Joint Committee on Taxation
October 1, 2003
JCX-87-03

ADDITIONAL MODIFICATIONS TO THE CHAIRMAN'S MARK OF S. 1637, THE "JUMPSTART OUR BUSINESS STRENGTH ('JOBS') ACT," SCHEDULED FOR MARKUP BY THE SENATE COMMITTEE ON FINANCE ON OCTOBER 1, 2003[1]

The following additional proposals would be included in the Chairman's Mark:

A. Increase Section 179 Expensing

Present Law

Present law provides that, in lieu of depreciation, a taxpayer with a sufficiently small amount of annual investment may elect to deduct such costs. The Jobs and Growth Tax Relief Reconciliation Act (JGTRRA) of 2003[2] increased the amount a taxpayer may deduct, for taxable years beginning in 2003 through 2005, to $100,000 of the cost of qualifying property placed in service for the taxable year.[3] In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. The $100,000 amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable year exceeds $400,000. Prior to the enactment of JGTRRA (and for taxable years beginning in 2006 and thereafter) a taxpayer with a sufficiently small amount of annual investment may elect to deduct up to $25,000 of the cost of qualifying property placed in service for the taxable year. The $25,000 amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable

[1] This document may be cited as Joint Committee on Taxation, *Additional Modifications to the Chairman's Mark of S. 1637, the "Jumpstart Our Business Strength ('JOBS') Act," Scheduled for Markup by the Senate Committee on Finance on October 1, 2003* (JCX-87-03), October 1, 2003.

[2] Pub. Law No. 108-27, sec. 202 (2003).

[3] Additional section 179 incentives are provided with respect to a qualified property used by a business in the New York Liberty Zone (sec. 1400(f)) or an empowerment zone (sec. 1397A).

year exceeds $200,000. In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business.

The amount eligible to be expensed for a taxable year may not exceed the taxable income for a taxable year that is derived from the active conduct of a trade or business (determined without regard to this provision). Any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding taxable years (subject to similar limitations). No general business credit under section 38 is allowed with respect to any amount for which a deduction is allowed under section 179.

Description of Proposal

The proposal provides that the $100,000 amount ($25,000 for taxable years beginning in 2006 and thereafter) is reduced (but not below zero) by only one half of the amount by which the cost of qualifying property placed in service during the taxable year exceeds $400,000 ($200,000 for taxable years beginning 2006 and thereafter).

Effective Date

The proposal is effective for taxable years beginning after December 31, 2002.

B. Three-Year Carryback of Net Operating Losses

Present Law

A net operating loss ("NOL") is, generally, the amount by which a taxpayer's allowable deductions exceed the taxpayer's gross income. A carryback of an NOL generally results in the refund of Federal income tax for the carryback year. A carryforward of an NOL reduces Federal income tax for the carryforward year.

In general, an NOL may be carried back two years and carried forward 20 years to offset taxable income in such years.[4] Different rules apply with respect to NOLs arising in certain circumstances. For example, a three-year carryback applies with respect to NOLs (1) arising from casualty or theft losses of individuals, or (2) attributable to Presidentially declared disasters for taxpayers engaged in a farming business or a small business. A five-year carryback period applies to NOLs from a farming loss (regardless of whether the loss was incurred in a Presidentially declared disaster area). Special rules also apply to real estate investment trusts (no carryback), specified liability losses (10-year carryback), and excess interest losses (no carryback to any year preceding a corporate equity reduction transaction).

The alternative minimum tax rules provide that a taxpayer's NOL deduction cannot reduce the taxpayer's alternative minimum taxable income ("AMTI") by more than 90 percent of the AMTI (determined without regard to the NOL deduction).

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[4] Sec. 172.

Section 202 of the Job Creation and Worker Assistance Act of 2002[5] ("JCWAA") provided a temporary extension of the general NOL carryback period to five years (from two years) for NOLs arising in taxable years ending in 2001 and 2002. In addition, the five-year carryback period applies to NOLs from these years that qualify under present law for a three-year carryback period (i.e., NOLs arising from casualty or theft losses of individuals or attributable to certain Presidentially declared disaster areas).

A taxpayer can elect to forgo the five-year carryback period. The election to forgo the five-year carryback period is made in the manner prescribed by the Secretary of the Treasury and must be made by the due date of the return (including extensions) for the year of the loss. The election is irrevocable. If a taxpayer elects to forgo the five-year carryback period, then the losses are subject to the rules that otherwise would apply under section 172 absent the provision.[6]

JCWAA also provided that an NOL deduction attributable to NOL carrybacks arising in taxable years ending in 2001 and 2002, as well as NOL carryforwards to these taxable years, may offset 100 percent of a taxpayer's AMTI.[7]

Description of Proposal

The proposal provides for a three-year carryback of NOLs for NOLs arising in taxable years ending in 2003.[8]

The proposal also allows an NOL deduction attributable to NOL carrybacks arising in taxable years ending in 2003 as well as NOL carryforwards to these taxable years, to offset 100 percent of a taxpayer's AMTI.

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[5] Pub. Law No. 107-147.

[6] Because JCWAA was enacted after some taxpayers had filed tax returns for years affected by the provision, a technical correction is needed to provide for a period of time in which prior decisions regarding the NOL carryback may be reviewed. Similarly, a technical correction is needed to modify the carryback adjustment procedures of sec. 6411 for NOLs arising in 2001 and 2002. These issues were addressed in a letter dated April 15, 2002, sent by the Chairmen and Ranking Members of the House Ways and Means Committee and Senate Finance Committee, as well as in guidance issued by the IRS pursuant to the Congressional letter (Rev. Proc. 2002-40, 2002-23 I.R.B. 1096, June 10, 2002).

[7] Section 172(b)(2) should be appropriately applied in computing AMTI to take proper account of the order that the NOL carryovers and carrybacks are used as a result of this provision. *See* section 56(d)(1)(B)(ii).

[8] Because certain taxpayers may have already filed tax returns (or be in the process of filing tax returns) for taxable years ending in 2003, the proposal contains special rules to provide until November 1, 2003 in which prior decisions regarding the NOL carryback may be reviewed by taxpayers.

Effective Date

The three-year carryback proposal is effective for net operating losses generated in taxable years ending in 2003. The proposal relating to AMTI is effective for NOL carrybacks arising in, and NOL carryforwards to, taxable years ending in 2003.

C. Qualified Tax Collection Contracts

Present Law

In fiscal years 1996 and 1997, the Congress earmarked $13 million for IRS to test the use of private debt collection companies. There were several constraints on this pilot project. First, because both IRS and OMB considered the collection of taxes to be an inherently governmental function, only government employees were permitted to collect the taxes.[9] The private debt collection companies were utilized to assist the IRS in locating and contacting taxpayers, reminding them of their outstanding tax liability, and suggesting payment options. If the taxpayer agreed at that point to make a payment, the taxpayer was transferred from the private debt collection company to the IRS. Second, the private debt collection companies were paid a flat fee for services rendered; the amount that was ultimately collected by the IRS was not taken into account in the payment mechanism.

The pilot program was discontinued because of disappointing results. GAO reported[10] that IRS collected $3.1 million attributable to the private debt collection company efforts; expenses were also $3.1 million. In addition, there were lost opportunity costs of $17 million to the IRS because collection personnel were diverted from their usual collection responsibilities to work on the pilot.

The IRS has in the last several years expressed renewed interest in the possible use of private debt collection companies; for example, IRS recently revised its extensive Request for Information concerning its possible use of private debt collection companies.[11]

In general, Federal agencies are permitted to enter into contracts with private debt collection companies for collection services to recover indebtedness owed to the United States.[12] That provision does not apply to the collection of debts under the Internal Revenue Code.[13]

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[9] Sec. 7801(a).

[10] GAO/GGD-97-129R Issues Affecting IRS' Collection Pilot (July 18, 1997).

[11] TIRNO-03-H-0001 (February 14, 2003), at www.procurement.irs.treas.gov. The basic request for information is 104 pages, and there are 16 additional attachments.

[12] 31 U.S.C. sec. 3718.

[13] 31 U.S.C. sec. 3718(f).

On February 3, 2003, the President submitted to the Congress his fiscal year 2004 budget proposal,[14] which proposed the use of private debt collection companies to collect Federal tax debts.

Description of Proposal

The proposal permits the IRS to use private debt collection companies to locate and contact taxpayers owing outstanding tax liabilities[15] of any type[16] and to arrange payment of those taxes by the taxpayers. Several steps are involved. First, the private debt collection company contacts the taxpayer by letter.[17] If the taxpayer's last known address is incorrect, the private debt collection company searches for the correct address. Second, the private debt collection company telephones the taxpayer to request full payment.[18] If the taxpayer cannot pay in full immediately, the private debt collection company offers the taxpayer an installment agreement providing for full payment of the taxes over a period of as long as three years. If the taxpayer is unable to pay the outstanding tax liability in full over a three-year period, the private debt collection company obtains financial information from the taxpayer and will provide this information to the IRS for further processing and action by the IRS.

The proposal specifies several procedural conditions under which the provision would operate. First, provisions of the Fair Debt Collection Practices Act apply to the private debt collection company. Second, taxpayer protections that are statutorily applicable to the IRS are also made statutorily applicable to the private sector debt collection companies. Third, the private sector debt collection companies are required to inform taxpayers of the availability of assistance from the Taxpayer Advocate. Fourth, subcontractors are prohibited from having

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[14] *See* Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2004* (H. Doc. 108-3, Vol. I), p. 274.

[15] There must be an assessment pursuant to section 6201 in order for there to be an outstanding tax liability.

[16] The bill generally applies to any type of tax imposed under the Internal Revenue Code. It is anticipated that the focus in implementing the provision will be: (a) taxpayers who have filed a return showing a balance due but who have failed to pay that balance in full; and (b) taxpayers who have been assessed additional tax by the IRS and who have made several voluntary payments toward satisfying their obligation but have not paid in full.

[17] Several portions of the provision require that the IRS disclose confidential taxpayer information to the private debt collection company. Section 6103(n) permits disclosure for "the providing of other services ... for purposes of tax administration." Accordingly, no amendment to 6103 is necessary to implement the provision. It is intended, however, that the IRS vigorously protect the privacy of confidential taxpayer information by disclosing the least amount of information possible to contractors consistent with the effective operation of the provision.

[18] The private debt collection company is not permitted to accept payment directly. Payments are required to be processed by IRS employees.

contact with taxpayers, providing quality assurance services, and composing debt collection notices; any other service provided by a subcontractor must receive prior approval from the IRS.

The proposal creates a revolving fund from the amounts collected by the private debt collection companies. The private debt collection companies will be paid out of this fund. The bill prohibits the payment of fees for all services in excess of 25 percent of the amount collected under a tax collection contract.[19]

Effective Date

The proposal is effective on the date of enactment.

[19] It is assumed that there will be competitive bidding for these contracts by private sector tax collection agencies and that vigorous bidding will drive the overhead costs down.