MINUTES OF THE MEETING
TAXATION COMMITTEE
MONTANA STATE SENATE

February 7, 1983

The twentieth meeting of the Taxation Committee was called to order by Chairman Pat M. Goodover at 8:30 a.m. in Room 415 of the Capitol Building.

ROLL CALL: All members were present.

CONSIDERATION OF SENATE BILL 97 (CONTINUED): The committee continued to hear testimony in opposition to SB 97.

Willa Hall, representing the Montana League of Women Voters, submitted written testimony attached as Exhibit A.

Gus Byrom, planning director of the Lewis and Clark County Planning Board, said the coal severance tax revenues constitute 10% of their budget. With federal cuts, their staff has been reduced from 12 to 5 and if there are further cuts, the staff will be reduced even more. They use these funds for planning economic growth and development and planning of capital facilities. They have prepared county road plans so the roads can tie into one another. The funds have been put to good use in Montana counties. His written statement is attached as Exhibit B.

Nancy Leifer, Development Bureau Chief of the Department of Commerce, submitted a written statement which is attached as Exhibit C.

Leo Berry, director of the Department of Natural Resources and Conservation, thought this bill was bad public policy. The Revenue Oversight Committee rejected SB 97 as a recommendation. There were some administrative problems at the time Mr. Berry took over as director of the department, but the program has been revamped and has received a clean bill of health from the legislature auditor. Mr. Berry felt the bill went beyond whether these were good or bad programs. We have moved into commercialism, he said. He cited figures on the number of grants and loans applied for and granted. He understood others to say that earmarking reduced flexibility. There is a good reason why these funds are earmarked and we should not disturb that. The distribution of the coal severance tax moneys is overseen by several committees; there is more oversight here than in any other program. He asked that the legislature not de-earmark those funds to put back into the general fund.

Don Reed, representing the Montana Environmental Information Center, submitted written testimony, attached as Exhibit D.

Senators Dorothy Eck and J.D. Lynch also wished to go on record as opposing SB 97.

Senator Mike Halligan also opposed the bill. He said he was contacted by Jobs Development Corporation regarding this bill. The Environmental Quality Council has monitored the program, and the necessary changes have been made.

Senator Elliott, in closing, asked that the committee review Willa Hall's (Montana League of Women Voters) testimony at an Environmental Quality Council meeting concerning the vital need for an "accountable legislative approach" to spending of the coal severance tax funds and not earmarking. The Montana League of Women Voters also supported a sunset review.

Senator Elliott said the earmarking process is like signing a blank check to the various programs and any legislative review is virtually lost.

Questions from the committee were called for.

Senator Mazurek asked Senator Elliott why, of all the earmarked accounts, they chose to eliminate the alternative energy research development and demonstration and county land planning accounts as to distribution of coal severance tax funds. Senator Elliott responded that there were other recommendations for other programs. The committee felt they should continue at the 50% level with no further earmarking. They felt the educational trust fund account helped all of Montana and so there was not as much a need to de-earmark those funds. That left county land planning and alternative energy research development and demonstration. They looked at the library assessment and soil conservation district accounts, but they were such new programs that they had no recommendations at this time for those accounts.

Senator Turnage asked Senator Elliott if they looked in depth into the individual grants and loans as to their successes and failures. Senator Elliott said that Mr. Berry had put the program into suspension when he was first appointed director of the department until he could establish new guidelines through the Environmental Quality Council. Senator Elliott said they were all quite aware that no one was happy about the programs that had been developed up to that time. They were generally aware of the successes and failures, he said, but not specifically aware of them. They used the date of July 1, 1985, because they didn't want to cut anyone off right away.

The hearing was closed on SB 97.

<u>CONSIDERATION OF HOUSE BILL 125:</u> Representative Stella Hansen, House District 96, sponsor of the bill, said this bill will allow a couple filing separate Montana individual income tax returns to deduct child and dependent care expenses. Most Montana couples file separately. The bill also requires that the child and dependent care deduction be divided equally between the spouses.

PROPONENTS

Steven Harper, representing the Women's Center, said he does accounting and income taxes and that this bill will clean up a further inequality of penalizing married people. See Exhibit E.

Stacy Flaherty, representing the Women's Lobbyist Fund, submitted a written statement attached as Exhibit F.

OPPONENTS

There were no opponents to HB 125.

Questions from the committee were called for.

Senator Hager asked why the deduction has to be split equally. Representative Hansen said that that was their first position.

Senator Crippen thought the fiscal note should be redone in block form. Senator Lynch asked Dan Bucks, from the Department of Revenue, if he agreed with the figures in the fiscal note. Mr. Bucks replied that they did concur in the figures.

Senator Hager suggested deleting lines 18 and 19 on page 2. Mr. Bucks commented that that would have a greater revenue impact but there was no way to predict the revenue impact. This fiscal note reflects the original version of the bill, he said. It assumes a 5% tax rate.

Senator Towe agreed with Senator Crippen that the fiscal note should be redone. The problem with doing it as a narrative is that there are no assumptions. He wondered why they weren't stated, how many people would be affected and how it would affect the foundation program.

The hearing was closed on HB 125.

CONSIDERATION OF SENATE BILL 244: Senator Thomas Towe, Senate District 34, said this matter was brought before the Revenue Oversight Committee. It addresses lump-sum distribution payments from pension plans. Federal law has a very complicated formula for taxing these lump-sum distributions. The tax is a tax separate from the income tax that is paid on the distribution. Senator Towe passed out a copy of the federal law, and it is attached as Exhibit G. Take the tax that would be due on 1/10 of the excess over $2,300 under the normal computation and multiply the result by 10. Everything over $2,300 is averaged. One-tenth is the tax rate in the lower bracket and it is multiplied by 10.

The Department of Revenue recommends that we cut through that formula and just tax 50% of the ordinary income portion of any lump-sum distribution. That is about where you end up when you use the federal equation anyway. This is a new tax in Montana. These lump-sum distributions now are avoiding tax altogether in the state of Montana.

PROPONENTS

Dan Bucks, deputy director of the Department of Revenue, said this bill is aimed at eliminating the inequities in the current tax system where taxpayers in similar situations are treated differently -- one who has lump-sum distribution versus one who has installment payments of distribution. He indicated on IRS Form 4972 what would be affected at the state level (line 2) (see Exhibit H). We could use a federal approach, he said, but we would have a long complicated form. He recommended using 50% of the lump-sum distribution as taxable income. Exhibit I compares the 50% method proposed in the bill and a 10-year averaging method used for federal income tax. The federal averaging method is higher. If the taxable income goes up, the 50% method could be higher than the federal method.

OPPONENTS

There were no opponents to SB 244.

Questions from the committee were called for.

Senator Lynch asked if it was more advantageous to the state to receive the tax all at once rather than over a period of time. Mr. Bucks stated that they do not receive the information on the IRS Form 4972 and they don't have the data with which to answer the question.

Senator Towe said that if a taxpayer takes a lump-sum distribution, the government comes out further ahead than if the taxpayer would have taken distribution over a period of time.

Senator Norman thought 50% appeared to be a rather arbitrary figure.

Senator Gage wondered if the bill could be put into effect for only the next two years as a trial period at 10% of the ordinary income portion so no one would be unduly penalized; then we could look at it during the next session.

Mr. Bucks said the income should be subject to some tax. Whatever the legislature can do to eliminate this inequity would be okay with the department. Ten percent would be much lower, he thought.

Senator Elliott explained that when you use the ten-year averaging method for total distribution, the capital gain distribution is not excluded. The reason the 50% is used is to get into the rate structure. Taking a flat 2% of the total distribution and adding that as an additional tax on the bottom of the return would be a very simple addition to the tax. He thought it was a better approach than the department's suggestion.

Senator Gage agreed with Senator Elliott, but wondered if a taxpayer in a low income bracket would be paying when he wouldn't otherwise have to pay taxes.

Senator Towe said the ordinary income law went into effect in 1969. The point that that makes is that we are picking up less than what the IRS does to make their computation when we pick up the ordinary income, which might justify keeping the percentage higher.

Mr. Bucks said the reason they didn't go the total distribution route was because the capital gains portion is subject to state tax in Montana, and if we did that, the capital gains portion would be taxed twice. If this were figured on IRS Form 4972, it would never reach Schedule D.

The hearing was closed on SB 244.

CONSIDERATION OF SENATE BILL 94 (CONTINUED): Senator Brown moved that SB 94 DO PASS. Senator Crippen said equity is something you try to achieve over a period of time. He felt the bill would pass but that the do-it-all-at-once approach was the wrong approach. There was enough testimony heard in this committee that there are inequities in the system. If we do this right now, we are going to hurt not only the oil companies but the poor taxpayers as well. Senator Crippen suggested an amendment that would phase this increase in over a period of time. He didn't know what period of time would be reasonable, but to do it all at once was not reasonable.

Senator Eck compared the taxpayer in a relatively wealthy county and a taxpayer in a poor county. The taxpayer in the wealthy county is paying many times more whether he is rich or poor. Twenty-five percent of the income tax goes into the foundation program and is spread equally over the whole state. Over 60% of the personal income upon which tax is paid comes from six urban counties, which means that those six counties are doing more than their share of supporting the foundation program, and yet no one has ever questioned that those taxpayers are paying more than their fair share. They are paying the highest property taxes to support the schools. The smaller counties with low tax bases need this bill. We have postponed it for too many years already.

Senator Crippen said he couldn't buy the philosophy of creating inequities in order to achieve equity. The coal tax and oil severance tax are examples of that. The means by which we got them there are inequitable. We are talking about all taxpayers under SB 94, and you have to treat them equally. They should be taxed on their ability to pay income tax.

Senator Lynch said that 10 years ago, we knew this inequity existed. We have given a 10-year break to the taxpayers, and now we are getting around to correcting it, by passing this bill.

Senator Gage said that we would be putting Montana in a worse condition than it is now. In 1981, if we had kept up with Wyoming oil production, we would have 722 more oil wells in Montana, $350 million more spent in Montana, 3 million more barrels of oil, $13 million more in severance taxes, net proceeds taxes, and income taxes in Montana.

Senator Eck said the basic question is: Are we going to uphold what the constitution requires as far as the state being responsible for our children's education? It is not a local responsibility except for administration of the program. At the 1972 Constitutional Convention, they said 75% of what is spent statewide in education is necessary for basics. It would be reasonable for basic education to be paid for across the board by property taxes and statewide income taxes. In 1972, the disparity was not there.

Senator McCallum figured that 43 counties will have their property taxes increased if this bill passes; only 13 counties will not have property tax increases.

Senator Turnage agreed with Senator Crippen, and suggested an increase of one-tenth of a mill a year. Once you plug in the additional 15 mills, he said, it will be there forever. Later on, when the energy-fortunate counties fail to produce, the additional 15 mills will still be with them.

Senator Norman, in reviewing the fiscal note, said that if SB 94 passes, the money would go into the state equalization fund, which would relieve pressure on the general fund. Those supporting the bill must have some commitment to raising the schedules.

Senator Brown said that in the counties that didn't need to spend all of the mills, the excess becomes part of the foundation program.

Senator Norman suggested funding the school foundation less and the general fund more because unless the schedules were raised, he couldn't see why anyone would want to pass SB 94.

Senator Gage said he didn't believe the state's portion of automobile fees were reflected at all, which could be as high as $9 million or $10 million. Further, they are also flowing back to the rich counties.

Senator Crippen said he saw a tendency of the legislature to do it all at once regardless of the consequences. It is a power we have, he said, and we should use it correctly and wisely.

We will achieve equity, but I think we are going to create inequities if we pass this bill.

Senator McCallum asked if, with the 15 mill permissive levy taken away, it meant they would not run special levies.

Senator Turnage moved that the committee pass consideration on SB 94 until a later date. His motion was seconded and carried.

The meeting adjourned at 10 a.m.

Pat M. Goodover

Chairman

ROLL CALL

SENATE TAXATION COMMITTEE

48th LEGISLATIVE SESSION -- 1983 Date 2/7/83

NAME	PRESENT	ABSENT	EXCUSED
SENATOR GOODOVER, CHAIRMAN	✓		
SENATOR McCALLUM, VICE CHAIRMAN	✓		
SENATOR BROWN	✓		
SENATOR CRIPPEN	✓		
SENATOR ELLIOTT	✓		
SENATOR GAGE	✓		
SENATOR TURNAGE	✓		
SENATOR SEVERSON	✓		
SENATOR HAGER	✓		
SENATOR ECK	✓		
SENATOR HALLIGAN	✓		
SENATOR LYNCH	✓		
SENATOR NORMAN	✓		
SENATOR TOWE	✓		
SENATOR MAZUREK	✓		

DATE February 7, 1983

COMMITTEE ON TAXATION

VISITORS' REGISTER

NAME (PLEASE PRINT)	REPRESENTING	BILL #	Check One: Support	Check One: Oppose
Willa Hall	League of Women Voters	97		✓
Nancy Leifer	MT. Dept. of Commerce	97		✓
Les Berry	DNRC	97		✓
Gus Byrom	Lewis & Clark Co.	97		✓
Sue [illegible]	self [illegible]			

(Please leave prepared statement with Secretary)

SENATE TAXATION COMMITTEE
EXHIBIT A
FEBRUARY 7, 1983
SB 97

NAME: Willa Hall DATE: 2-7-83

ADDRESS: 1502 Peosta

PHONE: 442-7495

REPRESENTING WHOM? League of Women Voters

APPEARING ON WHICH PROPOSAL: SB 97

DO YOU: SUPPORT? ______ AMEND? ______ OPPOSE? X

COMMENTS: We feel a the Alternative Energy Research Development & Demonstration account is vital to the purpose of the Coal tax & to Mont. We must continue to promote the development of alternative energy as our natural resources are depleted & to provide for the future. This account is basic to the purpose of the coal tax & therefore should remain in the coal tax until the goal of alternative energy is reached. The League does believe in sunset review & is concerned about the addition of earmarked accounts but this is an exception to our position

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

EXHIBIT B
FEBRUARY 7, 1983
SB 97

NAME: Gus Byrom DATE: Feb. 4, '83

ADDRESS: 1514 Boulder

PHONE: 443-0677

REPRESENTING WHOM? Lewis + Clark County

APPEARING ON WHICH PROPOSAL: SB 97

DO YOU: SUPPORT? ____ AMEND? ____ OPPOSE? X

COMMENTS: Deleting earmarked County land planning funds will seriously diminish Counties' ability to plan for growth, provide facilities for growth, and provide for orderly development.

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

Nancy Leifer, Montana Dept of Commerce
1424 Ninth Ave., Helena 449-3757

EXHIBIT C
FEBRUARY 7, 1983
SB 97

TESTIMONY ON SENATE BILL 97
Opponent
MONTANA DEPARTMENT OF COMMERCE

The Department of Commerce opposes Senate Bill 97, because this bill would eliminate the County Land Planning Fund.

The County Land Planning Fund has provided Montana's counties with approximately 2.5 million dollars since 1976. Counties have consistently put approximately 95% of these funds to good use every year. Only about 5% anually has been turned back to the Educational Trust Fund.

The Department has a direct interest in the continuance of this program because:

(1) It is the role of the Department to promote economic and community development. Counties have utilized the funds for these purposes.

(2) The funds have allowed Montana's local governments to address their own development needs. Local capacity to promote economic stability and growth depends on local government facilities and resources. Because these funds have allowed local governments to provide these facilities and related resources, the funds support the public/private partnership necessary to develop strong, economically healthy communities.

We urge the committee to consider the need for the funds, based on the following reasons:

(1) Nearly all counties use the funds.

(2) Federal funding for local planning has generally been eliminated.

(3) The funds are vital for most local planning programs, especially in rural counties where the funds provide 30-100% of the funding for local planning.

(4) The administrative procedures for utilizing the funds are minimal for the counties.

(5) The counties have flexibility in determining what type of planning projects they wish to undertake. This allows the funds to be used to fit local needs.

(6) Local governments have promoted cost efficiency, addressed critical public health and safety needs, and have promoted economic development through the use of these funds for projects such as: rural addressing systems, capital improvement planning, sewer and water system planning, andindustrial promotion activities.

Especially, now, during our efforts to promote new industry and produce permanent jobs, planners will be needed to help provide the information, technical expertise, and direct assistance necessary to plan for development. The current system of providing assistance to Montana's communities in planning their economic development and diversification has worked well and produced tangible results. Do we need to "fix" a wheel which is not broken?

Thank you for this opportunity to comment.

SENATE TAXATION COMMITTEE
EXHIBIT D
FEBRUARY 7, 1983
SB 97

SB 97

Presented to the Senate Committee on Taxation
By the Montana Environmental Information Center

February 4, 1983

SB 97 would end earmarking coal severance tax funds for the Alternative Energy Research Development and Demonstration Account and for the County Land Planning Account after July 1, 1985.

I will confine my comments today to the Alternative Energy Program. As the Department of Natural Resources and Conservation's report to the 1983 legislature states, the program "was established to reduce the state's reliance on fossil fuels through increased use of solar, wind, geothermal, small scale hydro, and biomass energy alternatives." Those are laudable goals.

More importantly, those goals are consistant with the purpose of the Coal Severance Tax. That is, the tax represents Montana's decision to develop a depletable resource and at the same time to plan for a future when those resources are no longer available. The Alternative Energy Program embodies that very principle, planning for that inevitable future.

The program has been dramatically improved since its inception to better serve the purposes for which it was created. This has been achieved through the availability of commercial loans, greater control over the paticipating projects, the increased use of targeted solicited projects, tougher administrative controls, and tighter monitoring.

This demonstrates DNRC's committment to continually improve the program to meet changing demands.

Finally, ending earmarking for this account represents the easy way out. It would ultimately increase revenues to the general fund in what will certainly still be tough fiscal times. That is no excuse. The alternative energy program deserves the stable support earmarked funds provide. Most importantly, the program is an intergral part of why our coal tax is good policy and defensible to those outside Montana who would limit our ability to make such policy.

Testimony of:

Don Reed
P. O. Box 1184, Helena, MT 59624
443-2520

Opposing SB 97

SENATE TAXATION COMMITTEE
EXHIBIT E
FEBRUARY 7, 1983
HOUSE BILL 125

NAME: Steve Harper DATE: Feb 7

ADDRESS: 301 S Oakes Helena

PHONE: 442-6927

REPRESENTING WHOM? Women Center

APPEARING ON WHICH PROPOSAL: Child Care Deduction HB 125

DO YOU: SUPPORT? X AMEND? ______ OPPOSE? ______

COMMENTS: accountant / taxpreparer in Helena

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

EXHIBIT F
FEBRUARY 7, 1983
HOUSE BILL 125

NAME: Stacy A. Flaherty DATE: 2/7/83

ADDRESS: Box 1099, Helena, MT 59624

PHONE: 449- 7917

REPRESENTING WHOM? Women's Lobbyist FUND

APPEARING ON WHICH PROPOSAL: HB125

DO YOU: SUPPORT? ✓ AMEND? ______ OPPOSE? ______

COMMENTS: The Women's Lobbyist Fund supports HB125.

We feel that HB125 is a fair and equitable bill that removes the technical inconviences and inequities of the current law for married couples who wish to file separately.

We urge your support of this bill. Thank you.

PLEASE LEAVE ANY PREPARED STATEMENTS WITH THE COMMITTEE SECRETARY.

SENATE TAXATION
Exhibit 4
FEB 7, 1983
SB 244

P.L. 94-455, § 1901(a)(57)(B):

Repealed Code Sec. 402(d). Applicable to taxable years beginning after December 31, 1976. Prior to repeal, Code Sec. 402(d) read as follows:

(d) CERTAIN EMPLOYEES' ANNUITIES.—Notwithstanding subsection (b) or any other provision of this subtitle, a contribution to a trust by an employer shall not be included in the gross income of the employee in the year in which the contribution is made if—

(1) such contribution is to be applied by the trustee for the purchase of annuity contracts for the benefit of such employee;

(2) such contribution is made to the trustee pursuant to a written agreement entered into prior to October 21, 1942, between the employer and the trustee, or between the employer and the employee; and

(3) under the terms of the trust agreement the employee is not entitled during his lifetime, except with the consent of the trustee, to any payments under annuity contracts purchased by the trustee other than annuity payments.

The employee shall include in his gross income the amounts received under such contracts for the year received as provided in section 72 (relating to annuities). This subsection shall have no application with respect to amounts contributed to a trust after June 1, 1949, if the trust on such date was exempt under section 165 (a) of the Internal Revenue Code of 1939. For purposes of this subsection, amounts paid by an employer for the purchase of annuity contracts which are transferred to the trustee shall be deemed to be contributions made to a trust or trustee and contributions applied by the trustee for the purchase of annuity contracts; the term "annuity contracts purchased by the trustee" shall include annuity contracts so purchased by the employer and transferred to the trustee; and the term "employee" shall include only a person who was in the employ of the employer, and was covered by the agreement referred to in paragraph (2), prior to October 21, 1942.

P.L. 88-272, § 232(e)(3):

Amended Code Sec. 402(d) to delete "except that section 72(e)(3) shall not apply" from the end of the second sentence.

' Effective with respect to taxable years beginning after December 31, 1963.

[Sec. 402(e)]

(e) TAX ON LUMP SUM DISTRIBUTIONS.—

(1) IMPOSITION OF SEPARATE TAX ON LUMP SUM DISTRIBUTIONS.—

(A) SEPARATE TAX.—There is hereby imposed a tax (in the amount determined under subparagraph (B)) on the ordinary income portion of a lump sum distribution.

(B) AMOUNT OF TAX.—The amount of tax imposed by subparagraph (A) for any taxable year shall be an amount equal to the amount of the initial separate tax for such taxable year multiplied by a fraction, the numerator of which is the ordinary income portion of the lump sum distribution for the taxable year and the denominator of which is the total taxable amount of such distribution for such year.

(C) INITIAL SEPARATE TAX.—The initial separate tax for any taxable year is an amount equal to 10 times the tax which would be imposed by subsection (c) of section 1 if the recipient were an individual referred to in such subsection and the taxable income were an amount equal to $2,300 plus one-tenth of the excess of—

(i) the total taxable amount of the lump sum distribution for the taxable year, over

(ii) the minimum distribution allowance.

(D) MINIMUM DISTRIBUTION ALLOWANCE.—For purposes of this paragraph, the minimum distribution allowance for the taxable year is an amount equal to—

(i) the lesser of $10,000 or one-half of the total taxable amount of the lump sum distribution for the taxable year, reduced (but not below zero) by

(ii) 20 percent of the amount (if any) by which such total taxable amount exceeds $20,000.

(E) LIABILITY FOR TAX.—The recipient shall be liable for the tax imposed by this paragraph.

(2) MULTIPLE DISTRIBUTIONS AND DISTRIBUTIONS OF ANNUITY CONTRACTS.—In the case of any recipient of a lump sum distribution for the taxable year with respect to whom during the 6-taxable-year period ending on the last day of the taxable year there has been one or more other lump sum distributions after December 31, 1973, or if the distribution (or any part thereof) is an annuity contract, in computing the tax imposed by paragraph (1)(A), the total taxable amounts of all such distributions during such 6-taxable-year period shall be aggregated, but the amount of tax so computed shall be reduced (but not below zero) by the sum of—

(A) the amount of the tax imposed by paragraph (1)(A) paid with respect to such other distributions, plus

(B) that portion of the tax on the aggregated total taxable amounts which is attributable to annuity contracts.

For purposes of this paragraph, a beneficiary of a trust to which a lump sum distribution is made shall be treated as the recipient of such distribution if the beneficiary is an employee (including an employee within the meaning of section 401(c)(1)) with respect to the plan under which the distribution is made or if the beneficiary is treated as the owner of such trust for purposes of subpart E of part I of subchapter J. In the case of the distribution of an annuity contract, the taxable amount of such distribution shall be deemed to be the current actuarial value of the contract, determined on the date of such distribution. In the case of a lump sum distribution with respect to any individual which is made only to two or more trusts, the tax imposed by paragraph (1)(A) shall be computed as if such distribution was made to a single trust, but the liability for such tax shall be apportioned among such trusts according to the relative amounts received by each. The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this paragraph.

(3) ALLOWANCE OF DEDUCTION.—The ordinary income portion of a lump sum distribution for the taxable year shall be allowed as a deduction from gross income for such taxable year, but only to the extent included in the taxpayer's gross income for such taxable year.

(4) DEFINITIONS AND SPECIAL RULES.—

[*Caution: Code Sec. 402(e)(4)(A), below, as amended by P.L. 97-34, is applicable to taxable years beginning after December 31, 1981. There is also a transitional rule applicable here.—CCH.*]

(A) LUMP SUM DISTRIBUTION.—For purposes of this section and section 403, the term "lump sum distribution" means the distribution or payment within one taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient—

(i) on account of the employee's death,

(ii) after the employee attains age 59½,

(iii) on account of the employee's separation from the service, or

(iv) after the employee has become disabled (within the meaning of section 72(m)(7))

from a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501 or from a plan described in section 403(a). Clause (iii) of this subparagraph shall be applied only with respect to an individual who is an employee without regard to section 401(c)(1), and clause (iv) shall be applied only with respect to an employee within the meaning of section 401(c)(1). Except for purposes of subsection (a)(2) and section 403(a)(2), a distribution of an annuity contract from a trust or annuity plan referred to in the first sentence of this subparagraph shall be treated as a lump sum distribution. For purposes of this subparagraph, a distribution to two or more trusts shall be treated as a distribution to one recipient. For purposes of this section and section 403, the balance to the credit of the employee does not include the accumulated deductible employee contributions under the plan (within the meaning of section 72(o)(5)).

(B) ELECTION OF LUMP SUM TREATMENT.—For purposes of this section and section 403, no amount which is not an annuity contract may be treated as a lump sum distribution under subparagraph (A) unless the taxpayer elects for the taxable year to have all such amounts received during such year so treated at the time and in the manner provided under regulations prescribed by the Secretary. Not more than one election may be made under this subparagraph with respect to any individual after such individual has attained age 59½. No election may be made under this subparagraph by any taxpayer other than an individual, an estate, or a trust. In the case of a lump sum distribution made with respect to an employee to two or more trusts, the election under this subparagraph shall be made by the personal representative of the employee.

(C) AGGREGATION OF CERTAIN TRUSTS AND PLANS.—For purposes of determining the balance to the credit of an employee under subparagraph (A)—

(i) all trusts which are part of a plan shall be treated as a single trust, all pension plans maintained by the employer shall be treated as a single plan, all profit-sharing plans maintained by the employer shall be treated as a single plan, and all stock bonus plans maintained by the employer shall be treated as a single plan, and

(ii) trusts which are not qualified trusts under section 401(a) and annuity contracts which do not satisfy the requirements of section 404(a)(2) shall not be taken into account.

(D) TOTAL TAXABLE AMOUNT.—For purposes of this section and section 403, the term "total taxable amount" means, with respect to a lump sum distribution, the amount of such distribution which exceeds the sum of—

 Exhibit G, p. 3

(i) the amounts considered contributed by the employee (determined by applying section 72(f)), which employee contributions shall be reduced by any amounts theretofore distributed to him which were not includible in gross income, and

(ii) the net unrealized appreciation attributable to that part of the distribution which consists of the securities of the employer corporation so distributed.

(E) ORDINARY INCOME PORTION.—For purposes of this section, the term "ordinary income portion" means, with respect to a lump sum distribution, so much of the total taxable amount of such distribution as is equal to the product of such total taxable amount multiplied by a fraction—

(i) the numerator of which is the number of calendar years of active participation by the employee in such plan after December 31, 1973, and

(ii) the denominator of which is the number of calendar years of active participation by the employee in such plan.

(F) EMPLOYEE.—For purposes of this subsection and subsection (a)(2), except as otherwise provided in subparagraph (A), the term "employee" includes an individual who is an employee within the meaning of section 401(c)(1) and the employer of such individual is the person treated as his employer under section 401(c)(4).

(G) COMMUNITY PROPERTY LAWS.—The provisions of this subsection, other than paragraph (3), shall be applied without regard to community property laws.

(H) MINIMUM PERIOD OF SERVICE.—For purposes of this subsection (but not for purposes of subsection (a)(2) or section 403(a)(2)(A)), no amount distributed to an employee from or under a plan may be treated as a lump sum distributed under subparagraph (A) unless he has been a participant in the plan for 5 or more taxable years before the taxable year in which such amounts are distributed.

(I) AMOUNTS SUBJECT TO PENALTY.—This subsection shall not apply to amounts described in clause (ii) of subparagraph (A) of section 72(m)(5) to the extent that section 72(m)(5) applies to such amounts.

[Caution: Code Sec. 402(e)(4)(J), below, as amended by P.L. 97-34, is applicable to taxable years beginning after December 31, 1981. There is also a transitional rule applicable here.—CCH.]

(J) UNREALIZED APPRECIATION OF EMPLOYER SECURITIES.—In the case of any distribution including securities of the employer corporation which, without regard to the requirement of subparagraph (H), would be treated as a lump sum distribution under subparagraph (A), there shall be excluded from gross income the net unrealized appreciation attributable to that part of the distribution which consists of securities of the employer corporation so distributed. In the case of any such distribution or any lump sum distribution including securities of the employer corporation, the amount of net unrealized appreciation of such securities and the resulting adjustments to the basis of such securities shall be determined under regulations prescribed by the Secretary. This subparagraph shall not apply to distributions of accumulated deductible employee contributions (within the meaning of section 77[72](o)(5)).

(K) SECURITIES.—For purposes of this subsection, the terms "securities" and "securities of the employer corporation" have the respective meanings provided by subsection (a)(3).

(L) ELECTION TO TREAT PRE-1974 PARTICIPATION AS POST-1973 PARTICIPATION.—For purposes of subparagraph (E), subsection (a)(2), and section 403(a)(2), if a taxpayer elects (at the time and in the manner provided under regulations prescribed by the Secretary), all calendar years of an employee's active participation in all plans in which the employee has been an active participant shall be considered years of active participation by such employee after December 31, 1973. An election made under this subparagraph, once made, shall be irrevocable and shall apply to all lump-sum distributions received by the taxpayer with respect to the employee. This subparagraph shall not apply if the taxpayer received a lump-sum distribution in a previous taxable year of the employee beginning after December 31, 1975, unless no portion of such lump-sum distribution was treated under section 402(a)(2) or 403(a)(2) as gain from the sale or exchange of a capital asset held for more than 1 year.

Form **4972**

Department of the Treasury
Internal Revenue Service

Special 10-Year Averaging Method

(For Total Distribution from Qualified Retirement Plan)

▶ Attach to Form 1040 or Form 1041. ▶ See separate instructions.

1981

EXHIBIT H
FEBRUARY 7, 1981
SB 244

Name(s) as shown on return	Identifying number

By checking this box ▶ ☐, I agree, for this and all other lump-sum distributions I receive for the same employee, not to treat any part as capital gain. I know this decision cannot be changed. (See Instruction F.)

Part I Use Part I if You Have Not Filed Form 4972 for Any Year after 1975

1	Capital gain part from payer's statement (Form 1099R, box 2)	1	
	If you are using the 10-year averaging method for the capital gain from the distribution as well as for the ordinary income, leave line 1 blank and include the capital gain on line 2 (see instruction F). Otherwise, enter the capital gain from your payer's statement (Form 1099R, box 2). If you are filing Schedule D and cannot take the exclusion on line 4 below or do not have to decrease the capital gain for Federal estate tax, enter the capital gain on your Schedule D also. See the separate instructions for line 1.		
2	Ordinary income part from payer's statement (Form 1099R, box 3). Enter here instead of on Form 1040 or Form 1041	2	
3	Add lines 1 and 2	3	
4	Death benefit exclusion (see instructions for line 4)	4	
5	Total taxable amount (subtract line 4 from line 3)	5	
6	Current actuarial value of annuity, if applicable (from Form 1099R, box 9)	6	
7	Adjusted total taxable amount (add lines 5 and 6). If this amount is $70,000 or more, skip lines 8 through 11, and enter this amount on line 12 also	7	
8	50% of line 7, but not more than $10,000 — 8		
9	Subtract $20,000 from line 7. Enter difference. If line 7 is $20,000 or less, enter zero — 9		
10	20% of line 9 — 10		
11	Minimum distribution allowance (subtract line 10 from line 8)	11	
12	Subtract line 11 from line 7	12	
13	Federal estate tax attributable to lump-sum distribution. Do not deduct on Form 1040 or Form 1041 the amount entered on this line that is attributable to the ordinary income entered on line 2. (See instructions for line 13)	13	
14	Subtract line 13 from line 12	14	
15	$2,300 plus 10% of line 14	15	
16	Tax on amount on line 15. Use Tax Rate Schedule X (Single Taxpayer Rate) in Form 1040 Instructions	16	
17	Multiply line 16 by 10. If no entry on line 6, skip lines 18 through 23, and enter this amount on line 24 also	17	
18	Divide line 6 by line 7 (carry percentage to four places)	18	%
19	Multiply line 11 by percentage on line 18	19	
20	Subtract line 19 from line 6	20	
21	$2,300 plus 10% of line 20	21	
22	Tax on amount on line 21. Use Tax Rate Schedule X (Single Taxpayer Rate) in Form 1040 Instructions	22	
23	Multiply line 22 by 10	23	
24	Subtract line 23 from line 17	24	
25	Divide line 2 by line 3 (carry percentage to four places)	25	%
26	Multiply line 24 by percentage on line 25	26	
27	Tax rate reduction credit for 1981 (multiply line 26 by .0125)	27	
28	Tax on ordinary income part of lump-sum distribution (subtract line 27 from line 26). Show this amount on Form 1040, line 36, or Form 1041, line 26b	28	

For Paperwork Reduction Act Notice, see separate instructions.

Part II Use Part II if You Filed Form 4972 for Any Other Year After 1975 or if You Received an Annuity Contract after 1975

			(a) Total received 1981	(b) Total received after 1975 and before 1981	(c) Total of columns (a) and (b)
1	Capital gain part from payer's statement (Form 1099R, box 2) *If you are using the 10-year averaging method for the capital gain from the distribution as well as for the ordinary income, leave line 1 blank and include the capital gain on line 2 (see instruction F). Otherwise, enter the capital gain from your payer's statement (Form 1099R, box 2). If you are filing Schedule D and cannot take the exclusion on line 4 below or do not have to decrease the capital gain for Federal estate tax, enter the capital gain on your Schedule D also. See separate instructions for line 1.*	1			
2	Ordinary income part from payer's statement (Form 1099R, box 3). Enter here instead of on Form 1040 or Form 1041	2			
3	Add lines 1 and 2	3			
4	Death benefit exclusion (see instructions for Part I, line 4)	4			
5	Total taxable amount (subtract line 4 from line 3)	5			
6	Current actuarial value of annuity if applicable (from Form 1099R, box 9)	6			

7	Adjusted total taxable amount (add lines 5 and 6, column (c)). If this amount is $70,000 or more, skip lines 8 through 11, and enter this amount on line 12 also	7	
8	50% of line 7, but not more than $10,000	8	
9	Subtract $20,000 from line 7. Enter difference. If line 7 is $20,000 or less, enter zero	9	
10	20% of line 9	10	
11	Minimum distribution allowance (subtract line 10 from line 8)	11	
12	Subtract line 11 from line 7	12	
13	Federal estate tax attributable to lump-sum distribution. Do not deduct on Form 1040 or Form 1041 the amount entered on this line that is attributable to the ordinary income entered on line 2. (See instructions for Part I, line 13)	13	
14	Subtract line 13 from line 12	14	
15	$2,300 plus 10% of line 14	15	
16	Tax on amount on line 15. Use Tax Rate Schedule X (Single Taxpayer Rate) in Form 1040 Instructions	16	
17	Multiply line 16 by 10. If no entry on line 6, skip lines 18 through 23, and enter this amount on line 24 also	17	
18	Divide line 6, column (c), by line 7 (carry percentage to four places)	18	%
19	Multiply line 11 by percentage on line 18	19	
20	Subtract line 19 from line 6, column (c)	20	
21	$2,300 plus 10% of line 20	21	
22	Tax on amount on line 21. Use Tax Rate Schedule X (Single Taxpayer Rate) in Form 1040 Instructions	22	
23	Multiply line 22 by 10	23	
24	Subtract line 23 from line 17	24	
25	Divide line 2, column (c), by line 3, column (c) (carry percentage to four places)	25	%
26	Tax on ordinary income parts of lump-sum distributions (multiply line 24 by percentage on line 25)	26	
27	Tax on ordinary income part of lump-sum distribution shown on Form 4972, Part I, line 24 or Part II, line 26 for 1976 through 1980	27	
28	Subtract line 27 from line 26	28	
29	Tax rate reduction credit for 1981 (multiply line 28 by .0125)	29	
30	Tax on ordinary income part of lump-sum distribution (subtract line 29 from line 28). Show this amount on Form 1040, line 36, or Form 1041, line 26b	30	

EXHIBIT I
FEBRUARY 7, 1983
SB 244

Senate Bill No. 244

With the assumption that the taxpayer has a $6,000 taxable income before consideration of ordinary income from a lump-sum distribution, the following example illustrates the difference between the "50%" method proposed in the bill and a 10 year averaging method used for federal income tax:

	Federal Method	"50% Method"
Taxable Income	$ 6,000	$ 6,000
50% of a $12,000 ordinary income from a lump-sum distribution		6,000
Total Taxable Value	$ 6,000	$ 12,000
Tax	218	597
Additional tax from 10 year averaging	426	
Total Tax	$ 644	$ 597