

TITLE I—INDIVIDUAL INCOME TAX PROVISIONS

Subtitle A—Rate Reductions; Increase in Standard Deduction and Personal Exemptions

SEC. 101. RATE REDUCTIONS.

(a) GENERAL RULE.—Section 1 (relating to tax imposed on individuals) is amended to read as follows:

“SECTION 1. TAX IMPOSED.

“(a) MARRIED INDIVIDUALS FILING JOINT RETURNS AND SURVIVING SPOUSES.—There is hereby imposed on the taxable income of—

“(1) every married individual (as defined in section 7703) who makes a single return jointly with his spouse under section 6013, and

“(2) every surviving spouse (as defined in section 2(a)), a tax determined in accordance with the following table:

“If taxable income is	The tax is:
Not over \$29,750	15% of taxable income.
Over \$29,750	\$4,462.50, plus 28% of the excess over \$29,750.

“(b) HEADS OF HOUSEHOLDS.—There is hereby imposed on the taxable income of every head of a household (as defined in section 2(b)) a tax determined in accordance with the following table:

“If taxable income is	The tax is:
Not over \$23,900	15% of taxable income.
Over \$23,900	\$3,585, plus 28% of the excess over \$23,900.

“(c) UNMARRIED INDIVIDUALS (OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLDS).—There is hereby imposed on the taxable income of every individual (other than a surviving spouse as defined in section 2(a) or the head of a household as defined in section 2(b)) who is not a married individual (as defined in section 7703) a tax determined in accordance with the following table:

“If taxable income is	The tax is:
Not over \$17,850	15% of taxable income.
Over \$17,850	\$2,677.50, plus 28% of the excess over \$17,850.

“(d) MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—There is hereby imposed on the taxable income of every married individual (as defined in section 7703) who does not make a single return jointly with his spouse under section 6013, a tax determined in accordance with the following table:

“If taxable income is	The tax is:
Not over \$14,875	15% of taxable income.
Over \$14,875	\$2,231.25, plus 28% of the excess over \$14,875.

“(e) ESTATES AND TRUSTS.—There is hereby imposed on the taxable income of—

- “(1) every estate, and
- “(2) every trust,

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“If taxable income is	The tax is:
Not over \$29,750	15% of taxable income.
Over \$29,750	\$4,462.50, plus 28% of the excess over \$29,750.

“(b) HEADS OF HOUSEHOLDS.—There is hereby imposed on the taxable income of every head of a household (as defined in section 2(b)) a tax determined in accordance with the following table:

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Not over \$23,900	15% of taxable income.
Over \$23,900	\$3,585, plus 28% of the excess over \$23,900.

“(c) UNMARRIED INDIVIDUALS (OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLDS).—There is hereby imposed on the taxable income of every individual (other than a surviving spouse as defined in section 2(a) or the head of a household as defined in section 2(b)) who is not a married individual (as defined in section 7703) a tax determined in accordance with the following table:

“If taxable income is	The tax is:
Not over \$17,850	15% of taxable income.
Over \$17,850	\$2,677.50, plus 28% of the excess over \$17,850.

“(d) MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—There is hereby imposed on the taxable income of every married individual (as defined in section 7703) who does not make a single return jointly with his spouse under section 6013, a tax determined in accordance with the following table:

“If taxable income is	The tax is:
Not over \$14,875	15% of taxable income.
Over \$14,875	\$2,231.25, plus 28% of the excess over \$14,875.

“(e) ESTATES AND TRUSTS.—There is hereby imposed on the taxable income of—

- “(1) every estate, and
- “(2) every trust,

taxable under this subsection a tax determined in accordance with the following table:

"If taxable income is	The tax is:
Not over \$5,000	15% of taxable income.
Over \$5,000	\$750, plus 28% of the excess over \$5,000.

"(f) ADJUSTMENTS IN TAX TABLES SO THAT INFLATION WILL NOT RESULT IN TAX INCREASES.—

"(1) IN GENERAL.—Not later than December 15 of 1988, and each subsequent calendar year, the Secretary shall prescribe tables which shall apply in lieu of the tables contained in subsections (a), (b), (c), (d), and (e) with respect to taxable years beginning in the succeeding calendar year.

"(2) METHOD OF PRESCRIBING TABLES.—The table which under paragraph (1) is to apply in lieu of the table contained in subsection (a), (b), (c), (d), or (e), as the case may be, with respect to taxable years beginning in any calendar year shall be prescribed—

"(A) by increasing the minimum and maximum dollar amounts for each rate bracket for which a tax is imposed under such table by the cost-of-living adjustment for such calendar year,

"(B) by not changing the rate applicable to any rate bracket as adjusted under subparagraph (A), and

"(C) by adjusting the amounts setting forth the tax to the extent necessary to reflect the adjustments in the rate brackets.

"(3) COST-OF-LIVING ADJUSTMENT.—For purposes of paragraph (2), the cost-of-living adjustment for any calendar year is the percentage (if any) by which—

"(A) the CPI for the preceding calendar year, exceeds

"(B) the CPI for the calendar year 1987.

"(4) CPI FOR ANY CALENDAR YEAR.—For purposes of paragraph (3), the CPI for any calendar year is the average of the Consumer Price Index as of the close of the 12-month period ending on August 31 of such calendar year.

"(5) CONSUMER PRICE INDEX.—For purposes of paragraph (4), the term 'Consumer Price Index' means the last Consumer Price Index for all-urban consumers published by the Department of Labor. For purposes of the preceding sentence, the revision of the Consumer Price Index which is most consistent with the Consumer Price Index for calendar year 1986 shall be used.

"(6) ROUNDING.—

"(A) IN GENERAL.—If any increase determined under paragraph (2)(A), subsection (g)(4), section 63(c)(4), or section 151(d)(3) is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.

"(B) TABLE FOR MARRIED INDIVIDUALS FILING SEPARATELY.—In the case of a married individual filing a separate return, subparagraph (A) (other than with respect to section 63(c)(4)) shall be applied by substituting '\$25' for '\$50' each place it appears.

"(g) PHASEOUT OF 15-PERCENT RATE AND PERSONAL EXEMPTIONS.—

"(1) IN GENERAL.—The amount of tax imposed by this section (determined without regard to this subsection) shall be increased by 5 percent of the excess (if any) of—

“(A) taxable income, over
 “(B) the applicable dollar amount.

“(2) **LIMITATION.**—The increase determined under paragraph (1) with respect to any taxpayer for any taxable year shall not exceed the sum of—

“(A) 13 percent of the maximum amount of taxable income to which the 15-percent rate applies under the table contained in subsection (a), (b), (c), or (e) (whichever applies), and

“(B) 28 percent of the deductions for personal exemptions allowable to the taxpayer for the taxable year under section 151.

In the case of any individual taxable under subsection (d), subparagraph (A) shall apply as if such individual were taxable under subsection (a).

“(3) **APPLICABLE DOLLAR AMOUNT.**—For purposes of paragraph (1), the applicable dollar amount shall be determined under the following table:

“In the case of a taxpayer to which the following subsection of this section applies:	The applicable dollar amount is:
Subsection (a).....	\$71,900
Subsection (b).....	61,650
Subsection (c).....	43,150
Subsection (d).....	35,950
Subsection (e).....	13,000.

“(4) **ADJUSTMENT FOR INFLATION.**—In the case of any taxable year beginning in a calendar year after 1988, each dollar amount contained in paragraph (3) shall be increased by an amount equal to—

“(A) such dollar amount, multiplied by
 “(B) the cost-of-living adjustment determined under subsection (f)(3) for the calendar year in which the taxable year begins.

“(h) **TAX SCHEDULES FOR TAXABLE YEARS BEGINNING IN 1987.**—In the case of any taxable year beginning in 1987—

“(1) subsection (g) shall not apply, and
 “(2) the following tables shall apply in lieu of the tables set forth in subsections (a), (b), (c), (d), and (e):

“(A) **MARRIED INDIVIDUALS FILING JOINT RETURNS AND SURVIVING SPOUSES.**—The table to apply for purposes of subsection (a) is as follows:

“If taxable income is	The tax is:
Not over \$3,000	11% of taxable income.
Over \$3,000 but not over \$28,000.....	\$330, plus 15% of the excess over \$3,000.
Over \$28,000 but not over \$45,000.....	\$4,080, plus 28% of the excess over \$28,000.
Over \$45,000 but not over \$90,000.....	\$8,840, plus 35% of the excess over \$45,000.
Over \$90,000	\$24,590, plus 38.5% of the excess over \$90,000.

“(B) **HEADS OF HOUSEHOLDS.**—The table to apply for purposes of subsection (b) is as follows:

“If taxable income is	The tax is:
Not over \$2,500	11% of taxable income.
Over \$2,500 but not over \$23,000.....	\$275, plus 15% of the excess over \$2,500.
Over \$23,000 but not over \$38,000.....	\$3,350, plus 28% of the excess over \$23,000.

"If taxable income is	The tax is:
Over \$38,000 but not over \$80,000.....	\$7,550, plus 35% of the excess over \$38,000.
Over \$80,000	\$22,250, plus 38.5% of the excess over \$80,000.

"(C) UNMARRIED INDIVIDUALS OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLDS.—The table to apply for purposes of subsection (c) is as follows:

"If taxable income is	The tax is:
Not over \$1,800	11% of taxable income.
Over \$1,800 but not over \$16,800.....	\$198, plus 15% of the excess over \$1,800.
Over \$16,800 but not over \$27,000.....	\$2,448, plus 28% of the excess over \$16,800.
Over \$27,000 but not over \$54,000.....	\$5,304, plus 35% of the excess over \$27,000.
Over \$54,000	\$14,754, plus 38.5% of the excess over \$54,000.

"(D) MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—The table to apply for purposes of subsection (d) is as follows:

"If taxable income is	The tax is:
Not over \$1,500	11% of taxable income.
Over \$1,500 but not over \$14,000.....	\$165, plus 15% of the excess over \$1,500.
Over \$14,000 but not over \$22,500.....	\$2,040, plus 28% of the excess over \$14,000.
Over \$22,500 but not over \$45,000.....	\$4,420, plus 35% of the excess over \$22,500.
Over \$45,000	\$12,295, plus 38.5% of the excess over \$45,000.

"(E) ESTATES AND TRUSTS.—The table to apply for purposes of subsection (e) is as follows:

"If taxable income is	The tax is:
Not over \$500	11% of taxable income.
Over \$500 but not over \$4,700.....	\$55, plus 15% of the excess over \$500.
Over \$4,700 but not over \$7,550.....	\$685, plus 28% of the excess over \$4,700.
Over \$7,550 but not over \$15,150.....	\$1,483, plus 35% of the excess over \$7,550.
Over \$15,150	\$4,143, plus 38.5% of the excess over \$15,150."

(b) **AMENDMENT OF SECTION 15.**—Subsection (d) of section 15 (relating to effect of changes in rates during a taxable year) is amended to read as follows:

"(d) SECTION NOT TO APPLY TO INFLATION ADJUSTMENTS.—This section shall not apply to any change in rates under subsection (f) of section 1 (relating to adjustments in tax tables so that inflation will not result in tax increases)."

SEC. 102. INCREASE IN STANDARD DEDUCTION.

(a) **GENERAL RULE.**—Section 63 (defining taxable income) is amended to read as follows:

"SEC. 63. TAXABLE INCOME DEFINED.

"(a) IN GENERAL.—Except as provided in subsection (b), for purposes of this subtitle, the term 'taxable income' means gross income minus the deductions allowed by this chapter (other than the standard deduction).

"(b) INDIVIDUALS WHO DO NOT ITEMIZE THEIR DEDUCTIONS.—In the case of an individual who does not elect to itemize his deductions for

the taxable year, for purposes of this subtitle, the term 'taxable income' means adjusted gross income, minus—

“(1) the standard deduction, and

“(2) the deduction for personal exemptions provided in section 151.

“(c) STANDARD DEDUCTION.—For purposes of this subtitle—

“(1) IN GENERAL.—Except as otherwise provided in this subsection, the term 'standard deduction' means the sum of—

“(A) the basic standard deduction, and

“(B) the additional standard deduction.

“(2) BASIC STANDARD DEDUCTION.—For purposes of paragraph (1), the basic standard deduction is—

“(A) \$5,000 in the case of—

“(i) a joint return, or

“(ii) a surviving spouse (as defined in section 2(a)),

“(B) \$4,400 in the case of a head of household (as defined in section 2(b)),

“(C) \$3,000 in the case of an individual who is not married and who is not a surviving spouse or head of household, or

“(D) \$2,500 in the case of a married individual filing a separate return.

“(3) ADDITIONAL STANDARD DEDUCTION FOR AGED AND BLIND.—For purposes of paragraph (1), the additional standard deduction is the sum of each additional amount to which the taxpayer is entitled under subsection (f).

“(4) ADJUSTMENTS FOR INFLATION.—In the case of any taxable year beginning in a calendar year after 1988, each dollar amount contained in paragraph (2) or (5)(A) or subsection (f) shall be increased by an amount equal to—

“(A) such dollar amount, multiplied by

“(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins.

“(5) LIMITATION ON STANDARD DEDUCTION IN THE CASE OF CERTAIN DEPENDENTS.—In the case of an individual with respect to whom a deduction under section 151 is allowable to another taxpayer for a taxable year beginning in the calendar year in which the individual's taxable year begins, the standard deduction applicable to such individual for such individual's taxable year shall not exceed the greater of—

“(A) \$500, or

“(B) such individual's earned income.

“(6) CERTAIN INDIVIDUALS, ETC., NOT ELIGIBLE FOR STANDARD DEDUCTION.—In the case of—

“(A) a married individual filing a separate return where either spouse itemizes deductions,

“(B) a nonresident alien individual,

“(C) a citizen of the United States entitled to the benefits of section 931 (relating to income from sources within possessions of the United States),

“(D) an individual making a return under section 443(a)(1) for a period of less than 12 months on account of a change in his annual accounting period, or

“(E) an estate or trust, common trust fund, or partnership,

the standard deduction shall be zero.

“(d) ITEMIZED DEDUCTIONS.—For purposes of this subtitle, the term ‘itemized deductions’ means the deductions allowable under this chapter other than—

“(1) the deductions allowable in arriving at adjusted gross income, and

“(2) the deduction for personal exemptions provided by section 151.

“(e) ELECTION TO ITEMIZE.—

“(1) IN GENERAL.—Unless an individual makes an election under this subsection for the taxable year, no itemized deduction shall be allowed for the taxable year. For purposes of this subtitle, the determination of whether a deduction is allowable under this chapter shall be made without regard to the preceding sentence.

“(2) TIME AND MANNER OF ELECTION.—Any election under this subsection shall be made on the taxpayer’s return, and the Secretary shall prescribe the manner of signifying such election on the return.

“(3) CHANGE OF ELECTION.—Under regulations prescribed by the Secretary, a change of election with respect to itemized deductions for any taxable year may be made after the filing of the return for such year. If the spouse of the taxpayer filed a separate return for any taxable year corresponding to the taxable year of the taxpayer, the change shall not be allowed unless, in accordance with such regulations—

“(A) the spouse makes a change of election with respect to itemized deductions, for the taxable year covered in such separate return, consistent with the change of treatment sought by the taxpayer, and

“(B) the taxpayer and his spouse consent in writing to the assessment (within such period as may be agreed on with the Secretary) of any deficiency, to the extent attributable to such change of election, even though at the time of the filing of such consent the assessment of such deficiency would otherwise be prevented by the operation of any law or rule of law.

This paragraph shall not apply if the tax liability of the taxpayer’s spouse for the taxable year corresponding to the taxable year of the taxpayer has been compromised under section 7122.

“(f) AGED OR BLIND ADDITIONAL AMOUNTS.—

“(1) ADDITIONAL AMOUNTS FOR THE AGED.—The taxpayer shall be entitled to an additional amount of \$600—

“(A) for himself if he has attained age 65 before the close of his taxable year, and

“(B) for the spouse of the taxpayer if the spouse has attained age 65 before the close of the taxable year and an additional exemption is allowable to the taxpayer for such spouse under section 151(b).

“(2) ADDITIONAL AMOUNT FOR BLIND.—The taxpayer shall be entitled to an additional amount of \$600—

“(A) for himself if he is blind at the close of the taxable year, and

“(B) for the spouse of the taxpayer if the spouse is blind as of the close of the taxable year and an additional exemption is allowable to the taxpayer for such spouse under section 151(b).

For purposes of subparagraph (B), if the spouse dies during the taxable year the determination of whether such spouse is blind shall be made as of the time of such death.

“(3) HIGHER AMOUNT FOR CERTAIN UNMARRIED INDIVIDUALS.—In the case of an individual who is not married and is not a surviving spouse, paragraphs (1) and (2) shall be applied by substituting ‘\$750’ for ‘\$600’.

“(4) BLINDNESS DEFINED.—For purposes of this subsection, an individual is blind only if his central visual acuity does not exceed 20/200 in the better eye with correcting lenses, or if his visual acuity is greater than 20/200 but is accompanied by a limitation in the fields of vision such that the widest diameter of the visual field subtends an angle no greater than 20 degrees.

“(g) MARITAL STATUS.—For purposes of this section, marital status shall be determined under section 7703.

“(h) TRANSITIONAL RULE FOR TAXABLE YEARS BEGINNING IN 1987.—In the case of any taxable year beginning in 1987, paragraph (2) of subsection (c) shall be applied—

“(1) by substituting ‘\$3,760’ for ‘\$5,000’,

“(2) by substituting ‘\$2,540’ for ‘\$4,400’,

“(3) by substituting ‘\$2,540’ for ‘\$3,000’, and

“(4) by substituting ‘\$1,880’ for ‘\$2,500’.

The preceding sentence shall not apply if the taxpayer is entitled to an additional amount determined under subsection (f) (relating to additional amount for aged and blind) for the taxable year.”

(b) TAX TABLES.—Section 3 (relating to tax tables for individuals) is amended by striking out subsection (a) and inserting in lieu thereof the following:

“(a) IMPOSITION OF TAX TABLE TAX.—

“(1) IN GENERAL.—In lieu of the tax imposed by section 1, there is hereby imposed for each taxable year on the taxable income of every individual—

“(A) who does not itemize his deductions for the taxable year, and

“(B) whose taxable income for such taxable year does not exceed the ceiling amount,

a tax determined under tables, applicable to such taxable year, which shall be prescribed by the Secretary and which shall be in such form as he determines appropriate. In the table so prescribed, the amounts of the tax shall be computed on the basis of the rates prescribed by section 1.

“(2) CEILING AMOUNT DEFINED.—For purposes of paragraph (1), the term ‘ceiling amount’ means, with respect to any taxpayer, the amount (not less than \$20,000) determined by the Secretary for the tax rate category in which such taxpayer falls.

“(3) AUTHORITY TO PRESCRIBE TABLES FOR TAXPAYERS WHO ITEMIZE DEDUCTIONS.—The Secretary may provide that this section shall apply also for any taxable year to individuals who itemize their deductions. Any tables prescribed under the preceding sentence shall be on the basis of taxable income.”

SEC. 103. INCREASE IN PERSONAL EXEMPTIONS.

(a) GENERAL RULE.—Subsection (f) of section 151 (defining exemption amount) is amended to read as follows:

“(f) EXEMPTION AMOUNT.—For purposes of this section—

“(1) IN GENERAL.—Except as provided in paragraph (2), the term ‘exemption amount’ means—

“(A) \$1,900 for taxable years beginning during 1987,

“(B) \$1,950 for taxable years beginning during 1988, and

“(C) \$2,000 for taxable years beginning after December 31, 1988.

“(2) EXEMPTION AMOUNT DISALLOWED IN THE CASE OF CERTAIN DEPENDENTS.—In the case of an individual with respect to whom a deduction under this section is allowable to another taxpayer for a taxable year beginning in the calendar year in which the individual's taxable year begins, the exemption amount applicable to such individual for such individual's taxable year shall be zero.

“(3) INFLATION ADJUSTMENT FOR YEARS AFTER 1989.—In the case of any taxable year beginning in a calendar year after 1989, the dollar amount contained in paragraph (1)(C) shall be increased by an amount equal to—

“(A) such dollar amount, multiplied by

“(B) the cost-of-living adjustment determined under section 1(f)(3), for the calendar year in which the taxable year begins, by substituting ‘calendar year 1988’ for ‘calendar year 1987’ in subparagraph (B) thereof.”

(b) REPEAL OF ADDITIONAL EXEMPTIONS FOR TAXPAYERS OVER AGE 65 OR BLIND.—Section 151 is amended by striking out subsections (c) and (d) and by redesignating subsections (e) and (f) as subsections (c) and (d), respectively.

SEC. 104. TECHNICAL AMENDMENTS.

(a) FILING REQUIREMENTS.—

(1) SECTION 6012.—

(A) Paragraph (1) of section 6012(a) (relating to persons required to make returns of income) is amended to read as follows:

“(1)(A) Every individual having for the taxable year gross income which equals or exceeds the exemption amount, except that a return shall not be required of an individual—

“(i) who is not married (determined by applying section 7703), is not a surviving spouse (as defined in section 2(a)), is not a head of a household (as defined in section 2(b)), and for the taxable year has gross income of less than the sum of the exemption amount plus the basic standard deduction applicable to such an individual,

“(ii) who is a head of a household (as so defined) and for the taxable year has gross income of less than the sum of the exemption amount plus the basic standard deduction applicable to such an individual,

“(iii) who is a surviving spouse (as so defined) and for the taxable year has gross income of less than the sum of the exemption amount plus the basic standard deduction applicable to such an individual, or

“(iv) who is entitled to make a joint return and whose gross income, when combined with the gross income of his spouse, is, for the taxable year, less than the sum of twice the exemption amount plus the basic standard deduction applicable to a joint return, but only if such individual and his spouse, at the close of the taxable year, had the same household as their home.

Clause (iv) shall not apply if for the taxable year such spouse makes a separate return or any other taxpayer is entitled to an exemption for such spouse under section 151(c).

“(B) The amount specified in clause (i), (ii), or (iii) of subparagraph (A) shall be increased by the amount of 1 additional standard deduction (within the meaning of section 63(c)(3)) in the case of an individual entitled to such deduction by reason of section 63(f)(1)(A) (relating to individuals age 65 or more), and the amount specified in clause (iv) of subparagraph (A) shall be increased by the amount of the additional standard deduction for each additional standard deduction to which the individual or his spouse is entitled by reason of section 63(f)(1).

“(C) The exception under subparagraph (A) shall not apply to any individual—

“(i) who is described in section 63(c)(5) and who has—

“(I) income (other than earned income) in excess of the amount in effect under section 63(c)(5)(A) (relating to limitation on standard deduction in the case of certain dependents), or

“(II) total gross income in excess of the standard deduction, or

“(ii) for whom the standard deduction is zero under section 63(c)(6).

“(D) For purposes of this subsection—

“(i) The terms ‘standard deduction’, ‘basic standard deduction’ and ‘additional standard deduction’ have the respective meanings given such terms by section 63(c).

“(ii) The term ‘exemption amount’ has the meaning given such term by section 151(d). In the case of an individual described in section 151(d)(2), the exemption amount shall be zero.”

(B) Paragraph (9) of section 6012(a) is amended by striking out “\$2,700 or more” and inserting in lieu thereof “not less than the sum of the exemption amount plus the basic standard deduction under section 63(c)(2)(D)”.

(2) SECTION 6013.—Subparagraph (A) of section 6013(b)(3) (relating to when return deemed filed) is amended—

(A) by striking out “(twice the exemption amount in case such spouse was 65 or over)” each place it appears,

(B) by striking out “section 151(f)” and inserting in lieu thereof “section 151(d)”, and

(C) by adding at the end thereof the following new sentence: “For purposes of clauses (ii) and (iii), if the spouse whose gross income is being compared to the exemption amount is 65 or over, such clauses shall be applied by substituting ‘the sum of the exemption amount and the additional standard deduction under section 63(c)(2) by reason of section 63(f)(1)(A)’ for ‘the exemption amount’.”

(b) OTHER AMENDMENTS.—

(1) SECTION 21, ETC.—

(A) Sections 21(b)(1)(A), 21(e)(6)(A), and 129(c)(1) are each amended by striking out “section 151(e)” and inserting in lieu thereof “section 151(c)”.

(B) Sections 21(e)(6)(B), 32(c)(1)(A)(i), 129(c)(2), and 152(e)(1)(A) are each amended by striking out “section 151(e)(3)” and inserting in lieu thereof “section 151(c)(3)”.

(2) SECTION 108.—Subparagraph (B) of section 108(b)(3) is amended by striking out “50 cents” and inserting in lieu thereof “33 $\frac{1}{3}$ cents”.

(3) SECTION 152, ETC.—Sections 152(d)(2) and 2032A(c)(7)(D) are each amended by striking out “section 151(e)(4)” and inserting in lieu thereof “section 151(c)(4)”.

(4) SECTION 172.—Subsection (d) of section 172 (relating to modifications) is amended by striking out paragraph (7).

(5) SECTION 402.—Subparagraph (B) of section 402(e)(1), as amended by section 1222(b), is amended by striking out “the zero bracket amount applicable to such individual for the taxable year plus”.

(6) SECTION 441.—Clause (iii) of section 441(f)(2)(B) (relating to change in accounting period) is amended by striking out “and by adding the zero bracket amount,”.

(7) SECTION 443.—

(A) Paragraph (1) of section 443(b) (relating to computation of tax on change of annual accounting period) is amended by striking out “, and adding the zero bracket amount”.

(B) Clause (ii) of section 443(b)(2)(A) (relating to computation based on 12-month period) is amended to read as follows:

“(ii) the tax computed on the modified taxable income for the short period.”

(8) SECTION 541.—Section 541 is amended by striking out “50 percent” and inserting in lieu thereof “28 percent (38.5 percent in the case of taxable years beginning in 1987)”.

(9) SECTION 613A.—Paragraph (1) of section 613A(d) (relating to limitation on percentage depletion based on taxable income) is amended by striking out “(reduced in the case of an individual by the zero bracket amount)”.

(10) SECTION 667.—Paragraph (2) of section 667(b) (relating to tax on amount deemed distributed by trust in preceding years) is amended to read as follows:

“(2) TREATMENT OF LOSS YEARS.—For purposes of paragraph (1), the taxable income of the beneficiary for any taxable year shall be deemed to be not less than zero.”

(11) SECTION 861.—Subsection (b) of section 861 (relating to taxable income from sources within the United States) is amended by striking out “the zero bracket amount” and inserting in lieu thereof “the standard deduction”.

(12) SECTION 862.—Subsection (b) of section 862 (relating to taxable income from sources without the United States) is amended by striking out “the zero bracket amount” and inserting in lieu thereof “the standard deduction”.

(13) SECTION 904.—Subsection (a) of section 904 (relating to limitation on foreign tax credit) is amended by striking out the last sentence.

(14) SECTION 1398.—Subsection (c) of section 1398 (relating to computation and payment of tax; zero bracket amount) is amended—

(A) by striking out “ZERO BRACKET AMOUNT” in the subsection heading and inserting in lieu thereof “BASIC STANDARD DEDUCTION”, and

(B) by striking out paragraph (3) and inserting in lieu thereof the following:

“(3) **BASIC STANDARD DEDUCTION.**—In the case of an estate which does not itemize deductions, the basic standard deduction for the estate for the taxable year shall be the same as for a married individual filing a separate return for such year.”

(15) **SECTION 3402.**—

(A) Paragraph (1) of section 3402(f) (relating to withholding exemptions) is amended by striking out subparagraphs (B) and (C) and by redesignating subparagraphs (D), (E), (F), and (G) as subparagraphs (B), (C), (D), and (E), respectively.

(B) Subparagraph (A) of section 3402(f)(1) is amended by inserting “unless he is an individual described in section 151(d)(2)” after “himself”.

(C) Subparagraph (B) of section 3402(f)(1), as redesignated by subparagraph (A), is amended by striking out “subparagraph (A), (B), (C), or (F)” and inserting in lieu thereof “subparagraph (A) or (D)”.

(D) Subparagraph (C) of section 3402(f)(1), as redesignated by subparagraph (A), is amended by striking out “section 151(e)” and inserting in lieu thereof “section 151(c)”.

(E) Subparagraph (E) of section 3402(f)(1), as redesignated by subparagraph (A), is amended by striking out “zero bracket” and inserting in lieu thereof “standard deduction”.

(F) The last sentence of paragraph (1) of section 3402(f) is amended—

(i) by striking out “subparagraph (G)” and inserting in lieu thereof “subparagraph (E)”, and

(ii) by striking out “zero bracket” and inserting in lieu thereof “standard deduction”.

(G) Paragraph (3) of section 3402(m) is amended by inserting “(including the additional standard deduction under section 63(c)(3) for the aged and blind)” after “deductions”.

(16) **SECTION 6014.**—

(A) Subsection (a) of section 6014 (relating to income tax return—tax not computed by taxpayer) is amended by striking out “who does not have an unused zero bracket amount (determined under section 63(e))” and inserting in lieu thereof “who is not described in section 6012(a)(1)(C)(i)”.

(B) Paragraph (4) of section 6014(b) is amended to read as follows:

“(4) to cases where the taxpayer itemizes his deductions or where the taxpayer claims a reduced standard deduction by reason of section 63(c)(5).”

(17) **SECTION 6212.**—Subparagraph (A) of section 6212(c)(2) (relating to cross references) is amended to read as follows:

“(A) Deficiency attributable to change of treatment with respect to itemized deductions, see section 63(e)(3).”

(18) **SECTION 6504.**—Paragraph (2) of section 6504 (relating to cross references) is amended to read as follows:

“(2) Change of treatment with respect to itemized deductions where taxpayer and his spouse make separate returns, see section 63(e)(3).”

Subtitle B—Provisions Related to Tax Credits

SEC. 111. INCREASE IN EARNED INCOME CREDIT.

(a) **INCREASE IN AMOUNT OF CREDIT.**—Subsection (a) of section 32 (relating to earned income credit) is amended—

- (1) by striking out “11 percent” and inserting in lieu thereof “14 percent”, and
- (2) by striking out “\$5,000” and inserting in lieu thereof “\$5,714”.

(b) **INCREASE IN INCOME LEVEL AT WHICH PHASEOUT BEGINS.**—Subsection (b) of section 32 is amended to read as follows:

“(b) **LIMITATION.**—The amount of the credit allowable to a taxpayer under subsection (a) for any taxable year shall not exceed the excess (if any) of—

- “(1) the maximum credit allowable under subsection (a) to any taxpayer, over
- “(2) 10 percent of so much of the adjusted gross income (or, if greater, the earned income) of the taxpayer for the taxable year as exceeds \$9,000.

In the case of any taxable year beginning in 1987, paragraph (2) shall be applied by substituting ‘\$6,500’ for ‘\$9,000’.”

(c) **INFLATION ADJUSTMENTS.**—Section 32 is amended by adding at the end thereof the following new subsection:

“(i) **INFLATION ADJUSTMENTS.**—

“(1) **IN GENERAL.**—In the case of any taxable year beginning after the applicable calendar year, each dollar amount referred to in paragraph (2)(B) shall be increased by an amount equal to—

- “(A) such dollar amount, multiplied by
- “(B) the cost-of-living adjustment determined under section 1(f)(3), for the calendar year in which the taxable year begins, by substituting ‘calendar year 1984’ for ‘calendar year 1987’ in subparagraph (B) thereof.

“(2) **DEFINITIONS, ETC.**—For purposes of paragraph (1)—

- “(A) **APPLICABLE CALENDAR YEAR.**—The term ‘applicable calendar year’ means—
 - “(i) 1986 in the case of the dollar amounts referred to in clause (i) or (ii) of subparagraph (B), and
 - “(ii) 1987 in the case of the dollar amount referred to in clause (iii) of subparagraph (B).
- “(B) **DOLLAR AMOUNTS.**—The dollar amounts referred to in this subparagraph are—

- “(i) the \$5,714 amount contained in subsection (a),
- “(ii) the \$6,500 amount contained in the last sentence of subsection (b), and
- “(iii) the \$9,000 amount contained in subsection (b)(2).

“(3) **ROUNDING.**—If any increase determined under paragraph (1) is not a multiple of \$10, such increase shall be rounded to the nearest multiple of \$10 (or, if such increase is a multiple of \$5, such increase shall be increased to the next higher multiple of \$10).”

(d) **CONFORMING AMENDMENTS.**—

(1) Paragraph (2) of section 32(f) (relating to amount of credit to be determined under tables) is amended by striking out subparagraphs (A) and (B) and inserting in lieu thereof the following:

“(A) for earned income between \$0 and the amount of earned income at which the credit is phased out under subsection (b), and

“(B) for adjusted gross income between the dollar amount at which the phaseout begins under subsection (b) and the amount of adjusted gross income at which the credit is phased out under subsection (b).”

(2) Subparagraph (B) of section 3507(c)(2) (relating to earned income advance amount) is amended by striking out clauses (i) and (ii) and inserting in lieu thereof the following:

“(i) of not more than 14 percent of earned income not in excess of the amount of earned income taken into account under section 32(a), which

“(ii) phases out between the amount of earned income at which the phaseout begins under subsection (b) of section 32 and the amount of earned income at which the credit under section 32 is phased out under such subsection, or”.

(3) Subparagraph (C) of section 3507(c)(2) is amended by striking out clauses (i) and (ii) and inserting in lieu thereof the following:

“(i) of not more than 14 percent of earned income not in excess of $\frac{1}{2}$ of the amount of earned income taken into account under section 32(a), which

“(ii) phases out between amounts of earned income which are $\frac{1}{2}$ of the amounts of earned income described in subparagraph (B)(ii).”

(e) **EMPLOYEE NOTIFICATION.**—The Secretary of the Treasury is directed to require, under regulations, employers to notify any employee who has not had any tax withheld from wages (other than an employee whose wages are exempt from withholding pursuant to section 3402(n) of the Internal Revenue Code of 1986) that such employee may be eligible for a refund because of the earned income credit.

SEC. 112. REPEAL OF CREDIT FOR CONTRIBUTIONS TO CANDIDATES FOR PUBLIC OFFICE.

(a) **GENERAL RULE.**—Section 24 (relating to contributions to candidates for public office) is hereby repealed.

(b) **TECHNICAL AMENDMENTS.**—

(1) Subsection (g) of section 527 (relating to treatment of newsletter funds) is amended—

(A) by striking out “section 24(c)(2)” in paragraph (1) and inserting in lieu thereof “paragraph (3)”, and

(B) by adding at the end thereof the following new paragraph:

“(3) **CANDIDATE.**—For purposes of paragraph (1), the term ‘candidate’ means, with respect to any Federal, State, or local elective public office, an individual who—

“(A) publicly announces that he is a candidate for nomination or election to such office, and

“(B) meets the qualifications prescribed by law to hold such office.”

(2) Subsection (a) of section 642 (relating to credits against tax for estates and trusts) is amended to read as follows:

“(a) **FOREIGN TAX CREDIT ALLOWED.**—An estate or trust shall be allowed the credit against tax for taxes imposed by foreign countries

and possessions of the United States, to the extent allowed by section 901, only in respect of so much of the taxes described in such section as is not properly allocable under such section to the beneficiaries."

(3) Paragraph (3) of section 901(i) (relating to cross references) is amended by striking out "section 642(a)(1)" and inserting in lieu thereof "section 642(a)".

(4) Paragraph (6) of section 7871(a) (relating to Indian tribal governments treated as States for certain purposes) is amended by striking out subparagraph (A) and by redesignating subparagraphs (B), (C), (D), (E), and (F) as subparagraphs (A), (B), (C), (D), and (E), respectively.

(5) The table of sections for subpart A of part IV of subchapter A of chapter 1 is amended by striking out the item relating to section 24.

Subtitle C—Provisions Related to Exclusions

SEC. 121. TAXATION OF UNEMPLOYMENT COMPENSATION.

Section 85 (relating to unemployment compensation) is amended to read as follows:

"SEC. 85. UNEMPLOYMENT COMPENSATION.

"(a) GENERAL RULE.—In the case of an individual, gross income includes unemployment compensation.

"(b) UNEMPLOYMENT COMPENSATION DEFINED.—For purposes of this section, the term 'unemployment compensation' means any amount received under a law of the United States or of a State which is in the nature of unemployment compensation."

SEC. 122. PRIZES AND AWARDS.

(a) EXCLUSION FROM GROSS INCOME.—

(1) IN GENERAL.—Section 74 (relating to prizes and awards) is amended—

(A) by striking out "Except as provided in subsection (b) and" in subsection (a) and inserting in lieu thereof "Except as otherwise provided in this section or",

(B) by striking out "EXCEPTION" in the heading for subsection (b) and inserting in lieu thereof "EXCEPTION FOR CERTAIN PRIZES AND AWARDS TRANSFERRED TO CHARITIES",

(C) by striking out "and" at the end of subsection (b)(1), by striking out the period at the end of subsection (b)(2) and inserting in lieu thereof "; and", and by adding after subsection (b)(2) the following new paragraph:

"(3) the prize or award is transferred by the payor to a governmental unit or organization described in paragraph (1) or (2) of section 170(c) pursuant to a designation made by the recipient.", and

(D) by adding at the end thereof the following new subsection:

"(c) EXCEPTION FOR CERTAIN EMPLOYEE ACHIEVEMENT AWARDS.—

"(1) IN GENERAL.—Gross income shall not include the value of an employee achievement award (as defined in section 274(j)) received by the taxpayer if the cost to the employer of the employee achievement award does not exceed the amount

allowable as a deduction to the employer for the cost of the employee achievement award.

“(2) EXCESS DEDUCTION AWARD.—If the cost to the employer of the employee achievement award received by the taxpayer exceeds the amount allowable as a deduction to the employer, then gross income includes the greater of—

“(A) an amount equal to the portion of the cost to the employer of the award that is not allowable as a deduction to the employer (but not in excess of the value of the award), or

“(B) the amount by which the value of the award exceeds the amount allowable as a deduction to the employer. The remaining portion of the value of such award shall not be included in the gross income of the recipient.

“(3) TREATMENT OF TAX-EXEMPT EMPLOYERS.—In the case of an employer exempt from taxation under this subtitle, any reference in this subsection to the amount allowable as a deduction to the employer shall be treated as a reference to the amount which would be allowable as a deduction to the employer if the employer were not exempt from taxation under this subtitle.

“(4) CROSS REFERENCE.—

“For provisions excluding certain de minimis fringes from gross income, see section 132(e).”

(2) CONFORMING AMENDMENTS.—

(A) Clause (i) of section 4941(d)(2)(G) is amended by striking out “section 74(b)” and inserting in lieu thereof “section 74(b) (without regard to paragraph (3) thereof)”.

(B) Paragraph (2) of section 4945(g) is amended by striking out “section 74(b)” and inserting in lieu thereof “section 74(b) (without regard to paragraph (3) thereof)”.

(b) AMOUNTS TRANSFERRED BY EMPLOYER NOT EXCLUDABLE AS GIFTS.—Section 102 (relating to gifts and inheritances) is amended by adding at the end thereof the following new subsection:

“(c) EMPLOYEE GIFTS.—

“(1) IN GENERAL.—Subsection (a) shall not exclude from gross income any amount transferred by or for an employer to, or for the benefit of, an employee.

“(2) CROSS REFERENCES.—

“For provisions excluding certain employee achievement awards from gross income, see section 74(c).

“For provisions excluding certain de minimis fringes from gross income, see section 132(e).”

(c) GIFTS.—Section 274(b) (relating to gifts) is amended—

(1) by adding “or” at the end of subparagraph (A) of paragraph (1),

(2) by striking out “or” at the end of subparagraph (B) of paragraph (1), and inserting in lieu thereof a period,

(3) by striking out subparagraph (C) of paragraph (1), and

(4) by striking out paragraph (3).

(d) DEDUCTION FOR COST OF EMPLOYEE ACHIEVEMENT AWARDS.—Section 274 (relating to certain entertainment, etc., expenses) is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:

“(j) EMPLOYEE ACHIEVEMENT AWARDS.—

“(1) GENERAL RULE.—No deduction shall be allowed under section 162 or section 212 for the cost of an employee achieve-

ment award except to the extent that such cost does not exceed the deduction limitations of paragraph (2).

“(2) DEDUCTION LIMITATIONS.—The deduction for the cost of an employee achievement award made by an employer to an employee—

“(A) which is not a qualified plan award, when added to the cost to the employer for all other employee achievement awards made to such employee during the taxable year which are not qualified plan awards, shall not exceed \$400, and

“(B) which is a qualified plan award, when added to the cost to the employer for all other employee achievement awards made to such employee during the taxable year (including employee achievement awards which are not qualified plan awards), shall not exceed \$1,600.

“(3) DEFINITIONS.—For purposes of this subsection—

“(A) EMPLOYEE ACHIEVEMENT AWARD.—The term ‘employee achievement award’ means an item of tangible personal property which is—

“(i) transferred by an employer to an employee for length of service achievement or safety achievement,

“(ii) awarded as part of a meaningful presentation, and

“(iii) awarded under conditions and circumstances that do not create a significant likelihood of the payment of disguised compensation.

“(B) QUALIFIED PLAN AWARD.—

“(i) IN GENERAL.—The term ‘qualified plan award’ means an employee achievement award awarded as part of an established written plan or program of the taxpayer which does not discriminate in favor of highly compensated employees (within the meaning of section 414(q)) as to eligibility or benefits.

“(ii) LIMITATION.—An employee achievement award shall not be treated as a qualified plan award for any taxable year if the average cost of all employee achievement awards which are provided by the employer during the year, and which would be qualified plan awards but for this subparagraph, exceeds \$400. For purposes of the preceding sentence, average cost shall be determined by including the entire cost of qualified plan awards, without taking into account employee achievement awards of nominal value.

“(4) SPECIAL RULES.—For purposes of this subsection—

“(A) PARTNERSHIPS.—In the case of an employee achievement award made by a partnership, the deduction limitations contained in paragraph (2) shall apply to the partnership as well as to each member thereof.

“(B) LENGTH OF SERVICE AWARDS.—An item shall not be treated as having been provided for length of service achievement if the item is received during the recipient’s 1st 5 years of employment or if the recipient received a length of service achievement award (other than an award excludable under section 132(e)(1)) during that year or any of the prior 4 years.

“(C) SAFETY ACHIEVEMENT AWARDS.—An item provided by an employer to an employee shall not be treated as having been provided for safety achievement if—

“(i) during the taxable year, employee achievement awards (other than awards excludable under section 132(e)(1)) for safety achievement have previously been awarded by the employer to more than 10 percent of the employees of the employer (excluding employees described in clause (ii)), or

“(ii) such item is awarded to a manager, administrator, clerical employee, or other professional employee.”.

(e) TREATMENT FOR PURPOSES OF EMPLOYMENT TAXES.—Each of the following provisions are amended by striking out “117 or” and inserting in lieu thereof “74(c), 117, or”:

- (1) Section 3121(a)(20).
- (2) Section 3231(e)(5).
- (3) Section 3306(b)(16).
- (4) Section 3401(a)(20).
- (5) Section 209(s) of the Social Security Act.

SEC. 123. SCHOLARSHIPS.

(a) IN GENERAL.—Section 117 (relating to scholarship and fellowship grants) is amended to read as follows:

“SEC. 117. QUALIFIED SCHOLARSHIPS.

“(a) GENERAL RULE.—Gross income does not include any amount received as a qualified scholarship by an individual who is a candidate for a degree at an educational organization described in section 170(b)(1)(A)(ii).

“(b) QUALIFIED SCHOLARSHIP.—For purposes of this section—

“(1) IN GENERAL.—The term ‘qualified scholarship’ means any amount received by an individual as a scholarship or fellowship grant to the extent the individual establishes that, in accordance with the conditions of the grant, such amount was used for qualified tuition and related expenses.

“(2) QUALIFIED TUITION AND RELATED EXPENSES.—For purposes of paragraph (1), the term ‘qualified tuition and related expenses’ means—

“(A) tuition and fees required for the enrollment or attendance of a student at an educational organization described in section 170(b)(1)(A)(ii), and

“(B) fees, books, supplies, and equipment required for courses of instruction at such an educational organization.

“(c) LIMITATION.—Subsections (a) and (d) shall not apply to that portion of any amount received which represents payment for teaching, research, or other services by the student required as a condition for receiving the qualified scholarship or qualified tuition reduction.

“(d) QUALIFIED TUITION REDUCTION.—

“(1) IN GENERAL.—Gross income shall not include any qualified tuition reduction.

“(2) QUALIFIED TUITION REDUCTION.—For purposes of this subsection, the term ‘qualified tuition reduction’ means the amount of any reduction in tuition provided to an employee of an organization described in section 170(b)(1)(A)(ii) for the edu-

cation (below the graduate level) at such organization (or another organization described in section 170(b)(1)(A)(ii) of—

“(A) such employee, or

“(B) any person treated as an employee (or whose use is treated as an employee use) under the rules of section 132(f).

“(3) REDUCTION MUST NOT DISCRIMINATE IN FAVOR OF HIGHLY COMPENSATED, ETC.—Paragraph (1) shall apply with respect to any qualified tuition reduction provided with respect to any officer, owner, or highly compensated employee only if such reduction is available on substantially the same terms to each member of a group of employees which is defined under a reasonable classification set up by the employer which does not discriminate in favor of officers, owners, or highly compensated employees (within the meaning of section 414(q)).”

(b) TECHNICAL AMENDMENTS.—

(1) Subsection (a) of section 74 is amended by striking out “(relating to scholarship and fellowship grants)” and inserting in lieu thereof “(relating to qualified scholarships)”.

(2) The second sentence of section 1441(b) (relating to income items) is amended to read as follows: “The items of income referred to in subsection (a) from which tax shall be deducted and withheld at the rate of 14 percent are amounts which are received by a nonresident alien individual who is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act and which are incident to a qualified scholarship to which section 117(a) applies, but only to the extent such amounts are includible in gross income.”

(3) Paragraph (6) of section 7871(a) (relating to Indian tribal governments treated as States for certain purposes), as amended by section 112, is amended by striking out subparagraph (B) and by redesignating subparagraphs (C), (D), and (E) as subparagraphs (B), (C), and (D), respectively.

(4) The table of sections for part III of subchapter B of chapter 1 is amended by striking out the item relating to section 117 and inserting in lieu thereof the following new item:

“Sec. 117. Qualified scholarships.”

Subtitle D—Provisions Related to Deductions

SEC. 131. REPEAL OF DEDUCTION FOR 2-EARNER MARRIED COUPLES.

(a) GENERAL RULE.—Section 221 (relating to deduction for 2-earner married couples) is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) Section 62 is amended by striking out paragraph (16).

(2) Subparagraph (A) of section 86(b)(2) is amended by striking out “sections 221,” and inserting in lieu thereof “sections”.

(3) The table of sections for part VII of subchapter B of chapter 1 is amended by striking out the item relating to section 221.

SEC. 132. 2-PERCENT FLOOR ON MISCELLANEOUS ITEMIZED DEDUCTIONS.

(a) GENERAL RULE.—Part I of subchapter B of chapter 1 (defining gross income, adjusted gross income, etc.) is amended by adding at the end thereof the following new section:

"SEC. 67. 2-PERCENT FLOOR ON MISCELLANEOUS ITEMIZED DEDUCTIONS.

"(a) GENERAL RULE.—In the case of an individual, the miscellaneous itemized deductions for any taxable year shall be allowed only to the extent that the aggregate of such deductions exceeds 2 percent of adjusted gross income.

"(b) MISCELLANEOUS ITEMIZED DEDUCTIONS.—For purposes of this section, the term 'miscellaneous itemized deductions' means the itemized deductions other than—

"(1) the deduction under section 163 (relating to interest),

"(2) the deduction under section 164 (relating to taxes),

"(3) the deduction under section 165(a) for losses described in subsection (c)(3) or (d) of section 165,

"(4) the deduction under section 170 (relating to charitable, etc., contributions and gifts),

"(5) the deduction under section 213 (relating to medical, dental, etc., expenses),

"(6) the deduction under section 217 (relating to moving expenses),

"(7) any deduction allowable for impairment-related work expenses,

"(8) the deduction under section 691(c) (relating to deduction for estate tax in case of income in respect of the decedent),

"(9) any deduction allowable in connection with personal property used in a short sale,

"(10) the deduction under section 1341 (relating to computation of tax where taxpayer restores substantial amount held under claim of right),

"(11) the deduction under section 72(b)(3) (relating to deduction where annuity payments cease before investment recovered),

"(12) the deduction under section 171 (relating to deduction for amortizable bond premium), and

"(13) the deduction under section 216 (relating to deductions in connection with cooperative housing corporations).

"(c) DISALLOWANCE OF INDIRECT DEDUCTION THROUGH PASS-THRU ENTITY.—The Secretary shall prescribe regulations which prohibit the indirect deduction through pass-thru entities of amounts which are not allowable as a deduction if paid or incurred directly by an individual and which contain such reporting requirements as may be necessary to carry out the purposes of this subsection. The preceding sentence shall not apply with respect to estates, trusts, cooperatives, and real estate investment trusts.

"(d) IMPAIRMENT-RELATED WORK EXPENSES.—For purposes of this section, the term 'impairment-related work expenses' means expenses—

"(1) of a handicapped individual (as defined in section 190(b)(3)) for attendant care services at the individual's place of employment and other expenses in connection with such place of employment which are necessary for such individual to be able to work, and

"(2) with respect to which a deduction is allowable under section 162 (determined without regard to this section).

"(e) DETERMINATION OF ADJUSTED GROSS INCOME IN CASE OF ESTATES AND TRUSTS.—For purposes of this section, the adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual, except that the deductions for osts

which are paid or incurred in connection with the administration of the estate or trust and would not have been incurred if the property were not held in such trust or estate shall be treated as allowable in arriving at adjusted gross income."

(b) TREATMENT OF TRADE AND BUSINESS DEDUCTIONS OF EMPLOYEES.—

(1) **IN GENERAL.**—Paragraph (2) of section 62 (defining adjusted gross income) is amended to read as follows:

"(2) CERTAIN TRADE AND BUSINESS DEDUCTIONS OF EMPLOYEES.—

"(A) REIMBURSED EXPENSES OF EMPLOYEES.—The deductions allowed by part VI (section 161 and following) which consist of expenses paid or incurred by the taxpayer, in connection with the performance by him of services as an employee, under a reimbursement or other expense allowance arrangement with his employer.

"(B) CERTAIN EXPENSES OF PERFORMING ARTISTS.—The deductions allowed by section 162 which consist of expenses paid or incurred by a qualified performing artist in connection with the performances by him of services in the performing arts as an employee."

(2) **DEFINITION OF QUALIFIED PERFORMING ARTIST.**—Section 62 is amended—

(A) by striking out "For purposes of this subtitle" and inserting in lieu thereof "(a) **GENERAL RULE.**—For purposes of this subtitle", and

(B) by adding at the end thereof the following new subsection:

"(b) QUALIFIED PERFORMING ARTIST.—

"(1) IN GENERAL.—For purposes of subsection (a)(2)(B), the term 'qualified performing artist' means, with respect to any taxable year, any individual if—

"(A) such individual performed services in the performing arts as an employee during the taxable year for at least 2 employers,

"(B) the aggregate amount allowable as a deduction under section 162 in connection with the performance of such services exceeds 10 percent of such individual's gross income attributable to the performance of such services, and

"(C) the adjusted gross income of such individual for the taxable year (determined without regard to subsection (a)(2)(B)) does not exceed \$16,000.

"(2) NOMINAL EMPLOYER NOT TAKEN INTO ACCOUNT.—An individual shall not be treated as performing services in the performing arts as an employee for any employer during any taxable year unless the amount received by such individual from such employer for the performance of such services during the taxable year equals or exceeds \$200.

"(3) SPECIAL RULES FOR MARRIED COUPLES.—

"(A) IN GENERAL.—Except in the case of a husband and wife who lived apart at all times during the taxable year, if the taxpayer is married at the close of the taxable year, subsection (a)(2)(B) shall apply only if the taxpayer and his spouse file a joint return for the taxable year.

"(B) APPLICATION OF PARAGRAPH (1).—In the case of a joint return—

“(i) paragraph (1) (other than subparagraph (C) thereof) shall be applied separately with respect to each spouse, but

“(ii) paragraph (1)(C) shall be applied with respect to their combined adjusted gross income.

“(C) DETERMINATION OF MARITAL STATUS.—For purposes of this subsection, marital status shall be determined under section 7703(a).

“(D) JOINT RETURN.—For purposes of this subsection, the term ‘joint return’ means the joint return of a husband and wife made under section 6013.”

(c) MOVING EXPENSE DEDUCTION NOT ALLOWABLE IN COMPUTING ADJUSTED GROSS INCOME.—Subsection (a) of section 62 (as amended by subsection (b)) is amended by striking out paragraph (8).

(d) CLERICAL AMENDMENT.—The table of sections for part I of subchapter B of chapter 1 is amended by adding at the end thereof the following new item:

“Sec. 67. 2-percent floor on miscellaneous itemized deductions.”

SEC. 133. MEDICAL EXPENSE DEDUCTION LIMITATION INCREASED.

Subsection (a) of section 213 (relating to deduction for medical, dental, etc., expenses) is amended by striking out “5 percent” and inserting in lieu thereof “7.5 percent”.

SEC. 134. REPEAL OF DEDUCTION FOR STATE AND LOCAL SALES TAXES.

(a) GENERAL RULE.—Subsection (a) of section 164 (relating to deduction for taxes) is amended—

(1) by striking out paragraph (4) and by redesignating paragraph (5) as paragraph (4), and

(2) by adding at the end thereof the following new sentence: “Notwithstanding the preceding sentence, any tax (not described in the first sentence of this subsection) which is paid or accrued by the taxpayer in connection with an acquisition or disposition of property shall be treated as part of the cost of the acquired property or, in the case of a disposition, as a reduction in the amount realized on the disposition.”

(b) CONFORMING AMENDMENTS.—Subsection (b) of section 164 is amended—

(1) by striking out paragraphs (2) and (5), and

(2) by redesignating paragraphs (3) and (4) as paragraphs (2) and (3), respectively.

SEC. 135. REPEAL OF DEDUCTION FOR ADOPTION EXPENSES.

(a) GENERAL RULE.—Section 222 (relating to deduction for adoption expenses) is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) Section 223 is redesignated as section 220.

(2) The table of sections for part VII of subchapter B of chapter 1 is amended by striking out the items relating to sections 222 and 223 and inserting in lieu thereof the following:

“Sec. 220. Cross references.”

Subtitle E—Miscellaneous Provisions

SEC. 141. REPEAL OF INCOME AVERAGING.

(a) **GENERAL RULE.**—Part I of subchapter Q of chapter 1 (relating to income averaging) is hereby repealed.

(b) **TECHNICAL AMENDMENTS.**—

(1) Subsection (b) of section 3 (relating to section inapplicable to certain individuals) is amended by striking out paragraph (1) and by redesignating paragraphs (2) and (3) as paragraphs (1) and (2), respectively.

(2) Subsection (b) of section 5 (relating to cross references relating to tax on individuals) is amended by striking out paragraph (2) and by redesignating paragraph (3) as paragraph (2).

(3) Subparagraph (B) of section 6511(d)(2) (relating to special rules applicable to income taxes) is amended to read as follows:

“(B) **APPLICABLE RULES.**—

“(i) **IN GENERAL.**—If the allowance of a credit or refund of an overpayment of tax attributable to a net operating loss carryback or a capital loss carryback is otherwise prevented by the operation of any law or rule of law other than section 7122 (relating to compromises), such credit or refund may be allowed or made, if claim therefor is filed within the period provided in subparagraph (A) of this paragraph.

“(ii) **TENTATIVE CARRYBACK ADJUSTMENTS.**—If the allowance of an application, credit, or refund of a decrease in tax determined under section 6411(b) is otherwise prevented by the operation of any law or rule of law other than section 7122, such application, credit, or refund may be allowed or made if application for a tentative carryback adjustment is made within the period provided in section 6411(a).

“(iii) **DETERMINATIONS BY COURTS TO BE CONCLUSIVE.**—In the case of any such claim for credit or refund or any such application for a tentative carryback adjustment, the determination by any court, including the Tax Court, in any proceeding in which the decision of the court has become final, shall be conclusive except with respect to—

“(I) the net operating loss deduction and the effect of such deduction, and

“(II) the determination of a short-term capital loss and the effect of such short-term capital loss, to the extent that such deduction or short-term capital loss is affected by a carryback which was not an issue in such proceeding.”

(c) **CLERICAL AMENDMENT.**—The table of parts for subchapter Q of chapter 1 is amended by striking out the item relating to part I.

SEC. 142. LIMITATIONS ON DEDUCTIONS FOR MEALS, TRAVEL, AND ENTERTAINMENT.

(a) **BUSINESS MEALS.**—

(1) **IN GENERAL.**—Section 274 (relating to disallowance of certain entertainment, etc. expenses), as amended by section 122(d), is amended by redesignating subsection (k) as subsection

(o) and by inserting after subsection (j) the following new subsection:

“(k) BUSINESS MEALS.—

“(1) IN GENERAL.—No deduction shall be allowed under this chapter for the expense of any food or beverages unless—

“(A) such expense is not lavish or extravagant under the circumstances, and

“(B) the taxpayer (or an employee of the taxpayer) is present at the furnishing of such food or beverages.

“(2) EXCEPTIONS.—Paragraph (1) shall not apply to any expense if subsection (a) does not apply to such expense by reason of paragraph (2), (3), (4), (7), (8), or (9) of subsection (e).”

(2) TECHNICAL AMENDMENTS.—

(A) Subsection (e) of section 274 (relating to specific exceptions to application of subsection (a)) is amended by striking out paragraph (1) and by redesignating paragraphs (2) through (10) as paragraphs (1) through (9), respectively.

(B) Paragraph (3) of section 274(e), as redesignated by subparagraph (A), is amended by striking out “paragraph (3)” and inserting in lieu thereof “paragraph (2)”.

(b) ADDITIONAL RESTRICTIONS ON EXPENSES FOR MEALS, TRAVEL, AND ENTERTAINMENT.—Section 274 is amended by inserting after the subsection added by subsection (a) the following new subsections:

“(1) ADDITIONAL LIMITATIONS ON ENTERTAINMENT TICKETS.—

“(1) ENTERTAINMENT TICKETS.—

“(A) IN GENERAL.—In determining the amount allowable as a deduction under this chapter for any ticket for any activity or facility described in subsection (d)(2), the amount taken into account shall not exceed the face value of such ticket.

“(B) EXCEPTION FOR CERTAIN CHARITABLE SPORTS EVENTS.—Subparagraph (A) shall not apply to any ticket for any sports event—

“(i) which is organized for the primary purpose of benefiting an organization which is described in section 501(c)(3) and exempt from tax under section 501(a),

“(ii) all of the net proceeds of which are contributed to such organization, and

“(iii) which utilizes volunteers for substantially all of the work performed in carrying out such event.

“(2) SKYBOXES, ETC.—

“(A) IN GENERAL.—In the case of a skybox or other private luxury box leased for more than 1 event, the amount allowable as a deduction under this chapter with respect to such events shall not exceed the sum of the face value of non-luxury box seat tickets for the seats in such box covered by the lease. For purposes of the preceding sentence, 2 or more related leases shall be treated as 1 lease.

“(B) PHASEIN.—In the case of—

“(i) a taxable year beginning in 1987, the amount disallowed under subparagraph (A) shall be $\frac{1}{3}$ of the amount which would be disallowed without regard to this subparagraph, and

“(ii) in the case of a taxable year beginning in 1988, the amount disallowed under subparagraph (A) shall be $\frac{2}{3}$ of the amount which would have been disallowed without regard to this subparagraph.”

“(m) **ADDITIONAL LIMITATIONS ON TRAVEL EXPENSES.**—

“(1) **LUXURY WATER TRANSPORTATION.**—

“(A) **IN GENERAL.**—No deduction shall be allowed under this chapter for expenses incurred for transportation by water to the extent such expenses exceed twice the aggregate per diem amounts for days of such transportation. For purposes of the preceding sentence, the term ‘per diem amounts’ means the highest amount generally allowable with respect to a day to employees of the executive branch of the Federal Government for per diem while away from home but serving in the United States.

“(B) **EXCEPTIONS.**—Subparagraph (A) shall not apply to—

“(i) any expense allocable to a convention, seminar, or other meeting which is held on any cruise ship, and

“(ii) any expense to which subsection (a) does not apply by reason of paragraph (2), (3), (4), (7), (8), or (9) of subsection (e).

“(2) **TRAVEL AS FORM OF EDUCATION.**—No deduction shall be allowed under this chapter for expenses for travel as a form of education.

“(n) **ONLY 80 PERCENT OF MEAL AND ENTERTAINMENT EXPENSES ALLOWED AS DEDUCTION.**—

“(1) **IN GENERAL.**—The amount allowable as a deduction under this chapter for—

“(A) any expense for food or beverages, and

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

shall not exceed 80 percent of the amount of such expense or item which would (but for this paragraph) be allowable as a deduction under this chapter.

“(2) **EXCEPTIONS.**—Paragraph (1) shall not apply to any expense if—

“(A) subsection (a) does not apply to such expense by reason of paragraph (2), (3), (4), (7), (8), or (9) of subsection (e),

“(B) in the case of an expense for food or beverages, such expense is excludable from the gross income of the recipient under section 132 by reason of subsection (e) thereof (relating to de minimis fringes),

“(C) such expense is covered by a package involving a ticket described in subsection (1)(1)(B), or

“(D) in the case of an expense for food or beverages before January 1, 1989, such expense is an integral part of a qualified meeting.

“(3) **QUALIFIED MEETING.**—For purposes of paragraph (2)(D), the term ‘qualified meeting’ means any convention, seminar, annual meeting, or similar business program with respect to which—

“(A) an expense for food or beverages is not separately stated,

“(B) more than 50 percent of the participants are away from home,

“(C) at least 40 individuals attend, and

“(D) such food and beverages are part of a program which includes a speaker.”

(c) **NO DEDUCTION ALLOWED FOR SEMINARS, ETC., FOR SECTION 212 PURPOSES.**—

(1) **IN GENERAL.**—Subsection (h) of section 274 (relating to attendance at conventions, etc.) is amended by adding at the end thereof the following new paragraph:

“(7) **SEMINARS, ETC. FOR SECTION 212 PURPOSES.**—No deduction shall be allowed under section 212 for expenses allocable to a convention, seminar, or similar meeting.”

(2) **TECHNICAL AMENDMENTS.**—Paragraphs (1), (2), (4), and (5) of section 274(h) are each amended—

(A) by striking out “or 212” each place it appears, and

(B) by striking out “or to an activity described in section 212 and” each place it appears.

(d) **DENIAL OF CHARITABLE CONTRIBUTION FOR CERTAIN TRAVEL EXPENSES.**—Section 170 (relating to charitable, etc., contributions and gifts) is amended by redesignating subsections (k) and (l) as subsections (l) and (m), respectively, and by inserting after subsection (j) the following new subsection:

“(k) **DENIAL OF DEDUCTION FOR CERTAIN TRAVEL EXPENSES.**—No deduction shall be allowed under this section for traveling expenses (including amounts expended for meals and lodging) while away from home, whether paid directly or by reimbursement, unless there is no significant element of personal pleasure, recreation, or vacation in such travel.”

SEC. 143. CHANGES IN TREATMENT OF HOBBY LOSS, ETC.

(a) **HOBBY LOSS.**—Subsection (d) of section 183 (relating to presumption) is amended—

(1) by striking out “2 or more of the taxable years in the period of 5 consecutive taxable years” and inserting in lieu thereof “3 or more of the taxable years in the period of 5 consecutive taxable years”, and

(2) by striking out the last sentence and inserting in lieu thereof the following: “In the case of an activity which consists in major part of the breeding, training, showing, or racing of horses, the preceding sentence shall be applied by substituting ‘2’ for ‘3’ and ‘7’ for ‘5’.”

(b) **TREATMENT OF RENTAL TO EMPLOYER UNDER SECTION 280A.**—Subsection (c) of section 280A (relating to exceptions for certain business or rental use; limitation on deductions for such use) is amended by adding at the end thereof the following new paragraph:

“(6) **TREATMENT OF RENTAL TO EMPLOYER.**—Paragraphs (1) and (3) shall not apply to any item which is attributable to the rental of the dwelling unit (or any portion thereof) by the taxpayer to his employer during any period in which the taxpayer uses the dwelling unit (or portion) in performing services as an employee of the employer.”

(c) **REVISION OF LIMITATION ON DEDUCTION FOR BUSINESS USE OF HOME.**—Paragraph (5) of section 280A(c) (relating to exceptions for certain business or rental use; limitation on deductions for such use) is amended by striking out subparagraph (B) and inserting in lieu thereof the following:

“(B) the sum of—

“(i) the deductions allocable to such use which are allowable under this chapter for the taxable year

whether or not such unit (or portion thereof) was so used, and

“(ii) the deductions allocable to the trade or business in which such use occurs (but which are not allocable to such use) for such taxable year.

Any amount not allowable as a deduction under this chapter by reason of the preceding sentence shall be taken into account as a deduction (allocable to such use) under this chapter for the succeeding taxable year.”

SEC. 144. DEDUCTION FOR MORTGAGE INTEREST AND REAL PROPERTY TAXES ALLOWABLE WHERE PARSONAGE ALLOWANCE OR MILITARY HOUSING ALLOWANCE RECEIVED.

Section 265 (relating to expenses and interest relating to tax-exempt income) is amended by adding at the end thereof the following new paragraph:

“(6) SECTION NOT TO APPLY WITH RESPECT TO PARSONAGE AND MILITARY HOUSING ALLOWANCES.—No deduction shall be denied under this section for interest on a mortgage on, or real property taxes on, the home of the taxpayer by reason of the receipt of an amount as—

“(A) a military housing allowance, or

“(B) a parsonage allowance excludable from gross income under section 107.”

Subtitle F—Effective Dates

SEC. 151. EFFECTIVE DATES.

(a) **GENERAL RULE.**—Except as otherwise provided in this section, the amendments made by this title shall apply to taxable years beginning after December 31, 1986.

(b) **UNEMPLOYMENT COMPENSATION.**—The amendment made by section 121 shall apply to amounts received after December 31, 1986, in taxable years ending after such date.

(c) **PRIZES AND AWARDS.**—The amendments made by section 122 shall apply to prizes and awards granted after December 31, 1986.

(d) **SCHOLARSHIPS.**—The amendments made by section 123 shall apply to taxable years beginning after December 31, 1986, but only in the case of scholarships and fellowships granted after August 16, 1986.

(e) **PARSONAGE AND MILITARY HOUSING ALLOWANCES.**—The amendment made by section 144 shall apply to taxable years beginning before, on, or after, December 31, 1986.

TITLE II—PROVISIONS RELATING TO CAPITAL COST

Subtitle A—Depreciation Provisions

SEC. 201. MODIFICATION OF ACCELERATED COST RECOVERY SYSTEM.

(a) **GENERAL RULE.**—Section 168 (relating to accelerated cost recovery system) is amended to read as follows: