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Business Tax Provisions that Expired in 2017 ("Tax Extenders")

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Summary

Twelve temporary business tax provisions expired at the end of 2017. All of these provisions had expired at the end of 2016 but were retroactively extended by the Bipartisan Budget Act of 2018 (BBA; P.L. 115-123) and made available for the 2017 tax year, although one provision was extended through 2021.

This report briefly summarizes and discusses the economic impact of selected business-related tax provisions that expired at the end of 2017, including the following.

Special business investment (cost recovery) provisions:

- Special Expensing Rules for Certain Film, Television, and Live Theatrical Productions
- Seven-Year Recovery Period for Motorsports Entertainment Complexes
- Three-Year Depreciation for Race Horses Two Years or Younger
- Accelerated Depreciation for Business Property on an Indian Reservation
- Election to Expense Advanced Mine Safety Equipment

Economic development provisions:

- Empowerment Zone Tax Incentives
- American Samoa Economic Development Credit

Other business-related provisions:

- Credit for Certain Expenditures for Maintaining Railroad Tracks
- Deduction Allowable with Respect to Income Attributable to Domestic Production Activities in Puerto Rico
- Indian Employment Tax Credit
- Mine Rescue Team Training Credit
- Special Rate for Qualified Timber Gains

This report does not include provisions that in the past have been classified as individual or energy-related. See CRS Report R44925, *Recently Expired Individual Tax Provisions ("Tax Extenders"): In Brief*, coordinated by Molly F. Sherlock; and CRS Report R44990, *Energy Tax Provisions That Expired in 2017 ("Tax Extenders")*, by Molly F. Sherlock, Donald J. Marples, and Margot L. Crandall-Hollick. For a general overview of tax provisions that expired in 2016, see CRS Report R44677, *Tax Provisions that Expired in 2016 ("Tax Extenders")*, by Molly F. Sherlock.

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Introduction

In the past, Congress has regularly acted to extend expired or expiring temporary tax provisions.[1] Collectively, these temporary tax provisions are often referred to as "tax extenders." Of the 33 temporary tax provisions that expired at the end of 2016, 13 were business-related tax provisions.

All 13 business tax provisions that expired at the end of 2016 have been included in recent tax extenders legislation, although one was extended through 2021, leaving 12 that expired at the end of 2017. The business tax extenders are diverse in purpose, providing various types of tax relief to businesses in different industries. Most recently, Congress extended expiring tax provisions in the Bipartisan Budget Act of 2018 (BBA18; P.L. 115-123). This law retroactively extended temporary tax provisions that had expired at the end of 2016 through 2017.

This report briefly summarizes and discusses the economic impact of the 12 business-related tax provisions that expired at the end of 2017. All but one of the business provisions that expired at the end of 2016 was extended in the BBA18. The one business-related tax provision that expired at the end of 2016 that was not extended in the BBA18 was a provision relating to the allocation of qualified zone academy bonds; zone academy bonds were eliminated in the tax legislation enacted in December 2018 (P.L. 115-97). The tax legislation also ended the domestic production activity deduction in general for tax years beginning after December 31, 2017, but a special provision extending the deduction in general to Puerto Rico for the last year (2017) of the domestic production activity deduction was included. One provision that expired in 2016, the temporary increase in the limit on cover over of rum excise taxes to Puerto Rico and the Virgin Islands, was extended through 2021 in the BBA18.

There are several options for Congress to consider regarding temporary provisions. Provisions that expired at the end of 2017 could be extended. The extension could be retroactive. The extensions also could be short-term, long-term, or permanent. Another option would be to allow expired provisions to remain expired.

The amount of revenue that would be lost by temporarily extending business tax provisions that expired at the end of 2017 is generally small (see **Table 1**). For each provision included in this report, the one-year extension in the BBA18 was estimated to reduce revenues by less than $300 million over the 10-year (2018 through 2027) budget window.

Another option would be to extend expired provisions and make them permanent. The Joint Committee on Taxation (JCT) estimated the effects of making 10 of the provisions permanent. The list excluded the extension of the production activities deduction for Puerto Rico (given that the production activities deduction is repealed in general going forward) and the lower tax rate for timber gains, which would no longer be relevant given the lower corporate tax rate. It also excluded the increase in the rum cover over. According to JCT, making the 10 business provisions that expired at the end of 2016 and were extended through 2017 permanent would reduce federal revenues by an estimated $7.6 billion over the 10-year (2018 through 2027) budget window. Extending the rum cover over for an additional six years would add about $4 billion based on the one-year revenue cost.

[1] For an overview of tax extenders, see CRS Report R44677, *Tax Provisions that Expired in 2016 ("Tax Extenders")*, by Molly F. Sherlock.

Table 1. Estimated Cost of Extending Expired Business Tax Provisions
(billions of dollars)

Provision	Cost of Extension in P.L. 115-123	Cost to Make Permanent
Special Business Investment (Cost Recovery) Provisions		
Special Expensing Rules for Certain Film, Television, and Live Theatrical Productions	-i-	$0.4
Seven-Year Recovery Period for Motorsports Entertainment Complexes	-i-	$0.5
Three-Year Depreciation for Race Horses Two Years or Younger	-i-	$0.1
Accelerated Depreciation for Business Property on an Indian Reservation	$0.1	$1.4
Election to Expense Advanced Mine Safety Equipment	—	-i-
Economic Development Provisions		
Empowerment Zone Tax Incentives	$0.3	$2.3
American Samoa Economic Development Credit	-i-	$0.1
Other Business Provisions		
Credit for Certain Expenditures for Maintaining Railroad Tracks	$0.2	$2.1
Deduction Allowable with Respect to Income Attributable to Domestic Production Activities in Puerto Rico	$0.1	*
Indian Employment Tax Credit	$0.1	$0.6
Mine Rescue Team Training Credit	-i-	-i-
Special Rate for Qualified Timber Gains	-i-	*

Sources: Joint Committee on Taxation, Estimated Budget Effect of the Revenue Provisions Contained in the "Bipartisan Budget Act of 2018," February 8, 2018, JCX-4-18 and Federal Tax Provisions Expired in 2017, March 9, 2018, JCX-5-18.

Notes: The cost of permanent extension is as reported by JCT for the 2018 to 2027 budget window. A "*" indicates that the provision is not included in JCT's list of Federal Tax Provisions Expired in 2017 policy scenario, although the provision does appear in JCT's list of expiring tax provisions. An "-i-" indicates an estimated revenue loss of less than $50 million between 2018 and 2027.

Special Business Investment (Cost Recovery) Provisions

The cost of assets that provide services over a period of time, such as machines or buildings, is deducted over a period of years as depreciation. The schedule of depreciation deductions depends on the life of the asset and the distribution of deductions over that life. Straight-line depreciation is used for structures, where equal amounts are deducted in each year. For equipment, deductions are accelerated with larger amounts deducted in earlier years. Equipment is most commonly depreciated over 5 years or 7 years, but some short-lived assets are depreciated over 3 years and some longer-lived assets are depreciated over 10, 15, or 20 years. Nonresidential structures are depreciated over 39 years. Aside from the desire for economic stimulus, traditional economic

theories suggest that tax depreciation should match as closely as possible economic (physical) depreciation of assets.

The depreciation provisions discussed below all allow earlier deductions for depreciation, which are valuable because of the time value of money. Expensing provisions allow a firm to deduct the cost of an asset the year it is placed in service.

Investment in certain assets (largely equipment with shorter lives) was eligible for bonus depreciation that allowed half of cost to be expensed (deducted immediately) in 2017, including some of the assets discussed below that are depreciated over 7 years or 5 years. This bonus depreciation was originally scheduled to begin phasing out in 2018. Legislation enacted in December 2017 (P.L. 115-97) would allow 100% expensing of equipment for several years going forward. The presence of bonus depreciation or expensing would make some temporary provisions more important (such as the benefits for motorsports complexes, which would otherwise become ineligible) and some less important (such as shortening lives for racehorses or Indian reservation property, or expensing for films and television), which would have received the benefit regardless.

Special Expensing Rules for Certain Film, Television, and Live Theatrical Productions[2]

Investments in film and television productions are generally recovered using the income forecast method. Under this method, depreciation deductions are based on the pattern of expected earnings.

The American Jobs Creation Act of 2004 (P.L. 108-357) included special rules to allow expensing for certain film and television production costs. The main purpose of the provision was to discourage "runaway" productions, or the production of films and television shows in other countries, where tax and other incentives are often offered. Initially, the provision was set to expire at the end of 2008. However, since 2008, the provision has regularly been extended as part of "tax extender" legislation. The Protecting Americans from Tax Hikes (PATH) Act of 2015, Division Q of the Consolidated Appropriations Act, 2016 (P.L. 114-113), in addition to extending the provision, expanded it to include live theatrical productions taking place after December 31, 2015. The provision was most recently extended in the BBA18 (P.L. 115-123).

Under the special expensing rules for film, television, and live theatrical productions, taxpayers may elect to deduct immediately up to $15 million of production costs ($20 million for productions produced in certain low-income and distressed communities) in the tax year incurred. Eligible productions are limited to those in which at least 75% of the compensation paid is for services performed in the United States. For productions that started before 2008, the expensing deduction is not allowed if the aggregate production cost exceeds $15 million ($20 million for productions in designated low-income and distressed communities). Qualifying live theatrical productions are those generally performed in venues with an audience capacity of not more than 3,000 (or 6,500 for seasonal productions performed no more than 10 weeks annually). The provisions would cover most theatrical productions (the largest of the Broadway theatres, for example, has a seating capacity of less than 2,000).[3]

[2] IRC Section 181(f).

[3] For information on Broadway Theatre seating capacity see the New York Show Tickets website, at http://www.nytix.com/Links/Broadway/broadwaytheatres.html.

The ability to expense (deduct immediately) certain film, television, and live theatrical production costs provides a benefit by allowing deductions to be taken earlier, thus deferring tax liability. The magnitude of the benefit depends on the average lag time from production to earning income. For many films, production costs would be deductible in the year the film is released. If the film is released one year after the production costs are incurred, which may be the case for independent and smaller productions, the provision accelerates cost recovery by one year. The benefit conferred by accelerating cost recovery deductions by one year is limited. Furthermore, taxpayers with limited or no tax liability may derive little or no benefit from the expensing allowance.

The primary policy objective of providing special tax incentives for film and television producers is to deter productions from moving overseas, lured by lower production costs as well as tax and other subsidies offered by foreign governments. Because live theatre is tied to audience location, "runaway" productions are not a concern. However, providing expensing for live theatrical production costs could encourage investment in such productions and provide parity with film and television. In evaluating this incentive, one consideration is the economic value of domestic film, television, and theatre production relative to the cost of the targeted tax benefits.

Seven-Year Recovery Period for Motorsports Entertainment Complexes[4]

An exception from the 39-year depreciation life for nonresidential structures exists for the theme and amusement park industry. Assets in this industry are assigned a recovery period of seven years. Historically, motorsports racing facilities have been included in this industry and also allowed a seven-year recovery period. However, ambiguities in the law led to questions about whether motorsports racing facilities were correctly categorized. When the Treasury reconsidered the appropriateness of this classification in 2004, Congress made the seven-year treatment mandatory through 2007 with the American Jobs Creation Act (P.L. 108-357). Since 2004, the provision has been extended as part of "tax extenders" legislation—most recently in the BBA18 (P.L. 115-123), which extended the provision through December 31, 2017. Without this provision, motorsports racing facilities would be depreciated over the standard 39-year life.

The tax authorities presumably estimated motorsports racing facilities to have slower depreciation rates than the seven-year life that applies to amusement park facilities. If so, this provision constitutes a subsidy to the auto racing industry that does not appear to have an obvious justification. Supporters argued that the provision preserves historical treatment and provides a stimulus to business. They also argued that the benefit helps make them more competitive with sports facilities that are often subsidized by state and local governments.

Three-Year Depreciation for Racehorses Two Years or Younger[5]

Race horses are tangible property, and taxpayers using racehorses in a trade or business must capitalize the cost of purchasing racehorses. The cost can then be recovered through annual depreciation deductions over time. The cost recovery period for racehorses is seven years, although racehorses that begin training after age two have a three-year recovery period. Under the temporary provision, this three-year recovery period is extended to all racehorses. In particular, all racehorses placed in service after December 31, 2008, have a three-year recovery period as a result of the Food, Conservation, and Energy Act of 2008 (P.L. 110-246), with provisions

[4] IRC Sections 168(i)(15) and 168(e)(3)(C)(ii).

[5] IRC Section 168(e)(3)(A).

subsequently extended. This provision was extended through 2017 by the BBA18 (P.L. 115-123). The industry claims that reducing the recovery period to three years more closely aligns the recovery period with the racing life of a horse. The IRS cost recovery period suggests a longer view. Some racehorses continue in productive activity after their racing career through breeding, as well as having a residual value for resale. A Treasury study estimated, taking those uses into account, an overall economic life of nine years.[6]

This provision does not affect breeders who race their own horses, because they deduct the cost of breeding and thus have no basis (capital investment) in the horses. The provision generally benefits investors who purchase horses.

Accelerated Depreciation for Business Property on an Indian Reservation[7]

The Omnibus Budget Reconciliation Act of 1993 (P.L. 103-66) contained a provision allowing businesses on Indian reservations to be eligible for accelerated depreciation (through a reduction in the applicable recovery periods) as part of an effort to increase investment in Indian Reservations. Since its initial temporary enactment, this provision has regularly been extended as part of "tax extenders" legislation—most recently in the BBA18 (P.L. 115-123), which extended the provision through December 31, 2017.

Extending the provision might encourage additional investment on Indian Reservations. However, if the main target of these provisions is an improvement in the economic status of individuals currently living on Indian Reservations, it is not clear to what extent this tax subsidy will succeed in that objective, as these subsidies are not given directly to workers but instead are received by businesses. Capital subsidies may not ultimately benefit workers. It is possible that capital equipment subsidies may encourage more capital-intensive businesses and make workers relatively worse off. In addition, workers would not benefit from higher wages resulting from an employer subsidy if the wage is determined by regulation (the minimum wage) that is set higher than the prevailing market wage.

Election to Expense Advanced Mine Safety Equipment[8]

Taxpayers can elect to expense 50% of the cost of advanced mine safety equipment. Advanced mine safety equipment property includes emergency communication technologies or devices that allow a miner to maintain constant communication with an individual not in the mine; electronic identification and location devices that allow individuals not in the mine to track the location and movement of miners in the mine; emergency oxygen-generating, self-rescue devices that provide oxygen for at least 90 minutes; prepositioned supplies of oxygen that can be used with self-rescue devices to provide each miner on a shift oxygen for at least 48 hours; and comprehensive atmospheric monitoring systems that monitor levels of carbon monoxide, methane, and oxygen in all areas of the mine, and that can detect smoke in a mine. To qualify, mine safety equipment must be used in a mine located in the United States.

[6] U.S. Department of the Treasury, Report to Congress on the Depreciation of Horses, March 1990, at https://www.treasury.gov/resource-center/tax-policy/Documents/Report-Depreciation-Horses-1990.pdf.

[7] IRC Section 168(j)(8).

[8] IRC Section 179E(g).

The cost of any mine safety equipment that is expensed under Section 179 is not taken into account when computing the 50% deduction for advanced mine safety equipment.[9] Under Section 179, in 2017, businesses will be able to deduct up to $510,000.[10] This expense deduction is allowed instead of depreciation. The ability to expense investments is subject to an investment limitation, and begins to phase out once investment exceeds $2,030,000 in 2017 (the expensing limit and investment limit are adjusted for inflation). Taxpayers must reduce their basis in qualified advanced mine safety equipment by the amount deducted.

The provision allowing for 50% of advanced mine safety equipment expenditures to be expensed was enacted in the Tax Relief and Health Care Act of 2006 (P.L. 109-432). It was initially scheduled to be effective for 2006, 2007, and 2008. It was temporarily extended in the Emergency Economic Stabilization Act (P.L. 110-343) and has subsequently been extended as part of "tax extenders" legislation.

Federal regulations are the government's primary policy instrument governing coal mine safety, with tax incentives playing a small role.[11] The election to expense advanced mine safety equipment, along with the mine rescue team training credit (discussed below), were enacted following the high-profile mining accident at Sago Mine. There was an uptick in coal mining fatalities in 2006—47 fatalities were reported (12 were a result of the Sago Mine disaster).[12] From 2007 through 2016, coal mining fatalities averaged 21 per year. During this period, fatalities were highest in 2010, reflecting the Upper Big Branch Mine disaster, where there were 29 fatalities. In the year with the lowest number of fatalities, 2016, there were 8. Coal mining fatalities have trended down over time. In recent years, some of this might be explained by a decline in coal production and the decline in the number of coal miners. The fatality rate, however, has also declined over time.

Expensing advanced mine safety equipment reduces the effective tax rate on such investments, and can encourage taxpayers to shift investment to qualifying equipment.

Economic Development Provisions

Empowerment Zone Tax Incentives[13]

Empowerment Zones (EZs) are federally designated geographic areas characterized by high levels of poverty and economic distress, where businesses and local governments may be eligible to receive federal grants and tax incentives.[14] Since 1993, Congress has authorized three rounds of EZs (1993, 1997, and 1999) with the objective of revitalizing selected economically distressed

[9] CRS Report RL31852, *The Section 179 and Bonus Depreciation Expensing Allowances: Current Law and Issues for the 114th Congress*, by Gary Guenther.

[10] The Section 179 expensing allowance had been a temporary provision, but was made permanent in the PATH Act of 2015.

[11] 30 C.F.R. §49. For background information, see CRS Report RL34429, *Coal Mine Safety and Health*. (This out-of-print CRS report is available to congressional clients from the authors upon request.)

[12] U.S. Department of Labor, Mine Safety and Health Administration, *Coal Fatalities for 1900 through 2016*, available at https://arlweb.msha.gov/stats/centurystats/coalstats.asp.

[13] For related provisions, see IRC Sections 1391, 1394, 1396, 1397A, and 1397B.

[14] For a list of EZs, see U.S. Department of Housing and Urban Development (HUD), "List of Current Empowerment Zones and Updated Contact Information," at http://portal.hud.gov/hudportal/HUD?src=/program_offices/comm_planning/economicdevelopment/programs/rc/ezcontacts.

communities. EZs are similar to Enterprise Communities (ECs) and Renewal Communities (RCs), which are also federally designated areas for the purposes of tax benefits and grants.

A number of studies have evaluated the effectiveness of the EZ, EC, and RC programs. The Government Accountability Office (GAO) and the Department of Housing and Urban Development (HUD) have failed to link EZ and EC designation with improvement in community outcomes.[15] Other research has found modest, if any, effects and calls into question the cost-effectiveness of these programs. This inability to link these programs to improvements in community level outcomes should not be interpreted as meaning that the EZ, EC, and RC programs did not aid economic development. The main conclusion from these studies is that the EZ, EC, and RC programs have not been shown to have caused a general improvement in the economic conditions of the localities. One possible cause for this inability to empirically show the program effects on a large geographic area is that the EZ tax incentives are relatively small. Another possibility is that the EZ tax incentives are targeted at business owners and do not provide direct benefits to workers in EZs.

Six tax incentives are typically related to EZs:[16] (1) local designation of an EZ;[17] (2) increased exclusion of gain;[18] (3) issuance of qualified, tax-exempt zone academy bonds (QZABs) in EZs;[19] (4) EZ employment credits under the Work Opportunity Tax Credit (WOTC);[20] (5) increased expensing under IRC Section 179 for businesses located in EZs;[21] and (6) nonrecognition of gain on rollover of EZ investments.[22]

EZs were created by legislation enacted in 1993, and most zones expired at the end of 2009. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312) extended the EZ and District of Columbia Enterprise Zone designations to December 31, 2011. The American Taxpayer Relief Act of 2012 (P.L. 112-240) extended EZ designations through 2013.[23] The Tax Increase Prevention Act of 2014 (P.L. 113-295) extended the EZ tax incentives for one year (through 2014). The Protecting Americans from Tax Hikes (PATH) Act of 2015 (P.L. 114-113) extended the EZ tax incentives for two years (through 2016) with a 10-year revenue cost of $502 million.[24] Additionally, P.L. 114-113 amended the requirements for tax-exempt enterprise zone facility bonds to treat an employee as a resident of a particular EZ if they

[15] For more discussion, see CRS Report R41639, *Empowerment Zones, Enterprise Communities, and Renewal Communities: Comparative Overview and Analysis*, by Donald J. Marples.

[16] For a quick reference chart with a description of each of these provisions, see U.S. Department of Housing and Urban Development (HUD), *Empowerment Zone Tax Incentives Summary Chart*, August 2013, at http://portal.hud.gov/hudportal/documents/huddoc?id=ez_tis_chart.pdf.

[17] IRC Sections 1391(d)(1)(A)(i) and (h)(2).

[18] IRC Sections 1202(a)(2) and 1391(d)(1)(A)(i).

[19] IRC Sections 1394 and 1391(d)(1)(A)(i).

[20] IRC Sections 1396 and 1391(d)(1)(A)(i). For more information of the WOTC, see CRS Report R43729, *The Work Opportunity Tax Credit*, by Benjamin Collins and Sarah A. Donovan.

[21] IRC Sections 1397A and 1391(d)(1)(A)(i). For more information on Section 179 expensing see CRS Report RL31852, *The Section 179 and Bonus Depreciation Expensing Allowances: Current Law and Issues for the 114th Congress*, by Gary Guenther.

[22] IRC Sections 1397B and 1391(d)(1)(A)(i).

[23] However, ATRA did not provide for the extension of the designation for the District of Columbia Enterprise Zone, and therefore that designation ended on December 31, 2011.

[24] JCT, Estimated Revenue Budget Effects of Division Q of Amendment #2 To The Senate Amendment To H.R. 2029 (Rules Committee Print 114-40), The "Protecting Americans From Tax Hikes Act of 2015," December 16, 2015, at https://www.jct.gov/publications.html?func=startdown&id=4860.

are a resident of a different EZ, EC, or qualified low-income community. The provisions were extended through 2017 by the BBA18 (P.L. 115-123).

For more analysis of EZs, see CRS Report R41639, *Empowerment Zones, Enterprise Communities, and Renewal Communities: Comparative Overview and Analysis*, by Donald J. Marples.

American Samoa Economic Development Credit[25]

The American Samoa economy is largely dependent on three sectors: public works and government, tuna canning, and the residual private sector (e.g., tourism and other services).

The American Samoa economic development credit (EDC) is a credit against U.S. corporate income tax in an amount equal to the sum of certain percentages of a domestic corporation's employee wages, employee fringe benefit expenses, and tangible property depreciation allowances for the taxable year with respect of the active conduct of a trade or business within American Samoa. The credit is available to U.S. corporations that, among other requirements, (1) claimed the now-expired possession tax credit (predecessor to the EDC) with respect to American Samoa for its last taxable year beginning before January 1, 2006; or (2) have qualified production activities income after December 31, 2011, in American Samoa (akin to production activities income eligible for Section 199 tax treatment in the United States).[26]

Proponents of the credit claim it encourages eligible companies to locate, retain, or expand manufacturing operations in the territory. Media reports suggest the main beneficiary of the EDC, thus far, has been StarKist, which has retained its cannery operations in American Samoa.[27]

The EDC was first enacted in the Tax Relief and Health Care Act of 2006 (P.L. 109-432) and originally expired at the end of 2007. This version of the EDC was only eligible to corporations that had previously claimed the possession tax credit. The EDC was extended by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312) through 2011. The American Tax Relief Act of 2012 (P.L. 112-240) extended the EDC through 2013 and expanded the EDC's criteria to include corporations that had not previously claimed the possession tax credit. The Tax Increase Prevention Act of 2014 (P.L. 113-295) extended the EDC for one year (through 2014) with a revenue cost of $14 million.[28] The Protecting Americans from Tax Hikes (PATH) Act of 2015 (P.L. 114-113) extended the EDC for two years (through 2016) with a 10-year revenue cost of $32 million.[29] The provision was extended through 2017 by the BBA18 (P.L. 115-123).

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[25] Section 119 of the Tax Relief and Health Care Act of 2006 (P.L. 109-432) as amended by Section 756 of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312), based on the rules of IRC Sections 30A and 936.

[26] See Section 936 of H.Rept. 109-455 and Section 329 of P.L. 112-240. See also JCT, *General Explanation of Tax Legislation Enacted in 2015*, JCS-1-16, March 2016, pp. 196-198, at https://www.jct.gov/publications.html?func=startdown&id=4509. For more information on Section 199, see CRS Report R41988, *The Section 199 Production Activities Deduction: Background and Analysis*, by Molly F. Sherlock.

[27] See "Starkist Am. Samoa Welcomes Tax Credit Extension," *Pacific Islands Report*, Pacific Islands Development Program at the East-West Center, December 23, 2015, at http://www.pireport.org/articles/2015/12/23/starkist-am-samoa-welcomes-tax-credit-extension.

[28] JCT, *Estimated Revenue Effects of* H.R. 5771, *the "Tax Increase Prevention Act of 2014,"* scheduled for consideration by the House of Representative on December 3, 2014, JCX-107-14R, December 3, 2014, at https://www.jct.gov/publications.html?func=startdown&id=4677.

[29] JCT, Estimated Revenue Budget Effects Of Division Q Of Amendment #2 To The Senate Amendment To H.R. 2029

Other Business Provisions

Credit for Certain Expenditures for Maintaining Railroad Tracks[30]

Qualified railroad track maintenance expenditures paid or incurred in a taxable year by eligible taxpayers qualify for a 50% business tax credit. The credit is limited to $3,500 times the number of miles of railroad track owned or leased by an eligible taxpayer. Qualified railroad track maintenance expenditures are amounts, which may be either repairs or capitalized costs, spent to maintain railroad track (including roadbed, bridges, and related track structures) owned or leased as of January 1, 2005, by a Class II or Class III (regional or local) railroad. Eligible taxpayers are smaller (Class II or Class III) railroads and any person who transports property using these rail facilities or furnishes property or services to such a person.

The taxpayer's basis in railroad track is reduced by the amount of the credit allowed (so that any deduction of cost or depreciation is only on the cost net of the credit). The credit cannot be carried back to years before 2005. The credit is allowed against the alternative minimum tax. The amount eligible is the gross expenditures, not taking into account reductions such as discounts or loan forgiveness.

The provision was enacted in the American Jobs Creation Act of 2004 (P.L. 108-357). The provision relating to discounts was added by the Tax Relief and Health Care Act of 2006 (P.L. 109-432). The credit was allowed against the alternative minimum tax by the Emergency Economic Stabilization Act of 2008 (P.L. 110-343).

This provision substantially lowers the cost of track maintenance for the qualifying short line (regional and local) railroads, with tax credits covering half the costs for those firms and individuals with sufficient tax liability. Class II and III railroads account for 31% of the nation's rail miles.[31] These regional railroads are particularly important in providing transportation of agricultural products.

Although no rationale was provided when the credit was introduced, sponsors of earlier free-standing legislation and industry advocates indicated that the purpose was to encourage the rehabilitation, rather than the abandonment, of short-line railroads. These railroads were spun off in the deregulation of railroads in the early 1980s. Advocates also indicated that this service is threatened by heavier 286,000-pound cars that must be used to connect with longer rail lines. They also suggested that preserving these local lines will reduce local truck traffic. There was also some indication that a tax credit was thought to be more likely to be achieved than grants.

The arguments stated by industry advocates and sponsors of the legislation are also echoed in assessments by the Federal Railroad Administration (FRA), which indicated the need for rehabilitation and improvement, especially to deal with heavier cars. The FRA also suggested that these firms have limited access to bank loans.

In general, special subsidies to industries and activities tend to lead to inefficient investment allocation, since in a competitive economy businesses should earn enough to maintain their capital. Nevertheless it may be judged or considered desirable to subsidize rail transportation to

(Rules Committee Print 114-40), The "Protecting Americans From Tax Hikes Act of 2015," JCX-143-15, December 16, 2015, at https://www.jct.gov/publications.html?func=startdown&id=4860.

[30] IRC Section 45G(f).

[31] *Class I Railroad Statistics*, Association of American Railroads, May 1, 2017, at https://www.aar.org/data-center/rail-traffic-data/.

reduce the congestion and pollution of highway traffic. At the same time, a tax credit may be less suited to remedy the problem than a direct grant because firms without sufficient tax liability cannot use the credit.

Deduction Allowable with Respect to Income Attributable to Domestic Production Activities in Puerto Rico[32]

The Section 199 domestic production activities deduction reduces tax rates on certain types of economic activity, primarily domestic manufacturing activities. Qualified domestic manufacturing activities qualify for a deduction equal to 9% of the lesser of taxable income derived from qualified production activities or taxable income. The effect of the deduction is to reduce the effective tax rate on income from qualified activities by 3.15 percentage points, from 35% to 31.85%. Before 2018, the Section 199 domestic production activities deduction was a permanent part of the Internal Revenue Code (IRC). Section 199 has been repealed, going forward, by the 2017 tax legislation (P.L. 115-97), so future extensions are unlikely.

When the Section 199 deduction was enacted as part of the American Jobs Creation Act of 2004 (P.L. 108-357), the term "United States," as used for the purposes of determining eligible domestic activities, included the 50 states and the District of Columbia, but not U.S. possessions or territories. In 2006, as part of the Tax Relief and Healthcare Act (P.L. 109-432), special rules that allowed Puerto Rico to be considered a part of the United States for the purposes of the Section 199 domestic production activities deduction were temporarily enacted. This temporary provision has recently been extended as part of "tax extenders" legislation.

The U.S. tax code generally treats U.S. possessions as foreign countries, and Puerto Rico maintains an independent tax system.[33] There are, however, many special rules interconnecting the Puerto Rican and U.S. tax systems. Before 1996, domestic corporations with business operations in the U.S. possessions could generally eliminate their U.S. tax liability on foreign-source income from operations in the possessions using the possessions tax credit. From 1996 through 2005, the Puerto Rico economic activity credit was available for domestic corporations with activities in Puerto Rico. Following the expiration of the possessions tax credit and Puerto Rico economic activity credit, companies with operations in Puerto Rico may find it more advantageous to structure as a controlled foreign corporation (CFC), thus benefitting from the option to defer U.S. tax on active income from those operations.

Allowing the Section 199 production activities deduction to be claimed on manufacturing activities in Puerto Rico can be viewed as an effort to provide similar tax treatment to income from manufacturing activities taking place in Puerto Rico and from the rest of the United States.[34] Absent this provision, U.S.-based manufacturers with operations in Puerto Rico, operating in flow-through form (e.g., a branch or partnership), would face a higher effective tax rate on manufacturing activities in Puerto Rico than other domestic manufacturing activities.

Allowing the Section 199 deduction for activities in Puerto Rico essentially extends a tax benefit designed for domestic corporations to a possession that is generally treated as a foreign country for tax purposes. This raises the question of why this tax benefit has been provided to Puerto Rico

[32] IRC Section 199(d)(8).

[33] See CRS Report R44651, *Tax Policy and U.S. Territories: Overview and Issues for Congress*, by Sean Lowry.

[34] See U.S. Congress, Joint Committee on Taxation, An Overview Of The Special Tax Rules Related To Puerto Rico And An Analysis Of The Tax And Economic Policy Implications Of Recent Legislative Options, 109th Cong., June 23, 2006, JCX-24-06, at https://www.jct.gov/publications.html?func=startdown&id=1496.

but no other U.S. possessions. Concerns have also been raised that extending Section 199 to Puerto Rico would create an incentive for U.S. companies operating in Puerto Rico to adopt a bifurcated structure, with certain activities being undertaken by a CFC and with other activities, specifically those that qualify for Section 199, being undertaken in a flow-through structure.[35] Since other domestic businesses do not have this organizational flexibility, this would provide greater potential benefits to manufacturers with operations in Puerto Rico. This could be the intent of the policy, if extending Section 199 to businesses in Puerto Rico is intended, in part, to encourage additional manufacturing activity in Puerto Rico.

For general information on the Section 199 deduction, see CRS Report R41988, *The Section 199 Production Activities Deduction: Background and Analysis*, by Molly F. Sherlock; and CRS In Focus IF10688, *Key Issues in Tax Reform: The Section 199 Deduction*, by Molly F. Sherlock.

Indian Employment Tax Credit[36]

The Indian employment tax credit is an incremental credit claimed by employers for qualified wages and health insurance costs. The credit is designed to encourage hiring of certain individuals—enrolled members of an Indian tribe and their spouses. There are restrictions limiting the benefit to services performed within an Indian reservation for individuals living on or near the reservation.

The Indian employment credit is 20% of the excess of qualified wages and health insurance costs over base-year expenses, paid by an employer. The credit is allowed for the first $20,000 in qualified wages and health insurance costs. The base year is 1993, such that the incentive is incremental to 1993 wages and health insurance costs (the base year has not been changed since the credit was enacted). The credit is not available for wages paid to an employee whose total wages exceed $30,000, as adjusted for inflation ($45,000 in 2015 and 2016). The employer must reduce their deduction for wages by the amount of the credit.

The Indian employment credit was first enacted in 1993, as part of the Omnibus Reconciliation Act of 1993 (P.L. 103-66). It was initially scheduled to expire at the end of 2003, but has been regularly extended, often retroactively. Past extensions of the Indian employment credit have extended the termination date without updating the base year. Some have proposed updating the base year, in an effort to (1) eliminate the need for taxpayers to maintain tax records dating back to 1993, and (2) restore the incremental design of the credit.[37]

Extending the Indian employment credit might encourage additional hiring of Indian tribe members and their spouses. While the Indian employment credit may not increase overall employment on or near Indian reservations, it might increase employment among tribe members.

Mine Rescue Team Training Credit[38]

Taxpayers that employ miners in underground mines located in the United States may be able to claim a tax credit for mine rescue team training expenses. The credit amount is limited to the lesser of (1) 20% of training program costs per employee (including wages paid to the employee

[35] Ibid., pp. 90-93.

[36] IRC Section 45A(f).

[37] See, for example, Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2017 Revenue Proposals*, Washington, DC, February 2016, pp. 39-41, at http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2017.pdf.

[38] IRC Section 45N(e).

while in training); or (2) $10,000. For a taxpayer to claim the credit for training provided to an employee, the employee must be a full-time miner who is eligible to serve as a mine rescue team member.

The mine rescue team training credit was enacted in the Tax Relief and Health Care Act of 2006 (P.L. 109-432). It was initially scheduled to be effective for 2006, 2007, and 2008. It was temporarily extended in the Emergency Economic Stabilization Act of 2008 (P.L. 110-343) and has subsequently been extended as part of "tax extenders" legislation.

The mine rescue team training credit was enacted at the end of 2006, following the high-profile mining accident at Sago Mine. There was an uptick in coal mining fatalities in 2006—47 fatalities were reported (12 were a result of the Sago Mine disaster).[39] From 2007 through 2016, coal mining fatalities averaged 21 per year. During this period, fatalities were highest in 2010, reflecting the Upper Big Branch Mine disaster, where there were 29 fatalities. In the year with the lowest number of fatalities, 2016, there were 8. Coal mining fatalities have trended down over time. In recent years, some of this might be explained by a decline in coal production and the decline in the number of coal miners. The fatality rate, however, has also declined over time.

A credit for mine rescue team training can encourage mine operators and employers to invest in additional training. The credit can also reduce the cost of complying with federal regulations regarding mine rescue team training.[40] Federal regulations are the government's primary policy instrument governing coal mine safety, with tax incentives playing a small role.[41]

Special Rate for Qualified Timber Gains[42]

For taxable years beginning in 2016, qualified timber gains of C corporations are subject to an alternative maximum tax rate of 23.8%. If net capital gains are less than timber gains, the 23.8% rate applies to net capital gains. A qualified timber gain is the net gain from the sale of cutting standing timber, disposing of timber with a retained economic interest, or the outright sale of timber. The special rate applies only to timber that has been held for more than 15 years. Typically, for C corporations, net capital gains are taxed at the same rate as ordinary income, with the maximum rate being 35%. Under the individual income tax, the maximum rate on net capital gains is 20%, with certain capital gains subject to an additional 3.8% tax.

This provision was enacted for one year as part of the Protecting Americans from Tax Hikes (PATH) Act of 2015 (P.L. 114-113). Taxpayers other than C corporations have long been able to treat gains from the cutting of timber or sale of standing timber as capital gains, so long as the timber was held for more than one year. The special rate enacted for 2016 extends this treatment to C corporations meeting a 15-year holding period requirement. Congress acted in the past to provide "greater equivalence to the capital gain tax treatment of timber gain" between companies operating under different organizational forms.[43] A 15% alternative tax rate for C corporation's

[39] U.S. Department of Labor, Mine Safety and Health Administration, *Coal Fatalities for 1900 through 2016*, at https://arlweb.msha.gov/stats/centurystats/coalstats.asp.

[40] More on federal requirements for mine rescue team training can be found on the U.S. Department of Labor, Mine Safety and Health Administration website, at https://www.msha.gov/training-education/mine-rescue-training.

[41] 30 C.F.R. §49. For background information, see CRS Report RL34429, *Coal Mine Safety and Health*. (This out-of-print CRS report is available to congressional clients from the authors upon request.)

[42] IRC Section 1201(b).

[43] Joint Committee on Taxation, "General Explanation of Tax Legislation Enacted in the 110th Congress," JCS-1-09, March 2009, pp. 97-102, at http://www.jct.gov/s-1-09.pdf.

qualified timber gains (or, if less, net capital gains) for timber that had been held more than 15 years was temporarily enacted in 2008, but was not extended.[44]

Proponents of the provision argue that timber sales should be treated as capital gains, but that the tax rate applied to timber gains earned by C corporations should be the same as the tax rate applied to timber gains earned by S corporations or other pass-through entities. Those opposed to the special rate argue that providing capital gains treatment to timber gains of C corporations allows this form of income to be lightly taxed, especially after accounting for other tax provisions that reduce effective corporate tax rates.

The 2017 tax legislation (P.L. 115-97) reduced the corporate rate to 21% going forward, so this provision will no longer be a benefit even if extended in the future.

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[44] The Food, Conservation, and Energy Act of 2008 (P.L. 110-246), also known as the "Farm Bill."