Certain Temporary Tax Provisions Scheduled to Expire in 2009 (“Extenders”)

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Summary

Numerous temporary tax provisions expired on December 31, 2009. Often referred to as "extenders," these provisions were originally enacted with expiration dates that have subsequently been extended, in some cases numerous times. The temporary nature of extenders can be considered useful as it allows policymakers to evaluate the effectiveness of the provisions on a regular basis. If an extender is found to be ineffective, its scheduled expiration allows several policymaking options, including allowing the provision to expire or redesigning the provision to improve its use as a policy tool. However, policymakers have, for the most part, considered the extenders as a group during the enactment process, and have not reviewed the unique strengths and weaknesses of specific provisions.

In the 111th Congress, a provision for the extension of certain expiring provisions was included in the House and Senate Budget Resolution (S.Con.Res. 13). The conference report for S.Con.Res. 13 was passed by both chambers on April 29, 2009. The House passed a package of expiring provisions, the *Tax Extenders Act of 2009* (H.R. 4213) on December 9, 2009. On March 1, 2010, the Senate officially began consideration of H.R. 4213. A Senate proposal, offered as a substitute amendment by Senate Finance Committee Chair Max Baucus and Senate Majority Leader Harry Reid, offered substitute text for H.R. 4213 that would be Title I, Extension of Expiring Provisions, in the proposed *American Workers, State, and Business Relief Act of 2010.* On March 10, 2010, the Senate passed H.R. 4213, which added several relatively low-cost tax extenders to the House-passed H.R. 4213. On May 28, 2010, the House voted 215 to 204 to pass a revised H.R. 4213 titled the *American Jobs and Closing Tax Loopholes Act*. The Joint Committee on Taxation estimates that the extension of 62 expiring provisions will cost $31.619 billion from FY2010 to FY2020. On June 24, 2010, Senator Reid was unable to invoke closure after three votes; consequently, he tabled the bill. In September, Congress is expected to reconsider the package of tax extenders.

This report's analysis of extenders considers the degrees to which extenders are actually temporary tax provisions and the tax benefits of an extender; the analysis examines efficiency, equity, and simplicity features.

Some tax extenders, which expired on December 31, 2009, are examined in this report. These extenders include the following tax credits: the tax credit for holders of qualified zone academy bonds, the tax credit for first-time homebuyers in the District of Columbia, the tax credits for research and experimentation expenses, the New Markets Tax Credit, the possession tax credit with respect to American Samoa, and a credit for certain expenditures for maintaining railroad tracks. The extenders include the following deductions: expenses for elementary and secondary school teachers; tuition expenses; corporate charitable contributions of computer technology, food inventory, and books; contributions of capital gain real property made for conservation; and state and local sales taxes. Also depreciation allowances are included for qualified leasehold and restaurant improvements, for property on Indian reservations, and a seven-year recovery period for motor sports entertainment complexes. Other temporary tax provisions include tax incentives for investment in the District of Columbia, an increased "cover over" of tax on distilled spirits from Puerto Rico and the U.S. Virgin Islands, penalty-free withdrawals from individual retirement plans (IRAs) for individuals called to active duty or for charitable giving, and mortgage revenue bonds for veterans.

This report will be updated as warranted by legislative events.

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Introduction

Numerous temporary tax provisions exist in the tax code. Often referred to as "extenders," these provisions were originally enacted with an expiration date that has then been temporarily extended, in some cases numerous times.[1]

Division C of P.L. 110-343, the Tax Extenders and Alternative Minimum Tax Relief Act of 2008 (which was included with the Emergency Economic Stabilization Act; EESA) was signed into law on Friday, October 3, 2008, retroactively extending the most recent set of temporary tax provisions for individuals and businesses that had expired in December 2007. The provisions were then scheduled to expire after December 31, 2009.

Prior to the extensions enacted in the 110th Congress, a majority of the temporary tax provisions had been extended by the Tax Relief and Health Care Act of 2006 (P.L. 109-432; TRHCA).

The extenders provided special tax treatment for certain types of activities and investment; they benefitted both individuals and corporations. The extenders included credits, deductions, and other provisions.

The tax credit extenders, which expired on December 31, 2009, include the tax credit for holders of qualified zone academy bonds, the tax credit for first-time homebuyers in the District of Columbia, the tax credit for research and experimentation expenses, the New Markets Tax Credit, the possession tax credit with respect to American Samoa, and a credit for certain Expenditures for Maintaining Railroad Tracks.

The deduction tax extenders, which also expired on December 31, 2009, include deductions for elementary and secondary school teachers; tuition expenses; corporate charitable contributions of computer technology, food inventory, and books; contributions of capital gain real property made for conservation; and state and local sales taxes. Also included are depreciation allowances for qualified leasehold and restaurant improvements, for property on Indian reservations, and a seven-year recovery period for motor sports entertainment complexes.

Other temporary tax provisions, expiring on December 31, 2009, include tax incentives for investment in the District of Columbia, an increased "cover over" of tax on distilled spirits from Puerto Rico and the U.S. Virgin Islands, an excise tax to induce parity in the application of certain mental health benefits, penalty-free withdrawals from individual retirement plans (IRAs) for individuals called to active duty or for charitable giving, and mortgage revenue bonds for veterans.

Legislation in the 111th Congress

In the 111th Congress, provision for the extension of certain expiring provisions has been included in the House and Senate Budget Resolution (S.Con.Res. 13). On December 9, 2009, the House

[1] See **Appendix** for a list of tax extenders included in public laws over the past 10 years.

passed H.R. 4213, the *Tax Extenders Act of 2009*. The Joint Committee on Taxation (JCT) estimated that this bill included tax extenders that would cost $31.164 billion over 10 years.[2]

A Senate proposal, offered as a substitute amendment by Senate Finance Committee Chair Max Baucus and Senate Majority Leader Harry Reid, offered substitute text for H.R. 4213 that would be a tax extender title in the proposed American Workers, State, and Business Relief Act of 2010. On March, 2010, the Senate version of H.R. 4213 passed.[3] The Joint Committee on Taxation estimated that the extension of expiring provisions would cost $34.088 billion from 2010 to 2015 and $33.735 billion from 2010 to 2020.[4] The Senate-passed H.R. 4213 added several relatively low-cost tax provisions, but the main difference between these two bills is the use of different offsets to pay for the tax extenders. The main offset in the House bill was a $24.6 billion (over 10 years) provision to change the tax treatment of carried interest. The primary offsets in the Senate bill (over 10 years) were a $21.65 billion "black liquor" provision and a $5.474 billion provision codifying the economic substance doctrine.[5] But the black liquor tax credit was subsequently used as a revenue provision in the Patient Protection and Affordable Care Act (P.L. 111-148). Members negotiated to resolve the differences between the two bills.[6] Much of the debate about offsets concerned a proposal to tax carried interest as ordinary income rather than capital gains.[7]

On May 28, 2010, the House voted 215 to 204 to pass a revised H.R. 4213 titled the *American Jobs and Closing Tax Loopholes Act of 2010*. Reportedly, House Democrats are referred to this bill as a "jobs bill" rather than as an extenders bill.[8] The JCT estimates that the extension of 62 expiring provisions will cost $31.619 billion from FY2010 to FY2020.[9] This bill reflects numerous compromises by Representatives. Because of concern of many Representatives about the cost of the bill, an extension of federal assistance to states for Medicaid and tax subsidies for displaced workers to buy health insurance were eliminated. The Congressional Budget Office and the Joint Committee on Taxation estimate that the *American Jobs and Closing Tax Loopholes Act of 2010* would have resulted in a net change in deficits of $54.228 billion over FY2010-FY2020.[10] Some Representatives objected to taxing carried interest at ordinary income tax rates. The revised H.R. 4213 would have taxed 50% of carried interest at ordinary rates through

[2] Joint Committee on Taxation, *Estimated Revenue Effects of H.R. 4213, the "Tax Extenders Act of 2009,"* JCX-59-09, Dec. 7, 2009, pp. 1-4.

[3] Revenue provisions of this act are shown in tabular form in the following publication: Joint Committee on Taxation, *Estimated Revenue Effects of the Revenue Provisions Contained in the "American Workers, State and Business Relief Act of 2010, as Passed by the Senate on March 10, 2010*, JCX-9-10, March 10, 2010, 8 pp.

[4] For an explanation of these provisions, see Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions Contained in the "American Workers, State and Business Relief Act of 2010," as Passed by the Senate on March 10, 2010*, JCX-11-10, March 11, 2010.

[5] Joint Committee on Taxation, Publication JCX-9-10, p. 6.

[6] Heather M. Rothman and Brett Ferguson, Final Details Being Hashed Out on Tax Extenders Bill, Lawmakers Say, *Daily Tax Report*, May 7, 2010, p. G7.

[7] For an analysis of this issue, see CRS Report RS22717, *Taxation of Private Equity and Hedge Fund Partnerships: Characterization of Carried Interest*, by Donald J. Marples; and CRS Report RS22689, *Taxation of Hedge Fund and Private Equity Managers*, by Mark Jickling and Donald J. Marples.

[8] Brent Ferguson, "Carried Interest Tax Hike Passes House in Extenders Bill; Senate Outlook Unclear," *Daily Report for Executives*, June 1, 2010, p. GG2.

[9] Joint Committee on Taxation, "Estimated Budget Effects of the Revenue Provisions Contained in H.R. 4213, The American Jobs and Closing Tax Loopholes Act of 2010, Scheduled for Consideration by the House of Representatives," (JCX-29-10), pp. 2-6.

[10] Congressional Budget Office and the Joint Committee on Taxation, *Budgetary Effects of H.R. 4213, the American Jobs and Closing Tax Loopholes Act of 2010*, May 28, 2010, p. 2.

December 31, 2012, and beginning January 1, 2013, 75% of carried interest will be taxed at ordinary income tax rates.[11] The revised H.R. 4213 also added numerous foreign tax provisions as revenue offsets.[12]

On June 8, 2010, the Senate began consideration of the *American Jobs and Closing Tax Loopholes Act of 2010*. Senate Majority Leader Harry Reid was unable to invoke closure after three votes. The Republican leadership objected to some of the revenue offsets in the legislation.[13] Consequently, Senator Reid tabled the legislation.[14]

H.R. 4213 included a provision to extend unemployment insurance benefits. Only this provision was preserved in an amended H.R. 4213 cited as the *Unemployment Compensation Extension Act of 2010*. While the Democratic Party leadership supported the bill, the Republican Party leadership opposed it because its estimated cost of $34 billion was not offset. The bill stated that this extension of unemployment benefits met the emergency designation under the rules of the *Statutory Pay-As-you-Go Act of 2010*, and thus did not need to be offset. On July 21, 2010, the Senate voted 59-39 to approve H.R. 4213, which provided an extension of emergency unemployment benefits to November 30, 2010.[15] On July 22, 2010, the House approved the bill, and then President Obama signed the bill into law (P.L. 111-205).

After Congress returns from recess in September, Congress is expected to reconsider the package of extenders.[16] This package may be included in legislation to extend the Bush tax cuts for individuals.

Tax Extenders in Initial H.R. 4213

Numerous tax extenders expiring at the end of 2009 were included in H.R. 4213 with a proposed extension of one year. These extenders in H.R. 4213 and their estimated revenue cost over 10 years were the following:[17]

[11] For a technical explanation of provisions of this bill, see Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions Contained in the "American Jobs and Closing Tax Loopholes Act of 2010," for Consideration on the Floor of the House of Representatives* (JCX-29-10), May 28, 2010, 188 pp.

[12] For an explanation of these revenue offsets, see CRS Report R40623, *Tax Havens: International Tax Avoidance and Evasion*, by Jane G. Gravelle.

[13] Brent Ferguson, "Senate Leaders Table Extenders Bill After Third Vote to Invoke Cloture Fails," *Daily Tax Report*, June 25, 2010, p. G5.

[14] Ibid.

[15] Derrick Cain, "Senate Passes Extension of UI Benefits; House Set to Approve, President to Sign," *Daily Tax Report*, July 7, 2010, p. EE17.

[16] Meg Shreve, "Levin Says Senate Likely to Move First on Tax Cuts as Boehner Attacks Democrats, White House," *Tax Notes Today*, p. 1.

[17] These provisions and their estimated revenue effects are from the initial H.R. 4213 passed by the House on Dec. 9, 2009.

I. General Provisions

A. Individual Tax Relief

- Deduction of state and local general sales taxes [$1,846 million over 10 years]
- Additional standard deduction for real property taxes [$1,460 million over 10 years]
- Above-the-line deduction for qualified tuition and related expenses [$1,529 million over 10 years]
- Above-the-line deduction for certain expenses of elementary and secondary school teachers [$228 million over 10 years]

B. Business Tax Relief

- Research tax credit (also known as research and experimentation tax credit and the R&D credit) [$6,996 million over 10 years]
- Exception under Subpart F for active financing income (sunset 12/31/10) [$3,923 million over 10 years]
- Look-through treatment of payments between related controlled foreign corporations [$574 million over 10 years]
- 15-year straight-line cost recovery for qualified leasehold, restaurant, and retail improvements [$5,390 million over 10 years]
- 7-year straight line cost recovery period for motorsports entertainment complexes [$45 million over 10 years]
- Railroad track maintenance credit [$165 million over 10 years]
- Special expensing rules for U.S. film and television productions [$51 million over 10 years]
- Expensing of "brownfields" environmental remediation costs [$159 million over 10 years]
- Mine rescue team training credit [$1 million over 10 years]
- Election to expense advanced mine-safety equipment [$5 million over 10 years]
- Employer wage credit for activated military reservists [$4 million over 10 years]
- 5-year depreciation for farming business machinery and equipment [$838 million over 5 years but no cost over 10 years]
- Special rules for regulated investment companies [$10 million over 10 years]
- Special rule for percentage depletion for marginal wells [$104 million over 10 years]

C. Charitable Provisions

- Provision encouraging contributions of capital gain real property for conservation purposes [$182 million over 10 years]
- Enhanced charitable deduction for contributions of food inventory [$78 million over 10 years]
- Enhanced charitable deduction for contributions of book inventories to public schools [$31 million over 10 years]
- Enhanced deduction for corporate contributions of computer equipment for educational purposes [$195 million over 210 years]
- Tax-free distributions from individual retirement plans for charitable purposes [$591 million over 10 years]
- Special tax treatment of certain payments to controlling exempt organizations [$20 million over 10 years]
- Exclusion of gain on the sale or exchange of certain brownfield sites from unrelated business taxable income [$47 million over 10 years]
- Special rule for S corporations making charitable contributions of property [$37 million over 10 years]

D. Miscellaneous Provisions

- Indian employment tax credit [$49 million over 10 years]
- Accelerated depreciation for business property on Indian reservations [$125 million over 10 years]
- Deduction allowable with respect to income attributable to domestic production activities in Puerto Rico [$185 million over 10 years]
- Increase in limit on cover over of rum excise tax revenues (from $10.50 to $13.25 per proof gallon) to Puerto Rico and the Virgin Island [$128 million over 10 years]
- Economic development credit for American Samoa [$18 million over 10 years]

II. Community Assistance Provisions

- Empowerment zone tax incentives [$381 million over 10 years]
- Renewal community tax incentives [$786 million over 10 years]
- New markets tax credit [$1,402 million over 10 years]
- Tax incentives for investment in the District of Columbia [$17 million over 10 years]
- Tax incentive for New York Liberty Zone: bonus depreciation and Liberty Zone bonds [$318 million over 10 years]
- Tax incentives for the Gulf Opportunity (“GO”) Zone [$32 million over 10 years]

- Election for refundable low-income housing credit for 2010 [$471 million over 10 years]

III. Disaster Tax Relief Provisions

- Individual casualty losses attributable to Federally declared disasters deductible without regard to AGI; $500 floor applicable to all casualty losses [$728 million over 10 years]
- Expensing of qualified disaster expenses [$32 million over 10 years]
- 5-year carry-back period for certain losses relating to federal disasters [$129 million over 10 years]
- Relaxed mortgage revenue bond limitations for federal disasters [$63 million over 10 years]
- Bonus depreciation for qualified disaster property [$1,434 million over 10 years]
- Increased expensing for qualified disaster assistance property under section 179 [$1 million over 10 years]

IV. Energy Tax Provisions

- Incentives for biodiesel and renewable diesel [$1,008 million over 10 years]
- Alternative motor vehicle credit for heavy hybrids [$7 million over 10 years]
- Alternative fuel credit for natural gas and liquefied petroleum gas [$125 million over 10 years]
- Special rule for sales or dispositions to implement FERC or State electric restructuring policy for qualified electric utilities [$163 million over 5 years but no cost over 10 years]

Analysis of Tax Extenders

Several tax provisions exist in the code, many of which have been extended at least twice since their original expiration date. Among the extenders, one provision was 20 years old, another was 10 years old, and nine other provisions had been in existence for five years or more. The durability of the extenders suggests they may be more than temporary in nature.

The analysis of temporary tax provisions is complex, involving the examination of issues of policymaking and economics. Tax incentives are designed to alter the behavior of those who are the intended beneficiaries. Economic analysis provides a framework to examine the success of temporary tax provisions in achieving their intended outcomes.

Extenders as Temporary Tax Provisions

The extenders are a recurring legislative issue because of their temporary nature. Each time an extender's expiration approaches, Congress faces the choice to extend the tax provision, redesign it, allow it to expire, or make it a permanent provision in the tax code. The reason for their temporary, yet normally extended character, may be, in part, tax revenue: temporary extensions have lower short-run revenue costs than permanent law, although the ostensible lack of permanence often masks the long-term costs associated with the provisions. Temporary tax provisions are often extended for one or two years at the most, and at the time of extension, the costs appear small enough to warrant nominal offsets as required under the pay-as-you-go rule. Yet, increasingly, the provisions have been extended for five and 10 years and have long-term revenue losses similar to other permanent parts of the tax code.

Extenders, like all tax benefits, affect revenue estimation as well. Budget estimates are required to be made assuming current law proceeds uninterrupted. As a result, revenue projections are made assuming temporary tax provisions expire according to current law. Thus, if temporary provisions are frequently extended automatically, revenue projections may be inaccurate.

It might also be argued that the temporary nature of the provisions is useful, quite apart from revenue considerations. The temporary nature of expiring provisions allows policymakers to evaluate their effectiveness and allow for reassessment of their value on a regular basis. In theory, extenders that fail to accomplish their purpose could be allowed to expire.

If provisions are thought to be ineffective, a policy alternative to allowing temporary provisions to expire is to redesign them. As an example, Congress replaced the Targeted Jobs Tax Credit, which was enacted in 1978, with the Work Opportunity Tax Credit in the Small Business Job Protection Act of 1996, P.L. 104-188. The temporary credit was initially effective for one year and then reauthorized by the Taxpayer Relief Act of 1997, P.L. 105-34, which also modified the credit by shortening the eligibility time, changing the subsidy rate, and adding a new group to the eligible population.

The extenders were not originally enacted at the same time. Many originated in one of the tax bills enacted during the late 1990s, and some in the mid 1980s. While their origins differ, the provisions have increasingly been considered as a group. Several of the extenders that expired in 2005 had been most recently extended by the Working Families Tax Relief Act of 2004, P.L. 108-311. Some of those temporary provisions were the Work Opportunity Tax Credit (WOTC), the Welfare-to-Work Tax Credit (WWTC), the credit for holders of qualified zone academy bonds, the deduction for capital investment in oil and gas produced from marginal wells, and the "cover over" of tax on distilled spirits from Puerto Rico and the U.S. Virgin Islands. Of those provisions, six had been extended by the Tax Relief Extension Act of 1999 (TREA; P.L. 106-170). Three of the six temporary provisions had been originally enacted by the Taxpayer Relief Act of 1997 (TRA; P.L. 105-34). The three provisions were the Welfare-to-Work Tax Credit (WWTC), the credit for holders of qualified zone academy bonds, and the deduction for capital investment in oil and gas produced from marginal wells.

Each extender is unique and addresses a separate topic in the tax code. Consideration of them as a group may ignore some of the strengths and weaknesses specific to individual provisions. Ideally, the purpose of each expiring provision should be clear, as well as the appropriateness of using the tax code to subsidize the targeted objective as opposed to a direct subsidy. Additionally, the benefits of the provisions should be examined to determine if they outweigh the costs of the provisions and to ensure that forgoing the tax revenue from the activity is justified relative to other policy goals.

Treating permanent provisions as temporary also leads to uncertainty for government and taxpayer planning and causes, in some cases, significant impacts. When taxpayers are uncertain whether temporary provisions will be extended, they may have difficulty making reliable and effective business plans. An example of government uncertainty involves state employment agencies that certify the workers who qualify for the Work Opportunity Tax Credit and the Welfare-to-Work Tax Credit. If those credits are not extended, the state certification workers would need to be reassigned to other tasks. If the credits are reinstated, the states would then have to reassign the workers a second time. Those workers would also face a backlog of pending certifications created during the lapse of the temporary provision.

Extenders as Tax Benefits

Temporary tax benefits are a form of federal subsidy that treats eligible activities favorably compared to others, and channels economic resources into qualified uses. Extenders influence how economic actors behave and how the economy's resources are employed. Like all tax benefits, economic theory suggests every extender can be evaluated by looking at the impact on economic efficiency, equity and simplicity. Temporary tax provisions may be efficient and effective in accomplishing their intended purpose, though not equitable. Alternatively, an extender may be equitable but not efficient. Policymakers may have to choose the economic objectives that matter most. Doing so on a case-by-case basis for extenders may prove to be the best option to achieve the desired results.

Efficiency

Extenders often provide subsidies to encourage more of an activity than would otherwise be undertaken. According to economic theory, in most cases an economy best satisfies the wants and needs of its participants if markets operate free from distortions by taxes and other factors. Market failures, however, may occur in some instances, and economic efficiency may actually be improved by tax distortions.[18] Thus, the ability of extenders to improve economic welfare depends on whether or not the extender is remedying a market failure. According to theory, an extender lowers efficiency if it distorts behavior in the absence of a market failure.

An extender is also considered effective to the degree that it stimulates the desired activity better than a direct subsidy. Direct spending programs are often more successful at targeting resources than indirect subsidies made through the tax system.

Equity

A tax is considered to be fair when it contributes to a socially desirable distribution of the tax burden. Tax benefits such as the extenders can result in individuals with similar incomes and expenses paying differing amounts of tax, depending on whether they engage in tax-subsidized activities. This differential treatment is a deviation from the standard of horizontal equity, which requires that people in equal positions should be treated equally.

Another component of fairness in taxation is vertical equity, which requires that tax burdens be distributed fairly among people with different abilities to pay. Most extenders benefit those who

[18] Market failure occurs when the marginal benefit of an action does not equal the marginal cost. For example, polluting forms of energy production cause social costs that are not taken into account by the producer; hence, there is an argument for taxing this type of energy or, alternatively, subsidizing less polluting firms.

have sufficient income to pay tax. Those individuals without sufficient income to pay tax do not have the opportunity to benefit from extenders. The disproportionate benefit of tax expenditures to individuals with higher incomes reduces the progressivity of the tax system, which is often viewed as a reduction in equity.

An example of the effect a tax benefit can have on vertical equity violation can be seen by identifying two individual teachers who have both incurred $250 in classroom-related expenses and are eligible to claim the above-the-line deduction for expenses. Yet the tax benefit to the two differs if they are in different tax brackets. A teacher with lower income, who may be in the 15% income tax bracket, receives a deduction with a value of $37.50, while another teacher, in the 31% bracket, receives a deduction value of $77.50. Thus, the higher income taxpayer, with presumably greater ability to pay taxes, receives a greater benefit than the lower income taxpayer.

Simplicity

Extenders contribute to the complexity of the tax code and raise the cost of administering the tax system. Those costs, which can be difficult to isolate and measure, are rarely included in the cost-benefit analysis of temporary tax provisions. The complexity of the tax code adds to the time cost of taxpayers in either learning how to claim various incentives and doing so, or an increased direct cost of paying tax professionals to perform the service for the taxpayer.

Tax extenders can be classified into three categories: temporary tax credits, temporary tax deductions, and other tax provisions. Some of the tax extenders in each of these categories, which were scheduled to expire in 2009, are examined in the rest of this report.

Temporary Tax Credits

Some of the temporary provisions scheduled to expire are tax credits, which are incentives that, when claimed, reduce the taxpayer's income tax liability. In general, a tax credit is more valuable than a similar tax deduction. A tax credit reduces the tax paid, dollar-for-dollar. Tax deductions lower taxable income.

Table 1. Tax Credits

Provision	Internal Revenue Code Section
Tax credit for holders of qualified zone academy bonds	1397E(e)(1)
Tax credit for first-time D.C. homebuyers	1400C(i)
Tax credit for research and experimentation	41(h)
New Markets Tax Credit	45(d)
Possession Tax Credit with respect to American Samoa	27(b), 936
Credit for Certain Railroad Track Expenditures	45G(f)

Source: CRS.

Tax Credit for Holders of Qualified Zone Academy Bonds

Qualified Zone Academy Bonds (QZAB), which were first introduced as part of the Taxpayer Relief Act of 1997 (P.L. 105-34), are a type of bond that offers the holder a nonrefundable federal tax credit instead of interest. Qualified zone academies are public schools and programs that provide education and training below the post-secondary level. Issuers of QZABs are required to use the proceeds to finance public school partnership programs in economically distressed areas. QZAB holders are limited to banks, insurance companies, and corporations actively engaged in the business of lending money.

Initially, state and local governments could issue QZABs only in 1998 and 1999, subject to a national limitation of $400 million each year. The Ticket to Work and Work Incentives Improvement Act of 1999, P.L. 106-170, extended this provision, authorizing up to $400 million of QZABs to be issued in 2000 and 2001, with any unused authority carried over for several years. The Job Creation and Worker Assistance Act of 2002, (P.L. 107-147), extended the QZAB program with an additional $400 million of bond capacity available for 2002 and 2003. The Working Families Tax Relief Act of 2004 (P.L. 108-311) authorized an additional extension through December 31, 2005. The Tax Relief and Health Care Act of 2006 (P.L. 109-432; TRHCA) enacted a two-year extension of the annual authorization amount of $400 million, through December 31, 2007, and the Emergency Economic Stabilization Act (P.L. 110-343, EESA) further extended that authorization through December 31, 2009. [19]

Tax Credit for First-Time Homebuyers in the District of Columbia

This credit allows a nonrefundable credit against federal taxes of up to $5,000 for the first-time purchase of a principal residence in the District of Columbia. The credit is available only once for homebuyers who acquire title to a qualifying principal residence after August 1997 and before December 31, 2005. The tax credit was created by the Taxpayer Relief Act of 1997 (P.L. 105-34) to provide an incentive to purchase a home in DC, thus increasing the rate of owner-occupied home ownership. Compared to neighboring Maryland (70.7%) and Virginia (75.1%), the District of Columbia's home ownership rate is significantly lower (42.7%).[20]

The credit was extended by the Working Families Tax Relief Act of 2004 (P.L. 108-311). TRHCA enacted a two-year extension of the tax credit, through December 31, 2007 and EESA further extended the credit through December 31, 2009.

Tax Credit for Research and Experimentation Expenses

A business credit for research expenses is available as a subsidy for research and experimentation (R&E) expenses paid or incurred through December 31, 2005. While the credit is often thought of as a single credit, it actually consists of four discrete credits for the 2009 tax year: (1) a regular

[19] For more detailed information, see CRS Report R40523, *Tax Credit Bonds: Overview and Analysis*, by Steven Maguire.

[20] U.S. Congress, Senate Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, committee print prepared by the Congressional Research Service, Library of Congress, 107th Cong., 2nd sess., S. Prt. 107-80 (Washington: GPO, 2002), pp. 213-215.

credit, (2) an alternative simplified credit (ASIC), (3) a basic research credit, and (4) an energy research credit.[21]

The R&E tax credit, originally enacted in the Economic Recovery Tax Act of 1981 (P.L. 97-34), has been extended 13 times, including by the Ticket to Work and Work Incentives Improvement Act of 1999 (P.L. 106-170) and by the Working Families Tax Relief Act of 2004 (P.L. 108-311). TRHCA retroactively extended the tax credit, through December 31, 2007, and modified the credit rules. EESA further extended it through December 31, 2009, and made additional modifications.[22]

New Markets Tax Credit

The New Markets Tax Credit (NMTC) program permits taxpayers to receive a credit against federal income taxes for making qualified equity investments in designated Community Development Entities (CDEs). Substantially all of the qualified equity investment must in turn be used by the CDE to provide investments in low-income communities. The credit provided to the investor totals 39% of the cost of the investment and is claimed over a seven-year credit allowance period. In each of the first three years, the investor receives a credit equal to 5% of the total amount paid for the stock or capital interest at the time of purchase. For the final four years, the value of the credit is 6% annually. Investors may not redeem their investments in CDEs prior to the conclusion of the seven-year period.[23]

The NMTC program was added by the Community Renewal Tax Relief Act of 2000, P.L. 106-554, and allows a maximum annual amount of qualified equity investments of $3.5 billion per year for 2006 and 2007. TRHCA extended the $3.5 billion annual allocation through 2008; EESA extended that amount through 2009.

Possession Tax Credit with Respect to American Samoa

Section 936 of the Internal Revenue Code allows certain domestic corporations with business operations in the U.S. possessions, including American Samoa. The tax credit is intended to offset the U.S. tax imposed on certain income related to operations in American Samoa. Income eligible for the Section 936 credit includes non-U.S. source income from the active conduct of a trade or business within a U.S. possession, the sale or exchange of substantially all of the assets that were used in such a trade or business, or certain possessions investments.

American Samoa has a tax system that mirrors U.S. tax law. Residents of American Samoa are taxed by both the United States and American Samoa. Nonresidents are taxed by American Samoa on their American Samoa-source income and income effectively connected with an American Samoa trade or business. American Samoa corporations are subject to U.S. tax on

[21] For more detailed information on the Research and Experimentation Tax credit, including its design, legislative history, effectiveness, and key policy issues, see CRS Report RL31181, *Research and Experimentation Tax Credit: Current Status and Selected Issues for Congress*, by Gary Guenther.

[22] Ibid.

[23] For more detailed information, see CRS Report RL34402, *New Markets Tax Credit: An Introduction*, by Donald J. Marples.

income effectively connected to a U.S. trade or business, and, in some cases, on passive income from U.S. sources and on U.S. branch profits.

To qualify for the possession tax credit for a taxable year, a domestic corporation must satisfy two conditions. First, at least 80% of the gross income of the corporation for the three-year period immediately preceding the close of the taxable year must be derived from sources within American Samoa. Second, the corporation must derive at least 75% of its gross income for that same period from the active conduct of a possession business.

TRHCA extended the credit through December 31, 2007, and EESA further extended it through December 31, 2009.

Credit for Certain Railroad Track Maintenance Expenditures

A 50% general business credit[24] was originally available to eligible taxpayers for qualified railroad track maintenance expenditures paid or incurred in tax years beginning after December 31, 2004, and beginning before January 1, 2008. The purpose of the credit is to enable small and mid-sized railroads to update and upgrade their track capacities in order to promote those railroads as an alternative to shipping freight on roadways.

The railroad track maintenance credit cannot exceed the product of $3,500 and the number of miles of railroad track owned or leased by or assigned to the eligible taxpayer (e.g., $3,500 x 200 miles). Eligible taxpayers include Class II and III railroads[25] and certain persons who are assigned tracks by a Class II or Class III railroad. Qualified railroad track maintenance expenditures include expenses for maintaining railroad track owned or leased, as of January 1, 2005, by a Class II or Class III railroad.

The railroad track maintenance credit was introduced by the American Jobs Creation Act of 2004 (P.L. 108-357) and EESA further extended it through December 31, 2009, and allowed the credit to be claimed against the alternative minimum tax (AMT).

Temporary Tax Deductions

Temporary tax deductions include provisions for individuals and corporations.

[24] The general business credit includes a number of credits designed to encourage certain business activities.

[25] The U.S. Department of Transportation's Surface Transportation Board's regulations divide railroads into three classes based on annual carrier operating revenues. Class I railroads are those with annual carrier operating revenues of $250 million or more (in 1991 dollars); Class II railroads are those with annual carrier operating revenues of more than $20 million but less than $250 million (in 1991 dollars); and Class III railroads are those with annual carrier operating revenues of $20 million or less (in 1991 dollars). See 49 CFR Part 1201, General Instruction 1-1(a).

Table 2. Tax Deductions

Provision	Internal Revenue Code Section
Expense deduction for elementary and secondary school teachers	62(a)(2)(D)
Deduction for tuition and related expenses	222
Enhanced deduction for corporate contributions of computer equipment for educational purposes	170(e)(6)(G)
Enhanced deduction for contributions of food inventory	170(e)(3)(C)(iv)
Enhanced deduction for contributions of book inventory to public schools	170(e)(3)(D)(iv)
Basis adjustment to stock of S corporations making charitable contributions to charity	1367(a)(2)
Contributions of capital gain real property made for conservation purposes	170(b)(1)(E)(vi)
State and local sales tax deduction	164
15-year straight-line cost recovery for qualified leasehold improvements	168(e)(3)(E)(iv)
15-year straight-line cost recovery for qualified restaurant improvements	168(e)(3)(E)(v)
Accelerated depreciation for property on Indian reservations	168(j)
Seven-year cost recovery period for motor sports entertainment complexes	168(i)(15)(D)

Source: CRS.

Expense Deduction for Elementary and Secondary School Teachers

An above-the-line deduction (i.e., a deduction for non-itemizers) for certain classroom expenses paid or incurred during the school year by eligible elementary and secondary school (K-12) teachers, among other educators, was authorized in the Job Creation and Worker Assistance Act of 2002. The provision, originally effective for taxable years beginning after December 31, 2001, allows for up to $250 annually of expenses paid or incurred for books, supplies, computer equipment, and supplementary materials to be deducted. Under previously expired law, teachers were allowed to deduct these expenses only when itemizing on the tax return and (as with other deductions) only if the total of all itemized deductions exceeded 2% of adjusted gross income.[26]

TRHCA retroactively extended the deduction for two years, through December 31, 2007, and EESA further extended the deduction through December 31, 2009.

Deduction for Tuition and Related Expenses

In June 2001, as a part of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA, P.L. 107-16), Congress passed a new set of rules regarding the deductibility of higher education expenses. Starting in 2002, a new deduction was created for post-secondary education expenses paid by taxpayers for themselves, their spouse, or dependents. This "above-the-line" deduction was for tuition and education-related expenses paid for enrollment at any accredited post-secondary institution. This temporary tuition deduction, available during tax years 2002

[26] For more detailed information see CRS Report RS21682, *The Tax Deduction for Classroom Expenses of Elementary and Secondary School Teachers*, by Linda Levine.

through 2005, was available to taxpayers regardless of whether they claimed the standard deduction or itemized deductions when filing their income tax return. The deduction was not restricted by the overall limitation on itemized deductions.

The "above-the-line" deduction was limited to $3,000 for 2002 and 2003. The deduction was limited to $4,000 for 2004 and 2005. It was generally available to taxpayers with adjusted gross incomes below $65,000 ($130,000 for married individuals filing jointly). For 2004 and 2005 the maximum that could be deducted was either $2,000 or $4,000 depending on adjusted gross income. If adjusted gross income was $65,000 or less ($130,000 or less for those filing a joint return), the maximum deduction was $4,000. If adjusted gross income was more than $80,000 ($160,000 for married individuals filing jointly), the deduction could not be claimed.

Only certain higher education expenses were allowable for deduction. For example, tuition and fees required for enrollment or attendance at an eligible post-secondary educational institution were allowable. However, taxpayers were required to subtract any scholarships, educational assistance allowances, or other nontaxable sources of income spent for educational purposes from the tuition and fees expense. This reduced amount was the qualified amount eligible for the deduction. Personal expenses and the cost of books were not allowable. Taxpayers could not claim a course involving sports, games, or hobbies, unless such course is part of the student's degree program.

The income tax code disallows education expenses claimed for certain tax incentive programs to be claimed for the deduction as well. Any qualified education expenses deducted as a business expense, claimed for an education tax credit, or paid with earnings from either a Coverdell education savings account or U.S. education savings bonds, could not be claimed for the "above-the-line" tuition and fees deduction.

Additionally, the use of the deduction is conditional on the tax status of the student in relationship to the taxpayer. If the taxpayer claims an exemption for a dependent who is an eligible student, the taxpayer can include expenses paid for the student in determining the deduction. If the dependent pays the qualified expenses and the taxpayer claims an exemption for that student, neither the taxpayer nor the dependent can deduct the expenses.

TRHCA retroactively extended the deduction for two years, through December 31, 2007, and EESA further extended the deduction through December 31, 2009.

Enhanced Deduction for Corporate Charitable Contributions of Computer Equipment for Educational Purposes

Section 170(e)(6) of the Internal Revenue Code allows for an enhanced deduction for corporate contributions of computer equipment to public libraries and elementary and secondary schools. Generally, tax law allows for certain contributions of inventory or other ordinary-income property, and short-term capital gain property to be made by C corporations[27] (S corporations,[28]

[27] The Internal Revenue Code normally subjects corporate profits to the corporate income tax under its subchapter C; corporations subject to income tax are thus often referred to as "C corporations."

[28] S corporations are not subject to the corporate income tax and their net profits are passed through to the individual shareholders (partners), the number of which must be limited to 75 or less, who are taxed on the profits under the individual income tax.

which are taxed as partnerships, are not eligible). In the case of charitable contributions, the amount of the deduction is limited to the taxpayer's basis (original investment) in the property. Special rules provide enhanced deductions for certain corporate contributions of inventory property for the care of the ill, the needy or infants and certain contributions of scientific equipment. Under these special rules, the amount of the enhanced deduction is equal to the donor's basis in the donated property plus one-half of the amount of ordinary income that would have been realized if the property had been sold.

Congress extended this special rule to provide an incentive for businesses to donate their computer equipment for the benefit of primary and secondary school students. Computer equipment includes computer software, computer or peripheral equipment, and fiber optic cable related to computer use. In addition to the augmented deduction benefit, the donor, by not selling the property, avoids realizing any capital gains and the subsequent income tax on those gains.

Originally authorized by the Taxpayer Relief Act of 1997 (P.L. 105-34), the provision was then extended for three years by the Community Renewal Tax Relief Act of 2000 (CRTRA, P.L. 106-554). CRTRA also expanded the deduction to include property donated to public libraries, property donated no later than three years (instead of two) after the date of taxpayer acquisition, and property donated after reacquisition by computer manufacturers. The most recent extension, through December 31, 2005, was authorized by the Working Families Tax Relief Act of 2004 (P.L. 108-311). TRHCA retroactively extended the deduction for two years, through December 31, 2007, and EESA further extended the deduction through December 31, 2009.

Enhanced Deduction for Contributions of Food Inventory

Tax law provides an enhanced deduction for certain charitable contributions of food inventory. This deduction has been limited to contributions made by a certain type of corporation, C corporations. The value of the existing deduction is the corporation's basis in the donated product plus one half of the amount of appreciation, as long as that amount is less than twice the corporation's basis in the product.

In general, if a charitable contribution is made in the form of property, the basis for the charitable deduction is dependent on the type of taxpayer (i.e., individual or form of business entity), to whom the property is donated, and for what purpose the donated property is to be used.

Corporate gifts of property that would generate capital gains if sold (e.g., stocks and bonds) are deductible by corporations at market value. However, gifts of depreciable property are deductible at the corporation's basis rather than fair market value. Thus, under current tax law, the deduction is reduced by previously taken depreciation. In the case of fully depreciated machinery and equipment, the allowable charitable contribution deduction would be zero.

Under current tax law, C corporations are provided more favorable tax treatment of contributions of certain types of inventory and other ordinary-income property to specified charitable organizations. This provision is temporarily available to S corporations, partnerships, and sole proprietorships. Through 2007, all donors are allowed to deduct their cost plus one-half the difference between their cost and the market value of the donated goods. However, in no case may the deduction's value exceed twice the cost basis.

For a donor to receive this enhanced deduction, the gift must be made to a "qualified" tax exempt organization. Further, the property must be "used by the donee solely for the care of the ill, the needy, or infants."[29] The donee is not permitted to exchange what has been transferred for money, other property, or services.[30] The donee must furnish to the donor a statement that it does not intend to transfer the donation and that it will be used for the care of the ill, the needy, or infants.[31] If the property is subject to regulation by the Federal Food, Drug, and Cosmetic Act it must satisfy the requirements on the date of transfer and for 180 days prior thereto.[32]

The enhanced deduction for food is available only for food that qualifies as "apparently wholesome food." "Apparently wholesome food" is defined under the Katrina Emergency Tax Relief Act of 2005 (KETRA) as food intended for human consumption that meets all quality and labeling standards imposed by federal, state, and local laws and regulations even though the food may not be readily marketable due to appearance, age, freshness, grade, size, surplus, or other conditions.[33]

In response to the devastation from Hurricane Katrina, the Katrina Emergency Tax Relief Act of 2005 (KETRA, P.L. 109-73) was enacted. That legislation included a temporary expansion of the tax deduction for charitable contributions of food inventory. The law allowed all donors of wholesome food inventory to benefit from the enhanced deduction for donations made between August 28, 2005, and January 1, 2006. The Pension Protection Act of 2006 (P.L. 109-280) extended the temporary expansion through January 1, 2008, and EESA further extended the enhanced deduction through December 31, 2009.

Enhanced Deduction for Contributions of Book Inventory to Public Schools

In response to the hurricane disasters along the Gulf coast in 2005, President Bush signed the Katrina Emergency Tax Relief Act of 2005 (P.L. 109-73), which temporarily modified the rules relating to charitable contributions in several ways, one being enhanced deductions for donations of book inventories to public schools. This provision was to terminate at the end of 2005, was later extended to December 31, 2007, by the Pension Protection Act of 2006 (P.L. 109-280) and EESA further extended the deduction through December 31, 2009.

Under this provision, any corporation (other than an S corporation[34]) that makes a qualified book contribution on or after August 28, 2005, and before January 1, 2008, may deduct its basis in the contributed property plus one-half of the property's appreciation in value, as long as the deduction does not exceed twice the property's basis. Before this enhanced deduction was enacted, companies could only deduct an amount equal to their cost for an item donated to a 501(c)(3) public charity (if the charity did not resell the item). However, the inventory or other property may have a fair market value higher than its cost.

[29] Internal Revenue Code §170(e)(3)(i).

[30] Internal Revenue Code §170(e)(3)(ii).

[31] Internal Revenue Code §170(e)(3)(iii).

[32] Internal Revenue Code §170(e)(3)(iiii).

[33] For more detailed information, see CRS Report RL31097, *Charitable Contributions of Food Inventory: Proposals for Change*, by Pamela J. Jackson.

[34] See footnote 28 for the definition of an S corporation.

A qualified book contribution is a charitable contribution of books to a public school that provides elementary or secondary education (kindergarten through grade 12) and maintains a regular faculty and curriculum with a regularly enrolled student body. The donee educational institution must certify that (1) the books are suitable in terms of currency, content, and quality for use in the school's educational programs, and (2) the school will actually use the books in its educational programs.

Basis Adjustment to Stock of S Corporations Making Charitable Contributions of Property

A temporary tax incentive to encourage S corporations[35] to make charitable donations of appreciated assets is available for tax years 2006 through 2009. Generally, a charitable contribution of property by an S corporation provides the corporation's shareholders with a fair market value deduction for gifts of property. In association with the charitable gift, shareholders must reduce their basis (cost) of shares in the corporation. Under the temporary provision, the shareholder reduces his or her basis in the stock of the S corporation by his or her pro rata share of the adjusted basis of the contributed property, rather than by the fair market value of the charitable contribution that flows through to the shareholder. The lower basis reduction results in a proportionately larger gain when the stock is later sold by the shareholder. Thus, the shareholder benefits by having that reduction determined by the basis of the property (which is a smaller amount) rather than the fair market value (a larger amount). For example, if an S corporation with one individual shareholder makes a charitable contribution of stock with a basis of $100 and a fair market value of $500, the shareholder will be treated as having made a $500 charitable contribution and will reduce the basis of their S corporation stock by $100.

This provision was enacted by the Pension Protection Act of 2006 (P.L. 109-280) and EESA further extended it through December 31, 2009.

Contributions of Capital Gain Real Property Made for Conservation Purposes

This provision, introduced by the Pension Protection Act of 2006 (P.L. 109-280), provides incentives for individuals to make qualified conservation contributions of real estate and ownership interests in real estate during 2006 and 2007. The act raises the charitable deduction limit for individuals from 30% to 50% of adjusted gross income for qualified conservation contributions, and allows taxpayers to carry these deductions forward for 15 years.

A qualified conservation contribution is a contribution of qualified real property interest to a government or publicly supported charity (or organization that is controlled by a government or publicly supported charity) exclusively for conservation purposes.[36] Qualified real property

[35] See footnote 28 for the definition of an S corporation.

[36] A qualified conservation contribution is one that is made for any one of the following four purposes: (1) the preservation of land areas for outdoor recreation by, or the education of, the general public; (2) the protection of a relatively natural habitat of fish, wildlife, or plants, or a similar ecosystem; (3) the preservation of open space (including farmland and forest land) where such preservation is for the scenic enjoyment of the general public, or made pursuant to a clearly delineated federal, state, or local government conservation policy that will yield a significant public benefit; and (4) the preservation of a historically important or a certified historic structure.

interest is either the entire interest of the donor[37], a remainder interest (which allows the donor to continue occupying the donated property during his or her lifetime), or a restriction (granted in perpetuity) on the use which may be made of the real property.

For qualified farmers or ranchers who contribute property used for agriculture or livestock production, the charitable deduction limit is raised to 100% of adjusted gross income, provided that such contribution does not prevent the use of the donated land for farming or ranching purposes. A "qualified farmer or rancher" is a taxpayer whose gross income from the trade or business of farming is greater than 50% of the taxpayer's gross income for the taxable year.

Private corporations that are engaged in farming or ranching activities may deduct up to 100% of adjusted taxable income for such contributions, provided that the terms of the gift did not limit the farming activities on the property. Such corporations could also carryover the deduction for a 15-year period.

This provision was effective for contributions made in taxable years beginning after December 31, 2005, and before January 1, 2008. When the Food, Conservation, and Energy Act of 2008 (P.L. 110-234) was signed into law on May 22, 2008, the provision was extended for two years. Thus, contributions made in taxable years beginning before January 1, 2010, are eligible for the provision.

State and Local Sales Tax Deduction

For taxable years beginning in 2004 through 2009, at the election of the taxpayer, an itemized deduction can be claimed for state and local general sales taxes in lieu of the itemized deduction for state and local income taxes. Enacted by the American Jobs Creation Act of 2004 (P.L. 108-357), the itemized deduction included individual income taxes, real property taxes, and personal property taxes paid by the taxpayer. The itemized deduction was not allowable against the alternative minimum tax.

Taxpayers had two options with respect to the determination of the sales tax deduction amount. Taxpayers could deduct the total amount of general state and local sales taxes paid by accumulating receipts showing general sales taxes paid. Alternatively, taxpayers could use allowable deduction tables created by the Secretary of the Treasury. The tables are based on average consumption by taxpayers on a state-by-state basis taking into account filing status, number of dependents, adjusted gross income, and rates of state and local general sales taxation.

The term "general sales tax" means a tax imposed at one rate with respect to the retail sale of a broad range of classes of items. However, in the case of certain items, like food, clothing, medical supplies, and motor vehicles, the fact that the tax does not apply with respect to some or all of such items is not taken into account in determining whether the tax applies with respect to a broad range of classes of items. The fact that the rate of tax applicable with respect to some or all of such items is lower than the general rate of tax is not taken into account in determining whether the tax is imposed at one rate.[38]

[37] Other than qualified mineral interest, which means subsurface oil, gas, or other minerals, and the right to access these minerals.

[38] For more detailed information see CRS Report RL32781, *Federal Deductibility of State and Local Taxes*, by Steven Maguire.

TRHCA retroactively extended the deduction for two years, through December 31, 2007, and EESA further extended the deduction through December 31, 2009.

Depreciation Allowances

A taxpayer is allowed to recover, through annual depreciation deductions, the cost of certain property used in a trade or business, or for the production of income. The amount of the depreciation deduction allowed with respect to tangible property for a taxable year is determined under the tax code's modified accelerated cost recovery system (MACRS). Under MACRS, the cost of eligible property is recovered over specific periods of time (recovery periods), depending upon the type of property, and at specified rates over the prescribed recovery periods.

The tax code allows depreciation allowances for improvements made on leased property and typically requires the use of MACRS to determine the actual amount of depreciation even if the MACRS recovery period assigned to the property is longer than the term of lease. If a leasehold improvement constitutes an addition or improvement to nonresidential real property already placed in service, the improvement is depreciated using the straight-line method over a 39-year recovery period. However, exceptions exist for certain qualified leasehold improvements and certain qualified restaurant property.

15-Year Straight-Line Cost Recovery for Qualified Leasehold Improvements

In the case of qualified leasehold improvement property, Section 168(e)(3)(E)(iv) of the Internal Revenue Code allows a 15-year recovery period for property placed in service before January 1, 2010. Property placed in service after that date and later is subject to the rules described above. Qualified leasehold improvement property is any improvement to an interior portion of a nonresidential building. The improvement must be placed in service more than three years after the date the building was first placed in service.

15-Year Straight-Line Cost Recovery for Qualified Restaurant Improvements

In the case of qualified restaurant property, Section 168(e)(3)(E)(v) of the Internal Revenue Code allows a 15-year recovery period for property placed in service before January 1, 2010. Property placed in service after that date and later is subject to the rules described above. Qualified restaurant property includes any improvement to a building where more than 50% of the building's square footage is devoted to the preparation of, and seating for on-premises consumption of, prepared meals. The improvement must be placed in service more than three years after the date the building was first placed in service.

TRHCA extended the provisions to apply to property placed in service through December 31, 2007, and EESA further extended the provisions to apply to property placed in service through December 31, 2009.

Accelerated Depreciation for Property on Indian Reservations

A temporary tax provision allows for the accelerated depreciation of qualified Indian reservation property that is placed in service after 1993 and before January 1, 2010. For business property on Indian reservations, IRC Section 168(j) allows for a shorter recovery period than is provided for under MACRS standards. The shorter periods applicable for Indian reservations are indicated below.

Table 3. Accelerated Depreciation for Property

MACRS Standard	Applicable Period for Indian Reservations
3-year property	2 years
5-year property	3 years
7-year property	4 years
10-year property	6 years
15-year property	9 years
20-year property	12 years
Nonresidential real property	22 years

The accelerated depreciation provision requires that property be used in the active conduct of business within an Indian reservation. The provision was enacted by the Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66) and extended by the Job Creation and Worker Assistance Act of 2002 (P.L. 107-147). TRHCA extended the accelerated provision through December, 31, 2007, and EESA further extended the provision through December 31, 2009.

Seven-Year Cost Recovery Period for Motor Sports Entertainment Complexes

Taxpayers generally capitalize the cost of property used in a trade or business and recover such cost over 15 years. An exception exists, however, for the theme and amusement park industry, whose assets are assigned a seven-year recovery period.

The American Jobs Creation Act of 2004 (AJCA; P.L. 108-357) assigned a seven-year modified accelerated cost recovery period to motorsports entertainment complexes, which include land improvements and support facilities, but not transportation equipment, warehouses, administrative buildings, hotels, or motels.

The provision is effective for property placed in service after October 22, 2004, and before 2010 as a result of the enactment of EESA.

The AJCA specifies that the provision applies to motorsports entertainment complexes permanently situated on land and, during the 36-month period following the first day of the month in which the facility is placed in service, hosts one or more racing events for automobiles (of any type), trucks, or motorcycles which are open to the public for the price of admission. Also covered by the provision are any ancillary facilities and land improvements in support of the complex's activities (including parking lots, sidewalks, waterways, bridges, fences, and landscaping); support facilities (including food and beverage retailing, souvenir vending, and other non-lodging accommodations); and appurtenances associated with such facilities and related attractions and amusements (including ticket booths, race track surfaces, suites and hospitality facilities, grandstands and viewing structures, props, walls, facilities that support the delivery of entertainment services, other special purpose structures, facades, shop interiors, and buildings).

Other Tax Provisions

District of Columbia Enterprise Zone

The District of Columbia (DC) Enterprise Zone includes the DC Enterprise Community and the census tracts in the District of Columbia with a poverty rate of at least 20%. Businesses in the DC Zone are eligible for the following tax benefits: (1) a wage credit equal to 20% of the first $15,000 in annual wages paid to qualified employees who resided within the District of Columbia; (2) $35,000 in increased Section 179 expensing; and (3) in certain circumstances, tax-exempt bond financing. Additionally, a capital gains exclusion is allowed for certain investments in small business stock held more than five years and made within the DC Zone, or within any District of Columbia census tract with a poverty rate of at least 10%.[39] The DC Zone incentives, created in the Taxpayer Relief Act of 1997 (P.L. 105-34), were applicable from January 1, 1998 through December 31, 2003, and then extended through December 31, 2005. TRHCA extended the provisions through December 31, 2007, and EESA further extended the provisions through December 31, 2009.

"Cover Over" of Tax on Distilled Spirits to Puerto Rico and the U.S. Virgin Islands

In general, federal excise taxes do not apply to items produced and consumed in Puerto Rico, the U.S. Virgin Islands (USVI), and other U.S. possessions. However, so that goods produced in the possessions do not have a tax-induced price advantage in U.S. markets over goods produced in the mainland, an "equalization tax" is levied on goods imported into the United States from Puerto Rico or the USVI. The tax is equal to the excise tax that applies to like items of domestic manufacture. That tax is then rebated or "covered over" to the Puerto Rico and USVI. The amounts covered over to Puerto Rico and the USVI are deposited into the treasuries of the two possessions for use as those possessions determine. The provision was granted because Congress believed that rebating the increased rate of tax would contribute to the economic stability of Puerto Rico and the USVI.[40]

In 1984, the Deficit Reduction Act, P.L. 98-369, increased excise taxes on U.S. distilled spirits to $12.50 from $10.50 per proof gallon; subsequent legislation increased the rate to $13.50. However, the 1984 Act also amended the Internal Revenue Code, Section 7652, by adding subsection (f) which initially imposed a $10.50 limitation on "cover over" of the tax on distilled spirits. In 1993, the Omnibus Reconciliation Act, P.L. 103-66, extended the limitation such that the cover over amount was increased to $11.30 per gallon effective for the five-year period beginning October 1, 1993. The Tax Relief Extension Act of 1999, P.L. 106-170, extended the amendment for an additional two years, increasing the rate to $13.25 and the Job Creation and Worker Assistance Act of 2002, P.L. 107-147, provided a second extension effective through December 31, 2003. A third extension was authorized by the Working Families Tax Relief Act of 2004, P.L. 108-311, which made the provision effective through December 31, 2005.

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[39] For more details, see U.S. Congress, Senate Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, committee print prepared by the Congressional Research Service, Library of Congress, 107th Cong., 2nd sess., S. Prt. 107-80 (Washington: GPO, 2002), pp. 317-320.

[40] U.S. House Committee Report to H.R. 3090, H.Rept. 107-251, Oct. 17, 2001.

TRHCA included a two-year extension of the $13.25 per proof gallon cover amount for rum brought into the United States through December 31, 2007, and EESA further extended the provision through December 31, 2009. After that date, the cover amount would revert to $10.50 per proof gallon.

Tax-Free Distributions from Individual Retirement Plans for Charitable Purposes

The Pension Protection Act of 2006 (P.L. 109-280) amended the Internal Revenue Code to allow certain individual retirement account (IRA) holders to exclude from gross income up to $100,000 in qualified distributions from these accounts for charitable purposes. Distributions are eligible for the exclusion only if made on or after the date the IRA owner attains age 70½. This provision, which applies to both traditional and Roth IRAs, was scheduled to expire at the end of 2007 and was extended by EESA through the end of 2009.[41]

A qualified charitable distribution is any distribution from an IRA directly by the IRA trustee to an organization described in Section 170(b)(1)(A). Examples of these organizations include churches, tax-exempt educational organizations, hospitals, university endowment foundations, and public and private charities.

Federal Unemployment Tax Act (FUTA) Surtax of 0.2%

The Federal Unemployment Tax Act (FUTA) of 1939 (P.L. 76-379) established a joint state and federal basis for financing unemployment compensation (UC) created in the Social Security Act of 1935 (P.L. 74-271). FUTA imposes a 6.2% gross tax rate on the first $7,000 paid annually by covered employers to each employee in covered positions.

Employers in states with UC programs approved by the federal government and no delinquent federal loans to their state Unemployment Trust Fund (UTF) account may credit 5.4 percentage points against the 6.2% tax rate, making the minimum net federal unemployment tax rate 0.8%. Since all states have approved programs, 0.8% is the effective federal tax rate. This federal revenue finances administration of the system, half of the Federal-State Extended Benefits (EB) Program, and a federal account for state loans. The individual states finance regular UC benefits, as well as half of the EB Program through state taxes authorized by the State Unemployment Tax Acts.[42]

As part of the Unemployment Compensation Amendments of 1976 (P.L. 94-566), Congress passed a surtax of 0.2% of taxable wages to be added to the permanent FUTA tax rate. Thus, the current effective 0.8% FUTA tax rate has two components: a permanent tax rate of 0.6%, and a surtax rate of 0.2%. The surtax was introduced to help repay loans to the states from the federal

[41] For more information about IRAs, see CRS Report RL30255, *Individual Retirement Accounts (IRAs): Issues and Proposed Expansion*, by Thomas L. Hungerford and Jane G. Gravelle, CRS Report RL31770, *Individual Retirement Accounts and 401(k) Plans: Early Withdrawals and Required Distributions*, by John J. Topoleski. Distributions, by Patrick Purcell, and CRS Report RS22766, *Qualified Charitable Distributions from Individual Retirement Accounts: A Fact Sheet*, by John J. Topoleski.

[42] For more detailed information see CRS Report RL33362, *Unemployment Insurance: Available Unemployment Benefits and Legislative Activity*, by Katelin P. Isaacs, Julie M. Whittaker, and Alison M. Shelton.

account in UTF. Congress has extended the surtax five times, most recently with the Taxpayer Relief Act of 1997 (P.L. 105-34), which extends the tax through December 31, 2007.

Except for nonprofit organizations, state and local governments, certain agricultural labor, and certain domestic service, FUTA covers employers who pay wages of at least $1,500 during any calendar quarter or who employed at least one worker in at least one day of each of 20 weeks in the current or prior year. FUTA does cover agricultural labor for employers who paid cash wages of at least $20,000 for agricultural labor in any calendar quarter or who employed 10 or more workers in at least one day in each of 20 different weeks in the current or prior year, as well as domestic service employers who paid cash wages of $1,000 or more for domestic service during any calendar quarter in the current or prior year.

H.R. 6 from the 110th Congress, which was signed into law on December 19, 2007 (P.L. 110-140), extends the 0.2% surtax through 2008 and EESA extended the surtax through 2009.

Appendix. Tax Extenders Enacted for Past 10 Years

Table A-1. Tax Extender Packages

Emergency Economic Stabilization Act of 2008 P.L. 110-343 Enacted October 3, 2008	Retroactively extended the most recent set of temporary tax provisions for individuals and businesses that had expired in December 2007. The provisions were then scheduled to expire after December 31, 2009. TITLE II—EXTENSION OF INDIVIDUAL TAX PROVISIONS Sec. 201. Deduction for State and local sales taxes. Sec. 202. Deduction of qualified tuition and related expenses. Sec. 203. Deduction for certain expenses of elementary and secondary school teachers. Sec. 204. Additional standard deduction for real property taxes for nonitemizers. Sec. 205. Tax-free distributions from individual retirement plans for charitable purposes. Sec. 206. Treatment of certain dividends of regulated investment companies. Sec. 207. Stock in RIC for purposes of determining estates of nonresidents not citizens. Sec. 208. Qualified investment entities. TITLE III—EXTENSION OF BUSINESS TAX PROVISIONS Sec. 301. Extension and modification of research credit. Sec. 302. New markets tax credit. Sec. 303. Subpart F exception for active financing income. Sec. 304. Extension of look-thru rule for related controlled foreign corporations. Sec. 305. Extension of 15-year straight-line cost recovery for qualified leasehold improvements and qualified restaurant improvements; 15-year straight-line cost recovery for certain improvements to retail space. Sec. 306. Modification of tax treatment of certain payments to controlling exempt organizations. Sec. 307. Basis adjustment to stock of S corporations making charitable contributions of property. Sec. 308. Increase in limit on cover over of rum excise tax to Puerto Rico and the Virgin Islands. Sec. 309. Extension of economic development credit for American Samoa. Sec. 310. Extension of mine rescue team training credit. Sec. 311. Extension of election to expense advanced mine safety

	equipment. Sec. 312. Deduction allowable with respect to income attributable to domestic production activities in Puerto Rico. Sec. 313. Qualified zone academy bonds. Sec. 314. Indian employment credit. Sec. 315. Accelerated depreciation for business property on Indian reservations. Sec. 316. Railroad track maintenance. Sec. 317. Seven-year cost recovery period for motorsports racing track facility. Sec. 318. Expensing of environmental remediation costs. Sec. 319. Extension of work opportunity tax credit for Hurricane Katrina employees. Sec. 320. Extension of increased rehabilitation credit for structures in the Gulf Opportunity Zone. Sec. 321. Enhanced deduction for qualified computer contributions. Sec. 322. Tax incentives for investment in the District of Columbia. Sec. 323. Enhanced charitable deductions for contributions of food inventory. Sec. 324. Extension of enhanced charitable deduction for contributions of book inventory. Sec. 325. Extension and modification of duty suspension on wool products; wool research fund; wool duty refunds.
The Tax Relief and Health Care Act of 2006 P.L. 109-432 Enacted December 20, 2006	TITLE I–Extension and modification of certain tax provisions through December 31, 2007. Sec. 101. Deduction for qualified tuition and related expenses. Sec. 102. Extension and modification of new markets tax credit. Sec. 103. Election to deduct State and local general sales taxes. Sec. 104. Extension and modification of research credit. Sec. 105. Work opportunity tax credit and welfare-to-work credit. Sec. 106. Election to include combat pay as earned income for purposes of earned income credit. Sec. 107. Extension and modification of qualified zone academy bonds. Sec. 108. Above-the-line deduction for certain expenses of elementary and secondary school teachers. Sec. 109. Extension and expansion of expensing of brownfields remediation costs. Sec. 110. Tax incentives for investment in the District of Columbia. Sec. 111. Indian employment tax credit. Sec. 112. Accelerated depreciation for business property on Indian reservations. Sec. 114. Cover over of tax on distilled spirits. Sec. 115. Parity in application of certain limits to mental health benefits. Sec. 116. Corporate donations of scientific property used for research and of computer

	technology and equipment. Sec. 117. Availability of medical savings accounts. Sec. 118. Taxable income limit on percentage depletion for oil and natural gas produced from marginal properties. Sec. 119. American Samoa economic development credit.
Working Families Tax Relief Act of 2004 P.L. 108-311 Enacted October 4, 2004	TITLE III–Retroactive extensions of certain expiring tax provisions, generally through December 31, 2005. Sec. 301. Research credit. Sec. 302. Parity in the application of certain limits to mental health benefits. Sec. 303. Work opportunity credit and welfare-to-work credit. Sec. 304. Qualified zone academy bonds. Sec. 305. Cover over of tax on distilled spirits. Sec. 306. Deduction for corporate donations of scientific property and computer technology. Sec. 307. Deduction for certain expenses of school teachers. Sec. 308. Expensing of environmental remediation costs. Sec. 309. Certain New York Liberty Zone benefits. Sec. 310. Tax incentives for investment in the District of Columbia. Sec. 312. Allowance of nonrefundable personal credits against regular and minimum tax liability. Sec. 313. Credit for electricity produced from certain renewable resources. Sec. 314. Taxable income limit on percentage depletion for oil and natural gas produced from marginal properties. Sec. 315. Indian employment tax credit. Sec. 316. Accelerated depreciation for business property on Indian reservation. Sec. 318. Elimination of phaseout of credit for qualified electric vehicles for 2004 and 2005. Sec. 319. Elimination of phaseout for deduction for clean-fuel vehicle property.
Job Creation and Worker Assistance Act of 2002 P.L. 107-147 Enacted March 9, 2002	TITLE VI—Extension of certain expiring tax provisions, generally through December 31, 2003. Sec. 601. Allowance of nonrefundable personal credits against regular and minimum tax liability. Sec. 602. Credit for qualified electric vehicles. Sec. 603. Credit for electricity produced from certain renewable resources. Sec. 604. Work opportunity credit. Sec. 605. Welfare-to-work credit. Sec. 606. Deduction for clean-fuel vehicles and certain refueling property. Sec. 607. Taxable income limit on percentage depletion for oil and natural gas produced from marginal properties. Sec. 608. Qualified zone academy bonds.

	Sec. 609. Cover over of tax on distilled spirits. Sec. 610. Parity in the application of certain limits to mental health benefits. Sec. 611. Temporary special rules for taxation of life insurance companies. Sec. 612. Availability of medical savings accounts. Sec. 613. Incentives for Indian employment and property on Indian reservations.
Tax Relief Extension Act of 1999 P.L. 106-170 Enacted December 17, 1999	TITLE V—TAX RELIEF EXTENSION ACT OF 1999 (Sec. 500. Short title of title; Subtitle A—Extensions of certain expiring tax provisions, generally through December 31, 2001) Sec. 501. Allowance of nonrefundable personal credits against regular and minimum tax liability. Sec. 502. Research credit. Sec. 504. Taxable income limit on percentage depletion for marginal production. Sec. 505. Work opportunity credit and welfare-to-work credit. Sec. 506. Employer-provided educational assistance. Sec. 507. Extension and modification of credit for producing electricity from certain renewable resources. Sec. 508. Extension of duty-free treatment under Generalized System of Preferences. Sec. 509. Extension of credit for holders of qualified zone academy bonds. Sec. 510. Extension of first-time homebuyer credit for District of Columbia. Sec. 511. Extension of expensing of environmental remediation costs. Sec. 512. Temporary increase in amount of rum excise tax covered over to Puerto Rico and Virgin Islands.

Source: Information in this table was compiled by Pamela Jackson and Jennifer Teefy.

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