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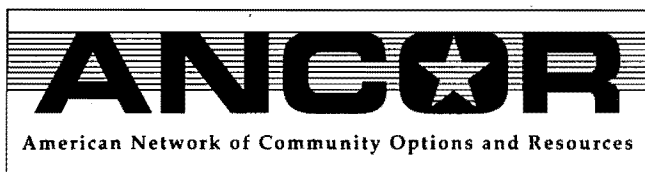
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ALL FOSTER CARE PAYMENTS SHOULD RECEIVE THE SAME INCOME TAX TREATMENT

Present Law Results in Disparate Income Tax Treatment of Foster Care Payments

Foster care providers are permitted to deduct payments for caring for foster individuals if detailed expense records are maintained to support such deductions.

However, in lieu of extensive record keeping, Section 131 of the Internal Revenue Code permits certain foster care providers to exclude from taxable income payments they receive to care for foster individuals. Who is eligible for this exclusion depends upon a complicated analysis of three factors: the age of the foster care individual, the type of foster care placement entity and the source of the foster care payments. See attached chart.

For children under 19 years old, Section 131 permits foster care providers to exclude payments from taxable income only when a State, a political subdivision thereof, or a charitable tax exempt placement agency places the individual and makes the foster care payments.

For adults age 19 years and older, Section 131 permits foster care providers to exclude payments from taxable income only when a State or political subdivision thereof places the individual and makes the foster care payments.

S. 670 and H.R. 1194 Would Simplify the Treatment of Foster Care Payments

S. 670 and H.R. 1194, both with the same content and simultaneously introduced by Senator Jeffords and Representative Lewis, respectively, would simplify the current rules for foster care payments. The bills would amend Section 131 to allow for the exclusion of foster care payments paid to families, regardless of the age of the foster care individual or whether the State or political subdivision works with a private agency to make the placement and payments. To ensure appropriate oversight, the bills require the placement agency to be either licensed or certified by a State or political subdivision thereof.

The proposed amendment in S. 670 and H.R. 1194 was included in the House, Senate, and Conference Committee versions of the Taxpayer Refund and Relief Act of 1999, H.R. 2488, the major tax bill passed by the Congress in August 1999. Under the Conference Report, the provision would be effective prospectively, for taxable years beginning after December 31, 1999.

Foster Care Payments Should Receive Uniform Income Tax Treatment

States and localities across the United States are increasingly relying on private agencies to arrange for foster care services for children and adults. However, foster care providers are reluctant to accept placements and payments by such private agencies when current law requires the provider to include such payments as taxable income and maintain extensive records to justify tax deductions. In contrast, if the foster care placements and payments are made by a State or political subdivision thereof, current law permits the provider to exclude such payments from taxable income. See *Micorescu v. Commissioner*, T.C. Memo 1998-398. Many foster care providers are thus deterred by current tax law from using private placement agencies, thereby reducing the availability of care alternatives for individuals requiring assistance. No rational basis exists for the current disparate treatment of payments received by foster care providers. S. 670 and H.R. 1194 remedy the problem.

**EXCLUDABILITY OF FOSTER CARE PAYMENTS FROM INCOME
UNDER SECTION 131 AS CURRENTLY IN EFFECT**

Placement Agency	Payor	Age of Foster Care Individual	Payment Excludable?
State or political subdivision	State or political subdivision	< 19 years	Yes
State or political subdivision	State or political subdivision	≥ 19 years	Yes
State or political subdivision	501(c)(3)	< 19 years	Yes
State or political subdivision	501(c)(3)	≥ 19 years	No
State or political subdivision	Not 501(c)(3)	< 19 years	No
State or political subdivision	Not 501(c)(3)	≥ 19 years	No
Licensed 501(c)(3)	State or political subdivision	< 19 years	Yes
Licensed 501(c)(3)	State or political subdivision	≥ 19 years	No
Licensed 501(c)(3)	501(c)(3)	< 19 years	Yes
Licensed 501(c)(3)	501(c)(3)	≥ 19 years	No
Licensed 501(c)(3)	Not 501(c)(3)	< 19 years	No
Licensed 501(c)(3)	Not 501(c)(3)	≥ 19 years	No
Not 501(c)(3)	State or political subdivision	< 19 years	No
Not 501(c)(3)	State or political subdivision	≥ 19 years	No
Not 501(c)(3)	501(c)(3)	< 19 years	No
Not 501(c)(3)	501(c)(3)	≥ 19 years	No
Not 501(c)(3)	Not 501(c)(3)	< 19 years	No
Not 501(c)(3)	Not 501(c)(3)	≥ 19 years	No

BACKGROUND ON THE TAX TREATMENT OF PRIVATELY ARRANGED FOSTER CARE

Government entities across the United States are increasingly relying on private agencies to arrange foster care services for children and adults.

Foster care providers bring children or adults into their own homes to live as family members. These foster homes have proven their efficacy when compared to institutional services and are a growing choice not only of state and local governments, but also of individuals who benefit from support in a home environment and of the families of such individuals. This type of residential alternative also adds to the available stock of community housing and expands the availability of qualified individuals who can provide support to both adults and children with disabilities. The private sector continues to play an important and growing role on behalf of many state and local governments by arranging for and supervising these homes.

Congress has recognized since 1983 that payments to foster care providers should receive special tax treatment.

In 1983, Congress first enacted Section 131 of the Internal Revenue Code to allow foster care providers to exclude from taxable income payments reimbursing such providers for expenses incurred to care for a foster child under 19 years old. The provision retroactively applied to taxable years beginning after December 31, 1978. Because the rule was limited to cover only payments which reimbursed particular foster care expenses, foster care providers still were required to maintain detailed records of such expenses in order to qualify for the exclusion.

In 1986, Congress again addressed the tax treatment of foster care payments. That year, Section 131 was simplified in two ways. First, the exclusion of foster care payments from income now applied to amounts paid for the provision of foster care, rather than amounts paid as reimbursements for qualified foster care expenses. Accordingly, it was no longer necessary for providers to maintain detailed expense records to establish the extent to which payments represented reimbursements of actual expenses. Second, the exclusion of foster care payments from income now applied to payments received for services provided to individuals age 19 years and older as long as a State (or political subdivision thereof) placed such individuals with the provider. Section 131, as amended in 1986, is currently in effect.

Thus, under current law, payments to foster care providers for care of individuals of any age are *uniformly excluded* from the gross income of a foster family only when a State (or political subdivision thereof) both places the individual and makes the payments. Further, payments to foster care providers who care for adults age 19 and older placed by an entity other than a State (or political subdivision thereof) are *uniformly included* in the provider's gross income -- even if such placements are made under a contract with a State (or political subdivision thereof). Similarly, payments for the care of children under age 19 who are placed with the foster care provider by an organization other than a State, a political subdivision thereof, or a licensed, tax-exempt charity are *uniformly included* in the provider's gross income.

Current statutory language discourages much-needed foster care providers from participating in foster care programs.

Under current law, foster care providers who receive payments that are not excludable under Section 131 are permitted to deduct payments for caring for foster individuals only if detailed expense records are maintained to support such deductions. As a result, otherwise-willing foster care providers are discouraged from accepting individuals placed by a private agency because such providers would be forced to keep extensive records of every expense made for individuals in their care in order to lower their taxes.

Recent judicial decisions reinforce disparate tax treatment.

Payments received by an adult foster care provider (and a child foster care provider, unless a Section 501(c)(3) organization is involved) are deductible when a private entity places the individual with the provider and makes the payments to the provider only when the provider substantiates such deductions with detailed records of expenses. However, payments received by a foster care provider are excludable from taxable income when a State or political subdivision of a State places the individual with the provider and makes the payments directly to the provider. The statutory language of Section 131 creates illogical differences in the tax treatment of the payments received by the foster care providers inasmuch as taxation results simply because placements are made by, and funding is transmitted through private entities. As a result, many cost-effective alternatives to institutional care are lost.

The Tax Court, on November 10, 1998, held that an Oregon family providing foster care services to adults in its home may not exclude from income payments received from the tax-exempt, charitable organization that placed such foster individuals with the family: *Micorescu v. Commissioner*, T.C. Memo 1998-398. The court reasoned that because the adult foster individuals were placed with the family by a tax-exempt, charitable organization rather than by the State or an agency of the State, such individuals were not "qualified foster individuals" within the meaning of Section 131. The court reached such conclusion even though the organization that placed the adults in the family's home both contracted with and received funds from the State of Oregon.

S. 670 and H.R. 1194 would eliminate the illogical differences in the tax treatment of payments received by foster care providers.

There is no logical basis for the disparate treatment imposed on amounts paid for foster care placements arranged by private entities. Since State and local governments are increasingly turning responsibility over to such private entities (e.g., for identifying and training foster care providers, placing individuals with foster care providers, transmitting State foster care program funds, and supervising quality assurance) all such payments received by foster care providers should be treated the same, regardless of the age of the foster care individual or whether the State or political subdivision works with a private agency to make the placement and payments. Foster care has demonstrated its cost effectiveness; and in a time of increased scrutiny of the use of public dollars, foster care should be encouraged. S. 670 and H.R. 1194 propose a much needed simplification of this unnecessarily complex provision of the Internal Revenue Code, by treating all such foster care payments the same.

See Attachment A for excerpts from the Committee Reports that accompanied the enactment and later amendment of Section 131.

See Attachment B for the text of Section 131.

See Attachment C for the Conference Report description and statutory language of H.R. 1194/S. 670 as included in the Taxpayer Refund and Relief Act of 1999

See Attachment D for Joint Tax Revenue Estimate

See Attachment E for Senator Jeffords' Dear Colleague.

See Attachment F for the text of S. 670.

See Attachment G for Senator Jeffords' introductory statement in support of s. 670.

See Attachment H for Representative Lewis' Dear Colleague.

See Attachment I for the text of H.R. 1194.

See Attachment J for Representative Lewis' introductory statement in support of H.R. 1194.

See Attachment K for the text of *Micorescu v. Commissioner*, T.C. Memo 1998-398, the recent Tax Court decision examining the tax treatment of foster care payments.

See Attachment L for a State-by-State listing of the estimated number of foster care providers in 1996.

See Attachment M for the text of testimony submitted to the House Ways & Means Oversight Subcommittee.

See Attachment N for the letter of support sent to House Ways and Means Committee Chairman Bill Archer.

See Attachment O for the letter of support sent to Senate Finance Committee Chairman William Roth.

Committee Reports on P.L. 99-514 (Tax Reform Act of 1986)

02 Explanation of provision.—The bill modifies the exclusion for certain foster care reimbursements so that the exclusion applies to amounts paid for qualified foster care, rather than amounts paid as reimbursements of qualified foster care expenses. As a result, recordkeeping to establish the extent to which payments reimburse particular foster care expenses will not be necessary.
—House Committee Report.

The conference agreement follows the House bill in eliminating the requirement of detailed recordkeeping as a condition for obtaining the exclusion. This provision otherwise does not expand the types of payments eligible for the exclusion.

Also, the conference agreement deletes the present-law limitation that the exclusion applies with respect to foster care only of children under age 19. (However, in the case of any foster home in which there is a foster care recipient who has attained age 19, foster care payments, including difficulty of care payments, are not excludable to the extent made for more than five such foster care recipients.) The conferees intend that this extension of the exclusion to adult foster care is limited to cases of individuals who provide foster care within their own homes to adults who have been placed in their care by an agency of the State or political subdivision thereof specifically designated as responsible for such function. The exclusion does not apply to payments to operators of boarding homes who provide room and board to adults who have not been placed in their care through the actions of a governmental agency responsible for adult foster care.

These provisions are effective for taxable years beginning on or after January 1, 1986.—Conference Committee Report.

Committee Report on P.L. 97-473 (1983)

03 House bill

The House bill excludes from the gross income of a foster parent amounts paid to reimburse the foster parent for the expense of caring for a foster child (under the age of 19) in the foster parent's home and difficulty of care payments. This exclusion, in the case of difficulty of care payments, is available with respect to payments for the care of up to 10 children.

Difficulty of care payments are payments that are compensation for providing the additional care of a foster child which is required by reason of a physical, mental, or emotional handicap with respect to which the State has determined that there is a need for additional compensation and which is provided in the home of the foster parent.

In order for payments to be excludable, the foster child with respect to whom payments are made must be placed by an agency of a State or political subdivision thereof, or by a State-licensed, private, tax-exempt agency.

The provision applies to taxable years beginning after December 31, 1978.

Senate amendment

The Senate amendment is similar to the House bill, with two exceptions. First, the Senate amendment excludes only difficulty of care payments, not reimbursements. Second, the amendment does not require private child-placing agencies to be licensed by the State.

Conference agreement

The conference agreement follows the House bill.
—Conference Committee Report.

Sec. 131. Certain foster care payments

(a) General rule

Gross income shall not include amounts received by a foster care provider during the taxable year as qualified foster care payments.

(b) Qualified foster care payment defined

For purposes of this section--

(1) In general

The term "qualified foster care payment" means any amount--

(A) which is paid by a State or political subdivision thereof or by a placement agency which is described in section 501(c)(3) and exempt from tax under section 501(a), and

(B) which is--

(i) paid to the foster care provider for caring for a qualified foster individual in the foster care provider's home, or

(ii) a difficulty of care payment.

(2) Qualified foster individual

The term "qualified foster individual" means any individual who is living in a foster family home in which such individual was placed by--

(A) an agency of a State or political subdivision thereof, or

(B) in the case of an individual who has not attained age 19, an organization which is licensed by a State (or political subdivision thereof) as a placement agency and which is described in section 501(c)(3) and exempt from tax under section 501(a).

(3) Limitation based on number of individuals over the age of 18

In the case of any foster home in which there is a qualified foster care individual who has attained age 19, foster care payments (other than difficulty of care payments) for any period to which such payments relate shall not be excludable from gross income under subsection (a) to the extent such payments are made for more than 5 such qualified foster individuals.

(c) Difficulty of care payments

For purposes of this section--

(1) Difficulty of care payments

The term "difficulty of care payments" means payments to individuals which are not described in subsection (b)(1)(B)(i), and which--

(A) are compensation for providing the additional care of a qualified foster individual which is--

(i) required by reason of a physical, mental, or emotional handicap of such individual with respect to which the State has determined that there is a need for additional compensation, and

(ii) provided in the home of the foster care provider, and

(B) are designated by the payor as compensation described in subparagraph (A).

(2) Limitation based on number of individuals

In the case of any foster home, difficulty of care payments for any period to which such payments relate shall not be excludable from gross income under subsection (a) to the extent such payments are made for more than--

(A) 10 qualified foster individuals who have not attained age 19, and

(B) 5 qualified foster individuals not described in subparagraph (A).

106TH Congress
1st Session

HOUSE OF REPRESENTATIVES

Report
106- 289

TAXPAYER REFUND AND RELIEF ACT OF 1999

CONFERENCE REPORT

To Accompany

H.R. 2488



August 4, 1999

**E. Expand the Exclusion from Income for Certain Foster Care Payments
(sec. 1301 of the House bill sec. 203 of the Senate amendment and sec. 131 of the Code)**

Present Law

Generally, a foster care provider may exclude qualified foster care payments, (including difficulty of care payments) from gross income if certain requirements are satisfied.⁵ First, such payments must be paid to the foster care providers by either (1) a State or political subdivision of a State; or (2) a tax-exempt placement agency. Second, the payments, including difficulty of care payments, must be paid to the foster care provider for the care of a "qualified foster individual" in the foster care provider's home. A qualified foster individual is an individual living in a foster care family home in which the individual was placed by: (1) an agency of the State or a political subdivision of a State; or (2) a tax-exempt placement agency if such individual was under the age of 19 at the time of placement. Third, the exclusion of foster care payments generally applies to qualified foster care payments for five or fewer foster care individuals over the age of 19 in a foster home. In the case of difficulty of care payments, the exclusion applies to payments for ten or fewer foster care individuals under the age of 19 in a foster home and to payments for five or fewer foster care individuals at least age 19 in a foster home.

House Bill

The House bill makes two principal modifications to the exclusion for qualified foster care payments. First, the House bill expands the list of persons eligible to make qualified foster care payments. Therefore, the exclusion applies to qualified payments made pursuant to a foster care program of a State or local government which are paid by either: (1) a State or political subdivision of a State; or (2) a qualified foster care placement agency, whether taxable or tax-exempt. Second, the bill expands the list of persons eligible to place foster care individuals. Specifically, the bill allows placements by either: (1) a State or a political subdivision of a State; or (2) a qualified foster care placement agency. For these purposes, a qualified foster care placement agency is defined as any placement agency which is licensed or certified by: (1) a State or political subdivision of a State; or (2) an entity designated by a State or political subdivision thereof, for the foster care program of such State or political subdivision to make payments to providers of foster care.

The House bill allows State and local governments to employ both tax-exempt and taxable entities to administer their foster care programs more efficiently; however, it does not extend the exclusion to payments outside such foster care programs (e.g., payments to a foster care provider from friends or relatives of foster care individual in its care).

⁵ A difficulty of care payment is a payment designated by the person making such payment as compensation for providing the additional care of a qualified foster care individual which is required by reason of a physical, mental, or emotional handicap of such individual and with respect to which the State has determined that there is a need for additional compensation.

Effective date.--The House bill provision is effective for taxable years beginning after December 31, 1999.

Senate Amendment

Same as the House bill.

Conference Agreement

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

follows through “shall be applied” and inserting “(other than with respect to sections 63(c)(4) and 151(d)(4)(A)) shall be applied”.

(2) Paragraph (4) of section 63(c) is amended by adding at the end the following flush sentence:

“The preceding sentence shall not apply to the amount referred to in paragraph (2)(A).”.

(d) *EFFECTIVE DATE.*—The amendments made by this section shall apply to taxable years beginning after December 31, 2000.

→ **SEC. 112. EXCLUSION FOR FOSTER CARE PAYMENTS TO
APPLY TO PAYMENTS BY QUALIFIED PLACE-
MENT AGENCIES.**

(a) *IN GENERAL.*—The matter preceding subparagraph (B) of section 131(b)(1) (defining qualified foster care payment) is amended to read as follows:

“(1) *IN GENERAL.*—The term ‘qualified foster care payment’ means any payment made pursuant to a foster care program of a State or political subdivision thereof—

“(A) which is paid by—

“(i) the State or political subdivision thereof, or

“(ii) a qualified foster care placement agency, and”.

(b) QUALIFIED FOSTER INDIVIDUALS TO INCLUDE INDIVIDUALS PLACED BY QUALIFIED PLACEMENT AGENCIES.—Subparagraph (B) of section 131(b)(2) (defining qualified foster individual) is amended to read as follows:

“(B) a qualified foster care placement agency.”.

(c) QUALIFIED FOSTER CARE PLACEMENT AGENCY DEFINED.—Subsection (b) of section 131 is amended by redesignating paragraph (3) as paragraph (4) and by inserting after paragraph (2) the following new paragraph:

“(3) QUALIFIED FOSTER CARE PLACEMENT AGENCY.—The term ‘qualified foster care placement agency’ means any placement agency which is licensed or certified by—

“(A) a State or political subdivision thereof,

or

“(B) an entity designated by a State or political subdivision thereof,

for the foster care program of such State or political subdivision to make foster care payments to providers of foster care.”.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1999.

ESTIMATED BUDGET EFFECTS OF THE CONFERENCE AGREEMENT FOR H.R. 2488

Fiscal Years 2000 - 2009

(Millions of Dollars)

Provision	Effective	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2000-04	2000-09
I. Broad-Based and Family Tax Relief Provisions													
A. Reduction in Individual Income Taxes - 15% rate reduced to 14.5% in 2001 and 2002, 14% in 2003 and thereafter; all other rates including AMT reduced by 1 percentage point in 2005; increase 14% bracket width for non-joint returns by \$3,000 in 2006; sunset after 2008	tyba 12/31/00	---	-7,927	-11,585	-20,207	-25,176	-37,718	-50,819	-54,740	-57,297	-17,105	-64,895	-282,574
B. Family Tax Relief													
1. Elimination of marriage penalty in standard deduction - standard deduction for joint return set at two times single standard deduction, phased in over 5 years; increase width of 14% bracket to 2 times the single bracket, phased in over 4 years beginning in 2005, sunset after 2008	tyba 12/31/00	---	-748	-1,841	-2,827	-3,921	-8,163	-17,724	-22,076	-27,563	-28,018	-9,337	-112,881
2. Marriage Penalty Relief Relating to the Earned Income Credit - increase the income starting and ending point for the earned income credit for married couples filing joint returns by \$2,000 indexed after 2006 (phaseout rate stays the same)	tyba 12/31/05	---	---	---	---	---	---	-263	-1,315	-1,302	-1,283	---	-4,163
→ 3. Tax exclusion for certain foster care payments	tyba 12/31/99	-6	-14	-21	-29	-37	-44	-52	-61	-70	-80	-106	-414
4. Expansion of adoption credit - for special needs adoption only, eliminate expense requirement and allow a \$10,000 tax credit for special needs adoptions beginning in 2001	tyba 12/31/00	---	-8	-28	-30	-33	-36	-39	-41	-42	-43	-99	-300
5. Increase the dependent care tax credit - increase percentage to 35% for AGI under \$30,000; increase percentage to 40% in 2006; index maximum expense limits for inflation; percentage phases down in 1% increments, but not below 20%, for each \$1,000 of AGI over \$30,000; expand allowable expenses to \$200 per month for all children under age 1 beginning in 2006	tyba 12/31/01	---	---	-71	-291	-313	-328	-541	-1,135	-1,093	-1,134	-675	-4,907

United States Senate

WASHINGTON, DC 20510

May 26, 1999

Dear Colleague:

Many of our State and local governments have decided that foster care placements—where families open their homes to an adult or child with disabilities or otherwise in need of government support—are the best way to serve those with special needs. Foster care affords those with special needs the opportunity to participate in the normal routines of home life that most of us take for granted.

Under our current tax laws, foster care providers are allowed to deduct expenses they incur caring for foster individuals; they are required to maintain detailed records to support these deductions. For certain foster care providers, section 131 of the Internal Revenue Code provides for a special exclusion for foster care payments. Foster families eligible for this exclusion need not report their foster care payments as income; nor do they have to maintain detailed records of household expenses for tax purposes. Eligibility for this exclusion depends on a complicated analysis of three factors: the age of the individual in foster care; the type of the foster care placement agency; and the source of the foster care payment.

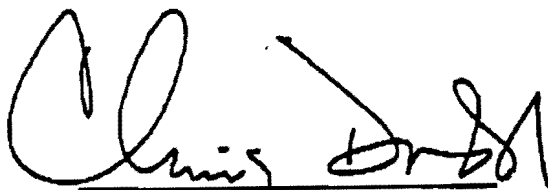
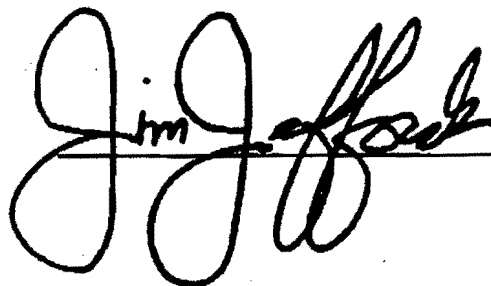
Increasingly, State and local governments are licensing or certifying experienced private agencies to arrange and make placements for foster care services. These agencies then enter into contracts with families to provide foster care. Unfortunately, foster care payments made under arrangements with private agencies often do not qualify for exclusion from income under section 131. We believe that section 131's disparate treatment of foster care payments impedes this arrangements. There are other problems with the current tax regime. For example, eligibility for the section 131 exclusion arbitrarily ends on the nineteenth birthday of the individual in foster care. As of that date, foster care payments, previously excludable from the provider's income, become taxable. This is so even if there has been no change in the foster individual's circumstances, and notwithstanding a governmental determination that the individual should remain in foster care.

Section 131 has led to a great deal of confusion among both governmental agencies and foster care providers. This confusion has discouraged governments from contracting with and taking advantage of the expertise and experience of private placement agencies. Because of confusion about the tax treatment of foster care payments, potential foster families have refused to participate in foster care programs.

Earlier this year, we introduced S. 670, which we believe will address the complexity of current law, support the decisions of local lawmakers who have chosen to rely on private placement agencies, and encourage more potential providers to participate in foster care programs. S. 670 amends Section 131, so that families will be allowed to exclude foster care payments from income, regardless of the age of the individual in foster care and regardless of whether a State or local government itself makes foster care placements and payments, or works with a licensed or certified agency to provide these services.

We urge you to co-sponsor S. 670. If you would like to be a co-sponsor, or have any questions about the bill, please contact Jeff Fox in Senator Jeffords' office at 224-5141 or Jim Fenton in Senator Dodd's office at 224-2823.

Sincerely,

Handwritten signature of Chris Dodd in black ink, written over a horizontal line.Handwritten signature of Jim Jeffords in black ink, written over a horizontal line.

106TH CONGRESS
1ST SESSION

S. 670

To amend the Internal Revenue Code of 1986 to provide that the exclusion from gross income for foster care payments shall also apply to payments by qualifying placement agencies, and for other purposes.

IN THE SENATE OF THE UNITED STATES

MARCH 19, 1999

Mr. JEFFORDS (for himself and Mr. DODD) introduced the following bill:
which was read twice and referred to the Committee on Finance

A BILL

To amend the Internal Revenue Code of 1986 to provide that the exclusion from gross income for foster care payments shall also apply to payments by qualifying placement agencies, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 **SECTION 1. EXCLUSION FOR FOSTER CARE PAYMENTS TO**
4 **APPLY TO PAYMENTS BY QUALIFYING PLACE-**
5 **MENT AGENCIES.**

6 (a) IN GENERAL.—The matter preceding subpara-
7 graph (B) of section 131(b)(1) of the Internal Revenue

1 Code of 1986 (defining qualified foster care payment) is
2 amended to read as follows:

3 “(1) IN GENERAL.—The term ‘qualified foster
4 care payment’ means any payment made pursuant to
5 a foster care program of a State or political subdivi-
6 sion thereof—

7 “(A) which is paid by—

8 “(i) a State or political subdivision
9 thereof, or

10 “(ii) a qualified foster care placement
11 agency, and”.

12 (b) QUALIFIED FOSTER INDIVIDUALS TO INCLUDE
13 INDIVIDUALS PLACED BY QUALIFYING PLACEMENT
14 AGENCIES.—Subparagraph (B) of section 131(b)(2) of
15 the Internal Revenue Code of 1986 (defining qualified fos-
16 ter individual) is amended to read as follows:

17 “(B) a qualified foster care placement
18 agency.”

19 (c) QUALIFIED FOSTER CARE PLACEMENT AGENCY
20 DEFINED.—Section 131(b) of the Internal Revenue Code
21 of 1986 is amended by redesignating paragraph (3) as
22 paragraph (4) and by inserting after paragraph (2) the
23 following:

24 “(3) QUALIFIED FOSTER CARE PLACEMENT
25 AGENCY.—The term ‘qualified foster care placement

1 agency' means any placement agency which is li-
2 censed or certified by a State or political subdivision
3 thereof to make foster care payments to providers of
4 foster care."

5 (d) EFFECTIVE DATE.—The amendments made by
6 this section shall apply to taxable years beginning after
7 December 31, 1998.

○

old the Federal Government accountable under the Nation's Federal water laws. Today, states, local governments and the private sector must all comply with each and every Federal, State, and local water requirement. The Federal Government does not.

Although Congress included provisions requiring Federal facilities to comply with the Nation's water pollution laws in 1972, the United States Supreme Court ruled that State governments could not impose certain fines and penalties against Federal agencies or violations of the Clean Water Act. While other legislation has forced the Federal Government to comply with other environmental statutes, Congress has not yet brought Federal facilities into compliance with the requirements on the prevention and control of water pollution.

This legislation, however, guarantees that the Federal Government is (1) held to the same enforcement mechanisms under the Clean Water Act as private entities, states, and localities; (2) complies with all of the Federal, State, and local requirements on the prevention and control of water pollution; and (3) is responsible for the payment of reasonable service charges.

The Clean Water Act celebrated its twenty-fifth anniversary two years ago. As a result, the entire nation has benefitted from cleaner water. In the interests of fairness, the Federal Government should not be granted immunity from the Nation's clean water laws any longer. For the sake of fairness, public safety and health, and environmental protection, the Federal Government should be held to the same standards for water pollution prevention and control as states, local governments and the private sector.

Mr. GRAMS. Mr. President, I rise today in support of the Federal Facilities Clean Water Compliance Act of 1999. I would like to thank Senator COVERDELL for bringing this important legislation forward again in the 106th Congress.

Quite simply, this legislation would force federal agencies to comply with the provisions of the Clean Water Act—something I believe most citizens assume already takes place. Unfortunately, when Congress passed the Clean Water Act in 1972, it left an out for federal agency compliance with the law by allowing them to claim "sovereign immunity" for protection against state actions or fines. So when federal agencies are not complying with provisions of the Clean Water Act, they can state in court that they are above the law.

I have always believed that the government must live under the same rules that it forces everyone else to live under. Any government which attempts to subvert the law or hide from responsibility by claiming "sovereign immunity" from environmental protection requirements, is a government that is above the people it serves, rather than a servant of the people. This legislation would reverse that trend,

and force the federal government to waive sovereign immunity when a state brings an action under the Clean Water Act. And the bill ensures that any money that state receives as a result of such an action is placed back into programs that protect the environment or defray the costs of environmental protection or enforcement.

I believe it is important that federal agencies comply with the environmental standards Congress mandates everyone else must comply. By passing the legislation we are offering today, we can restore a degree of certainty to the American people and to our states and localities that their federal government is not exempt from protecting the environment and that their federal government is not above the law. That is why I am proud to cosponsor this legislation. I look forward to working with Senators COVERDELL, DEWINE, and BREAUX over the coming weeks and months in bringing this matter before the full Senate for debate and a vote.

By Mr. JEFFORDS (for himself and Mr. DODD):

S. 670. A bill to amend the Internal Revenue Code of 1986 to provide that the exclusion from gross income for foster care payments shall also apply to payments by qualifying placement agencies, and for other purposes; to the Committee on Finance.

TAX CODE LEGISLATION

Mr. JEFFORDS. Mr. President, today I am introducing a bill that will eliminate unnecessary distinctions drawn by the Internal Revenue Code in the tax treatment of payments received by people who open their homes to care for foster children and adults. Currently, the law allows an exclusion from income for foster care payments received by some providers, while denying eligibility for the exclusion to other providers. My bill expands the law's exclusion for foster care payments. By simplifying the tax treatment of foster care payments, the bill will remove the inequities and uncertainties inherent in the current tax treatment.

Under current law, foster care providers are permitted to deduct expenditures incurred for the care of foster individuals. Providers must maintain detailed records to substantiate these deductions. In lieu of this detailed record keeping, section 131 of the Internal Revenue Code allows certain foster care providers to exclude from income the payments they receive for providing foster care. Eligibility for this exclusion depends upon a complicated analysis of three factors: the age of the person in foster care; the type of foster care placement agency; and the source of the foster care payments. For children under age 19 in foster care, section 131 permits providers to exclude payments when a State (or one of its political subdivisions) or a charitable tax-exempt placement agency places the individual in foster care and makes the foster care payments. For persons age

19 and older, section 131 permits providers to exclude foster care payments only when a State (or one of its political subdivisions) places the individual and makes the payments.

This bill will simplify these anachronistic tax rules by expanding the tax code's exclusion to include foster care payments for all persons in foster care, regardless of age. The exclusion will also be available when the foster care placement is made by a private foster care placement agency and even when foster care payments are received through a private foster care placement agency, rather than directly from a State (or one of its political subdivisions). To ensure appropriate oversight, the bill requires that the placement agency be either licensed by, or certified by, a State or a political subdivision thereof.

A qualified foster care payment under this bill must be made pursuant to a foster care program of a State or a political subdivision thereof. My intention is for this bill to cover the wide variety of foster care programs developed by States, some of which are part of larger State programs designed to provide a variety of home- and community-based services to individuals. These foster care programs place children—and in some cases adults—in homes of unrelated families who provide foster care on a full-time basis. Families providing foster care give those in their care the daily support and supervision typically given to a family member. Like traditional families, foster care providers ensure that foster children or adults have a healthy physical environment, get routine and emergency medical care, are adequately clothed and fed, and have satisfying leisure activities. Foster families provide those under their care with intellectual stimulation and emotional support that is all too often lacking in institutional or large congregate settings.

In some States, the State itself (or a political subdivision) administers both child and adult foster care programs. Many States, however, are increasingly entrusting administration of these programs to private placement agencies, approved through licensing or certification procedures, or government-designated intermediary tax-exempt organizations. Through the approval process, private placement agencies are accountable for their use of funds and for the quality of services they provide. The bill is intended to cover both those governmental foster care programs funded solely by State or political subdivision monies, and—especially in the case of adult foster care—programs funded by the federal government, typically through a State's Medicaid Home and Community-Based Waiver program approved by the federal government under 42 U.S.C. section 1396n(c).

While foster care for children has been in existence for decades, foster care for adults is a more recent phenomenon. Sometimes referred to as

"host homes" or "developmental homes," adult foster care facilities have proven to be an effective alternative to institutional care for adults with disabilities. My home State of Vermont has been at the forefront of efforts to develop individualized alternatives to institutional care. In 1993, Vermont closed the state institution for people with developmental disabilities. Vermont has chosen to rely on foster families, so that people with developmental disabilities can live in homes and participate in the regular routines of life that most of us take for granted. The foster care model has provided people with disabilities a cost-effective opportunity for successful lives in communities, with valued relationships with their foster families that have developed over time.

Vermont authorizes local developmental service providers to act as placement agencies and to contract with families willing to provide foster care in their homes. The tax law's disparate tax treatment of foster care payments impedes these types of arrangements. Persons providing foster care for individuals placed in their homes by the government can exclude foster care payments from income. For providers receiving payments from private agencies, however, the exclusion is not available (unless the individual in foster care is under age 19 and the placement agency is a nonprofit organization). Because of the complexity of current law, providers often receive conflicting advice from tax professionals regarding the proper tax treatment of foster care payments they receive. In addition, these rules discourage willing families from providing foster care in their homes to persons placed by private placement agencies, thus reducing the availability of care alternatives.

Mr. President, this bill will advance the development of family-based foster care services, a highly valued alternative to institutionalization. I urge my colleagues to support it.

• Mr. DODD. Mr. President, I am pleased to again introduce with my colleague, Senator JEFFORDS, a critically important piece of legislation that will ensure fair treatment for individuals and families who provide invaluable care to foster children and adults.

Foster care providers are currently permitted to deduct expenditures made while caring for foster individuals if detailed expense records are maintained to support such deductions. However, section 131 of the Internal Revenue Code permits certain foster care providers to exclude, from taxable income, payments they receive to care for foster individuals. Who specifically is available for this exclusion depends upon a complicated analysis of three factors: the age of the individual receiving foster care services, the type of foster care placement agency, and the source of the foster care payments.

Section 131 permits foster care providers to exclude payments from tax-

able income only when a state, or one of its political divisions, or a charitable tax exempt placement agency places the individual and makes the foster care payments for children less than 19 years of age. However, for adults over the age of 19, section 131 permits foster care providers to exclude payments from taxable income only when a state, or one of its divisions, places the individual and provides the foster care payments.

Mr. President, I believe we must move to eliminate the inequities and needless complexities of the current system. Because states and localities across the country are increasingly relying on private agencies to arrange for foster care services for both children and adults, this inequity will only become more apparent. Presently, some foster care providers are understandably reluctant to contract with private placement agencies because current law requires such providers to include foster care payments as taxable income. In contrast, current law permits providers who care for foster individuals placed in their homes by government agencies to exclude such payments from taxable income. Current law, therefore, discourages families from providing foster care on behalf of private placement agencies, thereby reducing badly-needed foster care opportunities for individuals requiring assistance.

The bill Senator JEFFORDS and I introduce today will greatly simplify the outdated tax rules applicable to foster care payments. Under our proposed legislation, foster care providers would be able to avoid onerous record keeping by excluding from income any foster care payment received regardless of the age of the individual receiving foster care services, the type of agency that placed the individual, or the source of foster care payments. To ensure appropriate oversight, this bill will require the placement agency to be licensed either by, or under contract with, a state or one of its political divisions.

Mr. President, this legislation accomplishes what current law does not—consistent and fair treatment of families and individuals who open their homes and their hearts to foster children and adults. While this modest proposal was unfortunately not adopted in the last Congress, it is my hope that foster parents may soon realize equitable treatment with the passage of this important legislation.

By Mr. LEAHY:

S. 671. A bill to amend the Trademark Act of 1946 to provide for the registration and protection of trademarks used in commerce, in order to carry out provisions of certain international conventions, and for other purposes; to the Committee on the Judiciary.

MADRID PROTOCOL IMPLEMENTATION ACT

Mr. LEAHY. Mr. President, I am pleased to introduce implementing legislation for the Protocol Relating to

the Madrid Agreement Concerning the International Registration of Marks (Protocol). Last Congress, I introduced an identical bill, S. 2191 which unfortunately the Senate did not consider.

This bill is part of my ongoing effort to update American intellectual property law to ensure that it serves to advance and protect American interests both here and abroad. The Protocol would help American businesses, and especially small- and medium-sized companies, protect their trademarks as they expand into international markets. Specifically, this legislation will conform American trademark application procedures to the terms of the Protocol in anticipation of the U.S.'s eventual ratification of the treaty. Ratification by the United States of this treaty would help create a "one stop" international trademark registration process, which would be an enormous benefit for American businesses. This bill is one of many measures I have introduced and supported over the past few years to ensure that American trademark holders receive strong protection in today's world of changing technology and complex international markets.

When I introduced this legislation last year, I also cosponsored S. 2193, legislation to implement the Trademark Law Treaty. S. 2193 simplified trademark registration requirements around the world by establishing a list of maximum requirements which Treaty member countries can impose on trademark applicants. The bill passed the Senate on September 17, 1998, and was signed by the President on October 30, 1998. I am proud of this legislation since all American businesses, and particularly small American businesses, will benefit as a result.

I have in the past supported legislation critical to keeping our trademark laws up-to-date. For example, last year I introduced S. 1727, which authorized a comprehensive study of the effects of adding new generic Top Level Domains on trademark and other intellectual property rights. This bill became law as part of the Next Generation Internet Research Act, S. 1609, which was signed into law on October 28, 1998. I also supported the Federal Trademark Dilution Act of 1996, enacted in the 104th Congress to provide intellectual property rights holders with the power to enjoin another person's commercial use of famous marks that would cause dilution of the mark's distinctive quality.

Together, these measures represent significant steps in our efforts to ensure that American trademark law adequately serves and promotes American interests.

The legislation I introduce today would ease the trademark registration burden on small- and medium-sized businesses by enabling businesses to obtain trademark protection in all signatory countries with a single trademark application filed with the Patent and Trademark Office. Currently, in order for American companies to protect their trademarks abroad, they

Congress of the United States

Washington, DC 20515

TAX RELIEF FOR FOSTER CARE FAMILIES

February 22, 1999

Dear Colleague:

Last year, thousands of needy children found foster homes through placement agencies. While most foster care families received a child through a State agency, some children were placed through a State designated private agency. As you may know, many States and local communities are now licensing and/or contracting with private agencies to provide foster care services for children and adults. These private, for-profit and non-profit agencies are qualified by the State to provide foster care services and must follow the regulations and guidelines required by the State agency.

Under current law, when a child is placed in a home by a State or non-profit agency the family receives a tax-free stipend to cover any additional expenses incurred. However, if a private, for-profit agency finds a foster home for a child the family is taxed on that same stipend or is required to maintain extensive records to justify tax deductions.

Families who open their homes to some of this country's most needy children should be treated fairly by the tax code.

Soon I will introduce a bill that will exclude these stipends from taxation for all families regardless of what type of State-authorized agency performed the placement. This legislation covers both foster children and adults.

I hope you will join me in co-sponsoring this legislation that supports families who reach out to those in need and encourages private placement agencies to continue their valuable service to local communities. If you have any questions, please call Eric Bergren in my office at 5-3501.

Sincerely,

A handwritten signature in black ink, appearing to read "Ron Lewis", written over a horizontal line.

Ron Lewis, M.C.

106TH CONGRESS
1ST SESSION

H. R. 1194

To amend the Internal Revenue Code of 1986 to provide that the exclusion from gross income for foster care payments shall also apply to payments by qualified placement agencies, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

MARCH 18, 1999

Mr. LEWIS of Kentucky (for himself, Mr. NUSSLE, Ms. PRYCE of Ohio, Mr. TERRY, Mrs. MINK of Hawaii, Mr. SHOWS, Mr. HAYWORTH, Mr. BEREUTER, Mr. BOUCHER, Mrs. MYRICK, Mr. RAMSTAD, Mr. BURTON of Indiana, Mr. McCRERY, Mr. HEFLEY, Mr. MARTINEZ, Mr. SCHAFER, Mr. PAYNE, Mr. DELAY, Mrs. NORTHUP, Mrs. CAPPS, Mr. McINNIS, and Mr. BLILEY) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to provide that the exclusion from gross income for foster care payments shall also apply to payments by qualified placement agencies, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

1 SECTION 1. EXCLUSION FOR FOSTER CARE PAYMENTS TO
2 APPLY TO PAYMENTS BY QUALIFIED PLACE-
3 MENT AGENCIES.

4 (a) IN GENERAL.—The matter preceding subpara-
5 graph (B) of section 131(b)(1) of the Internal Revenue
6 Code of 1986 (defining qualified foster care payment) is
7 amended to read as follows:

8 “(1) IN GENERAL.—The term ‘qualified foster
9 care payment’ means any payment made pursuant to
10 a foster care program of a State or political subdivi-
11 sion thereof—

12 “(A) which is paid by—

13 “(i) a State or political subdivision
14 thereof, or

15 “(ii) a qualified foster care placement
16 agency, and”.

17 (b) QUALIFIED FOSTER INDIVIDUALS TO INCLUDE
18 INDIVIDUALS PLACED BY QUALIFIED PLACEMENT AGEN-
19 CIES.—Subparagraph (B) of section 131(b)(2) of such
20 Code (defining qualified foster individual) is amended to
21 read as follows:

22 “(B) a qualified foster care placement
23 agency.”

24 (c) QUALIFIED FOSTER CARE PLACEMENT AGENCY
25 DEFINED.—Subsection (b) of section 131 of such Code
26 is amended by redesignating paragraph (3) as paragraph

1 (4) and by inserting after paragraph (2) the following new
2 paragraph:

3 “(3) QUALIFIED FOSTER CARE PLACEMENT
4 AGENCY.—The term ‘qualified foster care placement
5 agency’ means any placement agency which is li-
6 censed or certified by—

7 “(A) a State or political subdivision there-
8 of, or

9 “(B) an entity designated by a State or
10 political subdivision thereof,

11 for the foster care program of such State or political
12 subdivision to make foster care payments to pro-
13 viders of foster care.”

14 (d) EFFECTIVE DATE.—The amendments made by
15 this section shall apply to taxable years beginning after
16 December 31, 1998.

○

disabled housing development built by the Diocese of Rockville Center on Long Island and, initially at least, a controversial plan. Many residents in this middle class area resisted the notion of a subsidized apartment complex in their community. But St. Joseph's Village proved to be an outstanding neighbor and a model for the developments that followed it. Villagers often visit the nearby Hawkins Elementary School and read to students. This unique program, called "Reading Buddies," pairs up seniors with young children for mutual literary enjoyment. Other seniors devote their time preparing and serving to their fellow senior citizens at the local Senior Nutrition Center. Sixty other residents organized a project to donate money each month to improve the lives of three underprivileged children living abroad in Third World nations.

Mr. Speaker, words can hardly express the deep debt of gratitude we on Long Island owe to the residents of St. Joseph's Village for all they have done to serve our community and improve the lives of our neighbors. I ask my Congressional colleagues to join me, the community and all who have benefited from their generosity in thanking the residents for all their good work. And on this day of their 20th anniversary, we wish them many more years of success and good fortune.

FAIRNESS FOR FOSTER CARE FAMILIES ACT

HON. RON LEWIS

OF KENTUCKY

IN THE HOUSE OF REPRESENTATIVES

Thursday, March 18, 1999

Mr. LEWIS of Kentucky. Mr. Speaker, today I am introducing a bill that ensures that all foster care families are treated fairly under the Tax Code.

The Fairness for Foster Care Families Act simplifies the current rules for foster care payments and recognizes the increasing role that charitable tax exempt agencies and private for-profit agencies play in the placement of foster care children and adults.

In 1983, Congress amended the Internal Revenue Code to permit certain foster care families to exclude from taxable income payments they receive to cover the additional expenses incurred for caring for the individual. Unfortunately, the exclusion depended on a complicated analysis of three factors: the age of the foster care individual, the type of foster care placement agency and the source of the foster care payment.

Congress revisited the tax treatment of foster care payments in 1986. Although the process was simplified to an extent, some families were still left out. Those families could only receive a tax deduction if they maintained detailed expense records to support such deductions.

Under the Fairness for Foster Care Families Act, foster care providers would avoid this burdensome record keeping process. This bill guarantees that the payment is tax-free regardless of the age of the foster care individual or the type of agency that places the individual provided that the agency is licensed and certified by the State.

I hope my colleagues will join me in supporting this legislation.

HAPPY 300TH ANNIVERSARY TO THE SIKH NATION

HON. JOHN T. DOOLITTLE

OF CALIFORNIA

IN THE HOUSE OF REPRESENTATIVES

Thursday, March 18, 1999

Mr. DOOLITTLE. Mr. Speaker, Dr. Gurmit Singh Aulakh, President of the Council of Khalistan, has brought it to my attention that on April 13, the Sikhs will be celebrating their 300th anniversary. Sikhs have been significant contributors to America in several sectors of life, but their anniversary is significant for another reason. The Sikh Nation is currently one of several nations struggling to reclaim its freedom from Hindu India.

It is an interesting coincidence that April 13, the Sikhs' anniversary, is also the birthday of Thomas Jefferson, the author of our Declaration of Independence. This symmetry of events highlights the Sikh Nation's desire to be free. It is time that the Sikhs enjoy the freedom that we enjoy here in America.

In the Declaration of Independence, Jefferson wrote that all people "are endowed by their Creator with certain unalienable rights; that among these are life, liberty, and the pursuit of happiness; that whenever any form of government becomes destructive of these ends, it is the right of the people to alter or abolish it." In India, the government allows 70,000 Sikh political prisoners to rot in jail without charge or trial, some since 1984. They should be released on or before April 13 as a goodwill gesture. Instead, I fear that even more Sikhs will be endangered as "democratic, secular" India tries to maintain what it calls its "territorial integrity."

In the spirit of Jefferson, let the 300th anniversary of the Sikh Nation be an occasion to do whatever we can to support the Sikhs and the other nations of South Asia in their struggle to live in the glow of freedom. By stopping U.S. aid to India (which is one of the top five recipient countries) until human rights are universally respected, by declaring our support for self-determination through a free and fair plebiscite, and by imposing the same sanctions on India that we would impose on any other religious oppressor, we can share the blessings of liberty with the people of South Asia. This is the best thing that we can do to celebrate this important occasion with the Sikh Nation.

THE AMERICAN HEALTH SECURITY ACT OF 1999

HON. JIM McDERMOTT

OF WASHINGTON

IN THE HOUSE OF REPRESENTATIVES

Thursday, March 18, 1999

Mr. McDERMOTT. Mr. Speaker, I rise today to once again introduce the American Health Security Act. The single payer plan I propose is the only plan before Congress that will guarantee health care universality, affordability, security and choice.

While this Congress lacks the political will to enact comprehensive health reform, the underlying needs for reform remain prevalent: health care costs are more unaffordable to more people and the number of people without health insurance continues to rise. These

problems are compounded by increasing loss of health care choice and autonomy for those people who have insurance leading to disruptions in care and in relationships with providers.

The American Health Security Act I am introducing today embodies the characteristics of a truly American bill. It will give to all Americans the peace of mind—the security—to which all citizens should be entitled. It creates a system of health care delivered by physicians chosen by the patient. No one will have to leave their existing relationships with their doctors or hospitals or other providers. It is federally financed but administered at the state level, so the system is highly decentralized. And it provides new mechanisms to improve the quality of care every American receives.

The American Health Security Act (the Bill) provides universal health insurance coverage for all Americans as of January 1, 2000. It severs the link between employment and insurance. The federal government defines the standard benefit package, collects the premium, and distributes the premium funds to the states. The states, through negotiating panels comprised of representatives from business, labor, consumers and the state government, negotiate fees with the providers and the government controls the rate of price increases. The result is health care coverage that never changes when your personal situation does, never requires you to change the way you seek health care, and never causes disruption in your relationships with your providers.

The bill provides the coverage under a mechanism of global budgets to achieve controllable and measurable cost containment that will yield scorable savings over the next five years. Unlike other single-payer proposals of the past, it provides for almost exclusive state administration provided the states meet federal budget, benefit package, guarantee of free choice of provider, and quality assurance standards. This bill explicitly preserves free choice of provider by providing a mechanism for fee-for-service delivery to compete effectively with HMOs. It will not force Americans into HMO models.

The insurance mechanism of the American Health security Act is easy to use and understand. Quite simply, a patient visits the doctor or other provider. The provider then bills the state for the services provided under the standard benefit package and the state pays the bill on the patient's behalf, just as insurance companies pay medical bills on the patient's behalf now. The difference is that complicated and expensive formulas for patient co-payments, coinsurance, and deductibles in addition to premium costs are eliminated.

The standard benefit package is in fact extremely generous. It covers all inpatient and outpatient medical services without limits on duration or intensity except as delineated by outcomes research and practice guidelines based on quality standards. It provides for coverage of comprehensive long-term care, dental services, mental health services and prescription drugs. Cosmetic procedures and other "frill" benefits such as private rooms and comfort items are not covered.

The extent of state discretion is substantial. The federal budget is divided into quality assurance, administrative, operating, and medical education components. The system is financed 86% by the federal government and

T.C. Memo 398 printed in FULL format.

BENJAMIN B. AND DORINA MICORESCU, Petitioners v.
COMMISSIONER OF INTERNAL REVENUE, Respondent

Tax Ct. Dkt. No. 24964-96

UNITED STATES TAX COURT

T.C. Memo 1998-398; 1998 Tax Ct. Memo LEXIS 398; T.C.M.
(RIA) 98398

November 10, 1998, Filed

DISPOSITION: [*1] Decision will be entered under Rule 155.

CORE TERMS: adult, foster care, foster home, foster, enrollee, provider, medicaid, exempt, political subdivision, placement, resident, elderly, gross income, allocated, sentence, partnership agreement, parties agree, nonexempt, allocable, medicare, nontaxable, eligible, supplied, caring, petitioners received, eligibility, long-term, legislative history, business expenses, terminated

COUNSEL: Douglas G. Miller, for petitioners.

Ann M. Murphy, for respondent.

JUDGES: DEAN, SPECIAL TRIAL JUDGE.

OPINIONBY: DEAN

OPINION: MEMORANDUM OPINION

DEAN, SPECIAL TRIAL JUDGE: This case was heard pursuant to section 7443A(b) (3) and Rules 180, 181, and 182. n1 Respondent determined deficiencies in petitioners' Federal income taxes for the years 1992, 1993, and 1994 in the amounts of \$2,222, \$4,392, and \$5,906, respectively.

n1 Unless otherwise indicated, all section references are to the Internal Revenue Code in effect for the years in issue, and all Rule references are to the Tax Court Rules of Practice and Procedure.

After concessions by the parties, n2 the issues for decision are: (1) Whether petitioners are entitled to exclude from income the receipt of certain payments for adult foster home care; and (2) whether adult foster home care business expenses were correctly allocated by respondent [*5] to nonexempt adult foster home care income.

n2 The parties agree on the amount of "other expenses" that is deductible by petitioners. The parties agree that certain of petitioners' claimed expenses related to their adult foster home are subject to the rules of sec. 280A.

Many of the facts have been stipulated and are so found. The stipulation of facts and the attached exhibits are incorporated herein by reference.



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Petitioners resided in Portland, Oregon, at the time they filed their petition in this case.

BACKGROUND

During the years 1992, 1993, and 1994, petitioners were in the trade or business of providing adult foster home care for individuals in Portland, Oregon.

Petitioners were licensed by the Multnomah County Aging Services Division (ASD) as Level III adult foster home providers and were subject to Multnomah County Administrative Rules. ASD is an instrumentality of the State of Oregon that acts as a social service agency responsible for providing various services to individuals including determining eligibility for, and case management in, medicaid n3 for elderly persons.

n3 Medicaid is a State-administered program jointly funded by State and Federal Governments under tit. XIX of the Social Security Act Amendments of 1965 (SSA), Pub. L. 89-97, sec. 122, 79 Stat. 286, 343, current version at 42 U.S.C. secs. 1396-1396v (1994). It provides medical assistance for certain low-income people who meet specific eligibility criteria.

Medicare is Federal health insurance for the aged and disabled under tit. XVIII of the SSA, secs. 1801-1815, 79 Stat. 291-297, current version at 42 U.S.C. secs. 1395-1395ggg (1994 & Supp. III 1997). [*6]

The State of Oregon has applied for and received "waivers" from the Federal Health Care Financing Administration that allow it to use medicaid funds intended for nursing facility care, to provide community-based care services to nursing facility eligible individuals.

The State of Oregon provides health care for elderly medicaid-eligible individuals, including long-term adult foster care services. The State also contracts with health care providers to supply a variety of necessary services, including adult foster care. During the years at issue, ASD was a party to an Interagency Partnership Agreement (partnership agreement) with Providence ElderPlace, A Division of Shared Services of the Sisters of Providence (ElderPlace).

ElderPlace is not an agency of a State or of a political subdivision of a State. It is a State of Oregon medicaid service provider, a section 501(c)(3) health maintenance organization providing long-term care to the elderly funded through medicaid and medicare payments. ElderPlace is part of a demonstration project the purpose of which is to determine whether a private concern can provide the same services as medicaid and medicare at less cost in Government funds. [*7] n4 Although about 94 percent of ElderPlace enrollees are medicaid eligible, ElderPlace also has clients who are not medicaid eligible and clients who are not referred by the State.

n4 The ElderPlace program operates under provisions that allow States at their option to seek a Federal waiver of certain medicaid and medicare requirements in order to underwrite adult foster home care at a rate cheaper than that for the institutional care that they would otherwise need. The provisions had their inception with the "On LOK" program. See Social Security



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Amendments of 1983, Pub. L. 98-21, sec. 603(c), 97 Stat. 65, 168, amended by: (a) Consolidated Omnibus Budget Reconciliation Act of 1985, Pub. L. 99-272, sec. 9220, 100 Stat. 82, 183; (b) Omnibus Budget Reconciliation Act of 1986, Pub. L. 99-509, sec. 9412(b), 100 Stat. 1874, 2063; (c) Omnibus Budget Reconciliation Act of 1987, Pub. L. 100-203, sec. 4118(b), (g), 101 Stat. 1330, 1330-155 and 1330-156; and (d) Balanced Budget Act of 1997, Pub. L. 105-33, sec. 4801, 111 Stat. 251, 528, codified at 42 U.S.C. sec. 1395eee (1994 & Supp. III 1997) as the Programs of All-Inclusive Care for the Elderly (PACE).

Under the partnership agreement, [*8] ASD and ElderPlace "work together to address the needs of older adults in Multnomah County."

The partnership agreement provides that persons who elect to participate in the ElderPlace program must agree to receive all their health and long-term care services exclusively from ElderPlace. ElderPlace assumes the full cost for all services provided. In return, ElderPlace receives a payment monthly from medicare and medicaid for providing the full range of medical, social, and long-term care services that the participants need. The amount of such payments is based on the number of participants served.

Under the partnership agreement, ASD retains responsibility for "screening and intake" of elderly individuals. As part of its screening and intake of older adults for long-term care services, ASD agrees to "consider ElderPlace as one of the options available to the older adult." ASD will continue to determine eligibility for medicaid services and will screen persons for medicaid-waivered services to determine whether they are eligible for the ElderPlace program. Under the partnership agreement, ASD also remains responsible for "protective services" (protecting the elderly against abuse, [*9] neglect, exploitation, and abandonment).

But for the above-named purposes, individuals choosing to enroll in the ElderPlace program are removed from the ASD case management system and put into the ElderPlace system. ElderPlace case management activities include developing a "care plan" for the enrollee that takes into consideration the enrollee's need of transportation, medical equipment, supplies, medications, and therapies.

The State of Oregon and ElderPlace entered into a series of contracts between 1990 and 1994 in order to carry out the objectives of the partnership agreement.

Pursuant to the contracts with the State of Oregon, ElderPlace provided health services and, to those in need, personal services like assistance with bathing, grooming, and eating. These services were supplied through adult foster care home providers, such as petitioners, with whom ElderPlace contracted in turn. ElderPlace paid adult foster care home operators out of the funds paid to it by the State of Oregon.

Adult foster home operators who elected to care for residents enrolled in the ElderPlace program received payments negotiated separately with each homeowner, based on the level of service each would [*10] provide. ElderPlace did not, however, pay for room and board at adult foster homes. Room and board payments were the responsibility of the enrollee or the enrollee's representative and were paid at a rate determined by a schedule set by the State of Oregon.



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If an elderly person chose to enroll in the ElderPlace program, and foster care was appropriate, ElderPlace assisted in "locating adult foster care homes that have the capacity to meet their care needs and also have vacancies". ElderPlace supplied transportation to the enrollee or his representative to look at different foster homes. ElderPlace advised the enrollee or his representative as to whether one foster home would be better than another for the particular enrollee, based upon that enrollee's needs. Once a decision was made identifying the foster home in which the enrollee wanted to live, ElderPlace negotiated the enrollee's payment rate with the foster home operator of the selected home.

During each of the years 1992, 1993, and 1994, petitioners provided adult foster care to several persons in their home. All of the residents had attained the age of 19. Petitioners received adult foster care payments for the individuals [*11] from various sources, from their residents or their representatives, in some cases from the State of Oregon and in other cases from ElderPlace.

On their Federal income tax returns for 1992 through 1994, petitioners reported certain income and deductions from "ADULT FOSTER CARE" on Schedule C. Petitioners did not report as income amounts received from the State of Oregon or from ElderPlace. On their return for 1994, petitioners reported exclusions of State and ElderPlace payments from income and made a separate adjustment for expenses attributable to nontaxable income.

Respondent examined petitioners' returns and determined that petitioners improperly excluded self-employment income received from ElderPlace in the amounts of \$13,167, \$22,750, and \$32,366 for the years 1992, 1993, and 1994, respectively, and are entitled to claim additional business expenses associated with the income that was allocated under section 265.

DISCUSSION

The parties agree that payments petitioners received directly from residents, or their representatives, are taxable and that payments petitioners received for residents placed in their home directly by the State of Oregon are tax exempt under [*12] section 131. The parties disagree about whether payments petitioners received from ElderPlace are exempt from tax under section 131 and the proper allocation of expenses to exempt and nonexempt income under section 265.

SECTION 131 FOSTER CARE PAYMENTS

Section 131(a) provides that gross income shall not include "qualified foster care payments". A "qualified foster care payment" as described in section 131(b)(1) is any amount:

(A) which is paid by a State or political subdivision thereof or by a placement agency which is described in section 501(c)(3) and exempt from tax under section 501(a), and

(B) which is ---

(i) paid to the foster care provider for caring for a qualified foster



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individual in the foster care provider's home, or

(ii) a difficulty of care payment. n5

n5 Difficulty of care payments as described in sec. 131(c) are not at issue in this case.

A "qualified foster individual" is described in section 131(b) (2) as any individual living in a foster family home in which the individual was "placed by":

(A) an agency of a State or political subdivision thereof, or

(B) in the case of an individual who has not attained age 19, an organization which is licensed by a State [*13] (or political subdivision thereof) as a placement agency and which is described in section 501(c) (3) and exempt from tax under section 501(a).

Petitioners argue that the payments to them by ElderPlace are excluded from income under section 131 because they are qualified foster care payments. Even "though the check to the petitioners is made by Providence ElderPlace", petitioners contend that the payments, indirectly, are from the State of Oregon. Petitioners argue further that the legislative history of section 131 and the intent of Congress in enacting it was that a payment by an "intermediary" such as ElderPlace, made out of State funds "that a state has an obligation to provide", meets the requirements of section 131(b) (1) (A).

Respondent contends that the ElderPlace payments to petitioners are includable in gross income because the payments are not qualified foster care payments. They are not qualified foster care payments, maintains respondent, because the ElderPlace payments were not paid to petitioners for caring for "qualified foster individuals". Respondent points to the definition of a qualified foster individual in section 131(b) (2) as an individual living in a foster family [*14] home who was "placed there by" an agency of a State or political subdivision thereof. Since ElderPlace, not an agency of a State or political subdivision thereof, "placed" its enrollees with petitioners, the enrollees are not qualified foster individuals, argues respondent. Respondent concludes that the ElderPlace payments to petitioners do not meet the stated requirements.

QUALIFIED FOSTER INDIVIDUAL

The amounts in question can be qualified foster care payments only if they were paid to petitioners as foster care providers for qualified foster individuals. Sec. 131(b) (1) (B) (i); see supra note 5. Therefore, the focus of our analysis will be to decide whether ElderPlace enrollees in petitioners' home were qualified foster individuals.

To be a qualified foster individual, an individual in a foster home who has attained age 19 must have been "placed by" an agency of a State or political subdivision thereof. Sec. 131(b) (2) (A). If ElderPlace enrollees were not "placed by" an agency of a State or political subdivision thereof into petitioners' foster home, they are not qualified foster individuals.



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"PLACED BY" A STATE AGENCY

Petitioners deny that ElderPlace enrollees were "placed by" ElderPlace [*15] in their care. According to petitioners, none of the witnesses at trial gave any testimony that the ElderPlace program "placed" individuals in foster homes.

Petitioners further contend that the phrase "placed by" in section 131(b)(2) has no definition in the Internal Revenue Code or regulations, no legal definition in case law, and no definition in Oregon State statutes, administrative rules, or local county rules or ordinances. The words "place" or "placement" have, petitioners allege, no "customary meaning to those who are closely involved in adult foster care."

Without a working definition of the word, petitioners nonetheless argue that the elderly enrollees of the ElderPlace program were "placed" in their care, not by ElderPlace, but by the "actions" of a government agency, albeit indirectly. Petitioners urge us to examine the legislative history of section 131 to confirm their view.

Respondent replies that to be a "qualified foster individual", the plain language of section 131(b)(2) requires that individuals who have attained the age of 19 must be "placed by" an agency of a State or political subdivision thereof. Since ElderPlace, and not an agency of the State or political [*16] subdivision thereof, "placed", in the common usage of the term, its enrollees with petitioners, respondent maintains that the requirements of section 131(b)(2) were not met in petitioners' case.

PLAIN MEANING

The starting point for the interpretation of a statute is the language itself. *Consumer Prod. Safety Commn. v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980); *Dyer v. United States*, 832 F.2d 1062, 1066 (9th Cir. 1987). If the language of the statute is plain, clear, and unambiguous, "the sole function of the courts is to enforce it according to its terms." *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 241 (1989) (quoting *Caminetti v. United States*, 242 U.S. 470, 485 (1917)).

The Court must assume that the legislative purpose of the statute is expressed in the ordinary meaning of the words used. *American Tobacco Co. v. Patterson*, 456 U.S. 63, 68 (1982); *Richards v. United States*, 369 U.S. 1, 9 (1962); *Florida Hosp. Trust Fund v. Commissioner*, 103 T.C. 140, 152 (1994), *affd.* 71 F.3d 808 (11th Cir. 1996). [*17] Where there is a conflict in inferences between the language of the statute and the legislative history, the language of the statute generally prevails. *In re Stringer*, 847 F.2d 549, 551 (9th Cir. 1988); *Huntsberry v. Commissioner*, 83 T.C. 742, 747-748 (1984).

The common meaning of the verb "to place" is:

1: to distribute in an orderly manner: ARRANGE 2 a: to put in or as if in a particular place: SET b: to present for consideration (a question PLACED before the group) c: to put in a particular state (a performer under contract) d: to direct to a desired spot * * * 4: to find a place (as a home or employment) for * * * Webster's Ninth New Collegiate Dictionary 897 (1990).



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Examining the record in light of the common meaning of the verb "to place", we find that ElderPlace indeed placed elderly individuals in petitioners' foster home.

Petitioners called as a witness Mr. Donald M. Keister, director of ElderPlace and former deputy director of ASD. Mr. Keister testified that an individual who decided to enroll in the ElderPlace program would undergo an "assessment" to determine his or her needs. ElderPlace, for appropriate individuals, [*18] would then assist in locating adult foster homes, provide transportation to view the homes, provide advice as to which home might be best for the individual, and negotiate with the foster home a price to be paid for the care of the individual. On the basis of the latter fact, we assume that if a rate satisfactory to ElderPlace could not be negotiated, another home would be located or the individual would terminate enrollment in the ElderPlace program and attempt to be "placed" by the State.

In cross-examination, respondent's counsel asked whether ElderPlace enrollees might ask to move from one foster home to another, and Mr. Keister replied that such a situation may arise for a number of reasons. He continued to explain:

So, in essence, when that happens, we go through the same process that I described before.

Placements -- you know, movement also occurs through, you know, residential care facilities, they also occur to nursing facilities, depending upon what the care needs of the individual are.

Respondent called Mr. Jeffrey Miller to testify. Mr. Miller is employed by the State of Oregon as a medicaid policy analyst for the State Senior and Disabled Services Division. His position [*19] involves helping State field offices determine medicaid eligibility for individuals. Mr. Miller is familiar with the ElderPlace program. During his testimony the following exchange took place:

Q. To your knowledge, if a person chooses the ElderPlace waiver --

A. Uh-huh.

Q. -- is the State ever consulted as to where that person resides, in what adult foster care home?

A. We would have taken an application on that individual, and in such, we would have had the address of the person.

Q. Okay. But does the State at that point decide--if someone is enrolled in ElderPlace, does the State decide where that person resides?

A. No. The case management responsibilities would be with ElderPlace to do that.

Q. Okay. So ElderPlace would be the placing agency, is that correct?

A. They would be the ones making that decision.



There is additional evidence in the record on the issue of placement. During the years at issue, ElderPlace had a form "Adult Foster Care Contract" (contract) that it used to retain the services of adult foster home care providers. ElderPlace and petitioners used the contract for every ElderPlace program participant who was referred to petitioners in 1992, 1993, and 1994. Part [*20] III of the contract, Compensation and Billing, states that the "Provider" (petitioners) agrees to accept as full compensation the amounts set forth in an attached exhibit to the agreement. It is also agreed that "Each Participant placed with the Provider shall have his/her rate based on his/her individual Service Plan". n6 In part VIII of the agreement, Term and Termination, the parties agree that the "placement" may be terminated by either the Participant, the Provider, or ElderPlace upon 2 weeks' notice. "After the first two weeks of the Participant's placement," the service plan may be terminated by the Provider under circumstances enumerated in the agreement. No agency of the State or a political subdivision thereof was a party to the contract between ElderPlace and petitioners.

n6 Under the contract, a "Participant" is defined as a person enrolled in the ElderPlace program. The term "Service Plan" is defined as the plan determined for "each Participant PLACED with the Provider." (Emphasis added.)

LEGISLATIVE HISTORY

Petitioners insist, however, that individuals placed by ElderPlace were placed by an entity that had contracted with a State agency responsible for such matters. [*21] Therefore, the individuals placed by ElderPlace were placed by the State within the meaning of section 131(b)(2), petitioners conclude. They base their argument on the legislative history of section 131, which, they claim, shows that the use of the phrase "placed by" in section 131(b)(2) merely requires some indirect "State action" of a government agency.

For taxable years beginning before January 1, 1986, section 131 provided an exclusion from gross income for certain payments received by "foster parents" for caring for foster children. The Tax Reform Act of 1986, Pub. L. 99-514, section 1707, 100 Stat. 2085, 2781-2782, amended section 131 to extend to certain adult foster care payments the exclusion from gross income. Petitioners point to the language of H. Conf. Rept. 99-841 (Vol. II), at II-838 through II-839 (1986), 1986-3 C.B. (Vol. 4) 1, 838-839, which says:

The conferees intend that this extension of the exclusion to adult foster care is limited to cases of individuals who provide foster care within their own homes to adults who have been placed in their care by an agency of the State or political subdivision thereof specifically designated as responsible [*22] for such function. The exclusion does not apply to payments to operators of boarding homes who provide room and board to adults who have not been placed in their care through the actions of a governmental agency responsible for adult foster care.

Petitioners focus on the second sentence of the quoted language, specifically that part that says "THROUGH THE ACTIONS OF A GOVERNMENTAL AGENCY RESPONSIBLE FOR ADULT FOSTER CARE." (Emphasis added.) Because the second sentence does not say "BY AN AGENCY OF THE STATE OR POLITICAL SUBDIVISION THEREOF", petitioners conclude that "State action" includes their situation, an indirect, contractual



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relationship with the State through the entity with which they contracted.

Petitioners fail, however, to address the first sentence of the above excerpt that expresses the intent of Congress that section 131 apply only in the case of "ADULTS WHO HAVE BEEN PLACED IN THEIR CARE BY AN AGENCY OF THE STATE OR POLITICAL SUBDIVISION THEREOF SPECIFICALLY DESIGNATED AS RESPONSIBLE FOR SUCH FUNCTION." (Emphasis added.) What petitioners want is to interpret one sentence out of context. But words and phrases must be interpreted in context. Rules of statutory construction [*23] appropriate to interpreting the language at issue suggest that words are understood by the words associated with them and that a general term following specific terms takes its meaning from the kinds of things denoted by the specific terms. *Jarecki v. G.D. Searle & Co.*, 367 U.S. 303, 307 (1961); *F.W. Fitch Co. v. United States*, 323 U.S. 582, 585-586 (1945); *United States v. Lacy*, 119 F.3d 742, 748 (9th Cir. 1997).

We interpret the phrase "State action" in the second sentence of the above excerpt to refer to the intent of the first sentence that adults must have been "placed by" a State agency specifically designated as responsible for that function.

Our interpretation is further reinforced by referring to section 131(b)(2). A qualified foster individual is not only one placed by "an agency of a State or political subdivision thereof" but may be one also placed by:

(B) in the case of an individual who has not attained age 19, an organization which is licensed by a State (or political subdivision thereof) as a placement agency and which is described in section 501(c)(3) and exempt from tax under section [*24] 501(a). Sec. 131(b)(2)(B).

If Congress had intended the phrase "placed by an agency of a State or political subdivision thereof" contained in section 131(b)(2)(A) to include section 501(c)(3) entities such as ElderPlace, it could have used language similar to that used in section 131(b)(2)(B).

Petitioners counter with the argument that section 131(b)(2)(B) operates to exclude section 501(c)(3) organizations from the benefit of section 131 where "there is no state involvement"; that is, where the section 501(c)(3) organization does not receive State funds. While we are not sure how this bolsters their position, we note that the Court has already observed that petitioners' interpretation of section 131(b)(2)(B) is unsupported. See *Cato v. Commissioner*, 99 T.C. 633, 643 (1992), where the Court said: "There is no indication in any of the House or Senate hearings on the bill or in the reports of either congressional branch that would indicate that a distinction should be made that section 131 only applies if a tax-exempt agency is State funded."

We find that the intent of Congress as expressed in the pertinent legislative history comports with the plain meaning [*25] of the language in section 131. The record in this case makes it clear that enrollees in the ElderPlace program who were in petitioners' foster home were "placed by" ElderPlace in the home according to the ordinary use and plain meaning of the verb "to place".

The individuals placed in petitioners' home by ElderPlace were not qualified foster individuals because they were not placed by an agency of the State or a political subdivision thereof. Because the ElderPlace enrollees were not



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qualified foster individuals, amounts paid to petitioners for providing care for them cannot be qualified foster care payments.

MEDICAID POLICY

Petitioners further argue that a finding by the Court that section 131 does not cover their payments from ElderPlace would produce "absurd results" and that the future of this experimental program would be imperiled. The example of "absurd results" cited by petitioners is the case where a foster home resident elects in and out of the ElderPlace program, thereby rendering payments to the foster care provider taxable, or nontaxable, depending only upon who is making the payment, the State or ElderPlace.

Petitioners' analysis leads them to an incorrect conclusion. [*26] In the situation where an individual eligible for adult foster home care elects in and then out of the ElderPlace program, the PLACEMENT by ElderPlace is terminated, with notice to the provider according to the contract. If the State assumes responsibility for care of the individual, the State will then PLACE the individual; it is placement, not payment, that would determine the taxability of the payments in petitioners' example. We find the example cited by petitioners not to be "absurd" but merely the intended result of the statute as written by Congress. See *Tele-Communications, Inc. & Subs. v. Commissioner*, 95 T.C. 495, 507 (1990), *affd.* 12 F.3d 1005 (10th Cir. 1993).

Although petitioners assert that tax consequences may negatively affect the medicaid waiver or PACE program by placing an additional financial burden on ElderPlace and petitioners, or those similarly situated, we are not at liberty to ignore the plain wording of section 131. The purpose of medicaid is not to financially benefit health care providers but to aid patients. *Baptist Hosp. E. v. Secretary of HHS*, 802 F.2d 860, 868-869 (6th Cir. 1986), [*27] *revd.* on other grounds *sub nom. Bethesda Hosp. Association v. Bowen*, 485 U.S. 399 (1988); *Green v. Cashman*, 605 F.2d 945, 946 (6th Cir. 1979). In any event, petitioners' policy arguments do not override the terms of an unambiguous statute. See *In re Transcon Lines*, 58 F.3d 1432, 1437-1438 (9th Cir. 1995); *In re Kelly*, 841 F.2d 908, 913 (9th Cir. 1988).

We find that amounts received by petitioners from ElderPlace for adult foster home care are not qualified foster care payments under section 131(b) and are includable in gross income in each of the years at issue in this case.

EXPENSE ALLOCATION UNDER SECTION 265

The parties agree that petitioners incurred and paid certain expenses related to their operation of an adult foster home for all the years involved here. The parties also agree that petitioners received payments for providing adult foster home care for individuals, some of which are not includable in income.

Pertinent to these facts is section 265, which provides in part:

SEC. 265(a). General Rule. -- No deduction shall be allowed for --

(1) Expenses. -- Any amount [*28] otherwise allowable as a deduction which is allocable to one or more classes of income other than interest (whether or not any amount of income of that class or classes is received or accrued)



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wholly exempt from the taxes imposed by this subtitle, or any amount otherwise allowable under section 212 (relating to expenses for production of income) which is allocable to interest (whether or not any amount of such interest is received or accrued) wholly exempt from the taxes imposed by this subtitle.

Respondent determined that some of the adult foster home care expenses claimed by petitioners are expenses that are allocable to petitioner's tax-exempt income and are therefore nondeductible. Petitioner's position is that respondent's method of allocation is wrong.

Having determined that petitioners must include in income the payments received from ElderPlace, respondent argues that petitioners may deduct foster home care expenses only in the same ratio as the ratio of taxable income to total income.

Petitioners, rather than a pro rata allocation based on taxable and nontaxable income, would allocate expenses to three income categories: (a) To adult foster care "service" income, some of [*29] which is tax exempt; (b) to "room and board" income, almost all of which is taxable; n7 and (c) to income related to both "service" and "room and board". Petitioners characterize mortgage interest, real estate taxes and insurance, repairs, maintenance, depreciation, and food expense as "room and board" expenses. Petitioners want the Court to allocate most "room and board" expenses to "room and board" income and almost none of it to "service" income.

n7 The parties agree that petitioners had a resident, Mr. Authur (sic) Armstrong, whose room and board was paid by the Oregon Department of Veterans' Affairs in 1993 and 1994 and is tax exempt.

Under section 1.265-1(b)(1), Income Tax Regs., the term "class of exempt income", as that term is used in section 265, means any class of income wholly excluded from gross income or wholly exempt from tax. Allowable expenses directly allocable to any class of exempt income shall be allocated thereto and expenses directly allocable to any class of nonexempt income shall be likewise allocated thereto. Where an expense is indirectly allocable to both a class of nonexempt income and a class of exempt income, "a reasonable proportion thereof determined [*30] in the light of all the facts and circumstances in each case shall be allocated to each." Sec. 1.265- 1(c), Income Tax Regs.

The class of gross income for which petitioners' deductions are denied under section 265 is section 131 qualified foster care payments. In the case of petitioners, such payments are for "caring for a qualified foster individual IN THE FOSTER CARE PROVIDER'S HOME". Sec. 131(b)(1)(B) (emphasis supplied).

Under Oregon State law the term "adult foster home" means a "FAMILY HOME OR FACILITY IN WHICH RESIDENTIAL CARE IS PROVIDED for five or fewer adults who are not related to the provider by blood or marriage." Ore. Rev. Stat. sec. 443.705(1) (1992) (emphasis supplied). The term "residential care" means providing "ROOM AND BOARD AND SERVICES that assist the resident in activities of daily living". Ore. Rev. Stat. sec. 443.705(6) (1992) (emphasis supplied).

Although petitioners were separately paid for room and board for most residents, n8 petitioners' exempt and nonexempt foster care income was based on their home ownership. In order to qualify as having an adult foster home



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petitioners must under Federal and State law provide the appropriate services IN THEIR HOME. [*31] and they in fact did so in the years under consideration. The expenses for mortgage interest, real estate taxes, insurance, repairs and maintenance, utilities, depreciation, and "other" home expenses were incurred as a result of or incident to their adult foster home activity, and their income was derived from the use of their home as an adult foster home. There is a direct factual relationship between those expenses and all petitioners' adult foster home care income, both taxable and nontaxable.

n8 We note that there is no separately stated room and board amount for petitioners' "private pay" residents.

We find that petitioners' business expenses that they have characterized as "service" expenses, "room and board" expenses and other expenses are related to all of petitioners' adult, foster home care income and must be allocated between exempt foster home care income and nonexempt foster home care income. We further find that under the facts and circumstances of this case, respondent's method of proportional allocation of expenses between taxable and nontaxable income is correct. See *Mallinckrodt v. Commissioner*, 2 T.C. 1128, 1148 (1943), *affd.* 146 F.2d 1 (8th Cir. 1945); [*32] *McFarland v. Commissioner*, T.C. Memo. 1992-440.

To reflect the foregoing,

Decision will be entered under Rule 155.



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1996 Data From: *The State of the State in Developmental Disabilities - 5th edition* (1998)
Braddock, Hemp, Parish & Westrich, Published by AAMR

	<u># in Foster Care</u>	<u>Terminology Used to Identify Foster Care</u>
ALABAMA	0	
ALASKA	0	
ARIZONA	285/315	Child Development/adult Development
ARKANSAS	0	
CALIFORNIA	0*	(some included among 18,548 Community Care Facilities for 6 or fewer)
COLORADO	0*	(Host Homes are included among 1,842 homes for 4 or fewer)
CONNECTICUT	519	Community Training Homes
DELAWARE	99/68	Foster Care/Adult Family Living
DISTRICT OF COLUMBIA	91	foster homes
FLORIDA	409	foster homes
GEORGIA	0	
HAWAII	418	foster care
IDAHO	0*	(foster homes for children are included among 242 homes for 6 or fewer)
ILLINOIS	120/144	Home/Individual Programs & Special Home Placements
INDIANA	425	Alternative Family Homes
IOWA	168	foster homes
KANSAS	0	
KENTUCKY	279	Family Homes
LOUISIANA	144	foster homes
MAINE	0	
MARYLAND	262	foster homes
MASSACHUSETTS	790	foster homes
MICHIGAN	1,656	Family Foster Care
MINNESOTA	161/899	Children's Foster Homes/Adult Foster Homes
MISSISSIPPI	0	
MISSOURI	200	foster homes
MONTANA	177	foster homes
NEBRASKA	0	
NEVADA	97	Developmental Homes
NEW HAMPSHIRE	546	foster care
NEW JERSEY	1,745	Skill Development and Family Care Homes
NEW MEXICO	35	Surrogate Living
NEW YORK	4,054	Family Foster Care
NORTH CAROLINA	73	Alternative Family
NORTH DAKOTA	44	foster homes
OHIO	360	Family Homes
OKLAHOMA	0	
OREGON	88	Relative Foster Care
PENNSYLVANIA	1,145	foster homes
RHODE ISLAND	69	Adult Family Homes
SOUTH CAROLINA	130	Community Training Homes
SOUTH DAKOTA	23	foster homes
TENNESSEE	200	foster homes
TEXAS	73	foster homes
UTAH	82/12	Professional Parents/Adult Foster Care
VERMONT	522	Developmental Homes
VIRGINIA	86	Sponsored Placements
WASHINGTON	1,131	Adult Family Homes
WEST VIRGINIA	0*	(foster care included among 519 homes for 6 or fewer)
WISCONSIN	129/1,289/875	Children's Foster Homes/Adult Family Homes (for 1 or 2) (3 or 4)
WYOMING	32	foster homes
Total	20,469	

There is no indication in the report if these are arranged by governmental or non-governmental agencies, and in most states, there is no way of telling if the homes are for children or adults; nor are data provided on other disability groups.

* CA, CO, ID and WV also had people in foster care in 1996, but numbers are included in larger figures used for people in homes for 6 or fewer. ANCOR members in other states have indicated that they supported people in foster care as well.

**Written Statement of the
American Network of
Community Options and Resources
(ANCOR)**

**A Proposal to Address the
Current Complexity of Section 131 of the
Internal Revenue Code to Individuals
Receiving Foster Care Payments**

**Submitted for the Record for the
United States House Ways & Means Oversight Subcommittee Hearing on
the Impact of Complexity in the Tax Code on
Individual Taxpayers and Small Businesses**

May 25, 1999

Introduction and Overview

This testimony outlines the comments and suggestions of the American Network of Community Options and Resources ("ANCOR") relating to the current complexity of section 131 of the Code of 1986, as amended (the "Code"), which provides rules on the tax treatment of foster care payments received by individual taxpayers.

ANCOR was formed in 1970 to improve the quality of life of persons with disabilities and their families by coordinating the efforts of concerned providers of private support services. ANCOR is comprised of more than 650 organizations from across the United States together providing community support to more than 150,000 individuals with disabilities.

ANCOR strongly recommends that section 131 of the Code be amended to eliminate current law's complexity by uniformly allowing individual taxpayers to exclude from income the foster care payments they receive from State and local governmental sources. ANCOR believes that amending section 131 in this manner would (i) simplify the tax treatment of foster care payments for individual taxpayers, (ii) eliminate an impediment to State and local governmental efforts to reduce bureaucracy and costs for their foster care programs, and (iii) support State and local

governmental efforts to encourage much-needed individuals to participate in foster care programs.

Description of Current Law and Proposal

Current Law.

Section 131 of the Code as it currently exists creates a complex dichotomy in the tax treatment of individuals who serve as foster care providers for individuals in foster care under 19 years of age and for those who provide treatment to individuals in foster care over 19 years of age. For children under 19 years old, section 131 of the Code permits individual taxpayers to exclude foster care payments from taxable income when a government entity or charitable tax-exempt organization directly places the child and makes the foster care payments to the provider. For individuals 19 years of age or older, section 131 allows an individual taxpayer to exclude foster care payments from taxable income only when a governmental entity makes the placement and the payment. Thus, an individual's ability to exclude foster care payments, even if all such payments are derived from government funds, is linked to the type of agency that places the individual with the provider.

Proposed Change.

Congress should amend section 131 to allow all individuals who serve as providers of foster care the ability to exclude from income those foster care payments that they receive from a governmental source, regardless of whether a governmental entity placed the individual, provided that a governmental entity has either certified or licensed the placement agency. Amending section 131 in such a way would not only simplify the tax treatment of foster care payments and reduce the administrative burden on the Internal Revenue Service ("IRS"), but the change would also support the efforts of State and local governments to address the needs of their communities more effectively.

A. Current law is confusing to taxpayers and to the IRS.

As illustrated by Table 1, incongruent treatment of individual taxpayers who are foster care providers has created a complex system for determining when such providers can exclude their foster care payments from income.

Table 1- Excludability of Foster Care Payments from Income Under Section 131

Placement Agency	Payor	Age of Foster Care Individual	Payment Excludable?
State or political subdivision	State or political subdivision	<19 years	Yes
State or political subdivision	State or political subdivision	≥19 years	Yes
State or political subdivision	501(c)(3)	<19 years	Yes
State or political subdivision	501(c)(3)	≥19 years	No
State or political subdivision	Not 501(c)(3)	<19 years	No
State or political subdivision	Not 501(c)(3)	≥19 years	No
Licensed 501(c)(3)	State or political subdivision	<19 years	Yes
Licensed 501(c)(3)	State or political subdivision	≥19 years	No
Licensed 501(c)(3)	501(c)(3)	<19 years	Yes
Licensed 501(c)(3)	501(c)(3)	≥19 years	No
Licensed 501(c)(3)	Not 501(c)(3)	<19 years	No
Licensed 501(c)(3)	Not 501(c)(3)	≥19 years	No
Not 501(c)(3)	State or political subdivision	<19 years	No
Not 501(c)(3)	State or political subdivision	≥19 years	No
Not 501(c)(3)	501(c)(3)	<19 years	No
Not 501(c)(3)	501(c)(3)	≥19 years	No
Not 501(c)(3)	Not 501(c)(3)	<19 years	No
Not 501(c)(3)	Not 501(c)(3)	≥19 years	No

The confusion presented by current law is exemplified by the recent Tax Court decision in *Micorescu v. Commissioner*, T.C. Memo 1998-398. In *Micorescu*, the court held that an Oregon family providing foster care services to adults in the family's home could not exclude from income payments received from the private agency that placed the individuals with the family. The court reasoned that because the adult individuals were placed with the family by a private agency rather than by the State or an agency of the State, those individuals were not "qualified foster individuals" within the meaning of section 131. The court reached this conclusion even though the organization that placed the adults in the family's home both contracted with and received funds from the State of Oregon. Equal treatment of all families providing foster care services (i) who receive payments from an agency that operates under a license or certification by a government entity or (ii) who receive payments directly from a government entity would reduce the confusion that currently exists. Provider families, like the family involved in the *Micorescu* case, would know with certainty whether they could exclude their income.

Individual taxpayers are not alone in their confusion. Section 131 has proven so confusing that our members have reported many instances in which IRS officials and experienced certified public accountants and tax attorneys also have difficulty ascertaining when a payment is excludable. Our members can cite various examples of situations in which individual providers have been told informally by an IRS official and/or an experienced tax advisor that their foster care payments were to be excluded from taxable income, when in fact those payments were not excludable. Amending section 131 would, therefore, prevent not only the confusion individuals and their tax

advisors have over whether foster care payments are excludable, but also the confusion experienced by the IRS officials that are charged with administering the law.

B. Current law fails to support the decisions of State and local governments.

Governmental entities are becoming increasingly reliant on private agencies to place both children and adults with special needs in foster care. Governmental entities have found that foster care for adults with special needs reduces the expense that is usually incurred when maintaining group homes and institutional settings. In particular, the National Association of State Directors of Developmental Disabilities Services has found that over the past several years there has been a considerable increase in pressure on state agencies to reduce waiting lists. Additionally, State and local governments often use outside entities to make case-specific decisions (such as identification of those individuals who would benefit from foster care and those providers with whom such individuals should be placed) as a means of reducing bureaucracy in an already trying situation. Current law, however, fails to provide the same tax treatment to those individuals identified by private entities acting under a license or certification with States, counties and municipalities as is provided to individuals that are identified directly by the State. Disparate treatment exists despite the fact that from the governmental entities' perspectives, the activities are the same. As a result of the difference in treatment, State and local governments are discouraged from contracting with private agencies to make placement decisions. The tax code should support State and local governments that decide to cut costs, reduce bureaucracy and support individuals with special needs in their communities through expanding their foster care programs.

C. Current treatment of foster care payments discourages much-needed individuals from participating in foster care programs.

The confusion created by section 131's complex rules discourages many potential foster care individuals from participating in these programs. Despite the fact that individual taxpayers could, under these rules, offset taxable foster care payments (paid by non-qualified agencies) by treating expenditures made on behalf of a foster individual as a business expense deductions, such deductions are permitted only if the families maintain detailed expense records. Accordingly, otherwise willing providers are discouraged from accepting foster individuals placed by non-qualified agencies, because such providers are forced to endure the time and inconvenience associated with keeping extensive records. The result is a smaller pool of available, qualified and willing providers and a growing pool of individuals with special needs for whom group housing or institutional living is inappropriate. Amending section 131 as suggested would help address the increasing demand for providers of foster care services.

D. Legislation introduced this year would remedy these problems.

Bills were introduced in the House (H.R. 1194) and in the Senate (S. 670) that propose to simplify the current rules under section 131 for individuals receiving foster care payments. These bills would allow individual providers to exclude from income foster care payments received, regardless of the age of the individual in foster care and the type of entity that placed that individual. The exclusion would apply *only if* either (i) a state or local government or (ii) a "qualified foster care placement agency" made the foster care payments. Such payments would have to be made pursuant to a foster care program of such governmental entity. Further, to be qualified, a foster care placement entity would have to be licensed or certified by a state or local government to make foster care payments to providers of foster care.

Conclusion

ANCOR recommends amending section 131 of the Internal Revenue Code so that all governmental foster care payments received by individual taxpayer providers are treated the same. If enacted, current law's confusing and unfair tax rules would no longer discourage much-needed individual providers from participating in foster care programs. Amending section 131 in this fashion also will support State and local governments in their efforts to reduce bureaucracy and cut costs, provide more alternatives to institutionalization, while simplifying tax administrative burdens.

June 28, 1999

The Honorable Bill Archer
U.S. House of Representatives
1236 Longworth House Office Building
Washington, DC 20515-4307

Re: H.R.1194 (Simplification of Tax Treatment of Foster Care Payments)

Dear Chairman Archer:

We are writing to you in support of H.R.1194, which has been introduced by Representative Ron Lewis. Senators Jeffords and Dodd simultaneously introduced an identical bill, S.670, in the Senate.

H.R.1194 is designed to simplify and correct inequities in the current tax treatment of foster care payments. We respectfully request that you support this important legislation as part of the next appropriate vehicle.

Current law discourages families from providing foster care. Foster care providers are reluctant to contract with private (non-governmental) placement agencies because such providers are required by current law to include foster care payments as taxable income (unless the foster individual is under 19 years and the placement agency is a nonprofit organization), while providers who care for foster individuals placed in their homes by the government are permitted to exclude foster care payments from taxable income. In addition, due to the complexity of current law, foster care providers receive conflicting advice with respect to whether a particular payment may be excludable from taxable income.

H.R.1194 simplifies the tax treatment of foster care payments and thereby removes the inequities and uncertainties present in the current tax law. We strongly encourage your support of H.R.1194, which will advance the development of family-based foster care services.

American Network of Community Options and Resources (ANCOR)

American Congress of Community Supports and Employment Services

The Arc of Illinois

The Arc of Texas

Association of Developmental Disabilities Community Providers (New Mexico)

Association of Developmental Disabilities Providers (Massachusetts)

The Association for Individual Development (Illinois)

Association of Residential Resources in Minnesota

Bazelon Center for Mental Health Law

Child Care Association of Illinois

Community and Residential Services Association (Louisiana)

Connecticut Association of Nonprofits

Connecticut Community Providers Association

Easter Seals

Illinois Association of Rehabilitation Facilities

Indiana Association of Rehabilitation Facilities
Iowa Association of Community Providers
Lutheran Services in America
National Association of Developmental Disabilities Councils
National Association of State Directors of Developmental Disabilities Services, Inc.
Nebraska Association of Private Resources
New York State Association of Community and Residential Agencies
Ohio Provider Resource Association
Oklahoma Network of Community Options and Resources
Oregon Rehabilitation Association
Pennsylvania Association of Resources for People with Mental Retardation
Private Providers Association of Texas
Private Provider Network (New Hampshire)
Utah Association of Community Services
United Way of Illinois
Vermont Council of Developmental and Mental Health Services

June 28, 1999

The Honorable William Roth
U.S. Senate
219 Dirksen Senate Office Building
Washington, DC 20510

Re: S. 670 (Simplification of Tax Treatment of Foster Care Payments)

Dear Chairman Roth:

We are writing to you in support of S. 670, which has been introduced by Senators Jeffords and Dodd. Representative Ron Lewis simultaneously introduced an identical bill, H.R. 1194, in the House.

S. 670 is designed to simplify and correct inequities in the current tax treatment of foster care payments. We respectfully request that you support this important legislation as part of the next appropriate vehicle.

Current law discourages families from providing foster care. Foster care providers are reluctant to contract with private (non-governmental) placement agencies because such providers are required by current law to include foster care payments as taxable income (unless the foster individual is under 19 years and the placement agency is a nonprofit organization), while providers who care for foster individuals placed in their homes by the government are permitted to exclude foster care payments from taxable income. In addition, due to the complexity of current law, foster care providers receive conflicting advice with respect to whether a particular payment may be excludable from taxable income.

S.670 simplifies the tax treatment of foster care payments and thereby removes the inequities and uncertainties present in the current tax law. We strongly encourage your support of S. 670, which will advance the development of family-based foster care services.

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Oklahoma Network of Community Options and Resources
Oregon Rehabilitation Association
Pennsylvania Association of Resources for People with Mental Retardation
Private Providers Association of Texas
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Utah Association of Community Services
United Way of Illinois
Vermont Council of Developmental and Mental Health Services