dollars to make up for low prices. Yeah that's great, but if the prices were better then we wouldn't have to deal with this.

Now it's time for a new farm bill The House passed their version in October and the Senate passed theirs this month. There are several differences in the two bills. The House bill would spend about $36 billion over five years and the Senate bill would spend $44 billion in five years. The Senate has payment limitations, which would restrict large farms from receiving huge amounts of money from the government, and a ban on meatpackers owning livestock more than two weeks before slaughter. The House bill spends more on a farm safety net than the Senate bill. The House and Senate each have a committee and they are going to come up with a farm bill that everyone can agree with. They plan on meeting and coming up with a bill by Easter, before Congress recesses.

Something that every citizen can do, and should do, is write his or her congressperson. President Eisenhower once said, ''Farming looks mighty easy when your plow is a pencil, and you're a thousand miles from the cornfield.'' Tell your congressperson how much agriculture affects you. Let him or her know that you support the farm bill. Convince him. Sway him. Just let him know you are out here.

I live on a fifth-generation farm. Farming is all we have. Without it, we have nothing. My grandpa, my uncle and my father—farming is all they know. My brothers want to come back and farm, but will they be able to and will they even want to? Will the market prices be too low and the price to farm too high? Will a corporate farm buy us out? Losing a farm is not like losing a job; it is losing both your livelihood and your home. It's a way of life that is unique and it cannot simply be replaced with something else, because there is nothing else like it.

Something has to change or we can kiss agriculture goodbye not only on my farm, not only in Illinois, but in America. Something has to be done. It's time for change.

INDIVIDUAL AND SMALL BUSINESS TAX SIMPLIFICATION ACT OF 2002

HON. AMO HOUGHTON

OF NEW YORK

IN THE HOUSE OF REPRESENTATIVES

Tuesday, October 1, 2002

Mr. HOUGHTON. Mr. Speaker, today I am introducing a bill, the Individual and Small Business Tax Simplification Act, to address an ever-increasing problem. In 1935, there were 34 lines on Form 1040 and instructions were two pages. Today, there are well over 13,000 pages of forms and instructions. The tax code and regulations have mushroomed to over 9 million words. Approximately eighty-percent of the paperwork burden of the entire federal government is related to tax compliance, and the extent of this burden is staggering. In 2001, individual taxpayers spent an estimated 2½ billion hours on federal tax compliance. Businesses spent an additional 2 billion hours. The value of this lost time is incalculable, but it does not even include the economic cost of decisions based on a faulty understanding of the law. Nor does the 4½ billion hour total include time spent on planning. An added cost of complexity is that it undermines voluntary compliance. It is a haven for promoters of dubious schemes and it often produces unintended consequences.

There are legitimate reasons for some of this complexity. Defining income in a manner that is fair and easy to administer is inherently complex, and, it must be acknowledged, any tax measured by income—even a flat tax—must reflect the way income is earned in a complex economy such as our own. But, for a variety of reasons, the tax code has become far more complicated than necessary. In many cases, there is a clear answer to the question of whether a rational person would design a tax provision the same way from a clean slate. The objective of the legislation I am introducing today is to roll back this sort of complexity. One or more of the bill's provisions would simplify annual filing for every individual taxpayer.

This legislation builds on a bill that I introduced in the 106th Congress, the Tax Simplification and Burden Reduction Act. The Ways and Means Subcommittee on Oversight has held numerous hearings on tax simplification, and the bill draws on the record built at those hearings. Several of the provisions of this legislation appeared first as recommendations in the Joint Committee on Taxation's April, 2001 report, and the staff of the Joint Committee on Taxation has helped to refine all of the proposals contained in the bill. Other provisions originated with the work of the Tax Section of the American Bar Association and the American Institute of Certified Public Accountants. I welcome comments from other individuals and organizations on the bill and other simplification measures.

Our future as a nation depends on our ability to raise revenue in a manner that is fair and equitable. The Internal Revenue Code must be simplified to restore faith by all taxpayers in our tax system.

The proposal includes the following provisions:

I. INDIVIDUAL INCOME TAX SIMPLIFICATION

Alternative Minimum Tax—Inflation has caused many middle-income taxpayers to be subject to AMT by eroding the value of the AMT exemption. Rising state and local taxes have added to the problem, because state taxes are not deductible in calculating taxable income for AMT purposes. The failure to allow a state and local tax deduction for AMT purposes is one of the most unfair aspects of the Internal Revenue Code. It results in double taxation of income, and it forces taxpayers who live in states with higher income taxes to bear a larger percentage of the federal tax burden than those who live in states with lower taxes or no tax. If we allow the AMT to remain unaddressed, this unfair and inequitable disparity will worsen over time.

As a result of inflation, the Joint Committee on Taxation predicts that more than 35 million will pay AMT within ten years. Currently, AMT affects less than 2 million taxpayers. A recent study by the Urban-Brookings Tax Policy Center confirms this finding and further notes that if left unattended the AMT will shift a substantial portion of the tax burden of this country to urban and suburban middle-class taxpayers. Congress would not design a system with these features deliberately, and we should not allow it to happen by default.

Under the proposal, the AMT exemption would be adjusted for inflation since the date it was enacted and indexed for inflation in future years. State and local taxes would become fully deductible under the new AMT. The effect of these changes will be to restore AMT to its intended purpose and stop its growth.

Replace Head of Household Filing Status with New Exemption—Head of Household filing status has long been a leading-source of taxpayer confusion and mistakes during the filing season. In 2000, the IRS fielded over half a million taxpayer questions on filing status. An error on filing status can have consequences throughout the return, and it can lead to costly interest and penalty charges later on. To address this problem, the bill replaces Head of Household filing status with a $3,700 ''Single Parent Exemption.'' This amount will be indexed. The proposal, as a whole, is revenue neutral.

The bill achieves further simplification by cross referencing the new uniform definition of a qualifying child.

Simplified Taxation of Social Security Benefits—Under present law, determining whether and how much social security benefits are subject to tax is a highly involved process that requires the completion of an 18 line worksheet. Many taxpayers are not eligible to use this worksheet, and they must refer to a 27 page publication.

The bill would simplify the calculation by repealing the 85% inclusion rule that was enacted in 1993. This alone would remove 6 lines from the Form 1040 worksheet. Going further, the proposal would index the 50% inclusion rule for future inflation, and greatly simplify the calculation of income for purposes of this rule. Tax exempt interest will no longer be required to be added in the calculation. Indexation will mean that fewer taxpayers will be required to complete the calculation and include benefits in income.

Simplify Capital Gains Tax—Under present law, there are seven different capital gains rates that apply to various kinds of dispositions of property. There are special rates for taxpayers in lower tax brackets, for property held five years or more, and for gain on collectibles. Before 1986, there was one rule: 50% of capital gains are deductible. For any investor who has struggled to fill out Schedule D of Form 1040, it will come as welcome news that the bill proposes a return to the system in place prior to 1986.

No taxpayer will pay a higher capital gains rate under this proposal. By definition, the capital gains rate that individuals pay will be no more than one-half of their marginal income tax rate. Therefore, this proposal preserves the progressivity that is accomplished by a rate structure under current law, and the maximum rate will be no more than one-half of the highest marginal income tax rate. Thus, the maximum effective capital gains rate would be 19.3% in 2003, and an individual in the 10% bracket would have a 5% capital gains rate.

Repeal of 2% Floor on Miscellaneous Itemized Deductions—The bill follows the recommendation of the Joint Committee on Taxation that the 2% floor on miscellaneous itemized deductions should be repealed. This provision was originally enacted in 1986 to ease administrative burdens for the IRS and record keeping burdens for taxpayers.

Instead of easing taxpayers' burdens, it has caused extensive litigation and controversy over such matters as whether an individual is properly characterized as an employee or an independent contractor. It has also resulted in disparate treatment of similarly situated taxpayers. For example, an employee whose job requires him to pay out of pocket for travel, professional publications, or education is disadvantaged compared to a taxpayer in a similar job whose employer reimburses such items.

Simplify Taxation of Minor Children—This provision would eliminate the current restrictions on adding a minor child's income to the parent's return. A parent could freely elect to include the income of a child under 14 on his or her own tax return, regardless of the character and amount of the child's income. Parents and children would retain the ability to file separate returns, but the unearned income of a minor child would be subject to tax at the rates applicable to trusts. The single filing rate structure would continue to apply to the child's earned income.

Simplify Dependent Care Tax Benefits—The bill would conform differences between the Dependent Care Tax Credit and the Exclusion for Employer-Provided Dependent Care Assistance. The two programs serve identical purposes, but their rules are different. Under this proposal, the dollar limit on the amount creditable or excludable would be increased to $5,500, and the percentage creditable would be increased to 35%. These provisions would be further simplified by a cross-reference to the new uniform definition of a qualifying child.

Accelerate Repeal of PEP and PEASE—The bill would accelerate and make permanent the repeal of the overall limitation on itemized deductions (PEASE) and the personal exemption phaseout (PEP). These provisions add complexity and complicate planning for millions of taxpayers. The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) repeals these provisions over a period of years from 2006 to 2009, but, because of EGTRRA's sunset provisions, PEP and PEASE spring back to life in 2011.

Uniform Definition of a Child—One of the most challenging and difficult problems that taxpayers face each year is to navigate the multiple definitions of a qualifying child for the dependent exemption, the child tax credit, the dependent care credit, the earned income tax credit, and for purposes of determining head of household filing status. The bill would establish a uniform definition of a child based on the residence, relationship, and age of the child. The Proposal would replace the rule that requires taxpayers to prove that they provide more than one-half of a child's support with a preference for the parent who provides housing for the child for more than one-half of the year. In addition, the bill would establish that means-tested government benefits are generally disregarded in determining eligibility for tax benefits.

Combine HOPE and Lifetime Learning Credits—Like the dependent care credit and the exclusion for employer provided dependent care assistance, the HOPE and Lifetime Learning Credits (LTL) serve nearly identical purposes, but they have different rules. The LTL credit is a per-taxpayer credit, and it applies on up to $10,000 of qualifying, education expenses. The HOPE credit is a per-child credit, and it applies with respect to the first $2,000 of qualifying education expenses incurred during the first two years of post-secondary education. Both credits are for higher education, but taxpayers face a challenge to determine which credit is best for their circumstances. The bill would merge the two credits, providing a credit for one-half of the first $3,000 of post-secondary education expenses. This credit would apply on a per-child basis, and it would not be limited to the first two years of post-secondary education.

Uniform Definition of Qualifying Higher Education Expense—The bill adopts the recommendation of the Joint Committee on Taxation that there should be a uniform definition of higher education expense for purposes of the various education tax benefit programs. The varying definitions that exist in current law greatly complicate the task of determining which education benefit is best for the taxpayer.

II. SMALL BUSINESS TAX SIMPLIFICATION

Uniform Passthrough Entity Regime—This provision would combine the benefits of Subchapter S (S corporations) and Subchapter K (Partnerships) of the Internal Revenue Code in a single, unified passthrough entity regime based on Subchapter K. While at one time, Subchapter S provided the only avenue for prospective investors to avoid the corporate-level tax while retaining a full liability protection, the emergence and broad acceptance of limited liability companies (LLCs) has provided investors with an alternative. There are now two separate, fully-articulated passthrough entity regimes.

Maintaining two separate passthrough entity regimes is expensive and unnecessarily complicated. It increases costs both for taxpayers and for the IRS. At a time when the IRS is striving to train its auditors to understand passthrough entities, and a new class of investors is struggling to understand the pros and cons of the two regimes, the time is ripe to rationalize this most complex area of the Internal Revenue Code by reconciling Subchapter S and Subchapter K.

The objective of the proposal is to establish a single passthrough entity regime that preserves the major benefits of Subchapter S and Subchapter K. Domestic corporations that are not publicly traded would have a new election to be treated as a partnership for federal tax purposes, and the S election would be repealed. The proposal would therefore endorse, and extend, the 1996 Check-the-Box regulations to allow state law corporations to elect partnership status. Existing S corporations would be permitted to continue as S corporations for ten years at which time they would be required to elect partnership or corporate status.

So as not to undermine the corporate tax that will remain applicable to publicly traded corporations and other entities that elect to be taxed as corporations, a corporation that elects partnership status with undistributed earnings and profits will be required to track distributions of earnings under rules similar to IRC Section 1368. Similarly, electing corporations (including S corporations) with appreciated assets will be required to pay a built in gains tax if they sell or dispose of such assets within the first ten years after the election. However, corporations (including S corporations) that elect partnership status will not be required to recognize entity-level gain as a result of the election. The 8 proceeds of built in gain transactions will be added to historic earnings and profits and not currently taxed to the partners.

Consistent with the overall objective of preserving the benefits of Subchapter S, the proposal will establish a means for passthrough entities to engage in tax free reorganizations with entities classified as corporations. Under the proposal, a partnership engaged in an active trade or business may contribute substantially all of its assets to a new corporation and immediately thereafter engage in a tax free reorganization.

The bill would also adopt a recommendation of the American Institute of Certified Public Accountants and the American Bar Association that the definition of earnings from self-employment should not include the portion of a partner's distributive share that is attributable to capital. This proposal contains reasonable safe harbors and it would eliminate the disparate treatment of limited partners, S corporation shareholders, and limited liability company members. The current rules can only be described as a historical anachronism and a significant trap for the unwary. Additionally, the bill would adopt the recommendation of the Joint Committee on Taxation that the electing large partnership rules should be eliminated.

Some may argue that by repealing the S election, the proposal forces more taxpayers to contend with a more complex tax regime, but this is generally not true. If there is a demand, investors can create an investment vehicle with all the features of an S corporation by contract or they may select a state law business form that restricts flexibility, such as a corporation or close corporation. This would eliminate nearly all of Subchapter K's feared complexity. The relative complexity of Subchapter K stems from its greater flexibility. The proposal allows investors to regulate the level of tax complexity by voluntary agreement among the investors or through the investors' choice of a state law business entity.

Increase Section 179 Expensing Limit—The bill would increase the limit on expensing to $25,000 in the tax year after enactment and to $40,000 after 2012. This measure will greatly reduce complexity for many small businesses by minimizing controversy over whether an item should be expensed or capitalized.

Rollover of Property Held for Productive Use or Investment—Present law strongly favors sophisticated taxpayers over ordinary small business owners in the execution of like-kind exchange transactions. Thirty-seven pages of the Code of Federal Regulations is devoted to the topic of like-kind exchanges, and a library could be filled with the court decisions, revenue rulings, and letter rulings that Section 1031 of the IRC has engendered. Attorneys and exchange facilitators must execute hundreds of thousands of pages of documents each year to comply with the formalistic rule that prevents the owners of like-kind property from receiving cash in a like-kind exchange transaction.

There is a simple way to eliminate this paperwork: repeal the limitation on sales for cash and allow a like-kind exchange within 180 days before or after the disposition of relinquished property. The bill does this.

Repeal of Collapsible Corporation Rules—Finally, the bill would repeal the collapsible corporation rules that linger in the tax code as a trap for the unwary. These rules were enacted to prevent an abuse that has not existed since the repeal of the General Utilities doctrine. The repeal of these rules is long overdue.

I urge my colleagues to join me in cosponsoring this legislation.