August 10, 2001

Mr. John Angell
Majority Staff Director
Senate Finance Committee
United States Senate
219 Dirksen Office Building
Washington, DC  20510

Mr. Kolan Davis
Republican Staff Director/Chief Counsel
Senate Finance Committee
United States Senate
219 Dirksen Office Building
Washington, DC  20510

Re: Tax Code Complexity Hearing

Dear Messrs. Angell and Davis:

This letter is sent in response to a request from Senator Grassley that I submit additional information discussing my recommendations for reducing complexity in calculating taxes on capital gain income.

The capital gain regime applicable to individuals is excessively complex. Seventeen different rates of tax may apply to capital gain income. Individuals with net capital gain compute their tax liability by completing a 36-line tax computation on Schedule D of Form 1040. For taxable years beginning after 2000, additional lines will be needed to take into account five-year gains.

In our testimony, we noted that the taxation of capital gain would be simplified by establishing a single preferential rate and a single long-term holding period for all types of capital assets. Alternatively, in order to assure that the benefit is extended to all taxpayers regardless of their tax bracket, the special capital gain rate might be replaced by an exclusion for a specified percentage of long-term capital gain.

The Joint Committee on Taxation recommended in its simplification study that the current rate system for capital gain be replaced with a deduction for a fixed percentage of net capital gain. The recommendation would reinstate a deduction

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2 Net capital gain is the excess of the net long-term capital gain for the taxable year over the net short-term capital loss for the year. I.R.C. § 1211(b).
similar to the capital gain deduction in effect prior to the Tax Reform Act of 1986, and is substantively equivalent to the exclusion we recommended in our testimony.\(^3\)

The enactment of any of these recommendations would be a significant step in reducing complexity for individual taxpayers.

Very truly yours,

Richard M. Lipton  
Chair, Section of Taxation

cc: Senator Charles Grassley

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