MEMORANDUM

From: Finance Committee Tax Staff
Date: December 16, 2005
Re: Summary of Senate Amendment to H.R. 4440

Creates additional tax-exempt bond authority to help rebuild devastated infrastructure in the GO Zone. Provides Louisiana, Mississippi and Alabama the authority to issue a special class of private activity bonds, called GO Zone Bonds, outside of the state volume caps. Bond authority is approximately $7.9 billion for Louisiana, $4.8 billion for Mississippi and $2.1 billion for Alabama. These amounts are based on each State's population in the Zone, according to 2004 U.S. Census estimates. GO Zone Bonds can be issued by States and municipalities. Bond proceeds can be used to pay for acquisition, construction, and renovation of nonresidential real property, qualified low-income residential rental housing, single-family residential housing, and public utility property (e.g., gas, water, electric and telecommunication lines) located in the Zone. The current low-income housing targeting rules are relaxed so that more bond proceeds can be used to rebuild housing in the Zone. Up to $150,000 of GO Zone mortgage revenue bonds may be used to repair homes (as opposed to $15,000 under current law). In addition, the first-time homebuyer rule is waived. Interest payments on the bonds are not subject to the AMT. The authority to issue GO Zone Bonds expires after December 31, 2010. *Cost: $1.55 billion over ten years.*

Additional Advance Refunding for Bonds. Provides States and municipalities in the Katrina Go Zone with one additional advance refunding before January 1, 2011 for certain governmental bonds (including 501(c)(3) bonds). Also provides one advance refunding for certain private activity bonds used to finance airports, docks, and wharves. The additional authorization is up to $4.5 billion for Louisiana, $2.25 billion for Mississippi and $1.125 billion for Alabama. The provisions also applies to 501(c)(3) bonds prior to January 1, 2011. Advance refunding allows the bond issuer to restructure eligible debt by refinancing at a lower rate or spreading interest payments over a longer period of time. *Cost: $741 million over ten years.*

Expands Access to Low-Income Housing. Under current law, States receive allocations of low-income housing tax credits based on population. The provision allows States to allocate volumes of additional housing credit amounts amount in years 2006 to 2008 of $18 per person in the Zone as measured by 2004 population data. This will provide approximately $70 million for Louisiana, $37 million for Mississippi and $17 million for Alabama. The provision also increases the otherwise applicable housing credit ceiling amount for Florida and Texas by $3.5 million per state for 2006. Additionally, the Gulf Opportunity Zone, the Rita GO Zone, and the Wilma Go Zone will be treated as difficult development areas, allowing investors to calculate credits for a project on an amount equal to 130 percent of new construction or rehabilitation expenditures.

Provides 50-percent bonus depreciation to help businesses rebuild in the Zone. Permits businesses to claim an additional first-year depreciation deduction equal to 50 percent of the cost of new property investments made in the Zone. The additional deduction applies to purchased computer software, leasehold improvements, certain commercial and residential real estate expenditures and equipment. All depreciation deductions (including bonus depreciation) would be exempt from the AMT. The provision applies to property placed in service through December 31, 2007 (December 31, 2008 for real property). In addition, the Department of Treasury would be granted authority to extend the 2003 bonus depreciation deadline for placing long-lived property in service in certain circumstances for the Gulf Opportunity Zone, Rita Zone or Wilma Zone for up to one year.

Increase in Expensing for Small Businesses. Current law permits certain small businesses to deduct up to $100,000 of the cost of property used in the business. The provision would double this amount to $200,000 for qualifying expenditures made in the disaster area through 2007. This provision would also increase the level of investment at which benefits phase out from $400,000 to $1 million of qualifying purchases, thus allowing more businesses to use this tax benefit in rebuilding. This provision applies to all property placed in service in the Gulf Opportunity Zone after August 27, 2005 through 2007.

Partial Expensing for Demolition and Cleanup Costs. Under the provision, 50 percent of the costs (that would otherwise be capitalized) related to site cleanup and demolition would be deductible by businesses. Effective for amounts paid or incurred after August 27, 2005 through 2007. *Cost: $105 million over ten years.*

Expensing to Promote Cleanup of Brownfields. The provision extends the deductibility of costs of cleaning up Brownfields in the Katrina GO Zone for 2 years and allows expensing for the cleanup of petroleum products in the Katrina GO Zone. Effective for expenditures paid or incurred after August 27, 2005 through 2007. *Cost: $48 million over ten years.*

Increase in Rehabilitation Credit for Gulf Opportunity Zone Projects. The rehabilitation credit is raised from 1 percent to 13 percent of qualified expenditures for any qualified rehabilitated building other than a certified historic structure. It also raises the credit from 20 percent to 26 percent of qualified expenditures for any certified historic structure. *Cost: $78 million over ten years.*

Increased Expensing and NOL Carryback for Qualified Timber Property. Under current law, taxpayers may only deduct $10,000 of reforestation cost. The amendment raises the limit to $20,000 and allows losses to be carried back for 5 years, rather than the current 2-year carryback. The provision only applies to taxpayers owning less than 500 acres of timber in the Katrina (effective on 8/27/05), Rita (effective on 9/23/05), and Wilma (effective on 10/23/05) Zones. The increase in reforestation expensing limit is available for expenditures incurred prior to January 1, 2008. *Cost: Less than $1 million over ten years.*

Public Utility Casualty Loss Carryback. Taxpayers with casualty losses associated with public utility property caused by Hurricane Katrina can elect to carryback a net operating loss attributable to certain casualty losses 10 years. *Cost: $71 million over ten years.*

Net Operating Loss Carryback. The provision extends the net operating loss carryback period from 2 to 5 years for net operating losses attributable to (i) new investment and repairing existing investment in the areas damaged by Hurricane Katrina; (ii) business casualty losses caused by Hurricane Katrina; and (iii) moving expenses and temporary housing expenses for employees working in areas damaged by Hurricane Katrina. Provision is effective on date of enactment.

Gulf Tax Credit Bonds. Authorizes Gulf Opportunity Zone States to issue debt service tax credit bonds providing credits against Federal income tax instead of interest payments, so that these States can provide assistance to communities unable to meet their debt service requirements as a result of the hurricanes. Bonds would be required to mature before January 1, 2008. At least 95 percent of bond proceeds must be used to redeem or to pay principal, interest or premiums on outstanding bond, and such proceeds so used must be matched by an equal amount of State funds. The allocation of bonds per State would be $200 million for Louisiana, $100 million for Mississippi and $50 million for Alabama. *Cost: $57 million over ten years.*

New Markets Tax Credit. Allow an additional $300 million in 2005 and 2006 and an additional $400 million in 2007 for New Markets Tax Credit (NMTC) authority for community development entities (CDEs) operating in the Gulf Opportunity Zone. A NMTC allows businesses investing in low-income communities lacking access to capital to take a 39% tax credit over seven years for investments in qualified community development entities. *Cost: $387 million over ten years.*

Income Eligibility for Qualified Residential Rental Project Requirement. Allow operators of qualified residential rental projects to rely on the representations of prospective tenants displaced by Hurricane Katrina for purposes of determining whether the individuals satisfy the income limitations for qualified rental projects. Individual's tenancy must begin during the six-month period beginning on the date the individual was displaced by Hurricane Katrina. *Cost: Negligible revenue effect.*

Public Utility Disaster Loss Carryback. Allow public utilities to elect to treat casualty losses associated with public utility property caused by Hurricane Katrina as having occurred 5 years prior to the disaster. *Cost: $24 million over ten years.*

Employee Retention Credit: The *Katrina Emergency Tax Relief Act of 2005* (P.L. 109-73) provided a 40 percent tax credit for wages paid up to $6,000 if paid after August 28, 2005, and before December 31, 2005, by employers located in the Katrina GO Zone who continue to pay their employees while their business is inoperable. The provision modifies the tax credit so that the provision applies to Katrina, Rita and Wilma Zones without regard to the size of the employer. *Cost: $114 million over ten years.*

Tax benefits not available with respect to certain property. The provisions relating to additional first-year depreciation, increased expensing, and the five-year carryback of NOLs attributable to casualty losses, depreciation, or amortization do not apply with respect to certain property. Specifically, the provisions do not apply with respect to any private or commercial golf course, country club, massage parlor, hot tub facility, suntan facility, or any store the principal business of which is the sale of alcoholic beverages for consumption off premises. The provisions also do not apply with respect to any property used directly in connection with gambling, animal racing, or the on-site viewing of such racing, and with respect to buildings or portions of buildings dedicated to such activities (except if the portion so dedicated is less than 100 square feet).

Hope Scholarship and Lifetime Learning Credit. Current law allows a Hope Scholarship Credit in the first two years of postsecondary education equal to100% of the first $1,000 of qualified tuition and related expenses, and 50% of the next $1,000 for a maximum of $1,500. There is also a Lifetime Learning Credit available to students enrolled in one or more courses at the undergraduate or graduate level (whether or not pursuing a degree), equal to 20% of the first $10,000 in qualified tuition and related expenses. The provision doubles the Hope Credit dollar amounts so the maximum credit would be $3,000, and doubles the Lifetime Learning Credit percentage from 20% to 40%, for a maximum Lifetime Learning Credit of $4,000 for students attending undergraduate or graduate institutions in the Gulf Opportunity Zone. Room and board, books and fees would also be considered qualified expenses. Applies to tax years 2005 and 2006. *Cost: $55 million over ten years.*

Employer-Provided Housing and Employer Tax Credit. Allows an employee to exclude from gross income up to $600 per month for lodging provided by his or her employer located in the Katrina Go Zone. Provides a credit to the employer equal to 30% of the amount which is excludable from the gross income of the qualified employee. Applies to lodging provided beginning on the first day of the first month beginning after the date of enactment and ending on the date which is 6 months after that date. *Cost: $246 million over ten years.*

Early Withdrawals from Retirement Plans for Hurricanes Rita and Wilma. Present law discourages distributions from tax-preferred retirement plans with penalties and other limitations. The provision waives the 10 percent penalty tax for premature distributions from IRAs and qualified retirement plans for individuals who suffered an economic loss because of Rita or Wilma and whose principal residence is located in the Rita or Wilma disaster areas. Individuals eligible for this waiver would be permitted to pay income tax on such distributions ratably over a three-year period. Amounts distributed could be re-contributed to a qualified retirement plan over the three-year period following the distribution date and receive rollover treatment. The waiver of the 10 percent penalty, 3-year income averaging and recontribution provisions for retirement plan withdrawals will be limited to $100,000 per individual. Distributions for home purchases which were not finalized because of Hurricanes Rita or Wilma could also be re-contributed to a qualified retirement plan or IRA. Limitations on loans from qualified employer plans would be increased for Hurricane Rita and Hurricane Wilma victims by doubling the thresholds to the lesser of $100,000 or 100 percent of the individual's account balance. Payments due from hurricane victims on qualified plan loans on or after August 25, 2005, and before January 1, 2007, could be deferred, and twelve months could be added to the maximum repayment period of affected loans. *Cost: $174 million over ten years.*

Corporate Charitable Contributions Relief for Hurricanes Rita and Wilma. The amount allowed as a charitable deduction for a corporation in any taxable year may not exceed 10 percent of the corporation's taxable income. The provision temporarily waives limits regarding charitable cash contributions for Rita and Wilma relief. The provision is effective for contributions before January 1, 2006. *Cost: $91 million over ten years.*

Casualty Loss Provision. Under present law, non-business casualty losses are deductible by taxpayers who itemize only to the extent they exceed 10 percent of adjusted gross income and a $100 floor. In some circumstances, taxpayers are permitted to include a current-year casualty loss on an amended prior year return. The provision eliminates the 10 percent and $100 floor for casualty losses resulting from Hurricanes Rita (after 9/23/05) or Wilma (after 10/23/05) and incurred in the disaster area, including those claimed on amended returns. *Cost: $1.2 billion over ten years.*

Gulf Coast Recovery Bonds. Expresses the sense of Congress that one or more series of savings bonds should be designated as "Gulf Coast Recovery Bonds."

Combat Pay Treated as Earned Income for Purposes of the Earned Income Tax Credit (EIC). Pursuant to the *Working Families Tax Relief Act of 2004* (P.L. 108-311), combat pay may count as income for purposes of calculating the EITC. The provision expires in 2005. The Senate amendment extends the provision through 2006. *Cost: $14 million over ten years.*

Interest Suspension: The *Internal Revenue Service Restructuring and Reform Act of 1998* (P.L. 105-206) required IRS to suspend interest on tax deficiencies determined more than 18 months after the due date of the return. In the *American Jobs Creation Act of 2004* (P.L. 108-357), the suspension was eliminated for interest accrued after October 3, 2004 on deficiencies resulting from certain tax shelters. This provision expands this to pre-October 3, 2004 interest, completely eliminating the interest suspension on certain tax shelters. It contains a carve out for taxpayers participating in the IRS global tax shelter settlement initiative and also gives the Secretary exception authority in cases of reasonable cause and good faith. The provision eliminates interest suspension on tax due amended returns. The provision generally applies as if included in the AJCA; the amended return provision applies to documents filed after the date of enactment. *Raises: $50 million over ten years.*

One-year Extension of Authority for Undercover Operations. This provision extends through 2006 IRS authority to use the income earned by an undercover operation to pay additional expenses incurred in the undercover operation. Surpluses are required to be deposited into the General Fund and the IRS must conduct a detailed financial audit of such undercover operations and provide an annual audit report to the Congress on all such undercover operations. *Raises: Less than $500,000 over ten years.*

Disclosures to Facilitate Combined Employment Tax Reporting. Extends through 2006 IRS authority to disclose taxpayer identity information and signatures to States to allow for the filing of a federal employment tax form to be used by the appropriate state (thus eliminating the taxpayer's requirement to file a separate form with the state). *Provision has no revenue effect.*

Disclosures Relating to Terrorist Activities. Extends through 2006 authority to disclose confidential tax information to certain Federal law enforcement agency and Federal intelligence agency officers and employees for purposes of investigating terrorist incidents, threats, or activities and for analyzing intelligence concerning such activities. *Provision has no revenue effect.*

Disclosures Relating to Student Loans. Extends through 2006 authority to disclose certain taxpayer information (i.e., taxpayer name, mailing address, taxpayer identifying number, filing status and adjusted gross income) to the Department of Education needed by the Department to determine income contingent repayment of student loans. *Provision has no revenue effect.*

Tax Technical Corrections. These provisions are technical corrections needed with respect to the *American Jobs Creation Act of 2004*, and other enacted tax legislation. The initial version of technical corrections was introduced as S. 3019, the *Tax Technical Corrections Act of 2004*, in the 108th Congress, and a second version was introduced on as S. 1447, the *Tax Technical Corrections Act of 2005*. In both cases, the Committee on Ways and Means Chairman Bill Thomas introduced companion measures, H.R. 5395 and H.R. 3376. The Senate Finance Committee and the Committee on Ways and Means, in consultation with the Joint Committee on Taxation and the Department of the Treasury, are continuing to assess proposals for other technical corrections which may be needed to achieve congressional intent. *Provisions have no revenue effect.*

Trade Technical Correction. Makes technical correction to regional value-content methods for rules of origin lender under Public Law 109-53. *Provision has no revenue effect.*

Emergency Requirement. Clarifies that all effects on revenue from the provisions contained in the Senate Substitute fall under the emergency requirement of the Budget Reconciliation Act and do not affect net Budget totals.