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Office of the White House Press Secretary

THE WHITE HOUSE

FACT SHEET

THE TAX REFORM ACT OF 1976 (H.R. 10612)

President Ford today signed H.R. 10612, the Tax Reform Act of 1976. The bill is a major revision of the nation's tax code. It extends tax relief for low and moderate income taxpayers, seeks to increase the tax burden on those wealthy individuals who have used tax loopholes to reduce greatly their tax liability, provides incentives for investment by industry in new machinery and equipment, provides long-desired revisions in estate and gift taxation, and revises the tax treatment of income earned abroad by United States taxpayers.

MAJOR PROVISIONS

High Income, Low Tax Taxpayers. Many high-income individuals have used investments in so-called tax-shelter ventures to reduce their Federal income taxes. The 1976 tax bill contains provisions which will largely eliminate the use of such tax shelters.

-- The "at risk" limitation prevents the deduction of losses where a taxpayer is protected against incurring an economic loss in a venture.

-- Certain deductions made use of in tax shelter ventures, such as real estate construction period interest and taxes are modified.

-- The minimum tax is expanded and made applicable to more taxpayers.

These provisions deal adequately with most tax shelter abuses and will reduce investment in uneconomic activities solely to receive favorable tax benefits. These provisions apply to investments by non-corporate taxpayers in real estate, farming, oil and gas, movies and equipment leasing. A general "catch-all" provision applicable only to partnerships will help to prevent the proliferation of innovative tax shelter techniques.

The tax bill also contains other significant provisions which serve to reduce the tax loopholes often employed by high-income individuals. These include the capitalization of prepaid interest, a limitation on the amount of investment interest that can be deducted, the capitalization of partnership syndication and organization expenses, the clarification of the tax treatment of an allocation of a full year's losses of a partnership to partners admitted at the year end and a special allocation of a disproportionate amount of losses to those partners who receive the greatest tax benefit from them, and special depreciation recapture rules for sports franchises.

Capital Formation. The tax bill contains provisions specifically designed to encourage industry to expand their investment in new machinery and equipment. These include:

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-- The extension of the 10 percent investment tax credit through 1980.

-- A more liberal rule on the use of investment tax credit carryovers -- the so-called First-in-First-out (FIRO) rule.

-- An additional 1 percent investment tax credit and an additional 0.5 percent credit for matching employee contributions to an employee stock ownership plan ("ESOP"). The provision applies through 1980.

-- Liberal investment tax credit provisions for the shipping, railroad and the airline industry.

-- Modification of the tax rules to prevent profitable companies from buying unprofitable companies to obtain net operating loss carryovers.

-- The treatment of contributions in aid of construction of water and sewage facilities as contributions to capital, rather than taxable income.

<u>Estate and Gift Tax Provisions</u>. The tax bill contains important modifications in the Federal estate and gift tax laws, which will provide taxpayers with much needed relief.

-- The present $60,000 estate tax exemption is changed to a credit equivalent to a $175,000 exemption. The increase will be phased-in over a 5 year period.

-- The marital deduction allowed for interspousal transfers is substantially increased.

-- An extended estate tax payment period is provided for estate taxes attributable to farms and small businesses.

-- Real property used for farming or closely-held business purposes may be specially valued on the basis of its current use, rather than its highest value.

-- The basis of property held by a decedent and transferred to his heirs will be increased to its value on December 31, 1976 or $60,000, whichever is greater. The "step-up" in basis to the value of the property at the time of the decedent's death as provided by present law is eliminated.

-- Generation-skipping transfers that occurred after April 30, 1976 are generally subject to estate tax. A $250,000 exclusion is provided for transfers to grandchildren.

<u>Individual Income Tax Cuts</u>. The tax bill extends through December 31, 1977 the per capita tax credit -- applicable to all taxpayers -- and the refundable earned income credit -- applicable only to low-income families -- provided by the Revenue Adjustment Act of 1975. The tax bill also makes permanent the increase in the standard deduction to a maximum of $2,400 for single returns and $2,800 for joint returns provided by the Revenue Adjustment Act of 1975.

<u>Corporate Tax Cuts</u>. The tax bill extends through December 31, 1977 the reduction in the corporate tax rates and the increase in the surtax exemption to $50,000 which provide the greatest benefit to small corporations.

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Taxation of Foreign Income of United States Taxpayers. The tax bill substantially revises the tax provisions governing the taxation of income earned abroad by United States taxpayers.

-- The tax benefits of Domestic International Sales Corporations ("DISCs") are reduced by one-third. The DISC benefits are limited to export sales which exceed sales in a prescribed base period.

-- Foreign source income attributable to boycott related activity will lose the tax benefits of the foreign tax credit, DISC, and the deferral of United States tax on foreign source income. Boycott related activity consists of:

° Discrimination on the basis of nationality, religion or race in terms of hiring or selecting employees, managers or directors;

° Participation in a "secondary" boycott, i.e., a company agrees to refuse to do business with a specified country; and

° Participation in a "tertiary" boycott, i.e., a company agrees to refuse to do business with other companies which do business with a specified country.

-- Foreign bribe payments are deemed distributions to the United States parent corporation and do not reduce the earnings and profits of the foreign subsidiary.

-- Present law is modified to allow a United States citizen married to a non-resident alien to file a joint return.

-- The exemption from United States tax of interest paid to a non-resident alien or a foreign corporation on United States bank deposits is made permanent.

-- The amount of foreign taxes allowable as a credit with respect to foreign oil and gas extraction income is limited to 48%, rather than 50% as provided by present law.

Social Security Account Numbers. The tax bill expands the use of social security numbers. They may now be used by any State or political subdivision for tax administration, drivers' licenses, motor vehicle registration or for locating runaway parents.

Disclosure of Tax Return Information. The tax bill prescribes specific limitations on the disclosure of tax information to Congress, the White House, and to Federal, State and local agencies.

Private Letter Rulings. The tax bill mandates that Internal Revenue Service determinations issued after November 1, 1976 be made public. However, names and other identifying details are not required to be disclosed.

Capital Gains and Losses. The tax bill increases from $1,000 to $3,000 the amount of ordinary income against which capital losses may be offset and also increases from six months to one year the minimum holding period necessary to quality for capital gains treatment. Both modifications will be phased-in over a two year period.

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Minimum Tax for Corporations. The tax bill increases the corporate minimum tax to 15% and reduces the exemption to the greater of $10,000 or regular taxes. The tax bill also eliminates the current provision that allows a corporation to carry forward for up to seven years any regular taxes that are not used to offset preferences in the current year.

Individual Income Tax Provisions. The tax bill contains several measures which will simplify the task of individuals in preparing their Federal income tax returns. The tax bill also expands certain individual tax benefits.

-- The optional tax tables for computing tax liability are simplified and made available to more taxpayers.

-- The retirement income credit is greatly simplified. The maximum amount on which the credit is computed is expanded, while the reduction in the eligible base attributable to earned income is reduced.

-- The present exclusion from income of certain sick pay payments is repealed.

-- Deductions for the business use of a taxpayer's home and the rental of a vacation home are restricted.

-- The deductibility of expenses for attendance at foreign conventions are subject to specific limitations.

-- The special tax rules of present law governing the tax treatment of qualified stock options are repealed.

-- The present deduction for child care expenses is converted to a credit and substantially expanded.

-- The present deduction for moving expenses is liberalized.

-- The deduction for alimony payments is converted to a deduction from gross income -- a so-called "above-the-line" deduction.

Miscellaneous Provisions.

-- Employer contributions to and services received by an employee from a prepaid legal service plan are not taxable income to an employee.

-- Tax benefits are provided for the rehabilitation of, and tax advantages denied to taxpayers who demolish, certified historic structures.

-- The tax-free transfer of appreciated property to exchange funds established as partnerships or trusts is prohibited.

-- Public charities (other than churches) are permitted to lobby, provided that certain expenditure tests are satisfied.

-- The tax treatment of options is modified. Gain from the sale of an option and gain or loss from a closing transaction in options is treated as short-term capital gain or loss.

-- The tax rules governing the treatment of subchapter S corporations are liberalized to provide more flexibility in the organization of the corporation.

-- An accelerated deduction is provided companies for the cost of removing architectural or other barriers to handicapped or elderly persons.

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