



U.S. SENATE COMMITTEE ON

# Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

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## Grassley Hearing Examines Tax Incentives to Boost Rural Communities

SIoux CITY – Sen. Chuck Grassley, chairman of the Committee on Finance, today pledged to work to advance his latest comprehensive legislation increasing tax incentives and fairness for rural communities.

“In some areas the tax code is out of date, and it needs to come into the 21<sup>st</sup> Century,” Grassley said. “In other areas, tax laws are unfair to rural communities or don’t do enough to build economic growth. My goal with this legislation is to update tax laws and create new incentives that make sense for rural America.”

Grassley’s comments came at his Sioux City field hearing, “Saving America’s Great Places: The Role of Tax Incentives in Preserving Rural Communities.” Expert witnesses included Iowans from Davenport and Grundy Center.

The hearing focused on Grassley’s *Heartland Investment and Rural Employment (HIRE) Act*, introduced in July. The HIRE Act is a comprehensive package with a series of changes to benefit agricultural cooperatives, small businesses, affordable housing in rural communities, and other changes. Highlights include:

**Subchapter T commission.** Congress has not reviewed Subchapter T, the federal tax section governing agricultural cooperatives, in more than 40 years. The bill creates a commission to study the tax laws pertaining to cooperatives. The commission would study whether the subchapter should be modernized; the barriers to raising equity within a cooperative; and whether a new limited liability cooperative structure should be created for cooperatives that would benefit from being taxed, and for business purposes be treated under the more flexible rules of a limited liability company.

The commission would include cooperative experts from all over the country and would have one year to submit a report to the President and Congress with its findings and recommendations.

**Farmer co-op initiatives.** The IRS determined that some cooperatives should be exposed to a regular corporate tax due to the fact that they are using organic value-added practices rather than

manufactured value-added practices. “This is unfair, and needs to be fixed,” Grassley said. In addition, he said, cooperative producers should be allowed to receive the same tax benefits from general business credits as large companies. Grassley’s legislation addresses these problems. Updates for agricultural cooperatives include:

- ▶ a modification to cooperative marketing rules to include value-added processing involving animals;
- ▶ an extension of declaratory judgment procedures to farmers’ cooperative organizations;
- ▶ payment of dividends on stock of cooperatives without reducing patronage dividends;
- ▶ and the apportionment of credits, meaning cooperatives could allow eligible patrons the benefit of general business credits earned by the cooperative.

“The tax code has changed a lot in the last 40 years,” Grassley said. “At the very least, these changes need to happen so cooperatives can continue to compete effectively in the world-wide market.”

**FFARRM accounts.** These farmer savings accounts would allow farmers to contribute up to 20 percent of their income in an account, and deduct it in the same year. FFARRM accounts would be a very important risk management tool to help farmers put away money when there’s actual income, so that in the really bad times there would be a safety net. This Grassley-sponsored measure enjoys strong bipartisan support and was approved in 1999 as part of the *Taxpayer Relief Act*, which President Clinton vetoed.

**Reversing unfair IRS decisions on self-employment tax for farmers.** Grassley said farmers who participate in the Conservation Reserve Program are unnecessarily struggling during tax season because of a case pursued by the IRS. Court rulings treat CRP as farm income subject to the additional self-employment tax rate of 15 percent. Sen. Sam Brownback of Kansas has taken the lead on fixing this problem. This unfair tax not only ignores the intent of Congress in creating the CRP, but it also discourages farmers from using environmentally pro-active measures. “At a time when farmers are struggling to regain their footing economically and do the right thing environmentally, it’s important that Congress support them by upholding its promise on CRP,” Grassley said.

**A tax deduction for farmers and restaurants to donate to food banks.** Grassley has worked with Sen. Richard Lugar of Indiana to expand the current program in which companies can donate to food banks so that farmers can donate surplus food directly to needy food banks. Grassley said it would be “a win for the farmers and a big win for people who depend on food bank assistance.” In addition, the HIRE Act clarifies that cooperatives can elect to allow their patrons to take the deduction in a similar manner to the legislative changes pending on the ethanol small producers credit.

Specifically, the provision would make changes to the federal tax code that could greatly enhance the ability of local food pantries, homeless shelters and non-profit organizations to stock their shelves and help feed hungry families. It would let farmers, restaurant owners and small businesses take advantage of the tax deduction for food donations now available only to corporations. It would increase the tax deduction for donated food to include expenses incurred by the business owner or farmer. The provision has passed the full Senate as part of the charitable giving incentives bill, which is stalled.

“Every year, 96 billion pounds of food go to waste. We need to encourage new and existing

food donors to contribute to the campaign against hunger,” Grassley said.

**Income averaging for farmers who are caught in the Alternative Minimum Tax.** When Congress passed income averaging for farmers a few years ago, it neglected to take into account the problem of running into the alternative minimum tax, which many farmers are facing now. Grassley said this legislation would fix this growing problem.

**Expansion of first-time farmer loans, or aggie bonds.** This expands opportunities for beginning farmers who are in need of low-interest rate loans for capital purchases of farmland and equipment. Current law permits state authorities to issue tax-exempt bonds and to lend the proceeds from the sale of the bonds to beginning farmers and ranchers to finance the cost of acquiring land, buildings and equipment used in a farm or ranch operation.

Unfortunately, aggie bonds are subjected to a volume cap and must compete with big industrial projects for bond allocation. Grassley said aggie bonds share few similarities to industrial revenue bonds and should not be subjected to the volume cap established for IRBs. Insufficient allocation of funding due to the volume cap limits the effectiveness of this program. “We can’t stand by and allow the next generation of farmers to lose an opportunity to participate in farming because of competition with industry for reduced interest loan rates,” Grassley said.

**Reforms for small business.** Many small businesses are organized as S corporations, which pass through income and loss to shareholders. The shareholders take into account their shares of these items on their individual tax returns. The number and type of shareholders are limited. The Grassley bill reforms and simplifies the tax treatment of S corporations to encourage their continued growth as the nation’s chief job-creating force. For example, the bill provides that all family members can be treated as one shareholder for purposes of determining the total number of shareholders. Under current law, most family members have to be treated as separate shareholders, which limits the small business’ ability to diversify its investors and therefore better withstand business fluctuations. This is especially true for community and independent banks. Diversified ownership makes these banks stronger for the rural economy, and the expansion of S corporation ownership rules would allow many more to consider an S election.

The bill contains many other reforms to help small businesses.

Grassley’s legislation also includes important provisions from the *New Homestead Act*, originally sponsored by Sen. Byron Dorgan of North Dakota and 12 original co-sponsors including Sens. Chuck Hagel of Nebraska and Sam Brownback of Kansas. “I’m looking forward to Senator Brownback’s testimony on the *New Homestead Act* provisions,” Grassley said. “We’ve included these provisions in both the HIRE Act and the *Jumpstart Our Business Strength Act*, which awaits a conference with the House.”

The provisions included in the HIRE Act include the following:

**Rural business construction and qualified rural small business investment credits.** Under current law, there is no special assistance for businesses in counties that are losing population. Grassley’s provisions provide tax credits on expenditures on newly constructed rural investment buildings and starting or expanding a business, provided that the building or business is in a county that has lost at least 10 percent of its population over the last 20 years.

In addition, the HIRE Act includes a new proposal based upon a proposal in the President’s

budget:

**Tax credit for affordable housing.** Grassley’s bill contains a tax credit to encourage the development of new or substantially rehabilitated, affordable single-family housing in low-income areas for low-income residents. The housing would be useful in rural areas with housing shortages.

“There continues to be a housing shortage for retired seniors who definitely aren’t ready for a nursing home but may want to retire from the family farm to something more manageable like a condominium,” Grassley said. “In the older rural communities, those types of housing choices just don’t exist. This proposal allows us to reinvigorate the housing market with new options.”

Grassley said the hearing testimony built a strong case for Congress to act on the HIRE Act as soon as possible.

“Rural communities contribute a significant amount to the economy,” Grassley said. “Small businesses create most of the nation’s jobs, and many of them are based in small-town America. Family farmers are critical to our safe and abundant food supply. That’s true not only for the United States, but also for the countries around the world that receive our food products. We can help sustain thousands of rural communities by passing these common-sense reforms.”

The text of the HIRE Act is available at <http://finance.senate.gov/> under “legislation.”