The original documents are located in Box 36, folder "12/23/75 HR9968 Revenue Adjustment Act of 1975" of the White House Records Office: Legislation Case Files at the Gerald R. Ford Presidential Library.

APPROVED
DEC 23 1975

THE WHITE HOUSE

WASHINGTON

December 22, 1975

Posted in Colorado 12/23

MR PRESIDENT:

J. Archive 12/24

Attached for your consideration is H.R. 9968, the revised tax bill passed by the Congress after your veto of the earlier bill.

Because of your announced intention to sign the bill, the usual enrolled bill memorandum has not been prepared.

Jim Connor

94TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
1st Session } { No. 94-531

TAX EXEMPT STATUS OF OBLIGATIONS USED TO PROVIDE CERTAIN IRRIGATION FACILITIES

OCTOBER 3, 1975.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ULLMAN, from the Committee on Ways and Means, submitted the following

REPORT

[To accompany H.R. 9968]

The Committee on Ways and Means, to whom was referred the bill (H.R. 9968) to amend section 103 of the Internal Revenue Code of 1954 with respect to certain obligations used to provide irrigation facilities, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

I. SUMMARY

The bill, H.R. 9968, deals with the tax-exempt status of obligations the proceeds of which are to be used to reconstruct the American Falls Dam in Idaho. The dam is used for irrigation purposes but the water also has a subordinate use in generating electric energy. Under present law, an industrial development bond whose proceeds are used to build a dam that stores water for irrigation purposes may be eligible for tax-exempt status. However, in this case where the water has a subordinate use in generating electric energy, the eligibility of the bond issue for tax-exempt status is uncertain.

The American Falls Dam is under the supervision of the Bureau of Reclamation of the Department of Interior and has been restricted to two-thirds of its capacity because of certain structural defects. The Federal Government might well eventually appropriate the funds to reconstruct the dam. However, the American Falls Reservoir District is undertaking the reconstruction project now in order to make the dam fully operational. In addition, the Idaho Power Company is assisting the financing of the project and is to use the water for electric energy generation. It is the interrelationships of the use of the dam for furnishing water for irrigation purposes and the use of the water for electric energy that raises questions with the interpretation of the present exceptions to industrial development bond treatment. In view of

the special circumstances in this case, your committee believes it is appropriate to except the obligations for the reconstruction of the American Falls Dam from industrial development bond treatment which would allow these obligations to receive tax-exempt status.

Present Law

Present law provides that interest on obligations of State and local governments generally is exempt from Federal income tax. In 1968 tax-exempt status was withdrawn from industrial development bonds which State and local governments were using to finance and attract private industrial development within their jurisdictions.

Industrial development bonds are generally considered to be State or local obligations, a major portion of the proceeds of which are to be used in, and repaid by, a taxable trade or business. Such bonds are normally issued to acquire a facility for private business in which the beneficial ownership of the facility remains in the private trade or business, although (in order to secure repayment of the bonds) legal title normally remains with the State or local unit issuing the obligations.

When the industrial development bond limitation was enacted, exceptions were provided for certain small issues (sec. 103(c)(6)) and for certain specified public activities (sec. 103(c)(4)) in which cases tax-exempt status was continued. As initially enacted, one of the public activities for which an exemption was provided (sec. 103(c)(4)(E)) was "sewage or solid waste disposal facilities or facilities for the local furnishing of electric energy, gas or water."

In 1971, Congress amended the exception in subparagraph (E) to delete "water" and added the present law subparagraph (G) which extends the exception to "facilities for the furnishing of water, if available on reasonable demand to members of the general public."

As a result, in those cases where obligations are issued for facilities for the furnishing of water which meet the exception (under sec. 103(c)(4)(G)) but where the water is also used to generate electricity, it is uncertain as to whether the obligations would qualify for exempt status unless the use of the electric energy meets the "local" furnishing test (under sec. 103(c)(4)(E)), which has been interpreted to cover an area of two contiguous counties.

Reasons for the Bill

The American Falls Reservoir District applied to the Internal Revenue Service in June 1974 for a ruling that bonds to be issued to finance the replacement and rehabilitation of the American Falls Dam would qualify as a tax-exempt issue under section 103(c)(4)(G). The Internal Revenue Service, however, had questions of interpretation with respect to the interrelationship of the exceptions for facilities for furnishing of water and the local furnishing of electric energy and their application to the specific facts of this case. The committee reviewed the facts involved, as described below, and believed it is appropriate to specifically except the bond issue in this case as a result of the special circumstances.

The original American Falls dam was constructed in 1927 by the Bureau of Reclamation. The dam was restricted to two-thirds of its

1.7 million acre foot capacity in 1972 by the Bureau of Reclamation of the Department of the Interior for safety reasons because of excessive pressures on the dam which were caused by an alkali-aggregate reaction and deterioration in the concrete.

Legislation was enacted on December 28, 1973, to permit replacement and rehabilitation of the American Falls dam by the American Falls Reservoir District, which is a political subdivision of the State of Idaho. Replacement of the existing dam by the American Falls Reservoir District is an action to be taken in lieu of waiting for a Federal appropriation that would enable the Bureau of Reclamation to build the replacement dam.

The Act of December 28, 1973, also provides that upon completion of construction the United States shall take title to the dam as a feature of the Minidoka Project, located in the upper Snake River basin, Idaho.

As the constructing agent, the American Falls Reservoir District was authorized to contract with an electric utility for the use of the falling water at the dam for hydroelectric power generation. Revenues from such a contract will help defer the costs of constructing the dam. Prior to the adoption of the Act of December 28, 1973, the Idaho Power Company, which is a spaceholder in the reservoir and which owns and operates a powerplant below the existing dam, expressed interest in the execution of a falling water contract. Subsequent to the adoption of the Act, the District, as the constructing agency, entered into negotiations with the Secretary of the Interior, the Idaho Power Company and the other water users for the preparation of various contracts including a contract for the use of falling water.

It was intended that in normal circumstances, substantially all of the falling water would be made available to the Power Company only when water was released from the dam for irrigation purposes. There has been no intention to release water specifically for use by the Idaho Power Company to generate electricity, except for 45,000 acre-feet (2.65 percent of the storage capacity) whose release the power company can schedule for the purpose of generating electric energy. Thus, the use of water for electric energy would be subordinated to the use of the water for irrigation.

Although the Federal Government might well eventually completely finance the reconstruction of the American Falls Dam, the American Falls Reservoir District is undertaking the reconstruction now in order to make the dam fully operational for the spaceholders (rather than the present restricted two-thirds capacity). If it were not for the use of the water by the Idaho Power Company for hydroelectric power generation, any bonds issued by the Reservoir District would presently qualify for tax-exempt status. In this case the Idaho Power Company has a limited spaceholder right (under 3 percent) and is financing a large portion of the debt to assist the reconstruction of the dam and has use of the falling water for its hydroelectric power generation purposes. In addition, since the dam is to be turned over the the Federal Government after its reconstruction for ownership and operation, in effect, this financing can ve viewed as saving the Federal Government the expenditure it would have had to make to reconstruct the dam several years in the future. In view of these special circumstances, your committee believes it is appropriate to extend tax-exempt status to the bonds to be issued to finance the reconstruction of the dam.

Explanation of the Bill

Your committee's bill adds a new exception to industrial development bond treatment to specifically allow tax-exempt status for the bonds issued to reconstruct the American Falls Dam. This exception is to apply to obligations for a dam which furnishes water for irrigation purposes which has a subordinate use in connection with the generation of electric energy by water if substantially all of the stored water is contractually available for release from the dam for irrigation purposes and if the water released is available on reasonable demand for members of the general public.

The committee intends that subordinate use of water for generating electric energy means that less than 10 percent of the normal supply of stored water may contractually be scheduled for release by the power company and used for generating electric energy. "Normal" refers to conditions that generally prevail in the service area of this reservoir, and it is recognized that unusually wet or dry weather can cause a significant distortion in the 2.65 percent of water contractually scheduled for release to be used for generating electric energy. The committee intends that such unusual circumstances not be guiding in determining the subordinate use of water. In addition, "normal" use does not include a temporary increase in water released for the power company following contractual default by a spaceholder and his water share being made available to other spaceholders under the terms of the contract for the construction and operation of the dam and its facilities.

Thus, the provision applies the requirements of subsection (c)(4)(G) where substantially all of the stored water (under normal weather and climatic conditions) is available for release to be used for irrigation in the American Falls Reservoir District. The requirement that the released water be available on reasonable demand to members of the general public is retained in the new subsection (e). The committee understands that the American Falls project conforms with this requirement.

Your committee's bill is to apply to obligations issued after the date of the enactment of this Act.

IV. Effect on the Revenues of the Bill and Vote of the Committee in Reporting the Bill

In compliance with clause 7 of Rule XIII of the Rules of the House of Representatives, the following statement is made relative to the effect on the revenues of this bill. Your committee believes that the changes made by this bill will result in an annual revenue loss of about $1 million in each of the five fiscal years following the current fiscal year. No revenue loss is expected in the current fiscal year. The Treasury Department agrees with this statement.

In compliance with clause 2(l)(2)(B) of Rule XI of the Rules of the House of Representatives, the following statement is made relative to the vote by the committee on the motion to report the bill. The bill was ordered reported by a unanimous voice vote.

V. Changes in Existing Law Made by the Bill, as Reported

In compliance with clause 3 of Rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE CODE OF 1954

* * * * * * *

Chapter 1—Normal Taxes and Surtaxes

* * * * * * *

Subchapter B—Computation of Taxable Income

* * * * * * *

Part III—Items Specifically Excluded From Gross Income

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Sec. 103. Interest on Certain Governmental Obligations.

(a) General Rule.—Gross income does not include interest on—

(1) the obligations of a State, a Territory, or a possession of the United States, or any political subdivision of any of the foregoing, or of the District of Columbia;

(2) the obligations of the United States; or

(3) the obligations of a corporation organized under Act of Congress, if such corporation is an instrumentality of the United States and if under the respective Acts authorizing the issue of the obligations the interest is wholly exempt from the taxes imposed by this subtitle.

(b) Exception.—Subsection (a)(2) shall not apply to interest on obligations of the United States issued after September 1, 1917 (other than postal savings certificates of deposit, to the extent they represent deposits made before March 1, 1941), unless under the respective Acts authorizing the issuance thereof such interest is wholly exempt from the taxes imposed by this subtitle.

(c) Industrial Development Bonds.—

(1) Subsection (a)(1) not to apply.—Except as otherwise provided in this subsection, any industrial development bond shall be treated as an obligation not described in subsection (a)(1).

(2) Industrial development bond.—For purposes of this subsection, the term "industrial development bond" means any obligation—

(A) which is issued as part of an issue all or a major portion of the proceeds of which are to be used directly or indirectly in any trade or business carried on by any person who is not an exempt person (within the meaning of paragraph (3)), and

(B) the payment of the principal or interest on which (under the terms of such obligation or any underlying arrangement) is, in whole or in major part—

(i) secured by any interest in property used or to be used in a trade or business or in payments in respect of such property, or

(ii) to be derived from payments in respect of property, or borrowed money, used or to be used in a trade or business.

(3) EXEMPT PERSON.—For purposes of paragraph (2)(A), the term "exempt person" means—

(A) a governmental unit, or

(B) an organization described in section 501(c)(3) and exempt from tax under section 501(a) (but only with respect to a trade or business carried on by such organization which is not an unrelated trade or business, determined by applying section 513(a) to such organization).

(4) CERTAIN EXEMPT ACTIVITIES.—Paragraph (1) shall not apply to any obligation which is issued as part of an issue substantially all of the proceeds of which are to be used to provide—

(A) residential real property for family units,

(B) sports facilities,

(C) convention or trade show facilities,

(D) airports, docks, wharves, mass commuting facilities, parking facilities, or storage or training facilities directly related to any of the foregoing,

(E) sewage or solid waste disposal facilities or facilities for the local furnishing of electric energy or gas,

(F) air or water pollution control facilities, or

(G) facilities for the furnishing of water, if available on reasonable demand to members of the general public.

(5) INDUSTRIAL PARKS.—Paragraph (1) shall not apply to any obligation issued as part of an issue substantially all of the proceeds of which are to be used for the acquisition or development of land as the site for an industrial park. For purposes of the preceding sentence, the term "development of land" includes the provision of water, sewage, drainage, or similar facilities, or of transportation, power, or communication facilities, which are incidental to use of the site as an industrial park, but, except with respect to such facilities, does not include the provision of structures or buildings.

(6) EXEMPTION FOR CERTAIN SMALL ISSUES.—

(A) IN GENERAL.—Paragraph (1) shall not apply to any obligation issued as part of an issue the aggregate authorized face amount of which is $1,000,000 or less and substantially all of the proceeds of which are to be used (i) for the acquisition, construction, reconstruction, or improvement of land or property of a character subject to the allowance for depreciation, or (ii) to redeem part or all of a prior issue which was issued for purposes described in clause (i) or this clause.

(B) CERTAIN PRIOR ISSUES TAKEN INTO ACCOUNT.—If—

(i) the proceeds of two or more issues of obligations (whether or not the issuer of each such issue is the same)

are or will be used primarily with respect to facilities located in the same incorporated municipality or located in the same county (but not in any incorporated municipality),

(ii) the principal user of such facilities is or will be the same person or two or more related persons, and

(iii) but for this subparagraph, subparagraph (A) would apply to each such issue,

then, for purposes of subparagraph (A), in determining the aggregate face amount of any later issue there shall be taken into account the face amount of obligations issued under all prior such issues and outstanding at the time of such later issue (not including as outstanding any obligation which is to be redeemed from the proceeds of the later issue).

(C) RELATED PERSONS.—For purposes of this paragraph and paragraph (7), a person is a related person to another person if—

(i) the relationship between such persons would result in a disallowance of losses under section 267 or 707(b), or

(ii) such persons are members of the same controlled group of corporations (as defined in section 1563(a), except that "more than 50 percent" shall be substituted for "at least 80 percent" each place it appears therein).

(D) $5,000,000 LIMIT IN CERTAIN CASES.—At the election of the issuer, made at such time and in such manner as the Secretary or his delegate shall by regulations prescribe, with respect to any issue this paragraph shall be applied—

(i) by substituting "$5,000,000" for "$1,000,000" in subparagraph (A), and

(ii) in determining the aggregate face amount of such issue, by taking into account not only the amount described in subparagraph (B), but also the aggregate amount of capital expenditures with respect to facilities described in subparagraph (E) paid or incurred during the 6-year period beginning 3 years before the date of such issue and ending 3 years after such date (and financed otherwise than out of the proceeds of outstanding issues to which subparagraph (A) applied), as if the aggregate amount of such capital expenditures constituted the face amount of a prior outstanding issue described in subparagraph (B).

(E) FACILITIES TAKEN INTO ACCOUNT.—For purposes of subparagraph (D)(ii), the facilities described in this subparagraph are facilities—

(i) located in the same incorporated municipality or located in the same county (but not in any incorporated municipality), and

(ii) the principal user of which is or will be the same person or two or more related persons.

For purposes of clause (i), the determination of whether or not facilities are located in the same governmental unit shall be made as of the date of issue of the issue in question.

(F) CERTAIN CAPITAL EXPENDITURES NOT TAKEN INTO ACCOUNT.—For purposes of subparagraph (D)(ii), any capital expenditure—

(i) to replace property destroyed or damaged by fire, storm, or other casualty, to the extent of the fair market value of the property replaced,

(ii) required by a change made after the date of issue of the issue in question in a Federal or State law or local ordinance of general application or required by a change made after such date in rules and regulations of general application issued under such a law or ordinance, or

(iii) required by circumstances which could not be reasonably froeseen on such date of issue or arising out of a mistake of law or fact (but the aggregate amount of expenditures not taken into account under this clause with respect to any issue shall not exceed $1,000,000),

shall not be taken into account.

(G) LIMITATION ON LOSS OF TAX EXEMPTION.—In applying subparagraph (D)(ii) with respect to capital expenditures made after the date of any issue, no obligation issued as a part of such issue shall be treated as an obligation not described in subsection (a)(1) by reason of any such expenditure for any period before the date on which such expenditure is paid or incurred.

(H) CERTAIN REFINANCING ISSUES.—In the case of any issue described in subparagraph (A)(ii), an election may be made under subparagraph (D) only if all of the prior issues being redeemed are issues to which subparagraph (A) applies. In applying subparagraph (D)(ii) with respect to such a refinancing issue, capital expenditures shall be taken into account only for purposes of determining whether the prior issues being redeemed qualified (and would have continued to qualify) under subparagraph (A).

(7) EXCEPTION.—Paragraphs (4), (5), and (6) shall not apply with respect to any obligation for any period during which it is held by a person who is a substantial user of the facilities or a related person.

(d) ARBITRAGE BONDS.—

(1) SUBSECTION (a)(1) NOT TO APPLY.—Except as provided in this subsection, any arbitrage bond shall be treated as an obligation not described in subsection (a)(1).

(2) ARBITRAGE BOND.—For purposes of this subsection, the term "arbitrage bond" means any obligation which is issued as part of an issue all or a major portion of the proceeds of which are reasonably expected to be used directly or indirectly—

(A) to acquire securities (within the meaning of section 165(g)(2)(A) or (B)) or obligations (other than obligations described in subsection (a)(1)) which may be reasonably expected at the time of issuance of such issue, to produce a yield over the term of the issue which is materially higher (taking into account any discount or premium) than the yield on obligations of such issue, or

(B) to replace funds which were used directly or indirectly to acquire securities or obligations described in subparagraph (A).

(8) EXCEPTION.—Paragraph (1) shall not apply to any obligation—

(A) which is issued as part of an issue substantially all of the proceeds of which are reasonably expected to be used to provide permanent financing for real property used or to be used for residential purposes for the personnel of an educational institution (within the meaning of section 151(e)(4)) which grants baccalaureate or higher degrees, or to replace funds which were so used, and

(B) the yield on which over the term of the issue is not reasonably expected, at the time of issuance of such issue, to be substantially lower than the yield on obligations acquired or to be acquired in providing such financing.

This paragraph shall not apply with respect to any obligation for any period during which it is held by a person who is a substantial user of property financed by the proceeds of the issue of which such obligation is a part, or by a member of the family (within the meaning of section 318(a)(1)) of any such person.

(4) SPECIAL RULES.—For purposes of paragraph (1), an obligation shall not be treated as an arbitrage bond solely by reason of the fact that—

(A) the proceeds of the issue of which such obligation is a part may be invested for a temporary period in securities or other obligations until such proceeds are needed for the purpose for which such issue was issued, or

(B) an amount of the proceeds of the issue of which such obligation is a part may be invested in securities or other obligations which are part of a reasonably required reserve or replacement fund.

The amount referred to in subparagraph (B) shall not exceed 15 percent of the proceeds of the issue of which such obligation is a part unless the issuer establishes that a higher amount is necessary.

(5) REGULATIONS.—The Secretary or his delegate shall prescribe such regulations as may be necessary to carry out the purposes of this subsection.

(e) CERTAIN IRRIGATION DAMS.—A dam for the furnishing of water for irrigation purposes which has a subordinate use in connection with the generation of electric energy by water shall be treated as meeting the requirements of subsection (c)(4)(G) if—

(1) substantially all of the stored water is contractually available for release from such dam for irrigation purposes, and

(2) the water so released is available on reasonable demand to members of the general public.

[(e)] (f) CROSS REFERENCES.—

For provisions relating to the taxable status of—

(1) Bonds and certificates of indebtedness authorized by the First Liberty Bond Act, see sections 1 and 6 of that Act (40 Stat. 35, 36; 31 U.S.C. 746, 755);

(2) Bonds issued to restore or maintain the gold reserve, see section 2 of the Act of March 14, 1900 (31 Stat. 46; 31 U.S.C. 408);

(3) Bonds, notes, certificates of indebtedness, and Treasury bills authorized by the Second Liberty Bond Act, see sections 4, 5 (b) and (d), 7, 18 (b) and 22(d) of that Act as amended (40 Stat. 290; 46 Stat. 20, 775; 40 Stat. 291, 1310; 55 Stat. 8; 31 U.S.C. 752a, 754, 747, 753, 757c);

(4) Bonds, notes, and certificates of indebtedness of the United States and bonds of the War Finance Corporation owned by certain nonresidents, see section 3 of the Fourth Liberty Bond Act, as amended (40 Stat. 1311, § 4; 31 U.S.C. 750);

(5) Certificates of indebtedness issued after February 4, 1910, see section 2 of the Act of that date (36 Stat. 192; 31 U.S.C. 769);

(6) Consols of 1930, see section 11 of the Act of March 14, 1900 (31 Stat. 48; 31 U.S.C. 751);

(7) Obligations and evidences of ownership issued by the United States or any of its agencies or instrumentalities on or after March 28, 1942, see section 4 of the Public Debt Act of 1941, as amended (c. 147, 61 Stat. 180; 31 U.S.C. 742a);

(8) Commodity Credit Corporation obligations, see section 5 of the Act of March 8, 1938 (52 Stat. 108; 15 U.S.C. 713a–5);

(9) Debentures issued by Federal Housing Administrator, see sections 204(d) and 207(i) of the National Housing Act, as amended (52 Stat. 14, 20; 12 U.S.C. 1710, 1713);

(10) Debentures issued to mortgages by United States Maritime Commission, see section 1105(c) of the Merchant Marine Act, 1936, as amended (52 Stat. 972; 46 U.S.C. 1275);

(11) Federal Deposit Insurance Corporation obligations, see section 15 of the Federal Deposit Insurance Act (64 Stat. 890; 12 U.S.C. 1825);

(12) Federal Home Loan Bank obligations, see section 13 of the Federal Home Loan Bank Act, as amended (49 Stat. 295, § 8; 12 U.S.C. 1433);

(13) Federal savings and loan association loans, see section 5 (h) of the Home Owners' Loan Act of 1933, as amended (48 Stat. 133; U.S.C. 1464);

(14) Federal Savings and Loan Insurance Corporation obligations, see section 402(e) of the National Housing Act (48 Stat. 1257; 12 U.S.C. 1725);

(15) Home Owners' Loan Corporation bonds, see section 4(c) of the Home Owners' Loan Act of 1933, as amended (48 Stat. 644, c. 168; 12 U.S.C. 1463);

(16) Obligations of Central Bank for Cooperatives, production credit corporations, production credit associations, and banks for cooperatives, see section 63 of the Farm Credit Act of 1933 (48 Stat. 267; 12 U.S.C. 1138c);

(17) Panama Canal bonds, see section 1 of the Act of December 21, 1904 (34 Stat. 5; 31 U.S.C. 743), section 8 of the Act of June 28, 1902 (32 Stat. 484; 31 U.S.C. 744), and section 39 of the Tariff Act of 1909 (36 Stat. 117; 31 U.S.C. 745);

(18) Philippine bonds, etc., issued before the independence of the Philippines, see section 9 of the Philippine Independence Act (48 Stat. 463; 48 U.S.C. 1239);

(19) Postal savings bonds, see section 10 of the Act of June 25, 1910 (36 Stat. 817; 39 U.S.C. 760);

(20) Puerto Rican bonds, see section 3 of the Act of March 2, 1917, as amended (50 Stat. 855; 48 U.S.C. 745);

(21) Treasury notes issued to retire national bank notes, see section 18 of the Federal Reserve Act (38 Stat. 268; 12 U.S.C. 447);

(22) United States Housing Authority obligations, see sections 5(e) and 20(b) of the United States Housing Act of 1937 (50 Stat. 890, 898; 42 U.S.C. 1405, 1420);

(23) Virgin Islands insular and municipal bonds, see section 1 of the Act of October 27, 1949 (63 Stat. 940; 48 U.S.C. 1403).

VI. Other Matters Required To Be Discussed Under House Rules

In compliance with clauses 2(l)(3) and 2(l)(4) of Rule XI of the Rules of the House of Representatives, the following statements are made.

With regard to subdivision (A) of Clause 3, the Committee advises that its oversight findings led it to the conclusion that an amendment to the Internal Revenue Code is necessary to establish the eligibility of bons issued by the American Falls Reservoir District for a dam and related facilities for tax-exempt status as industrial development bonds.

In compliance with subdivision (B) of Clause 3, the committee states that the change made in section 103 of the Internal Revenue Code will produce an annual revenue loss of about $1 million at current tax rates for the period of maturity during which the bonds to be issued will be outstanding. Alternatively, the cost to the Federal Government of construction of this project as a direct expenditure presently is estimated at about $50 million.

With respect to subdivisions (C) and (D) of Clause 3, the Committee advises that no estimate or comparison has been prepared by the Director of the Congressional Budget Office relative to any of the provisions of H.R. 9968, nor have any oversight findings or recommendations been made by the Committee on Government Operations with respect to the subject matter contained in H.R. 9968.

In compliance with clause 2(l)(4) of Rule XI, the Committee states that the bonds to be issued followed enactment of H.R. 9968 are not expected to have an inflationary impact on prices and in costs in the operation of the national economy.

○

Calendar No. 546

94TH CONGRESS
1st Session

SENATE

REPORT
No. 94-570

TAX EXEMPT STATUS OF OBLIGATIONS USED TO PROVIDE CERTAIN IRRIGATION FACILITIES

DECEMBER 16 (legislative day, DECEMBER 15), 1975.—Ordered to be printed

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

REPORT

[To accompany H.R. 9968]

The Committee on Finance, to which was referred the bill (H.R. 9968) to amend section 103 of the Internal Revenue Code of 1954 with respect to certain obligations used to provide irrigation facilities, having considered the same, reports favorably thereon without amendment and recommends that the bill do pass.

I. SUMMARY

H.R. 9968 would clarify the tax-exempt status of obligations the proceeds of which are to be used to reconstruct the American Falls Dam in Idaho.

Present law provides that an industrial revenue bond whose proceeds are used to build a dam to store water for irrigation purposes may be eligible for tax-exempt status. Where, however, the water also has a subordinate use in generating electricity, the status of the bonds is not clear under existing law. The American Falls Dam is used principally for irrigation purposes, but the water has a subordinate use in generating electricity. H.R. 9968 provides that industrial revenue bonds issued in such a case may qualify for exempt status if substantially all of the stored water is contractually available for irrigation purposes and the water is available on reasonable demand to members of the general public.

II. GENERAL EXPLANATION OF THE BILL

Present law provides that interest on obligations of State and local governments generally is exempt from Federal income tax. In 1968 tax-exempt status was withdrawn from industrial development bonds

which State and local governments were using to finance and attract private industrial development within their jurisdictions.

Industrial development bonds are generally considered to be State or local obligations, a major portion of the proceeds of which are to be used in, and repaid by, a taxable trade or business. Such bonds are normally issued to acquire a facility for private business in which the beneficial ownership of the facility remains in the private trade or business, although (in order to secure repayment of the bonds) legal title normally remains with the State or local unit issuing the obligations.

When the industrial development bond limitation was enacted, exceptions were provided for certain small issues (sec. 103(c)(6)) and for certain specified public activities (sec. 103(c)(4)) in which cases tax-exempt status was continued. As initially enacted, one of the public activities for which an exemption was provided (sec. 103(c)(4)(E)) was "sewage or solid waste disposal facilities or facilities for the local furnishing of electric energy, gas or water."

In 1971, Congress amended the exception in subparagraph (E) to delete "water" and added the present law subparagraph (G) which extends the exception to "facilities for the furnishing of water, if available on reasonable demand to members of the general public."

As a result, in those cases where obligations are issued for facilities for the furnishing of water which meet the exception (under sec. 103(c)(4)(G)) but where the water is also used to generate electricity, it is uncertain as to whether the obligations would qualify for exempt status unless the use of the electric energy meets the "local" furnishing test (under sec. 103(c)(4)(E)), which has been interpreted to cover an area of two contiguous counties.

The American Falls Reservoir District applied to the Internal Revenue Service in June 1974 for a ruling that bonds to be issued to finance the replacement and rehabilitation of the American Falls Dam would qualify as a tax-exempt issue under section 103(c)(4)(G). The Internal Revenue Service, however, had questions of interpretation with respect to the interrelationship of the exceptions for facilities for furnishing of water and the local furnishing of electric energy and their application to the specific facts of this case. The committee reviewed the facts involved, as described below, and believed it is appropriate to specifically except the bond issue in this case as a result of the special circumstances.

The original American Falls Dam was constructed in 1927 by the Bureau of Reclamation. The dam was restricted to two-thirds of its 1.7 million acre foot capacity in 1972 by the Bureau of Reclamation of the Department of the Interior for safety reasons because of excessive pressures on the dam which were caused by an alkali-aggregate reaction and deterioration in the concrete.

Legislation was enacted on December 28, 1973, to permit replacement and rehabilitation of the American Falls Dam by the American Falls Reservoir District, which is a political subdivision of the State of Idaho. Replacement of the existing dam by the American Falls Reservoir District is an action to be taken in lieu of waiting for a Federal appropriation that would enable the Bureau of Reclamation to build the replacement dam.

The Act of December 28, 1973, also provides that upon completion of construction the United States shall take title to the dam as a feature of the Minidoka Project, located in the upper Snake River basin, Idaho.

As the constructing agent, the American Falls Reservoir District was authorized to contract with an electric utility for the use of the falling water at the dam for hydroelectirc power generation. Revenues from such a contract with help defer the costs of constructing the dam. Prior to the adoption of the Act of December 28, 1973, the Idaho Power Company, which is a spaceholder in the reservoir and which owns and operates a powerplant below the existing dam, expressed interest in the execution of a falling water contract. Subsequent to the adoption of the Act, the District, as the constructing agency, entered into negotiations with the Secretary of the Interior, the Idaho Power Company and the other water users for the preparation of various contracts including a contract for the use of falling water.

It was intended that in normal circumstances substantially all of the falling water would be made available to the Power Company only when water was released from the dam for irrigation purposes. There has been no intention to release water specifically for use by the Idaho Power Company to generate electricity, except for 45,000 acre-feet (2.65 percent of the storage capacity) whose release the power company, in its capacity as a space holder in the irrigation district, can schedule for the purpose of generating electric energy. Thus, the use of water for electric energy would be subordinated to the use of the water for irrigation.

Although the Federal Government might well eventually completely finance the reconstruction of the American Falls Dam, the American Falls Reservoir District is undertaking the reconstruction now in order to make the dam fully operational for the spaceholders (rather than the present restricted two-thirds capacity). If it were not for the use of the water by the Idaho Power Company for hydroelectric power generation, any bonds issued by the Reservoir District would presently qualify for tax-exempt status. In this case the Idaho Power Company has a limited spaceholder right (under 3 percent) and is financing a large portion of the debt to assist the reconstruction of the dam and has use of the falling water for its hydroelectric power generation purposes. In addition, since the dam is to be turned over to the Federal Government after its reconstruction for ownership and operation, in effect, this financing can be viewed as saving the Federal Government the expenditure it would have had to make to reconstruct the dam several years in the future. In view of these special circumstances, the committee believes it is appropriate to extend tax-exempt status to the bonds to be issued to finance the reconstruction of the dam.

The bill adds a new exception to industrial development bond treatment to specifically allow tax-exempt status for the bonds issued to reconstruct the American Falls Dam. This exception is to apply to obligations for a dam which furnishes water for irrigation purposes which has a subordinate use in connection with the generation of electric energy by water if substantially all of the stored water is contractually available for release from the dam for irrigation pur-

poses and if the water released is available on reasonable demand for members of the general public.

The committee intends that subordinate use of water for generating electric energy means that less than 10 percent of the normal supply of stored water may contractually be scheduled for release by the power company and used for generating electric energy. Normal refers to conditions that generally prevail in the service area of this reservoir, and it is recognized that unusually wet or dry weather can cause a significant distortion in the 2.65 percent of water contractually scheduled for release to be used for generating electric energy. The committee intends that such unusual circumstances not be guiding in determining the subordinate use of water. In addition, normal use does not include a temporary increase in water released for the power company following contractual default by a spaceholder and his water share being made available to other spaceholders under the terms of the contract for the construction and operation of the dam and its facilities.

Thus, the provision applies the requirements of subsection (c)(4)(G) where substantially all of the stored water (under normal weather and climatic conditions) is available for release to be used for irrigation in the American Falls Reservoir District. The requirement that the released water be available on reasonable demand to members of the general public is retained in the new subsection (e). The committee understands that the American Falls project conforms with this requirement.

The bill is to apply to obligations issued after the date of the enactment of this Act.

III. Costs of Carrying Out the Bill and Effect on the Revenues of the Bill

In compliance with section 252(a) of the Legislative Reorganization Act of 1970, the following statement is made relative to the costs to be incurred in carrying out this bill and the effect on the revenues of the bill.

The committee estimates that the bill, relating to the tax-exempt status of obligations used to provide certain irrigation facilities, will result in an annual revenue loss of about $1 million in each of the five fiscal years following the current fiscal year. No revenue loss is expected in the current fiscal year.

IV. Vote of Committee in Reporting the Bill

In compliance with section 133 of the Legislative Reorganization Act, as amended, the following statement is made relative to the vote of the committee on reporting the bill. This bill was ordered favorably reported by the committee without a rollcall vote and without objection.

V. Changes in Existing Law

In compliance with subsection (4) of rule XXIX of the Standing Rules of the Senate, changes in existing law made by the bill, as

reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE CODE OF 1954

* * * * * * *

Chapter 1—Normal Taxes and Surtaxes

* * * * * * *

Subchapter B—Computation of Taxable Income

* * * * * * *

Part III—Items Specifically Excluded From Gross Income

Sec. 103. Interest on Certain Governmental Obligations.

(a) General Rule.—Gross income does not include interest on—

(1) the obligations of a State, a Territory, or a possession of the United States, or any political subdivision of any of the foregoing, or of the District of Columbia;

(2) the obligations of the United States; or

(3) the obligations of a corporation organized under Act of Congress, if such corporation is an instrumentality of the United States and if under the respective Acts authorizing the issue of the obligations the interest is wholly exempt from the taxes imposed by this subtitle.

(b) Exception.—Subsection (a)(2) shall not apply to interest on obligations of the United States issued after September 1, 1917 (other than postal savings certificates of deposit, to the extent they represent deposits made before March 1, 1941), unless under the respective Acts authorizing the issuance thereof such interest is wholly exempt from the taxes imposed by this subtitle.

(c) Industrial Development Bonds.—

(1) Subsection (a)(1) not to apply.—Except as otherwise provided in this subsection, any industrial development bond shall be treated as an obligation not described in subsection (a)(1).

(2) Industrial development bond.—For purposes of this subsection, the term "industrial development bond" means any obligation—

(A) which is issued as part of an issue all or a major portion of the proceeds of which are to be used directly or indirectly in any trade or business carried on by any person who is not an exempt person (within the meaning of paragraph (3)), and

(B) the payment of the principal or interest on which (under the terms of such obligation or any underlying arrangement) is, in whole or in major part—

(i) secured by any interest in property used or to be used in a trade or business or in payments in respect of such property, or

(ii) to be derived from payments in respect of property, or borrowed money, used or to be used in a trade or business.

(3) EXEMPT PERSON.—For purposes of paragraph (2)(A), the term "exempt person" means—

(A) a governmental unit, or

(B) an organization described in section 501(c)(3) and exempt from tax under section 501(a) (but only with respect to a trade or business carried on by such organization which is not an unrelated trade or business, determined by applying section 513(a) to such organization).

(4) CERTAIN EXEMPT ACTIVITIES.—Paragraph (1) shall not apply to any obligation which is issued as part of an issue substantially all of the proceeds of which are to be used to provide—

(A) residential real property for family units,

(B) sports facilities,

(C) convention or trade show facilities,

(D) airports, docks, wharves, mass commuting facilities, parking facilities, or storage or training facilities directly related to any of the foregoing,

(E) sewage or solid waste disposal facilities or facilities for the local furnishing of electric energy or gas,

(F) air or water pollution control facilities, or

(G) facilities for the furnishing of water, if available on reasonable demand to members of the general public.

(5) INDUSTRIAL PARKS.—Paragraph (1) shall not apply to any obligation issued as part of an issue substantially all of the proceeds of which are to be used for the acquisition or development of land as the site for an industrial park. For purposes of the preceding sentence, the term "development of land" includes the provision of water, sewage, drainage, or similar facilities, or of transportation, power, or communication facilities, which are incidental to use of the site as an industrial park, but, except with respect to such facilities, does not include the provision of structures or buildings.

(6) EXEMPTION FOR CERTAIN SMALL ISSUES.—

(A) IN GENERAL.—Paragraph (1) shall not apply to any obligation issued as part of an issue the aggregate authorized face amount of which is $1,000,000 or less and substantially all of the proceeds of which are to be used (i) for the acquisition, construction, reconstruction, or improvement of land or property of a character subject to the allowance for depreciation, or (ii) to redeem part or all of a prior issue which was issued for purposes described in clause (i) or this clause.

(B) CERTAIN PRIOR ISSUES TAKEN INTO ACCOUNT.—If—

(i) the proceeds of two or more issues of obligations (whether or not the issuer of each such issue is the same) are or will be used primarily with respect to facilities located in the same incorporated municipality or located in the same county (but not in any incorporated municipality),

(ii) the principal user of such facilities is or will be the same person or two or more related persons, and

(iii) but for this subparagraph, subparagraph (A) would apply to each such issue,

then, for purposes of subparagraph (A), in determining the aggregate face amount of any later issue there shall be taken into account the face amount of obligations issued under all prior such issues and outstanding at the time of such later issue (not including as outstanding any obligation which is to be redeemed from the proceeds of the later issue).

(C) RELATED PERSONS.—For purposes of this paragraph and paragraph (7), a person is a related person to another person if—

(i) the relationship between such persons would result in a disallowance of losses under section 267 or 707(b), or

(ii) such persons are members of the same controlled group of corporations (as defined in section 1563(a), except that "more than 50 percent" shall be substituted for "at least 80 percent" each place it appears therein).

(D) $5,000,000 LIMIT IN CERTAIN CASES.—At the election of the issuer, made at such time and in such manner as the Secretary or his delegate shall by regulations prescribe, with respect to any issue this paragraph shall be applied—

(i) by substituting "$5,000,000" for "$1,000,000" in subparagraph (A), and

(ii) in determining the aggregate fact amount of such issue, by taking into account not only the amount described in subparagraph (B), but also the aggregate amount of capital expenditures with respect to facilities described in subparagraph (E) paid or incurred during the 6-year period beginning 3 years before the date of such issue and ending 3 years after such date (and financed otherwise than out of the proceeds of outstanding issues to which subparagraph (A) applied), as if the aggregate amount of such capital expenditures constituted the face amount of a prior outstanding issue described in subparagraph (B).

(E) FACILITIES TAKEN INTO ACCOUNT.—For purposes of subparagraph (D)(ii), the facilities described in this subparagraph are facilities—

(i) located in the same incorporated municipality or located in the same county (but not in any incorporated municipality), and

(ii) the principal user of which is or will be the same person or two or more related persons.

For purposes of clause (i), the determination of whether or not facilities are located in the same governmental unit shall be made as of the date of issue of the issue in question.

(F) CERTAIN CAPITAL EXPENDITURES NOT TAKEN INTO ACCOUNT.—For purposes of subparagraph (D)(ii), any capital expenditure—

(i) to replace property destroyed or damaged by fire, storm, or other casualty, to the extent of the fair market value of the property replaced,

(ii) required by a change made after the date of issue of the issue in question in a Federal or State law or local

ordinance of general application or required by a change made after such date in rules and regulations of general application issued under such a law or ordinance, or

(iii) required by circumstances which could not be reasonably foreseen on such date of issue or arising out of a mistake of law or fact (but the aggregate amount of expenditures not taken into account under this clause with respect to any issue shall not exceed $1,000,000), shall not be taken into account.

(G) LIMITATION ON LOSS OF TAX EXEMPTION.—In applying subparagraph (D)(ii) with respect to capital expenditures made after the date of any issue, no obligation issued as a part of such issue shall be treated as an obligation not described in subsection (a)(1) by reason of any such expenditure for any period before the date on which such expenditure is paid or incurred.

(H) CERTAIN REFINANCING ISSUES.— In the case of any issue described in subparagraph (A)(ii), an election may be made under subparagraph (D) only if all of the prior issues being redeemed are issues to which subparagraph (A) applies. In applying subparagraph (D)(ii) with respect to such a refinancing issue, capital expenditures shall be taken into account only for purposes of determining whether the prior issues being redeemed qualified (and would have continued to qualify) under subparagraph (A).

(7) EXCEPTION.—Paragraphs (4), (5), and (6) shall not apply with respect to any obligation for any period during which it is held by a person who is a substantial user of the facilities or a related person.

(d) ARBITRAGE BONDS.—

(1) SUBSECTION (a)(1) NOT TO APPLY.—Except as provided in this subsection, any arbitrage bond shall be treated as an obligation not described in subsection (a)(1).

(2) ARBITRAGE BOND.—For purposes of this subsection, the term "arbitrage bond" means any obligation which is issued as part of an issue all or a major portion of the proceeds of which are reasonably expected to be used directly or indirectly—

(A) to acquire securities (within the meaning of section 165(g)(2)(A) or (B) or obligations (other than obligations described in subsection (a)(1)) which may be reasonably expected at the time of issuance of such issue, to produce a yield over the term of the issue which is materially higher (taking into account any discount or premium) than the yield on obligations of such issue, or

(B) to replace funds which were used directly or indirectly to acquire securities or obligations described in subparagraph (A).

(3) EXCEPTION.—Paragraph (1) shall not apply to any obligation—

(A) which is issued as part of an issue substantially all of the proceeds of which are reasonably expected to be used to provide permanent financing for real property used or to be

used for residential purposes for the personnel of an educational institution (within the meaning of section 151(e)(4)) which grants baccalaureate or higher degrees, or to replace funds which were so used, and

(B) the yield on which over the term of the issue is not reasonably expected, at the time of issuance of such issue, to be substantially lower than the yield on obligations acquired or to be acquired in providing such financing.

This paragraph shall not apply with respect to any obligation for any period during which it is held by a person who is a substantial user of property financed by the proceeds of the issue of which such obligation is a part, or by a member of the family (within the meaning of section 318(a)(1)) of any such person.

(4) SPECIAL RULES.—For purposes of paragraph (1), an obligation shall not be treated as an arbitrage bond solely by reason of the fact that—

(A) the proceeds of the issue of which such obligation is a part may be invested for a temporary period in securities or other obligations until such proceeds are needed for the purpose for which such issue was issued, or

(B) an amount of the proceeds of the issue of which such obligation is a part may be invested in securities or other obligations which are part of a reasonably required reserve or replacement fund.

The amount referred to in subparagraph (B) shall not exceed 15 percent of the proceeds of the issue of which such obligation is a part unless the issuer establishes that a higher amount is necessary.

(5) REGULATIONS.—The Secretary or his delegate shall prescribe such regulations as may be necessary to carry out the purposes of this subsection.

(e) CERTAIN IRRIGATION DAMS.—A dam for the furnishing of water for irrigation purposes which has a subordinate use in connection with the generation of electric energy by water shall be treated as meeting the requirements of subsection (c)(4)(G) if—

(1) substantially all of the stored water is contractually available for release from such dam for irrigation purposes, and

(2) the water so released is available on reasonable demand to members of the general public.

[(e)] *(f)* CROSS REFERENCES.—

For provisions relating to the taxable status of—

(1) Bonds and certificates of indebtedness authorized by the First Liberty Bond Act, see sections 1 and 6 of that Act (40 Stat. 35, 36; 31 U.S.C. 746, 755);

(2) Bonds issued to restore or maintain the gold reserve, see section 2 of the Act of March 14, 1900 (31 Stat. 46; 31 U.S.C. 408);

(3) Bonds, notes, certificates of indebtedness, and Treasury bills authorized by the Second Liberty Bond Act, see sections 4, 5(b) and (d), 7, 18(b) and 22(d) of the Act as amended (40 Stat. 290; 46 Stat. 20, 775; 40 Stat. 291, 1310; 55 Stat. 8; 31 U.S.C. 752a, 754, 747, 753, 757c);

(4) Bonds, notes, and certificates of indebtedness of the United States and bonds of the War Finance Corporation owned by certain nonresidents, see section 3 of the Fourth Liberty Bond Act, as amended (40 Stat. 1311, § 4; 31 U.S.C. 750);

(5) Certificates of indebtedness issued after February 4, 1910, see section 2 of the Act of that date (36 Stat. 192; 31 U.S.C. 769);

(6) Consols of 1930, see section 11 of the Act of March 14, 1900 (31 Stat. 48; 31 U.S.C. 751);

(7) Obligations and evidences of ownership issued by the United States or any of its agencies or instrumentalities on or after March 28, 1942, see section 4 of the Public Debt Act of 1941, as amended (c. 147, 61 Stat. 180; 31 U.S.C. 742a);

(8) Commodity Credit Corporation obligations, see section 5 of the Act of March 8, 1938 (52 Stat. 108; 15 U.S.C. 713a–5);

(9) Debentures issued by Federal Housing Administrator, see sections 204(d) and 207(i) of the National Housing Act, as amended (52 Stat. 14, 20; 12 U.S.C. 1710, 1713);

(10) Debentures issued to mortgages by United States Maritime Commission, see section 1105(c) of the Merchant Marine Act, 1936, as amended (52 Stat. 972; 46 U.S.C. 1275);

(11) Federal Deposit Insurance Corporation obligations, see section 15 of the Federal Deposit Insurance Act (64 Stat. 890; 12 U.S.C. 1825);

(12) Federal Home Loan Bank obligations, see section 13 of the Federal Home Loan Bank Act, as amended (49 Stat. 295, § 8; 12 U.S.C. 1433);

(13) Federal savings and loan association loans, see section 5 (h) of the Home Owners' Loan Act of 1933, as amended (48 Stat. 133; U.S.C. 1464);

(14) Federal Savings and Loan Insurance Corporation obligations, see section 402(e) of the National Housing Act (48 Stat. 1257; 12 U.S.C. 1725);

(15) Home Owners' Loan Corporation bonds, see section 4(c) of the Home Owners' Loan Act of 1933, as amended (48 Stat. 644, c. 168; 12 U.S.C. 1463);

(16) Obligations of Central Bank for Cooperatives, production credit corporations, production credit associations, and banks for cooperatives, see section 63 of the Farm Credit Act of 1933 (48 Stat. 267; 12 U.S.C. 1138c);

(17) Panama Canal bonds, see section 1 of the Act of December 21, 1904 (34 Stat. 5; 31 U.S.C. 743), section 8 of the Act of June 28, 1902 (32 Stat. 484; 31 U.S.C. 744), and section 39 of the Tariff Act of 1909 (36 Stat. 117; 31 U.S.C. 745);

(18) Philippine bonds, etc., issued before the independence of the Philippines, see section 9 of the Philippine Independence Act (48 Stat. 463; 48 U.S.C. 1239);

(19) Postal savings bonds, see section 10 of the Act of June 25, 1910 (36 Stat. 817; 39 U.S.C. 760);

(20) Puerto Rican bonds, see section 3 of the Act of March 2, 1917, as amended (50 Stat. 855; 48 U.S.C. 745);

(21) Treasury notes issued to retire national bank notes, see section 18 of the Federal Reserve Act (38 Stat. 268; 12 U.S.C. 447);

(22) United States Housing Authority obligations, see sections 5(e) and 20(b) of the United States Housing Act of 1937 (50 Stat. 890, 898; 42 U.S.C. 1405, 1420);

(23) Virgin Islands insular and municipal bonds, see section 1 of the Act of October 27, 1949 (63 Stat. 940; 48 U.S.C. 1403).

○

H. R. 9968

Ninety-fourth Congress of the United States of America

AT THE FIRST SESSION

Begun and held at the City of Washington on Tuesday, the fourteenth day of January, one thousand nine hundred and seventy-five

An Act

To change certain income tax provisions of the Internal Revenue Code of 1954, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Revenue Adjustment Act of 1975".

SEC. 1A. DECLARATION OF POLICY.

(a) Congress is determined to continue the tax reduction for the first 6 months of 1976 in order to assure continued economic recovery.

(b) Congress is also determined to continue to control spending levels in order to reduce the national deficit.

(c) Congress reaffirms its commitments to the procedures established by the Congressional Budget and Impoundment Control Act of 1974 under which it has already established a binding spending ceiling for the fiscal year 1976.

(d) If the Congress adopts a continuation of the tax reduction provided by this Act beyond June 30, 1976, and if economic conditions warrant doing so, Congress shall provide, through the procedures in the Budget Act, for reductions in the level of spending in the fiscal year 1977 below what would otherwise occur, equal to any additional reduction in taxes (from the 1974 tax rate levels) provided for the fiscal year 1977: *Provided, however*, That nothing shall preclude the right of the Congress to pass a budget resolution containing a higher or lower expenditure figure if the Congress concludes that this is warranted by economic conditions or unforeseen circumstances.

SEC. 2. INDIVIDUAL INCOME TAX REDUCTIONS.

(a) LOW INCOME ALLOWANCE.—

(1) INCREASE.—Subsection (c) of section 141 of the Internal Revenue Code of 1954 (relating to low income allowance) is amended to read as follows:

"(c) LOW INCOME ALLOWANCE.—

"(1) IN GENERAL.—The low income allowance is—

"(A) $2,100 in the case of—

"(i) a joint return under section 6013, or

"(ii) a surviving spouse (as defined in section 2(a)),

"(B) $1,700 in the case of an individual who is not married and who is not a surviving spouse (as so defined), or

"(C) $1,050 in the case of a married individual filing a separate return.

"(2) APPLICATION OF 6-MONTH RULE.—Notwithstanding the provisions of paragraph (1), the following amounts shall be substituted for the amount set forth in paragraph (1)—

"(A) '$1,700' for '$2,100' in subparagraph (A),

"(B) '$1,500' for '$1,700' in subparagraph (B), and

"(C) '$850' for '$1,050' in subparagraph (C).".

(2) CHANGE IN FILING REQUIREMENTS TO REFLECT INCREASE IN LOW INCOME ALLOWANCE.—Paragraph (1)(A) of section 6012(a) of such Code (relating to persons required to make returns of income) is amended—

(A) by striking out "$2,350" in clause (i) of such paragraph and inserting in lieu thereof "$2,450";

(B) by striking out "$2,650" in clause (ii) of such paragraph and inserting in lieu thereof "$2,850"; and

(C) by striking out "$3,400" in clause (iii) of such paragraph and inserting in lieu thereof "$3,600".

(b) PERCENTAGE STANDARD DEDUCTION.—

(1) INCREASE.—Subsection (b) of section 141 of such Code (relating to percentage standard deduction) is amended to read as follows:

"(b) PERCENTAGE STANDARD DEDUCTION.—

"(1) GENERAL RULE.—The percentage standard deduction is an amount equal to 16 percent of adjusted gross income but not to exceed—

"(A) $2,800 in the case of—

"(i) a joint return under section 6013, or

"(ii) a surviving spouse (as defined in section 2(a)),

"(B) $2,400 in the case of an individual who is not married and who is not a surviving spouse (as so defined), or

"(C) $1,400 in the case of a married individual filing a separate return.

"(2) APPLICATION OF 6-MONTH RULE.—Notwithstanding the provisions of paragraph (1) of this subsection, the following amounts shall be substituted for the amounts set forth in paragraph (1)—

"(A) '$2,400' for '$2,800' in subparagraph (A),

"(B) '$2,200' for '$2,400' in subparagraph (B), and

"(C) '$1,200' for '$1,400' in subparagraph (C).".

(2) CONFORMING AMENDMENTS.—Section 3402(m) of such Code (relating to withholding allowances based on itemized deductions) is amended—

(A) by striking out "$2,600" in paragraph (1)(B) and inserting in lieu thereof "$2,800", and

(B) by striking out "$2,300" in such paragraph and inserting in lieu thereof "$2,400".

(c) EARNED INCOME CREDIT.—Subsections (a) and (b) of section 43 of such Code (relating to earned income credit) are amended to read as follows:

"(a) ALLOWANCE OF CREDIT.—

"(1) GENERAL RULE.—In the case of an eligible individual, there shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to 10 percent of so much of the earned income for the taxable year as does not exceed $4,000.

"(2) APPLICATION OF 6-MONTH RULE.—Notwithstanding the provisions of paragraph (1), the term '5 percent' shall be substituted for the term '10 percent' where it appears in that paragraph.".

"(b) LIMITATION.—

"(1) GENERAL RULE.—The amount of the credit allowable to a taxpayer under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount equal to 10 percent of so much of the adjusted gross income (or, if greater, the earned income) of the taxpayer for the taxable year as exceeds $4,000.

"(2) APPLICATION OF 6-MONTH RULE.—Notwithstanding the provisions of paragraph (1), the term '5 percent' shall be substituted for the term '10 percent' where it appears in that paragraph.".

(d) DISREGARD OF REFUND.—Any refund of Federal income taxes made to any individual by reason of section 43 of the Internal Revenue Code of 1954 (relating to earned income credit) shall not be taken into account as income or receipts for purposes of determining the eligibility, for the month in which such refund is made or any month thereafter which begins prior to July 1, 1976, of such individual or any other individual for benefits or assistance, or the amount or extent of benefits or assistance, under any Federal program or under any State or local program financed in whole or in part with Federal funds, but only if such individual (or the family unit of which he is a member) is a recipient of benefits or assistance under such a program for the month before the month in which such refund is made.

(e) EXTENSION OF CERTAIN LOW-INCOME ALLOWANCE, PERCENTAGE STANDARD DEDUCTION, AND TAX CREDIT PROVISIONS.—The last sentence of section 209(a) of the Tax Reduction Act of 1975 is amended to read as follows: "The amendments made by section 201(a) and 202(a) shall cease to apply to taxable years ending after December 31, 1975; those made by sections 201(b), 201(c), and 203 shall cease to apply to taxable years ending after December 31, 1976.".

(f) EXTENSION OF EARNED INCOME CREDIT.—Section 209(b) of the Tax Reduction Act of 1975 (relating to effective date for section 204) is amended by striking out "January 1, 1976," and inserting in lieu thereof "January 1, 1977.".

(g) EFFECTIVE DATE.—The amendments made by this section apply to taxable years ending after December 31, 1975, and before January 1, 1977.

SEC. 3. TAXABLE INCOME CREDIT.

(a) TAXABLE INCOME CREDIT.—

(1) IN GENERAL.—Section 42 of the Internal Revenue Code of 1954 (relating to credit for personal exemptions) is amended to read as follows:

"SEC. 42. TAXABLE INCOME CREDIT.

"(a) ALLOWANCE OF CREDIT.—

"(1) IN GENERAL.—In the case of an individual, there shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to the greater of—

"(A) 2 percent of so much of the taxpayer's taxable income for the taxable year as does not exceed $9,000; or

"(B) $35 multiplied by each exemption for which the taxpayer is entitled to a deduction for the taxable year under subsection (b) or (e) of section 151.

"(2) APPLICATION OF SIX-MONTH RULE.—Notwithstanding the provisions of paragraph (1) of this subsection, the percentage "1 percent" shall be substituted for "2 percent" in subparagraph (A) of such paragraph, and the amount "$17.50" shall be substituted for the amount "$35" in subparagraph (B) of such paragraph.

"(b) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) shall not exceed the amount of the tax imposed by this chapter for the taxable year. In determining the credits allowed under—

"(1) section 33 (relating to foreign tax credit),

"(2) section 37 (relating to retirement income credit),

"(3) section 38 (relating to investment in certain depreciable property),

"(4) section 40 (relating to expenses of work incentive programs), and

"(5) section 41 (relating to contributions to candidates for public office),

the tax imposed by this chapter shall (before any other reductions) be reduced by the credit allowed by this section.

"(c) SPECIAL RULE FOR MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—

"(1) IN GENERAL.—Notwithstanding subsection (a), in the case of a married individual who files a separate return for the taxable year, the amount of the credit allowable under subsection (a) for the taxable year shall be equal to either—

"(A) the amount determined under paragraph (1)(A) of subsection (a); or

"(B) if this subparagraph applies to the individual for the taxable year, the amount determined under paragraph (1)(B) of subsection (a).

For purposes of the preceding sentence, paragraph (1) of subsection (a) shall be applied by substituting '$4,500' for '$9,000'.

"(2) APPLICATION OF PARAGRAPH (1)(B).—Subparagraph (B) of paragraph (1) shall apply to any taxpayer for any taxable year if—

"(A) such taxpayer elects to have such subparagraph apply for such taxable year, and

"(B) the spouse of such taxpayer elects to have such subparagraph apply for any taxable year corresponding, for purposes of section 142(a), to the taxable year of the taxpayer.

Any such election shall be made at such time, and in such manner, as the Secretary or his delegate shall by regulations prescribe.

"(3) MARITAL STATUS.—For purposes of this subsection, the determination of marital status shall be made under section 143.

"(d) CERTAIN PERSONS NOT ELIGIBLE.—This section shall not apply to any estate or trust, nor shall it apply to any nonresident alien individual.".

(2) CLERICAL AMENDMENT.—The table of sections for subpart A of part IV of subchapter A of chapter 1 of such Code is amended by striking out the item relating to section 42 and inserting in lieu thereof the following:

"Sec. 42. Taxable income credit.".

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to taxable years ending after December 31, 1975. Such amendments shall cease to apply to taxable years ending after December 31, 1976.

SEC. 4. CORPORATE TAX RATES AND SURTAX EXEMPTION.

(a) CORPORATE NORMAL TAX.—Section 11(a) of the Internal Revenue Code of 1954 (relating to corporate normal tax) is amended to read as follows:

"(b) NORMAL TAX.—

"(1) GENERAL RULE.—The normal tax is equal to—

"(A) in the case of a taxable year ending after December 31, 1976, 22 percent of the taxable income, and

"(B) in the case of a taxable year ending after December 31, 1974, and before January 1, 1977, the sum of—

"(i) 20 percent of so much of the taxable income as does not exceed $25,000, plus

"(ii) 22 percent of so much of the taxable income as exceeds $25,000.

"(2) SIX-MONTH APPLICATION OF GENERAL RULE.—

"(A) CALENDAR YEAR TAXPAYERS.—Notwithstanding the provisions of paragraph (1), in the case of a taxpayer who has as his taxable year the calendar year 1976, the normal tax for such taxable year is equal to the sum of—

"(i) 21 percent of so much of the taxable income as does not exceed $25,000, plus

"(ii) 22 percent of so much of the taxable income as exceeds $25,000.

"(B) FISCAL YEAR TAXPAYERS.—Notwithstanding the provisions of paragraph (1), in the case of a taxpayer whose taxable year is not the calendar year, effective on July 1, 1976, paragraph (1) shall cease to apply and the normal tax shall be 22 percent.".

(b) CORPORATE SURTAX.—Section 11(c) of such Code (relating to surtax) is amended to read as follows:

"(c) SURTAX.—

"(1) GENERAL RULE.—The surtax is 26 percent of the amount by which the taxable income exceeds the surtax exemption for the taxable year.

"(2) SPECIAL RULE FOR 1976 FOR CALENDAR YEAR TAXPAYERS.—Notwithstanding the provisions of paragraph (1), in the case of a taxpayer who has as his taxable year the calendar year 1976, the surtax for such taxable year is—

"(A) 13 percent of the amount by which the taxable income exceeds the $25,000 surtax exemption (as in effect under subsection (d)(2)) but does not exceed $50,000, plus

"(B) 26 percent of the amount by which the taxable income exceeds $50,000.".

(c) SURTAX EXEMPTION.—Section 11(d) of such Code (relating to surtax exemption) is amended to read as follows:

"(d) SURTAX EXEMPTION.—

"(1) GENERAL RULE.—For purposes of this subtitle, the surtax exemption for any taxable year is $50,000, except that, with respect to a corporation to which section 1561 or 1564 (relating to surtax exemptions in case of certain controlled corporations) applies for the taxable year, the surtax exemption for the taxable year is the amount determined under such section.

"(2) SIX-MONTH APPLICATION OF GENERAL RULE.—Notwithstanding the provisions of paragraph (1)—

"(A) CALENDAR YEAR TAXPAYERS.—In the case of a taxpayer who has as his taxable year the calendar year 1976, the provisions of paragraph (1) shall be applied for such taxable year by substituting the amount '$25,000' for the amount '$50,000' appearing therein.

"(B) FISCAL YEAR TAXPAYERS.—In the case of a taxpayer whose taxable year is not the calendar year, effective on July 1, 1976, paragraph (1) shall be applied by substituting the amount '$25,000' for the amount '$50,000' appearing therein, and such substitution shall be treated, for purposes of section 21, as a change in a rate of tax.".

(d) TECHNICAL AND CONFORMING CHANGES.—

(1) Section 1561(a)(1) of such Code (relating to limitations on certain multiple tax benefits in the case of certain controlled corporations) as such section is in effect for taxable years ending after December 31, 1975, is amended by striking out "$25,000".

Section 962(c) of such Code (relating to surtax exemption for individuals electing to be subject to tax at corporate rates) as such section is in effect for taxable years ending after December 31, 1975, is amended by striking out "$25,000" and inserting in lieu thereof "the surtax exemption".

(2) Section 21(f) of such Code (relating to increase in surtax exemptions) is amended—

(A) by striking out "INCREASE" in the caption and inserting "CHANGE" in lieu thereof, and

(B) by inserting after "Tax Reduction Act of 1975" the following: "and the change made by section 3(c) of the Revenue Adjustment Act of 1975".

(e) EFFECTIVE DATES.—The amendments made by subsections (b), (c), and (d) apply to taxable years beginning after December 31, 1975. The amendment made by subsection (c) ceases to apply for taxable years beginning after December 31, 1976.

SEC. 5. WITHHOLDING; ESTIMATED TAX PAYMENTS.

(a) WITHHOLDING.—

(1) IN GENERAL.—Section 3402(a) of the Internal Revenue Code of 1954 (relating to income tax collected at source), as amended by section 205 of the Tax Reduction Act of 1975, is amended by inserting after the second sentence thereof the following: "The tables so prescribed with respect to wages paid after December 31, 1975, and before July 1, 1976, shall be the same as the tables prescribed under this subsection which were in effect on December 10, 1975.".

(2) TECHNICAL AMENDMENT.—Section 209(c) of the Tax Reduction Act of 1975 is amended by striking out "January 1, 1976" and inserting in lieu thereof "July 1, 1976".

(b) ESTIMATED TAX PAYMENTS BY INDIVIDUALS.—Section 6153 of such Code (relating to installment payments of estimated income tax by individuals) is amended by adding at the end thereof the following new subsection:

"(g) SIX-MONTH APPLICATION OF REVENUE ADJUSTMENT ACT OF 1975 CHANGES.—In the case of a taxpayer who has as his taxable year the calendar year 1976, the amount of any installment the payment of which is required to be made after December 31, 1975, and before July 1, 1976, may be computed without regard to section 42(a)(2), 43(a)(2), 43(b)(2), 141(b)(2), or 141(c)(2).".

(c) ESTIMATED TAX PAYMENTS BY CORPORATIONS.—Section 6154 of such Code (relating to installment payments of estimated income tax by corporations) is amended by adding at the end thereof the following new subsection:

"(h) SIX-MONTH APPLICATION OF REVENUE ADJUSTMENT ACT OF 1975 CHANGES.—In the case of a corporation which has as its taxable year the calendar year 1976, the amount of any installment the payment of which is required to be made after December 31, 1975, and before July 1, 1976, may be computed without regard to sections 11(b)(2), 11(c)(2), and 11(d)(2).".

SEC. 6. ROLLING STOCK.

(a) EXCLUSION FROM INCOME.—Section 883(a) of the Internal Revenue Code of 1954 is hereby amended by adding at the end thereof the following new paragraph:

"(3) RAILROAD ROLLING STOCK OF FOREIGN CORPORATIONS.—Earnings derived from payments by a common carrier for the use on a temporary basis (not expected to exceed a total of 90 days in any taxable year) of railroad rolling stock owned by a corporation of

a foreign country which grants an equivalent exemption to corporations organized in the United States."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to payments made after November 18, 1974.

SEC. 7. CERTAIN IRRIGATION FACILITIES.

(a) IN GENERAL.—Section 103 of the Internal Revenue Code of 1954 (relating to interest on certain governmental obligations) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) CERTAIN IRRIGATION DAMS.—A dam for the furnishing of water for irrigation purposes which has a subordinate use in connection with the generation of electric energy by water shall be treated as meeting the requirements of subsection (c) (4) (G) if—

"(1) substantially all of the stored water is contractually available for release from such dam for irrigation purposes, and

"(2) the water so released is available on reasonable demand to members of the general public.".

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to obligations issued after the date of the enactment of this Act.

Speaker of the House of Representatives.

Vice President of the United States and
President of the Senate.

FOR IMMEDIATE RELEASE DECEMBER 19, 1975

Office of the White House Press Secretary

THE WHITE HOUSE

STATEMENT BY THE PRESS SECRETARY

The President is very pleased by the actions taken in the Congress tonight on the tax bill.

The bill which has been enacted not only continues cuts in taxes for the first half of 1976 but also represents a good faith commitment by the Congress to match future tax reductions with dollar-for-dollar reductions in projected spending. This has been the essential issue at stake throughout these debates, and the President is gratified that the Congress has now accepted this principle.

The essence of the bill, then, is that taxpayers will continue to enjoy a measure of tax relief in 1976 and that for the first time in history, future reductions in taxes will lead to similar reductions in spending.

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