

A Birthday Greeting to the Tax Reform Act of 1986

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The Tax Reform Act of 1986 (the "TRA 86") was signed into law by President Ronald Reagan on October 22, 1986, exactly 38 years ago today. TRA 86 was sponsored by, among others, Representative Richard Gephardt (D-Missouri) in the U.S. House of Representatives and Senator Bill Bradley (D-New Jersey) in the U.S. Senate. It was strongly supported by the Chairman of the House Ways and Means Committee, Dan Rostenkowski (D-Illinois) and the Chairman of the Senate Finance Committee, Bob Packwood (R-Oregon).

TRA 86 is one of the most comprehensive pieces of tax reform legislation ever enacted in the United States. It was the result of a collaborative effort by Democrats and Republicans that spanned three years.

TRA 86's stated objectives were fourfold:

- Simplify the Code.
- Broaden the tax base.
- Make the Code fairer and more efficient.
- Create incentives for economic growth.

Many years after the passage of TRA 86, Senator Packwood is accredited with stating, when discussing how Democrats and Republicans worked together to get this mammoth tax bill passed:

"In six short days - with secret negotiations among seven Senate leaders from both sides of the aisle who could work together, and with give and take for the greater good - we had a piece of legislation that became the most significant change in the U.S. tax code since its creation some 75 years earlier."

TRA 86 was indeed a comprehensive overhaul of the Code. It touched almost every Chapter of the Code. Among the most notable changes to the Code, TRA 86 did the following:

- Inverted the corporate and individual income tax rates, leaving the top individual rate at 28 percent and the top corporate rate at 35 percent. In fact, for the first time in history, the top individual tax rate was lowered (from 50 percent to 28 percent), while the lowest individual tax rate was raised (from 11 percent to 15 percent). The corporate tax rate was lowered from 50 percent to 35 percent. In the end, we were

left with a top individual tax rate that was lower than the top corporate rate. This inversion led to the increased use of pass-through entities (e.g., the S corporation) by businesses operating in the United States.

- Repealed the income tax deduction for state and local taxes.
- Repealed income averaging.
- Repealed long-term capital gains preferential treatment.
- Introduced the passive activity loss rules.
- Extended the at-risk rules to real estate activities.
- Strengthened the corporate and individual alternative minimum tax regimes.
- Repealed the General Utilities doctrine.
- Beefed-up the built-in gains tax regime.
- Required most large C corporations to use the accrual method of accounting for income tax purposes.
- Limited the ability of corporations to carry forward net operating losses and excess tax credits following a change of control.
- Made extensive changes to the retirement plan and employee benefits provisions of the Code.
- Beefed up the tax shelter provisions of the Code.
- Beefed up the information reporting requirements.
- Allowed an estate and gift tax deduction for certain conservation easement donations.
- Introduced the kiddie tax.
- Revised the generation-skipping tax regime.

Happy Birthday, TRA 86!

You may not have achieved all of your goals, including creating incentives for economic growth in our country or to any significant degree simplifying the Code. You did, however, achieve other important feats, including:

- You likely broadened the tax base.
- Arguably, you made the Code somewhat more efficient and fairer.
- Most importantly, you taught us that lawmakers can work together in a bipartisan manner and pass significant tax legislation.

I am proud of you and those that participated in the bipartisan effort it took to give you life. You gave tax lawyers and accountants a lot of complex new Code provisions to master, and you created a huge amount of interesting work for us. For that, we are thankful.

It seems like you were brought into this world yesterday. However, it has been 38 years since your birth. Have a wonderful birthday, TRA 86!

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