

COMPUTER EQUIPMENT CONTRIBUTION ACT OF 1982

OCTOBER 1 (legislative day, SEPTEMBER 8), 1982.—Ordered to be printed

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

R E P O R T

[To accompany H.R. 5573]

The Committee on Finance, to which was referred the bill (H.R. 5573) to amend the Internal Revenue Code of 1954 to encourage contributions of computer equipment to elementary and secondary schools, having considered the bill, reports favorably thereon with amendments to the text, and an amendment to the title, and recommends that the bill as amended do pass.

The amendments are shown in the text of the bill in *italic*.

I. SUMMARY**A. Charitable Contributions of Computer Equipment to Qualified Organizations*****Present law***

Under present law, a donor of appreciated ordinary-income property (property the sale of which would not give rise to long-term capital gain) generally may deduct only the amount of the donor's basis in the property, rather than the fair market value (Code sec. 170(e)). For example, a manufacturer which donates a product from its inventory generally may deduct only its cost for the item.

Explanation of provisions

The bill, as amended by the committee, provides a special deduction rule for certain corporate charitable contributions of newly manufactured computer equipment to elementary or secondary schools for use at the school, or to museums or libraries for use at the museum or library, directly in the education of elementary or secondary school-children. For any one computer company, only contributions made during a single taxable year beginning in 1983, in 1984, or in 1985 are eligible for the special rule.

Under the amended bill, the maximum deduction allowed for charitable contributions of qualifying computer equipment (as defined in the bill) will equal the taxpayer's basis in the donated item plus one-half of the difference between fair market value at the time of the contribution and basis, but not to exceed 150 percent of the taxpayer's basis.

To qualify for the special deduction rule, the contribution must be made pursuant to a written plan of the donor corporation under which there will not be undue concentrations of the donor's contributions of computer equipment from either a geographic standpoint or from the standpoint of the relative economic status of the students of the donees which receive contributions from the donor. Among other requirements, the contribution must be made within six months after substantial completion of construction of the donated equipment.

B. Bad Debt Deductions of Commercial Banks

The bill provides that the applicable percentage for the percentage of outstanding loans method of computing the bad debt deduction of commercial banks is 1.0 percent. The 1.0-percent rate will remain effective so long as the provisions requiring withholding on dividends and interest remain in effect. The provision is effective for taxable years beginning after 1982.

The House-passed bill (H.R. 5573) did not contain this provision.

II. EXPLANATION OF THE BILL

A. Charitable Contributions of Computer Equipment to Qualified Organization (sec. 102 of the bill and sec. 170(e) of the Code)

Present Law

General reduction rule

The amount of a charitable deduction otherwise allowable for donated property generally must be reduced by the amount of any ordinary income which the donor would have realized had the property been sold for its fair market value at the date of the contribution (Code sec. 170(e)). Thus, a donor of appreciated ordinary-income property (property the sale of which would not give rise to long-term capital gain) generally may deduct only the donor's basis in the property, rather than the fair market value. For example, a manufacturer which donates a product from its inventory generally may deduct only its cost for the item.

Special rule for certain corporate contributions

A different rule applies to charitable contributions by corporations of two types of ordinary-income property if donated to certain exempt organizations for specified purposes. The special rule applies to corporate donations of ordinary-income property to a charitable organization to be used solely for care of the needy, the ill, or infants (such as donations by the producer or manufacturer of food, clothing, or medical equipment), where such use is related to the donee's charitable functions (sec. 170(e)(3)). Also, the special rule applies to corporate donations of newly manufactured scientific equipment to a college or university to be used for research (or research training) in the United States in the physical or biological sciences (sec. 170(e)(4)).

In these cases, the corporate donor is allowed a deduction equal to the sum of its basis in the property plus one-half of the unrealized appreciation (i.e., the difference between fair market value and basis), but not in excess of twice the basis.

Reasons for Change

The committee believes that an additional incentive is desirable to encourage manufacturers to contribute computers, on a charitable basis, to schools, libraries, and museums for use at the donee institution directly in the education of elementary and secondary schoolchildren, so that young students will become trained in today's technology. Skill in using computers has become important as more and more jobs require computer literacy.

The desirability of making available computers to schoolchildren makes it appropriate to provide, for a limited time, a greater tax

incentive than in present law for charitable contributions of computers, manufactured by the donor corporation no more than six months before contribution, which the donee uses directly in the education of schoolchildren. However, the committee does not intend that the increased deduction will be available for transfer of computer equipment which are not charitable in nature, such as if intended to enlarge the market for the transferor's products or services.

Explanation of Provisions

Overview

The bill, as amended by the committee, provides a special deduction rule for certain corporate charitable contributions of newly manufactured computer equipment to elementary or secondary schools for use at the school, or to museums or libraries for use at the museum or library, directly in the education of elementary or secondary schoolchildren. For any one computer company, only contributions made during a single taxable year beginning in 1983, in 1984, or in 1985 are eligible for the special rule.

Requirements for favorable treatment

In order for the special deduction rule to apply, there must be a charitable contribution by a corporation¹ of tangible personal property which satisfies all of the following requirements.

1. Qualifying computer equipment

The donated property must be tangible personal property which is inventory (within the meaning of sec. 1221(1)) and must be computer equipment as defined in the bill. Also, the donated computer equipment must be assembled by the taxpayer, and the taxpayer must be regularly engaged in the business of assembling and selling equipment of the same kind as the donated property.

The bill defines computer equipment qualifying for the special deduction rule to mean—

(1) a data processor² which can be programmed in at least three standard computer languages, which has a random access memory with a capacity for at least 32,000 bytes (determined by reference to the donated computer equipment, without regard to additional random access memory capacity which could be achieved through use of additional equipment which is not donated), and which is (or can be) connected with a screen for visual display of the data;

(2) a display screen, a printer, or a disc drive, but only if such equipment is donated by the taxpayer for use in connection with such a data processor donated by the taxpayer; and

(3) any installation equipment for equipment, donated by the taxpayer, which is described in (1) or (2). The term installation equipment is limited to cables and display screen, printer, or cassette recorder "hook up" equipment such as modulators, interface boards, or interface cards.

¹ The special deduction rule does not apply in the case of a corporation which is a subchapter S corporation, as defined in sec. 1371(b); a personal holding company, as defined in sec. 542; or a service organization, as defined in sec. 414(m)(3).

² For purposes of this definition, the term data processor also means a keyboard (or similar input equipment) donated as part of a data processor as defined in the bill.

Intangible computer property and tangible property which is not expressly listed in the bill's definition of computer equipment does not qualify for the special deduction rules under the bill.

2. Eligible donees

The computer equipment must be donated to a qualified organization, defined by the bill to mean—

(1) an educational organization (within the meaning of sec. 170(b)(1)(A)(ii))³;

(2) an elementary or secondary school operated as an activity of at tax-exempt section 501(c)(3) organization (such as a church), provided that such school normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on; or

(3) a museum or library which is described in section 501(c)(3) and tax-exempt under section 501(a), which is operated by a governmental unit referred to in section 170(c)(1), or which is operated as an activity of an organization described in section 501(c)(3) and tax-exempt under section 501(a).

Also, the donee must be located in the United States.

3. Governing body

The contribution of computer equipment to an eligible donee must be made through the donee's governing body.

For example, where State law provides that a local school board or school district has the authority to accept and administer charitable gifts for public schools under the jurisdiction of the board or district, the contribution must be made through such governing body. In the case of a private school, the contribution must be made through the school's board of trustees or other governing body.

4. Time of contribution

The contribution must be made within six months after substantial completion of construction of the computer equipment. For any one donor corporation, only contributions made during a single taxable year of the corporation beginning after December 31, 1982, and before January 1, 1986, with respect to which the corporation elects to have the provisions of section 102 of the bill apply, are eligible for the special rule in the bill. The election is to be made at such time and in such manner as the Treasury Department prescribes by regulations.⁴

³ An educational organization is described in sec. 170(b)(1)(A)(ii) "if its primary function is the presentation of formal instruction and it normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. The term includes institutions such as primary, secondary, preparatory, or high-schools * * *" and includes both public and private schools (Reg. § 1.170A-9(b)(1)). Under the bill, a State-run public vocational or technical education school (if it qualifies as an educational organization within the meaning of sec. 170(b)(1)(A)(ii)) is an eligible donee if the school admits students who have not either graduated from high school or earned a high school equivalency certificate.

⁴ In the case of a controlled group of corporations (within the meaning of sec. 1563(a)), the applicable taxable year shall be the same for all members of the controlled group. Also, for purposes of the applicable taxable year rule, a corporation and another corporation which succeeds to a substantial portion of the assets of such corporation are treated as one taxpayer.

5. Limitation to new equipment

The original use of the donated computer equipment must be by the donee.

6. Schoolchild education use requirement

Substantially all (at least 80 percent) of the use of the donated computer equipment by the donee must be at the location of the donee and must be directly in the education of elementary and secondary schoolchildren.

7. Prohibition on donee sale

The donated computer equipment may not be transferred by the donee in exchange for money, other property, or services.

8. Written confirmation

The donor corporation must receive a written statement from the donee representing that the use and disposition of the donated computer equipment will be in accordance with the preceding two requirements.

9. Distributional requirements

All contributions by any one donor corporation must be made pursuant to a written plan of the donor under which there will not be undue concentrations of the donor's contributions of computer equipment from either a geographic standpoint or from the standpoint of the relative economic status of the students of the donees which receive contributions from the donor. These distributional requirements are intended to insure a widespread distribution of donated property which will benefit a wide cross-section of elementary and secondary schoolchildren.

A determination of whether a donor's contribution plan meets these distributional requirements is to be made on an overall basis, taking into account all the donees which receive contributions from the donor under the plan (not just certain of such donees). If, under a plan, contributions are made through one or more governing bodies which have authority to allocate contributed equipment to particular schools under the body's jurisdiction (e.g., as where a school district allocates donated computer equipment only to its high schools), then a determination of whether the plan meets the distributional requirement as to a relative economic status of students is to be made by taking into account the relative economic status of students of all schools within the jurisdiction of the governing body.

The committee intends that under the distributional requirements of the bill, not more than 15 percent of all contributions from any one donor corporation may be made to donees located in any one State; that no more than one-third of such contributions may be made to donees where the median family income of schoolchildren significantly exceeds the national average; and that at least one-third of such contributions must be made to donees where the median family income of schoolchildren is significantly below the national average. The Treasury Department may, however, vary these percentage rules in appropriate cases, based on the facts and circumstances of such cases.

Charitable contribution required

Court cases have held that if a transfer to a charitable organization results in a benefit to the donor, no charitable deduction is allowed. For example, the U.S. Court of Claims has upheld denial of charitable deductions claimed by a manufacturer for discounts on purchase of sewing machines by schools, where the court had found that the discounts were offered for the predominant purpose of enlarging the market for the manufacturer's brand of sewing machines (*Singer Co. v U.S.*, 449 F.2d 413 (Ct. Cl. 1971)). The committee does not intend that the adoption of section 102 of this bill be interpreted as classifying computer equipment contributions as charitable contributions without regard to the donor-benefit rules expressed in the *Singer* case. Instead, the committee intends that a determination of whether a particular contribution of computer equipment qualifies as a charitable contribution is to be made on the basis of the general rules for defining charitable contributions under present law, as also apply to contributions of other types of property. The committee intends also that, to qualify under the bill, the contribution must be made out of disinterested generosity and must be intended for charitable purposes, as contrasted to promotional or other business purposes.

Allowable deduction

If all the requirements of the bill are satisfied, the charitable deduction allowed by the bill for a charitable contribution of qualifying computer equipment generally is for the sum of (1) the taxpayer's basis in the property plus (2) one-half of the unrealized appreciation (i.e., one-half of the difference between the property's fair market value⁵ determined at the time of the contribution and the donor's basis in the property). However, in no event is a deduction allowed for any amount in excess of 150 percent of the donor's basis in the property.

Effective Date

The provisions of section 102 of the bill will apply to taxable years beginning after 1982.

Revenue Effect

The provisions of section 102 of the bill are estimated to reduce fiscal year budget receipts by \$14 million in 1983, \$23 million in 1984, \$17 million in 1985, \$8 million in 1986, and a negligible amount thereafter.

⁵ Where donated property is a type which the taxpayer sells in the course of its business, the fair market value is the price which the taxpayer would have received if the taxpayer had sold the contributed property in the usual market in which it customarily sells, at the time and place of the contribution, and, in the case of a contribution of goods in quantity, in the quantity contributed. The usual market of a manufacturer or other producer consists of the wholesalers or other distributors to or through whom it customarily sells; but if it sells only at retail, the usual market consists of its retail customers (Reg. § 170A-1(c)(2)).

B. Bad Debt Deductions of Commercial Banks (sec. 201 of the bill and sec. 585 of the Code)

Present Law

Commercial banks compute their bad debt deductions under either the experience method or the percentage of outstanding loans method (Code sec. 585). Under the Tax Reform Act of 1969, the percentage of outstanding loans method is phased out over an 18-year period. Under the phase-out schedule established under the 1969 Act, bad debt deductions generally are permitted to the extent necessary to increase the bad debt reserve to the following percentages of eligible outstanding loans: 1969 to 1975, 1.8 percent; 1976-1981, 1.2 percent; and 1982-1987, 0.6 percent. After 1987, the bad debt deduction of commercial banks is to be computed under the experience method.

Section 267 of the Economic Recovery Tax Act of 1981 (ERTA) provided that the applicable percentage under the percentage of outstanding loans method of computing bad debt deductions of commercial banks is 1.0 percent for taxable years beginning in 1982, instead of the 0.6 percent provided by the Tax Reform Act of 1969. For years after 1982 and before 1988, the applicable percentage will be 0.6 percent.

Reasons for Change

Because of the downturn in recent economic conditions, commercial banks may experience significantly more bad debts than the bad debt reserves computed under the experience method would provide. Consequently, the committee believes that it would be inappropriate at this time to continue the phaseout of the percentage of outstanding loans method of computing bad debt reserves for commercial banks. In addition, the committee recognizes that compliance with the withholding rules of the Tax Equity and Fiscal Responsibility Act of 1982 involves some costs for commercial banks. Under these circumstances, the committee concluded that the applicable percentage under the percentage of outstanding loans method should continue at 1.0 percent so long as the provisions requiring withholding on interest (enacted in subtitle A of title III of the Tax Equity and Fiscal Responsibility Act of 1982) are in effect.

Explanation of Provisions

The bill provides that the applicable percentage under the percentage of outstanding loans method of computing bad debt deductions of commercial banks shall be 1.0 percent.¹ The 1.0 percent rate is to be effective for each taxable year that the provisions of the Tax Equity

¹ The deduction computed under sec. 585 as amended by the bill (i.e., with the applicable percentage being 1.0 percent) is subject to the reductions provided by Code section 291 as added by the Tax Equity and Fiscal Responsibility Act of 1982.

and Fiscal Responsibility Act requiring withholding on interest and dividends are in effect and not significantly narrowed as of the end of that taxable year.² The base year will continue to be the last taxable year beginning before 1976.

Effective Date

The provisions of section 201 of the bill will be effective for taxable years beginning after 1982.

Revenue Effect

The provisions of section 201 of the bill are estimated to reduce fiscal year budget receipts as follows: \$20 million in 1983, \$53 million in 1984, \$71 million in 1985, \$78 million in 1986, and \$84 million in 1987.

²If the provisions requiring withholding on interest and dividends are repealed or significantly narrowed, the applicable percentage will revert to the phaseout of the percentage of outstanding loans method as provided by present law.

III. COSTS OF CARRYING OUT THE BILL AND VOTE OF THE COMMITTEE IN REPORTING THE BILL

Budget Effects

In compliance with paragraph 11(a) of Rule XXVI of the Standing Rules of the Senate, the following statement is made relative to the budget effects of H.R. 5573, as reported.

Budget receipts

The table below summarizes the estimates of the effects on budget receipts of the provisions of the bill for fiscal years 1983-1987:

[Fiscal years; millions of dollars]

Provision	1983	1984	1985	1986	1987
1. Charitable contributions of computer equipment----	-14	-23	-17	-8	(¹)
2. Bad debt deductions of commercial banks-----	-20	-53	-71	-78	-84
Total -----	-34	-76	-88	-86	-84

¹ Negligible revenue loss.

The Treasury Department agrees with this statement.

Budget outlays

The bill involves no budget outlays.

Vote of the Committee

In compliance with paragraph 7(c) of Rule XXVI of the Standing Rules of the Senate, the following statement is made relative to the vote by the committee on the motion to report the bill. H.R. 5573, as amended, was ordered favorably reported by voice vote.

IV. REGULATORY IMPACT OF THE BILL AND OTHER MATTERS TO BE DISCUSSED UNDER SENATE RULES

Regulatory Impact

Pursuant to paragraph 11(b) of Rule XXVI of the Standing Rules of the Senate, the committee makes the following statement concerning the regulatory impact that might be incurred in carrying out the provisions of H.R. 5573, as reported.

Numbers of individuals and businesses who would be regulated

The bill does not involve new or expanded regulation of individuals or businesses.

Economic impact of regulation on individuals, consumers, and business

Section 102 of the bill provides a special deduction rule for certain corporate charitable contributions of newly manufactured computer equipment to schools for use at the school, or to museums or libraries for use at the museum or library, directly in the education of elementary or secondary schoolchildren. Section 201 of the bill provides, in certain circumstances, that the applicable percentage under the percentage of outstanding loans method of computing bad debt deductions of commercial banks shall be 1.0 percent for taxable years beginning after 1982, rather than 0.6 percent as applicable under present law.

Impact on personal privacy

The bill does not relate to the personal privacy of individuals.

Determination of the amount of paperwork

The bill will involve little additional paperwork for taxpayers. To be eligible, for the special deduction rule in section 102 of the bill, qualifying contributions of computer equipment must be made pursuant to a written plan of the donor corporation meeting the distributional requirements of the bill.

Other Matters

Consultation with Congressional Budget Office on budget estimates

In accordance with section 403 of the Budget Act, the committee advises that the Director of the Congressional Budget Office has examined the committee's budget estimates of the tax provisions of the bill (as shown in Section III of this report) and agrees with the methodology used and the committee's budget estimates.

New budget authority

In compliance with section 308(a) (1) of the Budget Act, and after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by the bill involve no budget authority.

Tax expenditures

In compliance with section 308(a) (2) of the Budget Act with respect to tax expenditures, and after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by sections 102 and 201 of the bill involve increased tax expenditures. A statement as to the estimated effect on budget receipts of the provisions of the bill is set forth in section III of this report.

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

In the opinion of the committee, it is necessary, in order to expedite the business of the Senate, to dispense with the requirements of paragraph 12 of Rule XXVI of the Standing Rules of the Senate (relating to the showing of changes in existing law made by the provisions of H.R. 5573, as reported by the committee).

