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U. S. DEPARTMENT OF LABOR

OFFICE OF THE SECRETARY

WASHINGTON

SEP 30 1976

Honorable James T. Lynn
Director
Office of Management and Budget
Washington, D.C. 20503

Dear Mr. Lynn:

This is in response to your request for our views on an enrolled bill, H.R. 10612, the Tax Reform Act of 1976. This enrolled bill would affect the Department of Labor's activities in the following areas.

The tax laws currently provide a tax credit for employers who hire qualified recipients of aid to families with dependent children (AFDC) who participate in the work incentive program (WIN), which is jointly administered by this Department and HEW. Under the WIN tax credit, an employer may credit against taxes 20 percent of the first twelve months of wages paid such employees, up to the first $25,000 in taxes plus one-half the excess over that amount. Another tax credit provision, the Federal welfare recipient employment incentive tax credit (welfare recipient tax credit) similarly permits employers to credit against taxes wages to hired AFDC recipients, with the same upper limit of creditable taxes but with no time restriction on applicable wages. The welfare recipient tax credit expired on July 1, 1976.

Section 2107 of the Tax Reform Act would double the upper limit on creditable taxes for both these credit provisions. It would place a 12-month restriction on applicable wages under the welfare recipient tax credit, conforming it to the WIN tax credit. It would also eliminate the provision allowing for recapture of taxes payable in the absence of the WIN tax credit if the employees are laid off because of business decline. The bill extends the welfare recipient credit through 1979.

We believe that these provisions regarding the WIN and welfare recipient tax credits will encourage greater employer hiring of AFDC and welfare recipients, thus contributing to greater employment and reduced public dependency.

Section 2134 of the Tax Reform Act provides a financial impetus to prepaid legal service plans by excluding from employees' income the contributions made to such plans and the value of the services rendered under them. This exclusion is available only to group legal service plans that qualify under standards set forth in the Act. The qualification standards are generally similar to those in the Code for other types of plans; they forbid discrimination in favor of highly paid employees, limit the types of organizations that may receive contributions, and require that contributions be used for the exclusive benefit of employees, their spouses and dependents. The exclusion is made available for the years 1977 through 1981, and a joint Labor-Treasury report on the desirability and feasibility of continuing the exclusion is made due at the end of 1980. Written group legal services plans in existence on June 4, 1976, will be considered qualified automatically until the later of 180 days after enactment or, for collectively bargained plans, the termination date of the last of the collective bargaining agreements relating to the plan (not including post-enactment extensions, and in no event later than December 31, 1981).

In accordance with the Department's generally favorable view of prepaid legal services arrangements, we support the tax exclusion as an effective means to promote greater use of such plans.

Presently the Employee Retirement Income Security Act (ERISA) provides for a congressional Joint Pension Task Force to study and report on certain aspects of pension and tax law. Section 803 of this tax reform bill expands the task force's scope of inquiry to include employee stock ownership plans (ESOPs) and extends until March 31, 1978, the date for the final report.

We favor this provision, which will contribute to greater knowledge of the appropriate status of ESOPs under Federal law.

In section 803 of the Tax Reform Act, the Congress reaffirms its interest in encouraging employee stock ownership plans (ESOPs). The stated reasons are that such plans assist in making capital funds available and spread stock ownership to corporate employees.

ESOPs fall within the coverage of title I of the Employee Retirement Income Security Act of 1974 (ERISA). Along with other eligible individual account plans, they are subject to special treatment in some respects; e.g., section 407(d) (3)(A)(ii) and section 408(e)(3)(A) lift restrictions on acquisition and sale of employer securities for ESOPs, and they alone are the subject for a statutory exemption for loans to a plan by a party in interest. Except for such statutory discriminations, ESOPs are governed by the general rules prescribed in the statute for employee benefit plans. The Secretary of Labor, as administrator of title I, issues regulations dealing with all aspects of that title, including its application of ESOPs.

In interpreting ERISA and framing regulations under it, the Secretary takes into consideration the legislative history of the statute. To a lesser but significant extent, the Secretary also considers, in his ongoing administration of ERISA, related legislative acts such as the enactment of special provisions for ESOPs in the Tax Reduction Act of 1975. Where it is consistent with the aims and principles of ERISA, the Secretary endeavors to take administrative and regulatory positions that are in harmony with later-enacted legislation.

Specifically, the Secretary's participation in the joint Labor Department - Treasury Department regulations on ESOPs was influenced by the ESOP provisions of the Tax Reduction Act of 1975. An attempt was made to carry out the ERISA policy of protecting the interests of participants and beneficiaries in a manner which would not unduly hamper the operation of ESOPs. The further Congressional expression in the Tax Reform Act of 1976 confirms the Department's commitment to that administrative approach.

Section 803 of the Tax Reform Act states in general terms that the Congress is "deeply concerned" that regulations which treat ESOPs as retirement plans may impose restrictions that will hinder their success. The statement of the managers of the bill on section 803 greatly extends and particularizes the statement of concern. It expressly references proposed regulations issued on July 30, 1976 by the Department of Labor and the Department of the Treasury. After declaring that the regulations "may make it virtually impossible for ESOPs, and especially leveraged ESOPs, to be established and function effectively," the statement discusses 12 specific provisions of the regulations. Each is described and criticized, and the conferees offer substitutes more favorable to promotion of ESOPs.

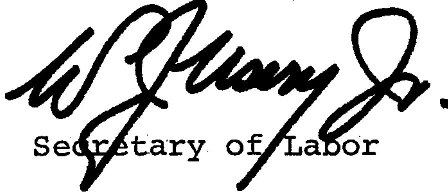
The matters discussed relate to prohibited transaction rules and other fiduciary standards of title I of the Act. The conference report accompanying ERISA (H. Rept. 93-1280, 93d Cong., 2d Sess.) points out that there are potential fiduciary problems inherent in the operation of ESOPs, and instructs the Labor and Treasury Departments to give "special scrutiny" to transactions subject to abuse. That Report, of course, represents the combined views of the labor committees, which have jurisdiction over title I of the Act, and the tax-finance committees with jurisdiction over the amendments to the Internal Revenue Code made by title II.

The statement of the manager on section 803 of the Tax Reform Act purports to convey a different expression of congressional intent on matters covered by the text and legislative history of ERISA, but it neither amends ERISA nor carries any evidence of consideration by the labor committees that have jurisdiction over title I of that Act. Plainly, then, it cannot be taken to amend the provisions of ERISA, and the weight to be given it as a guide in the interpretation of ERISA is debatable. In view of the history of ERISA, in which individual initiatives from the labor and tax committees were merged through a cooperative effort involving both, no partial commentary can, in our view, claim to be authoritative, particularly when it comes two full years after enactment of title I of ERISA, which is not amended in any regard by H.R. 10612.

The ESOP regulations are currently in proposed form, and the statements made in connection with the Tax Reform Act will, of course, be evaluated in arriving at final regulations. They cannot, however, override the Department's obligation in its administration of ERISA to honor the congressional mandates which appear in the text and legislative history of that Act.

The Department of Labor does not object to Presidential approval of the enrolled bill, H.R. 10612, the Tax Reform Act of 1976.

Sincerely,



Secretary of Labor

To - J. Johnston 9-30-76 4:45 p.m.

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

SEP 30 1976

MEMORANDUM FOR THE PRESIDENT

Subject: Enrolled Bill H.R. 10612 - Tax Reform Act of 1976
Sponsor - Rep. Ullman (D) Oregon

Last Day for Action

October 5, 1976 - Tuesday

Purpose

To improve income tax equity; to continue tax cuts provided in the Tax Reduction Act of 1975; to simplify certain tax provisions and delete unnecessary language; and to make "reforms" in the administration of the tax laws.

Agency Recommendations

Office of Management and Budget	Approval
Department of the Treasury	Approval
Department of Commerce	Approval
Department of Agriculture	Approval
Department of Defense	Approval
Department of Health, Education and Welfare	No objection
Department of Justice	No objection
Department of State	No objection
Department of Housing and Urban Development	No objection
Department of Labor	No objection (Informally)
Department of Transportation	No objection
Council of Economic Advisers	No objection
Federal Reserve Board	No objection (Informally)
Federal Home Loan Bank Board	No objection
Small Business Administration	No objection
Securities and Exchange Commission	No recommendation received

Discussion

H.R. 10612 makes extensive revisions in the United States Tax Code and continues the basic individual and corporate tax reductions enacted in 1975, making some of these reductions permanent. It substantially increases estate and gift tax exemptions and credits and generally provides more generous benefits for working parents needing child care and for the elderly. H.R. 10612 increases the minimum tax for individuals and corporations and tightens the treatment of tax shelters, capital gains, large interest deductions, and income earned abroad.

In other changes regarding foreign source income, the enrolled bill levies higher taxes on U.S. oil and gas companies operating abroad, taxes bribes immediately upon payment by U.S. companies to foreign officials, curtails existing tax deferral advantages conferred on DISC (Domestic International Sales Corporation) profits, and imposes tax penalties on U.S. companies which participate in the Arab boycott of Israel.

Domestically, certain major industries are given more liberal tax treatment through more generous loss offsets, higher investment credits, and more lenient amortization and depreciation rules. Such industries include life and mutual insurance, mutual funds, and airlines, railroads, and shipping.

Finally, the enrolled bill contains numerous provisions designed to simplify tax procedures, to delete unnecessary language from the Tax Code and otherwise to improve and clarify the administration of the tax laws.

Many of the provisions in H.R. 10612 reflect Administration initiatives or have been supported by the Administration. Others have been actively opposed. The attached table compares features of the enrolled bill with the Administration's tax proposals in terms of the size of tax cuts or increases and the associated revenue impact. The major or controversial provisions of H.R. 10612 are discussed in greater detail below.

INDIVIDUAL TAXPAYERS

Extension of 1975 Tax Reductions

H.R. 10612 makes permanent or extends the individual tax cuts enacted in 1975 and slightly expanded in 1976, including (1) the extra $35 tax credit (or, if greater, 2 percent of the first $9,000 of taxable income) a taxpayer may claim for each personal exemption; (2) the earned

income refundable tax credit for low income families with children which is pegged at 10 percent of the first $4,000 of earnings and phased out between $4-8,000; and (3) the higher minimum and maximum standard deductions, which are made permanent. Thus, the minimum standard deduction or low income allowance is fixed at $1,700 for single persons and $2,100 for couples filing joint returns. The percentage standard deduction is 16 percent of adjusted gross income with the maximum set at $2,400 for individuals and $2,800 for couples.

These reductions differ from your proposed deepened tax cuts which would have eliminated the $35 per exemption tax credit and earned income credit, but would have

— introduced a higher personal exemption ($1,000 versus the $750 current level)

— established a simplified standard deduction.

Tax Shelters

The bill strengthens the tax treatment of tax-shelter investments. Investors in oil and gas properties would be limited by the amount of their own capital "at risk" in deducting losses. A recapture provision is imposed when an oil or gas property is sold to prevent excess prior deductions for intangible drilling expenses from being used to convert ordinary income into capital-gains income. Real estate investors will be required to capitalize and amortize construction period interest and taxes. Phase-in rules include postponing any impact of this provision until 1981 for Government assisted low income housing projects. "At risk" limitations are also provided for farming, movie, and equipment leasing tax shelters.

These changes are not those preferred by the Administration as a means of correcting tax-shelter abuses, although they are roughly in accord with the Administration's objectives.

Minimum Tax

The bill significantly expands the "minimum tax" provision, which first entered the tax code in 1969. Under current law, a 10 percent tax is applied to the sum of an individual's or corporation's tax preferences less a $30,000 exemption and the taxpayer's regular income taxes.

The bill increases the rate of minimum tax on individuals from 10 to 15 percent and reduces the exemption to the greater of $10 thousand or one-half of regular income taxes. New preference items are added to the base of the minimum tax: a taxpayer's itemized deductions -- other than medical and casualty deductions -- in excess of 60 percent of adjusted gross income; intangible drilling costs for oil and gas in excess of deductions if costs were capitalized, and accelerated depreciation on all equipment leases.

The Administration opposed the concept of the minimum tax and had proposed a tax on "minimum taxable income" and the concept of Limitations on Artificial Losses (LAL) as a means of assuring greater tax equity and reducing the use of tax preferences rather than taxing the excessive use of preferences in the aggregate.

Estate and Gift Taxes

H.R. 10612 provides the first major reform of estate and gift taxes since 1941 by increasing substantially the amount the taxpayer may bequeath tax free. Currently, the estate tax exemption is $60,000 with a $30,000 exemption for lifetime gifts. The enrolled bill combines the estate and gift tax exemptions and converts them into a single tax credit. The new unified credit will be equivalent to a $120,000 exemption in 1977 and to a $175,000 exemption after 5 years.

H.R. 10612 increases the marital deduction for transfer between spouses by raising the estate tax deduction to the greater of $250,000 or half the estate. It also provides an unlimited marital deduction for the first $100,000 of lifetime transfers, no deduction for gifts between $100,000 and $200,000 and a 50 percent deduction for larger gifts. Current law provides that up to half an estate can be left to a spouse without tax and that half the value of lifetime gifts between husband and wife are tax free.

To encourage heirs to maintain and operate family firms or closely held businesses, a special valuation based on "current" rather than "highest and best" use is made available, provided the estate's value is not thereby reduced by more than $500,000 and provided the property is held at least 15 years. Such estates are also granted up to 15 years (instead of the current 10 years) to pay the estate tax, and the interest rate on the unpaid balance (up to $1 million) is lowered from the current 7 percent to 4 percent. Any estate may be granted a 10-year extension on its estate tax payment upon a showing of "reasonable cause" instead of the current requirement of "undue hardship."

The enrolled bill tightens the tax treatment of inherited capital assets. Under current law the basis of the inherited property is set at the property's fair market value, no matter how much the value has increased since the asset was purchased. Thus, the heir often begins with a higher basis which reduces his subsequent capital gains tax if he ever sells. H.R. 10612 establishes, beginning December 31, 1976, a minimum basis of $60,000 per estate, and requires that an heir's basis would be computed as the greater of 1) the value of the property on December 31, 1976, 2) the heir's share of the $60,000 minimum basis or 3) the original purchase price.

Finally, the enrolled bill requires that newly created "generation skipping trusts" be taxed but excludes up to $250,000 for transfers to each grandchild.

Retirement Income Credit

H.R. 10612 simplifies and makes more generous the existing 15 percent retirement income credit applicable to persons 65 and over. This provision allows earned income to be eligible for the credit instead of just pensions and other retirement-related income, and thus would aid retired persons with some income -- from any source -- and low social security benefits. The maximum amount on which the credit may be computed is raised for single persons (from $1,524 to $2,500), for couples filing joint returns with only one spouse 65 or older (from $2,286 to $2,500) and for joint returns where both spouses are 65 and older (from $3,048 to $3,750).

In addition, the provision of current law which reduces the retirement income credit by an amount equal to half the taxpayer's earned income between $1,200 and $1,700 and by all earnings above $1,700, is repealed. The new credit phases out for single persons with income above $7,500 and for married persons with income above $10,000.

Child Care

H.R. 10612 converts the existing itemized deduction for child care expenses to a 20 percent credit for child care costs and sets a maximum credit of $400 for one child and $800 for two or more children. Since the credit is subtracted directly from taxes owed, the benefit can be enjoyed by those who use the standard deduction and hence are more likely to be in the lower income bracket.

However, unlike current law which phases out the deduction at an income level above $35,000 and requires that both husband and wife work full-time, the enrolled bill removes the income limit and extends the tax break to couples where one spouse works part-time, or is a full-time student, and to divorced or separated parents having custody of a child. In addition, while existing law precludes the deductibility of payments to relatives for child care, the bill contains a "grandma" clause which makes payments to relatives eligible for the credit.

The Administration has supported the concept of a tax credit for child care costs as a move toward simplification, although it has expressed opposition to removal of the income ceiling.

Sick Pay Repeal

The bill repeals the provision in current law permitting an employee to exclude up to $100 of weekly pay from income during extended sick leave. An exclusion of up to $5,200 a year is provided for retired persons under age 65 who are permanently and totally disabled; however, there is a dollar-for-dollar reduction in the value of this exclusion for persons with incomes in excess of $15,000.

Capital Gains and Losses

H.R. 10612 increases the duration for holding an asset in order to qualify for long term capital gains treatment from 6 to 9 months in 1977 and to 12 months thereafter; however, for farm commodity futures contracts the 6-month period will continue. To offset this more restrictive capital gains treatment, the allowable deduction of capital losses from ordinary income will rise from $1,000 to $2,000 in 1977 and to $3,000 in 1978 and thereafter.

CORPORATIONS

Extension of 1975 Tax Reductions

The enrolled bill continues through 1977 the corporate tax rate reductions and increased surtax exemption which were enacted by the 1975 Tax Reduction Act. The 10 percent investment tax credit is extended to 1980 and liberalized to allow businesses to offset current income with unused credits from prior years instead of first using current year credits as required under existing law.

H.R. 10612 likewise extends to 1980 the one percent bonus enacted last year on top of the 10 percent investment credit for companies contributing an amount equal to the extra point to establish an Employee Stock Ownership Plan (ESOP). A further one-half percent bonus has been added in the bill for companies whose employees match the additional one-half percent tax credit.

The Administration has opposed since its enactment the 1 percent investment credit bonus for companies adopting an ESOP. The bonus simply results in 100 percent financing of ESOP's with tax dollars, with no benefits accruing to the tax paying public which ultimately puts up the funds. The preferred approach to greater stock ownership by low and middle income Americans — unfortunately ignored by the Congress — was your Broadened Stock Ownership Proposal (BSOP), which did not limit participation to specially situated individuals.

Minimum Tax

Along with raising the minimum tax on individuals, the bill increases the minimum tax on corporations from 10 to 15 percent of preference income. Current law reduces the base of the corporate minimum tax by the greater of $30,000 or regular taxes paid. The bill reduces the $30,000 exemption to $10,000. No new tax preference items are added to the base of the minimum tax for corporations.

In applying the new minimum tax provisions, preferential treatment is given to banks and savings and loan institutions and timber companies, which will effectively escape the minimum tax increase.

Offsetting Losses

H.R. 10612 permits most businesses to carry forward losses an additional 2 years to offset against income. Under current law companies may generally carry back losses for 3 years and any remaining losses forward for 5 years; regulated transportation businesses are permitted a 3-year carryback and 7-year carryforward benefit. Henceforth, most companies will be permitted a 3-year carryback and 7-year carryforward rule and regulated industries (transportation firms) will have 3 years back and 9 years forward. Alternatively, to avoid possible loss of investment tax credits and foreign tax credits a business may, for any one year, elect to carry operating losses forward only instead of first carrying them backward.

Beginning in 1978, the rules are tightened on acquisition of unprofitable firms by companies in search of losses to offset their profits. As a special benefit to life and other mutual insurance companies, however, the prohibition in current law is lifted on using the losses of nonlife insurance affiliates to offset parent company income, but this benefit will not begin for 5 years and is phased in over a 3-year period thereafter.

FOREIGN INCOME

Reduction in DISC Benefits

The enrolled bill reduces by about one-third existing benefits which permit companies to defer taxes on up to 50 percent of export profits of a Domestic International Sales Corporation (DISC). The new measure limits the DISC benefit to exports in excess of 67 percent of the annual average for the base period 1972 through 1975. After 1979, this base period will be moved forward one year at a time. Moreover, military exports will qualify for only half the regular DISC benefit.

The Administration has consistently opposed any cutback in DISC benefits, arguing that the full benefit is needed to encourage U.S. exports.

International Boycott

H.R. 10612 denies tax benefits to U.S. companies which participate in the Arab boycott of Israel. Boycott participants will lose those portions of their foreign tax credits, deferral of taxes on overseas earnings, and DISC benefits related to the boycott, but will be permitted to continue to enjoy tax benefits attributed to demonstrated nonboycott activities in boycott countries. A company will be deemed to participate in an international boycott if it agreed to

-- refrain from hiring employees on the basis of nationality, religion, or race.

-- refuse to do business with a specified country (i.e., "secondary" boycott).

-- refuse to do business with other countries which do business with a specified country (i.e., "tertiary" boycott).

ship products only by carriers not on an international boycott list.

This feature of the bill has been strongly opposed by Administration officials as an inappropriate remedy to the boycott problem, and one which will create severe foreign policy difficulties in attempting to enforce it. While the language in the enrolled bill is less punitive than proposed in the Senate version and may, therefore, permit more lenient administration of the measure, the provisions will, as Secretary Simon has noted, "penalize many business transactions in the Arab world unless the Arabs modify the boycott."

Other Provisions

The enrolled bill substantially revises existing law and adds new measures governing the taxation of income earned abroad by Americans. These changes include

— a reduction of the exclusion taxpayers receive on income earned abroad from $20,000, or in some cases $25,000, to $15,000.

— repeal of the option allowing companies to compute credit for payment of foreign taxes on a country-by-country basis. Henceforth, except for companies doing business in U.S. possessions and certain mining companies doing business abroad which may continue to use the per-country option for three more years, corporations will have to compute their credit for payment of foreign taxes on an overall basis, rather than per-country basis. Moreover, foreign losses that reduce U.S. taxes in one year will hereafter be subject to "recapture" in later years as the operation becomes profitable, thereby reducing allowable foreign tax credits.

— a cut back to 48 percent from 50 percent in the allowance for foreign taxes used to offset U.S. taxes payable on foreign oil and gas extraction income.

— removal of tax deferral benefits for foreign bribes paid by U.S. corporations. Companies that pay bribes to foreign officials will be subject to an immediate tax on the amount of the bribe and will no longer be permitted to defer tax on such payments.

The Administration generally supported these changes.

MISCELLANEOUS

In a number of areas the enrolled bill tightens tax exemptions, withholding rules, credits, and deductions to discourage further tax abuses or to close certain tax "loopholes". Important provisions in this category

— tighten restrictions on deductions for rent, utility bills, and other expenses attributed to an office at home. Deductions are allowed only when part of the home is used exclusively and regularly as the taxpayer's principal place of business or for meeting clients, patients, or customers in the normal course of business. Deductions may not exceed the amount of income earned by the business conducted at home.

— permit business and professional persons to deduct expenses for no more than two foreign conventions attended per year and limit deductions for meals, hotels, and other expenses to the applicable foreign per diem allowance given to U.S. government employees. Current law generally does not limit deductible expenses or the number of foreign conventions which may be attended.

— reduce the maximum annual deduction for interest payments on investment debts from a total of $25,000, plus net investment income, long-term capital gain, and half of any investment interest exceeding these amounts, to a total of $10,000 plus net investment income.

— disallow business deductions in excess of rental income for a vacation home rented out to others if the taxpayer uses it for personal purposes for more than two weeks or 10 percent of the days it was rented out. If the vacation home is rented out for less than 15 days per year, no income need be reported, but no business deductions may be claimed.

— require immediate tax withholding of 20 percent of race track winnings of more than $1000, of state lottery payoffs over $5000, and of any other gambling winnings over $1000 where the odds are at least 300 to one. Winnings from slot machines, kino, and bingo are exempted from this withholding requirement.

— change the treatment of qualified stock options issued to key corporate personnel by valuing such options as ordinary income rather than capital gains income. If the fair value cannot be determined at the time of issuance, the increase in the stock's price over the option price will be taxed as ordinary income when the option is exercised.

— broaden the prohibition on the tax-free transfer of appreciated property to exchange or swap funds established as partnerships and trusts. Current law already forbids tax-free transfers to exchange funds set up as corporations.

H.R. 10612 also liberalizes other tax provisions. Some of these new or expanded "tax breaks"

— change the existing deduction for alimony payments from an itemized deduction to a deduction from gross income — a so-called "above-the-line deduction — thus making it available to taxpayers who use the standard deduction.

— make permanent the current tax exemption (which was due to expire on December 31, 1976) for the interest foreign individuals and corporations receive on their U.S. bank deposits.

— provide for the tax-free treatment of the premiums and services of employee group prepaid legal insurance, thus placing group legal insurance on the same footing as group medical insurance.

— increase the deduction for moving expenses from $2,500 to $3,000, including house-hunting and house-selling, and decrease the minimum distance one must move to qualify for the deduction from 50 to 35 miles.

— encourage the acquisition and rehabilitation of certified, historic structures by permitting faster depreciation than at present while denying tax advantages to those who demolish such buildings.

— increase from $20,000 to $35,000 the exclusion for capital gains on the sale of a house by a taxpayer over 65.

The enrolled bill contains a number of technical provisions dealing with tax simplification and administrative reform. Inter alia these provisions

— establish additional rules for the disclosure of tax returns and return information and for public inspection of Internal Revenue Service private letter rulings after November 1, 1976.

— permit State and local governments to use Social Security account numbers for identifying individuals in administering the tax, welfare, motor vehicle and driver licensing laws.

— mandate federal withholding of State income taxes for members of the military, and withholding of State and local income taxes from the pay of National Guard and Reserve personnel.

— provide simplified tables for taxpayer use in computing tax liabilities.

AGENCY VIEWS

Included below are the views of those agencies which have strong reservations about specific provisions of H.R. 10612 although, on balance, no agency recommends withholding approval of the bill.

HEW

The Department does not object to approval of H.R. 10612, although it soon intends to submit for legislative clearance proposals to correct problems perceived with two provisions in the bill.

HEW believes that section 1202(a), which prohibits the disclosure to Federal agencies of tax returns and return information except as specifically authorized, will adversely affect ongoing statistical and research efforts of the Social Security Administration and the National Institute for Occupational Safety and Health. HEW also fears that this provision would probably preclude the disclosure of taxpayer mailing addresses to the Office of Education for its collection activities in connection with defaulted student loans.

In addition, the Department, in its views letter, objects to section 1207(e) which would exempt withholding of social security taxes from fishermen employed on boats with ten-man crews or less who receive their pay as part of the catch. The Department asserts that this provision raises questions about the status of these fishermen (i.e., are they self-employed or employees of others), is disadvantageous to them (they may be subject to social security contributions at the higher self-employment rate) and would result in a revenue loss to the social security trust fund.

Justice

Although expressing serious reservations about sections 1202 and 1205 of H.R. 10612, Justice declines to make a recommendation on whether the bill should be approved and defers instead to the Treasury Department.

Like HEW, Justice is concerned about section 1202's restrictions on making tax information available to other federal agencies. These restrictions will, in Justice's view, "seriously impede the unraveling of white-collar, official corruption and organized crime cases and will increase the difficulty of bringing narcotics traffickers to justice."

Section 1205 is viewed as having an equally adverse effect on law enforcement and tax administration efforts. This section permits a taxpayer to seek an injunction in the courts to block a subpoena of the records of third parties even though the taxpayer has no legally protectable interest in such records. In Justice's view, income tax investigations of organized crime and white-collar crime will be impeded because many third party records "would be available only after extended litigation..." and not until the statute of limitations on prosecuting such crimes has taken effect.

Federal Home Loan Bank Board

On the overall desirability of the proposed legislation, the Bank Board defers to other agencies more directly affected. However, the Board characterizes Section 301, relating to the minimum tax increase and tightened preference income deduction rules, as unwise. The Board believes that the increased tax liability of savings and loan institutions imposed by this Section will (1) lessen the incentive for such institutions to maintain a high percentage of assets in residential mortgage loans, (2) decrease after-tax income and retained earnings, thus making it difficult for thrift institutions to sustain growth while remaining in compliance with federal insurance reserve and net worth requirements, and (3) tend to push up home mortgage loan rates because of the larger tax "bite" on income. The Board concludes its views by urging that "changes in the tax liability of financial institutions be given special consideration apart from the general question of corporate income taxes."

Defense

While expressing reservations over two provisions in H.R. 10612, on balance Defense recommends approval of the bill.

The Department's concern with the first provision -- repeal of the exclusion from gross income of non-combat related disability payments for members of the armed forces who enter on duty after September 24, 1975 -- is based on the different tax treatment that will be accorded to members who may be similarly situated but have different entrance on duty dates. However, Defense defers to the judgment of Congress on this issue.

The second provision -- requiring the withholding of State and District of Columbia taxes of military personnel -- is viewed as creating a considerable administrative burden in its implementation. Accordingly, Defense intends to seek agreement with Treasury on the respective responsibilities and liabilities of each department in complying with this provision.

State

The Department strongly objects to two measures in the enrolled bill: the antiboycott provision and the provision dealing with voting procedures in the International Trade Commission (ITC). The boycott provision and the Administration's strong opposition to it have been discussed earlier in this memorandum.

The ITC voting procedures provision requires that, in the event the six Commissioners voting on a question of import injury are equally divided and the President declines to accept the views of either group, then the Congress can, by concurrent resolution, designate the views of either group of Commissioners as the ITC determination. A similar, though not identical, change applies to recommendations for remedy after injury has been found to exist.

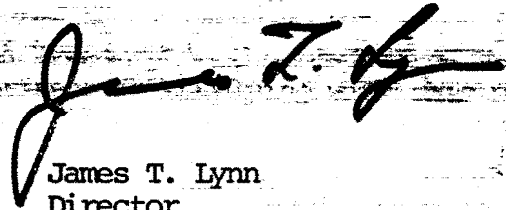
Under current law, the President's determination on import relief cases can be overridden by concurrent resolution only if his determination differs from the determination of an absolute majority of the Commission.

Similar provisions for Congressional override of Executive branch determinations are contained in other bills being considered by this Congress. Such instances of legislative encroachment on Executive perogatives are, in our view, unconstitutional and inconsistent with the principle of separation of powers, and should normally be opposed. In the present case, however, the effect of this new provision is to expand congressional veto power already embodied in the Trade Act of 1974. Accordingly, and especially in view of the overall desirability of H.R. 10612, we do not believe this provision warrants disapproval.

RECOMMENDATION

We agree with Treasury that, while the enrolled bill has certain undesirable features, it "is meritorious" and should be approved. The specific problems raised by several agencies which are described briefly above are not serious enough to warrant disapproval; and some problems can be overcome through future legislative amendments.

We are working with White House staff on a signing statement for your consideration which will be submitted separately.



James T. Lynn
Director

Enclosures

Revenue Impact

of

Administration Tax Proposals
compared with
H.R. 10612
(in billions of dollars)

	1977	1978	1979	1980	1981
I. Administration Proposals					
Tax Reductions (as estimated in the Mid-session Review of the 1977 Budget, July 16, 1976)	-24.8	-32.6	-34.6	-36.7	-38.9
Tax Reform					
Minimum taxable income	.4	.5	.5	.6	.6
Capital gains	.1	- .6	- .9	- 1.1	- 1.2
Home insulation credit	- .3	- .3	- .3	—	—
Sick pay and disability	.3	.3	.4	.4	.4
Repeal 30% foreign withholding	- .2	- .4	- .4	- .4	- .5
Retirement	- .3	- .3	- .3	- .3	- .3
Other income tax changes	- .1	- .1	.1	.2	.2
Subtotal-individual and corporate income tax	*	- .8	- .8	- .6	- .6
Estate and gift tax	- .1	- 1.1	- 1.5	- 2.0	- 2.5
Total	- .1	- 1.9	- 2.3	- 2.6	- 3.2
Grand Total	-24.9	-34.5	-36.9	-39.3	-42.1
II. H.R. 10612					
Extension of Tax Cuts (including outlay portion of the earned income credit)	-17.3	-13.8	- 8.0	- 8.3	- 7.2
Tax Reform					
Tax shelters	.4	.4	.5	.5	.5
Minimum and maximum tax	1.1	1.3	1.5	1.6	1.8
Tax simplification	- .4	- .4	- .5	- .5	- .5
Business-related individual income tax provisions	.2	.2	.3	.3	.3
Changes in the treatment of foreign income	.2	.1	.2	.2	.2
Amendments affecting DISC	.5	.6	.6	.6	.7
Other income tax changes	- .3	- .4	- .5	- .6	- .6
Subtotal-individual and corporate tax	1.6	1.7	2.0	2.1	2.5
Estate and gift tax	--	- .7	- .9	- 1.1	- 1.4
Total	1.6	1.0	1.1	1.1	1.0
Grand Total	-15.7	-12.8	- 6.9	- 7.2	- 6.2

*Less than $50 million
Note: Detail may not add to total due to rounding