THE WHITE HOUSE
WASHINGTON

May 24, 1985

MR. PRESIDENT:

Attached for your approval is H.R. 1869 - Amendment of Certain Taxpayer Recordkeeping Requirements.

This Bill has the approval of OMB, Treasury, and the Office of Policy Development, Legislative Affairs, and Cabinet Affairs. Counsel's Office has no objection.

David L. Chew

Please note: You are scheduled to sign this Bill today in ceremony. Legislative Affairs has requested two signing pens. They are attached for your convenience.

Hold - HR1869
Signing Ceremony
requested 5/20/85
by Leg. Affs. SBS

ISI 5/24/85

The President has seen

APPROVED MAY 24 1985

CEREMONY - 1:00 PM - OVAL OFFICE

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

Received SS
1985 MAY 22 PM 3:00

Archives 5/24/85

MAY 22 1985

MEMORANDUM FOR THE PRESIDENT

Subject: Enrolled Bill H.R. 1869 - Amendment of Certain Taxpayer Recordkeeping Requirements
Sponsors - Rep. Rostenkowski (D) Illinois and 20 others

Last Day for Action

May 31, 1985 - Friday

Purpose

To amend the Internal Revenue Code concerning recordkeeping requirements for business use of motor vehicles and certain other property.

Agency Recommendations

Office of Management and Budget	Approval
Department of the Treasury	Approval

Discussion

-- Background

Until 1984, the Internal Revenue Code permitted a taxpayer to deduct expenses incurred in the business use of an automobile only to the extent that he or she could establish the nature and extent of the business use. For travel away from home, adequate records or sufficient evidence corroborating the taxpayer's own statement was required. For local travel, the taxpayer had the burden of demonstrating, whether through records or otherwise, that the use of the automobile did, in fact, have a business purpose.

In spite of the rules regarding substantiation of business expenses in connection with the use of motor vehicles, taxpayer compliance was spotty, at best; overstated deductions for business use of automobiles were common. In 1979, the latest year for which data are available, the Internal Revenue Service (IRS) estimates that about one-half of the 11.3 million taxpayers who claimed deductions for business use of automobiles received more than $3 billion in excess tax benefits (i.e., tax benefits for which they did not qualify).

Congress addressed the substantiation problem in the Tax Reform Act of 1984, which was enacted as part of the Deficit Reduction Act of 1984, Public Law 98-369. The Internal Revenue Code was amended, effective January 1, 1985, to require taxpayers to substantiate business use of automobiles and certain other property (i.e., home computers) by "adequate contemporaneous records." The report of the conference committee on the Tax Reform Act of 1984 indicated that these records would "reflect with substantial accuracy the business use of the property," and that, with respect to automobiles, "logs recording the date of the trip and the mileage driven for business purposes must be kept."

In October 1984, the IRS promulgated proposed regulations to implement the new substantiation requirements. Revised proposed regulations were issued in February 1985.

-- Description of the Enrolled Bill

The enrolled bill, which passed the House by a vote of 412-1 and the Senate by voice vote, responds to concerns of many taxpayers that the substantiation requirements of the Tax Reform Act of 1984 and the IRS regulations implementing them are unduly burdensome and onerous. Key provisions of the enrolled bill are highlighted below.

- o Repeal of Contemporaneous Recordkeeping Requirement. The enrolled bill repeals the contemporaneous recordkeeping requirement of the Tax Reform Act of 1984 and reinstates the requirement of prior law that any deduction must be supported by "adequate records or . . . sufficient evidence corroborating the taxpayer's own statement." The conference report rejected a provision contained in the original House bill that would have required that any corroborating evidence be in writing. The conferees emphasized, however, that they recognize that different kinds of evidence have different probative value. In particular, the conference report states that oral evidence is of considerably less usefulness in substantiating a deduction than written records and urges the Internal Revenue Service and the courts to discount or reject evidence of limited or no probative value. To ensure greater compliance, the conferees want the IRS to issue appropriate forms or schedules for taxpayers to use in substantiating deductions. The substantiation requirements do not apply to certain vehicles (e.g., school buses) that by their nature receive little personal use.

- o Repeal of Provisions Concerning Return Preparers and Negligence Penalty. Under the Tax Reform Act of 1984, tax return preparers must advise taxpayers of the requirements for substantiating deductions for business use of automobiles and obtain written confirmation that the pertinent requirements

have been met. H.R. 1869 repeals this requirement. The Tax Reform Act also imposed a special no-fault negligence penalty applicable to any understatement of tax resulting from failure to comply with the substantiation requirements. The enrolled bill repeals this provision as well.

o Withholding Election for Personal Use of Employer-Provided Vehicle. Under authority extended to it by the 1984 Act, Treasury has issued regulations requiring the withholding of income and employment taxes with respect to taxable noncash fringe benefits, including an employee's personal use of a vehicle provided by his or her employer. The enrolled bill permits an employer to elect not to withhold taxes on the value of any vehicle fringe benefit provided to an employee; however, an employer so electing must report the value of the fringe benefit on the employee's W-2 form.

o Reduction in Limitations on Investment Tax Credit and Depreciation for Luxury Automobiles. Current law limits the investment tax credit that is available for automobiles to $1,000. Depreciation is limited to $4,000 for the year an automobile is placed in service and $6,000 for subsequent years. For years after 1984, these amounts are to be adjusted annually for inflation. To offset the revenue losses that will result from repeal of the contemporaneous record requirement, the enrolled bill reduces the existing limitations on the investment tax credit and depreciation for automobiles. In particular, the bill limits the investment tax credit to $675 and reduces allowable depreciation to $3,200 for the first taxable year and $4,800 for each subsequent year. Indexing for inflation is delayed for four years, until 1989.

-- Revenue Effects

Congressional Budget Office Estimates of Revenue Effects of H.R. 1869

Changes in Substantiation and Withholding Requirements, 1985-1990	-$885 million
Reduction in Investment Tax Credit and Depreciation, 1985-1990	+$1,005 million
Total	+$120 million

James M. Frey
Assistant Director for
Legislative Reference

Enclosures

Document No. _____

Received SS
1985 MAY 23 PM 4:44

WHITE HOUSE STAFFING MEMORANDUM

DATE: 5/22/85 **ACTION/CONCURRENCE/COMMENT DUE BY:** 9:00 A.M. TOMORROW 5/23

SUBJECT: H.R. 1869 - AMENDMENT OF CERTAIN TAXPAYER RECORDKEEPING REQUIREMENTS

	ACTION	FYI		ACTION	FYI
VICE PRESIDENT	☐	☑	LACY	☐	☐
REGAN	☐	☑	McFARLANE	☐	☐
STOCKMAN	☐	☐	OGLESBY	☑	☐
BUCHANAN	☑	☐	ROLLINS	☑	☐
CHAVEZ	☐	☐	RYAN	☐	☐
CHEW	☐P	☑S	SPEAKES	☐	☑
DANIELS	☐	☐	SPRINKEL	☐	☐
FIELDING	☑	☐	SVAHN	☑	☐
FRIEDERSDORF	☑	☐	TUTTLE	☐	☐
HENKEL	☐	☐	_____	☐	☐
HICKEY	☐	☐	_____	☐	☐
HICKS	☐	☐	_____	☐	☐
KINGON	☑	☐	_____	☐	☐

OK →

REMARKS:

Please provide any comments/recommendations by 9:00 a.m. tomorrow, May 23rd. Thank you.

RESPONSE:

David L. Chew
Staff Secretary
Ext. 2702

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

Received SS
1985 MAY 22 P4 3:00

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James M. Frey
Assistant Director for
Legislative Reference

Enclosures

Document No. 271544

5/23
HOLD
to see if
Signing ceremony
approved.

WHITE HOUSE STAFFING MEMORAND

DATE: 5/22/85 ACTION/CONCURRENCE/COMMENT DUE BY: 9 23

SUBJECT: H.R. 1869 - AMENDMENT OF CERTAIN TAXPAYER RECORDKEEPING REQUIREMENTS

	ACTION	FYI		ACTION	FYI
VICE PRESIDENT	☐	☑	LACY	☐	☐
REGAN	☐	☑	McFARLANE	☐	☐
STOCKMAN	☐	☐	OGLESBY approves	☑	☐
BUCHANAN	☑	☐	ROLLINS Concur	☑	☐
CHAVEZ	☐	☐	RYAN	☐	☐
CHEW	☐P	☑S	SPEAKES	☐	☑
DANIELS	☐	☐	SPRINKEL	☐	☐
FIELDING no legal obj	☑	☐	SVAHN OK 5/22	☑	☐
FRIEDERSDORF approves	☑	☐	TUTTLE	☐	☐
HENKEL	☐	☐	_____	☐	☐
HICKEY	☐	☐	_____	☐	☐
HICKS	☐	☐	_____	☐	☐
KINGON OK	☑	☐	_____	☐	☐

REMARKS:

Please provide any comments/recommendations by 9:00 a.m. tomorrow, May 23rd. Thank you.

RESPONSE:

LA - 2 signing pens
Wants signing ceremony

David L. Chew
Staff Secretary
Ext. 2702

THE GENERAL COUNSEL OF THE TREASURY
WASHINGTON, D.C. 20220

MAY 22 1985

Director, Office of Management and Budget
Executive Office of the President
Washington, D.C. 20503

Attention: Assistant Director for Legislative Reference

Dear Sir:

This is in reply to your request for the views of the Department of the Treasury concerning H.R. 1869, an enrolled bill "To amend the Internal Revenue Code of 1954 to repeal the contemporaneous recordkeeping requirements added by the Tax Reform Act of 1984, and for other purposes."

Section 1 of the bill repeals the requirement that a taxpayer maintain "contemporaneous records" and instead requires that "adequate records" or other "sufficient evidence" corroborating the taxpayer's statement be maintained to substantiate certain deductions and credits. Section 2 exempts from the substantiation requirements vehicles that are "not likely to be used more than a de minimis amount for personal purposes."

Section 3 of the bill authorizes employers to elect not to deduct and withhold taxes in the case of certain vehicle fringe benefits, provided that employees are notified of the election as provided by regulations issued by the Secretary of the Treasury and that the amount of the benefit is reported to the Internal Revenue Service. Section 4 changes the limitations on the investment tax credit and depreciation for luxury automobiles.

The Department of the Treasury supports the enrolled bill. The Department believes that the enrolled bill represents a constructive compromise between the Department's responsibility to protect and collect the revenue and the obligation of taxpayers to adequately substantiate deductions and credits.

Sincerely yours,

Margery Waxman

Acting General Counsel

Document No. _____

Received SS
1985 MAY 22 P

WHITE HOUSE STAFFING MEMORANDUM

DATE: 5/22/85 **ACTION/CONCURRENCE/COMMENT DUE BY:** 9:00 A.M. TOMORROW 5/23

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KINGON	☑	☐	_____	☐	☐

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RESPONSE: Sent to Tom Gibson

OK
AK

David L. Chew
Staff Secretary
Ext. 2702

ID # 175411 CA

OFFICE OF CABINET AFFAIRS
ACTION TRACKING WORKSHEET

Action resulting from:

☒ Document (attached)
☐ Telephone call
☐ Meeting (attach conference report if available)

Document Date: 5 / 22 / 85

From: Executive Office of the President - OMB

Date Received: 5 / 22/ 85

SUBJECT: H.R. 1869 - Amendment of Certain Taxpayer Recordkeeping Requirements

ACTION CODES:

A - Appropriate Action	D - Draft Response	R - Direct Reply w/Copy
B - Briefing Paper	F - Furnish Fact Sheet/Background	S - For Signature
C - Comment/Recommendation	I - Info Copy Only/No Action Necessary	X - Interim Reply

ROUTE TO:

Date Sent	Name	Action Codes	Date Due	Action Taken
85 /05/ 22	Tom Gibson	A	85 /05/ 23	
/ /			/ /	
/ /			/ /	
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/ /			/ /	
/ /			/ /	

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ORIGINATOR: ☐ Clarey ☐ Faoro ☐ Finnegan ☐ Gibson ☒ ~~Gonzales~~ Wenzel ☐ Herbolsheimer ☐ Kingon

Keep this worksheet attached to the original incoming material and when the assigned action is complete, return to:

OFFICE OF CABINET AFFAIRS
Attention: Adele Gonzalez (x2823), West Wing/Ground Floor

ID # 175411 CA

OFFICE OF CABINET AFFAIRS
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85/05/22	Wenzel / AHK		/ /	
/ /			/ /	
/ /			/ /	
/ /			/ /	
/ /			/ /	

COMMENTS: Please provide any comments/recommendations by 9:00 a.m. tomorrow, May 23rd. Thank you.

→ The bill should be signed. OMB: Tr. say yes.

o → The contemporaneous record keeping for business use of autos was targeted for repeal my a multitude of groups. Passed on voice vote in Senate, 412-1 in House.

o → Net revenue increase ($100 m), because of changes in tax credit & depreciation schedules for ~~corp~~ business autos.

o → Minor reg. ~~re-draft~~. re-right.

ORIGINATOR: ☐ Clarey ☐ Faoro ☐ Finnegan ☐ Gibson ☒ ~~Gonzalez~~ Wenzel ☐ Herbolsheimer ☐ Kingon

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Assistant Director for
Legislative Reference

Enclosures

THE WHITE HOUSE

WASHINGTON

May 22, 1985

MEMORANDUM FOR DAVID L. CHEW
DEPUTY ASSISTANT TO THE PRESIDENT AND
STAFF SECRETARY

FROM: SHERRIE M. COOKSEY SMC
ASSOCIATE COUNSEL TO THE PRESIDENT

SUBJECT: Enrolled Bill H.R. 1869 -- Amendment of Certain Taxpayer Recordkeeping Requirements

We have reviewed the above-referenced enrolled bill, which would repeal the contemporaneous recordkeeping requirement for business use of motor vehicles and certain other provisions of the Tax Reform Act of 1984, and have no legal objections to the President signing it.

Document No. _____

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RESPONSE: Recommend approval. 2 original signing pens will be requested but Requested ceremony pending before Scheduling. Please mail for decision. M. Rogers

David L. Chew
Staff Secretary
Ext. 2702

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David L. Chew
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CHAVEZ	☐	☐	RYAN	☐	☐
CHEW	☐P	☑	SPEAKES	☐	☑
DANIELS	☐	☐	SPRINKEL	☐	☐
FIELDING	☑	☐	SVAHN	☑	☐
FRIEDERSDORF	☑	☐	TUTTLE	☐	☐
HENKEL	☐	☐	_____	☐	☐
HICKEY	☐	☐	_____	☐	☐
HICKS	☐	☐	_____	☐	☐
KINGON	☑	☐	_____	☐	☐

REMARKS:

Please provide any comments/recommendations by 9:00 a.m. tomorrow, May 23rd. Thank you.

RESPONSE: Concur in approval recommendation.

David L. Chew
Staff Secretary
Ext. 2702

THE WHITE HOUSE

WASHINGTON

May 23, 1985

MEMORANDUM FOR DAVID L. CHEW

FROM: JOHN A. SVAHN JAS

SUBJECT: H.R. 1869 - Amendment of Certain Taxpayer Recordkeeping Requirements

The Office of Policy Development has no objection to the signing of H.R. 1869, Amendment of Certain Taxpayer Recordkeeping Requirements.

THE WHITE HOUSE

WASHINGTON

SCHEDULE PROPOSAL

May 20, 1985

TO: FREDERICK J. RYAN, JR., Director of Presidential Appointments and Scheduling

FROM: Max L. ~~Friedersdorf~~ MLF
M.B. Oglesby, Jr. MBO

REQUEST: To have a formal signing ceremony for H.R. 1869, an Act to repeal the contemporaneous recordkeeping requirements added to the Tax Reform Act of 1984.

PURPOSE: To recognize those Members of Congress who provided strong leadership in enacting H.R. 1869.

BACKGROUND: During the 98th Congress, an amendment to the Tax Reform Act of 1984 required that taxpayers maintain contemporaneous written records, or logs, of business vehicles when used for personal purposes. These records were to be used to substantiate certain business expense deductions or credits. After a tremendous public outcry in opposition, the Congress repealed this written recordkeeping requirement in H.R. 1869.

PREVIOUS PARTICIPATION: None on this issue.

DATE AND TIME: Between now and May 24, the scheduled date for adjournment for the Memorial Day recess.

DURATION: 10 minutes

LOCATION: The Oval Office

PARTICIPANTS: Participants list attached.

OUTLINE OF EVENTS:	Members to arrive through the Northwest Gate and be escorted from the West Lobby to the Oval Office for a formal signing ceremony with the President.
REMARKS REQUIRED:	Briefing paper to be provided.
MEDIA COVERAGE:	White House photographer only.
PROPOSED "PHOTO":	The President greeting the Members of Congress.
RECOMMENDED BY:	Max L. Friedersdorf M.B. Oglesby, Jr.
OPPOSED BY:	No opposition.
PROJECT OFFICER:	Fred McClure

Attachment A: Participants list

Attachment A

PARTICIPANTS

The President
The Vice President
Senator Robert Packwood (R-OR)
Senator James Abdnor (R-SD)
Senator John Heinz (R-PA)
Senator Malcolm Wallop (R-WY)
Senator Russell Long (D-LA)
Senator Lloyd Bentsen (D-TX)
Senator David Pryor (D-ARK)
Senator Edward Zorinsky (D-NE)

Appropriate House Members

Staff

Donald Regan
Max L. Friedersdorf
M.B. Oglesby, Jr.

Calendar No. 51

99TH CONGRESS
1st Session

SENATE

REPORT
99-23

REPEALING THE REQUIREMENT THAT CONTEMPORANEOUS RECORDS BE KEPT TO SUBSTANTIATE CERTAIN DEDUCTIONS AND CREDITS

APRIL 2 (legislative day, FEBRUARY 18), 1985.—Ordered to be printed

Mr. PACKWOOD, from the Committee on Finance, submitted the following

REPORT

[To accompany S. 245]

[Including cost estimate of the Congressional Budget Office]

The Committee on Finance, to which was referred the bill (S. 245) to repeal the requirement that contemporaneous records be kept to substantiate certain deductions and credits, having considered the same, reports favorably thereon with an amendment to the text and an amendment to the title and recommends that the bill as amended do pass.

The amendment to the text of the bill is shown in italics.

51-010 O

I. Explanation of the Bill

A. PRESENT LAW

Substantiation rules

Background

A taxpayer may deduct expenditures, including depreciation and operating costs, attributable to business use of an automobile or other means of transportation. No deduction is allowed for expenditures attributable to the personal use of an automobile or other property (other than for interest on purchase indebtedness or for certain State taxes). For example, the costs of commuting to and from work are personal expenses that are nondeductible pursuant to Code section 262.[1]

Under general tax law principles, the courts have held that a taxpayer bears the burden of proving both the eligibility of an expenditure as a deduction or credit and also the amount of any such eligible expenditure, including the expenses of using a car in the taxpayer's trade or business.[2]

In the Revenue Act of 1962, the Congress enacted Code section 274(d), under which a taxpayer must substantiate the business purpose, amount, and date of certain types of expenditures "by adequate records or by sufficient evidence corroborating his own statement." This provision was added because the Congress recognized that "in many instances deductions are obtained by disguising personal expenses as business expenses." [3] These specific substantiation rules were made applicable to (1) traveling expenses (including meals and lodging while away from home); (2) expenditures with respect to entertainment, amusement, or recreation activities or facilities; and (3) business gifts. Local travel expenses were not subject to this provision as enacted, but instead were subject to the general substantiation requirements applicable to all other business expenditures.

1984 Act amendments

Recordkeeping.—The Tax Reform Act of 1984 (P.L. 98-369) made several amendments to Code section 274(d), effective for taxable years beginning after December 31, 1984. First, the 1984 Act added a requirement that the taxpayer must keep "contemporaneous" records to substantiate deductions for expenditures subject to section 274(d). Second, the 1984 Act deleted from section 274(d) the alternative method of substantiating deductions, which was by means of sufficient evidence (written or oral) corroborating the taxpayer's own statement. Third, the 1984 Act made additional property subject to the requirements of section 274(d), including automobiles and other means of transportation. As a result, local travel expenses, like traveling expenses away from home, became subject to the section 274(d) rules.

[1] *Fausner* v. *Comm'r* 413 U.S. 838 (1973).
[2] See, e.g., *Interstate Transit Lines* v. *Comm'r* 319 U.S. 59, 593 (1943); *Comm'r* v. *Heininger*, 320 U.S. 467 (1943); *Gaines* v. *Comm'r*, 35 T.C.M. 1415 (1976).
[3] H. Rept. No. 87-1447, 87th Cong., 2d sess. (1962), at 19.

Tax preparer rules.—The 1984 Act required that paid income tax return preparers must advise the taxpayer of the section 274(d) substantiation requirements and obtain written confirmation from the taxpayer that these requirements were met. Failure to advise the taxpayer or to obtain the confirmation subjects the return preparer to a penalty of $25 for each failure, unless due to reasonable cause and not to willful neglect (sec. 6695(b)).

Special negligence penalty.—The 1984 Act provided that, for purposes of the section 6653 negligence penalty, any portion of an underpayment of tax due to a failure to comply with the section 274(d) recordkeeping requirements is treated as due to negligence, in the absence of clear and convincing evidence to the contrary. The penalty is five percent of the portion of the understatement attributable to the failure to comply with the section 274(d) recordkeeping requirements (sec. 6653(h)).

B. REASONS FOR CHANGE

The contemporaneous recordkeeping requirement and related compliance provisions enacted in the Tax Reform Act of 1984 reflected concerns of the Congress about significant overstatements of deductions and credits for claimed business use of automobiles and other types of property that typically are used for personal purposes, such as for commuting, vacation trips, personal errands and shopping excursions, etc. Many taxpayers who did make business use of automobiles or other vehicles failed to keep fully accurate records or based exaggerated claims of business use on inexact recollections at the time of filing their returns. To achieve increased compliance and accuracy, the Congress required that only contemporaneous records could be used to substantiate traveling expenses and the other types of expenditures listed in section 274(d), as revised by the 1984 Act. No definition of "contemporaneous" was set forth in the statute.

As businesses and individuals have sought to understand and comply with the contemporaneous recordkeeping requirement, it has become clear that the requirement sweeps too broadly and generally imposes excessive recordkeeping burdens on many taxpayers. While the Internal Revenue Service has modified its initial regulations interpreting the new requirement and has scheduled public hearings prior to adoption of final rules, the committee has concluded that the only appropriate actions that will provide a speedy and certain resolution to these problems are to repeal the "contemporaneous" requirement (and the tax return preparer and negligence penalty provisions) as added by the 1984 Act, to repeal the IRS temporary regulations interpreting the "contemporaneous" requirement, and to reinstate the prior-law substantiation standards under section 274(d) and the long-standing regulations thereunder.

C. EXPLANATION OF PROVISIONS

1. Repeal of 1984 Act provisions

Repeal of "contemporaneous"

The bill strikes the words "adequate contemporaneous records" from Code section 274(d) as if those words had never been a part of that provision, and inserts in lieu thereof the words "adequate records or by sufficient evidence corroborating the taxpayer's own statement". This is the substantiation standard that had been in effect prior to the Tax Reform Act of 1984 and that had been interpreted in long-standing IRS regulations originally issued in 1962.

The substantiation standard reinstated by the bill applies, as provided by section 274(d), to traveling expenses; entertainment, amusement, or recreation activities or facilities; business gifts; and, effective for taxable years beginning after 1984, and listed property (as defined in sec. 280F(d)(4)).

Repeal of return preparer provision

The bill repeals the provision of the 1984 Act requiring that a return preparer must specifically advise the taxpayer of the record-keeping requirements of section 274(d) and must obtain written confirmation from the taxpayer that such requirements were met (Code sec. 6695(b)). The bill provides that the Internal Revenue Code shall be applied and administered as if this provision had never been enacted.

Repeal of special negligence penalty

The bill repeals the provision of the 1984 Act providing a special negligence penalty rule (Code sec. 6653(h)) applicable to an underpayment of tax attributable to a failure to comply with the record-keeping requirements of section 274(d). The bill provides that the Internal Revenue Code shall be applied and administered as if this provision had never been enacted.

Repeal of certain regulations

The bill repeals all Treasury regulations (temporary or proposed) issued prior to the enactment of the bill which carry out the amendments made by paragraphs (1)(C), (2), and (3) of section 179(b) of the Tax Reform Act of 1984 that are repealed by this bill. These revoked regulations are to have no force and effect whatsoever.

2. Limited-use vehicles and certain flight benefits

The committee intends that Treasury regulations are to provide that the fair market value of an employee's commuting use of a limited-use vehicle furnished by the employer is excluded, as a working condition fringe, from the employee's gross income for Federal income tax purposes, and from the wage base (and, if applicable, from the benefit base) for purposes of income tax withholding and FICA, FUTA, and RRTA taxes. A limited-use vehicle is a vehicle the characteristics of which make it unlikely that it will be used more than a very minimal amount for personal purposes. Example of such limited-use vehicles include marked police and fire vehicles, ambulances used as such, school buses used as such, dump

trucks, cement mixers, refrigerated trucks, tractors, and specialized utility repair trucks used as such.

The committee also intends that the Treasury is to substitute the following safe-harbor valuation rules with respect to employee flights on employer-provided noncommercial aircraft that constitute taxable fringe benefits, for the valuation rules with respect to such benefits that are currently set forth in temporary regulations. The committee believes that these substitute safe-harbor rules reflect the intent of the Congress concerning the valuation of personal use of noncommercial aircraft under the fringe benefit rules in the Tax Reform Act of 1984.

Weight of aircraft	Includible value for control employees	Includible value for other employees
More than 10,000 pounds	First class fare	Value imputed to parent of airline employee.
More than 6,000 pounds but not more than 10,000 pounds.	Coach fare	¾ value imputed to parent of airline employee.
6,000 pounds or less	½ coach fare	½ value imputed to parent of airline employee.

The amount imputed to employees other than control employees is intended to be no more than the amount imputed to a parent of an airline employee, since it is difficult to distinguish the value of a standby flight on a commercial airline and a flight on a space-available basis on a similar noncommercial jet aircraft. However, the amount imputed to a parent of an airline employee under temporary Treasury regulations is presently 50 percent of the highest unrestricted coach fare for the trip which is charged by the carrier for which the employee works. The safe-harbor valuation regulations (as revised to reflect the committee's intent) are to utilize rules referring to commercial airline fares, such as Standard Initial Fare Level (SIFL) rates or industry average rates.

For purposes of the valuation rules in the table above, the term control employee means an employee (whether or not an officer) who controls the use of the aircraft for the trip, i.e., who controls either the use, scheduling, or destination of the aircraft.

D. EFFECTIVE DATE

The provisions of the bill repealing certain provisions enacted in the Tax Reform Act of 1984 take effect as if included in the amendments made by section 179(b) of the 1984 Act.

E. REVENUE EFFECT

The provisions of the bill are estimated to reduce fiscal year budget receipts by $48 million in 1985, $150 million in 1986, $225 million in 1987, $247 million in 1988, $259 million in 1989, and $270 million in 1990.

II. Budget Effects and Vote of the Committee

A. BUDGET EFFECTS

In compliance with paragraph 11(a) of Rule XXVI of the Standing Rules of the Senate, the following statement is made relative to the budget effects of S. 245, as reported by the committee.

Revenue effects

The revenue provisions of the bill are estimated to reduce fiscal year budget receipts by $48 million in 1985, $150 million in 1986, $225 million in 1987, $247 million in 1988, $259 million in 1989, and $270 million in 1990.

B. VOTE OF THE COMMITTEE

In compliance with paragraph 7(c) of Rule XXVI of the Standing Rules of the Senate, the following statement is made relative to the vote of the committee on the motion to report the bill, S. 245, as amended, was ordered favorably reported by a record vote.

III. Regulatory Impact of the Bill and Other Matters To Be Discussed Under Senate Rules

A REGULATORY IMPACT

Pursuant to paragraph 11(b) of Rule XXVI of the Standing Rules of the Senate, the committee makes the following statement concerning the regulatory impact that might be incurred in carrying out the provisions of S. 245, as reported.

Numbers of individuals and businesses who would be regulated

The bill does not involve new or expanded regulation of individuals or businesses. The bill reduces recordkeeping burdens on individuals and businesses.

Economic impact of regulation on individuals, consumers, and businesses

The bill repeals certain recordkeeping requirements imposed in the Tax Reform Act of 1984 and thereby reduces recordkeeping burdens on individuals and businesses.

Impact on personal privacy

The bill reduces recordkeeping burdens on individuals.

Determination of the amount of paperwork

The bill reduces paperwork burdens on individuals and businesses.

B. OTHER MATTERS

Consultation with Congressional Budget Office on budget estimates

In accordance with section 403 of the Budget Act, the committee advises that the Director of the Congressional Budget Office has examined the committee's budget estimates for the bill (as shown in Part II of this report) and agrees with the committee's budget estimates. The Director submitted the following statement.

U.S. Congress,
Congressional Budget Office,
Washington, DC, April 2, 1985.

Hon. Bob Packwood,
Chairman, Committee on Finance,
U.S. Senate, Washington, DC.

Dear Mr. Chairman: The Congressional Budget Office has examined S. 245, a bill which makes changes to certain provisions enacted in the Deficit Reduction Act of 1984 (DEFRA), as ordered reported by the Committee on Finance on April 2, 1985. The bill would repeal the contemporaneous recordkeeping requirement for certain deductions and credits imposed by DEFRA. In addition, the bill would change regulations governing the valuation of private use of corporate airplanes.

The Congressional Budget Office has reviewed and concurs with estimates of the revenue effects of the bill prepared by the staff of the Joint Committee on Taxation. The bill would reduce fiscal year revenues by $48 million in 1985, $150 million in 1986, $225 million in 1987, $247 million in 1988, $259 million in 1989, and $270 million in 1990.

If you wish further details on this estimate, we will be pleased to provide them.

With best wishes.

Sincerely,

Rudolph G. Penner.

New budget authority

In compliance with section 308(a)(1) of the Budget Act, and after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by the bill involve no new budget authority.

Tax expenditures

In compliance with section 308(a)(2) of the Budget Act with respect to tax expenditures, and after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by the bill will involve no new or increased tax expenditures.

IV. Changes in Existing Law Made by the Bill, as Reported

In the opinion of the committee, it is necessary, in order to expedite the business of the Senate, to dispense with the requirements of paragraph 12 of Rule XXVI of the Standing Rules of the Senate (relating to the showing of changes in existing law made by the provisions of S. 245, as reported by the committee).

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99TH CONGRESS
1st Session
HOUSE OF REPRESENTATIVES
REPORT
99-34

REPEAL OF THE CONTEMPORANEOUS RECORDKEEPING REQUIREMENTS

APRIL 2, 1985.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ROSTENKOWSKI, from the Committee on Ways and Means, submitted the following

REPORT

[To accompany H.R. 1869]

The Committee on Ways and Means, to whom was referred the bill (H.R. 1869) to repeal the contemporaneous recordkeeping requirements added by the Tax Reform Act of 1984, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

I. EXPLANATION OF THE BILL

A. PRESENT LAW

Substantiation rules

Background

A taxpayer may deduct expenditures, including depreciation and operating costs, attributable to business use of an automobile or other means of transportation. No deduction is allowed for expenditures attributable to the personal use of an automobile or other property (other than for interest on purchase indebtedness or for certain State taxes). For example, the costs of commuting to and from work are personal expenses that are nondeductible pursuant to Code section 262.[1]

Under general tax law principles, the courts have held that a taxpayer bears the burden of proving both the eligibility of an expenditure as a deduction or credit and also the amount of any such

[1] *Fausner* v. *Commissioner*, 413 U.S. 838 (1973).

51-006 O

eligible expenditure, including the expenses of using a car in the taxpayer's trade or business.[2]

In the Revenue Act of 1962, the Congress enacted Code section 274(d), under which a taxpayer must substantiate the business purpose, amount, and date of certain types of expenditures "by adequate records or by sufficient evidence corroborating his own statement." This provision was added because the Congress recognized that "in many instances, deductions are obtained by disguising personal expenses as business expenses." [3] These specific substantiation rules were made applicable to (1) traveling expenses (including meals and lodging while away from home); (2) expenditures with respect to entertainment, amusement, or recreation activities or facilities; and (3) business gifts. Local travel expenses were not subject to this provision as enacted, but instead were subject to the general substantiation requirements applicable to all other business expenditures.

1984 Act amendments

Recordkeeping.—The Tax Reform Act of 1984 (P.L. 98-369) made several amendments to Code section 274(d), effective for taxable years beginning after December 31, 1984. First, the 1984 Act added a requirement that the taxpayer must keep "contemporaneous" records to substantiate deductions for expenditures subject to sectioin 274(d). Second, the 1984 Act deleted from section 274(d) the alternative method of substantiating deductions, which was by means of sufficient evidence, (written or oral) corroborating the taxpayer's own statement. Third, the 1984 Act made additional property subject to the requirements of section 274(d), including automobiles and other means of transportation. As a result, local travel expenses, like traveling expenses away from home, became subject to the section 274(d) rules.

Tax preparer rules.—The 1984 Act required that paid income tax return preparers must advise the taxpayer of the section 274(d) substantiation requirements and obtain written confirmation from the taxpayer that these requirements were met. Failure to advise the taxpayer or to obtain the confirmation subjects the return preparer to a penalty of $25 for each failure, unless due to reasonable cause and not to willful neglect (sec. 6695(b)).

Special negligence penalty.—The 1984 Act provided that, for purposes of the section 6653 negligence penalty, any portion of an underpayment of tax due to a failure to comply with the section 274(d) recordkeeping requirements is treated as due to negligence, in the absence of clear and convincing evidence to the contrary. The penalty is five percent of the portion of the understatement attributable to the failure to comply with the section 274(d) recordkeeping requirements (sec. 6653(h)).

[2] See, e.g., *Interstate Transit Lines* v. *Comm'r* 319 U.S. 59, 593 (1943); *Comm'r* v. *Heininger*, 320 U.S. 467 (1943); *Gaines* v. *Comm'r*, 35 T.C.M. 1415 (1976).

[3] H. Rep. No. 87-1447 (March 16, 1962), at 19.

Limitations on ITC and depreciation for certain automobiles

General rules

In general, a 6-percent investment tax credit may be claimed for an eligible automobile, and its cost (reduced by one-half the amount of the 6-percent credit) may be recovered over three years. The accelerated recovery percentages, beginning with the first year, are 25, 38, and 37 percent. Other options with respect to the investment credit and depreciation are generally available.

However, limits generally are imposed on the amount of investment credit and annual depreciation deductions that are allowed for an automobile placed in service or leased by the taxpayer after June 18, 1984 (sec. 280F).[4] For an automobile subject to these limits and placed in service in 1984, (1) the investment tax credit is limited to $1,000, (2) depreciation in the first year is limited to $4,000, and (3) depreciation in any subsequent year is limited to $6,000.

For more expensive automobiles, the limits generally produce a recovery period longer than three years. If the depreciation limits result in unrecovered basis existing at the end of the recovery period otherwise applicable, then that basis may be recovered through a depreciation deduction in subsequent years equal to the lesser of the unrecovered basis of $6,000, if use of the automobile in those years is such that a depreciation deduction is otherwise allowable. The "unrecovered basis" means the excess of unadjusted basis over the aggregate amount of depreciation deductions that would have been allowed if 100 percent of the automobile's use had been in a trade or business or for the production of income.

The limits for any year are reduced by the proportion of total use in that year that is personal use.

Inflation adjustment to limits

For years after 1984, the $1,000, $4,000, and $6,000 limits are adjusted for inflation, as measured by the percentage growth of the automobile component of the Consumer Price Index for All Urban Consumers between October of the preceding year and October, 1983. The adjustment is rounded to the nearest $100. The adjusted limits for any year apply only to automobiles placed in service in that year.

B. REASONS FOR CHANGE

The contemporaneous recordkeeping requirement and related compliance provisions enacted in the Tax Reform Act of 1984 reflected concerns of the Congress about significant overstatements of deductions and credits for claimed business use of automobiles and other types of property that typically are used for personal pur-

[4] However, the limits do not apply to (1) certain automobiles acquired under binding contracts in effect before June 19, 1984; (2) ambulances and hearses used directly in the taxpayer's trade or business; (3) vehicles (such as taxicabs and limousines) used by the taxpayer directly in the trade or business of transporting persons or property for compensation or hire; and (4) regulations, trucks or vans.

Also, the limits do not apply to an automobile leased or held for leasing by a person regularly engaged in the business of leasing automobiles. Rather, the limitation affects the lessee, whose deductions for lease payments are reduced (according to tables prescribed by the Treasury) by amounts intended to approximate the results of placing the limits on the lessor.

poses, such as for commuting, vacation trips, personal errands and shopping excursions, etc. Many taxpayers who did make business use of automobiles or other vehicles failed to keep fully accurate records or based exaggerated claims of business use on inexact recollections at the time of filing their returns, To achieve increased compliance and accuracy, the Congress required that only contemporaneous records could be used to substantiate traveling expenses and the other types of expenditures listed in section 274(d), as revised by the Act. No definition of "contemporaneous" was set forth in the statute.

As businesses and individuals have sought to understand and comply with the contemporaneous recordkeeping requirement, it has become clear that the requirement sweeps too broadly and generally imposes excessive recordkeeping burdens on may taxpayers. While the Internal Revenue Service has modified its initial regulations and scheduled public hearings prior to adoption of final rules, the committee has concluded that the only appropriate actions that will provide a speedy and certain resolution to these problems are to repeal the "contemporaneous" requirement (and the tax return preparer and negligence penalty provisions) as added by the 1984 Act, to repeal the IRS temporary regulations interpreting the "contemporaneous" requirement, to reinstate with modifications generally the prior-law substantiation rules under section 274(d), and to except from these reinstated rules vehicles which, by reason of their nature, are not likely to be used more than a de minimis amount for personal purposes.

To provide guidance to taxpayers, the bill requires the IRS to issue regulations not later than October 1, 1985, carrying out the provisions of the bill. The bill specifies that these IRS regulations must fully reflect all the amendments made by the bill. In addition, IRS regulations must be consistent with the legislative history of the bill, including this report. Accordingly, any type of vehicle (such as farm tractors or combines, marked police or fire vehicles, etc.) that this report specifies are vehicles excepted from section 274(d) as qualified nonpersonal use vehicles must be so treated in the regulations.

The committee remains concerned about overstated claims of the extent of business use of automobiles or other property. The bill does not repeal all recordkeeping requirements for traveling expenses, etc. Indeed, the bill reinstates the prior-law substantiation requirements of section 274(d) as in effect prior to the 1984 Act amendments, with two modifications. First, a taxpayer who fails to maintain adequate records can substantiate expenditures subject to section 274(d) only by sufficient written evidence corroborating his or her own statement; oral evidence alone is not sufficient as corroboration for this purpose. Second, automobile expenses are made subject to the reinstated section 274(d) substantiation rules, effective for taxable years beginning after 1985; thus, such expenses are treated in the same manner as traveling expenses away from home.

In view of the budget deficit, the committee concluded that it is appropriate to balance the revenue loss resulting from the provisions of the bill repealing certain compliance rules enacted in the 1984 Act by adjusting the limitations set forth in section 280F on

the investment tax credit and depreciation deductions for automobiles.

C. EXPLANATION OF PROVISIONS

1. Repeal of 1984 Act provisions

Repeal of "contemporaneous"

The bill repeals the word "contemporaneous" from Code section 274(d) as if it had never been a part of that section. The bill also provides that the Internal Revenue Code is to be applied and administered as if the word "contemporaneous" had never been added to section 274(d).

Repeal of return preparer's provision

The bill repeals the provision of the 1984 Act requiring that a return preparer must specifically advise the taxpayer of the recordkeeping requirements of section 274(d) and must obtain written confirmation from the taxpayer that adequate contemporaneous records existed to support the claimed deductions or credits (Code sec. 6695(b)). The bill provides that the Internal Revenue Code shall be applied and administered as if this provision had never been enacted.

The committee believes that it is inappropriate to single out this one area of recordkeeping for special requirements, since return preparers already are responsible for the overall substantive accuracy of the preparation of the return. Also, because the committee intends (see below) that taxpayers claiming tax credits or depreciation for the use of automobiles and other listed property must indicate on the tax return whether the taxpayer has adequate records or sufficient written evidence supporting the claimed deductions and credits, the return preparer requirement is not needed. That is, if a return preparer signed a return that both claimed a deduction for the business use of a car and indicated that the taxpayer did not have the evidence required by the statute to justify the claims, the return preparer would be subject to existing penalties.

Repeal of special negligence penalty

The bill also repeals the provision of the 1984 Act providing a special negligence penalty rule applicable to an underpayment of tax attributable to a failure to comply with the recordkeeping requirements of section 274(d). The bill provides that the Internal Revenue Code shall be applied and administered as if this provision had never been enacted.

The committee believes that repealing this portion of the negligence penalty is needed to restore to the Internal Revenue Service and the courts discretion not to impose the negligence penalty for minor, inadvertent recordkeeping or computational errors. The committee emphasizes, however, that the regular negligence and fraud penalties will continue to be applicable if a taxpayer claims tax benefits that cannot be supported. The committee is concerned that these negligence and fraud penalties have not been applied by the Internal Revenue Service or the courts in a substantial number of instances where their application would be fully justified.

In one Tax Court case, for example, the taxpayer had kept detailed mileage records, required by his employer for reimbursement purposes, that indicated that his business use was approximately five percent of total use. On his tax return, the taxpayer claimed 70 percent business use, with no records to justify this claim. The Tax Court properly allowed only five percent business use. The Court did not, however, impose a negligence or fraud penalty. The committee believes that, in a case like this one, the negligence penalty should certainly be imposed, and that careful consideration should be given to imposing the civil fraud penalty.

In another Tax Court case, the taxpayer had kept detailed records so that he could be reimbursed by his employer, but claimed on his tax return approximately 35,000 miles of business use beyond what his records demonstrated, without any justification. No negligence penalty was imposed. In another case, the taxpayer produced a diary purporting to justify the claimed deductions. The Tax Court called the diary a "fabrication" and said that the taxpayer "was not telling the truth." The Court still permitted him a deduction, and did not impose the negligence or civil fraud penalty. Finally, another taxpayer apparently claimed a deduction for business mileage that exceeded the total mileage shown on his odometer, but the Tax Court did not impose a negligence or civil fraud penalty.

These cases indicate that the negligence and civil fraud penalties are not being administered by either the Internal Revenue Service or the courts in the manner that the Congress intended when it initially enacted these penalties. While minor, inadvertent recordkeeping or computational errors should not lead to the imposition of a substantial penalty, the committee believes that it is vital to the integrity of the tax system that honest taxpayers know that others who claim tax benefits far in excess of what can be justified will be subject to the negligence and fraud penalties.

Repeal of regulations

The bill repeals all Treasury Regulations (temporary or proposed) issued prior to the enactment of the bill that carry out the amendments made by section 179(b) of the Tax Reform Act of 1984. Thus, regulations issued to implement the changes to section 274(d) made by that Act, particularly the inclusion in that section of the word "contemporaneous," are revoked.[5] In addition, any regulations relating to the return preparer provision and the special negligence penalty (described above) are revoked.[6] These revoked regulations are to have no force and effect whatsoever.[7]

[5] Also, the regulations prohibiting the employer from including the entire value of the use of the automobile in the income of certain employees are revoked.

[6] The regulations relating to valuation issued under sections 61 and 132 are not, however, revoked.

[7] The committee revokes the regulations that provide for safe harbors for the use of highway vehicles. This change does not prohibit Treasury from developing similar safe harbors. To the extent that Treasury considers reinstating these safe harbors, the committee believes that Treasury should consider whether the standard requiring that farmers derive 70% of their income from farming may be too high.

2. Definition of adequate records

In general

The bill amends section 274 to require that taxpayers must maintain adequate records or sufficient written evidence corroborating the taxpayer's own statement to support the credits or deductions they are claiming.

The bill specifies that, in the alternate substantiation test, the sufficient corroborating evidence must be written. The committee believes that it is appropriate to require that taxpayers maintain written evidence to support their claims of tax credits and deductions. The written evidence must exist by the time tax return is filed.[8]

More specifically, in the case of travel, the committee intends that these records or evidence support the deductions or credits claimed. Adequate records or sufficient written evidence includes the following:

a. Account books
b. Diaries
c. Logs
d. Documentary evidence (receipts, paid bills)
e. Trip sheets
f. Expense reports
g. If the employee is required to make an adequate accounting to the employer and the reimbursement equals expenses, the employee is not required to report the expenses and reimbursement on his tax return
h. Written statements of witnesses

All of these types of documentation were specifically approved under prior law. The committee specifically approves of these means of documentation, and considers the longstanding Treasury Regulations on recordkeeping issued under section 274(d)[9] prior to the 1984 Act to reflect accurately its intent as to the documentation that taxpayers are required to maintain, except insofar as those regulations authorize the use of sufficient oral evidence corroborating the taxpayer's own statements and except that the written evidence must be compiled by the time the return is filed. The committee also believes that case law under section 274(d) generally reflects appropriate standards of recordkeeping, except insofar as those cases authorize the use of oral evidence corroborating the taxpayer's own statement. While taxpayers may choose to keep contemporaneous logs on the use of their automobiles, the Treasury is specifically prohibited from requiring that all taxpayers keep daily contemporaneous logs of their use of the automobile.

The committee believes that the written policy statements kept by the employer to implement a policy of no personal use (or no personal use except for commuting) qualify as sufficient written evidence corroborating the taxpayer's own statement. Therefore, the employee will not need to keep records under section 274(d) for

[8] In a few instances, the courts had permitted taxpayers to deduct amounts solely on the basis of oral evidence. The committee believes that requiring written evidence will be beneficial to taxpayers, because they will compile the necessary information by the time the tax return is filed.

[9] See Treas. Reg. sec. 1.274-5, initially published in the *Federal Register* on December 29, 1962.

the use of a vehicle that qualifies under either of these provisions. A written policy statement adopted by a governmental unit would be eligible for this rule. Thus, a resolution of the city council or a provision of state law or the state constitution would qualify, so long as the conditions described below are met.

The committee wants to continue the provision in the recent regulations that provided that no recordkeeping under section 274(d) is required if the employer provides a vehicle to an employee and prohibits personal use by the employee. In order to be eligible for this special rule, the following conditions must be met—

(a) The vehicle owned or leased by the employer is provided to one or more employees for use in connection with the employer's trade or business;

(2) When the vehicle is not being used for such business purposes, it is kept on the employer's business premises (or temporarily located elsewhere, e.g., for repair);

(3) Under the employer's policy, no employee may use the vehicle for personal purposes, other than de minimis personal use (such as a stop for lunch between two business deliveries);

(4) The employer reasonably believes that no employee uses the vehicle, other than de minimis use, for any personal purpose; and

(5) No employee using the vehicle lives at the employer's business premises.

To utilize this exception to the otherwise applicable substantiation requirement, there must be evidence that would enable the Internal Revenue Service to determine whether the use of the vehicle met the five conditions listed in the preceding paragraph.

The committee also wants to continue the provision in the recent regulations that provided that no recordkeeping under section 274(d) is required if the employer provides a vehicle to a specified employee and prohibits personal use by the employee, except for commuting. In order to be eligible for this rule, the following conditions must be met—

(1) The vehicle owned or leased by the employer is provided to one or more employees for use in connection with the employer's trade or business and is used in the employer's trade or business;

(2) For bona fide noncompensatory business reasons, the employer requires the employee to commute to and/or from work in the vehicle;

(3) The employer establishes a policy under which the employee may not use the vehicle for personal purposes, other than commuting or de minimis personal use (such as a stop for a personal errand between a business delivery and the employee's home);

(4) The employer reasonably believes that, except for de minimis use, the employee does not use the vehicle for any personal purpose other than commuting; and

(5) The employer accounts for the commuting use by including an appropriate amount in the employee's gross income. This special exception to the substantiation rule is not available if the employee using the vehicle for commuting is an officer or one-percent owner of the employer.

In order to utilize this exception to the otherwise applicable substantiation requirements, there must be evidence that would enable the Internal Revenue Service to determine whether the use of the vehicle meets the conditions set forth in the preceding paragraphs.

Information required on return

The committee wants to ensure that taxpayers claim only the deductions to which they are entitled without being unduly burdened by complex recordkeeping requirements. The committee also believes that taxpayers should provide sufficient information on their returns so that the Internal Revenue Service can make a preliminary evaluation of the appropriateness of the taxpayer's claimed deductions. Previously, the Internal Revenue Service found it difficult to make this sort of preliminary evaluation without auditing the taxpayer, which can also be a significant burden on the taxpayer. Therefore, the committee believes that taxpayers should all answer a few short questions on their returns if they claim the tax benefits for the business use of an automobile.

The committee believes that taxpayers will not be significantly burdened by responding to a few questions, most of them requiring a yes or no response. The committee directs that the following questions appear on the tax return, to be answered by taxpayers claiming credits or deductions for the business use of an automobile:

1. Total number of miles driven during the year: miles.

2. Percentage of personal use claimed: %.

3. Was the vehicle used for commuting Yes No. If Yes, the distance normally commuted: miles.

4. Was the vehicle available for personal use in off duty hours Yes No.

5. Is another vehicle available for personal use Yes No.

6. I have adequate records or sufficient written evidence to justify these deductions Yes No. If no, no deduction is permitted.

The committee notes that the requirement that these questions be included on the tax forms does not appear in the bill because the Internal Revenue Code does not generally specify the format or specific content of forms. The Internal Revenue Code does not need to be amended to provide the authority to require these questions, since that authority already exists in sections 6001 and 6011.

The committee intends that employees who claim deductions or credits for business use of their own car be asked these questions on Form 2106 (relating to employee business expenses); some of this information is already required to be provided on that form. Unincorporated taxpayers who claim these credits or deductions on either Schedules C or F (or on some other form) will be asked these questions on that form. Corporate taxpayers, as well as all other taxpayers and entities, will be asked these questions on the forms they are required to file.

The committee intends that employees give this information to their employers if the employer provided the car. Generally, the

employer would put this information on its tax return, since the employer is claiming the tax benefits of the use of the car. Employers who provide more than 5 cars to employees, however, would not have to include this information on the employer's return; the Internal Revenue Sevice could examine on audit the information that the employees provide to the employer. The employer would have to indicate on his return that he has received this information from the employees. The employer can rely on the employee's statement (unless the employer has reason to know it is false) to determine the credits and deductions to which the employer is entitled and to determine the amount of income, if any, the employer must include in the employee's income because of the employee's personal use of the employer's car.

The committee intends that similar questions be asked on the tax return about other listed property, such as yachts, airplanes, and computers. For computers, for example, the following questions should be asked:

1. Percentage of personal use claimed: %.
2. Was the computer located at your place of business or your home or both. If both, what percentage of the year was it at home: %.
3. Do you have records or written evidence to justify these deductions Yes No.

3. Vehicles with no personal use

The bill provides that any vehicle that by reason of its nature is not likely to be used more than a de minimis amount for personal purposes is exempt from the recordkeeping requirements of section 274(d).

The committee believes that this is an appropriate exemption from the recordkeeping requirements of section 274(d) because one of the purposes of those recordkeeping requirements is to ensure that taxpayers do not deduct as a business expense an expense that is really personal in nature. This purpose does not apply to a vehicle the characteristics of which make it highly unlikely that it will be used more than a very minimal amount for personal purposes. Consequently, the committee believes that it is appropriate to exempt these vehicles from the recordkeeping requirements of section 274(d). Taxpayers will still have to justify their claimed deductions for these vehicles as required under either section 162 or 212, which are the general provisions relating to business deductions.

The Internal Revenue Service had listed in its recent regulations under section 274(d) several examples of vehicles that by their nature are not likely to be used more than a de minimis amount for personal purposes:

a. forklifts,
b. cement mixers,
c. dump trucks (including garbage trucks),
d. refrigerated trucks,
e. tractors, and
f. combines.

The committee intends that these types of vehicles continue to be considered to be not susceptible to personal use. In addition, the committee believes that there are other types of vehicles that, because of their inherent nature or characteristics, are unlikely to be used more than a very minimal amount for personal purposes. The committee has identified the following types of vehicles as meeting this criterion:

a. delivery trucks with seating only for the driver,[10]
b. flatbed trucks,
c. any vehicle designed to carry cargo with a loaded gross vehicle weight over 14,000 pounds,
d. passenger buses used as such with a capacity of at least 20 passengers,
e. clearly marked police and fire vehicles,
f. ambulances used as such,
g. hearses used as such,
h. bucket trucks ("cherry pickers"),
i. cranes, and
j. derricks.

The committee recognizes that it may not have developed an exhaustive list of vehicles not susceptible to personal use. Therefore, the committee intends that the Internal Revenue Service expand this list through either regulations or revenue rulings to include those vehicles that the committee may not have included in this listing but that are appropriate for listing because by their nature it is highly unlikely that they will be used more than a very minimal amount for personal purposes.

A clearly marked police or fire vehicle is a vehicle, owned or leased by a governmental unit, that is clearly marked (through painted insignia or words) as a police or fire vehicle, the markings on which make it readily apparent that it is a police or fire vehicle. A marking on a license plate is not a clear marking.

The committee expects that it is appropriate for Treasury to provide in regulations that under certain conditions all use of such vehicles by an employee is excluded, as a working condition fringe benefit, from the employee's income and wages. If, for example, an employer requires, for bona fide business reasons, that the employee takes such a vehicle to his or her home when the employee is not working and that no personal use (e.g., shopping or recreation) is made of the vehicle, then all use of the vehicle could be considered business use which would be deductible under section 162, and thus excluded from income under section 132(d) as a working condition fringe.

The committee has not generally exempted from the recordkeeping requirement all pickup trucks and vans, because these vehicles can be easily used for personal purposes. Some taxpayers purchase these vehicles as substitutes for passenger sedans, and use them predominantly (or entirely) for personal purposes. One article has noted that, should vans be exempted, "taxpayers will have an opportunity to acquire luxury passenger vehicles with full tax benefits." On the other hand, however, the committee recognizes that this is not applicable to all vans. For example, a van that has only a front bench for seating, in which permanent shelving has been

[10] A vehicle with a jump seat (i.e., a seat that folds up flat) in addition to the seat only for the driver would also qualify.

installed, that constantly carries merchandise, and that has been specially painted with advertising or the company's name, is a vehicle not susceptible to personal use.

4. Withholding elections

As authorized by the legislative history of the 1984 Act, the Internal Revenue Service has provided (in temporary regulations) that an employer may withhold income and employment taxes due on taxable fringe benefits provided to an employee on a quarterly basis. For example, if the employee receives a $100 taxable benefit on January 10, withholding can be deferred by treating the benefit as paid on March 31.

The committee intends that the regulations are to be revised to allow an employer to elect, for income and employment tax purposes, to treat taxable fringe benefits (including personal use of employer-provided automobiles) as paid on a pay period, quarterly, semi-annual, or annual basis. Thus, in the example above, withholding could be deferred by treating the benefit as paid on June 30 or December 31.

In addition, the bill provides that an employer could elect not to withhold income taxes on the value of the personal use of an automobile that is included in the employee's income if (1) the employer gives the employee advance written notice of this election that nonwithholding is implemented as to that employee and (2) the employer includes the taxable amount of the benefit in the employee's income as reported on the Form W-2 provided by the employer to the employee for the year in which such benefit is received.[11] This election does not apply to FICA or RRTA taxes. The advance notice generally must be provided to the employee by January 1 of the year as to which the election is to apply; if an election is made for 1985, the notice must be provided by July 1, 1985. If the employer elects not to withhold income taxes, the employee can increase his withholding from regular wages by adjusting his Form W-4 so that the employee does not need to make estimated tax payments.

5. Limitations on ITC and depreciation

The bill reduces the limits on the amount of investment tax credit and annual depreciation decuctions that are allowed for an automobile as follows: (1) the investment tax credit is limited to $675; (2) depreciation in the first year is limited to $3600; and (3) depreciation in any subsequent year is limited to $5400.

For years after 1985, the limits provided in the bill are indexed for inflation, as measured by the percentage growth of the automobile component of the Consumer Price Index for All Urban Consumers between October of the preceding year and October 1984. Adjustments for inflation are otherwise determined as under present law. The committee intends that the Secretary of the Treasury shall prescribe the adjusted limits.

[11] These amounts will be treated as withheld upon for purposes of 280F(d)(6)(C)(i)(III).

D. EFFECTIVE DATES

Substantiation rules

The repeal of word "contemporaneous" from section 274(d) and the repeal of the return preparer's provision and the special negligence penalty enacted in the 1984 Act are effective as if those provisions had never been included in the 1984 Act.

The amendments to section 274(d) as reinstated—(1) providing that the evidence which can corroborate the taxpayer's own statement, in the absence of adequate records, is written evidence and (2) modifying the types of items subject to section 274(d)—are effective for taxable years beginning after December 31, 1985. The Internal Revenue Service is required to issue the regulations carrying out the provisions of the bill no later than October 1, 1985. This should give taxpayers sufficient time to prepare to comply with the provisions of this bill.

For taxable years beginning in 1985, the bill provides that prior law relating to recordkeeping applies. The committee believes that, because of the confusion that has existed since the start of the current year as to what recordkeeping requirements taxpayers would have to follow, taxpayers should be permitted for the current year to follow the rules that were in effect before the 1984 Act.

Limitations on ITC and depreciation

In general, the reduced limits on the investment tax credit and depreciaiton are effective for property placed in service by the taxpayer or leased by the taxpayer after April 2, 1985. However, property acquired by the taxpayer pursuant to a binding contract in effect on April 1, 1985, and at all times thereafter, is not subject to the reduced limits provided by the bill, if it is placed in service before August 1, 1985; and property of which the taxpayer is the lessee pursuant to a binding contract in effect on April 1, 1985, and all times thereafter, is not subject to the reduced limits if the taxpayer first uses the property under the lease before August 1, 1985. The reduced limits on the investment tax credit and depreciation are effective for the remainder of 1985; in 1986, those limits are indexed.

II. Budget Effects

In compliance with clause 7 of Rule XIII of the Rules of the House of Representatives, the following statement is made concerning the effect on the budget of the bill (H.R. 1869) as reported by the committee. The provisions of the bill as reported are estimated to decrease fiscal year budget receipts by $67 million in 1985, by $4 million in 1986, and increase receipts by $4 million in 1987, by $46 million in 1988, by $52 million in 1989, and by $57 million in 1990.

The Treasury Department agrees with this statement of budget effect.

III. Vote of the Committee and Other Matters To Be Discussed Under House Rules

A VOTE OF THE COMMITTEE

In compliance with clause 3(l)(2)(B) of Rule XI of the Rules of the House of Representatives, the following statement is made concerning the vote of the committee on the motion to report H.R. 1869. The bill, as amended, was ordered favorable reported by by voice vote.

B. OTHER MATTERS

In compliance with clauses 2(l)(3) and 2(l)(4) of Rule XI of the Rules of the House of Representatives, the following statements are made with respect to the committee action H.R. 1869.

Oversight findings

With respect to subdivision (A) of clause 2(l)(3) (relating to oversight findings), the committee advises that it was a result of the committee's review of the effect on individuals and businesses of the contemporaneous recordkeeping requirements enacted in the Tax Reform Act of 1984, as interpreted in temporary regulations issued by the IRS on October 15, 1984 and February 15, 1985, that the committee concluded that it is appropriate to repeal the contemporaneous requirements, to repeal the IRS temporary regulations interpreting that requirement, and to reinstate the prior law substantiation rules under Code section 274(d), with certain modifications. The committee held a hearing on this subject on March 5, 1985.

Tax expenditures

With respect to subdivision (B) of clause 2(l)(3), after consultation with the Director of the Congressional Budget Office, the committee states that the changes made by the bill as reported involve fiscal year decreases in tax expenditures of $17 million in 1985, $97 million in 1986, $130 million in 1987, $138 million in 1988, $144 million in 1989, and $151 million in 1990.

New budget authority

With respect to subdivision (B) of clause 2(l)(3) after consultation with the Director of the Congressional Budget Office, the committee states that the changes made by the bill as reported involve no new budget authority.

Congressional Budget Office estimates

Because of time constraints, it is not feasible to present a letter from the Director of the Congressional Budget Office before the bill is filed.

Oversight by Committee on Government Operations

With respect to subdivision (D) of clause 2(l)(3), the committee advises that no oversight findings or recommendations have been submitted to the Committee on Government Operations regarding the subject matter of the bill.

Inflationary impact

In compliance with clause 2(l)(4), the committee states that the enactment of the bill is not expected to have any inflationary impact on prices and costs in the operation of the national economy.

IV. Changes in Existing Law Made by the Bill, As Reported

In compliance with clause 3 of Rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE CODE OF 1954

* * * * * * *

Subtitle A—Income Taxes

* * * * * * *

CHAPTER 1—NORMAL TAXES AND SURTAXES

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Subchapter B—Computation of Taxable Income

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PART IX—ITEMS NOT DEDUCTIBLE

* * * * * * *

SEC. 274. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES.

(a) ENTERTAINMENT, AMUSEMENT OR RECREATION.—
(1) IN GENERAL.—* * *

* * * * * * *

(d) SUBSTANTIATION REQUIRED.—No deduction or credit shall be allowed—

(1) under section 162 or 212 for any traveling expense (including meals and lodging while away from home),

(2) for any item with respect to an acitivity which is of a type generally considered to constitute entertainment, amusement, or recreation, or with respect to a facility used in connection with such an activity,

(3) for any expense for gifts, or

(4) with respect to any listed property (as defined in section 280F(d)(4)),

unless the taxpayer substantiates by adequate [contemporaneous] records *or sufficient written evidence corroborating the taxpayer's own statement* (A) the amount of such expense or other item, (B) the time and place of the travel, entertainment, amusement, recre-

ation, or use of the facility or property, or the date and description of the gift, (C) the business purpose of the expense or other items, and (D) the business relationship to the taxpayer of persons entertained, using the facility or property, or receiving the gift. The Secretary may by regulations provide that some or all of the requirements of the preceding sentence shall not apply in the case of an expense which does not exceed an amount prescribed pursuant to such regulations. *This subsection shall not apply to any qualified nonpersonal use vehicle (as defined in subsection (i)).*

* * * * * * *

(i) QUALIFIED NONPERSONAL USE VEHICLE.—For purposes of subsection (d), the term "qualified nonpersonnal use vehicle" means any vehicle which, by reason of its nature, is not likely to be used more than a de minimis amount for personal purposes.

[(i)]*(j)* REGULATORY AUTHORITY.—The Secretary shall prescribe such regulations as he may deem necessary to carry out the purposes of this section, including regulations prescribing whether subsection (a) or subsection (b) applies in cases where both such subsections would otherwise apply.

* * * * * * *

SEC. 280F. LIMITATION ON INVESTMENT TAX CREDIT AND DEPRECIATION FOR LUXURY AUTOMOBILES; LIMITATION WHERE CERTAIN PROPERTY USED FOR PERSONAL PURPOSES.

(a) LIMITATION ON AMOUNT OF INVESTMENT TAX CREDIT AND DEPRECIATION FOR LUXURY AUTOMOBILES.—

(1) INVESTMENT TAX CREDIT.—The amount of the credit determined under section 46(a) for any passenger automobile shall not exceed [$1,000.] *$675.*

(2) DEPRECIATION.—

(A) LIMITATION.—The amount of the recovery deduction for any taxable year for any passenger automobile shall not exceed—

(i) [$4,000] *$3,600* for the first taxable year in the recovery period, and

(ii) [$6,000] *$5,400* for each succeeding taxable year in the recovery period.

(B) DISALLOWED DEDUCTIONS ALLOWED FOR YEARS AFTER RECOVERY PERIOD.—

(i) IN GENERAL.—Except as provided in clause (ii), the unrecovered basis of any passenger automobile shall be treated as an expense for the 1st taxable year after the recovery period. Any excess of the unrecovered basis over the limitation of clause (ii) shall be treated as an expense in the succeeding taxable year.

(ii) [$6,000] *$5,400* LIMITATION.—The amount treated as an expense under clause (i) for any taxable year shall not exceed [$6,000] *$5,400.*

(iii) PROPERTY MUST BE DEPRECIABLE.—No amount shall be allowable as a deduction by reason of this subparagraph with respect to any property for any taxable year unless a depreciation deduction would be allowable with respect to such property for such taxable year.

(iv) AMOUNT TREATED AS RECOVERY DEDUCTION.—For purposes of this subtitle, any amount allowable as a deduction by reason of this subparagraph shall be treated as a recovery deduction allowable under section 168.

(3) COORDINATION WITH REDUCTIONS IN AMOUNT ALLOWABLE BY REASON OF PERSONAL USE, ETC.—This subsection shall be applied before—

(A) the application of subsection (b), and

(B) the application of any other reduction in the amount of the credit determined under section 46(a) or any recovery deduction allowable under section 168 by reason of any use not qualifying the property for such credit or recovery deduction.

(4) SPECIAL RULE WHERE ELECTION OF REDUCED CREDIT IN LIEU OF THE BASIS ADJUSTMENT.—In the case of any election under section 48(q)(4) with respect to any passenger automobile, the limitation of paragraph (1) applicable to such passenger automobile shall be ⅔ of the amount which would be so applicable but for this paragraph.

* * * * * * *

(d) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) COORDINATION WITH SECTION 179.—Any deduction allowable under section 179 with respect to any listed property shall be subject to the limitations of subsections (a) and (b) in the same manner as if it were a recovery deduction allowable under section 168.

(2) SUBSEQUENT DEPRECIATION DEDUCTIONS REDUCED FOR DEDUCTIONS ALLOCABLE TO PERSONAL USE.—Solely for purposes of determining the amount of the recovery deduction for subsequent taxable years, if less than 100 percent of the use of any listed property during any taxable year is not use described in section 168(c)(1) (defining recovery property), all of the use of such property during such taxable year shall be treated as use so described.

(3) DEDUCTIONS OF EMPLOYEE.—

(A) IN GENERAL.—Any employee use of listed property shall not be treated as use in a trade or business for purposes of determining the amount of any credit allowable under section 38 to the employee or the amount of any recovery deduction allowable to the employee unless such use is for the convenience of the employer and required as a condition of employment.

(B) EMPLOYEE USE.—For purposes of subparagraph (A), the term "employee use" means any use in connection with the performance of services as an employee.

(4) LISTED PROPERTY.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the term "listed property" means—

(i) any passenger automobile,

(ii) any other property used as a means of transportation,

(iii) any property of a type generally used for purposes of entertainment, recreation, or amusement,

(iv) any computer or peripheral equipment (as defined in section 168(j)(5)(D)), and

(v) any other property of a type specified by the Secretary by regulations.

(B) EXCEPTION FOR CERTAIN COMPUTERS.—The term "listed property" shall not include any computer or peripheral equipment (as so defined) used exclusively at a regular business establishment. For purposes of the preceding sentence, any portion of a dwelling unit shall be treated as a regular business establishment if (and only if) the requirements of section 280A(c)(1) are met with respect to such portion.

(5) PASSENGER AUTOMOBILE.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the term "passenger automobile" means any 4-wheeled vehicle—

(i) which is manufactured primarily for use on public streets, roads, and highways, and

(ii) which is rated at 6,000 pounds gross vehicle weight or less.

(B) EXCEPTION FOR CERTAIN VEHICLES.—The term "passenger automobile" shall not include—

(i) any ambulance, hearse, or combination ambulance/hearse used by the taxpayer directly in a trade or business,

(ii) any vehicle used by the taxpayer directly in the trade or business of transporting persons or property for compensation or hire, and

(iii) under regulations, any truck or van.

(6) BUSINESS USE PERCENTAGE.—

(A) IN GENERAL.—The term "business use percentage" means the percentage of the use of any listed property during any taxable year which is a qualified business use.

(B) QUALIFIED BUSINESS USE.—Except as provided in subparagraph (C), the term "qualified business use" means any use in a trade or business of the taxpayer.

(C) EXCEPTION FOR CERTAIN USE BY 5-PERCENT OWNERS AND RELATED PERSONS.—

(i) IN GENERAL.—The term "qualified business use" shall not include—

(I) leasing property to any 5-percent owner or related person,

(II) use of property provided as compensation for the performance of services by a 5-percent owner or related person, or

(III) use of property provided as compensation for the performance of services by any person not described in subclause (II) unless an amount is included in the gross income of such person with respect to such use, and, where required, there was withholding under chapter 24.

(ii) SPECIAL RULE FOR AIRCRAFT.—Clause (i) shall not apply with respect to any aircraft if at least 25 percent of the total use of the aircraft during the taxable year consists of qualified business use not described in clause (i).

(D) DEFINITIONS.—For purposes of this paragraph—

(i) 5-PERCENT OWNER.—The term "5-percent owner" means any person who is a 5-percent owner with respect to the taxpayer (as defined in section 416(i)(1)(B)(i)).

(ii) RELATED PERSON.—The term "related person" means any person related to the taxpayer (within the meaning of section 267(b)).

(7) AUTOMOBILE PRICE INFLATION ADJUSTMENT.—

(A) IN GENERAL.—In the case of any passenger automobile, subsection (a) shall be applied by increasing each dollar amount contained in such subsection by the automobile price inflation adjustment for the calendar year in which such automobile is placed in service. Any increase under the preceding sentence shall be rounded to the nearest multiple of $100 (or if the increase is a multiple of $50, such increase shall be increased to the next higher multiple of $100).

(B) AUTOMOBILE PRICE INFLATION ADJUSTMENT.—For purposes of this paragraph—

(i) IN GENERAL.—The automobile price inflation adjustment for any calendar year is the percentage (if any) by which—

(I) the CBI automobile component for October of the preceding calendar year, exceeds

(II) the CBI automobile component for October of [1983.] *1984.*

In the case of [calendar year 1984,] *any calendar year before 1986,* the automobile price inflation adjustment shall be zero.

(ii) CPI AUTOMOBILE COMPONENT.—The term "CPI automobile component" means the automobile component of the Consumer Price Index for All Urban Consumers published by the Department of Labor.

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Subtitle C—Employment Taxes and Collection of Income Tax at Source

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CHAPTER 24—COLLECTION OF INCOME TAX AT SOURCE ON WAGES

* * * * * * *

SEC. 3402. INCOME TAX COLLECTED AT SOURCE.

(a) REQUIREMENT OF WITHHOLDING.—

(1) IN GENERAL.—* * *

* * * * * * *

(s) EXEMPTION FROM WITHHOLDING FOR ANY VEHICLE FRINGE BENEFIT.—

(1) EMPLOYER ELECTION NOT TO WITHHOLD.—The employer may elect not to deduct and withhold any tax under this chapter with respect to any vehicle fringe benefit provided to any employee if such employee is notified (at such time and in such manner as the Secretary shall by requlations prescribe) by the employer that the employer is making such election. The preceding sentence shall not apply to any vehicle fringe benefit unless the amount of such benefit is included by the employer on a statement timely furnished under section 6051.

(2) EMPLOYER MUST FURNISH W-2.—Any vehicle fringe benefit shall be treated as wages from which amounts are required to be deducted and withheld under this chapter for purposes of section 6051.

(3) VEHICLE FRINGE BENEFIT.—For purposes of this subsection, the term "vehicle fringe benefit" means any fringe benefit—

(A) which constitutes wages (as defined in section 3401), and

(B) which consists of providing a highway motor vehicle for the use of the employee.

* * * * * * *

SECTION 179 OF THE TAX REFORM ACT OF 1984

SEC. 179. LIMITATION ON AMOUNT OF DEPRECIATION AND INVESTMENT TAX CREDIT FOR LUXURY AUTOMOBILES; LIMITATION WHERE CERTAIN PROPERTY USED FOR PERSONAL PURPOSES.

(a) IN GENERAL.—* * *

(b) COMPLIANCE PROVISIONS.—

(1) AMENDMENT OF SECTION 274 (d).—* * *

[(2) DUTIES OF RETURN PREPARERS.—Subsection (b) of section 6695 (relating to failure to sign return) is amended to read as follows:

["(b) FAILURE TO INFORM TAXPAYER OF CERTAIN RECORDKEEPING REQUIREMENTS OR TO SIGN RETURN.—Any person who is an income tax return preparer with respect to any return or claim for refund and who is required by regulations to sign such return or claim—

["(1) shall advise the taxpayer of the substantiation requirements of section 274(d) and obtain written confirmation from the taxpayer that such requirements were met with respect to any deduction or credit claimed on such return or claim for refund and

["(2) shall sign such return or claim for refund.

Any person who fails to comply with the requirements of the preceding sentence with respect to any return or claim shall pay a penalty of $25 for such failure, unless it is shown that such failure is due to reasonable cause and not to willful neglect."

[(3) UNDERPAYMENT ATTRIBUTABLE TO FAILURE TO MEET SUBSTANTIATION REQUIREMENTS TREATED AS DUE TO NEGLIGENCE.—Section 6653 (relating to failure to pay tax) is amended by adding at the end thereof the following new subsection:

["(h) SPECIAL RULE IN THE CASE OF UNDERPAYMENT ATTRIBUTABLE TO FAILURE TO MEET CERTAIN SUBSTANTIATION REQUIREMENTS.—

["(1) IN GENERAL.—Any portion of an underpayment attributable to a failure to comply with the requirements of section 274(d) shall be treated, for purposes of subsection (a), as due to negligence in the absence of clear and convincing evidence to the contrary.

["(2) PENALTY TO APPLY ONLY TO PORTION OF UNDERPAYMENT DUE TO FAILURE TO MEET SUBSTANTIATION REQUIREMENTS.—If any penalty is imposed under subsection (a) by reason of paragraph (1), the amount of the penalty imposed by paragraph (1) of subsection (a) shall be 5 percent of the portion of the underpayment which is attributable to the failure described in paragraph (1)."]

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99TH CONGRESS
1st Session
HOUSE OF REPRESENTATIVES
REPORT
99-67

REPEAL OF CONTEMPORANEOUS RECORDKEEPING REQUIREMENTS

MAY 7, 1985.—Ordered to be printed

Mr. ROSTENKOWSKI, from the committee of conference, submitted the following

CONFERENCE REPORT

[To accompany H.R. 1869]

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 1869) to repeal the contemporaneous recordkeeping requirements added by the tax Reform Act of 1984, and for other purposes, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the House recede from its disagreement to the amendment of the Senate to the text of the bill and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

SECTION 1. REPEAL OF CONTEMPORANEOUS RECORDKEEPING REQUIREMENTS, ETC.

(a) CONTEMPORANEOUS RECORDKEEPING REQUIREMENTS.—Subsection (d) of section 274 of the Internal Revenue Code of 1954 (relating to substantiation requirements for certain deductions and credits) is amended by striking out "adequate contemporaneous records" and inserting in lieu thereof "adequate records or by sufficient evidence corroborating the taxpayer's own statement", and the Internal Revenue Code of 1954 shall be applied and administered as if the word "contemporaneous" had not been added to such subsection (d).

(b) PROVISIONS RELATING TO RETURN PREPARERS AND NEGLIGENCE PENALTY.—Paragraphs (2) and (3) of section 179(b) of the Tax Reform Act of 1984 are hereby repealed, and the Internal Revenue Code of 1954 shall be applied and administered as if such paragraphs (and the amendments made by such paragraphs) had not been enacted.

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(c) REPEAL OF REGULATIONS.—Regulations issued before the date of the enactment of this Act to carry out the amendments made by paragraphs (1)(C), (2), and (3) of section 179(b) of the Tax Reform Act of 1984 shall have no force and effect.

SEC. 2. SUBSTANTIATION REQUIREMENTS NOT TO APPLY TO CERTAIN VEHICLES WITH LITTLE PERSONAL USE.

(a) IN GENERAL.—Subsection (d) of section 274 of the Internal Revenue Code of 1954 (relating to substantiation required) is amended by adding at the end thereof the following new sentence: "This subsection shall not apply to any qualified nonpersonal use vehicle (as defined in subsection (i))."

(b) QUALIFIED NONPERSONAL USE VEHICLE DEFINED.—Section 274 of such Code is amended by redesignating subsection (i) as subsection (j) and by inserting after subsection (h) the following new subsection:

"(i) QUALIFIED NONPERSONAL USE VEHICLE.—For purposes of subsection (d), the term 'qualified nonpersonal use vehicle' means any vehicle which, by reason of its nature, is not likely to be used more than a de minimis amount for personal purposes."

SEC. 3. EXEMPTION FROM REQUIRED INCOME TAX WITHHOLDING FOR CERTAIN FRINGE BENEFITS.

Section 3402 of the Internal Revenue Code of 1954 (relating to income tax collected at source) is amended by adding at the end thereof the following new subsection:

"(s) EXEMPTION FROM WITHHOLDING FOR ANY VEHICLE FRINGE BENEFIT.—

"(1) EMPLOYER ELECTION NOT TO WITHHOLD.—The employer may elect not to deduct and withhold any tax under this chapter with respect to any vehicle fringe benefit provided to any employee if such employee is notified by the employer of such election (at such time and in such manner as the Secretary shall by regulations prescribe). The preceding sentence shall not apply to any vehicle fringe benefit unless the amount of such benefit is included by the employer on a statement timely furnished under section 6051.

"(2) EMPLOYER MUST FURNISH W-2.—Any vehicle fringe benefit shall be treated as wages from which amounts are required to be deducted and withheld under this chapter for purposes of section 6051.

"(3) VEHICLE FRINGE BENEFIT.—For purposes of this subsection, the term 'vehicle fringe benefit' means any fringe benefit—

"(A) which constitutes wages (as defined in section 3401), and

"(B) which consists of providing a highway motor vehicle for the use of the employee."

SEC. 4. REDUCTION IN LIMITATIONS ON INVESTMENT TAX CREDIT AND DEPRECIATION FOR LUXURY AUTOMOBILES.

(a) GENERAL RULE.—

(1) INVESTMENT TAX CREDIT.—Paragraph (1) of section 280F(a) of the Internal Revenue Code of 1954 (relating to investment tax credit) is amended by striking out "$1,000" and inserting in lieu thereof "$675".

(2) DEPRECIATION.—Paragraph (2) of section 280F(a) of such Code (relating to depreciation) is amended—

(A) by striking out "$4,000" in subparagraph (A)(i) and inserting in lieu thereof "$3,200", and

(B) by striking out "$6,000" each place it appears in subparagraphs (A)(ii) and (B)(ii) and inserting in lieu thereof "$4,800".

(b) 4-YEAR DEFERRAL OF INFLATION ADJUSTMENT.—

(1) ADJUSTMENT AFTER 1988.—Subparagraph (A) of section 280F(d)(7) of such Code (relating to automobile price inflation adjustment) is amended by striking out "passenger automobile" and inserting in lieu thereof "passenger automobile placed in service after 1988".

(2) 1987 BASE PERIOD.—Subclause (II) of section 280F(d)(7)(B)(i) of such Code is amended by striking out "1983" and inserting in lieu thereof "1987".

(3) TECHNICAL AMENDMENT.—Clause (i) of section 280F(d)(7)(B) of such Code is amended by striking out the last sentence.

SEC. 5. NEW REGULATIONS.

Not later than October 1, 1985, the Secretary of the Treasury or his delegate shall prescribe regulations to carry out the provisions of this Act which shall fully reflect such provisions.

SEC. 6. EFFECTIVE DATES.

(a) REPEALS.—The amendment and repeals made by subsections (a) and (b) of section 1 shall take effect as if included in the amendments made by section 179(b) of the Tax Reform Act of 1984.

(b) RESTORATION OF PRIOR LAW FOR 1985.—For taxable years beginning in 1985, section 274(d) of the Internal Revenue Code of 1954 shall apply as it read before the amendments made by section 179(b)(1) of the Tax Reform Act of 1984.

(c) EXCEPTION FROM SUBSTANTIATION REQUIREMENTS FOR QUALIFIED NONPERSONAL USE VEHICLES.—The amendments made by section 2 shall apply to taxable years beginning after December 31, 1985.

(d) WITHHOLDING AMENDMENT.—The amendment made by section 3 shall take effect on January 1, 1985.

(e) REDUCTION IN LIMITATIONS ON INVESTMENT TAX CREDIT AND DEPRECIATION.—

(1) Except as provided in paragraph (2), the amendments made by section 4 shall apply to—

(A) property placed in service after April 2, 1985, in taxable years ending after such date, and

(B) property leased after April 2, 1985, in taxable years ending after such date.

(2) The amendments made by section 4 shall not apply to any property—

(A) acquired by the taxpayer pursuant to a binding contract in effect on April 1, 1985, and at all times thereafter, but only if the property is placed in service before August 1, 1985, or

(B) of which the taxpayer is the lessee, but only if the lease is pursuant to a binding contract in effect on April 1,

1985, and at all times thereafter, and only if the taxpayer first uses such property under the lease before August 1, 1985.

And the Senate agree to the same.

That the House recede from its disagreement to the amendment of the Senate to the title of the bill and agree to the same.

JOINT EXPLANATORY STATEMENT OF THE COMMITTEE OF CONFERENCE

The managers on the part of the House and the Senate at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 1869) to repeal the contemporaneous recordkeeping requirements added by the Tax Reform Act of 1984, and for other purposes, submit the following joint statement to the House and the Senate in explanation of the effect of the action agreed upon by the managers and recommended in the accompanying conference report:

The Senate amendment to the text of the bill struck out all of the House bill after the enacting clause and inserted a substitute text.

The House recedes from its disagreement to the amendment of the Senate with an amendment which is a substitute for the House bill and the Senate amendment. The differences between the House bill, the Senate amendment, and the substitute agreed to in conference are noted below, except for clerical corrections, conforming changes made necessary by agreements reached by the conferees, and minor drafting and clarifying changes.

DAN ROSTENKOWSKI,
SAM M. GIBBONS,
J.J. PICKLE,
C.B. RANGEL,
PETE STARK,
JOHN J. DUNCAN,
BILL ARCHER,
GUY VANDER JAGT,
Managers on the Part of the House.

BOB PACKWOOD,
BOB DOLE,
W.V. ROTH, Jr.,
JOHN DANFORTH,
RUSSELL LONG,
LLOYD BENTSEN,
SPARK M. MATSUNAGA,
Managers on the Part of the Senate.

STATEMENT OF MANAGERS ON THE PART OF THE HOUSE

I. EXPLANATION OF PROVISIONS

A. Repeal of Requirement That Certain Records Must Be Contemporaneous (secs. 1.(a) and (c) and 2(a) of the House bill and secs. 1 (a) and (c) of the Senate amendment)

1. Repeal of "contemporaneous" requirement

Present law

The Tax Reform Act of 1984 (the 1984 Act) amended Code section 274(d) to require that taxpayers must maintain "adequate contemporaneous records" to substantiate deductions and credits for business use of automobiles and other listed property.

House bill

The House bill repeals the word "contemporaneous," effective as if it had never been enacted.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment.

2. Alternate substantiation method

Present law and background

Prior to the 1984 Act, taxpayers were required under section 274(d) to substantiate deductions for travel away from home (including meals and lodging), for items with respect to entertainment, amusement, or recreation activities of facilities, and for business gifts by adequate records or by sufficient evidence corroborating the taxpayer's own statement. In the case of an expense or item subject to substantiation under section 274(d), that provision required substantiation as to (1) the amount of such expense or other item, (2) the time and place of the travel, entertainment, amusement, recreation, or use of the facility, or the date and description of the gift, (3) the business purpose of the expense or other item, and (4) the business relationship to the taxpayer of persons entertained, using the facility, or receiving the gift. Prior to the 1984 Act, local travel (i.e., travel not away from home) was not subject to the section 274(d) substantiation standards.

Section 179(b) of the 1984 Act deleted from section 274(d) the alternate substantiation method of sufficient evidence corroborating the taxpayer's own statement. The 1984 Act also applied the section 274(d) substantiation requirements to deductions or credits claimed for use of listed property (as defined in sec. 280F(d)(4)). The categories of listed property include automobiles (whether used for local travel or travel away from home), other means of transportation, computers, etc.

House bill

The House bill provides that, as an alternative to maintaining adequate records, taxpayers may substantiate deductions and credits under section 274(d) by sufficient written evidence corroborating their own statement.

The committee report also requires that certain information concerning mileage and business use of vehicles, as well as similar information concerning business use of other listed property, must be requested on tax returns.

The House bill is effective on January 1, 1986. For 1985, the substantiation rules in effect prior to the 1984 Act would apply.

Senate amendment

The Senate amendment is similar to the House bill in that it provides for an alternate substantiation method. However, the Senate amendment does not require that the evidence must be written in order to qualify as sufficient under the alternate substantiation standard. The Senate amendment is effective January 1, 1985.

The Senate amendment does not specifically require that questions regarding the business use of automobiles and other listed property be asked on tax returns.

Conference agreement

Substantiation standards

In general

The conference agreement generally follows the Senate amendment as to the substantiation standards under section 274(d). Thus, section 274(d) is amended to require that a taxpayer must have adequate records or sufficient evidence corroborating the taxpayer's own statement to support credits or deductions for expenditures subject to the section 274(d) substantiation rules. As under pre-1984 Act law, section 274(d) as amended by the bill requires the taxpayer to substantiate (1) the amount of the expense or item subject to section 274(d), (2) the time and place of the travel, entertainment, amusement, recreation, or use of the facility or property, or the date and description of the gift, (3) the business purpose of the expense or other item, and (4) the business relationship to the taxpayer of persons entertained, using the facility or property, or receiving the gift.

The conferees believe that a taxpayer's uncorroborated statement as to the business use of an automobile or other listed property does not alone have sufficient probative value to warrant consideration by the Internal Revenue Service or the courts. Consequently, the conferees adopt for this purpose the standard of prior law applicable to travel away from home and business entertainment (sec. 274(d)) that requires taxpayers to provide either adequate records or sufficient evidence corroborating their own statements in order to support a deduction or credit under section 274(d). The more general substantiation standards applicable under section

162,[1] which have been interpreted to permit in certain circumstances uncorroborated statements by taxpayers to support business deductions not subject to section 274(d) or other special rules, are to have no application to deductions or credits with respect to local travel, computers, and other listed property first required (under this bill) to meet the section 274(d) substantiation standards beginning January 1, 1986, just as they are to have no application with respect to expenditures with respect to travel away from home, etc., which continue to be subject to section 274(d) substantiation standards.

The conference agreement does not include the provision of the House bill that would require that the sufficient evidence corroborating the taxpayer's own statement be written. The conferees believe that oral evidence corroborating the taxpayer's own statement, such as oral testimony from a disinterested, unrelated party describing the taxpayer's activities, may be of sufficient probative value that it should not be automatically excluded from consideration under section 274(d).

The conferees emphasize, however, that different types of evidence have different degrees of probative value. The conferees believe that oral evidence alone has considerably less probative value than written evidence. In addition, the conferees believe that the probative value of written evidence is greater the closer in time it relates to the expenditure. Thus, written evidence arising at or near the time of the expenditure, absent unusual circumstances, has much more probative value than evidence created years later, such as written evidence first prepared for audit or court.

The conferees specifically approve the types of substantiation that were required under prior law, and consider the longstanding Treasury regulations on recordkeeping issued under section 274(d)[2] prior to the 1984 Act to reflect accurately their intent as to the substantiation that taxpayers are required to maintain.[3] While taxpayers may choose to keep logs on the use of their automobiles, and while such evidence generally has more probative value than evidence developed later, the Treasury is specifically prohibited from requiring that taxpayers keep daily contemporaneous logs of their use of automobiles.

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[1] Under general tax law principles, the courts have held that a taxpayer bears the burden of proving both the eligibility of any expenditure claimed as a deduction or credit and also the amount of any such eligible expenditure, including the expenses of using a car in the taxpayer's trade or business. See, e.g., *Interstate Transit Lines* v. *Comm'r*, 319 U.S. 590, 593 (1943); *Comm'r* v. *Heininger*, 320 U.S. 467 (1943); *Gaines* v. *Comm'r*, 35 T.C.M. 1415 (1976).

[2] See Teas. Reg. sec. 1.274-5.

[3] Prior law provided that adequate records or sufficient evidence may take the following forms:

a. Account books
b. Diaries
c. Logs
d. Documentary evidence (receipts, paid bills)
e. Trip sheets
f. Expense reports
g. Statements of witnesses
h. If the employee is required to make an adequate accounting to the employer and the reimbursement equals expenses, the employee is not required to report the expenses and reimbursement on his or her tax return. (A reimbursement would equal expenses where the reimbursement is determined pursuant to data on the type of automobile and its availability for personal purposes, and on a reasonable allocation of local operating and fixed costs.)

The conferees expect the Internal Revenue Service and the courts to continue to weigh carefully the probative value of these, as well as all other, forms of evidence. The Service and the courts continue to have the ability to discount or reject totally evidence that has limited or no probative value (such as documents actually created much later than they purport to have been created). As noted above, section 274(d) requires that the records or evidence (whatever their particular form) most substantiate not just the amount of the expense, but also the time and place of the travel, entertainment, amusement, recreation, or use of the facility or property, or the date and description of the gift; the business purpose of the expense or other item; and the business relationship to the taxpayer of persons entertained, using the facility or property, or receiving the gift.

Although the conferees intend that the principles of these regulations fully apply to deductions and credits claimed for local travel and the use of other listed property under section 274(d), the conferees also recognize that these principles will need to be carefully applied to local travel and listed property not previously subject to section 274(d). This will need to be done because the nature of making these expenditures generally differs from the nature of making the types of expenditures that had been required to meet the section 274(d) substantiation standards prior to the 1984 Act, such as travel away from home and business meals. For example, deductions associated with local travel may be for annual amounts for items such as depreciation and insurance, rather than a series of discrete expenditures for meals or hotels. Also, expenses for travel away from home often involve a third party, such as an airline, train, or hotel, that provides a receipt for the taxpayer of the date and amount of the expenditure and the destination or location. Similarly, expenses for business meals generally occur in restaurants, which provide a similar receipt. While these receipts do not, of course, encompass all of the elements of the substantiation requirements under section 274(d),[4] they do aid taxpayers in their recordkeeping. Similar third party involvement generally is not available for local travel or the use of computers. Similarly, expenses for travel away from home or for business meals do not generally occur with the same frequency as individual local travel trips. Because the bill repeals the 1984 Act requirement of contemporaneous records, taxpayers are not required to maintain trip-by-trip logs and records encompassing each element of the substantiation standards of section 274(d) to justify a deduction or credit.

Consequently, the conferees recognize that some adjustment generally will need to be made in order to apply these principles to the specific factual circumstances surrounding expenditures for local travel and use of listed property not previously subject to section 274(d) rules. The conferees believe that the courts and the Treasury can make these required adjustments without sacrificing these principles, and without reverting to the section 162 standards (including the *Cohan* [5] rule), which the conferees have determined are

[4] For example, the third party is not in a position to record the business purpose of the trip or meal; the taxpayer must provide that information, which is required under the section 274(d) substantiation rules.

[5] *Cohan* v. *Commissioner*, 39 F.2d 540, 544 (2d Cir. 1930).

inadequate and unacceptable for purposes of section 274(d). In several cases previously decided under section 274(d), it is not clear that the courts had rejected the *Cohan* rule; the conferees believe that the courts must clearly and explicitly reject the *Cohan* rule for expenditures required to meet the substantiation requirements of section 274(d).

Written policy statements

The conferees intend that the two types of written policy statements satisfying the conditions described below, if initiated and kept by an employer to implement a policy of no personal use (or no personal use except for commuting) of a vehicle provided by the employer, qualify as sufficient evidence corroborating the taxpayer's own statement [6] and therefore will satisfy the employer's substantiation requirements under section 274(d). Therefore, the employee need not keep a separate set of records for purposes of the employer's substantiation requirements under section 274(d) with respect to use of a vehicle satisfying these written policy statement rules. A written policy statement adopted by a government unit as to employee use of its vehicles would be eligible for these exceptions to the section 274(d) substantiation rules. Thus, a resolution of a city council or a provision of state law or the state constitution would qualify as a written policy statement, so long as the conditions described below are met.

The first type of written policy statement that will satisfy the employer's substantiation requirements under section 274(d) is a policy that prohibits personal use by the employee. In order to be eligible for this special rule, all of the following conditions must be met—

(1) The vehicle is owned or leased by the employer and is provided to one or more employees for use in connection with the employer's trade or business;

(2) When the vehicle is not being used for such business purposes, it is kept on the employer's business premises (or temporarily located elsewhere, e.g., for repair);

(3) Under the employer's written policy, no employee may use the vehicle for personal purposes, other than de minimis personal use (such as a stop for lunch between two business deliveries);

(4) The employer reasonably believes that no employee uses the vehicle, other than de minimis use, for any personal purpose;

(5) No employee using the vehicle lives at the employer's business premises; and

(6) There must be evidence that would enable the Internal Revenue Service to determine whether the use of the vehicle met the five preceding conditions.

The second type of written policy statement that will satisfy the employer's substantiation requirements under section 274(d) is a policy that prohibits personal use by the employee, except for commuting. In order to be eligible for this rule, all of the following conditions must be met—

[6] The substance of these two special rules was set forth in the temporary Treasury regulations repealed by the bill. The conferees intend that these rules, as described in this report, be reinstated in the new regulations required by the bill.

(1) The vehicle is owned or leased by the employer and is provided to one or more employees for use in connection with the employer's trade or business and is used in the employer's trade or business;

(2) For bona fide noncompensatory business reasons, the employer requires the employee to commute to and/or from work in the vehicle;

(3) The employer establishes a written policy under which the employee may not use the vehicle for personal purposes, other than commuting or de minimis personal use (such as a stop for a personal errand between a business delivery and the employee's home);

(4) The employer reasonably believes that, except for de minimis use, the employee does not use the vehicle for any personal purpose other than commuting;

(5) The employer accounts for the commuting use by including an appropriate amount (specified in Treasury regulations) in the employee's gross income; [7] and

(6) There must be evidence that would enable the Internal Revenue Service to determine whether the use of the vehicle met the five preceding conditions.

This second type of written policy statement is not available if the employee using the vehicle for commuting is an officer or one-percent owner of the employer.[8]

Tax return questions

The conference agreement generally follows the House bill as to information to be requested on tax returns about business use of vehicles and other listed property.

The conferees want to ensure that taxpayers claim only the deductions and credits to which they are entitled, but without being unduly burdened by unnecessarily complex recordkeeping requirements. At the same time, the conferees believe that taxpayers should provide sufficient information on their returns so that the Internal Revenue Service can make a preliminary evaluation of the appropriateness of the taxpayer's claimed deductions. Previously, the Internal Revenue Service found it difficult to make such a preliminary evaluation without auditing the taxpayer, which can also be a significant burden on the taxpayer.

Therefore, the conferees intend that individual taxpayers (whether employees or self-employed) claiming deductions or credits for business use of an automobile or other listed property subject to the substantiation standards of section 274(d) are to provide on their returns the substance of the information (generally on appropriate existing tax forms) called for by all the questions as set forth in the House report on the bill.[9] Corporate taxpayers, as well as all

[7] Of course, if in fact the employee uses the vehicle for personal purposes in violation of the particular type of written policy statement, then the employee has additional gross income.

[8] This restriction, which makes this rule inapplicable to officers or one-percent owners, applies for substantiation purposes under the conference agreement. The treatment of commuting use of vehicles by such persons for valuation purposes is to be determined separately under Treasury regulations. No inference is intended, on the basis of the exclusion of officers and one-percent owners from eligibility under this substantiation rule, as to the treatment of commuting use of vehicles by such persons under valuation rules prescribed by Treasury regulations.

[9] In the case of a vehicle, the information required to be requested on the tax return relates to mileage (total, business, commuting, and other personal), percentage of business use, date placed

Continued

other taxpayers and entities, claiming such deductions or credits also are to be asked to supply such information on the forms or schedules they are required to file.

The conferees have carefully considered the fact that furnishing additional tax return information, although involving only a limited number of questions, requires some additional effort by taxpayers. However, the conferees note that computations involved with respect to vehicles (such as mileage and percentage of business use) normally would be made by taxpayers in the process of determining the proper amount of deductions and credits to claim, and that other information can be obtained through "yes" or "no" questions. Accordingly, to achieve better compliance and more accurate computations, the conference agreement directs the Internal Revenue Service to obtain this information on appropriate tax forms or schedules, notwithstanding any otherwise applicable paperwork reduction considerations.

The conferees intend that employees give this return information to their employers with respect to employer-provided vehicles. Generally, the employer would report this information on its tax return, since the employer is claiming the tax deductions or credits for use of the vehicle. An employer which provides more than five cars to its employees, however, would not have to include all this information on the employer's return; instead, such an employer must obtain this information from its employees, must so indicate on its return, and must retain the information received. The Internal Revenue Service could then examine on audit the information that the employees had provided to the employer. An employer may rely on such a statement from its employee (unless the employer knows or has reason to know it is false) to determine the credits and deductions to which the employer is entitled and to determine the amount, if any, which must be included in employee's income and wages by the employer because of the employee's commuting or other personal use of the employer-provided car.

Effective dates

The modification to the substantiation standards of section 274(d) that provides that taxpayers must substantiate deductions or credits subject to that provision by adequate records or sufficient evidence corroborating their own statement is effective January 1, 1985.

Use of listed property that was not subject to section 274(d) substantiation rules prior to the 1984 Act (such as local travel in an automobile or use of computers) is subject to the section 274(d) substantiation requirements effective January 1, 1986.[10] For 1985, use

in service, use of other vehicles and after-work use, whether the taxpayer has evidence to support the business use claimed on the return, and whether or not the evidence is written. In the case of other listed property subject to the section 274(d) rules, information should be requested in connection with appropriate tax forms or schedules as to type of property (e.g., yacht, computer, airplane, etc.), percentage of business use, whether the taxpayer has written evidence to support the business use claimed on the return, and whether or not the evidence is written. Under the conference agreement, the Internal Revenue Service is not required to request on returns the specific question relating to computers set forth as question 2 on page 10 of the committee report on the House Bill.

[10] This January 1, 1986 effective date applies only to the extent that use of listed property was first made subject to the substantiation standards of section 274(d) by the 1984 Act. Deductions

Continued

of such listed property is not subject to the special substantiation standards under section 274(d).

The tax return information (described above) must be requested on returns for taxable years beginning in 1985 (i.e., in the case of most individuals, returns which must be filed by April 15, 1986.)

3. Repeal of regulations

Present law

The Internal Revenue Service has issued temporary regulations implementing the recordkeeping provisions of section 179(b) of the 1984 Act.

House bill

The House bill repeals all Treasury regulations (temporary or proposed) issued prior to the enactment of this House bill that carry out the amendments made by section 179(b) of the Tax Reform Act of 1984. Thus, such regulations issued to implement the changes to section 274(d) made by that Act, particularly the inclusion in that section of the word "contemporaneous," are revoked.[11] In addition, any regulations relating to the return preparer provision and the special negligence penalty (described above) are revoked.[12] These revoked regulations are to have no force and effect whatsoever.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment. Thus, the conference agreement provides that regulations issued to carry out the amendments made by paragraphs (1)(C), (2), and (3) of section 179(b) of the 1984 Act shall have no force and effect.

B. Repeal of Provisions Relating to Return Preparers (sec. 1(b) of the House bill and sec. 1(c) of the Senate amendment)

Present law

Return preparers must advise taxpayers of the substantiation requirements under section 274(d) and obtain written confirmation that those requirements have been met (Code section 6695(b)).

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for expenses or items that were subject to the section 274(d) substantiation standards prior to the 1984 Act (such as use of an automobile for travel away from home or use of a yacht that is an entertainment, recreation, or amusement facility) remain subject to the section 274(d) substantiation standards for all taxable years ending after December 31, 1962.

[11] Also, the provisions of the temporary regulations that prohibit an employer from including the entire value of the use of an automobile in the income of certain employees are revoked. Thus, an employer is permitted to charge the entire value of an employer-provided car to an employee as income and wages (for income tax, FICA, FUTA, and RRTA withholding purposes). The employer may then reimburse the employee for the business use of the car, or the employee may claim a deduction on the employee's income tax return for the business use of the car.

[12] The bill only revokes such regulations (issued prior to enactment) carrying out such amendments made by sections 179(b)(1)(C), (2), and (3) of the 1984 Act. Thus, the bill does not revoke any other regulations, such as regulations issued under sections 61 and 132 (relating to valuation).

House bill

The House bill repeals this provision, effective as if it had never been enacted.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment.

C. Repeal of Special Negligence Penalty (sec. 1(b) of the House bill and sec. 1(c) of the Senate amendment)

Present law

A special no-fault negligence penalty (Code sec. 6653(h)) applies to the portion of any understatement of tax attributable to failure to meet the substantiation requirements of section 274(d).

House bill

The House bill repeals this special negligence penalty, effective as if it had never been enacted.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment. The conference agreement provides that the Internal Revenue Code shall be applied and administered as if this special negligence penalty had never been enacted.

The conferees believe that repealing this special negligence penalty is needed to restore to the Internal Revenue Service and the courts discretion not to impose the negligence penalty for minor, inadvertent recordkeeping or computational errors. The conferees emphasize, however, that the regular negligence and fraud penalties will continue to be applicable if a taxpayer claims tax benefits that cannot be supported. The conferees are concerned that these regular negligence and fraud penalties have not been applied by the Internal Revenue Service or the courts in a substantial number of instances where their application would be fully justified.

In one Tax Court case, for example, the taxpayer had kept detailed mileage records, required by his employer for reimbursement purposes, that indicated that his business use was approximately five percent of total use. On his tax return, the taxpayer claimed 70 percent business use, with no records to justify this claim. The Tax Court properly allowed only five percent business use. The Court did not, however, impose a negligence or fraud penalty. The conferees believe that, in a case like this one, the regular negligence penalty should certainly be imposed, and that careful consideration should be given to imposing the civil fraud penalty.

In another Tax Court case, the taxpayer had kept detailed records so that he could be reimbursed by his employer, but

claimed on his tax return approximately 35,000 miles of business use beyond what his records demonstrated, without any justification. No negligence penalty was imposed. In another case, the taxpayer produced a diary purporting to justify the claimed deductions. The Tax Court called the diary a "fabrication" and said that the taxpayer "was not telling the truth." The Court still permitted him a deduction, and did not impose the regular negligence or civil fraud penalty. Finally, another taxpayer apparently claimed a deduction for business mileage that exceeded the total mileage shown on his odometer, but the Tax Court did not impose a negligence or civil fraud penalty.

These cases indicate that the regular negligence and civil fraud penalties are not being administered by either the Internal Revenue Service or the courts in the manner that the Congress intended when it initially enacted these penalties. While minor, inadvertent recordkeeping or computational errors should not lead to the imposition of a substantial penalty, the conferees believe that it is vital to the integrity of the tax system that honest taxpayers know that others who claim tax benefits far in excess of what can be justified will be subject to the negligence and fraud penalties.

D. Exceptions From Section 274(d) Rules and Exclusion From Income for Certain Vehicles (sec. 2(b) of the House bill and sec. 2 of the Senate amendment)

Present law

Substantiation rules

Temporary Treasury regulations provided that, except for vehicles used for commuting, vehicles of a type ordinarily not susceptible to personal use do not constitute listed property to which the section 274(d) substantiation requirements apply. The regulations cited, as examples of such vehicles that are not susceptible to personal use, trucks specially designed for specific business purposes (such as refrigerated delivery trucks), special-purpose farm vehicles (such as tractors and combines), cement mixers, and forklifts.

Income inclusion

The fair market value of an employer-provided fringe benefit, such as personal use by an employee of an employer-provided vehicle, is included in the employee's gross income, and in wages for purposes of withholding and FICA, FUTA, and RRTA taxes, unless excluded under a specific statutory provision of the Code (secs. 61(a)(1), 3121(a), 3231(e), 3306(b), 3401(a)).

House bill

Substantiation rules

The House bill exempts from the section 274(d) substantiation rules (as modified by the bill) any vehicle that, by reason of its nature, is not likely to be used more than a de minimis amount for personal purposes. This provision is effective for taxable years beginning after December 31, 1985; thus, for 1985 the pre-1984 Act substantiation rules continue to apply with respect to such vehicles.

The committee report on the House bill lists the following vehicles as examples of vehicles exempted under the bill from the section 274(d) substantiation rules: (a) clearly marked police and fire vehicles (as described in the report); (b) delivery trucks with seating only for the driver, or only for the driver plus a folding jump seat; (c) flatbed trucks; (d) any vehicle designed to carry cargo with a loaded gross vehicle weight over 14,000 pounds; (e) passenger buses used as such with a capacity of at least 20 passengers; (f) ambulances used as such or hearses used as such; (g) bucket trucks ("cherry pickers"); (h) cranes and derricks; (i) forklifts; (j) cement mixers; (k) dump trucks (including garbage trucks); (l) refrigerated trucks; (m) tractors; and (n) combines.

The report on the House bill also states that the committee recognizes that it may not have developed an exhaustive list of vehicles not susceptible to personal use. Therefore, the report states, the committee intends that the Internal Revenue Service is to expand this list through either regulations or revenue rulings to include any vehicles not included in the listing in the report that are appropriate for listing because by their nature it is highly unlikely that they will be used more than a very minimal amount for personal purposes.

The report also states that the committee did not generally exempt from the section 274(d) substantiation rules all pickup trucks and vans, because these vehicles can easily be used for personal purposes. Some taxpayers purchase these vehicles as substitutes for passenger sedans, and use them predominantly (or entirely) for personal purposes. On the other hand, however, the committee report recognized that this is not applicable to all vans. For example, a van that has only a front bench for seating, in which permanent shelving [13] has been installed, that constantly carries merchandise, and that has been specially painted with advertising or the company's name, is a vehicle not susceptible to personal use.

Income inclusion

The committee report on the House bill states that it is appropriate for Treasury regulations to provide that under certain conditions all use by an employee of any employer-provided vehicle that is exempted under the House bill from the section 274(d) substantiation rules (see above) is excluded, as a working condition fringe benefit (sec. 132(a)(3)),[14] from the employee's gross income, and from wages (and, where appropriate, from the benefit base) for purposes of FICA, FUTA, and RRTA taxes. Such exclusions pursuant to Treasury regulations are to be effective as of January 1, 1985.

Senate amendment

Substantiation rules

The Senate amendment provides that the following vehicles are exempt from the section 274(d) substantiation rules (as modified by

[13] It is intended that this shelving fill most of the cargo area.

[14] Absent such a special exclusion, commuting use (or other personal use) by an employee of an employer-provided vehicle could not qualify as a working condition fringe benefit because the costs of commuting to and from work (or of other personal use of a vehicle) are nondeductible pursuant to Code section 262. *See, e.g., Fausner* v. *Comm'r*, 413 U.S. 838 (1973).

the amendment), and that any commuting or other personal use of such exempted vehicles is excluded from the user's gross income, and from wages (and, where appropriate, from the benefit base) for purposes of FICA, FUTA, and RRTA taxes, effective January 1, 1985:

(a) Vehicles required to be used as an integral part of the trade or business of an individual or of the employer (such as calling on customers or clients, making deliveries, or visiting job sites), so long as use in the trade or business is at least 75 percent of the vehicle's total use;

(b) Vehicles used by an employee for commuting, where the commuting is for a bona fide business purpose, where the employer does not permit the employee to make other personal use of the vehicle (other than de minimis use), and where use in the trade or business of the employer is at least 75 percent of total use; and

(c) Vehicles used by a governmental unit for police or other law enforcement purposes and vehicles used as an ambulance.

Income inclusion

The Senate amendment provides that any commuting or other personal use of such exempted vehicles (described above) is excluded from the user's gross income, and from wages (and, where appropriate, from the benefit base) for purposes of FICA, FUTA, and RRTA taxes, effective January 1, 1985.

ITC and depreciation caps

The Senate amendment provides that police and law enforcement vehicles and ambulances placed in service after June 18, 1984 are exempt from the investment tax credit and depreciation limitations set forth in section 280F.

Conference agreement

The conference agreement follows the House bill, with the following modifications.

The conferees intend that school buses (as defined in Code section 4221(d)(7)(C)), qualified specialized utility repair trucks, and qualified moving vans, in addition to the list above (items (a) through (n) in the description of the House bill), are also to be examples of vehicles that, by reason of their nature, are not likely to be used more than a de minimis amount for personal purposes.

The term "qualified specialized utility repair trucks" means trucks (not including vans or pickup trucks) specifically designed and used to carry heavy tools, testing equipment, or parts where (1) the shelves, racks, or other permanent interior construction which has been installed to carry and store such heavy items is such that it is unlikely that the truck will be used more than a very minimal amount for personal purposes [15] and (2) the employer requires the employee to drive the truck home in order to be able to respond in emergency situations for purposes of restoring or maintaining electricity, gas, telephone, water, sewer, or steam utility services.

[15] An example of this would be permanent shelving that fills most of the cargo area.

The term "qualified moving vans" means vans used by professional moving companies in the trade or business of moving household or business goods where no personal use of the van is allowed other than for travel to and from a move site (or for de minimis use), where personal use for travel to and from a move site is an irregular practice (i.e., not more than five times a month on average), and where personal use is limited to situations in which it is more convenient to the employer, because of the location of the employee's residence, for the van not to be returned to the employer's business location.

Also, the conferees agreed that the Treasury Department has authority to issue regulations exempting from the section 274(d) substantiation rules, and from inclusion in income and wages, officially authorized uses of unmarked vehicles by law enforcement officers. To qualify for this exemption, the personal use must be authorized by the Federal, State, county, or local governmental agency or department that owns or leases the vehicle and employs the officer, and must be for law-enforcement functions such as undercover work or reporting directly from home to a stakeout or surveillance site, or to an emergency situation. Use of an unmarked vehicle for vacation or recreation trips cannot qualify as an authorized use. The term "law enforcement officer" means an individual who is employed on a full-time basis by a governmental unit that is responsible for the prevention or investigation of crime involving injury to persons or property, who is authorized by law to carry firearms and execute search warrants and also to make arrests (other than merely a citizen arrest), and who regularly carries firearms (except when it is not possible to do this because of the requirements of undercover work). The term "law enforcement officer" does not include Internal Revenue Service special agents.

The conference agreement also provides that if, for example, a municipal government ordinance requires that police officers driving clearly marked police cars who are on duty at all times must take the vehicle home when the employee is not on his or her regular shift, and prohibits any personal use (except for this commuting use) of the vehicle outside the city (i.e., outside the limit of the officer's arrest powers), then all use of the vehicle could be considered in such regulations as an excludable working condition fringe.

E. Withholding Election (sec. 3 of the House bill)

Present law

As authorized under the 1984 Act, temporary Treasury regulations have provided for withholding (or payment) of income and employment taxes with respect to taxable noncash fringe benefits, such as an employee's personal use of an employer-provided vehicle, on a quarterly basis (Code sec. 3501(b)).

House bill

The House bill provides that an employer may elect not to deduct and withhold income taxes with respect to the noncash fringe benefit attributable to an employee's personal use of a highway motor vehicle provided by the employer. An employer making this election must so notify the employee (at such time and in such

manner as provided in Treasury regulations) and must include the fair market value of the benefit on the Form W-2 furnished to the employee. An electing employer must still withhold social security (or railroad retirement) taxes. This provision is effective as of January 1, 1985.

The committee report on the House bill states that the committee intends that the regulations are to be revised to allow an employer to elect, for income and employment tax purposes, to treat taxable fringe benefits (including personal use of employer-provided automobiles) as paid on a pay period, quarterly, semi-annual, or annual basis.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill.

F. Limitations on Investment Tax Credit and Depreciation for Automobiles (sec. 4 of the House bill)

Present law

The 1984 Act generally imposed limitations on the amount of investment tax credit and annual depreciation deductions that are allowed for an automobile placed in service or leased by the taxpayer after June 18, 1984.

For an automobile placed in service in 1984, (1) the investment tax credit is limited to $1,000; (2) depreciation in the first taxable year the automobile is placed in service is limited to $4,000; and (3) depreciation in any subsequent taxable year is limited to $6,000. For years after 1984, the limits are adjusted for inflation, as measured by the percentage growth of the automobile component of the Consumer Price Index for All Urban Consumers between October of the preceding year and October, 1983. The adjusted limits for any year apply only to automobiles placed in service in that year.

House bill

The limits on the amount of investment tax credit and annual depreciation deductions that may be claimed with respect to an automobile are reduced as follows under the House bill; (1) the investment tax credit is limited to $675; (2) depreciation in the first taxable year the automobile is placed in service is limited to $3,600 and (3) depreciation in any subsequent taxable year is limited to $5,400. For years after 1985, the reduced limits are indexed for inflation, as measured by the percentage growth of the automobile component of the Consumer Price Index for All Urban Consumers between October of the preceding year and October, 1984. Adjustments for inflation are otherwise determined as under present law. The committee report states that the committee intends that the Secretary of the Treasury prescribe all limits adjusted for inflation.

The reduced limits are generally effective for property placed in service or leased by the taxpayer after April 2, 1985. However, property acquired by the taxpayer pursuant to a binding contract in effect on April 1, 1985, and at all times thereafter, is not subject to the reduced limits if it is placed in service before August 1, 1985; and property of which the taxpayer is the lessee pursuant to a binding contract in effect on April 1, 1985, and all times thereafter, is not subject to the reduced limits if the taxpayer first uses the property under the lease before August 1, 1985.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill, with three modifications: (1) depreciation in the first taxable year is limited to $3,200; (2) depreciation in any subsequent taxable year is limited to $4,800; and (3) the reduced limits on the investment credit and depreciation are not indexed for inflation until 1989. For automobiles placed in service in any year after 1988, the reduced limits are adjusted for the percentage increase of the automobile component of the Consumer Price Index for All Urban Consumers between October of the preceding year and October, 1987. The conferees made these changes to the House bill to ensure that the conference agreement is revenue neutral.

G. New Regulations (sec. 5 of the House bill)

Present law

The Treasury Department has the authority to issue regulations under the Internal Revenue Code.

House bill

The House bill requires that the Treasury Department issue regulations to carry out the provisions of the House bill not later than October 1, 1985.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill. Because the conferees have delayed applicability of the section 274(d) substantiation rules to local travel, computers, etc., until January 1, 1986, the conferees believe that requiring regulations to be issued by October 1, 1985, will provide taxpayers with sufficient time to prepare to meet these requirements.

II. ESTIMATED REVENUE EFFECTS

ESTIMATED REVENUE EFFECTS OF PROVISIONS OF H.R. 1869 AS AGREED TO BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1985–90

[Millions of dollars]

Provision	1985	1986	1987	1988	1989	1990
Changes to Substantiation and Withholding Requirements	−172	−111	−151	−148	−149	−154
Reduction in Limitations on ITC and Depreciation for Autos	22	124	181	209	228	241
Total	−150	13	30	61	79	87

DAN ROSTENKOWSKI,
SAM M. GIBBONS,
J. J. PICKLE,
C. B. RANGEL,
PETE STARK,
JOHN J. DUNCAN,
BILL ARCHER,
GUY VANDER JAGT,
Managers on the Part of the House.

BOB PACKWOOD,
BOB DOLE,
W. V. ROTH, JR.,
JOHN DANFORTH,
RUSSELL LONG,
LLOYD BENTSEN,
SPARK M. MATSUNAGA,
Managers on the Part of the Senate.

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THE WHITE HOUSE

Office of the Press Secretary

For Immediate Release May 24, 1985

REMARKS OF THE PRESIDENT
DURING SIGNING CEREMONY FOR HR 1869

The Oval Office

1:03 P.M. EDT

THE PRESIDENT: I am delighted to have you here for this signing of HR 1869. It repeals a requirement for a very extensive regulation -- an unnecessary one, I think -- on people who use business vehicles for private purposes also. And I am glad to have you here and it is just a part of what I hope will be a larger tax reform later, so we can all be together for another signing. But more about that next week.

Q We are looking forward to it, Mr. President.

Q I hope the rest of the tax reform is as easy as this one was. I somehow doubt it.

THE PRESIDENT: You and me both.

This will gladden the hearts of many Americans and I know that you had there the public support in this.

Q Thank you. We appreciate you doing this, sir.

THE PRESIDENT: It is the least that I can do.

Q We are glad that you did that for the American working man and woman. That is what that is all about.

Q Particularly in my district. Thank you, Mr. President.

Q It is great for the people.

THE PRESIDENT: And, as I say, I think we can remove a few more regulations.

Q Mr. President, how would you like to give one of those pens to Jim Abdnor. It was his bill on the Senate side there.

SENATOR ABDNOR: Thank you, Mr. President.

THE PRESIDENT: All right.

Q Can another one of those pens be given away, or one has to go to the Archives? (Laughter.)

Q You mean the one in Nebraska?

Q Thank you, Mr. President. It shows common sense and logic prevail.

THE PRESIDENT: God bless you all.

Q Thank you.

Q The first stage in tax reform -- that is what I told Mr. Baker when he testified.

Q That was the up end.

MORE

Q That was the downturn. (Laughter)

Q I wish all our battles on deregulation were this easy.

THE PRESIDENT: Yes, I do, too. I think we have got a lot more to go.

Q Mr. President, did you know this was in the bill last year? Didn't you know this provision was in the bill last year? Why did you sign it last year with this onerous provision in it?

THE PRESIDENT: Because I didn't have line-item veto.

Q Mr. President, do you think the House version of the budget is really going to hurt national security?

THE PRESIDENT: I think I am going to wait and express my opinion when it gets to Congress.

Q You are concerned about it?

THE PRESIDENT: Yes, I am concerned.

Q Thank you very much, Mr. President.

END 1:06 P.M. EDT