing linked to their petroleum sales to the beneficiary countries. Mexico further provides preferential trade treatment to certain Caribbean-sourced products, and other technical and financial assistance. Venezuela and Colombia also are offering technical and financial assistance.

Title II embodies the trade incentives designed to complete the collective, integrated development program. It is intended to create limited, but assured, market access as a means for Caribbean producers to take advantage of the other development assistance. In addition, the title would authorize, under specific conditions, the deduction of business expenses associated with attending conventions in the beneficiary countries. This incentive is designed to spur development of the indigenous tourism industry.

C. GENERAL EXPLANATION OF TRADE AND TARIFF PROVISIONS (SUBTITLE A)

Present Law

The President has no current authority to reduce import duties. Section 101 of the Trade Act of 1974 (19 U.S.C. 2111), the President's basic tariff negotiating authority, expired in 1979.

Certain products originating in all of the potential beneficiary countries are currently eligible for preferential, duty-free entry into the United States pursuant to the Generalized System of Preferences (GSP). The GSP imposes several restrictions on the types and total value of imports of articles that are entitled to its benefits. Authority for the program, set forth in Title V of the Trade Act of 1974 (19 U.S.C. 2461-2465) expires January 3, 1985. In 1982 the CBI countries exported approximately $554 million of products to the United States duty-free under the GSP. (In addition, approximately $1.9 billion entered duty-free because of zero-duty most-favored-nation tariff rates.)

The Committee Amendment

Overview

Title II, as approved by the Committee, would authorize the President to proclaim, until September 30, 1995, duty-free treatment of imports from designated Caribbean Basin sources. This preferential treatment is subject to several conditions, as set forth in subtitle A.

First, products must be imported from eligible countries. Eligibility is defined according to binding and nonbinding criteria. For example, a beneficiary must be from among nations specified in the bill, and it cannot be Communist. Other criteria for eligibility are directed at the nations' treatment of U.S. private property. Thus, the bill requires a finding that any country that has expropriated U.S. property must be resolving any resulting dispute in accord with international law. Further, an existing discriminatory trade preference arrangement must be adjusted to eliminate any significant adverse effects it causes to U.S. commerce. A country must cooperate with U.S. efforts to interdict drug trafficking. Finally, a government must not be pirating broadcasts of U.S. copyrighted material and it cannot be party to an international agreement relating to extradition of U.S. citizens. The President, however, may waive certain of these requirements in the national security or economic interest.

Although they are nonbinding, the subtitle also sets forth several indicia of free market policies and good labor practices the President must take into account in determining the fitness of a potential beneficiary for inclusion in the CBI's trade preference scheme.

As a condition of maintaining eligibility, a country must maintain an approved "Stable Food Production Plan." These plans will consist of domestic programs to ensure that the CBI benefits do not adversely affect food crop production because of incentives to increase sugar and beef production for export.

Under subtitle A, the Congress retains some control over the designations. The President must notify and explain to Congress any decision to designate or to disqualify a beneficiary nation. He must also provide Congress a copy of his determination concerning countries involved in expropriation disputes or in damaging, discriminatory preference arrangements, and of any affirmative beneficiary determination based on national interest grounds.

Once designated as a beneficiary, a CBI country may export any article to this country duty-free, subject to certain exceptions, source requirements, and safeguard restrictions.

The following products are excepted from the duty-free authority of the title: (1) textile and apparel items that are subject to textile agreements; (2) certain articles that are not GSP-eligible (footwear, handbags, luggage, flat goods, work gloves, and leather wearing apparel); (3) containerized tuna; and (4) petroleum and petroleum products. In addition, sugar imports will be subject to measures to prevent interference with the domestic price support program.

Under existing law, increased tariffs or quotas may be imposed on products that are being imported in such quantities or under such conditions as to injure seriously a domestic industry or to threaten the national security (respectively, section 201 of the 1974 Trade Act, 19 U.S.C. 2251, and section 232 of the 1962 Trade Expansion Act, 19 U.S.C. 1862). These laws would apply to products imported under this program. Under subtitle A, suspension of the duty-free treatment afforded by this bill could be treated as an increase in duties if the International Trade Commission determines, pursuant to an investigation under section 201 of the 1974 Trade Act, that the serious injury to a domestic industry results from the duty-free treatment afforded by this bill.

The committee amendment further provides for a "fast-track" mechanism by which the President may proclaim, pending completion of an investigation under section 201 by the ITC, temporary suspension of duty-free treatment for certain perishable products. The Secretary of Agriculture is charged with making such a recommendation to the President within 14 days of a petition to do so, and the President must issue his determination within 7 days thereafter.

Besides providing rules for country and product eligibility, subtitle A establishes rules to determine whether any particular article for which duty-free treatment is sought qualifies as a product sourced in the eligible countries. The rules of origin are (1) that the article must be imported directly from a beneficiary country, and (2) it must contain at least 35 percent cumulative local value added within the eligible Basin countries (plus Puerto Rico and the Virgin Islands), 15 percent of which can be of U.S. origin. This percentage is the same percent rule as that required under the Generalized System of Preferences. The value must be the value of the materials plus the direct costs of manufacturing, as defined in the bill. Products merely packaged or diluted with water will not qualify for duty-free treatment.

Products imported from the insular possession currently are subject to MFN duty rates if they contain greater than 50 percent foreign value (70 percent for watches). The subtitle further would liberalize this rule to increase the allowable foreign value added to 70 percent for all products except those not entitled to duty-free entry under the bill. Those products would remain subject to the 50 percent rule.

Subtitle A also provides certain benefits and protections for Puerto Rico and the Virgin Islands. These include: (1) an increase in the amount of alcoholic beverages that may be brought back into the United States from the insular possessions by a returning resident; (2) authority to withdraw duty-free treatment of rum; (3) the exemption of a Virgin Islands rum production plant from certain requirements of the Federal Water Pollution Control Act; and (4) the inclusion of Puerto Rican and Virgin Islands producers among those entitled to seek import relief under section 201 of the Trade Act of 1974.

Section-by-Section Analysis

Section 201 creates the short title of the legislation, the "Caribbean Basin Economic Recovery Act."

Sections 211 and 216 (proclamation authority)

These sections confer authority upon the President to proclaim the duty-free treatment delineated elsewhere in the bill. This authority commences on the date of enactment and expires September 30, 1995.

Section 212 (eligible beneficiary countries)

Section 212 sets out the universe of nations potentially eligible for CBI benefits, and criteria that guide the President's decision to proclaim their individual eligibility.

Subsection (a): beneficiary country

Under subsection (a), "beneficiary country" means a nation that the President proclaims is eligible for the benefits extended under subtitle A. Before proclaiming such eligibility, the President must notify the Congress of his intention to do so and the reasons therefor. In addition, prior to terminating the beneficiary status of an eligible country, the President must provide the Congress with 60-days notice of this intent and the reasons for the decision. Termination of eligibility may occur, for example, pursuant to subsection (e) (conditions leading to eligibility have changed) or section 213(c) (failure to maintain a Stable Food Production Plan). The 60-day notice will allow the country time to redress the changed circumstances if it desires to do so, and further will provide sufficient notice for commercial transactions founded on CBI benefits to be adjusted as needed.

The terms "entered" and "TSUS" are defined for convenience of reference.

Subsection (b): eligibility requirements

Subsection (b) imposes certain specific limitations on eligibility. A beneficiary country cannot be a country or territory (or successor political entity) other than one listed in this subsection. The Committee amended S. 544 to delete Cuba from this list, although that nation would not have qualified in any case under the criteria described below.

Even if a country is on the list of potentially eligible countries, it must further satisfy the following requirements:

(1) *It cannot be a Communist country.*—Although this description is not intended to, and cannot, be a precise definition to be inflexibly applied in every case, the Committee intends that it shall be interpreted in accord with the historic meaning attached to it in other trade and economic assistance laws; that is, "dominated or controlled by communism." *See* Trade Reform Act of 1974, Report of the Committee on Finance on H.R. 10710, Rep. No. 93-1298, p. 213 (1974). This particularly implies a country's relationship with the Soviet Union. The Committee considered whether, despite this ban, Grenada and Nicaragua should be stricken from the list of eligible countries because of the self-proclaimed Marxist nature of the governments. The Committee, however, accepted the observations of the Secretary of State, and U.S. Trade Representative that without substantial change in their current policies, these two countries do not qualify under several of section 102(b)'s criteria. Further, the Committee is persuaded that because a significant private sector presence remains in these countries—and, indeed, is responsible in large measure for maintaining their economic viability—and that within the 12-year life of the program circumstances may change, on balance Grenada and Nicaragua should remain on the eligibility list.

(2) *The country must abide by international law with regard to expropriation of U.S. property.*—This means that if a nation has taken steps in fact or in effect to expropriate U.S. property (i.e., property 50 percent beneficially owned by U.S. citizens), it must take steps to provide prompt, adequate, and effective compensation. This may occur through direct negotiation or through some appropriate means of dispute settlement. If the President certifies to the Congress that the country is taking such steps to resolve in good faith the question of compensation, then the criterion will not be an automatic bar to eligibility.

The Committee amended the language of this subsection to make clear that it applies to the taking of intellectual and intangible property, as well as real property. U.S. trade interests increasingly involve matters affecting these types of property rights, and all should be protected.

The Committee further notes that, while most expropriation cases in the region are being settled or have been settled with little difficulty, at least two have been outstanding for an inordinately long period. These are separate cases involving the Government of Panama and, respectively, the Boston Panama Company and Citricos de Chiriqui. With regard to the first, a settlement apparently was agreed to but payment withheld by the Panamanian Government. In the second, a settlement has not been reached.

The CBI offers beneficiary countries a unilateral, one-way trade preference program as an incentive for their economic development. It is appropriate to seek in return good faith actions with respect to U.S. trade interests, particularly where, as here, there appears to be no question under international law that the companies are entitled to prompt, adequate, and effective compensation. Fur-

21-334 O - 83 - 5

ther, it is in the best interest of developing countries to demonstrate good faith in these matters as a way of assuring stability to interested foreign investors who offer the possibility of creating new business and employment opportunities.

The Committee concurs in the Administration's position not to finalize the pending Bilateral Investment Treaty with Panama until the two outstanding disputes are resolved. It understands further that the Department of State, as shown in the following letter, takes the same position with regard to extending CBI benefits to Panama should it be established that the properties were nationalized, expropriated, or otherwise seized, and Panama refuses good faith efforts to settle the dispute. The Committee intends this subsection to be interpreted accordingly.

U.S. DEPARTMENT OF STATE,
Washington, D.C.

Hon. ROBERT DOLE,
U.S. Senate.

DEAR SENATOR DOLE: In your mark-up of the Caribbean Basin Initiative legislation, the question of outstanding investment disputes was raised and the Department of State promised to provide the Committee with a letter clarifying how the CBI legislation might help us resolve outstanding disputes.

The Administration has acted strongly to encourage a settlement of U.S. citizen claims in the Boston-Panama and Citricos de Chiriqui, S.A., cases. In the Boston-Panama case, Department of State officials obtained commitments at the highest level from the Panamanian Government that they would proceed to settle the claim. Although the Government of Panama has not yet settled the matter as promised, it has established a commission to review the case.

While awaiting the results of the review, we continue to express high-level interest in all outstanding cases and have linked these outstanding investment disputes to the bilateral investment treaty, to the designation process in the Caribbean Basin Initiative legislation and to other issues.

As soon as the CBI legislation is passed, the Department will send a high-level team to each country to discuss the designation process. First on the agenda of the team to visit Panama will be discussion of all outstanding investment disputes. We will advise the Panamanians that should it be established that the properties were nationalized, expropriated or otherwise seized, and if good faith efforts to resolve these disputes as they promised can no longer be expected, then we would not recommend to the President that he grant a waiver under 102(b).

Sincerely,

JAMES H. MICHEL,
Deputy Assistant Secretary for Inter-American Affairs.

(3) *The country must act in good faith in recognizing as binding, or in enforcing, arbitral awards in favor of U.S. citizens.*—This may occur, for example, where the disputants agreed to submit the controversy to a mutually agreed upon arbitral panel.

(4) *The country must not grant preferential trade treatment to their imports of products from a developed country, if that treatment significantly and adversely affects U.S. commerce.*—The Committee encourages other developed countries to offer assistance to the Caribbean Basin nations, and some in fact do. But this assistance should not be at the expense of the United States. The Committee believes that if a beneficiary nation takes advantage of preferential access to the U.S. market, it should not injuriously discriminate againts U.S. exporters in favor of other developed country suppliers.

(5) *The government of an eligible country must refrain from broadcasting materials belonging to U.S.-copyright owners without their express consent.*—This provision responds to an unfair practice that increasingly threatens serious injury to significant U.S. trade interests. These interests are the commercial opportunities inhering in protected intellectual property; the unfair practice is the unauthorized appropriation of that property for uncompensated—and often competing—uses. The pirating of patented, copyrighted, or trademarked material not only deprives the owners of the profits of their effort, but it discourages innovation; causes widespread brand disparagement where, for example, copied articles are inferior, not backed by normal service, or do not satisfy product claims; and unfairly distorts trade to the detriment of the United States.

Perhaps spurred by increasingly sophisticated and available technologies, a relatively new aspect of these unfair trade practices is the interception and rebroadcast of satellite signals containing copyrighted materials. Like the more simple rebroadcast of copyrighted materials obtained through other means, satellite signal piracy denies the rightful owners the benefits of their creation, and by extension, adversely affects U.S. trade interests represented by the substantial export markets for these products.

The Committee is concerned that these practices are increasing, and indeed are occurring in the nations that may seek the benefits of the CBI. In particular, the Jamaican Broadcasting Corporation, a government-owned monopoly, is intercepting U.S. domestic satellite signals carrying copyrighted programs and rebroadcasting them for profit without the copyright owners' consent and without compensation. Elsewhere in the Caribbean Basin, private concerns are engaging in similar unfair acts. Testimony to the Committee alleged that in at least six countries (Panama, Belize, Honduras, the Bahamas, the Dominican Republic, and Costa Rica), private businessmen have established pay cable or subscription television systems relying, at least in part, on the unauthorized interception and rebroadcast of programs carried on U.S. domestic satellite signals.

U.S. motion pictures, television programs, and other copyrighted program material are valuable assets that should be protected against unauthorized use. It is in the trade interests of the United States to do so. As the Secretary of State testified to the Committee, it is also in the interests of developing countries to respect those property rights if they wish to reap the benefits of being a reliable trading partner and of attracting foreign investment. The Committee therefore endorses strongly the principles underlying the eligibility criteria of this section 212(b)(5) and of its companion section 212(c)(9).

As described below, certain of the eligibility requirements of section 212(b) may be waived if the President determines it to be in the overall national interest. As submitted, S. 544 did not include this fifth eligibility requirement among those that could be waived. Secretary of the State Shultz, while expressing the Administration's intention to seek satisfactory protection for U.S. copyright owners, stated his preference for including this eligibility criterion among those that are subject to waiver in the overall national interest. The Committee amended S. 554 in accord with his view.

The Committee, however, understands that the parties to the particular dispute involving the Jamaican Broadcasting Corporation are continuing to seek an amicable resolution of their differences over what can be broadcast and at what level of compensation. The Committee further sought and received assurances from the Department of State, as follows, that it will insist that the rights of U.S. copyright owners be respected.

U.S. DEPARTMENT OF STATE,
ASSISTANT SECRETARY OF STATE
FOR INTER-AMERICAN AFFAIRS,
Washington, D.C., May 12, 1983.

Hon. ROBERT DOLE,
Chairman, Committee on Finance,
U.S. Senate.

DEAR MR. CHAIRMAN: Further to the statement of Secretary Shultz in his April 13 testimony before the Committee on Finance, we believe that it would be constructive to include Sec. 102(b)(5) of S. 544, which relates to the unauthorized use of satellite signals, among the subsections which may be waived by the President if he determines that it is in the national economic or security interest of the United States and reports such determination to the Congress with his reasons therefor.

At this time, Sec. 102(b)(5) affects only Jamaica. Notwithstanding our important national security interest in Jamaica's continued economic progress, if waiver authority is included in the legislation, we would insist that the interest of American copyright owners will be protected in regard to both the permissible scope of acquisitions and compensation.

Sincerely,

THOMAS O. ENDERS.

The Committee does not expect CBI benefits to be extended unless these assurances are kept.

(6) *A country must cooperate with U.S. efforts to interdict unlawful narcotics trafficking.*—The Committee amended S. 544 to include this criterion, which is the same as the provision conditioning the receipt of benefits under the GSP (19 U.S.C. 2462(b)(5)). The Committee recognizes that governments cannot always control narcotics traffic originating within their lands. Nevertheless, helpful assistance to U.S. authorities can and should be rendered. The President will consider such factors in his determination whether

"adequate steps" are being taken to cooperate in combatting this threat to the United States

(7) *The country must be a party to an agreement regarding the extradition of U.S. citizens.*—Although most CBI beneficiary countries are party to such agreements, the Committee intends this provision to reinforce U.S. efforts to gain the return of persons fleeing this country to avoid arrest or imprisonment.

As in other trade and economic assistance programs, including the GSP, paragraphs (1), (2), (3), and (5) of the above eligibility criteria may be waived if the President determines that to do so is in the national economic or security interest and notifies the Congress of his reasons for doing so. Given the broad national security and economic interests of the United States in the success of the CBI, it may be appropriate to exercise this waiver in some critical circumstances. The Committee does not envision this to be the case, for example, under current circumstances with regard to the matter described above involving the interception of satellite signals by the Jamaican Broadcasting Corporation, or with regard to the two long-standing expropriation cases involving the Government of Panama.

Subsection (c): Discretionary eligibility criteria

In addition to the specific eligibility criteria described in section 212(b), subsection (c) enumerates several other factors the President must consider in determining whether to proclaim a nation eligible for subtitle A's benefits. In general, these criteria are designed to ensure that the nations are engaging in market-oriented policies and practices that will allow CBI benefits to work, and that are compatible with the interests of the United States.

These considerations are not binding, individually or collectively, on the President. But they do constitute a significant statement about the program's objectives and the sincerity of those nations that wish to benefit from it. The Committee anticipates and the bill requires that the President will consider fully these factors in reaching his eligibility determinations. In regard to criterion 10, the extent to which a country is prepared to cooperate in the administration of this title, the Committee intends that among other types of cooperation, the President would seek assurances of assistance in verifying that the origin requirements of section 213(a)(1)(B) are observed.

Subsection (d): MFN treatment for insular possessions

Products imported from the insular possessions currently are subject to MFN duty rates if they contain greater than 50 percent foreign value (70 percent for watches); if their foreign content is less, the products enter duty-free. This subsection is intended to ensure that such products receive treatment at least as favorable as imports from the CBI beneficiary countries, and therefore maintain their competitive position. Thus, any product that may enter duty-free from a beneficiary country will receive equivalent treatment if imported from an insular possession. This subsection should be read in conjunction with section 214, which liberalizes the rule of origin for products imported directly from the insular possessions.

Subsection (e): Termination of eligibility

The requirements of eligibility for CBI benefits are not intended to apply only to the President's initial determinations. Thus, if subsequent actions of a beneficiary country are such that it would have been ineligible in the first instance, subsection (e) requires the President to withdraw or to suspend its eligibility.

Section 213 (eligible articles)

Once designated as eligible under section 212, and as long as it maintains that status, a beneficiary country may export any article to this country duty-free, subject to certain exceptions, source requirements, and import safeguard restrictions. Section 213 establishes these limitations.

Subsection (a): Rule of origin

This subsection sets forth rules to determine whether any particular article for which duty-free treatment is sought qualifies as a product sourced in the eligible countries. The rules of origin are (1) that the article must be imported directly from a beneficiary country, and (2) it must contain at least 35 percent cumulative local value-added within the eligible Basin countries (plus Puerto Rico and the Virgin Islands), 15 percent of which can be of U.S. origin. This percentage is the same percent rule as in the Generalized System of Preferences, except for the allowance for U.S. value and for cumulation. The qualifying cumulative value is the sum of the cost or value of materials produced in the beneficiary countries (defined to include Puerto Rico and the Virgin Islands) plus the direct costs of processing there. "Direct costs of processing operations" further is defined to include actual labor and equipment costs directly allocable to the specific merchandise, and to exclude indirect costs such as profits and general business expenses.

Finally, the Secretary of the Treasury must promulgate regulations to implement these rules, in accord with standard U.S. practice. These rules shall provide that the article must be wholly the growth, product, or manufacture of a beneficiary country, or a new or different article of commerce produced in it. Specifically, this formulation excludes products merely packaged or combined in the country, or merely diluted by a liquid that does not materially alter the article's essential character.

These specific rules are designed to preclude the possibility of the beneficiary countries serving as mere conduits for articles that in reality originate outside the region. Further, by including value added in Puerto Rico, the Virgin Islands, and, to a limited extent, the United States, these rules will serve as an incentive for U.S. citizens to benefit from participating in the increased development the CBI should incite.

Subsection (b): Exceptions

Because they are covered by other import arrangements or are particularly import sensitive, certain products are specifically exempt from the President's authority to proclaim duty-free treatment under this bill. These are: (1) textile and apparel items that are subject to textile agreements; (2) certain articles that are not

GSP-eligible (footwear, handbags, luggage, flat goods, work gloves, and leather wearing apparel); (3) containerized tuna, and (4) petroleum and petroleum products. These products accounted for approximately 61 percent of total U.S. imports from the region in 1982. Of this amount, petroleum accounts for 56 percent.

Textile and apparel products "subject to textile agreements" are articles covered by the Arrangement Regarding International Trade in Textiles (the "Multi-Fibre Arrangement," or MFA) (25 UST 1001; TIAS 7840). These articles are described in headnote 9, schedule 3 of the Tariff Schedules of the United States (TSUS). Pursuant to the MFA, which is associated with the General Agreement on Tariffs and Trade, most U.S. imports of textile and apparel products are governed by bilateral quota agreements with the principal exporting countries. Three CBI beneficiary countries—Costa Rica, the Dominican Republic, and Haiti—are parties to such agreements. While duties on these products will not be suspended under this bill, the Administration has stated its intention to negotiate more favorable treatment for the CBI countries within overall U.S. textiles trade policy.

The articles exempted by paragraph (2) are ones produced by highly labor-intensive industries that have demonstrated sustained import sensitivity. The bill extends their GSP-exempt status to the CBI. Only those products among the described categories that are GSP-ineligible as of the date of enactment, whether by statute or administrative actions, are exempt. These are items described in the TSUS as follows: TSUS items 700.05–700.27, 700.29–700.53, 700.56–700.95 (nonrubber and footwear, except zoris); 705.35, 705.85, 705.86 (certain leather and rubber or plastic gloves); 706.05–706.16, 706.21–706.32, 706.34, 706.36, 706.38, 706.41, 706.43, 706.55, 706.62 (luggage, handbags, and flat goods); and 791.76 (certain leather wearing apparel).

Prepared or preserved tuna is also excluded because of the potentially high growth of imports relative to consumption, and the importance of the industry to the economies of Puerto Rico and American Samoa. This paragraph refers to articles encompassed by TSUS items 112.30 and 112.34.

The exclusion of petroleum and petroleum products derives from the unique nature of trade in those products and the overall national policy affecting them. Duties are not significant on these items. Nevertheless, there is substantial refining capacity in the region, and it would be relatively easy to mix large amounts of oil produced outside the region with oil of U.S. and local origin, and satisfy the 35 percent value-added rule of origin. This would encourage greater oil imports at a time when imports are falling and national security concerns dictate encouragement of that trend. Further, because refining operations are not labor intensive, duty-free access for petroleum products to the U.S. market is unlikely to encourage job creation in the beneficiary countries. The Committee therefore concludes that these items are properly excluded from the provisions of this title. To the extent such products may receive duty-free treatment under other provisions of law, this title will have no effect.

Subsection (c): Stable food production plans

The duty-free treatment afforded by the CBI may encourage some increased production of sugar and beef products in the beneficiary countries. To the extent this creates employment opportunities and economic growth, it is an expected and desirable result of the program. Because of the poor level of agricultural development in the region, however, and in view of the countries' explosive population growth, it would be inconsistent with the goals of the program if increased cash crop production for export displaced needed food crops. It is the purpose of this subsection to mitigate that danger.

As a condition of continued eligibility for CBI benefits—but not as a precondition to designation—a beneficiary country must prepare a "Stable Food Production Plan" that will describe what measures it will follow to ensure that the duty-free treatment provided by this title will not cause increased production of sugar and beef products adversely affecting current levels of food production and nutrition. The plan must be submitted to the President for approval within 90 days of its designation as a beneficiary country. The President will monitor the plans' implementation, and report biennially to the Congress on them. Failure to implement a plan successfully will result in suspension of duty-free treatment for sugar and beef products.

The Committee recognizes that many factors affect levels of food and cash crop production, and that increases in the latter will, among other benefits, generate wealth that can be expended for needed food products. Each country can best decide on its own how to maximize its agricultural resources, and the President will take each country's individual situation into account in determining the adequacy of these plans. Nevertheless, this provision should insure overall that the CBI avoids an unfortunate by-product of its primary development purpose.

Subsection (d): Special provisions for sugar

Section 213(d) of the bill provides special rules to ensure that duty-free treatment extended to imports of sugar under the bill do not interfere with or impair the price support program for sugar mandated by Congress.

Under current law, imports of sugar are subject to a column 1 (most-favored-nation) rate of duty of 2.8 cents per pound, which the President has authority to lower to 0.625 cents per pound. Under Headnote 2, subpart 10(A), schedule 1 of the Tariff schedules of the United States (TSUS), the President is also authorized to proclaim duties and quotas on imported sugar. Such quotas were in fact imposed on May 5, 1982 by the President. If in the future the President removed the current quota program, then there would still be a worldwide quota on imported sugar of 6.9 million short tons, raw value.

Moreover, under section 22 of the Agricultural Adjustment Act of 1933 (7 U.S.C. 624), the President may, on the basis of an investigation and report by the U.S. International Trade Commission (ITC), regulate commodity imports whenever he finds that such imports tend to render ineffective or materially to interfere with commodity price support programs of the United States. Section 22 fees, which are not U.S. duties for the purpose of any international obligations of the United States, may not exceed 50 percent *ad valorem* of imports during a representative period; section 22 quotas are subject to the same limitation. Currently, there is a section 22 finding in effect with respect to imported sugar.

Finally, sugar is a product that may be the subject of duty-free treatment under Title V of the Trade Act of 1974 (the Generalized System of Preferences or "GSP") subject to certain conditions. GSP does not free products from current headnote quotas or quotas or fees imposed under section 22. At the time the Committee considered the bill, all countries that could be designated pursuant to section 102 of the bill that export sugar to the United States receive GSP duty-free treatment for their sugar except the Dominican Republic. The Dominican Republic does not receive this benefit under GSP because its exports of sugar in 1982 exceeded limitations on GSP imports imposed under section 504(c) of the Trade Act of 1974 (the competitive need limitations). These limitations, in summary, are that GSP treatment is denied if U.S. imports of a product from a GSP beneficiary country exceed 50 percent of U.S. imports of the product or that country's exports of that product exceed a dollar figure which increases annually and was at the time the bill was approved about $53 million.

Subsection 213(d) provides special rules that apply to sugars, syrups, and molasses classified under TSUS items 155.20 and 155.30 when there is in effect a section 22 proclamation. However, nothing in the subsection disturbs any such proclamation; indeed, under subsection 213(g) of the bill, no section 22 fee or quota may be affected by any CBI decision. Moreover, under subsection 213(d)(4) of the bill, no action under any part of subsection 213(d) can result in a greater quantity of sugar, syrups, and molasses being imported from any one country than would be permitted under other provisions of law, such as under Headnote 2 described above.

However, the title does provide several special rules for beneficiary country sugar exporters.

First, for most beneficiary countries, this title authorizes duty-free treatment for sugar on the same basis as it is available under the GSP, with two exceptions. First, under subsection 213(d)(1)(A), the President may suspend or adjust upward the competitive need limitation on value (but not the percentage limitation) if he finds this will not interfere with the sugar price support program and that it is appropriate in light of market conditions.

Second, under subsection 213(d)(1)(B), a country may elect to seek, and the President may decide to grant, a special quota on sugar imports from that country. Both of these actions require that the recommendations of the Secretary of Agriculture be considered, and of course, no increases in duty-free sugar are possible beyond Headnote 2 or section 22 limits, if any.

Under subsection 213(d)(2), three countries have special rules applicable to them for the reason that they are, at the time this bill is being considered, in excess of GSP competitive need limitations (and therefore are not receiving duty-free treatment under GSP) or have recently needed this limit. For these three countries—the Dominican Republic, Guatemala, and Panama—there are absolute import quotas established in subsection 213(d)(2) of the bill of, respectively, 780,000, 210,000, and 160,000 metric tons. Again, however, if either Headnote 2 or section quotas are in effect at levels below the amounts set out for those three countries, then such a quota would override this law and is controlling.

Under subsection 213(d)(3), the President may adjust upward further the requested quotas he can establish under subsection 213(d)(1) or the statutory quotas under subsection 213(d)(2) if this will not interfere with U.S. sugar price support program and is appropriate in light of market conditions; or he may suspend duty-free treatment for all or part of this sugar to protect the price support program.

These authorities to adjust upward CBI sugar quotas would not be particularly beneficial under current conditions, except to the Dominican Republic. They would, however, be a substantial benefit if either the GSP expires in 1985 or current quotas under the headnote are increased, or eliminated altogether. In any event, the Committee understands and expects that the price support program Congress has previously enacted, and any such program Congress may in the future enact, will be defended under this bill as if there were no CBI program.

Subsection (e): Import relief provisions

Under current law, a domestic industry seriously injured by increasing imports may petition the ITC for a determination to that effect and a recommendation for import relief. If the ITC finds that increasing imports are a substantial cause of serious injury or the threat thereof to the domestic industry producing a like or directly competitive article, then the ITC must report its determination to the President within 6 months after receiving the petition and recommend either a remedy necessary to prevent or to remedy such injury, or adjustment assistance. In such cases, the President has 60 days to accept the ITC's recommendation and to implement it, to modify it, or to reject it. A decision not to grant relief or to provide it in a form or an amount different from the ITC's recommendation is subject to congressional override.

Any proclamation issued pursuant to these provisions of law that is in effect when duty-free treatment under this Act is proclaimed with regard to any country shall remain in effect unless and until that relief is modified or terminated. However, under subsection 213(e)(5), the President may reduce or terminate the application of import relief with regard to imports from beneficiary countries prior to its scheduled date pursuant to the criteria and procedures of subsections 203(h)(4) and 203(i) of the Trade Act of 1974. Under these provisions, import relief may be reduced or terminated by the President when he determines after taking into consideration advice received from the ITC under subsection (i), and after seeking the advice of the Secretaries of Commerce and Labor, that reduction or termination is in the national interest. Under subsection 203(i) of the Trade Act of 1974, the ITC is required to keep all import relief under review and advise the President of its judgment as to the probable economic effect of the extension, reduction, or termination of the relief. This may occur upon the request of the

President, upon the ITC's own motion, or upon petition of the industry concerned.

As to articles that receive duty-free treatment and are then the subject of import relief proceedings after enactment of this title, section 213(e)(2) requires that the ITC report to the President whether and to what extent its findings and recommendations apply to that article when imported from beneficiary countries. Under section 213(e)(3), the President may suspend duty-free treatment as an import relief remedy, because this subsection would provide the suspension of duty-free treatment is treated as an increase in duty under the import relief provisions of the Trade Act of 1974. However, under subsection 213(e)(4), no proclamation providing solely for suspension of CBI duty-free treatment may be made unless the ITC makes both an affirmative determination with respect to the article and a separate determination that the serious injury or threat thereof substantially caused by imports results from the duty-free treatment authorized by this title. An increase in duties under sections 201–203 of the Trade Act of 1974 coupled with a suspension of duty-free treatment would not require this additional ITC finding.

As to import relief in effect with respect to a Caribbean Basin product at the time of enactment of this bill, this subsection authorizes the President to reduce or to eliminate the relief selectively for the products originating in beneficiary countries if he follows the criteria and procedures of subsections 203(h) and 203(i) of the 1974 Trade Act (19 U.S.C. 2253(h), (i)).

Subsection (f): Perishable products

Because of the irreparable consequences that duty-free treatment may especially portend for perishable agricultural commodities, this subsection provides a special mechanism by which producers of such products may seek provisional protection pending the outcome of normal import relief procedures. These special procedures are available only with regard to the following products: (1) live plants; (2) fresh or chilled vegetables; (3) fresh mushrooms; (4) fresh fruit; (5) fresh cut flowers; and (6) concentrated citrus fruit juices. These items are specifically defined in the subsection by TSUS category.

Under this emergency procedure, in addition to filing a petition for relief with the International Trade Commission pursuant to section 201 of the 1974 Trade Act, a producer of a like or directly competitive perishable product may petition the Secretary of Agriculture to consider emergency relief. This petition may be filed at any time during the pendency of the section 201 proceeding. Within 14 days of filing, the Secretary must determine whether or not to recommend to the President that emergency action be taken. He will make an affirmative recommendation if he has reason to believe that a perishable product to which this section applies is being imported in such increased quantities as to be a substantial cause of serious injury, or threat thereof, to the petitioning industry. If the Secretary makes this affirmative recommendation, the President must within 7 days either determine not to act, or to proclaim a withdrawal of the duty-free treatment afforded by this bill. Emergency relief proclaimed by the President shall end when (1) the investigation under section 201 concludes and relief is proclaimed or denied, or (2) whenever the President determines that, because of changed circumstances, such relief is no longer warranted.

The standards and procedures of this emergency provision are patterned after existing import relief laws; specifically, section 201 and section 22 of the Agricultural Adjustment Act. The practice under those laws should guide its interpretation.

The Committee intends that this emergency mechanism be utilized to afford a particularly vulnerable class of petitioners the opportunity to take advantage of normal import relief procedures. The latter ordinarily require an investigation and determination period of 6 months—a period that, for perishable products, may render meaningful relief illusory. This subsection simply affords an opportunity in meritorious circumstances to restore MFN tariff treatment until a final decision on relief can be reached. By doing so, the title protects domestic growers against injurious import dangers that may have irreparable consequences.

Subsection (g): Section 22 fees and quotas

As described above with regard to subsection 213(d), section 22 of the Agricultural Adjustment Act of 1933 (7 U.S.C. 624) authorizes the President to impose import fees and quotas on products that are being imported in circumstances rendering ineffective (or tending to do so) a domestic price support program, or reducing substantially the domestic production of products supported by such a program. Fees imposed under section 22 may not be more than 50 percent *ad valorem,* and quotas must be at least 50 percent of the import level during a representative period. At the present time, fees on imported sugar are in effect pursuant to this law.

Subsection (g) makes clear that fees and quotas are to be imposed pursuant to section 22 without regard to the proclamation authority of this bill. Thus, imports of commodities may enter the United States duty-free pursuant to section 211, but nevertheless be subject to fees, as are all other imports of the same commodity. The beneficiary countries will maintain a relative duty advantage over other imports, and the President will be able to employ section 22 as intended, to protect price support programs.

Section 214 (Measures for Puerto Rico and the Insular Possessions)

The Commonwealth of Puerto Rico and the territory of the U.S. Virgin Islands enjoy the preferential access to the U.S. market the CBI would extend in part to the Basin countries. Both also are subject to U.S. minimum wage laws, environmental regulations, and other laws that impact upon business there but will not apply to the beneficiary countries. Thus, while they support the CBI, the governments of Puerto Rico and the Virgin Islands are concerned about possible adverse impacts of the program. Title II contains several provisions intended to benefit them specifically; most are in this section. Certain of these measures also are intended to ensure treatment of products from insular possessions outside of the Caribbean Basin equal to that of the beneficiary countries.

The principal U.S. insular areas are the Virgin Islands, American Samoa, Guam, and Puerto Rico. The Commonwealth of the Northern Mariana Islands will come under U.S. sovereignty upon termination of the Trusteeship Agreement, and will be included in the insular areas. Puerto Rico maintains a commonwealth relationship with the United States.

Subsection (a): Rule of origin

Articles imported from the insular possessions, because they are outside the U.S. customs territory, are subject to MFN duty rates if they contain greater than 50 percent foreign value. A special rule increases this limit to 70 percent for watches and watch movements. If these value-added rules are not exceeded, the products enter duty-free. Puerto Rico is part of U.S. customs territory, and duties are not imposed on products arriving in the United States directly from there.

Subsection (a) increases the 50 percent value-added rule to 70 percent for all products, except ones excluded from duty-free treatment under section 213(b). Thus, for all products for which this bill will offer preferential treatment, subsection (a) will ensure that the insular possessions receive a slightly more favorable rule-of-origin. Subsection 212(d), as described previously, further provides that duties imposed on any products satisfying this rule of origin shall receive treatment at least as favorable as provided in this act for beneficiary country exports. Together, these provisions will maintain or improve the position of the insular possessions compared to the beneficiary countries.

Subsection (b): Alcoholic beverages

Current law allows U.S. residents returning to the United States directly from an insular possession to bring with them up to 4 liters of distilled spirits duty-free, if 3 liters are acquired in the possessions. Subsection (b) will amend TSUS item 813.31 to increase the total allowable to 5 liters, at least one of which must be a product of the insular possessions, and at least four of which shall be acquired in American Samoa, Guam, or the U.S. Virgin Islands. This provision will particularly assist the Virgin Islands to counterbalance the potential increased competition arising from the duty-free treatment accorded alcoholic beverages produced in the beneficiary countries.

Subsection (c): Protection of rum excise tax transfer

This subsection will be explained in conjunction with section 221 later in this report (C. Explanation of Tax Provisions (subtitle B)).

Subsection (d): Repeal of MTN compensation authority

Section 1112 of the Trade Agreements Act of 1979 (19 U.S.C. 2582) authorizes the President to seek appropriations to be paid to the government of a U.S. possession if he determines that excise tax revenues have been reduced as a result of concessions made in the Tokyo Round of multilateral trade negotiations. The provision was aimed particularly at the threat of revenue loss from increased competition from imported distilled spirits. The provision has not been invoked.

Because section 221 and 214(c) of this bill are intended to provide a simpler and more direct method of compensation and protection, subsection (d) will repeal section 1112.

Subsection (e): Puerto Rican coffee tariffs

The Commonwealth of Puerto Rico retains authority to impose separate duties on coffee imported there pursuant to section 319 of the Tariff Act of 1930. This subsection will preserve that right, regardless whether coffee may enter the United States duty-free pursuant to the authority in section 211 of this bill.

Subsection (f): Import relief for possessions' producers

Section 201 of the Trade Act of 1974 (19 U.S.C. 2251) authorizes the International Trade Commission, upon petition by an entity that is representative of an industry, to conduct an investigation into whether an article is being imported in such increased quantities as to be a substantial cause of serious injury, or the threat thereof, to the domestic industry producing a like or directly competitive article. Upon an affirmative ITC determination, the President may proclaim temporary import relief measures, including higher duties. In certain circumstances, the ITC may treat as the domestic industry one or more producers in a particular geographic area.

Subsection (f) is intended to bring clearly within the ambit of section 201 producers located in Puerto Rico and the insular possessions. By doing so, the provision ensures that relief will be available to such producers. As their products will often be in the most directly competitive posture with the imports, it is proper that the ITC consider their circumstances in reaching the decision required by section 201.

Subsection (g): Rum stillage exemption

The Federal Water Pollution Control Act (FWPCA) applies to discharges from sources in the insular possessions. In recent years the Environmental Protection Agency has sought to apply certain FWPCA requirements to the principal rum producing plant in the Virgin Islands, alleging that the stillage discharged into the Caribbean Sea violates FWPCA standards. The plant and the government of the Virgin Islands strongly argue that these discharges do not harm the water quality because they are biodegradable and quickly dissipate in the oxygen-rich water.

The plant produces 95 percent of all Virgin Islands rum shipped to the United States, and thus indirectly generates 20 percent of that government's revenues. The cost of constructing and operating the treatment facility sought by the EPA is likely to exceed the current book value of the plant's fixed assets. The Virgin Islands government therefore is greatly concerned that the cost of satisfying the EPA's demands, coupled with increased competition from Caribbean rum producers not subject to such requirements, will cause the plant to fail, depriving the Virgin Islands of a significant source of revenue.

Subsection (g) would ameliorate the serious threat caused by the continuing dispute by exempting the rum stillage discharges from the requirements of sections 301 (other than toxic pollutant discharges), 306, and 403 of the FWPCA. There are three conditions to this exemption: (1) the exempted discharge must be from an existing point source attributable to rum manufacture; (2) the discharge must occur 1500 feet or more from shore; and (3) the Virgin Islands' Governor must determine that the discharge will not constitute a threat to public water supplies, the surrounding environment, human health, or recreational activities.

Federal law encourages reliance upon rum excise tax transfers by the Virgin Islands government as a significant revenue source. The imposition of Federal environmental and trade policies on the Virgin Islands that conflict with this basic revenue source requires an appropriate compromise. Given the unique environmental and economic circumstances surrounding this stillage discharge, and the environmental protections crafted into the limited exemption subsection (g) creates, the Committee concludes that this assistance to the Virgin Islands is necessary and appropriate.

Section 215 (International Trade Commission impact report)

The section requires the ITC to report regularly to the Congress on the economic impact of this Act on U.S. industries and consumers. The first report will be due 2 years after the date of enactment. Subsequent reports will be delivered for each calendar year thereafter. The reports must be delivered within 9 months after the end of the period that they analyze.

This section enumerates several factors for the ITC to assess. In general, these accord with factors the ITC normally assesses in the course of carrying out its statutory responsibilities. The Commission must receive information from the public in its preparation of these reports.

Section 216 (Effective date and termination of authority)

Subsection (a) of section 216 provides that subtitle A shall take effect on the date of enactment. The President thus may exercise his proclamation authority pursuant to section 211 at any time beginning with or after that date until it terminates.

Section 216(b) provides that no duty-free treatment proclaimed pursuant to this title shall be effective after September 30, 1995. This approximately 12-year period was chosen to demonstrate a long-term commitment to the beneficiary countries and to allow businesses sufficient time to gain a return on investments spurred by the program.

D. GENERAL EXPLANATION OF TAX PROVISIONS (SUBTITLE B)

Present Law

Rum excise taxes

An excise tax of $10.50 per proof gallon is imposed on distilled spirits (including rum) produced in or imported into the United States (defined to mean the 50 States and the District of Columbia) (Internal Revenue Code sec. 5001). The tax is imposed on the manufacturer or on the importer of the distilled spirits and is payable at the time the spirits are removed for consumption or sale from the distillery, or from customs custody in the case of imported spirits. Generally, merchandise manufactured in Puerto Rico and brought into the United States for consumption or sale or merchandise coming into the United States from the U.S. Virgin Islands is subject to a tax equal to the tax imposed in the United States upon similar merchandise of domestic manufacture (sec. 7652).

All taxes collected under the Internal Revenue Code on articles produced in Puerto Rico and transported to the United States (less the estimated amount necessary for payment of refunds and drawbacks), or consumed on the island, are deposited into the Treasury of Puerto Rico. Internal revenue collections (less certain amounts deposited into the U.S. Treasury as miscellaneous receipts) on articles produced in the Virgin Islands and transported to the United States are paid to the Treasury of the Virgin Islands.

The Virgin Islands Government may spend the money received under this provision during a fiscal year as the legislature may determine, provided that the approval of the President or his representative is obtained. It may carry no more than $5 million of such receipts forward from one year to the next; the excess is returned to the U.S. Treasury.

Business expense deduction for conventions in certain countries

A deduction is allowed for the ordinary and necessary expenses of carrying on a trade or business or income-producing activity, including transportation expenses and amounts expended for meals and lodging while away from home in pursuit of a trade or business or income-producing activity (Code sec. 162). Only such traveling expenses as are reasonable and necessary in the conduct of the taxpayer's business and directly attributable to it may be deducted. Fees charged for admission to a convention or other meeting generally are deductible if there is a sufficient relationship between the taxpayer's trade or business or income-seeking activity and attendance at the convention or other meeting. Therefore, generally, a deduction is allowed for the costs of attending a convention or seminar in pursuit of a trade or business or income-producing activity.

A special rule (Code sec. 274(h)) applies to expenses for attendance at conventions, seminars, or similar meetings if held outside the United States, its possessions, Canada, Mexico, or the Trust Territory of the Pacific Islands (the "North American area"). (Conventions, etc., held outside the North American area commonly are referred to as "foreign conventions.") No deduction is allowed for the expenses of attending a foreign convention unless the taxpayer establishes that the convention is directly related to the active conduct of a trade or business or income-producing activity and that it is as reasonable to hold the meeting outside the North American area as within it (sec. 274(h)(1)).[1] This rule applies both to the expenses paid by individuals attending such conventions and to expenses paid by employers of such individuals.

A deduction is allowed for up to $2,000 of the expenses allocable to attendance at a business convention or similar meeting directly related to a trade or business or income-producing activity of the taxpayer if the meeting is held on a U.S. flag cruise ship and if the ship calls on ports only in the United States and the U.S. possessions (sec. 274(h)(2)).

Exchange of tax information

Under current law, the United States has difficulty in obtaining information to enforce its tax laws when transactions occur (or when information is located) overseas. The United States has entered into income tax treaties that provide for exchanges of information to enable the United States and its treaty partner to enforce the tax laws which are covered by the treaty. However, the operation of exchange of information articles in some treaties is not satisfactory, because the other country may not disclose certain kinds of information, such as information regarding the ownership of bank accounts or the beneficial ownership of trusts or corporations. Moreover, the United States has treaties with few Caribbean countries, in part because some of those countries do not generally impose income taxes.

Reasons for Change

Rum excise taxes

Over 95 percent of the rum consumed in the United States is produced in Puerto Rico or the Virgin Islands. Although rum is a traditional Caribbean export, and the U.S. market has grown at an annual compound rate of 11 percent over the last 5 years, the United States imports only about $4 million worth of rum from the Caribbean countries, compared to $100 million in sales by Puerto Rico and the Virgin Islands. Given this market, and the protection and compensation provided in this title, the Committee concludes that the bill presents little threat to the Virgin Island or Puerto Rican rum industry, but offers an important trade incentive to the beneficiary nations.

Nevertheless, the elimination of duties on certain rum imported from Caribbean Basin countries under Subtitle A will reduce the

[1] Under the United States-Jamaican income tax treaty, deductions are permitted for certain expenses of attending a convention in Jamaica (Art. 25(7)). This treaty does not provide for reciprocal treatment by Jamaica of U.S. conventions. As part of the agreement granting favorable convention treatment to Jamaica, Jamaica made substantial concessions on the issues of treaty use by third-country persons and exchanges of tax information.

price of that imported rum to U.S. consumers. That price reduction in turn may reduce the U.S. sales of rum produced in Puerto Rico and the U.S. Virgin Islands from what such sales otherwise would have been. Any such reduction in U.S. sales of rum produced in Puerto Rico and the Virgin Islands will reduce revenues (from excise taxes collected on rum) transferred to the governments of these possessions. Although the Committee intends to benefit countries in the Caribbean Basin that meet certain criteria, it does not intend to do so at the expense of Puerto Rico and the Virgin Islands. Thus, sections 214(c) and 221 (described below) are designed to protect their revenues.

Business expense deductions for conventions in certain countries and exchange of tax information

Restriction of deductions for attending conventions to those held in the North American area has adversely affected service industries (such as the hotel and restaurant industries) in the Caribbean Basin. These industries are important to the economies of the area. Furthermore, granting deductions for conventions in Canada and Mexico, and in Jamaica by treaty, is perceived as unfair by the countries in the region.

Bermuda's reliance on service industries is similar to that of Caribbean Basin countries. The Committee does not want to treat this friendly country more harshly in this respect than the other countries in the region.

However, the Committee also recognizes that some Caribbean Basin countries have been used by persons seeking to evade or avoid U.S. taxes. The Committee believes that the favorable convention treatment should be available only to those countries which are willing to assist the United States in enforcing its tax laws.[2] Accordingly, the convention deduction is made available only for conventions in a country that enters into an exchange of information agreement with the United States.

The Committee provides modified standards for the exchange of civil tax information in certain circumstances. Although the Committee would prefer that exchange of information agreements be comprehensive, the Committee recognizes that in some cases the President may determine that the national security interest of the United States may be such that a more limited provision for the exchange of civil tax information is acceptable. Before acceptance of a limited provision, however, the Secretary of the Treasury, the person directly responsible for administration of U.S. tax laws, should determine that the limited provision serves a significant tax administration and enforcement purpose. The Committee does not believe that any modification of the standards for the exchange of criminal tax information is appropriate.

[2] The Committee is aware that as part of the agreement granting favorable convention treatment to Jamaica, Jamaica made substantial concessions in terms of a far reaching anti-treaty shopping provision, a note promising broad exchanges of information, and a promise to negotiate a mutual assistance treaty concerning criminal matters generally.

Explanation of Tax Provisions

Rum excise taxes (sections 214(c) and 221)

All distilled spirits excise taxes collected (under section 5001(a)(1) of the Internal Revenue Code) on rum imported into the United States from outside the country,[3] whether or not from a Caribbean Basin country, will be paid over to the treasuries of Puerto Rico and the Virgin Islands [4] under section 221.

These payments would be reduced by the estimated amount necessary for payment of refunds and drawbacks. The bill will not impose restrictions on the uses to which the Government of the Virgin Islands or the Government of Puerto Rico put the revenues they receive under this provision.

The Secretary of the Treasury will prescribe by regulation a formula for the division of tax collections between Puerto Rico and the Virgin Islands. The Secretary may change this formula from time to time.

Rum will be defined by reference to the Tariff Schedules of the United States, 19 U.S.C. 1201, so as to include *cana paraguaya,* a rum-like spirit. This provision will apply to rum imported into the United States after June 30, 1983.

Section 214(c) provides that if the amount covered over is reduced below the amount Puerto Rico and the Virgin Islands would have received had the imported rum been produced in those two jurisdictions, then the President shall consider ways to make up the loss. The subsection specifically states that he may withdraw duty-free treatment for rum. Whatever measures the President takes, he must report to the Congress on them.

Convention deductions and exchange of tax information (section 222)

Subtitle B will allow deductions for the ordinary and necessary expenses (in pursuit of a trade or business or income-producing activity) of attending conventions and similar meetings in those countries among the Caribbean Basin countries and Bermuda that meet three criteria discussed below. The taxpayer will not have to establish that holding a convention in a country meeting these criteria is as reasonable as holding it in another location.

First, the only countries that may qualify for this convention treatment will be beneficiary countries, as defined in section 212(a)(1)(A) of subtitle A, and Bermuda. As described heretofore with regard to sections 211 and 212, beneficiary countries are those among certain enumerated countries and territories,[5] including

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[3] No possession other than the Virgin Islands and Puerto Rico now produces rum for sale in the United States. The title will treat rum produced by other possessions like rum produced by foreign countries.

[4] Jamaica accounted for over 64 percent of all rum imported for consumption in the United States in 1982 from foreign countries; Barbados for over 11 percent. No other country accounted for as much as 6 percent of imports. U.S. Department of Commerce, *U.S. General Imports and Imports for Consumption December 1982,* 2-26 (issued March 1983).

[5] The countries and territories are: Anguilla, Antigua and Barbuda, the Bahamas, Barbados, Belize, Costa Rica, Cuba, Dominica, the Dominican Republic, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Nicaragua, Panama, Saint Lucia, Saint Vincent and the Grenadines, Surinam, Trinidad and Tobago, the Cayman Islands, Montserrat, the Netherlands Antilles, Saint Christopher-Nevis, Turks and Caicos Islands, and the British Virgin Islands. The bill defines country to include overseas dependent territories and possessions. Successor political entities of the enumerated countries and territories would be eligible for the benefits of the bill.

Guyana, Surinam, and countries located in the Caribbean and Central America, that the President designates as beneficiaries of this title.

Second, deductions will be available only for expenses of attending conventions held in countries with which an agreement with the United States to exchange tax information is in force at the time the convention begins. Subtitle B authorizes the Secretary of the Treasury to negotiate and to conclude such agreements, which may be bilateral or multilateral. Such an agreement will provide, on a reciprocal basis, for information relating to U.S. tax matters to be made available only to persons or authorities (including courts and administrative bodies) involved in the administration of U.S. taxes (including assessment and collection of taxes and enforcement and prosecution in respect of taxes) or oversight of the administration of such taxes (a role of the Senate Committee on Finance, the House Committee on Ways and Means, the Joint Committee on Taxation, and the General Accounting Office), or in the determination of appeals in respect of such taxes.

The exchange of information agreement will generally have to apply to and to include provisions relating to both civil and criminal tax matters within the U.S. meaning of those concepts. While the subtitle accords the Secretary discretion regarding what kinds of information will be included within the scope of the exchange of information provisions, it provides certain standards for such agreements. The agreement will have to apply to information relevant to tax matters of the United States or of the beneficiary country whether that information concerned nationals or residents of the United States or the beneficiary country or nationals or residents of a third country.

Subtitle B mandates that the agreement require production of information notwithstanding local rules requiring secrecy about such information as the ownership of bank accounts, trusts or bearer shares. In this respect, the agreements contemplated by the subtitle may go beyond the exchange of information articles of some U.S. tax treaties, which may not impose an obligation to supply information not obtainable under local law or administrative practice. The agreement will impose on the officials of each country a duty not to disclose this information to persons other than those involved in its tax administration. The provision makes it clear that exchange of information agreements will be treated as income tax conventions for the purpose of the Code rule that allows U.S. tax officials to disclose tax information to foreign tax officials pursuant to such conventions (sec. 6103(k)(4)).

The information to be exchanged under the agreement will not be limited to information about any particular class of transactions (such as expenses for conventions). The subtitle will require the exchange of such information as may be necessary or appropriate to carry out the tax laws of the United States or of the beneficiary country. The Committee intends that the information obtained be usable as evidence in court. Thus, the Committee intends that the exchange of information agreement provide that, if a party specifically requests, information shall be furnished in the form of depositions of witnesses and authenticated copies of unedited original documents (including books, papers, statements, records, accounts, and writings) in a form admissible into evidence. It is intended that, in general, the country have a process for obtaining the information required to be provided by that country.

A special rule provides for modified standards for exchange of information agreements in certain cases. This rule allows the requirement that the exchange of information agreement supersede provisions of local law regarding bank secrecy and nondisclosure of ownership of bearer shares to be waived in the case of information sought only for civil tax purposes if the President determines that such an exception to the standards for an exchange of information agreement is in the national security interest of the United States and if the Secretary of the Treasury determines that such an exchange of information agreement satisfying the modified standards would assist the administration and enforcement of U.S. tax laws.

An exchange of information agreement will generally become effective on signature. The text of the agreements will have to be transmitted to Congress no later than sixty days after the agreement has been signed, in accordance with the Case Act (1 U.S.C. section 112b).

An exchange of information agreement will be terminable by either country on reasonable notice. No deductions will be allowed for business expenses of conventions or similar meetings begun in a country after termination of the exchange of information agreement. Termination should occur if, for example, the other country is not abiding by its obligations under the agreement to supply information or to maintain confidentiality. Termination will occur in the manner set forth in the agreement.

Third, deductions will not be available for conventions in any country that begin after publication in the Federal Register of a finding by the Secretary that that country discriminates in its tax laws against conventions and similar meetings held in the United States or the U.S. possessions. The Secretary may withdraw such a finding by a subsequent announcement in the Federal Register.

This provision will apply to conventions beginning after June 30, 1983, but only if an exchange of information agreement is in effect on the day the convention began.

E. SENSE OF CONGRESS ON SUGAR IMPORTS (SUBTITLE C)

The Committee also amended S. 544 to express the sense of the Congress that no sugar should be imported into the United States from any community country in the Caribbean Basin or Central America. The term "Communist country" is used in this provision in the same sense it is used in section 212 of this title.

Sugar is a major cash crop of many countries in the region covered by the bill, some of which the President has said are threatened by international communism. The United States is a major market for this sugar and, because of domestic sugar programs, a profitable market for foreign sugar. Under current law, the United States does not import sugar from Cuba. Moreover, the President recently decided to reduce the sugar quota for Nicaragua as of October 1, 1983, to prevent its using sugar revenues to finance insurrection in Central America. The Committee felt that sugar exports to the United States should never be permitted to finance a Communist government in the region. This provision advises the Administration of Congressional views on this subject.

F. BUDGETARY IMPACT

The following estimate of the Congressional Budget Office is provided with respect to the budgetary impact of title II of the committee amendment:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, D.C., June 2, 1983.

Hon. ROBERT DOLE,
Chairman, Committee on Finance,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: In accordance with the Budget Act, the Congressional Budget Office has examined S. 544, the Caribbean Basin Economic Recovery Act. This bill provides for a combination of tax and tariff incentives designed to provide financial and trade assistance to Caribbean nations.

The bill does not provide any new budget authority or any new or increased tax expenditures.

The CBO has reviewed the estimates of the staffs of the Joint Committee on Taxation and the International Trade Commission and agrees with the resulting estimates. The bill is estimated to reduce budget receipts by the following amounts:

Revenue loss from S. 544 [title II of committee amendment]

Fiscal year:	*Millions*
1983	$16.5
1984	70.0
1985	70.0
1986	70.0
1987	70.0
1988	70.0

The enclosed table shows the breakdown of revenue losses associated with title I and title II of the bill.

Sincerely,

ALICE M. RIVLIN, *Director.*

ESTIMATED REVENUE EFFECTS OF S. 544, CARIBBEAN BASIN ECONOMIC RECOVERY ACT (AS REPORTED BY THE SENATE FINANCE COMMITTEE)

	Fiscal years					
	1983	1984	1985	1986	1987	1988
Title I: Duty-free provisions...	−14.5	−60	−60	−60	−60	−60
Title II—Tax Provisions:						
Excise taxes collected on rum from Puerto Rico and the Virgin Islands..	−2.0	−10.0	−10.0	−10.0	−10.0	−10.0
Allowance of expense deductions for Caribbean conventions..	([1])	([1])	([1])	([1])	([1])	([1])

[1] Less than $5 million.

G. VOTE OF THE COMMITTEE

The following statement is made relative to the vote by the Committee on the motion to approve title II. The Committee approved S. 544, as amended, which comprises the substance of this title, as approved by a vote of 15 ayes, 3 nays, and 1 present, on May 12, 1983.

TITLE III—ENTERPRISE ZONE TAX ACT

Present Law

Targeted jobs tax credit

The targeted jobs tax credit, which applies to wages paid to eligible individuals who begin work for the employer before January 1, 1985, is available on an elective basis for hiring individuals from one or more of 9 target groups. The target groups are (1) vocational rehabilitation referrals; (2) economically disadvantaged youths aged 18 through 24; (3) economically disadvantaged Vietnam-era veterans; (4) Supplemental Security Income (SSI) recipients; (5) general assistance recipients; (6) economically disadvantaged cooperative educational students; (7) economically disadvantaged former convicts; (8) AFDC recipients and WIN registrants; and (9) disadvantaged youths aged 16 or 17 for summer employment (effective for those who begin work for an employer after April 30, 1983).

The credit is equal to 50 percent of the first $6,000 of qualified first-year wages and 25 percent of qualified second-year wages paid to a member of a targeted group. Thus, the maximum credit is $3,000 per individual in the first year of employment and $1,500 per individual in the second year of employment. The employer's deduction for wages, however, must be reduced by the amount of the credit.

The credit is subject to several limitations. For example, wages may be taken into account for purposes of the credit only if more than one-half of the wages paid during the taxable year to an employee are for services in the employer's trade or business. In addition, wages for purposes of the credit do not include amounts paid to an individual for whom the employer is receiving payments for on-the-job training under a Federally-funded program.

For purposes of determining the years of employment of an employee and whether the $6,000 cap has been reached with respect to any employee, all employees of any corporation that are members of a controlled group of corporations are treated as if they are employees of a single corporation. Under the controlled group rules, the amount of credit allowed to the group is generally the same which would be allowed if the group were a single company. Comparable rules are provided for partnerships, proprietorships, and other trades or business (whether or not incorporated) under common control.

The credit may not exceed 90 percent of the employer's tax liability after being reduced by other nonrefundable credits. Excess credits may be carried back three years and carried forward fifteen years.

Investment tax credit

Under present law, a regular investment tax credit is allowed for investment in tangible personal property and other tangible property (generally not including buildings or structural components) used in connection with manufacturing, production, or certain other activities. For eligible property in the 3-year recovery class, a 6-percent regular investment tax credit is allowed. For other eligible property, a 10-percent regular investment tax credit is allowed.

Buildings and their structural components generally do not qualify for the regular investment tax credit. However, in the case of qualified rehabilitation expenditures, a 15-percent tax credit is allowed for nonresidential buildings at least 30 years old, a 20-percent tax credit is allowed for nonresidential buildings at least 40 years old, and a 25-percent tax credit is allowed for certified historical buildings. The regular and energy tax credits are not allowed to the extent that the rehabilitation credit is available. Unused investment tax credits may be carried back 3 years and carried forward for 15 years.

The basis of the asset, for such purposes as capital cost recovery deductions, is reduced by the full amount of the 15-percent or 20-percent rehabilitation tax credit and by half the investment tax credit for other types of property.

Capital gains taxation

In general

Under present law, gain or loss from the sale or exchange of a capital asset received special tax treatment. For this purpose, the term "capital asset" generally means any property held by the taxpayer. However, capital assets generally do not include (1) inventory, stock in trade, or property held primarily for sale to customers in the ordinary course of the taxpayer's trade or business, (2) depreciable or real property used in the taxpayer's trade or business, (3) specified literary or artistic property, (4) business accounts or notes receivable, or (5) certain U.S. publications. Although depreciable personal property and real property used in a trade or business are not capital assets, gains from sales or exchanges of those assets may be treated as capital gains under certain circumstances.

Noncorporate capital gains deduction

Noncorporate taxpayers may deduct from gross income 60 percent of the amount of any net capital gain (the excess of net long-term capital gain over net short-term capital loss) for the taxable year. (Long-term capital gain is defined as gain from the sale or exchange of a capital asset held for more than one year). The remaining 40 percent of the net capital gain is included in gross income and taxed at the otherwise applicable regular income tax rates. As a result, the highest tax rate applicable to a noncorporate taxpayer's entire net capital gain is 20 percent, i.e., 50 percent (the highest individual tax rate) times the 40 percent of the entire net capital gain includible in adjusted gross income.

Corporate capital gains tax

An alternative tax rate of 28 percent applies to a corporation's net capital gain (the excess of net long-term capital gain over net short-term capital loss) if the tax computed using that rate is lower than the corporation's regular tax. (The highest regular corporate tax rate is 46 percent for taxable income over $100,000.)

Minimum taxes

"Add-on" minimum tax

Present law imposes an "add-on" minimum tax for corporations on certain tax preference items. 18/46ths of a corporation's net capital gain is a tax preference subject to the minimum tax.

Alternative minimum tax

Under present law, noncorporate taxpayers are subject to an alternative minimum tax to the extent that it exceeds their regular income tax. The alternative minimum tax is based on the taxpayer's adjusted gross income, as reduced by allowed deductions, and increased by tax prefer items, including the 60 percent of net capital gains deducted in computing the regular tax. The alternative minimum tax rate is 20 percent for amounts in excess of a specified exemption amount.

Industrial development bonds

Interest on State and local government obligations generally is exempt from Federal income tax (obligations issued after June 30, 1983 must be in registered form to be exempt). However, subject to certain exceptions, interest on State and local issues of industrial development bonds is taxable. An obligation constitutes an industrial development bond (IDB) if (1) all or a major portion of the proceeds of the issue are to be used in any trade or business of a person other than a governmental unit or tax-exempt organization described in sec. 501(c)(3) and (2) payment of principal or interest on the obligation is secured by an interest in, or derived from payments with respect to, property or borrowed money used, or to be used, in a trade or business.

Present law provides an exception which exempts from tax interest on IDBs that are issued to finance the following types of exempt activities: (1) projects for low-income residential rental property, (2) sports facilities, (3) convention or trade show facilities, (4) airports, docks, wharves, mass commuting facilities, and parking facilities, (5) sewage and solid waste disposal facilities, and facilities for the local furnishing of electricity or gas, (6) air or water pollution control facilities, (7) certain facilities for the furnishing of water, (8) qualified hydroelectric generating facilities, and (9) qualified mass commuting vehicles. In addition, the interest on certain IDBs issued for the purpose of acquiring or developing land as a site for an industrial park is exempt from taxation.

Present law also provides an exception for certain "small issues" to the general rule of taxability of interest paid on industrial development bonds. This exception is not available for bond proceeds used for golf courses, country clubs, racetracks and other specified types of facilities. This exception applies to issues of $1 million or less if the proceeds are used for the acquisition, construction, or improvement of land or depreciable property.

At the election of the issuer, the $1 million limitation may be increased to $10 million. If this election is made, the exception is restricted to projects where the aggregate amount of outstanding exempt small issues and capital expenditures (financed otherwise than out of the proceeds of exempt small issues) made over or a six-year period does not exceed $10 million. Both the $1 million and $10 million limitations are determined by aggregating the face amount of all outstanding related issues, plus, in the case of the $10 million limitation, certain capital expenditures for all facilities used by the same or related principal users which are located within the same county or same incorporated municipality.

In general, the small issue exemption will not apply with respect to obligations issued after December 31, 1986.

Under present law, to the extent that certain facilities are financed by an IDB and the property is placed in service after December 31, 1982, such property generally is allowed cost recovery deductions at a slower rate than those allowed under ACRS or other accelerated cost recovery provisions of the Code. In lieu of deductions under ACRS, the cost of property financed with IDBs must be recovered using the straight-line method over the ACRS life for the property involved. This limitation applies to both the first owner of the property and to any subsequent owners who acquire the property while the IDBs (including any refunding issues) are outstanding.

However, the cost of the following types of facilities financed in whole or in part with IDBs may continue to be recovered under ACRS: low-income rental housing, municipal sewage and solid waste disposal facilities, air or water pollution control facilities used in connection with a plant or other property in operation before July 1, 1982, and facilities for which a UDAG grant equalling or exceeding 5 percent of the total capital expenditures on the facility is made.

Regulatory flexibility

The Regulatory Flexibility Act (5 USC secs. 602-612) requires Federal regulatory agencies to publish analyses of the economic impact on entities under its coverage of any proposed regulations and to discuss alternatives to those regulations. The Act requires Federal regulatory agencies to undertake a periodic review of their regulations to determine whether they should be changed to minimize their economic impact on the entities covered by the Act.

In general, the purpose of the Regulatory Flexibility Act is to require Federal agencies to fit regulatory and informational requirements to the scale of the businesses, organizations, and governmental jurisdictions subject to regulation. To achieve this goal, agencies are required to solicit and consider flexible regulatory proposals and to explain the rationale for their actions to assure that such proposals are given serious consideration. The Act requires that special attention is to be given to small entities. For example, in its initial regulatory flexibility analysis, an agency must describe the impact of a proposed rule on small entities.

Small entities, for purposes of the Regulatory Flexibility Act, are small businesses (generally independently owned and operated business enterprises that are not dominant in their fields of operation), small organizations (independently owned and operated not-for-profit enterprises that are not dominant in their fields), and small governmental jurisdictions (governments of cities, towns, townships, villages, school districts, or special districts, with populations of less than fifty thousand).

Foreign trade zones

Each port of entry is entitled to at least one foreign trade zone. In a foreign trade zone, foreign merchandise may be received by a company, and the merchandise is not considered to have entered U.S. Customs territory. Thus, dutiable goods may be received free of duty. These goods may be stored, sold, repaired, assembled, distributed, manufactured and displayed within the zone, and then exported or sent into Customs territory of the United States. When sent into Customs territory, the goods become subject to the laws affecting imported merchandise, such as the levy of customs duties.

Foreign trade zones are authorized by the Foreign Trade Zone Board, a Federal agency chaired by the Secretary of Commerce. Such zones typically consist of specific factories, warehouses, or industrial parks.

Reasons for Change

A dynamic economy constantly experiences change. Markets shift, companies expand and decline, and there are changes in the composition of consumer products and in the combination of labor, materials, and plant and equipment used in production. In a country as large and diverse as the United States, industrial change also means geographic change—movement among the major regions from rural to urban areas, and from central city to suburbs. Unless mobile or failed businesses are replaced by new enterprises, local areas decay, and unemployment tends to become endemic.

Most Federal Government programs directed at the unemployed and distressed local areas have been directed at alleviating the burdens on the individuals and communities. Generally, the belief has been that alleviation and basic support would suffice until economic activity in these areas was revived.

Some programs to stimulate local enterprise and farming have been put into effect, and loans have been made available through the Small Business Administration and Farmers Home Administration. In addition, grants to local governments have been made so that they can initiate community development programs that would stimulate local business.

Federal, State and local government resources, however, have not been adequate to overcome the inertia of distress, and a new approach has been developed that will place primary emphasis on the abilities of private enterprise to create employment and economic activity. The keynote of this program is to select a limited number of distressed urban and rural areas in which private enterprise could expand after being relieved of as much government restraint as possible. These new areas are called enterprise zones, and they are in part modeled after the free trade zones that stimulate international trade in various parts of the world.

Consequently, the establishment of enterprise zones is designed to create jobs in depressed areas, with an emphasis on jobs for disadvantaged workers, and also to redevelop and revitalize these geographic areas themselves.

The intent of the program is to create a freer environment in which new businesses can start and prosper. The target is to stimulate business that would not have been started anywhere else rather than to encourage relocations of existing businesses. Instead, it is intended that the market will decide what activities should take place in the enterprise zones.

Federal participation in creating the new economic environment will take the form of designating the eligible areas and providing various tax benefits: investment credits in addition to those already available; employment credits; and relief from capital gains taxation for gains due to enterprise zone activity. In addition, Federal regulatory agencies will be encouraged to reduce the restraints of their regulatory processes to the maximum reasonable extent.

Local and State governments will be required, when nominating local areas for designation as enterprise zones, to make commitments such as reductions or relief from taxes or regulatory burdens or to increase the scope or amount of governmental services. Local private organizations also are encouraged to make commitments to foster the success of enterprise zones; these activities may include provision of services to the zones which ordinarily are considered as part of the local government's jurisdiction.

Thus, the enterprise zone concept involves the commitment of Federal, State and local governments and local private organizations to create a freer economic environment in which new private business may prosper in depressed areas.

The Committee believes that the provision of title III will successfully implement these significant and innovative ideas on an experimental basis.

Explanation of Provisions

1. Designation of enterprise zones

Definition of enterprise zone

Under the committee amendment, an enterprise zone is any area which is nominated as an enterprise zone by one or more local governments and the State or States in which it is located, and which is approved by the Secretary of Housing and Urban Development (Secretary) after consultation with the Secretaries of Agriculture, Commerce, Labor, and the Treasury, the Director of the Office of Management and Budget, and the Administrator of the Small Business Administration. In the case of an enterprise zone on an Indian reservation, the Secretary of the Interior also must be consulted.

The term "State" include Puerto Rico, the Virgin Islands, Guam, American Samoa, the Northern Mariana Islands, and any other possession of the United States. The term "local government" includes any county, city, town, township, parish, village or other general purpose political subdivision of a State, any combination of these subdivisions that is recognized by the Secretary, and the District of Columbia. In the case of a nominated area on an Indian reservation, the reservation governing body, as determined by the Secretary of the Interior, is deemed to be both the State and local government.

Before designating any area as an enterprise zone, the Secretary must promulgate regulations, after consultation with the above Federal officials, describing (1) the nominating procedures, (2) the size and population characteristics of an enterprise zone, and (3) the procedures for comparing nominated areas using the criteria specified below for evaluating commitments made by State and local governments and for establishing priorities to be applied in making designations.

The Secretary may designate enterprise zones only during a 36-month period that begins on October 1, 1983, or the first day of the first month after the effective date of the regulations, whichever is later. (The tax benefits described below would be effective no earlier than January 1, 1984.) No more than 75 enterprise zones may be designated during this period. At least one-third of the zones designated must be areas which are outside a standard metropolitan statistical area, are within a jurisdiction or jurisdictions of local government that have a population of less than 50,000, or are found by the Secretary (after consultation with the Secretary of Commerce) to be rural.

The Secretary may not designate an area as an enterprise zone unless the local government and the State in which the nominated area is located have the authority to nominate, to make commitments with respect to the zone, and to assure that the commitments will be fulfilled. Nominations must be submitted in the form, and with the information, required in the Secretary's regulations. The Secretary also would have to determine that the information submitted with a nomination is reasonably accurate and that no portion of the nominated area was already included in an enterprise zone or an area nominated as an enterprise zone.

Period of effect of designation

Under the committee amendment, any enterprise zone designation remains in effect from the date of designation to the earliest of December 31 of the calendar year 24 years later, the date stipulated by the State and local governments in their nomination application, or the date the zone designation is revoked by the Secretary. The Secretary, after consulting with the same Federal officials who must be consulted in designating enterprise zones, may revoke a zone designation if he determines that the State or local government is not substantially complying with the required State or local government commitments (described below).

Within 60 days after the Secretary designates any area as an enterprise zone, the relevant State or local government must submit to the Secretary an inventory of historic properties within the area. For purposes of the tax and regulatory provisions of the committee amendment, the zone designation will not be deemed to be in effect until this inventory is submitted.

Area requirements

The Secretary may designate an area nominated as an enterprise zone only if it meets requirements concerning size, population, area boundaries, unemployment, poverty, and other signs of economic distress. A description of these requirements follows:

a. The area must be within the jurisdiction of the local government seeking the designation and have a continuous boundary.

b. The most recent census must show that the area's population is at least 1,000 (4,000 if any part of the area, other than a rural area, is located in a metropolitan statistical area with 50,000 or more people) or the area must be entirely within an Indian reservation (as determined by the Secretary of the Interior).

c. The nominating governments must certify and the Secretary accept that the area is one of pervasive poverty, unemployment and general distress, and is located wholly within an area which meets the requirements for Federal assistance under section 119 of the Housing and Community Development Act of 1974, as in effect on the date of enactment.[1]

d. The nominating governments must certify and the Secretary accept that at least one of four additional requirements is satisfied: (1) the rate of unemployment as determined by the appropriate available data, is at least 1½ times the national unemployment rate; (2) according to the most recent census data, each census tract in the area has a 20 percent or higher poverty rate (or each census county division, where not tracted; (3) at least 70 percent of the households living in the area have income below 80 percent of the median income of the households of the area within the jurisdiction of the local government which nominates the area (determined in the same manner as under section 119(b)(2) of the Housing and Community Development Act of 1974); or (4) the population of the area has decreased by 20 percent or more between 1970 and 1980, as determined from the most recent census available.

Required State and local government commitments

Under the committee amendment, no area may be designated as an enterprise zone unless the local government and the State in which it is located agreed in writing that, during any period that the area was an enterprise zone, these governments will follow a specified course of action designed to reduce the various burdens borne by employers or employees in the area.

This course of action may be implemented by the State and local governments and private nongovernmental entities, and may be funded from the proceeds of any Federal program. The course of action may include, but is not limited to, (1) a reduction of tax rates or fees applying within the enterprise zone, (2) an increase in the level or efficiency of local services within the enterprise zone, particularly through experiments with the supply of these services by nongovernmental entities, (3) elimination, reduction or simplifi-

[1] Section 119 establishes a program of urban development action grants (UDAG) to severely distressed cities and urban counties to alleviate physical and economic deterioration through reclamation of neighborhoods. The eligibility of a city, or area within a city, generally is based on some or all of the city's or area's poverty rate, age of housing stock, growth in per capita income, growth in population, growth in retailing and manufacturing employment, unemployment rate, and income distribution.

cation of governmental requirements applying within the enterprise zone, (4) program involvement by private entities, organizations, neighborhood associations and community groups, particularly those within the nominated area, including a commitment from these private entities to provide technical, financial or other assistance to, and jobs or job training for, employers, employees and residents of the area, and (5) mechanisms to increase the equity ownership of residents and employees in the zone. Under (5), a State or local government could, for example, establish a revolving fund to help with the financing of employee buyouts of businesses within the zone.

The Secretary may, by regulation, prescribe procedures for modifying, after zone designation, a course of action to which the State and local governments have committed themselves. The committee intends that these regulations will not allow all aspects of the course of action to be modified, but instead, only those which establish conditions on which businesses and employees have not substantially relied in making their decisions to invest, employ or work in the zone. For example, the Secretary might allow a reduction in police protection if the crime rate in the zone goes down, but should not allow a property tax abatement to be revoked with respect to a business that relied on the continued availability of this abatement in making its investment decision. However, the committee believes that such commitments could be revoked with respect to businesses and employees that may locate in the zone after the modification of a course of action is approved. In no case is it the committee's intention to authorize the Secretary to permit the withdrawal of a commitment from the course of action without the substitution of a commitment of equal value.

Priority of designation

The committee amendment provides criteria for the Secretary to use in choosing areas nominated to be enterprise zones. The Secretary is required to give special preference to those nominated areas for which the strongest and highest quality contributions to a course of action (as described above) have been promised by the nominating governments, taking into account their fiscal ability to provide tax relief. The Secretary also is required to give preference to nominated areas with the following characteristics: (1) strongest and highest quality contributions in addition to contributions under item 4 above; (2) most effective and enforceable guarantees provided by nominating State and local governments that proposed courses of action actually would be carried out for the duration of the designation; (3) high levels of poverty, unemployment and general distress, particularly areas near concentrations of disadvantaged workers or long-term unemployed individuals for whom employment would be a strong likelihood if the area were designated a enterprise zone; (4) zone size and location that primarily stimulate new economic activity and minimize unnecessary Federal tax losses; (5) most substantial commitments by private entities of additional resources and contributions, including creation of new or expanded business activities; and (6) nominated zones which best exhibit such other factors, to be determined by the Secretary, consistent with the program's intent and important in minimizing unnecessary loss of Federal tax revenues.

Evaluation and reporting requirements

The Secretary of Housing and Urban Development must prepare and submit to Congress a report on the effects of designating qualifying areas as enterprise zones in accomplishing the purposes of the legislation. The first report must be submitted not later than the close of the fourth calendar year after the year in which areas are first designated as enterprise zones. Subsequent reports will be submitted at four-year intervals.

Interaction with other Federal programs

Tax reductions

Any reduction of taxes under any required program of State and local commitments under the enterprise zone program will be disregarded in determining the eligibility of a State or local government for, or the amount or extent of, any assistance or benefits under any law of the United States, including general revenue sharing payments.

For example, under the general revenue sharing program, as authorized by the State and Local Fiscal Assistance Amendments of 1980 (P.L. 96-604), payments are made to local governments under formulas based on various factors, including income tax and total tax collections of the areas. Thus, under the committee amendment, tax reductions attributable to a required commitment to a course of action for an enterprise zone will not be taken into account in calculating the distribution of revenue sharing payments.

Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970

Designation of an enterprise zone will not constitute approval of a Federal or federally assisted program or project as those terms are used in the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970. No person displaced from real property located in an area designated as an enterprise zone will, by virtue of that designation, have any rights or be entitled to any benefit pursuant to that Act, such as moving expenses, reimbursement of business losses, or provision of replacement housing, as a result of such designation.

National Environmental Policy Act

Designation of an area as an enterprise zone does not constitute a Federal action for the purposes of applying the requirements of the National Environmental Policy Act or other provisions of Federal law relating to the protection of the environment. As a result, none of the Federal procedural requirements relating to environmental assessments and impact statements need to be met on account of the designation of an enterprise zone.

Although the committee amendment waives certain procedural requirements associated with environmental laws in connection with the designation of enterprise zones, the Committee intends that the desgination of an area as an enterprise zone is not to be an indication that the substantive provisions of these environmental laws are to be enforced differently within the zone than outside the zone. (Under Subtitle C of the amendment, however, the governments, following designation, could petition the appropriate Federal agency for waiver of any Federal regulations other than those that are for the purpose of protecting persons against discrimination, those whose waiver would directly violate a statutory requirement, or those whose waiver would be likely to present a significant risk to the public health.)

2. Tax credit for zone employers

In general

Under the committee amendment, enterprise zone employers are eligible to claim a tax credit equal to the sum of two parts—(1) an amount based on the increase in annual wages paid to employees working in the zone relative to wages paid to area employees in the period immediately before the area was designated as an enterprise zone, and (2) an amount based on wages paid in the current period to disadvantaged individuals working in the zone. The credit is limited to the taxpayer's tax liability, and unused credit amounts are carried back for 3 years or carried forward for the longer of 15 years or the remainder of the period during which the enterprise zone designation is in effect.

Qualified wages and qualified employees

The computation of the credit is based on a definition of qualified wages paid to qualified employees.

Under the amendment, a qualified employee is any employee 90 percent or more of whose services directly relate to the conduct of the employer's trade or business located in an enterprise zone and who performs at least 50 percent of his service for the employer in an enterprise zone. A qualified employee does not include an employee with respect to whom the employer claims the targeted jobs credit. Further, under rules similar to those applicable to the targeted jobs credit, qualified employees do not include individuals who are related to, or are dependents of, the employer or who work other than in a trade or business of the employer.

Qualified wages generally are defined to include amounts subject to FUTA (Federal Unemployment Tax Act), without regard to any dollar limit (currently $7,000 per year per employee). Special rules similar to those used in the targeted jobs credit provide for wages paid in connection with agricultural and railway labor not covered by FUTA. Qualified wages for any period do not include any amount of federally funded on-the-job training payments the employer receives or is entitled to receive for a qualified employee for the period.

Increased enterprise zone employment

The first part of the credit is equal to 10 percent of the excess of qualified wages paid or incurred during the taxable year to qualified employees in all enterprise zones over base period wages with respect to all zones. However, qualified wages are not taken into account if they are taken into account in determining the amount of credit based on wages paid to economically disadvantaged individuals.

Base period wages, for any enterprise zone, is the amount of wages which is paid during the 12-month period prior to zone designation, or, if earlier, the date on which the enterprise zone is designated under State law enacted after January 1, 1981, and which would have been qualified wages paid to individuals who would have been qualified employees if the designation had been in effect during this 12-month period. If the employer had no active trade or business in an area for which an enterprise zone designation was in effect for the taxable year for which the credit computation is made, base period wages for that enterprise zone are zero.

Qualified wages taken into account for this portion of the credit may not exceed 2½ times the FUTA wage base in effect for the calendar year ending in the taxable year for which the credit computation is made. This limit is used for the computation of base period wages as well as for the computation of current period qualified wages. If the FUTA wage base is increased, from one year to the next, then the amount of base period wages used in computing the credit in the second year must be recomputed to reflect the higher limit on the amount of wages per employee which may be taken into account.

The increased enterprise zone employment portion of the credit is phased out starting in the taxable year of the taxpayer in which falls the twenty-first anniversary of the enterprise zone designation or, if earlier, the date 4 years before the date the zone designation was to expire. For this taxable year, the credit is reduced to 7½ percent of qualified wages. The credit is then reduced by 2½ percentage points for each succeeding year until fully terminated.

Disadvantaged individuals

The second part of the credit is computed with respect to qualified wages paid to qualified employees who are qualified disadvantaged individuals.

This portion of the credit is allowable for a total of seven years with respect to any qualified employee. The credit is 50 percent of qualified wages paid to a qualified economically disadvantaged individual for services performed during the 36-month period beginning the day the individual began work in an enterprise zone for an employer. The credit is then reduced 10 percentage points during each of the succeeding twelve-month periods, to 40 percent of qualified wages attributable to services rendered in the fourth year, 30 percent of qualified wages attributable to services rendered in the fifth year, 20 percent of qualified wages attributable to services rendered in the sixth year, and 10 percent of qualified wages attributable to services rendered in the seventh year. The credit with respect to any one employee is not available after the seventh year of employment. These time periods do not take into account any period of time during which the individual is unemployed or any period of time during which the individual is employed by a taxpayer in an enterprise zone designated under a State law enacted after January 1, 1981, if this designation occurred prior to the Federal designation.

A qualified disadvantaged individual is anyone who is hired during the period an enterprise zone designation is in effect for the area in which the services which qualify the individual as a qualified employee are performed and who is either a member of an economically disadvantaged family or a general assistance or AFDC recipient as defined for purposes of the targeted jobs credit. Thus, in the first alternative, the individual has to be certified by the designated local agency as being a member of a family that had an income, including the cash value of food stamps, during the 6 months immediately preceding the month in which the determination occurs, which, on an annual basis, is equal to or less than the combined Aid to Families with Dependent Children (AFDC) and food stamp benefits available to a family of the same size with no countable income or resources. This combined benefit amount is computed first by determining the highest amount ordinarily paid under the AFDC program, in the State in which the family resides, to a family of the same size as the family being considered for tax credit eligibility. A family need not be of a type normally eligible for AFDC for the purposes of applying this standard. For example, the tax credit eligibility of a married couple with no children would be determined on the basis of the AFDC payment available to a single parent and one child, even though childless couples are not eligible for AFDC payments. Determinations throughout the entirety of each State are to use the highest benefit amount available in any locality in the State to an assistance unit with no income and resources and with maximum need. The food stamp portion of the combined benefit amount then will be computed by assuming that the household's only income consists of AFDC benefits in the amount just determined, that the household consists only of the AFDC unit for which the computation is made (e.g., that there are no unrelated individuals living in the household), and that the family is entitled to the standard deduction and the maximum amount of other deductions which ordinarily are allowed to a household, the income of which consists entirely of AFDC benefits.

Alternatively, to be eligible for this portion of the tax credit, the individual must be certified as having been placed in employment under a work incentive program, or as receiving assistance under either the AFDC program for the 90-day period preceding the hiring date or under a general assistance program for not less than 30 days ending within the 60-day period ending on the day the individual is hired by the employer. Only those general assistance programs designated by the Secretary of the Treasury as consisting of money, voucher, or scrip payments based on need are to be taken into account for this purpose. The Secretary is not to designate any program designed specifically by a State or local government for enterprise zone residents in order to determine eligibility for this credit.

The credit amount is reduced 25 percent in the first year in which the increased employment credit begins to phase out, and this reduction factor is increased by 25 percent each year thereafter.

Other rules

Rules analogous to those contained in the present targeted jobs and research and experimental expenditures tax credits control certification procedures (such as the rule requiring certification on or before the date on which the individual begins work for the employer) and allocation and computation of the credit for controlled groups of businesses, for subchapter S corporations and their shareholders, for estate and trusts and their beneficiaries, and for employers affected by acquisitions and dispositions. Special rules also are provided for taxpayers for which a zone designation is in effect only part of the taxable year or with a short taxable year.

Any credit taken with respect to an economically disadvantaged employee is recaptured if the employee is terminated at any time during the first 270 days after the employee begins work for the employer, with certain exceptions, including voluntary termination, disability, or misconduct of the employee, or substantial reduction of the business. However, if the major portion of a trade or business, or the major portion of a separate unit of a trade or business of an employer is acquired by another employer, than employment of any qualified employee is not terminated for purposes of this credit if the employee continues to be employed in that trade or business.

No deduction is allowable to an enterprise zone employer for that portion of wages paid or incurred for the taxable year equal to the amount of credits allowable under this provision for the taxable year.

3. Tax credit for zone employees

Under the committee amendment, qualified employees are entitled to a nonrefundable tax credit equal to 5 percent of qualified wages for the taxable year. For purposes of this credit, qualified wages are equal to all remuneration paid for services of a qualified employee, but not including any compensation received from the Federal Government or any State or subdivision of a State, up to 1½ times the wage base in effect for the purpose of the Federal Unemployment Tax Act (FUTA) (currently $7,000). Thus, the maximum credit for any taxable year until the FUTA base is changed is 5 percent of $10,500 or $525.

For purposes of this credit, a qualified employee is an individual at least 90 percent of whose services are directly related to an enterprise zone trade or business and at least 50 percent of whose services are performed in an enterprise zone, and who is not an employee of the Federal Government or any State or local subdivision of any State. The determination of whether an individual is a qualified employee is to be made separately with respect to each of the individual's employers.

The credit phases out starting in the taxable year of the employee in which falls the twenty-first anniversary of enterprise zone designation, or, if earlier, the date 4 years before the date the zone designation is to expire, and phases out completely in 4 years.

Employers are required to report to qualified employees the amount of wages paid to such employees.

4. Investment tax credit for zone property

Under the committee amendment, an additional investment tax credit is allowed for certain capital investments in an enterprise zone.

Zone personal property

For recovery property (other than 15-year real property) an additional 3-percent credit is available for 3-year recovery property, and an additional 5-percent credit is available for 5-year property, 10-year property and 15-year public utility property. Recovery property that does not meet the general eligibility requirements under section 48(a)(1) for the investment credit or that is not eligible for the investment credit because the property is used in connection with lodging (sec. 48(9)(3)) is eligible for the additional 3- or 5-percent credit, but not for the regular investment credit.

In order to be eligible for this additional credit, property has to be acquired and first placed in service by the taxpayer in an enterprise zone during the period the designation as a zone is in effect. The property must be eligible for ACRS but does not have to be new property. The taxpayer has to use the property predominantly in the active conduct of a trade or business within an enterprise zone and may not acquire the property from a related person. Property used or located outside the enterprise zone on a regular basis is not eligible for the additional credit. In order to facilitate enforcement of this rule, the Secretary may prescribe by regulation that certain types of mobile equipment are ineligible for the credit.

The credit rate is reduced by 25 percent in the first year in which the employment credit begins to be phased out, and by an additional 25 percent each year thereafter. The basis of property eligible for the additional 3- or 5-percent credit would be reduced by one-half of that credit.

New zone construction property

An additional 10-percent tax credit is available for 15-year real property (including lodging) located in an enterprise zone if the property is acquired or constructed by the taxpayer and used predominantly in the active conduct of a trade or business, including the rental of real estate, within the enterprise zone. The credit is in addition to any investment credit to which the property is entitled under present law (e.g., the rehabilitation tax credit in the case of qualified rehabilitation expenditures and the regular credit for elevators and escalators).

In the case of property acquired by the taxpayer, the additional credit is available only if the property is acquired after designation of the zone and only if the original use of the property commences with the taxpayer. In the case of property constructed, reconstructed, or erected by the taxpayer, the credit would be available only to the extent of any construction, reconstruction or erection after designation of the enterprise zone. The credit rate is reduced by 25 percent in the first year in which the employment credit begins to be phased out, and by an additional 25 percent each year thereafter.

The basis of property eligible for this additional 10-percent tax credit is reduced by the full amount of the additional credit allowable.

Recapture

If property for which an enterprise zone credit was claimed by a taxpayer ceases to be enterprise zone property of the taxpayer (other than by expiration or revocation of the designation of the zone), a portion of the enterprise zone credit is recaptured. Property would cease to be enterprise zone property of a taxpayer if, for example, the taxpayer disposed of the property, removed the property from the enterprize zone, or ceased to use the property in the active conduct of a trade or business within the enterprise zone.

The amount of the enterprise zone credit subject to recapture is the difference between the amount of credit allowed for the property and a recomputed credit based on the amount of time the property was enterprise zone property of the taxpayer. The recomputed credit bears the same ratio to the amount of credit originally allowed as the number of taxable years in which the property was enterprise zone property of the taxpayer bears to the number of years over which the property is depreciated for purposes of computing earnings and profits. The recapture periods are as follows:

	Years
3-year property	5
5-year property	12
10-year property	25
15-year public untility property	35
15-year real property	35

Thus, for example, no enterprise zone credit is recaptured with respect to 3-year recovery property if it remains enterprise zone property of the taxpayer for 5 taxable years. If this property were enterprise zone property of the taxpayer for only 4 taxable years, 20 percent of the enterprise zone credit is recaptured.

Carryover period

Unused investment tax credit amounts attributable to the additional enterprise zone percentage may be carried forward for the remaining life of the enterprise zone or 15 years, whichever is longer.

5. Elimination of capital gains taxation

The committee amendment eliminates taxes on net long-term capital gains resulting from the sale or exchange of (1) property used in an enterprise zone in the active conduct of a trade or business or (2) an interest in a "qualified enterprise zone business." Additionally, the bill excludes net long-term enterprise zone capital gains from classification as a tax preference item for purposes of the noncorporate and corporate minimum taxes.

Qualified property and qualified business

The amendment eliminates tax on net gain from sales or exchanges of "qualified enterprise zone property" otherwise eligible for long-term capital gain treatment. For this purpose, the term "qualified enterprise zone property" would mean (1) tangible personal property used predominantly by the taxpayer in an enterprise zone in the active conduct of a trade or business in a zone, (2) real property located in an enterprise zone and which is used predominantly by the taxpayer in the active conduct of a trade or business in a zone and (3) an interest in a corporation, partnership, or other entity if, for the two most recent taxable years of the entity ending before the date of disposition of the interest and beginning after the date on which the zone was designated, the entity was a "qualified enterprise zone business."

Under the provision, the term "qualified enterprise zone business" means any person (1) actively engaged in the conduct of a trade or business (including rental of real estate) during the two taxable years described in the previous sentence, (2) at least 80 percent of the gross receipts of which for the taxable year are attributable to the active conduct of a trade or business within an enterprise zone, and (3) substantially all of the tangible assets of which are located within an enterprise zone.

Under the amendment, gains and losses from the sale or exchange of qualified enterprise zone property are taken into account only to the extent they are properly allocable to periods during which the property is qualified enterprise zone property or, in the case of an interest in a zone business, periods during which the business is a qualified enterprise zone business. Thus, a determination of the fair market value of the property must be made as of the date the property begins to be used in the active conduct of a trade or business in a zone, in the case of tangible property, or as of the date on which a business begins to be a qualified enterprise zone business, in the case of an interest in a qualified enterprise zone business. In addition, net gain from the sale or exchange of an interest in a qualified enterprise zone business is not treated as gain from the sale or exchange of qualified property to the extent the gain was attributable to (1) any property contributed to the qualified business within the previous 12 months, (2) any interest in a business which is not a qualified business, or (3) any other intangible property not properly attributable to an active trade or business within an enterprise zone. Intangible property includes, but is not limited to, items described in section 936(h)(3)(B), such as patents, copyrights, trademarks and franchises. In determining whether intangible property is attributable to active trade or business within a zone, the Secretary is to take into account factors such as whether or not the intangible was acquired in an arm's-length transaction and the extent to which the intangible was developed within the zone.

Under the amendment, the special tax treatment for gain from sales or exchanges of qualified enterprise zone property does not cease to be available upon the termination or revocation of an area's designation as an enterprise zone. However, the treatment does not apply after the first sale or exchange of any item of qualified enterprise zone property after the designation ceases to apply.

Noncorporate capital gains deduction

The amendment allows a noncorporate taxpayer to deduct from gross income 100 percent of any net long-term capital gain from qualified enterprise zone property.

Corporate capital gains tax

The amendment allows a corporation to exclude from taxation all net long-term capital gain from qualified enterprise zone property.

Tax preferences for minimum tax purposes

The amendment eliminates net capital gains attributable to qualified enterprise zone property from classification as a tax preference item for purposes of the corporate and noncorporate minimum taxes.

6. Industrial development bonds

The committee amendment provides that the provision of present law which restricts the cost recovery deductions for property financed with tax-exempt bonds will not apply to enterprise zone property eligible for the additional investment credit described above.

The amendment also provides that the provision of present law which terminates the small issue exception after December 31, 1986, does not apply to any obligation which is part of an issue substantially all of the proceeds of which are used to finance facilities placed in service in an area for which an enterprise zone designation is in effect.

7. Tax simplification

The committee amendment provides that it is the sense of the Congress that the Internal Revenue Service should, in every way possible, simplify the administration and enforcement of the tax provisions added to the Internal Revenue Code by this bill.

8. Regulatory flexibility

Designation of zone entities of small entities for purposes of analysis of regulatory functions

The committee amendment expands the definition of a small entity, for purposes of the Regulatory Flexibility Act, to include any qualified zone business, any government designating an area as an enterprise zone to the extent any regulatory rule would affect the zone, and any not-for-profit enterprise operating within an enterprise zone.

Waiver or modification of agency rules in enterprise zones

Under the committee amendment, Federal agencies and regulatory bodies are given discretionary authority to relax or eliminate any regulatory requirements within enterprise zones except those affecting civil rights, safety and public health, or those required by statute, including any requirement of the Fair Labor Standards Act. This authority would be exercised only upon request of State and local governments.[2] Agencies are to make their determinations on requests not later than 90 days after their receipt. Such waivers or deterimінations will not be considered a rule, rulemaking, or regulations under the Administrative Procedure Act.

Coordination of housing and urban development programs in enterprise zones

The committee amendment provides that the Secretary of Housing and Urban Development is required to promote the coordination of programs under his jurisdiction and carried on in an enterprise zone and to consolidate requirements for related applications and reports required under these programs.

9. Establishment of foreign trade zones in enterprise zones

The committee amendment requires the Foreign Trade Zone Board to expedite on a priority basis the processing and approval, to the maximum extent practicable, of any application involving the establishment of a foreign trade zone within an enterprise zone. The Secretary of the Treasury is required to give the same urgent consideration to an application for establishment of a port of entry necessary to permit the establishment of a foreign trade zone within an enterprise zone.

Effective Date

The provisions relating to designations of enterprize zones, regulatory flexibility and foreign trade zones are effective on the date of enactment.

The provisions for tax credits for enterprise zone employers and employees are effective for taxable years beginning after December 31, 1983.

The extra investment tax credit for enterprise zone property is effective for periods after December 31, 1983, under rules similar to section 48(m) of the Internal Revenue Code.

The provisions eliminating capital gains taxation are effective for sales or exchanges after December 31, 1983.

The provisions related to industrial development bonds apply to obligations issued after December 31, 1983, in taxable years ending after such date.

Revenue Effect

The effect of the enterprise zone provisions on budget receipts will depend on the number, size, and characteristics of the zones designated by the Secretary of Housing and Urban Development. Because the amendment provides the Secretary with wide latitude in his choice, the committee is unable to provide specific cost estimates for these provisions.

The Treasury Department estimates that these provisions will reduce fiscal year receipts by $87 million in 1984, $400 million in 1985, $765 million in 1986, $1,058 million in 1987 and $1,142 million

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[2] Examples of regulations which could be relaxed include regulations governing exports, regulations affecting accounting treatment of loans made by national banks, regulations affecting inventory accounting for tax purposes, regulations affecting issuance of securities, and regulations affecting various energy performance, coal conversion, and conservation regulations.

in 1988. These estimates are based on particular assumptions about the size and characteristics of the zones. However, these assumptions are not mandated by the provisions of this amendment, and thus, these figures may either underestimate or overestimate the actual revenue loss by a considerable degree.

Treasury's estimates are based on the assumption that the zones selected by the Secretary of Housing and Urban Development would have, at the time of designation, average employment, other than in governments and non-profit institutions, of 7,000 and a mix of economic activities similar to those of a sample of distressed areas in several large cities and rural areas. The language of the amendment does not require this average employment and economic mix, however, so that the above figures may not estimate the actual revenue loss. If the average zone has, for example, only 3,500 employees, then actual revenue losses would be $0.04 billion, $0.2 billion, $0.4 billion, $0.5 billion, and $0.6 billion in fiscal years 1984 through 1988, respectively, if the assumptions about the economic mix were correct.

On the other hand, several factors could make the actual revenue loss higher than the Treasury estimates. First, the actual mix of economic activities in the zone or attracted to the zone could be very payroll intensive and have a high ratio of investment to payroll, substantially increasing the cost of the tax incentives relative to what was assumed. Second, the Treasury estimate assumes that 25 zones are designated annually during the 1984–1986 period. If more than 25 zones are designated in 1984 and 1985, the revenue loss would be larger in all years. Third, the average size of zones when they are actually designated by the Secretary could be much larger than an average taxable employment of 7,000. If, for example, employment in designated zones were to average 35,000 and the economic mix were the same as assumed by Treasury, fiscal year revenue losses would be $0.4 billion in 1984, $2.0 billion in 1985, $3.8 billion in 1986, $5.3 billion in 1987 and $5.7 billion in 1988.

TITLE IV—INTERNATIONAL TRADE AND INVESTMENT ACT*

A. SUMMARY

Title IV of the committee amendment amends Titles I and III of the Trade Act of 1974 by mandating new specific sector negotiating objectives with respect to trade in services, high technology products, and restrictions on foreign direct investment; by giving the President tariff modification authority on certain high technology items; by authorizing the establishment of intergovernmental advisory committees; by requiring the United States Trade Representative to analyze and report on significant barriers to trade in U.S. products and services and restrictions on foreign direct investment by U.S. persons; by clarifying the President's authority to retaliate with respect to any goods or sector, whether or not involved in the act retaliated against and to take action notwithstanding any other delegation of authority to regulatory agencies; by providing the President with the authority to propose "fast track" legislation under the authority of sections 102 and 151 of the Trade Act to carry out the objectives of section 301; by defining the term "commerce" to include foreign direct investment with implications for trade in goods and services, thereby permitting the President to retaliate against restrictions on such investment; by statutorily defining the terms "unjustifiable," "unreasonable," and "discriminatory"; by providing for the initiation of section 301 investigations by the USTR; by providing for delays of up to 90 days in the initiation of international consultations required by section 303; and by providing a specific exemption from the requirements of the Freedom of Information Act for information supplied under specified conditions during an investigation under section 301 and restrictions on the use of such information.

B. GENERAL EXPLANATION

Present Law

The President's principle authority to retaliate against foreign unfair trade practices is section 301 of the Trade Act of 1974 (19 U.S.C. 2411). Section 301 was amended by the Trade Agreements Act of 1979 (P.L. 96-39). Two major changes were made. The President's authority was expanded in order that he would have clear authority to pursue U.S. rights under any applicable trade agreements, and time limits were established for the conclusion of section 301 investigations.

Under section 301, as amended, the President is authorized, where appropriate, to use the authority set forth therein to enforce

*This title of the committee amendment was previously reported by the Committee on Finance in S. 144 (S. Rep No. 98-24, Mar. 14, 1983), and passed by the Senate on Apr. 2, 1983.

U.S. rights under trade agreements, including the various nontariff agreements negotiated in the Multilateral Trade Negotiating. The law provides a process through which private parties can seek U.S. government action to enforce rights created by these agreements. It requires that consultations be initiated under the dispute settlement procedure of the applicable international agreement, if any. The time requirements set forth in section 301 within which the President must act are also keyed to the dispute settlement procedure in the particular agreement under which the complaint is brought.

The President is also authorized, where appropriate, to use section 301 to respond to any "act, policy, or practice" of a foreign country that is inconsistent with the provisions of or denies benefits to the United States under any trade agreement, or is "unjustifiable," "unreasonable," or "discriminatory" and burdens or restricts United States commerce. All acts, policies, or practices covered under the 1974 Act are covered under section 301, as amended, notwithstanding the deletion of the specific reference to subsidies and access restrictions as unfair acts. Amendments to the 1979 Act also clarified that U.S. "commerce" includes all services associated with international trade and not just those associated with trade in merchandise.

The President's retaliatory authority remained basically unchanged in the 1979 Act. The President is authorized to take any action otherwise within his authority to respond to the foreign unfair actions. He is also authorized to suspend, withdraw, or modify trade agreement concessions or impose duties or other import restrictions or fees on the products or services of the foreign country.

Another change made by the 1979 Act was to provide a procedure through which the public could request from the USTR certain information on foreign trade policies or practices. If such information is not available, the USTR is required to request it from the relevant foreign government or decline to do so and inform the person making the request in writing of the reasons for refusing.

The Committee Amendment

Overview

Title IV of the committee amendment makes the following changes to the Trade Act of 1974:

(1) A new section 104A would be added providing specific negotiating objectives with respect to trade in services, high technology products, and restrictions on foreign direct investment;

(2) Section 135, which sets up a procedure through which trade negotiating advice is received from the private sector, would be amended to authorize the establishment of intergovernmental advisory committees;

(3) A new section 181 would be added requiring annual national trade estimates on significant barriers to the exportation of U.S. goods and services and restrictions on U.S. foreign direct investment, any action taken to eliminate these barriers, and consultations with the Finance and Ways and Means Com-

mittees on trade policy priorities to enhance market opportunities;

(4) Section 301 would be amended to provide the President with specific authority to retaliate against any goods or sector, whether or not involved in the act retaliated against and the President would specifically be authorized to retaliate against a good or service notwithstanding authority of regulatory agencies to deal with the same matters;

(5) Section 301 would be amended to authorize the President to retaliate against restrictions on foreign direct investment by U.S. persons with implications for trade in goods and services, or to otherwise carry out the objectives of 301 by proposing "fast track" legislation under the authority of sections 102 and 151 of the Trade Act of 1974;

(6) Section 301 would be amended by statutorily defining the terms "unreasonable", "unjustifiable" and "discriminatory" which currently exist in section 301 but are not defined;

(7) Section 302 would be amended to provide for the self-initiation of section 301 investigations by USTR;

(8) Section 303, which currently provides that international consultations must be initiated on the same date as an investigation is instituted under section 301 would be amended to provide for a delay of up to 90 days before the initiation of consultations; and

(9) Section 305 would be amended to provide for a specific exemption from the Freedom of Information Act for information received during an investigation under section 301 and restrictions on the use of such information.

Section-by-Section Analysis

Section 401 of title IV sets forth the short title, "the International Trade and Investment Act".

Section 402 sets forth the statement of purposes of title IV. These purposes include the fostering of U.S. economic growth and employment by expanding competitive U.S. exports through the achievement of commercial opportunities in foreign markets substantially equivalent to those accorded by the United States; improving the ability of the President to identify and analyze barriers to U.S. trade and investment; encouraging the expansion of international trade in services through the negotiation of international agreements; and enhancing the free flow of foreign direct investment through the negotiation of bilateral and multilateral agreements.

Section 403 of the committee amendment requires annual national trade estimates on significant barriers to U.S. commerce, reports to Congress on action taken (including but not limited to any action under section 301) on matters identified in the national trade estimates and administrative provisions related to these estimates. Under present law the Executive Branch has been slow to identify critical problems or to take advantage of trade agreements to enforce United States rights of market access. Formulating national trade estimates is a step in the direction of a more active policy of enforcing United States rights under trade agreements and identifying objectives for future negotiations.

Under *subsection (a),* the USTR, through the interagency Trade Policy Committee, would be required to identify the acts, policies, and practices which constitute significant barriers to or distortions of U.S. exports of goods or services and U.S. foreign direct investment. In addition to foreign barriers, these could include U.S. export disincentives.

The committee amendment specifies that the USTR shall identify and analyze acts, policies, and practices which restrict or distort foreign direct investment by U.S. persons especially if such investment has implications for trade in goods or services. It is the Committee's intention that the USTR should focus it efforts in the area of trade related investment issues and not on other issues, such as the expropriation of U.S. investment in foreign countries.

The committee amendment also requires the USTR to make an estimate of the trade distorting impact of any act, policy, or practice identified. In making the national trade estimates the USTR is directed to take into account a number of specified factors including the relative impact of the barriers, the availability of relevant information, and the extent to which the barriers are subject to international agreements as well as advice received under the advisory committee process. It is the Committee's intention in using the word "significant" and setting forth these factors among others to be considered that the USTR will proceed against those barriers to the expansion of market opportunities which are most important in terms of U.S. commercial interests and with respect to which there is the greatest likelihood of achieving solutions, particularly within accepted international procedures.

The specific inclusion of the Trade Policy Committee in this process is intended to make clear that the amendment in no way serves to reorganize existing agency functions. Rather the structure established under section 242(a) of the Trade Expansion Act of 1962 is to continue to be utilized. While it is the intention of the Committee that the national trade estimates should be as specific as practicable, it is not intended that they serve to prejudge or to prejudice any petitions which have been or may be brought under the dispute settlement process.

Subsection (b) requires the USTR to submit the analysis and estimate within one year of the date of enactment of the bill and annually thereafter to the Committees on Ways and Means and Finance. These reports are to include information on any action being taken with respect to the actions which have been identified and analyzed including but not limited to actions under section 301 or international negotiations or consultations. While not requiring that any particular action be taken, the Committee intends that the USTR should consider vigorously utilizing existing authorities and dispute settlement procedures to deal with the identified barriers and distortions. This subsection also requires the USTR to keep the Ways and Means and Finance Committees currently informed on trade policy priorities for the purpose of expanding market opportunities. These consultations are not statutorily tied to the analysis and reporting requirements, but it is the Committee's intention that the required consultations draw heavily on the information and estimates developed during this process. Information contained in national trade estimates may be classified or otherwise not be made public to the extent appropriate to the information contained therein.

In carrying out the requirements of this section, the head of each department or agency of the executive branch of the Government is authorized and directed to furnish to the USTR, or to the appropriate agency upon request, such data, reports, and information as necessary for the USTR to carry out his functions under this section. The authorization for agencies to furnish information to the "appropriate agency" is intended only to maintain existing interagency reporting relationships, such as that of the Federal Reserve with the Department of the Treasury, and is not intended to impair the ultimate transmission of information of the USTR. It is the Committee's intention that this authority should be used by the USTR to request only that information which is reasonably available to the particular agency. It is not intended to be a general grant of authority to require such agencies to gather information. The information may be requested and used to the extent not otherwise inconsistent with law. This specific limitation is intended by the Committee to make clear that information such as that obtained by the Internal Revenue Service is not within the scope of that which could be requested by or released to the USTR. It is also the Committee's intention that information to be made available to the USTR would be provided subject to lawful regulations governing the protection of national security, business confidential, or otherwise privileged information.

Section 404 of the committee amendment makes a number of amendments to Title III of the Trade Act of 1974. Section 301(a) currently provides that action under this section may be taken on a nondiscriminatory basis or solely against the products or services of the foreign country or instrumentality involved. The amendment amends current law to provide that the President may exercise his authority specifically with respect to any goods or sector, on a nondiscriminatory basis or solely against the foreign country or instrumentality involved, and without regard to whether or not such goods or sectors were involved in the act, policy, or practice identified. This change in language is not intended to confer new retaliatory authority on the President; rather it is intended to clarify the President's existing authority. The use of the word "product" in current law has raised questions as to whether its scope is limited to articles which have undergone some manufacturing or transforming process. The use of the word "goods" in intended to clarify that the President would have the authority to retaliate against any article whether or not it had undergone processing. Similarly the change from the word "service" to "sector" is intended to clarify that the President, in acting under section 301, could exercise his powers with respect to services offered by foreign countries or foreign nationals as well as with respect to foreign direct investment in the United States either under legislation proposed under the "fast track" authority which would be established or any other independent grant of authority. At present, such authority appears to be limited to the Mineral Lands Leasing Act of 1920 (30 USC 181) and section 48 of the Internal Revenue Code.

Section 301(b) currently authorizes the President to retaliate (1) by modifying trade agreement concessions and (2) by imposing duties or other import restrictions on the products of, or fees or restrictions on the services of a foreign country. The committee amendment makes the conforming changes of the word "goods" for the word "products" and would insert the phrase "notwithstanding any other provision of law" before the word "impose". This is intended to clarify the President's existing authority to impose restrictions notwithstanding the authority of an independent agency. While the authority of the President under section 301 is broad, the Committee does intend it to be used prudently. It may appropriately be used to impose restrictions on services previously licensed by an independent agency or by denying the grant of such a license, but the Committee does not anticipate the authority would be used to override U.S. treaty obligations.

The committee amendment also amends section 301(b) by adding a new subsection (3) authorizing the President to propose "fast track" legislation under the procedures of sections 102 and 151 of the Trade Act of 1974 to carry out the objectives of section 301 where additional retaliatory authority may be necessary. Since the definition of "commerce" in section 301(d) would also be amended to include foreign direct investment by U.S. persons with implications for trade in "goods or services", this would permit the President to propose "fast track" legislation providing for retaliation against, or designed to encourage the elimination of, restrictions on U.S. foreign direct investment. The Committee does not intend that the authority to propose "fast track" legislation in any way restrict the President's authority to propose legislation under nonfast track procedures. The choice of whether or not to utilize the "fast track" would be solely within the President's discretion. Under the amendment, all the requirements for "fast track" legislation set forth in sections 102 and 151 would be applicable, including 90 days consultation with the cognizant committees prior to submitting such legislation.

Section 301(d) currently contains a definition of the term "commerce". As set forth above, the committee amendment would amend subsection (d) by including in the term "commerce" foreign direct investment by U.S. persons with implications for trade in goods and services. It is not the Committee's understanding, however, that this language would preclude the USTR, where appropriate, from conducting an investigation on portfolio investments. It would also include in that subsection definitions of the terms "unreasonable", "unjustifiable", and "discriminatory", which currently exist in section 301 but are not statutorily defined. The definitions of these three terms are not intended to expand the scope of the President's authority with respect to the types of acts against which he can retaliate, other than with respect to foreign direct investment as notified above. It is the Committee's intention that the definitions clarify existing law and give emphasis to the President's authority to retaliate against certain types of acts, policies, and practices.

The term "unreasonable" is defined as any act, policy, or practice which, while not necessarily in voilation of or inconsistent with the international legal rights of the United States, is otherwise deemed to be unfair and inequitable. The term includes, but is not limited to, a denial of fair and equitable market opportunities, opportunities for the establishment of an enterprise, or provision of adequate protection of intellectual propety rights. The phrase "fair and equitable" is not defined, since it remains within the President's discretion to determine when circumstances exist which require action under this provision. The Committee believes the President will take into account a broad range of factors in making his determination as to when to proceed, but by including a specific noninclusive list in the bill wishes to emphasize that certain acts, policies and practices which are not necessarily in violation of specific international agreements are becoming increasingly harmful to U.S. interests and should be dealt with accordingly.

Among these acts are investment-distorting practices. Performance requirements and other restrictions that impair or distort the free flow of capital and inhibit U.S. firms from establishing themselves and operating abroad are increasingly and adversely affecting U.S. trade interests. The Committee has also received testimony and information concerning increasingly frequent problems regarding the denial of adequate protection by foreign countries of U.S. intellectual property rights. The term is intended to be understood in the broadest sense and shall include patents, trade marks, trade names, copyrights, and trade secrets. Some of the problems concerning intellectual property rights involve broad areas of invention not subject to patent coverage in foreign countries, such as chemical products; unreasonable forced licensing and forfeiture provisions for patents; unduly short patent rights involving the inability to enjoin infringement; very low or token fines where infringement is proved, protracted delay of proceedings with no interim relief available to the patent holder; practically impossible burdens of proof of process infringement placed on patent holder; and the like.

The Committee believes that in determining whether adequate protection is being provided for such rights the President should consider the scope and degree of protection of the foreign country's laws and procedures. A key factor in the USTR's determination of whether to initiate a section 301 petition should be a consideration of the appropriate legal action available to, or taken by, the aggrieved United States party to defend its rights in the subject country. The Committee expects, however, that if the U.S. Trade representative determines not to initiate a section 301 petition, due to pending action by a foreign country's judiciary, action on the petition should be postponed only for a reasonable period of time.

The term "unjustifiable" is defined as any act, policy, or practice which is in violation of or inconsistent with the international legal rights of the United States, including but not limited to a denial of national or most-favored-nation treatment, the right of establishment or a denial of protection of intellectual property rights. It is the belief of the Committee that this definition conforms with existing law and legislative history and is not an expansion of the category of unjustifiable actions against which retaliation can be taken. The definition continues to address actions by a foreign government that are inconsistent with U.S. international legal rights.

The term "discriminatory" is defined as including where appropiate any act, policy, or practice which denies national or most-favored-nation treatment to U.S. goods, services, or investment. The phrase "where appropriate" has been included in the definition only to take into account those situations in which a denial of national or most-favored-nation treatment, for example in the case of a GATT-compatible customs union, is not an appropriate basis for action.

The Committee amendment amends section 302 of the Trade Act by authorizing the USTR to self-initiate investigations under section 301. According to testimony received by the Committee, in many cases U.S. exporters adversely affected by foreign practices inconsistent with U.S. trade agreement rights do not petition for assistance under section 301 for legitimate reasons, such as lack of information or a fear of retaliation. Therefore, a vigorous policy of self-initiation is necessary to preserve U.S. market access. Under current law, the President is authorized to take action either as a result of petition-initiated investigation or, on his own motion, but the USTR is not authorized to initiate investigations to provide a foundation which advice could be provided to the President. While providing authority for the USTR to initiate investigations, the amendment provides that a decision to do so could only be taken after consultation with appropriate committees established under section 135. Under the amendment if the USTR determines to initiate this determination is to be published in the Federal Register and treated as if an affirmation on a petition had been made on the same date. This provision is intended to bring into play all the provisions applicable to cases initiated by petition.

It is anticipated that USTR-initiated cases would be the result of careful study, usually accomplished by national trade estimates, as well as careful coordination with statutory advisory committees. This process should, overall, result in a more coherent, aggressive, trade policy.

The Committee amendment amends section 302 to require that a summary of the petition on the basis of which an investigation is instituted, rather than the petition itself, be published in the Federal Register. Copies of the documents would be provided at cost. The publication of entire petitions in the Federal Register has become an increasingly costly undertaking. The Committee believes that publication of a summary together with the availability of the documents at reproduction cost will save money and at the same time provide the public with adequate notice and information with respect to cases which are instituted.

Section 303 of the Trade Act currently provides that on the date an affirmative determination is made to institute an investigation under section 301 the USTR must request consultations with the foreign country concerned regarding the issues raised in the petition. The administration has testified that the requirement of simultaneous initiation and requests for consultations has caused problems in several cases in which the petitions on which investigations are initiated did not provide an adequate basis for proceeding internationally. The Committee amendment amends section 303 to provide USTR with the authority to delay for up to 90 days any request for consultations for the purpose of verifying or improving the petition to insure an adequate basis for consultation. The amendment also requires the USTR to publish notice of the delay in the Federal Register and report to Congress on the reasons for such delay in the report currently required under section 306. It is the belief of the Committee that this authority should be used only in the unusual circumstances described and that the USTR should continue to make every effort to conclude section 301 actions within the prescribed normal time limits.

The Committee amendment also amends section 305 by adding a new subsection with respect to the treatment of confidential business information. The administration has testified that many U.S. firms or groups are reluctant to petition for investigations under section 301 because of their concern that confidential business information which they might provide during the course of the proceeding might be subject to disclosure or that they will be subject to retaliatory actions in the offending country. The amendment provides a specific exception from the Freedom of Information Act for business confidential information requested and received by the USTR in aid of any investigation under Chapter 1 of Title III of the Trade Act and provides that such information shall not be made available if submitted under the circumstances set forth therein. The amendment further provides the USTR with authority to prescribe regulations concerning provision of nonconfidential summaries of such information in order to give USTR the necessary flexibility in dealing with foreign countries or instrumentalities which provide such information but cannot be compelled to provide summaries. The amendment also authorizes the USTR to use the information or make it available to an employee of the Federal Government for use in a section 301 investigation but requires that it be made available to any other person only in a form in which it cannot be associated with the source of the information. The Committee believes that by protecting confidential information and its source these provisions will encourage and facilitate the filing of legitimate petitions under section 301, as well as encouraging and supporting self-initiated investigations.

Section 405 of the committee amendment amends Chapter 1 of title I of the Trade Act by adding a new section 104A providing specific negotiating objectives with respect to international trade in services and investment and high technology products. Under these provisions, principal U.S. negotiating objectives with respect to trade in services would be the reduction or elimination of barriers to or distortions of international trade in services and the development of internationally agreed rules, including dispute settlement procedures, to reduce or to eliminate such barriers. The terms "services" and "services associated with international trade" have not been defined. The Committee was concerned that any definition would be limiting. The intent of the Committee is that "services" and, for purposes of section 301 "services associated with international trade" be defined as broadly as possible.

Similarly, the committee amendment sets forth as negotiating objectives with respect to foreign direct investment, the reduction or elimination of artificial or trade distorting barriers, the development of rules, including dispute settlement procedures, to ensure the free flow of foreign direct investment, and the reduction or elimination of the trade-distortive effects of certain investment-related trade measures.

The committee amendment also provides U.S. negotiating objectives with respect to high technology products. Among these are to obtain and to preserve the maximum openness of trade and investment in high technology products and related services; to obtain the elimination or reduction of, or compensation for, the significantly distorting effects of foreign government actions which affect trade in high technology products identified in the studies which would be required under section 181; to obtain commitments that the official policy of foreign governments or instrumentalities will not discourage government or private procurement of foreign high technology products; to obtain the reduction or elimination of all tariffs and barriers on U.S. exports of high technology products particularly key commodity products (a term the committee uses to identify standardized products sold in substantial quantities throughout the world such as the 64,000 random access memory electronic silicon chip); to obtain commitments to foster national treatment; to obtain commitments to foster pursuit of joint scientific cooperation and to ensure that access to the results of cooperative efforts should not be impaired; and to provide minimum safeguards for the acquisition and enforcement of intellectual property rights and the property value of proprietary data.

Section 406 of the committee amendment contains additional provisions with respect to trade in services.

Subsection (a) provides that the USTR, through the interagency Trade Policy Committee, shall develop and coordinate U.S. policies concerning trade in services and that each department or agency responsible for the regulation of a service industry shall advise and work with the USTR concerning matters that have come to the department's or agency's attention with respect to the treatment of U.S. service sector interests in foreign markets or allegations of unfair practices by foreign governments or companies in a service sector. The Committee intends that the existing trade policy structure be utilized to develop and coordinate policies concerning trade in services but has specified that these efforts be carried out in conformance with existing provisions of law in order to ensure that no authority granted under this section be construed as altering the existing authority of any agency or department with respect to any specific service sector.

Subsection (b) would establish in the Department of Commerce a service industry development program.

Subsection (c) provides that it is the policy of the Congress that the President shall, as he deems appropriate, consult with state governments on issues of trade policy affecting them. It also authorizes the President to establish one or more intergovernmental policy advisory committees under the structure and procedures established in Section 135 of the Trade Act. It is the committee's intention that these intergovernmental advisory committees be established and utilized only in the areas, like insurance or procurement, where the states have particular interests and not across the broad spectrum of trade issues.

Section 407 of the committee amendment amends section 102 of the Trade Act by defining the term "international trade" to include foreign direct investment by United States persons, especially if such investment has implications for trade in goods and services. This change would provide the President with specific authority to negotiate with respect to barriers on such foreign direct investment.

Section 408 of the committee amendment provides the President with authority to enter into bilateral or multilateral agreements as may be necessary to achieve the objectives of this section and those set forth in the proposed section 104A(c) concerning high technology products.

Subsection (b) provides the President with a five-year authority to eliminate the duties on specified items within six item numbers of the Tariff Schedules of the United States in order to carry out any agreement concluded as a result of the negotiating objectives under the proposed section 104A.

C. BUDGETARY IMPACT

The following statement is made relative to the effect on revenues of title IV. The Committee does not expect any immediate impact on revenues from the tariff-reducing authority provided in title IV. It is expected that the negotiations authorized by title IV will not be completed for some time. If the full authority were used to eliminate duties on the seven specified items, the Committee estimates there could be a possible loss of customs revenues of between $400 million and $500 million by 1987.

D. VOTE OF THE COMMITTEE

The Committee states that on March 14, 1983, S. 144 as amended, which comprises the substance of title IV, was ordered favorably reported without objection.

TITLE V—PERMANENT EXTENSION OF TAX EXEMPTION FOR INTEREST ON QUALIFIED MORTGAGE BONDS

Present Law

In general

The Mortgage Subsidy Bond Tax Act of 1980 [1] imposed restrictions on the ability of State or local governments to issue bonds, the interest on which is tax-exempt, for the purpose of making mortgage loans on single-family residences.[2] The 1980 Act provides that interest on mortgage subsidy bonds is exempt from taxation only if the bonds are "qualified veterans' mortgage bonds" [3] or "qualified mortgage bonds."

Qualified mortgage bonds

In order for an issue of bonds to be qualified mortgage bonds, the following requirements must be met:

(1) The bonds must be issued before Janaury 1, 1984;

(2) The aggregate annual value of such bonds that a State, and local governments within the State, can issue is limited to the greater of (a) 9 percent of the average annual aggregate principal amount of mortgages executed during the 3 preceding years for single-family owner-occupied residences located within the State or (b) $200 million;

(3) The bond proceeds must be used to finance the purchase of single-family residences which are located within the jurisdiction of the issuing authority and which are reasonably expected to become the principal residences of the mortgagors;

(4) With limited exceptions, only new mortgage loans are permitted to be made from the bond proceeds;

(5) At least 20 percent of the proceeds of each issue must be available for financing in certain low-income "targeted" areas;

(6) At least 90 percent of the mortgage loans made from each issue generally must be made to mortgagors who did not have a present ownership interest in a principal residence at any time during the 3-year period ending on the date their mortgage loans are made;

(7) All of the mortgage loans must be made to finance the purchase of residences for which the acquisition cost is below prescribed levels; and

[1] Title XI of the Omnibus Reconciliation Act of 1980 (P.L. 96-499). The provisions adopted by this Act (Code sec. 103A) were subsequently amended by section 220 of the Tax Equity and Fiscal Responsibility Act of 1982 (P.L. 97-248) ("TEFRA").

[2] Tax-exempt industrial development bonds also may be issued to finance projects for certain multi-family residential rental housing. Tax-exemption for such bonds is permanent.

[3] Qualified veterans' mortgage bonds are general obligation bonds, the proceeds of which are used to finance mortgage loans to veterans. The tax-exemption for veterans' bonds is permanent.

(8) Each issue of qualified mortgage bonds must meet certain limitations regarding arbitrage, both as to mortgage loans and nonmortgage investments.

Reasons for Change

The Committee is concerned over the difficulty of many Americans in making first-time home purchases under present market conditions and over the present distressed state of the housing industry. The Committee is aware that some improvement in these conditions has occurred in recent months as interest rates have declined generally. However, the Committee believes that continuation of the present tax exemption for qualified mortgage bonds beyond 1983 is necessary both to enable more people to realize the goal of homeownership through availability of more affordable mortgage interest rates and to assist in achieving a full recovery of the housing industry.

Explanation of Provision

The Committee amendment makes permanent the tax exemption presently provided for interest on qualified mortgage bonds.

Effective Date

The Committee amendment is effective for bonds issued after December 31, 1983.

Revenue Effect

It is estimated that this provision will reduce fiscal year budget receipts by $0.1 billion in 1984, $0.2 billion in 1985, $0.5 billion in 1986, $0.8 billion in 1987, and $1.2 billion in 1988.

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