



CRS Report for Congress

Farm Legislation and Taxes in the 110th Congress

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Summary

On July 27, 2007, the House passed its version of the omnibus 2007 farm bill (H.R. 2419). The bill's spending provisions are estimated to increase federal spending on agriculture policy above the baseline level allowed by the FY2008 budget resolution. In order to comply with House pay-as-you-go budget rules, the bill included several revenue-raising provisions, the bulk of which would be produced by a proposal to restrict the use of tax-treaty benefits by foreign firms not actually resident in a treaty country. In October, the Senate Finance Committee approved S. 2242, a bill containing a number of agriculture-related tax provisions, but also containing energy and conservation measures along with a revenue-raising proposal designed to curtail tax shelters (codification of the "economic substance" doctrine). The Senate Finance Committee bill is estimated to be approximately "revenue neutral," gaining as much new tax revenue as it loses. However, it also contains an optional new tax credit that is estimated to have the effect of reducing outlays under an existing U.S. Department of Agriculture program by \$3.0 billion over five years, thus providing room for new spending in the Senate version of the farm bill without violating Senate budget rules. On December 14, the full Senate approved an omnibus farm bill (an amended version of H.R. 2419) containing the essential elements of the Finance Committee tax package. This report will be updated as legislative developments occur.

Taxes in the House Farm Bill

H.R. 2419 (introduced in the 110th Congress by Representative Collin Peterson on May 22, 2007) would increase tax revenue by an estimated \$3.7 billion over 5 years and by \$7.5 billion over 10 years. This estimated effect provides a matching offset for the estimated 5- and 10-year spending increases contained in the bill. The spending totals are net of an increase in non-tax revenues contained in Title XIII of the bill, estimated at \$2.2 billion over 5 years and \$6.1 billion over 10 years. **Table 1**, below, reports the revenue impact of the bill's tax and revenue provisions.

Table 1. Estimated Revenue Effect of H.R. 2419, the House-Passed Farm Bill

(in billions of dollars)

	5-Year Revenue Gain (FY2008-FY2012)	10-Year Revenue Gain (FY2008-FY2017)
Limitation on Tax-Treaty Benefits	+ \$3.2	+ \$7.5
Corporate Estimated Tax Payments	+ \$0.5	No effect
Total Increase in Tax Revenue	+ \$3.7	+ \$7.5
Increase in Offsetting Receipts	+ \$2.2	+ \$6.1

Source: Estimates by the Joint Committee on Taxation, as reported in U.S. Congressional Budget Office, *H.R. 2419: Farm, Nutrition, and Bioenergy Act of 2007*, October 5, 2007, at <http://www.cbo.gov/ftpdocs/86xx/doc8686/hr2419HPassed.pdf>.

Treaty Shopping Restrictions. By far the largest tax provision in the House bill is a provision designed to curb what is sometimes termed “treaty shopping” — that is, the use of the tax-reducing provisions of bilateral tax treaties by firms which are not actually residents of the countries party to the treaty. The provision would raise an estimated \$3.2 billion over 5 years and \$7.5 billion over 10 years, and incorporates the language of H.R. 3160, a stand-alone anti-treaty-shopping bill introduced by Representative Lloyd Doggett. Its context is this: foreign individuals and firms who invest in the United States are generally subject to a flat U.S. “withholding tax” on interest, dividend, royalty, and similar income paid to them by U.S. payers. Income generally subject to the tax includes payments by U.S.-chartered subsidiary corporations to their foreign parents. While the rate of the withholding tax is nominally 30%, it is often reduced or eliminated under the terms of one of the many bilateral tax treaties, which the United States (like most developed countries) has signed.

In some cases, the payment subject to the withholding tax may be tax-deductible by the payer under the corporate income tax. For example, U.S.-chartered corporations that are owned by foreign parent firms are ordinarily subject to the U.S. corporate income tax, but are permitted — subject to some restrictions — to deduct the interest they pay to their foreign parents on intra-firm debt. In such cases, the only tax applicable to a foreign investor’s U.S. income is thus the withholding tax. Where the withholding tax is reduced by treaty, little or no U.S. tax may therefore apply to the U.S.-source payments.

The provision’s proponents argue that in some cases foreign investors resident in countries where the withholding tax is not substantially reduced or eliminated can save taxes by arranging to receive their U.S. income through an intermediate entity chartered in a country whose U.S. treaty does eliminate the withholding tax. If the treaty country does not impose its own withholding tax (or has a treaty with the foreign parent’s home country), the intermediate subsidiary can simply pass the payments on to its ultimate foreign parent without incurring additional taxes. Supporters of the provision have argued that it will close what they characterize as a “loophole” that permits foreign firms to

unfairly avoid U.S. taxes.¹ The House bill provides that, where the withholding tax rate on a payment to an intermediate foreign entity is lower than the rate for a direct payment to a parent firm, the higher of the two rates will apply.

The provision's opponents argue that the measure would abrogate U.S. treaties and reduce employment-creating foreign investment in the United States.² Also, members of the congressional tax-writing committees have expressed concern about the tax committees being relied upon to provide budget offsets for other committees.³ The Bush Administration has stated that it "strongly opposes" the bill's tax-treaty provisions and has threatened to veto the bill for this and other reasons.⁴ On October 15, 2007, Chairman Charles Rangel of the House Ways and Means Committee introduced an omnibus tax bill (H.R. 3970, the Tax Reduction and Reform Act of 2007) containing among its provisions a proposal similar to the treaty provisions of H.R. 2419. The Rangel bill, however, contains modifications designed to reduce the possibility of conflict with existing tax treaties.

The remaining tax-related revenue-raising item in the House bill provides for a shifting forward of corporate estimated tax payments, increasing payments in FY2012 by \$0.5 billion and increasing them by the same amount in FY2013. In addition, the bill would increase revenues (i.e., increase "offsetting receipts") by imposing a "conservation of resources" fee on Outer Continental Shelf oil and gas leases, and by repealing royalty-relief for oil and gas production granted by the Energy Policy Act of 2005 (P.L. 109-58).

The Senate Conservation, Agriculture, and Energy Tax Bill

On October 25, 2007, the Senate Finance Committee reported a bill (S. 2242, the Heartland, Habitat, Harvest, and Horticulture Act, introduced the same day by Senator Max Baucus) containing a set of tax provisions related to energy, conservation, and agriculture. The bill contained both revenue-losing and revenue-raising provisions, but revenue estimates published by the Finance Committee indicated it would be approximately revenue neutral over both 5 and 10 years.⁵ The Finance Committee bill

¹ Citizens for Tax Justice, *Senate Should Enact the Doggett Proposal to Close Loophole that Allows Foreign Corporations to Dodge Taxes on U.S. Profits* (Washington, August 8, 2007).

² Brett Ferguson, "House Votes to Repeal Treaty Advantages for U.S. Subsidiaries as Part of Farm Bill," *BNA Daily Tax Report*, July 30, 2007, p. GG-1.

³ Brett Ferguson, "Doggett Proposes Closing Loopholes in Treaties to Raise Offset for Farm Measure," *BNA Daily Tax Report*, July 25, 2007, p. G-12. See also Meg Shrive, "Grassley Warns Against Violating Tax Treaties with Farm Bill Tax Provision," *Tax Notes*, August 20, 2007, p. 627.

⁴ Executive Office of the President, Office of Management and Budget, Statement of Administration Policy, July 25, 2007. Available at [<http://www.whitehouse.gov/omb/legislative/sap/110-1/hr2419sap-r.pdf>].

⁵ The bill would raise an estimated \$104 million over 5 years and \$284 million over 10 years. The estimates are by the Joint Committee on Taxation, published by the Senate Finance Committee: U.S. Congress, Senate, Committee on Finance, *Estimated Budget Effects of the* (continued...)

contained an optional conservation tax credit that may cause the amount of spending under an existing U.S. Department of Agriculture program to fall by \$3 billion over five years, thus providing room for new spending under the Senate farm bill without violating Senate pay-as-you-go budget rules.⁶ **Table 2**, below, presents revenue estimates published by the Senate Finance Committee for the main categories of revenue-losing and revenue-raising items in the bill.

Table 2. Estimated Revenue Effects of the Senate Finance Committee Bill

(in billions of dollars)

Revenue-Losing Items		
	5 Years	10 Years
Supplemental Agriculture Disaster Assistance Fund	- \$5.1	- \$5.1
Conservation Tax Provisions	- \$5.5	- \$7.2
Energy-Related Tax Provisions (Includes several revenue-raising items.)	- \$0.4	- \$1.5
Agriculture-Related Tax Items	- \$2.3	- \$0.8
Total Revenue-Losing Items	- \$13.3	- \$14.6
Revenue-Raising Items		
Economic Substance Doctrine	+ \$3.7	+ \$10.0
Leasing Restrictions (Sale-In/Lease-Out)	+ \$4.6	+ \$3.2
Corporate Estimated Taxes	+ \$4.3	No effect
Agriculture-Related Revenue-Raisers	+ \$0.3	+ \$0.6
Other Revenue-Raisers	+ \$0.2	+ \$0.1
Total Revenue-Raisers	+ \$12.9	+ \$14.9

Source: Estimates by the Joint Tax Committee, as published by Senate Committee on Finance.

The tax title of the farm bill passed by the full Senate on December 14 does not differ substantially from the Finance Committee bill. It includes several additional narrow revenue-

⁵ (...continued)

“*Heartland, Habitat, Harvest and Horticulture Act of 2007*,” Washington, October 2007 at [<http://finance.senate.gov/sitepages/leg/LEG%202007/Leg%20110%20102607chart.pdf>].

⁶ Noelle Straus, “Baucus at Center of Fight over Farm Bill Details,” *Helena Independent Record*, October 13, 2007, available at [http://www.helenair.com/articles/2007/10/13/montana/a011013_05.txt].

losing items that are fully offset by revenue-raising provisions estimated to increase revenue by \$1.035 billion over 10 years.⁷

Tax Cuts. Taken alone, the committee bill's tax cut provisions would reduce revenue by an estimated \$13.3 billion over 5 years and \$14.6 billion over 10 years.⁸ The tax-cut items fall into four groups, containing provisions related to conservation, energy, agriculture, and an agriculture disaster reserve fund. The *conservation provisions* are together estimated to reduce revenue by \$5.5 billion over 5 years and \$7.2 billion over 10 years. In general, the provisions provide tax incentives for various activities to conserve forests, wetlands, wildlife, and endangered species. The single largest tax cut, however, is the tax credit noted above that shifts the budget cost of the existing U.S. Department of Agriculture (USDA) Conservation Reserve Program (CRP) from the spending side of the ledger to the receipts side by permitting recipients to elect a tax credit in lieu of cash payments under the CRP program. It is likely that for most recipients, the credit would exceed the conservation payments in value because the tax credit would be excluded from taxable income while payments from the CRP are taxable.⁹ The provision would reduce revenue by a total of \$3.8 billion, which would occur in FY2009-FY2012.

The bill's *energy provisions* are generally a group of tax incentives to promote domestic fuel security taken from a broader energy tax-bill approved by the Finance Committee in June, although there are several narrow revenue-increasing items in the group. Together, the energy provisions would reduce revenue by an estimated net amount of \$405 million over 5 years and \$1.5 billion over 10 years. The single largest tax cut (\$1.1 billion over 10 years and \$282 million over 5 years) is a new tax credit for producers of cellulosic alcohol fuel production; other tax benefits include extension of biodiesel-fuel tax credits that would otherwise expire and a new tax credit for fossil-free alcohol production. Revenue raising items include a five-cent reduction in the ethanol fuel credit.

The bill's *agriculture provisions* are a set of tax benefits related to farming businesses that would together reduce revenue by \$2.3 billion over 10 years and by \$771 million over 10 years. The provisions include an expansion of an existing category of tax-free bonds that can be issued by state and local governments to support first-time farmers; creation of a new category of tax-free bonds that would support investment in certain types of rural infrastructure; and more generous depreciation-recapture rules for single-purpose agricultural property (e.g., livestock barns and greenhouses). The largest tax cut is more generous depreciation rules for farm machinery and equipment placed in service before 2010. The provision would reduce revenue by \$1.5 billion over 5 years, but by a

⁷ A description of the Senate-passed bill is available on the Finance Committee website, at <http://finance.senate.gov/sitepages/leg/LEG%202007/Leg%20110%20121807farmbill.pdf>].

⁸ Estimates by the Joint Committee on Taxation, as published in U.S. Congress, Senate, Committee on Finance, *Estimated Budget Effects of the "Heartland, Habitat, Harvest and Horticulture Act of 2007," as Reported by the Committee on Finance*, Washington, October 2007, at <http://finance.senate.gov/sitepages/leg/LEG%202007/Leg%20110%20102607summary.pdf>].

⁹ For the tax treatment of CRP payments, see U.S. Internal Revenue Service, *Farmer's Tax Guide*, Publication 225 (Washington: 2006), p. 11.

negligible amount over 10 years. (This pattern occurs because the provision has the effect of advancing the timing of depreciation deductions.)

The bill would create a trust fund that would provide disaster relief to farmers and ranchers in the case of losses not large enough to qualify for crop insurance payments. The fund's cost would be \$5.1 billion, all in the bill's first five years. It would be funded by customs revenues.

Revenue-Raising Provisions. The bill's revenue raising provisions would together increase revenue by an estimated \$13.3 billion over 5 years and \$14.9 billion over 10 years. The single largest item is a provision designed to curtail the use of tax shelters: a codification of the judicial "economic substance" doctrine that has developed in court cases related to tax shelters. In general terms, the doctrine denies the use of tax-reducing items — e.g., tax deductions and credits — generated by transactions that do not result in a meaningful change in the taxpayer's economic position. In general, the committee proposal integrates portions of the doctrine into the Internal Revenue Code. The committee's provisions would not apply unless a court determines the economic substance doctrine to be relevant, but when such a determination is made, it would apply a two-part ("conjunctive") test to a transaction, requiring that (1) the transaction change the taxpayer's economic position in a meaningful way (an "objective" test); and (2) the taxpayer has a substantial non-federal-tax purpose for engaging in the transaction. In addition, the proposal would apply a 30% penalty for tax understatements where economic substance is lacking.¹⁰

Proposals to codify the economic substance doctrine have been considered by Congress for a number of years. The Senate versions of both the American Jobs Creation Act of 2004 (P.L. 108-357) and Tax Increase Prevention and Reconciliation Act of 2005 (P.L. 109-222) contained economic-substance provisions that were dropped in conference. The current Finance Committee provision is similar to the previous proposals in broad outline — for example, its two-part test — but differs in some details, and is estimated to raise approximately one-third less revenue than the previous proposals.¹¹

Several of the remaining revenue-raising items apply to farm taxation, including a limitation on deductible farm losses, restrictions on like-kind exchange benefits, and increased reporting requirements, each in cases where the taxpayer receives Agriculture Program Payments or Commodity Credit Corporation loans. An additional revenue-raising item would change the effective date of existing restrictions on sale/lease back (SILO) transactions involving U.S. taxpayers and foreign entities not subject to U.S. tax. Under current law, deductible losses relating to such transactions would not be allowable for leases entered into after March 12, 2004; the proposal applies the restriction to leases entered into on or before that date.

¹⁰ U.S. Congress, Senate, Committee on Finance, *Heartland, Habitat, Harvest, and Horticulture Act of 2007*, report to accompany S. 2242, p. 110.

¹¹ For example, the current Finance Committee bill would apply a 30% understatement penalty rather than a 40% penalty as in previous bills. TIPRA's version was estimated to increase revenue by \$5.0 billion over 5 years and \$15.8 billion over 10 years (U.S. Joint Committee on Taxation, *Comparison of the Estimated Revenue Effects of the Tax Provisions Contained in H.R. 4297*, JCX-10-6, February 9, 2006, p. 5).

After some procedural drama, Congress passed sweeping new tax legislation on December 20, 2017. On December 19, 2017, the House passed H.R.1 by a vote of 227-203. In the early morning hours of December 20, 2017, the Senate passed H.R.1 by a vote of 51-48, but only after making several technical amendments to. Of the roughly 143 million tax filers in the U.S., about 48 million currently itemize deductions. The Act would significantly decrease that number. It would also remove the requirement that farm property is depreciated using the 150 percent declining balance method (except for 15 or 20-year property). These provisions apply to property placed in service after December 31, 2017.

Congressional Action. In the 110th Congress, H.R. 21 would reorient U.S. ocean policy (including fisheries), emphasizing ecosystem management, creating a Council of Advisors on Ocean Policy to advise the President, organizing Regional Ocean Partnerships, and developing Ocean Ecosystem Resource Information Systems. H.R. 27 would designate the U.S. EEZ as the "Ronald Wilson Reagan Exclusive Economic Zone of the United States."

Farm Legislation and Taxes in the 110. th. Congress. David L. Brumbaugh Specialist in Public Finance Government and Finance Division. Summary. H.R. 2419 (introduced in the 110th Congress by Representative Collin Peterson on May 22, 2007) would increase tax revenue by an estimated \$3.7 billion over 5 years and by \$7.5 billion over 10 years This estimated effect provides a matching offset for the estimated 5- and 10-year spending increases contained in the bill. The spending totals are net of an increase in non-tax revenues contained in Title XIII of the bill, estimated at \$2.2 billion over 5 years and \$6.1 billion over 10 years. Table 1, below, reports the revenue impact of the bill's tax and revenue provisions. CRS-2. American Veterinary Medical Association 110th Congress Legislative Agenda. At the heart of every omnibus farm bill is farm income and commodity price support. The patch for the 2007 tax year, as provided for in the Tax Increase Prevention Act of 2007 (PL 110-166), enacted on December 26, 2007, set the AMT exemption levels for 2007 at \$66,250 for joint filers and \$44,350 for single filers.

Legislation to Address the Issue of Unwanted/Retired Horses: If Congress decides that horses and other equids are prohibited from being processed for human consumption, it is estimated that each year an additional 90,000-115,000 unwanted U.S. horses would need to find an alternative method of care, or disposal if the horse is euthanized.