1996 Tax Legislation

Internal Revenue cumulative bulletin 1996–3

Department of the Treasury
Internal Revenue Service

In This Issue

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenue at the least cost; serve the public by continually improving the quality of our products and services; and perform in a manner warranting the highest degree of public confidence in our integrity, efficiency, and fairness.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

These principles of tax administration were previously published in the Internal Revenue Bulletin as Revenue Procedure 64–22, 1964–1 (Part 1) C.B. 689. They are restated here to emphasize their importance to all employees of the Internal Revenue Service.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

Cumulative Bulletin 1996–1 is a consolidation of all items of permanent nature published in the weekly Bulletins 1996–1 through 1996–26 for the period of January 1 through June 30, 1996.

The Internal Revenue Cumulative Bulletin is divided into four parts as follows:

Part I.—1986 Code.

This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.

This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.

To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Notice of Proposed Rulemaking.

The preambles and text of proposed regulations that were published in the **Federal Register** during this six month period are printed in this section. Included in this section is a list of person disbarred or suspended from practice before the Internal Revenue Service.

1996 PUBLIC LAWS

BOSNIA	=	Tax Benefits for Individuals Performing Services in Certain Hazardous Duty Areas (P.L. 104–117)
HIPPA	=	Health Insurance Portability and Accountability Act of 1996 (P.L. 104–191)
OCRA 96	=	Omnibus Consolidation Recissions and Appropriations Act of 1996 (P.L. 104–134)
SBJPA	=	Small Business Job Protection Act of 1996 (P.L. 104–188)
TBOR2	=	Taxpayer Bill of Rights 2 (P.L. 104–168)
WELFARE	=	Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (P.L. 104–193)

1986 Code Sections Added, Amended, or Repealed by Public Laws 104–117, 104–134, 104–168, 104–188, 104–191, and 104–193

The following sections of the Internal Revenue Code of 1986 are affected by the Health Insurance Portability and Accountability Act of 1996, the Omnibus Consolidated Recissions and Appropriations Act of 1996, the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, the Small Business Job Protection Act of 1996, the Tax Benefits for Individuals Performing Services in Certain Hazardous Duty Areas, and the Taxpayers Bill of Rights 2.

1986 Code Section	Law	Act Section
1(g)(7)(A)(ii)	SBJPA	1704(m)(1)
1(g)(7)(B)	SBJPA	1704(m)(2)(A)
	SBJPA	1704(m)(2)(B)
21(e)(10)	SBJPA	1615(b)
23	SBJPA	1807(a)
25(e)(1)(C)	SBJPA	1807(c)(1)
26(b)(2)(M)	SBJPA	1621(b)(1)
26(b)(2)(N)	SBJPA	1621(b)(1)
26(b)(2)(O)	SBJPA	1621(b)(1)
28	SBJPA	1205(a)(1)
28(b)(1)(D)	SBJPA	1204(e)
29(b)(6)(A)	SBJPA	1205(d)(3)
29(g)(1)(A)	SBJPA	1207(a)
30(b)(3)(A)	SBJPA	1205(d)(4)
30(d)(i)	SBJPA	1704(j)(4)(A)
30(d)(ii)	SBJPA	1704(j)(4)(A)
30A	SBJPA	1601(b)(1)
32(a)(2)(B)	WELFARE	910(a)
32(b)(2)	WELFARE	909(a)(3)
32(c)(1)(C)	WELFARE	910(a)
32(c)(1)(F)	WELFARE	451(a)
32(c)(5)	WELFARE	910(b)
32(f)(2)(B)	WELFARE	910(a)
32(i)(1)	WELFARE	909(a)(1)
32(i)(2)(B)	WELFARE	909(b)
32(i)(2)(C)	WELFARE	909(b)
32(i)(2)(D)	WELFARE	909(b)
32(i)(2)(E)	WELFARE	909(b)
32(j)	WELFARE	909(a)(2)
32(l)	WELFARE	451(b)
34(a)(3)	SBJPA	1606(b)
38(b)(2)	SBJPA	1201(e)(1)
38(b)(10)	SBJPA	1205(a)(2)
38(b)(11)	SBJPA	1205(a)(2)
38(b)(12)	SBJPA	1205(a)(2)
38(c)(2)(C)	SBJPA	1702(e)(4)
39(d)	SBJPA	1703(n)(1)(A)
	SBJPA	1703(n)(1)(B)
39(d)(7)	SBJPA	1205(c)
40(e)(1)(B)	SBJPA	1703(j)
41(b)(2)(D)(iii)	SBJPA	1201(e)(1)
	SBJPA	1201(e)(4)
41(b)(3)(C)	SBJPA	1204(d)
41(c)(3)(B)(i)	SBJPA	1204(b)
41(c)(4)	SBJPA	1204(c)
41(c)(5)	SBJPA	1204(c)
41(c)(6)	SBJPA	1204(c)
41(h)	SBJPA	1204(a)
42(c)(2)	SBJPA	1704(t)(64)
45B(b)(1)(A)	SBJPA	1112(a)(1)
45A(b)(1)(B)	SBJPA	1201(e)(1)
45B(b)(2)	SBJPA	1112(b)(1)
45C	SBJPA	1205(a)(1)
45C(a)	SBJPA	1205(d)(1)
45C(d)(2)	SBJPA	1205(d)(2)
45C(d)(3)	SBJPA	1205(d)(2)
45C(d)(4)	SBJPA	1205(d)(2)
45C(d)(5)	SBJPA	1205(d)(2)
45C(e)	SBJPA	1205(b)
50(a)(2)(C)	SBJPA	1704(t)(29)
50(a)(2)(E)	SBJPA	1702(h)(11)
50(d)	SBJPA	1616(b)(1)
51(a)	SBJPA	1201(a)
	SBJPA	1201(e)(1)
51(c)(1)	SBJPA	1201(f)
51(c)(4)	SBJPA	1201(d)
51(d)	SBJPA	1201(b)
51(d)(9)	WELFARE	110(l)(1)
51(g)	SBJPA	1201(e)(1)
51(i)(3)	SBJPA	1201(c)
51(j)	SBJPA	1201(e)(5)
52(e)(1)	SBJPA	1616(b)(2)
52(e)(2)	SBJPA	1616(b)(2)
52(e)(3)	SBJPA	1616(b)(2)
53(d)(1)(B)	SBJPA	1205(d)(5)(A)
	SBJPA	1205(d)(5)(B)
53(d)(1)(B)(iv)	SBJPA	1704(j)(1)
55(c)(1)	SBJPA	1401(b)(3)
	SBJPA	1601(b)(2)(A)
55(c)(2)	SBJPA	1205(d)(6)
56(d)(1)(B)(ii)	SBJPA	1702(e)(1)(A)
56(g)(4)(C)(ii)	SBJPA	1601(b)(2)(B)
	SBJPA	1704(t)(1)
56(g)(4)(C)(iii)	SBJPA	1601(b)(2)(C)
56(g)(4)(D)(iii)	SBJPA	1702(g)(4)
56(g)(4)(H)	SBJPA	1702(c)(1)
56(g)(4)(I)	SBJPA	1702(c)(1)
56(g)(4)(J)	SBJPA	1702(c)(1)
56(g)(6)	SBJPA	1621(b)(2)
57(a)(4)	SBJPA	1616(b)(3)
59(a)	SBJPA	1703(e)(1)
	SBJPA	1703(e)(2)
	SBJPA	1703(e)(3)
	SBJPA	1703(e)(4)

1986 Code Section	Law	Act Section
59(b)	SBJPA	1601(b)(2)(D)
59(j)(1)(B)	SBJPA	1704(m)(3)
59(j)(3)(B)	SBJPA	1702(a)(1)
62(a)(8)	SBJPA	1401(b)(4)
62(a)(16)	HIPPA	301(b)
72(b)(4)(A)	SBJPA	1704(l)(1)
72(d)	SBJPA	1403(a)
72(f)	SBJPA	1463(a)
72(m)(2)(A)	SBJPA	1704(t)(2)
72(m)(2)(B)	SBJPA	1704(t)(2)
72(m)(2)(C)	SBJPA	1704(t)(2)
72(p)(4)(A)(ii)	SBJPA	1704(t)(77)
72(t)(2)(B)	HIPPA	361(c)
72(t)(2)(D)	HIPPA	361(b)
72(t)(3)(A)	HIPPA	361(a)
72(t)(6)	SBJPA	1421(b)(4)(A)
86(b)(2)	SBJPA	1704(t)(3)
86(b)(2)(A)	SBJPA	1807(c)(2)
101(b)	SBJPA	1402(a)
101(c)	SBJPA	1402(b)(1)
101(g)	HIPPA	331(a)
104(a)	SBJPA	1605(b)
104(a)(2)	SBJPA	1605(a)
104(a)(3)	HIPPA	311(b)
104(c)	SBJPA	1605(c)
104(d)	SBJPA	1605(c)
106	HIPPA	301(c)(1)
106(c)	HIPPA	321(c)(2)
108(d)(9)(A)	SBJPA	1703(n)(2)
112	BOSNIA	1(a)
	SBJPA	1704(t)(4)(A)
	SBJPA	1704(t)(4)(B)
112(b)	BOSNIA	1(d)
112(c)	BOSNIA	1(d)
117(d)(2)(B)	SBJPA	1703(n)(14)
118(c)	SBJPA	1613(a)(1)(A)
	SBJPA	1613(a)(1)(B)
118(d)	SBJPA	1613(a)(1)(B)
118(e)	SBJPA	1613(a)(1)(A)
119(d)(4)	SBJPA	1123(a)
125(f)	HIPPA	301(d)
	HIPPA	321(c)(1)
127(c)(1)	SBJPA	1202(b)
127(d)	SBJPA	1202(a)
129(d)(8)(B)	SBJPA	1431(c)(1)(B)
133	SBJPA	1602(a)
135(b)(2)(B)(ii)	SBJPA	1703(d)
135(c)(4)(A)	SBJPA	1807(c)(2)
135(d)(1)(B)	SBJPA	1806(b)(1)
135(d)(1)(C)	SBJPA	1806(b)(1)
135(d)(1)(D)	SBJPA	1806(b)(1)
136(a)	SBJPA	1617(b)(1)
136(c)(1)	SBJPA	1617(a)
136(c)(2)	SBJPA	1617(b)(2)(A)
	SBJPA	1617(b)(2)(B)
137	SBJPA	1807(b)
138	SBJPA	1807(b)
142(f)(3)	SBJPA	1608(a)
143(d)(2)(C)	SBJPA	1703(n)(3)
143(m)(4)(C)(ii)	SBJPA	1702(d)(2)(A)
	SBJPA	1702(d)(2)(B)
	SBJPA	1702(d)(2)(C)
147(c)(2)(E)(i)	SBJPA	1117(b)
147(c)(2)(G)	SBJPA	1117(a)
149(g)(3)(B)(iii)	SBJPA	1704(b)(1)
150(d)(3)	SBJPA	1614(a)
151(d)(3)(C)(i)	SBJPA	1702(a)(2)
151(e)	SBJPA	1615(a)(1)
162(k)	SBJPA	1704(p)(3)
162(k)(1)	SBJPA	1704(p)(1)
162(k)(2)(A)(i)	SBJPA	1704(p)(2)
162(k)(2)(A)(ii)	SBJPA	1704(p)(2)
162(k)(2)(A)(iii)	SBJPA	1704(p)(2)
162(l)(1)	HIPPA	311(a)
162(l)(2)(C)	HIPPA	322(b)(2)(B)
163(j)(1)(B)	SBJPA	1704(f)(2)(A)
163(j)(6)(E)(ii)	SBJPA	1703(n)(4)
163(j)(7)	SBJPA	1704(f)(2)(B)
163(j)(8)	SBJPA	1704(f)(2)(B)
164(a)(4)	SBJPA	1704(t)(79)
164(a)(5)	SBJPA	1704(t)(79)
167(g)	SBJPA	1604(a)
167(h)	SBJPA	1604(a)
168(b)(3)(F)	SBJPA	1613(b)(1)
168(c)(1)	SBJPA	1613(b)(2)
168(e)(3)(B)	SBJPA	1702(h)(1)(B)
168(e)(3)(B)(vi)	SBJPA	1702(h)(1)(A)
168(e)(3)(E)(i)	SBJPA	1120(a)
168(e)(3)(E)(ii)	SBJPA	1120(a)
168(e)(3)(E)(iii)	SBJPA	1120(a)
168(e)(3)(F)	SBJPA	1613(b)(3)(B)
168(e)(5)	SBJPA	1613(b)(3)(A)
168(g)(2)(C)(iv)	SBJPA	1613(b)(4)
168(g)(3)	SBJPA	1613(b)(3)(B)
168(g)(3)(B)	SBJPA	1120(b)
168(g)(4)(K)	SBJPA	1702(h)(1)(C)
168(i)(8)	SBJPA	1121(a)
170(e)(1)	SBJPA	1316(b)
170(e)(5)(D)	SBJPA	1206(a)
172(b)(1)(E)(ii)	SBJPA	1702(h)(2)
172(h)(3)(B)(i)	SBJPA	1704(t)(5)
172(h)(4)(B)	SBJPA	1704(t)(30)
172(h)(4)(C)	SBJPA	1702(h)(16)
179(b)(1)	SBJPA	1111(a)
179(d)(1)	SBJPA	1702(h)(10)
	SBJPA	1702(h)(19)
179A(f)	SBJPA	1704(j)(2)
179A(g)	SBJPA	1704(j)(2)
196(c)	SBJPA	1201(e)(1)
213(d)(1)	HIPPA	322(b)(2)(A)
213(d)(1)(B)	HIPPA	322(a)
213(d)(1)(C)	HIPPA	322(a)

1986 Code Section	Law	Act Section
213(d)(1)(D)	HIPPA	322(a)
	HIPPA	322(b)(1)
213(d)(6)	HIPPA	322(b)(3)(A)
	HIPPA	322(b)(3)(B)
213(d)(7)	HIPPA	322(b)(4)
213(d)(10)	HIPPA	322(b)(2)(C)
213(d)(11)	HIPPA	322(b)(2)(C)
219(b)(4)	SBJPA	1421(b)(1)(A)
219(c)	SBJPA	1427(a)
219(f)(2)	SBJPA	1427(b)(1)
219(g)(1)	SBJPA	1427(b)(2)
219(g)(3)(A)	SBJPA	1807(c)(3)
219(g)(5)(A)(iv)	SBJPA	1421(b)(1)(B)
219(g)(5)(A)(vi)	SBJPA	1421(b)(1)(B)
220	HIPPA	301(a)
221	HIPPA	301(a)
243(b)(2)	SBJPA	1702(h)(8)
243(b)(3)(A)	SBJPA	1702(h)(4)
246(f)	SBJPA	1616(b)(4)
264(a)(4)	HIPPA	501(a)(1)
	HIPPA	501(a)(2)
	HIPPA	501(b)(1)
264(d)	HIPPA	501(b)(2)
280A(c)(1)(A)	SBJPA	1704(t)(39)
280A(c)(2)	SBJPA	1113(a)
280C(b)	SBJPA	1205(d)(7)(A)
	SBJPA	1205(d)(7)(B)
	SBJPA	1205(d)(7)(C)
280F(a)	SBJPA	1702(h)(5)
280G(b)(6)(B)	SBJPA	1421(b)(9)(A)
280G(b)(6)(C)	SBJPA	1421(b)(9)(A)
280G(b)(6)(D)	SBJPA	1421(b)(9)(A)
291(e)(1)(B)(i)	SBJPA	1616(b)(5)
291(e)(1)(B)(iv)	SBJPA	1602(b)(1)
291(e)(1)(B)(v)	SBJPA	1602(b)(1)
341(f)(3)	SBJPA	1702(h)(7)
355(d)(7)(A)	SBJPA	1704(t)(31)
382(l)(4)(B)(ii)	SBJPA	1621(b)(3)
401(a)(5)(D)(ii)	SBJPA	1431(c)(1)(B)
401(a)(5)(F)	SBJPA	1445(a)
401(a)(9)(C)	SBJPA	1404(a)
401(a)(17)(A)	SBJPA	1431(b)(2)
401(a)(20)	SBJPA	1704(t)(67)
401(a)(26)(A)	SBJPA	1432(a)
401(a)(26)(G)	SBJPA	1432(b)
401(a)(28)(B)(v)	SBJPA	1401(b)(5)
401(d)	SBJPA	1441(a)
401(k)(3)(A)	SBJPA	1433(c)(1)(A)
	SBJPA	1433(c)(1)(B)
	SBJPA	1433(c)(1)(C)
401(k)(3)(E)	SBJPA	1433(d)(1)
401(k)(3)(F)	SBJPA	1459(a)
401(k)(4)(B)	SBJPA	1426(a)
401(k)(7)(B)(i)	SBJPA	1443(b)
401(k)(7)(C)	SBJPA	1443(a)
401(k)(8)(C)	SBJPA	1433(e)(1)

1986 Code Section	Law	Act Section
401(k)(10)(B)(ii)	SBJPA	1401(b)(6)
401(k)(11)	SBJPA	1422(a)
401(k)(12)	SBJPA	1433(a)
401(m)(2)(A)	SBJPA	1433(c)(2)(A)
	SBJPA	1433(c)(2)(B)
	SBJPA	1433(c)(2)(C)
401(m)(3)	SBJPA	1433(d)(2)
401(m)(5)(C)	SBJPA	1459(b)
401(m)(6)(C)	SBJPA	1433(e)(2)
401(m)(10)	SBJPA	1422(b)
401(m)(11)	SBJPA	1422(b)
	SBJPA	1433(b)
401(m)(12)	SBJPA	1433(b)
402(c)(10)	SBJPA	1401(b)(2)
402(d)	SBJPA	1401(a)
402(e)(3)	SBJPA	1450(a)(2)
402(e)(4)(D)	SBJPA	1401(b)(1)
402(e)(5)	SBJPA	1401(b)(13)
402(g)(3)(A)	SBJPA	1704(t)(68)
402(g)(3)(B)	SBJPA	1421(b)(9)(B)
402(g)(3)(C)	SBJPA	1421(b)(9)(B)
402(g)(3)(D)	SBJPA	1421(b)(9)(B)
402(k)	SBJPA	1421(b)(3)(A)
403(b)	SBJPA	1450(a)(1)
403(b)(1)(E)	SBJPA	1450(c)(1)
403(b)(10)	SBJPA	1704(t)(69)
404(a)(2)	SBJPA	1704(t)(76)
404(a)(9)(C)	SBJPA	1316(d)(1)
404(a)(10)	SBJPA	1461(b)
404(j)(1)	SBJPA	1704(q)(1)
404(k)(1)	SBJPA	1316(d)(2)
404(l)	SBJPA	1431(b)(3)
404(m)	SBJPA	1421(b)(2)
406(c)	SBJPA	1401(b)(7)
406(e)(2)	SBJPA	1402(b)(2)
406(e)(3)	SBJPA	1402(b)(2)
407(c)	SBJPA	1401(b)(8)
407(e)(2)	SBJPA	1402(b)(2)
407(e)(3)	SBJPA	1402(b)(2)
408(d)(3)(G)	SBJPA	1421(b)(3)(B)
408(d)(5)	SBJPA	1427(b)(3)
408(i)	SBJPA	1421(b)(6)
	SBJPA	1455(b)(1)
408(k)(2)(C)	SBJPA	1431(c)(1)(B)
408(k)(6)(H)	SBJPA	1421(c)
408(l)	SBJPA	1421(b)(5)(B)
408(l)(2)	SBJPA	1421(b)(5)(A)
408(p)	SBJPA	1421(a)
411(a)(2)	SBJPA	1442(a)(1)
	SBJPA	1442(a)(2)
414(b)	SBJPA	1421(b)(9)(C)
414(c)	SBJPA	1421(b)(9)(C)
414(e)(5)	SBJPA	1461(a)
414(m)(4)(B)	SBJPA	1421(b)(9)(C)
414(n)(2)(C)	SBJPA	1454(a)
414(n)(3)(B)	SBJPA	1421(b)(9)(C)

1986 Code Section	Law	Act Section
414(q)(1)	SBJPA	1431(a)
414(q)(2)	SBJPA	1431(c)(1)(A)
414(q)(3)	SBJPA	1431(c)(1)(A)
414(q)(4)	SBJPA	1431(c)(1)(A)
	SBJPA	1434(b)(1)
414(q)(5)	SBJPA	1431(c)(1)(A)
	SBJPA	1431(c)(1)(E)
414(q)(6)	SBJPA	1431(b)(1)
414(q)(7)	SBJPA	1431(c)(1)(A)
	SBJPA	1462(a)
414(q)(8)	SBJPA	1431(c)(1)(A)
414(q)(9)	SBJPA	1431(c)(1)(A)
414(q)(10)	SBJPA	1431(c)(1)(A)
414(q)(11)	SBJPA	1431(c)(1)(A)
414(q)(12)	SBJPA	1431(c)(1)(A)
414(r)(2)(A)	SBJPA	1431(c)(1)(D)
414(s)(2)	SBJPA	1434(b)(2)
414(u)	SBJPA	1704(n)(1)
415(a)(1)(A)	SBJPA	1452(c)(1)(A)
415(a)(1)(B)	SBJPA	1452(c)(1)(B)
415(a)(1)(C)	SBJPA	1452(c)(1)(C)
415(b)(10)(C)	SBJPA	1444(d)(2)
415(b)(10)(C)(ii)	SBJPA	1444(d)(1)
415(b)(11)	SBJPA	1444(a)
415(b)(2)(E)	SBJPA	1449(b)(1)
	SBJPA	1449(b)(2)
415(b)(2)(I)	SBJPA	1444(c)
415(b)(5)(B)	SBJPA	1452(c)(2)
415(c)(3)(C)	SBJPA	1446(a)
415(c)(3)(D)	SBJPA	1434(a)
415(e)	SBJPA	1452(a)
415(f)(1)	SBJPA	1452(c)(3)
415(g)	SBJPA	1452(c)(4)
415(k)(1)(C)	SBJPA	1704(t)(75)
415(k)(1)(D)	SBJPA	1704(t)(75)
415(k)(1)(E)	SBJPA	1704(t)(75)
415(k)(1)(F)	SBJPA	1704(t)(75)
415(k)(2)(A)(i)	SBJPA	1452(c)(5)
415(k)(2)(A)(ii)	SBJPA	1452(c)(6)
415(m)	SBJPA	1444(b)(1)
416(g)(4)(G)	SBJPA	1421(b)(7)
416(h)	SBJPA	1452(c)(7)
416(i)(1)(A)	SBJPA	1431(c)(1)(C)
416(i)(1)(D)	SBJPA	1431(c)(1)(B)
417(a)(2)	SBJPA	1457(a)
417(a)(7)	SBJPA	1451(a)
419A(c)(3)	SBJPA	1704(t)(60)
420(e)(1)(C)	SBJPA	1704(t)(32)
424(c)(3)(B)	SBJPA	1702(h)(13)
457(b)(6)	SBJPA	1448(b)
457(c)(2)(B)(i)	SBJPA	1421(b)(3)(C)
457(e)(9)	SBJPA	1447(a)
457(e)(11)	SBJPA	1458(a)
457(e)(14)	SBJPA	1444(b)(2)
457(e)(15)	SBJPA	1447(b)
457(f)(2)(C)	SBJPA	1444(b)(3)
457(f)(2)(D)	SBJPA	1444(b)(3)
457(f)(2)(E)	SBJPA	1444(b)(3)
457(g)	SBJPA	1448(a)
460(b)(1)	SBJPA	1704(t)(28)
460(e)(6)(B)	SBJPA	1702(h)(15)
461(i)(3)(C)	SBJPA	1704(t)(78)
469(c)(3)(B)	SBJPA	1704(d)(1)
469(g)(1)(A)	SBJPA	1704(e)(1)
469(i)(3)(E)(ii)	SBJPA	1807(c)(4)
501(c)(4)	TBOR2	1311(b)(1)
501(c)(21)(D)(ii)	SBJPA	1704(j)(5)
501(c)(26)	HIPPA	341(a)
501(c)(27)	HIPPA	342(a)
501(n)	SBJPA	1114(a)
501(o)	SBJPA	1114(a)
512(b)(17)	SBJPA	1603(a)
512(d)	SBJPA	1115(a)
512(e)	SBJPA	1316(c)
529	SBJPA	1806(a)
537(b)(4)	SBJPA	1704(t)(33)
543(a)(2)(B)(ii)	SBJPA	1704(t)(6)
582(c)(1)	SBJPA	1621(b)(4)
584(h)	SBJPA	1805(a)
584(i)	SBJPA	1805(a)
585(a)(2)(A)	SBJPA	1616(b)(6)
593(e)(1)	SBJPA	1616(b)(7)(A)
	SBJPA	1616(b)(7)(C)
	SBJPA	1616(b)(7)(D)
	SBJPA	1616(b)(7)(E)
593(e)(1)(B)	SBJPA	1616(b)(7)(B)
593(f)	SBJPA	1616(a)
593(g)	SBJPA	1616(a)
595	SBJPA	1616(b)(8)
596	SBJPA	1616(b)(9)
613(e)(1)(B)	SBJPA	1704(t)(34)
613A(c)(3)(A)(i)	SBJPA	1702(e)(2)
641(d)	SBJPA	1302(d)
642(g)	SBJPA	1704(t)(8)
643(a)(7)	SBJPA	1906(b)
643(h)	SBJPA	1904(c)(1)
643(i)	SBJPA	1906(c)(1)
665(c)	SBJPA	1904(c)(2)
665(d)(2)	SBJPA	1904(b)(1)
668(a)	SBJPA	1906(a)
672(c)	SBJPA	1904(a)(2)
672(f)	SBJPA	1904(a)(1)
679(a)	SBJPA	1903(b)
679(a)(2)(B)	SBJPA	1903(a)(1)
679(a)(3)	SBJPA	1903(a)(2)
679(a)(4)	SBJPA	1903(c)
679(a)(5)	SBJPA	1903(c)
679(c)(2)(A)	SBJPA	1903(e)
679(c)(3)	SBJPA	1903(d)
679(d)	SBJPA	1903(f)
691(c)(5)	SBJPA	1401(b)(9)
724(d)(3)(B)	SBJPA	1704(t)(63)

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805(a)(4)(E)	SBJPA	1702(h)(3)
807(d)(3)(A)(iii)	HIPPA	321(b)
807(d)(3)(B)(ii)	SBJPA	1704(t)(61)
812(g)	SBJPA	1602(b)(2)
817(d)(2)(A)	SBJPA	1611(a)(1)
817(d)(2)(B)	SBJPA	1611(a)(1)
817(d)(2)(C)	SBJPA	1611(a)(1)
817(d)(3)(A)	SBJPA	1611(a)(2)
817(d)(3)(B)	SBJPA	1611(a)(2)
817(d)(3)(C)	SBJPA	1611(a)(2)
817A	SBJPA	1612(a)
818(g)	HIPPA	332(a)
832(b)(5)(C)(ii)	SBJPA	1702(h)(3)
832(b)(5)(D)(ii)	SBJPA	1702(h)(3)
833(c)(4)	HIPPA	351(a)
848(e)(1)(B)(ii)	HIPPA	301(h)
848(e)(1)(B)(iii)	HIPPA	301(h)
848(e)(1)(B)(iv)	HIPPA	301(h)
852(b)(5)(C)	SBJPA	1602(b)(3)
856(a)(4)	SBJPA	1704(t)(35)
856(c)(6)(E)	SBJPA	1621(b)(5)
860E(a)	SBJPA	1616(b)(10)(A)
	SBJPA	1616(b)(10)(B)
	SBJPA	1616(b)(10)(C)
	SBJPA	1616(b)(10)(D)
860E(a)(6)	SBJPA	1704(h)(1)
860F(a)(5)	SBJPA	1704(t)(74)
860G(a)(3)(B)	SBJPA	1621(b)(6)
860G(a)(3)(C)	SBJPA	1621(b)(6)
860G(a)(3)(D)	SBJPA	1621(b)(6)
860H	SBJPA	1621(a)
860I	SBJPA	1621(a)
860J	SBJPA	1621(a)
860K	SBJPA	1621(a)
860L	SBJPA	1621(a)
865(b)(2)	SBJPA	1704(f)(4)(A)
871(b)(1)	SBJPA	1401(b)(10)
871(f)(2)(B)	SBJPA	1954(b)(1)
877(a)	HIPPA	511(a)
	HIPPA	511(d)(2)
877(b)	SBJPA	1401(b)(11)
	HIPPA	511(d)(1)
877(b)(1)	HIPPA	511(b)(2)
877(c)	HIPPA	511(b)(1)
877(d)	HIPPA	511(b)(1)
	HIPPA	511(c)
877(e)	HIPPA	511(f)(1)
877(f)	HIPPA	511(f)(1)
884(f)(1)	SBJPA	1704(f)(3)(A)
884(f)(1)(B)	SBJPA	1704(f)(3)(A)
884(f)(2)	SBJPA	1704(f)(3)(A)
897(f)	SBJPA	1702(g)(2)
901(b)(5)	SBJPA	1904(b)(2)
904(d)(3)(G)	SBJPA	1501(b)(1)
	SBJPA	1501(b)(12)
	SBJPA	1703(i)(1)
904(f)(2)(B)(i)	SBJPA	1704(t)(36)
907(c)(4)(B)(iii)	SBJPA	1704(t)(36)
936(a)(4)(A)(ii)	SBJPA	1704(t)(80)
936(b)	SBJPA	1704(t)(37)
936(j)	SBJPA	1601(a)
951(a)(1)(A)	SBJPA	1501(a)(1)
951(a)(1)(B)	SBJPA	1501(a)(1)
951(a)(1)(C)	SBJPA	1501(a)(1)
956(b)(1)	SBJPA	1501(b)(2)
956(b)(3)	SBJPA	1501(b)(3)
956A	SBJPA	1501(a)(2)
956A(b)(1)	SBJPA	1703(i)(2)
956A(f)	SBJPA	1703(i)(3)
958(a)(1)	SBJPA	1704(t)(7)
958(b)	SBJPA	1703(i)(4)
959(a)	SBJPA	1501(b)(5)
959(a)(1)	SBJPA	1501(b)(4)
959(a)(2)	SBJPA	1501(b)(4)
959(a)(3)	SBJPA	1501(b)(4)
959(c)	SBJPA	1501(b)(6)
959(f)(1)	SBJPA	1501(b)(7)
959(f)(2)	SBJPA	1501(b)(8)
989(b)	SBJPA	1501(b)(9)
992(d)(3)	SBJPA	1616(b)(11)
1016(a)(24)	SBJPA	1807(c)(5)
1016(a)(25)	SBJPA	1807(c)(5)
1016(a)(26)	SBJPA	1807(c)(5)
1017(b)(4)(A)	SBJPA	1703(n)(5)
1033(b)	SBJPA	1610(a)
1033(h)	SBJPA	1119(b)(1)
	SBJPA	1119(b)(2)
	SBJPA	1119(b)(3)
1033(h)(2)	SBJPA	1119(a)
1033(h)(3)	SBJPA	1119(a)
1033(h)(4)	SBJPA	1119(a)
1038(f)	SBJPA	1616(b)(12)
1042(c)(1)(A)	SBJPA	1316(d)(3)
1042(c)(4)(A)(i)	SBJPA	1311(b)(3)
1042(c)(4)(B)(ii)	SBJPA	1616(b)(13)
1044(c)(2)	SBJPA	1703(a)
1201(a)	SBJPA	1703(f)
1202(e)(4)(C)	SBJPA	1621(b)(7)
1237(a)	SBJPA	1314(a)
1237(a)(2)(A)	SBJPA	1314(b)
1245(a)(3)	SBJPA	1703(n)(6)
1248(a)(i)	SBJPA	1702(g)(1)(A)
1248(a)(ii)	SBJPA	1702(g)(1)(A)
1248(e)(1)	SBJPA	1702(g)(1)(B)
1248(f)(1)(B)	SBJPA	1702(g)(1)(C)
1248(i)(l)	SBJPA	1702(g)(1)(D)
1250(e)(4)	SBJPA	1702(h)(18)
1274(b)(3)(B)(i)	SBJPA	1704(t)(78)
1274A(c)(1)(B)	SBJPA	1704(t)(62)
1277(c)	SBJPA	1616(b)(14)
1296(b)(2)(B)	SBJPA	1704(r)(1)
1296(b)(2)(C)	SBJPA	1704(r)(1)

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1296(b)(2)(D)	SBJPA	1704(r)(1)
1297(b)(9)	SBJPA	1501(b)(9)
	SBJPA	1501(b)(10)
1297(d)(2)	SBJPA	1703(i)(5)(B)
1297(d)(2)(A)	SBJPA	1703(i)(5)(A)
1297(d)(3)(B)	SBJPA	1501(b)(11)
1297(e)	SBJPA	1703(i)(6)
1297(e)(2)(B)(ii)	SBJPA	1501(b)(11)
1361(b)(1)(A)	SBJPA	1301
1361(b)(1)(B)	SBJPA	1316(a)(1)
1361(b)(2)(A)	SBJPA	1308(a)
	SBJPA	1315
1361(b)(2)(B)	SBJPA	1308(a)
	SBJPA	1616(b)(15)
1361(b)(2)(C)	SBJPA	1308(a)
1361(b)(2)(D)	SBJPA	1308(a)
1361(b)(2)(E)	SBJPA	1308(a)
1361(b)(3)	SBJPA	1308(b)
1361(c)(2)(A)	SBJPA	1303(1)
	SBJPA	1303(2)
1361(c)(2)(A)(v)	SBJPA	1302(a)
1361(c)(2)(B)(v)	SBJPA	1302(b)
1361(c)(5)(B)(iii)	SBJPA	1304
1361(c)(6)	SBJPA	1308(d)(1)
1361(c)(7)	SBJPA	1316(a)(2)
1361(e)	SBJPA	1302(c)
1361(e)(1)(A)(i)	SBJPA	1316(e)
1362(b)(5)	SBJPA	1305(b)
1362(d)(3)	SBJPA	1311(b)(1)(A)
	SBJPA	1311(b)(1)(B)
	SBJPA	1311(b)(1)(C)
1362(d)(3)(F)	SBJPA	1308(c)
1362(f)	SBJPA	1305(a)
1362(g)	SBJPA	1317(b)
1366(a)(1)	SBJPA	1302(e)
1366(d)(1)(A)	SBJPA	1309(a)(1)
1366(d)(3)(D)	SBJPA	1312
1366(g)	SBJPA	1307(c)(3)(A)
1367(a)(2)(E)	SBJPA	1702(h)(14)
1367(b)(4)	SBJPA	1313(a)
1368(d)	SBJPA	1309(a)(2)
1368(e)(1)(A)	SBJPA	1309(c)(1)
	SBJPA	1309(c)(2)
1368(e)(1)(C)	SBJPA	1309(b)
1371(a)	SBJPA	1310
1375	SBJPA	1311(b)(2)(C)
1375(a)(1)	SBJPA	1311(b)(2)(A)
1375(b)(3)	SBJPA	1311(b)(2)(B)
1377(a)(2)	SBJPA	1306
1377(b)(1)(A)	SBJPA	1307(a)
1377(b)(1)(B)	SBJPA	1307(a)
1377(b)(1)(C)	SBJPA	1307(a)
1377(b)(2)(A)	SBJPA	1307(b)
1377(b)(2)(B)	SBJPA	1307(b)
1377(b)(2)(C)	SBJPA	1307(b)
1394(e)(2)	SBJPA	1703(n)(7)(A)
	SBJPA	1703(n)(7)(B)
1396(c)(3)	SBJPA	1201(e)(4)
1397B(d)(5)(B)	SBJPA	1703(m)
1402(a)(8)	SBJPA	1456(a)
1445(e)(3)	SBJPA	1704(c)(1)
1463	SBJPA	1704(t)(9)
1491	SBJPA	1907(b)(1)
1494(c)	SBJPA	1902(a)
1504(b)(8)	SBJPA	1308(d)(2)
1504(c)(2)(B)(i)	SBJPA	1702(h)(6)
1561(a)	SBJPA	1703(f)
2102(c)(3)(A)	SBJPA	1704(f)(1)
2104(c)	SBJPA	1704(t)(38)
2107(a)	HIPPA	511(e)(1)(A)
2107(b)	HIPPA	511(e)(1)(C)
2107(c)(2)	HIPPA	511(e)(1)(B)
2107(c)(3)	HIPPA	511(e)(1)(B)
2107(d)	HIPPA	511(f)(2)(A)
2107(e)	HIPPA	511(f)(2)(A)
2501(a)(3)	HIPPA	511(e)(2)(A)
2501(a)(3)(E)	HIPPA	511(f)(2)(B)
2701(a)(3)(B)	SBJPA	1702(f)(1)(B)
2701(a)(3)(C)	SBJPA	1702(f)(1)(A)
2701(a)(4)(B)(i)	SBJPA	1702(f)(2)
2701(b)(2)(C)	SBJPA	1702(f)(3)(A)
2701(c)(1)(B)(i)	SBJPA	1702(f)(4)
2701(c)(3)(C)(i)	SBJPA	1702(f)(5)(A)
2701(c)(3)(C)(ii)	SBJPA	1702(f)(5)(B)
2701(d)(1)	SBJPA	1702(f)(1)(C)
2701(d)(3)(A)(iii)	SBJPA	1702(f)(6)
2701(d)(3)(B)(ii)	SBJPA	1702(f)(7)
2701(d)(4)	SBJPA	1702(f)(1)(C)
2701(d)(4)(C)	SBJPA	1702(f)(9)
2701(e)(3)(i)	SBJPA	1702(f)(3)(B)
2701(e)(3)(ii)	SBJPA	1702(f)(3)(B)
2701(e)(5)	SBJPA	1702(f)(8)(A)
	SBJPA	1702(f)(8)(B)
2701(e)(6)	SBJPA	1702(f)(10)
2702(a)(3)	SBJPA	1702(f)(11)(B)
2702(a)(3)(A)(i)	SBJPA	1702(f)(11)(A)
2702(a)(3)(A)(ii)	SBJPA	1702(f)(11)(A)
2702(a)(3)(A)(iii)	SBJPA	1702(f)(11)(A)
2702(a)(3)(A)(iv)	SBJPA	1702(f)(11)(A)
2702(a)(3)(B)	SBJPA	1702(f)(11)(B)
3121(a)(5)(F)	SBJPA	1421(b)(8)(A)
3121(a)(5)(G)	SBJPA	1421(b)(8)(A)
	SBJPA	1458(b)(1)
3121(a)(5)(H)	SBJPA	1421(b)(8)(A)
	SBJPA	1458(b)(1)
3121(a)(5)(I)	SBJPA	1458(b)(1)
3121(b)	SBJPA	1116(a)(1)(A)
3121(b)(20)(A)	SBJPA	1116(a)(1)(B)
3121(s)	SBJPA	1802(a)
3231(e)(10)	HIPPA	301(c)(2)(A)
3304(a)(16)	WELFARE	110(l)(2)
	WELFARE	316(g)(2)(A)

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3306(b)(5)(F)	SBJPA	1421(b)(8)(C)
3306(b)(5)(G)	SBJPA	1421(b)(8)(C)
3306(b)(5)(H)	SBJPA	1421(b)(8)(C)
3306(b)(15)	HIPPA	301(c)(2)(B)
3306(b)(16)	HIPPA	301(c)(2)(B)
3306(b)(17)	HIPPA	301(c)(2)(B)
3306(c)(1)(B)	SBJPA	1203(a)
3306(k)	SBJPA	1704(t)(10)
3401(a)(1)	BOSNIA	1(c)
	SBJPA	1704(t)(4)(C)
3401(a)(12)(D)	SBJPA	1421(b)(8)(D)
3401(a)(19)	HIPPA	301(c)(2)(C)
3401(a)(20)	HIPPA	301(c)(2)(C)
3401(a)(21)	HIPPA	301(c)(2)(C)
3405(e)(12)	SBJPA	1704(t)(71)
3508(b)(2)(A)(i)	SBJPA	1118(a)
3508(b)(2)(A)(ii)	SBJPA	1118(a)
3508(b)(2)(A)(iii)	SBJPA	1118(a)
4001(e)	SBJPA	1703(c)(1)
4001(f)	SBJPA	1607(a)
	SBJPA	1607(b)
4001(g)	SBJPA	1607(b)
4041(a)(1)(D)(i)	SBJPA	1208
4041(a)(1)(D)(ii)	SBJPA	1208
4041(a)(1)(D)(iii)	SBJPA	1208
4041(c)(2)	SBJPA	1609(g)(3)(A)
4041(c)(3)	SBJPA	1609(g)(3)(A)
	SBJPA	1609(g)(3)(B)
4041(c)(4)	SBJPA	1609(g)(3)(A)
4041(c)(5)	SBJPA	1609(a)(3)
	SBJPA	1609(g)(3)(A)
4041(k)(1)(A)	SBJPA	1609(g)(4)(A)
4041(k)(1)(B)	SBJPA	1609(g)(4)(A)
4041(k)(1)(C)	SBJPA	1609(g)(4)(A)
4081(a)(2)(A)(i)	SBJPA	1609(g)(1)
4081(a)(2)(A)(ii)	SBJPA	1609(g)(1)
4081(a)(2)(A)(iii)	SBJPA	1609(g)(1)
4081(d)	SBJPA	1609(a)(2)(A)
	SBJPA	1609(a)(2)(B)
4081(d)(1)	SBJPA	1609(g)(4)(B)
4081(d)(2)	SBJPA	1609(g)(2)
4081(d)(3)	SBJPA	1609(g)(2)
4082(c)	SBJPA	1801(a)
4082(d)	SBJPA	1801(a)
4082(e)	SBJPA	1801(a)
4091(b)(3)(A)	SBJPA	1609(a)(1)
4093(c)(2)(B)	SBJPA	1702(b)(2)(A)
4261(e)	SBJPA	1609(e)
4261(f)	SBJPA	1609(d)
4261(g)	SBJPA	1609(b)
4271(d)	SBJPA	1609(b)
4282(b)	SBJPA	1609(f)
4282(c)	SBJPA	1609(f)
4462(b)(1)(D)	SBJPA	1704(i)(1)
4682(d)(1)	SBJPA	1803(a)(1)
4682(g)(4)	SBJPA	1803(b)
4955(e)	TBOR2	1311(c)(1)
4958	TBOR2	1311(a)
4963(a)	TBOR2	1311(c)(2)
4963(b)	TBOR2	1311(c)(2)
4963(c)	TBOR2	1311(c)(2)
4971(f)(4)	SBJPA	1464(a)
4972(d)(1)(A)(ii)	SBJPA	1421(b)(9)(D)
4972(d)(1)(A)(iii)	SBJPA	1421(b)(9)(D)
4972(d)(1)(A)(iv)	SBJPA	1421(b)(9)(D)
4973	HIPPA	301(e)(1)
4973(a)	HIPPA	301(e)(1)
	HIPPA	301(e)(2)
	HIPPA	301(e)(3)
4973(b)(1)(A)	SBJPA	1704(t)(70)
4973(d)	HIPPA	.301(e)(4)
4975(a)	SBJPA	1453(a)
4975(c)(4)	HIPPA	.301(f)(1)
4975(d)(13)	SBJPA	1702(g)(3)
4975(e)(1)	HIPPA	.301(f)(2)
4977(c)	SBJPA	1704(t)(66)
4978(b)(2)	SBJPA	1602(b)(4)
4978B	SBJPA	1602(b)(5)(A)
4980A(c)(4)	SBJPA	1401(b)(12)(A)
	SBJPA	1401(b)(12)(B)
	SBJPA	1401(b)(12)(C)
4980A(g)	SBJPA	1452(b)
4980B(f)(2)(B)	HIPPA	421(c)(1)(A)
	HIPPA	421(c)(1)(B)
	HIPPA	421(c)(1)(C)
4980B(f)(2)(B)(i)	SBJPA	1704(g)(1)(A)
4980B(f)(6)(C)	HIPPA	421(c)(2)
4980B(g)(1)(A)	HIPPA	421(c)(3)
4980B(g)(2)	HIPPA	321(d)(1)
4980C	HIPPA	326(a)
4980D	HIPPA	402(a)
4980E	HIPPA	301(c)(4)
5041(c)(6)	SBJPA	1702(b)(5)
5041(c)(7)	SBJPA	1702(b)(5)
5061(b)(3)	SBJPA	1702(b)(6)
5134(c)(3)	SBJPA	1704(t)(12)
5206(f)(2)	SBJPA	1704(t)(13)
5354	SBJPA	1702(b)(7)
6013(b)(2)	TBOR2	402
6032(h)(2)(c)(i)	SBJPA	1809
6032(h)(2)(c)(ii)	SBJPA	1809
6033(b)(9)	TBOR2	1312(a)
6033(b)(10)	TBOR2	1312(a)
6033(b)(11)	TBOR2	1312(a)
6033(b)(12)	TBOR2	1312(a)
6033(b)(13)	TBOR2	1312(a)
6033(b)(14)	TBOR2	1312(a)
6033(e)(1)(B)(i)	SBJPA	1703(g)(2)

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6033(e)(1)(B)(iii)	SBJPA	1703(g)(1)
6033(f)	TBOR2	1312(b)
6033(g)	TBOR2	1312(b)
6037(c)	SBJPA	1307(c)(2)
6038(a)(1)(E)	SBJPA	1704(f)(5)(A)
6038(a)(1)(F)	SBJPA	1704(f)(5)(A)
6038(f)	SBJPA	1704(t)(40)
6038A(b)(2)	SBJPA	1704(f)(5)(B)
6038A(b)(3)	SBJPA	1704(f)(5)(B)
6038A(b)(4)	SBJPA	1704(f)(5)(B)
6038A(e)(4)(D)	SBJPA	1702(c)(5)(A)
	SBJPA	1702(c)(5)(B)
6039F	SBJPA	1905(a)
	HIPPA	512(a)
6041(d)(1)	TBOR2	1201(a)(1)
6041A(e)(1)	TBOR2	1201(a)(2)
6042(c)(1)	TBOR2	1201(a)(3)
6043	SBJPA	1704(t)(17)
6044(e)(1)	TBOR2	1201(a)(4)
6045(b)(1)	TBOR2	1201(a)(5)
6045(e)(3)	SBJPA	1704(o)(1)
6047(d)(1)	SBJPA	1455(b)(2)
6047(e)(1)	SBJPA	1602(b)(6)
6047(e)(2)	SBJPA	1602(b)(6)
6047(e)(3)	SBJPA	1602(b)(6)
6047(f)(1)	SBJPA	1455(d)(1)
6048	SBJPA	1901(a)
6049(c)(1)(A)	TBOR2	1201(a)(6)
6050A(a)(3)	SBJPA	1116(a)(1)(C)
6050A(a)(4)	SBJPA	1116(a)(1)(C)
6050A(a)(5)	SBJPA	1116(a)(1)(C)
6050B(b)(1)	TBOR2	1201(a)(7)
6050B(c)(1)	SBJPA	1704(t)(14)
6050H(d)(1)	TBOR2	1201(a)(8)
6050I(e)(1)	TBOR2	1201(a)(9)
6050J(e)	TBOR2	1201(a)(10)
6050K(b)(1)	TBOR2	1201(a)(11)
6050N(b)(1)	TBOR2	1201(a)(12)
6050P	OCRA 96	31001(m)(2)
6050P(a)	OCRA 96	31001(m)(2)
6050P(c)	OCRA 96	31001(m)(2)
6050P(d)	OCRA 96	31001(m)(2)
6050P(e)	OCRA 96	31001(m)(2)
6050Q	HIPPA	323(a)
6050R	SBJPA	1116(b)(1)
6051(a)(9)	HIPPA	301(c)(3)
6051(a)(10)	HIPPA	301(c)(3)
6051(a)(11)	HIPPA	301(c)(3)
6103(a)(3)	WELFARE	316(g)(4)(B)
6103(c)	TBOR2	1207
6103(e)(1)(A)(iv)	SBJPA	1704(t)(41)
6103(e)(8)	TBOR2	403(a)
6103(e)(9)	TBOR2	902(a)
6103(i)(3)(C)	OCRA 96	31001(i)(2)
6103(i)(8)	TBOR2	1206(b)(1)
6103(i)(10)(A)	OCRA 96	31001(g)(2)

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6103(l)(10)	WELFARE	110(l)(4)(A)
	WELFARE	110(l)(4)(B)
6103(l)(15)	TBOR2	1206(a)
6103(l)(6)(B)	WELFARE	316(g)(4)(A)
6103(l)(6)(C)	WELFARE	316(g)(4)(B)
6103(l)(7)(D)(i)	WELFARE	110(l)(3)
6103(p)(3)(A)	TBOR2	1206(b)(2)(A)
	TBOR2	1206(b)(2)(B)
6103(p)(4)	TBOR2	1206(b)(3)(A)
	TBOR2	1206(b)(3)(B)
	TBOR2	1206(b)(3)(C)
	WELFARE	110(l)(5)(A)
	WELFARE	110(l)(5)(B)
6103(p)(4)(F)	WELFARE	316(g)(4)(B)
6103(p)(4)(F)(ii)	TBOR2	1206(b)(4)(A)
	TBOR2	1206(b)(4)(B)
6104(e)(1)(A)	TBOR2	1313(a)(1)
6104(e)(2)(A)(ii)	TBOR2	1313(a)(2)
6104(e)(3)	TBOR2	1313(a)(3)
6109(e)	SBJPA	1615(a)(2)(A)
6109(f)	SBJPA	1704(t)(42)
6109(g)	SBJPA	1704(t)(42)
6159(b)(3)	TBOR2	201(b)
6159(b)(5)	TBOR2	201(a)
6159(c)	TBOR2	202(a)
6166(k)(6)	SBJPA	1704(t)(15)
6201(d)	TBOR2	602(a)
6201(e)	TBOR2	602(a)
6213(e)	TBOR2	1311(c)(3)
6213(g)(2)(D)	WELFARE	451(c)
6213(g)(2)(E)	WELFARE	451(c)
6213(g)(2)(F)	SBJPA	1615(c)
	WELFARE	451(c)
6213(g)(2)(G)	SBJPA	1615(c)
	WELFARE	451(c)
6213(g)(2)(H)	SBJPA	1615(c)
6214(e)	SBJPA	1704(t)(16)
6233(b)	SBJPA	1307(c)(3)(B)
6241	SBJPA	1307(c)(1)
6242	SBJPA	1307(c)(1)
6243	SBJPA	1307(c)(1)
6244	SBJPA	1307(c)(1)
6245	SBJPA	1307(c)(1)
6302(g)	SBJPA	1702(c)(3)
6305(a)	WELFARE	361(a)(1)
	WELFARE	361(a)(2)
	WELFARE	361(a)(3)
	WELFARE	361(a)(4)
6323(j)	TBOR2	501(a)
6334(a)(2)	TBOR2	502(a)(1)
	TBOR2	502(a)(2)
	TBOR2	502(a)(3)
6334(a)(3)	TBOR2	502(b)
6334(a)(11)(A)	WELFARE	110(l)(6)
6334(f)	TBOR2	502(c)
6343(d)	TBOR2	501(b)

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6402(a)	WELFARE	110(l)(7)(A)
6402(e)	WELFARE	110(l)(7)(B)
	WELFARE	110(l)(7)(C)
6402(f)	OCRA 96	31001(u)(2)
	WELFARE	110(l)(7)(B)
6402(g)	WELFARE	110(l)(7)(B)
6402(h)	WELFARE	110(l)(7)(B)
6402(i)	WELFARE	110(l)(7)(B)
6402(j)	WELFARE	110(l)(7)(B)
6404(e)	TBOR2	301(b)(1)
	TBOR2	301(b)(2)
6404(e)(1)	TBOR2	301(a)(1)
	TBOR2	301(a)(2)
6404(g)	TBOR2	302(a)
	TBOR2	701(c)(3)
6416(b)(1)	SBJPA	1702(b)(3)
6421(f)(2)(A)	SBJPA	1609(g)(4)(C)
6427(f)(4)	SBJPA	1703(k)
6427(g)	SBJPA	1606(a)
6427(i)(1)	SBJPA	1606(b)(2)(A)
	SBJPA	1606(b)(2)(B)
6427(i)(2)(A)	SBJPA	1606(b)(2)(A)
	SBJPA	1606(b)(2)(B)
6427(l)(4)	SBJPA	1702(b)(2)(B)
6501(m)	SBJPA	1702(e)(3)(A)
	SBJPA	1702(e)(3)(B)
	SBJPA	1703(n)(8)
	SBJPA	1704(j)(4)(B)
6501(n)	SBJPA	1702(e)(3)(A)
6501(o)	SBJPA	1702(e)(3)(A)
6503(j)	TBOR2	1002(c)
	SBJPA	1702(h)(17)(A)
6503(k)	TBOR2	1002(c)
	SBJPA	1702(h)(17)(B)
6503(k)(1)	TBOR2	1002(b)
6503(k)(2)(A)(i)	TBOR2	1002(a)
6503(k)(2)(A)(ii)	TBOR2	1002(a)
6503(k)(2)(A)(iii)	TBOR2	1002(a)
6503(l)	TBOR2	1002(c)
6601(e)(2)(A)	TBOR2	303(b)(1)
6601(e)(3)	TBOR2	303(a)
6621(c)(2)(A)	SBJPA	1702(c)(6)
6621(c)(2)(B)(i)	SBJPA	1702(c)(7)
6651(a)(3)	TBOR2	303(b)(2)
6651(g)	TBOR2	1301(a)
6652(c)(1)(A)	TBOR2	1314(a)
	TBOR2	1314(b)
6652(c)(1)(C)	SBJPA	1704(s)(1)
6652(c)(1)(D)	SBJPA	1704(s)(2)
6652(e)	SBJPA	1455(d)(2)
6652(i)	SBJPA	1455(c)(1)
	SBJPA	1455(c)(2)
6655(g)(3)	SBJPA	1703(h)
6656(c)	TBOR2	304(a)
6656(c)(1)	TBOR2	701(c)(3)
6656(d)	TBOR2	304(a)

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6672(b)	TBOR2	901(a)
6672(c)	TBOR2	901(a)
6672(d)	TBOR2	903(a)
6672(e)	TBOR2	904(a)
6677	SBJPA	1901(b)
6685	TBOR2	1313(b)
6693(a)	SBJPA	1455(d)(3)
	HIPPA	301(g)(1)
6693(c)	SBJPA	1421(b)(4)(B)
6693(d)	SBJPA	1421(b)(4)(B)
6714	SBJPA	1703(n)(9)(A)
6715	SBJPA	1703(n)(9)(A)
6724(d)(1)(A)	SBJPA	1455(a)(1)
6724(d)(1)(A)(vi)	SBJPA	1116(b)(2)(A)
6724(d)(1)(A)(vii)	SBJPA	1116(b)(2)(A)
6724(d)(1)(A)(viii)	SBJPA	1116(b)(2)(A)
6724(d)(1)(B)	SBJPA	1455(a)(1)
	SBJPA	1702(c)(2)(A)
	SBJPA	1702(c)(2)(B)
6724(d)(1)(B)(ix)	HIPPA	323(b)(1)
6724(d)(1)(B)(x)	HIPPA	323(b)(1)
6724(d)(1)(B)(xi)	HIPPA	323(b)(1)
6724(d)(1)(B)(xii)	HIPPA	323(b)(1)
6724(d)(1)(B)(xiii)	HIPPA	323(b)(1)
6724(d)(1)(B)(xiv)	HIPPA	323(b)(1)
6724(d)(1)(B)(xv)	HIPPA	323(b)(1)
6724(d)(1)(C)	SBJPA	1455(a)(1)
6724(d)(2)(Q)	HIPPA	323(b)(2)
6724(d)(2)(R)	SBJPA	1116(b)(2)(B)
	HIPPA	323(b)(2)
6724(d)(2)(S)	SBJPA	1116(b)(2)(B)
	SBJPA	1901(c)(1)
	HIPPA	323(b)(2)
6724(d)(2)(T)	SBJPA	1116(b)(2)(B)
	SBJPA	1901(c)(1)
	HIPPA	323(b)(2)
6724(d)(2)(U)	SBJPA	1116(b)(2)(B)
	SBJPA	1455(a)(2)
	SBJPA	1901(c)(1)
	HIPPA	323(b)(2)
6724(d)(2)(V)	SBJPA	1116(b)(2)(B)
	SBJPA	1455(a)(2)
6724(d)(2)(W)	SBJPA	1455(a)(2)
6724(d)(2)(X)	SBJPA	1455(a)(2)
6724(d)(3)(C)	SBJPA	1615(a)(2)(B)
6724(d)(3)(D)	SBJPA	1615(a)(2)(B)
6724(d)(3)(E)	SBJPA	1615(a)(2)(B)
	SBJPA	1704(j)(3)
7012(3)	SBJPA	1702(b)(4)(A)
7012(4)	SBJPA	1702(b)(4)(B)
7012(5)	SBJPA	1702(b)(4)(B)
7012(6)	SBJPA	1702(b)(4)(B)
7122(b)	TBOR2	503(a)
7213(a)(2)	TBOR2	1206(b)(5)
7232	SBJPA	1704(t)(20)(A)
	SBJPA	1704(t)(20)(B)

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7422(g)(2)	TBOR2	1311(c)(4)
7422(g)(3)	TBOR2	1311(c)(4)
7430(b)(1)	TBOR2	703(a)
7430(b)(3)	TBOR2	704(a)
7430(b)(4)	TBOR2	704(a)
7430(c)(1)	TBOR2	702(a)(1)
	TBOR2	702(a)(2)
	TBOR2	702(a)(3)
7430(c)(2)(B)	TBOR2	701(c)(1)
7430(c)(4)(A)(i)	TBOR2	701(a)
7430(c)(4)(A)(ii)	TBOR2	701(a)
7430(c)(4)(A)(iii)	TBOR2	701(a)
7430(c)(4)(B)	TBOR2	701(b)
7430(c)(4)(C)	TBOR2	701(b)
	TBOR2	701(c)(2)
7433(b)	TBOR2	801(a)
7433(d)(1)	TBOR2	802(a)
7434	TBOR2	601(a)
7435	TBOR2	601(a)
	TBOR2	1203(a)
7436	TBOR2	1203(a)
7454(b)	TBOR2	1311(c)(5)
	SBJPA	1704(t)(43)
7502(f)	TBOR2	1210
7508	BOSNIA	1(b)
7523(b)(3)(C)	WELFARE	110(l)(8)
7524	TBOR2	1204(a)
7608(c)(4)(B)	TBOR2	1205(c)(1)(A)
	TBOR2	1205(c)(1)(B)
	TBOR2	1205(c)(1)(C)
7608(c)(5)(C)	TBOR2	1205(c)(2)
7608(c)(6)	TBOR2	1205(b)
7609(a)(3)(G)	TBOR2	1001(a)
7609(a)(3)(H)	TBOR2	1001(a)
7609(a)(3)(I)	TBOR2	1001(a)
7611(h)(7)	SBJPA	1704(t)(59)
7623	TBOR2	1209(a)
7701(a)(19)(C)(xi)	SBJPA	1621(b)(8)
7701(a)(20)	SBJPA	1402(b)(3)
7701(a)(30)(C)	SBJPA	1907(a)(1)
7701(a)(30)(D)	SBJPA	1907(a)(1)
7701(a)(30)(E)	SBJPA	1907(a)(1)
7701(a)(31)	SBJPA	1907(a)(2)
7701(i)(2)(A)	SBJPA	1621(b)(9)
7702B	HIPPA	321(a)
7702B(g)	HIPPA	325
7802	TBOR2	101(b)(2)
7802(d)	TBOR2	101(a)
7805(b)	TBOR2	1101(a)
7811(a)	TBOR2	101(b)(1)(A)
7811(b)	TBOR2	102(a)(1)
	TBOR2	102(a)(2)
7811(c)	TBOR2	102(b)
7811(e)	TBOR2	101(b)(1)(B)
7811(f)	TBOR2	101(b)(1)(B)
7872(a)	SBJPA	1704(t)(58)(A)
7872(e)	SBJPA	1704(t)(58)(B)
7872(e)(2)	SBJPA	1704(t)(58)(A)
7872(f)(12)	SBJPA	1602(b)(7)
7872(f)(8)	SBJPA	1906(c)(2)
9502(b)	SBJPA	1609(c)(1)
9502(b)(2)	SBJPA	1609(g)(4)(D)
	SBJPA	1703(n)(10)
9502(d)(5)	SBJPA	1609(c)(3)
9502(f)(1)(A)	SBJPA	1609(g)(4)(C)
9502(f)(3)	SBJPA	1609(c)(2)
9707(d)(1)	SBJPA	1704(t)(65)
9801	HIPPA	401(a)
9802	HIPPA	401(a)
9803	HIPPA	401(a)
9804	HIPPA	401(a)
9805	HIPPA	401(a)
9806	HIPPA	401(a)

Non Code	Law	Act Section
RA 1987 10511(c)	BOSNIA	2

P. L. 104–117
TAX BENEFITS FOR INDIVIDUALS PERFORMING SERVICES IN CERTAIN HAZARDOUS DUTY AREAS

Act Section	1986 Code Section
1(a)	112
1(b)	7508
1(c)	3401(a)(1)
1(d)	112(c) 112(b)
	Non Code
2	RA 1987 10511(c)

P. L. 104–134
OMNIBUS CONSOLIDATED RECISSIONS AND APPROPRIATIONS ACT OF 1996

Act Section	1986 Code Section
31001(g)(2)	6103(l)(10)(A)
31001(i)(2)	6103(l)(3)(C)
31001(m)(2)	6050P
	6050P(a)
	6050P(c)
	6050P(d)
	6050P(e)
31001(u)(2).	6402(f)

P. L. 104–168
TAXPAYER BILL OF RIGHTS 2

Act Section	1986 Code Section
101(a)	7802(d)
101(b)(1)(A)	7811(a)
101(b)(1)(B)	7811(e)

Act Section	1986 Code Section
	7811(f)
101(b)(2)	7802
102(a)(1)	7811(b)
102(a)(2)	7811(b)
102(b)	7811(c)
201(a)	6159(b)(5)
201(b)	6159(b)(3)
202(a)	6159(c)
301(a)(1)	6404(e)(1)
301(a)(2)	6404(e)(1)
301(b)(1)	6404(e)
301(b)(2)	6404(e)
302(a)	6404(g)
303(a)	6601(e)(3)
303(b)(1)	6601(e)(2)(A)
303(b)(2)	6651(a)(3)
304(a)	6656(c)
	6656(d)
402	6013(b)(2)
403(a)	6103(e)(8)
501(a)	6323(j)
501(b)	6343(d)
502(a)(1)	6334(a)(2)
502(a)(2)	6334(a)(2)
502(a)(3)	6334(a)(2)
502(b)	6334(a)(3)
502(c)	6334(f)
503(a)	7122(b)
601(a)	7434
	7435
602(a)	6201(d)
	6201(e)
701(a)	7430(c)(4)(A)(i)
	7430(c)(4)(A)(ii)
7430(c)(4)(A)(iii)	
701(b)	7430(c)(4)(B)
	7430(c)(4)(C)
701(c)(1)	7430(c)(2)(B)
701(c)(2)	7430(c)(4)(C)
701(c)(3)	6404(g)
	6656(c)(1)
702(a)(1)	7430(c)(1)
702(a)(2)	7430(c)(1)
702(a)(3)	7430(c)(1)
703(a)	7430(b)(1)
704(a)	7430(b)(3)
	7430(b)(4)
801(a)	7433(b)
802(a)	7433(d)(1)
901(a)	6672(b)
	6672(c)
902(a)	6103(e)(9)
903(a)	6672(d)
904(a)	6672(e)
1001(a)	7609(a)(3)(G)
	7609(a)(3)(H)
	7609(a)(3)(I)

Act Section	1986 Code Section
1002(a)	6503(k)(2)(A)(i)
	6503(k)(2)(A)(ii)
	6503(k)(2)(A)(iii)
1002(b)	6503(k)(1)
1002(c)	6503(j)
	6503(k)
	6503(l)
1101(a)	7805(b)
1201(a)(1)	6041(d)(1)
1201(a)(2)	6041A(e)(1)
1201(a)(3)	6042(c)(1)
1201(a)(4)	6044(e)(1)
1201(a)(5)	6045(b)(1)
1201(a)(6)	6049(c)(1)(A)
1201(a)(7)	6050B(b)(1)
1201(a)(8)	6050H(d)(1)
1201(a)(9)	6050I(e)(1)
1201(a)(10)	6050J(e)
1201(a)(11)	6050K(b)(1)
1201(a)(12)	6050N(b)(1)
1203(a)	7435
	7436
1204(a)	7524
1205(b)	7608(c)(6)
1205(c)(1)(A)	7608(c)(4)(B)
1205(c)(1)(B)	7608(c)(4)(B)
1205(c)(1)(C)	7608(c)(4)(B)
1205(c)(2)	7608(c)(5)(C)
1206(a)	6103(l)(15)
1206(b)(1)	6103(i)(8)
1206(b)(2)(A)	6103(p)(3)(A)
1206(b)(2)(B)	6103(p)(3)(A)
1206(b)(3)(A)	6103(p)(4)
1206(b)(3)(B)	6103(p)(4)
1206(b)(3)(C)	6103(p)(4)
1206(b)(4)(A)	6103(p)(4)(F)(ii)
1206(b)(4)(B)	6103(p)(4)(F)(ii)
1206(b)(5)	7213(a)(2)
1207	6103(c)
1209(a)	7623
1210	7502(f)
1301(a)	6651(g)
1311(a)	4958
1311(b)(1)	501(c)(4)
1311(c)(1)	4955(e)
1311(c)(2)	4963(a)
	4963(b)
	4963(c)
1311(c)(3)	6213(e)
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1702(f)(4)	2701(c)(1)(B)(i)
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1702(f)(5)(B)	2701(c)(3)(C)(ii)
1702(f)(6)	2701(d)(3)(A)(iii)
1702(f)(7)	2701(d)(3)(B)(ii)
1702(f)(8)(A)	2701(e)(5)
1702(f)(8)(B)	2701(e)(5)
1702(f)(9)	2701(d)(4)(C)
1702(f)(10)	2701(e)(6)
1702(f)(11)(A)	2702(a)(3)(A)(i)
	2702(a)(3)(A)(ii)
	2702(a)(3)(A)(iii)
	2702(a)(3)(A)(iv)
1702(f)(11)(B)	2702(a)(3)
	2702(a)(3)(B)
1702(g)(1)(A)	1248(a)(i)
	1248(a)(ii)
1702(g)(1)(B)	1248(e)(1)
1702(g)(1)(C)	1248(f)(1)(B)
1702(g)(1)(D)	1248(i)(l)
1702(g)(2)	897(f)
1702(g)(3)	4975(d)(13)
1702(g)(4)	56(g)(4)(D)(iii)
1702(h)(1)(A)	168(e)(3)(B)(vi)
1702(h)(1)(B)	168(e)(3)(B)
1702(h)(1)(C)	168(g)(4)(K)
1702(h)(2)	172(b)(1)(E)(ii)
1702(h)(3)	805(a)(4)(E)
	832(b)(5)(C)(ii)
	832(b)(5)(D)(ii)
1702(h)(4)	243(b)(3)(A)

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1702(h)(5)	280F(a)
1702(h)(6)	1504(c)(2)(B)(i)
1702(h)(7)	341(f)(3)
1702(h)(8)	243(b)(2)
1702(h)(10)	179(d)(1)
1702(h)(11)	50(a)(2)(E)
1702(h)(13)	424(c)(3)(B)
1702(h)(14)	1367(a)(2)(E)
1702(h)(15)	460(e)(6)(B)
1702(h)(16)	172(h)(4)(C)
1702(h)(17)(A)	6503(j)
1702(h)(17)(B)	6503(k)
1702(h)(18)	1250(e)(4)
1702(h)(19)	179(d)(1)
1703(a)	1044(c)(2)
1703(c)(1)	4001(e)
1703(d)	135(b)(2)(B)(ii)
1703(e)(1)	59(a)
1703(e)(2)	59(a)
1703(e)(3)	59(a)
1703(e)(4)	59(a)
1703(f)	1201(a)
	1561(a)
1703(g)(1)	6033(e)(1)(B)(iii)
1703(g)(2)	6033(e)(1)(B)(i)
1703(h)	6655(g)(3)
1703(i)(1)	904(d)(3)(G)
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1703(i)(3)	956A(f)
1703(i)(4)	958(b)
1703(i)(5)(A)	1297(d)(2)(A)
1703(i)(5)(B)	1297(d)(2)
1703(i)(6)	1297(e)
1703(j)	40(e)(1)(B)
1703(k)	6427(f)(4)
1703(m)	1397B(d)(5)(B)
1703(n)(1)(A)	39(d)
1703(n)(1)(B)	39(d)
1703(n)(2)	108(d)(9)(A)
1703(n)(3)	143(d)(2)(C)
1703(n)(4)	163(j)(6)(E)(ii)
1703(n)(5)	1017(b)(4)(A)
1703(n)(6)	1245(a)(3)
1703(n)(7)(A)	1394(e)(2)
1703(n)(7)(B)	1394(e)(2)
1703(n)(8)	6501(m)
1703(n)(9)(A)	6714
	6715
1703(n)(10)	9502(b)(2)
1703(n)(14)	117(d)(2)(B)
1704(b)(1)	149(g)(3)(B)(iii)
1704(c)(1)	1445(e)(3)
1704(d)(1)	469(c)(3)(B)
1704(e)(1)	469(g)(1)(A)
1704(f)(1)	2102(c)(3)(A)
1704(f)(2)(A)	163(j)(1)(B)
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	163(j)(8)
1704(f)(3)(A)	884(f)(1)
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1704(f)(4)(A)	865(b)(2)
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1704(f)(5)(B)	6038A(b)(2)
	6038A(b)(3)
	6038A(b)(4)
1704(g)(1)(A)	4980B(f)(2)(B)(i)
1704(h)(1)	860E(a)(6)
1704(i)(1)	4462(b)(1)(D)
1704(j)(1)	53(d)(1)(B)(iv)
1704(j)(2)	179A(f)
	179A(g)
1704(j)(3)	6724(d)(3)(E)
1704(j)(4)(A)	30(d)(i)
	30(d)(ii)
1704(j)(4)(B)	6501(m)
1704(j)(5)	501(c)(21)(D)(ii)
1704(l)(1)	72(b)(4)(A)
1704(m)(1)	1(g)(7)(A)(ii)
1704(m)(2)(A)	1(g)(7)(B)
1704(m)(2)(B)	1(g)(7)(B)
1704(m)(3)	59(j)(1)(B)
1704(n)(1)	414(u)
1704(o)(1)	6045(e)(3)
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	162(k)(2)(A)(ii)
	162(k)(2)(A)(iii)
1704(p)(3)	162(k)
1704(q)(1)	404(j)(1)
1704(r)(1)	1296(b)(2)(B)
	1296(b)(2)(C)
	1296(b)(2)(D)
1704(s)(1)	6652(c)(1)(C)
1704(s)(2)	6652(c)(1)(D)
1704(t)(1)	56(g)(4)(C)(ii)
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	72(m)(2)(B)
	72(m)(2)(C)
1704(t)(3)	86(b)(2)
1704(t)(4)(A)	112
1704(t)(4)(B)	112
1704(t)(4)(C)	3401(a)(1)
1704(t)(5)	172(h)(3)(B)(i)
1704(t)(6)	543(a)(2)(B)(ii)
1704(t)(7)	958(a)(1)
1704(t)(8)	642(g)
1704(t)(9)	1463
1704(t)(10)	3306(k)
1704(t)(12)	5134(c)(3)
1704(t)(13)	5206(f)(2)
1704(t)(14)	6050B(c)(1)
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1704(t)(17)	6043
1704(t)(20)(A)	7232
1704(t)(20)(B)	7232
1704(t)(28)	460(b)(1)
1704(t)(29)	50(a)(2)(C)
1704(t)(30)	172(h)(4)(B)
1704(t)(31)	355(d)(7)(A)
1704(t)(32)	420(e)(1)(C)
1704(t)(33)	537(b)(4)
1704(t)(34)	613(e)(1)(B)
1704(t)(35)	856(a)(4)
1704(t)(36)	904(f)(2)(B)(i)
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1704(t)(37)	936(b)
1704(t)(38)	2104(c)
1704(t)(39)	280A(c)(1)(A)
1704(t)(40)	6038(f)
1704(t)(41)	6103(e)(1)(A)(iv)
1704(t)(42)	6109(f)
	6109(g)
1704(t)(43)	7454(b)
1704(t)(58)(A)	7872(a)
	7872(e)(2)
1704(t)(58)(B)	7872(e)
1704(t)(59)	7611(h)(7)
1704(t)(60)	419A(c)(3)
1704(t)(61)	807(d)(3)(B)(ii)
1704(t)(62)	1274A(c)(1)(B)
1704(t)(63)	724(d)(3)(B)
1704(t)(64)	42(c)(2)
1704(t)(65)	9707(d)(1)
1704(t)(66)	4977(c)
1704(t)(67)	401(a)(20)
1704(t)(68)	402(g)(3)(A)
1704(t)(69)	403(b)(10)
1704(t)(70)	4973(b)(1)(A)
1704(t)(71)	3405(e)(12)
1704(t)(74)	860F(a)(5)
1704(t)(75)	415(k)(1)(C)
	415(k)(1)(D)
	415(k)(1)(E)
	415(k)(1)(F)
1704(t)(76)	404(a)(2)
1704(t)(77)	72(p)(4)(A)(ii)
1704(t)(78)	461(i)(3)(C)
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1704(t)(79)	164(a)(4)
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1704(t)(80)	936(a)(4)(A)(ii)
1801(a)	4082(c)
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1802(a)	3121(s)
1803(a)(1)	4682(d)(1)
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1805(a)	584(h)
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1806(a)	529
1806(b)(1)	135(d)(1)(B)
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1807(a)	23
1807(b)	137
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1807(c)(2)	86(b)(2)(A)
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1807(c)(3)	219(g)(3)(A)
1807(c)(4)	469(i)(3)(E)(ii)
1807(c)(5)	1016(a)(24)
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	1016(a)(26)
1809	6032(h)(2)(C)(i)
	6032(h)(2)(C)(ii)
1901(a)	6048
1901(b)	6677
1901(c)(1)	6724(d)(2)(S)
	6724(d)(2)(T)
	6724(d)(2)(U)
1902(a)	1494(c)
1903(a)(1)	679(a)(2)(B)
1903(a)(2)	679(a)(3)
1903(b)	679(a)
1903(c)	679(a)(4)
	679(a)(5)
1903(d)	679(c)(3)
1903(e)	679(c)(2)(A)
1903(f)	679(d)
1904(a)(1)	672(f)
1904(a)(2)	672(c)
1904(b)(1)	665(d)(2)
1904(b)(2)	901(b)(5)
1904(c)(1)	643(h)
1904(c)(2)	665(c)
1905(a)	6039F
1906(a)	668(a)
1906(b)	643(a)(7)
1906(c)(1)	643(i)
1906(c)(2)	7872(f)(8)
1907(a)(1)	7701(a)(30)(C)
	7701(a)(30)(D)
	7701(a)(30)(E)
1907(a)(2)	7701(a)(31)
1907(b)(1)	1491
1954(b)(1)	871(f)(2)(B)

P. L. 104–191
HEALTH INSURANCE PORTABILITY AND ACCOUNTABILITY ACT OF 1996

Act Section	1986 Code Section
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	221

Act Section	1986 Code Section
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301(c)(2)(A)	3231(e)(10)
301(c)(2)(B)	3306(b)(15)
	3306(b)(16)
	3306(b)(17)
301(c)(2)(C)	3401(a)(19)
	3401(a)(20)
	3401(a)(21)
301(c)(3)	6051(a)(9)
	6051(a)(10)
	6051(a)(11)
301(c)(4)	4980E
301(d)	125(f)
301(e)(1)	4973
301(e)(2)	4973(a)
301(e)(3)	4973(a)
	4973(a)(3)
301(e)(4)	4973(d)
301(f)(1)	4975(c)(4)
301(f)(2)	4975(e)(1)
301(g)(1)	6693(a)
301(h)	848(e)(1)(B)(ii)
	848(e)(1)(B)(iii)
	848(e)(1)(B)(iv)
311(a)	162(l)(1)
311(b)	104(a)(3)
321(a)	7702B
321(b)	807(d)(3)(A)(iii)
321(c)(1)	125(f)
321(c)(2)	106(c)
321(d)(1)	4980B(g)(2)
322(a)	213(d)(1)(B)
	213(d)(1)(C)
	213(d)(1)(D)
322(b)(1)	213(d)(1)(D)
322(b)(2)(A)	213(d)(1)
322(b)(2)(B)	162(l)(2)(C)
322(b)(2)(C)	213(d)(10)
	213(d)(11)
322(b)(3)(A)	213(d)(6)
322(b)(3)(B)	213(d)(6)
322(b)(4)	213(d)(7)
323(a)	6050Q
323(b)(1)	6724(d)(1)(B)(ix)
	6724(d)(1)(B)(x)
	6724(d)(1)(B)(xi)
	6724(d)(1)(B)(xii)
	6724(d)(1)(B)(xiii)
	6724(d)(1)(B)(xiv)
	6724(d)(1)(B)(xv)
323(b)(2)	6724(d)(2)(Q)
	6724(d)(2)(R)
	6724(d)(2)(S)
	6724(d)(2)(T)
	6724(d)(2)(U)
325	7702B(g)
326(a)	4980C
331(a)	101(g)
332(a)	818(g)
341(a)	501(c)(26)
342(a)	501(c)(27)
351(a)	833(c)(4)
361(a)	72(t)(3)(A)
361(b)	72(t)(2)(D)
361(c)	72(t)(2)(B)
401(a)	9801
	9802
	9803
	9804
	9805
	9806
402(a)	4980D
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421(c)(1)(B)	4980B(f)(2)(B)
421(c)(1)(C)	4980B(f)(2)(B)
421(c)(2)	4980B(f)(6)(C)
421(c)(3)	4980B(g)(1)(A)
501(a)(1)	264(a)(4)
501(a)(2)	264(a)(4)
501(b)(1)	264(a)(4)
501(b)(2)	264(d)
511(a)	877(a)
511(b)(1)	877(c)
	877(d)
511(b)(2)	877(b)(1)
511(c)	877(d)
511(d)(1)	877(b)
511(d)(2)	877(a)
511(e)(1)(A)	2107(a)
511(e)(1)(B)	2107(c)(2)
	2107(c)(3)
511(e)(1)(C)	2107(b)
511(e)(2)(A)	2501(a)(3)
511(f)(1)	877(e)
	877(f)
511(f)(2)(A)	2107(d)
	2107(e)
511(f)(2)(B)	2501(a)(3)(E)
512(a)	6039F

P. L. 104-193
PERSONAL RESPONSIBILITY AND WORK OPPORTUNITY RECONCILIATION ACT OF 1996

Act Section	1986 Code Section
110(l)(1)	51(d)(9)
110(l)(2)	3304(a)(16)
110(l)(3)	6103(l)(7)(D)(i)
110(l)(4)(A)	6103(l)(10)
110(l)(4)(B)	6103(l)(10)
110(l)(5)(A)	6103(p)(4)
110(l)(5)(B)	6103(p)(4)
110(l)(6)	6334(a)(11)(A)

Act Section	1986 Code Section
110(l)(7)(A)	6402(a)
110(l)(7)(B)	6402(e)
	6402(f)
	6402(g)
	6402(h)
	6402(i)
	6402(j)
110(l)(7)(C)	6402(e)
110(l)(8)	7523(b)(3)(C)
316(g)(2)(A)	3304(a)(16)
316(g)(2)(B)	3304(a)(16)
316(g)(2)(C)	3304(a)(16)
316(g)(2)(D)	3304(a)(16)
316(g)(2)(E)	3304(a)(16)
316(g)(4)(A)	6103(l)(6)(B)
	6103(l)(6)(C)
316(g)(4)(B)(i)	6103(a)(3)
316(g)(4)(B)(ii)	6103(l)(6)(C)
316(g)(4)(B)(iii)	6103(p)(4)(F)
361(a)(1)	6305(a)
361(a)(2)	6305(a)
361(a)(3)	6305(a)
361(a)(4)	6305(a)
451(a)	32(c)(1)(F)
451(b)	32(l)
451(c)	6213(g)(2)(D)
	6213(g)(2)(E)
	6213(g)(2)(F)
	6213(g)(2)(G)
909(a)(1)	32(i)(1)
909(a)(2)	32(j)
909(a)(3)	32(b)(2)
909(b)	32(i)(2)(B)
	32(i)(2)(C)
	32(i)(2)(D)
	32(i)(2)(E)
910(a)	32(a)(2)(B)
	32(c)(1)(C)
	32(f)(2)(B)
910(b)	32(c)(5)

Public Law 104–117
104th Congress, H.R. 2778
March 20, 1996

An Act to provide that members of the Armed Forces performing services for the peacekeeping efforts in Bosnia and Herzegovina, Croatia, and Macedonia shall be entitled to tax benefits in the same manner as if such services were performed in a combat zone, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. TREATMENT OF CERTAIN INDIVIDUALS PERFORMING SERVICES IN CERTAIN HAZARDOUS DUTY AREAS.

(a) GENERAL RULE.—For purposes of the following provisions of the Internal Revenue Code of 1986, a qualified hazardous duty area shall be treated in the same manner as if it were a combat zone (as determined under section 112 of such Code):

(1) Section 2(a)(3) (relating to special rule where deceased spouse was in missing status).

(2) Section 112 (relating to the exclusion of certain combat pay of members of the Armed Forces).

(3) Section 692 (relating to income taxes of members of Armed Forces on death).

(4) Section 2201 (relating to members of the Armed Forces dying in combat zone or by reason of combat-zone-incurred wounds, etc.).

(5) Section 3401(a)(1) (defining wages relating to combat pay for members of the Armed Forces).

(6) Section 4253(d) (relating to the taxation of phone service originating from a combat zone from members of the Armed Forces).

(7) Section 6013(f)(1) (relating to joint return where individual is in missing status).

(8) Section 7508 (relating to time for performing certain acts postponed by reason of service in combat zone).

(b) QUALIFIED HAZARDOUS DUTY AREA.—For purposes of this section, the term "qualified hazardous duty area" means Bosnia and Herzegovina, Croatia, or Macedonia, if as of the date of the enactment of this section any member of the Armed Forces of the United States is entitled to special pay under section 310 of title 37, United States Code (relating to special pay; duty subject to hostile fire or imminent danger) for services performed in such country. Such term includes any such country only during the period such entitlement is in effect. Solely for purposes of applying section 7508 of the Internal Revenue Code of 1986, in the case of an individual who is performing services as part of Operation Joint Endeavor outside the United States while deployed away from such individual's permanent duty station, the term "qualified hazardous duty area" includes, during the period for which such entitlement is in effect, any area in which such services are performed.

(c) EXCLUSION OF COMBAT PAY FROM WITHHOLDING LIMITED TO AMOUNT EXCLUDABLE FROM GROSS INCOME.—Paragraph (1) of section 3401(a) of the Internal Revenue Code of 1986 (defining wages) is amended by inserting before the semicolon the following: "to the extent remuneration for such service is excludable from gross income under such section".

(d) INCREASE IN COMBAT PAY EXCLUSION FOR OFFICERS TO HIGHEST AMOUNT APPLICABLE TO ENLISTED PERSONNEL.—

(1) IN GENERAL.—Subsection (b) of section 112 of such Code (relating to commissioned officers) is amended by striking "$500" and inserting "the maximum enlisted amount".

(2) MAXIMUM ENLISTED AMOUNT.—Subsection (c) of section 112 of such Code (relating to definitions) is amended by adding at the end the following new paragraph:

"(5) The term 'maximum enlisted amount' means, for any month, the sum of—

"(A) the highest rate of basic pay payable for such month to any enlisted member of the Armed Forces of the United States at the highest pay grade applicable to enlisted members, and

"(B) in the case of an officer entitled to special pay under section 310 of title 37, United States Code, for such month, the amount of such special pay payable to such officer for such month.".

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the provisions of and amendments made by this section shall take effect on November 21, 1995.

(2) WITHHOLDING.—Subsection (a)(5) and the amendment made by subsection (c) shall apply to remuneration paid after the date of the enactment of this Act.

SEC. 2. EXTENSION OF INTERNAL REVENUE SERVICE USER FEES.

Subsection (c) of section 10511 of the Revenue Act of 1987 is amended by striking "October 1, 2000" and by inserting "October 1, 2003".

Approved March 20, 1996.

104TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
2d Session } { 104–465

TAX BENEFITS FOR INDIVIDUALS PERFORMING SERVICES IN CERTAIN HAZARDOUS DUTY AREAS

FEBRUARY 29, 1996.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ARCHER, from the Committee on Ways and Means, submitted the following

REPORT

[To accompany H.R. 2778]

[Including cost estimate of the Congressional Budget Office]

The Committee on Ways and Means, to whom was referred the bill (H.R. 2778) to provide that members of the Armed Forces performing services for the peacekeeping effort in the Republic of Bosnia and Herzegovina shall be entitled to certain tax benefits in the same manner as if such services were performed in a combat zone, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

CONTENTS

The amendments are as follows:

29–006

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. TREATMENT OF CERTAIN INDIVIDUALS PERFORMING SERVICES IN CERTAIN HAZARDOUS DUTY AREAS.

(a) GENERAL RULE.—For purposes of the following provisions of the Internal Revenue Code of 1986, a qualified hazardous duty area shall be treated in the same manner as if it were a combat zone (as determined under section 112 of such Code):

(1) Section 2(a)(3) (relating to special rule where deceased spouse was in missing status).

(2) Section 112 (relating to the exclusion of certain combat pay of members of the Armed Forces).

(3) Section 692 (relating to income taxes of members of Armed Forces on death).

(4) Section 2201 (relating to members of the Armed Forces dying in combat zone or by reason of combat-zone-incurred wounds, etc.).

(5) Section 340(a)(1) (defining wages relating to combat pay for members of the Armed Forces).

(6) Section 4253(d) (relating to the taxation of phone service originating from a combat zone from members of the Armed Forces).

(7) Section 6013(f)(1) (relating to joint return where individual is in missing status).

(8) Section 7508 (relating to time for performing certain acts postponed by reason of service in combat zone).

(b) QUALIFIED HAZARDOUS DUTY AREA.—For purposes of this section, the term "qualified hazardous duty area" means Bosnia and Herzegovina, Croatia, or Macedonia, if as of the date of the enactment of this section any member of the Armed Forces of the United States is entitled to special pay under section 310 of title 37, United States Code (relating to special pay; duty subject to hostile fire or imminent danger) for services performed in such country. Such term includes any such country only during the period such entitlement is in effect. Solely for purposes of applying section 7508 of the Internal Revenue Code of 1986, in the case of an individual who is performing services as part of Operation Joint Endeavor outside the United States while deployed away from such individual's permanent duty station, the term "qualified hazardous duty area" includes, during the period for which such entitlement is in effect, any area in which such services are performed.

(c) EXCLUSION OF COMBAT PAY FROM WITHHOLDING LIMITED TO AMOUNT EXCLUDABLE FROM GROSS INCOME.—Paragraph (1) of section 3401(a) of the Internal Revenue Code of 1986 (defining wages) is amended by inserting before the semicolon the following: "to the extent remuneration for such service is excludable from gross income under such section".

(d) INCREASE IN COMBAT PAY EXCLUSION FOR OFFICERS TO HIGHEST AMOUNT APPLICABLE TO ENLISTED PERSONNEL.—

(1) IN GENERAL.—Subsection (b) of section 112 of such Code (relating to commissioned officers) is amended by striking "$500" and inserting "the maximum enlisted amount".

(2) MAXIMUM ENLISTED AMOUNT.—Subsection (c) of section 112 of such Code (relating to definitions) is amended by adding at the end the following new paragraph:

"(5) The term 'maximum enlisted amount' means, for any month, the sum of—

"(A) the highest rate of basic pay payable for such month to any enlisted member of the Armed Forces of the United States at the highest pay grade applicable to enlisted members, and

"(B) in the case of an officer entitled to special pay under section 310 of title 37, United States Code, for such month, the amount of such special pay payable to such officer for such month."

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the provisions of and amendments made by this section shall take effect on November 21, 1995.

(2) WITHHOLDING.—Subsection (a)(5) and the amendment made by subsection (c) shall apply to remuneration paid after the date of the enactment of this Act.

SEC. 2. EXTENSION OF INTERNAL REVENUE SERVICE USER FEES.

Subsection (c) of section 10511 of the Revenue Act of 1987 is amended by striking "October 1, 2000" and by inserting "October 1, 2003".

Amend the title so as to read:

A bill to provide that members of the Armed Forces performing services for the peacekeeping efforts in Bosnia and Herzegovina, Croatia, and Macedonia shall be entitled to tax benefits in the same manner as if such services were performed in a combat zone, and for other purposes.

I. INTRODUCTION

A. Purpose and Summary

H.R. 2778, as amended: (1) provides that service in a qualified hazardous duty area (Bosnia and Herzegovina, Croatia, or Macedonia) is to be treated in the same manner as if it were a combat zone; (2) makes the suspension of time provisions of Code sec. 7508 applicable to other Operation Joint Endeavor personnel; (3) increases the dollar value of the officer combat pay exclusion from the present-law $500 per month limit to the highest rate of pay applicable to enlisted personnel plus the amount of hostile fire/imminent danger pay which the officer receives; and (4) extends IRS user fees for three additional years (until October 1, 2003) as a revenue offset to the other provisions.

B. Background and Need for Legislation

The bill, as amended, is intended to treat service by United States Armed Forces (and support) personnel in Bosnia and Herzegovina, Croatia, or Macedonia in the same manner as if it were combat zone service for purposes of the Internal Revenue Code as long as the personnel are entitled to receive hostile fire/imminent danger pay for services in such country. Members of the Armed Forces are in Bosnia and Herzegovina and Croatia as part of "Operation Joint Endeavor" (the NATO operation) and in Macedonia as part of "Operation Able Sentry" (the United Nations operation). The bill, as amended, also makes the suspension of time provisions of Code sec. 7508 applicable to other Operation Joint Endeavor personnel.

In addition, the bill, as amended, modifies the present-law exclusion from income for officer combat pay from a maximum of $500 per month to the highest rate of pay for enlisted personnel plus the amount of hostile fire/imminent danger pay which the officer receives. Finally, the bill, as amended, extended IRS user fees for three additional years (until October 1, 2003) as a revenue offset to the other provisions in order to make the bill deficit neutral.

C. Legislative History

H.R. 2778 was introduced by Mr. Bunning on December 14, 1995, and was amended by the Committee in a markup on February 28, 1996. An amendment in the nature of a substitute (offered by Chairman Archer and Mr. Gibbons) was adopted by a voice vote. The bill, as amended, was ordered favorably reported by a voice vote on February 28, 1996.

II. EXPLANATION OF THE BILL

PRESENT LAW

General time limits for filing tax returns

Present law provides that individuals generally must file their Federal income tax returns by April 15 of the year following the close of a taxable year (sec. 6072). Present law also provides that the Secretary may grant reasonable extensions of time for filing such returns (sec. 6081). Treasury regulations provide an additional automatic two-month extension (until June 15 for calendar-year individuals) for United States citizens and residents in military or naval service on duty outside the United States (Treas. Reg. sec. 1.6081–5(a)(6). No action is necessary to apply for this extension. This extension applies to both filing returns and paying the tax due.

Treasury regulations also provide, upon application on the proper form, an automatic four-month extension (until August 15 for calendar-year individuals) for any individual properly filing that form (Treas. Reg. sec. 1.6081–4T).

In general, individuals must make quarterly estimated tax payments by April 15, June 15, September 15, and January 15 of the following taxable year. Wage withholding is considered to be a payment of estimated taxes.

Suspension of time periods

In general, present law suspends the period of time for performing various acts under the Internal Revenue Code, such as filing tax returns, paying taxes, or filing a claim for credit or refund of tax, for any individual serving in the Armed Forces of the United States in an area designated as a "combat zone" during the period of combatant activities (sec. 7508). An individual who becomes a prisoner of war is considered to continue in active service and is therefore also eligible for these suspension of time provisions. The suspension of time also applies to an individual serving in support of such Armed Forces in the combat zone, such as Red Cross personnel, accredited correspondents, and civilian personnel acting under the direction of the Armed Forces in support of those Forces. The designation of a combat zone must be made by the President in an Executive Order. The President also designates the period of combatant activities in the combat zone (the starting date and the termination date of combat).

The suspension of time encompasses the period of service in the combat zone during the period of combatant activities in the zone. In addition, it encompasses any time of continuous hospitalization resulting from injury received in the combat zone [1] or time in missing in action status, plus the next 180 days.

The suspension of time applies to the following acts:

[1] Two special rules apply to continuous hospitalization inside the United States. First, the suspension of time provisions based on continuous hospitalization inside the United States are applicable only to the hospitalized individual; they are not applicable to the spouse of such individual. Second, in no event do the suspension of time provisions based on continuous hospitalization inside the United States extend beyond five years from the date the individual returns to the United States. These two special rules do not apply to continuous hospitalization outside the United States.

(1) Filing any return of income, estate, or gift tax (except employment and withholding taxes);
(2) Payment of any income, estate, or gift tax (except employment and withholding taxes);
(3) Filing a petition with the Tax Court for redetermination of a deficiency, or for review of a decision rendered by the Tax Court;
(4) Allowance of a credit or refund of any tax;
(5) Filing a claim for credit or refund of any tax;
(6) Bringing suit upon any such claim for credit or refund;
(7) Assessment of any tax;
(8) Giving or making any notice or demand for the payment of any tax, or with respect to any liability to the United States in respect of any tax;
(9) Collection of the amount of any liability in respect of any tax;
(10) Bringing suit by the United States in respect of any liability in respect of any tax; and
(11) Any other act required or permitted under the internal revenue laws specified in regulations prescribed under section 7508 by the Secretary of the Treasury.

Individuals may, if they choose, perform any of these acts during the period of suspension.

Spouses of qualifying individuals are entitled to the same suspension of time, except that the spouse is ineligible for this suspension for any taxable year beginning more than two years after the date of termination of combatant activities in the combat zone.

Exclusion for combat pay

Gross income does not include certain combat pay of members of the Armed Forces (sec. 112). If enlisted personnel serve in a combat zone during any part of any month, military pay for that month is excluded from gross income. In addition, if enlisted personnel are hospitalized as a result of injuries, wounds, or disease incurred in a combat zone, military pay for that month is also excluded from gross income; this exclusion is limited, however, to hospitalization during any part of any month beginning not more than two years after the end of combat in the zone. In the case of commissioned officers, these exclusions from income are limited to $500 per month of military pay.

Income tax withholding does not apply to military pay for any month in which an employee (whether enlisted personnel or commissioned officer) is entitled to the exclusion from income for combat pay (sec. 3401(a)(1)).

Exemption from tax upon death in a combat zone

An individual in active service as a member of the Armed Forces who dies while serving in a combat zone (or as a result of wounds, disease, or injury received while serving in a combat zone) is not subject to income tax for the year of death (as well as for any prior taxable year ending on or after the first day the individual served in the combat zone) (sec. 692). Special computational rules apply in the case of joint returns. A reduction in estate taxes is also pro-

vided with respect to individuals dying under these circumstances (sec. 2201).

Special rules permit the filing of a joint return where a spouse is in missing status as a result of service in a combat zone (sec. 6013(f)(1)). Special rules for determining surviving spouse status apply where the deceased spouse was in missing status as a result of service in a combat zone (sec. 2(a)(3)).

Exemption from telephone excise tax

The telephone excise tax is not imposed on "any toll telephone service" that originates in a combat zone (sec. 4253(d)).

Operation Desert Storm: Executive Order designating Persian Gulf Area as a combat zone

On January 21, 1991, President Bush signed Executive Order 12744, designating the Persian Gulf Area as a combat zone. This designation was retroactive to January 17, 1991, the date combat commenced in that area, and continues in effect until terminated by another Executive Order. An Executive Order terminating this combat zone designation has not been issued. Thus, individuals serving in the Persian Gulf Area are eligible for the suspension of time provisions and military pay exclusions (among other provisions) described above, beginning on January 17, 1991.

The Executive Order specifies that the Persian Gulf Area is the Persian Gulf, the Red Sea, the Gulf of Oman, part of the Arabian Sea, the Gulf of Aden, and the entire land areas of Iraq, Kuwait, Saudi Arabia, Oman, Bahrain, Qatar, and the United Arab Emirates.

The Department of Defense provides to the Internal Revenue Service, on a monthly basis, a computer tape with information regarding the military personnel whose service is in the combat zone designated by the Executive Order and who are therefore eligible for, among other provisions, the extension of time provisions of section 7508 and the exclusion from income provisions of section 112.

Operation Desert Shield: Legislative extension of time

On January 30, 1991, President Bush signed Public Law 102–2. This Act amended section 7508 by providing that any individual who performs Desert Shield services (and the spouse of such an individual) is entitled to the benefits of the suspension of time provisions of section 7508. Desert Shield services are defined as services in the Armed Forces of the United States (or in support of those Armed Forces) if such services are performed in the area designated by the President as the "Persian Gulf Desert Shield area" and such services are performed during the period beginning August 2, 1990, and ending on the date on which any portion of the area was designated by the President as a combat zone pursuant to section 112 (which was January 17, 1991).

Operation Joint Endeavor: Administrative extension of time

On December 12, 1995, the Internal Revenue Service announced[2] that it was administratively extending the time to file tax returns until December 15, 1996, for members of the Armed Forces "departing 'Operation Joint Endeavor'" on or after March 1, 1996. In addition, the IRS stated that the penalties for failure to file tax returns and failure to pay taxes would not be assessed with respect to these individuals. Also, the IRS stated that it would administratively place any balance due accounts into suspense status and suspend examinations while the member is serving in "Operation Joint Endeavor."

IRS user fees

The IRS provides written responses to questions of individuals, corporations, and organizations relating to their tax status or the effects of particular transactions for tax purposes. The IRS generally charges a fee for requests for a letter ruling, determination letter, opinion letter, or other similar ruling or determination. The Uruguay Round Agreements Act extended the IRS user fee program for five years (until October 1, 2000).

REASONS FOR CHANGE

The Committee believes that it is appropriate to apply the special tax rules applicable to combat zones to service in Bosnia and Herzegovina, Croatia, and Macedonia in the same manner as if they were a combat zone.

EXPLANATION OF PROVISIONS

Treatment of portions of former Yugoslavia as if they were a combat zone

The bill provides that a qualified hazardous duty area shall be treated in the same manner as if it were a combat zone for purposes of the following provisions of the Code:

(1) the special rule for determining surviving spouse status where the deceased spouse was in missing status as a result of service in a combat zone (sec. 2(a)(3));

(2) the exclusions from income for combat pay (sec. 112);

(3) forgiveness of income taxes of members of the Armed Forces dying in the combat zone or by reason of combat-zone incurred wounds (sec. 692);

(4) the reduction in estate taxes for members of the Armed Forces dying in the combat zone or by reason of combat-zone incurred wounds (sec. 2201);

(5) the exemption from income tax withholding for military pay for any month in which an employee is entitled to the exclusion from income (sec. 3401(a)(1));

(6) the exemption from the telephone excise tax for toll telephone service that originates in a combat zone (sec. 4253(d));

[2] Letter from John T. Lyons, Assistant Commissioner (International), Internal Revenue Service, to Lt. Col. David M. Pronchick, Armed Forces Tax Counsel, Department of Defense

(7) the special rule permitting filing of a joint return where a spouse is in missing status as a result of service in a combat zone (sec. 6013(f)(1)); and

(8) the suspension of time provisions (sec. 7508).

A qualified hazardous duty area means Bosnia and Herzegovina, Croatia, or Macedonia, if, as of the date of enactment, any member of the Armed Forces is entitled to hostile fire/imminent danger pay for services performed in such country. Members of the Armed Forces are in Bosnia and Herzegovina and Croatia as part of "Operation Joint Endeavor" (the NATO operation). Members of the Armed Forces are in Macedonia as part of "Operation Able Sentry" (the United Nations operation).

Suspension of time provisions for other Operation Joint Endeavor personnel

An individual who is performing services as part of Operation Joint Endeavor outside the United States while deployed away from the individual's permanent duty station will qualify for the suspension of time provisions in section 7508 of the Code during the period that hostile fire/imminent danger pay is paid in Bosnia and Herzegovina, Croatia, or Macedonia.

Combat pay exclusion for officers

In addition, the bill raises the dollar value of the exclusion from income for combat pay for officers in section 112 of the Code from the present-law level of $500 per month to the highest rate of basic pay at the highest pay grade that enlisted personnel may receive plus the amount of hostile fire/imminent danger pay which the officer receives. Currently, the highest level of basic pay received by enlisted members of the Armed Forces is $4,104.80 per month. The bill also conforms the wage withholding rules to the income exclusion rules for officers.

Extension of IRS user fees

The bill extends IRS user fees for three additional years (until October 1, 2003).

EFFECTIVE DATE

The bill generally is effective on November 21, 1995 (the date on which the Dayton Accord was initialed); the modifications to the wage withholding rules apply to remuneration paid after the date of enactment. The amendment relating to IRS user fees is effective on the date of enactment.

III. VOTES OF THE COMMITTEE

In compliance with cause 2(l)(2)(B) of rule XI of the Rules of the House of Representatives, the following statement is made concerning the votes of the Committee in its consideration of the bill, H.R. 2778.

Motion to report the bill

The bill, H.R. 2778, as amended, was ordered favorably reported by voice vote on February 28, 1996, with a quorum present.

Motion on substitute amendment

The Committee adopted an amendment in the nature of a substitute (offered by Chairman Archer and Mr. Gibbons) by voice vote, with a quorum present.

IV. BUDGET EFFECTS OF THE BILL

A. Committee Estimate of Budgetary Effects

In compliance with clause 7(a) of rule XIII of the Rules of the House of Representatives, the following statement is made concerning the effects on the budget of the bill, H.R. 2778, as reported.

The bill, as amended, is estimated to have the following effects on budget receipts for fiscal years 1996–2005:

ESTIMATED REVENUE EFFECTS OF H.R. 2778 AS AMENDED—FISCAL YEARS 1996–2005

[In Millions of Dollars]

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	1996–2000	1006–2005
1. Extend certain tax benefits to Armed Forces personnel serving in the former Yugoslavia; raise the monthly exclusion from income for combat pay for officers from $500/month to the highest pay level for enlisted personnel; and conform wage withholding rule to income exclusion rule for officers	11/21/95	−38	−45	(1)	.....	.....	.....	.....	.....	.....	.....	−83	−83
2. Extend IRS user fees through 9/30/03 [1]	10/1/00	.....	.....	.....	.....	.....	35	35	35	.....	.....	.....	105
Net totals	.....	−38	−45	(2)	.....	.....	35	35	35	.....	.....	−83	22

[1] Estimate provided by the Congressional Budget Office.
[2] Negligible revenue effect.

Note.—Details may not add to totals due to rounding.

Source: Joint Committee on Taxation.

B. STATEMENT REGARDING NEW BUDGET AUTHORITY AND TAX EXPENDITURES

In compliance with subdivision (B) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, the Committee states that the bill, as amended, involves no new or increased budget authority. The bill, as amended, involves increased tax expenditures for the income tax benefit provisions related to combat pay (for amounts, see Part IV.A., above).

C. COST ESTIMATE PREPARED BY THE CONGRESSIONAL BUDGET OFFICE

In compliance with subdivision (C) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, requiring a cost estimate prepared by the Congressional Budget Office (CBO), the following statement by CBO is provided.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, February 29, 1996.

Hon. BILL ARCHER,
Chairman, Committee on Ways and Means,
House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office and the Joint Committee on Taxation (JCT) have reviewed H.R. 2778, as ordered reported by the House Committee on Ways and Means on February 28, 1996. CBO and JCT estimate that this bill would reduce revenues by $38 million in 1996 and increase revenues by $22 million over the fiscal years 1996 through 2005. H.R. 2778 contains no intergovernmental or private sector mandates as defined in Public Law 104–4 and would impose no direct costs on state, local, or tribal governments.

H.R. 2778 provides members of the Armed Forces performing services for the peacekeeping efforts in Bosnia and Herzegovina, Croatia, and Macedonia with certain tax benefits granted to individuals performing services in a combat zone. JCT estimates that this provision would reduce revenues by $38 million in fiscal year 1996, $45 million in fiscal year 1997, and by a negligible amount in fiscal year 1998. In addition, H.R. 2778 extends the expiration of IRS user fees from October 1, 2000 to October 1, 2003. CBO estimates that this provision would increase revenues by $35 million, net of payroll and income tax offsets, in each of the fiscal years from 2001 through 2003. The revenue effects of H.R. 2778 are summarized in the table below.

REVENUE EFFECTS OF H.R. 2778

[By fiscal years, in millions of dollars]

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Extend tax benefits to soldiers in the former Yugoslavia	−38	−45	(1)	0	0	0	0	0	0	0
Extend IRS Fees through 10/1/03	0	0	0	0	0	35	35	35	0	0

[1] Negligible revenue effect.

Section 252 of the Balanced Budget and Emergency Deficit Control Act of 1985 sets up pay-as-you-go procedures for legislation af-

fecting receipts or direct spending through 1998. Because H.R. 2778 would affect receipts, pay-as-you-go procedures would apply to the bill. These effects are summarized in the table below.

PAY-AS-YOU-GO CONSIDERATION

[By fiscal years, in millions of dollars]

	1996	1997	1998
Changes in receipts	−38	−45	(1)
Changes in outlays	(2)	(2)	(2)

[1] Negligible revenue effect.
[2] Not applicable.

If you wish further details, please feel free to contact me or your staff may wish to contact Stephanie Weiner.

Sincerely,

JUNE E. O'NEILL, *Director.*

V. OTHER MATTERS TO BE DISCUSSED UNDER THE RULES OF THE HOUSE

A. COMMITTEE OVERSIGHT FINDINGS AND RECOMMENDATIONS

With respect to subdivision (A) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives (relating to oversight findings), the Committee advises that it was a result of the Committee's oversight activities concerning the tax treatment and tax return filing requirements of military (and support) personnel serving in "Operation Joint Endeavor" (in Bosnia and Herzegovina and Croatia) and "Operation Able Sentry" (in Macedonia), tax treatment of combat pay generally, and the need to provide a revenue offset for the bill that the Committee concluded that it is appropriate to enact the provisions contained in the bill as amended.

B. SUMMARY OF FINDINGS AND RECOMMENDATIONS OF THE COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT

With respect to subdivision (D) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, the Committee advises that no oversight findings or recommendations have been submitted to this Committee by the Committee on Government Reform and Oversight with respect to the provisions contained in the bill.

C. INFLATIONARY IMPACT STATEMENT

In compliance with clause 2(l)(4) of rule XI of the Rules of the House of Representatives, the Committee states that the provisions of the bill are not expected to have an overall inflationary impact on prices and costs in the operation of the national economy. As indicated above in Part IV of this report, the bill is projected to reduce the aggregate deficit by $22 million over fiscal years 1996–2005.

VI. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted

is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE ACT OF 1986

Subtitle A—Income Taxes

* * * * * * *

CHAPTER 1—NORMAL TAXES AND SURTAXES

* * * * * * *

Subchapter B—Computation of Taxable Income

* * * * * * *

PART III—ITEMS SPECIFICALLY EXCLUDED FROM GROSS INCOME

* * * * * * *

SEC. 112. CERTAIN COMBAT PAY OF MEMBERS OF THE ARMED FORCES.

(a) * * *

(b) COMMISSIONED OFFICERS.—Gross income does not include so much of the compensation as does not exceed **[**$500**]** *the maximum enlisted amount* received for active service as a commissioned officer in the Armed Forces of the United States for any month during any part of which such officer—

(1) served in a combat zone, or

(2) was hospitalized as a result of wounds, disease, or injury incurred while serving in a combat zone, but this paragraph shall not apply for any month beginning more than 2 years after the date of the termination of combatant activities in such zone.

With respect to service in the combat zone designated for purposes of the Vietnam conflict, paragraph (2) shall not apply to any month after January 1978.

(c) DEFINITIONS.—For purposes of this section—

(1) * * *

* * * * * * *

(5) The term "maximum enlisted amount" means, for any month, the sum of—

(A) the highest rate of basic pay payable for such month to any enlisted member of the Armed Forces of the United States at the highest pay grade applicable to enlisted members, and

(B) in the case of an officer entitled to special pay under section 310 of title 37, United States Code, for such month, the amount of such special pay payable to such officer for such month.

* * * * * * *

Subtitle C—Employment Taxes

* * * * * * *

CHAPTER 24—COLLECTION OF INCOME TAX AT SOURCE ON WAGES

* * * * * * *

SEC. 3401. DEFINITIONS.

(a) WAGES.—For purposes of this chapter, the term "wages" means all remuneration (other than fees paid to a public official) for services performed by an employee for his employer, including the cash value of all remuneration (including benefits) paid in any medium other than cash; except that such term shall not include remuneration paid—

(1) for active service performed in a month for which such employee is entitled to the benefits of section 112 (relating to certain combat pay of members of the Armed Forces of the United States) *to the extent remuneration for such service is excludable from gross income under such section; or*

* * * * * * *

SECTION 10511 OF THE INTERNAL REVENUE ACT OF 1987

SEC. 10511. FEES FOR REQUESTS FOR RULING, DETERMINATION, AND SIMILAR LETTERS.

(a) * * *

* * * * * * *

(c) APPLICATION OF SECTION.—Subsection (a) shall apply with respect to requests made on or after the 1st day of the second calendar month beginning after the date of the enactment of this Act and before September 30, 1990. Subsection (a) shall also apply with respect to requests made after September 30, 1990, and before October 1, [2000] *2003.*

○

Public Law 104–134
104th Congress, H.R. 3019[1]
April 26, 1996

An Act making appropriations for fiscal year 1996 to make a further downpayment toward a balanced budget, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

* * * * *

SEC. 2904. COMPOSITION OF NATIONAL COMMISSION ON RESTRUCTURING THE INTERNAL REVENUE SERVICE.

(a) IN GENERAL.—Section 637(b)-(2) of the Treasury, Postal Service, and General Government Appropriations Act, 1996 (Public Law 104–52, 109 Stat. 509) is amended—

(1) by striking "thirteen" and inserting "seventeen", and

(2) in subparagraphs (B) and (D)—

(A) by striking "Two" and inserting "Four", and

(B) by striking "one from private life" and inserting "three from private life".

(b) EFFECTIVE DATE.—The amendments made by this section shall take effect as if included in the provisions of the Treasury, Postal Service, and General Government Appropriations Act, 1996.

* * * * *

SEC. 31001. DEBT COLLECTION IMPROVEMENT ACT OF 1996.

* * * * *

(g)(2) INTERNAL REVENUE CODE OF 1986.—Subparagraph (A) of section 6103(1)(10) of the Internal Revenue Code of 1986 (26 U.S.C. 6103(1)(10)) is amended by inserting "and to officers and employees of the Department of the Treasury in connection with such reduction" after "6402".

* * * * *

[1] This publication of the law is restricted to excerpts involving tax matters.

(i)(2) INCLUDED FEDERAL LOAN PROGRAM DEFINED.—Subparagraph (C) of section 6103(1)(3) of the Internal Revenue Code of 1986 (relating to disclosure that applicant for Federal loan has tax delinquent account) is amended to read as follows:

"(C) INCLUDED FEDERAL LOAN PROGRAM DEFINED.—For purposes of this paragraph, the term 'included Federal loan program' means any program under which the United States or a Federal agency makes, guarantees, or insures loans.".

* * * * *

(m)(2) RETURNS RELATING TO CANCELLATION OF INDEBTEDNESS BY CERTAIN ENTITIES.—

(A) IN GENERAL.—Subsection (a) of section 6050P of the Internal Revenue Code of 1986 (relating to returns relating to the cancellation of indebtedness by certain financial entities) is amended by striking "applicable financial entity" and inserting "applicable entity".

(B) ENTITIES TO WHICH REQUIREMENT APPLIES.—Subsection (c) of section 6050P of such Code is amended—

(i) by redesignating paragraphs (1) and (2) as paragraphs (2) and (3), respectively, and inserting before paragraph (2) (as so redesignated) the following new paragraph:

"(1) APPLICABLE ENTITY.—The term 'applicable entity' means—

"(A) an executive, judicial, or legislative agency (as defined in section 3701(a)(4) of title 31, United States Code), and

"(B) an applicable financial entity.", and

(ii) in paragraph (3), as so redesignated, by striking "(1)(B)" and inserting "(1)(A) or (2)(B)".

(C) ALTERNATIVE PROCEDURE.—Section 6050P of such Code is amended by adding at the end the following new subsection:

"(e) ALTERNATIVE PROCEDURE.—In lieu of making a return required under subsection (a), an agency described in subsection (c)(1)(A) may submit to the Secretary (at such time and in such form as the Secretary may by regulations prescribe) information sufficient for the Secretary to complete such a return on behalf of such agency. Upon receipt of such information, the Secretary shall complete such return and provide a copy of such return to such agency."

(D) CONFORMING AMENDMENTS.—

(i) Subsection (d) of section 6050P of such Code is amended by striking "applicable financial entity" and inserting "applicable entity".

(ii) The heading of section 6050P of such Code is amended to read as follows:

"SEC. 6050P. RETURNS RELATING TO THE CANCELLATION OF INDEBTEDNESS BY CERTAIN ENTITIES."

(iii) The table of sections for subpart B of part III of subchapter A of chapter 61 of such Code is amended by striking the item relating to section 6050P and inserting the following new item:

"Section 6050P. Returns relating to the cancellation of indebtedness by certain entities."

(n) Effective October 1, 1995, section 11 of the Administrative Dispute Resolution Act (Public Law 101–552, U.S.C. 571 note) shall not apply to the amendment made by section 8(b) of such Act.

* * * * *

(u)(2) FEDERAL AGENCY DEFINED.—Section 6402(f) of the Internal Revenue Code of 1986 (26 U.S.C. 6402(f)) is amended to read as follows:

"(f) FEDERAL AGENCY.—For purposes of this section, the term 'Federal agency' means a department, agency or instrumentality of the United States, and includes a Government corporation (as such term is defined in section 103 of title 5, United States Code).".

* * * * *

Approved April 26, 1996.

Public Law 104–168
104th Congress, H.R. 2337
July 30, 1996

An Act to amend the Internal Revenue Code of 1986 to provide for increased taxpayer protections.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Taxpayer Bill of Rights 2.

SECTION 1. SHORT TITLE; AMENDMENT OF 1986 CODE; TABLE OF CONTENTS.

26 USC 1 note.

(a) SHORT TITLE.—This Act may be cited as the "Taxpayer Bill of Rights 2".

(b) AMENDMENT OF 1986 CODE.—Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

(c) TABLE OF CONTENTS.—

TITLE I—TAXPAYER ADVOCATE

SEC. 101. ESTABLISHMENT OF POSITION OF TAXPAYER ADVOCATE WITHIN INTERNAL REVENUE SERVICE.

(a) GENERAL RULE.—Section 7802 (relating to Commissioner of Internal Revenue; Assistant Commissioner (Employee Plans and

Exempt Organizations)) is amended by adding at the end the following new subsection:

Establishment. Government organization.

"(d) OFFICE OF TAXPAYER ADVOCATE.—

"(1) IN GENERAL.—There is established in the Internal Revenue Service an office to be known as the 'Office of the Taxpayer Advocate'. Such office shall be under the supervision and direction of an official to be known as the 'Taxpayer Advocate' who shall be appointed by and report directly to the Commissioner of Internal Revenue. The Taxpayer Advocate shall be entitled to compensation at the same rate as the highest level official reporting directly to the Deputy Commissioner of the Internal Revenue Service.

"(2) FUNCTIONS OF OFFICE.—

"(A) IN GENERAL.—It shall be the function of the Office of Taxpayer Advocate to—

"(i) assist taxpayers in resolving problems with the Internal Revenue Service,

"(ii) identify areas in which taxpayers have problems in dealings with the Internal Revenue Service,

"(iii) to the extent possible, propose changes in the administrative practices of the Internal Revenue Service to mitigate problems identified under clause (ii), and

"(iv) identify potential legislative changes which may be appropriate to mitigate such problems.

"(B) ANNUAL REPORTS.—

"(i) OBJECTIVES.—Not later than June 30 of each calendar year after 1995, the Taxpayer Advocate shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the objectives of the Taxpayer Advocate for the fiscal year beginning in such calendar year. Any such report shall contain full and substantive analysis, in addition to statistical information.

"(ii) ACTIVITIES.—Not later than December 31 of each calendar year after 1995, the Taxpayer Advocate shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the activities of the Taxpayer Advocate during the fiscal year ending during such calendar year. Any such report shall contain full and substantive analysis, in addition to statistical information, and shall—

"(I) identify the initiatives the Taxpayer Advocate has taken on improving taxpayer services and Internal Revenue Service responsiveness,

"(II) contain recommendations received from individuals with the authority to issue Taxpayer Assistance Orders under section 7811,

"(III) contain a summary of at least 20 of the most serious problems encountered by taxpayers, including a description of the nature of such problems,

"(IV) contain an inventory of the items described in subclauses (I), (II), and (III) for which action has been taken and the result of such action,

"(V) contain an inventory of the items described in subclauses (I), (II), and (III) for which action remains to be completed and the period during which each item has remained on such inventory,

"(VI) contain an inventory of the items described in subclauses (II) and (III) for which no action has been taken, the period during which each item has remained on such inventory, the reasons for the inaction, and identify any Internal Revenue Service official who is responsible for such inaction,

"(VII) identify any Taxpayer Assistance Order which was not honored by the Internal Revenue Service in a timely manner, as specified under section 7811(b),

"(VIII) contain recommendations for such administrative and legislative action as may be appropriate to resolve problems encountered by taxpayers,

"(IX) describe the extent to which regional problem resolution officers participate in the selection and evaluation of local problem resolution officers, and

"(X) include such other information as the Taxpayer Advocate may deem advisable.

"(iii) REPORT TO BE SUBMITTED DIRECTLY.—Each report required under this subparagraph shall be provided directly to the Committees referred to in clauses (i) and (ii) without any prior review or comment from the Commissioner, the Secretary of the Treasury, any other officer or employee of the Department of the Treasury, or the Office of Management and Budget.

"(3) RESPONSIBILITIES OF COMMISSIONER.—The Commissioner of Internal Revenue shall establish procedures requiring a formal response to all recommendations submitted to the Commissioner by the Taxpayer Advocate within 3 months after submission to the Commissioner.".

(b) CONFORMING AMENDMENTS.—

(1) Section 7811 (relating to Taxpayer Assistance Orders) is amended—

(A) by striking "the Office of Ombudsman" in subsection (a) and inserting "the Office of the Taxpayer Advocate", and

(B) by striking "Ombudsman" each place it appears (including in the headings of subsections (e) and (f)) and inserting "Taxpayer Advocate".

(2) The heading for section 7802 is amended to read as follows:

"SEC. 7802. COMMISSIONER OF INTERNAL REVENUE; ASSISTANT COMMISSIONERS; TAXPAYER ADVOCATE.".

(3) The table of sections for subchapter A of chapter 80 is amended by striking the item relating to section 7802 and inserting the following new item:

"Sec. 7802. Commissioner of Internal Revenue; Assistant Commissioners; Taxpayer Advocate.".

26 USC 7802 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date of the enactment of this Act.

SEC. 102. EXPANSION OF AUTHORITY TO ISSUE TAXPAYER ASSISTANCE ORDERS.

(a) TERMS OF ORDERS.—Subsection (b) of section 7811 (relating to terms of Taxpayer Assistance Orders) is amended—

(1) by inserting "within a specified time period" after "the Secretary", and

(2) by inserting "take any action as permitted by law," after "cease any action,".

(b) LIMITATION ON AUTHORITY TO MODIFY OR RESCIND.—Section 7811(c) (relating to authority to modify or rescind) is amended to read as follows:

"(c) AUTHORITY TO MODIFY OR RESCIND.—Any Taxpayer Assistance Order issued by the Taxpayer Advocate under this section may be modified or rescinded—

"(1) only by the Taxpayer Advocate, the Commissioner of Internal Revenue, or the Deputy Commissioner of Internal Revenue, and

"(2) only if a written explanation of the reasons for the modification or rescission is provided to the Taxpayer Advocate.".

26 USC 7811 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date of the enactment of this Act.

TITLE II—MODIFICATIONS TO INSTALLMENT AGREEMENT PROVISIONS

SEC. 201. NOTIFICATION OF REASONS FOR TERMINATION OF INSTALLMENT AGREEMENTS.

(a) TERMINATIONS.—Subsection (b) of section 6159 (relating to extent to which agreements remain in effect) is amended by adding at the end the following new paragraph:

"(5) NOTICE REQUIREMENTS.—The Secretary may not take any action under paragraph (2), (3), or (4) unless—

"(A) a notice of such action is provided to the taxpayer not later than the day 30 days before the date of such action, and

"(B) such notice includes an explanation why the Secretary intends to take such action.

The preceding sentence shall not apply in any case in which the Secretary believes that collection of any tax to which an agreement under this section relates is in jeopardy.".

(b) CONFORMING AMENDMENT.—Paragraph (3) of section 6159(b) is amended to read as follows:

"(3) SUBSEQUENT CHANGE IN FINANCIAL CONDITIONS.—If the Secretary makes a determination that the financial condition

of a taxpayer with whom the Secretary has entered into an agreement under subsection (a) has significantly changed, the Secretary may alter, modify, or terminate such agreement.".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date 6 months after the date of the enactment of this Act. 26 USC 6159 note.

SEC. 202. ADMINISTRATIVE REVIEW OF TERMINATION OF INSTALLMENT AGREEMENT.

(a) GENERAL RULE.—Section 6159 (relating to agreements for payment of tax liability in installments) is amended by adding at the end the following new subsection:

"(c) ADMINISTRATIVE REVIEW.—The Secretary shall establish procedures for an independent administrative review of terminations of installment agreements under this section for taxpayers who request such a review.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall take effect on January 1, 1997. 26 USC 6159 note.

TITLE III—ABATEMENT OF INTEREST AND PENALTIES

SEC. 301. EXPANSION OF AUTHORITY TO ABATE INTEREST.

(a) GENERAL RULE.—Paragraph (1) of section 6404(e) (relating to abatement of interest in certain cases) is amended—

(1) by inserting "unreasonable" before "error" each place it appears in subparagraphs (A) and (B), and

(2) by striking "in performing a ministerial act" each place it appears and inserting "in performing a ministerial or managerial act".

(b) CLERICAL AMENDMENT.—The subsection heading for subsection (e) of section 6404 is amended—

(1) by striking "ASSESSMENTS" and inserting "ABATEMENT", and

(2) by inserting "UNREASONABLE" before "ERRORS".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to interest accruing with respect to deficiencies or payments for taxable years beginning after the date of the enactment of this Act. 26 USC 6404 note.

SEC. 302. REVIEW OF IRS FAILURE TO ABATE INTEREST.

(a) IN GENERAL.—Section 6404 is amended by adding at the end the following new subsection:

"(g) REVIEW OF DENIAL OF REQUEST FOR ABATEMENT OF INTEREST.—

"(1) IN GENERAL.—The Tax Court shall have jurisdiction over any action brought by a taxpayer who meets the requirements referred to in section 7430(c)(4)(A)(iii) to determine whether the Secretary's failure to abate interest under this section was an abuse of discretion, and may order an abatement, if such action is brought within 180 days after the date of the mailing of the Secretary's final determination not to abate such interest. Courts.

"(2) SPECIAL RULES.— Applicability.

"(A) DATE OF MAILING.—Rules similar to the rules of section 6213 shall apply for purposes of determining the date of the mailing referred to in paragraph (1).

"(B) RELIEF.—Rules similar to the rules of section 6512(b) shall apply for purposes of this subsection.

"(C) REVIEW.—An order of the Tax Court under this subsection shall be reviewable in the same manner as a decision of the Tax Court, but only with respect to the matters determined in such order.".

26 USC 6404 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to requests for abatement after the date of the enactment of this Act.

SEC. 303. EXTENSION OF INTEREST-FREE PERIOD FOR PAYMENT OF TAX AFTER NOTICE AND DEMAND.

(a) GENERAL RULE.—Paragraph (3) of section 6601(e) (relating to payments made within 10 days after notice and demand) is amended to read as follows:

"(3) PAYMENTS MADE WITHIN SPECIFIED PERIOD AFTER NOTICE AND DEMAND.—If notice and demand is made for payment of any amount and if such amount is paid within 21 calendar days (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000) after the date of such notice and demand, interest under this section on the amount so paid shall not be imposed for the period after the date of such notice and demand.".

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (A) of section 6601(e)(2) is amended by striking "10 days from the date of notice and demand therefor" and inserting "21 calendar days from the date of notice and demand therefor (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000)".

(2) Paragraph (3) of section 6651(a) is amended by striking "10 days of the date of the notice and demand therefor" and inserting "21 calendar days from the date of notice and demand therefor (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000)".

26 USC 6601 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply in the case of any notice and demand given after December 31, 1996.

SEC. 304. ABATEMENT OF PENALTY FOR FAILURE TO MAKE REQUIRED DEPOSITS OF PAYROLL TAXES IN CERTAIN CASES.

(a) IN GENERAL.—Section 6656 (relating to failure to make deposit of taxes) is amended by adding at the end the following new subsections:

"(c) EXCEPTION FOR FIRST-TIME DEPOSITORS OF EMPLOYMENT TAXES.—The Secretary may waive the penalty imposed by subsection (a) on a person's inadvertent failure to deposit any employment tax if—

"(1) such person meets the requirements referred to in section 7430(c)(4)(A)(iii),

"(2) such failure occurs during the 1st quarter that such person was required to deposit any employment tax, and

"(3) the return of such tax was filed on or before the due date.

For purposes of this subsection, the term 'employment taxes' means the taxes imposed by subtitle C.

"(d) AUTHORITY TO ABATE PENALTY WHERE DEPOSIT SENT TO SECRETARY.—The Secretary may abate the penalty imposed by subsection (a) with respect to the first time a depositor is required to make a deposit if the amount required to be deposited is inadvertently sent to the Secretary instead of to the appropriate government depository.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to deposits required to be made after the date of the enactment of this Act. 26 USC 6656 note.

TITLE IV—JOINT RETURNS

SEC. 401. STUDIES OF JOINT RETURN-RELATED ISSUES.

The Secretary of the Treasury or his delegate and the Comptroller General of the United States shall each conduct separate studies of—

(1) the effects of changing the liability for tax on a joint return from being joint and several to being proportionate to the tax attributable to each spouse,

(2) the effects of providing that, if a divorce decree allocates liability for tax on a joint return filed before the divorce, the Secretary may collect such liability only in accordance with the decree,

(3) whether those provisions of the Internal Revenue Code of 1986 intended to provide relief to innocent spouses provide meaningful relief in all cases where such relief is appropriate, and

(4) the effect of providing that community income (as defined in section 66(d) of such Code) which, in accordance with the rules contained in section 879(a) of such Code, would be treated as the income of one spouse is exempt from a levy for failure to pay any tax imposed by subtitle A by the other spouse for a taxable year ending before their marriage.

The reports of such studies shall be submitted to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate within 6 months after the date of the enactment of this Act. Reports.

SEC. 402. JOINT RETURN MAY BE MADE AFTER SEPARATE RETURNS WITHOUT FULL PAYMENT OF TAX.

(a) GENERAL RULE.—Paragraph (2) of section 6013(b) (relating to limitations on filing of joint return after filing separate returns) is amended by striking subparagraph (A) and redesignating the following subparagraphs accordingly.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after the date of the enactment of this Act. 26 USC 6013 note.

SEC. 403. DISCLOSURE OF COLLECTION ACTIVITIES.

(a) IN GENERAL.—Subsection (e) of section 6103 (relating to disclosure to persons having material interest) is amended by adding at the end the following new paragraph:

"(8) DISCLOSURE OF COLLECTION ACTIVITIES WITH RESPECT TO JOINT RETURN.—If any deficiency of tax with respect to a joint return is assessed and the individuals filing such return are no longer married or no longer reside in the same household, upon request in writing by either of such individuals,

the Secretary shall disclose in writing to the individual making the request whether the Secretary has attempted to collect such deficiency from such other individual, the general nature of such collection activities, and the amount collected. The preceding sentence shall not apply to any deficiency which may not be collected by reason of section 6502.".

26 USC 6103 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to requests made after the date of the enactment of this Act.

TITLE V—COLLECTION ACTIVITIES

SEC. 501. MODIFICATIONS TO LIEN AND LEVY PROVISIONS.

(a) WITHDRAWAL OF CERTAIN NOTICES.—Section 6323 (relating to validity and priority against certain persons) is amended by adding at the end the following new subsection:

"(j) WITHDRAWAL OF NOTICE IN CERTAIN CIRCUMSTANCES.—

"(1) IN GENERAL.—The Secretary may withdraw a notice of a lien filed under this section and this chapter shall be applied as if the withdrawn notice had not been filed, if the Secretary determines that—

"(A) the filing of such notice was premature or otherwise not in accordance with administrative procedures of the Secretary,

"(B) the taxpayer has entered into an agreement under section 6159 to satisfy the tax liability for which the lien was imposed by means of installment payments, unless such agreement provides otherwise,

"(C) the withdrawal of such notice will facilitate the collection of the tax liability, or

"(D) with the consent of the taxpayer or the Taxpayer Advocate, the withdrawal of such notice would be in the best interests of the taxpayer (as determined by the Taxpayer Advocate) and the United States.

Any such withdrawal shall be made by filing notice at the same office as the withdrawn notice. A copy of such notice of withdrawal shall be provided to the taxpayer.

"(2) NOTICE TO CREDIT AGENCIES, ETC.—Upon written request by the taxpayer with respect to whom a notice of a lien was withdrawn under paragraph (1), the Secretary shall promptly make reasonable efforts to notify credit reporting agencies, and any financial institution or creditor whose name and address is specified in such request, of the withdrawal of such notice. Any such request shall be in such form as the Secretary may prescribe.".

(b) RETURN OF LEVIED PROPERTY IN CERTAIN CASES.—Section 6343 (relating to authority to release levy and return property) is amended by adding at the end the following new subsection:

"(d) RETURN OF PROPERTY IN CERTAIN CASES.—If—

"(1) any property has been levied upon, and

"(2) the Secretary determines that—

"(A) the levy on such property was premature or otherwise not in accordance with administrative procedures of the Secretary,

"(B) the taxpayer has entered into an agreement under section 6159 to satisfy the tax liability for which the levy

was imposed by means of installment payments, unless such agreement provides otherwise,

"(C) the return of such property will facilitate the collection of the tax liability, or

"(D) with the consent of the taxpayer or the Taxpayer Advocate, the return of such property would be in the best interests of the taxpayer (as determined by the Taxpayer Advocate) and the United States,

the provisions of subsection (b) shall apply in the same manner as if such property had been wrongly levied upon, except that no interest shall be allowed under subsection (c).".

(d) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date of the enactment of this Act. 26 USC 6323 note.

SEC. 502. MODIFICATIONS TO CERTAIN LEVY EXEMPTION AMOUNTS.

(a) FUEL, ETC.—Paragraph (2) of section 6334(a) (relating to fuel, provisions, furniture, and personal effects exempt from levy) is amended—

(1) by striking "If the taxpayer is the head of a family, so" and inserting "So",

(2) by striking "his household" and inserting "the taxpayer's household", and

(3) by striking "$1,650 ($1,550 in the case of levies issued during 1989)" and inserting "$2,500".

(b) BOOKS, ETC.—Paragraph (3) of section 6334(a) (relating to books and tools of a trade, business, or profession) is amended by striking "$1,100 ($1,050 in the case of levies issued during 1989)" and inserting "$1,250".

(c) INFLATION ADJUSTMENT.—Section 6334 (relating to property exempt from levy) is amended by adding at the end the following new subsection:

"(f) INFLATION ADJUSTMENT.—

"(1) IN GENERAL.—In the case of any calendar year beginning after 1997, each dollar amount referred to in paragraphs (2) and (3) of subsection (a) shall be increased by an amount equal to—

"(A) such dollar amount, multiplied by

"(B) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year, by substituting 'calendar year 1996' for 'calendar year 1992' in subparagraph (B) thereof.

"(2) ROUNDING.—If any dollar amount after being increased under paragraph (1) is not a multiple of $10, such dollar amount shall be rounded to the nearest multiple of $10.".

(d) EFFECTIVE DATE.—The amendments made by this section shall take effect with respect to levies issued after December 31, 1996. 26 USC 6334 note.

SEC. 503. OFFERS-IN-COMPROMISE.

(a) REVIEW REQUIREMENTS.—Subsection (b) of section 7122 (relating to records) is amended by striking "$500." and inserting "$50,000. However, such compromise shall be subject to continuing quality review by the Secretary.".

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act. 26 USC 7122 note.

TITLE VI—INFORMATION RETURNS

SEC. 601. CIVIL DAMAGES FOR FRAUDULENT FILING OF INFORMATION RETURNS.

(a) GENERAL RULE.—Subchapter B of chapter 76 (relating to proceedings by taxpayers and third parties) is amended by redesignating section 7434 as section 7435 and by inserting after section 7433 the following new section:

"SEC. 7434. CIVIL DAMAGES FOR FRAUDULENT FILING OF INFORMATION RETURNS.

"(a) IN GENERAL.—If any person willfully files a fraudulent information return with respect to payments purported to be made to any other person, such other person may bring a civil action for damages against the person so filing such return.

"(b) DAMAGES.—In any action brought under subsection (a), upon a finding of liability on the part of the defendant, the defendant shall be liable to the plaintiff in an amount equal to the greater of $5,000 or the sum of—

"(1) any actual damages sustained by the plaintiff as a proximate result of the filing of the fraudulent information return (including any costs attributable to resolving deficiencies asserted as a result of such filing),

"(2) the costs of the action, and

"(3) in the court's discretion, reasonable attorneys fees.

"(c) PERIOD FOR BRINGING ACTION.—Notwithstanding any other provision of law, an action to enforce the liability created under this section may be brought without regard to the amount in controversy and may be brought only within the later of—

"(1) 6 years after the date of the filing of the fraudulent information return, or

"(2) 1 year after the date such fraudulent information return would have been discovered by exercise of reasonable care.

"(d) COPY OF COMPLAINT FILED WITH IRS—Any person bringing an action under subsection (a) shall provide a copy of the complaint to the Internal Revenue Service upon the filing of such complaint with the court.

"(e) FINDING OF COURT TO INCLUDE CORRECT AMOUNT OF PAYMENT.—The decision of the court awarding damages in an action brought under subsection (a) shall include a finding of the correct amount which should have been reported in the information return.

"(f) INFORMATION RETURN.—For purposes of this section, the term 'information return' means any statement described in section 6724(d)(1)(A).".

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 76 is amended by striking the item relating to section 7434 and inserting the following:

"Sec. 7434. Civil damages for fraudulent filing of information returns.

"Sec. 7435. Cross references.".

26 USC 7434 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to fraudulent information returns filed after the date of the enactment of this Act.

SEC. 602. REQUIREMENT TO CONDUCT REASONABLE INVESTIGATIONS OF INFORMATION RETURNS.

(a) GENERAL RULE.—Section 6201 (relating to assessment authority) is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

"(d) REQUIRED REASONABLE VERIFICATION OF INFORMATION RETURNS.—In any court proceeding, if a taxpayer asserts a reasonable dispute with respect to any item of income reported on an information return filed with the Secretary under subpart B or C of part III of subchapter A of chapter 61 by a third party and the taxpayer has fully cooperated with the Secretary (including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer as reasonably requested by the Secretary), the Secretary shall have the burden of producing reasonable and probative information concerning such deficiency in addition to such information return.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall take effect on the date of the enactment of this Act. 26 USC 6201 note.

TITLE VII—AWARDING OF COSTS AND CERTAIN FEES

SEC. 701. UNITED STATES MUST ESTABLISH THAT ITS POSITION IN PROCEEDING WAS SUBSTANTIALLY JUSTIFIED.

(a) GENERAL RULE.—Subparagraph (A) of section 7430(c)(4) (defining prevailing party) is amended by striking clause (i) and by redesignating clauses (ii) and (iii) as clauses (i) and (ii), respectively.

(b) BURDEN OF PROOF ON UNITED STATES.—Paragraph (4) of section 7430(c) is amended by redesignating subparagraph (B) as subparagraph (C) and by inserting after subparagraph (A) the following new subparagraph:

"(B) EXCEPTION IF UNITED STATES ESTABLISHES THAT ITS POSITION WAS SUBSTANTIALLY JUSTIFIED.—

"(i) GENERAL RULE.—A party shall not be treated as the prevailing party in a proceeding to which subsection (a) applies if the United States establishes that the position of the United States in the proceeding was substantially justified.

"(ii) PRESUMPTION OF NO JUSTIFICATION IF INTERNAL REVENUE SERVICE DID NOT FOLLOW CERTAIN PUBLISHED GUIDANCE.—For purposes of clause (i), the position of the United States shall be presumed not to be substantially justified if the Internal Revenue Service did not follow its applicable published guidance in the administrative proceeding. Such presumption may be rebutted.

"(iii) APPLICABLE PUBLISHED GUIDANCE.—For purposes of clause (ii), the term 'applicable published guidance' means—

"(I) regulations, revenue rulings, revenue procedures, information releases, notices, and announcements, and

"(II) any of the following which are issued to the taxpayer: private letter rulings, technical advice memoranda, and determination letters.".

(c) CONFORMING AMENDMENTS.—

(1) Subparagraph (B) of section 7430(c)(2) is amended by striking "paragraph (4)(B)" and inserting "paragraph (4)(C)".

(2) Subparagraph (C) of section 7430(c)(4), as redesignated by subsection (b), is amended by striking "subparagraph (A)" and inserting "this paragraph".

(3) Sections 6404(g) and 6656(c)(1), as amended by this Act, are each amended by striking "section 7430(c)(4)(A)(iii)" and inserting "section 7430(c)(4)(A)(ii)".

26 USC 6404 note.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

SEC. 702. INCREASED LIMIT ON ATTORNEY FEES.

(a) IN GENERAL.—Paragraph (1) of section 7430(c) (defining reasonable litigation costs) is amended—

(1) by striking "$75" in clause (iii) of subparagraph (B) and inserting "$110",

(2) by striking "an increase in the cost of living or" in clause (iii) of subparagraph (B), and

(3) by adding after clause (iii) the following:

"In the case of any calendar year beginning after 1996, the dollar amount referred to in clause (iii) shall be increased by an amount equal to such dollar amount multiplied by the cost-of-living adjustment determined under section 1(f)(3) for such calendar year, by substituting 'calendar year 1995' for 'calendar year 1992' in subparagraph (B) thereof. If any dollar amount after being increased under the preceding sentence is not a multiple of $10, such dollar amount shall be rounded to the nearest multiple of $10.".

26 USC 7430 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

SEC. 703. FAILURE TO AGREE TO EXTENSION NOT TAKEN INTO ACCOUNT.

(a) IN GENERAL.—Paragraph (1) of section 7430(b) (relating to requirement that administrative remedies be exhausted) is amended by adding at the end the following new sentence: "Any failure to agree to an extension of the time for the assessment of any tax shall not be taken into account for purposes of determining whether the prevailing party meets the requirements of the preceding sentence.".

26 USC 7430 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

SEC. 704. AWARD OF LITIGATION COSTS PERMITTED IN DECLARATORY JUDGMENT PROCEEDINGS.

(a) IN GENERAL.—Subsection (b) of section 7430 is amended by striking paragraph (3) and by redesignating paragraph (4) as paragraph (3).

26 USC 7430 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

TITLE VIII—MODIFICATION TO RECOVERY OF CIVIL DAMAGES FOR UNAUTHORIZED COLLECTION ACTIONS

SEC. 801. INCREASE IN LIMIT ON RECOVERY OF CIVIL DAMAGES FOR UNAUTHORIZED COLLECTION ACTIONS.

(a) GENERAL RULE.—Subsection (b) of section 7433 (relating to damages) is amended by striking "$100,000" and inserting "$1,000,000".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to actions by officers or employees of the Internal Revenue Service after the date of the enactment of this Act. 26 USC 7433 note.

SEC. 802. COURT DISCRETION TO REDUCE AWARD FOR LITIGATION COSTS FOR FAILURE TO EXHAUST ADMINISTRATIVE REMEDIES.

(a) GENERAL RULE.—Paragraph (1) of section 7433(d) (relating to civil damages for certain unauthorized collection actions) is amended to read as follows:

"(1) AWARD FOR DAMAGES MAY BE REDUCED IF ADMINISTRATIVE REMEDIES NOT EXHAUSTED.—The amount of damages awarded under subsection (b) may be reduced if the court determines that the plaintiff has not exhausted the administrative remedies available to such plaintiff within the Internal Revenue Service.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act. 26 USC 7433 note.

TITLE IX—MODIFICATIONS TO PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX

SEC. 901. PRELIMINARY NOTICE REQUIREMENT.

(a) IN GENERAL.—Section 6672 (relating to failure to collect and pay over tax, or attempt to evade or defeat tax) is amended by redesignating subsection (b) as subsection (c) and by inserting after subsection (a) the following new subsection:

"(b) PRELIMINARY NOTICE REQUIREMENT.—

"(1) IN GENERAL.—No penalty shall be imposed under subsection (a) unless the Secretary notifies the taxpayer in writing by mail to an address as determined under section 6212(b) that the taxpayer shall be subject to an assessment of such penalty.

"(2) TIMING OF NOTICE.—The mailing of the notice described in paragraph (1) shall precede any notice and demand of any penalty under subsection (a) by at least 60 days.

"(3) STATUTE OF LIMITATIONS.—If a notice described in paragraph (1) with respect to any penalty is mailed before the expiration of the period provided by section 6501 for the assessment of such penalty (determined without regard to this paragraph), the period provided by such section for the assessment of such penalty shall not expire before the later of—

"(A) the date 90 days after the date on which such notice was mailed, or

"(B) if there is a timely protest of the proposed assessment, the date 30 days after the Secretary makes a final administrative determination with respect to such protest.

"(4) EXCEPTION FOR JEOPARDY.—This subsection shall not apply if the Secretary finds that the collection of the penalty is in jeopardy.".

26 USC 6672 note.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to proposed assessments made after June 30, 1996.

SEC. 902. DISCLOSURE OF CERTAIN INFORMATION WHERE MORE THAN 1 PERSON LIABLE FOR PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX.

(a) IN GENERAL.—Subsection (e) of section 6103 (relating to disclosure to persons having material interest), as amended by section 403, is amended by adding at the end the following new paragraph:

"(9) DISCLOSURE OF CERTAIN INFORMATION WHERE MORE THAN 1 PERSON SUBJECT TO PENALTY UNDER SECTION 6672.—If the Secretary determines that a person is liable for a penalty under section 6672(a) with respect to any failure, upon request in writing of such person, the Secretary shall disclose in writing to such person—

"(A) the name of any other person whom the Secretary has determined to be liable for such penalty with respect to such failure, and

"(B) whether the Secretary has attempted to collect such penalty from such other person, the general nature of such collection activities, and the amount collected.".

26 USC 6103 note.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall take effect on the date of the enactment of this Act.

SEC. 903. RIGHT OF CONTRIBUTION WHERE MORE THAN 1 PERSON LIABLE FOR PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX.

(a) IN GENERAL.—Section 6672 (relating to failure to collect and pay over tax, or attempt to evade or defeat tax) is amended by adding at the end the following new subsection:

"(d) RIGHT OF CONTRIBUTION WHERE MORE THAN 1 PERSON LIABLE FOR PENALTY.—If more than 1 person is liable for the penalty under subsection (a) with respect to any tax, each person who paid such penalty shall be entitled to recover from other persons who are liable for such penalty an amount equal to the excess of the amount paid by such person over such person's proportionate share of the penalty. Any claim for such a recovery may be made only in a proceeding which is separate from, and is not joined or consolidated with—

"(1) an action for collection of such penalty brought by the United States, or

"(2) a proceeding in which the United States files a counterclaim or third-party complaint for the collection of such penalty.".

26 USC 6672 note.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to penalties assessed after the date of the enactment of this Act.

SEC. 904. VOLUNTEER BOARD MEMBERS OF TAX-EXEMPT ORGANIZATIONS EXEMPT FROM PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX.

(a) IN GENERAL.—Section 6672 is amended by adding at the end the following new subsection:

"(e) EXCEPTION FOR VOLUNTARY BOARD MEMBERS OF TAX-EXEMPT ORGANIZATIONS.—No penalty shall be imposed by subsection (a) on any unpaid, volunteer member of any board of trustees or directors of an organization exempt from tax under subtitle A if such member—

"(1) is solely serving in an honorary capacity,

"(2) does not participate in the day-to-day or financial operations of the organization, and

"(3) does not have actual knowledge of the failure on which such penalty is imposed.

The preceding sentence shall not apply if it results in no person being liable for the penalty imposed by subsection (a).".

(b) PUBLIC INFORMATION REQUIREMENTS.— 26 USC 6672 note.

(1) IN GENERAL.—The Secretary of the Treasury or the Secretary's delegate (hereafter in this subsection referred to as the "Secretary") shall take such actions as may be appropriate to ensure that employees are aware of their responsibilities under the Federal tax depository system, the circumstances under which employees may be liable for the penalty imposed by section 6672 of the Internal Revenue Code of 1986, and the responsibility to promptly report to the Internal Revenue Service any failure referred to in subsection (a) of such section 6672. Such actions shall include—

(A) printing of a warning on deposit coupon booklets and the appropriate tax returns that certain employees may be liable for the penalty imposed by such section 6672, and

(B) the development of a special information packet.

(2) DEVELOPMENT OF EXPLANATORY MATERIALS.—The Secretary shall develop materials explaining the circumstances under which board members of tax-exempt organizations (including voluntary and honorary members) may be subject to penalty under section 6672 of such Code. Such materials shall be made available to tax-exempt organizations.

(3) IRS INSTRUCTIONS.—The Secretary shall clarify the instructions to Internal Revenue Service employees on the application of the penalty under section 6672 of such Code with regard to voluntary members of boards of trustees or directors of tax-exempt organizations.

TITLE X—MODIFICATIONS OF RULES RELATING TO SUMMONSES

SEC. 1001. ENROLLED AGENTS INCLUDED AS THIRD-PARTY RECORDKEEPERS.

(a) IN GENERAL.—Paragraph (3) of section 7609(a) (relating to third-party recordkeeper defined) is amended by striking "and" at the end of subparagraph (G), by striking the period at the end of subparagraph (H) and inserting "; and", and by adding at the end the following the subparagraph:

"(I) any enrolled agent.".

26 USC 7609 note.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to summonses issued after the date of the enactment of this Act.

SEC. 1002. SAFEGUARDS RELATING TO DESIGNATED SUMMONSES.

(a) STANDARD OF REVIEW.—Subparagraph (A) of section 6503(k)(2) (defining designated summons) is amended by redesignating clauses (i) and (ii) as clauses (ii) and (iii), respectively, and by inserting before clause (ii) (as so redesignated) the following new clause:

"(i) the issuance of such summons is preceded by a review of such issuance by the regional counsel of the Office of Chief Counsel for the region in which the examination of the corporation is being conducted,".

(b) LIMITATION ON PERSONS TO WHOM DESIGNATED SUMMONS MAY BE ISSUED.—Paragraph (1) of section 6503(k) is amended by striking "with respect to any return of tax by a corporation" and inserting "to a corporation (or to any other person to whom the corporation has transferred records) with respect to any return of tax by such corporation for a taxable year (or other period) for which such corporation is being examined under the coordinated examination program (or any successor program) of the Internal Revenue Service".

(c) CLERICAL AMENDMENT.—Section 6503 is amended by redesignating subsections (k) and (l) (as amended by this section) as subsections (j) and (k), respectively.

26 USC 6503 note.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to summonses issued after the date of the enactment of this Act.

26 USC 6503 note.

SEC. 1003. ANNUAL REPORT TO CONGRESS CONCERNING DESIGNATED SUMMONSES.

Not later than December 31 of each calendar year after 1995, the Secretary of the Treasury or his delegate shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the number of designated summonses (as defined in section 6503(j) of the Internal Revenue Code of 1986) which were issued during the preceding 12 months.

TITLE XI—RELIEF FROM RETROACTIVE APPLICATION OF TREASURY DEPARTMENT REGULATIONS

SEC. 1101. RELIEF FROM RETROACTIVE APPLICATION OF TREASURY DEPARTMENT REGULATIONS.

(a) IN GENERAL.—Subsection (b) of section 7805 (relating to rules and regulations) is amended to read as follows:

"(b) RETROACTIVITY OF REGULATIONS.—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, no temporary, proposed, or final regulation relating to the internal revenue laws shall apply to any taxable period ending before the earliest of the following dates:

"(A) The date on which such regulation is filed with the Federal Register.

"(B) In the case of any final regulation, the date on which any proposed or temporary regulation to which such final regulation relates was filed with the Federal Register.

"(C) The date on which any notice substantially describing the expected contents of any temporary, proposed, or final regulation is issued to the public.

"(2) EXCEPTION FOR PROMPTLY ISSUED REGULATIONS.—Paragraph (1) shall not apply to regulations filed or issued within 18 months of the date of the enactment of the statutory provision to which the regulation relates.

"(3) PREVENTION OF ABUSE.—The Secretary may provide that any regulation may take effect or apply retroactively to prevent abuse.

"(4) CORRECTION OF PROCEDURAL DEFECTS.—The Secretary may provide that any regulation may apply retroactively to correct a procedural defect in the issuance of any prior regulation.

"(5) INTERNAL REGULATIONS.—The limitation of paragraph (1) shall not apply to any regulation relating to internal Treasury Department policies, practices, or procedures.

"(6) CONGRESSIONAL AUTHORIZATION.—The limitation of paragraph (1) may be superseded by a legislative grant from Congress authorizing the Secretary to prescribe the effective date with respect to any regulation.

"(7) ELECTION TO APPLY RETROACTIVELY.—The Secretary may provide for any taxpayer to elect to apply any regulation before the dates specified in paragraph (1).

"(8) APPLICATION TO RULINGS.—The Secretary may prescribe the extent, if any, to which any ruling (including any judicial decision or any administrative determination other than by regulation) relating to the internal revenue laws shall be applied without retroactive effect.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to regulations which relate to statutory provisions enacted on or after the date of the enactment of this Act.

26 USC 7805 note.

TITLE XII—MISCELLANEOUS PROVISIONS

SEC. 1201. PHONE NUMBER OF PERSON PROVIDING PAYEE STATEMENTS REQUIRED TO BE SHOWN ON SUCH STATEMENT.

(a) GENERAL RULE.—The following provisions are each amended by striking "name and address" and inserting "name, address, and phone number of the information contact":

(1) Section 6041(d)(1).
(2) Section 6041A(e)(1).
(3) Section 6042(c)(1).
(4) Section 6044(e)(1).
(5) Section 6045(b)(1).
(6) Section 6049(c)(1)(A).
(7) Section 6050B(b)(1).
(8) Section 6050H(d)(1).
(9) Section 6050I(e)(1).

(10) Section 6050J(e).
(11) Section 6050K(b)(1).
(12) Section 6050N(b)(1).

26 USC 6041 note.

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to statements required to be furnished after December 31, 1996 (determined without regard to any extension).

26 USC 6311 note.

SEC. 1202. REQUIRED NOTICE OF CERTAIN PAYMENTS.

If any payment is received by the Secretary of the Treasury or his delegate from any taxpayer and the Secretary cannot associate such payment with such taxpayer, the Secretary shall make reasonable efforts to notify the taxpayer of such inability within 60 days after the receipt of such payment.

SEC. 1203. UNAUTHORIZED ENTICEMENT OF INFORMATION DISCLOSURE.

(a) IN GENERAL.—Subchapter B of chapter 76 (relating to proceedings by taxpayers and third parties), as amended by section 601(a), is amended by redesignating section 7435 as section 7436 and by inserting after section 7434 the following new section:

"SEC. 7435. CIVIL DAMAGES FOR UNAUTHORIZED ENTICEMENT OF INFORMATION DISCLOSURE.

"(a) IN GENERAL.—If any officer or employee of the United States intentionally compromises the determination or collection of any tax due from an attorney, certified public accountant, or enrolled agent representing a taxpayer in exchange for information conveyed by the taxpayer to the attorney, certified public accountant, or enrolled agent for purposes of obtaining advice concerning the taxpayer's tax liability, such taxpayer may bring a civil action for damages against the United States in a district court of the United States. Such civil action shall be the exclusive remedy for recovering damages resulting from such actions.

"(b) DAMAGES.—In any action brought under subsection (a), upon a finding of liability on the part of the defendant, the defendant shall be liable to the plaintiff in an amount equal to the lesser of $500,000 or the sum of—

"(1) actual, direct economic damages sustained by the plaintiff as a proximate result of the information disclosure, and

"(2) the costs of the action.

Damages shall not include the taxpayer's liability for any civil or criminal penalties, or other losses attributable to incarceration or the imposition of other criminal sanctions.

"(c) PAYMENT AUTHORITY.—Claims pursuant to this section shall be payable out of funds appropriated under section 1304 of title 31, United States Code.

"(d) PERIOD FOR BRINGING ACTION.—Notwithstanding any other provision of law, an action to enforce liability created under this section may be brought without regard to the amount in controversy and may be brought only within 2 years after the date the actions creating such liability would have been discovered by exercise of reasonable care.

"(e) MANDATORY STAY.—Upon a certification by the Commissioner or the Commissioner's delegate that there is an ongoing investigation or prosecution of the taxpayer, the district court before which an action under this section is pending shall stay all proceedings with respect to such action pending the conclusion of the investigation or prosecution.

"(f) CRIME-FRAUD EXCEPTION.—Subsection (a) shall not apply to information conveyed to an attorney, certified public accountant, or enrolled agent for the purpose of perpetrating a fraud or crime.".

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 76, as amended by section 601(b), is amended by striking the item relating to section 7435 and by adding at the end the following new items:

"Sec. 7435. Civil damages for unauthorized enticement of information disclosure.
"Sec. 7436. Cross references.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to actions after the date of the enactment of this Act. 26 USC 7435 note.

SEC. 1204. ANNUAL REMINDERS TO TAXPAYERS WITH OUTSTANDING DELINQUENT ACCOUNTS.

(a) IN GENERAL.—Chapter 77 (relating to miscellaneous provisions) is amended by adding at the end the following new section:

"SEC. 7524. ANNUAL NOTICE OF TAX DELINQUENCY.

"Not less often than annually, the Secretary shall send a written notice to each taxpayer who has a tax delinquent account of the amount of the tax delinquency as of the date of the notice.".

(b) CLERICAL AMENDMENT.—The table of sections for chapter 77 is amended by adding at the end the following new item:

"Sec. 7524. Annual notice of tax delinquency.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to calendar years after 1996. 26 USC 7524 note.

SEC. 1205. 5-YEAR EXTENSION OF AUTHORITY FOR UNDERCOVER OPERATIONS.

(a) IN GENERAL.—Paragraph (3) of section 7601(c) of the Anti-Drug Abuse Act of 1988 is amended by striking all that follows "this Act" and inserting a period.

(b) RESTORATION OF AUTHORITY FOR 5 YEARS.—Subsection (c) of section 7608 is amended by adding at the end the following new paragraph:

"(6) APPLICATION OF SECTION.—The provisions of this subsection—

"(A) shall apply after November 17, 1988, and before January 1, 1990, and

"(B) shall apply after the date of the enactment of this paragraph and before January 1, 2001.

All amounts expended pursuant to this subsection during the period described in subparagraph (B) shall be recovered to the extent possible, and deposited in the Treasury of the United States as miscellaneous receipts, before January 1, 2001.".

(c) ENHANCED OVERSIGHT.—

(1) ADDITIONAL INFORMATION REQUIRED IN REPORTS TO CONGRESS.—Subparagraph (B) of section 7608(c)(4) is amended—

(A) by striking "preceding the period" in clause (ii),

(B) by striking "and" at the end of clause (ii), and

(C) by striking clause (iii) and inserting the following:

"(iii) the number, by programs, of undercover investigative operations closed in the 1-year period for which such report is submitted, and

"(iv) the following information with respect to each undercover investigative operation pending as of the

end of the 1-year period for which such report is submitted or closed during such 1-year period—

"(I) the date the operation began and the date of the certification referred to in the last sentence of paragraph (1),

"(II) the total expenditures under the operation and the amount and use of the proceeds from the operation,

"(III) a detailed description of the operation including the potential violation being investigated and whether the operation is being conducted under grand jury auspices, and

"(IV) the results of the operation including the results of criminal proceedings.".

(2) AUDITS REQUIRED WITHOUT REGARD TO AMOUNTS INVOLVED.—Subparagraph (C) of section 7608(c)(5) is amended to read as follows:

"(C) UNDERCOVER INVESTIGATIVE OPERATION.—The term 'undercover investigative operation' means any undercover investigative operation of the Service; except that, for purposes of subparagraphs (A) and (C) of paragraph (4), such term only includes an operation which is exempt from section 3302 or 9102 of title 31, United States Code.".

26 USC 7608 note.

(3) EFFECTIVE DATE.—The amendments made by this subsection shall take effect on the date of the enactment of this Act.

SEC. 1206. DISCLOSURE OF FORM 8300 INFORMATION ON CASH TRANSACTIONS.

(a) IN GENERAL.—Subsection (l) of section 6103 (relating to disclosure of returns and return information for purposes other than tax administration) is amended by adding at the end the following new paragraph:

"(15) DISCLOSURE OF RETURNS FILED UNDER SECTION 6050I.—The Secretary may, upon written request, disclose to officers and employees of—

"(A) any Federal agency,

"(B) any agency of a State or local government, or

"(C) any agency of the government of a foreign country,

information contained on returns filed under section 6050I. Any such disclosure shall be made on the same basis, and subject to the same conditions, as apply to disclosures of information on reports filed under section 5313 of title 31, United States Code; except that no disclosure under this paragraph shall be made for purposes of the administration of any tax law.".

(b) CONFORMING AMENDMENTS.—

(1) Subsection (i) of section 6103 is amended by striking paragraph (8).

(2) Subparagraph (A) of section 6103(p)(3) is amended—

(A) by striking "(7)(A)(ii), or (8)" and inserting "or (7)(A)(ii)", and

(B) by striking "or (14)" and inserting "(14), or (15)".

(3) The material preceding subparagraph (A) of section 6103(p)(4) is amended—

(A) by striking "(5), or (8)" and inserting "or (5)",

(B) by striking "(i)(3)(B)(i), or (8)" and inserting "(i)(3)(B)(i),", and

(C) by striking "or (12)" and inserting "(12), or (15)".

(4) Clause (ii) of section 6103(p)(4)(F) is amended—

(A) by striking "(5), or (8)" and inserting "or (5)", and

(B) by striking "or (14)" and inserting "(14), or (15)".

(5) Paragraph (2) of section 7213(a) is amended by striking "or (12)" and inserting "(12), or (15)".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date of the enactment of this Act. 26 USC 6103 note.

SEC. 1207. DISCLOSURE OF RETURNS AND RETURN INFORMATION TO DESIGNEE OF TAXPAYER.

Subsection (c) of section 6103 (relating to disclosure of returns and return information to designee of taxpayer) is amended by striking "written request for or consent to such disclosure" and inserting "request for or consent to such disclosure".

SEC. 1208. STUDY OF NETTING OF INTEREST ON OVERPAYMENTS AND LIABILITIES.

(a) IN GENERAL.—The Secretary of the Treasury or his delegate shall—

(1) conduct a study of the manner in which the Internal Revenue Service has implemented the netting of interest on overpayments and underpayments and of the policy and administrative implications of global netting, and

(2) before submitting the report of such study, hold a public hearing to receive comments on the matters included in such study.

(b) REPORT.—The report of such study shall be submitted not later than 6 months after the date of the enactment of this Act to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate.

SEC. 1209. EXPENSES OF DETECTION OF UNDERPAYMENTS AND FRAUD, ETC.

(a) IN GENERAL.—Section 7623 (relating to expenses of detection and punishment of frauds) is amended to read as follows:

"SEC. 7623. EXPENSES OF DETECTION OF UNDERPAYMENTS AND FRAUD, ETC.

"The Secretary, under regulations prescribed by the Secretary, is authorized to pay such sums as he deems necessary for— Regulations.

"(1) detecting underpayments of tax, and

"(2) detecting and bringing to trial and punishment persons guilty of violating the internal revenue laws or conniving at the same,

in cases where such expenses are not otherwise provided for by law. Any amount payable under the preceding sentence shall be paid from the proceeds of amounts (other than interest) collected by reason of the information provided, and any amount so collected shall be available for such payments.".

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 78 is amended by striking the item relating to section 7623 and inserting the following new item:

"Sec. 7623. Expenses of detection of underpayments and fraud, etc.".

26 USC 7623 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date which is 6 months after the date of the enactment of this Act.

26 USC 7623 note.

(d) REPORT.—The Secretary of the Treasury or his delegate shall submit an annual report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the payments under section 7623 of the Internal Revenue Code of 1986 during the year and on the amounts collected for which such payments were made.

SEC. 1210. USE OF PRIVATE DELIVERY SERVICES FOR TIMELY-MAILING-AS-TIMELY-FILING RULE.

Section 7502 (relating to timely mailing treated as timely filing and paying) is amended by adding at the end the following new subsection:

"(f) TREATMENT OF PRIVATE DELIVERY SERVICES.—

"(1) IN GENERAL.—Any reference in this section to the United States mail shall be treated as including a reference to any designated delivery service, and any reference in this section to a postmark by the United States Postal Service shall be treated as including a reference to any date recorded or marked as described in paragraph (2)(C) by any designated delivery service.

"(2) DESIGNATED DELIVERY SERVICE.—For purposes of this subsection, the term 'designated delivery service' means any delivery service provided by a trade or business if such service is designated by the Secretary for purposes of this section. The Secretary may designate a delivery service under the preceding sentence only if the Secretary determines that such service—

"(A) is available to the general public,

"(B) is at least as timely and reliable on a regular basis as the United States mail,

"(C) records electronically to its data base, kept in the regular course of its business, or marks on the cover in which any item referred to in this section is to be delivered, the date on which such item was given to such trade or business for delivery, and

"(D) meets such other criteria as the Secretary may prescribe.

"(3) EQUIVALENTS OF REGISTERED AND CERTIFIED MAIL.—The Secretary may provide a rule similar to the rule of paragraph (1) with respect to any service provided by a designated delivery service which is substantially equivalent to United States registered or certified mail.".

26 USC 7803 note.

SEC. 1211. REPORTS ON MISCONDUCT OF IRS EMPLOYEES.

On or before June 1 of each calendar year after 1996, the Secretary of the Treasury shall submit to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate a report on—

(1) all categories of instances involving the misconduct of employees of the Internal Revenue Service during the preceding calendar year, and

(2) the disposition during the preceding calendar year of any such instances (without regard to the year of the misconduct).

TITLE XIII—REVENUE OFFSETS

Subtitle A—Application of Failure-to-Pay Penalty to Substitute Returns

SEC. 1301. APPLICATION OF FAILURE-TO-PAY PENALTY TO SUBSTITUTE RETURNS.

(a) GENERAL RULE.—Section 6651 (relating to failure to file tax return or to pay tax) is amended by adding at the end the following new subsection:

"(g) TREATMENT OF RETURNS PREPARED BY SECRETARY UNDER SECTION 6020(b).—In the case of any return made by the Secretary under section 6020(b)—

"(1) such return shall be disregarded for purposes of determining the amount of the addition under paragraph (1) of subsection (a), but

"(2) such return shall be treated as the return filed by the taxpayer for purposes of determining the amount of the addition under paragraphs (2) and (3) of subsection (a).".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply in the case of any return the due date for which (determined without regard to extensions) is after the date of the enactment of this Act.

26 USC 6651 note.

Subtitle B—Exicse Taxes on Amounts of Private Excess Benefits

SEC. 1311. EXCISE TAXES FOR FAILURE BY CERTAIN CHARITABLE ORGANIZATIONS TO MEET CERTAIN QUALIFICATION REQUIREMENTS.

(a) IN GENERAL.—Chapter 42 (relating to private foundations and certain other tax-exempt organizations) is amended by redesignating subchapter D as subchapter E and by inserting after subchapter C the following new subchapter:

"Subchapter D—Failure by Certain Charitable Organizations To Meet Certain Qualification Requirements

"Sec. 4958. Taxes on excess benefit transactions.

"SEC. 4958. TAXES ON EXCESS BENEFIT TRANSACTIONS.

"(a) INITIAL TAXES.—

"(1) ON THE DISQUALIFIED PERSON.—There is hereby imposed on each excess benefit transaction a tax equal to 25 percent of the excess benefit. The tax imposed by this paragraph shall be paid by any disqualified person referred to in subsection (f)(1) with respect to such transaction.

"(2) ON THE MANAGEMENT.—In any case in which a tax is imposed by paragraph (1), there is hereby imposed on the participation of any organization manager in the excess benefit transaction, knowing that it is such a transaction, a tax equal to 10 percent of the excess benefit, unless such participation is not willful and is due to reasonable cause. The tax imposed by this paragraph shall be paid by any organization manager who participated in the excess benefit transaction.

"(b) ADDITIONAL TAX ON THE DISQUALIFIED PERSON.—In any case in which an initial tax is imposed by subsection (a)(1) on an excess benefit transaction and the excess benefit involved in such transaction is not corrected within the taxable period, there is hereby imposed a tax equal to 200 percent of the excess benefit involved. The tax imposed by this subsection shall be paid by any disqualified person referred to in subsection (f)(1) with respect to such transaction.

"(c) EXCESS BENEFIT TRANSACTION; EXCESS BENEFIT.—For purposes of this section—

"(1) EXCESS BENEFIT TRANSACTION.—

"(A) IN GENERAL.—The term 'excess benefit transaction' means any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly to or for the use of any disqualified person if the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) received for providing such benefit. For purposes of the preceding sentence, an economic benefit shall not be treated as consideration for the performance of services unless such organization clearly indicated its intent to so treat such benefit.

"(B) EXCESS BENEFIT.—The term 'excess benefit' means the excess referred to in subparagraph (A).

"(2) AUTHORITY TO INCLUDE CERTAIN OTHER PRIVATE INUREMENT.—To the extent provided in regulations prescribed by the Secretary, the term 'excess benefit transaction' includes any transaction in which the amount of any economic benefit provided to or for the use of a disqualified person is determined in whole or in part by the revenues of 1 or more activities of the organization but only if such transaction results in inurement not permitted under paragraph (3) or (4) of section 501(c), as the case may be. In the case of any such transaction, the excess benefit shall be the amount of the inurement not so permitted.

"(d) SPECIAL RULES.—For purposes of this section—

"(1) JOINT AND SEVERAL LIABILITY.—If more than 1 person is liable for any tax imposed by subsection (a) or subsection (b), all such persons shall be jointly and severally liable for such tax.

"(2) LIMIT FOR MANAGEMENT.—With respect to any 1 excess benefit transaction, the maximum amount of the tax imposed by subsection (a)(2) shall not exceed $10,000.

"(e) APPLICABLE TAX-EXEMPT ORGANIZATION.—For purposes of this subchapter, the term 'applicable tax-exempt organization' means—

"(1) any organization which (without regard to any excess benefit) would be described in paragraph (3) or (4) of section 501(c) and exempt from tax under section 501(a), and

"(2) any organization which was described in paragraph (1) at any time during the 5-year period ending on the date of the transaction.

Such term shall not include a private foundation (as defined in section 509(a)).

"(f) OTHER DEFINITIONS.—For purposes of this section—

"(1) DISQUALIFIED PERSON.—The term 'disqualified person' means, with respect to any transaction—

"(A) any person who was, at any time during the 5-year period ending on the date of such transaction, in a position to exercise substantial influence over the affairs of the organization,

"(B) a member of the family of an individual described in subparagraph (A), and

"(C) a 35-percent controlled entity.

"(2) ORGANIZATION MANAGER.—The term 'organization manager' means, with respect to any applicable tax-exempt organization, any officer, director, or trustee of such organization (or any individual having powers or responsibilities similar to those of officers, directors, or trustees of the organization).

"(3) 35-PERCENT CONTROLLED ENTITY.—

"(A) IN GENERAL.—The term '35-percent controlled entity' means—

"(i) a corporation in which persons described in subparagraph (A) or (B) of paragraph (1) own more than 35 percent of the total combined voting power,

"(ii) a partnership in which such persons own more than 35 percent of the profits interest, and

"(iii) a trust or estate in which such persons own more than 35 percent of the beneficial interest.

"(B) CONSTRUCTIVE OWNERSHIP RULES.—Rules similar to the rules of paragraphs (3) and (4) of section 4946(a) shall apply for purposes of this paragraph.

"(4) FAMILY MEMBERS.—The members of an individual's family shall be determined under section 4946(d); except that such members also shall include the brothers and sisters (whether by the whole or half blood) of the individual and their spouses.

"(5) TAXABLE PERIOD.—The term 'taxable period' means, with respect to any excess benefit transaction, the period beginning with the date on which the transaction occurs and ending on the earliest of—

"(A) the date of mailing a notice of deficiency under section 6212 with respect to the tax imposed by subsection (a)(1), or

"(B) the date on which the tax imposed by subsection (a)(1) is assessed.

"(6) CORRECTION.—The terms 'correction' and 'correct' mean, with respect to any excess benefit transaction, undoing the excess benefit to the extent possible, and taking any additional measures necessary to place the organization in a financial position not worse than that in which it would be if the disqualified person were dealing under the highest fiduciary standards.".

(b) APPLICATION OF PRIVATE INUREMENT RULE TO TAX-EXEMPT ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—

(1) IN GENERAL.—Paragraph (4) of section 501(c) is amended by inserting "(A)" after "(4)" and by adding at the end the following:

"(B) Subparagraph (A) shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.".

26 USC 501 note.

(2) SPECIAL RULE FOR CERTAIN COOPERATIVES.—In the case of an organization operating on a cooperative basis which, before the date of the enactment of this Act, was determined by the Secretary of the Treasury or his delegate, to be described in section 501(c)(4) of the Internal Revenue Code of 1986 and exempt from tax under section 501(a) of such Code, the allocation or return of net margins or capital to the members of such organization in accordance with its incorporating statute and bylaws shall not be treated for purposes of such Code as the inurement of the net earnings of such organization to the benefit of any private shareholder or individual. The preceding sentence shall apply only if such statute and bylaws are substantially as such statute and bylaws were in existence on the date of the enactment of this Act.

(c) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) Subsection (e) of section 4955 is amended—

(A) by striking "SECTION 4945" in the heading and inserting "SECTIONS 4945 AND 4958", and

(B) by inserting before the period "or an excess benefit for purposes of section 4958".

(2) Subsections (a), (b), and (c) of section 4963 are each amended by inserting "4958," after "4955,".

(3) Subsection (e) of section 6213 is amended by inserting "4958 (relating to private excess benefit)," before "4971".

(4) Paragraphs (2) and (3) of section 7422(g) are each amended by inserting "4958," after "4955,".

(5) Subsection (b) of section 7454 is amended by inserting "or whether an organization manager (as defined in section 4958(f)(2)) has 'knowingly' participated in an excess benefit transaction (as defined in section 4958(c))," after "section 4912(b),".

(6) The table of subchapters for chapter 42 is amended by striking the last item and inserting the following:

"SUBCHAPTER D. Failure by certain charitable organizations to meet certain qualification requirements.

"SUBCHAPTER E. Abatement of first and second tier taxes in certain cases.".

(d) EFFECTIVE DATES.—

26 USC 4955 note.

(1) IN GENERAL.—The amendments made by this section (other than subsection (b)) shall apply to excess benefit transactions occurring on or after September 14, 1995.

26 USC 4955 note.

(2) BINDING CONTRACTS.—The amendments referred to in paragraph (1) shall not apply to any benefit arising from a transaction pursuant to any written contract which was binding on September 13, 1995, and at all times thereafter before such transaction occurred.

26 USC 501 note.

(3) APPLICATION OF PRIVATE INUREMENT RULE TO TAX-EXEMPT ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—

(A) IN GENERAL.—The amendment made by subsection (b) shall apply to inurement occurring on or after September 14, 1995.

(B) BINDING CONTRACTS.—The amendment made by subsection (b) shall not apply to any inurement occurring before January 1, 1997, pursuant to a written contract which was binding on September 13, 1995, and at all times thereafter before such inurement occurred.

SEC. 1312. REPORTING OF CERTAIN EXCISE TAXES AND OTHER INFORMATION.

(a) REPORTING BY ORGANIZATIONS DESCRIBED IN SECTION 501(c)(3).—Subsection (b) of section 6033 (relating to certain organizations described in section 501(c)(3)) is amended by striking "and" at the end of paragraph (9), by redesignating paragraph (10) as paragraph (14), and by inserting after paragraph (9) the following new paragraphs:

"(10) the respective amounts (if any) of the taxes paid by the organization during the taxable year under the following provisions:

"(A) section 4911 (relating to tax on excess expenditures to influence legislation),

"(B) section 4912 (relating to tax on disqualifying lobbying expenditures of certain organizations), and

"(C) section 4955 (relating to taxes on political expenditures of section 501(c)(3) organizations),

"(11) the respective amounts (if any) of the taxes paid by the organization, or any disqualified person with respect to such organization, during the taxable year under section 4958 (relating to taxes on private excess benefit from certain charitable organizations),

"(12) such information as the Secretary may require with respect to any excess benefit transaction (as defined in section 4958),

"(13) such information with respect to disqualified persons as the Secretary may prescribe, and".

(b) ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—Section 6033 is amended by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) the following new subsection:

"(f) CERTAIN ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—Every organization described in section 501(c)(4) which is subject to the requirements of subsection (a) shall include on the return required under subsection (a) the information referred to in paragraphs (11), (12) and (13) of subsection (b) with respect to such organization.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to returns for taxable years beginning after the date of the enactment of this Act. 26 USC 6033 note.

SEC. 1313. EXEMPT ORGANIZATIONS REQUIRED TO PROVIDE COPY OF RETURN.

(a) REQUIREMENT TO PROVIDE COPY.—

(1) Subparagraph (A) of section 6104(e)(1) (relating to public inspection of annual returns) is amended to read as follows:

"(A) IN GENERAL.—During the 3-year period beginning on the filing date—

"(i) a copy of the annual return filed under section 6033 (relating to returns by exempt organizations) by any organization to which this paragraph applies shall be made available by such organization for inspection during regular business hours by any individual at

the principal office of such organization and, if such organization regularly maintains 1 or more regional or district offices having 3 or more employees, at each such regional or district office, and

"(ii) upon request of an individual made at such principal office or such a regional or district office, a copy of such annual return shall be provided to such individual without charge other than a reasonable fee for any reproduction and mailing costs.

The request described in clause (ii) must be made in person or in writing. If the request under clause (ii) is made in person, such copy shall be provided immediately and, if made in writing, shall be provided within 30 days.".

(2) Clause (ii) of section 6104(e)(2)(A) is amended by inserting before the period at the end the following: "(and, upon request of an individual made at such principal office or such a regional or district office, a copy of the material requested to be available for inspection under this subparagraph shall be provided (in accordance with the last sentence of paragraph (1)(A)) to such individual without charge other than reasonable fee for any reproduction and mailing costs)".

(3) Subsection (e) of section 6104 is amended by adding at the end the following new paragraph:

"(3) LIMITATION.—Paragraph (1)(A)(ii) (and the corresponding provision of paragraph (2)) shall not apply to any request if, in accordance with regulations promulgated by the Secretary, the organization has made the requested documents widely available, or, the Secretary determines, upon application by an organization, that such request is part of a harassment campaign and that compliance with such request is not in the public interest.".

(b) INCREASE IN PENALTY FOR WILLFUL FAILURE TO ALLOW PUBLIC INSPECTION OF CERTAIN RETURNS, ETC.—Section 6685 is amended by striking "$1,000" and inserting "$5,000".

26 USC 6104 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to requests made on or after the 60th day after the Secretary of the Treasury first issues the regulations referred to section 6104(e)(3) of the Internal Revenue Code of 1986 (as added by subsection (a)(3)).

SEC. 1314. INCREASE IN PENALTIES ON EXEMPT ORGANIZATIONS FOR FAILURE TO FILE COMPLETE AND TIMELY ANNUAL RETURNS.

(a) IN GENERAL.—Subparagraph (A) of section 6652(c)(1) (relating to annual returns under section 6033) is amended by striking "$10" and inserting "$20" and by striking "$5,000" and inserting "$10,000".

(b) LARGER PENALTY ON ORGANIZATIONS HAVING GROSS RECEIPTS IN EXCESS OF $1,000,000.—Subparagraph (A) of section 6652(c)(1) is amended by adding at the end the following new sentence: "In the case of an organization having gross receipts exceeding $1,000,000 for any year, with respect to the return required under section 6033 for such year, the first sentence of this subparagraph shall be applied by substituting '$100' for '$20' and, in lieu of applying the second sentence of this subparagraph, the maximum penalty under this subparagraph shall not exceed $50,000.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to returns for taxable years ending on or after the date of the enactment of this Act. 26 USC 6652 note.

Approved July 30, 1996.

LEGISLATIVE HISTORY—H.R. 2337:

HOUSE REPORTS: No. 104–506 (Comm. on Ways and Means).
CONGRESSIONAL RECORD, Vol. 142 (1996):
Apr. 16, considered and passed House.
July 11, considered and passed Senate.
WEEKLY COMPILATION OF PRESIDENTIAL DOCUMENTS, Vol. 32 (1996):
July 30, Presidential remarks.

○

104TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
2d Session } { 104–506

TAXPAYER BILL OF RIGHTS 2

MARCH 28, 1996.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ARCHER, from the Committee on Ways and Means, submitted the following

REPORT

[To accompany H.R. 2337]

[Including cost estimate of the Congressional Budget Office]

The Committee on Ways and Means, to whom was referred the bill (H.R. 2337) to amend the Internal Revenue Code of 1986 to provide for increased taxpayer protections, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

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29–006

The amendment is as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. SHORT TITLE; AMENDMENT OF 1986 CODE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Taxpayer Bill of Rights 2".

(b) AMENDMENT OF 1986 CODE.—Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

(c) TABLE OF CONTENTS.—

TITLE I—TAXPAYER ADVOCATE

SEC. 101. ESTABLISHMENT OF POSITION OF TAXPAYER ADVOCATE WITHIN INTERNAL REVENUE SERVICE.

(a) GENERAL RULE.—Section 7802 (relating to Commissioner of Internal Revenue; Assistant Commissioner (Employee Plans and Exempt Organizations)) is amended by adding at the end the following new subsection:

"(d) OFFICE OF TAXPAYER ADVOCATE.—

"(1) IN GENERAL.—There is established in the Internal Revenue Service an office to be known as the 'Office of the Taxpayer Advocate'. Such office shall be under the supervision and direction of an official to be known as the 'Taxpayer Advocate' who shall be appointed by and report directly to the Commissioner of Internal Revenue. The Taxpayer Advocate shall be entitled to compensation at the same rate as the highest level official reporting directly to the Deputy Commissioner of the Internal Revenue Service.

"(2) FUNCTIONS OF OFFICE.—

"(A) IN GENERAL.—It shall be the function of the Office of Taxpayer Advocate to—

"(i) assist taxpayers in resolving problems with the Internal Revenue Service,

"(ii) identify areas in which taxpayers have problems in dealings with the Internal Revenue Service,

"(iii) to the extent possible, propose changes in the administrative practices of the Internal Revenue Service to mitigate problems identified under clause (ii), and

"(iv) identify potential legislative changes which may be appropriate to mitigate such problems.

"(B) ANNUAL REPORTS.—

"(i) OBJECTIVES.—Not later than June 30 of each calendar year after 1995, the Taxpayer Advocate shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the objectives of the Taxpayer Advocate for the fiscal year beginning in such calendar year. Any such report shall contain full and substantive analysis, in addition to statistical information.

"(ii) ACTIVITIES.—Not later than December 31 of each calendar year after 1995, the Taxpayer Advocate shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the activities of the Taxpayer Advocate during the fiscal year ending during such calendar year. Any such re-

port shall contain full and substantive analysis, in addition to statistical information, and shall—

"(I) identify the initiatives the Taxpayer Advocate has taken on improving taxpayer services and Internal Revenue Service responsiveness,

"(II) contain recommendations received from individuals with the authority to issue Taxpayer Assistance Orders under section 7811,

"(III) contain a summary of at least 20 of the most serious problems encountered by taxpayers, including a description of the nature of such problems,

"(IV) contain an inventory of the items described in subclauses (I), (II), and (III) for which action has been taken and the result of such action,

"(V) contain an inventory of the items described in subclauses (I), (II), and (III) for which action remains to be completed and the period during which each item has remained on such inventory,

"(VI) contain an inventory of the items described in subclauses (II) and (III) for which no action has been taken, the period during which each item has remained on such inventory, the reasons for the inaction, and identify any Internal Revenue Service official who is responsible for such inaction,

"(VII) identify any Taxpayer Assistance Order which was not honored by the Internal Revenue Service in a timely manner, as specified under section 7811(b),

"(VIII) contain recommendations for such administrative and legislative action as may be appropriate to resolve problems encountered by taxpayers,

"(IX) describe the extent to which regional problem resolution officers participate in the selection and evaluation of local problem resolution officers, and

"(X) include such other information as the Taxpayer Advocate may deem advisable.

"(iii) REPORT TO BE SUBMITTED DIRECTLY.—Each report required under this subparagraph shall be provided directly to the Committees referred to in clauses (i) and (ii) without any prior review or comment from the Commissioner, the Secretary of the Treasury, any other officer or employee of the Department of the Treasury, or the Office of Management and Budget.

"(3) RESPONSIBILITIES OF COMMISSIONER.—The Commissioner of Internal Revenue shall establish procedures requiring a formal response to all recommendations submitted to the Commissioner by the Taxpayer Advocate within 3 months after submission to the Commissioner.".

(b) CONFORMING AMENDMENTS.—

(1) Section 7811 (relating to Taxpayer Assistance Orders) is amended—

(A) by striking "the Office of Ombudsman" in subsection (a) and inserting "the Office of the Taxpayer Advocate", and

(B) by striking "Ombudsman" each place it appears (including in the headings of subsections (e) and (f)) and inserting "Taxpayer Advocate".

(2) The heading for section 7802 is amended to read as follows:

"SEC. 7802. COMMISSIONER OF INTERNAL REVENUE; ASSISTANT COMMISSIONERS; TAXPAYER ADVOCATE."

(3) The table of sections for subchapter A of chapter 80 is amended by striking the item relating to section 7802 and inserting the following new item:

"Sec. 7802. Commissioner of Internal Revenue; Assistant Commissioners; Taxpayer Advocate."

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date of the enactment of this Act.

SEC. 102. EXPANSION OF AUTHORITY TO ISSUE TAXPAYER ASSISTANCE ORDERS.

(a) TERMS OF ORDERS.—Subsection (b) of section 7811 (relating to terms of Taxpayer Assistance Orders) is amended—

(1) by inserting "within a specified time period" after "the Secretary", and

(2) by inserting "take any action as permitted by law," after "cease any action,".

(b) LIMITATION ON AUTHORITY TO MODIFY OR RESCIND.—Section 7811(c) (relating to authority to modify or rescind) is amended to read as follows:

"(c) AUTHORITY TO MODIFY OR RESCIND.—Any Taxpayer Assistance Order issued by the Taxpayer Advocate under this section may be modified or rescinded—

"(1) only by the Taxpayer Advocate, the Commissioner of Internal Revenue, or the Deputy Commissioner of Internal Revenue, and

"(2) only if a written explanation of the reasons for the modification or rescission is provided to the Taxpayer Advocate."

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date of the enactment of this Act.

TITLE II—MODIFICATIONS TO INSTALLMENT AGREEMENT PROVISIONS

SEC. 201. NOTIFICATION OF REASONS FOR TERMINATION OF INSTALLMENT AGREEMENTS.

(a) TERMINATIONS.—Subsection (b) of section 6159 (relating to extent to which agreements remain in effect) is amended by adding at the end the following new paragraph:

"(5) NOTICE REQUIREMENTS.—The Secretary may not take any action under paragraph (2), (3), or (4) unless—

"(A) a notice of such action is provided to the taxpayer not later than the day 30 days before the date of such action, and

"(B) such notice includes an explanation why the Secretary intends to take such action.

The preceding sentence shall not apply in any case in which the Secretary believes that collection of any tax to which an agreement under this section relates is in jeopardy."

(b) CONFORMING AMENDMENT.—Paragraph (3) of section 6159(b) is amended to read as follows:

"(3) SUBSEQUENT CHANGE IN FINANCIAL CONDITIONS.—If the Secretary makes a determination that the financial condition of a taxpayer with whom the Secretary has entered into an agreement under subsection (a) has significantly changed, the Secretary may alter, modify, or terminate such agreement."

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date 6 months after the date of the enactment of this Act.

SEC. 202. ADMINISTRATIVE REVIEW OF TERMINATION OF INSTALLMENT AGREEMENT.

(a) GENERAL RULE.—Section 6159 (relating to agreements for payment of tax liability in installments) is amended by adding at the end the following new subsection:

"(c) ADMINISTRATIVE REVIEW.—The Secretary shall establish procedures for an independent administrative review of terminations of installment agreements under this section for taxpayers who request such a review."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall take effect on January 1, 1997.

TITLE III—ABATEMENT OF INTEREST AND PENALTIES

SEC. 301. EXPANSION OF AUTHORITY TO ABATE INTEREST.

(a) GENERAL RULE.—Paragraph (1) of section 6404(e) (relating to abatement of interest in certain cases) is amended—

(1) by inserting "unreasonable" before "error" each place it appears in subparagraphs (A) and (B), and

(2) by striking "in performing a ministerial act" each place it appears and inserting "in performing a ministerial or managerial act".

(b) CLERICAL AMENDMENT.—The subsection heading for subsection (e) of section 6404 is amended—

(1) by striking "ASSESSMENTS" and inserting "ABATEMENT", and

(2) by inserting "UNREASONABLE" before "ERRORS".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to interest accruing with respect to deficiencies or payments for taxable years beginning after the date of the enactment of this Act.

SEC. 302. REVIEW OF IRS FAILURE TO ABATE INTEREST.

(a) IN GENERAL.—Section 6404 is amended by adding at the end the following new subsection:

"(g) REVIEW OF DENIAL OF REQUEST FOR ABATEMENT OF INTEREST.—

"(1) IN GENERAL.—The Tax Court shall have jurisdiction over any action brought by a taxpayer who meets the requirements referred to in section 7430(c)(4)(A)(iii) to determine whether the Secretary's failure to abate interest under this section was an abuse of discretion, and may order an abatement, if such action is brought within 180 days after the date of the mailing of the Secretary's final determination not to abate such interest.

"(2) SPECIAL RULES.—

"(A) DATE OF MAILING.—Rules similar to the rules of section 6213 shall apply for purposes of determining the date of the mailing referred to in paragraph (1).

"(B) RELIEF.—Rules similar to the rules of section 6512(b) shall apply for purposes of this subsection.

"(C) REVIEW.—An order of the Tax Court under this subsection shall be reviewable in the same manner as a decision of the Tax Court, but only with respect to the matters determined in such order."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to requests for abatement after the date of the enactment of this Act.

SEC. 303. EXTENSION OF INTEREST-FREE PERIOD FOR PAYMENT OF TAX AFTER NOTICE AND DEMAND.

(a) GENERAL RULE.—Paragraph (3) of section 6601(e) (relating to payments made within 10 days after notice and demand) is amended to read as follows:

"(3) PAYMENTS MADE WITHIN SPECIFIED PERIOD AFTER NOTICE AND DEMAND.—If notice and demand is made for payment of any amount and if such amount is paid within 21 calendar days (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000) after the date of such notice and demand, interest under this section on the amount so paid shall not be imposed for the period after the date of such notice and demand."

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (A) of section 6601(e)(2) is amended by striking "10 days from the date of notice and demand therefor" and inserting "21 calendar days from the date of notice and demand therefor (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000)".

(2) Paragraph (3) of section 6651(a) is amended by striking "10 days of the date of the notice and demand therefor" and inserting "21 calendar days from the date of notice and demand therefor (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply in the case of any notice and demand given after December 31, 1996.

SEC. 304. ABATEMENT OF PENALTY FOR FAILURE TO MAKE REQUIRED DEPOSITS OF PAYROLL TAXES IN CERTAIN CASES.

(a) IN GENERAL.—Section 6656 (relating to failure to make deposit of taxes) is amended by adding at the end the following new subsections:

"(c) EXCEPTION FOR FIRST-TIME DEPOSITORS OF EMPLOYMENT TAXES.—The Secretary may waive the penalty imposed by subsection (a) on a person's inadvertent failure to deposit any employment tax if—

"(1) such person meets the requirements referred to in section 7430(c)(4)(A)(iii),

"(2) such failure occurs during the 1st quarter that such person was required to deposit any employment tax, and

"(3) the return of such tax was filed on or before the due date.

For purposes of this subsection, the term 'employment taxes' means the taxes imposed by subtitle C.

"(d) AUTHORITY TO ABATE PENALTY WHERE DEPOSIT SENT TO SECRETARY.—The Secretary may abate the penalty imposed by subsection (a) with respect to the first time a depositor is required to make a deposit if the amount required to be deposited is inadvertently sent to the Secretary instead of to the appropriate government depository."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to deposits required to be made after the date of the enactment of this Act.

TITLE IV—JOINT RETURNS

SEC. 401. STUDIES OF JOINT RETURN-RELATED ISSUES.

The Secretary of the Treasury or his delegate and the Comptroller General of the United States shall each conduct separate studies of—

(1) the effects of changing the liability for tax on a joint return from being joint and several to being proportionate to the tax attributable to each spouse,

(2) the effects of providing that, if a divorce decree allocates liability for tax on a joint return filed before the divorce, the Secretary may collect such liability only in accordance with the decree,

(3) whether those provisions of the Internal Revenue Code of 1986 intended to provide relief to innocent spouses provide meaningful relief in all cases where such relief is appropriate, and

(4) the effect of providing that community income (as defined in section 66(d) of such Code) which, in accordance with the rules contained in section 879(a) of such Code, would be treated as the income of one spouse is exempt from a levy for failure to pay any tax imposed by subtitle A by the other spouse for a taxable year ending before their marriage.

The reports of such studies shall be submitted to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate within 6 months after the date of the enactment of this Act.

SEC. 402. JOINT RETURN MAY BE MADE AFTER SEPARATE RETURNS WITHOUT FULL PAYMENT OF TAX.

(a) GENERAL RULE.—Paragraph (2) of section 6013(b) (relating to limitations on filing of joint return after filing separate returns) is amended by striking subparagraph (A) and redesignating the following subparagraphs accordingly.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after the date of the enactment of this Act.

SEC. 403. DISCLOSURE OF COLLECTION ACTIVITIES.

(a) IN GENERAL.—Subsection (e) of section 6103 (relating to disclosure to persons having material interest) is amended by adding at the end the following new paragraph:

"(8) DISCLOSURE OF COLLECTION ACTIVITIES WITH RESPECT TO JOINT RETURN.—If any deficiency of tax with respect to a joint return is assessed and the individuals filing such return are no longer married or no longer reside in the same household, upon request in writing by either of such individuals, the Secretary shall disclose in writing to the individual making the request whether the Secretary has attempted to collect such deficiency from such other individual, the general nature of such collection activities, and the amount collected. The preceding sentence shall not apply to any deficiency which may not be collected by reason of section 6502."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to requests made after the date of the enactment of this Act.

TITLE V—COLLECTION ACTIVITIES

SEC. 501. MODIFICATIONS TO LIEN AND LEVY PROVISIONS.

(a) WITHDRAWAL OF CERTAIN NOTICES.—Section 6323 (relating to validity and priority against certain persons) is amended by adding at the end the following new subsection:

"(j) WITHDRAWAL OF NOTICE IN CERTAIN CIRCUMSTANCES.—

"(1) IN GENERAL.—The Secretary may withdraw a notice of a lien filed under this section and this chapter shall be applied as if the withdrawn notice had not been filed, if the Secretary determines that—

"(A) the filing of such notice was premature or otherwise not in accordance with administrative procedures of the Secretary,

"(B) the taxpayer has entered into an agreement under section 6159 to satisfy the tax liability for which the lien was imposed by means of installment payments, unless such agreement provides otherwise,

"(C) the withdrawal of such notice will facilitate the collection of the tax liability, or

"(D) with the consent of the taxpayer or the Taxpayer Advocate, the withdrawal of such notice would be in the best interests of the taxpayer (as determined by the Taxpayer Advocate) and the United States.

Any such withdrawal shall be made by filing notice at the same office as the withdrawn notice. A copy of such notice of withdrawal shall be provided to the taxpayer.

"(2) NOTICE TO CREDIT AGENCIES, ETC.—Upon written request by the taxpayer with respect to whom a notice of a lien was withdrawn under paragraph (1), the Secretary shall promptly make reasonable efforts to notify credit reporting agencies, and any financial institution or creditor whose name and address is

specified in such request, of the withdrawal of such notice. Any such request shall be in such form as the Secretary may prescribe."

(b) RETURN OF LEVIED PROPERTY IN CERTAIN CASES.—Section 6343 (relating to authority to release levy and return property) is amended by adding at the end the following new subsection:

"(d) RETURN OF PROPERTY IN CERTAIN CASES.—If—

"(1) any property has been levied upon, and

"(2) the Secretary determines that—

"(A) the levy on such property was premature or otherwise not in accordance with administrative procedures of the Secretary,

"(B) the taxpayer has entered into an agreement under section 6159 to satisfy the tax liability for which the levy was imposed by means of installment payments, unless such agreement provides otherwise,

"(C) the return of such property will facilitate the collection of the tax liability, or

"(D) with the consent of the taxpayer or the Taxpayer Advocate, the return of such property would be in the best interests of the taxpayer (as determined by the Taxpayer Advocate) and the United States,

the provisions of subsection (b) shall apply in the same manner as if such property had been wrongly levied upon, except that no interest shall be allowed under subsection (c)."

(d) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date of the enactment of this Act.

SEC. 502. MODIFICATIONS TO CERTAIN LEVY EXEMPTION AMOUNTS.

(a) FUEL, ETC.—Paragraph (2) of section 6334(a) (relating to fuel, provisions, furniture, and personal effects exempt from levy) is amended—

(1) by striking "If the taxpayer is the head of a family, so" and inserting "So",

(2) by striking "his household" and inserting "the taxpayer's household", and

(3) by striking "$1,650 ($1,550 in the case of levies issued during 1989)" and inserting "$2,500".

(b) BOOKS, ETC.—Paragraph (3) of section 6334(a) (relating to books and tools of a trade, business, or profession) is amended by striking "$1,100 ($1,050 in the case of levies issued during 1989)" and inserting "$1,250".

(c) INFLATION ADJUSTMENT.—Section 6334 (relating to property exempt from levy) is amended by adding at the end the following new subsection:

"(f) INFLATION ADJUSTMENT.—

"(1) IN GENERAL.—In the case of any calendar year beginning after 1997, each dollar amount referred to in paragraphs (2) and (3) of subsection (a) shall be increased by an amount equal to—

"(A) such dollar amount, multiplied by

"(B) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year, by substituting 'calendar year 1996' for 'calendar year 1992' in subparagraph (B) thereof.

"(2) ROUNDING.—If any dollar amount after being increased under paragraph (1) is not a multiple of $10, such dollar amount shall be rounded to the nearest multiple of $10.".

(d) EFFECTIVE DATE.—The amendments made by this section shall take effect with respect to levies issued after December 31, 1996.

SEC. 503. OFFERS-IN-COMPROMISE.

(a) REVIEW REQUIREMENTS.—Subsection (b) of section 7122 (relating to records) is amended by striking "$500." and inserting "$50,000. However, such compromise shall be subject to continuing quality review by the Secretary.".

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act.

TITLE VI—INFORMATION RETURNS

SEC. 601. CIVIL DAMAGES FOR FRAUDULENT FILING OF INFORMATION RETURNS.

(a) GENERAL RULE.—Subchapter B of chapter 76 (relating to proceedings by taxpayers and third parties) is amended by redesignating section 7434 as section 7435 and by inserting after section 7433 the following new section:

"SEC. 7434. CIVIL DAMAGES FOR FRAUDULENT FILING OF INFORMATION RETURNS.

"(a) IN GENERAL.—If any person willfully files a fraudulent information return with respect to payments purported to be made to any other person, such other person may bring a civil action for damages against the person so filing such return.

"(b) DAMAGES.—In any action brought under subsection (a), upon a finding of liability on the part of the defendant, the defendant shall be liable to the plaintiff in an amount equal to the greater of $5,000 or the sum of—

"(1) any actual damages sustained by the plaintiff as a proximate result of the filing of the fraudulent information return (including any costs attributable to resolving deficiencies asserted as a result of such filing),

"(2) the costs of the action, and

"(3) in the court's discretion, reasonable attorneys fees.

"(c) PERIOD FOR BRINGING ACTION.—Notwithstanding any other provision of law, an action to enforce the liability created under this section may be brought without regard to the amount in controversy and may be brought only within the later of—

"(1) 6 years after the date of the filing of the fraudulent information return, or

"(2) 1 year after the date such fraudulent information return would have been discovered by exercise of reasonable care.

"(d) COPY OF COMPLAINT FILED WITH IRS—Any person bringing an action under subsection (a) shall provide a copy of the complaint to the Internal Revenue Service upon the filing of such complaint with the court.

"(e) FINDING OF COURT TO INCLUDE CORRECT AMOUNT OF PAYMENT.—The decision of the court awarding damages in an action brought under subsection (a) shall include a finding of the correct amount which should have been reported in the information return.

"(f) INFORMATION RETURN.—For purposes of this section, the term 'information return' means any statement described in section 6724(d)(1)(A)."

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 76 is amended by striking the item relating to section 7434 and inserting the following:

"Sec. 7434. Civil damages for fraudulent filing of information returns.
"Sec. 7435. Cross references."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to fraudulent information returns filed after the date of the enactment of this Act.

SEC. 602. REQUIREMENT TO CONDUCT REASONABLE INVESTIGATIONS OF INFORMATION RETURNS.

(a) GENERAL RULE.—Section 6201 (relating to assessment authority) is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

"(d) REQUIRED REASONABLE VERIFICATION OF INFORMATION RETURNS.—In any court proceeding, if a taxpayer asserts a reasonable dispute with respect to any item of income reported on an information return filed with the Secretary under subpart B or C of part III of subchapter A of chapter 61 by a third party and the taxpayer has fully cooperated with the Secretary (including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer as reasonably requested by the Secretary), the Secretary shall have the burden of producing reasonable and probative information concerning such deficiency in addition to such information return."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall take effect on the date of the enactment of this Act.

TITLE VII—AWARDING OF COSTS AND CERTAIN FEES

SEC. 701. UNITED STATES MUST ESTABLISH THAT ITS POSITION IN PROCEEDING WAS SUBSTANTIALLY JUSTIFIED.

(a) GENERAL RULE.—Subparagraph (A) of section 7430(c)(4) (defining prevailing party) is amended by striking clause (i) and by redesignating clauses (ii) and (iii) as clauses (i) and (ii), respectively.

(b) BURDEN OF PROOF ON UNITED STATES.—Paragraph (4) of section 7430(c) is amended by redesignating subparagraph (B) as subparagraph (C) and by inserting after subparagraph (A) the following new subparagraph:

"(B) EXCEPTION IF UNITED STATES ESTABLISHES THAT ITS POSITION WAS SUBSTANTIALLY JUSTIFIED.—

"(i) GENERAL RULE.—A party shall not be treated as the prevailing party in a proceeding to which subsection (a) applies if the United States establishes that the position of the United States in the proceeding was substantially justified.

"(ii) PRESUMPTION OF NO JUSTIFICATION IF INTERNAL REVENUE SERVICE DIDN'T FOLLOW CERTAIN PUBLISHED GUIDANCE.—For purposes of clause (i), the position of the United States shall be presumed not to

be substantially justified if the Internal Revenue Service did not follow its applicable published guidance in the administrative proceeding. Such presumption may be rebutted.

"(iii) APPLICABLE PUBLISHED GUIDANCE.—For purposes of clause (ii), the term 'applicable published guidance' means—

"(I) regulations, revenue rulings, revenue procedures, information releases, notices, and announcements, and

"(II) any of the following which are issued to the taxpayer: private letter rulings, technical advice memoranda, and determination letters."

(c) CONFORMING AMENDMENTS.—

(1) Subparagraph (B) of section 7430(c)(2) is amended by striking "paragraph (4)(B)" and inserting "paragraph (4)(C)".

(2) Subparagraph (C) of section 7430(c)(4), as redesignated by subsection (b), is amended by striking "subparagraph (A)" and inserting "this paragraph".

(3) Sections 6404(g) and 6656(c)(1), as amended by this Act, are each amended by striking "section 7430(c)(4)(A)(iii)" and inserting "section 7430(c)(4)(A)(ii)".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

SEC. 702. INCREASED LIMIT ON ATTORNEY FEES.

(a) IN GENERAL.—Paragraph (1) of section 7430(c) (defining reasonable litigation costs) is amended—

(1) by striking "$75" in clause (iii) of subparagraph (B) and inserting "$110",

(2) by striking "an increase in the cost of living or" in clause (iii) of subparagraph (B), and

(3) by adding after clause (iii) the following:

"In the case of any calendar year beginning after 1996, the dollar amount referred to in clause (iii) shall be increased by an amount equal to such dollar amount multiplied by the cost-of-living adjustment determined under section 1(f)(3) for such calendar year, by substituting 'calendar year 1995' for 'calendar year 1992' in subparagraph (B) thereof. If any dollar amount after being increased under the preceding sentence is not a multiple of $10, such dollar amount shall be rounded to the nearest multiple of $10."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

SEC. 703. FAILURE TO AGREE TO EXTENSION NOT TAKEN INTO ACCOUNT.

(a) IN GENERAL.—Paragraph (1) of section 7430(b) (relating to requirement that administrative remedies be exhausted) is amended by adding at the end the following new sentence: "Any failure to agree to an extension of the time for the assessment of any tax shall not be taken into account for purposes of determining whether the prevailing party meets the requirements of the preceding sentence."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

SEC. 704. AWARD OF LITIGATION COSTS PERMITTED IN DECLARATORY JUDGMENT PROCEEDINGS.

(a) IN GENERAL.—Subsection (b) of section 7430 is amended by striking paragraph (3) and by redesignating paragraph (4) as paragraph (3).

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

TITLE VIII—MODIFICATION TO RECOVERY OF CIVIL DAMAGES FOR UNAUTHORIZED COLLECTION ACTIONS

SEC. 801. INCREASE IN LIMIT ON RECOVERY OF CIVIL DAMAGES FOR UNAUTHORIZED COLLECTION ACTIONS.

(a) GENERAL RULE.—Subsection (b) of section 7433 (relating to damages) is amended by striking "$100,000" and inserting "$1,000,000".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to actions by officers or employees of the Internal Revenue Service after the date of the enactment of this Act.

SEC. 802. COURT DISCRETION TO REDUCE AWARD FOR LITIGATION COSTS FOR FAILURE TO EXHAUST ADMINISTRATIVE REMEDIES.

(a) GENERAL RULE.—Paragraph (1) of section 7433(d) (relating to civil damages for certain unauthorized collection actions) is amended to read as follows:

"(1) AWARD FOR DAMAGES MAY BE REDUCED IF ADMINISTRATIVE REMEDIES NOT EXHAUSTED.—The amount of damages awarded under subsection (b) may be reduced if the court determines that the plaintiff has not exhausted the administrative remedies available to such plaintiff within the Internal Revenue Service."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in the case of proceedings commenced after the date of the enactment of this Act.

TITLE IX—MODIFICATIONS TO PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX

SEC. 901. PRELIMINARY NOTICE REQUIREMENT.

(a) IN GENERAL.—Section 6672 (relating to failure to collect and pay over tax, or attempt to evade or defeat tax) is amended by redesignating subsection (b) as subsection (c) and by inserting after subsection (a) the following new subsection:

"(b) PRELIMINARY NOTICE REQUIREMENT.—

"(1) IN GENERAL.—No penalty shall be imposed under subsection (a) unless the Secretary notifies the taxpayer in writing by mail to an address as determined under section 6212(b) that the taxpayer shall be subject to an assessment of such penalty.

"(2) TIMING OF NOTICE.—The mailing of the notice described in paragraph (1) shall precede any notice and demand of any penalty under subsection (a) by at least 60 days.

"(3) STATUTE OF LIMITATIONS.—If a notice described in paragraph (1) with respect to any penalty is mailed before the expiration of the period provided by section 6501 for the assessment of such penalty (determined without regard to this paragraph), the period provided by such section for the assessment of such penalty shall not expire before the later of—

"(A) the date 90 days after the date on which such notice was mailed, or

"(B) if there is a timely protest of the proposed assessment, the date 30 days after the Secretary makes a final administrative determination with respect to such protest.

"(4) EXCEPTION FOR JEOPARDY.—This subsection shall not apply if the Secretary finds that the collection of the penalty is in jeopardy."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to proposed assessments made after June 30, 1996.

SEC. 902. DISCLOSURE OF CERTAIN INFORMATION WHERE MORE THAN 1 PERSON LIABLE FOR PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX.

(a) IN GENERAL.—Subsection (e) of section 6103 (relating to disclosure to persons having material interest), as amended by section 403, is amended by adding at the end the following new paragraph:

"(9) DISCLOSURE OF CERTAIN INFORMATION WHERE MORE THAN 1 PERSON SUBJECT TO PENALTY UNDER SECTION 6672.—If the Secretary determines that a person is liable for a penalty under section 6672(a) with respect to any failure, upon request in writing of such person, the Secretary shall disclose in writing to such person—

"(A) the name of any other person whom the Secretary has determined to be liable for such penalty with respect to such failure, and

"(B) whether the Secretary has attempted to collect such penalty from such other person, the general nature of such collection activities, and the amount collected."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall take effect on the date of the enactment of this Act.

SEC. 903. RIGHT OF CONTRIBUTION WHERE MORE THAN 1 PERSON LIABLE FOR PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX.

(a) IN GENERAL.—Section 6672 (relating to failure to collect and pay over tax, or attempt to evade or defeat tax) is amended by adding at the end the following new subsection:

"(d) RIGHT OF CONTRIBUTION WHERE MORE THAN 1 PERSON LIABLE FOR PENALTY.—If more than 1 person is liable for the penalty under subsection (a) with respect to any tax, each person who paid such penalty shall be entitled to recover from other persons who are liable for such penalty an amount equal to the excess of the amount paid by such person over such person's proportionate share of the penalty. Any claim for such a recovery may be made only in a proceeding which is separate from, and is not joined or consolidated with—

"(1) an action for collection of such penalty brought by the United States, or

"(2) a proceeding in which the United States files a counterclaim or third-party complaint for the collection of such penalty."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to penalties assessed after the date of the enactment of this Act.

SEC. 904. VOLUNTEER BOARD MEMBERS OF TAX-EXEMPT ORGANIZATIONS EXEMPT FROM PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX.

(a) IN GENERAL.—Section 6672 is amended by adding at the end the following new subsection:

"(e) EXCEPTION FOR VOLUNTARY BOARD MEMBERS OF TAX-EXEMPT ORGANIZATIONS.—No penalty shall be imposed by subsection (a) on any unpaid, volunteer member of any board of trustees or directors of an organization exempt from tax under subtitle A if such member—

"(1) is solely serving in an honorary capacity,

"(2) does not participate in the day-to-day or financial operations of the organization, and

"(3) does not have actual knowledge of the failure on which such penalty is imposed.

The preceding sentence shall not apply if it results in no person being liable for the penalty imposed by subsection (a)."

(b) PUBLIC INFORMATION REQUIREMENTS.—

(1) IN GENERAL.—The Secretary of the Treasury or the Secretary's delegate (hereafter in this subsection referred to as the "Secretary") shall take such actions as may be appropriate to ensure that employees are aware of their responsibilities under the Federal tax depository system, the circumstances under which employees may be liable for the penalty imposed by section 6672 of the Internal Revenue Code of 1986, and the responsibility to promptly report to the Internal Revenue Service any failure referred to in subsection (a) of such section 6672. Such actions shall include—

(A) printing of a warning on deposit coupon booklets and the appropriate tax returns that certain employees may be liable for the penalty imposed by such section 6672, and

(B) the development of a special information packet.

(2) DEVELOPMENT OF EXPLANATORY MATERIALS.—The Secretary shall develop materials explaining the circumstances under which board members of tax-exempt organizations (including voluntary and honorary members) may be subject to penalty under section 6672 of such Code. Such materials shall be made available to tax-exempt organizations.

(3) IRS INSTRUCTIONS.—The Secretary shall clarify the instructions to Internal Revenue Service employees on the application of the penalty under section 6672 of such Code with regard to voluntary members of boards of trustees or directors of tax-exempt organizations.

TITLE X—MODIFICATIONS OF RULES RELATING TO SUMMONSES

SEC. 1001. ENROLLED AGENTS INCLUDED AS THIRD-PARTY RECORDKEEPERS.

(a) IN GENERAL.—Paragraph (3) of section 7609(a) (relating to third-party recordkeeper defined) is amended by striking "and" at the end of subparagraph (G), by striking the period at the end of subparagraph (H) and inserting "; and", and by adding at the end the following the subparagraph:

"(I) any enrolled agent."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to summonses issued after the date of the enactment of this Act.

SEC. 1002. SAFEGUARDS RELATING TO DESIGNATED SUMMONSES.

(a) STANDARD OF REVIEW.—Subparagraph (A) of section 6503(k)(2) (defining designated summons) is amended by redesignating clauses (i) and (ii) as clauses (ii) and (iii), respectively, and by inserting before clause (ii) (as so redesignated) the following new clause:

"(i) the issuance of such summons is preceded by a review of such issuance by the regional counsel of the Office of Chief Counsel for the region in which the examination of the corporation is being conducted,".

(b) LIMITATION ON PERSONS TO WHOM DESIGNATED SUMMONS MAY BE ISSUED.—Paragraph (1) of section 6503(k) is amended by striking "with respect to any return of tax by a corporation" and inserting "to a corporation (or to any other person to whom the corporation has transferred records) with respect to any return of tax by

such corporation for a taxable year (or other period) for which such corporation is being examined under the coordinated examination program (or any successor program) of the Internal Revenue Service".

(c) CLERICAL AMENDMENT.—Section 6503 is amended by redesignating subsections (k) and (l) (as amended by this section) as subsections (j) and (k), respectively.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to summonses issued after the date of the enactment of this Act.

SEC. 1003. ANNUAL REPORT TO CONGRESS CONCERNING DESIGNATED SUMMONSES.

Not later than December 31 of each calendar year after 1995, the Secretary of the Treasury or his delegate shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the number of designated summonses (as defined in section 6503(j) of the Internal Revenue Code of 1986) which were issued during the preceding 12 months.

TITLE XI—RELIEF FROM RETROACTIVE APPLICATION OF TREASURY DEPARTMENT REGULATIONS

SEC. 1101. RELIEF FROM RETROACTIVE APPLICATION OF TREASURY DEPARTMENT REGULATIONS.

(a) IN GENERAL.—Subsection (b) of section 7805 (relating to rules and regulations) is amended to read as follows:

"(b) RETROACTIVITY OF REGULATIONS.—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, no temporary, proposed, or final regulation relating to the internal revenue laws shall apply to any taxable period ending before the earliest of the following dates:

"(A) The date on which such regulation is filed with the Federal Register.

"(B) In the case of any final regulation, the date on which any proposed or temporary regulation to which such final regulation relates was filed with the Federal Register.

"(C) The date on which any notice substantially describing the expected contents of any temporary, proposed, or final regulation is issued to the public.

"(2) EXCEPTION FOR PROMPTLY ISSUED REGULATIONS.—Paragraph (1) shall not apply to regulations filed or issued within 18 months of the date of the enactment of the statutory provision to which the regulation relates.

"(3) PREVENTION OF ABUSE.—The Secretary may provide that any regulation may take effect or apply retroactively to prevent abuse.

"(4) CORRECTION OF PROCEDURAL DEFECTS.—The Secretary may provide that any regulation may apply retroactively to correct a procedural defect in the issuance of any prior regulation.

"(5) INTERNAL REGULATIONS.—The limitation of paragraph (1) shall not apply to any regulation relating to internal Treasury Department policies, practices, or procedures.

"(6) CONGRESSIONAL AUTHORIZATION.—The limitation of paragraph (1) may be superseded by a legislative grant from Congress authorizing the Secretary to prescribe the effective date with respect to any regulation.

"(7) ELECTION TO APPLY RETROACTIVELY.—The Secretary may provide for any taxpayer to elect to apply any regulation before the dates specified in paragraph (1).

"(8) APPLICATION TO RULINGS.—The Secretary may prescribe the extent, if any, to which any ruling (including any judicial decision or any administrative determination other than by regulation) relating to the internal revenue laws shall be applied without retroactive effect."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to regulations which relate to statutory provisions enacted on or after the date of the enactment of this Act.

TITLE XII—MISCELLANEOUS PROVISIONS

SEC. 1201. PHONE NUMBER OF PERSON PROVIDING PAYEE STATEMENTS REQUIRED TO BE SHOWN ON SUCH STATEMENT.

(a) GENERAL RULE.—The following provisions are each amended by striking "name and address" and inserting "name, address, and phone number of the information contact":

(1) Section 6041(d)(1).

(2) Section 6041A(e)(1).
(3) Section 6042(c)(1).
(4) Section 6044(e)(1).
(5) Section 6045(b)(1).
(6) Section 6049(c)(1)(A).
(7) Section 6050B(b)(1).
(8) Section 6050H(d)(1).
(9) Section 6050I(e)(1).
(10) Section 6050J(e).
(11) Section 6050K(b)(1).
(12) Section 6050N(b)(1).

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to statements required to be furnished after December 31, 1996 (determined without regard to any extension).

SEC. 1202. REQUIRED NOTICE OF CERTAIN PAYMENTS.

If any payment is received by the Secretary of the Treasury or his delegate from any taxpayer and the Secretary cannot associate such payment with such taxpayer, the Secretary shall make reasonable efforts to notify the taxpayer of such inability within 60 days after the receipt of such payment.

SEC. 1203. UNAUTHORIZED ENTICEMENT OF INFORMATION DISCLOSURE.

(a) IN GENERAL.—Subchapter B of chapter 76 (relating to proceedings by taxpayers and third parties), as amended by section 601(a), is amended by redesignating section 7435 as section 7436 and by inserting after section 7434 the following new section:

"SEC. 7435. CIVIL DAMAGES FOR UNAUTHORIZED ENTICEMENT OF INFORMATION DISCLOSURE.

"(a) IN GENERAL.—If any officer or employee of the United States intentionally compromises the determination or collection of any tax due from an attorney, certified public accountant, or enrolled agent representing a taxpayer in exchange for information conveyed by the taxpayer to the attorney, certified public accountant, or enrolled agent for purposes of obtaining advice concerning the taxpayer's tax liability, such taxpayer may bring a civil action for damages against the United States in a district court of the United States. Such civil action shall be the exclusive remedy for recovering damages resulting from such actions.

"(b) DAMAGES.—In any action brought under subsection (a), upon a finding of liability on the part of the defendant, the defendant shall be liable to the plaintiff in an amount equal to the lesser of $500,000 or the sum of—

"(1) actual, direct economic damages sustained by the plaintiff as a proximate result of the information disclosure, and

"(2) the costs of the action.

Damages shall not include the taxpayer's liability for any civil or criminal penalties, or other losses attributable to incarceration or the imposition of other criminal sanctions.

"(c) PAYMENT AUTHORITY.—Claims pursuant to this section shall be payable out of funds appropriated under section 1304 of title 31, United States Code.

"(d) PERIOD FOR BRINGING ACTION.—Notwithstanding any other provision of law, an action to enforce liability created under this section may be brought without regard to the amount in controversy and may be brought only within 2 years after the date the actions creating such liability would have been discovered by exercise of reasonable care.

"(e) MANDATORY STAY.—Upon a certification by the Commissioner or the Commissioner's delegate that there is an ongoing investigation or prosecution of the taxpayer, the district court before which an action under this section is pending shall stay all proceedings with respect to such action pending the conclusion of the investigation or prosecution.

"(f) CRIME-FRAUD EXCEPTION.—Subsection (a) shall not apply to information conveyed to an attorney, certified public accountant, or enrolled agent for the purpose of perpetrating a fraud or crime."

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 76, as amended by section 601(b), is amended by striking the item relating to section 7435 and by adding at the end the following new items:

"Sec. 7435. Civil damages for unauthorized enticement of information disclosure.
"Sec. 7436. Cross references."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to actions after the date of the enactment of this Act.

SEC. 1204. ANNUAL REMINDERS TO TAXPAYERS WITH OUTSTANDING DELINQUENT ACCOUNTS.

(a) IN GENERAL.—Chapter 77 (relating to miscellaneous provisions) is amended by adding at the end the following new section:

"SEC. 7524. ANNUAL NOTICE OF TAX DELINQUENCY.

"Not less often than annually, the Secretary shall send a written notice to each taxpayer who has a tax delinquent account of the amount of the tax delinquency as of the date of the notice."

(b) CLERICAL AMENDMENT.—The table of sections for chapter 77 is amended by adding at the end the following new item:

"Sec. 7524. Annual notice of tax delinquency."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to calendar years after 1996.

SEC. 1205. 5-YEAR EXTENSION OF AUTHORITY FOR UNDERCOVER OPERATIONS.

(a) IN GENERAL.—Paragraph (3) of section 7601(c) of the Anti-Drug Abuse Act of 1988 is amended by striking all that follows "this Act" and inserting a period.

(b) RESTORATION OF AUTHORITY FOR 5 YEARS.—Subsection (c) of section 7608 is amended by adding at the end the following new paragraph:

"(6) APPLICATION OF SECTION.—The provisions of this subsection—

"(A) shall apply after November 17, 1988, and before January 1, 1990, and

"(B) shall apply after the date of the enactment of this paragraph and before January 1, 2001.

All amounts expended pursuant to this subsection during the period described in subparagraph (B) shall be recovered to the extent possible, and deposited in the Treasury of the United States as miscellaneous receipts, before January 1, 2001."

(c) ENHANCED OVERSIGHT.—

(1) ADDITIONAL INFORMATION REQUIRED IN REPORTS TO CONGRESS.—Subparagraph (B) of section 7608(c)(4) is amended—

(A) by striking "preceding the period" in clause (ii),

(B) by striking "and" at the end of clause (ii), and

(C) by striking clause (iii) and inserting the following:

"(iii) the number, by programs, of undercover investigative operations closed in the 1-year period for which such report is submitted, and

"(iv) the following information with respect to each undercover investigative operation pending as of the end of the 1-year period for which such report is submitted or closed during such 1-year period—

"(I) the date the operation began and the date of the certification referred to in the last sentence of paragraph (1),

"(II) the total expenditures under the operation and the amount and use of the proceeds from the operation,

"(III) a detailed description of the operation including the potential violation being investigated and whether the operation is being conducted under grand jury auspices, and

"(IV) the results of the operation including the results of criminal proceedings."

(2) AUDITS REQUIRED WITHOUT REGARD TO AMOUNTS INVOLVED.—Subparagraph (C) of section 7608(c)(5) is amended to read as follows:

"(C) UNDERCOVER INVESTIGATIVE OPERATION.—The term 'undercover investigative operation' means any undercover investigative operation of the Service; except that, for purposes of subparagraphs (A) and (C) of paragraph (4), such term only includes an operation which is exempt from section 3302 or 9102 of title 31, United States Code."

(3) EFFECTIVE DATE.—The amendments made by this subsection shall take effect on the date of the enactment of this Act.

SEC. 1206. DISCLOSURE OF FORM 8300 INFORMATION ON CASH TRANSACTIONS.

(a) IN GENERAL.—Subsection (l) of section 6103 (relating to disclosure of returns and return information for purposes other than tax administration) is amended by adding at the end the following new paragraph:

"(15) DISCLOSURE OF RETURNS FILED UNDER SECTION 6050I.—The Secretary may, upon written request, disclose to officers and employees of—

"(A) any Federal agency,

"(B) any agency of a State or local government, or

"(C) any agency of the government of a foreign country,

information contained on returns filed under section 6050I. Any such disclosure shall be made on the same basis, and subject to the same conditions, as apply to disclosures of information on reports filed under section 5313 of title 31, United States Code; except that no disclosure under this paragraph shall be made for purposes of the administration of any tax law."

(b) CONFORMING AMENDMENTS.—

(1) Subsection (i) of section 6103 is amended by striking paragraph (8).

(2) Subparagraph (A) of section 6103(p)(3) is amended—

(A) by striking "(7)(A)(ii), or (8)" and inserting "or (7)(A)(ii)", and

(B) by striking "or (14)" and inserting "(14), or (15)".

(3) The material preceding subparagraph (A) of section 6103(p)(4) is amended—

(A) by striking "(5), or (8)" and inserting "or (5)",

(B) by striking "(i)(3)(B)(i), or (8)" and inserting "(i)(3)(B)(i),", and

(C) by striking "or (12)" and inserting "(12), or (15)".

(4) Clause (ii) of section 6103(p)(4)(F) is amended—

(A) by striking "(5), or (8)" and inserting "or (5)", and

(B) by striking "or (14)" and inserting "(14), or (15)".

(5) Paragraph (2) of section 7213(a) is amended by striking "or (12)" and inserting "(12), or (15)".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date of the enactment of this Act.

SEC. 1207. DISCLOSURE OF RETURNS AND RETURN INFORMATION TO DESIGNEE OF TAXPAYER.

Subsection (c) of section 6103 (relating to disclosure of returns and return information to designee of taxpayer) is amended by striking "written request for or consent to such disclosure" and inserting "request for or consent to such disclosure".

SEC. 1208. STUDY OF NETTING OF INTEREST ON OVERPAYMENTS AND LIABILITIES.

(a) IN GENERAL.—The Secretary of the Treasury or his delegate shall—

(1) conduct a study of the manner in which the Internal Revenue Service has implemented the netting of interest on overpayments and underpayments and of the policy and administrative implications of global netting, and

(2) before submitting the report of such study, hold a public hearing to receive comments on the matters included in such study.

(b) REPORT.—The report of such study shall be submitted not later than 6 months after the date of the enactment of this Act to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate.

SEC. 1209. EXPENSES OF DETECTION OF UNDERPAYMENTS AND FRAUD, ETC.

(a) IN GENERAL.—Section 7623 (relating to expenses of deduction and punishment of frauds) is amended to read as follows:

"SEC. 7623. EXPENSES OF DETECTION OF UNDERPAYMENTS AND FRAUD, ETC.

"The Secretary, under regulations prescribed by the Secretary, is authorized to pay such sums as he deems necessary for—

"(1) detecting underpayments of tax, and

"(2) detecting and bringing to trial and punishment persons guilty of violating the internal revenue laws or conniving at the same,

in cases where such expenses are not otherwise provided for by law. Any amount payable under the preceding sentence shall be paid from the proceeds of amounts (other than interest) collected by reason of the information provided, and any amount so collected shall be available for such payments.".

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 78 is amended by striking the item relating to section 7623 and inserting the following new item:

"Sec. 7623. Expenses of detection of underpayments and fraud, etc.".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the date which is 6 months after the date of the enactment of this Act.

(d) REPORT.—The Secretary of the Treasury or his delegate shall submit an annual report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the payments under section 7623 of the Internal Revenue Code of 1986 during the year and on the amounts collected for which such payments were made.

SEC. 1210. USE OF PRIVATE DELIVERY SERVICES FOR TIMELY-MAILING-AS-TIMELY-FILING RULE.

Section 7502 (relating to timely mailing treated as timely filing and paying) is amended by adding at the end the following new subsection:

"(f) TREATMENT OF PRIVATE DELIVERY SERVICES.—

"(1) IN GENERAL.—Any reference in this section to the United States mail shall be treated as including a reference to any designated delivery service, and any reference in this section to a postmark by the United States Postal Service shall be treated as including a reference to any date recorded or marked as described in paragraph (2)(C) by any designated delivery service.

"(2) DESIGNATED DELIVERY SERVICE.—For purposes of this subsection, the term 'designated delivery service' means any delivery service provided by a trade or business if such service is designated by the Secretary for purposes of this section. The Secretary may designate a delivery service under the preceding sentence only if the Secretary determines that such service—

"(A) is available to the general public,

"(B) is at least as timely and reliable on a regular basis as the United States mail,

"(C) records electronically to its data base, kept in the regular course of its business, or marks on the cover in which any item referred to in this section is to be delivered, the date on which such item was given to such trade or business for delivery, and

"(D) meets such other criteria as the Secretary may prescribe.

"(3) EQUIVALENTS OF REGISTERED AND CERTIFIED MAIL.—The Secretary may provide a rule similar to the rule of paragraph (1) with respect to any service provided by a designated delivery service which is substantially equivalent to United States registered or certified mail."

SEC. 1211. REPORTS ON MISCONDUCT OF IRS EMPLOYEES.

On or before June 1 of each calendar year after 1996, the Secretary of the Treasury shall submit to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate a report on—

(1) all categories of instances involving the misconduct of employees of the Internal Revenue Service during the preceding calendar year, and

(2) the disposition during the preceding calendar year of any such instances (without regard to the year of the misconduct).

TITLE XIII—REVENUE OFFSETS

Subtitle A—Application of Failure-to-Pay Penalty to Substitute Returns

SEC. 1301. APPLICATION OF FAILURE-TO-PAY PENALTY TO SUBSTITUTE RETURNS.

(a) GENERAL RULE.—Section 6651 (relating to failure to file tax return or to pay tax) is amended by adding at the end the following new subsection:

"(g) TREATMENT OF RETURNS PREPARED BY SECRETARY UNDER SECTION 6020(b).—In the case of any return made by the Secretary under section 6020(b)—

"(1) such return shall be disregarded for purposes of determining the amount of the addition under paragraph (1) of subsection (a), but

"(2) such return shall be treated as the return filed by the taxpayer for purposes of determining the amount of the addition under paragraphs (2) and (3) of subsection (a).".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply in the case of any return the due date for which (determined without regard to extensions) is after the date of the enactment of this Act.

Subtitle B—Excise Taxes on Amounts of Private Excess Benefits

SEC. 1311. EXCISE TAXES FOR FAILURE BY CERTAIN CHARITABLE ORGANIZATIONS TO MEET CERTAIN QUALIFICATION REQUIREMENTS.

(a) IN GENERAL.—Chapter 42 (relating to private foundations and certain other tax-exempt organizations) is amended by redesignating subchapter D as subchapter E and by inserting after subchapter C the following new subchapter:

"Subchapter D—Failure by Certain Charitable Organizations To Meet Certain Qualification Requirements

"SEC. 4958. TAXES ON EXCESS BENEFIT TRANSACTIONS.

"(a) INITIAL TAXES.—

"(1) ON THE DISQUALIFIED PERSON.—There is hereby imposed on each excess benefit transaction a tax equal to 25 percent of the excess benefit. The tax imposed by this paragraph shall be paid by any disqualified person referred to in subsection (f)(1) with respect to such transaction.

"(2) ON THE MANAGEMENT.—In any case in which a tax is imposed by paragraph (1), there is hereby imposed on the participation of any organization manager in the excess benefit transaction, knowing that it is such a transaction, a tax equal to 10 percent of the excess benefit, unless such participation is not willful and is due to reasonable cause. The tax imposed by this paragraph shall be paid by any organization manager who participated in the excess benefit transaction.

"(b) ADDITIONAL TAX ON THE DISQUALIFIED PERSON.—In any case in which an initial tax is imposed by subsection (a)(1) on an excess benefit transaction and the excess benefit involved in such transaction is not corrected within the taxable period, there is hereby imposed a tax equal to 200 percent of the excess benefit involved. The tax imposed by this subsection shall be paid by any disqualified person referred to in subsection (f)(1) with respect to such transaction.

"(c) EXCESS BENEFIT TRANSACTION; EXCESS BENEFIT.—For purposes of this section—

"(1) EXCESS BENEFIT TRANSACTION.—

"(A) IN GENERAL.—The term 'excess benefit transaction' means any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly to or for the use of any disqualified person if the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) received for providing such benefit. For purposes of the preceding sentence, an economic benefit shall not be treated as consideration for the performance of services unless such organization clearly indicated its intent to so treat such benefit.

"(B) EXCESS BENEFIT.—The term 'excess benefit' means the excess referred to in subparagraph (A).

"(2) AUTHORITY TO INCLUDE CERTAIN OTHER PRIVATE INUREMENT.—To the extent provided in regulations prescribed by the Secretary, the term 'excess benefit transaction' includes any transaction in which the amount of any economic benefit provided to or for the use of a disqualified person is determined in whole or in part by the revenues of 1 or more activities of the organization but only if such transaction results in inurement not permitted under paragraph (3) or (4) of section 501(c), as the case may be. In the case of any such transaction, the excess benefit shall be the amount of the inurement not so permitted.

"(d) SPECIAL RULES.—For purposes of this section—

"(1) JOINT AND SEVERAL LIABILITY.—If more than 1 person is liable for any tax imposed by subsection (a) or subsection (b), all such persons shall be jointly and severally liable for such tax.

"(2) LIMIT FOR MANAGEMENT.—With respect to any 1 excess benefit transaction, the maximum amount of the tax imposed by subsection (a)(2) shall not exceed $10,000.

"(e) APPLICABLE TAX-EXEMPT ORGANIZATION.—For purposes of this subchapter, the term 'applicable tax-exempt organization' means—

"(1) any organization which (without regard to any excess benefit) would be described in paragraph (3) or (4) of section 501(c) and exempt from tax under section 501(a), and

"(2) any organization which was described in paragraph (1) at any time during the 5-year period ending on the date of the transaction.

Such term shall not include a private foundation (as defined in section 509(a)).

"(f) OTHER DEFINITIONS.—For purposes of this section—

"(1) DISQUALIFIED PERSON.—The term 'disqualified person' means, with respect to any transaction—

"(A) any person who was, at any time during the 5-year period ending on the date of such transaction, in a position to exercise substantial influence over the affairs of the organization,

"(B) a member of the family of an individual described in subparagraph (A), and

"(C) a 35-percent controlled entity.

"(2) ORGANIZATION MANAGER.—The term 'organization manager' means, with respect to any applicable tax-exempt organization, any officer, director, or trustee of such organization (or any individual having powers or responsibilities similar to those of officers, directors, or trustees of the organization).

"(3) 35-PERCENT CONTROLLED ENTITY.—

"(A) IN GENERAL.—The term '35-percent controlled entity' means—

"(i) a corporation in which persons described in subparagraph (A) or (B) of paragraph (1) own more than 35 percent of the total combined voting power,

"(ii) a partnership in which such persons own more than 35 percent of the profits interest, and

"(iii) a trust or estate in which such persons own more than 35 percent of the beneficial interest.

"(B) CONSTRUCTIVE OWNERSHIP RULES.—Rules similar to the rules of paragraphs (3) and (4) of section 4946(a) shall apply for purposes of this paragraph.

"(4) FAMILY MEMBERS.—The members of an individual's family shall be determined under section 4946(d); except that such members also shall include the brothers and sisters (whether by the whole or half blood) of the individual and their spouses.

"(5) TAXABLE PERIOD.—The term 'taxable period' means, with respect to any excess benefit transaction, the period beginning with the date on which the transaction occurs and ending on the earliest of—

"(A) the date of mailing a notice of deficiency under section 6212 with respect to the tax imposed by subsection (a)(1), or

"(B) the date on which the tax imposed by subsection (a)(1) is assessed.

"(6) CORRECTION.—The terms 'correction' and 'correct' mean, with respect to any excess benefit transaction, undoing the excess benefit to the extent possible, and taking any additional measures necessary to place the organization in a financial position not worse than that in which it would be if the disqualified person were dealing under the highest fiduciary standards."

(b) APPLICATION OF PRIVATE INUREMENT RULE TO TAX-EXEMPT ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—

(1) IN GENERAL.—Paragraph (4) of section 501(c) is amended by inserting "(A)" after "(4)" and by adding at the end the following:

"(B) Subparagraph (A) shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual."

(2) SPECIAL RULE FOR CERTAIN COOPERATIVES.—In the case of an organization operating on a cooperative basis which, before the date of the enactment of this Act, was determined by the Secretary of the Treasury or his delegate, to be described in section 501(c)(4) of the Internal Revenue Code of 1986 and exempt from tax under section 501(a) of such Code, the allocation or return of net margins or capital to the members of such organization in accordance with its incorporating statute and bylaws shall not be treated for purposes of such Code as the inurement of the net earnings of such organization to the benefit of any private shareholder or individual. The preceding sentence shall apply only if such statute and bylaws are substantially as such statute and bylaws were in existence on the date of the enactment of this Act.

(c) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) Subsection (e) of section 4955 is amended—

(A) by striking "SECTION 4945" in the heading and inserting "SECTIONS 4945 AND 4958", and

(B) by inserting before the period "or an excess benefit for purposes of section 4958".

(2) Subsections (a), (b), and (c) of section 4963 are each amended by inserting "4958," after "4955,".

(3) Subsection (e) of section 6213 is amended by inserting "4958 (relating to private excess benefit)," before "4971".

(4) Paragraphs (2) and (3) of section 7422(g) are each amended by inserting "4958," after "4955,".

(5) Subsection (b) of section 7454 is amended by inserting "or whether an organization manager (as defined in section 4958(f)(2)) has 'knowingly' participated in an excess benefit transaction (as defined in section 4958(c))," after "section 4912(b),".

(6) The table of subchapters for chapter 42 is amended by striking the last item and inserting the following:

"SUBCHAPTER D. Failure by certain charitable organizations to meet certain qualification requirements.
"SUBCHAPTER E. Abatement of first and second tier taxes in certain cases."

(d) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section (other than subsection (b)) shall apply to excess benefit transactions occurring on or after September 14, 1995.

(2) BINDING CONTRACTS.—The amendments referred to in paragraph (1) shall not apply to any benefit arising from a transaction pursuant to any written contract which was binding on September 13, 1995, and at all times thereafter before such transaction occurred.

(3) APPLICATION OF PRIVATE INUREMENT RULE TO TAX-EXEMPT ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—

(A) IN GENERAL.—The amendment made by subsection (b) shall apply to inurement occurring on or after September 14, 1995.

(B) BINDING CONTRACTS.—The amendment made by subsection (b) shall not apply to any inurement occurring before January 1, 1997, pursuant to a written contract which was binding on September 13, 1995, and at all times thereafter before such inurement occurred.

SEC. 1312. REPORTING OF CERTAIN EXCISE TAXES AND OTHER INFORMATION.

(a) REPORTING BY ORGANIZATIONS DESCRIBED IN SECTION 501(c)(3).—Subsection (b) of section 6033 (relating to certain organizations described in section 501(c)(3)) is amended by striking "and" at the end of paragraph (9), by redesignating paragraph (10) as paragraph (14), and by inserting after paragraph (9) the following new paragraphs:

"(10) the respective amounts (if any) of the taxes paid by the organization during the taxable year under the following provisions:

"(A) section 4911 (relating to tax on excess expenditures to influence legislation),

"(B) section 4912 (relating to tax on disqualifying lobbying expenditures of certain organizations), and

"(C) section 4955 (relating to taxes on political expenditures of section 501(c)(3) organizations),

"(11) the respective amounts (if any) of the taxes paid by the organization, or any disqualified person with respect to such organization, during the taxable year under section 4958 (relating to taxes on private excess benefit from certain charitable organizations),

"(12) such information as the Secretary may require with respect to any excess benefit transaction (as defined in section 4958),

"(13) such information with respect to disqualified persons as the Secretary may prescribe, and".

(b) ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—Section 6033 is amended by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) the following new subsection:

"(f) CERTAIN ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—Every organization described in section 501(c)(4) which is subject to the requirements of subsection (a) shall include on the return required under subsection (a) the information referred to in paragraphs (11), (12) and (13) of subsection (b) with respect to such organization."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to returns for taxable years beginning after the date of the enactment of this Act.

SEC. 1313. EXEMPT ORGANIZATIONS REQUIRED TO PROVIDE COPY OF RETURN.

(a) REQUIREMENT TO PROVIDE COPY.—

(1) Subparagraph (A) of section 6104(e)(1) (relating to public inspection of annual returns) is amended to read as follows:

"(A) IN GENERAL.—During the 3-year period beginning on the filing date—

"(i) a copy of the annual return filed under section 6033 (relating to returns by exempt organizations) by any organization to which this paragraph applies shall be made available by such organization for inspection during regular business hours by any individual at the principal office of such organization and, if such organization regularly maintains 1 or more regional or district offices having 3 or more employees, at each such regional or district office, and

"(ii) upon request of an individual made at such principal office or such a regional or district office, a copy of such annual return shall be

provided to such individual without charge other than a reasonable fee for any reproduction and mailing costs.

The request described in clause (ii) must be made in person or in writing. If the request under clause (ii) is made in person, such copy shall be provided immediately and, if made in writing, shall be provided within 30 days."

(2) Clause (ii) of section 6104(e)(2)(A) is amended by inserting before the period at the end the following: "(and, upon request of an individual made at such principal office or such a regional or district office, a copy of the material requested to be available for inspection under this subparagraph shall be provided (in accordance with the last sentence of paragraph (1)(A)) to such individual without charge other than reasonable fee for any reproduction and mailing costs)".

(3) Subsection (e) of section 6104 is amended by adding at the end the following new paragraph:

"(3) LIMITATION.—Paragraph (1)(A)(ii) (and the corresponding provision of paragraph (2)) shall not apply to any request if, in accordance with regulations promulgated by the Secretary, the organization has made the requested documents widely available, or, the Secretary determines, upon application by an organization, that such request is part of a harassment campaign and that compliance with such request is not in the public interest."

(b) INCREASE IN PENALTY FOR WILLFUL FAILURE TO ALLOW PUBLIC INSPECTION OF CERTAIN RETURNS, ETC.—Section 6685 is amended by striking "$1,000" and inserting "$5,000".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to requests made on or after the 60th day after the Secretary of the Treasury first issues the regulations referred to section 6104(e)(3) of the Internal Revenue Code of 1986 (as added by subsection (a)(3)).

SEC. 1314. INCREASE IN PENALTIES ON EXEMPT ORGANIZATIONS FOR FAILURE TO FILE COMPLETE AND TIMELY ANNUAL RETURNS.

(a) IN GENERAL.—Subparagraph (A) of section 6652(c)(1) (relating to annual returns under section 6033) is amended by striking "$10" and inserting "$20" and by striking "$5,000" and inserting "$10,000".

(b) LARGER PENALTY ON ORGANIZATIONS HAVING GROSS RECEIPTS IN EXCESS OF $1,000,000.—Subparagraph (A) of section 6652(c)(1) is amended by adding at the end the following new sentence: "In the case of an organization having gross receipts exceeding $1,000,000 for any year, with respect to the return required under section 6033 for such year, the first sentence of this subparagraph shall be applied by substituting '$100' for '$20' and, in lieu of applying the second sentence of this subparagraph, the maximum penalty under this subparagraph shall not exceed $50,000."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to returns for taxable years ending on or after the date of the enactment of this Act.

I. INTRODUCTION

A. Purpose and summary

H.R. 2337, as amended, provides amendments relating to "Taxpayer Bill of Rights 2" (Titles I–XII) and two revenue offsets to pay for these provisions (Title XIII). The revenue offsets are (1) apply failure-to-pay penalty to substitute returns and (2) intermediate sanctions for certain tax-exempt organizations.

B. Background and need for legislation

The bill, as amended, is intended to provide for increased protections of taxpayer rights in complying with the Internal Revenue Code and in dealing with the Internal Revenue Service (IRS) in its administration of the tax laws.

The bill, as amended, establishes a Taxpayer Advocate within the IRS, expands the authority to issue Taxpayer Assistance Orders, modifies installment payment agreement provisions, revises provisions relating to abatement of interest and penalties and joint

returns, modifies lien and levy and offers-in-compromise provisions, provides that the Government must establish that its position in a proceeding was substantially justified, increases the limit on recovery of civil damages for unauthorized collection actions from $100,000 to $1,000,000, provides safeguards relating to designated summonses, provides relief from retroactive application of Treasury Department Regulations, requires notice to taxpayers of certain payments and annual reminders to taxpayers with outstanding delinquent accounts, and certain other provisions. The bill also applies the failure-to-pay penalty to substitute returns in the same manner as the penalty applies to delinquent filers. Further, the bill provides intermediate sanctions for certain tax-exempt organizations.

C. Legislative history

H.R. 2337 was introduced by Mrs. Johnson of Connecticut and Mr. Matsui on September 14, 1995, and was amended by the Committee in a markup on March 21, 1996. An amendment in the nature of a substitute (offered by Mrs. Johnson and Mr. Matsui) was adopted, as amended, by a voice vote. The bill, as amended, was ordered favorably reported by a voice vote on March 21, 1996.

Two amendments offered en bloc by Mrs. Johnson to the amendment in the nature of a substitute were adopted in one voice vote: (1) require annual reports on misconduct by IRS employees and (2) authorize the use of "qualified private delivery services" as meeting the "timely-mailing as timely-filing" rule of Code section 7502.

The provisions of Titles I–XII of the bill generally were included in the Committee's 1995 reconciliation submission to the House Committee on the Budget: Subtitle C of Title XIII of H.R. 2491 as passed by the House of Representatives in 1995. (See H.Rept. 104–280, October 17, 1995.) The conference agreement on H.R. 2491 contained certain of the House-passed Taxpayer Bill of Rights 2 provisions. The revenue-offset provisions in title XIII of the bill also were included in H.R. 2491 as passed by the Congress. H.R. 2491 was vetoed by the President.

II. EXPLANATION OF THE BILL

A. Taxpayer bill of rights 2 provisions

1. TAXPAYER ADVOCATE

a. Establishment of position of taxpayer advocate within Internal Revenue Service (sec. 101 of the bill and sec. 7802 of the code)

Present Law

The Office of the Taxpayer Ombudsman was created by the Internal Revenue Service (IRS) in 1979. The Taxpayer Ombudsman's duties are to serve as the primary advocate, within the IRS, for taxpayers. As the taxpayers' advocate, the Taxpayer Ombudsman participates in an ongoing review of IRS policies and procedures to determine their impact on taxpayers, receives ideas from the public concerning tax administration, identifies areas of the tax law that confuse or create an inequity for taxpayers, and supervises cases handled under the Problem Resolution Program. Under current

procedures, the Taxpayer Ombudsman is selected by the Commissioner of the IRS and serves at the Commissioner's discretion.

Reasons for change

To date, the Taxpayer Ombudsman has been a career civil servant selected by and serving at the pleasure of the IRS Commissioner. Some may perceive that the Taxpayer Ombudsman is not an independent advocate for taxpayers. In order to ensure that the Taxpayer Ombudsman has the necessary stature within the IRS to represent fully the interests of taxpayers, it is believed to be appropriate that the position be elevated to a position comparable to that of the Chief Counsel. In addition, in order to ensure that the Congress is systematically made aware of recurring and unresolved problems and difficulties taxpayers encounter in dealing with the IRS, the Taxpayer Ombudsman should have the authority and responsibility to make independent reports to the Congress in order to advise the tax-writing committees of those areas.

Explanation of provision

The bill establishes a new position, Taxpayer Advocate, within the IRS. This replaces the position of Taxpayer Ombudsman. The Taxpayer Advocate is appointed by and reports directly to the Commissioner. Compensation of the Taxpayer Advocate is at a level equal to that of the highest level official reporting directly to the Deputy Commissioner of the IRS.

The bill also establishes the Office of Taxpayer Advocate within the IRS. The functions of the office are (1) to assist taxpayers in resolving problems with the IRS, (2) to identify areas in which taxpayers have problems in dealings with the IRS, (3) to propose changes (to the extent possible) in the administrative practices of the IRS that will mitigate those problems, and (4) to identify potential legislative changes that may mitigate those problems.

While the Taxpayer Advocate would not have direct line authority over the regional and local Problem Resolution Officers (PROs), the Committee believes that all PROs should take direction from the Taxpayer Advocate and that they should operate with sufficient independence to assure that taxpayer rights are not being subordinated to pressure from local revenue officers, district directors, etc. Accordingly, the Committee recommends and encourages that regional PROs actively participate in the selection and evaluation of local PROs.

The Taxpayer Advocate is required to make two annual reports to the tax-writing committees. The first report is to contain the objectives of the Taxpayer Advocate for the next calendar year. This report is to contain full and substantive analysis, in addition to statistical information, and is due not later than June 30 of each year.

The second report is on the activities of the Taxpayer Advocate during the previous fiscal year. The report must identify the initiatives the Taxpayer Advocate has taken to improve taxpayer services and IRS responsiveness, contain recommendations received from individuals who have the authority to issue a Taxpayer Assistance Order (TAO), describe in detail the progress made in implementing these recommendations, contain a summary of at least 20 of the most serious problems which taxpayers have in dealing

with the IRS, include recommendations for such administrative and legislative action as may be appropriate to resolve such problems, describe the extent to which regional problem resolution officers participate in the selection and evaluation of local problem resolution officers, and include other such information as the Taxpayer Advocate may deem advisable. The Commissioner is required to establish internal procedures that will ensure a formal IRS response within three months to all recommendations submitted to the Commissioner by the Taxpayer Advocate. This second report is due not later than December 31 of each year.

The reports submitted to Congress by the Taxpayer Advocate are not subject to prior review by the Commissioner, the Secretary of the Treasury, any other officer or employee of the Department of the Treasury, or the Office of Management and Budget. The objective is for Congress to receive an unfiltered and candid report of the problems taxpayers are experiencing and what can be done to address them. The reports by the Taxpayer Advocate are not official legislative recommendations of the Administration; providing official legislative recommendations remains the responsibility of the Department of Treasury.

Effective date

The provision is effective on the date of enactment. The first annual reports of the Taxpayer Advocate are due in June and December, 1996.

b. Expansion of authority to issue taxpayer assistance orders (sec. 102 of the bill and sec. 7811 of the Code)

Present law

Section 7811(a) authorizes the Taxpayer Ombudsman to issue a Taxpayer Assistance Order (TAO). TAOs may order the release of taxpayer property levied upon by the IRS and may require the IRS to cease any action, or refrain from taking any action if, in the determination of the Taxpayer Ombudsman, the taxpayer is suffering or about to suffer a significant hardship as a result of the manner in which the internal revenue laws are being administered.

Reasons for change

The requirement that the significant hardship be as a result of the manner in which the internal revenue laws are being administered has resulted in confusion as to the circumstances which justify the issuance of a TAO. The most frequent situation where a TAO may be needed, but may not be authorized under present law, involves income tax refunds that are needed to relieve severe hardship of taxpayers. Another example involves the re-issuance of refund checks which have been sent by the IRS to an address at which the taxpayer no longer resides. While the mailing of the check to the incorrect address might in no way be due to the fault of the IRS, the normal delays in reissuing such a check may cause great hardship for the taxpayer. Also, the IRS Collection Division may take an enforcement action when the taxpayer has had no actual notice of the deficiency and is not afforded any opportunity to obtain an administrative review of the validity of the tax defi-

ciency. In cases like these, it may be appropriate for the Taxpayer Advocate to issue a TAO to temporarily stay the IRS collection action in order to allow for a review of the appropriateness of the proposed action.

Explanation of provision

The bill provides the Taxpayer Advocate with broader authority to affirmatively take any action as permitted by law with respect to taxpayers who would otherwise suffer a significant hardship as a result of the manner in which the IRS is administering the tax laws. In addition, the bill provides that a TAO may specify a time period within which the TAO must be followed. Further, the bill provides that only the Taxpayer Advocate, the Commissioner of the IRS, or the Deputy Commissioner, may modify or rescind a TAO. Any official who modifies or rescinds a TAO must provide the Taxpayer Advocate a written explanation of the reasons for the modification or rescission.

Effective date

The provision is effective on the date of enactment.

2. MODIFICATIONS TO INSTALLMENT AGREEMENT PROVISIONS

a. Notification of reasons for termination of installment agreements (sec. 201 of the bill and sec. 6159 of the Code)

Present law

Section 6159 authorizes the IRS to enter into written installment agreements with taxpayers to facilitate the collection of tax liabilities. In general, the IRS has the right to terminate (or in some instances, alter or modify) such agreements if the taxpayer provided inaccurate or incomplete information before the agreement was entered into, if the taxpayer fails to make a timely payment of an installment or another tax liability, if the taxpayer fails to provide the IRS with a requested update of financial condition, if the IRS determines that the financial condition of the taxpayer has changed significantly, or if the IRS believes collection of the tax liability is in jeopardy. If the IRS determines that the financial condition of a taxpayer that has entered into an installment agreement has changed significantly, the IRS must provide the taxpayer with a written notice that explains the IRS determination at least 30 days before altering, modifying, or terminating the installment agreement. No notice is statutorily required if the installment agreement is altered, modified, or terminated for other reasons.

Reasons for change

The Committee believes that the IRS generally should notify taxpayers if an installment agreement is altered, modified, or terminated.

Explanation of provision

The bill requires the IRS to notify taxpayers 30 days before altering, modifying, or terminating any installment agreement for any reason other than that the collection of tax is determined to be in

jeopardy. The IRS must include in the notification an explanation of why the IRS intends to take this action.

Effective date

The provision is effective six months after the date of enactment.

b. Administrative review of termination of installment agreements (sec. 202 of the bill and sec. 6159 of the Code)

Present law

The IRS is currently testing an appeal process for various collection actions, including installment agreements, that will permit taxpayers to appeal these collection actions to Appeals Division personnel.

Reasons for change

The Committee believes that taxpayers should be able to obtain an independent administrative review of terminations of installment agreements.

Explanation of provision

The bill requires the IRS to establish additional procedures for an independent administrative review of terminations of installment agreements for taxpayers who request a review.

Effective Date

The provision is effective on January 1, 1997.

3. ABATEMENT OF INTEREST AND PENALTIES

a. Expansion of authority to abate interest (sec. 301 of the bill and sec. 6404 of the code)

Present law

Any assessment of interest on any deficiency attributable in whole or in part to any error or delay by an officer or employee of the IRS (acting in his official capacity) in performing a ministerial act may be abated.

Reasons for change

The Committee believes that it is appropriate to expand the authority to abate interest to include delays caused by managerial acts of the IRS.

Explanation of provision

The bill permits the IRS to abate interest with respect to any unreasonable error or delay resulting from managerial acts as well as ministerial acts. This would include extensive delays resulting from managerial acts such as: the loss of records by the IRS, IRS personnel transfers, extended illnesses, extended personnel training, or extended leave. On the other hand, interest would not be abated for delays resulting from general administrative decisions. For example, the taxpayer could not claim that the IRS's decision on how to organize the processing of tax returns or its delay in implementing an improved computer system resulted in an unreasonable

delay in the Service's action on the taxpayer's tax return, and so the interest on any subsequent deficiency should be waived.

Effective date

The provision applies to interest accruing with respect to deficiencies or payments for taxable years beginning after the date of enactment.

b. Review of IRS failure to abate interest (sec. 302 of the bill and sec. 6404 of the Code)

Present law

Federal courts generally do not have the jurisdiction to review the IRS's failure to abate interest.

Reasons for change

The Committee believes that it is appropriate for the Tax Court to have jurisdiction to review IRS's failure to abate interest with respect to certain taxpayers.

Explanation of provision

The bill grants the Tax Court jurisdiction to determine whether the IRS's failure to abate interest for an eligible taxpayer was an abuse of discretion. The Tax Court may order an abatement of interest. The action must be brought within 180 days after the date of mailing of the Secretary's final determination not to abate interest. An eligible taxpayer must meet the net worth and size requirements imposed with respect to awards of attorney's fees. No inference is intended as to whether under present law any court has jurisdiction to review IRS's failure to abate interest.

Effective date

The provision applies to requests for abatement after the date of enactment.

c. Extension of interest-free period for payment of tax after notice and demand (sec. 303 of the bill and sec. 6601 of the code)

Present law

In general, a taxpayer must pay interest on late payments of tax. An interest-free period of 10 calendar days is provided to taxpayers who pay the tax due within 10 calendar days of notice and demand.

Reasons for change

The 10-day interest-free period was designed to give taxpayers time to receive the notice and pay the amount due. Because it may be very difficult for some taxpayers to remit payment within the ten-day period, particularly if the mail has delayed delivery of the notice, the IRS must recompute interest and send another notice to taxpayers.

Explanation of provision

The bill extends the interest-free period provided to taxpayers for the payment of the tax liability reflected in the notice from 10 cal-

endar days to 10 business days (21 calendar days, provided that the total tax liability shown on the notice of deficiency is less than $100,000).

Effective date

The provision applies in the case of any notice and demand given after December 31, 1996.

d. Abatement of penalty for failure to make required deposits of payroll taxes in certain cases (sec. 304 of the bill and sec. 6656 of the Code)

Present law

If any person who is required to deposit taxes imposed by the Internal Revenue Code with a government depository fails to deposit such taxes on or before the prescribed date, a penalty may be imposed, unless it is shown that such failure is due to reasonable cause and not willful neglect. The penalty contains a four-tiered structure in which the amount of the penalty varies with the length of time within which the taxpayer corrects the failure. The amount of the underpayment for this purpose is the excess of the amount of the tax required to be deposited over the amount of the tax, if any, deposited on or before the prescribed date.

Reasons for change

The Committee believes that it is appropriate to enumerate additional circumstances under which this penalty may be waived or abated.

Explanation of provision

The bill provides that the Secretary may waive this penalty with respect to an inadvertent failure to deposit any employment tax if: (a) the depositing entity meets the net worth requirements applicable for awards of attorney's fees; (b) the failure to deposit occurs during the first quarter that the depositing entity was required to deposit any employment tax; and (c) the return for the employment tax was filed on or before the due date.

The bill also provides that the Secretary may abate any penalty for failure to make deposits for the first time a depositing entity makes a deposit if it inadvertently sends the deposit to the Secretary instead of to the required government depository.

Effective date

The provision is effective on the date of enactment.

4. JOINT RETURNS

a. Studies of joint and several liability for married persons filing joint tax returns and other joint return-related issues (sec. 401 of the bill)

Present law

Spouses who file a joint tax return are each fully responsible for the accuracy of the return and for the full tax liability. This is true even though only one spouse may have earned the wages or income

which is shown on the return. This is "joint and several" liability. Spouses who wish to avoid joint liability may file as a "married person filing separately."

Spouses often file a joint tax return but then later are separated or divorced. If the IRS later disputes the accuracy of the joint tax returns, one spouse may be held liable for the entire tax deficiency stemming from erroneous deductions or omitted income attributable to the other spouse. Therefore, the "innocent" spouse may be held liable for the full deficiency in a subsequent audit occurring after the separation or divorce. This has resulted in a serious hardship being imposed on an "innocent spouse" in a number of cases.

In some cases, a couple addresses the responsibility for tax liability as part of their divorce decree. However, these agreements are not binding on the IRS because the IRS was not a party to the divorce proceeding. Thus, if a former spouse violates the tax responsibilities assigned to him or her in a divorce decree, the other spouse may not rely on the decree in dealing with the IRS.

While present law does contain provisions which give relief to certain innocent spouses in these situations, the provisions are narrowly drawn and strictly interpreted. Therefore, many former spouses are not able to qualify for the protections of the current "innocent spouse" rules.

In 1930, the Supreme Court ruled in *Poe v. Seaborn,* 282 U.S. 101 (1930), that all the earnings of a married couple in community property states were part of the marital property to which each spouse had an equal right. At the time, married couples generally welcomed this decision because it allowed couples in community property states to benefit from income "splitting" between the husband and wife for income tax purposes. Later, the Federal tax law was changed to allow all married taxpayers to "split" their income by means of filing a joint tax return.

While the income-splitting effect of *Poe* v. *Seaborn* is now moot, the decision continues to affect married couples in community property states, but in an adverse way. For example, there are cases where a divorced spouse owes the IRS a tax liability based on his or her joint return filed during the marital years. When this spouse remarries, the new spouse's income may become subject to levy in order to satisfy the tax deficiency of the prior spouse. In contrast, if the couple did not live in a community property state, the second spouse's wages could not be levied to pay a tax liability arising from this spouse's first marriage.

Reasons for change

The Committee believes that the traditional standard of joint and several liability for married couples filing a joint tax return should be re-examined.

Explanation of provision

The bill directs the Treasury Department and the General Accounting Office (GAO) to conduct separate studies analyzing the following:

(1) The effects of changing the current standard of "joint and several" liability for married couples to a "proportionate" liability

standard. That is, each spouse would be liable only for the income tax attributable to the income of each spouse.

(2) The effects of requiring the IRS to be bound by the terms of a divorce decree which addresses the responsibility for the tax liability on prior joint tax returns.

(3) Whether the current "innocent spouse" provisions provide meaningful relief to former spouses.

(4) The effects of overturning the application of *Poe* v. *Seaborn* for income tax purposes in community property states.

The Treasury Department and the GAO must examine the tax policy implications, the equity implications, and operational changes which would face the IRS if the liability standard were changed. For example, the studies must consider how a system of proportionate liability would change the way the IRS communicates with taxpayers, conducts audits of joint returns, and enforces tax lien and levies against married couples.

Effective date

The studies are due six months after the date of enactment.

b. Joint return may be made after separate returns without full payment of tax (sec. 402 of the bill and sec. 6013 of the Code)

Present law

Taxpayers who file separate returns and subsequently determine that their tax liability would have been less if they had filed a joint return are precluded by statute from reducing their tax liability by filing jointly if they are unable to pay the entire amount of the joint return liability before the expiration of the three-year period for making the election to file jointly.

Reasons for change

Not all taxpayers are able to pay the full amount owed on their returns by the filing deadline. In such circumstances, the IRS encourages the taxpayer to pay the tax as soon as possible or enter into an installment agreement. However, taxpayers who file separate returns and subsequently determine that their tax liability would have been less if they had filed a joint return are precluded from reducing their tax liability by filing jointly if they are unable to pay the entire amount of the joint return liability. This rule may be unfair to taxpayers experiencing financial difficulties.

Explanation of provision

The bill repeals the requirement of full payment of tax liability as a precondition to switching from married filing separately status to married filing jointly status.

Effective date

The provision applies to taxable years beginning after the date of the enactment.

c. Disclosure of collection activities with respect to joint returns (sec. 403 of the bill and sec. 6103 of the Code)

Present law

The IRS does not routinely disclose collection information to a former spouse that relates to tax liabilities attributable to a joint return that was filed when married.

Reasons for change

The Committee believes that it is appropriate to require the IRS to discuss with one former spouse the efforts it has made to collect the joint return tax liability from the other spouse.

Explanation of provision

If a tax deficiency with respect to a joint return is assessed, and the individuals filing the return are no longer married or no longer reside in the same household, the bill requires the IRS to disclose in writing (in response to a written request by one of the individuals) to that individual whether the IRS has attempted to collect the deficiency from the other individual, the general nature of the collection activities, and the amount (if any) collected.

Such requests must be made in writing. The IRS may develop procedures to address the frequency of such requests in order to prevent taxpayers from abusing this provision by making numerous requests without good cause. For example, one request per quarter would be a reasonable rate unless the taxpayer had good cause to seek more frequent information.

In making these disclosures, the IRS may omit the current home address and business location of the former spouse. This is designed to prevent the disclosure of such personal information to persons who might be hostile towards a former spouse.

Effective date

The provision is effective on the date of enactment.

5. COLLECTION ACTIVITIES

a. Modifications to lien and levy provisions

i. Withdrawal of public notice of lien (sec. 501(a) the bill and sec. 6323 of the Code)

Present law

The IRS must file a notice of lien in the public record, in order to protect the priority of a tax lien. A notice of tax lien provides public notice that a taxpayer owes the Government money. The IRS has discretion in filing such a notice, but may withdraw a filed notice only if the notice (and the underlying lien) was erroneously filed or if the underlying lien has been paid, bonded, or become unenforceable.

Reasons for change

The Committee believes that it is appropriate to give the IRS discretion to withdraw a notice of lien in other situations as well.

Explanation of provision

The bill allows the IRS to withdraw a public notice of tax lien prior to payment in full by the indebted taxpayer without prejudice, if the Secretary determines that (1) the filing of the notice was premature or otherwise not in accordance with the administrative procedures of the IRS, (2) the taxpayer has entered into an installment agreement to satisfy the tax liability with respect to which the lien was filed, (3) the withdrawal of the lien will facilitate collection of the tax liability, or (4) the withdrawal of the lien would be in the best interests of the taxpayer (as determined by the Taxpayer Advocate) and of the Government. The IRS must also provide a copy of the notice of withdrawal to the taxpayer. The bill also requires that, at the written request of the taxpayer, the IRS make reasonable efforts to give notice of the withdrawal of a lien to creditors, credit reporting agencies, and financial institutions specified by the taxpayer.

Effective date

The provision is effective on the date of enactment.

ii. Return of levied property (sec. 501(b) of the bill and sec. 6343 of the Code)

Present law

The IRS is authorized to levy on the property of a taxpayer as a means of collecting unpaid taxes. The IRS is able to return levied property to a taxpayer only when the taxpayer has fully paid its liability with respect to tax, interest, and penalty for which the property was levied.

Reasons for change

There are several situations where the IRS is not authorized to return levied-upon amounts, even when it believes doing so would be equitable and in the best interests of the taxpayer and the Government. For example, if the IRS enters into an installment agreement and, in contradiction to the terms of the installment agreement, the IRS levies on the taxpayer's property, the IRS is prohibited from returning the property to the taxpayer. The Committee believes that it is appropriate to give the IRS authority to return levied property in other circumstances as well.

Explanation of provision

The bill allows the IRS to return property (including money deposited in the Treasury) that has been levied upon if the Secretary determines that (1) the levy was premature or otherwise not in accordance with the administrative procedures of the IRS, (2) the taxpayer has entered into an installment agreement to satisfy the tax liability, (3) the return of the property will facilitate collection of the tax liability, or (4) the return of the property would be in the best interests of the taxpayer (as determined by the Taxpayer Advocate) and the Government.

Effective date

The provision is effective on the date of enactment.

iii. Modifications in certain levy exemption amounts (sec. 502 of the bill and sec. 6334 of the Code)

Present law

Property exempt from levy includes personal property with a value of up to $1,650 and books and tools of a trade with a value of up to $1,100.

Reasons for change

The Committee believes that these amounts should be increased and indexed for inflation.

Explanation of provision

The bill increases the exemption amount to $2,500 for personal property and increases the exemption amount to $1,250 for books and tools of a trade. These amounts are indexed for inflation commencing January 1, 1997.

Effective date

The provision is effective with respect to levies issued after December 31, 1996.

b. Offers-in-compromise (sec. 503 of the bill and sec. 7122 of the Code)

Present law

The IRS has the authority to settle a tax debt pursuant to an offer-in-compromise. IRS regulations provide that such offers can be accepted if: the taxpayer is unable to pay the full amount of the tax liability and it is doubtful that the tax, interest, and penalties can be collected or there is doubt as to the validity of the actual tax liability. Amounts over $500 can only be accepted if the reasons for the acceptance are documented in detail and supported by an opinion of the IRS Chief Counsel.

Reasons for change

The Committee believes that the $500 threshold amount requiring a written opinion from the IRS Chief Counsel slows the approval process for most offers-in-compromise and is unnecessarily low.

Explanation of provision

The bill increases from $500 to $50,000 the amount requiring a written opinion from the Office of Chief Counsel. Compromises below the $50,000 threshold must be subject to continuing quality review by the IRS.

Effective date

The provision is effective on the date of enactment.

6. INFORMATION RETURNS

a. Civil damages for fraudulent filing of information returns (sec. 601 of the bill and new sec. 7434 of the Code)

Present law

Federal law provides no private cause of action to a taxpayer who is injured because a fraudulent information return has been filed with the IRS asserting that payments have been made to the taxpayer.

Reasons for change

Some taxpayers may suffer significant personal loss and inconvenience as the result of the IRS receiving fraudulent information returns, which have been filed by persons intent on either defrauding the IRS or harassing taxpayers.

Explanation of provision

The bill provides that, if any person willfully files a fraudulent information return with respect to payments purported to have been made to another person, the other person may bring a civil action for damages against the person filing that return. A copy of the complaint initiating the action must be provided to the IRS. Recoverable damages are the greater of (1) $5,000 or (2) the amount of actual damages (including the costs of the action) and, in the court's discretion, reasonable attorney's fees. The court must specify in any decision awarding damages the correct amount (if any) that should have been reported on the information return. An action seeking damages under this provision must be brought within six years after the filing of the fraudulent information return, or one year after the fraudulent information return would have been discovered through the exercise of reasonable care, whichever is later.

The Committee does not want to open the door to unwarranted or frivolous actions or abusive litigation practices. The Committee is concerned, for example, about the possibility that an unfounded or frivolous action might be brought under this section by a current or former employee of an employer who is not pleased with one or more items that his or her current or former employer has included on the employee's Form W–2. Therefore, actions brought under this section will be subject to Rule 11 of the Federal Rules of Civil Procedure, relating to the imposition of sanctions in the case of unfounded or frivolous claims, to the same extent as other civil actions.

Effective date

The provision applies to fraudulent information returns filed after the date of enactment.

b. Requirement to conduct reasonable investigations of information returns (sec. 602 of the bill and sec. 6201 of the Code)

Present law

Deficiencies determined by the IRS are generally afforded a presumption of correctness.

Reasons for change

Taxpayers may encounter difficulties when a payor issues an erroneous information return and refuses to correct the information and report the change to the IRS, or when a fraudulent information return is filed.

Explanation of provision

The bill provides that, in any court proceeding, if a taxpayer asserts a reasonable dispute with respect to any item of income reported on an information return (Form 1099 or Form W-2) filed by a third party and the taxpayer has fully cooperated with the IRS, the Government has the burden of producing reasonable and probative information concerning the deficiency (in addition to the information return itself). Fully cooperating with the IRS includes (but is not limited to) the following: bringing the reasonable dispute over the item of income to the attention of the IRS within a reasonable period of time, and providing (within a reasonable period of time) access to and inspection of all witnesses, information, and documents within the control of the taxpayer (as reasonably requested by the Secretary).

Effective date

The provision is effective on the date of enactment.

7. AWARDING OF COSTS AND CERTAIN FEES

a. United States must establish that its position in a proceeding was substantially justified (sec. 701 of the bill and sec. 7430 of the Code)

Present law

Under section 7430, a taxpayer who successfully challenges a determination of deficiency by the IRS may recover attorney's fees and other administrative and litigation costs if the taxpayer qualifies as a "prevailing party." A taxpayer qualifies as a prevailing party if it: (1) establishes that the position of the United States was not substantially justified; (2) substantially prevails with respect to the amount in controversy or with respect to the most significant issue or set of issues presented; and (3) meets certain net worth and (if the taxpayer is a business) size requirements. A taxpayer must exhaust administrative remedies to be eligible to receive an award of attorney's fees.

Reasons for change

The Committee believes that it is appropriate for the IRS to demonstrate that it was substantially justified in maintaining its position when the taxpayer substantially prevails and that the IRS should be required to follow its published guidance and private guidance provided to taxpayers.

Explanation of provision

The bill provides that, once a taxpayer substantially prevails over the IRS in a tax dispute, the IRS has the burden of proof to establish that it was substantially justified in maintaining its position against the taxpayer. This will switch the current procedure which places the burden of proof on the taxpayer to establish that the IRS was not substantially justified in maintaining its position. Therefore, the successful taxpayer will receive an award of attorney's fees unless the IRS satisfies its burden of proof. The bill also establishes a rebuttable presumption that the position of the United States was not substantially justified if the IRS did not follow in the administrative proceeding (1) its published regulations, revenue rulings, revenue procedures, information releases, notices, or announcements, or (2) a private letter ruling, determination letter, or technical advice memorandum issued to the taxpayer. This provision only applies to the version of IRS guidance that is most current on the date the IRS's position was taken.

Effective date

The provision is effective for proceedings commenced after the date of enactment.

b. Increased limit on attorney's fees (sec. 702 of the bill and sec. 7430 of the Code)

Present law

Attorney's fees recoverable by prevailing parties as litigation or administrative costs was originally set at $75 per hour.

Reasons for change

The Committee believes that these amounts should be raised and indexed for inflation.

Explanation of provision

The bill raises the statutory rate to $110 per hour, indexed for inflation beginning after 1996.

Effective date

The provision applies to proceedings commenced after the date of enactment.

c. Failure to agree to extension not taken into account (sec. 703 of the bill and sec. 7430 of the Code)

Present law

To qualify for an award of attorney's fees, the taxpayer must have exhausted the administrative remedies available within the IRS.

Reasons for change

The IRS has taken the position in regulations that attorney's fees cannot be awarded if the taxpayer has not agreed to extend the statute of limitations. *In Minahan* v. *Commissioner,* 88 T.C. 492 (1987), the Tax Court held that regulation invalid insofar as it pro-

vides that a taxpayer's refusal to consent to extend the statute of limitations is to be taken into account in determining whether the taxpayer has exhausted administrative remedies available to the taxpayer.

Explanation of provision

The bill provides that any failure to agree to an extension of the statute of limitations cannot be taken into account for purposes of determining whether a taxpayer has exhausted the administrative remedies for purposes of determining eligibility for an award of attorney's fees.

Effective date

The provision applies to proceedings commenced after the date of enactment.

d. Award of litigation costs permitted in declaratory judgment proceedings (sec. 704 of the bill and sec. 7430 of the Code)

Present law

Section 7430(b)(3) denies any reimbursement for attorney's fees in all declaratory judgment actions, except those actions related to the revocation of an organization's qualification under section 501(c)(3) (relating to tax-exempt status).

Reasons for change

It is appropriate to treat declaratory judgment proceedings similar to other tax proceedings, with respect to eligibility for attorney's fees.

Explanation of provision

The bill eliminates the present-law restrictions on awarding attorney's fees in all declaratory judgment proceedings.

Effective date

The provision applies to proceedings commenced after the date of enactment.

8. MODIFICATION TO RECOVERY OF CIVIL DAMAGES FOR UNAUTHORIZED COLLECTION ACTIONS

a. Increase in limit on recovery of civil damages for unauthorized collection actions (sec. 801 of the bill and sec. 7433 of the Code)

Present law

A taxpayer may sue the United States for up to $100,000 of damages caused by an officer or employee of the IRS who recklessly or intentionally disregards provisions of the Internal Revenue Code or the Treasury regulations promulgated thereunder in connection with the collection of Federal tax with respect to the taxpayer.

Reasons for change

The Committee believes that the cap for damages caused by IRS employees should be raised.

Explanation of provision

The bill increases the cap from $100,000 to $1 million.

Effective date

The provision applies to unauthorized collection actions by IRS employees that occur after the date of enactment.

b. Court discretion to reduce award for litigation costs for failure to exhaust administrative remedies (sec. 802 of the bill and sec. 7433 of the Code)

Present law

A taxpayer suing the United States for civil damages for unauthorized collection activities must exhaust administrative remedies to be eligible for an award.

Reasons for change

There may be circumstances in which it is inappropriate to require a taxpayer to exhaust administrative remedies.

Explanation of provision

The bill permits (but does not require) a court to reduce an award if the taxpayer has not exhausted administrative remedies.

Effective date

The provision is effective for proceedings commenced after the date of enactment.

9. MODIFICATION TO PENALTY FOR FAILURE TO COLLECT AND PAY OVER TAX

a. Preliminary notice requirement (sec. 901 of the bill and sec. 6672 of the Code)

Present law

Under section 6672, a "responsible person" is subject to a penalty equal to the amount of trust fund taxes that are not collected or paid to the government on a timely basis. An individual the IRS has identified as a responsible person is permitted an administrative appeal on the question of responsibility.

Reasons for change

Some employees may not be fully aware of their personal liability under section 6672 for the failure to pay over trust fund taxes. The Committee believes that IRS could make additional efforts to assist the public in understanding its responsibilities.

Explanation of provision

The bill requires the IRS to issue a notice to an individual the IRS had determined to be a responsible person with respect to unpaid trust fund taxes at least 60 days prior to issuing a notice and demand for the penalty. The statute of limitations shall not expire before the date 90 days after the date on which the notice was

mailed. The provision does not apply if the Secretary finds that the collection of the penalty is in jeopardy.

Effective date

The provision applies to assessments made after June 30, 1996.

b. Disclosure of certain information where more than one person subject to penalty (sec. 902 of the bill and sec. 6103 of the Code)

Present law

The IRS may not disclose to a responsible person the IRS's efforts to collect unpaid trust fund taxes from other responsible persons, who may also be liable for the same tax liability.

Reasons for change

The Committee believes that it is appropriate to permit the IRS to disclose to a responsible person whether the IRS is imposing the penalty on any other responsible person, and whether the IRS has been successful in collecting the penalty against such a person.

Explanation of provision

The bill requires the IRS, if requested in writing by a person considered by the IRS to be a responsible person, to disclose in writing to that person the name of any other person the IRS has determined to be a responsible person with respect to the tax liability. The IRS is required to disclose in writing whether it has attempted to collect this penalty from other responsible persons, the general nature of those collection activities, and the amount (if any) collected. Failure by the IRS to follow this provision does not absolve any individual for any liability for this penalty.

Effective date

The provision is effective on the date of enactment.

c. Right of contribution from multiple responsible parties (sec. 903 of the bill and sec. 6672 of the code)

Present law

A responsible person may seek to recover part of the amount which he has paid to the IRS from other individuals who also may have the obligations of a responsible person but who have not yet contributed their proportionate share of their liability under section 6672. Taxpayers must pursue such claims for contribution under state law (to the extent state law permits such claims). The variations in state law sometimes make it difficult or impossible to press successful suits in state courts to force a contribution from other responsible persons.

Reasons for change

The IRS may collect this penalty from a responsible person from whom it can collect most easily, rather than from the person with the greatest culpability for the failure. It would accordingly promote fairness in the administration of the tax laws to establish a right of contribution among multiple responsible parties.

Explanation of provision

If more than one person is liable for this penalty, each person who paid the penalty is entitled to recover from other persons who are liable for the penalty an amount equal to the excess of the amount paid by such person over such person's proportionate share of the penalty. This proceeding is a Federal cause of action and must be entirely separate from any proceeding involving IRS's collection of the penalty from any responsible party (including a proceeding in which the United States files a counterclaim or third-party complaint for collection of the penalty).

Effective date

The provision applies to penalties assessed after the date of enactment.

d. Board members of tax-exempt organizations (sec. 904 of the bill and sec. 6672 of the code)

Present law

Under section 6672, "responsible persons" of tax-exempt organizations are subject to a penalty equal to the amount of trust fund taxes that are not collected and paid to the Government on a timely basis.

Reasons for change

Individuals who serve on the boards of tax-exempt organizations, on a voluntary or honorary basis, are often concerned that they will be held liable for unpaid taxes of the organization as a responsible person, even though their service may be strictly voluntary in nature, and they may not be involved in the day-to-day operations and financial decisions of the organization. The Committee believes that the IRS has not made adequate efforts to clarify the rules applicable to tax-exempt organizations.

Explanation of provision

The bill clarifies that the section 6672 responsible person penalty is not to be imposed on volunteer, unpaid members of any board of trustees or directors of a tax-exempt organization to the extent such members are solely serving in an honorary capacity, do not participate in the day-to-day or financial activities of the organization, and do not have actual knowledge of the failure. The provision cannot operate in such a way as to eliminate all responsible persons from responsibility.

The bill requires the IRS to develop materials to better inform board members of tax-exempt organizations (including voluntary or honorary members) that they may be treated as responsible persons. The IRS is required to make such materials routinely available to tax-exempt organizations. The bill also requires the IRS to clarify its instructions to IRS employees on application of the responsible person penalty with regard to honorary or volunteer members of boards of trustees or directors of tax-exempt organizations.

Effective date

The provision is effective on the date of enactment.

10. MODIFICATIONS OF RULES RELATING TO SUMMONSES

a. Enrolled agents included as third-party recordkeepers (sec. 1001 of the bill and sec. 7609 of the code)

Present law

Section 7609 contains special procedures that the IRS must follow before it issues a third-party summons. A third-party summons is a summons issued to a third-party recordkeeper compelling him to provide information with respect to the taxpayer. An example of this would be a summons served on a stock brokerage house to provide data on the securities trading of the taxpayer-client.

If a third-party summons is served on a third-party recordkeeper listed in section 7609(a)(3), then the taxpayer must receive notice of the summons and have an opportunity to challenge the summons in court. Otherwise the taxpayer has no statutory right to receive notice of the summons and accordingly he will not have the opportunity to challenge it in court.

Section 7609(a)(3) lists attorneys and accountants as third-party recordkeepers, but it does not list "enrolled agents", who are authorized to practice before the IRS.

Reasons for change

Because enrolled agents are authorized to practice before the IRS in a similar manner to attorneys and accountants, they should be accorded the same status as third-party recordkeepers as are attorneys and accountants.

Explanation of provision

The bill includes enrolled agents as third-party recordkeepers.

Effective date

The provision applies to summonses issued after the date of enactment.

b. Safeguards relating to designated summonses; annual report to Congress on designated summonses (secs. 1002 and 1003 of the bill and sec. 6503 of the Code)

Present law

The period for assessment of additional tax with respect to most tax returns, corporate or otherwise, is three years. The IRS and the taxpayer can together agree to extend the period, either for a specified period of time or indefinitely. The taxpayer may terminate an indefinite agreement to extend the period by providing notice to the IRS.

During an audit, the IRS may informally request that the taxpayer provide additional information necessary to arrive at a fair and accurate audit adjustment, if any adjustment is warranted. Not all taxpayers cooperate by providing the requested information on a timely basis. In some cases the IRS seeks information by issu-

ing an administrative summons. Such a summons will not be judicially enforced unless the Government (as a practical matter, the Department of Justice) seeks and obtains an order for enforcement in Federal court. In addition, a taxpayer may petition the court to quash an administrative summons where this is permitted by statute.[1]

In certain cases, the running of the assessment period is suspended during the period when the parties are in court to obtain or avoid judicial enforcement of an administrative summons. Such a suspension is provided in the case of litigation over a third-party summons (sec. 7609(e)) or litigation over a summons regarding the examination of a related party transaction. Such a suspension can also occur with respect to a corporate tax return if a summons is issued at least 60 days before the day on which the assessment period (as extended) is scheduled to expire. In this case, suspension is only permitted if the summons clearly states that it is a "designated summons" for this purpose. Only one summons may be treated as a designated summons for purposes of any one tax return. The limitations period is suspended during the judicial enforcement period of the designated summons and of any other summons relating to the same tax return that is issued within 30 days after the designated summons is issued.

Under current internal procedures of the IRS, no designated summons is issued unless first reviewed by the Office of Chief Counsel to the IRS, including review by an IRS Deputy Regional Counsel for the Region in which the examination of the corporation's return is being conducted.

Reasons for change

The Committee recognizes that issuance of a designated summons is a serious step in the examination of a tax return, given the fact that litigation over the summons would suspend the running of the period for assessing additional tax against the taxpayer under audit. The Committee believes that, in recognition of the seriousness of such a step, the IRS should be required to institute additional procedures to ensure high-level IRS review before any such summons is issued. The Committee also believes that it is important to place some restrictions on the taxpayers to whom IRS can issue a designated summons.

Explanation of provision

The bill requires that issuance of any designated summons with respect to a corporation's tax return must be preceded by review of such issuance by the Regional Counsel, Office of Chief Counsel to the IRS, for the Region in which the examination of the corporation's return is being conducted.

The bill also limits the use of a designated summons to corporations (or to any other person to whom the corporation has transferred records) that are being examined as part of the Coordinated Examination Program (CEP) or its successor. CEP audits cover about 1,600 of the largest corporate taxpayers. If a corporation

[1] Petitions to quash are permitted, for example, in connection with the examination of certain related party transactions under section 6038A(e)(4), and in the case of certain third-party summonses under section 7609(b)(2).

moves between CEP and non-CEP audit categories, only the tax years covered by the CEP may be the subject of a designated summons. The bill does not affect Code section 6038A(e)(1), which relates to a U.S. reporting corporation that acts merely as the agent of the foreign related party by receiving summonses on behalf of the foreign party.

The bill also requires that the Treasury report annually to the Congress on the number of designated summonses issued in the preceding 12 months.

Effective date

The provision applies to summonses issued after date of enactment.

11. RELIEF FROM RETROACTIVE APPLICATION OF TREASURY DEPARTMENT REGULATIONS (SEC. 1101 OF THE BILL AND SEC. 7805 OF THE CODE)

Present law

Under section 7805(b), Treasury may prescribe the extent (if any) to which regulations shall be applied without retroactive effect.

Reasons for change

The Committee believes that it is generally inappropriate for Treasury to issue retroactive regulations.

Explanation of provision

The bill provides that temporary and proposed regulations must have an effective date no earlier than the date of publication in the Federal Register or the date on which any notice substantially describing the expected contents of such regulation is issued to the public. Any regulations filed or issued within 18 months of the enactment of the statutory provision to which the regulation relates may be issued with retroactive effect. This general prohibition on retroactive regulations may be superseded by a legislative grant authorizing the Treasury to prescribe the effective date with respect to a statutory provision. The Treasury may issue retroactive temporary or proposed regulations to prevent abuse. The Treasury also may issue retroactive temporary, proposed, or final regulations to correct a procedural defect in the issuance of a regulation. Treasury may provide that taxpayers may elect to apply a temporary or proposed regulation retroactively from the date of publication of the regulation. Final regulations may take effect from the date of publication of the temporary or proposed regulation to which they relate. The provision does not apply to any regulation relating to internal Treasury Department policies, practices, or procedures. Present law with respect to rulings is unchanged.

Effective date

The provision applies with respect to regulations that relate to statutory provisions enacted on or after the date of enactment.

12. MISCELLANEOUS PROVISIONS

a. Phone numbers of person providing payee statement required to be shown on such statement (sec. 1201 of the bill and secs. 6041, 6041A, 6042, 6044, 6045, 6049, 6050B, 6050H, 6050I, 6050J, 6050K and 6050N of the Code)

Present law

Information returns must contain the name and address of the payor.

Reasons for change

Taxpayers often need to contact payors issuing information returns in order to resolve questions about the accuracy of the information provided to the IRS. Currently, payors are only required to provide their names and addresses on information returns. As a result, taxpayers may have difficulty in contacting the payor and resolving questions quickly.

Explanation of provision

The bill requires that information returns contain the name, address, and phone number of the information contact of the person required to make the information return. A payor may, for example, provide the phone number of the department with the relevant information. It is intended that the telephone number provide direct access to individuals with immediate resources to resolve a taxpayer's questions in an expeditious manner.

Effective date

The provision applies to statements required to be furnished after December 31, 1996 (determined without regard to any extension).

b. Required notice to taxpayers of certain payments (sec. 1202 of the bill)

Present law

If the IRS receives a payment without sufficient information to properly credit it to a taxpayer's account, the IRS may attempt to contact the taxpayer. If contact cannot be made, the IRS places the payment in an unidentified remittance file.

Reasons for change

If the IRS cannot associate a taxpayer's payment with a balance due, the IRS generally deposits the money and may not inform the taxpayer of the overpayment. For example, a check that is separated from a balance-due income tax return, which is subsequently lost, may not get credited to that taxpayer's account.

Explanation of provision

The bill requires the IRS to make reasonable efforts to notify, within 60 days, those taxpayers who have made payments which the IRS cannot associate with the taxpayer.

Effective date

The provision is effective on the date of enactment.

c. Unauthorized enticement of information disclosure (sec. 1203 of the bill and new sec. 7435 of the Code)

Present law

No statutory disincentive applies to IRS employees who entice a tax professional to disclose information about clients in exchange for the favorable treatment of the taxes of the professional.

Reasons for change

The Committee believes that it is improper for IRS employees to entice tax professionals into breaching their fiduciary responsibilities to their clients in exchange for favorable treatment on their own returns.

Explanation of provision

If any officer or employee of the United States intentionally compromises the determination or collection of any tax due from an attorney, certified public accountant, or enrolled agent representing a taxpayer in exchange for information conveyed by the taxpayer to the attorney, certified public accountant, or enrolled agent for purposes of obtaining advice concerning the taxpayer's tax liability, the taxpayer may bring a civil action for damages against the United States in a district court of the United States. Upon a finding of liability, damages shall equal the lesser of $500,000 or the sum of (1) actual economic damages sustained by the taxpayer as a proximate result of the information disclosure and (2) the costs of the action. These remedies shall not apply to information conveyed to an attorney, certified public accountant, or enrolled agent for the purpose of perpetrating a fraud or crime.

Effective date

The provision applies to actions taken after the date of enactment.

d. Annual reminders to taxpayers with outstanding delinquent accounts (sec. 1204 of the bill and new sec. 7524 of the Code)

Present law

There is no statutory requirement in the Code that the IRS send annual reminders to persons who have outstanding tax liabilities.

Reasons for change

Numerous taxpayers become delinquent in paying their tax liability. The delinquencies may occur because the person did not make enough payments through payroll withholding or quarterly estimated payments or because of an adjustment following an audit.

The IRS generally pursues larger tax deficiencies first, and then it pursues small deficiencies. Because of the limited amount of IRS resources to work collection cases, cases with smaller deficiencies may not be addressed for years. In the meantime, the taxpayer

may come to believe that the apparent lack of IRS collection activity means that it has abandoned its claim against the taxpayer. The taxpayer may be surprised when the IRS resumes collection action years later, when the 10-year statute of limitations on collections is close to expiring.

Explanation of provision

The bill requires the IRS to send taxpayers an annual reminder of their outstanding tax liabilities. The fact that a taxpayer did not receive a timely, annual reminder notice does not affect the tax liability.

Effective date

The provision requires the IRS to send annual reminder notices beginning in 1997.

e. Five-year extension of authority for undercover operations (sec. 1205 of the bill and sec. 7608 of the Code)

Present law

The Anti-Drug Abuse Act of 1988 exempted IRS undercover operations from the otherwise applicable statutory restrictions controlling the use of Government funds (which generally provide that all receipts be deposited in the general fund of the Treasury and all expenses be paid out of appropriated funds). In general, the exemption permits the IRS to "churn" the income earned by an undercover operation to pay additional expenses incurred in the undercover operation. The IRS is required to conduct a detailed financial audit of large undercover operations in which the IRS is churning funds and to provide an annual audit report to the Congress on all such large undercover operations. The exemption originally expired on December 31, 1989, and was extended by the Comprehensive Crime Control Act of 1990 to December 31, 1991. The IRS has not had the authority to churn funds from its undercover operations since 1991.

Reasons for change

Many other law enforcement agencies have churning authority. It is appropriate for IRS to have this authority as well.

Explanation of provision

The bill reinstates the IRS's offset authority under section 7608(c) from the date of enactment until January 1, 2001. The bill amends the IRS annual reporting requirement under section 7608(c)(4)(B) to require the provision of the following data: (1) the date the operation was initiated; (2) the date offsetting was approved; (3) the total current expenditures and the amount and use of proceeds of the operation; (4) a detailed description of the undercover operation projected to generate proceeds, including the potential violation being investigated, and whether the operation is being conducted under grand jury auspices; and (5) the results of the operation to date, including the results of criminal proceedings.

Effective date

The provision would be effective on the date of enactment.

f. Disclosure of returns on cash transactions (sec. 1206 of the bill and sec. 6103 of the Code)

Present law

The Internal Revenue Code prohibits disclosure of tax returns and return information, except to the extent specifically authorized by the Internal Revenue Code (sec. 6103). Unauthorized disclosure is a felony punishable by a fine not exceeding $5,000 or imprisonment of not more than five years, or both (sec. 7213). An action for civil damages also may be brought for unauthorized disclosure (sec. 7431). No tax information may be furnished by the IRS to another agency unless the other agency establishes procedures satisfactory to the IRS for safeguarding the tax information it receives (sec. 6103(p)).

Under section 6050I, any person who receives more than $10,000 in cash in one transaction (or two or more related transactions) in the course of a trade or business generally must file an information return (Form 8300) with the IRS specifying the name, address, and taxpayer identification number of the person from whom the cash was received and the amount of cash received.

The Anti-Drug Abuse Act of 1988 provided a special rule permitting the IRS to disclose these information returns to other Federal agencies for the purpose of administering Federal criminal statutes. The special rule originally was to expire after November 18, 1990, and was extended by the Comprehensive Crime Control Act of 1990 to November 18, 1992.

Reasons for change

Information filed on Form 8300 is very similar to information filed on Currency Transaction Reports (CTRs) under the Bank Secrecy Act. Both types of information reports should be subject to the same disclosure rules.

Explanation of provision

The bill permanently extends the special rule for disclosing Form 8300 information. Moreover, the bill permits disclosures not only to Federal agencies but also to State, local and foreign agencies and for civil, criminal and regulatory purposes (i.e., generally in the same manner as Currency Transaction Reports filed by financial institutions under the Bank Secrecy Act). Disclosure, however, is not permitted to any such agency for purposes of tax administration. The bill also (1) extends the dissemination policies and guidelines under section 6103 to people having access to Form 8300 information, and (2) applies section 6103 sanctions to persons having access to Form 8300 information that disclose this information without proper authorization.

Effective date

The provision is effective on the date of enactment.

g. Disclosure of returns and return information to designee of taxpayer (sec. 1207 of the bill and sec. 6103 of the Code)

Present law

Under present law, the IRS is authorized to disclose the return of any taxpayer, or return information pertaining to a taxpayer, to such person(s) as the taxpayer has designated in a written request.

Reasons for change

The IRS's move to a paperless system depends on the ease and functionality of electronic communication systems, e.g., telephones, facsimile machines, computers, communications networks, etc.

Explanation of provision

The bill deletes the word "written" from the requirement that "written consent" from the taxpayer is necessary for the disclosure of taxpayer information to a designated third party. Allowing the IRS to adopt alternatives to the written request requirement will expedite such changes and facilitate the development and implementation of Tax System Modernization projects. It is anticipated that the IRS will continue to utilize its regulatory authority to impose reasonable restrictions on the form in which a request is made, and that the IRS will in no event accept an unconfirmed verbal request.

Effective date

The provision is effective on the date of enactment.

h. Report on netting of interest on overpayments and liabilities (sec. 1208 of the bill)

Present law

If any portion of a tax is satisfied through the crediting of an overpayment of tax, no interest is imposed on that portion of the tax for any period during which, if the credit had not been made, interest would have been allowable.

The Tax Reform Act of 1986 first implemented an interest rate differential. The underpayment rate was set 1 percent higher than the overpayment rate. The Conference Report to the Tax Reform Act of 1986 stated:

> [t]o the extent a portion of tax due is satisfied by a credit of an overpayment, no interest is imposed on that portion of the tax. Consequently, if an underpayment of $1,000 occurs in year 1, and an overpayment of $1,000 occurs in year 2, no interest is imposed in year 2 because of the rule of section 6601(f). The IRS can at present net many of these offsetting overpayments and underpayments. Nevertheless, the IRS will require a transition period during which to coordinate differential interest rates . . . [t]he Secretary of the Treasury may prescribe regulations providing for netting of tax underpayments and overpayments through the period ending three years after the date of enactment of the bill. By that date, the IRS should have im-

plemented the most comprehensive netting procedures that are consistent with sound administrative practice.

The Omnibus Budget Reconciliation Act of 1990 increased the underpayment rate on certain large corporate underpayments to 3 percent higher than the overpayment rate. The Conference Report stated:

> Under present law, the Secretary has the authority to credit the amount of any overpayment against any liability under the Code * * * to the extent a portion of tax due is satisfied by a credit of an overpayment, no interest is imposed on that portion of the tax * * *. The Secretary should implement the most comprehensive crediting procedures under section 6402 that are consistent with sound administrative practice.

The General Agreement on Tariffs and Trade (GATT) reduced the overpayment rate on certain corporate tax refunds. The legislative history of the GATT legislation stated that:

> The Secretary of the Treasury should implement the most comprehensive crediting procedures under section 6402 that are consistent with sound administrative practice, and should do so as rapidly as is practicable.

Reasons for change

The Committee believes that it is important for the Committee to understand in detail how the IRS has implemented netting procedures to date. Congress has never adopted differential interest rates, or increased the amount of such differential, without at the same time also encouraging the IRS to implement comprehensive interest netting procedures. The Committee is concerned that the IRS has failed to implement comprehensive interest netting procedures and is interested in learning whether the delay stems from technical difficulties or substantive questions about the scope of such interest netting procedures.

Explanation of provision

The bill requires the Secretary of the Treasury to conduct a study of the manner in which the IRS has implemented the netting of interest on overpayments and underpayments and the policy and administrative implications of global netting. The Treasury is required to hold a public hearing to receive comments from any interested party prior to submitting the report of its study to the tax writing committees.

Effective date

The report is due six months after the date of enactment. The Committee understands that the Treasury has already announced that it will conduct this study and will complete it by October 1, 1996. The Committee anticipates that the Treasury will meet its own deadline.

i. Expenses of detection of underpayments and fraud (sec. 1209 of the bill and sec. 7623 of the Code)

Present law

Secretary may, pursuant to regulations, pay rewards for information leading to the detection and punishment of violations of the Internal Revenue laws.

Reasons for change

The Committee believes that improvements should be made to this program.

Explanation of provision

The bill clarifies that rewards may be paid for information relating to civil violations, as well as criminal violations. The bill also provides that the rewards are to be paid out of the proceeds of amounts (other than interest) collected by reason of the information provided. The bill also requires an annual report on the rewards program.

Effective date

The provision is effective six months after the date of enactment.

j. Use of private delivery services for timely-mailing-as-timely-filing rule (sec. 1210 of the bill and sec. 7502 of the Code)

Present law

The Code sets forth the rules for determining when a return, payment of tax, or other document required to be filed with the IRS is deemed to be filed or delivered on a timely basis (sec. 7502). In a recent case interpreting this section (V.L.Correia, 58 F.3d 468 (1995)), the U.S. Court of Appeals for the 9th Circuit upheld the Tax Court's ruling that the section's so-called "timely-mailing as timely-filing" rule does not apply to private delivery companies. Although the Appeals Court agreed that there is a legitimate policy rationale for extending the rule to private delivery companies, it concluded that only Congress, and not the courts, had the power to make such a change.

Reasons for change

There are many private delivery companies operating today which meet the U.S. Postal Service's ability to deliver documents quickly and securely. Every year, many taxpayers needlessly run afoul of the present-law rule because they make a reasonable assumption that using a private delivery service is adequate to show timely filing of their tax returns.

Explanation of provision

The Secretary of the Treasury is given authority to expand the "timely-mailing as timely-filing" rule to include a designated delivery service. A designated delivery service must be designated as such by the Secretary. The Secretary may designate a delivery service only if it meets the following criteria: (1) it is available to the general public; (2) it is at least as timely and reliable on a reg-

ular basis as the United States mail; (3) it satisfies recordkeeping criteria; and (4) it meets any additional criteria as the Secretary may prescribe. The provision also gives the Secretary similar authority with respect to equivalents for United States certified or registered mail.

Effective date

The provision is effective on the date of enactment.

k. Reports on misconduct by IRS employees (sec. 1211 of the bill)

Present law

The IRS Inspection Division investigates allegations of criminal misconduct or serious violations of the "Standards of Ethical Conduct for Employees of the Executive Branch" (5 CFR 2635) by IRS employees. In addition, IRS management addresses other types of taxpayer complaints relating to inappropriate behavior by IRS employees.

Reasons for change

Criminal actions resulting from Inspection Service investigations are a matter of public record, and press releases are issued in conjunction with the U.S. Attorney's office about such matters in accordance with exceptions that exist to tax disclosure and privacy constraints. However, information about administrative disciplinary actions are generally not available to the public. This may lead to a public perception that allegations of misconduct by IRS employees are not investigated or that misconduct goes unpunished.

Explanation of provision

The bill requires the IRS to make an annual report to the tax-writing committees, beginning June 1, 1997, on all categories of instances involving allegations of misconduct by IRS employees, arising either from internally identified cases or from taxpayer or third-party initiated complaints. The report must identify by IRS Region and primary activity involved (e.g., examination, collection, etc.), the nature of the misconduct or complaint, the number of instances received by category, and the disposition of these instances. This would include, but not be limited to, the following categories: number of employees reprimanded, terminated, or prosecuted; instances dismissed because of a finding that proper procedures were followed; and those initiated but not yet resolved. Instances covered by this process must include both written complaints of misconduct and those received by telephone through management channels. Each annual report will cover instances of misconduct that occurred during the preceding calendar year. Disposition of complaints not resolved by the time the report is prepared must be included in the report for the year in which resolution occurs.

Effective date

The first report is due by June 1, 1997.

B. Revenue Offsets

1. APPLICATION OF FAILURE-TO-PAY PENALTY TO SUBSTITUTE RETURNS (SEC. 1301 OF THE BILL AND SEC. 6651 OF THE CODE)

Present law

Section 6651(a)(2) provides that the IRS may assess a penalty for failure to pay tax from the due date of the return until the tax is paid. If no return is filed by the taxpayer and the IRS files a substitute return under section 6020, the tax on which the penalty is measured is considered a deficiency assessable under section 6212 or 6213, and the failure to pay penalty begins to accumulate 10 days after the IRS sends the taxpayer a notice and demand for payment of the tax.

Reasons for change

Under the current penalty system, there is an inequity between voluntarily filed delinquent returns and substitute returns. Taxpayers who file delinquent returns must pay a failure to file penalty from the due date of the return, whereas the taxpayer who forces the IRS to utilize a substitute return is not assessed the penalty until billed by the IRS.

Explanation of provision

The bill applies the failure to pay penalty to substitute returns in the same manner as the penalty applies to delinquent filers.

Effective date

The provision applies in the case of any return the due date for which (determined without regard to extensions) is after the date of enactment.

2. EXCISE TAXES ON AMOUNTS OF PRIVATE EXCESS BENEFITS (SEC. 1311–1314 OF THE BILL AND SECS. 501, 6033, 6104, 6652, 6685 AND NEW SECS. 4958, 6116, AND 6716 OF THE CODE)

Present law

Private inurement

Charities.—Section 501(c)(3) specifically conditions tax-exempt status for all organizations described in that section on the requirement that no part of the net earnings of the organization inures to the benefit of any private shareholder or individual (the so-called "private inurement test").

Social welfare organizations.—A tax-exempt social welfare organization described in section 501(c)(4) must be organized on a nonprofit basis and must be operated exclusively for the promotion of social welfare. In contrast to section 501(c)(3), however, there is no specific statutory rule in section 501(c)(4) prohibiting the net earnings of a social welfare organization described in section 501(c)(4) from inuring to the benefit of a private shareholder or individual.[2]

[2] Even where no prohibited private inurement exists, however, more than incidental private benefits conferred on individuals may result in the organization not being operated "exclusively"

Continued

Other organizations.—Other tax-exempt organizations, such as labor and agricultural organizations described in section 501(c)(5) and business leagues described in section 501(c)(6) are subject to the private inurement test, as a result of explicit statutory language or Treasury Department regulations.

Sanctions for private inurement and other violations of exemption standards

Organizations described in section 501(c)(3) are classified as either public charities or private foundations. Penalty excise taxes may be imposed under the Code when a public charity makes political expenditures (sec. 4955) or excessive lobbying expenditures (secs. 4911 and 4912). However, the Code generally does not provide for the imposition of penalty excise taxes in cases where a 501(c)(3) public charity or a section 501(c)(4) social welfare organization engages in a transaction that results in private inurement. In such cases, the only sanction that specifically is authorized under the Code is revocation of the organization's tax-exempt status. A transaction engaged in by a private foundation (but not a public charity) is subject to special penalty excise taxes under the Code if the transaction is a prohibited "self-dealing" transaction (sec. 4941) or does not accomplish a charitable purpose (sec. 4945).

Filing and public disclosure rules

Tax-exempt organizations (other than churches and certain small organizations) are required to file an annual information return (Form 990) with the Internal Revenue Service ("IRS"), setting forth the organization's items of gross income and expenses attributable to such income, disbursements for tax-exempt purposes, plus certain other information for the taxable year. Private foundations are required to allow public inspection at the foundation's principal office of their current annual information return. Other tax-exempt organizations, including public charities, are required to allow public inspection at the organization's principal office (and certain regional or district offices) of their annual information returns for the three most recent taxable years (sec. 6104(e)). The Code also requires that tax-exempt organizations allow public inspection of the organization's application to the IRS for recognition of tax-exempt status, the IRS determination letter, and certain related documents. In addition, upon written request to the IRS, members of the general public are permitted to inspect annual information returns of tax-exempt organizations and applications for recognition of tax-exempt status (and related documents) at the National Office of the IRS in Washington, D.C. A person making such a written request is notified by the IRS when the material is available for inspection at the National Office, where notes may be taken of the material open for inspection, photographs taken with the person's own equipment, or copies of such material obtained from the IRS for a fee (Treas. Reg. secs. 301.6104(a)–6 and 301.6104(b)–1).

Section 6652(c)(1)(A) provides that a tax-exempt organization that fails to file a complete and accurate Form 990 is subject to a

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for an exempt purpose. See, e.g., American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989).

penalty of $10 for each day during which such failure continues (with a maximum penalty with respect to any one return of the lesser of $5,000 or five percent of the organization's gross receipts for the year). Section 6652(c)(1)(C) provides that tax-exempt organizations that fail to make certain annual returns and applications for exemption available for public inspection are subject to a penalty of $10 for each day the failure continues (with a maximum penalty with respect to any one return not to exceed $5,000, and without limitation with respect to applications). In addition, section 6685 provides a penalty for willfully failing to make an annual return or application available for public inspection of $1,000 per return or application.

Reasons for change

To ensure that the advantages of tax-exempt status ultimately benefit the community and not private individuals, the bill extends the present-law section 501(c)(3) private inurement prohibition to nonprofit organizations described in section 501(c)(4) and provides for intermediate sanctions that may be imposed when nonprofit organizations described in section 501(c)(3) or 501(c)(4) engage in transactions with certain insiders that result in private inurement. The bill also enhances the oversight and public accountability of nonprofit organizations through additional reporting of information by nonprofit organizations to the Internal Revenue Service (IRS) and increased public access to documents filed by such organizations with the IRS.

Explanation of provision

Extend private inurement prohibition to social welfare organizations

The bill amends section 501(c)(4) explicitly to provide that a social welfare organization or other organization described in that section would be eligible for tax-exempt status only if no part of its net earnings inures to the benefit of any private shareholder or individual.

In addition, the bill provides that the private inurement rule will not be violated solely because of an allocation or return of net margins or capital to the members of a nonprofit association or organization that operates on a cooperative basis in accordance with its incorporating statute and bylaws (substantially as in existence on the date of enactment) and was determined to be exempt from Federal income tax under section 501(c)(4) prior to the date of enactment. However, such cooperative organizations are subject to the general private inurement proscription with respect to any other type of transaction.

Effective date.—This provision generally is effective on September 14, 1995. However, under a special transition rule, the provision does not apply to inurement occurring prior to January 1, 1997, if such inurement results from a written contract that was binding on September 13, 1995, and at all times thereafter before such inurement occurred, and the terms of which have not materially changed.

Intermediate sanctions for excess benefit transactions

The bill imposes penalty excise taxes as an intermediate sanction in cases where organizations exempt from tax under section 501(c)(3) or 501(c)(4) (other than private foundations, which are subject to a separate penalty regime under current law) engage in an "excess benefit transaction." In such cases, intermediate sanctions may be imposed on certain disqualified persons (i.e., insiders) who improperly benefit from an excess benefit transaction and on organization managers who participate in such a transaction knowing that it is improper.

An "excess benefit transaction" is defined as: (1) any transaction in which an economic benefit is provided to, or for the use of, any disqualified person if the value of the economic benefit provided directly by the organization (or indirectly through a controlled entity[3]) to such person exceeds the value of consideration (including performance of services) received by the organization for providing such benefit; and (2) to the extent provided in Treasury Department regulations, any transaction in which the amount of any economic benefit provided to, or for the use of, any disqualified person is determined in whole or in part by the revenues of the organization, provided that the transaction constitutes prohibited inurement under present-law section 501(c)(3) or under section 501(c)(4), as amended. Thus, "excess benefit transactions" subject to excise taxes include transactions in which a disqualified person engages in a non-fair-market-value transaction with an organization or receives unreasonable compensation, as well as financial arrangements (to the extent provided in Treasury regulations) under which a disqualified person receives payment based on the organization's income in a transaction that violates the present-law private inurement prohibition. The Treasury Department is instructed to issue prompt guidance providing examples of revenue-sharing arrangements that violate the private inurement prohibition; such guidance shall be applicable on a prospective basis.[4]

Existing tax-law standards (see sec. 162) apply in determining reasonableness of compensation and fair market value.[5] In applying such standards, the Committee intends that the parties to a transaction are entitled to rely on a rebuttable presumption of reasonableness with respect to a compensation arrangement with a disqualified person if such arrangement was approved by a board of directors or trustees (or committee thereof) that: (1) was composed entirely of individuals unrelated to and not subject to the

[3] A tax-exempt organization cannot avoid the private inurement proscription by causing a controlled entity to engage in an excess benefit transaction. Thus, for example, if a tax-exempt organization causes its taxable subsidiary to pay excessive compensation to an individual who is a disqualified person with respect to the parent organization, such transaction would be an excess benefit transaction.

[4] Under present law, certain revenue sharing arrangements have been determined not to constitute private inurement (see e.g., GCM 38283; GCM 38905; and GCM 39674) and, under the proposal, it would continue to be the case that not all revenue sharing arrangements would be improper private inurement. However, the Committee intends no inference that Treasury or the Internal Revenue Service are bound by any particular prior unpublished rulings in this area.

[5] In this regard, the Committee intends that an individual need not necessarily accept reduced compensation merely because he or she renders services to a tax-exempt, as opposed to a taxable, organization. Cf. Treas. Reg. sec. 53.4941(d)-3(c)(1).

control of the disqualified person(s) involved in the arrangement;[6] (2) obtained and relied upon appropriate data as to comparability (e.g., compensation levels paid by similarly situated organizations, both taxable and tax-exempt, for functionally comparable positions; the location of the organization, including the availability of similar specialties in the geographic area; independent compensation surveys by nationally recognized independent firms; or actual written offers from similar institutions competing for the services of the disqualified person); and (3) adequately documented the basis for its determination (e.g., the record includes an evaluation of the individual whose compensation was being established and the basis for determining that the individual's compensation was reasonable in light of that evaluation and data).[7] If these three criteria are satisfied, penalty excise taxes could be imposed under the proposal only if the IRS develops sufficient contrary evidence to rebut the probative value of the evidence put forth by the parties to the transaction (e.g., the IRS could establish that the compensation data relied upon by the parties was not for functionally comparable positions or that the disqualified person, in fact, did not substantially perform the responsibilities of such position). A similar rebuttable presumption would arise with respect to the reasonableness of the valuation of property sold or otherwise transferred (or purchased) by an organization to (or from) a disqualified person if the sale or transfer (or purchase) is approved by an independent board that uses appropriate comparability data and adequately documents its determination. The Secretary of the Treasury and IRS are instructed to issue guidance in connection with the reasonableness standard that incorporates this presumption.

The bill specifically provides that the payment of personal expenses and benefits to or for the benefit of disqualified persons, and non-fair-market-value transactions benefiting such persons, would be treated as compensation only if it is clear that the organization intended and made the payments as compensation for services. In determining whether such payments or transactions are, in fact, compensation, the relevant factors include whether the appropriate decision-making body approved the transfer as compensation in accordance with established procedures and whether the organization and the recipient reported the transfer (except in the case of nontaxable fringe benefits) as compensation on the relevant forms (i.e., the organization's Form 990, the Form W–2 or Form 1099 provided by the organization to the recipient, the recipient's Form 1040, and other required returns).[8]

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[6] A reciprocal approval arrangement whereby an individual approves compensation of the disqualified person, and the disqualified person, in turn, approves the individual's compensation does not satisfy the independence requirement.

[7] The fact that a State or local legislative or agency body may have authorized or approved of a particular compensation package paid to a disqualified person is not determinative of the reasonableness of compensation paid for purposes of the excise tax penalties provided for by the proposal. Similarly, such authorization or approval is not determinative of whether a revenue sharing arrangement violates the private inurement proscription.

[8] With the exception of nontaxable fringe benefits described in present-law section 132 and other types of nontaxable transfers such as employer-provided health benefits and contributions to qualified pension plans, an organization cannot demonstrate at the time of an IRS audit that it clearly indicated its intent to treat economic benefits provided to a disqualified person as compensation for services merely by claiming that such benefits may be viewed as part of the disqualified person's total compensation package. Rather, the organization would be required to provide substantiation that is contemporaneous with the transfer of economic benefits at issue.

Consistent with the rule that payment of personal expenses and benefits to or for the benefit of disqualified persons and nonfair-market value transactions benefiting such persons are treated as compensation only if it is clear that the organization intended and made the payments as compensation for services, any reimbursements by the organization of excise tax liability are treated as an excess benefit unless they are included in the disqualified person's compensation during the year the reimbursement is made. The total compensation package, including the amount of any reimbursement, is subject to the reasonableness requirement. Similarly, the payment by an applicable tax-exempt organization of premiums for an insurance policy providing liability insurance to a disqualified person for excess benefit taxes is an excess benefit transaction unless such premiums are treated as part of the compensation paid to such disqualified person.[9]

"Disqualified person" means any individual who is in a position to exercise substantial influence over the affairs of the organization, whether by virtue of being an organization manager or otherwise.[10] In addition, "disqualified persons" include certain family members and 35-percent owned entities[11] of a disqualified person, as well as any person who was a disqualified person at any time during the five-year period prior to the transaction at issue. A person having the title of "officer, director, or trustee" does not automatically have the status of a disqualified person.[12] In addition, the Secretary of Treasury has authority to promulgate rules exempting broad categories of individuals from the category of "disqualified persons" (e.g., full-time bona fide employees who receive economic benefits of less than a threshold amount or persons who have taken a vow of poverty).

A disqualified person who benefits from an excess benefit transaction is subject to a first-tier penalty tax equal to 25 percent of the amount of the excess benefit (i.e., the amount by which a transaction differs from fair market value, the amount of compensation exceeding reasonable compensation, or (under Treasury regulations) the amount of a prohibited transaction based on the organi-

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[9] In addition, because individuals may be both members of, and disqualified persons with respect to, a non-exclusive applicable tax-exempt organization (e.g., a museum or neighborhood civic organization) and receive certain benefits (e.g., free admission, discounted gift shop purchases) in their capacity as members (rather than in their capacity as disqualified persons), the Committee expects that the Treasury Department will provide guidance clarifying that such membership benefits may be excluded from consideration under the private inurement proscription and intermediate sanction rules.

[10] Under the bill, a person could be in a position to exercise substantial influence over a tax-exempt organization despite the fact that such person is not an employee of (and receives no compensation directly from) a tax-exempt organization, but is formally an employee of (and is directly compensated by) a subsidiary—even a taxable subsidiary—controlled by the parent tax-exempt organization.

[11] Family members are determined under present-law section 4946(d), except that such members also would include siblings (whether by whole or half blood) of the individual, and spouses of such siblings. "35-percent owned entities" mean corporations in which disqualified persons own stock possessing more than 35 percent of the combined voting power, as well as partnerships and trusts or estates in which disqualified persons own more than 35 percent of the profits interest or beneficial interest. As under present-law section 4946(a), the term "combined voting power" includes voting power represented by holdings of voting stock, actual or constructive, but does not include voting rights held only as a director or trustee. See Treas. Reg. sec. 53.4946–1(a)(5).

[12] The IRS has issued a general counsel memorandum indicating that all physicians are considered "insiders" for purposes of applying the private inurement proscription. The Committee intends that physicians will be disqualified persons only if they are in a position to exercise substantial influence over the affairs of an organization.

zation's gross or net income). Organization managers who participate in an excess benefit transaction knowing that it is an improper transaction are subject to a first-tier penalty tax of 10 percent of the amount of the excess benefit (subject to a maximum penalty of $10,000).[13]

Additional, second-tier taxes may be imposed on a disqualified person if there is no correction of the excess benefit transaction within a specified time period.[14] In such cases, the disqualified person is subject to a penalty tax equal to 200 percent of the amount of excess benefit. For this purpose, the term "correction" means undoing the excess benefit to the extent possible and taking any additional measures necessary to place the organization in a financial position not worse than that in which it would be if the disqualified person were dealing under the highest fiduciary standards.

The intermediate sanctions for "excess benefit transactions" may be imposed by the IRS in lieu of (or in addition to) revocation of an organization's tax-exempt status.[15] If more than one disqualified person or manager is liable for a penalty excise tax, then all such persons are jointly and severally liable for such tax. As under current law, a three-year statute of limitations applies, except in the case of fraud (sec. 6501). Under the bill, the IRS has authority to abate the excise tax penalty (under present-law section 4962) if it is established that the violation was due to reasonable cause and not due to willful neglect and the transaction at issue was corrected within the specified period.

To prevent avoidance of the penalty excise taxes in cases of private inurement of assets of a previously tax-exempt organization, the bill provides that an organization will be treated as an applicable tax-exempt organization subject to the excise taxes on excess benefit transactions if, at any time during the 5-year period preceding the transaction, it was a tax-exempt organization described in section 501(c)(3) or 501(c)(4), or a successor to such an organization.

Effective date.—The provision generally applies to excess benefit transactions occurring on or after September 14, 1995. The provision does not apply, however, to any benefits arising out of a transaction pursuant to a written contract which was binding on September 13, 1995, and at all times thereafter before such benefits arose, and the terms of which have not materially changed.

In addition, the Committee intends that parties to transactions entered into after September 13, 1995, and before January 1, 1997, are entitled to rely on the rebuttable presumption of reasonableness if, within a reasonable period (e.g., 90 days) after entering into the compensation package, the parties satisfy the three criteria

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[13] In determining who is an organization manager, the Committee intends that principles similar to those set forth in regulations issued under sections 4946 and 4955 with respect to final authority or responsibility for an expenditure be applied. (See Treas. Reg. secs. 53.4946–1(f)(1)(ii), 53.4946–1(f)(2), 53.4955–1(b)(2)(ii)(B), and 53.4955–1(b)(2)(iii)).

[14] Correction must be made on or prior to the earlier of (1) the date of mailing of a notice of deficiency under section 6212 with respect to the first-tier penalty excise tax imposed on the disqualified person, or (2) the date on which such tax is assessed.

[15] In general, the intermediate sanctions are the sole sanction imposed in those cases in which the excess benefit does not rise to a level where it calls into question whether, on the whole, the organization functions as a charitable or other tax-exempt organization. In practice, revocation of tax-exempt status, with or without the imposition of excise taxes, would occur only when the organization no longer operates as a charitable organization.

that give rise to the presumption. After December 31, 1996, the rebuttable presumption should arise only if the three criteria are satisfied prior to payment of the compensation (or, to the extent provided by the Secretary of the Treasury, within a reasonable period thereafter).

Additional filing and public disclosure rules

Reporting of information with respect to certain disqualified persons, excise tax penalties and excess benefit transactions.—Tax-exempt organizations are required to disclose on their Form 990 such information with respect to disqualified persons as the Secretary of the Treasury may prescribe. The Committee intends that this requirement is not intended to limit the Secretary's authority under section 6033(a)(1) to require information on annual returns filed by exempt organizations for the purpose of carrying out the internal revenue laws. In addition, exempt organizations are required to disclose on their Form 990 such information as the Secretary of the Treasury may require with respect to "excess benefit transactions" (described above) and any other excise tax penalties paid during the year under present-law sections 4911 (excess lobbying expenditures), 4912 (disqualifying lobbying expenditures), or 4955 (political expenditures), including the amount of the excise tax penalties paid with respect to such transactions, the nature of the activity, and the parties involved. [16]

Furnishing copies of documents.—The bill also provides that a tax-exempt organization that is subject to the public inspection rules of present-law section 6104(e)(1) (i.e., any tax-exempt organization, other than a private foundation, that files a Form 990) is required to comply with requests made in writing or in person from individuals who seek a copy of the organization's Form 990 or the organization's application for recognition of tax-exempt status and certain related documents. Upon such a request, the organization is required to supply copies without charge other than a reasonable fee for reproduction and mailing costs. If so requested, copies must be supplied of the Forms 990 for any of the organization's three most recent taxable years. If the request for copies is made in person, then the organization must immediately provide such copies. If the request for copies is made in writing, then copies must be provided within 30 days. However, an organization may be relieved of its obligation to provide copies if, in accordance with regulations to be promulgated by the Secretary of the Treasury, (1) the organization has made the requested documents widely available or (2) the Secretary of the Treasury determined, upon application by the organization, that the organization was subject to a harassment campaign such that a waiver of the obligation to provide copies would be in the public interest.

Penalties for failure to file timely or complete return.—The section 6652(c)(1)(A) penalty imposed on a tax-exempt organization that either fails to file a Form 990 in a timely manner or fails to include

[16] The penalties applicable to failure to file a timely, complete, and accurate return apply for failure to comply with these requirements. In addition, the Committee intends that the IRS implement its plan to require additional Form 990 reporting regarding (1) changes to the governing board or the certified accounting firm, (2) such information as the Treasury Secretary may require relating to professional fundraising fees paid by the organization, and (3) aggregate payments (by related entities) in excess of $100,000 to the highest-paid employees.

all required information on a Form 990 is increased from the present-law level of $10 for each day the failure continues (with a maximum penalty with respect to any one return of the lesser of $5,000 or five percent of the organization's gross receipts) to $20 for each day the failure continues (with a maximum penalty with respect to any one return of the lesser of $10,000 or five percent of the organization's gross receipts). Under the bill, organizations with annual gross receipts exceeding $1 million are subject to a penalty under section 6652(c)(1)(A) of $100 for each day the failure continues (with a maximum penalty with respect to any one return of $50,000). As under present law, no penalty may be imposed under section 6652(c)(1)(A) if it were shown that the failure to file a complete return was due to reasonable cause (sec. 6652(c)(3)).

Penalties for failure to allow public inspection or provide copies.—The section 6652(c)(1)(C) penalty imposed on tax-exempt organizations that fail to allow public inspection or provide copies of certain annual returns or applications for exemption is increased from the present-law level of $10 per day (with a maximum of $5,000) to $20 per day (with a maximum of $10,000). In addition, the section 6685 penalty for willful failure to allow public inspections or provide copies is increased from the present-law level of $1,000 to $5,000.

Effective date.—The public inspection provisions governing tax-exempt organizations generally apply to requests made no earlier than 60 days after the date on which the Treasury Department publishes the anti-harassment regulations required under the provisions. However, the Committee expects that organizations will comply voluntarily with the public inspection provisions prior to the issuance of such regulations. The provisions regarding the reporting on annual returns of excise tax penalties and excess benefit transactions are effective for returns with respect to taxable years beginning on or after the date of enactment.

III. VOTES OF THE COMMITTEE

In compliance with clause 2(l)(2)(B) of rule XI of the Rules of the House of Representatives, the following statement is made concerning the votes of the Committee in its consideration of the bill, H.R. 2337.

Motion to report the bill

The bill, H.R. 2337, as amended, was ordered favorably reported by voice vote on March 21, 1996, with a quorum present.

IV. BUDGET EFFECTS OF THE BILL

A. Committee Estimate of Budgetary Effects

In compliance with clause 7(a) of rule XIII of the Rules of the House of Representatives, the following statement is made concerning the effects on the budget of the bill, H.R. 2337, as reported.

The bill, as amended, is estimated to have the following effects on budget receipts for fiscal years 1996–2002:

ESTIMATED BUDGET EFFECTS OF H.R. 2337 AS APPROVED BY THE COMMITTEE ON WAYS AND MEANS, FISCAL YEARS 1996–2002

[Millions of Dollars]

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	1996–00	1996–02
I. Taxpayer Bill of Rights 2 (Titles I–XIII)										
1. Establishment of position of Taxpayer Advocate	DOE					No Revenue Effect				
2. Expansion of authority to issue Taxpayer Assistance Orders	DOE					No Revenue Effect				
3. Notification of reasons for termination of installment agreements.	6 ma DOE					No Revenue Effect				
4. Administrative review of termination of installment agreements.	1/1/97					No Revenue Effect				
5. Expansion of authority to abate interest	DOE	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)
6. Review of IRS failure to abate interest	DOE	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)
7. Extension of interest-free period for payment of tax	6/30/96	−2	−7	−8	−8	−8	−9	−9	−33	−51
8. Abate penalty for failure to deposit payroll tax:										
a. On-budget	DOE	−23	−1	−1	−1	−1	−1	−1	−27	−29
b. Off-budget (not reflected in net total)	DOE	−38	−1	−1	−1	−1	−1	−1	−42	−44
9. Studies of joint return-related issues	DOE					No Revenue Effect				
10. Joint return may be made after separate returns without full payment of tax.	DOE	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)
11. Disclosure of collection activities	DOE					No Revenue Effect				
12. Withdraw notice of lien	1/1/97					No Revenue Effect				
13. Return levied property	1/1/97					No Revenue Effect				
14. Increase levy exemption	1/1/97	.....	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)
15. Offers-in-compromise	DOE	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)
16. Civil damages for fraudulent filing of information return	DOE					No Revenue Effect				
17. Requirement to conduct reasonable investigation	DOE	−3	−6	−6	−6	−7	−8	−8	−28	−44
18. United States must establish that position in proceeding was substantially jusitified.	DOE	−2	−2	−2	−3	−3	−3	−3	−12	−18
19. Increased limit on attorney fees	DOE	−1	−1	−1	−1	−1	−1	−1	−5	−7
20. Failure to agree to extension not taken into account	DOE					No Revenue Effect				
21. Award of litigation costs permitted in declaratory judgment proceedings.	DOE	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)
22. Increase in limit on recovery of civil damages	DOE	−3	−3	−3	−3	−3	−3	−3	−15	−21
23. Court discretion to reduce award for litigation costs	DOE	−1	−1	−1	−1	−1	−1	−1	−5	−7
24. Preliminary notice requirement	6/30/96					No Revenue Effect				
25. Disclosure of certain information where more than one person liable for penalty.	DOE					No Revenue Effect				

26. Right of contribution where more than one person liable for penalty.	DOE	No Revenue Effect								
27. Volunteer board members of tax-exempt organizations exempt from penalty.	DOE	No Revenue Effect								
28. Enrolled agents included as third-party recordkeepers	DOE	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)
29. Safeguards relating to designated summonses	DOE	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)
30. Report on designated summonses	DOE	No Revenue Effect								
31. Relief from retroactive application of Treasury Department regulations with 18 month safe-harbor.	DOE	.....	−1	−4	−4	−4	−4	−4	−13	−21
32. Phone number of person providing payee statements	1/1/97	No Revenue Effect								
33. Required notice of certain payments	DOE	No Revenue Effect								
34. Unauthorized enticement of information disclosure	DOE	No Revenue Effect								
35. Annual reminders to taxpayers with delinquent accounts	1/1/97	.....	(3)	(3)	(3)	(3)	(3)	(3)	(4)	(4)
36. Reinstatement of authority for undercover operations through 12/31/00.	DOE	(3)	(3)	(3)	(3)	(3)	(3)	(3)	(4)	(4)
37. Disclosure of returns concerning cash transactions	DOE	No Revenue Effect								
38. Disclosure of returns and return information to designee of taxpayer.	DOE	No Revenue Effect								
39. Study of netting of interest on overpayments and liabilities	DOE	No Revenue Effect								
40. Expenses of detection of underpayments and fraud	6 ma DOE	Negligible Revenue Effect								
41. Use of private delivery services for "timely-mailing-as-timely-filing" rule.	DOE	No Revenue Effect								
42. Reports on misconduct by IRS employees	DOE	No Revenue Effect								
Subtotal: Taxpayer Bill of Rights 2		−35	−22	−26	−27	−28	−30	−30	−138	−198

ESTIMATED BUDGET EFFECTS OF H.R. 2337 AS APPROVED BY THE COMMITTEE ON WAYS AND MEANS, FISCAL YEARS 1996–2002—Continued

[Millions of Dollars]

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	1996–00	1996–02
II. REVENUE OFFSETS (Title XIII)										
1. Apply failure to pay penalty to substitute returns	rda DOE	1	3	29	30	32	33	35	95	163
2. Intermediate sanctions for certain tax-exempt organizations	9/14/95/ 1/1/96	4	4	4	5	5	5	6	22	33
Subtotal: Revenue Offsets		5	7	33	35	37	38	41	117	196
Net totals		−30	−15	7	8	9	8	11	−21	−2

Source. Joint Committee on Taxation:

[1] Loss of less than $1 million.
[2] Loss of less than $5 million.
[3] Gain of less than $1 million.
[4] Gain of less than $5 million.
[5] Gain of less than $10 million.
[6] Estimates provided by the Congressional Budget Office (CBO).

Note: Details may not add to totals due to rounding.
Legend for "Effective" column. DOE=date of enactment, rda DOE-returns due after date of enactment, 6 ma DOE=6 months after date of enactment.

B. Statement Regarding New Budget Authority and Tax Expenditures

In compliance with subdivision (B) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, the Committee states that the bill, as amended, involves no new or increased budget authority or tax expenditures.

C. Cost Estimate Prepared by the Congressional Budget Office

In compliance with subdivision (C) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, requiring a cost estimate prepared by the Congressional Budget Office (CBO), the following statement by CBO is provided.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, March 27, 1996.

Hon. BILL ARCHER,
Chairman, Committee on Ways and Means, U.S. House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office and the Joint Committee on Taxation (JCT) have reviewed H.R. 2337, the "Taxpayer Bill of Rights," as ordered reported by the House Committee on Ways and Means on March 21, 1996. The JCT estimates that this bill would decrease governmental receipts by $30 million in fiscal year 1996 and by $21 million over fiscal years 1996 through 2000. The revenue effects of H.R. 2337 are summarized in the table below. Please refer to the enclosed table for a more detailed estimate of the bill.

REVENUE EFFECTS OF H.R. 2337

[By fiscal year, in billions of dollars]

	1996	1997	1998	1999	2000	2001	2002
Projected revenues under current law[a]	1417.581	1475.165	1546.076	1617.969	1697.155	1786.356	1879.335
Proposed changes	−0.030	−0.015	0.007	0.008	0.009	0.008	0.011
Projected revenues under H.R. 2337	1417.551	1475.150	1546.083	1617.977	1697.164	1786.364	1879.346

a. Includes the revenue effects of P.L. 104–7 (H.R. 831), and P.L. 104–117 (H.R. 2778).

In accordance with the requirements of Public Law 104–4, the Unfunded Mandates Reform Act of 1995, JCT has determined that the provisions of the bill contain one unfunded intergovernmental mandate and three unfunded private sector mandates. These provisions would impose direct costs on the private sector of less than $100 million in each year and on governmental units of less than $50 million in each year from 1996–2002. Please refer to the enclosed letter for a more detailed account of these provisions.

Section 252 of the Balanced Budget and Emergency Deficit Control Act of 1985 sets up pay-as-you-go procedures for legislation affecting receipts or direct spending through 1998. Because H.R. 2337 would affect receipts, pay-as-you-go procedures would apply to the bill. These effects are summarized in the table below.

PAY-AS-YOU-GO CONSIDERATIONS

[By fiscal year, in millions of dollars]

	1996	1997	1998
Changes in receipts	−30	−15	7
Changes in outlays	(2)		

If you wish further details, please feel free to contact me or your staff may wish to contact Stephanie Weiner.

Sincerely,

JUNE E. O'NEILL, *Director.*

U.S. CONGRESS,
JOINT COMMITTEE ON TAXATION,
Washington, DC, March 27, 1996.

Mrs. JUNE O'NEILL,
Director, Congressional Budget Office, U.S. Congress, Washington, DC.

DEAR MRS. O'NEILL: We have reviewed H.R. 2337, the "Taxpayer Bill of Rights 2," as amended and passed by the House Committee on Ways and Means on March 21, 1996. In accordance with the requirements of Public Law 104–4, the Unfunded Mandates Reform Act of 1995 (the "Unfunded Mandates Act"), we have determined that the provisions of the bill contain one unfunded intergovernmental mandate and three unfunded private sector mandates.

Section 1201 of the bill requires that information returns include the phone number of the information contact. This is in addition to other information (such as name and address of the payor) that is already required to be included on information returns. The bill does not require that any additional information returns be filed. This provision would impose direct costs on the private sector of less than $100 million in each year and on governmental units of less than $50 million in each year 1996–2002.

Section 1311 of the bill extends the private inurement prohibition currently applicable to organization exempt from tax under Code section 501(c)(3) to organizations exempt from tax under Code section 501(c)(4). Section 1312 of the bill requires tax-exempt organizations to disclose on their annual information returns certain information with respect to disqualified persons, excise tax penalties, and excess benefit transactions. This information would be in addition to the information currently required to be provided. These provisions would impose direct costs on the private sector of less than $100 million in each year 1996–2002.

If you would like to discuss this matter in further detail, please feel free to contact me. Thank you for your cooperation in this matter.

Sincerely,

KENNETH J. KIES, *Chief of Staff.*

V. Other Matters To Be Discussed Under the Rules of the House

A. Committee Oversight Findings and Recommendations

With respect to subdivision (A) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives (relating to oversight findings), the Committee advises that it was a result of the Committee's oversight activities concerning protection of taxpayer rights and needed revenue offsets (applying failure-to-pay penalty to substitute returns and intermediate sanctions for certain tax-exempt organizations) that the Committee concluded that it is appropriate and timely to enact the provisions contained in the bill as amended.

B. Summary of Findings and Recommendations of the Committee on Government Reform and Oversight

With respect to subdivision (D) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, the Committee advises that no oversight findings or recommendations have been submitted to this Committee by the Committee on Government Reform and Oversight with respect to the provisions contained in the bill.

C. Inflationary Impact Statement

In compliance with clause 2(l)(4) of rule XI of the Rules of the House of Representatives, the Committee states that the provisions of the bill are not expected to have an overall inflationary impact on prices and costs in the national economy. As indicated in Part IV.A of this report, the estimated net budget effect of the bill, as amended, is projected to be a revenue reduction of only $2 million over the fiscal year period, 1996–2002.

D. Information Relating to Unfunded Mandates

This information is provided in accordance with section 423 of the Unfunded Mandates Reform Act of 1995 (Public Law 104–4).

The Committee has determined that the provisions of the bill contain one intergovernmental mandate and three unfunded private sector mandates.

Section 1201 of the bill requires that information returns include the telephone number of the information contact of the person required to make the information return. Currently, payors are only required to provide their names and addresses on information returns. This information would be in addition to the information that is currently required to be provided, but the bill would not require that any additional information returns be filed. The Committee believes that inclusion of the telephone number of the payor's information contact will make it easier for taxpayers to resolve questions about the accuracy of the information provided to the IRS on the information return. This provision would impose direct costs on the private sector of less than $100 million in each year and on governmental units of less than $50 million in each year 1996–2002.

Section 1311 of the bill extends the private inurement prohibition currently applicable to organizations exempt from tax under Code section 501(c)(3) to organizations exempt from tax under Code section 501(c)(4). Section 1312 of the bill requires tax-exempt organizations to disclose on their annual information returns certain information with respect to disqualified persons, excise taxes on amounts of private excess benefits, and excess benefit transactions. This information would be in addition to the information currently required to be provided, but the bill would not require that any additional information returns be filed. The Committee believes that inclusion of this information will enhance the oversight and public accountability of nonprofit organizations. These provisions would impose direct costs on the private sector of less than $100 million in each year 1996–2002.

E. Applicability of House Rule XXI5(c)

Rule XXI5(c) of the Rules of the House of Representatives provides that "No bill or joint resolution, amendment, or conference report carrying a Federal income tax rate increase shall be considered as passed or agreed to unless so determined by a vote of not less than three-fifths of the Members voting." The Committee has carefully reviewed the provisions of the bill to determine whether any of these provisions constitute a Federal income tax rate increase within the meaning of the House rules. It is the opinion of the Committee that there is no provision in the bill that constitutes a Federal income tax rate increase within the meaning of House rule XXI5(c) or (d).

VI. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE CODE OF 1986

* * * * * * *

Subtitle A—Income Taxes

* * * * * * *

CHAPTER 1—NORMAL TAXES AND SURTAXES

* * * * * * *

Subchapter F—Exempt Organizations

PART I—GENERAL RULE

* * * * * * *

SEC. 501. EXEMPTION FROM TAX ON CORPORATIONS, CERTAIN TRUSTS, ETC.

(a) * * *

* * * * * * *

(c) LIST OF EXEMPT ORGANIZATIONS.—The following organizations are referred to in subsection (a):

(1) * * *

* * * * * * *

(4)*(A)* Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

(B) Subparagraph (A) shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.

* * * * * * *

Subtitle D—Miscellaneous Excise Taxes

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CHAPTER 42—PRIVATE EXEMPT FOUNDATIONS AND CERTAIN OTHER TAX-EXEMPT ORGANIZATIONS

* * * * * * *

[SUBCHAPTER D. Abatement of first and second tier taxes in certain cases.]

SUBCHAPTER D. Failure by certain charitable organizations to meet certain qualification requirements.

SUBCHAPTER E. Abatement of first and second tier taxes in certain cases.

* * * * * * *

Subchapter C—Political Expenditures of Section 501(c)(3) Organizations

* * * * * * *

SEC. 4955. TAXES ON POLITICAL EXPENDITURES OF SECTION 501(c)(3) ORGANIZATIONS.

(a) * * *

* * * * * * *

(e) COORDINATION WITH [SECTION 4945] *SECTIONS 4945 AND 4958*.—If tax is imposed under this section with respect to any political expenditure, such expenditure shall not be treated as a taxable expenditure for purposes of section 4945 *or an excess benefit for purposes of section 4958*.

* * * * * * *

Subchapter D—Failure by Certain Charitable Organizations To Meet Certain Qualification Requirements

SEC. 4958. TAXES ON EXCESS BENEFIT TRANSACTIONS.

(a) INITIAL TAXES.—

(1) ON THE DISQUALIFIED PERSON.—There is hereby imposed on each excess benefit transaction a tax equal to 25 percent of the excess benefit. The tax imposed by this paragraph shall be paid by any disqualified person referred to in subsection (f)(1) with respect to such transaction.

(2) ON THE MANAGEMENT.—In any case in which a tax is imposed by paragraph (1), there is hereby imposed on the participation of any organization manager in the excess benefit transaction, knowing that it is such a transaction, a tax equal to 10 percent of the excess benefit, unless such participation is not willful and is due to reasonable cause. The tax imposed by this paragraph shall be paid by any organization manager who participated in the excess benefit transaction.

(b) ADDITIONAL TAX ON THE DISQUALIFIED PERSON.—In any case in which an initial tax is imposed by subsection (a)(1) on an excess benefit transaction and the excess benefit involved in such transaction is not corrected within the taxable period, there is hereby imposed a tax equal to 200 percent of the excess benefit involved. The tax imposed by this subsection shall be paid by any disqualified person referred to in subsection (f)(1) with respect to such transaction.

(c) EXCESS BENEFIT TRANSACTION; EXCESS BENEFIT.—For purposes of this section—

(1) EXCESS BENEFIT TRANSACTION.—

(A) IN GENERAL.—The term "excess benefit transaction" means any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly to or for the use of any disqualified person if the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) received for providing such benefit. For purposes of the preceding sentence, an economic benefit shall not be treated as consideration for the performance of services unless such organization clearly indicated its intent to so treat such benefit.

(B) EXCESS BENEFIT.—The term "excess benefit" means the excess referred to in subparagraph (A).

(2) AUTHORITY TO INCLUDE CERTAIN OTHER PRIVATE INUREMENT.—To the extent provided in regulations prescribed by the Secretary, the term "excess benefit transaction" includes any transaction in which the amount of any economic benefit provided to or for the use of a disqualified person is determined in whole or in part by the revenues of 1 or more activities of the organization but only if such transaction results in inurement not permitted under paragraph (3) or (4) of section 501(c), as the case may be. In the case of any such transaction, the excess benefit shall be the amount of the inurement not so permitted.

(d) SPECIAL RULES.—For purposes of this section—

(1) JOINT AND SEVERAL LIABILITY.—If more than 1 person is liable for any tax imposed by subsection (a) or subsection (b), all such persons shall be jointly and severally liable for such tax.

(2) LIMIT FOR MANAGEMENT.—With respect to any 1 excess benefit transaction, the maximum amount of the tax imposed by subsection (a)(2) shall not exceed $10,000.

(e) APPLICABLE TAX-EXEMPT ORGANIZATION.—For purposes of this subchapter, the term "applicable tax-exempt organization" means—

(1) any organization which (without regard to any excess benefit) would be described in paragraph (3) or (4) of section 501(c) and exempt from tax under section 501(a), and

(2) any organization which was described in paragraph (1) at any time during the 5-year period ending on the date of the transaction.

Such term shall not include a private foundation (as defined in section 509(a)).

(f) OTHER DEFINITIONS.—For purposes of this section—

(1) DISQUALIFIED PERSON.—The term "disqualified person" means, with respect to any transaction—

(A) any person who was, at any time during the 5-year period ending on the date of such transaction, in a position to exercise substantial influence over the affairs of the organization,

(B) a member of the family of an individual described in subparagraph (A), and

(C) a 35-percent controlled entity.

(2) ORGANIZATION MANAGER.—The term "organization manager" means, with respect to any applicable tax-exempt organization, any officer, director, or trustee of such organization (or any individual having powers or responsibilities similar to those of officers, directors, or trustees of the organization).

(3) 35-PERCENT CONTROLLED ENTITY.—

(A) IN GENERAL.—The term "35-percent controlled entity" means—

(i) a corporation in which persons described in subparagraph (A) or (B) of paragraph (1) own more than 35 percent of the total combined voting power,

(ii) a partnership in which such persons own more than 35 percent of the profits interest, and

(iii) a trust or estate in which such persons own more than 35 percent of the beneficial interest.

(B) CONSTRUCTIVE OWNERSHIP RULES.—Rules similar to the rules of paragraphs (3) and (4) of section 4946(a) shall apply for purposes of this paragraph.

(4) FAMILY MEMBERS.—The members of an individual's family shall be determined under section 4946(d); except that such members also shall include the brothers and sisters (whether by the whole or half blood) of the individual and their spouses.

(5) TAXABLE PERIOD.—The term "taxable period" means, with respect to any excess benefit transaction, the period beginning with the date on which the transaction occurs and ending on the earliest of—

(A) the date of mailing a notice of deficiency under section 6212 with respect to the tax imposed by subsection (a)(1), or

(B) the date on which the tax imposed by subsection (a)(1) is assessed.

(6) CORRECTION.—The terms "correction" and "correct" mean, with respect to any excess benefit transaction, undoing the excess benefit to the extent possible, and taking any additional measures necessary to place the organization in a financial position not worse than that in which it would be if the disqualified person were dealing under the highest fiduciary standards.

Subchapter [D] *E*—Abatement of First and Second Tier Taxes in Certain Cases

* * * * * * *

SEC. 4963. DEFINITIONS.

(a) FIRST TIER TAX.—For purposes of this subchapter, the term "first tier tax" means any tax imposed by subsection (a) of section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4955, *4958,* 4971, or 4975.

(b) SECOND TIER TAX.—For purposes of this subchapter, the term "second tier tax" means any tax imposed by subsection (b) of section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4955, *4958,* 4971, or 4975.

(c) TAXABLE EVENT.—For purposes of this subchapter, the term "taxable event" means any act (or failure to act) giving rise to liability for tax under section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4955, *4958,* 4971, or 4975.

Subtitle F—Procedure and Administration

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CHAPTER 61—INFORMATION AND RETURNS

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Subchapter A—Returns and Records

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PART II—TAX RETURNS OR STATEMENTS

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Subpart B—Income Tax Returns

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SEC. 6013. JOINT RETURNS OF INCOME TAX BY HUSBAND AND WIFE.

(a) * * *

(b) JOINT RETURN AFTER FILING SEPARATE RETURN.—

(1) * * *

(2) LIMITATIONS FOR MAKING OF ELECTION.—The election provided for in paragraph (1) may not be made—

[(A) unless there is paid in full at or before the time of the filing of the joint return the amount shown as tax upon such joint return; or]

[(B)] *(A)* after the expiration of 3 years from the last date prescribed by law for filing the return for such taxable year (determined without regard to any extension of time granted to either spouse); or

[(C)] *(B)* after there has been mailed to either spouse, with respect to such taxable year, a notice of deficiency under section 6212, if the spouse, as to such notice, files a petition with the Tax Court within the time prescribed in section 6213; or

[(D)] *(C)* after either spouse has commenced a suit in any court for the recovery of any part of the tax for such taxable year; or

[(E)] *(D)* after either spouse has entered into a closing agreement under section 7121 with respect to such taxable year, or after any civil or criminal case arising against either spouse with respect to such taxable year has been compromised under section 7122.

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PART III—INFORMATION RETURNS

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Subpart A—Information Concerning Persons Subject to Special Provisions

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SEC. 6033. RETURNS BY EXEMPT ORGANIZATIONS.

(a) * * *

(b) CERTAIN ORGANIZATIONS DESCRIBED IN SECTION 501(c)(3).—Every organization described in section 501(c)(3) which is subject to the requirements of subsection (a) shall furnish annually information, at such time and in such manner as the Secretary may by forms or regulations prescribe, setting forth—

(1) * * *

* * * * * * *

(9) such other information with respect to direct or indirect transfers to, and other direct or indirect transactions and relationships with, other organizations described in section 501(c) (other than paragraph (3) thereof) or section 527 as the Secretary may require to prevent—

(A) diversion of funds from the organization's exempt purpose, or

(B) misallocation of revenues or expenses, [and]

(10) the respective amounts (if any) of the taxes paid by the organization during the taxable year under the following provisions:

(A) section 4911 (relating to tax on excess expenditures to influence legislation),

(B) section 4912 (relating to tax on disqualifying lobbying expenditures of certain organizations), and

(C) section 4955 (relating to taxes on political expenditures of section 501(c)(3) organizations),

(11) the respective amounts (if any) of the taxes paid by the organization, or any disqualified person with respect to such organization, during the taxable year under section 4958 (relating to taxes on private excess benefit from certain charitable organizations),

(12) such information as the Secretary may require with respect to any excess benefit transaction (as defined in section 4958),

(13) such information with respect to disqualified persons as the Secretary may prescribe, and

[(10)] *(14)* such other information for purposes of carrying out the internal revenue laws as the Secretary may require.

* * * * * * *

(f) CERTAIN ORGANIZATIONS DESCRIBED IN SECTION 501(c)(4).—Every organization described in section 501(c)(4) which is subject to the requirements of subsection (a) shall include on the return required under subsection (a) the information referred to in paragraphs (11), (12) and (13) of subsection (b) with respect to such organization.

[(f)] *(g)* CROSS REFERENCE.—

For provisions relating to statements, etc., regarding exempt status of organizations, see section 6001.

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Subpart B—Information Concerning Transactions With Other Persons

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SEC. 6041. INFORMATION AT SOURCE.

(a) * * *

* * * * * * *

(d) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each person with respect to whom such a return is required a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the person required to make such return, and

* * * * * * *

SEC. 6041A. RETURNS REGARDING PAYMENTS OF REMUNERATION FOR SERVICES AND DIRECT SALES.

(a) * * *

* * * * * * *

(e) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS REQUIRED TO BE FURNISHED.—Every per-

son required to make a return under subsection (a) or (b) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

(1) the [name and address]*name, address, and phone number of the information contact* of the person required to make such return, and * * *

SEC. 6042. RETURNS REGARDING PAYMENTS OF DIVIDENDS AND CORPORATE EARNINGS AND PROFITS.

(a) * * *

* * * * * * *

(c) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the person required to make such return, and

* * * * * * *

SEC. 6044. RETURNS REGARDING PAYMENTS OF PATRONAGE DIVIDENDS.

(a) * * *

* * * * * * *

(e) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every cooperative required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the cooperative required to make such return, and

* * * * * * *

SEC. 6045. RETURNS OF BROKERS.

(a) * * *

(b) STATEMENTS TO BE FURNISHED TO CUSTOMERS.—Every person required to make a return under subsection (a) shall furnish to each customer whose name is required to be set forth in such return a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the person required to make such return, and

* * * * * * *

SEC. 6049. RETURNS REGARDING PAYMENTS OF INTEREST.

(a) * * *

* * * * * * *

(c) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—

(1) IN GENERAL.—Every person required to make a return under subsection (a) shall furnish to each person whose name

is required to be set forth in such return a written statement showing—

(A) the [name and address] *name, address, and phone number of the information contact* of the person required to make such return, and

* * * * * * *

SEC. 6050B. RETURNS RELATING TO UNEMPLOYMENT COMPENSATION.

(a) * * *

(b) Statements To Be Furnished to Individuals With Respect to Whom Information is Required.—Every person required to make a return under subsection (a) shall furnish to each individual whose name is required to be set forth in such return a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the person required to make such return, and

* * * * * * *

SEC. 6050H. RETURNS RELATING TO MORTGAGE INTEREST RECEIVED IN TRADE OR BUSINESS FROM INDIVIDUALS.

(a) * * *

* * * * * * *

(d) STATEMENTS TO BE FURNISHED TO INDIVIDUALS WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each individual whose name is required to be set forth in such return a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the person required to make such return, and

* * * * * * *

SEC. 6050I. RETURNS RELATING TO CASH RECEIVED IN TRADE OR BUSINESS, ETC.

(a) * * *

* * * * * * *

(e) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the person required to make such return, and

* * * * * * *

SEC. 6050J. RETURNS RELATING TO FORECLOSURES AND ABANDONMENTS OF SECURITY.

(a) * * *

* * * * * * *

(e) Statements To Be Furnished to Persons With Respect to Whom Information is Required To Be Furnished.—Every person required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing the [name and address] *name, address, and phone number of the information contact* of the person required to make such return. The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) was made.

SEC. 6050K. RETURNS RELATING TO EXCHANGES OF CERTAIN PARTNERSHIP INTERESTS.

(a) * * *

(b) STATEMENTS TO BE FURNISHED TO TRANSFEROR AND TRANSFEREE.—Every partnership required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the partnership required to make such return, and

SEC. 6050N. RETURNS REGARDING PAYMENTS OF ROYALTIES.

(a) * * *

(b) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—Every person required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

(1) the [name and address] *name, address, and phone number of the information contact* of the person required to make such return, and

* * * * * * *

Subchapter B—Miscellaneous Provisions

* * * * * * *

SEC. 6103. CONFIDENTIALITY AND DISCLOSURE OF RETURNS AND RETURN INFORMATION.

(a) * * *

* * * * * * *

(c) DISCLOSURE OF RETURNS AND RETURN INFORMATION TO DESIGNEE OF TAXPAYER.—The Secretary may, subject to such requirements and conditions as he may prescribe by regulations, disclose the return of any taxpayer, or return information with respect to such taxpayer, to such person or persons as the taxpayer may designate in a [written request for or consent to such disclosure] *request for or consent to such disclosure*, or to any other person at the taxpayer's request to the extent necessary to comply with a request for information or assistance made by the taxpayer to such other person. However, return information shall not be disclosed to

such person or persons if the Secretary determines that such disclosure would seriously impair Federal tax administration.

* * * * * * *

(e) DISCLOSURE TO PERSONS HAVING MATERIAL INTEREST.

(1) * * *

* * * * * * *

(8) DISCLOSURE OF COLLECTION ACTIVITIES WITH RESPECT TO JOINT RETURN.—If any deficiency of tax with respect to a joint return is assessed and the individuals filing such return are no longer married or no longer reside in the same household, upon request in writing by either of such individuals, the Secretary shall disclose in writing to the individual making the request whether the Secretary has attempted to collect such deficiency from such other individual, the general nature of such collection activities, and the amount collected. The preceding sentence shall not apply to any deficiency which may not be collected by reason of section 6502.

(9) DISCLOSURE OF CERTAIN INFORMATION WHERE MORE THAN 1 PERSON SUBJECT TO PENALTY UNDER SECTION 6672.—If the Secretary determines that a person is liable for a penalty under section 6672(a) with respect to any failure, upon request in writing of such person, the Secretary shall disclose in writing to such person—

(A) the name of any other person whom the Secretary has determined to be liable for such penalty with respect to such failure, and

(B) whether the Secretary has attempted to collect such penalty from such other person, the general nature of such collection activities, and the amount collected.

* * * * * * *

(i) Disclosure to Federal Officers or Employees for Administration of Federal Laws Not Relating to Tax Administration.—

(1) * * *

* * * * * * *

[(8) DISCLOSURE OF RETURNS FILED UNDER SECTION 6050I.—The Secretary may, upon written request, disclose returns filed under section 6050I to officers and employees of any Federal agency whose official duties require such disclosure for the administration of Federal criminal statutes not related to tax administration.]

* * * * * * *

(l) DISCLOSURE OF RETURNS AND RETURN INFORMATION FOR PURPOSES OTHER THAN TAX ADMINISTRATION.—

(1) * * *

* * * * * * *

(15) DISCLOSURE OF RETURNS FILED UNDER SECTION 6050I.—The Secretary may, upon written request, disclose to officers and employees of—

(A) any Federal agency,

(B) any agency of a State or local government, or

(C) any agency of the government of a foreign country,

information contained on returns filed under section 6050I. Any such disclosure shall be made on the same basis, and subject to the same conditions, as apply to disclosures of information on reports filed under section 5313 of title 31, United States Code; except that no disclosure under this paragraph shall be made for purposes of the administration of any tax law.

* * * * * * *

(p) PROCEDURE AND RECORDKEEPING.—

(1) * * *

* * * * * * *

(3) RECORDS OF INSPECTION AND DISCLOSURE.—

(A) System of recordkeeping.—Except as otherwise provided by this paragraph, the Secretary shall maintain a permanent system of standardized records or accountings of all requests for inspection or disclosure of returns and return information (including the reasons for and dates of such requests) and of returns and return information inspected or disclosed under this section. Notwithstanding the provisions of section 552a(c) of title 5, United States Code, the Secretary shall not be required to maintain a record or accounting of requests for inspection or disclosure of returns and return information, or of returns and return information inspected or disclosed, under the authority of subsections (c), (e), (h)(1), (3)(A), or (4), (i)(4), ~~[~~(7)(A)(ii), or (8)~~]~~ *or (7)(A)(ii)*, (k)(1), (2), or (6), (l)(1), (4)(B), (5), (7), (8), (9), (10), or (11), (12), (13), ~~[~~or (14)~~]~~ *(14), or (15)*, (m) or (n). The records or accountings required to be maintained under this paragraph shall be available for examination by the Joint Committee on Taxation or the Chief of Staff of such joint committee. Such record or accounting shall also be available for examination by such person or persons as may be, but only to the extent, authorized to make such examination under section 552a(c)(3) of title 5, United States Code.

* * * * * * *

(4) SAFEGUARDS.—Any Federal agency described in subsection (h)(2), (h)(6), (i)(1), (2), (3), ~~[~~(5), or (8)~~]~~ *or (5)*, (j)(1) or (2), (l)(1), (2), (3), (5), (10), (11), (13), or (14) or (o)(1), the General Accounting Office, or any agency, body, or commission described in subsection (d), ~~[~~(i)(3)(B)(i) or (8)~~]~~ *(i)(3)(B)(i)*, or (l)(6), (7), (8), (9), ~~[~~or (12)~~]~~ *(12), or (15)* shall, as a condition for receiving returns or return information—

(A) * * *

* * * * * * *

(F) upon completion of use of such returns or return information—

(i) in the case of an agency, body, or commission described in subsection (d), (i)(3)(B)(i), or (l)(6), (7), (8), or (9) return to the Secretary such returns or return information (along with any copies made therefrom) or make such returns or return information undisclosable

in any manner and furnish a written report to the Secretary describing such manner,

(ii) in the case of an agency described in subsections (h)(2), (h)(6), (i)(1), (2), (3), [(5), or (8)] *or (5)*, (j)(1) or (2), (l)(1), (2), (3), (5), (10), or (11), (12), (13), [or (14)] *(14), or (15)*, or (o)(1), or the General Accounting Office, either—

(I) * * *

* * * * * * *

SEC. 6104. PUBLICITY OF INFORMATION REQUIRED FROM CERTAIN EXEMPT ORGANIZATIONS AND CERTAIN TRUSTS.

(a) * * *

* * * * * * *

(e) PUBLIC INSPECTION OF CERTAIN ANNUAL RETURNS AND APPLICATIONS FOR EXEMPTION.—

(1) ANNUAL RETURNS.

[(A) IN GENERAL.—During the 3-year period beginning on the filing date, a copy of the annual return filed under section 6033 (relating to returns by exempt organizations) by any organization to which this paragraph applies shall be made available by such organization for inspection during regular business hours by any individual at the principal office of the organization and, if such organization regularly maintains 1 or more regional or district offices having 3 or more employees, at each such regional or district office.]

(A) IN GENERAL.—During the 3-year period beginning on the filing date—

(i) a copy of the annual return filed under section 6033 (relating to returns by exempt organizations) by any organization to which this paragraph applies shall be made available by such organization for inspection during regular business hours by any individual at the principal office of such organization and, if such organization regularly maintains 1 or more regional or district offices having 3 or more employees, at each such regional or district office, and

(ii) upon request of an individual made at such principal office or such a regional or district office, a copy of such annual return shall be provided to such individual without charge other than a reasonable fee for any reproduction and mailing costs.

The request described in clause (ii) must be made in person or in writing. If the request under clause (ii) is made in person, such copy shall be provided immediately and, if made in writing, shall be provided within 30 days.

* * * * * * *

(2) APPLICATION FOR EXEMPTION.—

(A) IN GENERAL.—If—

(i) an organization described in subsection (c) or (d) of section 501 is exempt from taxation under section 501(a), and

(ii) such organization filed an application for recognition of exemption under section 501, a copy of such application (together with a copy of any papers submitted in support of such application and any letter or other document issued by the Internal Revenue Service with respect to such application) shall be made available by the organization for inspection during regular business hours by any individual at the principal office of the organization and, if the organization regularly maintains 1 or more regional or district offices having 3 or more employees, at each such regional or district office *(and, upon request of an individual made at such principal office or such a regional or district office, a copy of the material requested to be available for inspection under this subparagraph shall be provided (in accordance with the last sentence of paragraph (1)(A)) to such individual without charge other than reasonable fee for any reproduction and mailing costs).*

* * * * * * *

(3) LIMITATION.—Paragraph (1)(A)(ii) (and the corresponding provision of paragraph (2)) shall not apply to any request if, in accordance with regulations promulgated by the Secretary, the organization has made the requested documents widely available, or, the Secretary determines, upon application by an organization, that such request is part of a harassment campaign and that compliance with such request is not in the public interest.

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CHAPTER 62—TIME AND PLACE FOR PAYING TAX

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Subchapter A—Place and Due Date for Payment of Tax

* * * * * * *

SEC. 6159. AGREEMENTS FOR PAYMENT OF TAX LIABILITY IN INSTALLMENTS.

(a) * * *

(b) EXTENT TO WHICH AGREEMENTS REMAIN IN EFFECT.—

(1) * * *

* * * * * * *

[(3) SUBSEQUENT CHANGE IN FINANCIAL CONDITIONS.—

[(A) IN GENERAL.—If the Secretary makes a determination that the financial condition of a taxpayer with whom the Secretary has entered into an agreement under subsection (a) has significantly changed, the Secretary may alter, modify, or terminate such agreement.

[(B) NOTICE.—Action may be taken by the Secretary under subparagraph (A) only if—

[(i) notice of such determination is provided to the taxpayer no later than 30 days prior to the date of such action, and

[(ii) such notice includes the reasons why the Secretary believes a significant change in the financial condition of the taxpayer has occurred.]

(3) SUBSEQUENT CHANGE IN FINANCIAL CONDITIONS.—If the Secretary makes a determination that the financial condition of a taxpayer with whom the Secretary has entered into an agreement under subsection (a) has significantly changed, the Secretary may alter, modify, or terminate such agreement.

* * * * * * *

(5) NOTICE REQUIREMENTS.—The Secretary may not take any action under paragraph (2), (3), or (4) unless—

(A) a notice of such action is provided to the taxpayer not later than the day 30 days before the date of such action, and

(B) such notice includes an explanation why the Secretary intends to take such action.

The preceding sentence shall not apply in any case in which the Secretary believes that collection of any tax to which an agreement under this section relates is in jeopardy.

(c) ADMINISTRATIVE REVIEW.—The Secretary shall establish procedures for an independent administrative review of terminations of installment agreements under this section for taxpayers who request such a review.

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CHAPTER 63—ASSESSMENT

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Subchapter A—In General

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SEC. 6201. ASSESSMENT AUTHORITY.

(a) * * *

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(d) REQUIRED REASONABLE VERIFICATION OF INFORMATION RETURNS.—In any court proceeding, if a taxpayer asserts a reasonable dispute with respect to any item of income reported on an information return filed with the Secretary under subpart B or C of part III of subchapter A of chapter 61 by a third party and the taxpayer has fully cooperated with the Secretary (including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer as reasonably requested by the Secretary), the Secretary shall have the burden of producing reasonable and probative information concerning such deficiency in addition to such information return.

[(d)] *(e)* DEFICIENCY PROCEEDINGS.—For special rules applicable to deficiencies of income, estate, gift, and certain excise taxes, see subchapter B.

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Subchapter B—Deficiency Procedures in the Case of Income, Estate, Gift, and Certain Excise Taxes

* * * * * * *

SEC. 6213. RESTRICTIONS APPLICABLE TO DEFICIENCIES; PETITION TO TAX COURT.

(a) * * *

* * * * * * *

(e) SUSPENSION OF FILING PERIOD FOR CERTAIN EXCISE TAXES.—The running of the time prescribed by subsection (a) for filing a petition in the Tax Court with respect to the taxes imposed by section 4941 (relating to taxes on self-dealing), 4942 (relating to taxes on failure to distribute income), 4943 (relating to taxes on excess business holdings), 4944 (relating to investments which jeopardize charitable purpose), 4945 (relating to taxes on taxable expenditures), 4951 (relating to taxes on self-dealing), or 4952 (relating to taxes on taxable expenditures), 4955 (relating to taxes on political expenditures), *4958 (relating to private excess benefit),* 4971 (relating to excise taxes on failure to meet minimum funding standard), 4975 (relating to excise taxes on prohibited transactions) shall be suspended for any period during which the Secretary has extended the time allowed for making correction under section 4963(e).

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CHAPTER 64—COLLECTION

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Subchapter C—Lien for Taxes

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SEC. 6323. VALIDITY AND PRIORITY AGAINST CERTAIN PERSONS.

(a) * * *

* * * * * * *

(j) WITHDRAWAL OF NOTICE IN CERTAIN CIRCUMSTANCES.—

(1) IN GENERAL.—The Secretary may withdraw a notice of a lien filed under this section and this chapter shall be applied as if the withdrawn notice had not been filed, if the Secretary determines that—

(A) the filing of such notice was premature or otherwise not in accordance with administrative procedures of the Secretary,

(B) the taxpayer has entered into an agreement under section 6159 to satisfy the tax liability for which the lien was imposed by means of installment payments, unless such agreement provides otherwise,

(C) the withdrawal of such notice will facilitate the collection of the tax liability, or

(D) with the consent of the taxpayer or the Taxpayer Advocate, the withdrawal of such notice would be in the best interests of the taxpayer (as determined by the Taxpayer Advocate) and the United States.

Any such withdrawal shall be made by filing notice at the same office as the withdrawn notice. A copy of such notice of withdrawal shall be provided to the taxpayer.

(2) NOTICE TO CREDIT AGENCIES, ETC.—Upon written request by the taxpayer with respect to whom a notice of a lien was withdrawn under paragraph (1), the Secretary shall promptly make reasonable efforts to notify credit reporting agencies, and any financial institution or creditor whose name and address is specified in such request, of the withdrawal of such notice. Any such request shall be in such form as the Secretary may prescribe.

* * * * * * *

Subchapter D—Seizure of Property for Collection of Taxes

* * * * * * *

SEC. 6334. PROPERTY EXEMPT FROM LEVY.

(a) ENUMERATION.—There shall be exempt from levy—

(1) WEARING APPAREL AND SCHOOL BOOKS.—Such items of wearing apparel and such school books as are necessary for the taxpayer or for members of his family;

(2) FUEL, PROVISIONS, FURNITURE, AND PERSONAL EFFECTS.—[If the taxpayer is the head of a family, so] *So* much of the fuel, provisions, furniture, and personal effects in [his household] *the taxpayer's household*, and of the arms for personal use, livestock, and poultry of the taxpayer, as does not exceed [$1,650 ($1,550 in the case of levies issued during 1989)] *$2,500* in value;

(3) BOOKS AND TOOLS OF A TRADE, BUSINESS, OR PROFESSION.—So many of the books and tools necessary for the trade, business, or profession of the taxpayer as do not exceed in the aggregate [$1,100 ($1,050 in the case of levies issued during 1989)] *$1,250*, in value;

* * * * * * *

(f) INFLATION ADJUSTMENT.—

(1) IN GENERAL.—In the case of any calendar year beginning after 1997, each dollar amount referred to in paragraphs (2) and (3) of subsection (a) shall be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year, by substituting 'calendar year 1996' for "calendar year 1992" in subparagraph (B) thereof.

(2) ROUNDING.—If any dollar amount after being increased under paragraph (1) is not a multiple of $10, such dollar amount shall be rounded to the nearest multiple of $10.

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SEC. 6343. AUTHORITY TO RELEASE LEVY AND RETURN PROPERTY.

(a) * * *

* * * * * * *

(d) RETURN OF PROPERTY IN CERTAIN CASES.—If—

(1) any property has been levied upon, and

(2) the Secretary determines that—

(A) the levy on such property was premature or otherwise not in accordance with administrative procedures of the Secretary,

(B) the taxpayer has entered into an agreement under section 6159 to satisfy the tax liability for which the levy was imposed by means of installment payments, unless such agreement provides otherwise,

(C) the return of such property will facilitate the collection of the tax liability, or

(D) with the consent of the taxpayer or the Taxpayer Advocate, the return of such property would be in the best interests of the taxpayer (as determined by the Taxpayer Advocate) and the United States,

the provisions of subsection (b) shall apply in the same manner as if such property had been wrongly levied upon, except that no interest shall be allowed under subsection (c).

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CHAPTER 65—ABATEMENTS, CREDITS, AND REFUNDS

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Subchapter A—Procedure in General

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SEC. 6404. ABATEMENTS.

(a) * * *

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(e) [ASSESSMENTS] *ABATEMENT* OF INTEREST ATTRIBUTABLE TO *UNREASONABLE* ERRORS AND DELAYS BY INTERNAL REVENUE SERVICE.—

(1) IN GENERAL.—In the case of any assessment of interest on—

(A) any deficiency attributable in whole or in part to any *unreasonable* error or delay by an officer or employee of the Internal Revenue Service (acting in his official capacity) in performing a ministerial *or managerial* act, or

(B) any payment of any tax described in section 6212(a) to the extent that any *unreasonable* error or delay in such payment is attributable to such an officer or employee

being erroneous or dilatory in performing a ministerial *or managerial* act,

the Secretary may abate the assessment of all or any part of such interest for any period. For purposes of the preceding sentence, an error or delay shall be taken into account only if no significant aspect of such error or delay can be attributed to the taxpayer involved, and after the Internal Revenue Service has contacted the taxpayer in writing with respect to such deficiency or payment.

* * * * * * *

(g) REVIEW OF DENIAL OF REQUEST FOR ABATEMENT OF INTEREST.—

(1) IN GENERAL.—The Tax Court shall have jurisdiction over any action brought by a taxpayer who meets the requirements referred to in section 7430(c)(4)(A)(ii) to determine whether the Secretary's failure to abate interest under this section was an abuse of discretion, and may order an abatement, if such action is brought within 180 days after the date of the mailing of the Secretary's final determination not to abate such interest.

(2) SPECIAL RULES.—

(A) DATE OF MAILING.—Rules similar to the rules of section 6213 shall apply for purposes of determining the date of the mailing referred to in paragraph (1).

(B) RELIEF.—Rules similar to the rules of section 6512(b) shall apply for purposes of this subsection.

(C) REVIEW.—An order of the Tax Court under this subsection shall be reviewable in the same manner as a decision of the Tax Court, but only with respect to the matters determined in such order.

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CHAPTER 66—LIMITATIONS

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Subchapter A—Limitations on Assessment and Collection

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SEC. 6503. SUSPENSION OF RUNNING OF PERIOD OF LIMITATION.

(a) * * *

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[(k)**]** *(j)* EXTENSION IN CASE OF CERTAIN SUMMONSES.—

(1) IN GENERAL.—If any designated summons is issued by the Secretary **[**with respect to any return of tax by a corporation**]** *to a corporation (or to any other person to whom the corporation has transferred records) with respect to any return of tax by such corporation for a taxable year (or other period) for which such corporation is being examined under the coordinated examination program (or any successor program) of the Internal Revenue Service*, the running of any period of limita-

tions provided in section 6501 on the assessment of such tax shall be suspended—

(A) * * *

* * * * * * *

(2) DESIGNATED SUMMONS.—For purposes of this subsection—

(A) IN GENERAL.—The term "designated summons" means any summons issued for purposes of determining the amount of any tax imposed by this title if—

(i) the issuance of such summons is preceded by a review of such issuance by the regional counsel of the Office of Chief Counsel for the region in which the examination of the corporation is being conducted,

[(i)] *(ii)* such summons is issued at least 60 days before the day on which the period prescribed in section 6501 for the assessment of such tax expires (determined with regard to extensions), and

[(ii)] *(iii)* such summons clearly states that it is a designated summons for purposes of this subsection.

[(l)] *(k)* CROSS REFERENCES.—

For suspension in case of—

* * * * * * *

CHAPTER 67—INTEREST

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Subchapter A—Interest on Underpayments

* * * * * * *

SEC. 6601. INTEREST ON UNDERPAYMENT, NONPAYMENT, OR EXTENSIONS OF TIME FOR PAYMENT, OF TAX.

(a) * * *

* * * * * * *

(e) APPLICABLE RULES.—Except as otherwise provided in this title—

(1) * * *

(2) INTEREST ON PENALTIES, ADDITIONAL AMOUNTS, OR ADDITIONS TO THE TAX.—

(A) IN GENERAL.—Interest shall be imposed under subsection (a) in respect of any assessable penalty, additional amount, or addition to the tax (other than an addition to tax imposed under section 6651(a)(1), or 6653 or under part II of subchapter A of chapter 68) only if such assessable penalty, additional amount, or addition to the tax is not paid within [10 days from the date of notice and demand therefor] *21 calendar days from the date of notice and demand therefor (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000)*, and in such case interest shall be imposed only

for the period from the date of the notice and demand to the date of payment.

* * * * * * *

[(3) PAYMENTS MADE WITHIN 10 DAYS AFTER NOTICE AND DEMAND.—If notice and demand is made for payment of any amount, and if such amount is paid within 10 days after the date of such notice and demand interest under this section on the amount so paid shall not be imposed for the period after the date of such notice and demand.]

(3) PAYMENTS MADE WITHIN SPECIFIED PERIOD AFTER NOTICE AND DEMAND.—If notice and demand is made for payment of any amount and if such amount is paid within 21 calendar days (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000) after the date of such notice and demand, interest under this section on the amount so paid shall not be imposed for the period after the date of such notice and demand.

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CHAPTER 68—ADDITIONS TO THE TAX, ADDITIONAL AMOUNTS, AND ASSESSABLE PENALTIES

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Subchapter A—Additions to the Tax and Additionl Amounts

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PART I—GENERAL PROVISIONS

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SEC. 6651. FAILURE TO FILE TAX RETURN OR TO PAY TAX.

(a) ADDITION TO THE TAX.—In case of failure—

(1) * * *

* * * * * * *

(3) to pay any amount in respect of any tax required to be shown on a return specified in paragraph (1) which is not so shown (including an assessment made pursuant to section 6213(b)) within [10 days of the date of the notice and demand therefor] *21 calendar days from the date of notice and demand therefor (10 business days if the amount for which such notice and demand is made equals or exceeds $100,000)*, unless it is shown that such failure is due to reasonable cause and not due to willful neglect, there shall be added to the amount of tax stated in such notice and demand 0.5 percent of the amount of such tax if the failure is for not more than 1 month, with an additional 0.5 percent for each additional month or fraction

thereof during which such failure continues, not exceeding 25 percent in the aggregate.

* * * * * * *

(g) TREATMENT OF RETURNS PREPARED BY SECRETARY UNDER SECTION 6020(b).—In the case of any return made by the Secretary under section 6020(b)—

(1) such return shall be disregarded for purposes of determining the amount of the addition under paragraph (1) of subsection (a), but

(2) such return shall be treated as the return filed by the taxpayer for purposes of determining the amount of the addition under paragraphs (2) and (3) of subsection (a).

SEC. 6652. FAILURE TO FILE CERTAIN INFORMATION RETURNS, REGISTRATION STATEMENTS, ETC.

(a) * * *

* * * * * * *

(c) RETURNS BY EXEMPT ORGANIZATIONS AND BY CERTAIN TRUSTS.—

(1) ANNUAL RETURNS UNDER SECTION 6033.—

(A) PENALTY ON ORGANIZATION.—In the case of—

(i) a failure to file a return required under section 6033 (relating to returns by exempt organizations) on the date and in the manner prescribed therefor (determined with regard to any extension of time for filing), or

(ii) a failure to include any of the information required to be shown on a return filed under section 6033 or to show the correct information,

there shall be paid by the exempt organization [$10] *$20* for each day during which such failure continues. The maximum penalty under this subparagraph on failures with respect to any 1 return shall not exceed the lesser of [$5,000] *$10,000* or 5 percent of the gross receipts of the organization for the year. *In the case of an organization having gross receipts exceeding $1,000,000 for any year, with respect to the return required under section 6033 for such year, the first sentence of this subparagraph shall be applied by substituting "$100" for "$20" and, in lieu of applying the second sentence of this subparagraph, the maximum penalty under this subparagraph shall not exceed $50,000.*

* * * * * * *

SEC. 6656. FAILURE TO MAKE DEPOSIT OF TAXES OR OVERSTATEMENT OF DEPOSITS.

(a) * * *

* * * * * * *

(c) EXCEPTION FOR FIRST-TIME DEPOSITORS OF EMPLOYMENT TAXES.—The Secretary may waive the penalty imposed by subsection (a) on a person's inadvertent failure to deposit any employment tax if—

(1) such person meets the requirements referred to in section 7430(c)(4)(A)(ii),

(2) such failure occurs during the 1st quarter that such person was required to deposit any employment tax, and

(3) the return of such tax was filed on or before the due date. For purposes of this subsection, the term "employment taxes" means the taxes imposed by subtitle C.

(d) AUTHORITY TO ABATE PENALTY WHERE DEPOSIT SENT TO SECRETARY.—The Secretary may abate the penalty imposed by subsection (a) with respect to the first time a depositor is required to make a deposit if the amount required to be deposited is inadvertently sent to the Secretary instead of to the appropriate government depository.

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Subchapter B—Assessable Penalties

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PART I—GENERAL PROVISIONS

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SEC. 6672. FAILURE TO COLLECT AND PAY OVER TAX, OR ATTEMPT TO EVADE OR DEFEAT TAX.

(a) * * *

(b) PRELIMINARY NOTICE REQUIREMENT.—

(1) IN GENERAL.—No penalty shall be imposed under subsection (a) unless the Secretary notifies the taxpayer in writing by mail to an address as determined under section 6212(b) that the taxpayer shall be subject to an assessment of such penalty.

(2) TIMING OF NOTICE.—The mailing of the notice described in paragraph (1) shall precede any notice and demand of any penalty under subsection (a) by at least 60 days.

(3) STATUTE OF LIMITATIONS.—If a notice described in paragraph (1) with respect to any penalty is mailed before the expiration of the period provided by section 6501 for the assessment of such penalty (determined without regard to this paragraph), the period provided by such section for the assessment of such penalty shall not expire before the later of—

(A) the date 90 days after the date on which such notice was mailed, or

(B) if there is a timely protest of the proposed assessment, the date 30 days after the Secretary makes a final administrative determination with respect to such protest.

(4) EXCEPTION FOR JEOPARDY.—This subsection shall not apply if the Secretary finds that the collection of the penalty is in jeopardy.

[(b)] *(c)* EXTENSION OF PERIOD OF COLLECTION WHERE BOND IS FILED.—

(1) IN GENERAL.—If, within 30 days after the day on which notice and demand of any penalty under subsection (a) is made against any person, such person—

(A) * * *

* * * * * * *

(d) RIGHT OF CONTRIBUTION WHERE MORE THAN 1 PERSON LIABLE FOR PENALTY.—If more than 1 person is liable for the penalty under subsection (a) with respect to any tax, each person who paid such penalty shall be entitled to recover from other persons who are liable for such penalty an amount equal to the excess of the amount paid by such person over such person's proportionate share of the penalty. Any claim for such a recovery may be made only in a proceeding which is separate from, and is not joined or consolidated with—

(1) an action for collection of such penalty brought by the United States, or

(2) a proceeding in which the United States files a counterclaim or third-party complaint for the collection of such penalty.

(e) EXCEPTION FOR VOLUNTARY BOARD MEMBERS OF TAX-EXEMPT ORGANIZATIONS.—No penalty shall be imposed by subsection (a) on any unpaid, volunteer member of any board of trustees or directors of an organization exempt from tax under subtitle A if such member—

(1) is solely serving in an honorary capacity,

(2) does not participate in the day-to-day or financial operations of the organization, and

(3) does not have actual knowledge of the failure on which such penalty is imposed.

The preceding sentence shall not apply if it results in no person being liable for the penalty imposed by subsection (a).

* * * * * * *

SEC. 6685. ASSESSABLE PENALTY WITH RESPECT TO PUBLIC INSPECTION REQUIREMENTS FOR CERTAIN TAX-EXEMPT ORGANIZATIONS.

In addition to the penalty imposed by section 7207 (relating to fraudulent returns, statements, or other documents), any person who is required to comply with the requirements of subsection (d) or (e) of section 6104 and who fails to so comply with respect to any return or application, if such failure is willful, shall pay a penalty of [$1,000] *$5,000* with respect to each such return or application.

* * * * * * *

CHAPTER 74—CLOSING AGREEMENTS AND COMPROMISES

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SEC. 7122. COMPROMISES.

(a) AUTHORIZATION.—The Secretary may compromise any civil or criminal case arising under the internal revenue laws prior to reference to the Department of Justice for prosecution or defense; and the Attorney General or his delegate may compromise any such case after reference to the Department of Justice for prosecution or defense.

(b) RECORD.—Whenever a compromise is made by the Secretary in any case, there shall be placed on file in the office of the Secretary the opinion of the General Counsel for the Department of the Treasury or his delegate, with his reasons therefor, with a statement of—

(1) The amount of tax assessed,

(2) The amount of interest, additional amount, addition to the tax, or assessable penalty, imposed by law on the person against whom the tax is assessed, and

(3) The amount actually paid in accordance with the terms of the compromise.

Notwithstanding the foregoing provisions of this subsection, no such opinion shall be required with respect to the compromise of any civil case in which the unpaid amount of tax assessed (including any interest, additional amount, addition to the tax, or assessable penalty) is less than [$500.] *$50,000. However, such compromise shall be subject to continuing quality review by the Secretary.*

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CHAPTER 75—CRIMES, OTHER OFFENSES, AND FORFEITURES

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Subchapter A—Crimes

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PART I—GENERAL PROVISIONS

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SEC. 7213. UNAUTHORIZED DISCLOSURE OF INFORMATION.

(a) RETURNS AND RETURN INFORMATION.—

(1) FEDERAL EMPLOYEES AND OTHER PERSONS.—It shall be unlawful for any officer or employee of the United States or any person described in section 6103(n) (or an officer or employee of any such person), or any former officer or employee, willfully to disclose to any person, except as authorized in this title, any return or return information (as defined in section 6103(b)). Any violation of this paragraph shall be a felony punishable upon conviction by a fine in any amount not exceeding $5,000, or imprisonment of not more than 5 years, or both, together with the costs of prosecution, and if such offense is committed by any officer or employee of the United States, he shall, in addition to any other punishment, be dismissed from office or discharged from employment upon conviction for such offense.

(2) STATE AND OTHER EMPLOYEES.—It shall be unlawful for any person (not described in paragraph (1)) willfully to disclose to any person, except as authorized in this title, any return or return information (as defined in section 6103(b)) acquired by him or another person under subsection (d), (i)(3)(B)(i), (l)(6),

(7), (8), (9), (10), [or (12)] *(12), or (15)*, or (m)(2), (4), (6), or (7) of section 6103. Any violation of this paragraph shall be a felony punishable by a fine in any amount not exceeding $5,000, or imprisonment of not more than 5 years, or both, together with the costs of prosecution.

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CHAPTER 76—JUDICIAL PROCEEDINGS

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Subchapter B—Proceedings by Taxpayers and Third Parties

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SEC. 7422. CIVIL ACTIONS FOR REFUND

(a) * * *

* * * * * * *

(g) SPECIAL RULES FOR CERTAIN EXCISE TAXES IMPOSED BY CHAPTER 42 OR 43.—

(1) * * *

(2) LIMITATION ON SUIT FOR REFUND.—No suit may be maintained under this section for the credit or refund of any tax imposed under section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4955, *4958,* 4971, or 4975 with respect to any act (or failure to act) giving rise to liability for tax under such sections, unless no other suit has been maintained for credit or refund of, and no petition has been filed in the Tax Court with respect to a deficiency in, any other tax imposed by such sections with respect to such act (or failure to act).

(3) FINAL DETERMINATION OF ISSUES.—For purposes of this section, any suit for the credit or refund of any tax imposed under section 4941, 4942, 4943, 4944, 4945, 4951, 4952, 4955, *4958,* 4971, or 4975 with respect to any act (or failure to act) giving rise to liability for tax under such sections, shall constitute a suit to determine all questions with respect to any other tax imposed with respect to such act (or failure to act) under such sections, and failure by the parties to such suit to bring any such question before the Court shall constitute a bar to such question.

* * * * * * *

SEC. 7430. AWARDING OF COSTS AND CERTAIN FEES

(a) * * *

(b) LIMITATIONS.—

(1) REQUIREMENT THAT ADMINISTRATIVE REMEDIES BE EXHAUSTED.—A judgment for reasonable litigation costs shall not be awarded under subsection (a) in any court proceeding unless the court determines that the prevailing party has exhausted the administrative remedies available to such party within the Internal Revenue Service. *Any failure to agree to an extension of the time for the assessment of any tax shall not be taken into account for purposes of determining whether the prevailing party meets the requirements of the preceding sentence.*

(2) ONLY COSTS ALLOCABLE TO THE UNITED STATES.—An award under subsection (a) shall be made only for reasonable litigation and administrative costs which are allocable to the United States and not to any other party.

[(3) EXCLUSION OF DECLARATORY JUDGMENT PROCEEDINGS.—

[(A) IN GENERAL.—No award for reasonable litigation costs may be made under subsection (a) with respect to any declaratory judgment proceeding.

[(B) EXCEPTION FOR SECTION 501(C)(3) DETERMINATION REVOCATION PROCEEDINGS.—Subparagraph (A) shall not apply to any proceeding which involves the revocation of a determination that the organization is described in section 501(c)(3).

[(4)] *(3)* COSTS DENIED WHERE PARTY PREVAILING PROTRACTS PROCEEDINGS.—No award for reasonable litigation and administrative costs may be made under subsection (a) with respect to any portion of the administrative or court proceeding during which the prevailing party has unreasonably protracted such proceeding.

(c) DEFINITIONS.—For purposes of this section—

(1) REASONABLE LITIGATION COSTS.—The term "reasonable litigation costs" includes—

(A) reasonable court costs, and

(B) based upon prevailing market rates for the kind or quality of services furnished—

(i) * * *

* * * * * * *

(iii) reasonable fees paid or incurred for the services of attorneys in connection with the court proceeding, except that such fees shall not be in excess of [$75] *$110* per hour unless the court determines that [an increase in the cost of living or] a special factor, such as the limited availability of qualified attorneys for such proceeding, justifies a higher rate.

In the case of any calendar year beginning after 1996, the dollar amount referred to in clause (iii) shall be increased by an amount equal to such dollar amount multiplied by the cost-of-living adjustment determined under section 1(f)(3) for such calendar year, by substituting "calendar year 1995" for "calendar year 1992" in subparagraph (B) thereof. If any dollar amount after being increased under the preceding sentence is not a multiple of $10, such dollar amount shall be rounded to the nearest multiple of $10.

(2) REASONABLE ADMINISTRATIVE COSTS.—The term "reasonable administrative costs" means—

(A) any administrative fees or similar charges imposed by the Internal Revenue Service, and

(B) expenses, costs, and fees described in paragraph (1)(B), except that any determination made by the court under clause (ii) or (iii) thereof shall be made by the Internal Revenue Service in cases where the determination under [paragraph (4)(B)] *paragraph (4)(C)* of the awarding of reasonable administrative costs is made by the Internal Revenue Service.

Such term shall only include costs incurred on or after the earlier of (i) the date of the receipt by the taxpayer of the notice of the decision of the Internal Revenue Service Office of Appeals, or (ii) the date of the notice of deficiency.

* * * * * * *

(4) PREVAILING PARTY.—

(A) IN GENERAL.—The term "prevailing party" means any party in any proceeding to which subsection (a) applies (other than the United States or any creditor of the taxpayer involved)—

[(i) which establishes that the position of the United States in the proceeding was not substantially justified,

[(ii)] *(i)* which—

(I) has substantially prevailed with respect to the amount in controversy, or

(II) has substantially prevailed with respect to the most significant issue or set of issues presented, and

[(iii)] *(ii)* which meets the requirements of the 1st sentence of section 2412(d)(1)(B) of title 28, United States Code (as in effect on October 22, 1986) except to the extent differing procedures are established by rule of court and meets the requirements of section 2412(d)(2)(B) of such title 28 (as so in effect).

(B) EXCEPTION IF UNITED STATES ESTABLISHES THAT ITS POSITION WAS SUBSTANTIALLY JUSTIFIED.—

(i) GENERAL RULE.—A party shall not be treated as the prevailing party in a proceeding to which subsection (a) applies if the United States establishes that the position of the United States in the proceeding was substantially justified.

(ii) PRESUMPTION OF NO JUSTIFICATION IF INTERNAL REVENUE SERVICE DIDN'T FOLLOW CERTAIN PUBLISHED GUIDANCE.—For purposes of clause (i), the position of the United States shall be presumed not to be substantially justified if the Internal Revenue Service did not follow its applicable published guidance in the administrative proceeding. Such presumption may be rebutted.

(iii) APPLICABLE PUBLISHED GUIDANCE.—For purposes of clause (ii), the term "applicable published guidance" means—

(I) regulations, revenue rulings, revenue procedures, information releases, notices, and announcements, and

(II) any of the following which are issued to the taxpayer: private letter rulings, technical advice memoranda, and determination letters.

[(B)] *(C)* DETERMINATION AS TO PREVAILING PARTY.—Any determination under [subparagraph (A)] *this paragraph* as to whether a party is a prevailing party shall be made by agreement of the parties or—

(i) * * *

* * * * * * *

SEC. 7433. CIVIL DAMAGES FOR CERTAIN UNAUTHORIZED COLLECTION ACTIONS

(a) * * *

(b) DAMAGES.—In any action brought under subsection (a), upon a finding of liability on the part of the defendant, the defendant shall be liable to the plaintiff in an amount equal to the lesser of [$100,000] *$1,000,000* or the sum of—

(1) * * *

* * * * * * *

(d) LIMITATIONS.—

[(1) REQUIREMENT THAT ADMINISTRATIVE REMEDIES BE EXHAUSTED.—A judgment for damages shall not be awarded under subsection (b) unless the court determines that the plaintiff has exhausted the administrative remedies available to such plaintiff within the Internal Revenue Service.]

(1) AWARD FOR DAMAGES MAY BE REDUCED IF ADMINISTRATIVE REMEDIES NOT EXHAUSTED.—The amount of damages awarded under subsection (b) may be reduced if the court determines that the plaintiff has not exhausted the administrative remedies available to such plaintiff within the Internal Revenue Service.

* * * * * * *

SEC. 7434. CIVIL DAMAGES FOR FRAUDULENT FILING OF INFORMATION RETURNS.

(a) IN GENERAL.—If any person willfully files a fraudulent information return with respect to payments purported to be made to any other person, such other person may bring a civil action for damages against the person so filing such return.

(b) DAMAGES.—In any action brought under subsection (a), upon a finding of liability on the part of the defendant, the defendant shall be liable to the plaintiff in an amount equal to the greater of $5,000 or the sum of—

(1) any actual damages sustained by the plaintiff as a proximate result of the filing of the fraudulent information return (including any costs attributable to resolving deficiencies asserted as a result of such filing),

(2) the costs of the action, and

(3) in the court's discretion, reasonable attorneys fees.

(c) PERIOD FOR BRINGING ACTION.—Notwithstanding any other provision of law, an action to enforce the liability created under this

section may be brought without regard to the amount in controversy and may be brought only within the later of—

(1) 6 years after the date of the filing of the fraudulent information return, or

(2) 1 year after the date such fraudulent information return would have been discovered by exercise of reasonable care.

(d) COPY OF COMPLAINT FILED WITH IRS—Any person bringing an action under subsection (a) shall provide a copy of the complaint to the Internal Revenue Service upon the filing of such complaint with the court.

(e) FINDING OF COURT TO INCLUDE CORRECT AMOUNT OF PAYMENT.—The decision of the court awarding damages in an action brought under subsection (a) shall include a finding of the correct amount which should have been reported in the information return.

(f) INFORMATION RETURN.—For purposes of this section, the term "information return" means any statement described in section 6724(d)(1)(A).

SEC. 7435. CIVIL DAMAGES FOR UNAUTHORIZED ENTICEMENT OF INFORMATION DISCLOSURE.

(a) IN GENERAL.—If any officer or employee of the United States intentionally compromises the determination or collection of any tax due from an attorney, certified public accountant, or enrolled agent representing a taxpayer in exchange for information conveyed by the taxpayer to the attorney, certified public accountant, or enrolled agent for purposes of obtaining advice concerning the taxpayer's tax liability, such taxpayer may bring a civil action for damages against the United States in a district court of the United States. Such civil action shall be the exclusive remedy for recovering damages resulting from such actions.

(b) DAMAGES.—In any action brought under subsection (a), upon a finding of liability on the part of the defendant, the defendant shall be liable to the plaintiff in an amount equal to the lesser of $500,000 or the sum of—

(1) actual, direct economic damages sustained by the plaintiff as a proximate result of the information disclosure, and

(2) the costs of the action.

Damages shall not include the taxpayer's liability for any civil or criminal penalties, or other losses attributable to incarceration or the imposition of other criminal sanctions.

(c) PAYMENT AUTHORITY.—Claims pursuant to this section shall be payable out of funds appropriated under section 1304 of title 31, United States Code.

(d) PERIOD FOR BRINGING ACTION.—Notwithstanding any other provision of law, an action to enforce liability created under this section may be brought without regard to the amount in controversy and may be brought only within 2 years after the date the actions creating such liability would have been discovered by exercise of reasonable care.

(e) MANDATORY STAY.—Upon a certification by the Commissioner or the Commissioner's delegate that there is an ongoing investigation or prosecution of the taxpayer, the district court before which an action under this section is pending shall stay all proceedings with respect to such action pending the conclusion of the investigation or prosecution.

(f) CRIME-FRAUD EXCEPTION.—Subsection (a) shall not apply to information conveyed to an attorney, certified public accountant, or enrolled agent for the purpose of perpetrating a fraud or crime.

SEC. [7434.] *7436.* CROSS REFERENCES

(1) * * *

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Subchapter C—The Tax Court

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PART II—PROCEDURE

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SEC. 7454. BURDEN OF PROOF IN FRAUD, FOUNDATION MANAGER, AND TRANSFEREE CASES

(a) * * *

(b) FOUNDATION MANAGERS.—In any proceeding involving the issue whether a foundation manager (as defined in section 4946(b)) has "knowingly" participated in an act of self-dealing (within the meaning of section 4941), participated in an investment which jeopardizes the carrying out of exempt purposes (within the meaning of section 4944), or agreed to the making of a taxable expenditure (within the meaning of section 4945), or whether the trustee of a trust described in section 501(c)(21) has "knowingly" participated in an act of self-dealing (within the meaning of section 4951) or agreed to the making of a taxable expenditure (within the meaning of section 4952), or whether an organization manager (as defined in section 4955(e)(2)) has "knowingly" agreed to the making of a political expenditure (within the meaning of section 4955), or whether an organization manager (as defined in section 4912(d)(2)) has "knowingly" agreed to the making of disqualifying lobbying expenditures within the meaning of section 4912(b), *or whether an organization manager (as defined in section 4958(f)(2)) has "knowingly" participated in an excess benefit transaction (as defined in section 4958(c)),* the burden of proof in respect of such issue shall be upon the Secretary.

* * * * * * *

CHAPTER 77—MISCELLANEOUS PROVISIONS

SEC. 7502. TIMELY MAILING TREATED AS TIMELY FILING AND PAYING

(a) * * *

* * * * * * *

(f) TREATMENT OF PRIVATE DELIVERY SERVICES.—

(1) IN GENERAL.—Any reference in this section to the United States mail shall be treated as including a reference to any des-

ignated delivery service, and any reference in this section to a postmark by the United States Postal Service shall be treated as including a reference to any date recorded or marked as described in paragraph (2)(C) by any designated delivery service.

(2) DESIGNATED DELIVERY SERVICE.—For purposes of this subsection, the term "designated delivery service" means any delivery service provided by a trade or business if such service is designated by the Secretary for purposes of this section. The Secretary may designate a delivery service under the preceding sentence only if the Secretary determines that such service—

(A) is available to the general public,

(B) is at least as timely and reliable on a regular basis as the United States mail,

(C) records electronically to its data base, kept in the regular course of its business, or marks on the cover in which any item referred to in this section is to be delivered, the date on which such item was given to such trade or business for delivery, and

(D) meets such other criteria as the Secretary may prescribe.

(3) EQUIVALENTS OF REGISTERED AND CERTIFIED MAIL.—The Secretary may provide a rule similar to the rule of paragraph (1) with respect to any service provided by a designated delivery service which is substantially equivalent to United States registered or certified mail.

* * * * * * *

SEC. 7524. ANNUAL NOTICE OF TAX DELINQUENCY.

Not less often than annually, the Secretary shall send a written notice to each taxpayer who has a tax delinquent account of the amount of the tax delinquency as of the date of the notice.

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CHAPTER 78—DISCOVERY OF LIABILITY AND ENFORCEMENT OF TITLE

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Subchapter A—Examination and Inspection

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SEC. 7608. AUTHORITY OF INTERNAL REVENUE ENFORCEMENT OFFICERS

(a) * * *

* * * * * * *

(c) RULES RELATING TO UNDERCOVER OPERATIONS.—

(1) * * *

* * * * * * *

(4) AUDITS

(A) * * *

(B) The Service shall also submit a report annually to the Congress specifying as to its undercover investigative operations—

(i) the number, by programs, of undercover investigative operations pending as of the end of the 1-year period for which such report is submitted;

(ii) the number, by programs, of undercover investigative operations commenced in the 1-year period [preceding the period] for which such report is submitted; [and

[(iii) the number, by programs, of undercover investigative operations closed in the 1-year period preceding the period for which such report is submitted and, with respect to each such closed undercover operation, the results obtained and any civil claims made with respect thereto.]

(iii) the number, by programs, of undercover investigative operations closed in the 1-year period for which such report is submitted, and

(iv) the following information with respect to each undercover investigative operation pending as of the end of the 1-year period for which such report is submitted or closed during such 1-year period—

(I) the date the operation began and the date of the certification referred to in the last sentence of paragraph (1),

(II) the total expenditures under the operation and the amount and use of the proceeds from the operation,

(III) a detailed description of the operation including the potential violation being investigated and whether the operation is being conducted under grand jury auspices, and

(IV) the results of the operation including the results of criminal proceedings.

(5) DEFINITIONS.—For purposes of paragraph (4)—

(A) * * *

* * * * * * *

[(C) UNDERCOVER INVESTIGATIVE OPERATION.—The terms "undercover investigative operation" and "undercover operation" mean any undercover investigative operation of the Service—

[(i) in which—

[(I) the gross receipts (excluding interest earned) exceed $50,000; or

[(II) expenditures, both recoverable and nonrecoverable (other than expenditures for salaries of employees), exceed $150,000; and

[(ii) which is exempt from section 3302 or 9102 of title 31, United States Code.

Clauses (i) and (ii) shall not apply with respect to the report required under subparagraph (B) of paragraph (4).]

(C) UNDERCOVER INVESTIGATIVE OPERATION.—The term "undercover investigative operation" means any undercover investigative operation of the Service; except that, for purposes of subparagraphs (A) and (C) of paragraph (4), such term only includes an operation which is exempt from section 3302 or 9102 of title 31, United States Code.

(6) APPLICATION OF SECTION.—The provisions of this subsection—

(A) shall apply after November 17, 1988, and before January 1, 1990, and

(B) shall apply after the date of the enactment of this paragraph and before January 1, 2001.

All amounts expended pursuant to this subsection during the period described in subparagraph (B) shall be recovered to the extent possible, and deposited in the Treasury of the United States as miscellaneous receipts, before January 1, 2001.

SEC. 7609. SPECIAL PROCEDURES FOR THIRD-PARTY SUMMONSES

(a) NOTICE.—

(1) * * *

* * * * * * *

(3) THIRD-PARTY RECORDKEEPER DEFINED.—For purposes of this subsection, the term "third-party recordkeeper" means—

(A) * * *

* * * * * * *

(G) any barter exchange (as defined in section 6045(c)(3)); [and]

(H) any regulated investment company (as defined in section 851) and any agent of such regulated investment company when acting as an agent thereof[.]; *and*

(I) any enrolled agent.

* * * * * * *

Subchapter B—General Powers and Duties

Sec. 7621. Internal revenue districts.

* * * * * * *

[Sec. 7623. Expenses of detection and punishment of frauds.]

Sec. 7623. Expenses of detection of underpayments and fraud, etc.

* * * * * * *

[SEC. 7623. EXPENSES OF DETECTION AND PUNISHMENT OF FRAUDS

[The Secretary, under regulations prescribed by the Secretary, is authorized to pay such sums, not exceeding in the aggregate the sum appropriated therefor, as he may deem necessary for detecting and bringing to trial and punishment persons guilty of violating the internal revenue laws, or conniving at the same, in cases where such expenses are not otherwise provided for by law.]

SEC. 7623. EXPENSES OF DETECTION OF UNDERPAYMENTS AND FRAUD, ETC.

The Secretary, under regulations prescribed by the Secretary, is authorized to pay such sums as he deems necessary for—

(1) detecting underpayments of tax, and

(2) detecting and bringing to trial and punishment persons guilty of violating the internal revenue laws or conniving at the same,

in cases where such expenses are not otherwise provided for by law. Any amount payable under the preceding sentence shall be paid from the proceeds of amounts (other than interest) collected by reason of the information provided, and any amount so collected shall be available for such payments.

* * * * * * *

CHAPTER 80—GENERAL RULES

* * * * * * *

Subchapter A—Application of Internal Revenue Law

Sec. 7801. Authority of the Department of the Treasury.
[Sec. 7802. Commissioner of Internal Revenue; Assistant Commissioner (Employee Plans and Exempt Organizations).]
Sec. 7802. Commissioner of Internal Revenue; Assistant Commissioners; Taxpayer Advocate.

* * * * * * *

[SEC. 7802. COMMISSIONER OF INTERNAL REVENUE; ASSISTANT COMMISSIONER (EMPLOYEE PLANS AND EXEMPT ORGANIZATIONS)]

SEC. 7802. COMMISSIONER OF INTERNAL REVENUE; ASSISTANT COMMISSIONERS; TAXPAYER ADVOCATE.

(a) * * *

* * * * * * *

(d) OFFICE OF TAXPAYER ADVOCATE.—

(1) IN GENERAL.—There is established in the Internal Revenue Service an office to be known as the "Office of the Taxpayer Advocate". Such office shall be under the supervision and direction of an official to be known as the "Taxpayer Advocate" who shall be appointed by and report directly to the Commissioner of Internal Revenue. The Taxpayer Advocate shall be entitled to compensation at the same rate as the highest level official reporting directly to the Deputy Commissioner of the Internal Revenue Service.

(2) FUNCTIONS OF OFFICE.—

(A) IN GENERAL.—It shall be the function of the Office of Taxpayer Advocate to—

(i) assist taxpayers in resolving problems with the Internal Revenue Service,

(ii) identify areas in which taxpayers have problems in dealings with the Internal Revenue Service,

(iii) to the extent possible, propose changes in the administrative practices of the Internal Revenue Service to mitigate problems identified under clause (ii), and

(iv) identify potential legislative changes which may be appropriate to mitigate such problems.

(B) ANNUAL REPORTS.—

(i) OBJECTIVES.—Not later than June 30 of each calendar year after 1995, the Taxpayer Advocate shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the objectives of the Taxpayer Advocate for the fiscal year beginning in such calendar year. Any such report shall contain full and substantive analysis, in addition to statistical information.

(ii) ACTIVITIES.—Not later than December 31 of each calendar year after 1995, the Taxpayer Advocate shall report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate on the activities of the Taxpayer Advocate during the fiscal year ending during such calendar year. Any such report shall contain full and substantive analysis, in addition to statistical information, and shall—

(I) identify the initiatives the Taxpayer Advocate has taken on improving taxpayer services and Internal Revenue Service responsiveness,

(II) contain recommendations received from individuals with the authority to issue Taxpayer Assistance Orders under section 7811,

(III) contain a summary of at least 20 of the most serious problems encountered by taxpayers, including a description of the nature of such problems,

(IV) contain an inventory of the items described in subclauses (I), (II), and (III) for which action has been taken and the result of such action,

(V) contain an inventory of the items described in subclauses (I), (II), and (III) for which action remains to be completed and the period during which each item has remained on such inventory,

(VI) contain an inventory of the items described in subclauses (II) and (III) for which no action has been taken, the period during which each item has remained on such inventory, the reasons for the inaction, and identify any Internal Revenue Service official who is responsible for such inaction,

(VII) identify any Taxpayer Assistance Order which was not honored by the Internal Revenue Service in a timely manner, as specified under section 7811(b),

(VIII) contain recommendations for such administrative and legislative action as may be appropriate to resolve problems encountered by taxpayers,

(IX) describe the extent to which regional problem resolution officers participate in the selection and evaluation of local problem resolution officers, and

(X) include such other information as the Taxpayer Advocate may deem advisable.

(iii) REPORT TO BE SUBMITTED DIRECTLY.—Each report required under this subparagraph shall be provided directly to the Committees referred to in clauses (i) and (ii) without any prior review or comment from the Commissioner, the Secretary of the Treasury, any other officer or employee of the Department of the Treasury, or the Office of Management and Budget.

(3) RESPONSIBILITIES OF COMMISSIONER.—The Commissioner of Internal Revenue shall establish procedures requiring a formal response to all recommendations submitted to the Commissioner by the Taxpayer Advocate within 3 months after submission to the Commissioner.

* * * * * * *

SEC. 7805. RULES AND REGULATIONS

(a) * * *

[(b) RETROACTIVITY OF REGULATIONS OR RULINGS.—The Secretary may prescribe the extent, if any, to which any ruling or regulation, relating to the internal revenue laws, shall be applied without retroactive effect.]

(b) RETROACTIVITY OF REGULATIONS.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, no temporary, proposed, or final regulation relating to the internal revenue laws shall apply to any taxable period ending before the earliest of the following dates:

(A) The date on which such regulation is filed with the Federal Register.

(B) In the case of any final regulation, the date on which any proposed or temporary regulation to which such final regulation relates was filed with the Federal Register.

(C) The date on which any notice substantially describing the expected contents of any temporary, proposed, or final regulation is issued to the public.

(2) EXCEPTION FOR PROMPTLY ISSUED REGULATIONS.—Paragraph (1) shall not apply to regulations filed or issued within 18 months of the date of the enactment of the statutory provision to which the regulation relates.

(3) PREVENTION OF ABUSE.—The Secretary may provide that any regulation may take effect or apply retroactively to prevent abuse.

(4) CORRECTION OF PROCEDURAL DEFECTS.—The Secretary may provide that any regulation may apply retroactively to correct a procedural defect in the issuance of any prior regulation.

(5) INTERNAL REGULATIONS.—The limitation of paragraph (1) shall not apply to any regulation relating to internal Treasury Department policies, practices, or procedures.

(6) CONGRESSIONAL AUTHORIZATION.—The limitation of paragraph (1) may be superseded by a legislative grant from Congress authorizing the Secretary to prescribe the effective date with respect to any regulation.

(7) ELECTION TO APPLY RETROACTIVELY.—The Secretary may provide for any taxpayer to elect to apply any regulation before the dates specified in paragraph (1).

(8) APPLICATION TO RULINGS.—The Secretary may prescribe the extent, if any, to which any ruling (including any judicial decision or any administrative determination other than by regulation) relating to the internal revenue laws shall be applied without retroactive effect.

* * * * * * *

SEC. 7811. TAXPAYER ASSISTANCE ORDERS

(a) AUTHORITY TO ISSUE.—Upon application filed by a taxpayer with [the Office of Ombudsman] *the Office of the Taxpayer Advocate* (in such form, manner, and at such time as the Secretary shall by regulations prescribe), the [Ombudsman] *Taxpayer Advocate* may issue a Taxpayer Assistance Order if, in the determination of the [Ombudsman] *Taxpayer Advocate*, the taxpayer is suffering or about to suffer a significant hardship as a result of the manner in which the internal revenue laws are being administered by the Secretary.

(b) TERMS OF A TAXPAYER ASSISTANCE ORDER.—The terms of a Taxpayer Assistance Order may require the Secretary *within a specified time period*—

(1) to release property of the taxpayer levied upon, or

(2) to cease any action, *take any action as permitted by law,* or refrain from taking any action, with respect to the taxpayer under—

(A) chapter 64 (relating to collection),

(B) subchapter B of chapter 70 (relating to bankruptcy and receiverships),

(C) chapter 78 (relating to discovery of liability and enforcement of title), or

(D) any other provision of law which is specifically described by the [Ombudsman] *Taxpayer Advocate* in such order.

[(c) AUTHORITY TO MODIFY OR RESCIND.—Any Taxpayer Assistance Order issued by the Ombudsman under this section may be modified or rescinded only by the Ombudsman, a district director, a service center director, a compliance center director, a regional director of appeals, or any superior of any such person.]

(c) AUTHORITY TO MODIFY OR RESCIND.—Any Taxpayer Assistance Order issued by the Taxpayer Advocate under this section may be modified or rescinded—

(1) only by the Taxpayer Advocate, the Commissioner of Internal Revenue, or the Deputy Commissioner of Internal Revenue, and

(2) only if a written explanation of the reasons for the modification or rescission is provided to the Taxpayer Advocate.

(d) SUSPENSION OF RUNNING OF PERIOD OF LIMITATION.—The running of any period of limitation with respect to any action described in subsection (b) shall be suspended for—

(1) the period beginning on the date of the taxpayer's application under subsection (a) and ending on the date of the [Om-

budsman's] *Taxpayer Advocate's* decision with respect to such application, and

(2) any period specified by the [Ombudsman] *Taxpayer Advocate* in a Taxpayer Assistance Order issued pursuant to such application.

(e) INDEPENDENT ACTION OF [OMBUDSMAN] *TAXPAYER ADVOCATE*.—Nothing in this section shall prevent the [Ombudsman] *Taxpayer Advocate* from taking any action in the absence of an application under subsection (a).

(f) [OMBUDSMAN] *TAXPAYER ADVOCATE*.—For purposes of this section, the term "[Ombudsman] *Taxpayer Advocate*" includes any designee of the [Ombudsman] *Taxpayer Advocate*.

* * * * * * *

SECTION 7601 OF THE ANTI-DRUG ABUSE ACT OF 1988

SEC. 7601. DISCLOSURE OF INFORMATION ON CASH TRANSACTIONS; UNDERCOVER ACTIVITIES OF INTERNAL REVENUE SERVICE.

(a) * * *

* * * * * * *

(c) ENHANCEMENT OF UNDERCOVER CAPABILITIES OF THE INTERNAL REVENUE SERVICE.—

(1) * * *

* * * * * * *

(3) EFFECTIVE DATE.—The amendments made by this subsection shall take effect on the date of the enactment of this Act [and shall cease to apply after December 31, 1989; and all amounts expended pursuant to such amendments shall be recovered to the extent possible, and deposited in the Treasury of the United States as miscellaneous receipts, before January 1, 1990.].

* * * * * * *

○

Public Law 104–188
104th Congress, H.R. 3448
August 20, 1996

An Act to provide tax relief for small businesses, to protect jobs, to create opportunities, to increase the take home pay of workers, to amend the Portal-to-Portal Act of 1947 relating to the payment of wages to employees who use employer owned vehicles, and to amend the Fair Labor Standards Act of 1938 to increase the minimum wage rate and to prevent job loss by providing flexibility to employers in complying with minimum wage and overtime requirements under that Act.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Small Business Job Protection Act of 1996.
26 USC 1 note.

SECTION 1. SHORT TITLE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Small Business Job Protection Act of 1996".

(b) TABLE OF CONTENTS.—

29-139 O - 96 (188)

TITLE I—SMALL BUSINESS AND OTHER TAX PROVISIONS

SEC. 1101. AMENDMENT OF 1986 CODE.

Except as otherwise expressly provided, whenever in this title an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

26 USC 6654 note.

SEC. 1102. UNDERPAYMENTS OF ESTIMATED TAX.

No addition to the tax shall be made under section 6654 or 6655 of the Internal Revenue Code of 1986 (relating to failure to pay estimated tax) with respect to any underpayment of an installment required to be paid before the date of the enactment of this Act to the extent such underpayment was created or increased by any provision of this title.

Subtitle A—Expensing; Etc.

SEC. 1111. INCREASE IN EXPENSE TREATMENT FOR SMALL BUSINESSES.

26 USC 179.

(a) GENERAL RULE.—Paragraph (1) of section 179(b) (relating to dollar limitation) is amended to read as follows:

"(1) DOLLAR LIMITATION.—The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed the following applicable amount:

"If the taxable year begins in:	The applicable amount is:
1997	18,000
1998	18,500
1999	19,000
2000	20,000
2001 or 2002	24,000
2003 or thereafter	25,000.".

26 USC 179 note.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1996.

SEC. 1112. TREATMENT OF EMPLOYEE TIPS.

(a) EMPLOYEE CASH TIPS.—

(1) REPORTING REQUIREMENT NOT CONSIDERED.—Subparagraph (A) of section 45B(b)(1) (relating to excess employer social security tax) is amended by inserting "(without regard to whether such tips are reported under section 6053)" after "section 3121(q)".

(2) TAXES PAID.—Subsection (d) of section 13443 of the Revenue Reconciliation Act of 1993 is amended by inserting ", with respect to services performed before, on, or after such date" after "1993". 26 USC 38 note.

(3) EFFECTIVE DATE.—The amendments made by this subsection shall take effect as if included in the amendments made by, and the provisions of, section 13443 of the Revenue Reconciliation Act of 1993. 26 USC 45B note.

(b) TIPS FOR EMPLOYEES DELIVERING FOOD OR BEVERAGES.—

(1) IN GENERAL.—Paragraph (2) of section 45B(b) is amended to read as follows:

"(2) ONLY TIPS RECEIVED FOR FOOD OR BEVERAGES TAKEN INTO ACCOUNT.—In applying paragraph (1), there shall be taken into account only tips received from customers in connection with the providing, delivering, or serving of food or beverages for consumption if the tipping of employees delivering or serving food or beverages by customers is customary.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to tips received for services performed after December 31, 1996. 26 USC 45B note.

SEC. 1113. TREATMENT OF STORAGE OF PRODUCT SAMPLES.

(a) IN GENERAL.—Paragraph (2) of section 280A(c) is amended by striking "inventory" and inserting "inventory or product samples".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1995. 26 USC 280A note.

SEC. 1114. TREATMENT OF CERTAIN CHARITABLE RISK POOLS.

(a) GENERAL RULE.—Section 501 (relating to exemption from tax on corporations, certain trusts, etc.) is amended by redesignating subsection (n) as subsection (o) and by inserting after subsection (m) the following new subsection:

"(n) CHARITABLE RISK POOLS.—

"(1) IN GENERAL.—For purposes of this title—

"(A) a qualified charitable risk pool shall be treated as an organization organized and operated exclusively for charitable purposes, and

"(B) subsection (m) shall not apply to a qualified charitable risk pool.

"(2) QUALIFIED CHARITABLE RISK POOL.—For purposes of this subsection, the term 'qualified charitable risk pool' means any organization—

"(A) which is organized and operated solely to pool insurable risks of its members (other than risks related to medical malpractice) and to provide information to its members with respect to loss control and risk management,

"(B) which is comprised solely of members that are organizations described in subsection (c)(3) and exempt from tax under subsection (a), and

"(C) which meets the organizational requirements of paragraph (3).

"(3) ORGANIZATIONAL REQUIREMENTS.—An organization (hereinafter in this subsection referred to as the 'risk pool') meets the organizational requirements of this paragraph if—

"(A) such risk pool is organized as a nonprofit organization under State law provisions authorizing risk pooling arrangements for charitable organizations,

"(B) such risk pool is exempt from any income tax imposed by the State (or will be so exempt after such pool qualifies as an organization exempt from tax under this title),

"(C) such risk pool has obtained at least $1,000,000 in startup capital from nonmember charitable organizations,

"(D) such risk pool is controlled by a board of directors elected by its members, and

"(E) the organizational documents of such risk pool require that—

"(i) each member of such pool shall at all times be an organization described in subsection (c)(3) and exempt from tax under subsection (a),

"(ii) any member which receives a final determination that it no longer qualifies as an organization described in subsection (c)(3) shall immediately notify the pool of such determination and the effective date of such determination, and

"(iii) each policy of insurance issued by the risk pool shall provide that such policy will not cover the insured with respect to events occurring after the date such final determination was issued to the insured.

An organization shall not cease to qualify as a qualified charitable risk pool solely by reason of the failure of any of its members to continue to be an organization described in subsection (c)(3) if, within a reasonable period of time after such pool is notified as required under subparagraph (C)(ii), such pool takes such action as may be reasonably necessary to remove such member from such pool.

"(4) OTHER DEFINITIONS.—For purposes of this subsection—

"(A) STARTUP CAPITAL.—The term 'startup capital' means any capital contributed to, and any program-related investments (within the meaning of section 4944(c)) made in, the risk pool before such pool commences operations.

"(B) NONMEMBER CHARITABLE ORGANIZATION.—The term 'nonmember charitable organization' means any organization which is described in subsection (c)(3) and exempt from tax under subsection (a) and which is not a member of the risk pool and does not benefit (directly or indirectly) from the insurance coverage provided by the pool to its members.".

26 USC 501 note.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after the date of the enactment of this Act.

SEC. 1115. TREATMENT OF DUES PAID TO AGRICULTURAL OR HORTICULTURAL ORGANIZATIONS.

(a) GENERAL RULE.—Section 512 (defining unrelated business taxable income) is amended by adding at the end the following new subsection:

"(d) TREATMENT OF DUES OF AGRICULTURAL OR HORTICULTURAL ORGANIZATIONS.—

"(1) IN GENERAL.—If—

"(A) an agricultural or horticultural organization described in section 501(c)(5) requires annual dues to be paid in order to be a member of such organization, and

"(B) the amount of such required annual dues does not exceed $100,

in no event shall any portion of such dues be treated as derived by such organization from an unrelated trade or business by reason of any benefits or privileges to which members of such organization are entitled.

"(2) INDEXATION OF $100 AMOUNT.—In the case of any taxable year beginning in a calendar year after 1995, the $100 amount in paragraph (1) shall be increased by an amount equal to—

"(A) $100, multiplied by

"(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting 'calendar year 1994' for 'calendar year 1992' in subparagraph (B) thereof.

"(3) DUES.—For purposes of this subsection, the term 'dues' means any payment (whether or not designated as dues) which is required to be made in order to be recognized by the organization as a member of the organization.".

(b) EFFECTIVE DATES.— 26 USC 512 note.

(1) IN GENERAL.—The amendment made by this section shall apply to taxable years beginning after December 31, 1986.

(2) TRANSITIONAL RULE.—If—

(A) for purposes of applying part III of subchapter F of chapter 1 of the Internal Revenue Code of 1986 to any taxable year beginning before January 1, 1987, an agricultural or horticultural organization did not treat any portion of membership dues received by it as income derived in an unrelated trade or business, and

(B) such organization had a reasonable basis for not treating such dues as income derived in an unrelated trade or business,

then, for purposes of applying such part III to any such taxable year, in no event shall any portion of such dues be treated as derived in an unrelated trade or business.

(3) REASONABLE BASIS.—For purposes of paragraph (2), an organization shall be treated as having a reasonable basis for not treating membership dues as income derived in an unrelated trade or business if the taxpayer's treatment of such dues was in reasonable reliance on any of the following:

(A) Judicial precedent, published rulings, technical advice with respect to the organization, or a letter ruling to the organization.

(B) A past Internal Revenue Service audit of the organization in which there was no assessment attributable

to the reclassification of membership dues for purposes of the tax on unrelated business income.

(C) Long-standing recognized practice of agricultural or horticultural organizations.

SEC. 1116. CLARIFICATION OF EMPLOYMENT TAX STATUS OF CERTAIN FISHERMEN.

(a) CLARIFICATION OF EMPLOYMENT TAX STATUS.—

(1) AMENDMENTS OF INTERNAL REVENUE CODE OF 1986.—

(A) DETERMINATION OF SIZE OF CREW.—Subsection (b) of section 3121 (defining employment) is amended by adding at the end the following new sentence:

"For purposes of paragraph (20), the operating crew of a boat shall be treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals.".

(B) CERTAIN CASH REMUNERATION PERMITTED.—Subparagraph (A) of section 3121(b)(20) is amended to read as follows:

"(A) such individual does not receive any cash remuneration other than as provided in subparagraph (B) and other than cash remuneration—

"(i) which does not exceed $100 per trip;

"(ii) which is contingent on a minimum catch; and

"(iii) which is paid solely for additional duties (such as mate, engineer, or cook) for which additional cash remuneration is traditional in the industry,".

(C) CONFORMING AMENDMENT.—Section 6050A(a) is amended by striking "and" at the end of paragraph (3), by striking the period at the end of paragraph (4) and inserting "; and", and by adding at the end the following new paragraph:

"(5) any cash remuneration described in section 3121(b)(20)(A).".

(2) AMENDMENT OF SOCIAL SECURITY ACT.—

(A) DETERMINATION OF SIZE OF CREW.—Subsection (a) of section 210 of the Social Security Act is amended by adding at the end the following new sentence:

42 USC 410.

"For purposes of paragraph (20), the operating crew of a boat shall be treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals.".

(B) CERTAIN CASH REMUNERATION PERMITTED.—Subparagraph (A) of section 210(a)(20) of such Act is amended to read as follows:

"(A) such individual does not receive any additional compensation other than as provided in subparagraph (B) and other than cash remuneration—

"(i) which does not exceed $100 per trip;

"(ii) which is contingent on a minimum catch; and

"(iii) which is paid solely for additional duties (such as mate, engineer, or cook) for which additional cash remuneration is traditional in the industry,".

(3) EFFECTIVE DATES.—

26 USC 3121 note.

(A) IN GENERAL.—The amendments made by this subsection shall apply to remuneration paid—

(i) after December 31, 1994, and

(ii) after December 31, 1984, and before January 1, 1995, unless the payor treated such remuneration (when paid) as being subject to tax under chapter 21 of the Internal Revenue Code of 1986.

(B) REPORTING REQUIREMENT.—The amendment made by paragraph (1)(C) shall apply to remuneration paid after December 31, 1996.

(b) INFORMATION REPORTING.—

(1) IN GENERAL.—Subpart B of part III of subchapter A of chapter 68 (relating to information concerning transactions with other persons) is amended by inserting after section 6050Q the following new section:

"SEC. 6050R. RETURNS RELATING TO CERTAIN PURCHASES OF FISH.

"(a) REQUIREMENT OF REPORTING.—Every person—

"(1) who is engaged in the trade or business of purchasing fish for resale from any person engaged in the trade or business of catching fish; and

"(2) who makes payments in cash in the course of such trade or business to such a person of $600 or more during any calendar year for the purchase of fish,

shall make a return (at such times as the Secretary may prescribe) described in subsection (b) with respect to each person to whom such a payment was made during such calendar year.

"(b) RETURN.—A return is described in this subsection if such return—

"(1) is in such form as the Secretary may prescribe, and

"(2) contains—

"(A) the name, address, and TIN of each person to whom a payment described in subsection (a)(2) was made during the calendar year;

"(B) the aggregate amount of such payments made to such person during such calendar year and the date and amount of each such payment, and

"(C) such other information as the Secretary may require.

"(c) STATEMENT TO BE FURNISHED WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

"(1) the name and address of the person required to make such a return, and

"(2) the aggregate amount of payments to the person required to be shown on the return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) is required to be made.

"(d) DEFINITIONS.—For purposes of this section:

"(1) CASH.—The term 'cash' has the meaning given such term by section 6050I(d).

"(2) FISH.—The term 'fish' includes other forms of aquatic life.".

(2) TECHNICAL AMENDMENTS.—

(A) Subparagraph (A) of section 6724(d)(1) is amended by striking "or" at the end of clause (vi), by striking "and" at the end of clause (vii) and inserting "or", and by adding at the end the following new clause:

"(viii) section 6050R (relating to returns relating to certain purchases of fish), and".

(B) Paragraph (2) of section 6724(d) is amended by redesignating subparagraphs (R) through (U) as subparagraphs (S) through (V), respectively, and by inserting after subparagraph (Q) the following new subparagraph:

"(R) section 6050R(c) (relating to returns relating to certain purchases of fish),".

(C) The table of sections for subpart B of part III of subchapter A of chapter 68 is amended by inserting after the item relating to 6050Q the following new item:

"Sec. 6050R. Returns relating to certain purchases of fish.".

26 USC 6050R note.

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to payments made after December 31, 1997.

SEC. 1117. MODIFICATIONS OF TAX-EXEMPT BOND RULES FOR FIRST-TIME FARMERS.

(a) ACQUISITION FROM RELATED PERSON ALLOWED.—Section 147(c)(2) (relating to exception for first-time farmers) is amended by adding at the end the following new subparagraph:

"(G) ACQUISITION FROM RELATED PERSON.—For purposes of this paragraph and section 144(a), the acquisition by a first-time farmer of land or personal property from a related person (within the meaning of section 144(a)(3)) shall not be treated as an acquisition from a related person, if—

"(i) the acquisition price is for the fair market value of such land or property, and

"(ii) subsequent to such acquisition, the related person does not have a financial interest in the farming operation with respect to which the bond proceeds are to be used.".

(b) SUBSTANTIAL FARMLAND AMOUNT DOUBLED.—Clause (i) of section 147(c)(2)(E) (defining substantial farmland) is amended by striking "15 percent" and inserting "30 percent".

26 USC 147 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to bonds issued after the date of the enactment of this Act.

SEC. 1118. NEWSPAPER DISTRIBUTORS TREATED AS DIRECT SELLERS.

(a) IN GENERAL.—Section 3508(b)(2)(A) is amended by striking "or" at the end of clause (i), by inserting "or" at the end of clause (ii), and by inserting after clause (ii) the following new clause:

"(iii) is engaged in the trade or business of the delivering or distribution of newspapers or shopping news (including any services directly related to such trade or business),".

26 USC 3508 note.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to services performed after December 31, 1995.

SEC. 1119. APPLICATION OF INVOLUNTARY CONVERSION RULES TO PRESIDENTIALLY DECLARED DISASTERS.

(a) IN GENERAL.—Section 1033(h) is amended by redesignating paragraphs (2) and (3) as paragraphs (3) and (4), respectively, and by inserting after paragraph (1) the following new paragraph:

"(2) TRADE OR BUSINESS AND INVESTMENT PROPERTY.—If a taxpayer's property held for productive use in a trade or business or for investment is compulsorily or involuntarily converted as a result of a Presidentially declared disaster, tangible property of a type held for productive use in a trade or business shall be treated for purposes of subsection (a) as property similar or related in service or use to the property so converted.".

(b) CONFORMING AMENDMENTS.—Section 1033(h) is amended—

(1) by striking "residence" in paragraph (3) (as redesignated by subsection (a)) and inserting "property",

(2) by striking "PRINCIPAL RESIDENCES" in the heading and inserting "PROPERTY", and

(3) by striking "(1) IN GENERAL.—" and inserting "(1) PRINCIPAL RESIDENCES.—".

(c) EXPANSION OF OKLAHOMA CITY ENTERPRISE COMMUNITY.—Notwithstanding sections 1391 and 1392(a)(3)(D) of the Internal Revenue Code of 1986, the boundaries of the enterprise community for Oklahoma City, Oklahoma, designated by the Secretary of Housing and Urban Development on December 21, 1994, may be extended with respect to census tracts located in the area damaged due to the bombing of the Alfred P. Murrah Federal Building in Oklahoma City on April 19, 1995, primarily in the area bounded on the south by Robert S. Kerr Avenue, on the north by North 13th Street, on the east by Oklahoma Avenue, and on the west by Shartel Avenue.

(d) EFFECTIVE DATE.— 26 USC 1033 note.

(1) IN GENERAL.—The amendments made by this section shall apply to disasters declared after December 31, 1994, in taxable years ending after such date.

(2) SUBSECTION (c).—Subsection (c) shall take effect on the date of the enactment of this Act.

SEC. 1120. CLASS LIFE FOR GAS STATION CONVENIENCE STORES AND SIMILAR STRUCTURES.

(a) IN GENERAL.—Section 168(e)(3)(E) (classifying certain property as 15-year property) is amended by striking "and" at the end of clause (i), by striking the period at the end of clause (ii) and inserting ", and", and by adding at the end the following new clause:

"(iii) any section 1250 property which is a retail motor fuels outlet (whether or not food or other convenience items are sold at the outlet).".

(b) CONFORMING AMENDMENT.—Subparagraph (B) of section 168(g)(3) is amended by inserting after the item relating to subparagraph (E)(ii) in the table contained therein the following new item:

"(E)(iii) ..... 20".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to property which is placed in service on or after the date of the enactment of this Act and to which section 168 of the Internal Revenue Code of 1986 applies after the amendment made by section 201 of the Tax Reform Act of 1986. A taxpayer 26 USC 168 note.

may elect (in such form and manner as the Secretary of the Treasury may prescribe) to have such amendments apply with respect to any property placed in service before such date and to which such section so applies.

SEC. 1121. TREATMENT OF ABANDONMENT OF LESSOR IMPROVEMENTS AT TERMINATION OF LEASE.

(a) IN GENERAL.—Paragraph (8) of section 168(i) is amended to read as follows:

"(8) TREATMENT OF LEASEHOLD IMPROVEMENTS.—

"(A) IN GENERAL.—In the case of any building erected (or improvements made) on leased property, if such building or improvement is property to which this section applies, the depreciation deduction shall be determined under the provisions of this section.

"(B) TREATMENT OF LESSOR IMPROVEMENTS WHICH ARE ABANDONED AT TERMINATION OF LEASE.—An improvement—

"(i) which is made by the lessor of leased property for the lessee of such property, and

"(ii) which is irrevocably disposed of or abandoned by the lessor at the termination of the lease by such lessee,

shall be treated for purposes of determining gain or loss under this title as disposed of by the lessor when so disposed of or abandoned.".

26 USC 168 note.

(b) EFFECTIVE DATE.—Subparagraph (B) of section 168(i)(8) of the Internal Revenue Code of 1986, as added by the amendment made by subsection (a), shall apply to improvements disposed of or abandoned after June 12, 1996.

SEC. 1122. SPECIAL RULES RELATING TO DETERMINATION WHETHER INDIVIDUALS ARE EMPLOYEES FOR PURPOSES OF EMPLOYMENT TAXES.

26 USC 3401 note.

(a) IN GENERAL.—Section 530 of the Revenue Act of 1978 is amended by adding at the end the following new subsection:

"(e) SPECIAL RULES FOR APPLICATION OF SECTION.—

"(1) NOTICE OF AVAILABILITY OF SECTION.—An officer or employee of the Internal Revenue Service shall, before or at the commencement of any audit inquiry relating to the employment status of one or more individuals who perform services for the taxpayer, provide the taxpayer with a written notice of the provisions of this section.

"(2) RULES RELATING TO STATUTORY STANDARDS.—For purposes of subsection (a)(2)—

"(A) a taxpayer may not rely on an audit commenced after December 31, 1996, for purposes of subparagraph (B) thereof unless such audit included an examination for employment tax purposes of whether the individual involved (or any individual holding a position substantially similar to the position held by the individual involved) should be treated as an employee of the taxpayer,

"(B) in no event shall the significant segment requirement of subparagraph (C) thereof be construed to require a reasonable showing of the practice of more than 25 percent of the industry (determined by not taking into account the taxpayer), and

"(C) in applying the long-standing recognized practice requirement of subparagraph (C) thereof—

"(i) such requirement shall not be construed as requiring the practice to have continued for more than 10 years, and

"(ii) a practice shall not fail to be treated as long-standing merely because such practice began after 1978.

"(3) AVAILABILITY OF SAFE HARBORS.—Nothing in this section shall be construed to provide that subsection (a) only applies where the individual involved is otherwise an employee of the taxpayer.

"(4) BURDEN OF PROOF.—

"(A) IN GENERAL.—If—

"(i) a taxpayer establishes a prima facie case that it was reasonable not to treat an individual as an employee for purposes of this section, and

"(ii) the taxpayer has fully cooperated with reasonable requests from the Secretary of the Treasury or his delegate,

then the burden of proof with respect to such treatment shall be on the Secretary.

"(B) EXCEPTION FOR OTHER REASONABLE BASIS.—In the case of any issue involving whether the taxpayer had a reasonable basis not to treat an individual as an employee for purposes of this section, subparagraph (A) shall only apply for purposes of determining whether the taxpayer meets the requirements of subparagraph (A), (B), or (C) of subsection (a)(2).

"(5) PRESERVATION OF PRIOR PERIOD SAFE HARBOR.—If—

"(A) an individual would (but for the treatment referred to in subparagraph (B)) be deemed not to be an employee of the taxpayer under subsection (a) for any prior period, and

"(B) such individual is treated by the taxpayer as an employee for employment tax purposes for any subsequent period,

then, for purposes of applying such taxes for such prior period with respect to the taxpayer, the individual shall be deemed not to be an employee.

"(6) SUBSTANTIALLY SIMILAR POSITION.—For purposes of this section, the determination as to whether an individual holds a position substantially similar to a position held by another individual shall include consideration of the relationship between the taxpayer and such individuals.".

(b) EFFECTIVE DATES.— 26 USC 3401 note.

(1) IN GENERAL.—The amendment made by this section shall apply to periods after December 31, 1996.

(2) NOTICE BY INTERNAL REVENUE SERVICE.—Section 530(e)(1) of the Revenue Act of 1978 (as added by subsection (a)) shall apply to audits which commence after December 31, 1996.

(3) BURDEN OF PROOF.—

(A) IN GENERAL.—Section 530(e)(4) of the Revenue Act of 1978 (as added by subsection (a)) shall apply to disputes involving periods after December 31, 1996.

(B) NO INFERENCE.—Nothing in the amendments made by this section shall be construed to infer the proper treat-

ment of the burden of proof with respect to disputes involving periods before January 1, 1997.

SEC. 1123. TREATMENT OF HOUSING PROVIDED TO EMPLOYEES BY ACADEMIC HEALTH CENTERS.

(a) IN GENERAL.—Paragraph (4) of section 119(d) (relating to lodging furnished by certain educational institutions to employees) is amended to read as follows:

"(4) EDUCATIONAL INSTITUTION, ETC.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'educational institution' means—

"(i) an institution described in section 170(b)(1)(A)(ii) (or an entity organized under State law and composed of public institutions so described), or

"(ii) an academic health center.

"(B) ACADEMIC HEALTH CENTER.—For purposes of subparagraph (A), the term 'academic health center' means an entity—

"(i) which is described in section 170(b)(1)(A)(iii),

"(ii) which receives (during the calendar year in which the taxable year of the taxpayer begins) payments under subsection (d)(5)(B) or (h) of section 1886 of the Social Security Act (relating to graduate medical education), and

"(iii) which has as one of its principal purposes or functions the providing and teaching of basic and clinical medical science and research with the entity's own faculty.".

26 USC 119 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 1995.

Subtitle B—Extension of Certain Expiring Provisions

SEC. 1201. WORK OPPORTUNITY TAX CREDIT.

(a) AMOUNT OF CREDIT.—Subsection (a) of section 51 (relating to amount of credit) is amended by striking "40 percent" and inserting "35 percent".

(b) MEMBERS OF TARGETED GROUPS.—Subsection (d) of section 51 is amended to read as follows:

"(d) MEMBERS OF TARGETED GROUPS.—For purposes of this subpart—

"(1) IN GENERAL.—An individual is a member of a targeted group if such individual is—

"(A) a qualified IV–A recipient,

"(B) a qualified veteran,

"(C) a qualified ex-felon,

"(D) a high-risk youth,

"(E) a vocational rehabilitation referral,

"(F) a qualified summer youth employee, or

"(G) a qualified food stamp recipient.

"(2) QUALIFIED IV–A RECIPIENT.—

"(A) IN GENERAL.—The term 'qualified IV–A recipient' means any individual who is certified by the designated local agency as being a member of a family receiving assist-

ance under a IV–A program for at least a 9-month period ending during the 9-month period ending on the hiring date.

"(B) IV–A PROGRAM.—For purposes of this paragraph, the term 'IV–A program' means any program providing assistance under a State plan approved under part A of title IV of the Social Security Act (relating to assistance for needy families with minor children) and any successor of such program.

"(3) QUALIFIED VETERAN.—

"(A) IN GENERAL.—The term 'qualified veteran' means any veteran who is certified by the designated local agency as being—

"(i) a member of a family receiving assistance under a IV–A program (as defined in paragraph (2)(B)) for at least a 9-month period ending during the 12-month period ending on the hiring date, or

"(ii) a member of a family receiving assistance under a food stamp program under the Food Stamp Act of 1977 for at least a 3-month period ending during the 12-month period ending on the hiring date.

"(B) VETERAN.—For purposes of subparagraph (A), the term 'veteran' means any individual who is certified by the designated local agency as—

"(i)(I) having served on active duty (other than active duty for training) in the Armed Forces of the United States for a period of more than 180 days, or

"(II) having been discharged or released from active duty in the Armed Forces of the United States for a service-connected disability, and

"(ii) not having any day during the 60-day period ending on the hiring date which was a day of extended active duty in the Armed Forces of the United States.

For purposes of clause (ii), the term 'extended active duty' means a period of more than 90 days during which the individual was on active duty (other than active duty for training).

"(4) QUALIFIED EX-FELON.—The term 'qualified ex-felon' means any individual who is certified by the designated local agency—

"(A) as having been convicted of a felony under any statute of the United States or any State,

"(B) as having a hiring date which is not more than 1 year after the last date on which such individual was so convicted or was released from prison, and

"(C) as being a member of a family which had an income during the 6 months immediately preceding the earlier of the month in which such income determination occurs or the month in which the hiring date occurs, which, on an annual basis, would be 70 percent or less of the Bureau of Labor Statistics lower living standard.

Any determination under subparagraph (C) shall be valid for the 45-day period beginning on the date such determination is made.

"(5) HIGH-RISK YOUTH.—

"(A) IN GENERAL.—The term 'high-risk youth' means any individual who is certified by the designated local agency—

"(i) as having attained age 18 but not age 25 on the hiring date, and

"(ii) as having his principal place of abode within an empowerment zone or enterprise community.

"(B) YOUTH MUST CONTINUE TO RESIDE IN ZONE.—In the case of a high-risk youth, the term 'qualified wages' shall not include wages paid or incurred for services performed while such youth's principal place of abode is outside an empowerment zone or enterprise community.

"(6) VOCATIONAL REHABILITATION REFERRAL.—The term 'vocational rehabilitation referral' means any individual who is certified by the designated local agency as—

"(A) having a physical or mental disability which, for such individual, constitutes or results in a substantial handicap to employment, and

"(B) having been referred to the employer upon completion of (or while receiving) rehabilitative services pursuant to—

"(i) an individualized written rehabilitation plan under a State plan for vocational rehabilitation services approved under the Rehabilitation Act of 1973, or

"(ii) a program of vocational rehabilitation carried out under chapter 31 of title 38, United States Code.

"(7) QUALIFIED SUMMER YOUTH EMPLOYEE.—

"(A) IN GENERAL.—The term 'qualified summer youth employee' means any individual—

"(i) who performs services for the employer between May 1 and September 15,

"(ii) who is certified by the designated local agency as having attained age 16 but not 18 on the hiring date (or if later, on May 1 of the calendar year involved),

"(iii) who has not been an employee of the employer during any period prior to the 90-day period described in subparagraph (B)(i), and

"(iv) who is certified by the designated local agency as having his principal place of abode within an empowerment zone or enterprise community.

"(B) SPECIAL RULES FOR DETERMINING AMOUNT OF CREDIT.—For purposes of applying this subpart to wages paid or incurred to any qualified summer youth employee—

"(i) subsection (b)(2) shall be applied by substituting 'any 90-day period between May 1 and September 15' for 'the 1-year period beginning with the day the individual begins work for the employer', and

"(ii) subsection (b)(3) shall be applied by substituting '$3,000' for '$6,000'.

The preceding sentence shall not apply to an individual who, with respect to the same employer, is certified as a member of another targeted group after such individual has been a qualified summer youth employee.

"(C) YOUTH MUST CONTINUE TO RESIDE IN ZONE.—Paragraph (5)(B) shall apply for purposes of subparagraph (A)(iv).

"(8) QUALIFIED FOOD STAMP RECIPIENT.—

"(A) IN GENERAL.—The term 'qualified food stamp recipient' means any individual who is certified by the designated local agency—

"(i) as having attained age 18 but not age 25 on the hiring date, and

"(ii) as being a member of a family—

"(I) receiving assistance under a food stamp program under the Food Stamp Act of 1977 for the 6-month period ending on the hiring date, or

"(II) receiving such assistance for at least 3 months of the 5-month period ending on the hiring date, in the case of a member of a family who ceases to be eligible for such assistance under section 6(o) of the Food Stamp Act of 1977.

"(B) PARTICIPATION INFORMATION.—Notwithstanding any other provision of law, the Secretary of the Treasury and the Secretary of Agriculture shall enter into an agreement to provide information to designated local agencies with respect to participation in the food stamp program. Contracts.

"(9) HIRING DATE.—The term 'hiring date' means the day the individual is hired by the employer.

"(10) DESIGNATED LOCAL AGENCY.—The term 'designated local agency' means a State employment security agency established in accordance with the Act of June 6, 1933, as amended (29 U.S.C. 49–49n).

"(11) SPECIAL RULES FOR CERTIFICATIONS.—

"(A) IN GENERAL.—An individual shall not be treated as a member of a targeted group unless—

"(i) on or before the day on which such individual begins work for the employer, the employer has received a certification from a designated local agency that such individual is a member of a targeted group, or

"(ii)(I) on or before the day the individual is offered employment with the employer, a pre-screening notice is completed by the employer with respect to such individual, and

"(II) not later than the 21st day after the individual begins work for the employer, the employer submits such notice, signed by the employer and the individual under penalties of perjury, to the designated local agency as part of a written request for such a certification from such agency.

For purposes of this paragraph, the term 'pre-screening notice' means a document (in such form as the Secretary shall prescribe) which contains information provided by the individual on the basis of which the employer believes that the individual is a member of a targeted group.

"(B) INCORRECT CERTIFICATIONS.—If—

"(i) an individual has been certified by a designated local agency as a member of a targeted group, and

"(ii) such certification is incorrect because it was based on false information provided by such individual,

the certification shall be revoked and wages paid by the employer after the date on which notice of revocation is

received by the employer shall not be treated as qualified wages.

"(C) EXPLANATION OF DENIAL OF REQUEST.—If a designated local agency denies a request for certification of membership in a targeted group, such agency shall provide to the person making such request a written explanation of the reasons for such denial.".

(c) MINIMUM EMPLOYMENT PERIOD.—Paragraph (3) of section 51(i) (relating to certain individuals ineligible) is amended to read as follows:

"(3) INDIVIDUALS NOT MEETING MINIMUM EMPLOYMENT PERIOD.—No wages shall be taken into account under subsection (a) with respect to any individual unless such individual either—

"(A) is employed by the employer at least 180 days (20 days in the case of a qualified summer youth employee), or

"(B) has completed at least 400 hours (120 hours in the case of a qualified summer youth employee) of services performed for the employer.".

(d) TERMINATION.—Paragraph (4) of section 51(c) (relating to wages defined) is amended to read as follows:

"(4) TERMINATION.—The term 'wages' shall not include any amount paid or incurred to an individual who begins work for the employer—

"(A) after December 31, 1994, and before October 1, 1996, or

"(B) after September 30, 1997.".

(e) REDESIGNATION OF CREDIT.—

(1) Sections 38(b)(2), 41(b)(2)(D)(iii), 45A(b)(1)(B), 51 (a) and (g), and 196(c) are each amended in the text by striking "targeted jobs credit" each place it appears and inserting "work opportunity credit".

(2) The subpart heading for subpart F of part IV of subchapter A of chapter 1 is amended by striking "**Targeted Jobs Credit**" and inserting "**Work Opportunity Credit**".

(3) The table of subparts for such part IV is amended by striking "targeted jobs credit" and inserting "work opportunity credit".

(4) The headings for sections 41(b)(2)(D)(iii) and 1396(c)(3) are each amended by striking "TARGETED JOBS CREDIT" and inserting "WORK OPPORTUNITY CREDIT".

(5) The heading for subsection (j) of section 51 is amended by striking "TARGETED JOBS CREDIT" and inserting "WORK OPPORTUNITY CREDIT".

(f) TECHNICAL AMENDMENT.—Paragraph (1) of section 51(c) is amended by striking ", subsection (d)(8)(D),".

26 USC 38 note.

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to individuals who begin work for the employer after September 30, 1996.

SEC. 1202. EMPLOYER-PROVIDED EDUCATIONAL ASSISTANCE PROGRAMS.

(a) EXTENSION.—Subsection (d) of section 127 (relating to educational assistance programs) is amended by striking "December 31, 1994." and inserting "May 31, 1997. In the case of any taxable year beginning in 1997, only expenses paid with respect to courses

beginning before July 1, 1997, shall be taken into account in determining the amount excluded under this section.".

(b) LIMITATION TO EDUCATION BELOW GRADUATE LEVEL.—The last sentence of section 127(c)(1) is amended by inserting before the period the following: ", and such term also does not include any payment for, or the provision of any benefits with respect to, any graduate level course of a kind normally taken by an individual pursuing a program leading to a law, business, medical, or other advanced academic or professional degree".

(c) EFFECTIVE DATES.— 26 USC 127 note.

(1) EXTENSION.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1994.

(2) GRADUATE EDUCATION.—The amendment made by subsection (b) shall apply with respect to expenses relating to courses beginning after June 30, 1996.

(3) EXPEDITED PROCEDURES.—The Secretary of the Treasury shall establish expedited procedures for the refund of any overpayment of taxes imposed by the Internal Revenue Code of 1986 which is attributable to amounts excluded from gross income during 1995 or 1996 under section 127 of such Code, including procedures waiving the requirement that an employer obtain an employee's signature where the employer demonstrates to the satisfaction of the Secretary that any refund collected by the employer on behalf of the employee will be paid to the employee.

SEC. 1203. FUTA EXEMPTION FOR ALIEN AGRICULTURAL WORKERS.

(a) IN GENERAL.—Subparagraph (B) of section 3306(c)(1) (defining employment) is amended by striking "before January 1, 1995,".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to services performed after December 31, 1994.

SEC. 1204. RESEARCH CREDIT.

(a) IN GENERAL.—Subsection (h) of section 41 (relating to credit for research activities) is amended to read as follows:

"(h) TERMINATION.—

"(1) IN GENERAL.—This section shall not apply to any amount paid or incurred—

"(A) after June 30, 1995, and before July 1, 1996, or

"(B) after May 31, 1997.

Notwithstanding the preceding sentence, in the case of a taxpayer making an election under subsection (c)(4) for its first taxable year beginning after June 30, 1996, and before July 1, 1997, this section shall apply to amounts paid or incurred during the first 11 months of such taxable year.

"(2) COMPUTATION OF BASE AMOUNT.—In the case of any taxable year with respect to which this section applies to a number of days which is less than the total number of days in such taxable year, the base amount with respect to such taxable year shall be the amount which bears the same ratio to the base amount for such year (determined without regard to this paragraph) as the number of days in such taxable year to which this section applies bears to the total number of days in such taxable year.".

(b) BASE AMOUNT FOR START-UP COMPANIES.—Clause (i) of section 41(c)(3)(B) (relating to start-up companies) is amended to read as follows:

"(i) TAXPAYERS TO WHICH SUBPARAGRAPH APPLIES.—The fixed-base percentage shall be determined under this subparagraph if—

"(I) the first taxable year in which a taxpayer had both gross receipts and qualified research expenses begins after December 31, 1983, or

"(II) there are fewer than 3 taxable years beginning after December 31, 1983, and before January 1, 1989, in which the taxpayer had both gross receipts and qualified research expenses.".

(c) ELECTION OF ALTERNATIVE INCREMENTAL CREDIT.—Subsection (c) of section 41 is amended by redesignating paragraphs (4) and (5) as paragraphs (5) and (6), respectively, and by inserting after paragraph (3) the following new paragraph:

"(4) ELECTION OF ALTERNATIVE INCREMENTAL CREDIT.—

"(A) IN GENERAL.—At the election of the taxpayer, the credit determined under subsection (a)(1) shall be equal to the sum of—

"(i) 1.65 percent of so much of the qualified research expenses for the taxable year as exceeds 1 percent of the average described in subsection (c)(1)(B) but does not exceed 1.5 percent of such average,

"(ii) 2.2 percent of so much of such expenses as exceeds 1.5 percent of such average but does not exceed 2 percent of such average, and

"(iii) 2.75 percent of so much of such expenses as exceeds 2 percent of such average.

"(B) ELECTION.—An election under this paragraph may be made only for the first taxable year of the taxpayer beginning after June 30, 1996. Such an election shall apply to the taxable year for which made and all succeeding taxable years unless revoked with the consent of the Secretary.".

(d) INCREASED CREDIT FOR CONTRACT RESEARCH EXPENSES WITH RESPECT TO CERTAIN RESEARCH CONSORTIA.—Paragraph (3) of section 41(b) is amended by adding at the end the following new subparagraph:

"(C) AMOUNTS PAID TO CERTAIN RESEARCH CONSORTIA.—

"(i) IN GENERAL.—Subparagraph (A) shall be applied by substituting '75 percent' for '65 percent' with respect to amounts paid or incurred by the taxpayer to a qualified research consortium for qualified research on behalf of the taxpayer and 1 or more unrelated taxpayers. For purposes of the preceding sentence, all persons treated as a single employer under subsection (a) or (b) of section 52 shall be treated as related taxpayers.

"(ii) QUALIFIED RESEARCH CONSORTIUM.—The term 'qualified research consortium' means any organization which—

"(I) is described in section 501(c)(3) or 501(c)(6) and is exempt from tax under section 501(a),

"(II) is organized and operated primarily to conduct scientific research, and

"(III) is not a private foundation.".

(e) CONFORMING AMENDMENT.—Subparagraph (D) of section 28(b)(1) is amended by inserting ", and before July 1, 1996, and periods after May 31, 1997" after "June 30, 1995".

(f) EFFECTIVE DATES.— 26 USC 41 note.

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years ending after June 30, 1996.

(2) SUBSECTIONS (c) AND (d).—The amendments made by subsections (c) and (d) shall apply to taxable years beginning after June 30, 1996.

(3) ESTIMATED TAX.—The amendments made by this section shall not be taken into account under section 6654 or 6655 of the Internal Revenue Code of 1986 (relating to failure to pay estimated tax) in determining the amount of any installment required to be paid for a taxable year beginning in 1997.

SEC. 1205. ORPHAN DRUG TAX CREDIT.

(a) RECATEGORIZED AS A BUSINESS CREDIT.—

(1) IN GENERAL.—Section 28 (relating to clinical testing expenses for certain drugs for rare diseases or conditions) is transferred to subpart D of part IV of subchapter A of chapter 1, inserted after section 45B, and redesignated as section 45C.

(2) CONFORMING AMENDMENT.—Subsection (b) of section 38 (relating to general business credit) is amended by striking "plus" at the end of paragraph (10), by striking the period at the end of paragraph (11) and inserting ", plus", and by adding at the end the following new paragraph:

"(12) the orphan drug credit determined under section 45C(a).".

(3) CLERICAL AMENDMENTS.—

(A) The table of sections for subpart B of such part IV is amended by striking the item relating to section 28.

(B) The table of sections for subpart D of such part IV is amended by adding at the end the following new item:

"Sec. 45C. Clinical testing expenses for certain drugs for rare diseases or conditions.".

(b) CREDIT TERMINATION.—Subsection (e) of section 45C, as redesignated by subsection (a)(1), is amended to read as follows:

"(e) TERMINATION.—This section shall not apply to any amount paid or incurred—

"(1) after December 31, 1994, and before July 1, 1996, or

"(2) after May 31, 1997.".

(c) NO PRE-JULY 1, 1996 CARRYBACKS.—Subsection (d) of section 39 (relating to carryback and carryforward of unused credits) is amended by adding at the end the following new paragraph:

"(7) NO CARRYBACK OF SECTION 45C CREDIT BEFORE JULY 1, 1996.—No portion of the unused business credit for any taxable year which is attributable to the orphan drug credit determined under section 45C may be carried back to a taxable year ending before July 1, 1996.".

(d) ADDITIONAL CONFORMING AMENDMENTS.—

(1) Section 45C(a), as redesignated by subsection (a)(1), is amended by striking "There shall be allowed as a credit against the tax imposed by this chapter for the taxable year"

and inserting "For purposes of section 38, the credit determined under this section for the taxable year is".

(2) Section 45C(d), as so redesignated, is amended by striking paragraph (2) and by redesignating paragraphs (3), (4), and (5) as paragraphs (2), (3), and (4).

(3) Section 29(b)(6)(A) is amended by striking "sections 27 and 28" and inserting "section 27".

(4) Section 30(b)(3)(A) is amended by striking "sections 27, 28, and 29" and inserting "sections 27 and 29".

(5) Section 53(d)(1)(B) is amended—

(A) by striking "or not allowed under section 28 solely by reason of the application of section 28(d)(2)(B)," in clause (iii), and

(B) by striking "or not allowed under section 28 solely by reason of the application of section 28(d)(2)(B)" in clause (iv)(II).

(6) Section 55(c)(2) is amended by striking "28(d)(2),".

(7) Section 280C(b) is amended—

(A) by striking "section 28(b)" in paragraph (1) and inserting "section 45C(b)",

(B) by striking "section 28" in paragraphs (1) and (2)(A) and inserting "section 45C", and

(C) by striking "subsection (d)(2) thereof" in paragraphs (1) and (2)(A) and inserting "section 38(c)".

26 USC 29 note. (e) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts paid or incurred in taxable years ending after June 30, 1996.

SEC. 1206. CONTRIBUTIONS OF STOCK TO PRIVATE FOUNDATIONS.

(a) IN GENERAL.—Subparagraph (D) of section 170(e)(5) (relating to special rule for contributions of stock for which market quotations are readily available) is amended to read as follows:

"(D) TERMINATION.—This paragraph shall not apply to contributions made—

"(i) after December 31, 1994, and before July 1, 1996, or

"(ii) after May 31, 1997.".

26 USC 170 note. (b) EFFECTIVE DATE.—The amendment made by this section shall apply to contributions made after June 30, 1996.

SEC. 1207. EXTENSION OF BINDING CONTRACT DATE FOR BIOMASS AND COAL FACILITIES.

(a) IN GENERAL.—Subparagraph (A) of section 29(g)(1) (relating to extension of certain facilities) is amended by striking "January 1, 1997" and inserting "July 1, 1998" and by striking "January 1, 1996" and inserting "January 1, 1997".

26 USC 29 note. (b) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act.

SEC. 1208. MORATORIUM FOR EXCISE TAX ON DIESEL FUEL SOLD FOR USE OR USED IN DIESEL-POWERED MOTORBOATS.

Subparagraph (D) of section 4041(a)(1) (relating to the imposition of tax on diesel fuel and special motor fuels) is amended by redesignating clauses (i) and (ii) as clauses (ii) and (iii), respectively, and by inserting before clause (ii) (as redesignated) the following new clause:

"(i) no tax shall be imposed by subsection (a) or (d)(1) during the period beginning on the date which

is 7 days after the date of the enactment of the Small Business Job Protection Act of 1996 and ending on December 31, 1997,".

Subtitle C—Provisions Relating to S Corporations

SEC. 1301. S CORPORATIONS PERMITTED TO HAVE 75 SHAREHOLDERS.

Subparagraph (A) of section 1361(b)(1) (defining small business corporation) is amended by striking "35 shareholders" and inserting "75 shareholders".

SEC. 1302. ELECTING SMALL BUSINESS TRUSTS.

(a) GENERAL RULE.—Subparagraph (A) of section 1361(c)(2) (relating to certain trusts permitted as shareholders) is amended by inserting after clause (iv) the following new clause:

"(v) An electing small business trust.".

(b) CURRENT BENEFICIARIES TREATED AS SHAREHOLDERS.—Subparagraph (B) of section 1361(c)(2) is amended by adding at the end the following new clause:

"(v) In the case of a trust described in clause (v) of subparagraph (A), each potential current beneficiary of such trust shall be treated as a shareholder; except that, if for any period there is no potential current beneficiary of such trust, such trust shall be treated as the shareholder during such period.".

(c) ELECTING SMALL BUSINESS TRUST DEFINED.—Section 1361 (defining S corporation) is amended by adding at the end the following new subsection:

"(e) ELECTING SMALL BUSINESS TRUST DEFINED.—

"(1) ELECTING SMALL BUSINESS TRUST.—For purposes of this section—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'electing small business trust' means any trust if—

"(i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, or (III) an organization described in paragraph (2), (3), (4), or (5) of section 170(c) which holds a contingent interest and is not a potential current beneficiary,

"(ii) no interest in such trust was acquired by purchase, and

"(iii) an election under this subsection applies to such trust.

"(B) CERTAIN TRUSTS NOT ELIGIBLE.—The term 'electing small business trust' shall not include—

"(i) any qualified subchapter S trust (as defined in subsection (d)(3)) if an election under subsection (d)(2) applies to any corporation the stock of which is held by such trust, and

"(ii) any trust exempt from tax under this subtitle.

"(C) PURCHASE.—For purposes of subparagraph (A), the term 'purchase' means any acquisition if the basis of the property acquired is determined under section 1012.

"(2) POTENTIAL CURRENT BENEFICIARY.—For purposes of this section, the term 'potential current beneficiary' means,

with respect to any period, any person who at any time during such period is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust. If a trust disposes of all of the stock which it holds in an S corporation, then, with respect to such corporation, the term 'potential current beneficiary' does not include any person who first met the requirements of the preceding sentence during the 60-day period ending on the date of such disposition.

"(3) ELECTION.—An election under this subsection shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent taxable years of such trust unless revoked with the consent of the Secretary.

"(4) CROSS REFERENCE.—

"For special treatment of electing small business trusts, see section 641(d).".

(d) TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—Section 641 (relating to imposition of tax on trusts) is amended by adding at the end the following new subsection:

"(d) SPECIAL RULES FOR TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—

"(1) IN GENERAL.—For purposes of this chapter—

"(A) the portion of any electing small business trust which consists of stock in 1 or more S corporations shall be treated as a separate trust, and

"(B) the amount of the tax imposed by this chapter on such separate trust shall be determined with the modifications of paragraph (2).

"(2) MODIFICATIONS.—For purposes of paragraph (1), the modifications of this paragraph are the following:

"(A) Except as provided in section 1(h), the amount of the tax imposed by section 1(e) shall be determined by using the highest rate of tax set forth in section 1(e).

"(B) The exemption amount under section 55(d) shall be zero.

"(C) The only items of income, loss, deduction, or credit to be taken into account are the following:

"(i) The items required to be taken into account under section 1366.

"(ii) Any gain or loss from the disposition of stock in an S corporation.

"(iii) To the extent provided in regulations, State or local income taxes or administrative expenses to the extent allocable to items described in clauses (i) and (ii).

No deduction or credit shall be allowed for any amount not described in this paragraph, and no item described in this paragraph shall be apportioned to any beneficiary.

"(D) No amount shall be allowed under paragraph (1) or (2) of section 1211(b).

"(3) TREATMENT OF REMAINDER OF TRUST AND DISTRIBUTIONS.—For purposes of determining—

"(A) the amount of the tax imposed by this chapter on the portion of any electing small business trust not treated as a separate trust under paragraph (1), and

"(B) the distributable net income of the entire trust,

the items referred to in paragraph (2)(C) shall be excluded. Except as provided in the preceding sentence, this subsection shall not affect the taxation of any distribution from the trust.

"(4) TREATMENT OF UNUSED DEDUCTIONS WHERE TERMINATION OF SEPARATE TRUST.—If a portion of an electing small business trust ceases to be treated as a separate trust under paragraph (1), any carryover or excess deduction of the separate trust which is referred to in section 642(h) shall be taken into account by the entire trust.

"(5) ELECTING SMALL BUSINESS TRUST.—For purposes of this subsection, the term 'electing small business trust' has the meaning given such term by section 1361(e)(1).".

(e) TECHNICAL AMENDMENT.—Paragraph (1) of section 1366(a) is amended by inserting ", or of a trust or estate which terminates," after "who dies".

SEC. 1303. EXPANSION OF POST-DEATH QUALIFICATION FOR CERTAIN TRUSTS.

Subparagraph (A) of section 1361(c)(2) (relating to certain trusts permitted as shareholders) is amended—

(1) by striking "60-day period" each place it appears in clauses (ii) and (iii) and inserting "2-year period", and

(2) by striking the last sentence in clause (ii).

SEC. 1304. FINANCIAL INSTITUTIONS PERMITTED TO HOLD SAFE HARBOR DEBT.

Clause (iii) of section 1361(c)(5)(B) (defining straight debt) is amended by striking "or a trust described in paragraph (2)" and inserting "a trust described in paragraph (2), or a person which is actively and regularly engaged in the business of lending money".

SEC. 1305. RULES RELATING TO INADVERTENT TERMINATIONS AND INVALID ELECTIONS.

(a) GENERAL RULE.—Subsection (f) of section 1362 (relating to inadvertent terminations) is amended to read as follows:

"(f) INADVERTENT INVALID ELECTIONS OR TERMINATIONS.—If—

"(1) an election under subsection (a) by any corporation—

"(A) was not effective for the taxable year for which made (determined without regard to subsection (b)(2)) by reason of a failure to meet the requirements of section 1361(b) or to obtain shareholder consents, or

"(B) was terminated under paragraph (2) or (3) of subsection (d),

"(2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent,

"(3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken—

"(A) so that the corporation is a small business corporation, or

"(B) to acquire the required shareholder consents, and

"(4) the corporation, and each person who was a shareholder in the corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period,

then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.".

(b) LATE ELECTIONS, ETC.—Subsection (b) of section 1362 is amended by adding at the end the following new paragraph:

"(5) AUTHORITY TO TREAT LATE ELECTIONS, ETC., AS TIMELY.—If—

"(A) an election under subsection (a) is made for any taxable year (determined without regard to paragraph (3)) after the date prescribed by this subsection for making such election for such taxable year or no such election is made for any taxable year, and

"(B) the Secretary determines that there was reasonable cause for the failure to timely make such election,

the Secretary may treat such an election as timely made for such taxable year (and paragraph (3) shall not apply).".

26 USC 1362 note.

(c) EFFECTIVE DATE.—The amendments made by subsections (a) and (b) shall apply with respect to elections for taxable years beginning after December 31, 1982.

SEC. 1306. AGREEMENT TO TERMINATE YEAR.

Paragraph (2) of section 1377(a) (relating to pro rata share) is amended to read as follows:

"(2) ELECTION TO TERMINATE YEAR.—

"(A) IN GENERAL.—Under regulations prescribed by the Secretary, if any shareholder terminates the shareholder's interest in the corporation during the taxable year and all affected shareholders and the corporation agree to the application of this paragraph, paragraph (1) shall be applied to the affected shareholders as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination.

"(B) AFFECTED SHAREHOLDERS.—For purposes of subparagraph (A), the term 'affected shareholders' means the shareholder whose interest is terminated and all shareholders to whom such shareholder has transferred shares during the taxable year. If such shareholder has transferred shares to the corporation, the term 'affected shareholders' shall include all persons who are shareholders during the taxable year.".

SEC. 1307. EXPANSION OF POST-TERMINATION TRANSITION PERIOD.

(a) IN GENERAL.—Paragraph (1) of section 1377(b) (relating to post-termination transition period) is amended by striking "and" at the end of subparagraph (A), by redesignating subparagraph (B) as subparagraph (C), and by inserting after subparagraph (A) the following new subparagraph:

"(B) the 120-day period beginning on the date of any determination pursuant to an audit of the taxpayer which follows the termination of the corporation's election and which adjusts a subchapter S item of income, loss, or deduction of the corporation arising during the S period (as defined in section 1368(e)(2)), and".

(b) DETERMINATION DEFINED.—Paragraph (2) of section 1377(b) is amended by striking subparagraphs (A) and (B), by redesignating subparagraph (C) as subparagraph (B), and by inserting before subparagraph (B) (as so redesignated) the following new subparagraph:

"(A) a determination as defined in section 1313(a), or".

(c) REPEAL OF SPECIAL AUDIT PROVISIONS FOR SUBCHAPTER S ITEMS.—

(1) GENERAL RULE.—Subchapter D of chapter 63 (relating to tax treatment of subchapter S items) is hereby repealed. 26 USC 6241 *et seq.*

(2) CONSISTENT TREATMENT REQUIRED.—Section 6037 (relating to return of S corporation) is amended by adding at the end the following new subsection:

"(c) SHAREHOLDER'S RETURN MUST BE CONSISTENT WITH CORPORATE RETURN OR SECRETARY NOTIFIED OF INCONSISTENCY.—

"(1) IN GENERAL.—A shareholder of an S corporation shall, on such shareholder's return, treat a subchapter S item in a manner which is consistent with the treatment of such item on the corporate return.

"(2) NOTIFICATION OF INCONSISTENT TREATMENT.—

"(A) IN GENERAL.—In the case of any subchapter S item, if—

"(i)(I) the corporation has filed a return but the shareholder's treatment on his return is (or may be) inconsistent with the treatment of the item on the corporate return, or

"(II) the corporation has not filed a return, and

"(ii) the shareholder files with the Secretary a statement identifying the inconsistency,

paragraph (1) shall not apply to such item.

"(B) SHAREHOLDER RECEIVING INCORRECT INFORMATION.—A shareholder shall be treated as having complied with clause (ii) of subparagraph (A) with respect to a subchapter S item if the shareholder—

"(i) demonstrates to the satisfaction of the Secretary that the treatment of the subchapter S item on the shareholder's return is consistent with the treatment of the item on the schedule furnished to the shareholder by the corporation, and

"(ii) elects to have this paragraph apply with respect to that item.

"(3) EFFECT OF FAILURE TO NOTIFY.—In any case—

"(A) described in subparagraph (A)(i)(I) of paragraph (2), and

"(B) in which the shareholder does not comply with subparagraph (A)(ii) of paragraph (2),

any adjustment required to make the treatment of the items by such shareholder consistent with the treatment of the items on the corporate return shall be treated as arising out of mathematical or clerical errors and assessed according to section 6213(b)(1). Paragraph (2) of section 6213(b) shall not apply to any assessment referred to in the preceding sentence.

"(4) SUBCHAPTER S ITEM.—For purposes of this subsection, the term 'subchapter S item' means any item of an S corporation to the extent that regulations prescribed by the Secretary provide that, for purposes of this subtitle, such item is more appropriately determined at the corporation level than at the shareholder level.

"(5) ADDITION TO TAX FOR FAILURE TO COMPLY WITH SECTION.—

"For addition to tax in the case of a shareholder's negligence in connection with, or disregard of, the requirements of this section, see part II of subchapter A of chapter 68.".

(3) CONFORMING AMENDMENTS.—

(A) Section 1366 is amended by striking subsection (g).

(B) Subsection (b) of section 6233 is amended to read as follows:

"(b) SIMILAR RULES IN CERTAIN CASES.—If a partnership return is filed for any taxable year but it is determined that there is no entity for such taxable year, to the extent provided in regulations, rules similar to the rules of subsection (a) shall apply.".

(C) The table of subchapters for chapter 63 is amended by striking the item relating to subchapter D.

SEC. 1308. S CORPORATIONS PERMITTED TO HOLD SUBSIDIARIES.

(a) IN GENERAL.—Paragraph (2) of section 1361(b) (defining ineligible corporation) is amended by striking subparagraph (A) and by redesignating subparagraphs (B), (C), (D), and (E) as subparagraphs (A), (B), (C), and (D), respectively.

(b) TREATMENT OF CERTAIN WHOLLY OWNED S CORPORATION SUBSIDIARIES.—Section 1361(b) (defining small business corporation) is amended by adding at the end the following new paragraph:

"(3) TREATMENT OF CERTAIN WHOLLY OWNED SUBSIDIARIES.—

"(A) IN GENERAL.—For purposes of this title—

"(i) a corporation which is a qualified subchapter S subsidiary shall not be treated as a separate corporation, and

"(ii) all assets, liabilities, and items of income, deduction, and credit of a qualified subchapter S subsidiary shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

"(B) QUALIFIED SUBCHAPTER S SUBSIDIARY.—For purposes of this paragraph, the term 'qualified subchapter S subsidiary' means any domestic corporation which is not an ineligible corporation (as defined in paragraph (2)), if—

"(i) 100 percent of the stock of such corporation is held by the S corporation, and

"(ii) the S corporation elects to treat such corporation as a qualified subchapter S subsidiary.

"(C) TREATMENT OF TERMINATIONS OF QUALIFIED SUBCHAPTER S SUBSIDIARY STATUS.—For purposes of this title, if any corporation which was a qualified subchapter S subsidiary ceases to meet the requirements of subparagraph (B), such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the S corporation in exchange for its stock.

"(D) ELECTION AFTER TERMINATION.—If a corporation's status as a qualified subchapter S subsidiary terminates, such corporation (and any successor corporation) shall not be eligible to make—

"(i) an election under subparagraph (B)(ii) to be treated as a qualified subchapter S subsidiary, or

"(ii) an election under section 1362(a) to be treated as an S corporation,

before its 5th taxable year which begins after the 1st taxable year for which such termination was effective, unless the Secretary consents to such election.".

(c) CERTAIN DIVIDENDS NOT TREATED AS PASSIVE INVESTMENT INCOME.—Paragraph (3) of section 1362(d) is amended by adding at the end the following new subparagraph:

"(F) TREATMENT OF CERTAIN DIVIDENDS.—If an S corporation holds stock in a C corporation meeting the requirements of section 1504(a)(2), the term 'passive investment income' shall not include dividends from such C corporation to the extent such dividends are attributable to the earnings and profits of such C corporation derived from the active conduct of a trade or business.".

(d) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 1361 is amended by striking paragraph (6).

(2) Subsection (b) of section 1504 (defining includible corporation) is amended by adding at the end the following new paragraph:

"(8) An S corporation.".

SEC. 1309. TREATMENT OF DISTRIBUTIONS DURING LOSS YEARS.

(a) ADJUSTMENTS FOR DISTRIBUTIONS TAKEN INTO ACCOUNT BEFORE LOSSES.—

(1) Subparagraph (A) of section 1366(d)(1) (relating to losses and deductions cannot exceed shareholder's basis in stock and debt) is amended by striking "paragraph (1)" and inserting "paragraphs (1) and (2)(A)".

(2) Subsection (d) of section 1368 (relating to certain adjustments taken into account) is amended by adding at the end the following new flush sentence:

"In the case of any distribution made during any taxable year, the adjusted basis of the stock shall be determined with regard to the adjustments provided in paragraph (1) of section 1367(a) for the taxable year.".

(b) ACCUMULATED ADJUSTMENTS ACCOUNT.—Paragraph (1) of section 1368(e) (relating to accumulated adjustments account) is amended by adding at the end the following new subparagraph:

"(C) NET LOSS FOR YEAR DISREGARDED.—

"(i) IN GENERAL.—In applying this section to distributions made during any taxable year, the amount in the accumulated adjustments account as of the close of such taxable year shall be determined without regard to any net negative adjustment for such taxable year.

"(ii) NET NEGATIVE ADJUSTMENT.—For purposes of clause (i), the term 'net negative adjustment' means, with respect to any taxable year, the excess (if any) of—

"(I) the reductions in the account for the taxable year (other than for distributions), over

"(II) the increases in such account for such taxable year.".

(c) CONFORMING AMENDMENTS.—Subparagraph (A) of section 1368(e)(1) is amended—

(1) by striking "as provided in subparagraph (B)" and inserting "as otherwise provided in this paragraph", and

(2) by striking "section 1367(b)(2)(A)" and inserting "section 1367(a)(2)".

SEC. 1310. TREATMENT OF S CORPORATIONS UNDER SUBCHAPTER C.

Subsection (a) of section 1371 (relating to application of subchapter C rules) is amended to read as follows:

"(a) APPLICATION OF SUBCHAPTER C RULES.—Except as otherwise provided in this title, and except to the extent inconsistent with this subchapter, subchapter C shall apply to an S corporation and its shareholders.".

26 USC 1361 note.

SEC. 1311. ELIMINATION OF CERTAIN EARNINGS AND PROFITS.

(a) IN GENERAL.—If—

(1) a corporation was an electing small business corporation under subchapter S of chapter 1 of the Internal Revenue Code of 1986 for any taxable year beginning before January 1, 1983, and

(2) such corporation is an S corporation under subchapter S of chapter 1 of such Code for its first taxable year beginning after December 31, 1996,

the amount of such corporation's accumulated earnings and profits (as of the beginning of such first taxable year) shall be reduced by an amount equal to the portion (if any) of such accumulated earnings and profits which were accumulated in any taxable year beginning before January 1, 1983, for which such corporation was an electing small business corporation under such subchapter S.

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (3) of section 1362(d), as amended by section 1308, is amended—

(A) by striking "SUBCHAPTER C" in the paragraph heading and inserting "ACCUMULATED",

(B) by striking "subchapter C" in subparagraph (A)(i)(I) and inserting "accumulated", and

(C) by striking subparagraph (B) and redesignating the following subparagraphs accordingly.

(2)(A) Subsection (a) of section 1375 is amended by striking "subchapter C" in paragraph (1) and inserting "accumulated".

(B) Paragraph (3) of section 1375(b) is amended to read as follows:

"(3) PASSIVE INVESTMENT INCOME, ETC.—The terms 'passive investment income' and 'gross receipts' have the same respective meanings as when used in paragraph (3) of section 1362(d).".

(C) The section heading for section 1375 is amended by striking "**subchapter C**" and inserting "**accumulated**".

(D) The table of sections for part III of subchapter S of chapter 1 is amended by striking "subchapter C" in the item relating to section 1375 and inserting "accumulated".

(3) Clause (i) of section 1042(c)(4)(A) is amended by striking "section 1362(d)(3)(D)" and inserting "section 1362(d)(3)(C)".

SEC. 1312. CARRYOVER OF DISALLOWED LOSSES AND DEDUCTIONS UNDER AT-RISK RULES ALLOWED.

Paragraph (3) of section 1366(d) (relating to carryover of disallowed losses and deductions to post-termination transition period) is amended by adding at the end the following new subparagraph:

"(D) AT-RISK LIMITATIONS.—To the extent that any increase in adjusted basis described in subparagraph (B) would have increased the shareholder's amount at risk under section 465 if such increase had occurred on the day preceding the commencement of the post-termination transition period, rules similar to the rules described in subparagraphs (A) through (C) shall apply to any losses disallowed by reason of section 465(a).".

SEC. 1313. ADJUSTMENTS TO BASIS OF INHERITED S STOCK TO REFLECT CERTAIN ITEMS OF INCOME.

(a) IN GENERAL.—Subsection (b) of section 1367 (relating to adjustments to basis of stock of shareholders, etc.) is amended by adding at the end the following new paragraph:

"(4) ADJUSTMENTS IN CASE OF INHERITED STOCK.—

"(A) IN GENERAL.—If any person acquires stock in an S corporation by reason of the death of a decedent or by bequest, devise, or inheritance, section 691 shall be applied with respect to any item of income of the S corporation in the same manner as if the decedent had held directly his pro rata share of such item.

"(B) ADJUSTMENTS TO BASIS.—The basis determined under section 1014 of any stock in an S corporation shall be reduced by the portion of the value of the stock which is attributable to items constituting income in respect of the decedent.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply in the case of decedents dying after the date of the enactment of this Act. 26 USC 1367 note.

SEC. 1314. S CORPORATIONS ELIGIBLE FOR RULES APPLICABLE TO REAL PROPERTY SUBDIVIDED FOR SALE BY NONCORPORATE TAXPAYERS.

(a) IN GENERAL.—Subsection (a) of section 1237 (relating to real property subdivided for sale) is amended by striking "other than a corporation" in the material preceding paragraph (1) and inserting "other than a C corporation".

(b) CONFORMING AMENDMENT.—Subparagraph (A) of section 1237(a)(2) is amended by inserting "an S corporation which included the taxpayer as a shareholder," after "controlled by the taxpayer,".

SEC. 1315. FINANCIAL INSTITUTIONS.

Subparagraph (A) of section 1361(b)(2) (defining ineligible corporation), as redesignated by section 1308(a), is amended to read as follows:

"(A) a financial institution which uses the reserve method of accounting for bad debts described in section 585,".

SEC. 1316. CERTAIN EXEMPT ORGANIZATIONS ALLOWED TO BE SHAREHOLDERS.

(a) ELIGIBILITY TO BE SHAREHOLDERS.—

(1) IN GENERAL.—Subparagraph (B) of section 1361(b)(1) (defining small business corporation) is amended to read as follows:

"(B) have as a shareholder a person (other than an estate, a trust described in subsection (c)(2), or an organiza-

tion described in subsection (c)(7)) who is not an individual,".

(2) ELIGIBLE EXEMPT ORGANIZATIONS.—Section 1361(c) (relating to special rules for applying subsection (b)) is amended by adding at the end the following new paragraph:

"(7) CERTAIN EXEMPT ORGANIZATIONS PERMITTED AS SHAREHOLDERS.—For purposes of subsection (b)(1)(B), an organization which is—

"(A) described in section 401(a) or 501(c)(3), and

"(B) exempt from taxation under section 501(a),

may be a shareholder in an S corporation.".

(b) CONTRIBUTIONS OF S CORPORATION STOCK.—Section 170(e)(1) (relating to certain contributions of ordinary income and capital gain property) is amended by adding at the end the following new sentence: "For purposes of applying this paragraph in the case of a charitable contribution of stock in an S corporation, rules similar to the rules of section 751 shall apply in determining whether gain on such stock would have been long-term capital gain if such stock were sold by the taxpayer.".

(c) TREATMENT OF INCOME.—Section 512 (relating to unrelated business taxable income), as amended by section 1113, is amended by adding at the end the following new subsection:

"(e) SPECIAL RULES APPLICABLE TO S CORPORATIONS.—

"(1) IN GENERAL.—If an organization described in section 1361(c)(7) holds stock in an S corporation—

"(A) such interest shall be treated as an interest in an unrelated trade or business, and

"(B) notwithstanding any other provision of this part—

"(i) all items of income, loss, or deduction taken into account under section 1366(a), and

"(ii) any gain or loss on the disposition of the stock in the S corporation,

shall be taken into account in computing the unrelated business taxable income of such organization.

"(2) BASIS REDUCTION.—Except as provided in regulations, for purposes of paragraph (1), the basis of any stock acquired by purchase (within the meaning of section 1012) shall be reduced by the amount of any dividends received by the organization with respect to the stock.".

(d) CERTAIN BENEFITS NOT APPLICABLE TO S CORPORATIONS.—

(1) CONTRIBUTION TO ESOPS.—Paragraph (9) of section 404(a) (relating to certain contributions to employee ownership plans) is amended by inserting at the end the following new subparagraph:

"(C) S CORPORATIONS.—This paragraph shall not apply to an S corporation.".

(2) DIVIDENDS ON EMPLOYER SECURITIES.—Paragraph (1) of section 404(k) (relating to deduction for dividends on certain employer securities) is amended by striking "a corporation" and inserting "a C corporation".

(3) EXCHANGE TREATMENT.—Subparagraph (A) of section 1042(c)(1) (defining qualified securities) is amended by striking "domestic corporation" and inserting "domestic C corporation".

(e) CONFORMING AMENDMENT.—Clause (i) of section 1361(e)(1)(A), as added by section 1302, is amended by striking "which holds a contingent interest and is not a potential current beneficiary".

(f) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1997. 26 USC 170 note.

SEC. 1317. EFFECTIVE DATE.

(a) IN GENERAL.—Except as otherwise provided in this subtitle, the amendments made by this subtitle shall apply to taxable years beginning after December 31, 1996. 26 USC 641 note.

(b) TREATMENT OF CERTAIN ELECTIONS UNDER PRIOR LAW.—For purposes of section 1362(g) of the Internal Revenue Code of 1986 (relating to election after termination), any termination under section 1362(d) of such Code in a taxable year beginning before January 1, 1997, shall not be taken into account. 26 USC 1362 note.

Subtitle D—Pension Simplification

CHAPTER 1—SIMPLIFIED DISTRIBUTION RULES

SEC. 1401. REPEAL OF 5-YEAR INCOME AVERAGING FOR LUMP-SUM DISTRIBUTIONS.

(a) IN GENERAL.—Subsection (d) of section 402 (relating to taxability of beneficiary of employees' trust) is amended to read as follows:

"(d) TAXABILITY OF BENEFICIARY OF CERTAIN FOREIGN SITUS TRUSTS.—For purposes of subsections (a), (b), and (c), a stock bonus, pension, or profit-sharing trust which would qualify for exemption from tax under section 501(a) except for the fact that it is a trust created or organized outside the United States shall be treated as if it were a trust exempt from tax under section 501(a).".

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (D) of section 402(e)(4) (relating to other rules applicable to exempt trusts) is amended to read as follows:

"(D) LUMP-SUM DISTRIBUTION.—For purposes of this paragraph—

"(i) IN GENERAL.—The term 'lump-sum distribution' means the distribution or payment within one taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient—

"(I) on account of the employee's death,

"(II) after the employee attains age 59½,

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

"(IV) after the employee has become disabled (within the meaning of section 72(m)(7)),

from a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501 or from a plan described in section 403(a). Subclause (III) of this clause shall be applied only with respect to an individual who is an employee without regard to section 401(c)(1), and subclause (IV) shall be applied only with respect to an employee within the meaning of section 401(c)(1). For purposes of this clause, a distribution to two or more trusts shall be treated as a distribution to one recipient. For purposes of this paragraph, the balance to the credit of the employee does not include the accumulated deductible employee contributions under the plan (within the meaning of section 72(o)(5)).

"(ii) AGGREGATION OF CERTAIN TRUSTS AND PLANS.—For purposes of determining the balance to the credit of an employee under clause (i)—

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

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

"(iii) COMMUNITY PROPERTY LAWS.—The provisions of this paragraph shall be applied without regard to community property laws.

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

"(v) BALANCE TO CREDIT OF EMPLOYEE NOT TO INCLUDE AMOUNTS PAYABLE UNDER QUALIFIED DOMESTIC RELATIONS ORDER.—For purposes of this paragraph, the balance to the credit of an employee shall not include any amount payable to an alternate payee under a qualified domestic relations order (within the meaning of section 414(p)).

"(vi) TRANSFERS TO COST-OF-LIVING ARRANGEMENT NOT TREATED AS DISTRIBUTION.—For purposes of this paragraph, the balance to the credit of an employee under a defined contribution plan shall not include any amount transferred from such defined contribution plan to a qualified cost-of-living arrangement (within the meaning of section 415(k)(2)) under a defined benefit plan.

"(vii) LUMP-SUM DISTRIBUTIONS OF ALTERNATE PAYEES.—If any distribution or payment of the balance to the credit of an employee would be treated as a lump-sum distribution, then, for purposes of this paragraph, the payment under a qualified domestic relations order (within the meaning of section 414(p)) of the balance to the credit of an alternate payee who is the spouse or former spouse of the employee shall be treated as a lump-sum distribution. For purposes of this clause, the balance to the credit of the alternate payee shall not include any amount payable to the employee.".

(2) Section 402(c) (relating to rules applicable to rollovers from exempt trusts) is amended by striking paragraph (10).

(3) Paragraph (1) of section 55(c) (defining regular tax) is amended by striking "shall not include any tax imposed by section 402(d) and".

(4) Paragraph (8) of section 62(a) (relating to certain portion of lump-sum distributions from pension plans taxed under section 402(d)) is hereby repealed.

(5) Section 401(a)(28)(B) (relating to coordination with distribution rules) is amended by striking clause (v).

(6) Subparagraph (B)(ii) of section 401(k)(10) (relating to distributions that must be lump-sum distributions) is amended to read as follows:

"(ii) LUMP-SUM DISTRIBUTION.—For purposes of this subparagraph, the term 'lump-sum distribution' has the meaning given such term by section 402(e)(4)(D) (without regard to subclauses (I), (II), (III), and (IV) of clause (i) thereof).".

(7) Section 406(c) (relating to termination of status as deemed employee not to be treated as separation from service for purposes of limitation of tax) is hereby repealed.

(8) Section 407(c) (relating to termination of status as deemed employee not to be treated as separation from service for purposes of limitation of tax) is hereby repealed.

(9) Section 691(c) (relating to deduction for estate tax) is amended by striking paragraph (5).

(10) Paragraph (1) of section 871(b) (relating to imposition of tax) is amended by striking "section 1, 55, or 402(d)(1)" and inserting "section 1 or 55".

(11) Subsection (b) of section 877 (relating to alternative tax) is amended by striking "section 1, 55, or 402(d)(1)" and inserting "section 1 or 55".

(12) Section 4980A(c)(4) is amended—

(A) by striking "to which an election under section 402(d)(4)(B) applies" and inserting "(as defined in section 402(e)(4)(D)) with respect to which the individual elects to have this paragraph apply",

(B) by adding at the end the following new flush sentence:

"An individual may elect to have this paragraph apply to only one lump-sum distribution.", and

(C) by striking the heading and inserting:

"(4) SPECIAL ONE-TIME ELECTION.—".

(13) Section 402(e) is amended by striking paragraph (5).

(c) EFFECTIVE DATES.— 26 USC 402 note.

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1999.

(2) RETENTION OF CERTAIN TRANSITION RULES.—The amendments made by this section shall not apply to any distribution for which the taxpayer is eligible to elect the benefits of section 1122(h) (3) or (5) of the Tax Reform Act of 1986. Notwithstanding the preceding sentence, individuals who elect such benefits after December 31, 1999, shall not be eligible for 5-year averaging under section 402(d) of the Internal Revenue Code of 1986 (as in effect immediately before such amendments).

SEC. 1402. REPEAL OF $5,000 EXCLUSION OF EMPLOYEES' DEATH BENEFITS.

(a) IN GENERAL.—Subsection (b) of section 101 is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 101 is amended by striking "subsection (a) or (b)" and inserting "subsection (a)".

(2) Sections 406(e) and 407(e) are each amended by striking paragraph (2) and by redesignating paragraph (3) as paragraph (2).

(3) Section 7701(a)(20) is amended by striking ", for the purpose of applying the provisions of section 101(b) with respect to employees' death benefits".

26 USC 101 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to decedents dying after the date of the enactment of this Act.

SEC. 1403. SIMPLIFIED METHOD FOR TAXING ANNUITY DISTRIBUTIONS UNDER CERTAIN EMPLOYER PLANS.

(a) GENERAL RULE.—Subsection (d) of section 72 (relating to annuities; certain proceeds of endowment and life insurance contracts) is amended to read as follows:

"(d) SPECIAL RULES FOR QUALIFIED EMPLOYER RETIREMENT PLANS.—

"(1) SIMPLIFIED METHOD OF TAXING ANNUITY PAYMENTS.—

"(A) IN GENERAL.—In the case of any amount received as an annuity under a qualified employer retirement plan—

"(i) subsection (b) shall not apply, and

"(ii) the investment in the contract shall be recovered as provided in this paragraph.

"(B) METHOD OF RECOVERING INVESTMENT IN CONTRACT.—

"(i) IN GENERAL.—Gross income shall not include so much of any monthly annuity payment under a qualified employer retirement plan as does not exceed the amount obtained by dividing—

"(I) the investment in the contract (as of the annuity starting date), by

"(II) the number of anticipated payments determined under the table contained in clause (iii) (or, in the case of a contract to which subsection (c)(3)(B) applies, the number of monthly annuity payments under such contract).

"(ii) CERTAIN RULES MADE APPLICABLE.—Rules similar to the rules of paragraphs (2) and (3) of subsection (b) shall apply for purposes of this paragraph.

"(iii) NUMBER OF ANTICIPATED PAYMENTS.—

"If the age of the primary annuitant on the annuity starting date is:	The number of anticipated payments is:
Not more than 55	360
More than 55 but not more than 60	310
More than 60 but not more than 65	260
More than 65 but not more than 70	210
More than 70	160.

"(C) ADJUSTMENT FOR REFUND FEATURE NOT APPLICABLE.—For purposes of this paragraph, investment in the contract shall be determined under subsection (c)(1) without regard to subsection (c)(2).

"(D) SPECIAL RULE WHERE LUMP SUM PAID IN CONNECTION WITH COMMENCEMENT OF ANNUITY PAYMENTS.—If, in connection with the commencement of annuity payments under any qualified employer retirement plan, the taxpayer receives a lump-sum payment—

"(i) such payment shall be taxable under subsection (e) as if received before the annuity starting date, and

"(ii) the investment in the contract for purposes of this paragraph shall be determined as if such payment had been so received.

"(E) EXCEPTION.—This paragraph shall not apply in any case where the primary annuitant has attained age 75 on the annuity starting date unless there are fewer than 5 years of guaranteed payments under the annuity.

"(F) ADJUSTMENT WHERE ANNUITY PAYMENTS NOT ON MONTHLY BASIS.—In any case where the annuity payments are not made on a monthly basis, appropriate adjustments in the application of this paragraph shall be made to take into account the period on the basis of which such payments are made.

"(G) QUALIFIED EMPLOYER RETIREMENT PLAN.—For purposes of this paragraph, the term 'qualified employer retirement plan' means any plan or contract described in paragraph (1), (2), or (3) of section 4974(c).

"(2) TREATMENT OF EMPLOYEE CONTRIBUTIONS UNDER DEFINED CONTRIBUTION PLANS.—For purposes of this section, employee contributions (and any income allocable thereto) under a defined contribution plan may be treated as a separate contract.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in cases where the annuity starting date is after the 90th day after the date of the enactment of this Act. 26 USC 72 note.

SEC. 1404. REQUIRED DISTRIBUTIONS.

(a) IN GENERAL.—Section 401(a)(9)(C) (defining required beginning date) is amended to read as follows:

"(C) REQUIRED BEGINNING DATE.—For purposes of this paragraph—

"(i) IN GENERAL.—The term 'required beginning date' means April 1 of the calendar year following the later of—

"(I) the calendar year in which the employee attains age 70½, or

"(II) the calendar year in which the employee retires.

"(ii) EXCEPTION.—Subclause (II) of clause (i) shall not apply—

"(I) except as provided in section 409(d), in the case of an employee who is a 5-percent owner (as defined in section 416) with respect to the plan year ending in the calendar year in which the employee attains age 70½, or

"(II) for purposes of section 408 (a)(6) or (b)(3).

"(iii) ACTUARIAL ADJUSTMENT.—In the case of an employee to whom clause (i)(II) applies who retires in a calendar year after the calendar year in which the employee attains age 70½, the employee's accrued benefit shall be actuarially increased to take into account the period after age 70½ in which the employee was not receiving any benefits under the plan.

"(iv) EXCEPTION FOR GOVERNMENTAL AND CHURCH PLANS.—Clauses (ii) and (iii) shall not apply in the case of a governmental plan or church plan. For purposes of this clause, the term 'church plan' means a plan maintained by a church for church employees, and the term 'church' means any church (as defined in section 3121(w)(3)(A)) or qualified church-controlled organization (as defined in section 3121(w)(3)(B)).".

26 USC 401 note.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to years beginning after December 31, 1996.

CHAPTER 2—INCREASED ACCESS TO RETIREMENT PLANS

Subchapter A—Simple Savings Plans

SEC. 1421. ESTABLISHMENT OF SAVINGS INCENTIVE MATCH PLANS FOR EMPLOYEES OF SMALL EMPLOYERS.

(a) IN GENERAL.—Section 408 (relating to individual retirement accounts) is amended by redesignating subsection (p) as subsection (q) and by inserting after subsection (o) the following new subsection:

"(p) SIMPLE RETIREMENT ACCOUNTS.—

"(1) IN GENERAL.—For purposes of this title, the term 'simple retirement account' means an individual retirement plan (as defined in section 7701(a)(37))—

"(A) with respect to which the requirements of paragraphs (3), (4), and (5) are met; and

"(B) with respect to which the only contributions allowed are contributions under a qualified salary reduction arrangement.

"(2) QUALIFIED SALARY REDUCTION ARRANGEMENT.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'qualified salary reduction arrangement' means a written arrangement of an eligible employer under which—

"(i) an employee eligible to participate in the arrangement may elect to have the employer make payments—

"(I) as elective employer contributions to a simple retirement account on behalf of the employee, or

"(II) to the employee directly in cash,

"(ii) the amount which an employee may elect under clause (i) for any year is required to be expressed as a percentage of compensation and may not exceed a total of $6,000 for any year,

"(iii) the employer is required to make a matching contribution to the simple retirement account for any year in an amount equal to so much of the amount the employee elects under clause (i)(I) as does not exceed the applicable percentage of compensation for the year, and

"(iv) no contributions may be made other than contributions described in clause (i) or (iii).

"(B) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—

"(i) IN GENERAL.—An employer shall be treated as meeting the requirements of subparagraph (A)(iii) for any year if, in lieu of the contributions described in such clause, the employer elects to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 60-day period for such year under paragraph (5)(C).

"(ii) COMPENSATION LIMITATION.—The compensation taken into account under clause (i) for any year shall not exceed the limitation in effect for such year under section 401(a)(17).

"(C) DEFINITIONS.—For purposes of this subsection—

"(i) ELIGIBLE EMPLOYER.—

"(I) IN GENERAL.—The term 'eligible employer' means, with respect to any year, an employer which had no more than 100 employees who received at least $5,000 of compensation from the employer for the preceding year.

"(II) 2-YEAR GRACE PERIOD.—An eligible employer who establishes and maintains a plan under this subsection for 1 or more years and who fails to be an eligible employer for any subsequent year shall be treated as an eligible employer for the 2 years following the last year the employer was an eligible employer. If such failure is due to any acquisition, disposition, or similar transaction involving an eligible employer, the preceding sentence shall apply only in accordance with rules similar to the rules of section 410(b)(6)(C)(i).

"(ii) APPLICABLE PERCENTAGE.—

"(I) IN GENERAL.—The term 'applicable percentage' means 3 percent.

"(II) ELECTION OF LOWER PERCENTAGE.—An employer may elect to apply a lower percentage (not less than 1 percent) for any year for all employees eligible to participate in the plan for such year if the employer notifies the employees of such lower percentage within a reasonable period of time before the 60-day election period for such year under paragraph (5)(C). An employer may not elect a lower percentage under this subclause for any year if that election would result in the applicable percentage being lower than 3 percent in more than 2 of the years in the 5-year period ending with such year.

"(III) SPECIAL RULE FOR YEARS ARRANGEMENT NOT IN EFFECT.—If any year in the 5-year period described in subclause (II) is a year prior to the first year for which any qualified salary reduction arrangement is in effect with respect to the employer (or any predecessor), the employer shall be treated as if the level of the employer matching

contribution was at 3 percent of compensation for such prior year.

"(D) ARRANGEMENT MAY BE ONLY PLAN OF EMPLOYER.—

"(i) IN GENERAL.—An arrangement shall not be treated as a qualified salary reduction arrangement for any year if the employer (or any predecessor employer) maintained a qualified plan with respect to which contributions were made, or benefits were accrued, for service in any year in the period beginning with the year such arrangement became effective and ending with the year for which the determination is being made.

"(ii) QUALIFIED PLAN.—For purposes of this subparagraph, the term 'qualified plan' means a plan, contract, pension, or trust described in subparagraph (A) or (B) of section 219(g)(5).

"(E) COST-OF-LIVING ADJUSTMENT.—The Secretary shall adjust the $6,000 amount under subparagraph (A)(ii) at the same time and in the same manner as under section 415(d), except that the base period taken into account shall be the calendar quarter ending September 30, 1996, and any increase under this subparagraph which is not a multiple of $500 shall be rounded to the next lower multiple of $500.

"(3) VESTING REQUIREMENTS.—The requirements of this paragraph are met with respect to a simple retirement account if the employee's rights to any contribution to the simple retirement account are nonforfeitable. For purposes of this paragraph, rules similar to the rules of subsection (k)(4) shall apply.

"(4) PARTICIPATION REQUIREMENTS.—

"(A) IN GENERAL.—The requirements of this paragraph are met with respect to any simple retirement account for a year only if, under the qualified salary reduction arrangement, all employees of the employer who—

"(i) received at least $5,000 in compensation from the employer during any 2 preceding years, and

"(ii) are reasonably expected to receive at least $5,000 in compensation during the year,

are eligible to make the election under paragraph (2)(A)(i) or receive the nonelective contribution described in paragraph (2)(B).

"(B) EXCLUDABLE EMPLOYEES.—An employer may elect to exclude from the requirement under subparagraph (A) employees described in section 410(b)(3).

"(5) ADMINISTRATIVE REQUIREMENTS.—The requirements of this paragraph are met with respect to any simplified retirement account if, under the qualified salary reduction arrangement—

"(A) an employer must—

"(i) make the elective employer contributions under paragraph (2)(A)(i) not later than the close of the 30-day period following the last day of the month with respect to which the contributions are to be made, and

"(ii) make the matching contributions under paragraph (2)(A)(iii) or the nonelective contributions under

paragraph (2)(B) not later than the date described in section 404(m)(2)(B),

"(B) an employee may elect to terminate participation in such arrangement at any time during the year, except that if an employee so terminates, the arrangement may provide that the employee may not elect to resume participation until the beginning of the next year, and

"(C) each employee eligible to participate may elect, during the 60-day period before the beginning of any year (and the 60-day period before the first day such employee is eligible to participate), to participate in the arrangement, or to modify the amounts subject to such arrangement, for such year.

"(6) DEFINITIONS.—For purposes of this subsection—

"(A) COMPENSATION.—

"(i) IN GENERAL.—The term 'compensation' means amounts described in paragraphs (3) and (8) of section 6051(a).

"(ii) SELF-EMPLOYED.—In the case of an employee described in subparagraph (B), the term 'compensation' means net earnings from self-employment determined under section 1402(a) without regard to any contribution under this subsection.

"(B) EMPLOYEE.—The term 'employee' includes an employee as defined in section 401(c)(1).

"(C) YEAR.—The term 'year' means the calendar year.

"(7) USE OF DESIGNATED FINANCIAL INSTITUTION.—A plan shall not be treated as failing to satisfy the requirements of this subsection or any other provision of this title merely because the employer makes all contributions to the individual retirement accounts or annuities of a designated trustee or issuer. The preceding sentence shall not apply unless each plan participant is notified in writing (either separately or as part of the notice under subsection (l)(2)(C)) that the participant's balance may be transferred without cost or penalty to another individual account or annuity in accordance with subsection (d)(3)(G).".

(b) TAX TREATMENT OF SIMPLE RETIREMENT ACCOUNTS.—

(1) DEDUCTIBILITY OF CONTRIBUTIONS BY EMPLOYEES.—

(A) Section 219(b) (relating to maximum amount of deduction) is amended by adding at the end the following new paragraph:

"(4) SPECIAL RULE FOR SIMPLE RETIREMENT ACCOUNTS.—This section shall not apply with respect to any amount contributed to a simple retirement account established under section 408(p).".

(B) Section 219(g)(5)(A) (defining active participant) is amended by striking "or" at the end of clause (iv) and by adding at the end the following new clause:

"(vi) any simple retirement account (within the meaning of section 408(p)), or".

(2) DEDUCTIBILITY OF EMPLOYER CONTRIBUTIONS.—Section 404 (relating to deductions for contributions of an employer to pension, etc. plans) is amended by adding at the end the following new subsection:

"(m) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—

"(1) IN GENERAL.—Employer contributions to a simple retirement account shall be treated as if they are made to a plan subject to the requirements of this section.

"(2) TIMING.—

"(A) DEDUCTION.—Contributions described in paragraph (1) shall be deductible in the taxable year of the employer with or within which the calendar year for which the contributions were made ends.

"(B) CONTRIBUTIONS AFTER END OF YEAR.—For purposes of this subsection, contributions shall be treated as made for a taxable year if they are made on account of the taxable year and are made not later than the time prescribed by law for filing the return for the taxable year (including extensions thereof).".

(3) CONTRIBUTIONS AND DISTRIBUTIONS.—

(A) Section 402 (relating to taxability of beneficiary of employees' trust) is amended by adding at the end the following new subsection:

"(k) TREATMENT OF SIMPLE RETIREMENT ACCOUNTS.—Rules similar to the rules of paragraphs (1) and (3) of subsection (h) shall apply to contributions and distributions with respect to a simple retirement account under section 408(p).".

(B) Section 408(d)(3) is amended by adding at the end the following new subparagraph:

"(G) SIMPLE RETIREMENT ACCOUNTS.—This paragraph shall not apply to any amount paid or distributed out of a simple retirement account (as defined in subsection (p)) unless—

"(i) it is paid into another simple retirement account, or

"(ii) in the case of any payment or distribution to which section 72(t)(6) does not apply, it is paid into an individual retirement plan.".

(C) Clause (i) of section 457(c)(2)(B) is amended by striking "section 402(h)(1)(B)" and inserting "section 402(h)(1)(B) or (k)".

(4) PENALTIES.—

(A) EARLY WITHDRAWALS.—Section 72(t) (relating to additional tax in early distributions) is amended by adding at the end the following new paragraph:

"(6) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—In the case of any amount received from a simple retirement account (within the meaning of section 408(p)) during the 2-year period beginning on the date such individual first participated in any qualified salary reduction arrangement maintained by the individual's employer under section 408(p)(2), paragraph (1) shall be applied by substituting '25 percent' for '10 percent'.".

(B) FAILURE TO REPORT.—Section 6693 is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

"(c) PENALTIES RELATING TO SIMPLE RETIREMENT ACCOUNTS.—

"(1) EMPLOYER PENALTIES.—An employer who fails to provide 1 or more notices required by section 408(l)(2)(C) shall pay a penalty of $50 for each day on which such failures continue.

"(2) TRUSTEE PENALTIES.—A trustee who fails—

"(A) to provide 1 or more statements required by the last sentence of section 408(i) shall pay a penalty of $50 for each day on which such failures continue, or

"(B) to provide 1 or more summary descriptions required by section 408(l)(2)(B) shall pay a penalty of $50 for each day on which such failures continue.

"(3) REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed under this subsection with respect to any failure which the taxpayer shows was due to reasonable cause.".

(5) REPORTING REQUIREMENTS.—

(A) Section 408(l) is amended by adding at the end the following new paragraph:

"(2) SIMPLE RETIREMENT ACCOUNTS.—

"(A) NO EMPLOYER REPORTS.—Except as provided in this paragraph, no report shall be required under this section by an employer maintaining a qualified salary reduction arrangement under subsection (p).

"(B) SUMMARY DESCRIPTION.—The trustee of any simple retirement account established pursuant to a qualified salary reduction arrangement under subsection (p) shall provide to the employer maintaining the arrangement, each year a description containing the following information:

"(i) The name and address of the employer and the trustee.

"(ii) The requirements for eligibility for participation.

"(iii) The benefits provided with respect to the arrangement.

"(iv) The time and method of making elections with respect to the arrangement.

"(v) The procedures for, and effects of, withdrawals (including rollovers) from the arrangement.

"(C) EMPLOYEE NOTIFICATION.—The employer shall notify each employee immediately before the period for which an election described in subsection (p)(5)(C) may be made of the employee's opportunity to make such election. Such notice shall include a copy of the description described in subparagraph (B).".

(B) Section 408(l) is amended by striking "An employer" and inserting the following:

"(1) IN GENERAL.—An employer".

(6) REPORTING REQUIREMENTS.—Section 408(i) is amended by adding at the end the following new flush sentence:

"In the case of a simple retirement account under subsection (p), only one report under this subsection shall be required to be submitted each calendar year to the Secretary (at the time provided under paragraph (2)) but, in addition to the report under this subsection, there shall be furnished, within 30 days after each calendar year, to the individual on whose behalf the account is maintained a statement with respect to the account balance as of the close of, and the account activity during, such calendar year.".

(7) EXEMPTION FROM TOP-HEAVY PLAN RULES.—Section 416(g)(4) (relating to special rules for top-heavy plans) is amended by adding at the end the following new subparagraph:

"(G) SIMPLE RETIREMENT ACCOUNTS.—The term 'top-heavy plan' shall not include a simple retirement account under section 408(p).".

(8) EMPLOYMENT TAXES.—

(A) Paragraph (5) of section 3121(a) is amended by striking "or" at the end of subparagraph (F), by inserting "or" at the end of subparagraph (G), and by adding at the end the following new subparagraph:

"(H) under an arrangement to which section 408(p) applies, other than any elective contributions under paragraph (2)(A)(i) thereof,".

26 USC 409.

(B) Section 209(a)(4) of the Social Security Act is amended by inserting "; or (J) under an arrangement to which section 408(p) of such Code applies, other than any elective contributions under paragraph (2)(A)(i) thereof" before the semicolon at the end thereof.

(C) Paragraph (5) of section 3306(b) is amended by striking "or" at the end of subparagraph (F), by inserting "or" at the end of subparagraph (G), and by adding at the end the following new subparagraph:

"(H) under an arrangement to which section 408(p) applies, other than any elective contributions under paragraph (2)(A)(i) thereof,".

(D) Paragraph (12) of section 3401(a) is amended by adding the following new subparagraph:

"(D) under an arrangement to which section 408(p) applies; or".

(9) CONFORMING AMENDMENTS.—

(A) Section 280G(b)(6) is amended by striking "or" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", or" and by adding after subparagraph (C) the following new subparagraph:

"(D) a simple retirement account described in section 408(p).".

(B) Section 402(g)(3) is amended by striking "and" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", and", and by adding after subparagraph (C) the following new subparagraph:

"(D) any elective employer contribution under section 408(p)(2)(A)(i).".

(C) Subsections (b), (c), (m)(4)(B), and (n)(3)(B) of section 414 are each amended by inserting "408(p)," after "408(k),".

(D) Section 4972(d)(1)(A) is amended by striking "and" at the end of clause (ii), by striking the period at the end of clause (iii) and inserting ", and", and by adding after clause (iii) the following new clause:

"(iv) any simple retirement account (within the meaning of section 408(p)).".

(c) REPEAL OF SALARY REDUCTION SIMPLIFIED EMPLOYEE PENSIONS.—Section 408(k)(6) is amended by adding at the end the following new subparagraph:

"(H) TERMINATION.—This paragraph shall not apply to years beginning after December 31, 1996. The preceding sentence shall not apply to a simplified employee pension

if the terms of such pension, as in effect on December 31, 1996, provide that an employee may make the election described in subparagraph (A).".

(d) MODIFICATIONS OF ERISA.—

(1) REPORTING REQUIREMENTS.—Section 101 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1021) is amended by redesignating subsection (g) as subsection (h) and by inserting after subsection (f) the following new subsection:

"(g) SIMPLE RETIREMENT ACCOUNTS.—

"(1) NO EMPLOYER REPORTS.—Except as provided in this subsection, no report shall be required under this section by an employer maintaining a qualified salary reduction arrangement under section 408(p) of the Internal Revenue Code of 1986.

"(2) SUMMARY DESCRIPTION.—The trustee of any simple retirement account established pursuant to a qualified salary reduction arrangement under section 408(p) of such Code shall provide to the employer maintaining the arrangement each year a description containing the following information:

"(A) The name and address of the employer and the trustee.

"(B) The requirements for eligibility for participation.

"(C) The benefits provided with respect to the arrangement.

"(D) The time and method of making elections with respect to the arrangement.

"(E) The procedures for, and effects of, withdrawals (including rollovers) from the arrangement.

"(3) EMPLOYEE NOTIFICATION.—The employer shall notify each employee immediately before the period for which an election described in section 408(p)(5)(C) of such Code may be made of the employee's opportunity to make such election. Such notice shall include a copy of the description described in paragraph (2)."

(2) FIDUCIARY DUTIES.—Section 404(c) of such Act (29 U.S.C. 1104(c)) is amended by inserting "(1)" after "(c)", by redesignating paragraphs (1) and (2) as subparagraphs (A) and (B), respectively, and by adding at the end the following new paragraph:

"(2) In the case of a simple retirement account established pursuant to a qualified salary reduction arrangement under section 408(p) of the Internal Revenue Code of 1986, a participant or beneficiary shall, for purposes of paragraph (1), be treated as exercising control over the assets in the account upon the earliest of—

"(A) an affirmative election among investment options with respect to the initial investment of any contribution,

"(B) a rollover to any other simple retirement account or individual retirement plan, or

"(C) one year after the simple retirement account is established.

No reports, other than those required under section 101(g), shall be required with respect to a simple retirement account established pursuant to such a qualified salary reduction arrangement.".

26 USC 72 note.

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1422. EXTENSION OF SIMPLE PLAN TO 401(k) ARRANGEMENTS.

(a) ALTERNATIVE METHOD OF SATISFYING SECTION 401(k) NONDISCRIMINATION TESTS.—Section 401(k) (relating to cash or deferred arrangements) is amended by adding at the end the following new paragraph:

"(11) ADOPTION OF SIMPLE PLAN TO MEET NONDISCRIMINATION TESTS.—

"(A) IN GENERAL.—A cash or deferred arrangement maintained by an eligible employer shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement meets—

"(i) the contribution requirements of subparagraph (B),

"(ii) the exclusive plan requirements of subparagraph (C), and

"(iii) the vesting requirements of section 408(p)(3).

"(B) CONTRIBUTION REQUIREMENTS.—

"(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement—

"(I) an employee may elect to have the employer make elective contributions for the year on behalf of the employee to a trust under the plan in an amount which is expressed as a percentage of compensation of the employee but which in no event exceeds $6,000,

"(II) the employer is required to make a matching contribution to the trust for the year in an amount equal to so much of the amount the employee elects under subclause (I) as does not exceed 3 percent of compensation for the year, and

"(III) no other contributions may be made other than contributions described in subclause (I) or (II).

"(ii) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—An employer shall be treated as meeting the requirements of clause (i)(II) for any year if, in lieu of the contributions described in such clause, the employer elects (pursuant to the terms of the arrangement) to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 60th day before the beginning of such year.

"(C) EXCLUSIVE PLAN REQUIREMENT.—The requirements of this subparagraph are met for any year to which this paragraph applies if no contributions were made, or benefits were accrued, for services during such year under any qualified plan of the employer on behalf of any employee eligible to participate in the cash or deferred

arrangement, other than contributions described in subparagraph (B).

"(D) DEFINITIONS AND SPECIAL RULE.—

"(i) DEFINITIONS.—For purposes of this paragraph, any term used in this paragraph which is also used in section 408(p) shall have the meaning given such term by such section.

"(ii) COORDINATION WITH TOP-HEAVY RULES.—A plan meeting the requirements of this paragraph for any year shall not be treated as a top-heavy plan under section 416 for such year.".

(b) ALTERNATIVE METHODS OF SATISFYING SECTION 401(m) NONDISCRIMINATION TESTS.—Section 401(m) (relating to nondiscrimination test for matching contributions and employee contributions) is amended by redesignating paragraph (10) as paragraph (11) and by adding after paragraph (9) the following new paragraph:

"(10) ALTERNATIVE METHOD OF SATISFYING TESTS.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

"(A) meets the contribution requirements of subparagraph (B) of subsection (k)(11),

"(B) meets the exclusive plan requirements of subsection (k)(11)(C), and

"(C) meets the vesting requirements of section 408(p)(3).".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning after December 31, 1996. 26 USC 401 note.

Subchapter B—Other Provisions

SEC. 1426. TAX-EXEMPT ORGANIZATIONS ELIGIBLE UNDER SECTION 401(k).

(a) IN GENERAL.—Subparagraph (B) of section 401(k)(4) is amended to read as follows:

"(B) ELIGIBILITY OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.—

"(i) TAX-EXEMPTS ELIGIBLE.—Except as provided in clause (ii), any organization exempt from tax under this subtitle may include a qualified cash or deferred arrangement as part of a plan maintained by it.

"(ii) GOVERNMENTS INELIGIBLE.—A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement if it is part of a plan maintained by a State or local government or political subdivision thereof, or any agency or instrumentality thereof. This clause shall not apply to a rural cooperative plan or to a plan of an employer described in clause (iii).

"(iii) TREATMENT OF INDIAN TRIBAL GOVERNMENTS.—An employer which is an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in

part by any of the foregoing may include a qualified cash or deferred arrangement as part of a plan maintained by the employer.".

26 USC 401 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to plan years beginning after December 31, 1996, but shall not apply to any cash or deferred arrangement to which clause (i) of section 1116(f)(2)(B) of the Tax Reform Act of 1986 applies.

SEC. 1427. HOMEMAKERS ELIGIBLE FOR FULL IRA DEDUCTION.

(a) SPOUSAL IRA COMPUTED ON BASIS OF COMPENSATION OF BOTH SPOUSES.—Subsection (c) of section 219 (relating to special rules for certain married individuals) is amended to read as follows:

"(c) SPECIAL RULES FOR CERTAIN MARRIED INDIVIDUALS.—

"(1) IN GENERAL.—In the case of an individual to whom this paragraph applies for the taxable year, the limitation of paragraph (1) of subsection (b) shall be equal to the lesser of—

"(A) the dollar amount in effect under subsection (b)(1)(A) for the taxable year, or

"(B) the sum of—

"(i) the compensation includible in such individual's gross income for the taxable year, plus

"(ii) the compensation includible in the gross income of such individual's spouse for the taxable year reduced by the amount allowed as a deduction under subsection (a) to such spouse for such taxable year.

"(2) INDIVIDUALS TO WHOM PARAGRAPH (1) APPLIES.—Paragraph (1) shall apply to any individual if—

"(A) such individual files a joint return for the taxable year, and

"(B) the amount of compensation (if any) includible in such individual's gross income for the taxable year is less than the compensation includible in the gross income of such individual's spouse for the taxable year.".

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (2) of section 219(f) (relating to other definitions and special rules) is amended by striking "subsections (b) and (c)" and inserting "subsection (b)".

(2) Section 219(g)(1) is amended by striking "(c)(2)" and inserting "(c)(1)(A)".

(3) Section 408(d)(5) is amended by striking "$2,250" and inserting "the dollar amount in effect under section 219(b)(1)(A)".

26 USC 219 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

CHAPTER 3—NONDISCRIMINATION PROVISIONS

SEC. 1431. DEFINITION OF HIGHLY COMPENSATED EMPLOYEES; REPEAL OF FAMILY AGGREGATION.

(a) IN GENERAL.—Paragraph (1) of section 414(q) (defining highly compensated employee) is amended to read as follows:

"(1) IN GENERAL.—The term 'highly compensated employee' means any employee who—

"(A) was a 5-percent owner at any time during the year or the preceding year, or

"(B) for the preceding year—

"(i) had compensation from the employer in excess of $80,000, and

"(ii) if the employer elects the application of this clause for such preceding year, was in the top-paid group of employees for such preceding year.

The Secretary shall adjust the $80,000 amount under subparagraph (B) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1996.".

(b) REPEAL OF FAMILY AGGREGATION RULES.—

(1) IN GENERAL.—Paragraph (6) of section 414(q) is hereby repealed.

(2) COMPENSATION LIMIT.—Paragraph (17)(A) of section 401(a) is amended by striking the last sentence.

(3) DEDUCTION.—Subsection (l) of section 404 is amended by striking the last sentence.

(c) CONFORMING AMENDMENTS.—

(1)(A) Subsection (q) of section 414 is amended by striking paragraphs (2), (5), and (12) and by redesignating paragraphs (3), (4), (7), (8), (9), (10), and (11) as paragraphs (2) through (8), respectively.

(B) Sections 129(d)(8)(B), 401(a)(5)(D)(ii), 408(k)(2)(C), and 416(i)(1)(D) are each amended by striking "section 414(q)(7)" and inserting "section 414(q)(4)".

(C) Section 416(i)(1)(A) is amended by striking "section 414(q)(8)" and inserting "section 414(q)(5)".

(D) Subparagraph (A) of section 414(r)(2) is amended by striking "subsection (q)(8)" and inserting "subsection (q)(5)".

(E) Section 414(q)(5), as redesignated by subparagraph (A), is amended by striking "under paragraph (4), or the number of officers taken into account under paragraph (5)".

(2) Section 1114(c)(4) of the Tax Reform Act of 1986 is amended by adding at the end the following new sentence: "Any reference in this paragraph to section 414(q) shall be treated as a reference to such section as in effect on the day before the date of the enactment of the Small Business Job Protection Act of 1996.". 26 USC 414 note.

(d) EFFECTIVE DATE.— 26 USC 414 note.

(1) IN GENERAL.—The amendments made by this section shall apply to years beginning after December 31, 1996, except that in determining whether an employee is a highly compensated employee for years beginning in 1997, such amendments shall be treated as having been in effect for years beginning in 1996.

(2) FAMILY AGGREGATION.—The amendments made by subsection (b) shall apply to years beginning after December 31, 1996.

SEC. 1432. MODIFICATION OF ADDITIONAL PARTICIPATION REQUIREMENTS.

(a) GENERAL RULE.—Section 401(a)(26)(A) (relating to additional participation requirements) is amended to read as follows:

"(A) IN GENERAL.—In the case of a trust which is a part of a defined benefit plan, such trust shall not constitute a qualified trust under this subsection unless on

each day of the plan year such trust benefits at least the lesser of—

"(i) 50 employees of the employer, or

"(ii) the greater of—

"(I) 40 percent of all employees of the employer, or

"(II) 2 employees (or if there is only 1 employee, such employee).".

(b) SEPARATE LINE OF BUSINESS TEST.—Section 401(a)(26)(G) (relating to separate line of business) is amended by striking "paragraph (7)" and inserting "paragraph (2)(A) or (7)".

26 USC 401 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1996.

SEC. 1433. NONDISCRIMINATION RULES FOR QUALIFIED CASH OR DEFERRED ARRANGEMENTS AND MATCHING CONTRIBUTIONS.

(a) ALTERNATIVE METHODS OF SATISFYING SECTION 401(k) NONDISCRIMINATION TESTS.—Section 401(k) (relating to cash or deferred arrangements), as amended by section 1422, is amended by adding at the end the following new paragraph:

"(12) ALTERNATIVE METHODS OF MEETING NONDISCRIMINATION REQUIREMENTS.—

"(A) IN GENERAL.—A cash or deferred arrangement shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement—

"(i) meets the contribution requirements of subparagraph (B) or (C), and

"(ii) meets the notice requirements of subparagraph (D).

"(B) MATCHING CONTRIBUTIONS.—

"(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement, the employer makes matching contributions on behalf of each employee who is not a highly compensated employee in an amount equal to—

"(I) 100 percent of the elective contributions of the employee to the extent such elective contributions do not exceed 3 percent of the employee's compensation, and

"(II) 50 percent of the elective contributions of the employee to the extent that such elective contributions exceed 3 percent but do not exceed 5 percent of the employee's compensation.

"(ii) RATE FOR HIGHLY COMPENSATED EMPLOYEES.—The requirements of this subparagraph are not met if, under the arrangement, the rate of matching contribution with respect to any elective contribution of a highly compensated employee at any rate of elective contribution is greater than that with respect to an employee who is not a highly compensated employee.

"(iii) ALTERNATIVE PLAN DESIGNS.—If the rate of any matching contribution with respect to any rate of elective contribution is not equal to the percentage required under clause (i), an arrangement shall not be treated as failing to meet the requirements of clause (i) if—

"(I) the rate of an employer's matching contribution does not increase as an employee's rate of elective contributions increase, and

"(II) the aggregate amount of matching contributions at such rate of elective contribution is at least equal to the aggregate amount of matching contributions which would be made if matching contributions were made on the basis of the percentages described in clause (i).

"(C) NONELECTIVE CONTRIBUTIONS.—The requirements of this subparagraph are met if, under the arrangement, the employer is required, without regard to whether the employee makes an elective contribution or employee contribution, to make a contribution to a defined contribution plan on behalf of each employee who is not a highly compensated employee and who is eligible to participate in the arrangement in an amount equal to at least 3 percent of the employee's compensation.

"(D) NOTICE REQUIREMENT.—An arrangement meets the requirements of this paragraph if, under the arrangement, each employee eligible to participate is, within a reasonable period before any year, given written notice of the employee's rights and obligations under the arrangement which—

"(i) is sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and

"(ii) is written in a manner calculated to be understood by the average employee eligible to participate.

"(E) OTHER REQUIREMENTS.—

"(i) WITHDRAWAL AND VESTING RESTRICTIONS.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) of this paragraph unless the requirements of subparagraphs (B) and (C) of paragraph (2) are met with respect to all employer contributions (including matching contributions) taken into account in determining whether the requirements of subparagraphs (B) and (C) of this paragraph are met.

"(ii) SOCIAL SECURITY AND SIMILAR CONTRIBUTIONS NOT TAKEN INTO ACCOUNT.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) unless such requirements are met without regard to subsection (l), and, for purposes of subsection (l), employer contributions under subparagraph (B) or (C) shall not be taken into account.

"(F) OTHER PLANS.—An arrangement shall be treated as meeting the requirements under subparagraph (A)(i) if any other plan maintained by the employer meets such requirements with respect to employees eligible under the arrangement.".

(b) ALTERNATIVE METHODS OF SATISFYING SECTION 401(m) NONDISCRIMINATION TESTS.—Section 401(m) (relating to nondiscrimination test for matching contributions and employee contributions), as amended by section 1422(b), is amended by redesignating paragraph (11) as paragraph (12) and by adding after paragraph (10) the following new paragraph:

"(11) ALTERNATIVE METHOD OF SATISFYING TESTS.—

"(A) IN GENERAL.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

"(i) meets the contribution requirements of subparagraph (B) or (C) of subsection (k)(12),

"(ii) meets the notice requirements of subsection (k)(12)(D), and

"(iii) meets the requirements of subparagraph (B).

"(B) LIMITATION ON MATCHING CONTRIBUTIONS.—The requirements of this subparagraph are met if—

"(i) matching contributions on behalf of any employee may not be made with respect to an employee's contributions or elective deferrals in excess of 6 percent of the employee's compensation,

"(ii) the rate of an employer's matching contribution does not increase as the rate of an employee's contributions or elective deferrals increase, and

"(iii) the matching contribution with respect to any highly compensated employee at any rate of an employee contribution or rate of elective deferral is not greater than that with respect to an employee who is not a highly compensated employee.".

(c) YEAR FOR COMPUTING NONHIGHLY COMPENSATED EMPLOYEE PERCENTAGE.—

(1) CASH OR DEFERRED ARRANGEMENTS.—Section 401(k)(3)(A) is amended—

(A) by striking "such year" in clause (ii) and inserting "the plan year",

(B) by striking "for such plan year" in clause (ii) and inserting "for the preceding plan year", and

(C) by adding at the end the following new sentence: "An arrangement may apply clause (ii) by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary.".

(2) MATCHING AND EMPLOYEE CONTRIBUTIONS.—Section 401(m)(2)(A) is amended—

(A) by inserting "for such plan year" after "highly compensated employees",

(B) by inserting "for the preceding plan year" after "eligible employees" each place it appears in clause (i) and clause (ii), and

(C) by adding at the end the following flush sentence: "This subparagraph may be applied by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary.".

(d) SPECIAL RULE FOR DETERMINING AVERAGE DEFERRAL PERCENTAGE FOR FIRST PLAN YEAR, ETC.—

(1) Paragraph (3) of section 401(k) is amended by adding at the end the following new subparagraph:

"(E) For purposes of this paragraph, in the case of the first plan year of any plan (other than a successor plan), the amount taken into account as the actual deferral percentage of nonhighly compensated employees for the preceding plan year shall be—

"(i) 3 percent, or

"(ii) if the employer makes an election under this subclause, the actual deferral percentage of nonhighly compensated employees determined for such first plan year.".

(2) Paragraph (3) of section 401(m) is amended by adding at the end the following: "Rules similar to the rules of subsection (k)(3)(E) shall apply for purposes of this subsection.".

(e) DISTRIBUTION OF EXCESS CONTRIBUTIONS AND EXCESS AGGREGATE CONTRIBUTIONS.—

(1) Subparagraph (C) of section 401(k)(8) (relating to arrangement not disqualified if excess contributions distributed) is amended by striking "on the basis of the respective portions of the excess contributions attributable to each of such employees" and inserting "on the basis of the amount of contributions by, or on behalf of, each of such employees".

(2) Subparagraph (C) of section 401(m)(6) (relating to method of distributing excess aggregate contributions) is amended by striking "on the basis of the respective portions of such amounts attributable to each of such employees" and inserting "on the basis of the amount of contributions on behalf of, or by, each such employee".

(f) EFFECTIVE DATES.— 26 USC 401 note.

(1) IN GENERAL.—The amendments made by this section shall apply to years beginning after December 31, 1998.

(2) EXCEPTIONS.—The amendments made by subsections (c), (d), and (e) shall apply to years beginning after December 31, 1996.

SEC. 1434. DEFINITION OF COMPENSATION FOR SECTION 415 PURPOSES.

(a) GENERAL RULE.—Section 415(c)(3) (defining participant's compensation) is amended by adding at the end the following new subparagraph:

"(D) CERTAIN DEFERRALS INCLUDED.—The term 'participant's compensation' shall include—

"(i) any elective deferral (as defined in section 402(g)(3)), and

"(ii) any amount which is contributed or deferred by the employer at the election of the employee and which is not includible in the gross income of the employee by reason of section 125 or 457.".

(b) CONFORMING AMENDMENTS.—

(1) Section 414(q)(4), as redesignated by section 1431, is amended to read as follows:

"(4) COMPENSATION.—For purposes of this subsection, the term 'compensation' has the meaning given such term by section 415(c)(3).".

(2) Section 414(s)(2) is amended by inserting "not" after "elect" in the text and heading thereof.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1997. 26 USC 414 note.

CHAPTER 4—MISCELLANEOUS PROVISIONS

SEC. 1441. PLANS COVERING SELF-EMPLOYED INDIVIDUALS.

(a) AGGREGATION RULES.—Section 401(d) (relating to additional requirements for qualification of trusts and plans benefiting owner-employees) is amended to read as follows:

"(d) CONTRIBUTION LIMIT ON OWNER-EMPLOYEES.—A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the plan provides that contributions on behalf of any owner-employee may be made only with respect to the earned income of such owner-employee which is derived from the trade or business with respect to which such plan is established.".

26 USC 401 note.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1996.

SEC. 1442. ELIMINATION OF SPECIAL VESTING RULE FOR MULTIEMPLOYER PLANS.

(a) AMENDMENTS TO 1986 CODE.—Paragraph (2) of section 411(a) (relating to minimum vesting standards) is amended—

(1) by striking "subparagraph (A), (B), or (C)" and inserting "subparagraph (A) or (B)"; and

(2) by striking subparagraph (C).

(b) AMENDMENTS TO ERISA.—Paragraph (2) of section 203(a) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1053(a)) is amended—

(1) by striking "subparagraph (A), (B), or (C)" and inserting "subparagraph (A) or (B)"; and

(2) by striking subparagraph (C).

26 USC 411 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning on or after the earlier of—

(1) the later of—

(A) January 1, 1997, or

(B) the date on which the last of the collective bargaining agreements pursuant to which the plan is maintained terminates (determined without regard to any extension thereof after the date of the enactment of this Act), or

(2) January 1, 1999.

Such amendments shall not apply to any individual who does not have more than 1 hour of service under the plan on or after the 1st day of the 1st plan year to which such amendments apply.

SEC. 1443. DISTRIBUTIONS UNDER RURAL COOPERATIVE PLANS.

(a) DISTRIBUTIONS FOR HARDSHIP OR AFTER A CERTAIN AGE.—Section 401(k)(7) is amended by adding at the end the following new subparagraph:

"(C) SPECIAL RULE FOR CERTAIN DISTRIBUTIONS.—A rural cooperative plan which includes a qualified cash or deferred arrangement shall not be treated as violating the requirements of section 401(a) or of paragraph (2) merely by reason of a hardship distribution or a distribution to a participant after attainment of age 59½. For purposes of this section, the term 'hardship distribution' means a distribution described in paragraph (2)(B)(i)(IV) (without

regard to the limitation of its application to profit-sharing or stock bonus plans).".

(b) PUBLIC UTILITY DISTRICTS.—Clause (i) of section 401(k)(7)(B) (defining rural cooperative) is amended to read as follows:

"(i) any organization which—

"(I) is engaged primarily in providing electric service on a mutual or cooperative basis, or

"(II) is engaged primarily in providing electric service to the public in its area of service and which is exempt from tax under this subtitle or which is a State or local government (or an agency or instrumentality thereof), other than a municipality (or an agency or instrumentality thereof),".

(c) EFFECTIVE DATES.— 26 USC 401 note.

(1) DISTRIBUTIONS.—The amendments made by subsection (a) shall apply to distributions after the date of the enactment of this Act.

(2) PUBLIC UTILITY DISTRICTS.—The amendments made by subsection (b) shall apply to plan years beginning after December 31, 1996.

SEC. 1444. TREATMENT OF GOVERNMENTAL PLANS UNDER SECTION 415.

(a) COMPENSATION LIMIT.—Subsection (b) of section 415 is amended by adding immediately after paragraph (10) the following new paragraph:

"(11) SPECIAL LIMITATION RULE FOR GOVERNMENTAL PLANS.—In the case of a governmental plan (as defined in section 414(d)), subparagraph (B) of paragraph (1) shall not apply.".

(b) TREATMENT OF CERTAIN EXCESS BENEFIT PLANS.—

(1) IN GENERAL.—Section 415 is amended by adding at the end the following new subsection:

"(m) TREATMENT OF QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENTS.—

"(1) GOVERNMENTAL PLAN NOT AFFECTED.—In determining whether a governmental plan (as defined in section 414(d)) meets the requirements of this section, benefits provided under a qualified governmental excess benefit arrangement shall not be taken into account. Income accruing to a governmental plan (or to a trust that is maintained solely for the purpose of providing benefits under a qualified governmental excess benefit arrangement) in respect of a qualified governmental excess benefit arrangement shall constitute income derived from the exercise of an essential governmental function upon which such governmental plan (or trust) shall be exempt from tax under section 115.

"(2) TAXATION OF PARTICIPANT.—For purposes of this chapter—

"(A) the taxable year or years for which amounts in respect of a qualified governmental excess benefit arrangement are includible in gross income by a participant, and

"(B) the treatment of such amounts when so includible by the participant,

shall be determined as if such qualified governmental excess benefit arrangement were treated as a plan for the deferral of compensation which is maintained by a corporation not

exempt from tax under this chapter and which does not meet the requirements for qualification under section 401.

"(3) QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENT.—For purposes of this subsection, the term 'qualified governmental excess benefit arrangement' means a portion of a governmental plan if—

"(A) such portion is maintained solely for the purpose of providing to participants in the plan that part of the participant's annual benefit otherwise payable under the terms of the plan that exceeds the limitations on benefits imposed by this section,

"(B) under such portion no election is provided at any time to the participant (directly or indirectly) to defer compensation, and

"(C) benefits described in subparagraph (A) are not paid from a trust forming a part of such governmental plan unless such trust is maintained solely for the purpose of providing such benefits.".

(2) COORDINATION WITH SECTION 457.—Subsection (e) of section 457 is amended by adding at the end the following new paragraph:

"(14) TREATMENT OF QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENTS.—Subsections (b)(2) and (c)(1) shall not apply to any qualified governmental excess benefit arrangement (as defined in section 415(m)(3)), and benefits provided under such an arrangement shall not be taken into account in determining whether any other plan is an eligible deferred compensation plan.".

(3) CONFORMING AMENDMENT.—Paragraph (2) of section 457(f) is amended by striking "and" at the end of subparagraph (C), by striking the period at the end of subparagraph (D) and inserting ", and", and by inserting immediately thereafter the following new subparagraph:

"(E) a qualified governmental excess benefit arrangement described in section 415(m).".

(c) EXEMPTION FOR SURVIVOR AND DISABILITY BENEFITS.—Paragraph (2) of section 415(b) is amended by adding at the end the following new subparagraph:

"(I) EXEMPTION FOR SURVIVOR AND DISABILITY BENEFITS PROVIDED UNDER GOVERNMENTAL PLANS.—Subparagraph (C) of this paragraph and paragraph (5) shall not apply to—

"(i) income received from a governmental plan (as defined in section 414(d)) as a pension, annuity, or similar allowance as the result of the recipient becoming disabled by reason of personal injuries or sickness, or

"(ii) amounts received from a governmental plan by the beneficiaries, survivors, or the estate of an employee as the result of the death of the employee.".

(d) REVOCATION OF GRANDFATHER ELECTION.—

(1) IN GENERAL.—Subparagraph (C) of section 415(b)(10) is amended by adding at the end the following new clause:

"(ii) REVOCATION OF ELECTION.—An election under clause (i) may be revoked not later than the last day of the third plan year beginning after the date of the enactment of this clause. The revocation shall

apply to all plan years to which the election applied and to all subsequent plan years. Any amount paid by a plan in a taxable year ending after the revocation shall be includible in income in such taxable year under the rules of this chapter in effect for such taxable year, except that, for purposes of applying the limitations imposed by this section, any portion of such amount which is attributable to any taxable year during which the election was in effect shall be treated as received in such taxable year.".

(2) CONFORMING AMENDMENT.—Subparagraph (C) of section 415(b)(10) is amended by striking "This" and inserting:

"(i) IN GENERAL.—This".

(e) EFFECTIVE DATE.— 26 USC 415 note.

(1) IN GENERAL.—The amendments made by subsections (a), (b), and (c) shall apply to years beginning after December 31, 1994. The amendments made by subsection (d) shall apply with respect to revocations adopted after the date of the enactment of this Act.

(2) TREATMENT FOR YEARS BEGINNING BEFORE JANUARY 1, 1995.—Nothing in the amendments made by this section shall be construed to imply that a governmental plan (as defined in section 414(d) of the Internal Revenue Code of 1986) fails to satisfy the requirements of section 415 of such Code for any taxable year beginning before January 1, 1995.

SEC. 1445. UNIFORM RETIREMENT AGE.

(a) DISCRIMINATION TESTING.—Paragraph (5) of section 401(a) (relating to special rules relating to nondiscrimination requirements) is amended by adding at the end the following new subparagraph:

"(F) SOCIAL SECURITY RETIREMENT AGE.—For purposes of testing for discrimination under paragraph (4)—

"(i) the social security retirement age (as defined in section 415(b)(8)) shall be treated as a uniform retirement age, and

"(ii) subsidized early retirement benefits and joint and survivor annuities shall not be treated as being unavailable to employees on the same terms merely because such benefits or annuities are based in whole or in part on an employee's social security retirement age (as so defined).".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to years beginning after December 31, 1996. 26 USC 401 note.

SEC. 1446. CONTRIBUTIONS ON BEHALF OF DISABLED EMPLOYEES.

(a) ALL DISABLED PARTICIPANTS RECEIVING CONTRIBUTIONS.—Section 415(c)(3)(C) is amended by adding at the end the following: "If a defined contribution plan provides for the continuation of contributions on behalf of all participants described in clause (i) for a fixed or determinable period, this subparagraph shall be applied without regard to clauses (ii) and (iii).".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to years beginning after December 31, 1996. 26 USC 415 note.

SEC. 1447. TREATMENT OF DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.

(a) SPECIAL RULES FOR PLAN DISTRIBUTIONS.—Paragraph (9) of section 457(e) (relating to other definitions and special rules) is amended to read as follows:

"(9) BENEFITS NOT TREATED AS MADE AVAILABLE BY REASON OF CERTAIN ELECTIONS, ETC.—

"(A) TOTAL AMOUNT PAYABLE IS $3,500 OR LESS.—The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to receive such amount (or the plan may distribute such amount without the participant's consent) if—

"(i) such amount does not exceed $3,500, and

"(ii) such amount may be distributed only if—

"(I) no amount has been deferred under the plan with respect to such participant during the 2-year period ending on the date of the distribution, and

"(II) there has been no prior distribution under the plan to such participant to which this subparagraph applied.

A plan shall not be treated as failing to meet the distribution requirements of subsection (d) by reason of a distribution to which this subparagraph applies.

"(B) ELECTION TO DEFER COMMENCEMENT OF DISTRIBUTIONS.—The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to defer commencement of distributions under the plan if—

"(i) such election is made after amounts may be available under the plan in accordance with subsection (d)(1)(A) and before commencement of such distributions, and

"(ii) the participant may make only 1 such election.".

(b) COST-OF-LIVING ADJUSTMENT OF MAXIMUM DEFERRAL AMOUNT.—Subsection (e) of section 457, as amended by section 1444(b)(2) (relating to governmental plans), is amended by adding at the end the following new paragraph:

"(15) COST-OF-LIVING ADJUSTMENT OF MAXIMUM DEFERRAL AMOUNT.—The Secretary shall adjust the $7,500 amount specified in subsections (b)(2) and (c)(1) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1994, and any increase under this paragraph which is not a multiple of $500 shall be rounded to the next lowest multiple of $500.".

26 USC 457 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1448. TRUST REQUIREMENT FOR DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS.

(a) IN GENERAL.—Section 457 is amended by adding at the end the following new subsection:

"(g) GOVERNMENTAL PLANS MUST MAINTAIN SET-ASIDES FOR EXCLUSIVE BENEFIT OF PARTICIPANTS.—

"(1) IN GENERAL.—A plan maintained by an eligible employer described in subsection (e)(1)(A) shall not be treated as an eligible deferred compensation plan unless all assets and income of the plan described in subsection (b)(6) are held in trust for the exclusive benefit of participants and their beneficiaries.

"(2) TAXABILITY OF TRUSTS AND PARTICIPANTS.—For purposes of this title—

"(A) a trust described in paragraph (1) shall be treated as an organization exempt from taxation under section 501(a), and

"(B) notwithstanding any other provision of this title, amounts in the trust shall be includible in the gross income of participants and beneficiaries only to the extent, and at the time, provided in this section.

"(3) CUSTODIAL ACCOUNTS AND CONTRACTS.—For purposes of this subsection, custodial accounts and contracts described in section 401(f) shall be treated as trusts under rules similar to the rules under section 401(f).".

(b) CONFORMING AMENDMENT.—Paragraph (6) of section 457(b) is amended by inserting "except as provided in subsection (g)," before "which provides that".

(c) EFFECTIVE DATES.— 26 USC 457 note.

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to assets and income described in section 457(b)(6) of the Internal Revenue Code of 1986 held by a plan on and after the date of the enactment of this Act.

(2) TRANSITION RULE.—In the case of a plan in existence on the date of the enactment of this Act, a trust need not be established by reason of the amendments made by this section before January 1, 1999.

SEC. 1449. TRANSITION RULE FOR COMPUTING MAXIMUM BENEFITS UNDER SECTION 415 LIMITATIONS.

(a) IN GENERAL.—Subparagraph (A) of section 767(d)(3) of the Uruguay Round Agreements Act is amended to read as follows: 26 USC 411 note.

"(A) EXCEPTION.—A plan that was adopted and in effect before December 8, 1994, shall not be required to apply the amendments made by subsection (b) with respect to benefits accrued before the earlier of—

"(i) the later of the date a plan amendment applying the amendments made by subsection (b) is adopted or made effective, or

"(ii) the first day of the first limitation year beginning after December 31, 1999.

Determinations under section 415(b)(2)(E) of the Internal Revenue Code of 1986 before such earlier date shall be made with respect to such benefits on the basis of such section as in effect on December 7, 1994 (except that the modification made by section 1449(b) of the Small Business Job Protection Act of 1996 shall be taken into account), and the provisions of the plan as in effect on December 7, 1994, but only if such provisions of the plan meet the requirements of such section (as so in effect).".

(b) MODIFICATION OF CERTAIN ASSUMPTIONS FOR ADJUSTING BENEFITS OF DEFINED BENEFIT PLANS FOR EARLY RETIREES.—Subparagraph (E) of section 415(b)(2) (relating to limitation on certain assumptions) is amended—

(1) by striking "Except as provided in clause (ii), for purposes of adjusting any benefit or limitation under subparagraph (B) or (C)," in clause (i) and inserting "For purposes of adjusting any limitation under subparagraph (C) and, except as provided in clause (ii), for purposes of adjusting any benefit under subparagraph (B),", and

(2) by striking "For purposes of adjusting the benefit or limitation of any form of benefit subject to section 417(e)(3)," in clause (ii) and inserting "For purposes of adjusting any benefit under subparagraph (B) for any form of benefit subject to section 417(e)(3),".

26 USC 415 note. (c) EFFECTIVE DATE.—The amendments made by this section shall take effect as if included in the provisions of section 767 of the Uruguay Round Agreements Act.

26 USC 411 note. (d) TRANSITIONAL RULE.—In the case of a plan that was adopted and in effect before December 8, 1994, if—

(1) a plan amendment was adopted or made effective on or before the date of the enactment of this Act applying the amendments made by section 767 of the Uruguay Round Agreements Act, and

(2) within 1 year after the date of the enactment of this Act, a plan amendment is adopted which repeals the amendment referred to in paragraph (1),

the amendment referred to in paragraph (1) shall not be taken into account in applying section 767(d)(3)(A) of the Uruguay Round Agreements Act, as amended by subsection (a).

SEC. 1450. MODIFICATIONS OF SECTION 403(b).

26 USC 403 note. (a) MULTIPLE SALARY REDUCTION AGREEMENTS PERMITTED.—

(1) GENERAL RULE.—For purposes of section 403(b) of the Internal Revenue Code of 1986, the frequency that an employee is permitted to enter into a salary reduction agreement, the salary to which such an agreement may apply, and the ability to revoke such an agreement shall be determined under the rules applicable to cash or deferred elections under section 401(k) of such Code.

(2) CONSTRUCTIVE RECEIPT.—Section 402(e)(3) is amended by inserting "or which is part of a salary reduction agreement under section 403(b)" after "section 401(k)(2))".

(3) EFFECTIVE DATE.—This subsection shall apply to taxable years beginning after December 31, 1995.

(b) TREATMENT OF INDIAN TRIBAL GOVERNMENTS.—

(1) IN GENERAL.—In the case of any contract purchased in a plan year beginning before January 1, 1995, section 403(b) of the Internal Revenue Code of 1986 shall be applied as if any reference to an employer described in section 501(c)(3) of the Internal Revenue Code of 1986 which is exempt from tax under section 501 of such Code included a reference to an employer which is an Indian tribal government (as defined by section 7701(a)(40) of such Code), a subdivision of an Indian tribal government (determined in accordance with section 7871(d) of such Code), an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corpora-

tion chartered under Federal, State, or tribal law which is owned in whole or in part by any of the foregoing.

(2) ROLLOVERS.—Solely for purposes of applying section 403(b)(8) of such Code to a contract to which paragraph (1) applies, a qualified cash or deferred arrangement under section 401(k) of such Code shall be treated as if it were a plan or contract described in clause (ii) of section 403(b)(8)(A) of such Code.

(c) ELECTIVE DEFERRALS.—

(1) IN GENERAL.—Subparagraph (E) of section 403(b)(1) is amended to read as follows:

"(E) in the case of a contract purchased under a salary reduction agreement, the contract meets the requirements of section 401(a)(30),".

(2) EFFECTIVE DATE.—The amendment made by this subsection shall apply to years beginning after December 31, 1995, except a contract shall not be required to meet any change in any requirement by reason of such amendment before the 90th day after the date of the enactment of this Act. 26 USC 403 note.

SEC. 1451. SPECIAL RULES RELATING TO JOINT AND SURVIVOR ANNUITY EXPLANATIONS.

(a) AMENDMENT TO INTERNAL REVENUE CODE.—Section 417(a) is amended by adding at the end the following new paragraph:

"(7) SPECIAL RULES RELATING TO TIME FOR WRITTEN EXPLANATION.—Notwithstanding any other provision of this subsection—

"(A) EXPLANATION MAY BE PROVIDED AFTER ANNUITY STARTING DATE.—

"(i) IN GENERAL.—A plan may provide the written explanation described in paragraph (3)(A) after the annuity starting date. In any case to which this subparagraph applies, the applicable election period under paragraph (6) shall not end before the 30th day after the date on which such explanation is provided.

"(ii) REGULATORY AUTHORITY.—The Secretary may by regulations limit the application of clause (i), except that such regulations may not limit the period of time by which the annuity starting date precedes the provision of the written explanation other than by providing that the annuity starting date may not be earlier than termination of employment.

"(B) WAIVER OF 30-DAY PERIOD.—A plan may permit a participant to elect (with any applicable spousal consent) to waive any requirement that the written explanation be provided at least 30 days before the annuity starting date (or to waive the 30-day requirement under subparagraph (A)) if the distribution commences more than 7 days after such explanation is provided.".

(b) AMENDMENT TO ERISA.—Section 205(c) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1055(c)) is amended by adding at the end the following new paragraph:

"(8) Notwithstanding any other provision of this subsection—

"(A)(i) A plan may provide the written explanation described in paragraph (3)(A) after the annuity starting

date. In any case to which this subparagraph applies, the applicable election period under paragraph (7) shall not end before the 30th day after the date on which such explanation is provided.

"(ii) The Secretary may by regulations limit the application of clause (i), except that such regulations may not limit the period of time by which the annuity starting date precedes the provision of the written explanation other than by providing that the annuity starting date may not be earlier than termination of employment.

"(B) A plan may permit a participant to elect (with any applicable spousal consent) to waive any requirement that the written explanation be provided at least 30 days before the annuity starting date (or to waive the 30-day requirement under subparagraph (A)) if the distribution commences more than 7 days after such explanation is provided.".

26 USC 417 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning after December 31, 1996.

SEC. 1452. REPEAL OF LIMITATION IN CASE OF DEFINED BENEFIT PLAN AND DEFINED CONTRIBUTION PLAN FOR SAME EMPLOYEE; EXCESS DISTRIBUTIONS.

(a) IN GENERAL.—Section 415(e) is repealed.

(b) EXCESS DISTRIBUTIONS.—Section 4980A is amended by adding at the end the following new subsection:

"(g) LIMITATION ON APPLICATION.—This section shall not apply to distributions during years beginning after December 31, 1996, and before January 1, 2000, and such distributions shall be treated as made first from amounts not described in subsection (f).".

(c) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 415(a) is amended—

(A) by adding "or" at the end of subparagraph (A),

(B) by striking ", or" at the end of subparagraph (B) and inserting a period, and

(C) by striking subparagraph (C).

(2) Subparagraph (B) of section 415(b)(5) is amended by striking "and subsection (e)".

(3) Paragraph (1) of section 415(f) is amended by striking "subsections (b), (c), and (e)" and inserting "subsections (b) and (c)".

(4) Subsection (g) of section 415 is amended by striking "subsections (e) and (f)" in the last sentence and inserting "subsection (f)".

(5) Clause (i) of section 415(k)(2)(A) is amended to read as follows:

"(i) any contribution made directly by an employee under such an arrangement shall not be treated as an annual addition for purposes of subsection (c), and".

(6) Clause (ii) of section 415(k)(2)(A) is amended by striking "subsections (c) and (e)" and inserting "subsection (c)".

(7) Section 416 is amended by striking subsection (h).

26 USC 415 note.

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to limitation years beginning after December 31, 1999.

(2) EXCESS DISTRIBUTIONS.—The amendment made by subsection (b) shall apply to years beginning after December 31, 1996.

SEC. 1453. TAX ON PROHIBITED TRANSACTIONS.

(a) IN GENERAL.—Section 4975(a) is amended by striking "5 percent" and inserting "10 percent".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to prohibited transactions occurring after the date of the enactment of this Act. 26 USC 4975 note.

SEC. 1454. TREATMENT OF LEASED EMPLOYEES.

(a) GENERAL RULE.—Subparagraph (C) of section 414(n)(2) (defining leased employee) is amended to read as follows:

"(C) such services are performed under primary direction or control by the recipient.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to years beginning after December 31, 1996, but shall not apply to any relationship determined under an Internal Revenue Service ruling issued before the date of the enactment of this Act pursuant to section 414(n)(2)(C) of the Internal Revenue Code of 1986 (as in effect on the day before such date) not to involve a leased employee. 26 USC 414 note.

SEC. 1455. UNIFORM PENALTY PROVISIONS TO APPLY TO CERTAIN PENSION REPORTING REQUIREMENTS.

(a) PENALTIES.—

(1) STATEMENTS.—Paragraph (1) of section 6724(d) is amended by striking "and" at the end of subparagraph (A), by striking the period at the end of subparagraph (B) and inserting ", and", and by inserting after subparagraph (B) the following new subparagraph:

"(C) any statement of the amount of payments to another person required to be made to the Secretary under—

"(i) section 408(i) (relating to reports with respect to individual retirement accounts or annuities), or

"(ii) section 6047(d) (relating to reports by employers, plan administrators, etc.).".

(2) REPORTS.—Paragraph (2) of section 6724(d) is amended by striking "or" at the end of subparagraph (U), by striking the period at the end of subparagraph (V) and inserting a comma, and by inserting after subparagraph (V) the following new subparagraphs:

"(W) section 408(i) (relating to reports with respect to individual retirement plans) to any person other than the Secretary with respect to the amount of payments made to such person, or

"(X) section 6047(d) (relating to reports by plan administrators) to any person other than the Secretary with respect to the amount of payments made to such person.".

(b) MODIFICATION OF REPORTABLE DESIGNATED DISTRIBUTIONS.—

(1) SECTION 408.—Subsection (i) of section 408 (relating to individual retirement account reports) is amended by inserting "aggregating $10 or more in any calendar year" after "distributions".

(2) SECTION 6047.—Paragraph (1) of section 6047(d) (relating to reports by employers, plan administrators, etc.) is amended by adding at the end the following new sentence: "No return or report may be required under the preceding sentence with respect to distributions to any person during any year unless such distributions aggregate $10 or more.".

(c) QUALIFYING ROLLOVER DISTRIBUTIONS.—Section 6652(i) is amended—

(1) by striking "the $10" and inserting "$100", and

(2) by striking "$5,000" and inserting "$50,000".

(d) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 6047(f) is amended to read as follows:

"(1) For provisions relating to penalties for failures to file returns and reports required under this section, see sections 6652(e), 6721, and 6722.".

(2) Subsection (e) of section 6652 is amended by adding at the end the following new sentence: "This subsection shall not apply to any return or statement which is an information return described in section 6724(d)(1)(C)(ii) or a payee statement described in section 6724(d)(2)(X).".

(3) Subsection (a) of section 6693 is amended by adding at the end the following new sentence: "This subsection shall not apply to any report which is an information return described in section 6724(d)(1)(C)(i) or a payee statement described in section 6724(d)(2)(W).".

26 USC 408 note.

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to returns, reports, and other statements the due date for which (determined without regard to extensions) is after December 31, 1996.

SEC. 1456. RETIREMENT BENEFITS OF MINISTERS NOT SUBJECT TO TAX ON NET EARNINGS FROM SELF-EMPLOYMENT.

(a) IN GENERAL.—Section 1402(a)(8) (defining net earnings from self-employment) is amended by inserting ", but shall not include in such net earnings from self-employment the rental value of any parsonage or any parsonage allowance (whether or not excludable under section 107) provided after the individual retires, or any other retirement benefit received by such individual from a church plan (as defined in section 414(e)) after the individual retires" before the semicolon at the end.

26 USC 1402 note.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning before, on, or after December 31, 1994.

26 USC 414 note.

SEC. 1457. SAMPLE LANGUAGE FOR SPOUSAL CONSENT AND QUALIFIED DOMESTIC RELATIONS FORMS.

(a) DEVELOPMENT OF SAMPLE LANGUAGE.—Not later than January 1, 1997, the Secretary of the Treasury shall develop—

(1) sample language for inclusion in a form for the spousal consent required under section 417(a)(2) of the Internal Revenue Code of 1986 and section 205(c)(2) of the Employee Retirement Income Security Act of 1974 which—

(A) is written in a manner calculated to be understood by the average person, and

(B) discloses in plain form—

(i) whether the waiver to which the spouse consents is irrevocable, and

(ii) whether such waiver may be revoked by a qualified domestic relations order, and

(2) sample language for inclusion in a form for a qualified domestic relations order described in section 414(p)(1)(A) of such Code and section 206(d)(3)(B)(i) of such Act which—

(A) meets the requirements contained in such sections, and

(B) the provisions of which focus attention on the need to consider the treatment of any lump sum payment, qualified joint and survivor annuity, or qualified preretirement survivor annuity.

(b) PUBLICITY.—The Secretary of the Treasury shall include publicity for the sample language developed under subsection (a) in the pension outreach efforts undertaken by the Secretary.

SEC. 1458. TREATMENT OF LENGTH OF SERVICE AWARDS TO VOLUNTEERS PERFORMING FIRE FIGHTING OR PREVENTION SERVICES, EMERGENCY MEDICAL SERVICES, OR AMBULANCE SERVICES.

(a) IN GENERAL.—Paragraph (11) of section 457(e) (relating to deferred compensation plans of State and local governments and tax-exempt organizations) is amended to read as follows:

"(11) CERTAIN PLANS EXCLUDED.—

"(A) IN GENERAL.—The following plans shall be treated as not providing for the deferral of compensation:

"(i) Any bona fide vacation leave, sick leave, compensatory time, severance pay, disability pay, or death benefit plan.

"(ii) Any plan paying solely length of service awards to bona fide volunteers (or their beneficiaries) on account of qualified services performed by such volunteers.

"(B) SPECIAL RULES APPLICABLE TO LENGTH OF SERVICE AWARD PLANS.—

"(i) BONA FIDE VOLUNTEER.—An individual shall be treated as a bona fide volunteer for purposes of subparagraph (A)(ii) if the only compensation received by such individual for performing qualified services is in the form of—

"(I) reimbursement for (or a reasonable allowance for) reasonable expenses incurred in the performance of such services, or

"(II) reasonable benefits (including length of service awards), and nominal fees for such services, customarily paid by eligible employers in connection with the performance of such services by volunteers.

"(ii) LIMITATION ON ACCRUALS.—A plan shall not be treated as described in subparagraph (A)(ii) if the aggregate amount of length of service awards accruing with respect to any year of service for any bona fide volunteer exceeds $3,000.

"(C) QUALIFIED SERVICES.—For purposes of this paragraph, the term 'qualified services' means fire fighting and prevention services, emergency medical services, and ambulance services.".

(b) EXEMPTION FROM SOCIAL SECURITY TAXES.—

(1) Subsection (a)(5) of section 3121, as amended by section 1421, is amended by striking "(or)" at the end of subparagraph (G), by inserting "or" at the end of subparagraph (H), and by adding at the end the following new subparagraph:

"(I) under a plan described in section 457(e)(11)(A)(ii) and maintained by an eligible employer (as defined in section 457(e)(1)).".

42 USC 409.

(2) Section 209(a)(4) of the Social Security Act is amended by inserting "; or (K) under a plan described in section 457(e)(11)(A)(ii) of the Internal Revenue Code of 1986 and maintained by an eligible employer (as defined in section 457(e)(1) of such Code)" before the semicolon at the end thereof.

(c) EFFECTIVE DATE.—

26 USC 457 note.

(1) SUBSECTION (a).—The amendment made by subsection (a) shall apply to accruals of length of service awards after December 31, 1996.

26 USC 3121 note.

(2) SUBSECTION (b).—The amendments made by subsection (b) shall apply to remuneration paid after December 31, 1996.

SEC. 1459. ALTERNATIVE NONDISCRIMINATION RULES FOR CERTAIN PLANS THAT PROVIDE FOR EARLY PARTICIPATION.

(a) CASH OR DEFERRED ARRANGEMENTS.—Paragraph (3) of section 401(k) (relating to application of participation and discrimination standards), as amended by section 1433(d)(1) of this Act, is amended by adding at the end the following new subparagraph:

"(F) SPECIAL RULE FOR EARLY PARTICIPATION.—If an employer elects to apply section 410(b)(4)(B) in determining whether a cash or deferred arrangement meets the requirements of subparagraph (A)(i), the employer may, in determining whether the arrangement meets the requirements of subparagraph (A)(ii), exclude from consideration all eligible employees (other than highly compensated employees) who have not met the minimum age and service requirements of section 410(a)(1)(A).".

(b) MATCHING CONTRIBUTIONS.—Paragraph (5) of section 401(m) (relating to employees taken into consideration) is amended by adding at the end the following new subparagraph:

"(C) SPECIAL RULE FOR EARLY PARTICIPATION.—If an employer elects to apply section 410(b)(4)(B) in determining whether a plan meets the requirements of section 410(b), the employer may, in determining whether the plan meets the requirements of paragraph (2), exclude from consideration all eligible employees (other than highly compensated employees) who have not met the minimum age and service requirements of section 410(a)(1)(A).".

26 USC 401 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning after December 31, 1998.

SEC. 1460. CLARIFICATION OF APPLICATION OF ERISA TO INSURANCE COMPANY GENERAL ACCOUNTS.

(a) IN GENERAL.—Section 401 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1101) is amended by adding at the end the following new subsection:

Proposed regulations.

"(c)(1)(A) Not later than June 30, 1997, the Secretary shall issue proposed regulations to provide guidance for the purpose of determining, in cases where an insurer issues 1 or more policies to or for the benefit of an employee benefit plan (and such policies are supported by assets of such insurer's general account), which

assets held by the insurer (other than plan assets held in its separate accounts) constitute assets of the plan for purposes of this part and section 4975 of the Internal Revenue Code of 1986 and to provide guidance with respect to the application of this title to the general account assets of insurers.

"(B) The proposed regulations under subparagraph (A) shall be subject to public notice and comment until September 30, 1997.

"(C) The Secretary shall issue final regulations providing the guidance described in subparagraph (A) not later than December 31, 1997. Regulations.

"(D) Such regulations shall only apply with respect to policies which are issued by an insurer on or before December 31, 1998, to or for the benefit of an employee benefit plan which is supported by assets of such insurer's general account. With respect to policies issued on or before December 31, 1998, such regulations shall take effect at the end of the 18-month period following the date on which such regulations become final.

"(2) The Secretary shall ensure that the regulations issued under paragraph (1)—

"(A) are administratively feasible, and

"(B) protect the interests and rights of the plan and of its participants and beneficiaries (including meeting the requirements of paragraph (3)).

"(3) The regulations prescribed by the Secretary pursuant to paragraph (1) shall require, in connection with any policy issued by an insurer to or for the benefit of an employee benefit plan to the extent that the policy is not a guaranteed benefit policy (as defined in subsection (b)(2)(B))—

"(A) that a plan fiduciary totally independent of the insurer authorize the purchase of such policy (unless such purchase is a transaction exempt under section 408(b)(5)),

"(B) that the insurer describe (in such form and manner as shall be prescribed in such regulations), in annual reports and in policies issued to the policyholder after the date on which such regulations are issued in final form pursuant to paragraph (1)(C)—

"(i) a description of the method by which any income and expenses of the insurer's general account are allocated to the policy during the term of the policy and upon the termination of the policy, and

"(ii) for each report, the actual return to the plan under the policy and such other financial information as the Secretary may deem appropriate for the period covered by each such annual report,

"(C) that the insurer disclose to the plan fiduciary the extent to which alternative arrangements supported by assets of separate accounts of the insurer (which generally hold plan assets) are available, whether there is a right under the policy to transfer funds to a separate account and the terms governing any such right, and the extent to which support by assets of the insurer's general account and support by assets of separate accounts of the insurer might pose differing risks to the plan, and

"(D) that the insurer manage those assets of the insurer which are assets of such insurer's general account (irrespective of whether any such assets are plan assets) with the care, skill, prudence, and diligence under the circumstances then

prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, taking into account all obligations supported by such enterprise.

"(4) Compliance by the insurer with all requirements of the regulations issued by the Secretary pursuant to paragraph (1) shall be deemed compliance by such insurer with sections 404, 406, and 407 with respect to those assets of the insurer's general account which support a policy described in paragraph (3).

"(5)(A) Subject to subparagraph (B), any regulations issued under paragraph (1) shall not take effect before the date on which such regulations become final.

"(B) No person shall be subject to liability under this part or section 4975 of the Internal Revenue Code of 1986 for conduct which occurred before the date which is 18 months following the date described in subparagraph (A) on the basis of a claim that the assets of an insurer (other than plan assets held in a separate account) constitute assets of the plan, except—

"(i) as otherwise provided by the Secretary in regulations intended to prevent avoidance of the regulations issued under paragraph (1), or

"(ii) as provided in an action brought by the Secretary pursuant to paragraph (2) or (5) of section 502(a) for a breach of fiduciary responsibilities which would also constitute a violation of Federal or State criminal law.

The Secretary shall bring a cause of action described in clause (ii) if a participant, beneficiary, or fiduciary demonstrates to the satisfaction of the Secretary that a breach described in clause (ii) has occurred.

"(6) Nothing in this subsection shall preclude the application of any Federal criminal law.

"(7) For purposes of this subsection, the term 'policy' includes a contract.".

29 USC 1101 note.

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendment made by this section shall take effect on January 1, 1975.

(2) CIVIL ACTIONS.—The amendment made by this section shall not apply to any civil action commenced before November 7, 1995.

SEC. 1461. SPECIAL RULES FOR CHAPLAINS AND SELF-EMPLOYED MINISTERS.

(a) IN GENERAL.—Section 414(e) (defining church plan) is amended by adding at the end the following new paragraph:

"(5) SPECIAL RULES FOR CHAPLAINS AND SELF-EMPLOYED MINISTERS.—

"(A) CERTAIN MINISTERS MAY PARTICIPATE.—For purposes of this part—

"(i) IN GENERAL.—An employee of a church or a convention or association of churches shall include a duly ordained, commissioned, or licensed minister of a church who, in connection with the exercise of his or her ministry—

"(I) is a self-employed individual (within the meaning of section 401(c)(1)(B)), or

"(II) is employed by an organization other than an organization described in section 501(c)(3).

"(ii) TREATMENT AS EMPLOYER AND EMPLOYEE.—

"(I) SELF-EMPLOYED.—A minister described in clause (i)(I) shall be treated as his or her own employer which is an organization described in section 501(c)(3) and which is exempt from tax under section 501(a).

"(II) OTHERS.—A minister described in clause (i)(II) shall be treated as employed by an organization described in section 501(c)(3) and exempt from tax under section 501(a).

"(B) SPECIAL RULES FOR APPLYING SECTION 403(b) TO SELF-EMPLOYED MINISTERS.—In the case of a minister described in subparagraph (A)(i)(I)—

"(i) the minister's includible compensation under section 403(b)(3) shall be determined by reference to the minister's earned income (within the meaning of section 401(c)(2)) from such ministry rather than the amount of compensation which is received from an employer, and

"(ii) the years (and portions of years) in which such minister was a self-employed individual (within the meaning of section 401(c)(1)(B)) with respect to such ministry shall be included for purposes of section 403(b)(4).

"(C) EFFECT ON NON-DENOMINATIONAL PLANS.—If a duly ordained, commissioned, or licensed minister of a church in the exercise of his or her ministry participates in a church plan (within the meaning of this section) and in the exercise of such ministry is employed by an employer not eligible to participate in such church plan, then such employer may exclude such minister from being treated as an employee of such employer for purposes of applying sections 401(a)(3), 401(a)(4), and 401(a)(5), as in effect on September 1, 1974, and sections 401(a)(4), 401(a)(5), 401(a)(26), 401(k)(3), 401(m), 403(b)(1)(D) (including section 403(b)(12)), and 410 to any stock bonus, pension, profit-sharing, or annuity plan (including an annuity described in section 403(b) or a retirement income account described in section 403(b)(9)). The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purpose of, and prevent the abuse of, this subparagraph. Regulations.

"(D) COMPENSATION TAKEN INTO ACCOUNT ONLY ONCE.—If any compensation is taken into account in determining the amount of any contributions made to, or benefits to be provided under, any church plan, such compensation shall not also be taken into account in determining the amount of any contributions made to, or benefits to be provided under, any other stock bonus, pension, profit-sharing, or annuity plan which is not a church plan.".

(b) CONTRIBUTIONS BY CERTAIN MINISTERS TO RETIREMENT INCOME ACCOUNTS.—Section 404(a) (relating to deduction for contributions of an employer to an employees' trust or annuity plan and compensation under a deferred-payment plan) is amended by adding at the end the following new paragraph:

"(10) CONTRIBUTIONS BY CERTAIN MINISTERS TO RETIREMENT INCOME ACCOUNTS.—In the case of contributions made by a minister described in section 414(e)(5) to a retirement income account described in section 403(b)(9) and not by a person other than such minister, such contributions—

"(A) shall be treated as made to a trust which is exempt from tax under section 501(a) and which is part of a plan which is described in section 401(a), and

"(B) shall be deductible under this subsection to the extent such contributions do not exceed the limit on elective deferrals under section 402(g), the exclusion allowance under section 403(b)(2), or the limit on annual additions under section 415.

For purposes of this paragraph, all plans in which the minister is a participant shall be treated as one plan.".

26 USC 404 note. (c) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1996.

SEC. 1462. DEFINITION OF HIGHLY COMPENSATED EMPLOYEE FOR PRE-ERISA RULES FOR CHURCH PLANS.

(a) IN GENERAL.—Section 414(q) (defining highly compensated employee), as amended by section 1431(c)(1)(A) of this Act, is amended by adding at the end the following new paragraph:

"(7) CERTAIN EMPLOYEES NOT CONSIDERED HIGHLY COMPENSATED AND EXCLUDED EMPLOYEES UNDER PRE-ERISA RULES FOR CHURCH PLANS.—In the case of a church plan (as defined in subsection (e)), no employee shall be considered an officer, a person whose principal duties consist of supervising the work of other employees, or a highly compensated employee for any year unless such employee is a highly compensated employee under paragraph (1) for such year.".

26 USC 414 note. (b) SAFEHARBOR AUTHORITY.—The Secretary of the Treasury may design nondiscrimination and coverage safe harbors for church plans.

26 USC 414 note. (c) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to years beginning after December 31, 1996.

SEC. 1463. RULE RELATING TO INVESTMENT IN CONTRACT NOT TO APPLY TO FOREIGN MISSIONARIES.

(a) IN GENERAL.—The last sentence of section 72(f) is amended by inserting ", or to the extent such credits are attributable to services performed as a foreign missionary (within the meaning of section 403(b)(2)(D)(iii))" before the last period.

26 USC 72 note. (b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1464. WAIVER OF EXCISE TAX ON FAILURE TO PAY LIQUIDITY SHORTFALL.

(a) IN GENERAL.—Section 4971(f) (relating to failure to pay liquidity shortfall) is amended by adding at the end the following new paragraph:

"(4) WAIVER BY SECRETARY.—If the taxpayer establishes to the satisfaction of the Secretary that—

"(A) the liquidity shortfall described in paragraph (1) was due to reasonable cause and not willful neglect, and

"(B) reasonable steps have been taken to remedy such liquidity shortfall,

the Secretary may waive all or part of the tax imposed by this subsection.".

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect as if included in the amendment made by clause (ii) of section 751(a)(9)(B) of the Retirement Protection Act of 1994 (108 Stat. 5020). 26 USC 4971 note.

SEC. 1465. DATE FOR ADOPTION OF PLAN AMENDMENTS. 26 USC 401 note.

If any amendment made by this subtitle requires an amendment to any plan or annuity contract, such amendment shall not be required to be made before the first day of the first plan year beginning on or after January 1, 1998, if—

(1) during the period after such amendment takes effect and before such first plan year, the plan or contract is operated in accordance with the requirements of such amendment, and

(2) such amendment applies retroactively to such period.

In the case of a governmental plan (as defined in section 414(d) of the Internal Revenue Code of 1986), this section shall be applied by substituting "2000" for "1998".

Subtitle E—Foreign Simplification

SEC. 1501. REPEAL OF INCLUSION OF CERTAIN EARNINGS INVESTED IN EXCESS PASSIVE ASSETS.

(a) IN GENERAL.—

(1) REPEAL OF INCLUSION.—Paragraph (1) of section 951(a) (relating to amounts included in gross income of United States shareholders) is amended by striking subparagraph (C), by striking "; and" at the end of subparagraph (B) and inserting a period, and by adding "and" at the end of subparagraph (A).

(2) REPEAL OF INCLUSION AMOUNT.—Section 956A (relating to earnings invested in excess passive assets) is repealed.

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (G) of section 904(d)(3), as amended by section 1703(i)(1), is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(2) Paragraph (1) of section 956(b) is amended to read as follows:

"(1) APPLICABLE EARNINGS.—For purposes of this section, the term 'applicable earnings' means, with respect to any controlled foreign corporation, the sum of—

"(A) the amount (not including a deficit) referred to in section 316(a)(1), and

"(B) the amount referred to in section 316(a)(2),

but reduced by distributions made during the taxable year and by earnings and profits described in section 959(c)(1).".

(3) Paragraph (3) of section 956(b) is amended to read as follows:

"(3) SPECIAL RULE WHERE CORPORATION CEASES TO BE CONTROLLED FOREIGN CORPORATION.—If any foreign corporation ceases to be a controlled foreign corporation during any taxable year—

"(A) the determination of any United States shareholder's pro rata share shall be made on the basis of stock owned (within the meaning of section 958(a)) by such share-

holder on the last day during the taxable year on which the foreign corporation is a controlled foreign corporation,

"(B) the average referred to in subsection (a)(1)(A) for such taxable year shall be determined by only taking into account quarters ending on or before such last day, and

"(C) in determining applicable earnings, the amount taken into account by reason of being described in paragraph (2) of section 316(a) shall be the portion of the amount so described which is allocable (on a pro rata basis) to the part of such year during which the corporation is a controlled foreign corporation.".

(4) Subsection (a) of section 959 (relating to exclusion from gross income of previously taxed earnings and profits) is amended by adding "or" at the end of paragraph (1), by striking "or" at the end of paragraph (2), and by striking paragraph (3).

(5) Subsection (a) of section 959 is amended by striking "paragraphs (2) and (3)" in the last sentence and inserting "paragraph (2)".

(6) Subsection (c) of section 959 is amended by adding at the end the following flush sentence:

"References in this subsection to section 951(a)(1)(C) and subsection (a)(3) shall be treated as references to such provisions as in effect on the day before the date of the enactment of the Small Business Job Protection Act of 1996.".

(7) Paragraph (1) of section 959(f) is amended to read as follows:

"(1) IN GENERAL.—For purposes of this section, amounts that would be included under subparagraph (B) of section 951(a)(1) (determined without regard to this section) shall be treated as attributable first to earnings described in subsection (c)(2), and then to earnings described in subsection (c)(3).".

(8) Paragraph (2) of section 959(f) is amended by striking "subparagraphs (B) and (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(9) Subsection (b) of section 989 is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(10) Paragraph (9) of section 1297(b) is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(11) Subsections (d)(3)(B) and (e)(2)(B)(ii) of section 1297 are each amended by striking "or section 956A".

(12) Subparagraph (G) of section 904(d)(3) is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(c) CLERICAL AMENDMENT.—The table of sections for subpart F of part III of subchapter N of chapter 1 is amended by striking the item relating to section 956A.

26 USC 904 note.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years of foreign corporations beginning after December 31, 1996, and to taxable years of United States shareholders within which or with which such taxable years of foreign corporations end.

Subtitle F—Revenue Offsets

PART I—GENERAL PROVISIONS

SEC. 1601. TERMINATION OF PUERTO RICO AND POSSESSION TAX CREDIT.

(a) IN GENERAL.—Section 936 is amended by adding at the end the following new subsection:

"(j) TERMINATION.—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, this section shall not apply to any taxable year beginning after December 31, 1995.

"(2) TRANSITION RULES FOR ACTIVE BUSINESS INCOME CREDIT.—Except as provided in paragraph (3)—

"(A) ECONOMIC ACTIVITY CREDIT.—In the case of an existing credit claimant—

"(i) with respect to a possession other than Puerto Rico, and

"(ii) to which subsection (a)(4)(B) does not apply, the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 2002.

"(B) SPECIAL RULE FOR REDUCED CREDIT.—

"(i) IN GENERAL.—In the case of an existing credit claimant to which subsection (a)(4)(B) applies, the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 1998.

"(ii) ELECTION IRREVOCABLE AFTER 1997.—An election under subsection (a)(4)(B)(iii) which is in effect for the taxpayer's last taxable year beginning before 1997 may not be revoked unless it is revoked for the taxpayer's first taxable year beginning in 1997 and all subsequent taxable years.

"(C) ECONOMIC ACTIVITY CREDIT FOR PUERTO RICO.—

"For economic activity credit for Puerto Rico, see section 30A.

"(3) ADDITIONAL RESTRICTED CREDIT.—

"(A) IN GENERAL.—In the case of an existing credit claimant—

"(i) the credit under subsection (a)(1)(A) shall be allowed for the period beginning with the first taxable year after the last taxable year to which subparagraph (A) or (B) of paragraph (2), whichever is appropriate, applied and ending with the last taxable year beginning before January 1, 2006, except that

"(ii) the aggregate amount of taxable income taken into account under subsection (a)(1)(A) for any such taxable year shall not exceed the adjusted base period income of such claimant.

"(B) COORDINATION WITH SUBSECTION (a)(4).—The amount of income described in subsection (a)(1)(A) which is taken into account in applying subsection (a)(4) shall be such income as reduced under this paragraph.

"(4) ADJUSTED BASE PERIOD INCOME.—For purposes of paragraph (3)—

"(A) IN GENERAL.—The term 'adjusted base period income' means the average of the inflation-adjusted possession incomes of the corporation for each base period year.

"(B) INFLATION-ADJUSTED POSSESSION INCOME.—For purposes of subparagraph (A), the inflation-adjusted possession income of any corporation for any base period year shall be an amount equal to the sum of—

"(i) the possession income of such corporation for such base period year, plus

"(ii) such possession income multiplied by the inflation adjustment percentage for such base period year.

"(C) INFLATION ADJUSTMENT PERCENTAGE.—For purposes of subparagraph (B), the inflation adjustment percentage for any base period year means the percentage (if any) by which—

"(i) the CPI for 1995, exceeds

"(ii) the CPI for the calendar year in which the base period year for which the determination is being made ends.

For purposes of the preceding sentence, the CPI for any calendar year is the CPI (as defined in section 1(f)(5)) for such year under section 1(f)(4).

"(D) INCREASE IN INFLATION ADJUSTMENT PERCENTAGE FOR GROWTH DURING BASE YEARS.—The inflation adjustment percentage (determined under subparagraph (C) without regard to this subparagraph) for each of the 5 taxable years referred to in paragraph (5)(A) shall be increased by—

"(i) 5 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1995;

"(ii) 10.25 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1994;

"(iii) 15.76 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1993;

"(iv) 21.55 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1992; and

"(v) 27.63 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1991.

"(5) BASE PERIOD YEAR.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'base period year' means each of 3 taxable years which are among the 5 most recent taxable years of the corporation ending before October 14, 1995, determined by disregarding—

"(i) one taxable year for which the corporation had the largest inflation-adjusted possession income, and

"(ii) one taxable year for which the corporation had the smallest inflation-adjusted possession income.

"(B) CORPORATIONS NOT HAVING SIGNIFICANT POSSESSION INCOME THROUGHOUT 5-YEAR PERIOD.—

"(i) IN GENERAL.—If a corporation does not have significant possession income for each of the most

recent 5 taxable years ending before October 14, 1995, then, in lieu of applying subparagraph (A), the term 'base period year' means only those taxable years (of such 5 taxable years) for which the corporation has significant possession income; except that, if such corporation has significant possession income for 4 of such 5 taxable years, the rule of subparagraph (A)(ii) shall apply.

"(ii) SPECIAL RULE.—If there is no year (of such 5 taxable years) for which a corporation has significant possession income—

"(I) the term 'base period year' means the first taxable year ending on or after October 14, 1995, but

"(II) the amount of possession income for such year which is taken into account under paragraph (4) shall be the amount which would be determined if such year were a short taxable year ending on September 30, 1995.

"(iii) SIGNIFICANT POSSESSION INCOME.—For purposes of this subparagraph, the term 'significant possession income' means possession income which exceeds 2 percent of the possession income of the taxpayer for the taxable year (of the period of 6 taxable years ending with the first taxable year ending on or after October 14, 1995) having the greatest possession income.

"(C) ELECTION TO USE ONE BASE PERIOD YEAR.—

"(i) IN GENERAL.—At the election of the taxpayer, the term 'base period year' means—

"(I) only the last taxable year of the corporation ending in calendar year 1992, or

"(II) a deemed taxable year which includes the first ten months of calendar year 1995.

"(ii) BASE PERIOD INCOME FOR 1995.—In determining the adjusted base period income of the corporation for the deemed taxable year under clause (i)(II), the possession income shall be annualized and shall be determined without regard to any extraordinary item.

"(iii) ELECTION.—An election under this subparagraph by any possession corporation may be made only for the corporation's first taxable year beginning after December 31, 1995, for which it is a possession corporation. The rules of subclauses (II) and (III) of subsection (a)(4)(B)(iii) shall apply to the election under this subparagraph.

"(D) ACQUISITIONS AND DISPOSITIONS.—Rules similar to the rules of subparagraphs (A) and (B) of section 41(f)(3) shall apply for purposes of this subsection.

"(6) POSSESSION INCOME.—For purposes of this subsection, the term 'possession income' means, with respect to any possession, the income referred to in subsection (a)(1)(A) determined with respect to that possession. In no event shall possession income be treated as being less than zero.

"(7) SHORT YEARS.—If the current year or a base period year is a short taxable year, the application of this subsection

shall be made with such annualizations as the Secretary shall prescribe.

"(8) SPECIAL RULES FOR CERTAIN POSSESSIONS.—

"(A) IN GENERAL.—In the case of an existing credit claimant with respect to an applicable possession, this section (other than the preceding paragraphs of this subsection) shall apply to such claimant with respect to such applicable possession for taxable years beginning after December 31, 1995, and before January 1, 2006.

"(B) APPLICABLE POSSESSION.—For purposes of this paragraph, the term 'applicable possession' means Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.

"(9) EXISTING CREDIT CLAIMANT.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'existing credit claimant' means a corporation—

"(i)(I) which was actively conducting a trade or business in a possession on October 13, 1995, and

"(II) with respect to which an election under this section is in effect for the corporation's taxable year which includes October 13, 1995, or

"(ii) which acquired all of the assets of a trade or business of a corporation which—

"(I) satisfied the requirements of subclause (I) of clause (i) with respect to such trade or business, and

"(II) satisfied the requirements of subclause (II) of clause (i).

"(B) NEW LINES OF BUSINESS PROHIBITED.—If, after October 13, 1995, a corporation which would (but for this subparagraph) be an existing credit claimant adds a substantial new line of business (other than in an acquisition described in subparagraph (A)(ii)), such corporation shall cease to be treated as an existing credit claimant as of the close of the taxable year ending before the date of such addition.

"(C) BINDING CONTRACT EXCEPTION.—If, on October 13, 1995, and at all times thereafter, there is in effect with respect to a corporation a binding contract for the acquisition of assets to be used in, or for the sale of assets to be produced from, a trade or business, the corporation shall be treated for purposes of this paragraph as actively conducting such trade or business on October 13, 1995. The preceding sentence shall not apply if such trade or business is not actively conducted before January 1, 1996.

"(10) SEPARATE APPLICATION TO EACH POSSESSION.—For purposes of determining—

"(A) whether a taxpayer is an existing credit claimant, and

"(B) the amount of the credit allowed under this section,

this subsection (and so much of this section as relates to this subsection) shall be applied separately with respect to each possession.".

(b) ECONOMIC ACTIVITY CREDIT FOR PUERTO RICO.—

(1) IN GENERAL.—Subpart B of part IV of subchapter A of chapter 1 is amended by adding at the end the following new section:

"SEC. 30A. PUERTO RICAN ECONOMIC ACTIVITY CREDIT.

"(a) ALLOWANCE OF CREDIT.—

"(1) IN GENERAL.—Except as otherwise provided in this section, if the conditions of both paragraph (1) and paragraph (2) of subsection (b) are satisfied with respect to a qualified domestic corporation, there shall be allowed as a credit against the tax imposed by this chapter an amount equal to the portion of the tax which is attributable to the taxable income, from sources without the United States, from—

"(A) the active conduct of a trade or business within Puerto Rico, or

"(B) the sale or exchange of substantially all of the assets used by the taxpayer in the active conduct of such trade or business.

In the case of any taxable year beginning after December 31, 2001, the aggregate amount of taxable income taken into account under the preceding sentence (and in applying subsection (d)) shall not exceed the adjusted base period income of such corporation, as determined in the same manner as under section 936(j).

"(2) QUALIFIED DOMESTIC CORPORATION.—For purposes of paragraph (1), the term 'qualified domestic corporation' means a domestic corporation—

"(A) which is an existing credit claimant with respect to Puerto Rico, and

"(B) with respect to which section 936(a)(4)(B) does not apply for the taxable year.

"(3) SEPARATE APPLICATION.—For purposes of determining—

"(A) whether a taxpayer is an existing credit claimant with respect to Puerto Rico, and

"(B) the amount of the credit allowed under this section,

this section (and so much of section 936 as relates to this section) shall be applied separately with respect to Puerto Rico.

"(b) CONDITIONS WHICH MUST BE SATISFIED.—The conditions referred to in subsection (a) are—

"(1) 3-YEAR PERIOD.—If 80 percent or more of the gross income of the qualified domestic corporation for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within a possession (determined without regard to section 904(f)).

"(2) TRADE OR BUSINESS.—If 75 percent or more of the gross income of the qualified domestic corporation for such period or such part thereof was derived from the active conduct of a trade or business within a possession.

"(c) CREDIT NOT ALLOWED AGAINST CERTAIN TAXES.—The credit provided by subsection (a) shall not be allowed against the tax imposed by—

"(1) section 59A (relating to environmental tax),

"(2) section 531 (relating to the tax on accumulated earnings),

"(3) section 541 (relating to personal holding company tax), or

"(4) section 1351 (relating to recoveries of foreign expropriation losses).

"(d) LIMITATIONS ON CREDIT FOR ACTIVE BUSINESS INCOME.—The amount of the credit determined under subsection (a) for any taxable year shall not exceed the sum of the following amounts:

"(1) 60 percent of the sum of—

"(A) the aggregate amount of the qualified domestic corporation's qualified possession wages for such taxable year, plus

"(B) the allocable employee fringe benefit expenses of the qualified domestic corporation for such taxable year.

"(2) The sum of—

"(A) 15 percent of the depreciation allowances for the taxable year with respect to short-life qualified tangible property,

"(B) 40 percent of the depreciation allowances for the taxable year with respect to medium-life qualified tangible property, and

"(C) 65 percent of the depreciation allowances for the taxable year with respect to long-life qualified tangible property.

"(3) If the qualified domestic corporation does not have an election to use the method described in section 936(h)(5)(C)(ii) (relating to profit split) in effect for the taxable year, the amount of the qualified possession income taxes for the taxable year allocable to nonsheltered income.

"(e) ADMINISTRATIVE PROVISIONS.—For purposes of this title—

"(1) the provisions of section 936 (including any applicable election thereunder) shall apply in the same manner as if the credit under this section were a credit under section 936(a)(1)(A) for a domestic corporation to which section 936(a)(4)(A) applies,

"(2) the credit under this section shall be treated in the same manner as the credit under section 936, and

"(3) a corporation to which this section applies shall be treated in the same manner as if it were a corporation electing the application of section 936.

"(f) DEFINITIONS.—For purposes of this section, any term used in this section which is also used in section 936 shall have the same meaning given such term by section 936.

"(g) APPLICATION OF SECTION.—This section shall apply to taxable years beginning after December 31, 1995, and before January 1, 2006.".

(2) CONFORMING AMENDMENTS.—

(A) Paragraph (1) of section 55(c) is amended by striking "and the section 936 credit allowable under section 27(b)" and inserting ", the section 936 credit allowable under section 27(b), and the Puerto Rican economic activity credit under section 30A".

(B) Subclause (I) of section 56(g)(4)(C)(ii) is amended—

(i) by inserting "30A," before "936", and

(ii) by striking "and (i)" and inserting ", (i), and (j)".

(C) Clause (iii) of section 56(g)(4)(C) is amended by adding at the end the following new subclause:

"(VI) APPLICATION TO SECTION 30A CORPORATIONS.—References in this clause to section 936 shall be treated as including references to section 30A.".

(D) Subsection (b) of section 59 is amended by striking "section 936," and all that follows and inserting "section 30A or 936, alternative minimum taxable income shall not include any income with respect to which a credit is determined under section 30A or 936.".

(E) The table of sections for subpart B of part IV of subchapter A of chapter 1 is amended by adding at the end the following new item:

"Sec. 30A. Puerto Rican economic activity credit.".

(F)(i) The heading for subpart B of part IV of subchapter A of chapter 1 is amended to read as follows:

"Subpart B—Other Credits".

(ii) The table of subparts for part IV of subchapter A of chapter 1 is amended by striking the item relating to subpart B and inserting the following new item:

"Subpart B. Other credits.".

(c) EFFECTIVE DATE.— 26 USC 30A note.

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1995.

(2) SPECIAL RULE FOR QUALIFIED POSSESSION SOURCE INVESTMENT INCOME.—The amendments made by this section shall not apply to qualified possession source investment income received or accrued before July 1, 1996, without regard to the taxable year in which received or accrued.

(3) SPECIAL TRANSITION RULE FOR PAYMENT OF ESTIMATED TAX INSTALLMENT.—In determining the amount of any installment due under section 6655 of the Internal Revenue Code of 1986 after the date of the enactment of this Act and before October 1, 1996, only ½ of any increase in tax (for the taxable year for which such installment is made) by reason of the amendments made by subsections (a) and (b) shall be taken into account. Any reduction in such installment by reason of the preceding sentence shall be recaptured by increasing the next required installment for such year by the amount of such reduction.

SEC. 1602. REPEAL OF EXCLUSION FOR INTEREST ON LOANS USED TO ACQUIRE EMPLOYER SECURITIES.

(a) IN GENERAL.—Section 133 (relating to interest on certain loans used to acquire employer securities) is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (B) of section 291(e)(1) is amended by striking clause (iv) and by redesignating clause (v) as clause (iv).

(2) Section 812 is amended by striking subsection (g).

(3) Paragraph (5) of section 852(b) is amended by striking subparagraph (C).

(4) Paragraph (2) of section 4978(b) is amended by striking subparagraph (A) and all that follows and inserting the following:

"(A) first from qualified securities to which section 1042 applied acquired during the 3-year period ending on the date of the disposition, beginning with the securities first so acquired, and

"(B) then from any other employer securities.

If subsection (d) applies to a disposition, the disposition shall be treated as made from employer securities in the opposite order of the preceding sentence.".

(5)(A) Section 4978B (relating to tax on disposition of employer securities to which section 133 applied) is hereby repealed.

(B) The table of sections for chapter 43 is amended by striking the item relating to section 4978B.

(6) Subsection (e) of section 6047 is amended by striking paragraphs (1), (2), and (3) and inserting the following new paragraphs:

"(1) any employer maintaining, or the plan administrator (within the meaning of section 414(g)) of, an employee stock ownership plan which holds stock with respect to which section 404(k) applies to dividends paid on such stock, or

"(2) both such employer or plan administrator,".

(7) Subsection (f) of section 7872 is amended by striking paragraph (12).

(8) The table of sections for part III of subchapter B of chapter 1 is amended by striking the item relating to section 133.

26 USC 133 note.

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to loans made after the date of the enactment of this Act.

(2) REFINANCINGS.—The amendments made by this section shall not apply to loans made after the date of the enactment of this Act to refinance securities acquisition loans (determined without regard to section 133(b)(1)(B) of the Internal Revenue Code of 1986, as in effect on the day before the date of the enactment of this Act) made on or before such date or to refinance loans described in this paragraph if—

(A) the refinancing loans meet the requirements of section 133 of such Code (as so in effect),

(B) immediately after the refinancing the principal amount of the loan resulting from the refinancing does not exceed the principal amount of the refinanced loan (immediately before the refinancing), and

(C) the term of such refinancing loan does not extend beyond the last day of the term of the original securities acquisition loan.

For purposes of this paragraph, the term "securities acquisition loan" includes a loan from a corporation to an employee stock ownership plan described in section 133(b)(3) of such Code (as so in effect).

(3) EXCEPTION.—Any loan made pursuant to a binding written contract in effect before June 10, 1996, and at all times thereafter before such loan is made, shall be treated

for purposes of paragraphs (1) and (2) as a loan made on or before the date of the enactment of this Act.

SEC. 1603. CERTAIN AMOUNTS DERIVED FROM FOREIGN CORPORATIONS TREATED AS UNRELATED BUSINESS TAXABLE INCOME.

(a) GENERAL RULE.—Subsection (b) of section 512 (relating to modifications) is amended by adding at the end the following new paragraph:

"(17) TREATMENT OF CERTAIN AMOUNTS DERIVED FROM FOREIGN CORPORATIONS.—

"(A) IN GENERAL.—Notwithstanding paragraph (1), any amount included in gross income under section 951(a)(1)(A) shall be included as an item of gross income derived from an unrelated trade or business to the extent the amount so included is attributable to insurance income (as defined in section 953) which, if derived directly by the organization, would be treated as gross income from an unrelated trade or business. There shall be allowed all deductions directly connected with amounts included in gross income under the preceding sentence.

"(B) EXCEPTION.—

"(i) IN GENERAL.—Subparagraph (A) shall not apply to income attributable to a policy of insurance or reinsurance with respect to which the person (directly or indirectly) insured is—

"(I) such organization,

"(II) an affiliate of such organization which is exempt from tax under section 501(a), or

"(III) a director or officer of, or an individual who (directly or indirectly) performs services for, such organization or affiliate but only if the insurance covers primarily risks associated with the performance of services in connection with such organization or affiliate.

"(ii) AFFILIATE.—For purposes of this subparagraph—

"(I) IN GENERAL.—The determination as to whether an entity is an affiliate of an organization shall be made under rules similar to the rules of section 168(h)(4)(B).

"(II) SPECIAL RULE.—Two or more organizations (and any affiliates of such organizations) shall be treated as affiliates if such organizations are colleges or universities described in section 170(b)(1)(A)(ii) or organizations described in section 170(b)(1)(A)(iii) and participate in an insurance arrangement that provides for any profits from such arrangement to be returned to the policyholders in their capacity as such.

"(C) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this paragraph, including regulations for the application of this paragraph in the case of income paid through 1 or more entities or between 2 or more chains of entities.".

26 USC 512 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to amounts included in gross income in any taxable year beginning after December 31, 1995.

SEC. 1604. DEPRECIATION UNDER INCOME FORECAST METHOD.

(a) GENERAL RULE.—Section 167 (relating to depreciation) is amended by redesignating subsection (g) as subsection (h) and by inserting after subsection (f) the following new subsection:

"(g) DEPRECIATION UNDER INCOME FORECAST METHOD.—

"(1) IN GENERAL.—If the depreciation deduction allowable under this section to any taxpayer with respect to any property is determined under the income forecast method or any similar method—

"(A) the income from the property to be taken into account in determining the depreciation deduction under such method shall be equal to the amount of income earned in connection with the property before the close of the 10th taxable year following the taxable year in which the property was placed in service,

"(B) the adjusted basis of the property shall only include amounts with respect to which the requirements of section 461(h) are satisfied,

"(C) the depreciation deduction under such method for the 10th taxable year beginning after the taxable year in which the property was placed in service shall be equal to the adjusted basis of such property as of the beginning of such 10th taxable year, and

"(D) such taxpayer shall pay (or be entitled to receive) interest computed under the look-back method of paragraph (2) for any recomputation year.

"(2) LOOK-BACK METHOD.—The interest computed under the look-back method of this paragraph for any recomputation year shall be determined by—

"(A) first determining the depreciation deductions under this section with respect to such property which would have been allowable for prior taxable years if the determination of the amounts so allowable had been made on the basis of the sum of the following (instead of the estimated income from such property)—

"(i) the actual income earned in connection with such property for periods before the close of the recomputation year, and

"(ii) an estimate of the future income to be earned in connection with such property for periods after the recomputation year and before the close of the 10th taxable year following the taxable year in which the property was placed in service,

"(B) second, determining (solely for purposes of computing such interest) the overpayment or underpayment of tax for each such prior taxable year which would result solely from the application of subparagraph (A), and

"(C) then using the adjusted overpayment rate (as defined in section 460(b)(7)), compounded daily, on the overpayment or underpayment determined under subparagraph (B).

For purposes of the preceding sentence, any cost incurred after the property is placed in service (which is not treated as a

separate property under paragraph (5)) shall be taken into account by discounting (using the Federal mid-term rate determined under section 1274(d) as of the time such cost is incurred) such cost to its value as of the date the property is placed in service. The taxpayer may elect with respect to any property to have the preceding sentence not apply to such property.

"(3) EXCEPTION FROM LOOK-BACK METHOD.—Paragraph (1)(D) shall not apply with respect to any property which had a cost basis of $100,000 or less.

"(4) RECOMPUTATION YEAR.—For purposes of this subsection, except as provided in regulations, the term 'recomputation year' means, with respect to any property, the 3d and the 10th taxable years beginning after the taxable year in which the property was placed in service, unless the actual income earned in connection with the property for the period before the close of such 3d or 10th taxable year is within 10 percent of the income earned in connection with the property for such period which was taken into account under paragraph (1)(A).

"(5) SPECIAL RULES.—

"(A) CERTAIN COSTS TREATED AS SEPARATE PROPERTY.—For purposes of this subsection, the following costs shall be treated as separate properties:

"(i) Any costs incurred with respect to any property after the 10th taxable year beginning after the taxable year in which the property was placed in service.

"(ii) Any costs incurred after the property is placed in service and before the close of such 10th taxable year if such costs are significant and give rise to a significant increase in the income from the property which was not included in the estimated income from the property.

"(B) SYNDICATION INCOME FROM TELEVISION SERIES.—In the case of property which is 1 or more episodes in a television series, income from syndicating such series shall not be required to be taken into account under this subsection before the earlier of—

"(i) the 4th taxable year beginning after the date the first episode in such series is placed in service, or

"(ii) the earliest taxable year in which the taxpayer has an arrangement relating to the future syndication of such series.

"(C) SPECIAL RULES FOR FINANCIAL EXPLOITATION OF CHARACTERS, ETC.—For purposes of this subsection, in the case of television and motion picture films, the income from the property shall include income from the exploitation of characters, designs, scripts, scores, and other incidental income associated with such films, but only to the extent that such income is earned in connection with the ultimate use of such items by, or the ultimate sale of merchandise to, persons who are not related persons (within the meaning of section 267(b)) to the taxpayer.

"(D) COLLECTION OF INTEREST.—For purposes of subtitle F (other than sections 6654 and 6655), any interest required to be paid by the taxpayer under paragraph (1)

for any recomputation year shall be treated as an increase in the tax imposed by this chapter for such year.

"(E) DETERMINATIONS.—For purposes of paragraph (2), determinations of the amount of income earned in connection with any property shall be made in the same manner as for purposes of applying the income forecast method; except that any income from the disposition of such property shall be taken into account.

"(F) TREATMENT OF PASS-THRU ENTITIES.—Rules similar to the rules of section 460(b)(4) shall apply for purposes of this subsection."

26 USC 167 note.

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendment made by subsection (a) shall apply to property placed in service after September 13, 1995.

(2) BINDING CONTRACTS.—The amendment made by subsection (a) shall not apply to any property produced or acquired by the taxpayer pursuant to a written contract which was binding on September 13, 1995, and at all times thereafter before such production or acquisition.

(3) UNDERPAYMENTS OF INCOME TAX.—No addition to tax shall be made under section 6662 of such Code as a result of the application of subsection (d) of that section (relating to substantial understatements of income tax) with respect to any underpayment of income tax for any taxable year ending before such date of enactment, to the extent such underpayment was created or increased by the amendments made by subsection (a).

SEC. 1605. REPEAL OF EXCLUSION FOR PUNITIVE DAMAGES AND FOR DAMAGES NOT ATTRIBUTABLE TO PHYSICAL INJURIES OR SICKNESS.

(a) IN GENERAL.—Paragraph (2) of section 104(a) (relating to compensation for injuries or sickness) is amended to read as follows:

"(2) the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness;".

(b) EMOTIONAL DISTRESS AS SUCH TREATED AS NOT PHYSICAL INJURY OR PHYSICAL SICKNESS.—Section 104(a) is amended by striking the last sentence and inserting the following new sentence: "For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. The preceding sentence shall not apply to an amount of damages not in excess of the amount paid for medical care (described in subparagraph (A) or (B) of section 213(d)(1)) attributable to emotional distress.".

(c) APPLICATION OF PRIOR LAW FOR STATES IN WHICH ONLY PUNITIVE DAMAGES MAY BE AWARDED IN WRONGFUL DEATH ACTIONS.—Section 104 is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

"(c) APPLICATION OF PRIOR LAW IN CERTAIN CASES.—The phrase '(other than punitive damages)' shall not apply to punitive damages awarded in a civil action—

"(1) which is a wrongful death action, and

"(2) with respect to which applicable State law (as in effect on September 13, 1995 and without regard to any modification

after such date) provides, or has been construed to provide by a court of competent jurisdiction pursuant to a decision issued on or before September 13, 1995, that only punitive damages may be awarded in such an action.

This subsection shall cease to apply to any civil action filed on or after the first date on which the applicable State law ceases to provide (or is no longer construed to provide) the treatment described in paragraph (2).".

(d) EFFECTIVE DATE.— 26 USC 104 note.

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to amounts received after the date of the enactment of this Act, in taxable years ending after such date.

(2) EXCEPTION.—The amendments made by this section shall not apply to any amount received under a written binding agreement, court decree, or mediation award in effect on (or issued on or before) September 13, 1995.

SEC. 1606. REPEAL OF DIESEL FUEL TAX REBATE TO PURCHASERS OF DIESEL-POWERED AUTOMOBILES AND LIGHT TRUCKS.

(a) IN GENERAL.—Section 6427 (relating to fuels not used for taxable purposes) is amended by striking subsection (g).

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (3) of section 34(a) is amended to read as follows:

"(3) under section 6427 with respect to fuels used for nontaxable purposes or resold during the taxable year (determined without regard to section 6427(k)).".

(2) Paragraphs (1) and (2)(A) of section 6427(i) are each amended—

(A) by striking "(g),", and

(B) by striking "(or a qualified diesel powered highway vehicle purchased)" each place it appears.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to vehicles purchased after the date of the enactment of this Act. 26 USC 34 note.

SEC. 1607. EXTENSION AND PHASEDOWN OF LUXURY PASSENGER AUTOMOBILE TAX.

(a) EXTENSION.—Subsection (f) of section 4001 is amended by striking "1999" and inserting "2002".

(b) PHASEDOWN.—Section 4001 is amended by redesignating subsection (f) (as amended by subsection (a) of this section) as subsection (g) and by inserting after subsection (e) the following new subsection:

"(f) PHASEDOWN.—For sales occurring in calendar years after 1995 and before 2003, subsection (a) shall be applied by substituting for '10 percent' the percentage determined in accordance with the following table:

"If the calendar year is:	The percentage is:
1996	9 percent
1997	8 percent
1998	7 percent
1999	6 percent
2000	5 percent
2001	4 percent
2002	3 percent

26 USC 4001 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to sales occurring after the date which is 7 days after the date of the enactment of this Act.

SEC. 1608. TERMINATION OF FUTURE TAX-EXEMPT BOND FINANCING FOR LOCAL FURNISHERS OF ELECTRICITY AND GAS.

(a) IN GENERAL.—Section 142(f) (relating to local furnishing of electric energy or gas) is amended by adding at the end the following new paragraphs:

"(3) TERMINATION OF FUTURE FINANCING.—For purposes of this section, no bond may be issued as part of an issue described in subsection (a)(8) with respect to a facility for the local furnishing of electric energy or gas on or after the date of the enactment of this paragraph unless—

"(A) the facility will—

"(i) be used by a person who is engaged in the local furnishing of that energy source on January 1, 1997, and

"(ii) be used to provide service within the area served by such person on January 1, 1997, (or within a county or city any portion of which is within such area), or

"(B) the facility will be used by a successor in interest to such person for the same use and within the same service area as described in subparagraph (A).

"(4) ELECTION TO TERMINATE TAX-EXEMPT BOND FINANCING BY CERTAIN FURNISHERS.—

"(A) IN GENERAL.—In the case of a facility financed with bonds issued before the date of the enactment of this paragraph which would cease to be tax-exempt by reason of the failure to meet the local furnishing requirement of subsection (a)(8) as a result of a service area expansion, such bonds shall not cease to be tax-exempt bonds (and section 150(b)(4) shall not apply) if the person engaged in such local furnishing by such facility makes an election described in subparagraph (B).

"(B) ELECTION.—An election is described in this subparagraph if it is an election made in such manner as the Secretary prescribes, and such person (or its predecessor in interest) agrees that—

"(i) such election is made with respect to all facilities for the local furnishing of electric energy or gas, or both, by such person,

"(ii) no bond exempt from tax under section 103 and described in subsection (a)(8) may be issued on or after the date of the enactment of this paragraph with respect to all such facilities of such person,

"(iii) any expansion of the service area—

"(I) is not financed with the proceeds of any exempt facility bond described in subsection (a)(8), and

"(II) is not treated as a nonqualifying use under the rules of paragraph (2), and

"(iv) all outstanding bonds used to finance the facilities for such person are redeemed not later than 6 months after the later of—

"(I) the earliest date on which such bonds may be redeemed, or

"(II) the date of the election.

"(C) RELATED PERSONS.—For purposes of this paragraph, the term 'person' includes a group of related persons (within the meaning of section 144(a)(3)) which includes such person.".

(b) NO INFERENCE WITH RESPECT TO OUTSTANDING BONDS.— The use of the term "person" in section 142(f)(3) of the Internal Revenue Code of 1986, as added by subsection (a), shall not be construed to affect the tax-exempt status of interest on any bonds issued before the date of the enactment of this Act. 26 USC 142 note.

SEC. 1609. EXTENSION OF AIRPORT AND AIRWAY TRUST FUND EXCISE TAXES.

(a) FUEL TAX.—

(1) Subparagraph (A) of section 4091(b)(3) is amended to read as follows:

"(A) The rate of tax specified in paragraph (1) shall be 4.3 cents per gallon—

"(i) after December 31, 1995, and before the date which is 7 calendar days after the date of the enactment of the Small Business Job Protection Act of 1996, and

"(ii) after December 31, 1996.".

(2) Section 4081(d) is amended—

(A) by adding at the end the following new paragraph:

"(3) AVIATION GASOLINE.—After December 31, 1996, the rate of tax specified in subsection (a)(2)(A)(i) on aviation gasoline shall be 4.3 cents per gallon.", and

(B) by inserting "(other than the tax on aviation gasoline)" after "subsection (a)(2)(A)".

(3) Section 4041(c)(5) is amended by inserting ", and during the period beginning on the date which is 7 calendar days after the date of the enactment of the Small Business Job Protection Act of 1996 and ending on December 31, 1996" after "December 31, 1995".

(b) TICKET TAXES.—Sections 4261(g) and 4271(d) are each amended by striking "January 1, 1996" and inserting "January 1, 1996, and to transportation beginning on or after the date which is 7 calendar days after the date of the enactment of the Small Business Job Protection Act of 1996 and before January 1, 1997".

(c) TRANSFERS TO AIRPORT AND AIRWAY TRUST FUND.—

(1) Subsection (b) of section 9502 is amended by striking "January 1, 1996" each place it appears and inserting "January 1, 1997".

(2) Paragraph (3) of section 9502(f) is amended to read as follows:

"(3) TERMINATION.—Notwithstanding the preceding provisions of this subsection, the Airport and Airway Trust Fund financing rate shall be zero with respect to—

"(A) taxes imposed after December 31, 1995, and before the date which is 7 calendar days after the date of the enactment of the Small Business Job Protection Act of 1996, and

"(B) taxes imposed after December 31, 1996.".

(3) Subsection (d) of section 9502 is amended by adding at the end the following new paragraph:

"(5) TRANSFERS FROM AIRPORT AND AIRWAY TRUST FUND ON ACCOUNT OF REFUNDS OF TAXES ON TRANSPORTATION BY AIR.—The Secretary of the Treasury shall pay from time to time from the Airport and Airway Trust Fund into the general fund of the Treasury amounts equivalent to the amounts paid after December 31, 1995, under section 6402 (relating to authority to make credits or refunds) or section 6415 (relating to credits or refunds to persons who collected certain taxes) in respect of taxes under sections 4261 and 4271.".

(d) EXCISE TAX EXEMPTION FOR CERTAIN EMERGENCY MEDICAL TRANSPORTATION BY AIR AMBULANCE.—Subsection (f) of section 4261 (relating to imposition of tax on transportation by air) is amended to read as follows:

"(f) EXEMPTION FOR AIR AMBULANCES PROVIDING CERTAIN EMERGENCY MEDICAL TRANSPORTATION.—No tax shall be imposed under this section or section 4271 on any air transportation for the purpose of providing emergency medical services—

"(1) by helicopter, or

"(2) by a fixed-wing aircraft equipped for and exclusively dedicated to acute care emergency medical services.".

(e) EXEMPTION FOR CERTAIN HELICOPTER USES.—Subsection (e) of section 4261 is amended by adding at the end the following new sentence: "In the case of helicopter transportation described in paragraph (1), this subsection shall be applied by treating each flight segment as a distinct flight.".

(f) FLIGHT-BY-FLIGHT DETERMINATION OF AVAILABILITY FOR HIRE FOR AFFILIATED GROUPS.—Section 4282 is amended by redesignating subsection (b) as subsection (c) and by inserting after subsection (a) the following new subsection:

"(b) AVAILABILITY FOR HIRE.—For purposes of subsection (a), the determination of whether an aircraft is available for hire by persons who are not members of an affiliated group shall be made on a flight-by-flight basis."

(g) CONSOLIDATION OF TAXES ON AVIATION GASOLINE.—

(1) IN GENERAL.—Subparagraph (A) of section 4081(a)(2) (relating to imposition of tax on gasoline and diesel fuel) is amended by redesignating clause (ii) as clause (iii) and by striking clause (i) and inserting the following:

"(i) in the case of gasoline other than aviation gasoline, 18.3 cents per gallon,

"(ii) in the case of aviation gasoline, 19.3 cents per gallon, and".

(2) TERMINATION.—Subsection (d) of section 4081 is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following new paragraph:

"(2) AVIATION GASOLINE.—On and after January 1, 1997, the rate specified in subsection (a)(2)(A)(ii) shall be 4.3 cents per gallon."

(3) REPEAL OF RETAIL LEVEL TAX.—

(A) Subsection (c) of section 4041 is amended by striking paragraphs (2) and (3) and by redesignating paragraphs (4) and (5) as paragraphs (2) and (3), respectively.

(B) Paragraph (3) of section 4041(c), as redesignated by paragraph (1), is amended by striking "paragraphs (1) and (2)" and inserting "paragraph (1)".

(4) CONFORMING AMENDMENTS.—

(A) Paragraph (1) of section 4041(k) is amended by adding "and" at the end of subparagraph (A), by striking ", and" at the end of subparagraph (B) and inserting a period, and by striking subparagraph (C).

(B) Paragraph (1) of section 4081(d) is amended by striking "each rate of tax specified in subsection (a)(2)(A)" and inserting "the rates of tax specified in clauses (i) and (iii) of subsection (a)(2)(A)".

(C) Sections 6421(f)(2)(A) and 9502(f)(1)(A) are each amended by striking "section 4041(c)(4)" and inserting "section 4041(c)(2)".

(D) Paragraph (2) of section 9502(b) is amended by striking "14 cents" and inserting "15 cents".

(h) FLOOR STOCKS TAXES ON AVIATION FUEL.— 26 USC 4091 note.

(1) IMPOSITION OF TAX.—In the case of aviation fuel on which tax was imposed under section 4091 of the Internal Revenue Code of 1986 before the tax-increase date described in paragraph (3)(A)(i) and which is held on such date by any person, there is hereby imposed a floor stocks tax of 17.5 cents per gallon.

(2) LIABILITY FOR TAX AND METHOD OF PAYMENT.—

(A) LIABILITY FOR TAX.—A person holding aviation fuel on a tax-increase date to which the tax imposed by paragraph (1) applies shall be liable for such tax.

(B) METHOD OF PAYMENT.—The tax imposed by paragraph (1) shall be paid in such manner as the Secretary shall prescribe.

(C) TIME FOR PAYMENT.—The tax imposed by paragraph (1) with respect to any tax-increase date shall be paid on or before the first day of the 7th month beginning after such tax-increase date.

(3) DEFINITIONS.—For purposes of this subsection—

(A) TAX INCREASE DATE.—The term "tax-increase date" means the date which is 7 calendar days after the date of the enactment of this Act.

(B) AVIATION FUEL.—The term "aviation fuel" has the meaning given such term by section 4093 of such Code.

(C) HELD BY A PERSON.—Aviation fuel shall be considered as "held by a person" if title thereto has passed to such person (whether or not delivery to the person has been made).

(D) SECRETARY.—The term "Secretary" means the Secretary of the Treasury or his delegate.

(4) EXCEPTION FOR EXEMPT USES.—The tax imposed by paragraph (1) shall not apply to aviation fuel held by any person on any tax-increase date exclusively for any use for which a credit or refund of the entire tax imposed by section 4091 of such Code is allowable for aviation fuel purchased on or after such tax-increase date for such use.

(5) EXCEPTION FOR CERTAIN AMOUNTS OF FUEL.—

(A) IN GENERAL.—No tax shall be imposed by paragraph (1) on aviation fuel held on any tax-increase date by any person if the aggregate amount of aviation fuel

held by such person on such date does not exceed 2,000 gallons. The preceding sentence shall apply only if such person submits to the Secretary (at the time and in the manner required by the Secretary) such information as the Secretary shall require for purposes of this paragraph.

(B) EXEMPT FUEL.—For purposes of subparagraph (A), there shall not be taken into account fuel held by any person which is exempt from the tax imposed by paragraph (1) by reason of paragraph (4).

(C) CONTROLLED GROUPS.—For purposes of this paragraph—

(i) CORPORATIONS.—

(I) IN GENERAL.—All persons treated as a controlled group shall be treated as 1 person.

(II) CONTROLLED GROUP.—The term "controlled group" has the meaning given to such term by subsection (a) of section 1563 of such Code; except that for such purposes the phrase "more than 50 percent" shall be substituted for the phrase "at least 80 percent" each place it appears in such subsection.

(ii) NONINCORPORATED PERSONS UNDER COMMON CONTROL.—Under regulations prescribed by the Secretary, principles similar to the principles of clause (i) shall apply to a group of persons under common control where 1 or more of such persons is not a corporation.

(6) OTHER LAW APPLICABLE.—All provisions of law, including penalties, applicable with respect to the taxes imposed by section 4091 of such Code shall, insofar as applicable and not inconsistent with the provisions of this subsection, apply with respect to the floor stock taxes imposed by paragraph (1) to the same extent as if such taxes were imposed by such section 4091.

26 USC 4041 note.

(i) EFFECTIVE DATE.—The amendments made by this section shall take effect on the 7th calendar day after the date of the enactment of this Act, except that the amendments made by subsection (b) shall not apply to any amount paid before such date.

SEC. 1610. BASIS ADJUSTMENT TO PROPERTY HELD BY CORPORATION WHERE STOCK IN CORPORATION IS REPLACEMENT PROPERTY UNDER INVOLUNTARY CONVERSION RULES.

(a) IN GENERAL.—Subsection (b) of section 1033 is amended to read as follows:

"(b) BASIS OF PROPERTY ACQUIRED THROUGH INVOLUNTARY CONVERSION.—

"(1) CONVERSIONS DESCRIBED IN SUBSECTION (a)(1).—If the property was acquired as the result of a compulsory or involuntary conversion described in subsection (a)(1), the basis shall be the same as in the case of the property so converted—

"(A) decreased in the amount of any money received by the taxpayer which was not expended in accordance with the provisions of law (applicable to the year in which such conversion was made) determining the taxable status of the gain or loss upon such conversion, and

"(B) increased in the amount of gain or decreased in the amount of loss to the taxpayer recognized upon

such conversion under the law applicable to the year in which such conversion was made.

"(2) CONVERSIONS DESCRIBED IN SUBSECTION (a)(2).—In the case of property purchased by the taxpayer in a transaction described in subsection (a)(2) which resulted in the nonrecognition of any part of the gain realized as the result of a compulsory or involuntary conversion, the basis shall be the cost of such property decreased in the amount of the gain not so recognized; and if the property purchased consists of more than 1 piece of property, the basis determined under this sentence shall be allocated to the purchased properties in proportion to their respective costs.

"(3) PROPERTY HELD BY CORPORATION THE STOCK OF WHICH IS REPLACEMENT PROPERTY.—

"(A) IN GENERAL.—If the basis of stock in a corporation is decreased under paragraph (2), an amount equal to such decrease shall also be applied to reduce the basis of property held by the corporation at the time the taxpayer acquired control (as defined in subsection (a)(2)(E)) of such corporation.

"(B) LIMITATION.—Subparagraph (A) shall not apply to the extent that it would (but for this subparagraph) require a reduction in the aggregate adjusted bases of the property of the corporation below the taxpayer's adjusted basis of the stock in the corporation (determined immediately after such basis is decreased under paragraph (2)).

"(C) ALLOCATION OF BASIS REDUCTION.—The decrease required under subparagraph (A) shall be allocated—

"(i) first to property which is similar or related in service or use to the converted property,

"(ii) second to depreciable property (as defined in section 1017(b)(3)(B)) not described in clause (i), and

"(iii) then to other property.

"(D) SPECIAL RULES.—

"(i) REDUCTION NOT TO EXCEED ADJUSTED BASIS OF PROPERTY.—No reduction in the basis of any property under this paragraph shall exceed the adjusted basis of such property (determined without regard to such reduction).

"(ii) ALLOCATION OF REDUCTION AMONG PROPERTIES.—If more than 1 property is described in a clause of subparagraph (C), the reduction under this paragraph shall be allocated among such property in proportion to the adjusted bases of such property (as so determined).".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to involuntary conversions occurring after the date of the enactment of this Act.

26 USC 1033 note.

SEC. 1611. TREATMENT OF CERTAIN INSURANCE CONTRACTS ON RETIRED LIVES.

(a) GENERAL RULE.—

(1) Paragraph (2) of section 817(d) (defining variable contract) is amended by striking "or" at the end of subparagraph (A), by striking "and" at the end of subparagraph (B) and

inserting "or", and by inserting after subparagraph (B) the following new subparagraph:

"(C) provides for funding of insurance on retired lives as described in section 807(c)(6), and".

(2) Paragraph (3) of section 817(d) is amended by striking "or" at the end of subparagraph (A), by striking the period at the end of subparagraph (B) and inserting ", or", and by inserting after subparagraph (B) the following new subparagraph:

"(C) in the case of funds held under a contract described in paragraph (2)(C), the amounts paid in, or the amounts paid out, reflect the investment return and the market value of the segregated asset account.".

26 USC 817 note.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1995.

SEC. 1612. TREATMENT OF MODIFIED GUARANTEED CONTRACTS.

(a) GENERAL RULE.—Subpart E of part I of subchapter L of chapter 1 (relating to definitions and special rules) is amended by inserting after section 817 the following new section:

"SEC. 817A. SPECIAL RULES FOR MODIFIED GUARANTEED CONTRACTS.

"(a) COMPUTATION OF RESERVES.—In the case of a modified guaranteed contract, clause (ii) of section 807(e)(1)(A) shall not apply.

"(b) SEGREGATED ASSETS UNDER MODIFIED GUARANTEED CONTRACTS MARKED TO MARKET.—

"(1) IN GENERAL.—In the case of any life insurance company, for purposes of this subtitle—

"(A) Any gain or loss with respect to a segregated asset shall be treated as ordinary income or loss, as the case may be.

"(B) If any segregated asset is held by such company as of the close of any taxable year—

"(i) such company shall recognize gain or loss as if such asset were sold for its fair market value on the last business day of such taxable year, and

"(ii) any such gain or loss shall be taken into account for such taxable year.

Proper adjustment shall be made in the amount of any gain or loss subsequently realized for gain or loss taken into account under the preceding sentence. The Secretary may provide by regulations for the application of this subparagraph at times other than the times provided in this subparagraph.

"(2) SEGREGATED ASSET.—For purposes of paragraph (1), the term 'segregated asset' means any asset held as part of a segregated account referred to in subsection (d)(1) under a modified guaranteed contract.

"(c) SPECIAL RULE IN COMPUTING LIFE INSURANCE RESERVES.—For purposes of applying section 816(b)(1)(A) to any modified guaranteed contract, an assumed rate of interest shall include a rate of interest determined, from time to time, with reference to a market rate of interest.

"(d) MODIFIED GUARANTEED CONTRACT DEFINED.—For purposes of this section, the term 'modified guaranteed contract' means a contract not described in section 817—

"(1) all or part of the amounts received under which are allocated to an account which, pursuant to State law or regulation, is segregated from the general asset accounts of the company and is valued from time to time with reference to market values,

"(2) which—

"(A) provides for the payment of annuities,

"(B) is a life insurance contract, or

"(C) is a pension plan contract which is not a life, accident, or health, property, casualty, or liability contract,

"(3) for which reserves are valued at market for annual statement purposes, and

"(4) which provides for a net surrender value or a policyholder's fund (as defined in section 807(e)(1)).

If only a portion of a contract is not described in section 817, such portion shall be treated for purposes of this section as a separate contract.

"(e) REGULATIONS.—The Secretary may prescribe regulations—

"(1) to provide for the treatment of market value adjustments under sections 72, 7702, 7702A, and 807(e)(1)(B),

"(2) to determine the interest rates applicable under sections 807(c)(3), 807(d)(2)(B), and 812 with respect to a modified guaranteed contract annually, in a manner appropriate for modified guaranteed contracts and, to the extent appropriate for such a contract, to modify or waive the applicability of section 811(d),

"(3) to provide rules to limit ordinary gain or loss treatment to assets constituting reserves for modified guaranteed contracts (and not other assets) of the company,

"(4) to provide appropriate treatment of transfers of assets to and from the segregated account, and

"(5) as may be necessary or appropriate to carry out the purposes of this section.".

(b) CLERICAL AMENDMENT.—The table of sections for subpart E of part I of subchapter L of chapter 1 is amended by inserting after the item relating to section 817 the following new item:

"Sec. 817A. Special rules for modified guaranteed contracts.".

(c) EFFECTIVE DATE.— 26 USC 817A note.

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1995.

(2) TREATMENT OF NET ADJUSTMENTS.—Except as provided in paragraph (3), in the case of any taxpayer required by the amendments made by this section to change its calculation of reserves to take into account market value adjustments and to mark segregated assets to market for any taxable year—

(A) such changes shall be treated as a change in method of accounting initiated by the taxpayer,

(B) such changes shall be treated as made with the consent of the Secretary, and

(C) the adjustments required by reason of section 481 of the Internal Revenue Code of 1986, shall be taken into account as ordinary income by the taxpayer for the taxpayer's first taxable year beginning after December 31, 1995.

(3) LIMITATION ON LOSS RECOGNITION AND ON DEDUCTION FOR RESERVE INCREASES.—

(A) LIMITATION ON LOSS RECOGNITION.—

(i) IN GENERAL.—The aggregate loss recognized by reason of the application of section 481 of the Internal Revenue Code of 1986 with respect to section 817A(b) of such Code (as added by this section) for the first taxable year of the taxpayer beginning after December 31, 1995, shall not exceed the amount included in the taxpayer's gross income for such year by reason of the excess (if any) of—

(I) the amount of life insurance reserves as of the close of the prior taxable year, over

(II) the amount of such reserves as of the beginning of such first taxable year,

to the extent such excess is attributable to subsection (a) of such section 817A. Notwithstanding the preceding sentence, the adjusted basis of each segregated asset shall be determined as if all such losses were recognized.

(ii) DISALLOWED LOSS ALLOWED OVER PERIOD.—The amount of the loss which is not allowed under clause (i) shall be allowed ratably over the period of 7 taxable years beginning with the taxpayer's first taxable year beginning after December 31, 1995.

(B) LIMITATION ON DEDUCTION FOR INCREASE IN RESERVES.—

(i) IN GENERAL.—The deduction allowed for the first taxable year of the taxpayer beginning after December 31, 1995, by reason of the application of section 481 of such Code with respect to section 817A(a) of such Code (as added by this section) shall not exceed the aggregate built-in gain recognized by reason of the application of such section 481 with respect to section 817A(b) of such Code (as added by this section) for such first taxable year.

(ii) DISALLOWED DEDUCTION ALLOWED OVER PERIOD.—The amount of the deduction which is disallowed under clause (i) shall be allowed ratably over the period of 7 taxable years beginning with the taxpayer's first taxable year beginning after December 31, 1995.

(iii) BUILT-IN GAIN.—For purposes of this subparagraph, the built-in gain on an asset is the amount equal to the excess of—

(I) the fair market value of the asset as of the beginning of the first taxable year of the taxpayer beginning after December 31, 1995, over

(II) the adjusted basis of such asset as of such time.

SEC. 1613. TREATMENT OF CONTRIBUTIONS IN AID OF CONSTRUCTION.

(a) TREATMENT OF CONTRIBUTIONS IN AID OF CONSTRUCTION.—

(1) IN GENERAL.—Section 118 (relating to contributions to the capital of a corporation) is amended—

(A) by redesignating subsection (c) as subsection (e), and

(B) by inserting after subsection (b) the following new subsections:

"(c) SPECIAL RULES FOR WATER AND SEWERAGE DISPOSAL UTILITIES.—

"(1) GENERAL RULE.—For purposes of this section, the term 'contribution to the capital of the taxpayer' includes any amount of money or other property received from any person (whether or not a shareholder) by a regulated public utility which provides water or sewerage disposal services if—

"(A) such amount is a contribution in aid of construction,

"(B) in the case of contribution of property other than water or sewerage disposal facilities, such amount meets the requirements of the expenditure rule of paragraph (2), and

"(C) such amount (or any property acquired or constructed with such amount) is not included in the taxpayer's rate base for ratemaking purposes.

"(2) EXPENDITURE RULE.—An amount meets the requirements of this paragraph if—

"(A) an amount equal to such amount is expended for the acquisition or construction of tangible property described in section 1231(b)—

"(i) which is the property for which the contribution was made or is of the same type as such property, and

"(ii) which is used predominantly in the trade or business of furnishing water or sewerage disposal services,

"(B) the expenditure referred to in subparagraph (A) occurs before the end of the second taxable year after the year in which such amount was received, and

"(C) accurate records are kept of the amounts contributed and expenditures made, the expenditures to which contributions are allocated, and the year in which the contributions and expenditures are received and made.

"(3) DEFINITIONS.—For purposes of this subsection—

"(A) CONTRIBUTION IN AID OF CONSTRUCTION.—The term 'contribution in aid of construction' shall be defined by regulations prescribed by the Secretary, except that such term shall not include amounts paid as service charges for starting or stopping services.

"(B) PREDOMINANTLY.—The term 'predominantly' means 80 percent or more.

"(C) REGULATED PUBLIC UTILITY.—The term 'regulated public utility' has the meaning given such term by section 7701(a)(33), except that such term shall not include any utility which is not required to provide water or sewerage disposal services to members of the general public in its service area.

"(4) DISALLOWANCE OF DEDUCTIONS AND CREDITS; ADJUSTED BASIS.—Notwithstanding any other provision of this subtitle, no deduction or credit shall be allowed for, or by reason of, any expenditure which constitutes a contribution in aid of construction to which this subsection applies. The adjusted basis of any property acquired with contributions in aid of construction to which this subsection applies shall be zero.

"(d) STATUTE OF LIMITATIONS.—If the taxpayer for any taxable year treats an amount as a contribution to the capital of the taxpayer described in subsection (c), then—

"(1) the statutory period for the assessment of any deficiency attributable to any part of such amount shall not expire before the expiration of 3 years from the date the Secretary is notified by the taxpayer (in such manner as the Secretary may prescribe) of—

"(A) the amount of the expenditure referred to in subparagraph (A) of subsection (c)(2),

"(B) the taxpayer's intention not to make the expenditures referred to in such subparagraph, or

"(C) a failure to make such expenditure within the period described in subparagraph (B) of subsection (c)(2), and

"(2) such deficiency may be assessed before the expiration of such 3-year period notwithstanding the provisions of any other law or rule of law which would otherwise prevent such assessment.".

(2) CONFORMING AMENDMENT.—Section 118(b) is amended by inserting "except as provided in subsection (c)," before "the term".

26 USC 118 note.

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to amounts received after June 12, 1996.

(b) RECOVERY METHOD AND PERIOD FOR WATER UTILITY PROPERTY.—

(1) REQUIREMENT TO USE STRAIGHT LINE METHOD.—Section 168(b)(3) is amended by adding at the end the following new subparagraph:

"(F) Water utility property described in subsection (e)(5).".

(2) 25-YEAR RECOVERY PERIOD.—The table contained in section 168(c)(1) is amended by inserting the following item after the item relating to 20-year property:

"Water utility property ..... 25 years".

(3) WATER UTILITY PROPERTY.—

(A) IN GENERAL.—Section 168(e) is amended by adding at the end the following new paragraph:

"(5) WATER UTILITY PROPERTY.—The term 'water utility property' means property—

"(A) which is an integral part of the gathering, treatment, or commercial distribution of water, and which, without regard to this paragraph, would be 20-year property, and

"(B) any municipal sewer.".

(B) CONFORMING AMENDMENTS.—Section 168 is amended—

(i) by striking subparagraph (F) of subsection (e)(3), and

(ii) by striking the item relating to subparagraph (F) in the table in subsection (g)(3).

(4) ALTERNATIVE SYSTEM.—Clause (iv) of section 168(g)(2)(C) is amended by inserting "or water utility property" after "tunnel bore".

26 USC 168 note.

(5) EFFECTIVE DATE.—The amendments made by this subsection shall apply to property placed in service after June 12, 1996, other than property placed in service pursuant to

a binding contract in effect before June 10, 1996, and at all times thereafter before the property is placed in service.

SEC. 1614. ELECTION TO CEASE STATUS AS QUALIFIED SCHOLARSHIP FUNDING CORPORATION.

(a) IN GENERAL.—Subsection (d) of section 150 (relating to definitions and special rules) is amended by adding at the end the following new paragraph:

"(3) ELECTION TO CEASE STATUS AS QUALIFIED SCHOLARSHIP FUNDING CORPORATION.—

"(A) IN GENERAL.—Any qualified scholarship funding bond, and qualified student loan bond, outstanding on the date of the issuer's election under this paragraph (and any bond (or series of bonds) issued to refund such a bond) shall not fail to be a tax-exempt bond solely because the issuer ceases to be described in subparagraphs (A) and (B) of paragraph (2) if the issuer meets the requirements of subparagraphs (B) and (C) of this paragraph.

"(B) ASSETS AND LIABILITIES OF ISSUER TRANSFERRED TO TAXABLE SUBSIDIARY.—The requirements of this subparagraph are met by an issuer if—

"(i) all of the student loan notes of the issuer and other assets pledged to secure the repayment of qualified scholarship funding bond indebtedness of the issuer are transferred to another corporation within a reasonable period after the election is made under this paragraph;

"(ii) such transferee corporation assumes or otherwise provides for the payment of all of the qualified scholarship funding bond indebtedness of the issuer within a reasonable period after the election is made under this paragraph;

"(iii) to the extent permitted by law, such transferee corporation assumes all of the responsibilities, and succeeds to all of the rights, of the issuer under the issuer's agreements with the Secretary of Education in respect of student loans;

"(iv) immediately after such transfer, the issuer, together with any other issuer which has made an election under this paragraph in respect of such transferee, hold all of the senior stock in such transferee corporation; and

"(v) such transferee corporation is not exempt from tax under this chapter.

"(C) ISSUER TO OPERATE AS INDEPENDENT ORGANIZATION DESCRIBED IN SECTION 501(C)(3).—The requirements of this subparagraph are met by an issuer if, within a reasonable period after the transfer referred to in subparagraph (B)—

"(i) the issuer is described in section 501(c)(3) and exempt from tax under section 501(a);

"(ii) the issuer no longer is described in subparagraphs (A) and (B) of paragraph (2); and

"(iii) at least 80 percent of the members of the board of directors of the issuer are independent members.

"(D) SENIOR STOCK.—For purposes of this paragraph, the term 'senior stock' means stock—

"(i) which participates pro rata and fully in the equity value of the corporation with all other common stock of the corporation but which has the right to payment of liquidation proceeds prior to payment of liquidation proceeds in respect of other common stock of the corporation;

"(ii) which has a fixed right upon liquidation and upon redemption to an amount equal to the greater of—

"(I) the fair market value of such stock on the date of liquidation or redemption (whichever is applicable); or

"(II) the fair market value of all assets transferred in exchange for such stock and reduced by the amount of all liabilities of the corporation which has made an election under this paragraph assumed by the transferee corporation in such transfer;

"(iii) the holder of which has the right to require the transferee corporation to redeem on a date that is not later than 10 years after the date on which an election under this paragraph was made and pursuant to such election such stock was issued; and

"(iv) in respect of which, during the time such stock is outstanding, there is not outstanding any equity interest in the corporation having any liquidation, redemption or dividend rights in the corporation which are superior to those of such stock.

"(E) INDEPENDENT MEMBER.—The term 'independent member' means a member of the board of directors of the issuer who (except for services as a member of such board) receives no compensation directly or indirectly—

"(i) for services performed in connection with such transferee corporation, or

"(ii) for services as a member of the board of directors or as an officer of such transferee corporation.

For purposes of clause (ii), the term 'officer' includes any individual having powers or responsibilities similar to those of officers.

"(F) COORDINATION WITH CERTAIN PRIVATE FOUNDATION TAXES.—For purposes of sections 4942 (relating to the excise tax on a failure to distribute income) and 4943 (relating to the excise tax on excess business holdings), the transferee corporation referred to in subparagraph (B) shall be treated as a functionally related business (within the meaning of section 4942(j)(4)) with respect to the issuer during the period commencing with the date on which an election is made under this paragraph and ending on the date that is the earlier of—

"(i) the last day of the last taxable year for which more than 50 percent of the gross income of such transferee corporation is derived from, or more than 50 percent of the assets (by value) of such transferee corporation consists of, student loan notes incurred under the Higher Education Act of 1965; or

"(ii) the last day of the taxable year of the issuer during which occurs the date which is 10 years after the date on which the election under this paragraph is made.

"(G) ELECTION.—An election under this paragraph may be revoked only with the consent of the Secretary.".

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act. 26 USC 150 note.

SEC. 1615. CERTAIN TAX BENEFITS DENIED TO INDIVIDUALS FAILING TO PROVIDE TAXPAYER IDENTIFICATION NUMBERS.

(a) PERSONAL EXEMPTION.—

(1) IN GENERAL.—Section 151 (relating to allowance of deductions for personal exemptions) is amended by adding at the end the following new subsection:

"(e) IDENTIFYING INFORMATION REQUIRED.—No exemption shall be allowed under this section with respect to any individual unless the TIN of such individual is included on the return claiming the exemption.".

(2) CONFORMING AMENDMENTS.—

(A) Subsection (e) of section 6109 is repealed.

(B) Section 6724(d)(3) is amended by adding "and" at the end of subparagraph (C), by striking subparagraph (D), and by redesignating subparagraph (E) as subparagraph (D).

(b) DEPENDENT CARE CREDIT.—Subsection (e) of section 21 (relating to expenses for household and dependent care services necessary for gainful employment) is amended by adding at the end the following new paragraph:

"(10) IDENTIFYING INFORMATION REQUIRED WITH RESPECT TO QUALIFYING INDIVIDUALS.—No credit shall be allowed under this section with respect to any qualifying individual unless the TIN of such individual is included on the return claiming the credit.".

(c) EXTENSION OF PROCEDURES APPLICABLE TO MATHEMATICAL OR CLERICAL ERRORS.—Section 6213(g)(2) (relating to the definition of mathematical or clerical errors), as amended by the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, is amended by striking "and" at the end of subparagraph (F), by striking the period at the end of subparagraph (G) and inserting ", and", and by inserting at the end the following new subparagraph:

"(H) an omission of a correct TIN required under section 21 (relating to expenses for household and dependent care services necessary for gainful employment) or section 151 (relating to allowance of deductions for personal exemptions).".

(d) EFFECTIVE DATE.— 26 USC 21 note.

(1) IN GENERAL.—The amendments made by this section shall apply with respect to returns the due date for which (without regard to extensions) is on or after the 30th day after the date of the enactment of this Act.

(2) SPECIAL RULE FOR 1995 AND 1996.—In the case of returns for taxable years beginning in 1995 or 1996, a taxpayer shall not be required by the amendments made by this section to provide a taxpayer identification number for a child who is born after October 31, 1995, in the case of a taxable year

beginning in 1995 or November 30, 1996, in the case of a taxable year beginning in 1996.

SEC. 1616. REPEAL OF BAD DEBT RESERVE METHOD FOR THRIFT SAVINGS ASSOCIATIONS.

(a) IN GENERAL.—Section 593 (relating to reserves for losses on loans) is amended by adding at the end the following new subsections:

"(f) TERMINATION OF RESERVE METHOD.—Subsections (a), (b), (c), and (d) shall not apply to any taxable year beginning after December 31, 1995.

"(g) 6-YEAR SPREAD OF ADJUSTMENTS.—

"(1) IN GENERAL.—In the case of any taxpayer who is required by reason of subsection (f) to change its method of computing reserves for bad debts—

"(A) such change shall be treated as a change in a method of accounting,

"(B) such change shall be treated as initiated by the taxpayer and as having been made with the consent of the Secretary, and

"(C) the net amount of the adjustments required to be taken into account by the taxpayer under section 481(a)—

"(i) shall be determined by taking into account only applicable excess reserves, and

"(ii) as so determined, shall be taken into account ratably over the 6-taxable year period beginning with the first taxable year beginning after December 31, 1995.

"(2) APPLICABLE EXCESS RESERVES.—

"(A) IN GENERAL.—For purposes of paragraph (1), the term 'applicable excess reserves' means the excess (if any) of—

"(i) the balance of the reserves described in subsection (c)(1) (other than the supplemental reserve) as of the close of the taxpayer's last taxable year beginning before January 1, 1996, over

"(ii) the lesser of—

"(I) the balance of such reserves as of the close of the taxpayer's last taxable year beginning before January 1, 1988, or

"(II) the balance of the reserves described in subclause (I), reduced in the same manner as under section 585(b)(2)(B)(ii) on the basis of the taxable years described in clause (i) and this clause.

"(B) SPECIAL RULE FOR THRIFTS WHICH BECOME SMALL BANKS.—In the case of a bank (as defined in section 581) which was not a large bank (as defined in section 585(c)(2)) for its first taxable year beginning after December 31, 1995—

"(i) the balance taken into account under subparagraph (A)(ii) shall not be less than the amount which would be the balance of such reserves as of the close of its last taxable year beginning before such date if the additions to such reserves for all taxable years had been determined under section 585(b)(2)(A), and

"(ii) the opening balance of the reserve for bad debts as of the beginning of such first taxable year shall be the balance taken into account under subparagraph (A)(ii) (determined after the application of clause (i) of this subparagraph).

The preceding sentence shall not apply for purposes of paragraphs (5) and (6) or subsection (e)(1).

"(3) RECAPTURE OF PRE-1988 RESERVES WHERE TAXPAYER CEASES TO BE BANK.—If, during any taxable year beginning after December 31, 1995, a taxpayer to which paragraph (1) applied is not a bank (as defined in section 581), paragraph (1) shall apply to the reserves described in paragraph (2)(A)(ii) and the supplemental reserve; except that such reserves shall be taken into account ratably over the 6-taxable year period beginning with such taxable year.

"(4) SUSPENSION OF RECAPTURE IF RESIDENTIAL LOAN REQUIREMENT MET.—

"(A) IN GENERAL.—In the case of a bank which meets the residential loan requirement of subparagraph (B) for the first taxable year beginning after December 31, 1995, or for the following taxable year—

"(i) no adjustment shall be taken into account under paragraph (1) for such taxable year, and

"(ii) such taxable year shall be disregarded in determining—

"(I) whether any other taxable year is a taxable year for which an adjustment is required to be taken into account under paragraph (1), and

"(II) the amount of such adjustment.

"(B) RESIDENTIAL LOAN REQUIREMENT.—A taxpayer meets the residential loan requirement of this subparagraph for any taxable year if the principal amount of the residential loans made by the taxpayer during such year is not less than the base amount for such year.

"(C) RESIDENTIAL LOAN.—For purposes of this paragraph, the term 'residential loan' means any loan described in clause (v) of section 7701(a)(19)(C) but only if such loan is incurred in acquiring, constructing, or improving the property described in such clause.

"(D) BASE AMOUNT.—For purposes of subparagraph (B), the base amount is the average of the principal amounts of the residential loans made by the taxpayer during the 6 most recent taxable years beginning on or before December 31, 1995. At the election of the taxpayer who made such loans during each of such 6 taxable years, the preceding sentence shall be applied without regard to the taxable year in which such principal amount was the highest and the taxable year in such principal amount was the lowest. Such an election may be made only for the first taxable year beginning after such date, and, if made for such taxable year, shall apply to the succeeding taxable year unless revoked with the consent of the Secretary.

"(E) CONTROLLED GROUPS.—In the case of a taxpayer which is a member of any controlled group of corporations described in section 1563(a)(1), subparagraph (B) shall be applied with respect to such group.

"(5) CONTINUED APPLICATION OF FRESH START UNDER SECTION 585 TRANSITIONAL RULES.—In the case of a taxpayer to which paragraph (1) applied and which was not a large bank (as defined in section 585(c)(2)) for its first taxable year beginning after December 31, 1995:

"(A) IN GENERAL.—For purposes of determining the net amount of adjustments referred to in section 585(c)(3)(A)(iii), there shall be taken into account only the excess (if any) of the reserve for bad debts as of the close of the last taxable year before the disqualification year over the balance taken into account by such taxpayer under paragraph (2)(A)(ii) of this subsection.

"(B) TREATMENT UNDER ELECTIVE CUT-OFF METHOD.—For purposes of applying section 585(c)(4)—

"(i) the balance of the reserve taken into account under subparagraph (B) thereof shall be reduced by the balance taken into account by such taxpayer under paragraph (2)(A)(ii) of this subsection, and

"(ii) no amount shall be includible in gross income by reason of such reduction.

"(6) SUSPENDED RESERVE INCLUDED AS SECTION 381(c) ITEMS.—The balance taken into account by a taxpayer under paragraph (2)(A)(ii) of this subsection and the supplemental reserve shall be treated as items described in section 381(c).

"(7) CONVERSIONS TO CREDIT UNIONS.—In the case of a taxpayer to which paragraph (1) applied which becomes a credit union described in section 501(c) and exempt from taxation under section 501(a)—

"(A) any amount required to be included in the gross income of the credit union by reason of this subsection shall be treated as derived from an unrelated trade or business (as defined in section 513), and

"(B) for purposes of paragraph (3), the credit union shall not be treated as if it were a bank.

"(8) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out this subsection and subsection (e), including regulations providing for the application of such subsections in the case of acquisitions, mergers, spin-offs, and other reorganizations.".

(b) CONFORMING AMENDMENTS.—

(1) Subsection (d) of section 50 is amended by adding at the end the following new sentence:

"Paragraphs (1)(A), (2)(A), and (4) of the section 46(e) referred to in paragraph (1) of this subsection shall not apply to any taxable year beginning after December 31, 1995."

(2) Subsection (e) of section 52 is amended by striking paragraph (1) and by redesignating paragraphs (2) and (3) as paragraphs (1) and (2), respectively.

(3) Subsection (a) of section 57 is amended by striking paragraph (4).

(4) Section 246 is amended by striking subsection (f).

(5) Clause (i) of section 291(e)(1)(B) is amended by striking "or to which section 593 applies".

(6) Subparagraph (A) of section 585(a)(2) is amended by striking "other than an organization to which section 593 applies".

(7)(A) The material preceding subparagraph (A) of section 593(e)(1) is amended by striking "by a domestic building and loan association or an institution that is treated as a mutual savings bank under section 591(b)" and inserting "by a taxpayer having a balance described in subsection (g)(2)(A)(ii)".

(B) Subparagraph (B) of section 593(e)(1) is amended to read as follows:

"(B) then out of the balance taken into account under subsection (g)(2)(A)(ii) (properly adjusted for amounts charged against such reserves for taxable years beginning after December 31, 1987),".

(C) The second sentence of section 593(e)(1) is amended by striking "the association or an institution that is treated as a mutual savings bank under section 591(b)" and inserting "a taxpayer having a balance described in subsection (g)(2)(A)(ii)".

(D) The third sentence of section 593(e)(1) is amended by striking "an association" and inserting "a taxpayer having a balance described in subsection (g)(2)(A)(ii)".

(E) Paragraph (1) of section 593(e) is amended by adding at the end the following new sentence: "This paragraph shall not apply to any distribution of all of the stock of a bank (as defined in section 581) to another corporation if, immediately after the distribution, such bank and such other corporation are members of the same affiliated group (as defined in section 1504) and the provisions of section 5(e) of the Federal Deposit Insurance Act (as in effect on December 31, 1995) or similar provisions are in effect.".

(8) Section 595 is hereby repealed.

(9) Section 596 is hereby repealed.

(10) Subsection (a) of section 860E is amended—

(A) by striking "Except as provided in paragraph (2), the" in paragraph (1) and inserting "The",

(B) by striking paragraphs (2) and (4) and redesignating paragraphs (3), (5), and (6) as paragraphs (2), (3), and (4), respectively,

(C) by striking in paragraph (2) (as so redesignated) all that follows "subsection" and inserting a period, and

(D) by striking the last sentence of paragraph (4) (as so redesignated).

(11) Paragraph (3) of section 992(d) is amended by striking "or 593".

(12) Section 1038 is amended by striking subsection (f).

(13) Clause (ii) of section 1042(c)(4)(B) is amended by striking "or 593".

(14) Subsection (c) of section 1277 is amended by striking "or to which section 593 applies".

(15) Subparagraph (B) of section 1361(b)(2) is amended by striking "or to which section 593 applies".

(16) The table of sections for part II of subchapter H of chapter 1 is amended by striking the items relating to sections 595 and 596.

(c) EFFECTIVE DATES.— 26 USC 593 note.

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall apply to taxable years beginning after December 31, 1995.

(2) SUBSECTION (b)(7)(B).—The amendments made by subsection (b)(7)(B) shall not apply to any distribution with respect to preferred stock if—

(A) such stock is outstanding at all times after October 31, 1995, and before the distribution, and

(B) such distribution is made before the date which is 1 year after the date of the enactment of this Act (or, in the case of stock which may be redeemed, if later, the date which is 30 days after the earliest date that such stock may be redeemed).

(3) SUBSECTION (b)(8).—The amendment made by subsection (b)(8) shall apply to property acquired in taxable years beginning after December 31, 1995.

(4) SUBSECTION (b)(10).—The amendments made by subsection (b)(10) shall not apply to any residual interest held by a taxpayer if such interest has been held by such taxpayer at all times after October 31, 1995.

SEC. 1617. EXCLUSION FOR ENERGY CONSERVATION SUBSIDIES LIMITED TO SUBSIDIES WITH RESPECT TO DWELLING UNITS.

(a) IN GENERAL.—Paragraph (1) of section 136(c) (defining energy conservation measure) is amended by striking "energy demand—" and all that follows and inserting "energy demand with respect to a dwelling unit.".

(b) CONFORMING AMENDMENTS.—

(1) Subsection (a) of section 136 is amended to read as follows:

"(a) EXCLUSION.—Gross income shall not include the value of any subsidy provided (directly or indirectly) by a public utility to a customer for the purchase or installation of any energy conservation measure.".

(2) Paragraph (2) of section 136(c) is amended—

(A) by striking subparagraph (A) and by redesignating subparagraphs (B) and (C) as subparagraphs (A) and (B), respectively, and

(B) by striking "AND SPECIAL RULES" in the paragraph heading.

26 USC 136 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts received after December 31, 1996, unless received pursuant to a written binding contract in effect on September 13, 1995, and at all times thereafter.

PART II—FINANCIAL ASSET SECURITIZATION INVESTMENTS

SEC. 1621. FINANCIAL ASSET SECURITIZATION INVESTMENT TRUSTS.

(a) IN GENERAL.—Subchapter M of chapter 1 is amended by adding at the end the following new part:

"PART V—FINANCIAL ASSET SECURITIZATION INVESTMENT TRUSTS

"SEC. 860H. TAXATION OF A FASIT; OTHER GENERAL RULES.

"(a) TAXATION OF FASIT.—A FASIT as such shall not be subject to taxation under this subtitle (and shall not be treated as a trust, partnership, corporation, or taxable mortgage pool).

"(b) TAXATION OF HOLDER OF OWNERSHIP INTEREST.—In determining the taxable income of the holder of the ownership interest in a FASIT—

"(1) all assets, liabilities, and items of income, gain, deduction, loss, and credit of a FASIT shall be treated as assets, liabilities, and such items (as the case may be) of such holder,

"(2) the constant yield method (including the rules of section 1272(a)(6)) shall be applied under an accrual method of accounting in determining all interest, acquisition discount, original issue discount, and market discount and all premium deductions or adjustments with respect to each debt instrument of the FASIT,

"(3) there shall not be taken into account any item of income, gain, or deduction allocable to a prohibited transaction, and

"(4) interest accrued by the FASIT which is exempt from tax imposed by this subtitle shall, when taken into account by such holder, be treated as ordinary income.

"(c) TREATMENT OF REGULAR INTERESTS.—For purposes of this title—

"(1) a regular interest in a FASIT, if not otherwise a debt instrument, shall be treated as a debt instrument,

"(2) section 163(e)(5) shall not apply to such an interest, and

"(3) amounts includible in gross income with respect to such an interest shall be determined under an accrual method of accounting.

"SEC. 860I. GAIN RECOGNITION ON CONTRIBUTIONS TO A FASIT AND IN OTHER CASES.

"(a) TREATMENT OF PROPERTY ACQUIRED BY FASIT.—

"(1) PROPERTY ACQUIRED FROM HOLDER OF OWNERSHIP INTEREST OR RELATED PERSON.—If property is sold or contributed to a FASIT by the holder of the ownership interest in such FASIT (or by a related person) gain (if any) shall be recognized to such holder (or person) in an amount equal to the excess (if any) of such property's value under subsection (d) on the date of such sale or contribution over its adjusted basis on such date.

"(2) PROPERTY ACQUIRED OTHER THAN FROM HOLDER OF OWNERSHIP INTEREST OR RELATED PERSON.—Property which is acquired by a FASIT other than in a transaction to which paragraph (1) applies shall be treated—

"(A) as having been acquired by the holder of the ownership interest in the FASIT for an amount equal to the FASIT's cost of acquiring such property, and

"(B) as having been sold by such holder to the FASIT at its value under subsection (d) on such date.

"(b) GAIN RECOGNITION ON PROPERTY OUTSIDE FASIT WHICH SUPPORTS REGULAR INTERESTS.—If property held by the holder of the ownership interest in a FASIT (or by any person related to such holder) supports any regular interest in such FASIT—

"(1) gain shall be recognized to such holder (or person) in the same manner as if such holder (or person) had sold such property at its value under subsection (d) on the earliest date such property supports such an interest, and

"(2) such property shall be treated as held by such FASIT for purposes of this part.

"(c) DEFERRAL OF GAIN RECOGNITION.—The Secretary may prescribe regulations which—

"(1) provide that gain otherwise recognized under subsection (a) or (b) shall not be recognized before the earliest date on which such property supports any regular interest in such FASIT or any indebtedness of the holder of the ownership interest (or of any person related to such holder), and

"(2) provide such adjustments to the other provisions of this part to the extent appropriate in the context of the treatment provided under paragraph (1).

"(d) VALUATION.—For purposes of this section—

"(1) IN GENERAL.—The value of any property under this subsection shall be—

"(A) in the case of a debt instrument which is not traded on an established securities market, the sum of the present values of the reasonably expected payments under such instrument determined (in the manner provided by regulations prescribed by the Secretary)—

"(i) as of the date of the event resulting in the gain recognition under this section, and

"(ii) by using a discount rate equal to 120 percent of the applicable Federal rate (as defined in section 1274(d)), or such other discount rate specified in such regulations, compounded semiannually, and

"(B) in the case of any other property, its fair market value.

"(2) SPECIAL RULE FOR REVOLVING LOAN ACCOUNTS.—For purposes of paragraph (1)—

"(A) each extension of credit (other than the accrual of interest) on a revolving loan account shall be treated as a separate debt instrument, and

"(B) payments on such extensions of credit having substantially the same terms shall be applied to such extensions beginning with the earliest such extension.

"(e) SPECIAL RULES.—

"(1) NONRECOGNITION RULES NOT TO APPLY.—Gain required to be recognized under this section shall be recognized notwithstanding any other provision of this subtitle.

"(2) BASIS ADJUSTMENTS.—The basis of any property on which gain is recognized under this section shall be increased by the amount of gain so recognized.

"SEC. 860J. NON-FASIT LOSSES NOT TO OFFSET CERTAIN FASIT INCLUSIONS.

"(a) IN GENERAL.—The taxable income of the holder of the ownership interest or any high-yield interest in a FASIT for any taxable year shall in no event be less than the sum of—

"(1) such holder's taxable income determined solely with respect to such interests (including gains and losses from sales and exchanges of such interests), and

"(2) the excess inclusion (if any) under section 860E(a)(1) for such taxable year.

"(b) COORDINATION WITH SECTION 172.—Any increase in the taxable income of any holder of the ownership interest or a high-yield interest in a FASIT for any taxable year by reason of subsection (a) shall be disregarded—

"(1) in determining under section 172 the amount of any net operating loss for such taxable year, and

"(2) in determining taxable income for such taxable year for purposes of the second sentence of section 172(b)(2).

"(c) COORDINATION WITH MINIMUM TAX.—For purposes of part VI of subchapter A of this chapter—

"(1) the reference in section 55(b)(2) to taxable income shall be treated as a reference to taxable income determined without regard to this section,

"(2) the alternative minimum taxable income of any holder of the ownership interest or a high-yield interest in a FASIT for any taxable year shall in no event be less than such holder's taxable income determined solely with respect to such interests, and

"(3) any increase in taxable income under this section shall be disregarded for purposes of computing the alternative tax net operating loss deduction.

"(d) AFFILIATED GROUPS.—All members of an affiliated group filing a consolidated return shall be treated as one taxpayer for purposes of this section.

"SEC. 860K. TREATMENT OF TRANSFERS OF HIGH-YIELD INTERESTS TO DISQUALIFIED HOLDERS.

"(a) GENERAL RULE.—In the case of any high-yield interest which is held by a disqualified holder—

"(1) the gross income of such holder shall not include any income (other than gain) attributable to such interest, and

"(2) amounts not includible in the gross income of such holder by reason of paragraph (1) shall be included (at the time otherwise includible under paragraph (1)) in the gross income of the most recent holder of such interest which is not a disqualified holder.

"(b) EXCEPTIONS.—Rules similar to the rules of paragraphs (4) and (7) of section 860E(e) shall apply to the tax imposed by reason of the inclusion in gross income under subsection (a).

"(c) DISQUALIFIED HOLDER.—For purposes of this section, the term 'disqualified holder' means any holder other than—

"(1) an eligible corporation (as defined in section 860L(a)(2)), or

"(2) a FASIT.

"(d) TREATMENT OF INTERESTS HELD BY SECURITIES DEALERS.—

"(1) IN GENERAL.—Subsection (a) shall not apply to any high-yield interest held by a disqualified holder if such holder is a dealer in securities who acquired such interest exclusively for sale to customers in the ordinary course of business (and not for investment).

"(2) CHANGE IN DEALER STATUS.—

"(A) IN GENERAL.—In the case of a dealer in securities which is not an eligible corporation (as defined in section 860L(a)(2)), if—

"(i) such dealer ceases to be a dealer in securities, or

"(ii) such dealer commences holding the high-yield interest for investment,

there is hereby imposed (in addition to other taxes) an excise tax equal to the product of the highest rate of tax specified in section 11(b)(1) and the income of such dealer attributable to such interest for periods after the date of such cessation or commencement.

"(B) HOLDING FOR 31 DAYS OR LESS.—For purposes of subparagraph (A)(ii), a dealer shall not be treated as holding an interest for investment before the thirty-second day after the date such dealer acquired such interest unless such interest is so held as part of a plan to avoid the purposes of this paragraph.

"(C) ADMINISTRATIVE PROVISIONS.—The deficiency procedures of subtitle F shall apply to the tax imposed by this paragraph.

"(e) TREATMENT OF HIGH-YIELD INTERESTS IN PASS-THRU ENTITIES.—

"(1) IN GENERAL.—If a pass-thru entity (as defined in section 860E(e)(6)) issues a debt or equity interest—

"(A) which is supported by any regular interest in a FASIT, and

"(B) which has an original yield to maturity which is greater than each of—

"(i) the sum determined under clauses (i) and (ii) of section 163(i)(1)(B) with respect to such debt or equity interest, and

"(ii) the yield to maturity to such entity on such regular interest (determined as of the date such entity acquired such interest),

there is hereby imposed on the pass-thru entity a tax (in addition to other taxes) equal to the product of the highest rate of tax specified in section 11(b)(1) and the income of the holder of such debt or equity interest which is properly attributable to such regular interest. For purposes of the preceding sentence, the yield to maturity of any equity interest shall be determined under regulations prescribed by the Secretary.

Regulations.

"(2) EXCEPTION.—Paragraph (1) shall not apply to arrangements not having as a principal purpose the avoidance of the purposes of this subsection.

"SEC. 860L. DEFINITIONS AND OTHER SPECIAL RULES.

"(a) FASIT.—

"(1) IN GENERAL.—For purposes of this title, the terms 'financial asset securitization investment trust' and 'FASIT' mean any entity—

"(A) for which an election to be treated as a FASIT applies for the taxable year,

"(B) all of the interests in which are regular interests or the ownership interest,

"(C) which has only one ownership interest and such ownership interest is held directly by an eligible corporation,

"(D) as of the close of the third month beginning after the day of its formation and at all times thereafter, substan-

tially all of the assets of which (including assets treated as held by the entity under section 860I(b)(2)) consist of permitted assets, and

"(E) which is not described in section 851(a).

A rule similar to the rule of the last sentence of section 860D(a) shall apply for purposes of this paragraph.

"(2) ELIGIBLE CORPORATION.—For purposes of paragraph (1)(C), the term 'eligible corporation' means any domestic C corporation other than—

"(A) a corporation which is exempt from, or is not subject to, tax under this chapter,

"(B) an entity described in section 851(a) or 856(a),

"(C) a REMIC, and

"(D) an organization to which part I of subchapter T applies.

"(3) ELECTION.—An entity (otherwise meeting the requirements of paragraph (1)) may elect to be treated as a FASIT. Except as provided in paragraph (5), such an election shall apply to the taxable year for which made and all subsequent taxable years unless revoked with the consent of the Secretary.

"(4) TERMINATION.—If any entity ceases to be a FASIT at any time during the taxable year, such entity shall not be treated as a FASIT after the date of such cessation.

"(5) INADVERTENT TERMINATIONS, ETC.—Rules similar to the rules of section 860D(b)(2)(B) shall apply to inadvertent failures to qualify or remain qualified as a FASIT.

"(6) PERMITTED ASSETS NOT TREATED AS INTEREST IN FASIT.—Except as provided in regulations prescribed by the Secretary, any asset which is a permitted asset at the time acquired by a FASIT shall not be treated at any time as an interest in such FASIT.

"(b) INTERESTS IN FASIT.—For purposes of this part—

"(1) REGULAR INTEREST.—

"(A) IN GENERAL.—The term 'regular interest' means any interest which is issued by a FASIT after the startup date with fixed terms and which is designated as a regular interest if—

"(i) such interest unconditionally entitles the holder to receive a specified principal amount (or other similar amount),

"(ii) interest payments (or other similar amounts), if any, with respect to such interest are determined based on a fixed rate, or, except as otherwise provided by the Secretary, at a variable rate permitted under section 860G(a)(1)(B)(i),

"(iii) such interest does not have a stated maturity (including options to renew) greater than 30 years (or such longer period as may be permitted by regulations),

"(iv) the issue price of such interest does not exceed 125 percent of its stated principal amount, and

"(v) the yield to maturity on such interest is less than the sum determined under section 163(i)(1)(B) with respect to such interest.

An interest shall not fail to meet the requirements of clause (i) merely because the timing (but not the amount) of the principal payments (or other similar amounts) may

be contingent on the extent that payments on debt instruments held by the FASIT are made in advance of anticipated payments and on the amount of income from permitted assets.

"(B) HIGH-YIELD INTERESTS.—

"(i) IN GENERAL.—The term 'regular interest' includes any high-yield interest.

"(ii) HIGH-YIELD INTEREST.—The term 'high-yield interest' means any interest which would be described in subparagraph (A) but for—

"(I) failing to meet the requirements of one or more of clauses (i), (iv), or (v) thereof, or

"(II) failing to meet the requirement of clause (ii) thereof but only if interest payments (or other similar amounts), if any, with respect to such interest consist of a specified portion of the interest payments on permitted assets and such portion does not vary during the period such interest is outstanding.

"(2) OWNERSHIP INTEREST.—The term 'ownership interest' means the interest issued by a FASIT after the startup day which is designated as an ownership interest and which is not a regular interest.

"(c) PERMITTED ASSETS.—For purposes of this part—

"(1) IN GENERAL.—The term 'permitted asset' means—

"(A) cash or cash equivalents,

"(B) any debt instrument (as defined in section 1275(a)(1)) under which interest payments (or other similar amounts), if any, at or before maturity meet the requirements applicable under clause (i) or (ii) of section 860G(a)(1)(B),

"(C) foreclosure property,

"(D) any asset—

"(i) which is an interest rate or foreign currency notional principal contract, letter of credit, insurance, guarantee against payment defaults, or other similar instrument permitted by the Secretary, and

"(ii) which is reasonably required to guarantee or hedge against the FASIT's risks associated with being the obligor on interests issued by the FASIT,

"(E) contract rights to acquire debt instruments described in subparagraph (B) or assets described in subparagraph (D),

"(F) any regular interest in another FASIT, and

"(G) any regular interest in a REMIC.

"(2) DEBT ISSUED BY HOLDER OF OWNERSHIP INTEREST NOT PERMITTED ASSET.—The term 'permitted asset' shall not include any debt instrument issued by the holder of the ownership interest in the FASIT or by any person related to such holder or any direct or indirect interest in such a debt instrument. The preceding sentence shall not apply to cash equivalents and to any other investment specified in regulations prescribed by the Secretary.

"(3) FORECLOSURE PROPERTY.—

"(A) IN GENERAL.—The term 'foreclosure property' means property—

"(i) which would be foreclosure property under section 856(e) (determined without regard to paragraph (5) thereof) if such property were real property acquired by a real estate investment trust, and

"(ii) which is acquired in connection with the default or imminent default of a debt instrument held by the FASIT unless the security interest in such property was created for the principal purpose of permitting the FASIT to invest in such property.

Solely for purposes of subsection (a)(1), the determination of whether any property is foreclosure property shall be made without regard to section 856(e)(4).

"(B) AUTHORITY TO REDUCE GRACE PERIOD.—In the case of property other than real property and other than personal property incident to real property, the Secretary may by regulation reduce for purposes of subparagraph (A) the periods otherwise applicable under paragraphs (2) and (3) of section 856(e).

"(d) STARTUP DAY.—For purposes of this part—

"(1) IN GENERAL.—The term 'startup day' means the date designated in the election under subsection (a)(3) as the startup day of the FASIT. Such day shall be the beginning of the first taxable year of the FASIT.

"(2) TREATMENT OF PROPERTY HELD ON STARTUP DAY.—All property held (or treated as held under section 860I(c)(2)) by an entity as of the startup day shall be treated as contributed to such entity on such day by the holder of the ownership interest in such entity.

"(e) TAX ON PROHIBITED TRANSACTIONS.—

"(1) IN GENERAL.—There is hereby imposed for each taxable year of a FASIT a tax equal to 100 percent of the net income derived from prohibited transactions. Such tax shall be paid by the holder of the ownership interest in the FASIT.

"(2) PROHIBITED TRANSACTIONS.—For purposes of this part, the term 'prohibited transaction' means—

"(A) the receipt of any income derived from any asset that is not a permitted asset,

"(B) except as provided in paragraph (3), the disposition of any permitted asset,

"(C) the receipt of any income derived from any loan originated by the FASIT, and

"(D) the receipt of any income representing a fee or other compensation for services (other than any fee received as compensation for a waiver, amendment, or consent under permitted assets (other than foreclosure property) held by the FASIT).

"(3) EXCEPTION FOR INCOME FROM CERTAIN DISPOSITIONS.—

"(A) IN GENERAL.—Paragraph (2)(B) shall not apply to a disposition which would not be a prohibited transaction (as defined in section 860F(a)(2)) by reason of—

"(i) clause (ii), (iii), or (iv) of section 860F(a)(2)(A), or

"(ii) section 860F(a)(5), if the FASIT were treated as a REMIC and debt instruments described in subsection (c)(1)(B) were treated as qualified mortgages.

"(B) SUBSTITUTION OF DEBT INSTRUMENTS; REDUCTION OF OVER-COLLATERALIZATION.—Paragraph (2)(B) shall not apply to—

"(i) the substitution of a debt instrument described in subsection (c)(1)(B) for another debt instrument which is a permitted asset, or

"(ii) the distribution of a debt instrument contributed by the holder of the ownership interest to such holder in order to reduce over-collateralization of the FASIT,

but only if a principal purpose of acquiring the debt instrument which is disposed of was not the recognition of gain (or the reduction of a loss) as a result of an increase in the market value of the debt instrument after its acquisition by the FASIT.

"(C) LIQUIDATION OF CLASS OF REGULAR INTERESTS.—Paragraph (2)(B) shall not apply to the complete liquidation of any class of regular interests.

"(4) NET INCOME.—For purposes of this subsection, net income shall be determined in accordance with section 860F(a)(3).

"(f) COORDINATION WITH OTHER PROVISIONS.—

"(1) WASH SALES RULES.—Rules similar to the rules of section 860F(d) shall apply to the ownership interest in a FASIT.

"(2) SECTION 475.—Except as provided by the Secretary by regulations, if any security which is sold or contributed to a FASIT by the holder of the ownership interest in such FASIT was required to be marked-to-market under section 475 by such holder, section 475 shall continue to apply to such security; except that in applying section 475 while such security is held by the FASIT, the fair market value of such security for purposes of section 475 shall not be less than its value under section 860I(d).

"(g) RELATED PERSON.—For purposes of this part, a person (hereinafter in this subsection referred to as the 'related person') is related to any person if—

"(1) the related person bears a relationship to such person specified in section 267(b) or section 707(b)(1), or

"(2) the related person and such person are engaged in trades or businesses under common control (within the meaning of subsections (a) and (b) of section 52).

For purposes of paragraph (1), in applying section 267(b) or 707(b)(1), '20 percent' shall be substituted for '50 percent'.

"(h) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this part, including regulations to prevent the abuse of the purposes of this part through transactions which are not primarily related to securitization of debt instruments by a FASIT.".

(b) TECHNICAL AMENDMENTS.—

(1) Paragraph (2) of section 26(b) is amended by striking "and" at the end of subparagraph (M), by striking the period at the end of subparagraph (N) and inserting ", and", and by adding at the end the following new subparagraph:

"(O) section 860K (relating to treatment of transfers of high-yield interests to disqualified holders).".

(2) Paragraph (6) of section 56(g) is amended by striking "or REMIC" and inserting "REMIC, or FASIT".

(3) Clause (ii) of section 382(l)(4)(B) is amended by striking "or a REMIC to which part IV of subchapter M applies" and inserting "a REMIC to which part IV of subchapter M applies, or a FASIT to which part V of subchapter M applies".

(4) Paragraph (1) of section 582(c) is amended by inserting ", and any regular interest in a FASIT," after "REMIC".

(5) Subparagraph (E) of section 856(c)(6) is amended by adding at the end the following new sentence: "The principles of the preceding provisions of this subparagraph shall apply to regular interests in a FASIT.".

(6) Paragraph (3) of section 860G(a) is amended by striking "and" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", and", and by inserting after subparagraph (C) the following new subparagraph:

"(D) any regular interest in a FASIT which is transferred to, or purchased by, the REMIC as described in clauses (i) and (ii) of subparagraph (A) but only if 95 percent or more of the value of the assets of such FASIT is at all times attributable to obligations described in subparagraph (A) (without regard to such clauses).".

(7) Subparagraph (C) of section 1202(e)(4) is amended by striking "or REMIC" and inserting "REMIC, or FASIT".

(8) Clause (xi) of section 7701(a)(19)(C) is amended to read as follows:

"(xi) any regular or residual interest in a REMIC, and any regular interest in a FASIT, but only in the proportion which the assets of such REMIC or FASIT consist of property described in any of the preceding clauses of this subparagraph; except that if 95 percent or more of the assets of such REMIC or FASIT are assets described in clauses (i) through (x), the entire interest in the REMIC or FASIT shall qualify.".

(9) Subparagraph (A) of section 7701(i)(2) is amended by inserting "or a FASIT" after "a REMIC".

(c) CLERICAL AMENDMENT.—The table of parts for subchapter M of chapter 1 is amended by adding at the end the following new item:

"Part V. Financial asset securitization investment trusts.".

(d) EFFECTIVE DATE.—The amendments made by this section shall take effect on September 1, 1997. 26 USC 26 note.

(e) TREATMENT OF EXISTING SECURITIZATION ENTITIES.— 26 USC 860I note.

(1) IN GENERAL.—In the case of the holder of the ownership interest in a pre-effective date FASIT—

(A) gain shall not be recognized under section 860L(d)(2) of the Internal Revenue Code of 1986 on property deemed contributed to the FASIT, and

(B) gain shall not be recognized under section 860I of such Code on property contributed to such FASIT,

until such property (or portion thereof) ceases to be properly allocable to a pre-FASIT interest.

(2) ALLOCATION OF PROPERTY TO PRE-FASIT INTEREST.—For purposes of paragraph (1), property shall be allocated to a pre-FASIT interest in such manner as the Secretary of the Treasury may prescribe, except that all property in a FASIT

shall be treated as properly allocable to pre-FASIT interests if the fair market value of all such property does not exceed 107 percent of the aggregate principal amount of all outstanding pre-FASIT interests.

(3) DEFINITIONS.—For purposes of this subsection—

(A) PRE-EFFECTIVE DATE FASIT.—The term "pre-effective date FASIT" means any FASIT if the entity (with respect to which the election under section 860L(a)(3) of such Code was made) is in existence on August 31, 1997.

(B) PRE-FASIT INTEREST.—The term "pre-FASIT interest" means any interest in the entity referred to in subparagraph (A) which was issued before the startup day (other than any interest held by the holder of the ownership interest in the FASIT).

Subtitle G—Technical Corrections

SEC. 1701. COORDINATION WITH OTHER SUBTITLES.

For purposes of applying the amendments made by any subtitle of this title other than this subtitle, the provisions of this subtitle shall be treated as having been enacted immediately before the provisions of such other subtitles.

26 USC 1 note.

SEC. 1702. AMENDMENTS RELATED TO REVENUE RECONCILIATION ACT OF 1990.

(a) AMENDMENTS RELATED TO SUBTITLE A.—

(1) Subparagraph (B) of section 59(j)(3) is amended by striking "section 1(i)(3)(B)" and inserting "section 1(g)(3)(B)".

(2) Clause (i) of section 151(d)(3)(C) is amended by striking "joint of a return" and inserting "joint return".

(b) AMENDMENTS RELATED TO SUBTITLE B.—

26 USC 6724.

(1) Paragraph (1) of section 11212(e) of the Revenue Reconciliation Act of 1990 is amended by striking "Paragraph (1) of section 6724(d)" and inserting "Subparagraph (B) of section 6724(d)(1)".

(2)(A) Subparagraph (B) of section 4093(c)(2), as in effect before the amendments made by the Revenue Reconciliation Act of 1993, is amended by inserting before the period "unless such fuel is sold for exclusive use by a State or any political subdivision thereof".

(B) Paragraph (4) of section 6427(l), as in effect before the amendments made by the Revenue Reconciliation Act of 1993, is amended by inserting before the period "unless such fuel was used by a State or any political subdivision thereof".

(3) Paragraph (1) of section 6416(b) is amended by striking "chapter 32 or by section 4051" and inserting "chapter 31 or 32".

(4) Section 7012 is amended—

(A) by striking "production or importation of gasoline" in paragraph (3) and inserting "taxes on gasoline and diesel fuel", and

(B) by striking paragraph (4) and redesignating paragraphs (5) and (6) as paragraphs (4) and (5), respectively.

(5) Subsection (c) of section 5041 is amended by striking paragraph (6) and by inserting the following new paragraphs:

"(6) CREDIT FOR TRANSFEREE IN BOND.—If—

"(A) wine produced by any person would be eligible for any credit under paragraph (1) if removed by such person during the calendar year,

"(B) wine produced by such person is removed during such calendar year by any other person (hereafter in this paragraph referred to as the 'transferee') to whom such wine was transferred in bond and who is liable for the tax imposed by this section with respect to such wine, and

"(C) such producer holds title to such wine at the time of its removal and provides to the transferee such information as is necessary to properly determine the transferee's credit under this paragraph,

then, the transferee (and not the producer) shall be allowed the credit under paragraph (1) which would be allowed to the producer if the wine removed by the transferee had been removed by the producer on that date.

"(7) REGULATIONS.—The Secretary may prescribe such regulations as may be necessary to carry out the purposes of this subsection, including regulations—

"(A) to prevent the credit provided in this subsection from benefiting any person who produces more than 250,000 wine gallons of wine during a calendar year, and

"(B) to assure proper reduction of such credit for persons producing more than 150,000 wine gallons of wine during a calendar year.".

(6) Paragraph (3) of section 5061(b) is amended to read as follows:

"(3) section 5041(f),".

(7) Section 5354 is amended by inserting "(taking into account the appropriate amount of credit with respect to such wine under section 5041(c))" after "any one time".

(c) AMENDMENTS RELATED TO SUBTITLE C.—

(1) Paragraph (4) of section 56(g) is amended by redesignating subparagraphs (I) and (J) as subparagraphs (H) and (I), respectively.

(2) Subparagraph (B) of section 6724(d)(1) is amended—

(A) by striking "or" at the end of clause (xii), and

(B) by striking the period at the end of clause (xiii) and inserting ", or".

(3) Subsection (g) of section 6302 is amended by inserting ", 22," after "chapters 21".

(4) The earnings and profits of any insurance company to which section 11305(c)(3) of the Revenue Reconciliation Act of 1990 applies shall be determined without regard to any deduction allowed under such section; except that, for purposes of applying sections 56 and 902, and subpart F of part III of subchapter N of chapter 1 of the Internal Revenue Code of 1986, such deduction shall be taken into account. 26 USC 832 note.

(5) Subparagraph (D) of section 6038A(e)(4) is amended—

(A) by striking "any transaction to which the summons relates" and inserting "any affected taxable year", and

(B) by adding at the end thereof the following new sentence: "For purposes of this subparagraph, the term 'affected taxable year' means any taxable year if the determination of the amount of tax imposed for such taxable

year is affected by the treatment of the transaction to which the summons relates.".

(6) Subparagraph (A) of section 6621(c)(2) is amended by adding at the end thereof the following new flush sentence:

"The preceding sentence shall be applied without regard to any such letter or notice which is withdrawn by the Secretary.".

(7) Clause (i) of section 6621(c)(2)(B) is amended by striking "this subtitle" and inserting "this title".

(d) AMENDMENTS RELATED TO SUBTITLE D.—

26 USC 41 note.

(1) Notwithstanding section 11402(c) of the Revenue Reconciliation Act of 1990, the amendment made by section 11402(b)(1) of such Act shall apply to taxable years ending after December 31, 1989.

(2) Clause (ii) of section 143(m)(4)(C) is amended—

(A) by striking "any month of the 10-year period" and inserting "any year of the 4-year period",

(B) by striking "succeeding months" and inserting "succeeding years", and

(C) by striking "over the remainder of such period (or, if lesser, 5 years)" and inserting "to zero over the succeeding 5 years".

(e) AMENDMENTS RELATED TO SUBTITLE E.—

(1)(A) Clause (ii) of section 56(d)(1)(B) is amended to read as follows:

"(ii) appropriate adjustments in the application of section 172(b)(2) shall be made to take into account the limitation of subparagraph (A).".

26 USC 56 note.

(B) For purposes of applying sections 56(g)(1) and 56(g)(3) of the Internal Revenue Code of 1986 with respect to taxable years beginning in 1991 and 1992, the reference in such sections to the alternative tax net operating loss deduction shall be treated as including a reference to the deduction under section 56(h) of such Code as in effect before the amendments made by section 1915 of the Energy Policy Act of 1992.

(2) Clause (i) of section 613A(c)(3)(A) is amended by striking "the table contained in".

(3) Section 6501 is amended—

(A) by striking subsection (m) (relating to deficiency attributable to election under section 44B) and by redesignating subsections (n) and (o) as subsections (m) and (n), respectively, and

(B) by striking "section 40(f) or 51(j)" in subsection (m) (as redesignated by subparagraph (A)) and inserting "section 40(f), 43, or 51(j)".

(4) Subparagraph (C) of section 38(c)(2) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990) is amended by inserting before the period at the end of the first sentence the following: "and without regard to the deduction under section 56(h)".

26 USC 53 note.

(5) The amendment made by section 1913(b)(2)(C)(i) of the Energy Policy Act of 1992 shall apply to taxable years beginning after December 31, 1990.

(f) AMENDMENTS RELATED TO SUBTITLE F.—

(1)(A) Section 2701(a)(3) is amended by adding at the end thereof the following new subparagraph:

"(C) VALUATION OF QUALIFIED PAYMENTS WHERE NO LIQUIDATION, ETC. RIGHTS.—In the case of an applicable retained interest which is described in subparagraph (B)(i) but not subparagraph (B)(ii), the value of the distribution right shall be determined without regard to this section.".

(B) Section 2701(a)(3)(B) is amended by inserting "CERTAIN" before "QUALIFIED" in the heading thereof.

(C) Sections 2701 (d)(1) and (d)(4) are each amended by striking "subsection (a)(3)(B)" and inserting "subsection (a)(3)(B) or (C)".

(2) Clause (i) of section 2701(a)(4)(B) is amended by inserting "(or, to the extent provided in regulations, the rights as to either income or capital)" after "income and capital".

(3)(A) Section 2701(b)(2) is amended by adding at the end thereof the following new subparagraph:

"(C) APPLICABLE FAMILY MEMBER.—For purposes of this subsection, the term 'applicable family member' includes any lineal descendant of any parent of the transferor or the transferor's spouse.".

(B) Section 2701(e)(3) is amended—

(i) by striking subparagraph (B), and

(ii) by striking so much of paragraph (3) as precedes "shall be treated as holding" and inserting:

"(3) ATTRIBUTION OF INDIRECT HOLDINGS AND TRANSFERS.—An individual".

(C) Section 2704(c)(3) is amended by striking "section 2701(e)(3)(A)" and inserting "section 2701(e)(3)".

(4) Clause (i) of section 2701(c)(1)(B) is amended to read as follows:

"(i) a right to distributions with respect to any interest which is junior to the rights of the transferred interest,".

(5)(A) Clause (i) of section 2701(c)(3)(C) is amended to read as follows:

"(i) IN GENERAL.—Payments under any interest held by a transferor which (without regard to this subparagraph) are qualified payments shall be treated as qualified payments unless the transferor elects not to treat such payments as qualified payments. Payments described in the preceding sentence which are held by an applicable family member shall be treated as qualified payments only if such member elects to treat such payments as qualified payments.".

(B) The first sentence of section 2701(c)(3)(C)(ii) is amended to read as follows: "A transferor or applicable family member holding any distribution right which (without regard to this subparagraph) is not a qualified payment may elect to treat such right as a qualified payment, to be paid in the amounts and at the times specified in such election.".

(C) The time for making an election under the second sentence of section 2701(c)(3)(C)(i) of the Internal Revenue Code of 1986 (as amended by subparagraph (A)) shall not expire before the due date (including extensions) for filing the transferor's return of the tax imposed by section 2501 of such Code for the first calendar year ending after the date of enactment. 26 USC 2701 note.

(6) Section 2701(d)(3)(A)(iii) is amended by striking "the period ending on the date of".

(7) Subclause (I) of section 2701(d)(3)(B)(ii) is amended by inserting "or the exclusion under section 2503(b)," after "section 2523,".

(8) Section 2701(e)(5) is amended—

(A) by striking "such contribution to capital or such redemption, recapitalization, or other change" in subparagraph (A) and inserting "such transaction", and

(B) by striking "the transfer" in subparagraph (B) and inserting "such transaction".

(9) Section 2701(d)(4) is amended by adding at the end thereof the following new subparagraph:

"(C) TRANSFER TO TRANSFERORS.—In the case of a taxable event described in paragraph (3)(A)(ii) involving a transfer of an applicable retained interest from an applicable family member to a transferor, this subsection shall continue to apply to the transferor during any period the transferor holds such interest.".

(10) Section 2701(e)(6) is amended by inserting "or to reflect the application of subsection (d)" before the period at the end thereof.

(11)(A) Section 2702(a)(3)(A) is amended—

(i) by striking "to the extent" and inserting "if" in clause (i),

(ii) by striking "or" at the end of clause (i),

(iii) by striking the period at the end of clause (ii) and inserting ", or", and

(iv) by adding at the end thereof the following new clause:

"(iii) to the extent that regulations provide that such transfer is not inconsistent with the purposes of this section.".

(B)(i) Section 2702(a)(3) is amended by striking "incomplete transfer" each place it appears and inserting "incomplete gift".

(ii) The heading for section 2702(a)(3)(B) is amended by striking "INCOMPLETE TRANSFER" and inserting "INCOMPLETE GIFT".

(g) AMENDMENTS RELATED TO SUBTITLE G.—

(1)(A) Subsection (a) of section 1248 is amended—

(i) by striking ", or if a United States person receives a distribution from a foreign corporation which, under section 302 or 331, is treated as an exchange of stock" in paragraph (1), and

(ii) by adding at the end thereof the following new sentence: "For purposes of this section, a United States person shall be treated as having sold or exchanged any stock if, under any provision of this subtitle, such person is treated as realizing gain from the sale or exchange of such stock.".

(B) Paragraph (1) of section 1248(e) is amended by striking ", or receives a distribution from a domestic corporation which, under section 302 or 331, is treated as an exchange of stock".

(C) Subparagraph (B) of section 1248(f)(1) is amended by striking "or 361(c)(1)" and inserting "355(c)(1), or 361(c)(1)".

(D) Paragraph (1) of section 1248(i) is amended to read as follows:

"(1) IN GENERAL.—If any shareholder of a 10-percent corporate shareholder of a foreign corporation exchanges stock of the 10-percent corporate shareholder for stock of the foreign corporation, such 10-percent corporate shareholder shall recognize gain in the same manner as if the stock of the foreign corporation received in such exchange had been—

"(A) issued to the 10-percent corporate shareholder, and

"(B) then distributed by the 10-percent corporate shareholder to such shareholder in redemption or liquidation (whichever is appropriate).

The amount of gain recognized by such 10-percent corporate shareholder under the preceding sentence shall not exceed the amount treated as a dividend under this section.".

(2) Section 897 is amended by striking subsection (f).

(3) Paragraph (13) of section 4975(d) is amended by striking "section 408(b)" and inserting "section 408(b)(12)".

(4) Clause (iii) of section 56(g)(4)(D) is amended by inserting ", but only with respect to taxable years beginning after December 31, 1989" before the period at the end thereof.

(5)(A) Paragraph (11) of section 11701(a) of the Revenue Reconciliation Act of 1990 (and the amendment made by such paragraph) are hereby repealed, and section 7108(r)(2) of the Revenue Reconciliation Act of 1989 shall be applied as if such paragraph (and amendment) had never been enacted. 26 USC 42 note.

(B) Subparagraph (A) shall not apply to any building if the owner of such building establishes to the satisfaction of the Secretary of the Treasury or his delegate that such owner reasonably relied on the amendment made by such paragraph (11).

(h) AMENDMENTS RELATED TO SUBTITLE H.—

(1)(A) Clause (vi) of section 168(e)(3)(B) is amended by striking "or" at the end of subclause (I), by striking the period at the end of subclause (II) and inserting ", or", and by adding at the end thereof the following new subclause:

"(III) is described in section 48(l)(3)(A)(ix) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990).".

(B) Subparagraph (B) of section 168(e)(3) (relating to 5-year property) is amended by adding at the end the following flush sentence:

"Nothing in any provision of law shall be construed to treat property as not being described in clause (vi)(I) (or the corresponding provisions of prior law) by reason of being public utility property (within the meaning of section 48(a)(3)).".

(C) Subparagraph (K) of section 168(g)(4) is amended by striking "section 48(a)(3)(A)(iii)" and inserting "section 48(l)(3)(A)(ix) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)".

(2) Clause (ii) of section 172(b)(1)(E) is amended by striking "subsection (m)" and inserting "subsection (h)".

(3) Sections 805(a)(4)(E), 832(b)(5)(C)(ii)(II), and 832(b)(5)(D)(ii)(II) are each amended by striking "243(b)(5)" and inserting "243(b)(2)".

(4) Subparagraph (A) of section 243(b)(3) is amended by inserting "of" after "In the case".

(5) The subsection heading for subsection (a) of section 280F is amended by striking "INVESTMENT TAX CREDIT AND".

(6) Clause (i) of section 1504(c)(2)(B) is amended by inserting "section" before "243(b)(2)".

(7) Paragraph (3) of section 341(f) is amended by striking "351, 361, 371(a), or 374(a)" and inserting "351, or 361".

(8) Paragraph (2) of section 243(b) is amended to read as follows:

"(2) AFFILIATED GROUP.—For purposes of this subsection:

"(A) IN GENERAL.—The term 'affiliated group' has the meaning given such term by section 1504(a), except that for such purposes sections 1504(b)(2), 1504(b)(4), and 1504(c) shall not apply.

"(B) GROUP MUST BE CONSISTENT IN FOREIGN TAX TREATMENT.—The requirements of paragraph (1)(A) shall not be treated as being met with respect to any dividend received by a corporation if, for any taxable year which includes the day on which such dividend is received—

"(i) 1 or more members of the affiliated group referred to in paragraph (1)(A) choose to any extent to take the benefits of section 901, and

"(ii) 1 or more other members of such group claim to any extent a deduction for taxes otherwise creditable under section 901.".

26 USC 861. (9) The amendment made by section 11813(b)(17) of the Revenue Reconciliation Act of 1990 shall be applied as if the material stricken by such amendment included the closing parenthesis after "section 48(a)(5)".

(10) Paragraph (1) of section 179(d) is amended by striking "in a trade or business" and inserting "a trade or business".

(11) Subparagraph (E) of section 50(a)(2) is amended by striking "section 48(a)(5)(A)" and inserting "section 48(a)(5)".

26 USC 56. (12) The amendment made by section 11801(c)(9)(G)(ii) of the Revenue Reconciliation Act of 1990 shall be applied as if it struck "Section 422A(c)(2)" and inserted "Section 422(c)(2)".

(13) Subparagraph (B) of section 424(c)(3) is amended by striking "a qualified stock option, an incentive stock option, an option granted under an employee stock purchase plan, or a restricted stock option" and inserting "an incentive stock option or an option granted under an employee stock purchase plan".

(14) Subparagraph (E) of section 1367(a)(2) is amended by striking "section 613A(c)(13)(B)" and inserting "section 613A(c)(11)(B)".

(15) Subparagraph (B) of section 460(e)(6) is amended by striking "section 167(k)" and inserting "section 168(e)(2)(A)(ii)".

(16) Subparagraph (C) of section 172(h)(4) is amended by striking "subsection (b)(1)(M)" and inserting "subsection (b)(1)(E)".

(17) Section 6503 is amended—

(A) by redesignating the subsection relating to extension in case of certain summonses as subsection (j), and

(B) by redesignating the subsection relating to cross references as subsection (k).

(18) Paragraph (4) of section 1250(e) is hereby repealed.

(19) Paragraph (1) of section 179(d) is amended by adding at the end the following new sentence: "Such term shall not

include any property described in section 50(b) and shall not include air conditioning or heating units.".

"(i) EFFECTIVE DATE.—Except as otherwise expressly provided, any amendment made by this section shall take effect as if included in the provision of the Revenue Reconciliation Act of 1990 to which such amendment relates.". 26 USC 38 note.

SEC. 1703. AMENDMENTS RELATED TO REVENUE RECONCILIATION ACT OF 1993.

(a) AMENDMENT RELATED TO SECTION 13114.—Paragraph (2) of section 1044(c) is amended to read as follows: 26 USC 1044.

"(2) PURCHASE.—The taxpayer shall be considered to have purchased any property if, but for subsection (d), the unadjusted basis of such property would be its cost within the meaning of section 1012.".

(b) AMENDMENTS RELATED TO SECTION 13142.—

(1) Subparagraph (B) of section 13142(b)(6) of the Revenue Reconciliation Act of 1993 is amended to read as follows: 26 USC 42 note.

"(B) FULL-TIME STUDENTS, WAIVER AUTHORITY, AND PROHIBITED DISCRIMINATION.—The amendments made by paragraphs (2), (3), and (4) shall take effect on the date of the enactment of this Act.".

(2) Subparagraph (C) of section 13142(b)(6) of such Act is amended by striking "paragraph (2)" and inserting "paragraph (5)".

(c) AMENDMENT RELATED TO SECTION 13161.—

(1) IN GENERAL.—Subsection (e) of section 4001 (relating to inflation adjustment) is amended to read as follows: 26 USC 4001.

"(e) INFLATION ADJUSTMENT.—

"(1) IN GENERAL.—The $30,000 amount in subsection (a) and section 4003(a) shall be increased by an amount equal to—

"(A) $30,000, multiplied by

"(B) the cost-of-living adjustment under section 1(f)(3) for the calendar year in which the vehicle is sold, determined by substituting 'calendar year 1990' for 'calendar year 1992' in subparagraph (B) thereof.

"(2) ROUNDING.—If any amount as adjusted under paragraph (1) is not a multiple of $2,000, such amount shall be rounded to the next lowest multiple of $2,000.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect on the date of the enactment of this Act. 26 USC 4001 note.

(d) AMENDMENT RELATED TO SECTION 13201.—Clause (ii) of section 135(b)(2)(B) is amended by inserting before the period at the end thereof the following: ", determined by substituting 'calendar year 1989' for 'calendar year 1992' in subparagraph (B) thereof". 26 USC 135.

(e) AMENDMENTS RELATED TO SECTION 13203.—Subsection (a) of section 59 is amended— 26 USC 59.

(1) by striking "the amount determined under section 55(b)(1)(A)" in paragraph (1)(A) and (2)(A)(i) and inserting "the pre-credit tentative minimum tax",

(2) by striking "specified in section 55(b)(1)(A)" in paragraph (1)(C) and inserting "specified in subparagraph (A)(i) or (B)(i) of section 55(b)(1) (whichever applies)",

(3) by striking "which would be determined under section 55(b)(1)(A)" in paragraph (2)(A)(ii) and inserting "which would be the pre-credit tentative minimum tax", and

(4) by adding at the end thereof the following new paragraph:

"(3) PRE-CREDIT TENTATIVE MINIMUM TAX.—For purposes of this subsection, the term 'pre-credit tentative minimum tax' means—

"(A) in the case of a taxpayer other than a corporation, the amount determined under the first sentence of section 55(b)(1)(A)(i), or

"(B) in the case of a corporation, the amount determined under section 55(b)(1)(B)(i).".

(f) AMENDMENT RELATED TO SECTION 13221.—Sections 1201(a) and 1561(a) are each amended by striking "last sentence" each place it appears and inserting "last 2 sentences".

(g) AMENDMENTS RELATED TO SECTION 13222.—

(1) Subparagraph (B) of section 6033(e)(1) is amended by adding at the end thereof the following new clause:

"(iii) COORDINATION WITH SECTION 527(f).—This subsection shall not apply to any amount on which tax is imposed by reason of section 527(f).".

(2) Clause (i) of section 6033(e)(1)(B) is amended by striking "this subtitle" and inserting "section 501".

(h) AMENDMENT RELATED TO SECTION 13225.—Paragraph (3) of section 6655(g) is amended by striking all that follows "'3rd month'" in the sentence following subparagraph (C) and inserting ", subsection (e)(2)(A) shall be applied by substituting '2 months' for '3 months' in clause (i)(I), the election under clause (i) of subsection (e)(2)(C) may be made separately for each installment, and clause (ii) of subsection (e)(2)(C) shall not apply.".

(i) AMENDMENTS RELATED TO SECTION 13231.—

(1) Subparagraph (G) of section 904(d)(3) is amended by striking "section 951(a)(1)(B)" and inserting "subparagraph (B) or (C) of section 951(a)(1)".

(2) Paragraph (1) of section 956A(b) is amended to read as follows:

"(1) the amount (not including a deficit) referred to in section 316(a)(1) to the extent such amount was accumulated in prior taxable years beginning after September 30, 1993, and".

(3) Subsection (f) of section 956A is amended by inserting before the period at the end thereof: "and regulations coordinating the provisions of subsections (c)(3)(A) and (d)".

(4) Subsection (b) of section 958 is amended by striking "956(b)(2)" each place it appears and inserting "956(c)(2)".

(5)(A) Subparagraph (A) of section 1297(d)(2) is amended by striking "The adjusted basis of any asset" and inserting "The amount taken into account under section 1296(a)(2) with respect to any asset".

(B) The paragraph heading of paragraph (2) of section 1297(d) is amended to read as follows:

"(2) AMOUNT TAKEN INTO ACCOUNT.—".

(6) Subsection (e) of section 1297 is amended by inserting "For purposes of this part—" after the subsection heading.

(j) AMENDMENT RELATED TO SECTION 13241.—Subparagraph (B) of section 40(e)(1) is amended to read as follows:

"(B) for any period before January 1, 2001, during which the rates of tax under section 4081(a)(2)(A) are 4.3 cents per gallon.".

(k) AMENDMENT RELATED TO SECTION 13242.—Paragraph (4) of section 6427(f) is amended by striking "1995" and inserting "1999".

(l) AMENDMENT RELATED TO SECTION 13261.—Clause (iii) of section 13261(g)(2)(A) of the Revenue Reconciliation Act of 1993 is amended by striking "by the taxpayer" and inserting "by the taxpayer or a related person". 26 USC 197 note.

(m) AMENDMENT RELATED TO SECTION 13301.—Subparagraph (B) of section 1397B(d)(5) is amended by striking "preceding".

(n) CLERICAL AMENDMENTS.—

(1) Subsection (d) of section 39 is amended—

(A) by striking "45" in the heading of paragraph (5) and inserting "45A", and

(B) by striking "45" in the heading of paragraph (6) and inserting "45B".

(2) Subparagraph (A) of section 108(d)(9) is amended by striking "paragraph (3)(B)" and inserting "paragraph (3)(C)".

(3) Subparagraph (C) of section 143(d)(2) is amended by striking the period at the end thereof and inserting a comma.

(4) Clause (ii) of section 163(j)(6)(E) is amended by striking "which is a" and inserting "which is".

(5) Subparagraph (A) of section 1017(b)(4) is amended by striking "subsection (b)(2)(D)" and inserting "subsection (b)(2)(E)".

(6) So much of section 1245(a)(3) as precedes subparagraph (A) thereof is amended to read as follows:

"(3) SECTION 1245 PROPERTY.—For purposes of this section, the term 'section 1245 property' means any property which is or has been property of a character subject to the allowance for depreciation provided in section 167 and is either—".

(7) Paragraph (2) of section 1394(e) is amended—

(A) by striking "(i)" and inserting "(A)", and

(B) by striking "(ii)" and inserting "(B)".

(8) Subsection (m) of section 6501 (as redesignated by section 1602) is amended by striking "or 51(j)" and inserting "45B, or 51(j)".

(9)(A) The section 6714 added by section 13242(b)(1) of the Revenue Reconciliation Act of 1993 is hereby redesignated as section 6715.

(B) The table of sections for part I of subchapter B of chapter 68 is amended by striking "6714" in the item added by such section 13242(b)(2) of such Act and inserting "6715".

(10) Paragraph (2) of section 9502(b) is amended by inserting "and before" after "1982,".

(11) Subsection (a)(3) of section 13206 of the Revenue Reconciliation Act of 1993 is amended by striking "this section" and inserting "this subsection". 26 USC 1258 note.

(12) Paragraph (1) of section 13215(c) of the Revenue Reconciliation Act of 1993 is amended by striking "Public Law 92–21" and inserting "Public Law 98–21". 42 USC 401 note.

(13) Paragraph (2) of section 13311(e) of the Revenue Reconciliation Act of 1993 is amended by striking "section 1393(a)(3)" and inserting "section 1393(a)(2)". 26 USC 38 note.

(14) Subparagraph (B) of section 117(d)(2) is amended by striking "section 132(f)" and inserting "section 132(h)".

26 USC 39 note. (o) EFFECTIVE DATE.—Any amendment made by this section shall take effect as if included in the provision of the Revenue Reconciliation Act of 1993 to which such amendment relates.

SEC. 1704. MISCELLANEOUS PROVISIONS.

26 USC 401, 420, 4980. (a) APPLICATION OF AMENDMENTS MADE BY TITLE XII OF OMNIBUS BUDGET RECONCILIATION ACT OF 1990.—Except as otherwise expressly provided, whenever in title XII of the Omnibus Budget Reconciliation Act of 1990 an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

(b) TREATMENT OF CERTAIN AMOUNTS UNDER HEDGE BOND RULES.—

(1) IN GENERAL.—Clause (iii) of section 149(g)(3)(B) is amended to read as follows:

"(iii) AMOUNTS HELD PENDING REINVESTMENT OR REDEMPTION.—Amounts held for not more than 30 days pending reinvestment or bond redemption shall be treated as invested in bonds described in clause (i).".

26 USC 149 note. (2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 7651 of the Omnibus Budget Reconciliation Act of 1989.

(c) TREATMENT OF CERTAIN DISTRIBUTIONS UNDER SECTION 1445.—

(1) IN GENERAL.—Paragraph (3) of section 1445(e) is amended by adding at the end thereof the following new sentence: "Rules similar to the rules of the preceding provisions of this paragraph shall apply in the case of any distribution to which section 301 applies and which is not made out of the earnings and profits of such a domestic corporation.".

26 USC 1445 note. (2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to distributions after the date of the enactment of this Act.

(d) TREATMENT OF CERTAIN CREDITS UNDER SECTION 469.—

(1) IN GENERAL.—Subparagraph (B) of section 469(c)(3) is amended by adding at the end thereof the following new sentence: "If the preceding sentence applies to the net income from any property for any taxable year, any credits allowable under subpart B (other than section 27(a)) or D of part IV of subchapter A for such taxable year which are attributable to such property shall be treated as credits not from a passive activity to the extent the amount of such credits does not exceed the regular tax liability of the taxpayer for the taxable year which is allocable to such net income.".

26 USC 469 note. (2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1986.

(e) TREATMENT OF DISPOSITIONS UNDER PASSIVE LOSS RULES.—

(1) IN GENERAL.—Subparagraph (A) of section 469(g)(1) is amended to read as follows:

"(A) IN GENERAL.—If all gain or loss realized on such disposition is recognized, the excess of—

"(i) any loss from such activity for such taxable year (determined after the application of subsection (b)), over

"(ii) any net income or gain for such taxable year from all other passive activities (determined after the application of subsection (b)),

shall be treated as a loss which is not from a passive activity.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1986. 26 USC 469 note.

(f) MISCELLANEOUS AMENDMENTS TO FOREIGN PROVISIONS.—

(1) COORDINATION OF UNIFIED ESTATE TAX CREDIT WITH TREATIES.—Subparagraph (A) of section 2102(c)(3) is amended by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, property shall not be treated as situated in the United States if such property is exempt from the tax imposed by this subchapter under any treaty obligation of the United States.".

(2) TREATMENT OF CERTAIN INTEREST PAID TO RELATED PERSON.—

(A) Subparagraph (B) of section 163(j)(1) is amended by inserting before the period at the end thereof the following: "(and clause (ii) of paragraph (2)(A) shall not apply for purposes of applying this subsection to the amount so treated)".

(B) Subsection (j) of section 163 is amended by redesignating paragraph (7) as paragraph (8) and by inserting after paragraph (6) the following new paragraph:

"(7) COORDINATION WITH PASSIVE LOSS RULES, ETC.—This subsection shall be applied before sections 465 and 469.".

(C) The amendments made by this paragraph shall apply as if included in the amendments made by section 7210(a) of the Revenue Reconciliation Act of 1989. 26 USC 163 note.

(3) TREATMENT OF INTEREST ALLOCABLE TO EFFECTIVELY CONNECTED INCOME.—

(A) IN GENERAL.—

(i) Subparagraph (B) of section 884(f)(1) is amended by striking "to the extent" and all that follows down through "subparagraph (A)" and inserting "to the extent that the allocable interest exceeds the interest described in subparagraph (A)".

(ii) The second sentence of section 884(f)(1) is amended by striking "reasonably expected" and all that follows down through the period at the end thereof and inserting "reasonably expected to be allocable interest.".

(iii) Paragraph (2) of section 884(f) is amended to read as follows:

"(2) ALLOCABLE INTEREST.—For purposes of this subsection, the term 'allocable interest' means any interest which is allocable to income which is effectively connected (or treated as effectively connected) with the conduct of a trade or business in the United States.".

(B) EFFECTIVE DATE.—The amendments made by subparagraph (A) shall take effect as if included in the 26 USC 884 note.

amendments made by section 1241(a) of the Tax Reform Act of 1986.

(4) CLARIFICATION OF SOURCE RULE.—

(A) IN GENERAL.—Paragraph (2) of section 865(b) is amended by striking "863(b)" and inserting "863".

26 USC 865 note.

(B) EFFECTIVE DATE.—The amendment made by subparagraph (A) shall take effect as if included in the amendments made by section 1211 of the Tax Reform Act of 1986.

(5) REPEAL OF OBSOLETE PROVISIONS.—

(A) Paragraph (1) of section 6038(a) is amended by striking ", and" at the end of subparagraph (E) and inserting a period, and by striking subparagraph (F).

(B) Subsection (b) of section 6038A is amended by adding "and" at the end of paragraph (2), by striking ", and" at the end of paragraph (3) and inserting a period, and by striking paragraph (4).

(g) CLARIFICATION OF TREATMENT OF MEDICARE ENTITLEMENT UNDER COBRA PROVISIONS.—

(1) IN GENERAL.—

(A) Subclause (V) of section 4980B(f)(2)(B)(i) is amended to read as follows:

"(V) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in paragraph (3)(B) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this clause before the close of the 36-month period beginning on the date the covered employee became so entitled.".

29 USC 1162.

(B) Clause (v) of section 602(2)(A) of the Employee Retirement Income Security Act of 1974 is amended to read as follows:

"(v) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in section 603(2) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this subparagraph before the close of the 36-month period beginning on the date the covered employee became so entitled.".

42 USC 300bb–2.

(C) Clause (iv) of section 2202(2)(A) of the Public Health Service Act is amended to read as follows:

"(iv) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in section 2203(2) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this subparagraph before the close

of the 36-month period beginning on the date the covered employee became so entitled.".

(2) EFFECTIVE DATE.—The amendments made by this subsection shall apply to plan years beginning after December 31, 1989. 26 USC 4980B note.

(h) TREATMENT OF CERTAIN REMIC INCLUSIONS.—

(1) IN GENERAL.—Subsection (a) of section 860E is amended by adding at the end thereof the following new paragraph:

"(6) COORDINATION WITH MINIMUM TAX.—For purposes of part VI of subchapter A of this chapter—

"(A) the reference in section 55(b)(2) to taxable income shall be treated as a reference to taxable income determined without regard to this subsection,

"(B) the alternative minimum taxable income of any holder of a residual interest in a REMIC for any taxable year shall in no event be less than the excess inclusion for such taxable year, and

"(C) any excess inclusion shall be disregarded for purposes of computing the alternative tax net operating loss deduction.

The preceding sentence shall not apply to any organization to which section 593 applies, except to the extent provided in regulations prescribed by the Secretary under paragraph (2).".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 671 of the Tax Reform Act of 1986 unless the taxpayer elects to apply such amendment only to taxable years beginning after the date of the enactment of this Act. 26 USC 860E note.

(i) EXEMPTION FROM HARBOR MAINTENANCE TAX FOR CERTAIN PASSENGERS.—

(1) IN GENERAL.—Subparagraph (D) of section 4462(b)(1) (relating to special rule for Alaska, Hawaii, and possessions) is amended by inserting before the period the following: ", or passengers transported on United States flag vessels operating solely within the State waters of Alaska or Hawaii and adjacent international waters".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 1402(a) of the Harbor Maintenance Revenue Act of 1986. 26 USC 4462 note.

(j) AMENDMENTS RELATED TO REVENUE PROVISIONS OF ENERGY POLICY ACT OF 1992.—

(1) Effective with respect to taxable years beginning after December 31, 1990, subclause (II) of section 53(d)(1)(B)(iv) is amended to read as follows:

"(II) the adjusted net minimum tax for any taxable year is the amount of the net minimum tax for such year increased in the manner provided in clause (iii).".

(2) Subsection (g) of section 179A is redesignated as subsection (f).

(3) Subparagraph (E) of section 6724(d)(3) is amended by striking "section 6109(f)" and inserting "section 6109(h)".

(4)(A) Subsection (d) of section 30 is amended—

(i) by inserting "(determined without regard to subsection (b)(3))" before the period at the end of paragraph (1) thereof, and

(ii) by adding at the end thereof the following new paragraph:

"(4) ELECTION TO NOT TAKE CREDIT.—No credit shall be allowed under subsection (a) for any vehicle if the taxpayer elects to not have this section apply to such vehicle.".

(B) Subsection (m) of section 6501 (as redesignated by section 1602) is amended by striking "section 40(f)" and inserting "sections 30(d)(4), 40(f)".

(5) Subclause (III) of section 501(c)(21)(D)(ii) is amended by striking "section 101(6)" and inserting "section 101(7)" and by striking "1752(6)" and inserting "1752(7)".

26 USC 468A. (6) Paragraph (1) of section 1917(b) of the Energy Policy Act of 1992 shall be applied as if "at a rate" appeared instead of "at the rate" in the material proposed to be stricken.

26 USC 142. (7) Paragraph (2) of section 1921(b) of the Energy Policy Act of 1992 shall be applied as if a comma appeared after "(2)" in the material proposed to be stricken.

26 USC 737. (8) Subsection (a) of section 1937 of the Energy Policy Act of 1992 shall be applied as if "Subpart B" appeared instead of "Subpart C".

26 USC 401 note. (k) TREATMENT OF QUALIFIED FOOTBALL COACHES PLAN.—

(1) IN GENERAL.—For purposes of the Internal Revenue Code of 1986, a qualified football coaches plan—

(A) shall be treated as a multiemployer collectively bargained plan, and

(B) notwithstanding section 401(k)(4)(B) of such Code, may include a qualified cash and deferred arrangement under section 401(k) of such Code.

(2) QUALIFIED FOOTBALL COACHES PLAN.—For purposes of this subsection, the term "qualified football coaches plan" means any defined contribution plan which is established and maintained by an organization—

(A) which is described in section 501(c) of such Code,

(B) the membership of which consists entirely of individuals who primarily coach football as full-time employees of 4-year colleges or universities described in section 170(b)(1)(A)(ii) of such Code, and

(C) which was in existence on September 18, 1986.

(3) EFFECTIVE DATE.—This subsection shall apply to years beginning after December 22, 1987.

(l) DETERMINATION OF UNRECOVERED INVESTMENT IN ANNUITY CONTRACT.—

(1) IN GENERAL.—Subparagraph (A) of section 72(b)(4) is amended by inserting "(determined without regard to subsection (c)(2))" after "contract".

26 USC 72 note. (2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 1122(c) of the Tax Reform Act of 1986.

(m) MODIFICATIONS TO ELECTION TO INCLUDE CHILD'S INCOME ON PARENT'S RETURN.—

(1) ELIGIBILITY FOR ELECTION.—Clause (ii) of section 1(g)(7)(A) (relating to election to include certain unearned income of child on parent's return) is amended to read as follows:

"(ii) such gross income is more than the amount described in paragraph (4)(A)(ii)(I) and less than 10 times the amount so described,".

(2) COMPUTATION OF TAX.—Subparagraph (B) of section 1(g)(7) (relating to income included on parent's return) is amended—

(A) by striking "$1,000" in clause (i) and inserting "twice the amount described in paragraph (4)(A)(ii)(I)", and

(B) by amending subclause (II) of clause (ii) to read as follows:

"(II) for each such child, 15 percent of the lesser of the amount described in paragraph (4)(A)(ii)(I) or the excess of the gross income of such child over the amount so described, and".

(3) MINIMUM TAX.—Subparagraph (B) of section 59(j)(1) is amended by striking "$1,000" and inserting "twice the amount in effect for the taxable year under section 63(c)(5)(A)".

(4) EFFECTIVE DATE.—The amendments made by this subsection shall apply to taxable years beginning after December 31, 1995. 26 USC 1 note.

(n) TREATMENT OF CERTAIN VETERANS' REEMPLOYMENT RIGHTS.—

(1) IN GENERAL.—Section 414 is amended by adding at the end the following new subsection:

"(u) SPECIAL RULES RELATING TO VETERANS' REEMPLOYMENT RIGHTS UNDER USERRA.—

"(1) TREATMENT OF CERTAIN CONTRIBUTIONS MADE PURSUANT TO VETERANS' REEMPLOYMENT RIGHTS.—If any contribution is made by an employer or an employee under an individual account plan with respect to an employee, or by an employee to a defined benefit plan that provides for employee contributions, and such contribution is required by reason of such employee's rights under chapter 43 of title 38, United States Code, resulting from qualified military service, then—

"(A) such contribution shall not be subject to any otherwise applicable limitation contained in section 402(g), 402(h), 403(b), 404(a), 404(h), 408, 415, or 457, and shall not be taken into account in applying such limitations to other contributions or benefits under such plan or any other plan, with respect to the year in which the contribution is made,

"(B) such contribution shall be subject to the limitations referred to in subparagraph (A) with respect to the year to which the contribution relates (in accordance with rules prescribed by the Secretary), and

"(C) such plan shall not be treated as failing to meet the requirements of section 401(a)(4), 401(a)(26), 401(k)(3), 401(k)(11), 401(k)(12), 401(m), 403(b)(12), 408(k)(3), 408(k)(6), 408(p), 410(b), or 416 by reason of the making of (or the right to make) such contribution.

For purposes of the preceding sentence, any elective deferral or employee contribution made under paragraph (2) shall be treated as required by reason of the employee's rights under such chapter 43.

"(2) REEMPLOYMENT RIGHTS UNDER USERRA WITH RESPECT TO ELECTIVE DEFERRALS.—

"(A) IN GENERAL.—For purposes of this subchapter and section 457, if an employee is entitled to the benefits of chapter 43 of title 38, United States Code, with respect to any plan which provides for elective deferrals, the employer sponsoring the plan shall be treated as meeting the requirements of such chapter 43 with respect to such elective deferrals only if such employer—

"(i) permits such employee to make additional elective deferrals under such plan (in the amount determined under subparagraph (B) or such lesser amount as is elected by the employee) during the period which begins on the date of the reemployment of such employee with such employer and has the same length as the lesser of—

"(I) the product of 3 and the period of qualified military service which resulted in such rights, and

"(II) 5 years, and

"(ii) makes a matching contribution with respect to any additional elective deferral made pursuant to clause (i) which would have been required had such deferral actually been made during the period of such qualified military service.

"(B) AMOUNT OF MAKEUP REQUIRED.—The amount determined under this subparagraph with respect to any plan is the maximum amount of the elective deferrals that the individual would have been permitted to make under the plan in accordance with the limitations referred to in paragraph (1)(A) during the period of qualified military service if the individual had continued to be employed by the employer during such period and received compensation as determined under paragraph (7). Proper adjustment shall be made to the amount determined under the preceding sentence for any elective deferrals actually made during the period of such qualified military service.

"(C) ELECTIVE DEFERRAL.—For purposes of this paragraph, the term 'elective deferral' has the meaning given such term by section 402(g)(3); except that such term shall include any deferral of compensation under an eligible deferred compensation plan (as defined in section 457(b)).

"(D) AFTER-TAX EMPLOYEE CONTRIBUTIONS.—References in subparagraphs (A) and (B) to elective deferrals shall be treated as including references to employee contributions.

"(3) CERTAIN RETROACTIVE ADJUSTMENTS NOT REQUIRED.—For purposes of this subchapter and subchapter E, no provision of chapter 43 of title 38, United States Code, shall be construed as requiring—

"(A) any crediting of earnings to an employee with respect to any contribution before such contribution is actually made, or

"(B) any allocation of any forfeiture with respect to the period of qualified military service.

"(4) LOAN REPAYMENT SUSPENSIONS PERMITTED.—If any plan suspends the obligation to repay any loan made to an employee from such plan for any part of any period during which such employee is performing service in the uniformed services (as defined in chapter 43 of title 38, United States

Code), whether or not qualified military service, such suspension shall not be taken into account for purposes of section 72(p), 401(a), or 4975(d)(1).

"(5) QUALIFIED MILITARY SERVICE.—For purposes of this subsection, the term 'qualified military service' means any service in the uniformed services (as defined in chapter 43 of title 38, United States Code) by any individual if such individual is entitled to reemployment rights under such chapter with respect to such service.

"(6) INDIVIDUAL ACCOUNT PLAN.—For purposes of this subsection, the term 'individual account plan' means any defined contribution plan (including any tax-sheltered annuity plan under section 403(b), any simplified employee pension under section 408(k), any qualified salary reduction arrangement under section 408(p), and any eligible deferred compensation plan (as defined in section 457(b)).

"(7) COMPENSATION.—For purposes of sections 403(b)(3), 415(c)(3), and 457(e)(5), an employee who is in qualified military service shall be treated as receiving compensation from the employer during such period of qualified military service equal to—

"(A) the compensation the employee would have received during such period if the employee were not in qualified military service, determined based on the rate of pay the employee would have received from the employer but for absence during the period of qualified military service, or

"(B) if the compensation the employee would have received during such period was not reasonably certain, the employee's average compensation from the employer during the 12-month period immediately preceding the qualified military service (or, if shorter, the period of employment immediately preceding the qualified military service).

"(8) USERRA REQUIREMENTS FOR QUALIFIED RETIREMENT PLANS.—For purposes of this subchapter and section 457, an employer sponsoring a retirement plan shall be treated as meeting the requirements of chapter 43 of title 38, United States Code, only if each of the following requirements is met:

"(A) An individual reemployed under such chapter is treated with respect to such plan as not having incurred a break in service with the employer maintaining the plan by reason of such individual's period of qualified military service.

"(B) Each period of qualified military service served by an individual is, upon reemployment under such chapter, deemed with respect to such plan to constitute service with the employer maintaining the plan for the purpose of determining the nonforfeitability of the individual's accrued benefits under such plan and for the purpose of determining the accrual of benefits under such plan.

"(C) An individual reemployed under such chapter is entitled to accrued benefits that are contingent on the making of, or derived from, employee contributions or elective deferrals only to the extent the individual makes payment to the plan with respect to such contributions or deferrals. No such payment may exceed the amount the

individual would have been permitted or required to contribute had the individual remained continuously employed by the employer throughout the period of qualified military service. Any payment to such plan shall be made during the period beginning with the date of reemployment and whose duration is 3 times the period of the qualified military service (but not greater than 5 years).

"(9) PLANS NOT SUBJECT TO TITLE 38.—This subsection shall not apply to any retirement plan to which chapter 43 of title 38, United States Code, does not apply.

"(10) REFERENCES.—For purposes of this section, any reference to chapter 43 of title 38, United States Code, shall be treated as a reference to such chapter as in effect on December 12, 1994 (without regard to any subsequent amendment).".

(2) AMENDMENT TO ERISA.—Section 408(b)(1) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1148(b)) is amended by adding at the end the following new sentence: "A loan made by a plan shall not fail to meet the requirements of the preceding sentence by reason of a loan repayment suspension described under section 414(u)(4) of the Internal Revenue Code of 1986.".

29 USC 1108.

(3) EFFECTIVE DATE.—The amendments made by this subsection shall be effective as of December 12, 1994.

26 USC 414 note.

(o) REPORTING OF REAL ESTATE TRANSACTIONS.—

(1) IN GENERAL.—Paragraph (3) of section 6045(e) (relating to prohibition of separate charge for filing return) is amended by adding at the end the following new sentence: "Nothing in this paragraph shall be construed to prohibit the real estate reporting person from taking into account its cost of complying with such requirement in establishing its charge (other than a separate charge for complying with such requirement) to any customer for performing services in the case of a real estate transaction.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in section 1015(e)(2)(A) of the Technical and Miscellaneous Revenue Act of 1988.

26 USC 6045 note.

(p) CLARIFICATION OF DENIAL OF DEDUCTION FOR STOCK REDEMPTION EXPENSES.

(1) IN GENERAL.—Paragraph (1) of section 162(k) is amended by striking "the redemption of its stock" and inserting "the reacquisition of its stock or of the stock of any related person (as defined in section 465(b)(3)(C))".

(2) CERTAIN DEDUCTIONS PERMITTED.—Subparagraph (A) of section 162(k)(2) is amended by striking "or" at the end of clause (i), by redesignating clause (ii) as clause (iii), and by inserting after clause (i) the following new clause:

"(ii) deduction for amounts which are properly allocable to indebtedness and amortized over the term of such indebtedness, or".

(3) CLERICAL AMENDMENT.—The subsection heading for subsection (k) of section 162 is amended by striking "REDEMPTION" and inserting "REACQUISITION".

26 USC 162 note.

(4) EFFECTIVE DATE.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by this subsection shall apply

to amounts paid or incurred after September 13, 1995, in taxable years ending after such date.

(B) PARAGRAPH (2).—The amendment made by paragraph (2) shall take effect as if included in the amendment made by section 613 of the Tax Reform Act of 1986.

(q) CLERICAL AMENDMENT TO SECTION 404.—

(1) IN GENERAL.—Paragraph (1) of section 404(j) is amended by striking "(10)" and inserting "(9)".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 713(d)(4)(A) of the Deficit Reduction Act of 1984. 26 USC 404 note.

(r) PASSIVE INCOME NOT TO INCLUDE FSC INCOME, ETC.—

(1) IN GENERAL.—Paragraph (2) of section 1296(b) is amended by striking "or" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", or", and by inserting after subparagraph (C) the following new subparagraph:

"(D) which is foreign trade income of an FSC or export trade income of an export trade corporation (as defined in section 971).".

(2) EFFECTIVE DATE.—The amendments made by paragraph (1) shall take effect as if included in the amendments made by section 1235 of the Tax Reform Act of 1986. 26 USC 1296 note.

(s) TECHNICAL CORRECTION OF INTERMEDIATE SANCTIONS PROVISIONS.—

(1) Subparagraph (C) of section 6652(c)(1) is amended by striking "$10" and inserting "$20", and by striking "$5,000" and inserting "$10,000".

(2) Subparagraph (D) of section 6652(c)(1) is amended by striking "$10" and inserting "$20".

(t) MISCELLANEOUS CLERICAL AMENDMENTS.—

(1) Subclause (II) of section 56(g)(4)(C)(ii) is amended by striking "of the subclause" and inserting "of subclause".

(2) Paragraph (2) of section 72(m) is amended by inserting "and" at the end of subparagraph (A), by striking subparagraph (B), and by redesignating subparagraph (C) as subparagraph (B).

(3) Paragraph (2) of section 86(b) is amended by striking "adusted" and inserting "adjusted".

(4)(A) The heading for section 112 is amended by striking "**COMBAT PAY**" and inserting "**COMBAT ZONE COMPENSATION**".

(B) The item relating to section 112 in the table of sections for part III of subchapter B of chapter 1 is amended by striking "combat pay" and inserting "combat zone compensation".

(C) Paragraph (1) of section 3401(a) is amended by striking "combat pay" and inserting "combat zone compensation".

(5) Clause (i) of section 172(h)(3)(B) is amended by striking the comma at the end thereof and inserting a period.

(6) Clause (ii) of section 543(a)(2)(B) is amended by striking "section 563(c)" and inserting "section 563(d)".

(7) Paragraph (1) of section 958(a) is amended by striking "sections 955(b)(1) (A) and (B), 955(c)(2)(A)(ii), and 960(a)(1)" and inserting "section 960(a)(1)".

(8) Subsection (g) of section 642 is amended by striking "under 2621(a)(2)" and inserting "under section 2621(a)(2)".

(9) Section 1463 is amended by striking "this subsection" and inserting "this section".

(10) Subsection (k) of section 3306 is amended by inserting a period at the end thereof.

(11) The item relating to section 4472 in the table of sections for subchapter B of chapter 36 is amended by striking "and special rules".

(12) Paragraph (3) of section 5134(c) is amended by striking "section 6662(a)" and inserting "section 6665(a)".

(13) Paragraph (2) of section 5206(f) is amended by striking "section 5(e)" and inserting "section 105(e)".

(14) Paragraph (1) of section 6050B(c) is amended by striking "section 85(c)" and inserting "section 85(b)".

(15) Subsection (k) of section 6166 is amended by striking paragraph (6).

(16) Subsection (e) of section 6214 is amended to read as follows:

"(e) CROSS REFERENCE.—

"For provision giving Tax Court jurisdiction to order a refund of an overpayment and to award sanctions, see section 6512(b)(2).".

(17) The section heading for section 6043 is amended by striking the semicolon and inserting a comma.

(18) The item relating to section 6043 in the table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking the semicolon and inserting a comma.

(19) The table of sections for part I of subchapter A of chapter 68 is amended by striking the item relating to section 6662.

(20)(A) Section 7232 is amended—

(i) by striking "**LUBRICATING OIL,**" in the heading, and

(ii) by striking "lubricating oil," in the text.

(B) The table of sections for part II of subchapter A of chapter 75 is amended by striking "lubricating oil," in the item relating to section 7232.

(21) Paragraph (1) of section 6701(a) of the Omnibus Budget Reconciliation Act of 1989 is amended by striking "subclause (IV)" and inserting "subclause (V)". 26 USC 4980B.

(22) Clause (ii) of section 7304(a)(2)(D) of such Act is amended by striking "subsection (c)(2)" and inserting "subsection (c)". 26 USC 4979A.

(23) Paragraph (1) of section 7646(b) of such Act is amended by striking "section 6050H(b)(1)" and inserting "section 6050H(b)(2)". 26 USC 6050H.

(24) Paragraph (10) of section 7721(c) of such Act is amended by striking "section 6662(b)(2)(C)(ii)" and inserting "section 6661(b)(2)(C)(ii)". 26 USC 461.

(25) Subparagraph (A) of section 7811(i)(3) of such Act is amended by inserting "the first place it appears" before "in clause (i)". 26 USC 954.

(26) Paragraph (10) of section 7841(d) of such Act is amended by striking "section 381(a)" and inserting "section 381(c)". 26 USC 381.

(27) Paragraph (2) of section 7861(c) of such Act is amended by inserting "the second place it appears" before "and inserting". 26 USC 401 note.

(28) Paragraph (1) of section 460(b) is amended by striking "the look-back method of paragraph (3)" and inserting "the look-back method of paragraph (2)".

(29) Subparagraph (C) of section 50(a)(2) is amended by striking "subsection (c)(4)" and inserting "subsection (d)(5)".

(30) Subparagraph (B) of section 172(h)(4) is amended by striking the material following the heading and preceding clause (i) and inserting "For purposes of subsection (b)(2)—".

(31) Subparagraph (A) of section 355(d)(7) is amended by inserting "section" before "267(b)".

(32) Subparagraph (C) of section 420(e)(1) is amended by striking "mean" and inserting "means".

(33) Paragraph (4) of section 537(b) is amended by striking "section 172(i)" and inserting "section 172(f)".

(34) Subparagraph (B) of section 613(e)(1) is amended by striking the comma at the end thereof and inserting a period.

(35) Paragraph (4) of section 856(a) is amended by striking "section 582(c)(5)" and inserting "section 582(c)(2)".

(36) Sections 904(f)(2)(B)(i) and 907(c)(4)(B)(iii) are each amended by inserting "(as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)" after "section 172(h)".

(37) Subsection (b) of section 936 is amended by striking "subparagraphs (D)(ii)(I)" and inserting "subparagraphs (D)(ii)".

(38) Subsection (c) of section 2104 is amended by striking "subparagraph (A), (C), or (D) of section 861(a)(1)" and inserting "section 861(a)(1)(A)".

(39) Subparagraph (A) of section 280A(c)(1) is amended to read as follows:

"(A) as the principal place of business for any trade or business of the taxpayer,".

(40) Section 6038 is amended by redesignating the subsection relating to cross references as subsection (f).

(41) Clause (iv) of section 6103(e)(1)(A) is amended by striking all that follows "provisions of" and inserting "section 1(g) or 59(j);".

(42) The subsection (f) of section 6109 of the Internal Revenue Code of 1986 which was added by section 2201(d) of Public Law 101–624 is redesignated as subsection (g).

(43) Subsection (b) of section 7454 is amended by striking "section 4955(e)(2)" and inserting "section 4955(f)(2)".

(44) Subsection (d) of section 11231 of the Revenue Reconciliation Act of 1990 shall be applied as if "comma" appeared instead of "period" and as if the paragraph (9) proposed to be added ended with a comma. 26 USC 9507 note.

(45) Paragraph (1) of section 11303(b) of the Revenue Reconciliation Act of 1990 shall be applied as if "paragraph" appeared instead of "subparagraph" in the material proposed to be stricken. 26 USC 832.

(46) Subsection (f) of section 11701 of the Revenue Reconciliation Act of 1990 is amended by inserting "(relating to definitions)" after "section 6038(e)". 26 USC 6038.

(47) Subsection (i) of section 11701 of the Revenue Reconciliation Act of 1990 shall be applied as if "subsection" appeared instead of "section" in the material proposed to be stricken. 26 USC 1253.

(48) Subparagraph (B) of section 11801(c)(2) of the Revenue Reconciliation Act of 1990 shall be applied as if "section 56(g)" appeared instead of "section 59(g)". 26 USC 56.

26 USC 247. (49) Subparagraph (C) of section 11801(c)(8) of the Revenue Reconciliation Act of 1990 shall be applied as if "reorganizations" appeared instead of "reorganization" in the material proposed to be stricken.

26 USC 1042. (50) Subparagraph (H) of section 11801(c)(9) of the Revenue Reconciliation Act of 1990 shall be applied as if "section 1042(c)(1)(B)" appeared instead of "section 1042(c)(2)(B)".

26 USC 593. (51) Subparagraph (F) of section 11801(c)(12) of the Revenue Reconciliation Act of 1990 shall be applied as if "and (3)" appeared instead of "and (E)".

26 USC 6302. (52) Subparagraph (A) of section 11801(c)(22) of the Revenue Reconciliation Act of 1990 shall be applied as if "chapters 21" appeared instead of "chapter 21" in the material proposed to be stricken.

26 USC 42. (53) Paragraph (3) of section 11812(b) of the Revenue Reconciliation Act of 1990 shall be applied by not executing the amendment therein to the heading of section 42(d)(5)(B).

26 USC 168. (54) Clause (i) of section 11813(b)(9)(A) of the Revenue Reconciliation Act of 1990 shall be applied as if a comma appeared after "(3)(A)(ix)" in the material proposed to be stricken.

26 USC prec. 261. (55) Subparagraph (F) of section 11813(b)(13) of the Revenue Reconciliation Act of 1990 shall be applied as if "tax" appeared after "investment" in the material proposed to be stricken.

26 USC 1016. (56) Paragraph (19) of section 11813(b) of the Revenue Reconciliation Act of 1990 shall be applied as if "Paragraph (20) of section 1016(a), as redesignated by section 11801," appeared instead of "Paragraph (21) of section 1016(a)".

26 USC 4481. (57) Paragraph (5) section 8002(a) of the Surface Transportation Revenue Act of 1991 shall be applied as if "4481(e)" appeared instead of "4481(c)".

(58) Section 7872 is amended—

(A) by striking "foregone" each place it appears in subsections (a) and (e)(2) and inserting "forgone", and

(B) by striking "FOREGONE" in the heading for subsection (e) and the heading for paragraph (2) of subsection (e) and inserting "FORGONE".

(59) Paragraph (7) of section 7611(h) is amended by striking "approporiate" and inserting "appropriate".

(60) The heading of paragraph (3) of section 419A(c) is amended by striking "SEVERENCE" and inserting "SEVERANCE".

(61) Clause (ii) of section 807(d)(3)(B) is amended by striking "Commissoners' " and inserting "Commissioners' ".

(62) Subparagraph (B) of section 1274A(c)(1) is amended by striking "instument" and inserting "instrument".

(63) Subparagraph (B) of section 724(d)(3) by striking "Subparagaph" and inserting "Subparagraph".

(64) The last sentence of paragraph (2) of section 42(c) is amended by striking "of 1988".

(65) Paragraph (1) of section 9707(d) is amended by striking "diligence," and inserting "diligence".

(66) Subsection (c) of section 4977 is amended by striking "section 132(i)(2)" and inserting "section 132(h)".

(67) The last sentence of section 401(a)(20) is amended by striking "section 211" and inserting "section 521".

(68) Subparagraph (A) of section 402(g)(3) is amended by striking "subsection (a)(8)" and inserting "subsection (e)(3)".

(69) The last sentence of section 403(b)(10) is amended by striking "an direct" and inserting "a direct".

(70) Subparagraph (A) of section 4973(b)(1) is amended by striking "sections 402(c)" and inserting "section 402(c)".

(71) Paragraph (12) of section 3405(e) is amended by striking "(b)(3)" and inserting "(b)(2)".

(72) Paragraph (41) of section 521(b) of the Unemployment Compensation Amendments of 1992 shall be applied as if "section" appeared instead of "sections" in the material proposed to be stricken. 26 USC 4973.

(73) Paragraph (27) of section 521(b) of the Unemployment Compensation Amendments of 1992 shall be applied as if "Section 691(c)(5)" appeared instead of "Section 691(c)". 26 USC 691.

(74) Paragraph (5) of section 860F(a) is amended by striking "paragraph (1)" and inserting "paragraph (2)".

(75) Paragraph (1) of section 415(k) is amended by adding "or" at the end of subparagraph (C), by striking subparagraphs (D) and (E), and by redesignating subparagraph (F) as subparagraph (D).

(76) Paragraph (2) of section 404(a) is amended by striking "(18),".

(77) Clause (ii) of section 72(p)(4)(A) is amended to read as follows:

> "(ii) SPECIAL RULE.—The term 'qualified employer plan' shall include any plan which was (or was determined to be) a qualified employer plan or a government plan.".

(78) Sections 461(i)(3)(C) and 1274(b)(3)(B)(i) are each amended by striking "section 6662(d)(2)(C)(ii)" and inserting "section 6662(d)(2)(C)(iii)".

(79) Subsection (a) of section 164 is amended by striking the paragraphs relating to the generation-skipping tax and the environmental tax imposed by section 59A and by inserting after paragraph (3) the following new paragraphs:

"(4) The GST tax imposed on income distributions.

"(5) The environmental tax imposed by section 59A.".

(80) Subclause (I) of section 936(a)(4)(A)(ii) is amended by striking "deprecation" and inserting "depreciation".

Subtitle H—Other Provisions

SEC. 1801. EXEMPTION FROM DIESEL FUEL DYEING REQUIREMENTS WITH RESPECT TO CERTAIN STATES.

(a) IN GENERAL.—Section 4082 (relating to exemptions for diesel fuel) is amended by redesignating subsections (c) and (d) as subsections (d) and (e), respectively, and by inserting after subsection (b) the following new subsection:

"(c) EXCEPTION TO DYEING REQUIREMENTS.—Paragraph (2) of subsection (a) shall not apply with respect to any diesel fuel—

> "(1) removed, entered, or sold in a State for ultimate sale or use in an area of such State during the period such area is exempted from the fuel dyeing requirements under subsection (i) of section 211 of the Clean Air Act (as in effect on the date of the enactment of this subsection) by the Administrator

of the Environmental Protection Agency under paragraph (4) of such subsection (i) (as so in effect), and

"(2) the use of which is certified pursuant to regulations issued by the Secretary.".

26 USC 4082 note.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to fuel removed, entered, or sold on or after the first day of the first calendar quarter beginning after the date of the enactment of this Act.

26 USC 3121 note.

SEC. 1802. TREATMENT OF CERTAIN UNIVERSITY ACCOUNTS.

(a) IN GENERAL.—For purposes of subsection (s) of section 3121 of the Internal Revenue Code of 1986 (relating to concurrent employment by 2 or more employers)—

(1) the following entities shall be deemed to be related corporations that concurrently employ the same individual:

(A) a State university which employs health professionals as faculty members at a medical school, and

(B) an agency account of a State university which is described in subparagraph (A) and from which there is distributed to such faculty members payments forming a part of the compensation that the State, or such State university, as the case may be, agrees to pay to such faculty members, but only if—

(i) such agency account is authorized by State law and receives the funds for such payments from a faculty practice plan described in section 501(c)(3) of such Code and exempt from tax under section 501(a) of such Code,

(ii) such payments are distributed by such agency account to such faculty members who render patient care at such medical school, and

(iii) such faculty members comprise at least 30 percent of the membership of such faculty practice plan, and

(2) remuneration which is disbursed by such agency account to any such faculty member of the medical school described in paragraph (1)(A) shall be deemed to have been actually disbursed by the State, or such State university, as the case may be, as a common paymaster and not to have been actually disbursed by such agency account.

(b) EFFECTIVE DATE.—The provisions of subsection (a) shall apply to remuneration paid after December 31, 1996.

SEC. 1803. MODIFICATIONS TO EXCISE TAX ON OZONE-DEPLETING CHEMICALS.

(a) RECYCLED HALON.—

(1) IN GENERAL.—Section 4682(d)(1) (relating to recycling) is amended by inserting ", or on any recycled halon imported from any country which is a signatory to the Montreal Protocol on Substances that Deplete the Ozone Layer" before the period at the end.

26 USC 4682 note.

(2) CERTIFICATION SYSTEM.—The Secretary of the Treasury, after consultation with the Administrator of the Environmental Protection Agency, shall develop a certification system to ensure compliance with the recycling requirement for imported halon under section 4682(d)(1) of the Internal Revenue Code of 1986, as amended by paragraph (1).

(b) CHEMICALS USED AS PROPELLANTS IN METERED-DOSE INHALERS TAX-EXEMPT.—Paragraph (4) of section 4682(g) (relating to phase-in of tax on certain substances) is amended to read as follows:

"(4) CHEMICALS USED AS PROPELLANTS IN METERED-DOSE INHALERS.—

"(A) TAX-EXEMPT.—

"(i) IN GENERAL.—No tax shall be imposed by section 4681 on—

"(I) any use of any substance as a propellant in metered-dose inhalers, or

"(II) any qualified sale by the manufacturer, producer, or importer of any substance.

"(ii) QUALIFIED SALE.—For purposes of clause (i), the term 'qualified sale' means any sale by the manufacturer, producer, or importer of any substance—

"(I) for use by the purchaser as a propellant in metered-dose inhalers, or

"(II) for resale by the purchaser to a 2d purchaser for such use by the 2d purchaser.

The preceding sentence shall apply only if the manufacturer, producer, and importer, and the 1st and 2d purchasers (if any) meet such registration requirements as may be prescribed by the Secretary.

"(B) OVERPAYMENTS.—If any substance on which tax was paid under this subchapter is used by any person as a propellant in metered-dose inhalers, credit or refund without interest shall be allowed to such person in an amount equal to the tax so paid. Amounts payable under the preceding sentence with respect to uses during the taxable year shall be treated as described in section 34(a) for such year unless claim thereof has been timely filed under this subparagraph.".

(c) EFFECTIVE DATES.— 26 USC 4682 note.

(1) RECYCLED HALON.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the amendment made by subsection (a)(1) shall take effect on January 1, 1997.

(B) HALON-1211.—In the case of Halon-1211, the amendment made by subsection (a)(1) shall take effect on January 1, 1998.

(2) METERED-DOSE INHALERS.—The amendment made by subsection (b) shall take effect on the 7th day after the date of the enactment of this Act.

SEC. 1804. TAX-EXEMPT BONDS FOR SALE OF ALASKA POWER ADMINISTRATION FACILITY. 26 USC 142 note.

Sections 142(f)(3) (as added by section 1608) and 147(d) of the Internal Revenue Code of 1986 shall not apply in determining whether any private activity bond issued after the date of the enactment of this Act and used to finance the acquisition of the Snettisham hydroelectric project from the Alaska Power Administration is a qualified bond for purposes of such Code.

SEC. 1805. NONRECOGNITION TREATMENT FOR CERTAIN TRANSFERS BY COMMON TRUST FUNDS TO REGULATED INVESTMENT COMPANIES.

(a) GENERAL RULE.—Section 584 (relating to common trust funds) is amended by redesignating subsection (h) as subsection (i) and by inserting after subsection (g) the following new subsection:

"(h) NONRECOGNITION TREATMENT FOR CERTAIN TRANSFERS TO REGULATED INVESTMENT COMPANIES.—

"(1) IN GENERAL.—If—

"(A) a common trust fund transfers substantially all of its assets to one or more regulated investment companies in exchange solely for stock in the company or companies to which such assets are so transferred, and

"(B) such stock is distributed by such common trust fund to participants in such common trust fund in exchange solely for their interests in such common trust fund,

no gain or loss shall be recognized by such common trust fund by reason of such transfer or distribution, and no gain or loss shall be recognized by any participant in such common trust fund by reason of such exchange.

"(2) BASIS RULES.—

"(A) REGULATED INVESTMENT COMPANY.—The basis of any asset received by a regulated investment company in a transfer referred to in paragraph (1)(A) shall be the same as it would be in the hands of the common trust fund.

"(B) PARTICIPANTS.—The basis of the stock which is received in an exchange referred to in paragraph (1)(B) shall be the same as that of the property exchanged. If stock in more than one regulated investment company is received in such exchange, the basis determined under the preceding sentence shall be allocated among the stock in each such company on the basis of respective fair market values.

"(3) TREATMENT OF ASSUMPTIONS OF LIABILITY.—

"(A) IN GENERAL.—In determining whether the transfer referred to in paragraph (1)(A) is in exchange solely for stock in one or more regulated investment companies, the assumption by any such company of a liability of the common trust fund, and the fact that any property transferred by the common trust fund is subject to a liability, shall be disregarded.

"(B) SPECIAL RULE WHERE ASSUMED LIABILITIES EXCEED BASIS.—

"(i) IN GENERAL.—If, in any transfer referred to in paragraph (1)(A), the assumed liabilities exceed the aggregate adjusted bases (in the hands of the common trust fund) of the assets transferred to the regulated investment company or companies—

"(I) notwithstanding paragraph (1), gain shall be recognized to the common trust fund on such transfer in an amount equal to such excess,

"(II) the basis of the assets received by the regulated investment company or companies in such transfer shall be increased by the amount so recognized, and

"(III) any adjustment to the basis of a participant's interest in the common trust fund as a result of the gain so recognized shall be treated as occurring immediately before the exchange referred to in paragraph (1)(B).

If the transfer referred to in paragraph (1)(A) is to two or more regulated investment companies, the basis increase under subclause (II) shall be allocated among such companies on the basis of the respective fair market values of the assets received by each of such companies.

"(ii) ASSUMED LIABILITIES.—For purposes of clause (i), the term 'assumed liabilities' means the aggregate of—

"(I) any liability of the common trust fund assumed by any regulated investment company in connection with the transfer referred to in paragraph (1)(A), and

"(II) any liability to which property so transferred is subject.

"(4) COMMON TRUST FUND MUST MEET DIVERSIFICATION RULES.—This subsection shall not apply to any common trust fund which would not meet the requirements of section 368(a)(2)(F)(ii) if it were a corporation. For purposes of the preceding sentence, Government securities shall not be treated as securities of an issuer in applying the 25-percent and 50-percent test and such securities shall not be excluded for purposes of determining total assets under clause (iv) of section 368(a)(2)(F).".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to transfers after December 31, 1995. 26 USC 584 note.

SEC. 1806. QUALIFIED STATE TUITION PROGRAMS.

(a) IN GENERAL.—Subchapter F of chapter 1 (relating to exempt organizations) is amended by adding at the end the following new part:

"PART VIII—QUALIFIED STATE TUITION PROGRAMS

"Sec. 529. Qualified State tuition programs.

"SEC. 529. QUALIFIED STATE TUITION PROGRAMS.

"(a) GENERAL RULE.—A qualified State tuition program shall be exempt from taxation under this subtitle. Notwithstanding the preceding sentence, such program shall be subject to the taxes imposed by section 511 (relating to imposition of tax on unrelated business income of charitable organizations).

"(b) QUALIFIED STATE TUITION PROGRAM.—For purposes of this section—

"(1) IN GENERAL.—The term 'qualified State tuition program' means a program established and maintained by a State or agency or instrumentality thereof—

"(A) under which a person—

"(i) may purchase tuition credits or certificates on behalf of a designated beneficiary which entitle the beneficiary to the waiver or payment of qualified higher education expenses of the beneficiary, or

"(ii) may make contributions to an account which is established for the purpose of meeting the qualified higher education expenses of the designated beneficiary of the account, and

"(B) which meets the other requirements of this subsection.

"(2) CASH CONTRIBUTIONS.—A program shall not be treated as a qualified State tuition program unless it provides that purchases or contributions may only be made in cash.

"(3) REFUNDS.—A program shall not be treated as a qualified State tuition program unless it imposes a more than de minimis penalty on any refund of earnings from the account which are not—

"(A) used for qualified higher education expenses of the designated beneficiary,

"(B) made on account of the death or disability of the designated beneficiary, or

"(C) made on account of a scholarship (or allowance or payment described in section 135(d)(1) (B) or (C)) received by the designated beneficiary to the extent the amount of the refund does not exceed the amount of the scholarship, allowance, or payment.

"(4) SEPARATE ACCOUNTING.—A program shall not be treated as a qualified State tuition program unless it provides separate accounting for each designated beneficiary.

"(5) NO INVESTMENT DIRECTION.—A program shall not be treated as a qualified State tuition program unless it provides that any contributor to, or designated beneficiary under, such program may not direct the investment of any contributions to the program (or any earnings thereon).

"(6) NO PLEDGING OF INTEREST AS SECURITY.—A program shall not be treated as a qualified State tuition program if it allows any interest in the program or any portion thereof to be used as security for a loan.

"(7) PROHIBITION ON EXCESS CONTRIBUTIONS.—A program shall not be treated as a qualified State tuition program unless it provides adequate safeguards to prevent contributions on behalf of a designated beneficiary in excess of those necessary to provide for the qualified higher education expenses of the beneficiary.

"(c) TAX TREATMENT OF DESIGNATED BENEFICIARIES AND CONTRIBUTORS.—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, no amount shall be includible in gross income of—

"(A) a designated beneficiary under a qualified State tuition program, or

"(B) a contributor to such program on behalf of a designated beneficiary,

with respect to any distribution or earnings under such program.

"(2) CONTRIBUTIONS.—In no event shall a contribution to a qualified State tuition program on behalf of a designated beneficiary be treated as a taxable gift for purposes of chapter 12.

"(3) DISTRIBUTIONS.—

"(A) IN GENERAL.—Any distribution under a qualified State tuition program shall be includible in the gross

income of the distributee in the manner as provided under section 72 to the extent not excluded from gross income under any other provision of this chapter.

"(B) IN-KIND DISTRIBUTIONS.—Any benefit furnished to a designated beneficiary under a qualified State tuition program shall be treated as a distribution to the beneficiary.

"(C) CHANGE IN BENEFICIARIES.—

"(i) ROLLOVERS.—Subparagraph (A) shall not apply to that portion of any distribution which, within 60 days of such distribution, is transferred to the credit of another designated beneficiary under a qualified State tuition program who is a member of the family of the designated beneficiary with respect to which the distribution was made.

"(ii) CHANGE IN DESIGNATED BENEFICIARIES.—Any change in the designated beneficiary of an interest in a qualified State tuition program shall not be treated as a distribution for purposes of subparagraph (A) if the new beneficiary is a member of the family of the old beneficiary.

"(D) OPERATING RULES.—For purposes of applying section 72—

"(i) to the extent provided by the Secretary, all qualified State tuition programs of which an individual is a designated beneficiary shall be treated as one program,

"(ii) all distributions during a taxable year shall be treated as one distribution, and

"(iii) the value of the contract, income on the contract, and investment in the contract shall be computed as of the close of the calendar year in which the taxable year begins.

"(4) ESTATE TAX INCLUSION.—The value of any interest in any qualified State tuition program which is attributable to contributions made by an individual to such program on behalf of any designated beneficiary shall be includible in the gross estate of the contributor for purposes of chapter 11.

"(5) SPECIAL RULE FOR APPLYING SECTION 2503(e).—For purposes of section 2503(e), the waiver (or payment to an educational institution) of qualified higher education expenses of a designated beneficiary under a qualified State tuition program shall be treated as a qualified transfer.

"(d) REPORTING REQUIREMENTS.—

"(1) IN GENERAL.—If there is a distribution to any individual with respect to an interest in a qualified State tuition program during any calendar year, each officer or employee having control of the qualified State tuition program or their designee shall make such reports as the Secretary may require regarding such distribution to the Secretary and to the designated beneficiary or the individual to whom the distribution was made. Any such report shall include such information as the Secretary may prescribe.

"(2) TIMING OF REPORTS.—Any report required by this subsection—

"(A) shall be filed at such time and in such matter as the Secretary prescribes, and

"(B) shall be furnished to individuals not later than January 31 of the calendar year following the calendar year to which such report relates.

"(e) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) DESIGNATED BENEFICIARY.—The term 'designated beneficiary' means—

"(A) the individual designated at the commencement of participation in the qualified State tuition program as the beneficiary of amounts paid (or to be paid) to the program,

"(B) in the case of a change in beneficiaries described in subsection (c)(2)(C), the individual who is the new beneficiary, and

"(C) in the case of an interest in a qualified State tuition program purchased by a State or local government or an organization described in section 501(c)(3) and exempt from taxation under section 501(a) as part of a scholarship program operated by such government or organization, the individual receiving such interest as a scholarship.

"(2) MEMBER OF FAMILY.—The term 'member of the family' has the same meaning given such term as section 2032A(e)(2).

"(3) QUALIFIED HIGHER EDUCATION EXPENSES.—The term 'qualified higher education expenses' means tuition, fees, books, supplies, and equipment required for the enrollment or attendance of a designated beneficiary at an eligible educational institution (as defined in section 135(c)(3)).

"(4) APPLICATION OF SECTION 514.—An interest in a qualified State tuition program shall not be treated as debt for purposes of section 514.".

(b) CONFORMING AMENDMENTS.—

(1) Section 135(d)(1) is amended by striking "or" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", or", and by adding at the end the following new subparagraph:

"(D) a payment, waiver, or reimbursement of qualified higher education expenses under a qualified State tuition program (within the meaning of section 529(b)).".

(2) The table of parts for subchapter F of chapter 1 is amended by adding at the end the following new item:

"Part VIII. Qualified State tuition programs.".

26 USC 529 note.

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years ending after the date of the enactment of this Act.

(2) TRANSITION RULE.—If—

(A) a State or agency or instrumentality thereof maintains, on the date of the enactment of this Act, a program under which persons may purchase tuition credits or certificates on behalf of, or make contributions for education expenses of, a designated beneficiary, and

(B) such program meets the requirements of a qualified State tuition program before the later of—

(i) the date which is 1 year after such date of enactment, or

(ii) the first day of the first calendar quarter after the close of the first regular session of the State legislature that begins after such date of enactment,

the amendments made by this section shall apply to contributions (and earnings allocable thereto) made before the date such program meets the requirements of such amendments without regard to whether any requirements of such amendments are met with respect to such contributions and earnings.

For purposes of subparagraph (B)(ii), if a State has a 2-year legislative session, each year of such session shall be deemed to be a separate regular session of the State legislature.

SEC. 1807. ADOPTION ASSISTANCE.

(a) IN GENERAL.—Subpart A of part IV of subchapter A of chapter 1 (relating to nonrefundable personal credits) is amended by inserting after section 22 the following new section:

"SEC. 23. ADOPTION EXPENSES.

"(a) ALLOWANCE OF CREDIT.—

"(1) IN GENERAL.—In the case of an individual, there shall be allowed as a credit against the tax imposed by this chapter the amount of the qualified adoption expenses paid or incurred by the taxpayer.

"(2) YEAR CREDIT ALLOWED.—The credit under paragraph (1) with respect to any expense shall be allowed—

"(A) for the taxable year following the taxable year during which such expense is paid or incurred, or

"(B) in the case of an expense which is paid or incurred during the taxable year in which the adoption becomes final, for such taxable year.

"(b) LIMITATIONS.—

"(1) DOLLAR LIMITATION.—The aggregate amount of qualified adoption expenses which may be taken into account under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed $5,000 ($6,000, in the case of a child with special needs).

"(2) INCOME LIMITATION.—

"(A) IN GENERAL.—The amount allowable as a credit under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so allowable (determined without regard to this paragraph but with regard to paragraph (1)) as—

"(i) the amount (if any) by which the taxpayer's adjusted gross income exceeds $75,000, bears to

"(ii) $40,000.

"(B) DETERMINATION OF ADJUSTED GROSS INCOME.—For purposes of subparagraph (A), adjusted gross income shall be determined—

"(i) without regard to sections 911, 931, and 933, and

"(ii) after the application of sections 86, 135, 137, 219, and 469.

"(3) DENIAL OF DOUBLE BENEFIT.—

"(A) IN GENERAL.—No credit shall be allowed under subsection (a) for any expense for which a deduction or credit is allowed under any other provision of this chapter.

"(B) GRANTS.—No credit shall be allowed under subsection (a) for any expense to the extent that funds for such expense are received under any Federal, State, or local program.

"(c) CARRYFORWARDS OF UNUSED CREDIT.—If the credit allowable under subsection (a) for any taxable year exceeds the limitation imposed by section 26(a) for such taxable year reduced by the sum of the credits allowable under this subpart (other than this section), such excess shall be carried to the succeeding taxable year and added to the credit allowable under subsection (a) for such taxable year. No credit may be carried forward under this subsection to any taxable year following the fifth taxable year after the taxable year in which the credit arose. For purposes of the preceding sentence, credits shall be treated as used on a first-in first-out basis.

"(d) DEFINITIONS.—For purposes of this section—

"(1) QUALIFIED ADOPTION EXPENSES.—The term 'qualified adoption expenses' means reasonable and necessary adoption fees, court costs, attorney fees, and other expenses—

"(A) which are directly related to, and the principal purpose of which is for, the legal adoption of an eligible child by the taxpayer,

"(B) which are not incurred in violation of State or Federal law or in carrying out any surrogate parenting arrangement,

"(C) which are not expenses in connection with the adoption by an individual of a child who is the child of such individual's spouse, and

"(D) which are not reimbursed under an employer program or otherwise.

"(2) ELIGIBLE CHILD.—The term 'eligible child' means any individual—

"(A) who—

"(i) has not attained age 18, or

"(ii) is physically or mentally incapable of caring for himself, and

"(B) in the case of qualified adoption expenses paid or incurred after December 31, 2001, who is a child with special needs.

"(3) CHILD WITH SPECIAL NEEDS.—The term 'child with special needs' means any child if—

"(A) a State has determined that the child cannot or should not be returned to the home of his parents,

"(B) such State has determined that there exists with respect to the child a specific factor or condition (such as his ethnic background, age, or membership in a minority or sibling group, or the presence of factors such as medical conditions or physical, mental, or emotional handicaps) because of which it is reasonable to conclude that such child cannot be placed with adoptive parents without providing adoption assistance, and

"(C) such child is a citizen or resident of the United States (as defined in section 217(h)(3)).

"(e) SPECIAL RULES FOR FOREIGN ADOPTIONS.—In the case of an adoption of a child who is not a citizen or resident of the United States (as defined in section 217(h)(3))—

"(1) subsection (a) shall not apply to any qualified adoption expense with respect to such adoption unless such adoption becomes final, and

"(2) any such expense which is paid or incurred before the taxable year in which such adoption becomes final shall be taken into account under this section as if such expense were paid or incurred during such year.

"(f) FILING REQUIREMENTS.—

"(1) MARRIED COUPLES MUST FILE JOINT RETURNS.—Rules similar to the rules of paragraphs (2), (3), and (4) of section 21(e) shall apply for purposes of this section.

"(2) TAXPAYER MUST INCLUDE TIN.—

"(A) IN GENERAL.—No credit shall be allowed under this section with respect to any eligible child unless the taxpayer includes (if known) the name, age, and TIN of such child on the return of tax for the taxable year.

"(B) OTHER METHODS.—The Secretary may, in lieu of the information referred to in subparagraph (A), require other information meeting the purposes of subparagraph (A), including identification of an agent assisting with the adoption.

"(g) BASIS ADJUSTMENTS.—For purposes of this subtitle, if a credit is allowed under this section for any expenditure with respect to any property, the increase in the basis of such property which would (but for this subsection) result from such expenditure shall be reduced by the amount of the credit so allowed.

"(h) REGULATIONS.—The Secretary shall prescribe such regulations as may be appropriate to carry out this section and section 137, including regulations which treat unmarried individuals who pay or incur qualified adoption expenses with respect to the same child as 1 taxpayer for purposes of applying the dollar limitation in subsection (b)(1) of this section and in section 137(b)(1).".

(b) EXCLUSION OF AMOUNTS RECEIVED UNDER EMPLOYER'S ADOPTION ASSISTANCE PROGRAMS.—Part III of subchapter B of chapter 1 (relating to items specifically excluded from gross income) is amended by redesignating section 137 as section 138 and by inserting after section 136 the following new section:

"SEC. 137. ADOPTION ASSISTANCE PROGRAMS.

"(a) IN GENERAL.—Gross income of an employee does not include amounts paid or expenses incurred by the employer for qualified adoption expenses in connection with the adoption of a child by an employee if such amounts are furnished pursuant to an adoption assistance program.

"(b) LIMITATIONS.—

"(1) DOLLAR LIMITATION.—The aggregate amount excludable from gross income under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed $5,000 ($6,000, in the case of a child with special needs).

"(2) INCOME LIMITATION.—The amount excludable from gross income under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so excludable (determined without regard to this paragraph but with regard to paragraph (1)) as—

"(A) the amount (if any) by which the taxpayer's adjusted gross income exceeds $75,000, bears to

"(B) $40,000.

"(3) DETERMINATION OF ADJUSTED GROSS INCOME.—For purposes of paragraph (2), adjusted gross income shall be determined—

"(A) without regard to this section and sections 911, 931, and 933, and

"(B) after the application of sections 86, 135, 219, and 469.

"(c) ADOPTION ASSISTANCE PROGRAM.—For purposes of this section, an adoption assistance program is a separate written plan of an employer for the exclusive benefit of such employer's employees—

"(1) under which the employer provides such employees with adoption assistance, and

"(2) which meets requirements similar to the requirements of paragraphs (2), (3), (5), and (6) of section 127(b).

An adoption reimbursement program operated under section 1052 of title 10, United States Code (relating to armed forces) or section 514 of title 14, United States Code (relating to members of the Coast Guard) shall be treated as an adoption assistance program for purposes of this section.

"(d) QUALIFIED ADOPTION EXPENSES.—For purposes of this section, the term 'qualified adoption expenses' has the meaning given such term by section 23(d) (determined without regard to reimbursements under this section).

"(e) CERTAIN RULES TO APPLY.—Rules similar to the rules of subsections (e), (f), and (g) of section 23 shall apply for purposes of this section.

"(f) TERMINATION.—This section shall not apply to amounts paid or expenses incurred after December 31, 2001.".

(c) CONFORMING AMENDMENTS.—

(1) Subparagraph (C) of section 25(e)(1) is amended by inserting "and section 23" after "this section".

(2) Sections 86(b)(2)(A) and 135(c)(4)(A) are each amended by inserting "137," before "911".

(3) Clause (i) of section 219(g)(3)(A) is amended by inserting ", 137," before "and 911".

(4) Clause (ii) of section 469(i)(3)(E) is amended to read as follows:

"(ii) the amounts excludable from gross income under sections 135 and 137,".

(5) Subsection (a) of section 1016 is amended by striking "and" at the end of paragraph (24), by striking the period at the end of paragraph (25) and inserting ", and", and by adding at the end the following new paragraph:

"(26) to the extent provided in sections 23(g) and 137(e).".

(6) The table of sections for subpart A of part IV of subchapter A of chapter 1 is amended by inserting after the item relating to section 22 the following new item:

"Sec. 23. Adoption expenses.".

(7) The table of sections for part III of subchapter B of chapter 1 is amended by striking the item relating to section 137 and inserting the following:

"Sec. 137. Adoption assistance programs.
"Sec. 138. Cross reference to other Acts.".

(d) STUDY AND REPORT.—The Secretary of the Treasury shall study the effect on adoptions of the tax credit and gross income exclusion established by the amendments made by this section and shall submit a report regarding the study to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives not later than January 1, 2000. 26 USC 23 note.

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1808. REMOVAL OF BARRIERS TO INTERETHNIC ADOPTION.

(a) STATE PLAN REQUIREMENTS.—Section 471(a) of the Social Security Act (42 U.S.C 671(a)) is amended—

(1) by striking "and" at the end of paragraph (16);

(2) by striking the period at the end of paragraph (17) and inserting "; and"; and

(3) by adding at the end the following:

"(18) not later than January 1, 1997, provides that neither the State nor any other entity in the State that receives funds from the Federal Government and is involved in adoption or foster care placements may—

"(A) deny to any person the opportunity to become an adoptive or a foster parent, on the basis of the race, color, or national origin of the person, or of the child, involved; or

"(B) delay or deny the placement of a child for adoption or into foster care, on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved.".

(b) ENFORCEMENT.—Section 474 of such Act (42 U.S.C. 674) is amended by adding at the end the following:

"(d)(1) If, during any quarter of a fiscal year, a State's program operated under this part is found, as a result of a review conducted under section 1123A, or otherwise, to have violated section 471(a)(18) with respect to a person or to have failed to implement a corrective action plan within a period of time not to exceed 6 months with respect to such violation, then, notwithstanding subsection (a) of this section and any regulations promulgated under section 1123A(b)(3), the Secretary shall reduce the amount otherwise payable to the State under this part, for that fiscal year quarter and for any subsequent quarter of such fiscal year, until the State program is found, as a result of a subsequent review under section 1123A, to have implemented a corrective action plan with respect to such violation, by—

"(A) 2 percent of such otherwise payable amount, in the case of the 1st such finding for the fiscal year with respect to the State;

"(B) 3 percent of such otherwise payable amount, in the case of the 2nd such finding for the fiscal year with respect to the State; or

"(C) 5 percent of such otherwise payable amount, in the case of the 3rd or subsequent such finding for the fiscal year with respect to the State.

In imposing the penalties described in this paragraph, the Secretary shall not reduce any fiscal year payment to a State by more than 5 percent.

"(2) Any other entity which is in a State that receives funds under this part and which violates section 471(a)(18) during a

fiscal year quarter with respect to any person shall remit to the Secretary all funds that were paid by the State to the entity during the quarter from such funds.

"(3)(A) Any individual who is aggrieved by a violation of section 471(a)(18) by a State or other entity may bring an action seeking relief from the State or other entity in any United States district court.

"(B) An action under this paragraph may not be brought more than 2 years after the date the alleged violation occurred.

"(4) This subsection shall not be construed to affect the application of the Indian Child Welfare Act of 1978.".

42 USC 1996b.

(c) CIVIL RIGHTS.—

(1) PROHIBITED CONDUCT.—A person or government that is involved in adoption or foster care placements may not—

(A) deny to any individual the opportunity to become an adoptive or a foster parent, on the basis of the race, color, or national origin of the individual, or of the child, involved; or

(B) delay or deny the placement of a child for adoption or into foster care, on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved.

(2) ENFORCEMENT.—Noncompliance with paragraph (1) is deemed a violation of title VI of the Civil Rights Act of 1964.

(3) NO EFFECT ON THE INDIAN CHILD WELFARE ACT OF 1978.—This subsection shall not be construed to affect the application of the Indian Child Welfare Act of 1978.

(d) CONFORMING AMENDMENT.—Section 553 of the Howard M. Metzenbaum Multiethnic Placement Act of 1994 (42 U.S.C. 5115a) is repealed.

26 USC 6302 note.

SEC. 1809. 6-MONTH DELAY OF ELECTRONIC FUND TRANSFER REQUIREMENT.

Notwithstanding any other provision of law, the increase in the applicable required percentages for fiscal year 1997 in clauses (i)(IV) and (ii)(IV) of section 6302(h)(2)(C) of the Internal Revenue Code of 1986 shall not take effect before July 1, 1997.

Subtitle I—Foreign Trust Tax Compliance

SEC. 1901. IMPROVED INFORMATION REPORTING ON FOREIGN TRUSTS.

(a) IN GENERAL.—Section 6048 (relating to returns as to certain foreign trusts) is amended to read as follows:

"SEC. 6048. INFORMATION WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

"(a) NOTICE OF CERTAIN EVENTS.—

"(1) GENERAL RULE.—On or before the 90th day (or such later day as the Secretary may prescribe) after any reportable event, the responsible party shall provide written notice of such event to the Secretary in accordance with paragraph (2).

"(2) CONTENTS OF NOTICE.—The notice required by paragraph (1) shall contain such information as the Secretary may prescribe, including—

"(A) the amount of money or other property (if any) transferred to the trust in connection with the reportable event, and

"(B) the identity of the trust and of each trustee and beneficiary (or class of beneficiaries) of the trust.

"(3) REPORTABLE EVENT.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'reportable event' means—

"(i) the creation of any foreign trust by a United States person,

"(ii) the transfer of any money or property (directly or indirectly) to a foreign trust by a United States person, including a transfer by reason of death, and

"(iii) the death of a citizen or resident of the United States if—

"(I) the decedent was treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, or

"(II) any portion of a foreign trust was included in the gross estate of the decedent.

"(B) EXCEPTIONS.—

"(i) FAIR MARKET VALUE SALES.—Subparagraph (A)(ii) shall not apply to any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value and the rules of section 679(a)(3) shall apply.

"(ii) DEFERRED COMPENSATION AND CHARITABLE TRUSTS.—Subparagraph (A) shall not apply with respect to a trust which is—

"(I) described in section 402(b), 404(a)(4), or 404A, or

"(II) determined by the Secretary to be described in section 501(c)(3).

"(4) RESPONSIBLE PARTY.—For purposes of this subsection, the term 'responsible party' means—

"(A) the grantor in the case of the creation of an inter vivos trust,

"(B) the transferor in the case of a reportable event described in paragraph (3)(A)(ii) other than a transfer by reason of death, and

"(C) the executor of the decedent's estate in any other case.

"(b) UNITED STATES GRANTOR OF FOREIGN TRUST.—

"(1) IN GENERAL.—If, at any time during any taxable year of a United States person, such person is treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, such person shall be responsible to ensure that—

"(A) such trust makes a return for such year which sets forth a full and complete accounting of all trust activities and operations for the year, the name of the United States agent for such trust, and such other information as the Secretary may prescribe, and

"(B) such trust furnishes such information as the Secretary may prescribe to each United States person (i) who

is treated as the owner of any portion of such trust or (ii) who receives (directly or indirectly) any distribution from the trust.

"(2) TRUSTS NOT HAVING UNITED STATES AGENT.—

"(A) IN GENERAL.—If the rules of this paragraph apply to any foreign trust, the determination of amounts required to be taken into account with respect to such trust by a United States person under the rules of subpart E of part I of subchapter J of chapter 1 shall be determined by the Secretary.

"(B) UNITED STATES AGENT REQUIRED.—The rules of this paragraph shall apply to any foreign trust to which paragraph (1) applies unless such trust agrees (in such manner, subject to such conditions, and at such time as the Secretary shall prescribe) to authorize a United States person to act as such trust's limited agent solely for purposes of applying sections 7602, 7603, and 7604 with respect to—

"(i) any request by the Secretary to examine records or produce testimony related to the proper treatment of amounts required to be taken into account under the rules referred to in subparagraph (A), or

"(ii) any summons by the Secretary for such records or testimony.

The appearance of persons or production of records by reason of a United States person being such an agent shall not subject such persons or records to legal process for any purpose other than determining the correct treatment under this title of the amounts required to be taken into account under the rules referred to in subparagraph (A). A foreign trust which appoints an agent described in this subparagraph shall not be considered to have an office or a permanent establishment in the United States, or to be engaged in a trade or business in the United States, solely because of the activities of such agent pursuant to this subsection.

"(C) OTHER RULES TO APPLY.—Rules similar to the rules of paragraphs (2) and (4) of section 6038A(e) shall apply for purposes of this paragraph.

"(c) REPORTING BY UNITED STATES BENEFICIARIES OF FOREIGN TRUSTS.—

"(1) IN GENERAL.—If any United States person receives (directly or indirectly) during any taxable year of such person any distribution from a foreign trust, such person shall make a return with respect to such trust for such year which includes—

"(A) the name of such trust,

"(B) the aggregate amount of the distributions so received from such trust during such taxable year, and

"(C) such other information as the Secretary may prescribe.

"(2) INCLUSION IN INCOME IF RECORDS NOT PROVIDED.—

"(A) IN GENERAL.—If adequate records are not provided to the Secretary to determine the proper treatment of any distribution from a foreign trust, such distribution shall be treated as an accumulation distribution includible in the gross income of the distributee under chapter 1. To

the extent provided in regulations, the preceding sentence shall not apply if the foreign trust elects to be subject to rules similar to the rules of subsection (b)(2)(B).

"(B) APPLICATION OF ACCUMULATION DISTRIBUTION RULES.—For purposes of applying section 668 in a case to which subparagraph (A) applies, the applicable number of years for purposes of section 668(a) shall be ½ of the number of years the trust has been in existence.

"(d) SPECIAL RULES.—

"(1) DETERMINATION OF WHETHER UNITED STATES PERSON MAKES TRANSFER OR RECEIVES DISTRIBUTION.—For purposes of this section, in determining whether a United States person makes a transfer to, or receives a distribution from, a foreign trust, the fact that a portion of such trust is treated as owned by another person under the rules of subpart E of part I of subchapter J of chapter 1 shall be disregarded.

"(2) DOMESTIC TRUSTS WITH FOREIGN ACTIVITIES.—To the extent provided in regulations, a trust which is a United States person shall be treated as a foreign trust for purposes of this section and section 6677 if such trust has substantial activities, or holds substantial property, outside the United States.

"(3) TIME AND MANNER OF FILING INFORMATION.—Any notice or return required under this section shall be made at such time and in such manner as the Secretary shall prescribe.

"(4) MODIFICATION OF RETURN REQUIREMENTS.—The Secretary is authorized to suspend or modify any requirement of this section if the Secretary determines that the United States has no significant tax interest in obtaining the required information.".

(b) INCREASED PENALTIES.—Section 6677 (relating to failure to file information returns with respect to certain foreign trusts) is amended to read as follows:

"SEC. 6677. FAILURE TO FILE INFORMATION WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

"(a) CIVIL PENALTY.—In addition to any criminal penalty provided by law, if any notice or return required to be filed by section 6048—

"(1) is not filed on or before the time provided in such section, or

"(2) does not include all the information required pursuant to such section or includes incorrect information,

the person required to file such notice or return shall pay a penalty equal to 35 percent of the gross reportable amount. If any failure described in the preceding sentence continues for more than 90 days after the day on which the Secretary mails notice of such failure to the person required to pay such penalty, such person shall pay a penalty (in addition to the amount determined under the preceding sentence) of $10,000 for each 30-day period (or fraction thereof) during which such failure continues after the expiration of such 90-day period. In no event shall the penalty under this subsection with respect to any failure exceed the gross reportable amount.

"(b) SPECIAL RULES FOR RETURNS UNDER SECTION 6048(b).—In the case of a return required under section 6048(b)—

"(1) the United States person referred to in such section shall be liable for the penalty imposed by subsection (a), and

"(2) subsection (a) shall be applied by substituting '5 percent' for '35 percent'.

"(c) GROSS REPORTABLE AMOUNT.—For purposes of subsection (a), the term 'gross reportable amount' means—

"(1) the gross value of the property involved in the event (determined as of the date of the event) in the case of a failure relating to section 6048(a),

"(2) the gross value of the portion of the trust's assets at the close of the year treated as owned by the United States person in the case of a failure relating to section 6048(b)(1), and

"(3) the gross amount of the distributions in the case of a failure relating to section 6048(c).

"(d) REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed by this section on any failure which is shown to be due to reasonable cause and not due to willful neglect. The fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the required information is not reasonable cause.

"(e) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a).".

(c) CONFORMING AMENDMENTS.—

(1) Paragraph (2) of section 6724(d) is amended by striking "or" at the end of subparagraph (S), by striking the period at the end of subparagraph (T) and inserting ", or", and by inserting after subparagraph (T) the following new subparagraph:

"(U) section 6048(b)(1)(B) (relating to foreign trust reporting requirements).".

(2) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking the item relating to section 6048 and inserting the following new item:

"Sec. 6048. Information with respect to certain foreign trusts.".

(3) The table of sections for part I of subchapter B of chapter 68 is amended by striking the item relating to section 6677 and inserting the following new item:

"Sec. 6677. Failure to file information with respect to certain foreign trusts.".

26 USC 6048 note.

(d) EFFECTIVE DATES.—

(1) REPORTABLE EVENTS.—To the extent related to subsection (a) of section 6048 of the Internal Revenue Code of 1986, as amended by this section, the amendments made by this section shall apply to reportable events (as defined in such section 6048) occurring after the date of the enactment of this Act.

(2) GRANTOR TRUST REPORTING.—To the extent related to subsection (b) of such section 6048, the amendments made by this section shall apply to taxable years of United States persons beginning after December 31, 1995.

(3) REPORTING BY UNITED STATES BENEFICIARIES.—To the extent related to subsection (c) of such section 6048, the amendments made by this section shall apply to distributions received after the date of the enactment of this Act.

SEC. 1902. COMPARABLE PENALTIES FOR FAILURE TO FILE RETURN RELATING TO TRANSFERS TO FOREIGN ENTITIES.

(a) IN GENERAL.—Section 1494 is amended by adding at the end the following new subsection:

"(c) PENALTY.—In the case of any failure to file a return required by the Secretary with respect to any transfer described in section 1491, the person required to file such return shall be liable for the penalties provided in section 6677 in the same manner as if such failure were a failure to file a notice under section 6048(a).".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to transfers after the date of the enactment of this Act.

26 USC 1494 note.

SEC. 1903. MODIFICATIONS OF RULES RELATING TO FOREIGN TRUSTS HAVING ONE OR MORE UNITED STATES BENEFICIARIES.

(a) TREATMENT OF TRUST OBLIGATIONS, ETC.—

(1) Paragraph (2) of section 679(a) is amended by striking subparagraph (B) and inserting the following:

"(B) TRANSFERS AT FAIR MARKET VALUE.—To any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value.".

(2) Subsection (a) of section 679 (relating to foreign trusts having one or more United States beneficiaries) is amended by adding at the end the following new paragraph:

"(3) CERTAIN OBLIGATIONS NOT TAKEN INTO ACCOUNT UNDER FAIR MARKET VALUE EXCEPTION.—

"(A) IN GENERAL.—In determining whether paragraph (2)(B) applies to any transfer by a person described in clause (ii) or (iii) of subparagraph (C), there shall not be taken into account—

"(i) except as provided in regulations, any obligation of a person described in subparagraph (C), and

"(ii) to the extent provided in regulations, any obligation which is guaranteed by a person described in subparagraph (C).

"(B) TREATMENT OF PRINCIPAL PAYMENTS ON OBLIGATION.—Principal payments by the trust on any obligation referred to in subparagraph (A) shall be taken into account on and after the date of the payment in determining the portion of the trust attributable to the property transferred.

"(C) PERSONS DESCRIBED.—The persons described in this subparagraph are—

"(i) the trust,

"(ii) any grantor or beneficiary of the trust, and

"(iii) any person who is related (within the meaning of section 643(i)(2)(B)) to any grantor or beneficiary of the trust.".

(b) EXEMPTION OF TRANSFERS TO CHARITABLE TRUSTS.—Subsection (a) of section 679 is amended by striking "section 404(a)(4) or 404A" and inserting "section 6048(a)(3)(B)(ii)".

(c) OTHER MODIFICATIONS.—Subsection (a) of section 679 is amended by adding at the end the following new paragraphs:

"(4) SPECIAL RULES APPLICABLE TO FOREIGN GRANTOR WHO LATER BECOMES A UNITED STATES PERSON.—

"(A) IN GENERAL.—If a nonresident alien individual has a residency starting date within 5 years after directly or indirectly transferring property to a foreign trust, this section and section 6048 shall be applied as if such individual transferred to such trust on the residency starting date an amount equal to the portion of such trust attributable to the property transferred by such individual to such trust in such transfer.

"(B) TREATMENT OF UNDISTRIBUTED INCOME.—For purposes of this section, undistributed net income for periods before such individual's residency starting date shall be taken into account in determining the portion of the trust which is attributable to property transferred by such individual to such trust but shall not otherwise be taken into account.

"(C) RESIDENCY STARTING DATE.—For purposes of this paragraph, an individual's residency starting date is the residency starting date determined under section 7701(b)(2)(A).

"(5) OUTBOUND TRUST MIGRATIONS.—If—

"(A) an individual who is a citizen or resident of the United States transferred property to a trust which was not a foreign trust, and

"(B) such trust becomes a foreign trust while such individual is alive,

then this section and section 6048 shall be applied as if such individual transferred to such trust on the date such trust becomes a foreign trust an amount equal to the portion of such trust attributable to the property previously transferred by such individual to such trust. A rule similar to the rule of paragraph (4)(B) shall apply for purposes of this paragraph.".

(d) MODIFICATIONS RELATING TO WHETHER TRUST HAS UNITED STATES BENEFICIARIES.—Subsection (c) of section 679 is amended by adding at the end the following new paragraph:

"(3) CERTAIN UNITED STATES BENEFICIARIES DISREGARDED.—A beneficiary shall not be treated as a United States person in applying this section with respect to any transfer of property to foreign trust if such beneficiary first became a United States person more than 5 years after the date of such transfer.".

(e) TECHNICAL AMENDMENT.—Subparagraph (A) of section 679(c)(2) is amended to read as follows:

"(A) in the case of a foreign corporation, such corporation is a controlled foreign corporation (as defined in section 957(a)),".

(f) REGULATIONS.—Section 679 is amended by adding at the end the following new subsection:

"(d) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.".

26 USC 679 note.

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to transfers of property after February 6, 1995.

SEC. 1904. FOREIGN PERSONS NOT TO BE TREATED AS OWNERS UNDER GRANTOR TRUST RULES.

(a) GENERAL RULE.—

(1) Subsection (f) of section 672 (relating to special rule where grantor is foreign person) is amended to read as follows:

"(f) SUBPART NOT TO RESULT IN FOREIGN OWNERSHIP.—

"(1) IN GENERAL.—Notwithstanding any other provision of this subpart, this subpart shall apply only to the extent such application results in an amount (if any) being currently taken into account (directly or through 1 or more entities) under this chapter in computing the income of a citizen or resident of the United States or a domestic corporation.

"(2) EXCEPTIONS.—

"(A) CERTAIN REVOCABLE AND IRREVOCABLE TRUSTS.—Paragraph (1) shall not apply to any portion of a trust if—

"(i) the power to revest absolutely in the grantor title to the trust property to which such portion is attributable is exercisable solely by the grantor without the approval or consent of any other person or with the consent of a related or subordinate party who is subservient to the grantor, or

"(ii) the only amounts distributable from such portion (whether income or corpus) during the lifetime of the grantor are amounts distributable to the grantor or the spouse of the grantor.

"(B) COMPENSATORY TRUSTS.—Except as provided in regulations, paragraph (1) shall not apply to any portion of a trust distributions from which are taxable as compensation for services rendered.

"(3) SPECIAL RULES.—Except as otherwise provided in regulations prescribed by the Secretary—

"(A) a controlled foreign corporation (as defined in section 957) shall be treated as a domestic corporation for purposes of paragraph (1), and

"(B) paragraph (1) shall not apply for purposes of applying section 1296.

"(4) RECHARACTERIZATION OF PURPORTED GIFTS.—In the case of any transfer directly or indirectly from a partnership or foreign corporation which the transferee treats as a gift or bequest, the Secretary may recharacterize such transfer in such circumstances as the Secretary determines to be appropriate to prevent the avoidance of the purposes of this subsection.

"(5) SPECIAL RULE WHERE GRANTOR IS FOREIGN PERSON.—If—

"(A) but for this subsection, a foreign person would be treated as the owner of any portion of a trust, and

"(B) such trust has a beneficiary who is a United States person,

such beneficiary shall be treated as the grantor of such portion to the extent such beneficiary has made (directly or indirectly) transfers of property (other than in a sale for full and adequate consideration) to such foreign person. For purposes of the preceding sentence, any gift shall not be taken into account to the extent such gift would be excluded from taxable gifts under section 2503(b).

"(6) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out

the purposes of this subsection, including regulations providing that paragraph (1) shall not apply in appropriate cases.".

(2) The last sentence of subsection (c) of section 672 is amended by inserting "subsection (f) and" before "sections 674".

(b) CREDIT FOR CERTAIN TAXES.—

(1) Paragraph (2) of section 665(d) is amended by adding at the end the following new sentence: "Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust under subpart E but for section 672(f), the term 'taxes imposed on the trust' includes the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on the settlor or such other person in respect of trust income.".

(2) Paragraph (5) of section 901(b) is amended by adding at the end the following new sentence: "Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust under subpart E but for section 672(f), the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on the settlor or such other person in respect of trust income.".

(c) DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS THROUGH NOMINEES.—

(1) Section 643 is amended by adding at the end the following new subsection:

"(h) DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS THROUGH NOMINEES.—For purposes of this part, any amount paid to a United States person which is derived directly or indirectly from a foreign trust of which the payor is not the grantor shall be deemed in the year of payment to have been directly paid by the foreign trust to such United States person.".

(2) Section 665 is amended by striking subsection (c).

26 USC 643 note.

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided by paragraph (2), the amendments made by this section shall take effect on the date of the enactment of this Act.

(2) EXCEPTION FOR CERTAIN TRUSTS.—The amendments made by this section shall not apply to any trust—

(A) which is treated as owned by the grantor under section 676 or 677 (other than subsection (a)(3) thereof) of the Internal Revenue Code of 1986, and

(B) which is in existence on September 19, 1995.

The preceding sentence shall not apply to the portion of any such trust attributable to any transfer to such trust after September 19, 1995.

26 USC 1491 note.

(e) TRANSITIONAL RULE.—If—

(1) by reason of the amendments made by this section, any person other than a United States person ceases to be treated as the owner of a portion of a domestic trust, and

(2) before January 1, 1997, such trust becomes a foreign trust, or the assets of such trust are transferred to a foreign trust,

no tax shall be imposed by section 1491 of the Internal Revenue Code of 1986 by reason of such trust becoming a foreign trust or the assets of such trust being transferred to a foreign trust.

SEC. 1905. INFORMATION REPORTING REGARDING FOREIGN GIFTS.

(a) IN GENERAL.—Subpart A of part III of subchapter A of chapter 61 is amended by inserting after section 6039E the following new section:

"SEC. 6039F. NOTICE OF LARGE GIFTS RECEIVED FROM FOREIGN PERSONS.

"(a) IN GENERAL.—If the value of the aggregate foreign gifts received by a United States person (other than an organization described in section 501(c) and exempt from tax under section 501(a)) during any taxable year exceeds $10,000, such United States person shall furnish (at such time and in such manner as the Secretary shall prescribe) such information as the Secretary may prescribe regarding each foreign gift received during such year.

"(b) FOREIGN GIFT.—For purposes of this section, the term 'foreign gift' means any amount received from a person other than a United States person which the recipient treats as a gift or bequest. Such term shall not include any qualified transfer (within the meaning of section 2503(e)(2)) or any distribution properly disclosed in a return under section 6048(c).

"(c) PENALTY FOR FAILURE TO FILE INFORMATION.—

"(1) IN GENERAL.—If a United States person fails to furnish the information required by subsection (a) with respect to any foreign gift within the time prescribed therefor (including extensions)—

"(A) the tax consequences of the receipt of such gift shall be determined by the Secretary, and

"(B) such United States person shall pay (upon notice and demand by the Secretary and in the same manner as tax) an amount equal to 5 percent of the amount of such foreign gift for each month for which the failure continues (not to exceed 25 percent of such amount in the aggregate).

"(2) REASONABLE CAUSE EXCEPTION.—Paragraph (1) shall not apply to any failure to report a foreign gift if the United States person shows that the failure is due to reasonable cause and not due to willful neglect.

"(d) COST-OF-LIVING ADJUSTMENT.—In the case of any taxable year beginning after December 31, 1996, the $10,000 amount under subsection (a) shall be increased by an amount equal to the product of such amount and the cost-of-living adjustment for such taxable year under section 1(f)(3), except that subparagraph (B) thereof shall be applied by substituting '1995' for '1992'.

"(e) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.".

(b) CLERICAL AMENDMENT.—The table of sections for such subpart is amended by inserting after the item relating to section 6039E the following new item:

"Sec. 6039F. Notice of large gifts received from foreign persons.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts received after the date of the enactment of this Act in taxable years ending after such date.

26 USC 6039F note.

SEC. 1906. MODIFICATION OF RULES RELATING TO FOREIGN TRUSTS WHICH ARE NOT GRANTOR TRUSTS.

(a) MODIFICATION OF INTEREST CHARGE ON ACCUMULATION DISTRIBUTIONS.—Subsection (a) of section 668 (relating to interest charge on accumulation distributions from foreign trusts) is amended to read as follows:

"(a) GENERAL RULE.—For purposes of the tax determined under section 667(a)—

"(1) INTEREST DETERMINED USING UNDERPAYMENT RATES.—The interest charge determined under this section with respect to any distribution is the amount of interest which would be determined on the partial tax computed under section 667(b) for the period described in paragraph (2) using the rates and the method under section 6621 applicable to underpayments of tax.

"(2) PERIOD.—For purposes of paragraph (1), the period described in this paragraph is the period which begins on the date which is the applicable number of years before the date of the distribution and which ends on the date of the distribution.

"(3) APPLICABLE NUMBER OF YEARS.—For purposes of paragraph (2)—

"(A) IN GENERAL.—The applicable number of years with respect to a distribution is the number determined by dividing—

"(i) the sum of the products described in subparagraph (B) with respect to each undistributed income year, by

"(ii) the aggregate undistributed net income.

The quotient determined under the preceding sentence shall be rounded under procedures prescribed by the Secretary.

"(B) PRODUCT DESCRIBED.—For purposes of subparagraph (A), the product described in this subparagraph with respect to any undistributed income year is the product of—

"(i) the undistributed net income for such year, and

"(ii) the sum of the number of taxable years between such year and the taxable year of the distribution (counting in each case the undistributed income year but not counting the taxable year of the distribution).

"(4) UNDISTRIBUTED INCOME YEAR.—For purposes of this subsection, the term 'undistributed income year' means any prior taxable year of the trust for which there is undistributed net income, other than a taxable year during all of which the beneficiary receiving the distribution was not a citizen or resident of the United States.

"(5) DETERMINATION OF UNDISTRIBUTED NET INCOME.—Notwithstanding section 666, for purposes of this subsection, an accumulation distribution from the trust shall be treated as reducing proportionately the undistributed net income for undistributed income years.

"(6) PERIODS BEFORE 1996.—Interest for the portion of the period described in paragraph (2) which occurs before January 1, 1996, shall be determined—

"(A) by using an interest rate of 6 percent, and

"(B) without compounding until January 1, 1996.".

(b) ABUSIVE TRANSACTIONS.—Section 643(a) is amended by inserting after paragraph (6) the following new paragraph:

"(7) ABUSIVE TRANSACTIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this part, including regulations to prevent avoidance of such purposes.".

(c) TREATMENT OF LOANS FROM TRUSTS.—

(1) IN GENERAL.—Section 643 (relating to definitions applicable to subparts A, B, C, and D) is amended by adding at the end the following new subsection:

"(i) LOANS FROM FOREIGN TRUSTS.—For purposes of subparts B, C, and D—

"(1) GENERAL RULE.—Except as provided in regulations, if a foreign trust makes a loan of cash or marketable securities directly or indirectly to—

"(A) any grantor or beneficiary of such trust who is a United States person, or

"(B) any United States person not described in subparagraph (A) who is related to such grantor or beneficiary,

the amount of such loan shall be treated as a distribution by such trust to such grantor or beneficiary (as the case may be).

"(2) DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—

"(A) CASH.—The term 'cash' includes foreign currencies and cash equivalents.

"(B) RELATED PERSON.—

"(i) IN GENERAL.—A person is related to another person if the relationship between such persons would result in a disallowance of losses under section 267 or 707(b). In applying section 267 for purposes of the preceding sentence, section 267(c)(4) shall be applied as if the family of an individual includes the spouses of the members of the family.

"(ii) ALLOCATION.—If any person described in paragraph (1)(B) is related to more than one person, the grantor or beneficiary to whom the treatment under this subsection applies shall be determined under regulations prescribed by the Secretary.

"(C) EXCLUSION OF TAX-EXEMPTS.—The term 'United States person' does not include any entity exempt from tax under this chapter.

"(D) TRUST NOT TREATED AS SIMPLE TRUST.—Any trust which is treated under this subsection as making a distribution shall be treated as not described in section 651.

"(3) SUBSEQUENT TRANSACTIONS REGARDING LOAN PRINCIPAL.—If any loan is taken into account under paragraph (1), any subsequent transaction between the trust and the original borrower regarding the principal of the loan (by way of complete or partial repayment, satisfaction, cancellation, discharge, or otherwise) shall be disregarded for purposes of this title."

(2) TECHNICAL AMENDMENT.—Paragraph (8) of section 7872(f) is amended by inserting ", 643(i)," before "or 1274" each place it appears.

(d) EFFECTIVE DATES.—

26 USC 668 note.

(1) INTEREST CHARGE.—The amendment made by subsection (a) shall apply to distributions after the date of the enactment of this Act.

26 USC 643 note.

(2) ABUSIVE TRANSACTIONS.—The amendment made by subsection (b) shall take effect on the date of the enactment of this Act.

26 USC 643 note.

(3) LOANS FROM TRUSTS.—The amendment made by subsection (c) shall apply to loans of cash or marketable securities made after September 19, 1995.

SEC. 1907. RESIDENCE OF TRUSTS, ETC.

(a) TREATMENT AS UNITED STATES PERSON.—

(1) IN GENERAL.—Paragraph (30) of section 7701(a) is amended by striking "and" at the end of subparagraph (C) and by striking subparagraph (D) and by inserting the following new subparagraphs:

"(D) any estate (other than a foreign estate, within the meaning of paragraph (31)), and

"(E) any trust if—

"(i) a court within the United States is able to exercise primary supervision over the administration of the trust, and

"(ii) one or more United States fiduciaries have the authority to control all substantial decisions of the trust.".

(2) CONFORMING AMENDMENT.—Paragraph (31) of section 7701(a) is amended to read as follows:

"(31) FOREIGN ESTATE OR TRUST.—

"(A) FOREIGN ESTATE.—The term 'foreign estate' means an estate the income of which, from sources without the United States which is not effectively connected with the conduct of a trade or business within the United States, is not includible in gross income under subtitle A.

"(B) FOREIGN TRUST.—The term 'foreign trust' means any trust other than a trust described in subparagraph (E) of paragraph (30).".

26 USC 7701 note.

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply—

(A) to taxable years beginning after December 31, 1996, or

(B) at the election of the trustee of a trust, to taxable years ending after the date of the enactment of this Act.

Such an election, once made, shall be irrevocable.

(b) DOMESTIC TRUSTS WHICH BECOME FOREIGN TRUSTS.—

(1) IN GENERAL.—Section 1491 (relating to imposition of tax on transfers to avoid income tax) is amended by adding at the end the following new flush sentence:

"If a trust which is not a foreign trust becomes a foreign trust, such trust shall be treated for purposes of this section as having transferred, immediately before becoming a foreign trust, all of its assets to a foreign trust."

(2) EFFECTIVE DATE.—The amendment made by this subsection shall take effect on the date of the enactment of this Act. 26 USC 1491 note.

Subtitle J—Generalized System of Preferences

GSP Renewal Act of 1996.

SEC. 1951. SHORT TITLE. 19 USC 2101 note.

This subtitle may be cited as the "GSP Renewal Act of 1996".

SEC. 1952. GENERALIZED SYSTEM OF PREFERENCES.

(a) IN GENERAL.—Title V of the Trade Act of 1974 is amended to read as follows:

"TITLE V—GENERALIZED SYSTEM OF PREFERENCES

"SEC. 501. AUTHORITY TO EXTEND PREFERENCES. 19 USC 2461.

"The President may provide duty-free treatment for any eligible article from any beneficiary developing country in accordance with the provisions of this title. In taking any such action, the President shall have due regard for—

"(1) the effect such action will have on furthering the economic development of developing countries through the expansion of their exports;

"(2) the extent to which other major developed countries are undertaking a comparable effort to assist developing countries by granting generalized preferences with respect to imports of products of such countries;

"(3) the anticipated impact of such action on United States producers of like or directly competitive products; and

"(4) the extent of the beneficiary developing country's competitiveness with respect to eligible articles.

"SEC. 502. DESIGNATION OF BENEFICIARY DEVELOPING COUNTRIES. 19 USC 2462.

"(a) AUTHORITY TO DESIGNATE COUNTRIES.—

"(1) BENEFICIARY DEVELOPING COUNTRIES.—The President is authorized to designate countries as beneficiary developing countries for purposes of this title.

"(2) LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRIES.—The President is authorized to designate any beneficiary developing country as a least-developed beneficiary developing country for purposes of this title, based on the considerations in section 501 and subsection (c) of this section.

"(b) COUNTRIES INELIGIBLE FOR DESIGNATION.—

"(1) SPECIFIC COUNTRIES.—The following countries may not be designated as beneficiary developing countries for purposes of this title:

"(A) Australia.
"(B) Canada.
"(C) European Union member states.
"(D) Iceland.
"(E) Japan.
"(F) Monaco.
"(G) New Zealand.

"(H) Norway.

"(I) Switzerland.

President. "(2) OTHER BASES FOR INELIGIBILITY.—The President shall not designate any country a beneficiary developing country under this title if any of the following applies:

"(A) Such country is a Communist country, unless—

"(i) the products of such country receive nondiscriminatory treatment,

"(ii) such country is a WTO Member (as such term is defined in section 2(10) of the Uruguay Round Agreements Act) (19 U.S.C. 3501(10)) and a member of the International Monetary Fund, and

"(iii) such country is not dominated or controlled by international communism.

"(B) Such country is a party to an arrangement of countries and participates in any action pursuant to such arrangement, the effect of which is—

"(i) to withhold supplies of vital commodity resources from international trade or to raise the price of such commodities to an unreasonable level, and

"(ii) to cause serious disruption of the world economy.

"(C) Such country affords preferential treatment to the products of a developed country, other than the United States, which has, or is likely to have, a significant adverse effect on United States commerce.

"(D)(i) Such country—

"(I) has nationalized, expropriated, or otherwise seized ownership or control of property, including patents, trademarks, or copyrights, owned by a United States citizen or by a corporation, partnership, or association which is 50 percent or more beneficially owned by United States citizens,

"(II) has taken steps to repudiate or nullify an existing contract or agreement with a United States citizen or a corporation, partnership, or association which is 50 percent or more beneficially owned by United States citizens, the effect of which is to nationalize, expropriate, or otherwise seize ownership or control of property, including patents, trademarks, or copyrights, so owned, or

"(III) has imposed or enforced taxes or other exactions, restrictive maintenance or operational conditions, or other measures with respect to property, including patents, trademarks, or copyrights, so owned, the effect of which is to nationalize, expropriate, or otherwise seize ownership or control of such property, unless clause (ii) applies.

"(ii) This clause applies if the President determines that—

"(I) prompt, adequate, and effective compensation has been or is being made to the citizen, corporation, partnership, or association referred to in clause (i),

"(II) good faith negotiations to provide prompt, adequate, and effective compensation under the applicable provisions of international law are in progress, or the country described in clause (i) is other-

wise taking steps to discharge its obligations under international law with respect to such citizen, corporation, partnership, or association, or

"(III) a dispute involving such citizen, corporation, partnership, or association over compensation for such a seizure has been submitted to arbitration under the provisions of the Convention for the Settlement of Investment Disputes, or in another mutually agreed upon forum,

and the President promptly furnishes a copy of such determination to the Senate and House of Representatives.

"(E) Such country fails to act in good faith in recognizing as binding or in enforcing arbitral awards in favor of United States citizens or a corporation, partnership, or association which is 50 percent or more beneficially owned by United States citizens, which have been made by arbitrators appointed for each case or by permanent arbitral bodies to which the parties involved have submitted their dispute.

"(F) Such country aids or abets, by granting sanctuary from prosecution to, any individual or group which has committed an act of international terrorism.

"(G) Such country has not taken or is not taking steps to afford internationally recognized worker rights to workers in the country (including any designated zone in that country).

Subparagraphs (D), (E), (F), and (G) shall not prevent the designation of any country as a beneficiary developing country under this title if the President determines that such designation will be in the national economic interest of the United States and reports such determination to the Congress with the reasons therefor.

"(c) FACTORS AFFECTING COUNTRY DESIGNATION.—In determining whether to designate any country as a beneficiary developing country under this title, the President shall take into account—

"(1) an expression by such country of its desire to be so designated;

"(2) the level of economic development of such country, including its per capita gross national product, the living standards of its inhabitants, and any other economic factors which the President deems appropriate;

"(3) whether or not other major developed countries are extending generalized preferential tariff treatment to such country;

"(4) the extent to which such country has assured the United States that it will provide equitable and reasonable access to the markets and basic commodity resources of such country and the extent to which such country has assured the United States that it will refrain from engaging in unreasonable export practices;

"(5) the extent to which such country is providing adequate and effective protection of intellectual property rights;

"(6) the extent to which such country has taken action to—

"(A) reduce trade distorting investment practices and policies (including export performance requirements); and

"(B) reduce or eliminate barriers to trade in services; and

"(7) whether or not such country has taken or is taking steps to afford to workers in that country (including any designated zone in that country) internationally recognized worker rights.

"(d) WITHDRAWAL, SUSPENSION, OR LIMITATION OF COUNTRY DESIGNATION.—

"(1) IN GENERAL.—The President may withdraw, suspend, or limit the application of the duty-free treatment accorded under this title with respect to any country. In taking any action under this subsection, the President shall consider the factors set forth in section 501 and subsection (c) of this section.

"(2) CHANGED CIRCUMSTANCES.—The President shall, after complying with the requirements of subsection (f)(2), withdraw or suspend the designation of any country as a beneficiary developing country if, after such designation, the President determines that as the result of changed circumstances such country would be barred from designation as a beneficiary developing country under subsection (b)(2). Such country shall cease to be a beneficiary developing country on the day on which the President issues an Executive order or Presidential proclamation revoking the designation of such country under this title.

President. "(3) ADVICE TO CONGRESS.—The President shall, as necessary, advise the Congress on the application of section 501 and subsection (c) of this section, and the actions the President has taken to withdraw, to suspend, or to limit the application of duty-free treatment with respect to any country which has failed to adequately take the actions described in subsection (c).

"(e) MANDATORY GRADUATION OF BENEFICIARY DEVELOPING COUNTRIES.—If the President determines that a beneficiary developing country has become a 'high income' country, as defined by the official statistics of the International Bank for Reconstruction and Development, then the President shall terminate the designation of such country as a beneficiary developing country for purposes of this title, effective on January 1 of the second year following the year in which such determination is made.

"(f) CONGRESSIONAL NOTIFICATION.—

"(1) NOTIFICATION OF DESIGNATION.—

"(A) IN GENERAL.—Before the President designates any country as a beneficiary developing country under this title, the President shall notify the Congress of the President's intention to make such designation, together with the considerations entering into such decision.

"(B) DESIGNATION AS LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRY.—At least 60 days before the President designates any country as a least-developed beneficiary developing country, the President shall notify the Congress of the President's intention to make such designation.

"(2) NOTIFICATION OF TERMINATION.—If the President has designated any country as a beneficiary developing country under this title, the President shall not terminate such designation unless, at least 60 days before such termination, the President has notified the Congress and has notified such country

of the President's intention to terminate such designation, together with the considerations entering into such decision.

"SEC. 503. DESIGNATION OF ELIGIBLE ARTICLES. 19 USC 2463.

"(a) ELIGIBLE ARTICLES.—

"(1) DESIGNATION.—

"(A) IN GENERAL.—Except as provided in subsection (b), the President is authorized to designate articles as eligible articles from all beneficiary developing countries for purposes of this title by Executive order or Presidential proclamation after receiving the advice of the International Trade Commission in accordance with subsection (e).

"(B) LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRIES.—Except for articles described in subparagraphs (A), (B), and (E) of subsection (b)(1) and articles described in paragraphs (2) and (3) of subsection (b), the President may, in carrying out section 502(d)(1) and subsection (c)(1) of this section, designate articles as eligible articles only for countries designated as least-developed beneficiary developing countries under section 502(a)(2) if, after receiving the advice of the International Trade Commission in accordance with subsection (e) of this section, the President determines that such articles are not import-sensitive in the context of imports from least-developed beneficiary developing countries.

"(C) THREE-YEAR RULE.—If, after receiving the advice of the International Trade Commission under subsection (e), an article has been formally considered for designation as an eligible article under this title and denied such designation, such article may not be reconsidered for such designation for a period of 3 years after such denial.

"(2) RULE OF ORIGIN.—

"(A) GENERAL RULE.—The duty-free treatment provided under this title shall apply to any eligible article which is the growth, product, or manufacture of a beneficiary developing country if—

"(i) that article is imported directly from a beneficiary developing country into the customs territory of the United States; and

"(ii) the sum of—

"(I) the cost or value of the materials produced in the beneficiary developing country or any two or more such countries that are members of the same association of countries and are treated as one country under section 507(2), plus

"(II) the direct costs of processing operations performed in such beneficiary developing country or such member countries, is not less than 35 percent of the appraised value of such article at the time it is entered.

"(B) EXCLUSIONS.—An article shall not be treated as the growth, product, or manufacture of a beneficiary developing country by virtue of having merely undergone—

"(i) simple combining or packaging operations, or

"(ii) mere dilution with water or mere dilution with another substance that does not materially alter the characteristics of the article.

"(3) REGULATIONS.—The Secretary of the Treasury, after consulting with the United States Trade Representative, shall prescribe such regulations as may be necessary to carry out paragraph (2), including, but not limited to, regulations providing that, in order to be eligible for duty-free treatment under this title, an article—

"(A) must be wholly the growth, product, or manufacture of a beneficiary developing country, or

"(B) must be a new or different article of commerce which has been grown, produced, or manufactured in the beneficiary developing country.

"(b) ARTICLES THAT MAY NOT BE DESIGNATED AS ELIGIBLE ARTICLES.—

"(1) IMPORT SENSITIVE ARTICLES.—The President may not designate any article as an eligible article under subsection (a) if such article is within one of the following categories of import-sensitive articles:

"(A) Textile and apparel articles which were not eligible articles for purposes of this title on January 1, 1994, as this title was in effect on such date.

"(B) Watches, except those watches entered after June 30, 1989, that the President specifically determines, after public notice and comment, will not cause material injury to watch or watch band, strap, or bracelet manufacturing and assembly operations in the United States or the United States insular possessions.

"(C) Import-sensitive electronic articles.

"(D) Import-sensitive steel articles.

"(E) Footwear, handbags, luggage, flat goods, work gloves, and leather wearing apparel which were not eligible articles for purposes of this title on January 1, 1995, as this title was in effect on such date.

"(F) Import-sensitive semimanufactured and manufactured glass products.

"(G) Any other articles which the President determines to be import-sensitive in the context of the Generalized System of Preferences.

"(2) ARTICLES AGAINST WHICH OTHER ACTIONS TAKEN.—An article shall not be an eligible article for purposes of this title for any period during which such article is the subject of any action proclaimed pursuant to section 203 of this Act (19 U.S.C. 2253) or section 232 or 351 of the Trade Expansion Act of 1962 (19 U.S.C. 1862, 1981).

"(3) AGRICULTURAL PRODUCTS.—No quantity of an agricultural product subject to a tariff-rate quota that exceeds the in-quota quantity shall be eligible for duty-free treatment under this title.

"(c) WITHDRAWAL, SUSPENSION, OR LIMITATION OF DUTY-FREE TREATMENT; COMPETITIVE NEED LIMITATION.—

"(1) IN GENERAL.—The President may withdraw, suspend, or limit the application of the duty-free treatment accorded under this title with respect to any article, except that no rate of duty may be established with respect to any article pursuant to this subsection other than the rate which would apply but for this title. In taking any action under this subsection, the President shall consider the factors set forth in sections 501 and 502(c).

"(2) COMPETITIVE NEED LIMITATION.—

"(A) BASIS FOR WITHDRAWAL OF DUTY-FREE TREATMENT.—

"(i) IN GENERAL.—Except as provided in clause (ii) and subject to subsection (d), whenever the President determines that a beneficiary developing country has exported (directly or indirectly) to the United States during any calendar year beginning after December 31, 1995—

"(I) a quantity of an eligible article having an appraised value in excess of the applicable amount for the calendar year, or

"(II) a quantity of an eligible article equal to or exceeding 50 percent of the appraised value of the total imports of that article into the United States during any calendar year,

the President shall, not later than July 1 of the next calendar year, terminate the duty-free treatment for that article from that beneficiary developing country.

"(ii) ANNUAL ADJUSTMENT OF APPLICABLE AMOUNT.—For purposes of applying clause (i), the applicable amount is—

"(I) for 1996, $75,000,000, and

"(II) for each calendar year thereafter, an amount equal to the applicable amount in effect for the preceding calendar year plus $5,000,000.

"(B) COUNTRY DEFINED.—For purposes of this paragraph, the term 'country' does not include an association of countries which is treated as one country under section 507(2), but does include a country which is a member of any such association.

"(C) REDESIGNATIONS.—A country which is no longer treated as a beneficiary developing country with respect to an eligible article by reason of subparagraph (A) may, subject to the considerations set forth in sections 501 and 502, be redesignated a beneficiary developing country with respect to such article if imports of such article from such country did not exceed the limitations in subparagraph (A) during the preceding calendar year.

"(D) LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRIES.—Subparagraph (A) shall not apply to any least-developed beneficiary developing country.

"(E) ARTICLES NOT PRODUCED IN THE UNITED STATES EXCLUDED.—Subparagraph (A)(i)(II) shall not apply with respect to any eligible article if a like or directly competitive article was not produced in the United States on January 1, 1995.

"(F) DE MINIMIS WAIVERS.—

"(i) IN GENERAL.—The President may disregard subparagraph (A)(i)(II) with respect to any eligible article from any beneficiary developing country if the aggregate appraised value of the imports of such article into the United States during the preceding calendar year does not exceed the applicable amount for such preceding calendar year.

"(ii) APPLICABLE AMOUNT.—For purposes of applying clause (i), the applicable amount is—

"(I) for calendar year 1996, $13,000,000, and

"(II) for each calendar year thereafter, an amount equal to the applicable amount in effect for the preceding calendar year plus $500,000.

"(d) WAIVER OF COMPETITIVE NEED LIMITATION.—

"(1) IN GENERAL.—The President may waive the application of subsection (c)(2) with respect to any eligible article of any beneficiary developing country if, before July 1 of the calendar year beginning after the calendar year for which a determination described in subsection (c)(2)(A) was made with respect to such eligible article, the President—

"(A) receives the advice of the International Trade Commission under section 332 of the Tariff Act of 1930 on whether any industry in the United States is likely to be adversely affected by such waiver,

"(B) determines, based on the considerations described in sections 501 and 502(c) and the advice described in subparagraph (A), that such waiver is in the national economic interest of the United States, and

"(C) publishes the determination described in subparagraph (B) in the Federal Register.

"(2) CONSIDERATIONS BY THE PRESIDENT.—In making any determination under paragraph (1), the President shall give great weight to—

"(A) the extent to which the beneficiary developing country has assured the United States that such country will provide equitable and reasonable access to the markets and basic commodity resources of such country, and

"(B) the extent to which such country provides adequate and effective protection of intellectual property rights.

"(3) OTHER BASES FOR WAIVER.—The President may waive the application of subsection (c)(2) if, before July 1 of the calendar year beginning after the calendar year for which a determination described in subsection (c)(2) was made with respect to a beneficiary developing country, the President determines that—

"(A) there has been a historical preferential trade relationship between the United States and such country,

"(B) there is a treaty or trade agreement in force covering economic relations between such country and the United States, and

"(C) such country does not discriminate against, or impose unjustifiable or unreasonable barriers to, United States commerce,

and the President publishes that determination in the Federal Register.

"(4) LIMITATIONS ON WAIVERS.—

"(A) IN GENERAL.—The President may not exercise the waiver authority under this subsection with respect to a quantity of an eligible article entered during any calendar year beginning after 1995, the aggregate appraised value of which equals or exceeds 30 percent of the aggregate appraised value of all articles that entered duty-free under this title during the preceding calendar year.

"(B) OTHER WAIVER LIMITS.—The President may not exercise the waiver authority provided under this sub-

section with respect to a quantity of an eligible article entered during any calendar year beginning after 1995, the aggregate appraised value of which exceeds 15 percent of the aggregate appraised value of all articles that have entered duty-free under this title during the preceding calendar year from those beneficiary developing countries which for the preceding calendar year—

"(i) had a per capita gross national product (calculated on the basis of the best available information, including that of the International Bank for Reconstruction and Development) of $5,000 or more; or

"(ii) had exported (either directly or indirectly) to the United States a quantity of articles that was duty-free under this title that had an aggregate appraised value of more than 10 percent of the aggregate appraised value of all articles that entered duty-free under this title during that year.

"(C) CALCULATION OF LIMITATIONS.—There shall be counted against the limitations imposed under subparagraphs (A) and (B) for any calendar year only that value of any eligible article of any country that—

"(i) entered duty-free under this title during such calendar year; and

"(ii) is in excess of the value of that article that would have been so entered during such calendar year if the limitations under subsection (c)(2)(A) applied.

"(5) EFFECTIVE PERIOD OF WAIVER.—Any waiver granted under this subsection shall remain in effect until the President determines that such waiver is no longer warranted due to changed circumstances.

"(e) INTERNATIONAL TRADE COMMISSION ADVICE.—Before designating articles as eligible articles under subsection (a)(1), the President shall publish and furnish the International Trade Commission with lists of articles which may be considered for designation as eligible articles for purposes of this title. The provisions of sections 131, 132, 133, and 134 shall be complied with as though action under section 501 and this section were action under section 123 to carry out a trade agreement entered into under section 123.

"(f) SPECIAL RULE CONCERNING PUERTO RICO.—No action under this title may affect any tariff duty imposed by the Legislature of Puerto Rico pursuant to section 319 of the Tariff Act of 1930 on coffee imported into Puerto Rico.

"SEC. 504. REVIEW AND REPORT TO CONGRESS. 19 USC 2464.

"The President shall submit an annual report to the Congress on the status of internationally recognized worker rights within each beneficiary developing country. President.

"SEC. 505. DATE OF TERMINATION. 19 USC 2465.

"No duty-free treatment provided under this title shall remain in effect after May 31, 1997.

"SEC. 506. AGRICULTURAL EXPORTS OF BENEFICIARY DEVELOPING COUNTRIES. 19 USC 2466.

"The appropriate agencies of the United States shall assist beneficiary developing countries to develop and implement meas-

ures designed to assure that the agricultural sectors of their economies are not directed to export markets to the detriment of the production of foodstuffs for their citizenry.

19 USC 2467.

"SEC. 507. DEFINITIONS.

"For purposes of this title:

"(1) BENEFICIARY DEVELOPING COUNTRY.—The term 'beneficiary developing country' means any country with respect to which there is in effect an Executive order or Presidential proclamation by the President designating such country as a beneficiary developing country for purposes of this title.

"(2) COUNTRY.—The term 'country' means any foreign country or territory, including any overseas dependent territory or possession of a foreign country, or the Trust Territory of the Pacific Islands. In the case of an association of countries which is a free trade area or customs union, or which is contributing to comprehensive regional economic integration among its members through appropriate means, including, but not limited to, the reduction of duties, the President may by Executive order or Presidential proclamation provide that all members of such association other than members which are barred from designation under section 502(b) shall be treated as one country for purposes of this title.

"(3) ENTERED.—The term 'entered' means entered, or withdrawn from warehouse for consumption, in the customs territory of the United States.

"(4) INTERNATIONALLY RECOGNIZED WORKER RIGHTS.—The term 'internationally recognized worker rights' includes—

"(A) the right of association;

"(B) the right to organize and bargain collectively;

"(C) a prohibition on the use of any form of forced or compulsory labor;

"(D) a minimum age for the employment of children; and

"(E) acceptable conditions of work with respect to minimum wages, hours of work, and occupational safety and health.

"(5) LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRY.—The term 'least-developed beneficiary developing country' means a beneficiary developing country that is designated as a least-developed beneficiary developing country under section 502(a)(2).".

(b) TABLE OF CONTENTS.—The items relating to title V in the table of contents of the Trade Act of 1974 are amended to read as follows:

"TITLE V—GENERALIZED SYSTEM OF PREFERENCES

19 USC 2461 note.

SEC. 1953. EFFECTIVE DATE.

(a) IN GENERAL.—The amendments made by this subtitle apply to articles entered on or after October 1, 1996.

(b) RETROACTIVE APPLICATION.—

(1) GENERAL RULE.—Notwithstanding section 514 of the Tariff Act of 1930 or any other provision of law and subject to subsection (c)—

(A) any article that was entered—

(i) after July 31, 1995, and

(ii) before January 1, 1996, and

to which duty-free treatment under title V of the Trade Act of 1974 would have applied if the entry had been made on July 31, 1995, shall be liquidated or reliquidated as free of duty, and the Secretary of the Treasury shall refund any duty paid with respect to such entry, and

(B) any article that was entered—

(i) after December 31, 1995, and

(ii) before October 1, 1996, and

to which duty-free treatment under title V of the Trade Act of 1974 (as amended by this subtitle) would have applied if the entry had been made on or after October 1, 1996, shall be liquidated or reliquidated as free of duty, and the Secretary of the Treasury shall refund any duty paid with respect to such entry.

(2) LIMITATION ON REFUNDS.—No refund shall be made pursuant to this subsection before October 1, 1996.

(3) ENTRY.—As used in this subsection, the term "entry" includes a withdrawal from warehouse for consumption.

(c) REQUESTS.—Liquidation or reliquidation may be made under subsection (b) with respect to an entry only if a request therefor is filed with the Customs Service, within 180 days after the date of the enactment of this Act, that contains sufficient information to enable the Customs Service—

(1) to locate the entry; or

(2) to reconstruct the entry if it cannot be located.

SEC. 1954. CONFORMING AMENDMENTS.

(a) TRADE LAWS.—

(1) Section 1211(b) of the Omnibus Trade and Competitiveness Act of 1988 (19 U.S.C. 3011(b)) is amended—

(A) in paragraph (1), by striking "(19 U.S.C. 2463(a), 2464(c)(3))" and inserting "(as in effect on July 31, 1995)"; and

(B) in paragraph (2), by striking "(19 U.S.C. 2464(c)(1))" and inserting the following: "(as in effect on July 31, 1995)".

(2) Section 203(c)(7) of the Andean Trade Preference Act (19 U.S.C. 3202(c)(7)) is amended by striking "502(a)(4)" and inserting "507(4)".

(3) Section 212(b)(7) of the Caribbean Basin Economic Recovery Act (19 U.S.C. 2702(b)(7)) is amended by striking "502(a)(4)" and inserting "507(4)".

(4) General note 3(a)(iv)(C) of the Harmonized Tariff Schedule of the United States is amended by striking "sections 503(b) and 504(c)" and inserting "subsections (a), (c), and (d) of section 503".

(5) Section 201(a)(2) of the North American Free Trade Agreement Implementation Act (19 U.S.C. 3331(a)(2)) is amended by striking "502(a)(2) of the Trade Act of 1974 (19 U.S.C. 2462(a)(2))" and inserting "502(f)(2) of the Trade Act of 1974".

(6) Section 131 of the Uruguay Round Agreements Act (19 U.S.C. 3551) is amended in subsections (a) and (b)(1) by striking "502(a)(4)" and inserting "507(4)".

(b) OTHER LAWS.—

(1) Section 871(f)(2)(B) of the Internal Revenue Code of 1986 is amended by striking "within the meaning of section 502" and inserting "under title V".

(2) Section 2202(8) of the Export Enhancement Act of 1988 (15 U.S.C. 4711(8)) is amended by striking "502(a)(4)" and inserting "507(4)".

(3) Section 231A(a) of the Foreign Assistance Act of 1961 (22 U.S.C. 2191a(a)) is amended—

(A) in paragraph (1) by striking "502(a)(4) of the Trade Act of 1974 (19 U.S.C. 2462(a)(4))" and inserting "507(4) of the Trade Act of 1974";

(B) in paragraph (2) by striking "505(c) of the Trade Act of 1974 (19 U.S.C. 2465(c))" and inserting "504 of the Trade Act of 1974"; and

(C) in paragraph (4) by striking "502(a)(4)" and inserting "507(4)".

(4) Section 1621(a)(1) of the International Financial Institutions Act (22 U.S.C. 262p–4p(a)(1)) is amended by striking "502(a)(4)" and inserting "507(4)".

(5) Section 103B of the Agricultural Act of 1949 (7 U.S.C. 1444–2) is amended in subsections (a)(5)(F)(v) and (n)(1)(C) by striking "503(d) of the Trade Act of 1974 (19 U.S.C. 2463(d))" and inserting "503(b)(3) of the Trade Act of 1974".

Employee Commuting Flexibility Act of 1996.
29 USC 251 note.

SEC. 2101. SHORT TITLE.

This section and sections 2102 and 2103 may be cited as the "Employee Commuting Flexibility Act of 1996".

SEC. 2102. PROPER COMPENSATION FOR USE OF EMPLOYER VEHICLES.

Section 4(a) of the Portal-to-Portal Act of 1947 (29 U.S.C. 254(a)) is amended by adding at the end the following: "For purposes of this subsection, the use of an employer's vehicle for travel by an employee and activities performed by an employee which are incidental to the use of such vehicle for commuting shall not be considered part of the employee's principal activities if the use of such vehicle for travel is within the normal commuting area for the employer's business or establishment and the use of the employer's vehicle is subject to an agreement on the part of the employer and the employee or representative of such employee.".

29 USC 254 note.

SEC. 2103. EFFECTIVE DATE.

The amendment made by section 2101 shall take effect on the date of the enactment of this Act and shall apply in determining the application of section 4 of the Portal-to-Portal Act of 1947 to an employee in any civil action brought before such date of enactment but pending on such date.

Minimum Wage Increase Act of 1996.
29 USC 201 note.

SEC. 2104. MINIMUM WAGE INCREASE.

(a) SHORT TITLE.—This section may be cited as the "Minimum Wage Increase Act of 1996".

(b) AMENDMENT.—Paragraph (1) of section 6(a) of the Fair Labor Standards Act of 1938 (29 U.S.C. 206(a)) is amended to read as follows:

"(1) except as otherwise provided in this section, not less than $4.25 an hour during the period ending on September 30, 1996, not less than $4.75 an hour during the year beginning on October 1, 1996, and not less than $5.15 an hour beginning September 1, 1997;".

(c) CONFORMING AMENDMENT.—Section 6 of such Act (29 U.S.C. 206) is amended by striking subsection (c).

SEC. 2105. FAIR LABOR STANDARDS ACT AMENDMENTS.

(a) COMPUTER PROFESSIONALS.—Section 13(a) of the Fair Labor Standards Act of 1938 (29 U.S.C. 213(a)) is amended by striking the period at the end of paragraph (16) and inserting "; or" and by adding after that paragraph the following:

"(17) any employee who is a computer systems analyst, computer programmer, software engineer, or other similarly skilled worker, whose primary duty is—

"(A) the application of systems analysis techniques and procedures, including consulting with users, to determine hardware, software, or system functional specifications;

"(B) the design, development, documentation, analysis, creation, testing, or modification of computer systems or programs, including prototypes, based on and related to user or system design specifications;

"(C) the design, documentation, testing, creation, or modification of computer programs related to machine operating systems; or

"(D) a combination of duties described in subparagraphs (A), (B), and (C) the performance of which requires the same level of skills, and

who, in the case of an employee who is compensated on an hourly basis, is compensated at a rate of not less than $27.63 an hour.".

(b) TIP CREDIT.—The last sentence of section 3(m) of the Fair Labor Standards Act of 1938 (29 U.S.C. 203(m)) is amended by striking "previous sentence" and inserting "preceding 2 sentences" and by striking "(1)" and "(2)" and such section is amended by striking the next to last sentence and inserting the following: "In determining the wage an employer is required to pay a tipped employee, the amount paid such employee by the employee's employer shall be an amount equal to—

"(1) the cash wage paid such employee which for purposes of such determination shall be not less than the cash wage required to be paid such an employee on the date of the enactment of this paragraph; and

"(2) an additional amount on account of the tips received by such employee which amount is equal to the difference between the wage specified in paragraph (1) and the wage in effect under section 6(a)(1).

The additional amount on account of tips may not exceed the value of the tips actually received by an employee.".

(c) OPPORTUNITY WAGE.—Section 6 of the Fair Labor Standards Act of 1938 (29 U.S.C. 206) is amended by adding at the end the following:

"(g)(1) In lieu of the rate prescribed by subsection (a)(1), any employer may pay any employee of such employer, during the first 90 consecutive calendar days after such employee is initially

employed by such employer, a wage which is not less than $4.25 an hour.

"(2) No employer may take any action to displace employees (including partial displacements such as reduction in hours, wages, or employment benefits) for purposes of hiring individuals at the wage authorized in paragraph (1).

"(3) Any employer who violates this subsection shall be considered to have violated section 15(a)(3).

"(4) This subsection shall only apply to an employee who has not attained the age of 20 years.".

Approved August 20, 1996.

LEGISLATIVE HISTORY—H.R. 3448:

HOUSE REPORTS: Nos. 104–586 (Comm. on Ways and Means) and 104–737 (Comm. of Conference).
SENATE REPORTS: No. 104–281 (Comm. on Finance).
CONGRESSIONAL RECORD, Vol. 142 (1996):
May 22, considered and passed House.
July 8, 9, considered and passed Senate, amended.
Aug. 2, House and Senate agreed to conference report.
WEEKLY COMPILATION OF PRESIDENTIAL DOCUMENTS, Vol. 32 (1996):
Aug. 20, Presidential remarks and statement.

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104TH CONGRESS
2d Session

HOUSE OF REPRESENTATIVES

REPORT
104–586

SMALL BUSINESS JOB PROTECTION ACT OF 1996

REPORT

OF THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

ON

H.R. 3448

together with

SUPPLEMENTAL AND DISSENTING VIEWS

[Together with cost estimate of the Congressional Budget Office]

MAY 20, 1996.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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104TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
2d Session } { 104–586

SMALL BUSINESS JOB PROTECTION ACT OF 1996

MAY 20, 1996.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ARCHER, from the Committee on Ways and Means, submitted the following

REPORT

together with

SUPPLEMENTAL AND DISSENTING VIEWS

[To accompany H.R. 3448]

[Including cost estimate of the Congressional Budget Office]

The Committee on Ways and Means, to whom was referred the bill (H.R. 3448) to provide tax relief for small businesses, to protect jobs, to create opportunities, to increase the take home pay of workers, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Strike out all after the enacting clause and insert in lieu thereof the following:

SECTION 1. SHORT TITLE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Small Business Job Protection Act of 1996".

(b) TABLE OF CONTENTS.—

TITLE I—SMALL BUSINESS AND OTHER TAX PROVISIONS

SEC. 1101. AMENDMENT OF 1986 CODE.

Except as otherwise expressly provided, whenever in this title an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

SEC. 1102. UNDERPAYMENTS OF ESTIMATED TAX.

No addition to the tax shall be made under section 6654 or 6655 of the Internal Revenue Code of 1986 (relating to failure to pay estimated tax) with respect to any underpayment of an installment required to be paid before the date of the enactment of this Act to the extent such underpayment was created or increased by any provision of this title.

Subtitle A—Expensing; Etc.

SEC. 1111. INCREASE IN EXPENSE TREATMENT FOR SMALL BUSINESSES.

(a) GENERAL RULE.—Paragraph (1) of section 179(b) (relating to dollar limitation) is amended to read as follows:

"(1) DOLLAR LIMITATION.—The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed the following applicable amount:

"If the taxable year begins in:	The applicable amount is:
1996	$18,500
1997	19,000
1998	20,000
1999	21,000
2000	22,000
2001	23,000
2002	23,500
2003 or thereafter	25,000."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1995.

SEC. 1112. TREATMENT OF EMPLOYEE TIPS.

(a) EMPLOYEE CASH TIPS.—

(1) REPORTING REQUIREMENT NOT CONSIDERED.—Subparagraph (A) of section 45B(b)(1) (relating to excess employer social security tax) is amended by inserting "(without regard to whether such tips are reported under section 6053)" after "section 3121(q)".

(2) TAXES PAID.—Subsection (d) of section 13443 of the Revenue Reconciliation Act of 1993 is amended by inserting ", with respect to services performed before, on, or after such date" after "1993".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall take effect as if included in the amendments made by, and the provisions of, section 13443 of the Revenue Reconciliation Act of 1993.

(b) TIPS FOR EMPLOYEES DELIVERING FOOD OR BEVERAGES.—

(1) IN GENERAL.—Paragraph (2) of section 45B(b) is amended to read as follows:

"(2) ONLY TIPS RECEIVED FOR FOOD OR BEVERAGES TAKEN INTO ACCOUNT.—In applying paragraph (1), there shall be taken into account only tips received from customers in connection with the delivering or serving of food or beverages for consumption if the tipping of employees delivering or serving food or beverages by customers is customary."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to tips received for services performed after December 31, 1996.

SEC. 1113. TREATMENT OF STORAGE OF PRODUCT SAMPLES.

(a) IN GENERAL.—Paragraph (2) of section 280A(c) is amended by striking "inventory" and inserting "inventory or product samples".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1995.

SEC. 1114. TREATMENT OF CERTAIN CHARITABLE RISK POOLS.

(a) GENERAL RULE.—Section 501 (relating to exemption from tax on corporations, certain trusts, etc.) is amended by redesignating subsection (n) as subsection (o) and by inserting after subsection (m) the following new subsection:

"(n) CHARITABLE RISK POOLS.—

"(1) IN GENERAL.—For purposes of this title—

"(A) a qualified charitable risk pool shall be treated as an organization organized and operated exclusively for charitable purposes, and

"(B) subsection (m) shall not apply to a qualified charitable risk pool.

"(2) QUALIFIED CHARITABLE RISK POOL.—For purposes of this subsection, the term 'qualified charitable risk pool' means any organization—

"(A) which is organized and operated solely to pool insurable risks of its members (other than risks related to medical malpractice) and to provide information to its members with respect to loss control and risk management,

"(B) which is comprised solely of members that are organizations described in subsection (c)(3) and exempt from tax under subsection (a), and

"(C) which meets the organizational requirements of paragraph (3).

"(3) ORGANIZATIONAL REQUIREMENTS.—An organization (hereinafter in this subsection referred to as the 'risk pool') meets the organizational requirements of this paragraph if—

"(A) such risk pool is organized as a nonprofit organization under State law provisions authorizing risk pooling arrangements for charitable organizations,

"(B) such risk pool is exempt from any income tax imposed by the State (or will be so exempt after such pool qualifies as an organization exempt from tax under this title),

"(C) such risk pool has obtained at least $1,000,000 in startup capital from nonmember charitable organizations,

"(D) such risk pool is controlled by a board of directors elected by its members, and

"(E) the organizational documents of such risk pool require that—

"(i) each member of such pool shall at all times be an organization described in subsection (c)(3) and exempt from tax under subsection (a),

"(ii) any member which receives a final determination that it no longer qualifies as an organization described in subsection (c)(3) shall immediately notify the pool of such determination and the effective date of such determination, and

"(iii) each policy of insurance issued by the risk pool shall provide that such policy will not cover the insured with respect to events occurring after the date such final determination was issued to the insured.

An organization shall not cease to qualify as a qualified charitable risk pool solely by reason of the failure of any of its members to continue to be an organization described in subsection (c)(3) if, within a reasonable period of time after such pool is notified as required under subparagraph (C)(ii), such pool takes such action as may be reasonably necessary to remove such member from such pool.

"(4) OTHER DEFINITIONS.—For purposes of this subsection—

"(A) STARTUP CAPITAL.—The term 'startup capital' means any capital contributed to, and any program-related investments (within the meaning of section 4944(c)) made in, the risk pool before such pool commences operations.

"(B) NONMEMBER CHARITABLE ORGANIZATION.—The term 'nonmember charitable organization' means any organization which is described in subsection (c)(3) and exempt from tax under subsection (a) and which is not a member of the risk pool and does not benefit (directly or indirectly) from the insurance coverage provided by the pool to its members."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after the date of the enactment of this Act.

SEC. 1115. TREATMENT OF DUES PAID TO AGRICULTURAL OR HORTICULTURAL ORGANIZATIONS.

(a) GENERAL RULE.—Section 512 (defining unrelated business taxable income) is amended by adding at the end thereof the following new subsection:

"(d) TREATMENT OF DUES OF AGRICULTURAL OR HORTICULTURAL ORGANIZATIONS.—

"(1) IN GENERAL.—If—

"(A) an agricultural or horticultural organization described in section 501(c)(5) requires annual dues to be paid in order to be a member of such organization, and

"(B) the amount of such required annual dues does not exceed $100,

in no event shall any portion of such dues be treated as derived by such organization from an unrelated trade or business by reason of any benefits or privileges to which members of such organization are entitled.

"(2) INDEXATION OF $100 AMOUNT.—In the case of any taxable year beginning in a calendar year after 1995, the $100 amount in paragraph (1) shall be increased by an amount equal to—

"(A) $100, multiplied by

"(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting 'calendar year 1994' for 'calendar year 1992' in subparagraph (B) thereof.

"(3) DUES.—For purposes of this subsection, the term 'dues' includes any payment required to be made in order to be recognized by the organization as a member of the organization."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1994.

SEC. 1116. CLARIFICATION OF EMPLOYMENT TAX STATUS OF CERTAIN FISHERMEN; INFORMATION REPORTING.

(a) CLARIFICATION OF EMPLOYMENT TAX STATUS.—

(1) AMENDMENTS OF INTERNAL REVENUE CODE OF 1986.—

(A) DETERMINATION OF SIZE OF CREW.—Subsection (b) of section 3121 (defining employment) is amended by adding at the end thereof the following new sentence:

"For purposes of paragraph (20), the operating crew of a boat shall be treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals."

(B) CERTAIN CASH REMUNERATION PERMITTED.—Subparagraph (A) of section 3121(b)(20) is amended to read as follows:

"(A) such individual does not receive any cash remuneration other than as provided in subparagraph (B) and other than cash remuneration—

"(i) which does not exceed $100 per trip;

"(ii) which is contingent on a minimum catch; and

"(iii) which is paid solely for additional duties (such as mate, engineer, or cook) for which additional cash remuneration is traditional in the industry,".

(C) CONFORMING AMENDMENT.—Section 6050A(a) is amended by striking "and" at the end of paragraph (3), by striking the period at the end of paragraph (4) and inserting "; and", and by adding at the end thereof the following new paragraph:

"(5) any cash remuneration described in section 3121(b)(20)(A)."

(2) AMENDMENT OF SOCIAL SECURITY ACT.—

(A) DETERMINATION OF SIZE OF CREW.—Subsection (a) of section 210 of the Social Security Act is amended by adding at the end thereof the following new sentence:

"For purposes of paragraph (20), the operating crew of a boat shall be treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals."

(B) CERTAIN CASH REMUNERATION PERMITTED.—Subparagraph (A) of section 210(a)(20) of such Act is amended to read as follows:

"(A) such individual does not receive any additional compensation other than as provided in subparagraph (B) and other than cash remuneration—

"(i) which does not exceed $100 per trip;

"(ii) which is contingent on a minimum catch; and

"(iii) which is paid solely for additional duties (such as mate, engineer, or cook) for which additional cash remuneration is traditional in the industry,".

(3) EFFECTIVE DATE.—

(A) IN GENERAL.—The amendments made by this subsection shall apply to remuneration paid after December 31, 1996.

(B) SPECIAL RULE.—The amendments made by this subsection (other than paragraph (1)(C)) shall also apply to remuneration paid after December 31, 1984, and before January 1, 1997, unless the payor treated such remunera-

tion (when paid) as being subject to tax under chapter 21 of the Internal Revenue Code of 1986.

(b) INFORMATION REPORTING.—

(1) IN GENERAL.—Subpart B of part III of subchapter A of chapter 68 (relating to information concerning transactions with other persons) is amended by adding at the end the following new section:

"SEC. 6050Q. RETURNS RELATING TO CERTAIN PURCHASES OF FISH.

"(a) REQUIREMENT OF REPORTING.—Every person—

"(1) who is engaged in the trade or business of purchasing fish for resale from any person engaged in the trade or business of catching fish; and

"(2) who makes payments in cash in the course of such trade or business to such a person of $600 or more during any calendar year for the purchase of fish,

shall make a return (at such times as the Secretary may prescribe) described in subsection (b) with respect to each person to whom such a payment was made during such calendar year.

"(b) RETURN.—A return is described in this subsection if such return—

"(1) is in such form as the Secretary may prescribe, and

"(2) contains—

"(A) the name, address, and TIN of each person to whom a payment described in subsection (a)(2) was made during the calendar year;

"(B) the aggregate amount of such payments made to such person during such calendar year and the date and amount of each such payment, and

"(C) such other information as the Secretary may require.

"(c) STATEMENT TO BE FURNISHED WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

"(1) the name and address of the person required to make such a return, and

"(2) the aggregate amount of payments to the person required to be shown on the return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) is required to be made.

"(d) DEFINITIONS.—For purposes of this section:

"(1) CASH.—The term 'cash' has the meaning given such term by section 6050I(d).

"(2) FISH.—The term 'fish' includes other forms of aquatic life.".

(2) TECHNICAL AMENDMENTS.—

(A) Subparagraph (A) of section 6724(d)(1) is amended by striking "or" at the end of clause (vi), by striking "and" at the end of clause (vii) and inserting "or", and by adding at the end the following new clause:

"(viii) section 6050Q (relating to returns relating to certain purchases of fish), and".

(B) Paragraph (2) of section 6724(d) is amended by redesignating subparagraphs (Q) through (T) as subparagraphs (R) through (U), respectively, and by inserting after subparagraph (P) the following new subparagraph:

"(Q) section 6050Q(c) (relating to returns relating to certain purchases of fish),".

(C) The table of sections for subpart B of part III of subchapter A of chapter 68 is amended by adding at the end the following new item:

"Sec. 6050Q. Returns relating to certain purchases of fish.".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to payments made after December 31, 1996.

Subtitle B—Extension of Certain Expiring Provisions

SEC. 1201. WORK OPPORTUNITY TAX CREDIT.

(a) AMOUNT OF CREDIT.—Subsection (a) of section 51 (relating to amount of credit) is amended by striking "40 percent" and inserting "35 percent".

(b) MEMBERS OF TARGETED GROUPS.—Subsection (d) of section 51 is amended to read as follows:

"(d) MEMBERS OF TARGETED GROUPS.—For purposes of this subpart—

"(1) IN GENERAL.—An individual is a member of a targeted group if such individual is—

"(A) a qualified IV–A recipient,

"(B) a qualified veteran,

"(C) a qualified ex-felon,

"(D) a high-risk youth,

"(E) a vocational rehabilitation referral, or

"(F) a qualified summer youth employee.

"(2) QUALIFIED IV–A RECIPIENT.—

"(A) IN GENERAL.—The term 'qualified IV–A recipient' means any individual who is certified by the designated local agency as being a member of a family receiving assistance under a IV–A program for at least a 9-month period ending during the 9-month period ending on the hiring date.

"(B) IV–A PROGRAM.—For purposes of this paragraph, the term 'IV–A program' means any program providing assistance under a State plan approved under part A of title IV of the Social Security Act (relating to assistance for needy families with minor children) and any successor of such program.

"(3) QUALIFIED VETERAN.—

"(A) IN GENERAL.—The term 'qualified veteran' means any veteran who is certified by the designated local agency as being—

"(i) a member of a family receiving assistance under a IV–A program (as defined in paragraph (2)(B)) for at least a 9-month period ending during the 12-month period ending on the hiring date, or

"(ii) a member of a family receiving assistance under a food stamp program under the Food Stamp Act of 1977 for at least a 3-month period ending during the 12-month period ending on the hiring date.

"(B) VETERAN.—For purposes of subparagraph (A), the term 'veteran' means any individual who is certified by the designated local agency as—

"(i)(I) having served on active duty (other than active duty for training) in the Armed Forces of the United States for a period of more than 180 days, or

"(II) having been discharged or released from active duty in the Armed Forces of the United States for a service-connected disability, and

"(ii) not having any day during the 60-day period ending on the hiring date which was a day of extended active duty in the Armed Forces of the United States.

For purposes of clause (ii), the term 'extended active duty' means a period of more than 90 days during which the individual was on active duty (other than active duty for training).

"(4) QUALIFIED EX-FELON.—The term 'qualified ex-felon' means any individual who is certified by the designated local agency—

"(A) as having been convicted of a felony under any statute of the United States or any State,

"(B) as having a hiring date which is not more than 1 year after the last date on which such individual was so convicted or was released from prison, and

"(C) as being a member of a family which had an income during the 6 months immediately preceding the earlier of the month in which such income determination occurs or the month in which the hiring date occurs, which, on an annual basis, would be 70 percent or less of the Bureau of Labor Statistics lower living standard.

Any determination under subparagraph (C) shall be valid for the 45-day period beginning on the date such determination is made.

"(5) HIGH-RISK YOUTH.—

"(A) IN GENERAL.—The term 'high-risk youth' means any individual who is certified by the designated local agency—

"(i) as having attained age 18 but not age 25 on the hiring date, and

"(ii) as having his principal place of abode within an empowerment zone or enterprise community.

"(B) YOUTH MUST CONTINUE TO RESIDE IN ZONE.—In the case of a high-risk youth, the term 'qualified wages' shall not include wages paid or incurred for services performed while such youth's principal place of abode is outside an empowerment zone or enterprise community.

"(6) VOCATIONAL REHABILITATION REFERRAL.—The term 'vocational rehabilitation referral' means any individual who is certified by the designated local agency as—

"(A) having a physical or mental disability which, for such individual, constitutes or results in a substantial handicap to employment, and

"(B) having been referred to the employer upon completion of (or while receiving) rehabilitative services pursuant to—

"(i) an individualized written rehabilitation plan under a State plan for vocational rehabilitation services approved under the Rehabilitation Act of 1973, or

"(ii) a program of vocational rehabilitation carried out under chapter 31 of title 38, United States Code.

"(7) QUALIFIED SUMMER YOUTH EMPLOYEE.—

"(A) IN GENERAL.—The term 'qualified summer youth employee' means any individual—

"(i) who performs services for the employer between May 1 and September 15,

"(ii) who is certified by the designated local agency as having attained age 16 but not 18 on the hiring date (or if later, on May 1 of the calendar year involved),

"(iii) who has not been an employee of the employer during any period prior to the 90-day period described in subparagraph (B)(i), and

"(iv) who is certified by the designated local agency as having his principal place of abode within an empowerment zone or enterprise community.

"(B) SPECIAL RULES FOR DETERMINING AMOUNT OF CREDIT.—For purposes of applying this subpart to wages paid or incurred to any qualified summer youth employee—

"(i) subsection (b)(2) shall be applied by substituting 'any 90-day period between May 1 and September 15' for 'the 1-year period beginning with the day the individual begins work for the employer', and

"(ii) subsection (b)(3) shall be applied by substituting '$3,000' for '$6,000'.

The preceding sentence shall not apply to an individual who, with respect to the same employer, is certified as a member of another targeted group after such individual has been a qualified summer youth employee.

"(C) YOUTH MUST CONTINUE TO RESIDE IN ZONE.—Paragraph (5)(B) shall apply for purposes of this paragraph.

"(8) HIRING DATE.—The term 'hiring date' means the day the individual is hired by the employer.

"(9) DESIGNATED LOCAL AGENCY.—The term 'designated local agency' means a State employment security agency established in accordance with the Act of June 6, 1933, as amended (29 U.S.C. 49-49n).

"(10) SPECIAL RULES FOR CERTIFICATIONS.—

"(A) IN GENERAL.—An individual shall not be treated as a member of a targeted group unless—

"(i) on or before the day on which such individual begins work for the employer, the employer has received a certification from a designated local agency that such individual is a member of a targeted group, or

"(ii)(I) on or before the day the individual is offered employment with the employer, a pre-screening notice is completed by the employer with respect to such individual, and

"(II) not later than the 14th day after the individual begins work for the employer, the employer submits such notice, signed by the employer and the individual under penalties of perjury, to the designated local agency as part of a written request for such a certification from such agency.

For purposes of this paragraph, the term 'pre-screening notice' means a document (in such form as the Secretary shall prescribe) which contains information provided by the individual on the basis of which the employer believes that the individual is a member of a targeted group.

"(B) INCORRECT CERTIFICATIONS.—If—

"(i) an individual has been certified by a designated local agency as a member of a targeted group, and

"(ii) such certification is incorrect because it was based on false information provided by such individual,

the certification shall be revoked and wages paid by the employer after the date on which notice of revocation is received by the employer shall not be treated as qualified wages.

"(C) EXPLANATION OF DENIAL OF REQUEST.—If a designated local agency denies a request for certification of membership in a targeted group, such

agency shall provide to the person making such request a written explanation of the reasons for such denial."

(c) MINIMUM EMPLOYMENT PERIOD.—Paragraph (3) of section 51(i) (relating to certain individuals ineligible) is amended to read as follows:

"(3) INDIVIDUALS NOT MEETING MINIMUM EMPLOYMENT PERIOD.—No wages shall be taken into account under subsection (a) with respect to any individual unless such individual either—

"(A) is employed by the employer at least 180 days (20 days in the case of a qualified summer youth employee), or

"(B) has completed at least 500 hours (120 hours in the case of a qualified summer youth employee) of services performed for the employer."

(d) TERMINATION.—Paragraph (4) of section 51(c) (relating to wages defined) is amended to read as follows:

"(4) TERMINATION.—The term 'wages' shall not include any amount paid or incurred to an individual who begins work for the employer—

"(A) after December 31, 1994, and before July 1, 1996, or

"(B) after June 30, 1997."

(e) REDESIGNATION OF CREDIT.—

(1) Sections 38(b)(2) and 51(a) are each amended by striking "targeted jobs credit" and inserting "work opportunity credit".

(2) The subpart heading for subpart F of part IV of subchapter A of chapter 1 is amended by striking "**Targeted Jobs Credit**" and inserting "**Work Opportunity Credit**".

(3) The table of subparts for such part IV is amended by striking "targeted jobs credit" and inserting "work opportunity credit".

(4) The heading for paragraph (3) of section 1396(c) is amended by striking "TARGETED JOBS CREDIT" and inserting "WORK OPPORTUNITY CREDIT".

(f) TECHNICAL AMENDMENT.—Paragraph (1) of section 51(c) is amended by striking ", subsection (d)(8)(D),".

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to individuals who begin work for the employer after June 30, 1996.

SEC. 1202. EMPLOYER-PROVIDED EDUCATIONAL ASSISTANCE PROGRAMS.

(a) EXTENSION.—Subsection (d) of section 127 (relating to educational assistance programs) is amended by striking "December 31, 1994" and inserting "December 31, 1996".

(b) LIMITATION TO EDUCATION BELOW GRADUATE LEVEL.—The last sentence of section 127(c)(1) is amended by inserting before the period "or at the graduate level".

(c) EFFECTIVE DATES.—

(1) EXTENSION.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1994.

(2) LIMITATION.—The amendment made by subsection (b) shall apply to taxable years beginning after December 31, 1995.

(3) EXPEDITED PROCEDURES.—The Secretary of the Treasury shall establish expedited procedures for the refund of any overpayment of taxes imposed by chapter 24 of the Internal Revenue Code of 1986 which is attributable to amounts excluded from gross income during 1995 or 1996 under section 127 of such Code, including procedures waiving the requirement that an employer obtain an employee's signature where the employer demonstrates to the satisfaction of the Secretary that any refund collected by the employer on behalf of the employee will be paid to the employee.

SEC. 1203. FUTA EXEMPTION FOR ALIEN AGRICULTURAL WORKERS.

(a) IN GENERAL.—Subparagraph (B) of section 3306(c)(1) (defining employment) is amended by striking "before January 1, 1995,".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to services performed after December 31, 1994.

Subtitle C—Provisions Relating to S Corporations

SEC. 1301. S CORPORATIONS PERMITTED TO HAVE 75 SHAREHOLDERS.

Subparagraph (A) of section 1361(b)(1) (defining small business corporation) is amended by striking "35 shareholders" and inserting "75 shareholders".

SEC. 1302. ELECTING SMALL BUSINESS TRUSTS.

(a) GENERAL RULE.—Subparagraph (A) of section 1361(c)(2) (relating to certain trusts permitted as shareholders) is amended by inserting after clause (iv) the following new clause:

"(v) An electing small business trust."

(b) CURRENT BENEFICIARIES TREATED AS SHAREHOLDERS.—Subparagraph (B) of section 1361(c)(2) is amended by adding at the end the following new clause:

"(v) In the case of a trust described in clause (v) of subparagraph (A), each potential current beneficiary of such trust shall be treated as a shareholder; except that, if for any period there is no potential current beneficiary of such trust, such trust shall be treated as the shareholder during such period."

(c) ELECTING SMALL BUSINESS TRUST DEFINED.—Section 1361 (defining S corporation) is amended by adding at the end the following new subsection:

"(e) ELECTING SMALL BUSINESS TRUST DEFINED.—

"(1) ELECTING SMALL BUSINESS TRUST.—For purposes of this section—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'electing small business trust' means any trust if—

"(i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, or (III) an organization described in paragraph (2), (3), (4), or (5) of section 170(c) which holds a contingent interest and is not a potential current beneficiary,

"(ii) no interest in such trust was acquired by purchase, and

"(iii) an election under this subsection applies to such trust.

"(B) CERTAIN TRUSTS NOT ELIGIBLE.—The term 'electing small business trust' shall not include—

"(i) any qualified subchapter S trust (as defined in subsection (d)(3)) if an election under subsection (d)(2) applies to any corporation the stock of which is held by such trust, and

"(ii) any trust exempt from tax under this subtitle.

"(C) PURCHASE.—For purposes of subparagraph (A), the term 'purchase' means any acquisition if the basis of the property acquired is determined under section 1012.

"(2) POTENTIAL CURRENT BENEFICIARY.—For purposes of this section, the term 'potential current beneficiary' means, with respect to any period, any person who at any time during such period is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust. If a trust disposes of all of the stock which it holds in an S corporation, then, with respect to such corporation, the term 'potential current beneficiary' does not include any person who first met the requirements of the preceding sentence during the 60-day period ending on the date of such disposition.

"(3) ELECTION.—An election under this subsection shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent taxable years of such trust unless revoked with the consent of the Secretary.

"(4) CROSS REFERENCE.—

"For special treatment of electing small business trusts, see section 641(d)."

(d) TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—Section 641 (relating to imposition of tax on trusts) is amended by adding at the end the following new subsection:

"(d) SPECIAL RULES FOR TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—

"(1) IN GENERAL.—For purposes of this chapter—

"(A) the portion of any electing small business trust which consists of stock in 1 or more S corporations shall be treated as a separate trust, and

"(B) the amount of the tax imposed by this chapter on such separate trust shall be determined with the modifications of paragraph (2).

"(2) MODIFICATIONS.—For purposes of paragraph (1), the modifications of this paragraph are the following:

"(A) Except as provided in section 1(h), the amount of the tax imposed by section 1(e) shall be determined by using the highest rate of tax set forth in section 1(e).

"(B) The exemption amount under section 55(d) shall be zero.

"(C) The only items of income, loss, deduction, or credit to be taken into account are the following:

"(i) The items required to be taken into account under section 1366.

"(ii) Any gain or loss from the disposition of stock in an S corporation.

"(iii) To the extent provided in regulations, State or local income taxes or administrative expenses to the extent allocable to items described in clauses (i) and (ii).

No deduction or credit shall be allowed for any amount not described in this paragraph, and no item described in this paragraph shall be apportioned to any beneficiary.

"(D) No amount shall be allowed under paragraph (1) or (2) of section 1211(b).

"(3) TREATMENT OF REMAINDER OF TRUST AND DISTRIBUTIONS.—For purposes of determining—

"(A) the amount of the tax imposed by this chapter on the portion of any electing small business trust not treated as a separate trust under paragraph (1), and

"(B) the distributable net income of the entire trust,

the items referred to in paragraph (2)(C) shall be excluded. Except as provided in the preceding sentence, this subsection shall not affect the taxation of any distribution from the trust.

"(4) TREATMENT OF UNUSED DEDUCTIONS WHERE TERMINATION OF SEPARATE TRUST.—If a portion of an electing small business trust ceases to be treated as a separate trust under paragraph (1), any carryover or excess deduction of the separate trust which is referred to in section 642(h) shall be taken into account by the entire trust.

"(5) ELECTING SMALL BUSINESS TRUST.—For purposes of this subsection, the term 'electing small business trust' has the meaning given such term by section 1361(e)(1)."

(e) TECHNICAL AMENDMENT.—Paragraph (1) of section 1366(a) is amended by inserting ", or of a trust or estate which terminates," after "who dies".

SEC. 1303. EXPANSION OF POST-DEATH QUALIFICATION FOR CERTAIN TRUSTS.

Subparagraph (A) of section 1361(c)(2) (relating to certain trusts permitted as shareholders) is amended—

(1) by striking "60-day period" each place it appears in clauses (ii) and (iii) and inserting "2-year period", and

(2) by striking the last sentence in clause (ii).

SEC. 1304. FINANCIAL INSTITUTIONS PERMITTED TO HOLD SAFE HARBOR DEBT.

Clause (iii) of section 1361(c)(5)(B) (defining straight debt) is amended by striking "or a trust described in paragraph (2)" and inserting "a trust described in paragraph (2), or a person which is actively and regularly engaged in the business of lending money".

SEC. 1305. RULES RELATING TO INADVERTENT TERMINATIONS AND INVALID ELECTIONS.

(a) GENERAL RULE.—Subsection (f) of section 1362 (relating to inadvertent terminations) is amended to read as follows:

"(f) INADVERTENT INVALID ELECTIONS OR TERMINATIONS.—If—

"(1) an election under subsection (a) by any corporation—

"(A) was not effective for the taxable year for which made (determined without regard to subsection (b)(2)) by reason of a failure to meet the requirements of section 1361(b) or to obtain shareholder consents, or

"(B) was terminated under paragraph (2) or (3) of subsection (d),

"(2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent,

"(3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken—

"(A) so that the corporation is a small business corporation, or

"(B) to acquire the required shareholder consents, and

"(4) the corporation, and each person who was a shareholder in the corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period,

then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary."

(b) LATE ELECTIONS, ETC.—Subsection (b) of section 1362 is amended by adding at the end the following new paragraph:

"(5) AUTHORITY TO TREAT LATE ELECTIONS, ETC., AS TIMELY.—If—

"(A) an election under subsection (a) is made for any taxable year (determined without regard to paragraph (3)) after the date prescribed by this

subsection for making such election for such taxable year or no such election is made for any taxable year, and

"(B) the Secretary determines that there was reasonable cause for the failure to timely make such election,

the Secretary may treat such an election as timely made for such taxable year (and paragraph (3) shall not apply)."

(c) EFFECTIVE DATE.—The amendments made by subsection (a) and (b) shall apply with respect to elections for taxable years beginning after December 31, 1982.

SEC. 1306. AGREEMENT TO TERMINATE YEAR.

Paragraph (2) of section 1377(a) (relating to pro rata share) is amended to read as follows:

"(2) ELECTION TO TERMINATE YEAR.—

"(A) IN GENERAL.—Under regulations prescribed by the Secretary, if any shareholder terminates the shareholder's interest in the corporation during the taxable year and all affected shareholders and the corporation agree to the application of this paragraph, paragraph (1) shall be applied to the affected shareholders as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination.

"(B) AFFECTED SHAREHOLDERS.—For purposes of subparagraph (A), the term 'affected shareholders' means the shareholder whose interest is terminated and all shareholders to whom such shareholder has transferred shares during the taxable year. If such shareholder has transferred shares to the corporation, the term 'affected shareholders' shall include all persons who are shareholders during the taxable year."

SEC. 1307. EXPANSION OF POST-TERMINATION TRANSITION PERIOD.

(a) IN GENERAL.—Paragraph (1) of section 1377(b) (relating to post-termination transition period) is amended by striking "and" at the end of subparagraph (A), by redesignating subparagraph (B) as subparagraph (C), and by inserting after subparagraph (A) the following new subparagraph:

"(B) the 120-day period beginning on the date of any determination pursuant to an audit of the taxpayer which follows the termination of the corporation's election and which adjusts a subchapter S item of income, loss, or deduction of the corporation arising during the S period (as defined in section 1368(e)(2)), and".

(b) DETERMINATION DEFINED.—Paragraph (2) of section 1377(b) is amended by striking subparagraphs (A) and (B), by redesignating subparagraph (C) as subparagraph (B), and by inserting before subparagraph (B) (as so redesignated) the following new subparagraph:

"(A) a determination as defined in section 1313(a), or".

(c) REPEAL OF SPECIAL AUDIT PROVISIONS FOR SUBCHAPTER S ITEMS.—

(1) GENERAL RULE.—Subchapter D of chapter 63 (relating to tax treatment of subchapter S items) is hereby repealed.

(2) CONSISTENT TREATMENT REQUIRED.—Section 6037 (relating to return of S corporation) is amended by adding at the end the following new subsection:

"(c) SHAREHOLDER'S RETURN MUST BE CONSISTENT WITH CORPORATE RETURN OR SECRETARY NOTIFIED OF INCONSISTENCY.—

"(1) IN GENERAL.—A shareholder of an S corporation shall, on such shareholder's return, treat a subchapter S item in a manner which is consistent with the treatment of such item on the corporate return.

"(2) NOTIFICATION OF INCONSISTENT TREATMENT.—

"(A) IN GENERAL.—In the case of any subchapter S item, if—

"(i)(I) the corporation has filed a return but the shareholder's treatment on his return is (or may be) inconsistent with the treatment of the item on the corporate return, or

"(II) the corporation has not filed a return, and

"(ii) the shareholder files with the Secretary a statement identifying the inconsistency,

paragraph (1) shall not apply to such item.

"(B) SHAREHOLDER RECEIVING INCORRECT INFORMATION.—A shareholder shall be treated as having complied with clause (ii) of subparagraph (A) with respect to a subchapter S item if the shareholder—

"(i) demonstrates to the satisfaction of the Secretary that the treatment of the subchapter S item on the shareholder's return is consistent with the treatment of the item on the schedule furnished to the shareholder by the corporation, and

"(ii) elects to have this paragraph apply with respect to that item.

"(3) EFFECT OF FAILURE TO NOTIFY.—In any case—

"(A) described in subparagraph (A)(i)(I) of paragraph (2), and

"(B) in which the shareholder does not comply with subparagraph (A)(ii) of paragraph (2),

any adjustment required to make the treatment of the items by such shareholder consistent with the treatment of the items on the corporate return shall be treated as arising out of mathematical or clerical errors and assessed according to section 6213(b)(1). Paragraph (2) of section 6213(b) shall not apply to any assessment referred to in the preceding sentence.

"(4) SUBCHAPTER S ITEM.—For purposes of this subsection, the term 'subchapter S item' means any item of an S corporation to the extent that regulations prescribed by the Secretary provide that, for purposes of this subtitle, such item is more appropriately determined at the corporation level than at the shareholder level.

"(5) ADDITION TO TAX FOR FAILURE TO COMPLY WITH SECTION.—

"For addition to tax in the case of a shareholder's negligence in connection with, or disregard of, the requirements of this section, see part II of subchapter A of chapter 68."

(3) CONFORMING AMENDMENTS.—

(A) Section 1366 is amended by striking subsection (g).

(B) Subsection (b) of section 6233 is amended to read as follows:

"(b) SIMILAR RULES IN CERTAIN CASES.—If a partnership return is filed for any taxable year but it is determined that there is no entity for such taxable year, to the extent provided in regulations, rules similar to the rules of subsection (a) shall apply."

(C) The table of subchapters for chapter 63 is amended by striking the item relating to subchapter D.

SEC. 1308. S CORPORATIONS PERMITTED TO HOLD SUBSIDIARIES.

(a) IN GENERAL.—Paragraph (2) of section 1361(b) (defining ineligible corporation) is amended by striking subparagraph (A) and by redesignating subparagraphs (B), (C), (D), and (E) as subparagraphs (A), (B), (C), and (D), respectively.

(b) TREATMENT OF CERTAIN WHOLLY OWNED S CORPORATION SUBSIDIARIES.—Section 1361(b) (defining small business corporation) is amended by adding at the end the following new paragraph:

"(3) TREATMENT OF CERTAIN WHOLLY OWNED SUBSIDIARIES.—

"(A) IN GENERAL.—For purposes of this title—

"(i) a corporation which is a qualified subchapter S subsidiary shall not be treated as a separate corporation, and

"(ii) all assets, liabilities, and items of income, deduction, and credit of a qualified subchapter S subsidiary shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

"(B) QUALIFIED SUBCHAPTER S SUBSIDIARY.—For purposes of this paragraph, the term 'qualified subchapter S subsidiary' means any domestic corporation which is not an ineligible corporation (as defined in paragraph (2)), if—

"(i) 100 percent of the stock of such corporation is held by the S corporation, and

"(ii) the S corporation elects to treat such corporation as a qualified subchapter S subsidiary.

"(C) TREATMENT OF TERMINATIONS OF QUALIFIED SUBCHAPTER S SUBSIDIARY STATUS.—For purposes of this title, if any corporation which was a qualified subchapter S subsidiary ceases to meet the requirements of subparagraph (B), such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the S corporation in exchange for its stock."

(c) CERTAIN DIVIDENDS NOT TREATED AS PASSIVE INVESTMENT INCOME.—Paragraph (3) of section 1362(d) is amended by adding at the end the following new subparagraph:

"(F) TREATMENT OF CERTAIN DIVIDENDS.—If an S corporation holds stock in a C corporation meeting the requirements of section 1504(a)(2), the term 'passive investment income' shall not include dividends from such C corporation to the extent such dividends are attributable to the earnings and profits of such C corporation derived from the active conduct of a trade or business."

(d) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 1361 is amended by striking paragraph (6).

(2) Subsection (b) of section 1504 (defining includible corporation) is amended by adding at the end the following new paragraph:

"(8) An S corporation."

SEC. 1309. TREATMENT OF DISTRIBUTIONS DURING LOSS YEARS.

(a) ADJUSTMENTS FOR DISTRIBUTIONS TAKEN INTO ACCOUNT BEFORE LOSSES.—

(1) Subparagraph (A) of section 1366(d)(1) (relating to losses and deductions cannot exceed shareholder's basis in stock and debt) is amended by striking "paragraph (1)" and inserting "paragraphs (1) and (2)(A)".

(2) Subsection (d) of section 1368 (relating to certain adjustments taken into account) is amended by adding at the end the following new sentence:

"In the case of any distribution made during any taxable year, the adjusted basis of the stock shall be determined with regard to the adjustments provided in paragraph (1) of section 1367(a) for the taxable year."

(b) ACCUMULATED ADJUSTMENTS ACCOUNT.—Paragraph (1) of section 1368(e) (relating to accumulated adjustments account) is amended by adding at the end the following new subparagraph:

"(C) NET LOSS FOR YEAR DISREGARDED.—

"(i) IN GENERAL.—In applying this section to distributions made during any taxable year, the amount in the accumulated adjustments account as of the close of such taxable year shall be determined without regard to any net negative adjustment for such taxable year.

"(ii) NET NEGATIVE ADJUSTMENT.—For purposes of clause (i), the term 'net negative adjustment' means, with respect to any taxable year, the excess (if any) of—

"(I) the reductions in the account for the taxable year (other than for distributions), over

"(II) the increases in such account for such taxable year."

(c) CONFORMING AMENDMENTS.—Subparagraph (A) of section 1368(e)(1) is amended—

(1) by striking "as provided in subparagraph (B)" and inserting "as otherwise provided in this paragraph", and

(2) by striking "section 1367(b)(2)(A)" and inserting "section 1367(a)(2)".

SEC. 1310. TREATMENT OF S CORPORATIONS UNDER SUBCHAPTER C.

Subsection (a) of section 1371 (relating to application of subchapter C rules) is amended to read as follows:

"(a) APPLICATION OF SUBCHAPTER C RULES.—Except as otherwise provided in this title, and except to the extent inconsistent with this subchapter, subchapter C shall apply to an S corporation and its shareholders."

SEC. 1311. ELIMINATION OF CERTAIN EARNINGS AND PROFITS.

(a) IN GENERAL.—If—

(1) a corporation was an electing small business corporation under subchapter S of chapter 1 of the Internal Revenue Code of 1986 for any taxable year beginning before January 1, 1983, and

(2) such corporation is an S corporation under subchapter S of chapter 1 of such Code for its first taxable year beginning after December 31, 1996,

the amount of such corporation's accumulated earnings and profits (as of the beginning of such first taxable year) shall be reduced by an amount equal to the portion (if any) of such accumulated earnings and profits which were accumulated in any taxable year beginning before January 1, 1983, for which such corporation was an electing small business corporation under such subchapter S.

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (3) of section 1362(d), as amended by section 1308, is amended—

(A) by striking "SUBCHAPTER C" in the paragraph heading and inserting "ACCUMULATED",

(B) by striking "subchapter C" in subparagraph (A)(i)(I) and inserting "accumulated", and

(C) by striking subparagraph (B) and redesignating the following subparagraphs accordingly.

(2)(A) Subsection (a) of section 1375 is amended by striking "subchapter C" in paragraph (1) and inserting "accumulated".

(B) Paragraph (3) of section 1375(b) is amended to read as follows:

"(3) PASSIVE INVESTMENT INCOME, ETC.—The terms 'passive investment income' and 'gross receipts' have the same respective meanings as when used in paragraph (3) of section 1362(d)."

(C) The section heading for section 1375 is amended by striking "subchapter c" and inserting "accumulated".

(D) The table of sections for part III of subchapter S of chapter 1 is amended by striking "subchapter C" in the item relating to section 1375 and inserting "accumulated".

(3) Clause (i) of section 1042(c)(4)(A) is amended by striking "section 1362(d)(3)(D)" and inserting "section 1362(d)(3)(C)".

SEC. 1312. CARRYOVER OF DISALLOWED LOSSES AND DEDUCTIONS UNDER AT-RISK RULES ALLOWED.

Paragraph (3) of section 1366(d) (relating to carryover of disallowed losses and deductions to post-termination transition period) is amended by adding at the end the following new subparagraph:

"(D) AT-RISK LIMITATIONS.—To the extent that any increase in adjusted basis described in subparagraph (B) would have increased the shareholder's amount at risk under section 465 if such increase had occurred on the day preceding the commencement of the post-termination transition period, rules similar to the rules described in subparagraphs (A) through (C) shall apply to any losses disallowed by reason of section 465(a)."

SEC. 1313. ADJUSTMENTS TO BASIS OF INHERITED S STOCK TO REFLECT CERTAIN ITEMS OF INCOME.

(a) IN GENERAL.—Subsection (b) of section 1367 (relating to adjustments to basis of stock of shareholders, etc.) is amended by adding at the end the following new paragraph:

"(4) ADJUSTMENTS IN CASE OF INHERITED STOCK.—

"(A) IN GENERAL.—If any person acquires stock in an S corporation by reason of the death of a decedent or by bequest, devise, or inheritance, section 691 shall be applied with respect to any item of income of the S corporation in the same manner as if the decedent had held directly his pro rata share of such item.

"(B) ADJUSTMENTS TO BASIS.—The basis determined under section 1014 of any stock in an S corporation shall be reduced by the portion of the value of the stock which is attributable to items constituting income in respect of the decedent."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply in the case of decedents dying after the date of the enactment of this Act.

SEC. 1314. S CORPORATIONS ELIGIBLE FOR RULES APPLICABLE TO REAL PROPERTY SUBDIVIDED FOR SALE BY NONCORPORATE TAXPAYERS.

(a) IN GENERAL.—Subsection (a) of section 1237 (relating to real property subdivided for sale) is amended by striking "other than a corporation" in the material preceding paragraph (1) and inserting "other than a C corporation".

(b) CONFORMING AMENDMENT.—Subparagraph (A) of section 1237(a)(2) is amended by inserting "an S corporation which included the taxpayer as a shareholder," after "controlled by the taxpayer,".

SEC. 1315. EFFECTIVE DATE.

(a) IN GENERAL.—Except as otherwise provided in this subtitle, the amendments made by this subtitle shall apply to taxable years beginning after December 31, 1996.

(b) TREATMENT OF CERTAIN ELECTIONS UNDER PRIOR LAW.—For purposes of section 1362(g) of the Internal Revenue Code of 1986 (relating to election after termination), any termination under section 1362(d) of such Code in a taxable year beginning before January 1, 1997, shall not be taken into account.

Subtitle D—Pension Simplification

CHAPTER 1—SIMPLIFIED DISTRIBUTION RULES

SEC. 1401. REPEAL OF 5-YEAR INCOME AVERAGING FOR LUMP-SUM DISTRIBUTIONS.

(a) IN GENERAL.—Subsection (d) of section 402 (relating to taxability of beneficiary of employees' trust) is amended to read as follows:

"(d) TAXABILITY OF BENEFICIARY OF CERTAIN FOREIGN SITUS TRUSTS.—For purposes of subsections (a), (b), and (c), a stock bonus, pension, or profit-sharing trust which would qualify for exemption from tax under section 501(a) except for the fact that it is a trust created or organized outside the United States shall be treated as if it were a trust exempt from tax under section 501(a)."

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (D) of section 402(e)(4) (relating to other rules applicable to exempt trusts) is amended to read as follows:

"(D) LUMP-SUM DISTRIBUTION.—For purposes of this paragraph—

"(i) IN GENERAL.—The term 'lump sum distribution' means the distribution or payment within one taxable year of the recipient of the bal-

ance to the credit of an employee which becomes payable to the recipient—

"(I) on account of the employee's death,

"(II) after the employee attains age 59½,

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

"(IV) after the employee has become disabled (within the meaning of section 72(m)(7)),

from a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501 or from a plan described in section 403(a). Subclause (III) of this clause shall be applied only with respect to an individual who is an employee without regard to section 401(c)(1), and subclause (IV) shall be applied only with respect to an employee within the meaning of section 401(c)(1). For purposes of this clause, a distribution to two or more trusts shall be treated as a distribution to one recipient. For purposes of this paragraph, the balance to the credit of the employee does not include the accumulated deductible employee contributions under the plan (within the meaning of section 72(o)(5)).

"(ii) AGGREGATION OF CERTAIN TRUSTS AND PLANS.—For purposes of determining the balance to the credit of an employee under clause (i)—

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

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

"(iii) COMMUNITY PROPERTY LAWS.—The provisions of this paragraph shall be applied without regard to community property laws.

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

"(v) BALANCE TO CREDIT OF EMPLOYEE NOT TO INCLUDE AMOUNTS PAYABLE UNDER QUALIFIED DOMESTIC RELATIONS ORDER.—For purposes of this paragraph, the balance to the credit of an employee shall not include any amount payable to an alternate payee under a qualified domestic relations order (within the meaning of section 414(p)).

"(vi) TRANSFERS TO COST-OF-LIVING ARRANGEMENT NOT TREATED AS DISTRIBUTION.—For purposes of this paragraph, the balance to the credit of an employee under a defined contribution plan shall not include any amount transferred from such defined contribution plan to a qualified cost-of-living arrangement (within the meaning of section 415(k)(2)) under a defined benefit plan.

"(vii) LUMP-SUM DISTRIBUTIONS OF ALTERNATE PAYEES.—If any distribution or payment of the balance to the credit of an employee would be treated as a lump-sum distribution, then, for purposes of this paragraph, the payment under a qualified domestic relations order (within the meaning of section 414(p)) of the balance to the credit of an alternate payee who is the spouse or former spouse of the employee shall be treated as a lump-sum distribution. For purposes of this clause, the balance to the credit of the alternate payee shall not include any amount payable to the employee."

(2) Section 402(c) (relating to rules applicable to rollovers from exempt trusts) is amended by striking paragraph (10).

(3) Paragraph (1) of section 55(c) (defining regular tax) is amended by striking "shall not include any tax imposed by section 402(d) and".

(4) Paragraph (8) of section 62(a) (relating to certain portion of lump-sum distributions from pension plans taxed under section 402(d)) is hereby repealed.

(5) Section 401(a)(28)(B) (relating to coordination with distribution rules) is amended by striking clause (v).

(6) Subparagraph (B)(ii) of section 401(k)(10) (relating to distributions that must be lump-sum distributions) is amended to read as follows:

"(ii) LUMP-SUM DISTRIBUTION.—For purposes of this subparagraph, the term 'lump-sum distribution' has the meaning given such term by section 402(e)(4)(D) (without regard to subclauses (I), (II), (III), and (IV) of clause (i) thereof)."

(7) Section 406(c) (relating to termination of status as deemed employee not to be treated as separation from service for purposes of limitation of tax) is hereby repealed.

(8) Section 407(c) (relating to termination of status as deemed employee not to be treated as separation from service for purposes of limitation of tax) is hereby repealed.

(9) Section 691(c) (relating to deduction for estate tax) is amended by striking paragraph (5).

(10) Paragraph (1) of section 871(b) (relating to imposition of tax) is amended by striking "section 1, 55, or 402(d)(1)" and inserting "section 1 or 55".

(11) Subsection (b) of section 877 (relating to alternative tax) is amended by striking "section 1, 55, or 402(d)(1)" and inserting "section 1 or 55".

(12) Section 4980A(c)(4) is amended—

(A) by striking "to which an election under section 402(d)(4)(B) applies" and inserting "(as defined in section 402(e)(4)(D)) with respect to which the individual elects to have this paragraph apply",

(B) by adding at the end the following new flush sentence:

"An individual may elect to have this paragraph apply to only one lump-sum distribution.", and

(C) by striking the heading and inserting:

"(4) SPECIAL ONE-TIME ELECTION.—".

(13) Section 402(e) is amended by striking paragraph (5).

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1998.

(2) RETENTION OF CERTAIN TRANSITION RULES.—Notwithstanding any other provision of this section, the amendments made by this section shall not apply to any distribution for which the taxpayer elects the benefits of section 1122 (h)(3) or (h)(5) of the Tax Reform Act of 1986. For purposes of the preceding sentence, the rules of sections 402(c)(10) and 402(d) of the Internal Revenue Code of 1986 (as in effect before the amendments made by this Act) shall apply.

SEC. 1402. REPEAL OF $5,000 EXCLUSION OF EMPLOYEES' DEATH BENEFITS.

(a) IN GENERAL.—Subsection (b) of section 101 is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 101 is amended by striking "subsection (a) or (b)" and inserting "subsection (a)".

(2) Sections 406(e) and 407(e) are each amended by striking paragraph (2) and by redesignating paragraph (3) as paragraph (2).

(3) Section 7701(a)(20) is amended by striking ", for the purpose of applying the provisions of section 101(b) with respect to employees' death benefits".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to decedents dying after the date of the enactment of this Act.

SEC. 1403. SIMPLIFIED METHOD FOR TAXING ANNUITY DISTRIBUTIONS UNDER CERTAIN EMPLOYER PLANS.

(a) GENERAL RULE.—Subsection (d) of section 72 (relating to annuities; certain proceeds of endowment and life insurance contracts) is amended to read as follows:

"(d) SPECIAL RULES FOR QUALIFIED EMPLOYER RETIREMENT PLANS.—

"(1) SIMPLIFIED METHOD OF TAXING ANNUITY PAYMENTS.—

"(A) IN GENERAL.—In the case of any amount received as an annuity under a qualified employer retirement plan—

"(i) subsection (b) shall not apply, and

"(ii) the investment in the contract shall be recovered as provided in this paragraph.

"(B) METHOD OF RECOVERING INVESTMENT IN CONTRACT.—

"(i) IN GENERAL.—Gross income shall not include so much of any monthly annuity payment under a qualified employer retirement plan as does not exceed the amount obtained by dividing—

"(I) the investment in the contract (as of the annuity starting date), by

"(II) the number of anticipated payments determined under the table contained in clause (iii) (or, in the case of a contract to which subsection (c)(3)(B) applies, the number of monthly annuity payments under such contract).

"(ii) CERTAIN RULES MADE APPLICABLE.—Rules similar to the rules of paragraphs (2) and (3) of subsection (b) shall apply for purposes of this paragraph.

"(iii) NUMBER OF ANTICIPATED PAYMENTS.—

"If the age of the primary annuitant on the annuity starting date is:	The number of anticipated payments is:
Not more than 55	360
More than 55 but not more than 60	310
More than 60 but not more than 65	260
More than 65 but not more than 70	210
More than 70	160.

"(C) ADJUSTMENT FOR REFUND FEATURE NOT APPLICABLE.—For purposes of this paragraph, investment in the contract shall be determined under subsection (c)(1) without regard to subsection (c)(2).

"(D) SPECIAL RULE WHERE LUMP SUM PAID IN CONNECTION WITH COMMENCEMENT OF ANNUITY PAYMENTS.—If, in connection with the commencement of annuity payments under any qualified employer retirement plan, the taxpayer receives a lump sum payment—

"(i) such payment shall be taxable under subsection (e) as if received before the annuity starting date, and

"(ii) the investment in the contract for purposes of this paragraph shall be determined as if such payment had been so received.

"(E) EXCEPTION.—This paragraph shall not apply in any case where the primary annuitant has attained age 75 on the annuity starting date unless there are fewer than 5 years of guaranteed payments under the annuity.

"(F) ADJUSTMENT WHERE ANNUITY PAYMENTS NOT ON MONTHLY BASIS.—In any case where the annuity payments are not made on a monthly basis, appropriate adjustments in the application of this paragraph shall be made to take into account the period on the basis of which such payments are made.

"(G) QUALIFIED EMPLOYER RETIREMENT PLAN.—For purposes of this paragraph, the term 'qualified employer retirement plan' means any plan or contract described in paragraph (1), (2), or (3) of section 4974(c).

"(2) TREATMENT OF EMPLOYEE CONTRIBUTIONS UNDER DEFINED CONTRIBUTION PLANS.—For purposes of this section, employee contributions (and any income allocable thereto) under a defined contribution plan may be treated as a separate contract."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in cases where the annuity starting date is after the 90th day after the date of the enactment of this Act.

SEC. 1404. REQUIRED DISTRIBUTIONS.

(a) IN GENERAL.—Section 401(a)(9)(C) (defining required beginning date) is amended to read as follows:

"(C) REQUIRED BEGINNING DATE.—For purposes of this paragraph—

"(i) IN GENERAL.—The term 'required beginning date' means April 1 of the calendar year following the later of—

"(I) the calendar year in which the employee attains age 70½, or

"(II) the calendar year in which the employee retires.

"(ii) EXCEPTION.—Subclause (II) of clause (i) shall not apply—

"(I) except as provided in section 409(d), in the case of an employee who is a 5-percent owner (as defined in section 416) with respect to the plan year ending in the calendar year in which the employee attains age 70½, or

"(II) for purposes of section 408 (a)(6) or (b)(3).

"(iii) ACTUARIAL ADJUSTMENT.—In the case of an employee to whom clause (i)(II) applies who retires in a calendar year after the calendar year in which the employee attains age 70½, the employee's accrued benefit shall be actuarially increased to take into account the period after age 70½ in which the employee was not receiving any benefits under the plan.

"(iv) EXCEPTION FOR GOVERNMENTAL AND CHURCH PLANS.—Clauses (ii) and (iii) shall not apply in the case of a governmental plan or church plan. For purposes of this clause, the term 'church plan' means a plan maintained by a church for church employees, and the term 'church' means any church (as defined in section 3121(w)(3)(A)) or qualified church-controlled organization (as defined in section 3121(w)(3)(B))."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to years beginning after December 31, 1996.

CHAPTER 2—INCREASED ACCESS TO PENSION PLANS

Subchapter A—Simple Savings Plans

SEC. 1421. ESTABLISHMENT OF SAVINGS INCENTIVE MATCH PLANS FOR EMPLOYEES OF SMALL EMPLOYERS.

(a) IN GENERAL.—Section 408 (relating to individual retirement accounts) is amended by redesignating subsection (p) as subsection (q) and by inserting after subsection (o) the following new subsection:

"(p) SIMPLE RETIREMENT ACCOUNTS.—

"(1) IN GENERAL.—For purposes of this title, the term 'simple retirement account' means an individual retirement plan (as defined in section 7701(a)(37))—

"(A) with respect to which the requirements of paragraphs (3), (4), and (5) are met; and

"(B) with respect to which the only contributions allowed are contributions under a qualified salary reduction arrangement.

"(2) QUALIFIED SALARY REDUCTION ARRANGEMENT.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'qualified salary reduction arrangement' means a written arrangement of an eligible employer under which—

"(i) an employee eligible to participate in the arrangement may elect to have the employer make payments—

"(I) as elective employer contributions to a simple retirement account on behalf of the employee, or

"(II) to the employee directly in cash,

"(ii) the amount which an employee may elect under clause (i) for any year is required to be expressed as a percentage of compensation and may not exceed a total of $6,000 for any year,

"(iii) the employer is required to make a matching contribution to the simple retirement account for any year in an amount equal to so much of the amount the employee elects under clause (i)(I) as does not exceed the applicable percentage of compensation for the year, and

"(iv) no contributions may be made other than contributions described in clause (i) or (iii).

"(B) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—An employer shall be treated as meeting the requirements of subparagraph (A)(iii) for any year if, in lieu of the contributions described in such clause, the employer elects to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 30-day period for such year under paragraph (5)(C).

"(C) DEFINITIONS.—For purposes of this subsection—

"(i) ELIGIBLE EMPLOYER.—The term 'eligible employer' means an employer who employs 100 or fewer employees on any day during the year.

"(ii) APPLICABLE PERCENTAGE.—

"(I) IN GENERAL.—The term 'applicable percentage' means 3 percent.

"(II) ELECTION OF LOWER PERCENTAGE.—An employer may elect to apply a lower percentage (not less than 1 percent) for any year for all employees eligible to participate in the plan for such year if the employer notifies the employees of such lower percentage within a reasonable period of time before the 30-day election period for such year under paragraph (5)(C). An employer may not elect a lower percentage under this subclause for any year if that election would result in the applicable percentage being lower than 3 percent in more than 2 of the years in the 5-year period ending with such year.

"(III) SPECIAL RULE FOR YEARS ARRANGEMENT NOT IN EFFECT.—If any year in the 5-year period described in subclause (II) is a year prior to the first year for which any qualified salary reduction arrangement is in effect with respect to the employer (or any predecessor), the employer shall be treated as if the level of the employer matching contribution was at 3 percent of compensation for such prior year.

"(D) ARRANGEMENT MAY BE ONLY PLAN OF EMPLOYER.—

"(i) IN GENERAL.—An arrangement shall not be treated as a qualified salary reduction arrangement for any year if the employer (or any predecessor employer) maintained a qualified plan with respect to which contributions were made, or benefits were accrued, for service in any year in the period beginning with the year such arrangement became effective and ending with the year for which the determination is being made.

"(ii) QUALIFIED PLAN.—For purposes of this subparagraph, the term 'qualified plan' means a plan, contract, pension, or trust described in subparagraph (A) or (B) of section 219(g)(5).

"(E) COST-OF-LIVING ADJUSTMENT.—The Secretary shall adjust the $6,000 amount under subparagraph (A)(ii) at the same time and in the same manner as under section 415(d), except that the base period taken into account shall be the calendar quarter ending September 30, 1995, and any increase under this subparagraph which is not a multiple of $500 shall be rounded to the next lower multiple of $500.

"(3) VESTING REQUIREMENTS.—The requirements of this paragraph are met with respect to a simple retirement account if the employee's rights to any contribution to the simple retirement account are nonforfeitable. For purposes of this paragraph, rules similar to the rules of subsection (k)(4) shall apply.

"(4) PARTICIPATION REQUIREMENTS.—

"(A) IN GENERAL.—The requirements of this paragraph are met with respect to any simple retirement account for a year only if, under the qualified salary reduction arrangement, all employees of the employer who—

"(i) received at least $5,000 in compensation from the employer during any 2 preceding years, and

"(ii) are reasonably expected to receive at least $5,000 in compensation during the year,

are eligible to make the election under paragraph (2)(A)(i) or receive the nonelective contribution described in paragraph (2)(B).

"(B) EXCLUDABLE EMPLOYEES.—An employer may elect to exclude from the requirement under subparagraph (A) employees described in section 410(b)(3).

"(5) ADMINISTRATIVE REQUIREMENTS.—The requirements of this paragraph are met with respect to any simplified retirement account if, under the qualified salary reduction arrangement—

"(A) an employer must—

"(i) make the elective employer contributions under paragraph (2)(A)(i) not later than the close of the 30-day period following the last day of the month with respect to which the contributions are to be made, and

"(ii) make the matching contributions under paragraph (2)(A)(iii) or the nonelective contributions under paragraph (2)(B) not later than the date described in section 404(m)(2)(B),

"(B) an employee may elect to terminate participation in such arrangement at any time during the year, except that if an employee so terminates, the arrangement may provide that the employee may not elect to resume participation until the beginning of the next year, and

"(C) each employee eligible to participate may elect, during the 30-day period before the beginning of any year (and the 30-day period before the first day such employee is eligible to participate), to participate in the arrangement, or to modify the amounts subject to such arrangement, for such year.

"(6) DEFINITIONS.—For purposes of this subsection—

"(A) COMPENSATION.—

"(i) IN GENERAL.—The term 'compensation' means amounts described in paragraphs (3) and (8) of section 6051(a).

"(ii) SELF-EMPLOYED.—In the case of an employee described in subparagraph (B), the term 'compensation' means net earnings from self-employment determined under section 1402(a) without regard to any contribution under this subsection.

"(B) EMPLOYEE.—The term 'employee' includes an employee as defined in section 401(c)(1).

"(C) YEAR.—The term 'year' means the calendar year."

(b) TAX TREATMENT OF SIMPLE RETIREMENT ACCOUNTS.—

(1) DEDUCTIBILITY OF CONTRIBUTIONS BY EMPLOYEES.—

(A) Section 219(b) (relating to maximum amount of deduction) is amended by adding at the end the following new paragraph:

"(4) SPECIAL RULE FOR SIMPLE RETIREMENT ACCOUNTS.—This section shall not apply with respect to any amount contributed to a simple retirement account established under section 408(p)."

(B) Section 219(g)(5)(A) (defining active participant) is amended by striking "or" at the end of clause (iv) and by adding at the end the following new clause:

"(vi) any simple retirement account (within the meaning of section 408(p)), or".

(2) DEDUCTIBILITY OF EMPLOYER CONTRIBUTIONS.—Section 404 (relating to deductions for contributions of an employer to pension, etc. plans) is amended by adding at the end the following new subsection:

"(m) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—

"(1) IN GENERAL.—Employer contributions to a simple retirement account shall be treated as if they are made to a plan subject to the requirements of this section.

"(2) TIMING.—

"(A) DEDUCTION.—Contributions described in paragraph (1) shall be deductible in the taxable year of the employer with or within which the calendar year for which the contributions were made ends.

"(B) CONTRIBUTIONS AFTER END OF YEAR.—For purposes of this subsection, contributions shall be treated as made for a taxable year if they are made on account of the taxable year and are made not later than the time prescribed by law for filing the return for the taxable year (including extensions thereof)."

(3) CONTRIBUTIONS AND DISTRIBUTIONS.—

(A) Section 402 (relating to taxability of beneficiary of employees' trust) is amended by adding at the end the following new subsection:

"(k) TREATMENT OF SIMPLE RETIREMENT ACCOUNTS.—Rules similar to the rules of paragraphs (1) and (3) of subsection (h) shall apply to contributions and distributions with respect to a simple retirement account under section 408(p)."

(B) Section 408(d)(3) is amended by adding at the end the following new subparagraph:

"(G) SIMPLE RETIREMENT ACCOUNTS.—This paragraph shall not apply to any amount paid or distributed out of a simple retirement account (as defined in section 408(p)) unless—

"(i) it is paid into another simple retirement account, or

"(ii) in the case of any payment or distribution to which section 72(t)(8) does not apply, it is paid into an individual retirement plan."

(C) Clause (i) of section 457(c)(2)(B) is amended by striking "section 402(h)(1)(B)" and inserting "section 402(h)(1)(B) or (k)".

(4) PENALTIES.—

(A) EARLY WITHDRAWALS.—Section 72(t) (relating to additional tax in early distributions), as amended by this Act, is amended by adding at the end the following new paragraph:

"(6) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—In the case of any amount received from a simple retirement account (within the meaning of section 408(p)) during the 2-year period beginning on the date such individual first participated in any qualified salary reduction arrangement maintained by the individual's employer under section 408(p)(2), paragraph (1) shall be applied by substituting '25 percent' for '10 percent'."

(B) FAILURE TO REPORT.—Section 6693 is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

"(c) PENALTIES RELATING TO SIMPLE RETIREMENT ACCOUNTS.—

"(1) EMPLOYER PENALTIES.—An employer who fails to provide 1 or more notices required by section 408(l)(2)(C) shall pay a penalty of $50 for each day on which such failures continue.

"(2) TRUSTEE PENALTIES.—A trustee who fails—

"(A) to provide 1 or more statements required by the last sentence of section 408(i) shall pay a penalty of $50 for each day on which such failures continue, or

"(B) to provide 1 or more summary descriptions required by section 408(l)(2)(B) shall pay a penalty of $50 for each day on which such failures continue.

"(3) REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed under this subsection with respect to any failure which the taxpayer shows was due to reasonable cause."

(5) REPORTING REQUIREMENTS.—

(A) Section 408(l) is amended by adding at the end the following new paragraph:

"(2) SIMPLE RETIREMENT ACCOUNTS.—

"(A) NO EMPLOYER REPORTS.—Except as provided in this paragraph, no report shall be required under this section by an employer maintaining a qualified salary reduction arrangement under subsection (p).

"(B) SUMMARY DESCRIPTION.—The trustee of any simple retirement account established pursuant to a qualified salary reduction arrangement under subsection (p) shall provide to the employer maintaining the arrangement, each year a description containing the following information:

"(i) The name and address of the employer and the trustee.

"(ii) The requirements for eligibility for participation.

"(iii) The benefits provided with respect to the arrangement.

"(iv) The time and method of making elections with respect to the arrangement.

"(v) The procedures for, and effects of, withdrawals (including rollovers) from the arrangement.

"(C) EMPLOYEE NOTIFICATION.—The employer shall notify each employee immediately before the period for which an election described in subsection (p)(5)(C) may be made of the employee's opportunity to make such election. Such notice shall include a copy of the description described in subparagraph (B)."

(B) Section 408(l) is amended by striking "An employer" and inserting the following:

"(1) IN GENERAL.—An employer".

(6) REPORTING REQUIREMENTS.—Section 408(i) is amended by adding at the end the following new flush sentence:

"In the case of a simple retirement account under subsection (p), only one report under this subsection shall be required to be submitted each calendar year to the Secretary (at the time provided under paragraph (2)) but, in addition to the report under this subsection, there shall be furnished, within 30 days after each calendar year, to the individual on whose behalf the account is maintained a statement with respect to the account balance as of the close of, and the account activity during, such calendar year."

(7) EXEMPTION FROM TOP-HEAVY PLAN RULES.—Section 416(g)(4) (relating to special rules for top-heavy plans) is amended by adding at the end the following new subparagraph:

"(G) SIMPLE RETIREMENT ACCOUNTS.—The term 'top-heavy plan' shall not include a simple retirement account under section 408(p)."

(8) EMPLOYMENT TAXES.—

(A) Paragraph (5) of section 3121(a) is amended by striking "or" at the end of subparagraph (F), by inserting "or" at the end of subparagraph (G), and by adding at the end the following new subparagraph:

"(H) under an arrangement to which section 408(p) applies, other than any elective contributions under paragraph (2)(A)(i) thereof,".

(B) Section 209(a)(4) of the Social Security Act is amended by inserting ", or (J) under an arrangement to which section 408(p) of such Code applies, other than any elective contributions under paragraph (2)(A)(i) thereof" before the semicolon at the end thereof.

(C) Paragraph (5) of section 3306(b) is amended by striking "or" at the end of subparagraph (F), by inserting "or" at the end of subparagraph (G), and by adding at the end the following new subparagraph:

"(H) under an arrangement to which section 408(p) applies, other than any elective contributions under paragraph (2)(A)(i) thereof,".

(D) Paragraph (12) of section 3401(a) is amended by adding the following new subparagraph:

"(D) under an arrangement to which section 408(p) applies; or".

(9) CONFORMING AMENDMENTS.—

(A) Section 280G(b)(6) is amended by striking "or" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", or" and by adding after subparagraph (C) the following new subparagraph:

"(D) a simple retirement account described in section 408(p)."

(B) Section 402(g)(3) is amended by striking "and" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", and", and by adding after subparagraph (C) the following new subparagraph:

"(D) any elective employer contribution under section 408(p)(2)(A)(i)."

(C) Subsections (b), (c), (m)(4)(B), and (n)(3)(B) of section 414 are each amended by inserting "408(p)," after "408(k),".

(D) Section 4972(d)(1)(A) is amended by striking "and" at the end of clause (ii), by striking the period at the end of clause (iii) and inserting ", and", and by adding after clause (iii) the following new clause:

"(iv) any simple retirement account (within the meaning of section 408(p))."

(c) REPEAL OF SALARY REDUCTION SIMPLIFIED EMPLOYEE PENSIONS.—Section 408(k)(6) is amended by adding at the end the following new subparagraph:

"(H) TERMINATION.—This paragraph shall not apply to years beginning after December 31, 1996. The preceding sentence shall not apply to a simplified employee pension if the terms of such pension, as in effect on December 31, 1996, provide that an employee may make the election described in subparagraph (A)."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1422. EXTENSION OF SIMPLE PLAN TO 401(k) ARRANGEMENTS.

(a) ALTERNATIVE METHOD OF SATISFYING SECTION 401(k) NONDISCRIMINATION TESTS.—Section 401(k) (relating to cash or deferred arrangements) is amended by adding at the end the following new paragraph:

"(11) ADOPTION OF SIMPLE PLAN TO MEET NONDISCRIMINATION TESTS.—

"(A) IN GENERAL.—A cash or deferred arrangement maintained by an eligible employer shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement meets—

"(i) the contribution requirements of subparagraph (B),

"(ii) the exclusive benefit requirements of subparagraph (C), and

"(iii) the vesting requirements of section 408(p)(3).

"(B) CONTRIBUTION REQUIREMENTS.—

"(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement—

"(I) an employee may elect to have the employer make elective contributions for the year on behalf of the employee to a trust under the plan in an amount which is expressed as a percentage of compensation of the employee but which in no event exceeds $6,000,

"(II) the employer is required to make a matching contribution to the trust for the year in an amount equal to so much of the amount the employee elects under subclause (I) as does not exceed 3 percent of compensation for the year, and

"(III) no other contributions may be made other than contributions described in subclause (I) or (II).

"(ii) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—An employer shall be treated as meeting the requirements of clause (i)(II) for any year if, in lieu of the contributions described in such clause, the employer elects (pursuant to the terms of the arrangement) to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 30th day before the beginning of such year.

"(C) EXCLUSIVE BENEFIT.—The requirements of this subparagraph are met for any year to which this paragraph applies if no contributions were made, or benefits were accrued, for services during such year under any qualified plan of the employer on behalf of any employee eligible to participate in the cash or deferred arrangement, other than contributions described in subparagraph (B).

"(D) DEFINITIONS AND SPECIAL RULE.—

"(i) DEFINITIONS.—For purposes of this paragraph, any term used in this paragraph which is also used in section 408(p) shall have the meaning given such term by such section.

"(ii) COORDINATION WITH TOP-HEAVY RULES.—A plan meeting the requirements of this paragraph for any year shall not be treated as a top-heavy plan under section 416 for such year."

(b) ALTERNATIVE METHODS OF SATISFYING SECTION 401(m) NONDISCRIMINATION TESTS.—Section 401(m) (relating to nondiscrimination test for matching contribu-

tions and employee contributions) is amended by redesignating paragraph (10) as paragraph (11) and by adding after paragraph (9) the following new paragraph:

"(10) ALTERNATIVE METHOD OF SATISFYING TESTS.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

"(A) meets the contribution requirements of subparagraph (B) of subsection (k)(11),

"(B) meets the exclusive benefit requirements of subsection (k)(11)(C), and

"(C) meets the vesting requirements of section 408(p)(3)."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning after December 31, 1996.

Subchapter B—Other Provisions

SEC. 1426. TAX-EXEMPT ORGANIZATIONS ELIGIBLE UNDER SECTION 401(k).

(a) IN GENERAL.—Subparagraph (B) of section 401(k)(4) is amended to read as follows:

"(B) ELIGIBILITY OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.—

"(i) TAX-EXEMPTS ELIGIBLE.—Except as provided in clause (ii), any organization exempt from tax under this subtitle may include a qualified cash or deferred arrangement as part of a plan maintained by it.

"(ii) GOVERNMENTS INELIGIBLE.—A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement if it is part of a plan maintained by a State or local government or political subdivision thereof, or any agency or instrumentality thereof. This clause shall not apply to a rural cooperative plan or to a plan of an employer described in clause (iii).

"(iii) TREATMENT OF INDIAN TRIBAL GOVERNMENTS.—An employer which is an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of the foregoing shall be treated as an organization exempt from tax under this subtitle for purposes of clause (i)."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to plan years beginning after December 31, 1996, but shall not apply to any cash or deferred arrangement to which clause (i) of section 1116(f)(2)(B) of the Tax Reform Act of 1986 applies.

CHAPTER 3—NONDISCRIMINATION PROVISIONS

SEC. 1431. DEFINITION OF HIGHLY COMPENSATED EMPLOYEES; REPEAL OF FAMILY AGGREGATION.

(a) IN GENERAL.—Paragraph (1) of section 414(q) (defining highly compensated employee) is amended to read as follows:

"(1) IN GENERAL.—The term 'highly compensated employee' means any employee who—

"(A) was a 5-percent owner at any time during the year or the preceding year, or

"(B) for the preceding year—

"(i) had compensation from the employer in excess of $80,000, and

"(ii) was in the top-paid group of the employer.

The Secretary shall adjust the $80,000 amount under subparagraph (B) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1996."

(b) REPEAL OF FAMILY AGGREGATION RULES.—

(1) IN GENERAL.—Paragraph (6) of section 414(q) is hereby repealed.

(2) COMPENSATION LIMIT.—Paragraph (17)(A) of section 401(a) is amended by striking the last sentence.

(3) DEDUCTION.—Subsection (l) of section 404 is amended by striking the last sentence.

(c) CONFORMING AMENDMENTS.—

(1)(A) Subsection (q) of section 414 is amended by striking paragraphs (2), (5), (8), and (12) and by redesignating paragraphs (3), (4), (7), (9), (10), and (11) as paragraphs (2) through (7), respectively.

(B) Sections 129(d)(8)(B), 401(a)(5)(D)(ii), 408(k)(2)(C), and 416(i)(1)(D) are each amended by striking "section 414(q)(7)" and inserting "section 414(q)(4)".

(C) Section 416(i)(1)(A) is amended by striking "section 414(q)(8)" and inserting "section 414(r)(9)".

(2)(A) Section 414(r) is amended by adding at the end the following new paragraph:

"(9) EXCLUDED EMPLOYEES.—For purposes of this subsection, the following employees shall be excluded:

"(A) Employees who have not completed 6 months of service.

"(B) Employees who normally work less than 17½ hours per week.

"(C) Employees who normally work not more than 6 months during any year.

"(D) Employees who have not attained the age of 21.

"(E) Except to the extent provided in regulations, employees who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and the employer.

Except as provided by the Secretary, the employer may elect to apply subparagraph (A), (B), (C), or (D) by substituting a shorter period of service, smaller number of hours or months, or lower age for the period of service, number of hours or months, or age (as the case may be) specified in such subparagraph."

(B) Subparagraph (A) of section 414(r)(2) is amended by striking "subsection (q)(8)" and inserting "paragraph (9)".

(3) Section 1114(c)(4) of the Tax Reform Act of 1986 is amended by adding at the end the following new sentence: "Any reference in this paragraph to section 414(q) shall be treated as a reference to such section as in effect on the day before the date of the enactment of the Small Business Job Protection Act of 1996.".

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to years beginning after December 31, 1996, except that in determining whether an employee is a highly compensated employee for years beginning in 1997, such amendments shall be treated as having been in effect for years beginning in 1996.

(2) FAMILY AGGREGATION.—The amendments made by subsection (b) shall apply to years beginning after December 31, 1996.

SEC. 1432. MODIFICATION OF ADDITIONAL PARTICIPATION REQUIREMENTS.

(a) GENERAL RULE.—Section 401(a)(26)(A) (relating to additional participation requirements) is amended to read as follows:

"(A) IN GENERAL.—In the case of a trust which is a part of a defined benefit plan, such trust shall not constitute a qualified trust under this subsection unless on each day of the plan year such trust benefits at least the lesser of—

"(i) 50 employees of the employer, or

"(ii) the greater of—

"(I) 40 percent of all employees of the employer, or

"(II) 2 employees (or if there is only 1 employee, such employee)."

(b) SEPARATE LINE OF BUSINESS TEST.—Section 401(a)(26)(G) (relating to separate line of business) is amended by striking "paragraph (7)" and inserting "paragraph (2)(A) or (7)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1996.

SEC. 1433. NONDISCRIMINATION RULES FOR QUALIFIED CASH OR DEFERRED ARRANGEMENTS AND MATCHING CONTRIBUTIONS.

(a) ALTERNATIVE METHODS OF SATISFYING SECTION 401(k) NONDISCRIMINATION TESTS.—Section 401(k) (relating to cash or deferred arrangements), as amended by section 1422, is amended by adding at the end the following new paragraph:

"(12) ALTERNATIVE METHODS OF MEETING NONDISCRIMINATION REQUIREMENTS.—

"(A) IN GENERAL.—A cash or deferred arrangement shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement—

"(i) meets the contribution requirements of subparagraph (B) or (C), and

"(ii) meets the notice requirements of subparagraph (D).

"(B) MATCHING CONTRIBUTIONS.—

"(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement, the employer makes matching contributions on

behalf of each employee who is not a highly compensated employee in an amount equal to—

"(I) 100 percent of the elective contributions of the employee to the extent such elective contributions do not exceed 3 percent of the employee's compensation, and

"(II) 50 percent of the elective contributions of the employee to the extent that such elective contributions exceed 3 percent but do not exceed 5 percent of the employee's compensation.

"(ii) RATE FOR HIGHLY COMPENSATED EMPLOYEES.—The requirements of this subparagraph are not met if, under the arrangement, the rate of matching contribution with respect to any elective contribution of a highly compensated employee at any rate of elective contribution is greater than that with respect to an employee who is not a highly compensated employee.

"(iii) ALTERNATIVE PLAN DESIGNS.—If the rate of any matching contribution with respect to any rate of elective contribution is not equal to the percentage required under clause (i), an arrangement shall not be treated as failing to meet the requirements of clause (i) if—

"(I) the rate of an employer's matching contribution does not increase as an employee's rate of elective contributions increase, and

"(II) the aggregate amount of matching contributions at such rate of elective contribution is at least equal to the aggregate amount of matching contributions which would be made if matching contributions were made on the basis of the percentages described in clause (i).

"(C) NONELECTIVE CONTRIBUTIONS.—The requirements of this subparagraph are met if, under the arrangement, the employer is required, without regard to whether the employee makes an elective contribution or employee contribution, to make a contribution to a defined contribution plan on behalf of each employee who is not a highly compensated employee and who is eligible to participate in the arrangement in an amount equal to at least 3 percent of the employee's compensation.

"(D) NOTICE REQUIREMENT.—An arrangement meets the requirements of this paragraph if, under the arrangement, each employee eligible to participate is, within a reasonable period before any year, given written notice of the employee's rights and obligations under the arrangement which—

"(i) is sufficiently accurate and comprehensive to appraise the employee of such rights and obligations, and

"(ii) is written in a manner calculated to be understood by the average employee eligible to participate.

"(E) OTHER REQUIREMENTS.—

"(i) WITHDRAWAL AND VESTING RESTRICTIONS.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) of this paragraph unless the requirements of subparagraphs (B) and (C) of paragraph (2) are met with respect to all employer contributions (including matching contributions) taken into account in determining whether the requirements of subparagraphs (B) and (C) of this paragraph are met.

"(ii) SOCIAL SECURITY AND SIMILAR CONTRIBUTIONS NOT TAKEN INTO ACCOUNT.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) unless such requirements are met without regard to subsection (l), and, for purposes of subsection (l), employer contributions under subparagraph (B) or (C) shall not be taken into account.

"(F) OTHER PLANS.—An arrangement shall be treated as meeting the requirements under subparagraph (A)(i) if any other plan maintained by the employer meets such requirements with respect to employees eligible under the arrangement."

(b) ALTERNATIVE METHODS OF SATISFYING SECTION 401(m) NONDISCRIMINATION TESTS.—Section 401(m) (relating to nondiscrimination test for matching contributions and employee contributions), as amended by this Act, is amended by redesignating paragraph (11) as paragraph (12) and by adding after paragraph (10) the following new paragraph:

"(11) ALTERNATIVE METHOD OF SATISFYING TESTS.—

"(A) IN GENERAL.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

"(i) meets the contribution requirements of subparagraph (B) or (C) of subsection (k)(12),

"(ii) meets the notice requirements of subsection (k)(12)(D), and

"(iii) meets the requirements of subparagraph (B).

"(B) LIMITATION ON MATCHING CONTRIBUTIONS.—The requirements of this subparagraph are met if—

"(i) matching contributions on behalf of any employee may not be made with respect to an employee's contributions or elective deferrals in excess of 6 percent of the employee's compensation,

"(ii) the rate of an employer's matching contribution does not increase as the rate of an employee's contributions or elective deferrals increase, and

"(iii) the matching contribution with respect to any highly compensated employee at any rate of an employee contribution or rate of elective deferral is not greater than that with respect to an employee who is not a highly compensated employee."

(c) YEAR FOR COMPUTING NONHIGHLY COMPENSATED EMPLOYEE PERCENTAGE.—

(1) CASH OR DEFERRED ARRANGEMENTS.—Clause (ii) of section 401(k)(3)(A) is amended—

(A) by striking "such year" and inserting "the plan year",

(B) by striking "for such plan year" and inserting "for the preceding plan year", and

(C) by adding at the end the following new sentence: "An arrangement may apply this clause by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary."

(2) MATCHING AND EMPLOYEE CONTRIBUTIONS.—Section 401(m)(2)(A) is amended—

(A) by inserting "for such plan year" after "highly compensated employees",

(B) by inserting "for the preceding plan year" after "eligible employees" each place it appears in clause (i) and clause (ii), and

(C) by adding at the end the following flush sentence: "This subparagraph may be applied by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided the Secretary."

(d) SPECIAL RULE FOR DETERMINING AVERAGE DEFERRAL PERCENTAGE FOR FIRST PLAN YEAR, ETC.—

(1) Paragraph (3) of section 401(k) is amended by adding at the end the following new subparagraph:

"(E) For purposes of this paragraph, in the case of the first plan year of any plan (other than a successor plan), the amount taken into account as the actual deferral percentage of nonhighly compensated employees for the preceding plan year shall be—

"(i) 3 percent, or

"(ii) if the employer makes an election under this subclause, the actual deferral percentage of nonhighly compensated employees determined for such first plan year."

(2) Paragraph (3) of section 401(m) is amended by adding at the end the following: "Rules similar to the rules of subsection (k)(3)(E) shall apply for purposes of this subsection."

(e) DISTRIBUTION OF EXCESS CONTRIBUTIONS AND EXCESS AGGREGATE CONTRIBUTIONS.—

(1) Subparagraph (C) of section 401(k)(8) (relating to arrangement not disqualified if excess contributions distributed) is amended by striking "on the basis of the respective portions of the excess contributions attributable to each of such employees" and inserting "on the basis of the amount of contributions by, or on behalf of, each of such employees".

(2) Subparagraph (C) of section 401(m)(6) (relating to method of distributing excess aggregate contributions) is amended by striking "on the basis of the respective portions of such amounts attributable to each of such employees" and inserting "on the basis of the amount of contributions on behalf of, or by, each such employee".

(f) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to years beginning after December 31, 1998.

(2) EXCEPTIONS.—The amendments made by subsections (c), (d), and (e) shall apply to years beginning after December 31, 1996.

SEC. 1434. DEFINITION OF COMPENSATION FOR SECTION 415 PURPOSES.

(a) GENERAL RULE.—Section 415(c)(3) (defining participant's compensation) is amended by adding at the end the following new subparagraph:

"(D) CERTAIN DEFERRALS INCLUDED.—The term 'participant's compensation' shall include—

"(i) any elective deferral (as defined in section 402(g)(3)), and

"(ii) any amount which is contributed by the employer at the election of the employee and which is not includible in the gross income of the employee under section 125 or 457."

(b) CONFORMING AMENDMENTS.—

(1) Section 414(q)(4), as redesignated by section 1431, is amended to read as follows:

"(4) COMPENSATION.—For purposes of this subsection, the term 'compensation' has the meaning given such term by section 415(c)(3)."

(2) Section 414(s)(2) is amended by inserting "not" after "elect" in the text and heading thereof.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1997.

CHAPTER 4—MISCELLANEOUS PROVISIONS

SEC. 1441. PLANS COVERING SELF-EMPLOYED INDIVIDUALS.

(a) AGGREGATION RULES.—Section 401(d) (relating to additional requirements for qualification of trusts and plans benefiting owner-employees) is amended to read as follows:

"(d) CONTRIBUTION LIMIT ON OWNER-EMPLOYEES.—A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the plan provides that contributions on behalf of any owner-employee may be made only with respect to the earned income of such owner-employee which is derived from the trade or business with respect to which such plan is established."

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1996.

SEC. 1442. ELIMINATION OF SPECIAL VESTING RULE FOR MULTIEMPLOYER PLANS.

(a) IN GENERAL.—Paragraph (2) of section 411(a) (relating to minimum vesting standards) is amended—

(1) by striking "subparagraph (A), (B), or (C)" and inserting "subparagraph (A) or (B)"; and

(2) by striking subparagraph (C).

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning on or after the earlier of—

(1) the later of—

(A) January 1, 1997, or

(B) the date on which the last of the collective bargaining agreements pursuant to which the plan is maintained terminates (determined without regard to any extension thereof after the date of the enactment of this Act), or

(2) January 1, 1999.

Such amendments shall not apply to any individual who does not have more than 1 hour of service under the plan on or after the 1st day of the 1st plan year to which such amendments apply.

SEC. 1443. DISTRIBUTIONS UNDER RURAL COOPERATIVE PLANS.

(a) DISTRIBUTIONS FOR HARDSHIP OR AFTER A CERTAIN AGE.—Section 401(k)(7) is amended by adding at the end the following new subparagraph:

"(C) SPECIAL RULE FOR CERTAIN DISTRIBUTIONS.—A rural cooperative plan which includes a qualified cash or deferred arrangement shall not be treated as violating the requirements of section 401(a) or of paragraph (2) merely by reason of a hardship distribution or a distribution to a participant after attainment of age 59½. For purposes of this section, the term 'hardship distribution' means a distribution described in paragraph (2)(B)(i)(IV) (without regard to the limitation of its application to profit-sharing or stock bonus plans)."

(b) PUBLIC UTILITY DISTRICTS.—Clause (i) of section 401(k)(7)(B) (defining rural cooperative) is amended to read as follows:

"(i) any organization which—

"(I) is engaged primarily in providing electric service on a mutual or cooperative basis, or

"(II) is engaged primarily in providing electric service to the public in its area of service and which is exempt from tax under this subtitle or which is a State or local government (or an agency or instrumentality thereof), other than a municipality (or an agency or instrumentality thereof),".

(c) EFFECTIVE DATES.—

(1) DISTRIBUTIONS.—The amendments made by subsection (a) shall apply to distributions after the date of the enactment of this Act.

(2) RURAL COOPERATIVE.—The amendments made by subsection (b) shall apply to plan years beginning after December 31, 1996.

SEC. 1444. TREATMENT OF GOVERNMENTAL PLANS UNDER SECTION 415.

(a) COMPENSATION LIMIT.—Subsection (b) of section 415 is amended by adding immediately after paragraph (10) the following new paragraph:

"(11) SPECIAL LIMITATION RULE FOR GOVERNMENTAL PLANS.—In the case of a governmental plan (as defined in section 414(d)), subparagraph (B) of paragraph (1) shall not apply."

(b) TREATMENT OF CERTAIN EXCESS BENEFIT PLANS.—

(1) IN GENERAL.—Section 415 is amended by adding at the end the following new subsection:

"(m) TREATMENT OF QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENTS.—

"(1) GOVERNMENTAL PLAN NOT AFFECTED.—In determining whether a governmental plan (as defined in section 414(d)) meets the requirements of this section, benefits provided under a qualified governmental excess benefit arrangement shall not be taken into account. Income accruing to a governmental plan (or to a trust that is maintained solely for the purpose of providing benefits under a qualified governmental excess benefit arrangement) in respect of a qualified governmental excess benefit arrangement shall constitute income derived from the exercise of an essential governmental function upon which such governmental plan (or trust) shall be exempt from tax under section 115.

"(2) TAXATION OF PARTICIPANT.—For purposes of this chapter—

"(A) the taxable year or years for which amounts in respect of a qualified governmental excess benefit arrangement are includible in gross income by a participant, and

"(B) the treatment of such amounts when so includible by the participant, shall be determined as if such qualified governmental excess benefit arrangement were treated as a plan for the deferral of compensation which is maintained by a corporation not exempt from tax under this chapter and which does not meet the requirements for qualification under section 401.

"(3) QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENT.—For purposes of this subsection, the term 'qualified governmental excess benefit arrangement' means a portion of a governmental plan if—

"(A) such portion is maintained solely for the purpose of providing to participants in the plan that part of the participant's annual benefit otherwise payable under the terms of the plan that exceeds the limitations on benefits imposed by this section,

"(B) under such portion no election is provided at any time to the participant (directly or indirectly) to defer compensation, and

"(C) benefits described in subparagraph (A) are not paid from a trust forming a part of such governmental plan unless such trust is maintained solely for the purpose of providing such benefits."

(2) COORDINATION WITH SECTION 457.—Subsection (e) of section 457 is amended by adding at the end the following new paragraph:

"(14) TREATMENT OF QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENTS.—Subsections (b)(2) and (c)(1) shall not apply to any qualified governmental excess benefit arrangement (as defined in section 415(m)(3)), and benefits provided under such an arrangement shall not be taken into account in determining whether any other plan is an eligible deferred compensation plan."

(3) CONFORMING AMENDMENT.—Paragraph (2) of section 457(f) is amended by striking "and" at the end of subparagraph (C), by striking the period at the end of subparagraph (D) and inserting ", and", and by inserting immediately thereafter the following new subparagraph:

"(E) a qualified governmental excess benefit arrangement described in section 415(m)."

(c) EXEMPTION FOR SURVIVOR AND DISABILITY BENEFITS.—Paragraph (2) of section 415(b) is amended by adding at the end the following new subparagraph:

"(I) EXEMPTION FOR SURVIVOR AND DISABILITY BENEFITS PROVIDED UNDER GOVERNMENTAL PLANS.—Subparagraph (C) of this paragraph and paragraph (5) shall not apply to—

"(i) income received from a governmental plan (as defined in section 414(d)) as a pension, annuity, or similar allowance as the result of the recipient becoming disabled by reason of personal injuries or sickness, or

"(ii) amounts received from a governmental plan by the beneficiaries, survivors, or the estate of an employee as the result of the death of the employee."

(d) REVOCATION OF GRANDFATHER ELECTION.—

(1) IN GENERAL.—Subparagraph (C) of section 415(b)(10) is amended by adding at the end the following new clause:

"(ii) REVOCATION OF ELECTION.—An election under clause (i) may be revoked not later than the last day of the third plan year beginning after the date of the enactment of this clause. The revocation shall apply to all plan years to which the election applied and to all subsequent plan years. Any amount paid by a plan in a taxable year ending after the revocation shall be includible in income in such taxable year under the rules of this chapter in effect for such taxable year, except that, for purposes of applying the limitations imposed by this section, any portion of such amount which is attributable to any taxable year during which the election was in effect shall be treated as received in such taxable year."

(2) CONFORMING AMENDMENT.—Subparagraph (C) of section 415(b)(10) is amended by striking "This" and inserting:

"(i) IN GENERAL.—This".

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by subsections (a), (b), and (c) shall apply to years beginning after December 31, 1994. The amendments made by subsection (d) shall apply with respect to revocations adopted after the date of the enactment of this Act.

(2) TREATMENT FOR YEARS BEGINNING BEFORE JANUARY 1, 1995.—Nothing in the amendments made by this section shall be construed to infer that a governmental plan (as defined in section 414(d) of the Internal Revenue Code of 1986) fails to satisfy the requirements of section 415 of such Code for any taxable year beginning before January 1, 1995.

SEC. 1445. UNIFORM RETIREMENT AGE.

(a) DISCRIMINATION TESTING.—Paragraph (5) of section 401(a) (relating to special rules relating to nondiscrimination requirements) is amended by adding at the end the following new subparagraph:

"(F) SOCIAL SECURITY RETIREMENT AGE.—For purposes of testing for discrimination under paragraph (4)—

"(i) the social security retirement age (as defined in section 415(b)(8)) shall be treated as a uniform retirement age, and

"(ii) subsidized early retirement benefits and joint and survivor annuities shall not be treated as being unavailable to employees on the same terms merely because such benefits or annuities are based in whole or in part on an employee's social security retirement age (as so defined)."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to years beginning after December 31, 1996.

SEC. 1446. CONTRIBUTIONS ON BEHALF OF DISABLED EMPLOYEES.

(a) ALL DISABLED PARTICIPANTS RECEIVING CONTRIBUTIONS.—Section 415(c)(3)(C) is amended by adding at the end the following: "If a defined contribution plan provides for the continuation of contributions on behalf of all participants described in clause (i) for a fixed or determinable period, this subparagraph shall be applied without regard to clauses (ii) and (iii)."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to years beginning after December 31, 1996.

SEC. 1447. TREATMENT OF DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.

(a) SPECIAL RULES FOR PLAN DISTRIBUTIONS.—Paragraph (9) of section 457(e) (relating to other definitions and special rules) is amended to read as follows:

"(9) BENEFITS NOT TREATED AS MADE AVAILABLE BY REASON OF CERTAIN ELECTIONS, ETC.—

"(A) TOTAL AMOUNT PAYABLE IS $3,500 OR LESS.—The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to receive such amount (or the plan may distribute such amount without the participant's consent) if—

"(i) such amount does not exceed $3,500, and

"(ii) such amount may be distributed only if—

"(I) no amount has been deferred under the plan with respect to such participant during the 2-year period ending on the date of the distribution, and

"(II) there has been no prior distribution under the plan to such participant to which this subparagraph applied.

A plan shall not be treated as failing to meet the distribution requirements of subsection (d) by reason of a distribution to which this subparagraph applies.

"(B) ELECTION TO DEFER COMMENCEMENT OF DISTRIBUTIONS.—The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to defer commencement of distributions under the plan if—

"(i) such election is made after amounts may be available under the plan in accordance with subsection (d)(1)(A) and before commencement of such distributions, and

"(ii) the participant may make only 1 such election."

(b) COST-OF-LIVING ADJUSTMENT OF MAXIMUM DEFERRAL AMOUNT.—Subsection (e) of section 457, as amended by section 1444(b)(2) (relating to governmental plans), is amended by adding at the end the following new paragraph:

"(15) COST-OF-LIVING ADJUSTMENT OF MAXIMUM DEFERRAL AMOUNT.—The Secretary shall adjust the $7,500 amount specified in subsections (b)(2) and (c)(1) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1994, and any increase under this paragraph which is not a multiple of $500 shall be rounded to the next lowest multiple of $500."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1448. TRUST REQUIREMENT FOR DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS.

(a) IN GENERAL.—Section 457 is amended by adding at the end the following new subsection:

"(g) GOVERNMENTAL PLANS MUST MAINTAIN SET-ASIDES FOR EXCLUSIVE BENEFIT OF PARTICIPANTS.—

"(1) IN GENERAL.—A plan maintained by an eligible employer described in subsection (e)(1)(A) shall not be treated as an eligible deferred compensation plan unless all assets and income of the plan described in subsection (b)(6) are held in trust for the exclusive benefit of participants and their beneficiaries.

"(2) TAXABILITY OF TRUSTS AND PARTICIPANTS.—For purposes of this title—

"(A) a trust described in paragraph (1) shall be treated as an organization exempt from taxation under section 501(a), and

"(B) notwithstanding any other provision of this title, amounts in the trust shall be includible in the gross income of participants and beneficiaries only to the extent, and at the time, provided in this section.

"(3) CUSTODIAL ACCOUNTS AND CONTRACTS.—For purposes of this subsection, custodial accounts and contracts described in section 401(f) shall be treated as trusts under rules similar to the rules under section 401(f)."

(b) CONFORMING AMENDMENT.—Paragraph (6) of section 457(b) is amended by inserting "except as provided in subsection (g)," before "which provides that".

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to assets and income described in section 457(b)(6) of the Internal Revenue Code of 1986 held by a plan on and after the date of the enactment of this Act.

(2) TRANSITION RULE.—In the case of assets and income described in paragraph (1) held by a plan on the date of the enactment of this Act, a trust need not be established by reason of the amendments made by this section before January 1, 1999.

SEC. 1449. TRANSITION RULE FOR COMPUTING MAXIMUM BENEFITS UNDER SECTION 415 LIMITATIONS.

(a) IN GENERAL.—Subparagraph (A) of section 767(d)(3) of the Uruguay Round Agreements Act is amended to read as follows:

"(A) EXCEPTION.—A plan that was adopted and in effect before December 8, 1994, shall not be required to apply the amendments made by subsection (b) with respect to benefits accrued before the earlier of—

"(i) the later of the date a plan amendment applying such amendment is adopted or made effective, or

"(ii) the first day of the first limitation year beginning after December 31, 1999.

Determinations under section 415(b)(2)(E) of the Internal Revenue Code of 1986 before such earlier date shall be made with respect to such benefits on the basis of such section as in effect on December 7, 1994 (except that the modification made by section 1449(b) of the Small Business Job Protection Act of 1996 shall be taken into account), and the provisions of the plan as in effect on December 7, 1994, but only if such provisions of the plan meet the requirements of such section (as so in effect)."

(b) MODIFICATION OF CERTAIN ASSUMPTIONS FOR ADJUSTING BENEFITS OF DEFINED BENEFIT PLANS FOR EARLY RETIREES.—Subparagraph (E) of section 415(b)(2) (relating to limitation on certain assumptions) is amended—

(1) by striking "Except as provided in clause (ii), for purposes of adjusting any benefit or limitation under subparagraph (B) or (C)," in clause (i) and inserting "For purposes of adjusting any limitation under subparagraph (C) and, except as provided in clause (ii), for purposes of adjusting any benefit under subparagraph (B),", and

(2) by striking "For purposes of adjusting the benefit or limitation of any form of benefit subject to section 417(e)(3)," in clause (ii) and inserting "For purposes of adjusting any benefit under subparagraph (B) for any form of benefit subject to section 417(e)(3),".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect as if included in the provisions of section 767 of the Uruguay Round Agreements Act.

(d) TRANSITIONAL RULE.—In the case of a plan that was adopted and in effect before December 8, 1994, if—

(1) a plan amendment was adopted or made effective on or before the date of the enactment of this Act applying the amendments made by section 767 of the Uruguay Round Agreements Act, and

(2) within 1 year after the date of the enactment of this Act, a plan amendment is adopted which repeals the amendment referred to in paragraph (1),

the amendment referred to in paragraph (1) shall not be taken into account in applying section 767(d)(3)(A) of the Uruguay Round Agreements Act, as amended by subsection (a).

SEC. 1450. MODIFICATIONS OF SECTION 403(b).

(a) MULTIPLE SALARY REDUCTION AGREEMENTS PERMITTED.—

(1) GENERAL RULE.—For purposes of section 403(b) of the Internal Revenue Code of 1986, the frequency that an employee is permitted to enter into a salary reduction agreement, the salary to which such an agreement may apply, and the ability to revoke such an agreement shall be determined under the rules applicable to cash or deferred elections under section 401(k) of such Code.

(2) EFFECTIVE DATE.—This subsection shall apply to taxable years beginning after December 31, 1995.

(b) TREATMENT OF INDIAN TRIBAL GOVERNMENTS.—

(1) IN GENERAL.—In the case of any contract purchased in a plan year beginning before January 1, 1995, section 403(b) of the Internal Revenue Code of 1986 shall be applied as if any reference to an employer described in section 501(c)(3) of the Internal Revenue Code of 1986 which is exempt from tax under section 501 of such Code included a reference to an employer which is an Indian tribal government (as defined by section 7701(a)(40) of such Code), a subdivision of an Indian tribal government (determined in accordance with section 7871(d) of such Code), an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of the foregoing.

(2) ROLLOVERS.—Solely for purposes of applying section 403(b)(8) of such Code to a contract to which paragraph (1) applies, a qualified cash or deferred arrangement under section 401(k) of such Code shall be treated as if it were a plan or contract described in clause (ii) of section 403(b)(8)(A) of such Code.

(c) ELECTIVE DEFERRALS.—

(1) IN GENERAL.—Subparagraph (E) of section 403(b)(1) is amended to read as follows:

"(E) in the case of a contract purchased under a salary reduction agreement, the contract meets the requirements of section 401(a)(30),".

(2) EFFECTIVE DATE.—The amendment made by this subsection shall apply to years beginning after December 31, 1995, except a contract shall not be required to meet any change in any requirement by reason of such amendment before the 90th day after the date of the enactment of this Act.

SEC. 1451. WAIVER OF MINIMUM PERIOD FOR JOINT AND SURVIVOR ANNUITY EXPLANATION BEFORE ANNUITY STARTING DATE.

(a) GENERAL RULE.—For purposes of section 417(a)(3)(A) of the Internal Revenue Code of 1986 (relating to plan to provide written explanations), the minimum period prescribed by the Secretary of the Treasury between the date that the explanation referred to in such section is provided and the annuity starting date shall not apply if waived by the participant and, if applicable, the participant's spouse.

(b) EFFECTIVE DATE.—Subsection (a) shall apply to plan years beginning after December 31, 1996.

SEC. 1452. REPEAL OF LIMITATION IN CASE OF DEFINED BENEFIT PLAN AND DEFINED CONTRIBUTION PLAN FOR SAME EMPLOYEE; EXCESS DISTRIBUTIONS.

(a) IN GENERAL.—Section 415(e) is repealed.

(b) EXCESS DISTRIBUTIONS.—Section 4980A is amended by adding at the end the following new subsection:

"(g) LIMITATION ON APPLICATION.—This section shall not apply to distributions during years beginning after December 31, 1995, and before January 1, 1999, and such distributions shall be treated as made first from amounts not described in subsection (f)."

(c) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 415(a) is amended—

(A) by adding "or" at the end of subparagraph (A),

(B) by striking ", or" at the end of subparagraph (B) and inserting a period, and

(C) by striking subparagraph (C).

(2) Subparagraph (B) of section 415(b)(5) is amended by striking "and subsection (e)".

(3) Paragraph (1) of section 415(f) is amended by striking "subsections (b), (c), and (e)" and inserting "subsections (b) and (c)".

(4) Subsection (g) of section 415 is amended by striking "subsections (e) and (f)" in the last sentence and inserting "subsection (f)".

(5) Clause (i) of section 415(k)(2)(A) is amended to read as follows:

"(i) any contribution made directly by an employee under such an arrangement shall not be treated as an annual addition for purposes of subsection (c), and".

(6) Clause (ii) of section 415(k)(2)(A) is amended by striking "subsections (c) and (e)" and inserting "subsection (c)".

(7) Section 416 is amended by striking subsection (h).

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to limitation years beginning after December 31, 1998.

(2) EXCESS DISTRIBUTIONS.—The amendment made by subsection (b) shall apply to years beginning after December 31, 1995.

SEC. 1453. TAX ON PROHIBITED TRANSACTIONS.

(a) IN GENERAL.—Section 4975(a) is amended by striking "5 percent" and inserting "10 percent".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to prohibited transactions occurring after the date of the enactment of this Act.

SEC. 1454. TREATMENT OF LEASED EMPLOYEES.

(a) GENERAL RULE.—Subparagraph (C) of section 414(n)(2) (defining leased employee) is amended to read as follows:

"(C) such services are performed under primary direction or control by the recipient."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to years beginning after December 31, 1996, but shall not apply to any relationship determined under an Internal Revenue Service ruling issued before the date of the enactment of this Act pursuant to section 414(n)(2)(C) of the Internal Revenue Code of 1986 (as in effect on the day before such date) not to involve a leased employee.

SEC. 1455. UNIFORM PENALTY PROVISIONS TO APPLY TO CERTAIN PENSION REPORTING REQUIREMENTS.

(a) PENALTIES.—

(1) STATEMENTS.—Paragraph (1) of section 6724(d) is amended by striking "and" at the end of subparagraph (A), by striking the period at the end of subparagraph (B) and inserting ", and", and by inserting after subparagraph (B) the following new subparagraph:

"(C) any statement of the amount of payments to another person required to be made to the Secretary under—

"(i) section 408(i) (relating to reports with respect to individual retirement accounts or annuities), or

"(ii) section 6047(d) (relating to reports by employers, plan administrators, etc.)."

(2) REPORTS.—Paragraph (2) of section 6724(d), as amended by section 1116, is amended by striking "or" at the end of subparagraph (T), by striking the period at the end of subparagraph (U) and inserting a comma, and by inserting after subparagraph (U) the following new subparagraphs:

"(V) section 408(i) (relating to reports with respect to individual retirement plans) to any person other than the Secretary with respect to the amount of payments made to such person, or

"(W) section 6047(d) (relating to reports by plan administrators) to any person other than the Secretary with respect to the amount of payments made to such person."

(b) MODIFICATION OF REPORTABLE DESIGNATED DISTRIBUTIONS.—

(1) SECTION 408.—Subsection (i) of section 408 (relating to individual retirement account reports) is amended by inserting "aggregating $10 or more in any calendar year" after "distributions".

(2) SECTION 6047.—Paragraph (1) of section 6047(d) (relating to reports by employers, plan administrators, etc.) is amended by adding at the end the following new sentence: "No return or report may be required under the preceding sentence with respect to distributions to any person during any year unless such distributions aggregate $10 or more."

(c) QUALIFYING ROLLOVER DISTRIBUTIONS.—Section 6652(i) is amended—

(1) by striking "the $10" and inserting "$100", and

(2) by striking "$5,000" and inserting "$50,000".

(d) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 6047(f) is amended to read as follows:

"(1) For provisions relating to penalties for failures to file returns and reports required under this section, see sections 6652(e), 6721, and 6722."

(2) Subsection (e) of section 6652 is amended by adding at the end the following new sentence: "This subsection shall not apply to any return or statement which is an information return described in section 6724(d)(1)(C)(ii) or a payee statement described in section 6724(d)(2)(W)."

(3) Subsection (a) of section 6693 is amended by adding at the end the following new sentence: "This subsection shall not apply to any report which is an information return described in section 6724(d)(1)(C)(i) or a payee statement described in section 6724(d)(2)(V)."

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to returns, reports, and other statements the due date for which (determined without regard to extensions) is after December 31, 1996.

SEC. 1456. RETIREMENT BENEFITS OF MINISTERS NOT SUBJECT TO TAX ON NET EARNINGS FROM SELF-EMPLOYMENT.

(a) IN GENERAL.—Section 1402(a)(8) (defining net earning from self-employment) is amended by inserting ", but shall not include in such net earnings from self-employment the rental value of any parsonage (whether or not excludable under section 107) provided after the individual retires, or any other retirement benefit received by such individual from a church plan (as defined in section 414(e)) after the individual retires" before the semicolon at the end.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning before, on, or after December 31, 1994.

SEC. 1457. DATE FOR ADOPTION OF PLAN AMENDMENTS.

If any amendment made by this subtitle requires an amendment to any plan or annuity contract, such amendment shall not be required to be made before the first day of the first plan year beginning on or after January 1, 1997, if—

(1) during the period after such amendment takes effect and before such first plan year, the plan or contract is operated in accordance with the requirements of such amendment, and

(2) such amendment applies retroactively to such period.

In the case of a governmental plan (as defined in section 414(d) of the Internal Revenue Code of 1986), this section shall be applied by substituting "1999" for "1997".

Subtitle E—Foreign Simplification

SEC. 1501. REPEAL OF INCLUSION OF CERTAIN EARNINGS INVESTED IN EXCESS PASSIVE ASSETS.

(a) IN GENERAL.—

(1) REPEAL OF INCLUSION.—Paragraph (1) of section 951(a) (relating to amounts included in gross income of United States shareholders) is amended by striking subparagraph (C), by striking "; and" at the end of subparagraph (B) and inserting a period, and by adding "and" at the end of subparagraph (A).

(2) REPEAL OF INCLUSION AMOUNT.—Section 956A (relating to earnings invested in excess passive assets) is repealed.

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 956(b) is amended to read as follows:

"(1) APPLICABLE EARNINGS.—For purposes of this section, the term 'applicable earnings' means, with respect to any controlled foreign corporation, the sum of—

"(A) the amount (not including a deficit) referred to in section 316(a)(1), and

"(B) the amount referred to in section 316(a)(2),

but reduced by distributions made during the taxable year."

(2) Paragraph (3) of section 956(b) is amended to read as follows:

"(3) SPECIAL RULE WHERE CORPORATION CEASES TO BE CONTROLLED FOREIGN CORPORATION.—If any foreign corporation ceases to be a controlled foreign corporation during any taxable year—

"(A) the determination of any United States shareholder's pro rata share shall be made on the basis of stock owned (within the meaning of section 958(a)) by such shareholder on the last day during the taxable year on which the foreign corporation is a controlled foreign corporation,

"(B) the average referred to in subsection (a)(1)(A) for such taxable year shall be determined by only taking into account quarters ending on or before such last day, and

"(C) in determining applicable earnings, the amount taken into account by reason of being described in paragraph (2) of section 316(a) shall be the portion of the amount so described which is allocable (on a pro rata basis) to the part of such year during which the corporation is a controlled foreign corporation."

(3) Subsection (a) of section 959 (relating to exclusion from gross income of previously taxed earnings and profits) is amended by adding "or" at the end of paragraph (1), by striking "or" at the end of paragraph (2), and by striking paragraph (3).

(4) Subsection (a) of section 959 is amended by striking "paragraphs (2) and (3)" in the last sentence and inserting "paragraph (2)".

(5) Subsection (c) of section 959 is amended by adding at the end the following flush sentence:

"References in this subsection to section 951(a)(1)(C) and subsection (a)(3) shall be treated as references to such provisions as in effect on the day before the date of the enactment of the Small Business Job Protection Act of 1996."

(6) Paragraph (1) of section 959(f) is amended to read as follows:

"(1) IN GENERAL.—For purposes of this section, amounts that would be included under subparagraph (B) of section 951(a)(1) (determined without regard to this section) shall be treated as attributable first to earnings described in subsection (c)(2), and then to earnings described in subsection (c)(3)."

(7) Paragraph (2) of section 959(f) is amended by striking "subparagraphs (B) and (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(8) Subsection (b) of section 989 is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(9) Paragraph (9) of section 1297(b) is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(10) Subsections (d)(3)(B) and (e)(2)(B)(ii) of section 1297 are each amended by striking "or section 956A".

(c) CLERICAL AMENDMENT.—The table of sections for subpart F of part III of subchapter N of chapter 1 is amended by striking the item relating to section 956A.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years of foreign corporations beginning after December 31, 1996, and to taxable years of United States shareholders within which or with which such taxable years of foreign corporations end.

Subtitle F—Revenue Offsets

SEC. 1601. TERMINATION OF PUERTO RICO AND POSSESSION TAX CREDIT.

(a) IN GENERAL.—Section 936 is amended by adding at the end the following new subsection:

"(j) TERMINATION.—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, this section shall not apply to any taxable year beginning after December 31, 1995.

"(2) TRANSITION RULES FOR ACTIVE BUSINESS INCOME CREDIT.—Except as provided in paragraph (3)—

"(A) ECONOMIC ACTIVITY CREDIT.—In the case of an existing credit claimant—

"(i) with respect to a possession other than Puerto Rico, and

"(ii) to which subsection (a)(4)(B) does not apply,

the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 2002.

"(B) SPECIAL RULE FOR REDUCED CREDIT.—

"(i) IN GENERAL.—In the case of an existing credit claimant to which subsection (a)(4)(B) applies, the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 1998.

"(ii) ELECTION IRREVOCABLE AFTER 1997.—An election under subsection (a)(4)(B)(iii) which is in effect for the taxpayer's last taxable year beginning before 1997 may not be revoked unless it is revoked for the taxpayer's first taxable year beginning in 1997 and all subsequent taxable years.

"(C) ECONOMIC ACTIVITY CREDIT FOR PUERTO RICO.—

"For economic activity credit for Puerto Rico, see section 30A.

"(3) ADDITIONAL RESTRICTED CREDIT.—

"(A) IN GENERAL.—In the case of an existing credit claimant—

"(i) the credit under subsection (a)(1)(A) shall be allowed for the period beginning with the first taxable year after the last taxable year to which subparagraph (A) or (B) of paragraph (2), whichever is appropriate, applied and ending with the last taxable year beginning before January 1, 2006, except that

"(ii) the aggregate amount of taxable income taken into account under subsection (a)(1)(A) for any such taxable year shall not exceed the adjusted base period income of such claimant.

"(B) COORDINATION WITH SUBSECTION (a)(4).—The amount of income described in subsection (a)(1)(A) which is taken into account in applying subsection (a)(4) shall be such income as reduced under this paragraph.

"(4) ADJUSTED BASE PERIOD INCOME.—For purposes of paragraph (3)—

"(A) IN GENERAL.—The term 'adjusted base period income' means the average of the inflation-adjusted possession incomes of the corporation for each base period year.

"(B) INFLATION-ADJUSTED POSSESSION INCOME.—For purposes of subparagraph (A), the inflation-adjusted possession income of any corporation for any base period year shall be an amount equal to the sum of—

"(i) the possession income of such corporation for such base period year, plus

"(ii) such possession income multiplied by the inflation adjustment percentage for such base period year.

"(C) INFLATION ADJUSTMENT PERCENTAGE.—For purposes of subparagraph (B), the inflation adjustment percentage for any base period year means the percentage (if any) by which—

"(i) the CPI for 1995, exceeds

"(ii) the CPI for the calendar year in which the base period year for which the determination is being made ends.

For purposes of the preceding sentence, the CPI for any calendar year is the CPI (as defined in section 1(f)(5)) for such year under section 1(f)(4).

"(D) INCREASE IN INFLATION ADJUSTMENT PERCENTAGE FOR GROWTH DURING BASE YEARS.—The inflation adjustment percentage (determined under subparagraph (C) without regard to this subparagraph) for each of the 5 taxable years referred to in paragraph (5)(A) shall be increased by—

"(i) 5 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1995;

"(ii) 10.25 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1994;

"(iii) 15.76 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1993;

"(iv) 21.55 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1992; and

"(v) 27.63 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1991.

"(5) BASE PERIOD YEAR.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'base period year' means each of 3 taxable years which are among the 5 most recent taxable years of the corporation ending before October 14, 1995, determined by disregarding—

"(i) one taxable year for which the corporation had the largest inflation-adjusted possession income, and

"(ii) one taxable year for which the corporation had the smallest inflation-adjusted possession income.

"(B) CORPORATIONS NOT HAVING SIGNIFICANT POSSESSION INCOME THROUGHOUT 5-YEAR PERIOD.—

"(i) IN GENERAL.—If a corporation does not have significant possession income for each of the most recent 5 taxable years ending before October 14, 1995, then, in lieu of applying subparagraph (A), the term 'base period year' means only those taxable years (of such 5 taxable years) for which the corporation has significant possession income; except that, if such corporation has significant possession income for 4 of such 5 taxable years, the rule of subparagraph (A)(ii) shall apply.

"(ii) SPECIAL RULE.—If there is no year (of such 5 taxable years) for which a corporation has significant possession income—

"(I) the term 'base period year' means the first taxable year ending on or after October 14, 1995, but

"(II) the amount of possession income for such year which is taken into account under paragraph (4) shall be the amount which would be determined if such year were a short taxable year ending on September 30, 1995.

"(iii) SIGNIFICANT POSSESSION INCOME.—For purposes of this subparagraph, the term 'significant possession income' means possession income which exceeds 2 percent of the possession income of the taxpayer for the taxable year (of the period of 6 taxable years ending with the first taxable year ending on or after October 14, 1995) having the greatest possession income.

"(C) ELECTION TO USE ONE BASE PERIOD YEAR.—

"(i) IN GENERAL.—At the election of the taxpayer, the term 'base period year' means—

"(I) only the last taxable year of the corporation ending in calendar year 1992, or

"(II) a deemed taxable year which includes the first ten months of calendar year 1995.

"(ii) BASE PERIOD INCOME FOR 1995.—In determining the adjusted base period income of the corporation for the deemed taxable year under clause (i)(II), the possession income shall be annualized and shall be determined without regard to any extraordinary item.

"(iii) ELECTION.—An election under this subparagraph by any possession corporation may be made only for the corporation's first taxable year beginning after December 31, 1995, for which it is a possession corporation. The rules of subclauses (II) and (III) of subsection (a)(4)(B)(iii) shall apply to the election under this subparagraph.

"(D) ACQUISITIONS AND DISPOSITIONS.—Rules similar to the rules of subparagraphs (A) and (B) of section 41(f)(3) shall apply for purposes of this subsection.

"(6) POSSESSION INCOME.—For purposes of this subsection, the term 'possession income' means, with respect to any possession, the income referred to in subsection (a)(1)(A) determined with respect to that possession. In no event shall possession income be treated as being less than zero.

"(7) SHORT YEARS.—If the current year or a base period year is a short taxable year, the application of this subsection shall be made with such annualizations as the Secretary shall prescribe.

"(8) SPECIAL RULES FOR CERTAIN POSSESSIONS.—

"(A) IN GENERAL.—In the case of an existing credit claimant with respect to an applicable possession, this section (other than the preceding paragraphs of this subsection) shall apply to such claimant with respect to such applicable possession for taxable years beginning after December 31, 1995, and before January 1, 2006.

"(B) APPLICABLE POSSESSION.—For purposes of this paragraph, the term 'applicable possession' means Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.

"(9) EXISTING CREDIT CLAIMANT.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'existing credit claimant' means a corporation—

"(i) which was actively conducting a trade or business in a possession on October 13, 1995, and

"(ii) with respect to which an election under this section is in effect for the corporation's taxable year which includes October 13, 1995.

"(B) NEW LINES OF BUSINESS PROHIBITED.—If, after October 13, 1995, a corporation which would (but for this subparagraph) be an existing credit claimant adds a substantial new line of business, such corporation shall cease to be treated as an existing credit claimant as of the close of the taxable year ending before the date of such addition.

"(C) BINDING CONTRACT EXCEPTION.—If, on October 13, 1995, and at all times thereafter, there is in effect with respect to a corporation a binding contract for the acquisition of assets to be used in, or for the sale of assets to be produced from, a trade or business, the corporation shall be treated for purposes of this paragraph as actively conducting such trade or business on October 13, 1995. The preceding sentence shall not apply if such trade or business is not actively conducted before January 1, 1996.

"(10) SEPARATE APPLICATION TO EACH POSSESSION.—For purposes of determining—

"(A) whether a taxpayer is an existing credit claimant, and

"(B) the amount of the credit allowed under this section,

this subsection (and so much of this section as relates to this subsection) shall be applied separately with respect to each possession."

(b) ECONOMIC ACTIVITY CREDIT FOR PUERTO RICO.—

(1) IN GENERAL.—Subpart B of part IV of subchapter A of chapter 1 is amended by adding at the end the following new section:

"SEC. 30A. PUERTO RICAN ECONOMIC ACTIVITY CREDIT.

"(a) ALLOWANCE OF CREDIT.—

"(1) IN GENERAL.—Except as otherwise provided in this section, if the conditions of both paragraph (1) and paragraph (2) of subsection (b) are satisfied with respect to a qualified domestic corporation, there shall be allowed as a credit against the tax imposed by this chapter an amount equal to the portion of the tax which is attributable to the taxable income, from sources without the United States, from—

"(A) the active conduct of a trade or business within Puerto Rico, or

"(B) the sale or exchange of substantially all of the assets used by the taxpayer in the active conduct of such trade or business.

In the case of any taxable year beginning after December 31, 2001, the aggregate amount of taxable income taken into account under the preceding sentence (and in applying subsection (d)) shall not exceed the adjusted base period income of such corporation, as determined in the same manner as under section 936(j).

"(2) QUALIFIED DOMESTIC CORPORATION.—For purposes of paragraph (1), the term 'qualified domestic corporation' means a domestic corporation—

"(A) which is an existing credit claimant with respect to Puerto Rico, and

"(B) with respect to which section 936(a)(4)(B) does not apply for the taxable year.

"(3) SEPARATE APPLICATION.—For purposes of determining—

"(A) whether a taxpayer is an existing credit claimant with respect to Puerto Rico, and

"(B) the amount of the credit allowed under this section,

this section (and so much of section 936 as relates to this section) shall be applied separately with respect to Puerto Rico.

"(b) CONDITIONS WHICH MUST BE SATISFIED.—The conditions referred to in subsection (a) are—

"(1) 3-YEAR PERIOD.—If 80 percent or more of the gross income of the qualified domestic corporation for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within a possession (determined without regard to section 904(f)).

"(2) TRADE OR BUSINESS.—If 75 percent or more of the gross income of the qualified domestic corporation for such period or such part thereof was derived from the active conduct of a trade or business within a possession.

"(c) CREDIT NOT ALLOWED AGAINST CERTAIN TAXES.—The credit provided by subsection (a) shall not be allowed against the tax imposed by—

"(1) section 59A (relating to environmental tax),

"(2) section 531 (relating to the tax on accumulated earnings),

"(3) section 541 (relating to personal holding company tax), or

"(4) section 1351 (relating to recoveries of foreign expropriation losses).

"(d) LIMITATIONS ON CREDIT FOR ACTIVE BUSINESS INCOME.—The amount of the credit determined under subsection (a) for any taxable year shall not exceed the sum of the following amounts:

"(1) 60 percent of the sum of—

"(A) the aggregate amount of the qualified domestic corporation's qualified possession wages for such taxable year, plus

"(B) the allocable employee fringe benefit expenses of the qualified domestic corporation for such taxable year.

"(2) The sum of—

"(A) 15 percent of the depreciation allowances for the taxable year with respect to short-life qualified tangible property,

"(B) 40 percent of the depreciation allowances for the taxable year with respect to medium-life qualified tangible property, and

"(C) 65 percent of the depreciation allowances for the taxable year with respect to long-life qualified tangible property.

"(3) If the qualified domestic corporation does not have an election to use the method described in section 936(h)(5)(C)(ii) (relating to profit split) in effect for the taxable year, the amount of the qualified possession income taxes for the taxable year allocable to nonsheltered income.

"(e) ADMINISTRATIVE PROVISIONS.—For purposes of this title—

"(1) the provisions of section 936 (including any applicable election thereunder) shall apply in the same manner as if the credit under this section were a credit under section 936(a)(1)(A) for a domestic corporation to which section 936(a)(4)(A) applies,

"(2) the credit under this section shall be treated in the same manner as the credit under section 936, and

"(3) a corporation to which this section applies shall be treated in the same manner as if it were a corporation electing the application of section 936.

"(f) DEFINITIONS.—For purposes of this section, any term used in this section which is also used in section 936 shall have the same meaning given such term by section 936.

"(g) APPLICATION OF SECTION.—This section shall apply to taxable years beginning after December 31, 1995, and before January 1, 2006."

(2) CONFORMING AMENDMENTS.—

(A) Paragraph (1) of section 55(c) is amended by striking "and the section 936 credit allowable under section 27(b)" and inserting ", the section 936 credit allowable under section 27(b), and the Puerto Rican economic activity credit under section 30A".

(B) Subclause (I) of section 56(g)(4)(C)(ii) is amended—

(i) by inserting "30A," before "936", and

(ii) by striking "and (i)" and inserting ", (i), and (j)".

(C) Clause (iii) of section 56(g)(4)(C) is amended by adding at the end the following new subclause:

"(VI) APPLICATION TO SECTION 30A CORPORATIONS.—References in this clause to section 936 shall be treated as including references to section 30A."

(D) Subsection (b) of section 59 is amended by striking "section 936," and all that follows and inserting "section 30A or 936, alternative minimum taxable income shall not include any income with respect to which a credit is determined under section 30A or 936.".

(E) The table of sections for subpart B of part IV of subchapter A of chapter 1 is amended by adding at the end the following new item:

"Sec. 30A. Puerto Rican economic activity credit."

(F)(i) The heading for subpart B of part IV of subchapter A of chapter 1 is amended to read as follows:

"Subpart B—Other Credits".

(ii) The table of subparts for part IV of subchapter A of chapter 1 is amended by striking the item relating to subpart B and inserting the following new item:

"Subpart B. Other credits."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1995.

SEC. 1602. REPEAL OF EXCLUSION FOR INTEREST ON LOANS USED TO ACQUIRE EMPLOYER SECURITIES.

(a) IN GENERAL.—Section 133 (relating to interest on certain loans used to acquire employer securities) is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (B) of section 291(e)(1) is amended by striking clause (iv) and by redesignating clause (v) as clause (iv).

(2) Section 812 is amended by striking subsection (g).

(3) Paragraph (5) of section 852(b) is amended by striking subparagraph (C).

(4) Paragraph (2) of section 4978(b) is amended by striking subparagraph (A) and all that follows and inserting the following:

"(A) first from qualified securities to which section 1042 applied acquired during the 3-year period ending on the date of the disposition, beginning with the securities first so acquired, and

"(B) then from any other employer securities.

If subsection (d) applies to a disposition, the disposition shall be treated as made from employer securities in the opposite order of the preceding sentence.".

(5)(A) Section 4978B (relating to tax on disposition of employer securities to which section 133 applied) is hereby repealed.

(B) The table of sections for chapter 43 is amended by striking the item relating to section 4978B.

(6) Subsection (e) of section 6047 is amended by striking paragraphs (1), (2), and (3) and inserting the following new paragraphs:

"(1) any employer maintaining, or the plan administrator (within the meaning of section 414(g)) of, an employee stock ownership plan which holds stock with respect to which section 404(k) applies to dividends paid on such stock, or

"(2) both such employer or plan administrator,".

(7) Subsection (f) of section 7872 is amended by striking paragraph (12).

(8) The table of sections for part III of subchapter B of chapter 1 is amended by striking the item relating to section 133.

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to loans made after October 13, 1995.

(2) REFINANCINGS.—The amendments made by this section shall not apply to loans made after October 13, 1995, to refinance securities acquisition loans (determined without regard to section 133(b)(1)(B) of the Internal Revenue Code of 1986, as in effect on the day before the date of the enactment of this Act) made on or before such date or to refinance loans described in this paragraph if—

(A) the refinancing loans meet the requirements of section 133 of such Code (as so in effect),

(B) immediately after the refinancing the principal amount of the loan resulting from the refinancing does not exceed the principal amount of the refinanced loan (immediately before the refinancing), and

(C) the term of such refinancing loan does not extend beyond the last day of the term of the original securities acquisition loan.

For purposes of this paragraph, the term "securities acquisition loan" includes a loan from a corporation to an employee stock ownership plan described in section 133(b)(3) of such Code (as so in effect).

(3) EXCEPTION.—Any loan made pursuant to a binding written contract in effect on October 13, 1995, and at all times thereafter before such loan is made, shall be treated for purposes of paragraphs (1) and (2) as a loan made before such date.

SEC. 1603. CERTAIN AMOUNTS DERIVED FROM FOREIGN CORPORATIONS TREATED AS UNRELATED BUSINESS TAXABLE INCOME.

(a) GENERAL RULE.—Subsection (b) of section 512 (relating to modifications) is amended by adding at the end the following new paragraph:

"(17) TREATMENT OF CERTAIN AMOUNTS DERIVED FROM FOREIGN CORPORATIONS.—

"(A) IN GENERAL.—Notwithstanding paragraph (1), any amount included in gross income under section 951(a)(1)(A) shall be included as an item of gross income derived from an unrelated trade or business to the extent the amount so included is attributable to insurance income (as defined in section 953) which, if derived directly by the organization, would be treated as gross income from an unrelated trade or business. There shall be allowed all deductions directly connected with amounts included in gross income under the preceding sentence.

"(B) EXCEPTION.—Subparagraph (A) shall not apply to income attributable to a policy of insurance or reinsurance with respect to which the person (directly or indirectly) insured is—

"(i) such organization,

"(ii) an affiliate of such organization which is exempt from tax under section 501(a), or

"(iii) a director or officer of, or an individual who (directly or indirectly) performs services for, such organization or affiliate but only if the insurance covers primarily risks associated with the performance of services in connection with such organization or affiliate.

For purposes of this subparagraph, the determination as to whether an entity is an affiliate of an organization shall be made under rules similar to the rules of section 168(h)(4)(B).

"(C) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this paragraph, including regulations for the application of this paragraph in the case of income paid through 1 or more entities or between 2 or more chains of entities."

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to amounts included in gross income in any taxable year beginning after December 31, 1995.

SEC. 1604. DEPRECIATION UNDER INCOME FORECAST METHOD.

(a) GENERAL RULE.—Section 167 (relating to depreciation) is amended by redesignating subsection (g) as subsection (h) and by inserting after subsection (f) the following new subsection:

"(g) DEPRECIATION UNDER INCOME FORECAST METHOD.—

"(1) IN GENERAL.—If the depreciation deduction allowable under this section to any taxpayer with respect to any property is determined under the income forecast method or any similar method—

"(A) the income from the property to be taken into account in determining the depreciation deduction under such method shall be equal to the amount of income earned in connection with the property before the close of the 10th taxable year following the taxable year in which the property was placed in service,

"(B) the adjusted basis of the property shall only include amounts with respect to which the requirements of section 461(h) are satisfied,

"(C) the depreciation deduction under such method for the 10th taxable year beginning after the taxable year in which the property was placed in service shall be equal to the adjusted basis of such property as of the beginning of such 10th taxable year, and

"(D) such taxpayer shall pay (or be entitled to receive) interest computed under the look-back method of paragraph (2) for any recomputation year.

"(2) LOOK-BACK METHOD.—The interest computed under the look-back method of this paragraph for any recomputation year shall be determined by—

"(A) first determining the depreciation deductions under this section with respect to such property which would have been allowable for prior taxable

years if the determination of the amounts so allowable had been made on the basis of the sum of the following (instead of the estimated income from such property)—

"(i) the actual income earned in connection with such property for periods before the close of the recomputation year, and

"(ii) an estimate of the future income to be earned in connection with such property for periods after the recomputation year and before the close of the 10th taxable year following the taxable year in which the property was placed in service,

"(B) second, determining (solely for purposes of computing such interest) the overpayment or underpayment of tax for each such prior taxable year which would result solely from the application of subparagraph (A), and

"(C) then using the adjusted overpayment rate (as defined in section 460(b)(7)), compounded daily, on the overpayment or underpayment determined under subparagraph (B).

For purposes of the preceding sentence, any cost incurred after the property is placed in service (which is not treated as a separate property under paragraph (5)) shall be taken into account by discounting (using the Federal mid-term rate determined under section 1274(d) as of the time such cost is incurred) such cost to its value as of the date the property is placed in service. The taxpayer may elect with respect to any property to have the preceding sentence not apply to such property.

"(3) EXCEPTION FROM LOOK-BACK METHOD.—Paragraph (1)(D) shall not apply with respect to any property which, when placed in service by the taxpayer, had a basis of $100,000 or less.

"(4) RECOMPUTATION YEAR.—For purposes of this subsection, except as provided in regulations, the term 'recomputation year' means, with respect to any property, the 3d and the 10th taxable years beginning after the taxable year in which the property was placed in service, unless the actual income earned in connection with the property for the period before the close of such 3d or 10th taxable year is within 10 percent of the income earned in connection with the property for such period which was taken into account under paragraph (1)(A).

"(5) SPECIAL RULES.—

"(A) CERTAIN COSTS TREATED AS SEPARATE PROPERTY.—For purposes of this subsection, the following costs shall be treated as separate properties:

"(i) Any costs incurred with respect to any property after the 10th taxable year beginning after the taxable year in which the property was placed in service.

"(ii) Any costs incurred after the property is placed in service and before the close of such 10th taxable year if such costs are significant and give rise to a significant increase in the income from the property which was not included in the estimated income from the property.

"(B) SYNDICATION INCOME FROM TELEVISION SERIES.—In the case of property which is an episode in a television series, income from syndicating such series shall not be required to be taken into account under this subsection before the earlier of—

"(i) the 4th taxable year beginning after the date the first episode in such series is placed in service, or

"(ii) the earliest taxable year in which the taxpayer has an arrangement relating to the future syndication of such series.

"(C) SPECIAL RULES FOR FINANCIAL EXPLOITATION OF CHARACTERS, ETC.—For purposes of this subsection, in the case of television and motion picture films, the income from the property shall include income from the exploitation of characters, designs, scripts, scores, and other incidental income associated with such films, but only to the extent that such income is earned in connection with the ultimate use of such items by, or the ultimate sale of merchandise to, persons who are not related persons (within the meaning of section 267(b)) to the taxpayer.

"(D) COLLECTION OF INTEREST.—For purposes of subtitle F (other than sections 6654 and 6655), any interest required to be paid by the taxpayer under paragraph (1) for any recomputation year shall be treated as an increase in the tax imposed by this chapter for such year.

"(E) DETERMINATIONS.—For purposes of paragraph (2), determinations of the amount of income earned in connection with any property shall be made in the same manner as for purposes of applying the income forecast method; except that any income from the disposition of such property shall be taken into account.

"(F) TREATMENT OF PASS-THRU ENTITIES.—Rules similar to the rules of section 460(b)(4) shall apply for purposes of this subsection."

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendment made by subsection (a) shall apply to property placed in service after September 13, 1995.

(2) BINDING CONTRACTS.—The amendment made by subsection (a) shall not apply to any property produced or acquired by the taxpayer pursuant to a written contract which was binding on September 13, 1995, and at all times thereafter before such production or acquisition.

SEC. 1605. REPEAL OF EXCLUSION FOR PUNITIVE DAMAGES AND FOR DAMAGES NOT ATTRIBUTABLE TO PHYSICAL INJURIES OR SICKNESS.

(a) IN GENERAL.—Paragraph (2) of section 104(a) (relating to compensation for injuries or sickness) is amended to read as follows:

"(2) the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness;".

(b) EMOTIONAL DISTRESS AS SUCH TREATED AS NOT PHYSICAL INJURY OR PHYSICAL SICKNESS.—Section 104(a) is amended by striking the last sentence and inserting the following new sentence: "For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. The preceding sentence shall not apply to an amount of damages not in excess of the amount paid for medical care (described in subparagraph (A) or (B) of section 213(d)(1)) attributable to emotional distress.".

(c) APPLICATION OF PRIOR LAW FOR STATES IN WHICH ONLY PUNITIVE DAMAGES MAY BE AWARDED IN WRONGFUL DEATH ACTIONS.—Section 104 is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

"(c) APPLICATION OF PRIOR LAW IN CERTAIN CASES.—The phrase '(other than punitive damages)' shall not apply to punitive damages awarded in a civil action—

"(1) which is a wrongful death action, and

"(2) with respect to which applicable State law (as in effect on September 13, 1995 and without regard to any modification after such date) provides, or has been construed to provide by a court of competent jurisdiction pursuant to a decision issued on or before September 13, 1995, that only punitive damages may be awarded in such an action.

This subsection shall cease to apply to any civil action filed on or after the first date on which the applicable State law ceases to provide (or is no longer construed to provide) the treatment described in paragraph (2)."

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to amounts received after June 30, 1996, in taxable years ending after such date.

(2) EXCEPTION.—The amendments made by this section shall not apply to any amount received under a written binding agreement, court decree, or mediation award in effect on (or issued on or before) September 13, 1995.

SEC. 1606. REPEAL OF DIESEL FUEL TAX REBATE TO PURCHASERS OF DIESEL-POWERED AUTOMOBILES AND LIGHT TRUCKS.

(a) IN GENERAL.—Section 6427 (relating to fuels not used for taxable purposes) is amended by striking subsection (g).

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (3) of section 34(a) is amended to read as follows:

"(3) under section 6427 with respect to fuels used for nontaxable purposes or resold during the taxable year (determined without regard to section 6427(k)).".

(2) Paragraphs (1) and (2)(A) of section 6427(i) are each amended—

(A) by striking "(g),", and

(B) by striking "(or a qualified diesel powered highway vehicle purchased)" each place it appears.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to vehicles purchased after the date of the enactment of this Act.

Subtitle G—Technical Corrections

SEC. 1701. COORDINATION WITH OTHER SUBTITLES.

For purposes of applying the amendments made by any subtitle of this title other than this subtitle, the provisions of this subtitle shall be treated as having been enacted immediately before the provisions of such other subtitles.

SEC. 1702. AMENDMENTS RELATED TO REVENUE RECONCILIATION ACT OF 1990.

(a) AMENDMENTS RELATED TO SUBTITLE A.—

(1) Subparagraph (B) of section 59(j)(3) is amended by striking "section 1(i)(3)(B)" and inserting "section 1(g)(3)(B)".

(2) Clause (i) of section 151(d)(3)(C) is amended by striking "joint of a return" and inserting "joint return".

(b) AMENDMENTS RELATED TO SUBTITLE B.—

(1) Paragraph (1) of section 11212(e) of the Revenue Reconciliation Act of 1990 is amended by striking "Paragraph (1) of section 6724(d)" and inserting "Subparagraph (B) of section 6724(d)(1)".

(2)(A) Subparagraph (B) of section 4093(c)(2), as in effect before the amendments made by the Revenue Reconciliation Act of 1993, is amended by inserting before the period "unless such fuel is sold for exclusive use by a State or any political subdivision thereof".

(B) Paragraph (4) of section 6427(l), as in effect before the amendments made by the Revenue Reconciliation Act of 1993, is amended by inserting before the period "unless such fuel was used by a State or any political subdivision thereof".

(3) Paragraph (1) of section 6416(b) is amended by striking "chapter 32 or by section 4051" and inserting "chapter 31 or 32".

(4) Section 7012 is amended—

(A) by striking "production or importation of gasoline" in paragraph (3) and inserting "taxes on gasoline and diesel fuel", and

(B) by striking paragraph (4) and redesignating paragraphs (5) and (6) as paragraphs (4) and (5), respectively.

(5) Subsection (c) of section 5041 is amended by striking paragraph (6) and by inserting the following new paragraphs:

"(6) CREDIT FOR TRANSFEREE IN BOND.—If—

"(A) wine produced by any person would be eligible for any credit under paragraph (1) if removed by such person during the calendar year,

"(B) wine produced by such person is removed during such calendar year by any other person (hereafter in this paragraph referred to as the 'transferee') to whom such wine was transferred in bond and who is liable for the tax imposed by this section with respect to such wine, and

"(C) such producer holds title to such wine at the time of its removal and provides to the transferee such information as is necessary to properly determine the transferee's credit under this paragraph,

then, the transferee (and not the producer) shall be allowed the credit under paragraph (1) which would be allowed to the producer if the wine removed by the transferee had been removed by the producer on that date.

"(7) REGULATIONS.—The Secretary may prescribe such regulations as may be necessary to carry out the purposes of this subsection, including regulations—

"(A) to prevent the credit provided in this subsection from benefiting any person who produces more than 250,000 wine gallons during a calendar year, and

"(B) to assure proper reduction of such credit for persons producing more than 150,000 wine gallons of wine during a calendar year."

(6) Paragraph (3) of section 5061(b) is amended to read as follows:

"(3) section 5041(f),".

(7) Section 5354 is amended by inserting "(taking into account the appropriate amount of credit with respect to such wine under section 5041(c))" after "any one time".

(c) AMENDMENTS RELATED TO SUBTITLE C.—

(1) Paragraph (4) of section 56(g) is amended by redesignating subparagraphs (I) and (J) as subparagraphs (H) and (I), respectively.

(2) Subparagraph (B) of section 6724(d)(1) is amended—

(A) by striking "or" at the end of clause (xii), and

(B) by striking the period at the end of clause (xiii) and inserting ", or".

(3) Subsection (g) of section 6302 is amended by inserting ", 22," after "chapters 21".

(4) The earnings and profits of any insurance company to which section 11305(c)(3) of the Revenue Reconciliation Act of 1990 applies shall be determined without regard to any deduction allowed under such section; except that, for purposes of applying sections 56 and 902, and subpart F of part III of subchapter N of chapter 1 of the Internal Revenue Code of 1986, such deduction shall be taken into account.

(5) Subparagraph (D) of section 6038A(e)(4) is amended—

(A) by striking "any transaction to which the summons relates" and inserting "any affected taxable year", and

(B) by adding at the end thereof the following new sentence: "For purposes of this subparagraph, the term 'affected taxable year' means any taxable year if the determination of the amount of tax imposed for such taxable year is affected by the treatment of the transaction to which the summons relates.".

(6) Subparagraph (A) of section 6621(c)(2) is amended by adding at the end thereof the following new flush sentence:

"The preceding sentence shall be applied without regard to any such letter or notice which is withdrawn by the Secretary.".

(7) Clause (i) of section 6621(c)(2)(B) is amended by striking "this subtitle" and inserting "this title".

(d) AMENDMENTS RELATED TO SUBTITLE D.—

(1) Notwithstanding section 11402(c) of the Revenue Reconciliation Act of 1990, the amendment made by section 11402(b)(1) of such Act shall apply to taxable years ending after December 31, 1989.

(2) Clause (ii) of section 143(m)(4)(C) is amended—

(A) by striking "any month of the 10-year period" and inserting "any year of the 4-year period",

(B) by striking "succeeding months" and inserting "succeeding years", and

(C) by striking "over the remainder of such period (or, if lesser, 5 years)" and inserting "to zero over the succeeding 5 years".

(e) AMENDMENTS RELATED TO SUBTITLE E.—

(1)(A) Clause (ii) of section 56(d)(1)(B) is amended to read as follows:

"(ii) appropriate adjustments in the application of section 172(b)(2) shall be made to take into account the limitation of subparagraph (A)."

(B) For purposes of applying sections 56(g)(1) and 56(g)(3) of the Internal Revenue Code of 1986 with respect to taxable years beginning in 1991 and 1992, the reference in such sections to the alternative tax net operating loss deduction shall be treated as including a reference to the deduction under section 56(h) of such Code as in effect before the amendments made by section 1915 of the Energy Policy Act of 1992.

(2) Clause (i) of section 613A(c)(3)(A) is amended by striking "the table contained in".

(3) Section 6501 is amended—

(A) by striking subsection (m) (relating to deficiency attributable to election under section 44B) and by redesignating subsections (n) and (o) as subsections (m) and (n), respectively, and

(B) by striking "section 40(f) or 51(j)" in subsection (m) (as redesignated by subparagraph (A)) and inserting "section 40(f), 43, or 51(j)".

(4) Subparagraph (C) of section 38(c)(2) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990) is amended by inserting before the period at the end of the first sentence the following: "and without regard to the deduction under section 56(h)".

(5) The amendment made by section 1913(b)(2)(C)(i) of the Energy Policy Act of 1992 shall apply to taxable years beginning after December 31, 1990.

(f) AMENDMENTS RELATED TO SUBTITLE F.—

(1)(A) Section 2701(a)(3) is amended by adding at the end thereof the following new subparagraph:

"(C) VALUATION OF QUALIFIED PAYMENTS WHERE NO LIQUIDATION, ETC. RIGHTS.—In the case of an applicable retained interest which is described in subparagraph (B)(i) but not subparagraph (B)(ii), the value of the distribution right shall be determined without regard to this section."

(B) Section 2701(a)(3)(B) is amended by inserting "CERTAIN" before "QUALIFIED" in the heading thereof.

(C) Sections 2701 (d)(1) and (d)(4) are each amended by striking "subsection (a)(3)(B)" and inserting "subsection (a)(3) (B) or (C)".

(2) Clause (i) of section 2701(a)(4)(B) is amended by inserting "(or, to the extent provided in regulations, the rights as to either income or capital)" after "income and capital".

(3)(A) Section 2701(b)(2) is amended by adding at the end thereof the following new subparagraph:

"(C) APPLICABLE FAMILY MEMBER.—For purposes of this subsection, the term 'applicable family member' includes any lineal descendant of any parent of the transferor or the transferor's spouse."

(B) Section 2701(e)(3) is amended—

(i) by striking subparagraph (B), and

(ii) by striking so much of paragraph (3) as precedes "shall be treated as holding" and inserting:

"(3) ATTRIBUTION OF INDIRECT HOLDINGS AND TRANSFERS.—An individual".

(C) Section 2704(c)(3) is amended by striking "section 2701(e)(3)(A)" and inserting "section 2701(e)(3)".

(4) Clause (i) of section 2701(c)(1)(B) is amended to read as follows:

"(i) a right to distributions with respect to any interest which is junior to the rights of the transferred interest,".

(5)(A) Clause (i) of section 2701(c)(3)(C) is amended to read as follows:

"(i) IN GENERAL.—Payments under any interest held by a transferor which (without regard to this subparagraph) are qualified payments shall be treated as qualified payments unless the transferor elects not to treat such payments as qualified payments. Payments described in the preceding sentence which are held by an applicable family member shall be treated as qualified payments only if such member elects to treat such payments as qualified payments."

(B) The first sentence of section 2701(c)(3)(C)(ii) is amended to read as follows: "A transferor or applicable family member holding any distribution right which (without regard to this subparagraph) is not a qualified payment may elect to treat such right as a qualified payment, to be paid in the amounts and at the times specified in such election.".

(C) The time for making an election under the second sentence of section 2701(c)(3)(C)(i) of the Internal Revenue Code of 1986 (as amended by subparagraph (A)) shall not expire before the due date (including extensions) for filing the transferor's return of the tax imposed by section 2501 of such Code for the first calendar year ending after the date of enactment.

(6) Section 2701(d)(3)(A)(iii) is amended by striking "the period ending on the date of".

(7) Subclause (I) of section 2701(d)(3)(B)(ii) is amended by inserting "or the exclusion under section 2503(b)," after "section 2523,".

(8) Section 2701(e)(5) is amended—

(A) by striking "such contribution to capital or such redemption, recapitalization, or other change" in subparagraph (A) and inserting "such transaction", and

(B) by striking "the transfer" in subparagraph (B) and inserting "such transaction".

(9) Section 2701(d)(4) is amended by adding at the end thereof the following new subparagraph:

"(C) TRANSFER TO TRANSFERORS.—In the case of a taxable event described in paragraph (3)(A)(ii) involving a transfer of an applicable retained interest from an applicable family member to a transferor, this subsection shall continue to apply to the transferor during any period the transferor holds such interest."

(10) Section 2701(e)(6) is amended by inserting "or to reflect the application of subsection (d)" before the period at the end thereof.

(11)(A) Section 2702(a)(3)(A) is amended—

(i) by striking "to the extent" and inserting "if" in clause (i),

(ii) by striking "or" at the end of clause (i),

(iii) by striking the period at the end of clause (ii) and inserting ", or", and

(iv) by adding at the end thereof the following new clause:

"(iii) to the extent that regulations provide that such transfer is not inconsistent with the purposes of this section."

(B)(i) Section 2702(a)(3) is amended by striking "incomplete transfer" each place it appears and inserting "incomplete gift".

(ii) The heading for section 2702(a)(3)(B) is amended by striking "INCOMPLETE TRANSFER" and inserting "INCOMPLETE GIFT".

(g) AMENDMENTS RELATED TO SUBTITLE G.—

(1)(A) Subsection (a) of section 1248 is amended—

(i) by striking ", or if a United States person receives a distribution from a foreign corporation which, under section 302 or 331, is treated as an exchange of stock" in paragraph (1), and

(ii) by adding at the end thereof the following new sentence: "For purposes of this section, a United States person shall be treated as having sold or exchanged any stock if, under any provision of this subtitle, such person is treated as realizing gain from the sale or exchange of such stock.".

(B) Paragraph (1) of section 1248(e) is amended by striking ", or receives a distribution from a domestic corporation which, under section 302 or 331, is treated as an exchange of stock".

(C) Subparagraph (B) of section 1248(f)(1) is amended by striking "or 361(c)(1)" and inserting "355(c)(1), or 361(c)(1)".

(D) Paragraph (1) of section 1248(i) is amended to read as follows:

"(1) IN GENERAL.—If any shareholder of a 10-percent corporate shareholder of a foreign corporation exchanges stock of the 10-percent corporate shareholder for stock of the foreign corporation, such 10-percent corporate shareholder shall recognize gain in the same manner as if the stock of the foreign corporation received in such exchange had been—

"(A) issued to the 10-percent corporate shareholder, and

"(B) then distributed by the 10-percent corporate shareholder to such shareholder in redemption or liquidation (whichever is appropriate).

The amount of gain recognized by such 10-percent corporate shareholder under the preceding sentence shall not exceed the amount treated as a dividend under this section."

(2) Section 897 is amended by striking subsection (f).

(3) Paragraph (13) of section 4975(d) is amended by striking "section 408(b)" and inserting "section 408(b)(12)".

(4) Clause (iii) of section 56(g)(4)(D) is amended by inserting ", but only with respect to taxable years beginning after December 31, 1989" before the period at the end thereof.

(5)(A) Paragraph (11) of section 11701(a) of the Revenue Reconciliation Act of 1990 (and the amendment made by such paragraph) are hereby repealed, and section 7108(r)(2) of the Revenue Reconciliation Act of 1989 shall be applied as if such paragraph (and amendment) had never been enacted.

(B) Subparagraph (A) shall not apply to any building if the owner of such building establishes to the satisfaction of the Secretary of the Treasury or his delegate that such owner reasonably relied on the amendment made by such paragraph (11).

(h) AMENDMENTS RELATED TO SUBTITLE H.—

(1)(A) Clause (vi) of section 168(e)(3)(B) is amended by striking "or" at the end of subclause (I), by striking the period at the end of subclause (II) and inserting ", or", and by adding at the end thereof the following new subclause:

"(III) is described in section 48(l)(3)(A)(ix) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)."

(B) Subparagraph (B) of section 168(e)(3) (relating to 5-year property) is amended by adding at the end the following flush sentence:

"Nothing in any provision of law shall be construed to treat property as not being described in clause (vi)(I) (or the corresponding provisions of prior law) by reason of being public utility property (within the meaning of section 48(a)(3))."

(C) Subparagraph (K) of section 168(g)(4) is amended by striking "section 48(a)(3)(A)(iii)" and inserting "section 48(l)(3)(A)(ix) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)".

(2) Clause (ii) of section 172(b)(1)(E) is amended by striking "subsection (m)" and inserting "subsection (h)".

(3) Sections 805(a)(4)(E), 832(b)(5)(C)(ii)(II), and 832(b)(5)(D)(ii)(II) are each amended by striking "243(b)(5)" and inserting "243(b)(2)".

(4) Subparagraph (A) of section 243(b)(3) is amended by inserting "of" after "In the case".

(5) The subsection heading for subsection (a) of section 280F is amended by striking "INVESTMENT TAX CREDIT AND".

(6) Clause (i) of section 1504(c)(2)(B) is amended by inserting "section" before "243(b)(2)".

(7) Paragraph (3) of section 341(f) is amended by striking "351, 361, 371(a), or 374(a)" and inserting "351, or 361".

(8) Paragraph (2) of section 243(b) is amended to read as follows:

"(2) AFFILIATED GROUP.—For purposes of this subsection:

"(A) IN GENERAL.—The term 'affiliated group' has the meaning given such term by section 1504(a), except that for such purposes sections 1504(b)(2), 1504(b)(4), and 1504(c) shall not apply.

"(B) GROUP MUST BE CONSISTENT IN FOREIGN TAX TREATMENT.—The requirements of paragraph (1)(A) shall not be treated as being met with respect to any dividend received by a corporation if, for any taxable year which includes the day on which such dividend is received—

"(i) 1 or more members of the affiliated group referred to in paragraph (1)(A) choose to any extent to take the benefits of section 901, and

"(ii) 1 or more other members of such group claim to any extent a deduction for taxes otherwise creditable under section 901."

(9) The amendment made by section 11813(b)(17) of the Revenue Reconciliation Act of 1990 shall be applied as if the material stricken by such amendment included the closing parenthesis after "section 48(a)(5)".

(10) Paragraph (1) of section 179(d) is amended by striking "in a trade or business" and inserting "a trade or business".

(11) Subparagraph (E) of section 50(a)(2) is amended by striking "section 48(a)(5)(A)" and inserting "section 48(a)(5)".

(12) The amendment made by section 11801(c)(9)(G)(ii) of the Revenue Reconciliation Act of 1990 shall be applied as if it struck "Section 422A(c)(2)" and inserted "Section 422(c)(2)".

(13) Subparagraph (B) of section 424(c)(3) is amended by striking "a qualified stock option, an incentive stock option, an option granted under an employee stock purchase plan, or a restricted stock option" and inserting "an incentive stock option or an option granted under an employee stock purchase plan".

(14) Subparagraph (E) of section 1367(a)(2) is amended by striking "section 613A(c)(13)(B)" and inserting "section 613A(c)(11)(B)".

(15) Subparagraph (B) of section 460(e)(6) is amended by striking "section 167(k)" and inserting "section 168(e)(2)(A)(ii)".

(16) Subparagraph (C) of section 172(h)(4) is amended by striking "subsection (b)(1)(M)" and inserting "subsection (b)(1)(E)".

(17) Section 6503 is amended—

(A) by redesignating the subsection relating to extension in case of certain summonses as subsection (j), and

(B) by redesignating the subsection relating to cross references as subsection (k).

(18) Paragraph (4) of section 1250(e) is hereby repealed.

(i) EFFECTIVE DATE.—Except as otherwise expressly provided—

(1) the amendments made by this section shall be treated as amendments to the Internal Revenue Code of 1986 as amended by the Revenue Reconciliation Act of 1993; and

(2) any amendment made by this section shall apply to periods before the date of the enactment of this section in the same manner as if it had been included in the provision of the Revenue Reconciliation Act of 1990 to which such amendment relates.

SEC. 1703. AMENDMENTS RELATED TO REVENUE RECONCILIATION ACT OF 1993.

(a) AMENDMENT RELATED TO SECTION 13114.—Paragraph (2) of section 1044(c) is amended to read as follows:

"(2) PURCHASE.—The taxpayer shall be considered to have purchased any property if, but for subsection (d), the unadjusted basis of such property would be its cost within the meaning of section 1012."

(b) AMENDMENTS RELATED TO SECTION 13142.—

(1) Subparagraph (B) of section 13142(b)(6) of the Revenue Reconciliation Act of 1993 is amended to read as follows:

"(B) FULL-TIME STUDENTS, WAIVER AUTHORITY, AND PROHIBITED DISCRIMINATION.—The amendments made by paragraphs (2), (3), and (4) shall take effect on the date of the enactment of this Act."

(2) Subparagraph (C) of section 13142(b)(6) of such Act is amended by striking "paragraph (2)" and inserting "paragraph (5)".

(c) AMENDMENT RELATED TO SECTION 13161.—

(1) IN GENERAL.—Subsection (e) of section 4001 (relating to inflation adjustment) is amended to read as follows:

"(e) INFLATION ADJUSTMENT.—

"(1) IN GENERAL.—The $30,000 amount in subsection (a) and section 4003(a) shall be increased by an amount equal to—

"(A) $30,000, multiplied by

"(B) the cost-of-living adjustment under section 1(f)(3) for the calendar year in which the vehicle is sold, determined by substituting 'calendar year 1990' for 'calendar year 1992' in subparagraph (B) thereof.

"(2) ROUNDING.—If any amount as adjusted under paragraph (1) is not a multiple of $2,000, such amount shall be rounded to the next lowest multiple of $2,000."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect on the date of the enactment of this Act.

(d) AMENDMENT RELATED TO SECTION 13201.—Clause (ii) of section 135(b)(2)(B) is amended by inserting before the period at the end thereof the following: ", determined by substituting 'calendar year 1989' for 'calendar year 1992' in subparagraph (B) thereof".

(e) AMENDMENTS RELATED TO SECTION 13203.—Subsection (a) of section 59 is amended—

(1) by striking "the amount determined under section 55(b)(1)(A)" in paragraph (1)(A) and (2)(A)(i) and inserting "the pre-credit tentative minimum tax",

(2) by striking "specified in section 55(b)(1)(A)" in paragraph (1)(C) and inserting "specified in subparagraph (A)(i) or (B)(i) of section 55(b)(1) (whichever applies)",

(3) by striking "which would be determined under section 55(b)(1)(A)" in paragraph (2)(A)(ii) and inserting "which would be the pre-credit tentative minimum tax", and

(4) by adding at the end thereof the following new paragraph:

"(3) PRE-CREDIT TENTATIVE MINIMUM TAX.—For purposes of this subsection, the term 'pre-credit tentative minimum tax' means—

"(A) in the case of a taxpayer other than a corporation, the amount determined under the first sentence of section 55(b)(1)(A)(i), or

"(B) in the case of a corporation, the amount determined under section 55(b)(1)(B)(i)."

(f) AMENDMENT RELATED TO SECTION 13221.—Sections 1201(a) and 1561(a) are each amended by striking "last sentence" each place it appears and inserting "last 2 sentences".

(g) AMENDMENTS RELATED TO SECTION 13222.—

(1) Subparagraph (B) of section 6033(e)(1) is amended by adding at the end thereof the following new clause:

"(iii) COORDINATION WITH SECTION 527(f).—This subsection shall not apply to any amount on which tax is imposed by reason of section 527(f).".

(2) Clause (i) of section 6033(e)(1)(B) is amended by striking "this subtitle" and inserting "section 501".

(h) AMENDMENT RELATED TO SECTION 13225.—Paragraph (3) of section 6655(g) is amended by striking all that follows "'3rd month'" in the sentence following subparagraph (C) and inserting ", subsection (e)(2)(A) shall be applied by substituting '2 months' for '3 months' in clause (i)(I), the election under clause (i) of subsection (e)(2)(C) may be made separately for each installment, and clause (ii) of subsection (e)(2)(C) shall not apply.".

(i) AMENDMENTS RELATED TO SECTION 13231.—

(1) Subparagraph (G) of section 904(d)(3) is amended by striking "section 951(a)(1)(B)" and inserting "subparagraph (B) or (C) of section 951(a)(1)".

(2) Paragraph (1) of section 956A(b) is amended to read as follows:

"(1) the amount (not including a deficit) referred to in section 316(a)(1) to the extent such amount was accumulated in prior taxable years beginning after September 30, 1993, and".

(3) Subsection (f) of section 956A is amended by inserting before the period at the end thereof: "and regulations coordinating the provisions of subsections (c)(3)(A) and (d)".

(4) Subsection (b) of section 958 is amended by striking "956(b)(2)" each place it appears and inserting "956(c)(2)".

(5)(A) Subparagraph (A) of section 1297(d)(2) is amended by striking "The adjusted basis of any asset" and inserting "The amount taken into account under section 1296(a)(2) with respect to any asset".

(B) The paragraph heading of paragraph (2) of section 1297(d) is amended to read as follows:

"(2) AMOUNT TAKEN INTO ACCOUNT.—".

(6) Subsection (e) of section 1297 is amended by inserting "For purposes of this part—" after the subsection heading.

(j) AMENDMENT RELATED TO SECTION 13241.—Subparagraph (B) of section 40(e)(1) is amended to read as follows:

"(B) for any period before January 1, 2001, during which the rates of tax under section 4081(a)(2)(A) are 4.3 cents per gallon."

(k) AMENDMENT RELATED TO SECTION 13261.—Clause (iii) of section 13261(g)(2)(A) of the Revenue Reconciliation Act of 1993 is amended by striking "by the taxpayer" and inserting "by the taxpayer or a related person".

(l) AMENDMENT RELATED TO SECTION 13301.—Subparagraph (B) of section 1397B(d)(5) is amended by striking "preceding".

(m) CLERICAL AMENDMENTS.—

(1) Subsection (d) of section 39 is amended—

(A) by striking "45" in the heading of paragraph (5) and inserting "45A", and

(B) by striking "45" in the heading of paragraph (6) and inserting "45B".

(2) Subparagraph (A) of section 108(d)(9) is amended by striking "paragraph (3)(B)" and inserting "paragraph (3)(C)".

(3) Subparagraph (C) of section 143(d)(2) is amended by striking the period at the end thereof and inserting a comma.

(4) Clause (ii) of section 163(j)(6)(E) is amended by striking "which is a" and inserting "which is".

(5) Subparagraph (A) of section 1017(b)(4) is amended by striking "subsection (b)(2)(D)" and inserting "subsection (b)(2)(E)".

(6) So much of section 1245(a)(3) as precedes subparagraph (A) thereof is amended to read as follows:

"(3) SECTION 1245 PROPERTY.—For purposes of this section, the term 'section 1245 property' means any property which is or has been property of a character subject to the allowance for depreciation provided in section 167 and is either—
".

(7) Paragraph (2) of section 1394(e) is amended—

(A) by striking "(i)" and inserting "(A)", and

(B) by striking "(ii)" and inserting "(B)".

(8) Subsection (m) of section 6501 (as redesignated by section 1602) is amended by striking "or 51(j)" and inserting "45B, or 51(j)".

(9)(A) The section 6714 added by section 13242(b)(1) of the Revenue Reconciliation Act of 1993 is hereby redesignated as section 6715.

(B) The table of sections for part I of subchapter B of chapter 68 is amended by striking "6714" in the item added by such section 13242(b)(2) of such Act and inserting "6715".

(10) Paragraph (2) of section 9502(b) is amended by inserting "and before" after "1982,".

(11) Subsection (a)(3) of section 13206 of the Revenue Reconciliation Act of 1993 is amended by striking "this section" and inserting "this subsection".

(12) Paragraph (1) of section 13215(c) of the Revenue Reconciliation Act of 1993 is amended by striking "Public Law 92–21" and inserting "Public Law 98–21".

(13) Paragraph (2) of section 13311(e) of the Revenue Reconciliation Act of 1993 is amended by striking "section 1393(a)(3)" and inserting "section 1393(a)(2)".

(14) Subparagraph (B) of section 117(d)(2) is amended by striking "section 132(f)" and inserting "section 132(h)".

(n) EFFECTIVE DATE.—Any amendment made by this section shall take effect as if included in the provision of the Revenue Reconciliation Act of 1993 to which such amendment relates.

SEC. 1704. MISCELLANEOUS PROVISIONS.

(a) APPLICATION OF AMENDMENTS MADE BY TITLE XII OF OMNIBUS BUDGET RECONCILIATION ACT OF 1990.—Except as otherwise expressly provided, whenever in title XII of the Omnibus Budget Reconciliation Act of 1990 an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

(b) TREATMENT OF CERTAIN AMOUNTS UNDER HEDGE BOND RULES.—

(1) Clause (iii) of section 149(g)(3)(B) is amended to read as follows:

"(iii) AMOUNTS HELD PENDING REINVESTMENT OR REDEMPTION.—Amounts held for not more than 30 days pending reinvestment or bond redemption shall be treated as invested in bonds described in clause (i)."

(2) The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 7651 of the Omnibus Budget Reconciliation Act of 1989.

(c) TREATMENT OF CERTAIN DISTRIBUTIONS UNDER SECTION 1445.—

(1) IN GENERAL.—Paragraph (3) of section 1445(e) is amended by adding at the end thereof the following new sentence: "Rules similar to the rules of the preceding provisions of this paragraph shall apply in the case of any distribution to which section 301 applies and which is not made out of the earnings and profits of such a domestic corporation."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to distributions after the date of the enactment of this Act.

(d) TREATMENT OF CERTAIN CREDITS UNDER SECTION 469.—

(1) IN GENERAL.—Subparagraph (B) of section 469(c)(3) is amended by adding at the end thereof the following new sentence: "If the preceding sentence applies to the net income from any property for any taxable year, any credits allowable under subpart B (other than section 27(a)) or D of part IV of subchapter A for such taxable year which are attributable to such property shall be treated as credits not from a passive activity to the extent the amount of such credits does not exceed the regular tax liability of the taxpayer for the taxable year which is allocable to such net income."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1986.

(e) TREATMENT OF DISPOSITIONS UNDER PASSIVE LOSS RULES.—

(1) IN GENERAL.—Subparagraph (A) of section 469(g)(1) is amended to read as follows:

"(A) IN GENERAL.—If all gain or loss realized on such disposition is recognized, the excess of—

"(i) any loss from such activity for such taxable year (determined after the application of subsection (b)), over

"(ii) any net income or gain for such taxable year from all other passive activities (determined after the application of subsection (b)),

shall be treated as a loss which is not from a passive activity."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1986.

(f) MISCELLANEOUS AMENDMENTS TO FOREIGN PROVISIONS.—

(1) COORDINATION OF UNIFIED ESTATE TAX CREDIT WITH TREATIES.—Subparagraph (A) of section 2102(c)(3) is amended by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, property shall not be treated as situated in the United States if such property is exempt from the tax imposed by this subchapter under any treaty obligation of the United States."

(2) TREATMENT OF CERTAIN INTEREST PAID TO RELATED PERSON.—

(A) Subparagraph (B) of section 163(j)(1) is amended by inserting before the period at the end thereof the following: "(and clause (ii) of paragraph (2)(A) shall not apply for purposes of applying this subsection to the amount so treated)".

(B) Subsection (j) of section 163 is amended by redesignating paragraph (7) as paragraph (8) and by inserting after paragraph (6) the following new paragraph:

"(7) COORDINATION WITH PASSIVE LOSS RULES, ETC.—This subsection shall be applied before sections 465 and 469."

(C) The amendments made by this paragraph shall apply as if included in the amendments made by section 7210(a) of the Revenue Reconciliation Act of 1989.

(3) TREATMENT OF INTEREST ALLOCABLE TO EFFECTIVELY CONNECTED INCOME.—

(A) IN GENERAL.—

(i) Subparagraph (B) of section 884(f)(1) is amended by striking "to the extent" and all that follows down through "subparagraph (A)" and inserting "to the extent that the allocable interest exceeds the interest described in subparagraph (A)".

(ii) The second sentence of section 884(f)(1) is amended by striking "reasonably expected" and all that follows down through the period at the end thereof and inserting "reasonably expected to be allocable interest."

(iii) Paragraph (2) of section 884(f) is amended to read as follows:

"(2) ALLOCABLE INTEREST.—For purposes of this subsection, the term 'allocable interest' means any interest which is allocable to income which is effectively connected (or treated as effectively connected) with the conduct of a trade or business in the United States."

(B) EFFECTIVE DATE.—The amendments made by subparagraph (A) shall take effect as if included in the amendments made by section 1241(a) of the Tax Reform Act of 1986.

(4) CLARIFICATION OF SOURCE RULE.—

(A) IN GENERAL.—Paragraph (2) of section 865(b) is amended by striking "863(b)" and inserting "863".

(B) EFFECTIVE DATE.—The amendment made by subparagraph (A) shall take effect as if included in the amendments made by section 1211 of the Tax Reform Act of 1986.

(5) REPEAL OF OBSOLETE PROVISIONS.—

(A) Paragraph (1) of section 6038(a) is amended by striking ", and" at the end of subparagraph (E) and inserting a period, and by striking subparagraph (F).

(B) Subsection (b) of section 6038A is amended by adding "and" at the end of paragraph (2), by striking ", and" at the end of paragraph (3) and inserting a period, and by striking paragraph (4).

(g) TREATMENT OF ASSIGNMENT OF INTEREST IN CERTAIN BOND-FINANCED FACILITIES.—

(1) IN GENERAL.—Subparagraph (A) of section 1317(3) of the Tax Reform Act of 1986 is amended by adding at the end thereof the following new sentence: "A facility shall not fail to be treated as described in this subparagraph by reason of an assignment (or an agreement to an assignment) by the governmental unit on whose behalf the bonds are issued of any part of its interest in the property financed by such bonds to another governmental unit."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in such section 1317 on the date of the enactment of the Tax Reform Act of 1986.

(h) CLARIFICATION OF TREATMENT OF MEDICARE ENTITLEMENT UNDER COBRA PROVISIONS.—

(1) IN GENERAL.—

(A) Subclause (V) of section 4980B(f)(2)(B)(i) is amended to read as follows:

"(V) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in paragraph (3)(B) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this clause before the close of the 36-month period beginning on the date the covered employee became so entitled."

(B) Clause (v) of section 602(2)(A) of the Employee Retirement Income Security Act of 1974 is amended to read as follows:

"(v) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in section 603(2) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this subparagraph before the close of the 36-month period beginning on the date the covered employee became so entitled."

(C) Clause (iv) of section 2202(2)(A) of the Public Health Service Act is amended to read as follows:

"(iv) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in section 2203(2) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this subparagraph before the close of the 36-month period beginning on the date the covered employee became so entitled."

(2) EFFECTIVE DATE.—The amendments made by this subsection shall apply to plan years beginning after December 31, 1989.

(i) TREATMENT OF CERTAIN REMIC INCLUSIONS.—

(1) IN GENERAL.—Subsection (a) of section 860E is amended by adding at the end thereof the following new paragraph:

"(6) COORDINATION WITH MINIMUM TAX.—For purposes of part VI of subchapter A of this chapter—

"(A) the reference in section 55(b)(2) to taxable income shall be treated as a reference to taxable income determined without regard to this subsection,

"(B) the alternative minimum taxable income of any holder of a residual interest in a REMIC for any taxable year shall in no event be less than the excess inclusion for such taxable year, and

"(C) any excess inclusion shall be disregarded for purposes of computing the alternative tax net operating loss deduction.

The preceding sentence shall not apply to any organization to which section 593 applies, except to the extent provided in regulations prescribed by the Secretary under paragraph (2)."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 671 of the Tax Reform Act of 1986 unless the taxpayer elects to apply such amendment only to taxable years beginning after the date of the enactment of this Act.

(j) EXEMPTION FROM HARBOR MAINTENANCE TAX FOR CERTAIN PASSENGERS.—

(1) IN GENERAL.—Subparagraph (D) of section 4462(b)(1) (relating to special rule for Alaska, Hawaii, and possessions) is amended by inserting before the period the following: ", or passengers transported on United States flag vessels operating solely within the State waters of Alaska or Hawaii and adjacent international waters".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 1402(a) of the Harbor Maintenance Revenue Act of 1986.

(k) AMENDMENTS RELATED TO REVENUE PROVISIONS OF ENERGY POLICY ACT OF 1992.—

(1) Effective with respect to taxable years beginning after December 31, 1990, subclause (II) of section 53(d)(1)(B)(iv) is amended to read as follows:

"(II) the adjusted net minimum tax for any taxable year is the amount of the net minimum tax for such year increased in the manner provided in clause (iii)."

(2) Subsection (g) of section 179A is redesignated as subsection (f).

(3) Subparagraph (E) of section 6724(d)(3) is amended by striking "section 6109(f)" and inserting "section 6109(h)".

(4)(A) Subsection (d) of section 30 is amended—

(i) by inserting "(determined without regard to subsection (b)(3))" before the period at the end of paragraph (1) thereof, and

(ii) by adding at the end thereof the following new paragraph:

"(4) ELECTION TO NOT TAKE CREDIT.—No credit shall be allowed under subsection (a) for any vehicle if the taxpayer elects to not have this section apply to such vehicle."

(B) Subsection (m) of section 6501 (as redesignated by section 1602) is amended by striking "section 40(f)" and inserting "section 30(d)(4), 40(f)".

(5) Subclause (III) of section 501(c)(21)(D)(ii) is amended by striking "section 101(6)" and inserting "section 101(7)" and by striking "1752(6)" and inserting "1752(7)".

(6) Paragraph (1) of section 1917(b) of the Energy Policy Act of 1992 shall be applied as if "at a rate" appeared instead of "at the rate" in the material proposed to be stricken.

(7) Paragraph (2) of section 1921(b) of the Energy Policy Act of 1992 shall be applied as if a comma appeared after "(2)" in the material proposed to be stricken.

(8) Subsection (a) of section 1937 of the Energy Policy Act of 1992 shall be applied as if "Subpart B" appeared instead of "Subpart C".

(l) TREATMENT OF QUALIFIED FOOTBALL COACHES PLAN.—

(1) IN GENERAL.—Subparagraph (F) of section 3(37) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002(37)(F)) is amended by redesignating clause (ii) as clause (iii) and by inserting after clause (i) the following new clause:

"(ii) For purposes of the Internal Revenue Code of 1986—

"(I) clause (i) shall apply, and

"(II) a qualified football coaches plan shall be treated as a multiemployer collectively bargained plan.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to years beginning after December 22, 1987.

(m) DETERMINATION OF UNRECOVERED INVESTMENT IN ANNUITY CONTRACT.—

(1) IN GENERAL.—Subparagraph (A) of section 72(b)(4) is amended by inserting "(determined without regard to subsection (c)(2))" after "contract".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 1122(c) of the Tax Reform Act of 1986.

(n) MODIFICATIONS TO ELECTION TO INCLUDE CHILD'S INCOME ON PARENT'S RETURN.—

(1) ELIGIBILITY FOR ELECTION.—Clause (ii) of section 1(g)(7)(A) (relating to election to include certain unearned income of child on parent's return) is amended to read as follows:

"(ii) such gross income is more than the amount described in paragraph (4)(A)(ii)(I) and less than 10 times the amount so described,".

(2) COMPUTATION OF TAX.—Subparagraph (B) of section 1(g)(7) (relating to income included on parent's return) is amended—

(A) by striking "$1,000" in clause (i) and inserting "twice the amount described in paragraph (4)(A)(ii)(I)", and

(B) by amending subclause (II) of clause (ii) to read as follows:

"(II) for each such child, 15 percent of the lesser of the amount described in paragraph (4)(A)(ii)(I) or the excess of the gross income of such child over the amount so described, and".

(3) MINIMUM TAX.—Subparagraph (B) of section 59(j)(1) is amended by striking "$1,000" and inserting "twice the amount in effect for the taxable year under section 63(c)(5)(A)".

(4) EFFECTIVE DATE.—The amendments made by this subsection shall apply to taxable years beginning after December 31, 1995.

(o) TREATMENT OF CERTAIN VETERANS' REEMPLOYMENT RIGHTS.—

(1) IN GENERAL.—Section 414 is amended by adding at the end the following new subsection:

"(u) SPECIAL RULES RELATING TO VETERANS' REEMPLOYMENT RIGHTS UNDER USERRA.—

"(1) TREATMENT OF CERTAIN CONTRIBUTIONS MADE PURSUANT TO VETERANS' REEMPLOYMENT RIGHTS.—If any contribution is made by an employer or an employee under an individual account plan with respect to an employee, or by an employee to a defined benefit plan that provides for employee contributions, and such contribution is required by reason of such employee's rights under chapter 43 of title 38, United States Code, resulting from qualified military service, then—

"(A) such contribution shall not be subject to any otherwise applicable limitation contained in section 402(g), 402(h), 403(b), 404(a), 404(h), 408, 415, or 457, and shall not be taken into account in applying such limitations to other contributions or benefits under such plan or any other plan, with respect to the year in which the contribution is made,

"(B) such contribution shall be subject to the limitations referred to in subparagraph (A) with respect to the year to which the contribution relates (in accordance with rules prescribed by the Secretary), and

"(C) such plan shall not be treated as failing to meet the requirements of section 401(a)(4), 401(a)(26), 401(k)(3), 401(k)(11), 401(k)(12), 401(m), 403(b)(12), 408(k)(3), 408(k)(6), 408(p), 410(b), or 416 by reason of the making of (or the right to make) such contribution.

For purposes of the preceding sentence, any elective deferral or employee contribution made under paragraph (2) shall be treated as required by reason of the employee's rights under such chapter 43.

"(2) REEMPLOYMENT RIGHTS UNDER USERRA WITH RESPECT TO ELECTIVE DEFERRALS.—

"(A) IN GENERAL.—For purposes of this subchapter and section 457, if an employee is entitled to the benefits of chapter 43 of title 38, United States Code, with respect to any plan which provides for elective deferrals, the employer sponsoring the plan shall be treated as meeting the requirements of such chapter 43 with respect to such elective deferrals only if such employer—

"(i) permits such employee to make additional elective deferrals under such plan (in the amount determined under subparagraph (B) or such lesser amount as is elected by the employee) during the period which begins on the date of the reemployment of such employee with such employer and has the same length as the lesser of—

"(I) the product of 3 and the period of qualified military service which resulted in such rights, and

"(II) 5 years, and

"(ii) makes a matching contribution with respect to any additional elective deferral made pursuant to clause (i) which would have been re-

quired had such deferral actually been made during the period of such qualified military service.

"(B) AMOUNT OF MAKEUP REQUIRED.—The amount determined under this subparagraph with respect to any plan is the maximum amount of the elective deferrals that the individual would have been permitted to make under the plan in accordance with the limitations referred to in paragraph (1)(A) during the period of qualified military service if the individual had continued to be employed by the employer during such period and received compensation as determined under paragraph (7). Proper adjustment shall be made to the amount determined under the preceding sentence for any elective deferrals actually made during the period of such qualified military service.

"(C) ELECTIVE DEFERRAL.—For purposes of this paragraph, the term 'elective deferral' has the meaning given such term by section 402(g)(3); except that such term shall include any deferral of compensation under an eligible deferred compensation plan (as defined in section 457(b)).

"(D) AFTER-TAX EMPLOYEE CONTRIBUTIONS.—References in subparagraphs (A) and (B) to elective deferrals shall be treated as including references to employee contributions.

"(3) CERTAIN RETROACTIVE ADJUSTMENTS NOT REQUIRED.—For purposes of this subchapter and subchapter E, no provision of chapter 43 of title 38, United States Code, shall be construed as requiring—

"(A) any crediting of earnings to an employee with respect to any contribution before such contribution is actually made, or

"(B) any allocation of any forfeiture with respect to the period of qualified military service.

"(4) LOAN REPAYMENT SUSPENSIONS PERMITTED.—If any plan suspends the obligation to repay any loan made to an employee from such plan for any part of any period during which such employee is performing service in the uniformed services (as defined in chapter 43 of title 38, United States Code), whether or not qualified military service, such suspension shall not be taken into account for purposes of section 72(p), 401(a), or 4975(d)(1).

"(5) QUALIFIED MILITARY SERVICE.—For purposes of this subsection, the term 'qualified military service' means any service in the uniformed services (as defined in chapter 43 of title 38, United States Code) by any individual if such individual is entitled to reemployment rights under such chapter with respect to such service.

"(6) INDIVIDUAL ACCOUNT PLAN.—For purposes of this subsection, the term 'individual account plan' means any defined contribution plan (including any tax-sheltered annuity plan under section 403(b), any simplified employee pension under section 408(k), any qualified salary reduction arrangement under section 408(p), and any eligible deferred compensation plan (as defined in section 457(b)).

"(7) COMPENSATION.—For purposes of sections 403(b)(3), 415(c)(3), and 457(e)(5), an employee who is in qualified military service shall be treated as receiving compensation from the employer during such period of qualified military service equal to—

"(A) the compensation the employee would have received during such period if the employee were not in qualified military service, determined based on the rate of pay the employee would have received from the employer but for absence during the period of qualified military service, or

"(B) if the compensation the employee would have received during such period was not reasonably certain, the employee's average compensation from the employer during the 12-month period immediately preceding the qualified military service (or, if shorter, the period of employment immediately preceding the qualified military service).

"(8) USERRA REQUIREMENTS FOR QUALIFIED RETIREMENT PLANS.—For purposes of this subchapter and section 457, an employer sponsoring a retirement plan shall be treated as meeting the requirements of chapter 43 of title 38, United States Code, only if each of the following requirements is met:

"(A) An individual reemployed under such chapter is treated with respect to such plan as not having incurred a break in service with the employer maintaining the plan by reason of such individual's period of qualified military service.

"(B) Each period of qualified military service served by an individual is, upon reemployment under such chapter, deemed with respect to such plan to constitute service with the employer maintaining the plan for the purpose of determining the nonforfeitability of the individual's accrued benefits

under such plan and for the purpose of determining the accrual of benefits under such plan.

"(C) An individual reemployed under such chapter is entitled to accrued benefits that are contingent on the making of, or derived from, employee contributions or elective deferrals only to the extent the individual makes payment to the plan with respect to such contributions or deferrals. No such payment may exceed the amount the individual would have been permitted or required to contribute had the individual remained continuously employed by the employer throughout the period of qualified military service. Any payment to such plan shall be made during the period beginning with the date of reemployment and whose duration is 3 times the period of the qualified military service (but not greater than 5 years).

"(9) PLANS NOT SUBJECT TO TITLE 38.—This subsection shall not apply to any retirement plan to which chapter 43 of title 38, United States Code, does not apply.

"(10) REFERENCES.—For purposes of this section, any reference to chapter 43 of title 38, United States Code, shall be treated as a reference to such chapter as in effect on December 12, 1994 (without regard to any subsequent amendment)."

(2) EFFECTIVE DATE.—The amendment made by this subsection shall be effective as of December 12, 1994.

(p) REPORTING OF REAL ESTATE TRANSACTIONS.—

(1) IN GENERAL.—Paragraph (3) of section 6045(e) (relating to prohibition of separate charge for filing return) is amended by adding at the end the following new sentence: "Nothing in this paragraph shall be construed to prohibit the real estate reporting person from taking into account its cost of complying with such requirement in establishing its charge (other than a separate charge for complying with such requirement) to any customer for performing services in the case of a real estate transaction."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in section 1015(e)(2)(A) of the Technical and Miscellaneous Revenue Act of 1988.

(q) CLARIFICATION OF DENIAL OF DEDUCTION FOR STOCK REDEMPTION EXPENSES.

(1) IN GENERAL.—Paragraph (1) of section 162(k) is amended by striking "the redemption of its stock" and inserting "the reacquisition of its stock or of the stock of any related person (as defined in section 465(b)(3)(C))".

(2) CERTAIN DEDUCTIONS PERMITTED.—Subparagraph (A) of section 162(k)(2) is amended by striking "or" at the end of clause (i), by redesignating clause (ii) as clause (iii), and by inserting after clause (i) the following new clause:

"(ii) deduction for amounts which are properly allocable to indebtedness and amortized over the term of such indebtedness, or".

(3) CLERICAL AMENDMENT.—The subsection heading for subsection (k) of section 162 is amended by striking "REDEMPTION" and inserting "REACQUISITION".

(4) EFFECTIVE DATE.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by this subsection shall apply to amounts paid or incurred after September 13, 1995, in taxable years ending after such date.

(B) PARAGRAPH (2).—The amendment made by paragraph (2) shall take effect as if included in the amendment made by section 613 of the Tax Reform Act of 1986.

(r) CLERICAL AMENDMENT TO SECTION 404.—

(1) IN GENERAL.—Paragraph (1) of section 404(j) is amended by striking "(10)" and inserting "(9)".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 713(d)(4)(A) of the Deficit Reduction Act of 1984.

(s) PASSIVE INCOME NOT TO INCLUDE FSC INCOME, ETC.—

(1) IN GENERAL.—Paragraph (2) of section 1296(b) is amended by striking "or" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", or", and by inserting after subparagraph (C) the following new subparagraph:

"(D) which is foreign trade income of a FSC or export trade income of an export trade corporation (as defined in section 971)."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 1235 of the Tax Reform Act of 1986.

(t) MISCELLANEOUS CLERICAL AMENDMENTS.—

(1) Subclause (II) of section 56(g)(4)(C)(ii) is amended by striking "of the subclause" and inserting "of subclause".

(2) Paragraph (2) of section 72(m) is amended by inserting "and" at the end of subparagraph (A), by striking subparagraph (B), and by redesignating subparagraph (C) as subparagraph (B).

(3) Paragraph (2) of section 86(b) is amended by striking "adusted" and inserting "adjusted".

(4)(A) The heading for section 112 is amended by striking "combat pay" and inserting "combat zone compensation".

(B) The item relating to section 112 in the table of sections for part III of subchapter B of chapter 1 is amended by striking "combat pay" and inserting "combat zone compensation".

(C) Paragraph (1) of section 3401(a) is amended by striking "combat pay" and inserting "combat zone compensation".

(5) Clause (i) of section 172(h)(3)(B) is amended by striking the comma at the end thereof and inserting a period.

(6) Clause (ii) of section 543(a)(2)(B) is amended by striking "section 563(c)" and inserting "section 563(d)".

(7) Paragraph (1) of section 958(a) is amended by striking "sections 955(b)(1)(A) and (B), 955(c)(2)(A)(ii), and 960(a)(1)" and inserting "section 960(a)(1)".

(8) Subsection (g) of section 642 is amended by striking "under 2621(a)(2)" and inserting "under section 2621(a)(2)".

(9) Section 1463 is amended by striking "this subsection" and inserting "this section".

(10) Subsection (k) of section 3306 is amended by inserting a period at the end thereof.

(11) The item relating to section 4472 in the table of sections for subchapter B of chapter 36 is amended by striking "and special rules".

(12) Paragraph (3) of section 5134(c) is amended by striking "section 6662(a)" and inserting "section 6665(a)".

(13) Paragraph (2) of section 5206(f) is amended by striking "section 5(e)" and inserting "section 105(e)".

(14) Paragraph (1) of section 6050B(c) is amended by striking "section 85(c)" and inserting "section 85(b)".

(15) Subsection (k) of section 6166 is amended by striking paragraph (6).

(16) Subsection (e) of section 6214 is amended to read as follows:

"(e) CROSS REFERENCE.—

"For provision giving Tax Court jurisdiction to order a refund of an overpayment and to award sanctions, see section 6512(b)(2)."

(17) The section heading for section 6043 is amended by striking the semicolon and inserting a comma.

(18) The item relating to section 6043 in the table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking the semicolon and inserting a comma.

(19) The table of sections for part I of subchapter A of chapter 68 is amended by striking the item relating to section 6662.

(20)(A) Section 7232 is amended—

(i) by striking "lubricating oil," in the heading, and

(ii) by striking "lubricating oil," in the text.

(B) The table of sections for part II of subchapter A of chapter 75 is amended by striking "lubricating oil," in the item relating to section 7232.

(21) Paragraph (1) of section 6701(a) of the Omnibus Budget Reconciliation Act of 1989 is amended by striking "subclause (IV)" and inserting "subclause (V)".

(22) Clause (ii) of section 7304(a)(2)(D) of such Act is amended by striking "subsection (c)(2)" and inserting "subsection (c)".

(23) Paragraph (1) of section 7646(b) of such Act is amended by striking "section 6050H(b)(1)" and inserting "section 6050H(b)(2)".

(24) Paragraph (10) of section 7721(c) of such Act is amended by striking "section 6662(b)(2)(C)(ii)" and inserting "section 6661(b)(2)(C)(ii)".

(25) Subparagraph (A) of section 7811(i)(3) of such Act is amended by inserting "the first place it appears" before "in clause (i)".

(26) Paragraph (10) of section 7841(d) of such Act is amended by striking "section 381(a)" and inserting "section 381(c)".

(27) Paragraph (2) of section 7861(c) of such Act is amended by inserting "the second place it appears" before "and inserting".

(28) Paragraph (1) of section 460(b) is amended by striking "the look-back method of paragraph (3)" and inserting "the look-back method of paragraph (2)".

(29) Subparagraph (C) of section 50(a)(2) is amended by striking "subsection (c)(4)" and inserting "subsection (d)(5)".

(30) Subparagraph (B) of section 172(h)(4) is amended by striking the material following the heading and preceding clause (i) and inserting "For purposes of subsection (b)(2)—".

(31) Subparagraph (A) of section 355(d)(7) is amended by inserting "section" before "267(b)".

(32) Subparagraph (C) of section 420(e)(1) is amended by striking "mean" and inserting "means".

(33) Paragraph (4) of section 537(b) is amended by striking "section 172(i)" and inserting "section 172(f)".

(34) Subparagraph (B) of section 613(e)(1) is amended by striking the comma at the end thereof and inserting a period.

(35) Paragraph (4) of section 856(a) is amended by striking "section 582(c)(5)" and inserting "section 582(c)(2)".

(36) Sections 904(f)(2)(B)(i) and 907(c)(4)(B)(iii) are each amended by inserting "(as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)" after "section 172(h)".

(37) Subsection (b) of section 936 is amended by striking "subparagraphs (D)(ii)(I)" and inserting "subparagraphs (D)(ii)".

(38) Subsection (c) of section 2104 is amended by striking "subparagraph (A), (C), or (D) of section 861(a)(1)" and inserting "section 861(a)(1)(A)".

(39) Subparagraph (A) of section 280A(c)(1) is amended to read as follows:

"(A) as the principal place of business for any trade or business of the taxpayer,".

(40) Section 6038 is amended by redesignating the subsection relating to cross references as subsection (f).

(41) Clause (iv) of section 6103(e)(1)(A) is amended by striking all that follows "provisions of" and inserting "section 1(g) or 59(j);".

(42) The subsection (f) of section 6109 of the Internal Revenue Code of 1986 which was added by section 2201(d) of Public Law 101–624 is redesignated as subsection (g).

(43) Subsection (b) of section 7454 is amended by striking "section 4955(e)(2)" and inserting "section 4955(f)(2)".

(44) Subsection (d) of section 11231 of the Revenue Reconciliation Act of 1990 shall be applied as if "comma" appeared instead of "period" and as if the paragraph (9) proposed to be added ended with a comma.

(45) Paragraph (1) of section 11303(b) of the Revenue Reconciliation Act of 1990 shall be applied as if "paragraph" appeared instead of "subparagraph" in the material proposed to be stricken.

(46) Subsection (f) of section 11701 of the Revenue Reconciliation Act of 1990 is amended by inserting "(relating to definitions)" after "section 6038(e)".

(47) Subsection (i) of section 11701 of the Revenue Reconciliation Act of 1990 shall be applied as if "subsection" appeared instead of "section" in the material proposed to be stricken.

(48) Subparagraph (B) of section 11801(c)(2) of the Revenue Reconciliation Act of 1990 shall be applied as if "section 56(g)" appeared instead of "section 59(g)".

(49) Subparagraph (C) of section 11801(c)(8) of the Revenue Reconciliation Act of 1990 shall be applied as if "reorganizations" appeared instead of "reorganization" in the material proposed to be stricken.

(50) Subparagraph (H) of section 11801(c)(9) of the Revenue Reconciliation Act of 1990 shall be applied as if "section 1042(c)(1)(B)" appeared instead of "section 1042(c)(2)(B)".

(51) Subparagraph (F) of section 11801(c)(12) of the Revenue Reconciliation Act of 1990 shall be applied as if "and (3)" appeared instead of "and (E)".

(52) Subparagraph (A) of section 11801(c)(22) of the Revenue Reconciliation Act of 1990 shall be applied as if "chapters 21" appeared instead of "chapter 21" in the material proposed to be stricken.

(53) Paragraph (3) of section 11812(b) of the Revenue Reconciliation Act of 1990 shall be applied by not executing the amendment therein to the heading of section 42(d)(5)(B).

(54) Clause (i) of section 11813(b)(9)(A) of the Revenue Reconciliation Act of 1990 shall be applied as if a comma appeared after "(3)(A)(ix)" in the material proposed to be stricken.

(55) Subparagraph (F) of section 11813(b)(13) of the Revenue Reconciliation Act of 1990 shall be applied as if "tax" appeared after "investment" in the material proposed to be stricken.

(56) Paragraph (19) of section 11813(b) of the Revenue Reconciliation Act of 1990 shall be applied as if "Paragraph (20) of section 1016(a), as redesignated by section 11801," appeared instead of "Paragraph (21) of section 1016(a)".

(57) Paragraph (5) section 8002(a) of the Surface Transportation Revenue Act of 1991 shall be applied as if "4481(e)" appeared instead of "4481(c)".

(58) Section 7872 is amended—

(A) by striking "foregone" each place it appears in subsections (a) and (e)(2) and inserting "forgone", and

(B) by striking "FOREGONE" in the heading for subsection (e) and the heading for paragraph (2) of subsection (e) and inserting "FORGONE".

(59) Paragraph (7) of section 7611(h) is amended by striking "approporiate" and inserting "appropriate".

(60) The heading of paragraph (3) of section 419A(c) is amended by striking "SEVERENCE" and inserting "SEVERANCE".

(61) Clause (ii) of section 807(d)(3)(B) is amended by striking "Commissoners' " and inserting "Commissioners' ".

(62) Subparagraph (B) of section 1274A(c)(1) is amended by striking "instument" and inserting "instrument".

(63) Subparagraph (B) of section 724(d)(3) by striking "Subparagaph" and inserting "Subparagraph".

(64) The last sentence of paragraph (2) of section 42(c) is amended by striking "of 1988".

(65) Paragraph (1) of section 9707(d) is amended by striking "diligence," and inserting "diligence".

(66) Subsection (c) of section 4977 is amended by striking "section 132(i)(2)" and inserting "section 132(h)".

(67) The last sentence of section 401(a)(20) is amended by striking "section 211" and inserting "section 521".

(68) Subparagraph (A) of section 402(g)(3) is amended by striking "subsection (a)(8)" and inserting "subsection (e)(3)".

(69) The last sentence of section 403(b)(10) is amended by striking "an direct" and inserting "a direct".

(70) Subparagraph (A) of section 4973(b)(1) is amended by striking "sections 402(c)" and inserting "section 402(c)".

(71) Paragraph (12) of section 3405(e) is amended by striking "(b)(3)" and inserting "(b)(2)".

(72) Paragraph (41) of section 521(b) of the Unemployment Compensation Amendments of 1992 shall be applied as if "section" appeared instead of "sections" in the material proposed to be stricken.

(73) Paragraph (27) of section 521(b) of the Unemployment Compensation Amendments of 1992 shall be applied as if "Section 691(c)(5)" appeared instead of "Section 691(c)".

(74) Paragraph (5) of section 860F(a) is amended by striking "paragraph (1)" and inserting "paragraph (2)".

(75) Paragraph (1) of section 415(k) is amended by adding "or" at the end of subparagraph (C), by striking subparagraphs (D) and (E), and by redesignating subparagraph (F) as subparagraph (D).

(76) Paragraph (2) of section 404(a) is amended by striking "(18),".

(77) Clause (ii) of section 72(p)(4)(A) is amended to read as follows:

"(ii) SPECIAL RULE.—The term 'qualified employer plan' shall not include any plan which was (or was determined to be) a qualified employer plan or a government plan."

(78) Sections 461(i)(3)(C) and 1274(b)(3)(B)(i) are each amended by striking "section 6662(d)(2)(C)(ii)" and inserting "section 6662(d)(2)(C)(iii)".

(79) Subsection (a) of section 164 is amended by striking the paragraphs relating to the generation-skipping tax and the environmental tax imposed by section 59A and by inserting after paragraph (3) the following new paragraphs:

"(4) The GST tax imposed on income distributions.

"(5) The environmental tax imposed by section 59A."

(u) CERTAIN PROPERTY NOT TREATED AS SECTION 179 PROPERTY.—

(1) IN GENERAL.—Paragraph (1) of section 179(d) is amended by adding at the end thereof the following new sentence: "Such term shall not include any property described in section 50(b) and shall not include air conditioning or heating units and horses."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to property placed in service after May 14, 1996.

I. INTRODUCTION

A. Purpose and Summary

The purpose of the Small Business Job Protection Act is to reduce the tax barriers that interfere with the ability of America's small businesses to grow and create jobs. The bill accomplishes this objective through a variety of provisions that are designed to provide flexibility to and reduced costs for small businesses and their workers. In addition, the pension reforms in the bill will help tens of millions of Americans save for retirement and will make these retirement savings more secure.

The bill includes the following principal provisions: (1) increase in expensing for small business from $17,500 to $25,000; (2) expansion of the FICA tip credit; (3) extension of certain expiring provisions, including the work opportunity tax credit and employer-provided educational assistance; (4) reforms of rules governing S corporations; and (5) extensive pension reforms. The bill also includes other small business-related tax provisions. To offset the cost of these provisions, the bill: (1) phases out and repeals the Puerto Rico and possession tax credit; (2) repeals the 50-percent interest income exclusion for financial institution loans to ESOPs; (3) applies a look-through rules for purposes of characterizing certain subpart F income as unrelated business income; (4) modifies the income forecast method of determining depreciation deductions; (5) modifies the exclusion of damages received on account of personal injury or sickness; and (6) repeals advance refunds of the diesel fuel tax for purchasers of diesel-powered cars, vans, and light trucks. Finally, the bill also contains a number of technical corrections provisions.

B. Background and Need for Legislation

Many of the items contained in the Small Business Job Protection Act were contained in the Balanced Budget Act of 1995 (H.R. 2491), which was passed by the Congress and vetoed by President Clinton. The need for this legislation is as urgent today as it was when Congress passed the Balanced Budget Act of 1995.

Small business are the most vibrant segment of our economy. They are responsible for the lion's share of job growth and ingenuity in this country. However, recordkeeping and other actions required to comply with the tax laws impose significant costs on small businesses. The tax laws should be easier for small businesses to comply with and as small of a burden as possible. Similarly, education and employment opportunity must be strongly encouraged. The Small Business Job Protection Act is an important first step in this regard.

C. Legislative History

Committee bill

H.R. 3448 was introduced by Chairman Archer on May 14, 1996. The bill was considered in a Committee markup on May 14, 1996, and was ordered favorably reported, as amended, by a roll call vote of 33 yeas and 3 nays.

The Chairman's amendment in the nature of a substitute added two provisions to the bill as introduced: (1) clarify that the present-law rule in section 280A permits deductions for expenses related to a storage unit in a taxpayer's home regularly used for inventory or product samples; and (2) prospectively deny expensing for certain property, including property described in section 50(b), air conditioning and heating units, and horses.

In addition, the Committee approved four other amendments (by voice vote) to the Chairman's amendment in the nature of a substitute: (1) an amendment by Mr. Crane to provide an exception if there is a binding contract negotiated before the October 13, 1995, effective date of the bill's repeal of the 50-percent interest exclusion for employee stock ownership plan loans; (2) an amendment by Mr. Thomas (California) to provide tax-exempt status for certain charitable risk pool organizations operated solely to pool insurance risks of section 501(c)(3) charitable organizations; (3) an amendment by Mr. Camp to exclude from unrelated business income certain dues paid to agricultural and horticultural organizations; and (4) an amendment by Mr. Neal relating to the employment tax status of certain fishermen who receive compensation in the form of a portion of the catch, with a revenue offset to require reporting on certain purchases of fish. The Committee approved the Chairman's amendment in the nature of a substitute, as amended, by voice vote.

Committee hearings

Committee hearings have been held during the 104th Congress related to various provisions of the bill.

Full Committee hearings were held on January 5 and 10–12, 1995 on the "Contract With America" revenue provisions generally, and January 24–26 and 31, and February 1, 1995, on savings and investment provisions. The increased expensing for small business was included in these hearings. Oversight Subcommittee held a hearing on expiring tax provisions on May 9, 1995. The subchapter S and pension simplification provisions were derived from previous Committee tax simplification provisions. These provisions, and the revenue-offset provisions, were also included in the Balanced Budget Act of 1995 as passed by the Congress and vetoed by the President.

II. EXPLANATION OF THE BILL

SMALL BUSINESS AND OTHER TAX PROVISIONS

A. Small Business Provisions

1. Increase in expensing for small businesses (sec. 1111 of the bill and sec. 179 of the Code)

Present Law

In lieu of depreciation, a taxpayer with a sufficiently small amount of annual investment may elect to deduct up to $17,500 of the cost of qualifying property placed in service for the taxable year (sec. 179).[1] In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. The $17,500 amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable year exceeds $200,000. In addition, the amount eligible to be expensed for a taxable year may not exceed the taxable income of the taxpayer for the year that is derived from the active conduct of a trade or business (determined without regard to this provision). Any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding taxable years (subject to similar limitations).

Reasons for Change

The Committee believes that section 179 expensing provides two important benefits for small businesses. First, it lowers the cost of capital for tangible property used in a trade or business. Second, it eliminates depreciation recordkeeping requirements with respect to expensed property. The Committee would enhance these benefits by increasing the amount allowed to be expensed under section 179.

Explanation of Provision

The bill increases the $17,500 amount allowed to be expensed under Code section 179 to $25,000. The increase is phased in as follows:

Taxable year beginning in—	*Maximum expensing*
1996	$18,500
1997	19,000
1998	20,000
1999	21,000
2000	22,000

[1] The amount permitted to be expensed under Code section 179 is increased by up to an additional $20,000 for certain property placed in service by a business located in an empowerment zone (sec. 1397A).

Taxable year beginning in—	Maximum expensing
2001	23,000
2002	23,500
2003 and thereafter	25,000

Effective Date

The provision is effective for property placed in service in taxable years beginning after December 31, 1995, subject to the phase-in schedule set forth above.

2. Tax credit for Social Security taxes paid with respect to employee cash tips (sec. 1112 of the bill and sec. 45B of the Code)

Present Law

Employee tip income is treated as employer-provided wages for purposes of the Federal Insurance Contributions Act ("FICA"). Employees are required to report to the employer the amount of tips received. The Omnibus Budget Reconciliation Act of 1993 ("OBRA 1993") provided a business tax credit with respect to certain employer FICA taxes paid with respect to tips treated as paid by the employer. The credit applies to tips received from customers in connection with the provision of food or beverages for consumption on the premises of an establishment with respect to which the tipping of employees is customary. OBRA 1993 provided that the FICA tip credit is effective for taxes paid after December 31, 1993. Temporary Treasury regulations provide that the tax credit is available only with respect to tips reported by the employee. The temporary regulations also provide that the credit is effective for FICA taxes paid by an employer after December 31, 1993, with respect to tips received for services performed after December 31, 1993.

Reasons for Change

The Committee believes it appropriate to clarify the effective date and scope of the credit for FICA taxes paid on employer cash tips. Despite the statutory language, there has been some confusion regarding the effective date. The FICA tip credit was included in the Senate version of H.R. 4210, the Tax Fairness and Economic Growth Act of 1992, and was included in the conference agreement of H.R. 4210 as passed by the 102d Congress and vetoed by President Bush. The effective date of that provision would have applied to "tips received and wages paid after the date of enactment." The FICA tip credit was also included in the House and Senate versions of H.R. 11, the Revenue Act of 1992, as considered by the 102d Congress. The effective date of both those provisions was the same as in H.R. 4210, specifically tips received and wages paid after the date of enactment. The provision was included in the conference agreement of the H.R. 11, as adopted by the Congress and vetoed by President Bush; however, the effective date of that provision was modified to apply to "taxes paid after" December 31, 1992, i.e., no limitation with respect to tips earned after December 31, 1992, was included.

In 1993, the House and Senate versions of the Omnibus Budget Reconciliation Act of 1993 ("OBRA 1993") did not contain the FICA

tip provision, but it was included in the conference agreement. The FICA tip provision that was included in OBRA 1993 has the same effective date as the provision in the conference agreement for H.R. 11, except that the date was moved one year, to taxes paid after December 31, 1993. The Committee believes that the legislative history of this provision indicates intent to change the effective date, and that the Treasury's interpretation of that date is not consistent with the provision as finally adopted.

The Committee also believes it appropriate to apply the credit to all persons who provide food and beverages, whether for consumption on or off the premises.

Explanation of Provision

The bill clarifies the credit with respect to employer FICA taxes paid on tips by providing that the credit is (1) available whether or not the employee reported the tips on which the employer FICA taxes were paid pursuant to section 6053(a), and (2) effective with respect to taxes paid after December 31, 1993, regardless of when the services with respect to which the tips are received were performed.

The bill also modifies the credit so that it applies with respect to tips received from customers in connection with the provision of food or beverages, regardless of whether the food or beverages are for consumption on the premises of the establishment.

Effective Date

The clarifications relating to the effective date and nonreported tips are effective as if included in OBRA 1993. The provision expanding the tip credit to the provision of food or beverages not for consumption on the premises of the establishment is effective with respect to FICA taxes paid on tips received with respect to services performed after December 31, 1996.

3. Home office deduction: Treatment of storage of product samples (sec. 1113 of the bill and sec. 280A of the Code)

Present Law

A taxpayer's business use of his or her home may give rise to a deduction for the business portion of expenses related to operating the home (e.g., a portion of rent or depreciation and repairs). Code section 280A(c)(1) provides, however, that business deductions generally are allowed only with respect to a portion of a home that is used exclusively and regularly in one of the following ways: (1) as the principal place of business for a trade or business; (2) as a place of business used to meet with patients, clients, or customers in the normal course of the taxpayer's trade or business; or (3) in connection with the taxpayer's trade or business, if the portion so used constitutes a separate structure not attached to the dwelling unit. In the case of an employee, the Code further requires that the business use of the home must be for the convenience of the employer (sec. 280A(c)(1)). These rules apply to houses, apartments, condominiums, mobile homes, boats, and other similar property used as the taxpayer's home (sec. 280A(f)(1)).

Section 280A(c)(2) contains a special rule that allows a home office deduction for business expenses related to a space within a home that is used on a regular (even if not exclusive) basis as a storage unit for the inventory of the taxpayer's trade or business of selling products at retail or wholesale, but only if the home is the sole fixed location of such trade or business.

Home office deductions may not be claimed if they create (or increase) a net loss from a business activity, although such deductions may be carried over to subsequent taxable years (sec. 280A(c)(5)).

Reasons for Change

The Committee believes that present-law section 280A(c)(2) should be clarified so that taxpayers who sell products at retail or wholesale, and regularly store such products at home, need not attempt to distinguish between inventory and product samples. This clarification will simplify the administration of present-law section 280A(c)(2).

Explanation of Provision

The bill clarifies that the special rule contained in present-law section 280A(c)(2) permits deductions for expenses related to a storage unit in a taxpayer's home regularly used for inventory or product samples (or both) of the taxpayer's trade or business of selling products at retail or wholesale, provided that the home is the sole fixed location of such trade or business.

Effective Date

The provision applies to taxable years beginning after December 31, 1995.

4. Treatment of certain charitable risk pools (sec. 1114 of the bill and new sec. 501(n) of the Code)

Present Law

Organizations described in section 501(c)(3) (which are referred to as "charities") generally are exempt from Federal income tax and are eligible to receive tax-deductible contributions and to use the proceeds of tax-exempt financing. Section 501(c)(3) requires that an organization be organized and operated exclusively for a charitable or other specifically enumerated exempt purpose in order to qualify for tax-exempt status under that section.

Section 501(c)(3) provides that an organization that is organized and operated exclusively for charitable purposes is entitled to tax-exempt status under that section only if the organization satisfies the additional requirements that no part of its net earnings inures to the benefit of any private individual or shareholder (referred to as the "private inurement test") and only if the organization does not engage in political campaign activity on behalf of (or in opposition to) any candidate for public office and does not engage in substantial lobbying activities.

Section 501(m) provides that an organization described in section 501(c)(3) or 501(c)(4) of the Code is exempt from tax only if no sub-

stantial part of its activities consists of providing commercial-type insurance. For purposes of this rule, commercial-type insurance does not include insurance provided at substantially below cost to a class of charitable recipients.

Present law does not specifically accord tax-exempt status to an organization that pools insurable risks of a group of tax-exempt organizations described in section 501(c)(3).

Reasons for Change

The Committee believes that providing tax-exempt status to not-for-profit risk pools whose members are exclusively tax-exempt charitable organizations, and which obtain significant capital from nonmember charitable organizations, will help make liability insurance more affordable to charitable organizations.

Explanation of Provision

Under the bill, a qualified charitable risk pool is treated as organized and operated exclusively for charitable purposes. The provision makes inapplicable to a qualified charitable risk pool the present-law rule under section 501(m) that a charitable organization described in section 501(c)(3) is exempt from tax only if no substantial part of its activities consists of providing commercial-type insurance.

The bill defines a qualified charitable risk pool as an organization organized and operated solely to pool insurable risks of its members (other than medical malpractice risks) and to provide information to its members with respect to loss control and risk management. Because a qualified charitable risk pool must be organized and operated solely to pool insurable risks of its members and to provide information to members with respect to loss control and risk management, no profit or other benefit may be accorded to any member of the organization other than through providing members with insurance coverage below the cost of comparable commercial coverage and through providing members with loss control and risk management information. Only charitable tax-exempt organizations described in section 501(c)(3) may be members of a qualified charitable risk pool.

The bill further requires that a qualified charitable risk pool is required to (1) be organized as a nonprofit organization under State law authorizing risk pooling for charitable organizations; (2) be exempt from State income tax; (3) obtain at least $1 million in start-up capital from nonmember charitable organizations; (4) be controlled by a board of directors elected by its members; and (5) provide in its organizational documents that members must be tax-exempt charitable organizations at all times, and if a member loses that status it must immediately notify the organization, and that no insurance coverage applies to a member after the date of any final determination that the member no longer qualifies as a tax-exempt charitable organization.

To be entitled to tax-exempt status under section 501(c)(3), a qualified charitable risk pool described in the provision also must satisfy the other requirements of that section (i.e., the private

inurement test and the prohibition of political campaign activities and substantial lobbying).

Effective Date

The provision applies to taxable years beginning after the date of enactment.

5. Treatment of dues paid to agricultural or horticultural organizations (sec. 1115 of the bill and sec. 512 of the Code)

Present Law

Tax-exempt organizations generally are subject to the unrelated business income tax ("UBIT") on income derived from a trade or business regularly carried on that is not substantially related to the performance of the organization's tax-exempt functions (secs. 511–514). Dues payments made to a membership organization generally are not subject to the UBIT. However, several courts have held that, with respect to postal labor organizations, dues payments were subject to the UBIT when received from individuals who were not postal workers, but who became "associate" members for the purpose of obtaining health insurance available to members of the organization. See *National League of Postmasters of the United States* v. *Commissioner*, No. 8032–93, T.C. Memo (May 11, 1995); *American Postal Workers Union, AFL–CIO* v. *United States*, 925 F.2d 480 (D.C. Cir. 1991); *National Association of Postal Supervisors* v. *United States*, 944 F.2d 859 (Fed. Cir. 1991).

In Rev. Proc. 95–21 (issued March 23, 1995), the IRS set forth its position regarding when associate member dues payments received by an organization described in section 501(c)(5) will be treated as subject to the UBIT. The IRS stated that dues payments from associate members will not be treated as subject to UBIT unless, for the relevant period, "the associate member category has been formed or availed of for the principal purpose of producing unrelated business income." Thus, under Rev. Proc. 95–21, the focus of the inquiry is upon the organization's purposes in forming the associate member category (and whether the purposes of that category of membership are substantially related to the organization's exempt purposes other than through the production of income) rather than upon the motive of the individuals who join as associate members.

Reasons for Change

The Committee believes that it is appropriate to clarify the treatment of certain limited dues payments from associate members of organizations described in section 501(c)(5) to curtail expensive and time consuming controversies regarding the treatment of such payments for purposes of the UBIT and to facilitate administration of the Code.

Explanation of Provision

Under the bill, if an agricultural or horticultural organization described in section 501(c)(5) requires annual dues not exceeding

$100 to be paid in order to be a member of such organization, then in no event will any portion of such dues be subject to the UBIT by reason of any benefits or privileges to which members of such organization are entitled. For taxable years beginning after 1995, the $100 amount will be indexed for inflation. The term "dues" is defined as "any payment required to be made in order to be recognized by the organization as a member of the organization." Thus, if a person is recognized as a member of an organization by virtue of having paid annual dues for his or her membership, then any subsequent payments made by that person during the year to purchase another membership in the same organization would not be within the scope of the provision.

Effective Date

The provision applies to taxable years beginning after December 31, 1994.

6. Clarify employment tax status of certain fishermen (sec. 1116(a) of the bill and sec. 3121(b)(20) of the Code)

Present Law

Under present law, service as a crew member on a fishing vessel is generally excluded from the definition of employment for purposes of income tax withholding on wages and for purposes of the Federal Insurance Contributions Act (FICA) and the Federal Unemployment Tax Act (FUTA) taxes if the operating crew of the boat normally consists of fewer than 10 individuals, the individual receives a share of the catch based on the total catch, and the individual does not receive cash remuneration other than proceeds from the sale of the individual's share of the catch. Crew members to which the exemption applies are subject to self-employment taxes. Special reporting requirements apply to the operators of boats on which exempt crew members serve.

Reasons for Change

The Committee believes that providing a statutory definition for determining whether the crew of a fishing boat normally consists of fewer than 10 individuals would make the provision easier to apply and administer. Providing that the exemption continues to apply if an individual receives, in addition to a share of the catch, a small amount of cash for certain duties performed would recognize long-standing industry practice.

Explanation of Provision

The operating crew of a boat is treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals. In addition, the exemption applies if the crew member receives, in addition to the cash remuneration permitted under present law, cash remuneration which does not exceed $100 per trip, is contingent on a minimum catch, and is paid solely for additional duties (e.g., as mate, engineer, or cook) for which additional cash remuneration is customary. The reporting

requirements applicable to boat operators are modified to take into account the additional cash remuneration that may be paid under the proposal.

Effective Date

The provision applies to remuneration paid after December 31, 1996. In addition, the provision applies to remuneration paid after December 31, 1984, and before January 1, 1997, unless the payor treated such remuneration when paid as subject to wage withholding and employment taxes.

7. Reporting requirements for purchasers of fish (sec. 1116(b) of the bill and new sec. 6050Q of the Code)

Present Law

Under present law, a person engaged in a trade or business who makes payments during the calendar year of $600 or more to a person for "rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable gains, profits, or other income" must file an information return with the Internal Revenue Service reporting the amount of such payments, as well as the name, address, and taxpayer identification number of the person to whom such payments were made (Code sec. 6041). A similar statement must also be furnished to the person to whom such payments were made. Treasury regulations provide that payments for "merchandise" are not required to be reported under this provision (Treas. reg. sec. 1.6041–3(d)). Consequently, information reporting is generally not required with respect to purchases of fish or other forms of aquatic life. Information reporting is required by a person engaged in a trade or business who, in the course of that trade or business, receives more than $10,000 in cash in one transaction (or several related transactions) (Code sec. 6050I).

Reasons for Change

The Committee believes that requiring information reporting will enhance compliance with the internal revenue laws.

Explanation of Provision

The provision requires persons engaged in the trade or business of purchasing fish for resale who pay more than $600 in cash in a calendar year for fish or other forms of aquatic life from any seller engaged in the trade or business of catching fish to file information reports with the Secretary regarding such purchases. A copy of the report must be provided to the seller.

Effective Date

The provision is effective for purchases made after December 31, 1996.

B. Extension of Certain Expiring Provisions

1. Work opportunity tax credit (sec. 1201 of the bill and sec. 51 of the Code)

Prior Law

General rules

Prior to January 1, 1995, the targeted jobs tax credit was available on an elective basis for employers hiring individuals from one or more of nine targeted groups. The credit generally was equal to 40 percent of qualified first-year wages. Qualified first-year wages consisted of wages attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual began work for the employer. For a vocational rehabilitation referral, however, the period began the day the individual began work for the employer on or after the beginning of the individual's vocational rehabilitation plan.

No more than $6,000 of wages during the first year of employment were permitted to be taken into account with respect to any individual. Thus, the maximum credit per individual was $2,400.

With respect to economically disadvantaged summer youth employees, the credit was equal to 40 percent of up to $3,000 of qualified first-year wages, for a maximum credit of $1,200.

The deduction for wages was reduced by the amount of the credit.

Certification of members of targeted groups

In general, an individual was not treated as a member of a targeted group unless certification that the individual was a member of such a group was received or requested in writing by the employer from the designated local agency on or before the day on which the individual began work for the employer. In the case of a certification of an economically disadvantaged youth participating in a cooperative education program, this requirement was satisfied if the certification was requested or received from the participating school on or before the day on which the individual began work for the employer. The "designated local agency" was the State employment security agency.

If a certification was incorrect because it was based on false information provided as to the employee's membership in a targeted group, the certification was revoked. Wages paid after the revocation notice was received by the employer were not treated as qualified wages.

The U.S. Employment Service, in consultation with the Internal Revenue Service, was directed to take whatever steps necessary to keep employers informed of the availability of the credit.

Targeted groups eligible for the credit

The nine groups eligible for the credit were either recipients of payments under means-tested transfer programs, economically disadvantaged (as measured by family income), or disabled individuals.

(1) Vocational rehabilitation referrals

Vocational rehabilitation referrals were those individuals who had a physical or mental disability that constituted a substantial handicap to employment and who had been referred to the employer while receiving, or after completing, vocational rehabilitation services under an individualized, written rehabilitation plan under a State plan approved under the Rehabilitation Act of 1973, or under a rehabilitation plan for veterans carried out under Chapter 31 of Title 38, U.S. Code. Certification was provided by the designated local employment agency upon assurances from the vocational rehabilitation agency that the employee had met the above conditions.

(2) Economically disadvantaged youths

Economically disadvantaged youths were individuals certified by the designated local employment agency as (1) members of economically disadvantaged families and (2) at least age 18 but not age 23 on the date they were hired by the employer. An individual was determined to be a member of an economically disadvantaged family if, during the six months immediately preceding the earlier of the month in which the determination occurred or the month in which the hiring date occurred, the individual's family income was, on an annual basis, not more than 70 percent of the Bureau of Labor Statistics' lower living standard. A determination that an individual was a member of an economically disadvantaged family was valid for 45 days from the date on which the determination was made.

Except as otherwise noted below, a determination of whether an individual was a member of an economically disadvantaged family was made on the same basis and was subject to the same 45-day limitation, where required in connection with the four other targeted groups that excluded individuals who were not economically disadvantaged.

(3) Economically disadvantaged Vietnam-era veterans

The third targeted group was Vietnam-era veterans certified by the designated local employment agency as members of economically disadvantaged families. For these purposes, a Vietnam-era veteran was an individual who had served on active duty (other than for training) in the Armed Forces for more than 180 days, or who had been discharged or released from active duty in the Armed Forces for a service-connected disability, but in either case, the active duty must have taken place after August 4, 1964, and before May 8, 1975. However, any individual who had served for a period of more than 90 days during which the individual was on active duty (other than for training) was not an eligible employee if any of this active duty occurred during the 60-day period ending on the date the individual was hired by the employer. This latter rule was intended to prevent employers who hired current members of the armed services (or those departed from service within the last 60-days) from receiving the credit.

(4) SSI recipients

The fourth targeted group was individuals receiving either Supplemental Security Income ("SSI") under Title XVI of the Social Security Act or State supplements described in section 1616 of that Act or section 212 of P.L. 93-66. To be an eligible employee, the individual must have received SSI payments during at least a one-month period ending during the 60-day period that ended on the date the individual was hired by the employer. The designated local agency was to issue the certification after a determination by the agency making the payments that these conditions had been fulfilled.

(5) General assistance recipients

General assistance recipients were individuals who received general assistance for a period of not less than 30 days if that period ended within the 60-day period ending on the date the individual was hired by the employer. General assistance programs were State and local programs that provided individuals with money payments, vouchers, or scrip based on need. These programs were referred to by a wide variety of names, including home relief, poor relief, temporary relief, and direct relief. Because of the wide variety of such programs, Congress provided that a recipient was an eligible employee only after the program had been designated by the Secretary of the Treasury as a program that provided money payments, vouchers, or scrip to needy individuals. Certification was performed by the designated local agency.

(6) Economically disadvantaged former convicts

The sixth targeted group included any individual who was certified by the designated local employment agency as (1) having at some time been convicted of a felony under State or Federal law, (2) being a member of an economically disadvantaged family, and (3) having been hired within five years of the later of release from prison or date of conviction.

(7) Economically disadvantaged cooperative education students

The seventh targeted group was youths who (1) actively participated in qualified cooperative education programs, (2) had attained age 16 but had not attained age 20, (3) had not graduated from high school or vocational school, and (4) were members of economically disadvantaged families. The definitions of a qualified cooperative education program and a qualified school were similar to those used in the Vocational Education Act of 1963. Thus, a qualified cooperative education program meant a program of vocational education for individuals who, through written cooperative arrangements between a qualified school and one or more employers, received instruction, including required academic instruction, by alternation of study in school with a job in any occupational field, but only if these two experiences were planned and supervised by the school and the employer so that each experience contributed to the student's education and employability.

For this purpose, a qualified school was (1) a specialized high school used exclusively or principally for the provision of vocational

education to individuals who were available for study in preparation for entering the labor market, (2) the department of a high school used exclusively or principally for providing vocational education to individuals who were available for study in preparation for entering the labor market, or (3) a technical or vocational school used exclusively or principally for the provision of vocational education to individuals who had completed or left high school and who were available for study in preparation for entering the labor market. In order for a nonpublic school to be a qualified school, it must have been exempt from income tax under section 501(a) of the Code.

The certification was performed by the school participating in the cooperative education program. After initial certification, an individual remained a member of the targeted group only while meeting the program participation, age, and degree status requirements of (a), (b), and (c), above.

(8) AFDC recipients

The eighth targeted group included any individual who was certified by the designated local employment agency as being eligible for Aid to Families with Dependent Children ("AFDC") and as having continually received such aid during the 90 days before being hired by the employer.

(9) Economically disadvantaged summer youth employees

The ninth targeted group included youths who performed services during any 90-day period between May 1 and September 15 of a given year and who were certified by the designated local agency as (1) being 16 or 17 years of age on the hiring date and (2) a member of an economically disadvantaged family. A youth must not have been an employee of the employer prior to that 90-day period. With respect to any particular employer, an employee could qualify only one time for this summer youth credit. If, after the end of the 90-day period, the employer continued to employ a youth who was certified during the 90-day period as a member of another targeted group, the limit on qualified first-year wages took into account wages paid to the youth while a qualified summer youth employee.

Definition of wages

In general, wages eligible for the credit were defined by reference to the definition of wages under the Federal Unemployment Tax Act (FUTA) in section 3306(b) of the Code, except that the dollar limits did not apply. Because wages paid to economically disadvantaged cooperative education students and to certain agricultural and railroad employees were not FUTA wages, special rules were provided for these wages.

Wages were taken into account for purposes of the credit only if more than one-half of the wages paid during the taxable year to an employee were for services in the employer's trade or business. The test as to whether more than one-half of an employee's wages were for services in a trade or business was applied to each separate employer without treating related employers as a single employer.

Other rules

In order to prevent taxpayers from eliminating all tax liability by reason of the credit, the amount of the credit could not exceed 90 percent of the taxpayer's income tax liability. Furthermore, the credit was allowed only after certain other nonrefundable credits had been taken. If, after applying these other credits, 90 percent of an employer's remaining tax liability for the year was less than the targeted jobs tax credit, the excess credit could be carried back three years and carried forward 15 years.

All employees of all corporations that were members of a controlled group of corporations were to be treated as if they were employees of the same corporation for purposes of determining the years of employment of any employee and wages for any employee up to $6,000. Generally, under the controlled group rules, the credit allowed the group was the same as if the group were a single company. A comparable rule was provided in the case of partnerships, sole proprietorships, and other trades or businesses (whether or not incorporated) that were under common control, so that all employees of such organizations generally were to be treated as if they were employed by a single person. The amount of targeted jobs tax credit allowable to each member of the controlled group was its proportionate share of the wages giving rise to the credit.

No credit was available for the hiring of certain related individuals (primarily dependents or owners of the taxpayer). The credit was also not available for wages paid to an individual who was employed by the employer at any time during which the individual was not a certified member of a targeted group.

No credit was available for wages paid by an employer to an individual for services that were the same as, or substantially similar to, those services performed by employees participating in, or affected by, a strike or lockout during the period of such strike or lockout. This rule applied to wages paid to individuals whose principal place of employment was a plant or facility where there was a strike or lockout.

No credit was allowed for wages paid unless the eligible individual was either (1) employed by the employer for at least 90 days (14 days in the case of economically disadvantaged summer youth employees) or (2) had completed at least 120 hours (20 hours for summer youth) of services performed for the employer.

Reasons for Change

While the prior-law targeted jobs tax credit was the subject of some criticism, the Committee believes that a tax credit mechanism can provide an important incentive for employers to undertake the expense of providing jobs and training to economically disadvantaged individuals, many of whom are underskilled and/or undereducated. The bill creates a new program whose design will focus on individuals with poor workplace attachments, streamline administrative burdens, promote longer-term employment, and thereby reduce costs relative to the prior-law program. The Committee intends that this short-term program will provide the Congress and the Treasury and Labor Departments an opportunity to

assess fully the operation and effectiveness of the new credit as a hiring incentive.

Explanation of Provision

General rules

The bill replaces the targeted jobs tax credit with the "work opportunity tax credit." The work opportunity tax credit is available on an elective basis for employers hiring individuals from one or more of six targeted groups. The credit generally is equal to 35 percent of qualified wages. Qualified wages consist of wages attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual begins work for the employer. For a vocational rehabilitation referral, however, the period will begin on the day the individual begins work for the employer on or after the beginning of the individual's vocational rehabilitation plan as under prior law.

Generally, no more than $6,000 of wages during the first year of employment is permitted to be taken into account with respect to any individual. Thus, the maximum credit per individual is $2,100. With respect to qualified summer youth employees, the maximum credit is 35 percent of up to $3,000 of qualified first-year wages, for a maximum credit of $1,050.

The deduction for wages is reduced by the amount of the credit.

Certification of members of targeted groups

In general, an individual is not be treated as a member of a targeted group unless: (1) on or before the day the individual begins work for the employer, the employer received in writing a certification from the designated local agency that the individual is a member of a specific targeted group, or (2) on or before the day the individual is offered work with the employer, a pre-screening notice is completed with respect to that individual by the employer and within 14 days after the individual begins work for the employer, the employer submits such notice, signed by the employer and the individual under penalties of perjury, to the designated local agency as part of a written request for certification. The pre-screening notice will contain the information provided to the employer by the individual that forms the basis of the employer's belief that the individual is a member of a targeted group.

If a certification is incorrect because it is based on false information provided as to the individual's membership in a targeted group, the certification will be revoked. No credit will be allowed on wages paid after receipt by the employer of the revocation notice.

If a designated local agency rejects a certification request it will have to provide a written explanation of the basis of the rejection.

Targeted groups eligible for the credit

(1) Families receiving AFDC

An eligible recipient is an individual certified by the designated local employment agency as being a member of a family eligible to receive benefits under AFDC or its successor program for a period of at least nine months part of which is during the 9-month period

ending on the hiring date. For these purposes, each member of the family receiving such assistance is treated as receiving such assistance and therefore is treated as an eligible recipient.

(2) Qualified ex-felon

A qualified ex-felon is an individual certified as: (1) having been convicted of a felony under any State or Federal law, (2) being a member of a family that had an income during the six months before the earlier of the date of determination or the hiring date which on an annual basis is 70 percent or less of the Bureau of Labor Statistics lower living standard, and (3) having a hiring date within one year of release from prison or date of conviction.

(3) High-risk-youth

A high-risk youth is an individual certified as being at least 18 but not 25 on the hiring date and as having a principal place of abode within an empowerment zone or enterprise community (as defined under Subchapter U of the Internal Revenue Code). Qualified wages will not include wages paid or incurred for services performed after the individual moves outside an empowerment zone or enterprise community.

(4) Vocational rehabilitation referral

Vocational rehabilitation referrals are those individuals who have a physical or mental disability that constitutes a substantial handicap to employment and who have been referred to the employer while receiving, or after completing, vocational rehabilitation services under an individualized, written rehabilitation plan under a State plan approved under the Rehabilitation Act of 1973 or under a rehabilitation plan for veterans carried out under Chapter 31 of Title 38, U.S. Code. Certification will be provided by the designated local employment agency upon assurances from the vocational rehabilitation agency that the employee has met the above conditions.

(5) Qualified summer youth employee

Qualified summer youth employees are individuals: (1) who perform services during any 90-day period between May 1 and September 15, (2) who are certified by the designated local agency as being 16 or 17 years of age on the hiring date, (3) who have not been an employee of that employer before, and (4) who are certified by the designated local agency as having a principal place of abode within an empowerment zone or enterprise community (as defined under Subchapter U of the Internal Revenue Code). As with high-risk youths, no credit is available on wages paid or incurred for service performed after the qualified summer youth moves outside of an empowerment zone or enterprise community. If, after the end of the 90-day period, the employer continues to employ a youth who was certified during the 90-day period as a member of another targeted group, the limit on qualified first-year wages will take into account wages paid to the youth while a qualified summer youth employee.

(6) Qualified Veteran

A qualified veteran is a veteran who is a member of a family certified as receiving assistance under: (1) AFDC for a period of at least nine months part of which is during the 12-month period ending on the hiring date, or (2) a food stamp program under the Food Stamp Act of 1977 for a period of at least three months part of which is during the 12-month period ending on the hiring date.

Further, a qualified veteran is an individual who has served on active duty (other than for training) in the Armed Forces for more than 180 days or who has been discharged or released from active duty in the Armed Forces for a service-connected disability. However, any individual who has served for a period of more than 90 days during which the individual was on active duty (other than for training) is not an eligible employee if any of this active duty occurred during the 60-day period ending on the date the individual was hired by the employer. This latter rule is intended to prevent employers who hire current members of the armed services (or those departed from service within the last 60 days) from receiving the credit.

Definition of wages and other rules

In general, wages eligible for the credit are defined by reference to the definition of wages under the Federal Unemployment Tax Act ("FUTA") in section 3306(b) of the Code, except that the dollar limits do not apply.

Wages are taken into account for purposes of the credit only if more than one-half of the wages paid during the taxable year to an employee are for services in the employer's trade or business. The test as to whether more than one-half of an employee's wages are for services in a trade or business are applied to each separate employer without treating related employers as a single employer.

In order to prevent taxpayers from eliminating all tax liability by reason of the credit, the amount of the credit may not exceed 90 percent of the taxpayer's income tax liability. Furthermore, the credit is allowed only after certain other nonrefundable credits had been taken. If, after applying these other credits, 90 percent of an employer's remaining tax liability for the year is less than the targeted jobs tax credit, the excess credit can be carried back three years and carried forward 15 years.

All employees of all corporations that are members of a controlled group of corporations are treated as if they were employees of the same corporation for purposes of determining the years of employment of any employee and wages for any employee up to $6,000. Generally, under the controlled group rules, the credit allowed the group is the same as if the group were a single company. A comparable rule is provided in the case of partnerships, sole proprietorships, and other trades or businesses (whether or not incorporated) that are under common control, so that all employees of such organizations generally are treated as if they was employed by a single person. The amount of the credit allowable to each member of the controlled group is its proportionate share of the wages giving rise to the credit.

No credit is available for the hiring of certain related individuals (primarily dependents or owners of the taxpayer). The credit is also

not available for wages paid to an individual who is employed by the employer at any time during which the individual is not a certified member of a targeted group.

No credit is available for wages paid by an employer to an individual for services that are the same as, or substantially similar to, those services performed by employees participating in, or affected by, a strike or lockout during the period of such strike or lockout. This rule applies to wages paid to individuals whose principal place of employment is a plant or facility where there is a strike or lockout.

Minimum employment period

No credit is allowed for wages paid unless the eligible individual is employed by the employer for at least 180 days (20 days in the case of a qualified summer youth employee) or 500 hours (120 hours in the case of a qualified summer youth employee).

Effective Date

The credit is effective for wages paid or incurred to a qualified individual who begins work for an employer after June 30, 1996, and before July 1, 1997.

2. Employer-provided educational assistance (sec. 1202 of the bill and sec. 127 of the Code)

Present and Prior Law

For taxable years beginning before January 1, 1995, an employee's gross income and wages did not include amounts paid or incurred by the employer for educational assistance provided to the employee if such amounts were paid or incurred pursuant to an educational assistance program that met certain requirements. This exclusion, which expired for taxable years beginning after December 31, 1994, was limited to $5,250 of educational assistance with respect to an individual during a calendar year. The exclusion applied whether or not the education was job related. In the absence of this exclusion, educational assistance is excludable from income only if it is related to the employee's current job.

Reasons for Change

The section 127 exclusion for employer-provided educational assistance was first established on a temporary basis by the Revenue Act of 1978 (through 1983). It subsequently was extended, again on a temporary basis, by Public Law 98–611 (through 1985), by the Tax Reform Act of 1986 (through 1987), by the Technical and Miscellaneous Revenue Act of 1988 (through 1988), by the Omnibus Budget Reconciliation Act of 1989 (through September 30, 1990), by the Omnibus Budget Reconciliation Act of 1990 (through 1991), by the Tax Extension Act of 1991 (through June 30, 1992), and by the Omnibus Budget Reconciliation Act of 1993 (through December 31, 1994). Public Law 98–611 adopted a $5,000 annual limit on the exclusion; this limit was subsequently raised to $5,250 in the Tax Reform Act of 1986. The Technical and Miscellaneous Revenue Act of 1988 made the exclusion inapplicable to graduate-level courses.

The restriction on graduate-level courses was repealed by the Omnibus Budget Reconciliation Act of 1990, effective for taxable years beginning after December 31, 1990.

The Committee believes that the exclusion for employer-provided educational assistance should be extended because it provides needed assistance to workers and aids U.S. competitiveness by encouraging a better-educated work force. The need to balance the Federal budget necessitates some modification to the exclusion, as well as limiting it (as other expiring tax provisions), to a temporary extension. The Committee believes that the exclusion for employer-provided education should be targeted to those most in need of educational assistance—low- and middle-income employees who seek to obtain education which improves their skills and qualifies them for better jobs. Accordingly, the Committee believes it appropriate to reinstate the restriction on graduate-level education. However, due to the past practice of extending the exclusion after it has expired, the Committee is concerned that some taxpayers may have assumed that the exclusion would be available for graduate education during 1995. Thus, the restriction on graduate-level education is effective beginning in 1996.

Explanation of Provision

The bill extends the exclusion for employer-provided educational assistance for taxable years beginning after December 31, 1994, and before January 1, 1997. In years beginning after December 31, 1995, the exclusion would not apply with respect to graduate-level courses.

To the extent employers have previously filed Forms W–2 reporting the amount of educational assistance provided as taxable wages, present Treasury regulations would require the employer to file Forms W–2c (i.e., corrected Forms W–2) with the Internal Revenue Service.[2] It is intended that employers would also be required to provide copies of Form W–2c to affected employees.

The Secretary is directed to establish expedited procedures for the refund of any overpayment of employment taxes paid on excludable educational assistance provided in 1995 and 1996, including procedures for waiving the requirement that an employer obtain an employee's signature if the employer demonstrates to the satisfaction of the Secretary that any refund collected by the employer on behalf of the employee will be paid to the employee.

Because the exclusion is extended, no interest and penalties should be imposed if an employer failed to withhold income and employment taxes on excludable educational assistance or failed to report such educational assistance. Further, it is intended that the Secretary establish expedited procedures for refunding any interest and penalties relating to educational assistance previously paid.

Effective Date

The provision is effective with respect to taxable years beginning after December 31, 1994, and before January 1, 1997, and the re-

[2] Treasury regulation section 31.6051–1(c).

striction of the exclusion to undergraduate education is effective for taxable years beginning after December 31, 1995.

3. Permanent extension of FUTA exemption for alien agricultural workers (sec. 1203 of the bill and sec. 3306 of the Code)

Present Law

Generally, the Federal Unemployment Tax ("FUTA") is imposed on farm operators who (1) employ 10 or more agricultural workers for some portion of each of 20 different days, each day being in a different calendar week or (2) have a quarterly payroll for agricultural services of at least $20,000. An exclusion from FUTA was provided, however, for labor performed by an alien admitted to the United States to perform agricultural labor under section 214(c) and 101(a)(15)(H) of the Immigration and Nationality Act. This exclusion was effective for labor performed before January 1, 1995.

Reasons for Change

The committee believes that the FUTA exemption is appropriate in light of the ineligibility of those workers for FUTA benefits. Further, a permanent extension will provide certainty to taxpayers, ease tax administration, and obviate the need for further short-term extensions.

Explanation of Provision

The bill permanently extends the FUTA exemption for alien agricultural workers.

Effective Date

The provision is effective for labor performed on or after January 1, 1995.

C. Provisions Relating to S Corporations

1. S corporations permitted to have 75 shareholders (sec. 1301 of the bill and sec. 1361 of the Code)

Present Law

The taxable income or loss of an S corporation is taken into account by the corporation's shareholders, rather than by the entity, whether or not such income is distributed. A small business corporation may elect to be treated as an S corporation. A "small business corporation" is defined as a domestic corporation which is not an ineligible corporation and which does not have (1) more than 35 shareholders, (2) as a shareholder, a person (other than certain trusts or estates) who is not an individual, (3) a nonresident alien as a shareholder, and (4) more than one class of stock. For purposes of the 35-shareholder limitation, a husband and wife are treated as one shareholder.

Reasons for Change

The Committee believes that increasing the maximum number of shareholders of an S corporation will facilitate corporate ownership by additional family members, employees and capital investors.

Explanation of Provision

The provision increases maximum number of shareholders from 35 to 75.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

2. Electing small business trusts (sec. 1302 of the bill and sec. 1361 of the Code)

Present Law

Under present law, trusts other than grantor trusts, voting trusts, certain testamentary trusts and "qualified subchapter S trusts" may not be shareholders in a S corporation. A "qualified subchapter S trust" is a trust which, under its terms, (1) is required to have only one current income beneficiary (for life), (2) any corpus distributed during the life of the beneficiary must be distributed to the beneficiary, (3) the beneficiary's income interest must terminate at the earlier of the beneficiary's death or the termination of the trust, and (4) if the trust terminates during the beneficiary's life, the trust assets must be distributed to the beneficiary. All the income (as defined for local law purposes) must be currently distributed to that beneficiary. The beneficiary is treated as the owner of the portion of the trust consisting of the stock in the S corporation.

Reasons for Change

The Committee believes that a trust that provides for income to be distributed to (or accumulated for) a class of individuals should be allowed to hold S corporation stock. This would allow an individual to establish a trust to hold S corporation stock and "spray" income among family members (or others) who are beneficiaries of the trust. The Committee believes allowing such an arrangement will facilitate family financial planning.

Explanation of Provision

In general

The provision allows stock in an S corporation to be held by certain trusts ("electing small business trusts"). In order to qualify for this treatment, all beneficiaries of the trust must be individuals or estates eligible to be S corporation shareholders, except that charitable organizations may hold contingent remainder interests. No interest in the trust may be acquired by purchase. For this purpose, "purchase" means any acquisition of property with a cost

basis (determined under sec. 1012). Thus, interests in the trust must be acquired by reason of gift, bequest, etc.

A trust must elect to be treated as an electing small business trust. An election applies to the taxable year for which made and could be revoked only with the consent of the Secretary of the Treasury or his delegate.

Each potential current beneficiary of the trust is counted as a shareholder for purposes of the proposed 75 shareholder limitation (or if there were no potential current beneficiaries, the trust would be treated as the shareholder). A potential current income beneficiary means any person, with respect to the applicable period, who is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust. Where the trust disposes of all the stock in an S corporation, any person who first became so eligible during the 60 days before the disposition is not treated as a potential current beneficiary.

A qualified subchapter S trust with respect to which an election is in effect or an exempt trust is not eligible to qualify as an electing small business trust.

Treatment of items relating to S corporation stock

The portion of the trust which consists of stock in one or more S corporations is treated as a separate trust for purposes of computing the income tax attributable to the S corporation stock held by the trust. The trust is taxed at the highest individual rate (currently, 39.6 percent on ordinary income and 28 percent on net capital gain) on this portion of the trust's income. The taxable income attributable to this portion includes (1) the items of income, loss, or deduction allocated to it as an S corporation shareholder under the rules of subchapter S, (2) gain or loss from the sale of the S corporation stock, and (3) to the extent provided in regulations, any state or local income taxes and administrative expenses of the trust properly allocable to the S corporation stock. Otherwise allowable capital losses are allowed only to the extent of capital gains.

In computing the trust's income tax on this portion of the trust, no deduction is allowed for amounts distributed to beneficiaries, and no deduction or credit is allowed for any item other than the items described above. This income is not included in the distributable net income of the trust, and thus is not included in the beneficiaries' income. No item relating to the S corporation stock could be apportioned to any beneficiary.

On the termination of all or any portion of an electing small business trust the loss carryovers or excess deductions referred to in section 642(h) is taken into account by the entire trust, subject to the usual rules on termination of the entire trust.

Treatment of remainder of items held by trust

In determining the tax liability with regard to the remaining portion of the trust, the items taken into account by the subchapter S portion of the trust are disregarded. Although distributions from the trust are deductible in computing the taxable income on this portion of the trust, under the usual rules of subchapter J, the trust's distributable net income does not include any income attributable to the S corporation stock.

Termination of trust and conforming amendment applicable to all trusts

Where the trust terminates before the end of the S corporation's taxable year, the trust takes into account its pro rata share of S corporation items for its final year. The bill makes a conforming amendment applicable to all trusts and estates clarifying that this is the present-law treatment of trusts and estates that terminate before the end of the S corporation's taxable year.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

3. Expansion of post-death qualification for certain trusts (sec. 1303 of the bill and sec. 1361 of the Code)

Present Law

Under present law, trusts other than grantor trusts, voting trusts, certain testamentary trusts and "qualified subchapter S trusts" may not be shareholders in a S corporation. A grantor trust may remain an S corporation shareholder for 60 days after the death of the grantor. The 60-day period is extended to 2 years if the entire corpus of the trust is includable in the gross estate of the deemed owner. In addition, a trust may be an S corporation shareholder for 60 days after the transfer of S corporation pursuant to a will.

Reasons for Change

The Committee believes that the 60-day holding period applicable to certain testamentary trusts should be expanded to facilitate estate administration.

Explanation of Provision

The provision expands the post-death holding period to 2 years for all testamentary trusts.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

4. Financial institutions permitted to hold safe harbor debt (sec. 1304 of the bill and sec. 1361 of the Code)

Present Law

A small business corporation eligible to be an S corporation may not have more than one class of stock. Certain debt ("straight debt") is not treated as a second class of stock so long as such debt is an unconditional promise to pay on demand or on a specified date a sum certain in money if: (1) the interest rate (and interest payment dates) are not contingent on profits, the borrower's discretion, or similar factors; (2) there is no convertibility (directly or in-

directly) into stock, and (3) the creditor is an individual (other than a nonresident alien), an estate, or certain qualified trusts.

Reasons for Change

The Committee believes that bona fide debt should not be excluded from the subchapter S safe harbor simply because the debt is held by a financial institution.

Explanation of Provision

The definition of "straight debt" is expanded to include debt held by creditors, other than individuals, that are actively and regularly engaged in the business of lending money.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

5. Rules relating to inadvertent terminations and invalid elections (sec. 1305 of the bill and sec. 1362 of the Code)

Present Law

Under present law, if the Internal Revenue Service ("IRS") determines that a corporation's Subchapter S election is inadvertently terminated, the IRS can waive the effect of the terminating event for any period if the corporation timely corrects the event and if the corporation and shareholders agree to be treated as if the election had been in effect for that period. Such waivers generally are obtained through the issuance of a private letter ruling. Present law does not grant the IRS the ability to waive the effect of an inadvertent invalid Subchapter S election.

In addition, under present law, a small business corporation must elect to be an S corporation no later than the 15th day of the third month of the taxable year for which the election is effective. The IRS may not validate a late election.

Reasons for Change

The Committee believes that the Secretary of the Treasury should have the same authority to validate inadvertently defective subchapter S elections as it has for inadvertent subchapter S terminations.

Explanation of Provision

Under the provision, the authority of the IRS to waive the effect of an inadvertent termination is extended to allow the Service to waive the effect of an invalid election caused by an inadvertent failure to qualify as a small business corporation or to obtain the required shareholder consents (including elections regarding qualified subchapter S trusts), or both. The provision also allows the IRS to treat a late Subchapter S election as timely where the Service determines that there was reasonable cause for the failure to make the election timely. The IRS may exercise this authority in cases where the taxpayer never filed an election. It is intended that the

IRS be reasonable in exercising this authority and apply standards that are similar to those applied under present law to inadvertent subchapter S terminations and other late or invalid elections.

Effective Date

The provision applies to taxable years beginning after December 31, 1982.[3]

6. Agreement to terminate year (sec. 1306 of the bill and sec. 1377 of the Code)

Present Law

In general, each item of S corporation income, deduction and loss is allocated to shareholders on a per-share, per-day basis. However, if any shareholder terminates his or her interest in an S corporation during a taxable year, the S corporation, with the consent of all its shareholders, may elect to allocate S corporation items by closing its books as of the date of such termination rather than apply the per-share, per-day rule.

Reasons for Change

The Committee believes that the election to close the books of an S corporation does not need the consent of a shareholder whose tax liability is unaffected by the election.

Explanation of Provision

The provision provides that, under regulations to be prescribed by the Secretary of the Treasury, the election to close the books of the S corporation upon the termination of a shareholder's interest is made by all affected shareholders and the corporation, rather than by all shareholders. The closing of the books applies only to the affected shareholders. For this purpose, "affected shareholders" means any shareholder whose interest is terminated and all shareholders to whom such shareholder has transferred shares during the year. If a shareholder transferred shares to the corporation, "affected shareholders" includes all persons who were shareholders during the year.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

7. Expansion of post-termination transition period (sec. 1307 of the bill and secs. 1377 and 6037 of the Code)

Present Law

Distributions made by a former S corporation during its post-termination period are treated in the same manner as if the distributions were made by an S corporation (e.g., treated by shareholders as nontaxable distributions to the extent of the accumulated ad-

[3] This is the effective date of the present-law provision regarding inadvertent terminations.

justment account). Distributions made after the post-termination period are generally treated as made by a C corporation (i.e., treated by shareholders as taxable dividends to the extent of earnings and profits).

The "post-termination period" is the period beginning on the day after the last day of the last taxable year of the S corporation and ending on the later of: (1) a date that is one year later, or (2) the due date for filing the return for the last taxable year and the 120-day period beginning on the date of a determination that the corporation's S corporation election had terminated for a previous taxable year.

In addition, the audit procedures adopted by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") with respect to partnerships also apply to S corporations. Thus, the tax treatment of items is determined at the corporate, rather than individual level.

Reasons for Change

The Committee believes that the current scope of the "post-termination period" is insufficient under present law. In addition, the Committee believes that the TEFRA audit procedures should be inapplicable to entities with a limited number of owners.

Explanation of Provision

The present-law definition of post-termination period is expanded to include the 120-day period beginning on the date of any determination pursuant to an audit of the taxpayer that follows the termination of the S corporation's election and that adjusts a subchapter S item of income, loss or deduction of the S corporation during the S period. In addition, the definition of "determination" is expanded to include a final disposition of the Secretary of the Treasury of a claim for refund and, under regulations, certain agreements between the Secretary and any person, relating to the tax liability of the person.

In addition, the provision repeals the TEFRA audit provisions applicable to S corporations and provides other rules to require consistency between the returns of the S corporation and its shareholders.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

8. S corporations permitted to hold subsidiaries (sec. 1308 of the bill and secs. 1361 and 1362 of the Code)

Present Law

A small business corporation may not be a member of an affiliated group of corporations (other than by reason of ownership in certain inactive corporations). Thus, an S corporation may not own 80 percent or more of the stock of another corporation (whether an S corporation or a C corporation).

In addition, a small business corporation may not have as a shareholder another corporation (whether an S corporation or a C corporation).

Reasons for Change

The Committee understands that there are situations where taxpayers may wish to separate different trades or businesses in different corporate entities. The Committee believes that, in such situations, shareholders should be allowed to arrange these separate corporate entities under parent-subsidiary arrangements as well as brother-sister arrangements.

Explanation of Provision

C corporation subsidiaries

An S corporation is allowed to own 80 percent or more of the stock of a C corporation. The C corporation subsidiary could elect to join in the filing of a consolidated return with its affiliated C corporations. An S corporation is not allowed to join in such election. Dividends received by an S corporation from a C corporation in which the S corporation has an 80 percent or greater ownership stake is not treated as passive investment income for purposes of sections 1362 and 1375 to the extent the dividends are attributable to the earnings and profits of the C corporation derived from the active conduct of a trade or business.

S corporation subsidiaries

In addition, an S corporation is allowed to own a qualified subchapter S subsidiary. The term "qualified subchapter S subsidiary" means a domestic corporation that is not an ineligible corporation (i.e., a corporation that would be eligible to be an S corporation if the stock of the corporation were held directly by the shareholders of its parent S corporation) if (1) 100 percent of the stock of the subsidiary were held by its S corporation parent and (2) for which the parent elects to treat as a qualified subchapter S subsidiary. If a subsidiary ceases to be a qualified S corporation subsidiary (either because the subsidiary fails to qualify or the parent revokes the election) another such election may not be made for the subsidiary by the parent for five years without the consent of the Secretary of the Treasury.

Under the election, the qualified subchapter S subsidiary is not treated as a separate corporation and all the assets, liabilities, and items of income, deduction, and credit of the subsidiary are treated as the assets, liabilities, and items of income, deduction, and credit of the parent S corporation. Thus, transactions between the S corporation parent and qualified S corporation subsidiary are not taken into account and items of the subsidiary (including accumulated earnings and profits, passive investment income, built-in gains, etc.) are considered to be items of the parent. In addition, if a subsidiary ceases to be a qualified subchapter S subsidiary (e.g., fails to meet the wholly-owned requirement), the subsidiary will be treated as a new corporation acquiring all of its assets (and

assuming all of its liabilities) immediately before such cessation from the parent S corporation in exchange for its stock.[4]

Under the provision, if an election is made to treat an existing corporation (whether or not its stock was acquired from another person or previously held by the S corporation) as a qualified subchapter S subsidiary, the subsidiary will be deemed to have liquidated under sections 332 and 337 immediately before the election is effective. The built-in gains tax under section 1374 and the LIFO recapture tax under section 1363(d) may apply where the subsidiary was previously a C corporation. Where the stock of the subsidiary was acquired by the S corporation in a qualified stock purchase, an election under section 338 with respect to the subsidiary may be made.

Because the parent and each subsidiary corporation that is a qualified subchapter S subsidiary are treated for Federal income tax purposes as a single corporation, debt issued by a subsidiary to a shareholder of the parent corporation will be treated as debt of the parent for purposes of determining the amount of losses that may flow through to shareholders of the parent corporation under section 1366(d)(1)(B). The Secretary of the Treasury may prescribe rules as to the order that losses pass through where debt of both the parent and subsidiary corporations are held by shareholders of the parent. To the extent a shareholder of the parent S corporation is not at-risk with respect to losses of a subsidiary, the at-risk rules of section 465 may cause losses of the subsidiary to be suspended.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

9. Treatment of distributions during loss years (sec. 1309 of the bill and secs. 1366 and 1368 of the Code)

Present Law

Under present law, the amount of loss an S corporation shareholder may take into account for a taxable year cannot exceed the sum of the shareholder's adjusted basis in his or her stock of the corporation and the adjusted basis in any indebtedness of the corporation to the shareholder. Any excess loss is carried forward.

Any distribution to a shareholder by an S corporation generally is tax-free to the shareholder to the extent of the shareholder's adjusted basis of his or her stock. The shareholder's adjusted basis is reduced by the tax-free amount of the distribution. Any distribution in excess of the shareholder's adjusted basis is treated as gain from the sale or exchange of property.

Under present law, income (whether or not taxable) and expenses (whether or not deductible) serve, respectively, to increase and decrease an S corporation shareholder's basis in the stock of the corporation. These rules require that the adjustments to basis

[4] Similar rules apply with respect to wholly owned subsidiaries of real estate investment trusts (REITs) under section 856(i) of present law.

for items of both income and loss for any taxable year apply before the adjustment for distributions applies.[5]

These rules limiting losses and allowing tax-free distributions up to the amount of the shareholder's adjusted basis are similar in certain respects to the rules governing the treatment of losses and cash distributions by partnerships. Under the partnership rules (unlike the S corporation rules), for any taxable year, a partner's basis is first increased by items of income, then decreased by distributions, and finally is decreased by losses for that year.[6]

In addition, if the S corporation has accumulated earnings and profits,[7] any distribution in excess of the amount in an "accumulated adjustments account" will be treated as a dividend (to the extent of the accumulated earnings and profits). A dividend distribution does not reduce the adjusted basis of the shareholder's stock. The "accumulated adjustments account" generally is the amount of the accumulated undistributed post-1982 gross income less deductions.

Reasons for Change

The Committee believes that the rules regarding the treatment of distributions by S corporations during loss years should be the same as the rules applicable to partnerships.

Explanation of Provision

The provision provides that the adjustments for distributions made by an S corporation during a taxable year are taken into account before applying the loss limitation for the year. Thus, distributions during a year reduce the adjusted basis for purposes of determining the allowable loss for the year, but the loss for a year does not reduce the adjusted basis for purposes of determining the tax status of the distributions made during that year.

The provision also provides that in determining the amount in the accumulated adjustment account for purposes of determining the tax treatment of distributions made during a taxable year by an S corporation having accumulated earnings and profits, net negative adjustments (i.e., the excess of losses and deductions over income) for that taxable year are disregarded.

The following examples illustrate the application of these provisions:

Example 1.—X is the sole shareholder of corporation A, a calendar year S corporation with no accumulated earnings and profits. X's adjusted basis in the stock of A on January 1, 1998, is $1,000 and X holds no debt of A. During 1998, A makes a distribution to X of $600, recognizes a capital gain of $200 and sustains an operating loss of $900. Under the bill, X's adjusted basis in the A stock is increased to $1,200 ($1,000 plus $200 capital gain recognized) pursuant to section 1368(d) to determine the effect of the distribution. X's adjusted basis is then reduced by the amount of the distribution to $600 ($1,200 less $600) to determine the application of

[5] See section 1368(d)(1); H. Rept. 97–826, p. 17; S. Rept. 97–640, p. 18; Treas. Reg. sec. 1.1367–1(e).

[6] Treas. Reg. sec. 1.704–1(d)(2); Rev.Rul. 66-94, 1966–1 C.B. 166.

[7] An S corporation may have earnings and profits from years prior to its subchapter S election or from pre-1983 subchapter S years.

the loss limitation of section 1366(d)(1). X is allowed to take into account $600 of A's operating loss, which reduces X's adjusted basis to zero. The remaining $300 loss is carried forward pursuant to section 1366(d)(2).

Example 2.—The facts are the same as in Example 1, except that on January 1, 1998, A has accumulated earnings and profits of $500 and an accumulated adjustments account of $200. Under the bill, because there is a net negative adjustment for the year, no adjustment is made to the accumulated adjustments account before determining the effect of the distribution under section 1368(c).

As to A, $200 of the $600 distribution is a distribution of A's accumulated adjustments account, reducing the accumulated adjustments account to zero. The remaining $400 of the distribution is a distribution of accumulated earnings and profits ("E & P") and reduces A's E & P to $100. A's accumulated adjustments account is then increased by $200 to reflect the recognized capital gain and reduced by $900 to reflect the operating loss, leaving a negative balance in the accumulated adjustment account on January 1, 1999, of $700 (zero plus $200 less $900).

As to X, $200 of the distribution is applied against X's adjusted basis of $1,200 ($1,000 plus $200 capital gain recognized), reducing X's adjusted basis to $1,000. The remaining $400 of the distribution is taxable as a dividend and does not reduce X's adjusted basis. Because X's adjusted basis is $1,000, the loss limitation does not apply to X, who may deduct the entire $900 operating loss. X's adjusted basis is then decreased to reflect the $900 operating loss. Accordingly, X's adjusted basis on January 1, 1999, is $100 ($1,000 plus $200 less $200 less $900).

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

10. Treatment of S corporations under subchapter C (sec. 1310 of the bill and sec. 1371 of the Code)

Present Law

Present law contains several provisions relating to the treatment of S corporations as corporations generally for purposes of the Internal Revenue Code.

First, under present law, the taxable income of an S corporation is computed in the same manner as in the case of an individual (sec. 1363(b)). Under this rule, the provisions of the Code governing the computation of taxable income which are applicable only to corporations, such as the dividends received deduction, do not apply to S corporations.

Second, except as otherwise provided by the Internal Revenue Code and except to the extent inconsistent with subchapter S, subchapter C (i.e., the rules relating to corporate distributions and adjustments) applies to an S corporation and its shareholders (sec. 1371(a)(1)). Under this second rule, provisions such as the corporate reorganization provisions apply to S corporations. Thus, a C corporation may merge into an S corporation tax-free.

for items of both income and loss for any taxable year apply before the adjustment for distributions applies.[5]

These rules limiting losses and allowing tax-free distributions up to the amount of the shareholder's adjusted basis are similar in certain respects to the rules governing the treatment of losses and cash distributions by partnerships. Under the partnership rules (unlike the S corporation rules), for any taxable year, a partner's basis is first increased by items of income, then decreased by distributions, and finally is decreased by losses for that year.[6]

In addition, if the S corporation has accumulated earnings and profits,[7] any distribution in excess of the amount in an "accumulated adjustments account" will be treated as a dividend (to the extent of the accumulated earnings and profits). A dividend distribution does not reduce the adjusted basis of the shareholder's stock. The "accumulated adjustments account" generally is the amount of the accumulated undistributed post-1982 gross income less deductions.

Reasons for Change

The Committee believes that the rules regarding the treatment of distributions by S corporations during loss years should be the same as the rules applicable to partnerships.

Explanation of Provision

The provision provides that the adjustments for distributions made by an S corporation during a taxable year are taken into account before applying the loss limitation for the year. Thus, distributions during a year reduce the adjusted basis for purposes of determining the allowable loss for the year, but the loss for a year does not reduce the adjusted basis for purposes of determining the tax status of the distributions made during that year.

The provision also provides that in determining the amount in the accumulated adjustment account for purposes of determining the tax treatment of distributions made during a taxable year by an S corporation having accumulated earnings and profits, net negative adjustments (i.e., the excess of losses and deductions over income) for that taxable year are disregarded.

The following examples illustrate the application of these provisions:

Example 1.—X is the sole shareholder of corporation A, a calendar year S corporation with no accumulated earnings and profits. X's adjusted basis in the stock of A on January 1, 1998, is $1,000 and X holds no debt of A. During 1998, A makes a distribution to X of $600, recognizes a capital gain of $200 and sustains an operating loss of $900. Under the bill, X's adjusted basis in the A stock is increased to $1,200 ($1,000 plus $200 capital gain recognized) pursuant to section 1368(d) to determine the effect of the distribution. X's adjusted basis is then reduced by the amount of the distribution to $600 ($1,200 less $600) to determine the application of

[5] See section 1368(d)(1); H. Rept. 97–826, p. 17; S. Rept. 97–640, p. 18; Treas. Reg. sec. 1.1367–1(e).

[6] Treas. Reg. sec. 1.704–1(d)(2); Rev.Rul. 66-94, 1966–1 C.B. 166.

[7] An S corporation may have earnings and profits from years prior to its subchapter S election or from pre-1983 subchapter S years.

the loss limitation of section 1366(d)(1). X is allowed to take into account $600 of A's operating loss, which reduces X's adjusted basis to zero. The remaining $300 loss is carried forward pursuant to section 1366(d)(2).

Example 2.—The facts are the same as in Example 1, except that on January 1, 1998, A has accumulated earnings and profits of $500 and an accumulated adjustments account of $200. Under the bill, because there is a net negative adjustment for the year, no adjustment is made to the accumulated adjustments account before determining the effect of the distribution under section 1368(c).

As to A, $200 of the $600 distribution is a distribution of A's accumulated adjustments account, reducing the accumulated adjustments account to zero. The remaining $400 of the distribution is a distribution of accumulated earnings and profits ("E & P") and reduces A's E & P to $100. A's accumulated adjustments account is then increased by $200 to reflect the recognized capital gain and reduced by $900 to reflect the operating loss, leaving a negative balance in the accumulated adjustment account on January 1, 1999, of $700 (zero plus $200 less $900).

As to X, $200 of the distribution is applied against X's adjusted basis of $1,200 ($1,000 plus $200 capital gain recognized), reducing X's adjusted basis to $1,000. The remaining $400 of the distribution is taxable as a dividend and does not reduce X's adjusted basis. Because X's adjusted basis is $1,000, the loss limitation does not apply to X, who may deduct the entire $900 operating loss. X's adjusted basis is then decreased to reflect the $900 operating loss. Accordingly, X's adjusted basis on January 1, 1999, is $100 ($1,000 plus $200 less $200 less $900).

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

10. Treatment of S corporations under subchapter C (sec. 1310 of the bill and sec. 1371 of the Code)

Present Law

Present law contains several provisions relating to the treatment of S corporations as corporations generally for purposes of the Internal Revenue Code.

First, under present law, the taxable income of an S corporation is computed in the same manner as in the case of an individual (sec. 1363(b)). Under this rule, the provisions of the Code governing the computation of taxable income which are applicable only to corporations, such as the dividends received deduction, do not apply to S corporations.

Second, except as otherwise provided by the Internal Revenue Code and except to the extent inconsistent with subchapter S, subchapter C (i.e., the rules relating to corporate distributions and adjustments) applies to an S corporation and its shareholders (sec. 1371(a)(1)). Under this second rule, provisions such as the corporate reorganization provisions apply to S corporations. Thus, a C corporation may merge into an S corporation tax-free.

Finally, an S corporation in its capacity as a shareholder of another corporation is treated as an individual for purposes of subchapter C (sec. 1371(a)(2)). In 1988, the Internal Revenue Service took the position that this rule prevents the tax-free liquidation of a C corporation into an S corporation because a C corporation cannot liquidate tax-free when owned by an individual shareholder.[8] In 1992, the Internal Revenue Service reversed its position, stating that the prior ruling was incorrect.[9]

Reasons for Change

The Committee wishes to clarify that the position taken by the Internal Revenue Service in 1992 that allows the tax-free liquidation of a C corporation into an S corporation represents the proper policy.

Explanation of Provision

The provision repeals the rule that treats an S corporation in its capacity as a shareholder of another corporation as an individual. Thus, the provision clarifies that the liquidation of a C corporation into an S corporation will be governed by the generally applicable subchapter C rules, including the provisions of sections 332 and 337 allowing the tax-free liquidation of a corporation into its parent corporation. Following a tax-free liquidation, the built-in gains of the liquidating corporation may later be subject to tax under section 1374 upon a subsequent disposition. An S corporation also will be eligible to make a section 338 election (assuming all the requirements are otherwise met), resulting in immediate recognition of all the acquired C corporation's gains and losses (and the resulting imposition of a tax).

The repeal of this rule does not change the general rule governing the computation of income of an S corporation. For example, it does not allow an S corporation, or its shareholders, to claim a dividends received deduction with respect to dividends received by the S corporation, or to treat any item of income or deduction in a manner inconsistent with the treatment accorded to individual taxpayers.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

11. Elimination of certain earnings and profits (sec. 1311 of the bill and secs. 1362 and 1375 of the Code)

Present Law

Under present law, the accumulated earnings and profits of a corporation are not increased for any year in which an election to be treated as an S corporation is in effect. However, under the subchapter S rules in effect before revision in 1982, a corporation electing subchapter S for a taxable year increased its accumulated earn-

[8] PLR 8818049 (Feb. 10, 1988).
[9] PLR 9245004 (July 28, 1992).

ings and profits if its earnings and profits for the year exceeded both its taxable income for the year and its distributions out of that year's earnings and profits. As a result of this rule, a shareholder may later be required to include in his or her income the accumulated earnings and profits when it is distributed by the corporation. The 1982 revision to subchapter S repealed this rule for earnings attributable to taxable years beginning after 1982 but did not do so for previously accumulated S corporation earnings and profits.

Reasons for Change

The Committee believes that the existence of pre-1983 earnings and profits of an S corporation unnecessarily complicates corporate recordkeeping and constitutes a potential trap for the unwary.

Explanation of Provision

The provision provides that if a corporation is an S corporation for its first taxable year beginning after December 31, 1996, the accumulated earnings and profits of the corporation as of the beginning of that year is reduced by the accumulated earnings and profits (if any) accumulated in any taxable year beginning before January 1, 1983, for which the corporation was an electing small business corporation under subchapter S. Thus, such a corporation's accumulated earnings and profits are solely attributable to taxable years for which an S election was not in effect. This rule is generally consistent with the change adopted in 1982 limiting the S shareholder's taxable income attributable to S corporation earnings to his or her share of the taxable income of the S corporation.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

12. Carryover of disallowed losses and deductions under at-risk rules (sec. 1312 of the bill and sec. 1366 of the Code)

Present Law

Under section 1366, the amount of loss an S corporation shareholder may take into account cannot exceed the sum of the shareholder's adjusted basis in his or her stock of the corporation and the unadjusted basis in any indebtedness of the corporation to the shareholder. Any disallowed loss is carried forward to the next taxable year. Any loss that is disallowed for the last taxable year of the S corporation may be carried forward to the post-termination period. The "post-termination period" is the period beginning on the day after the last day of the last taxable year of the S corporation and ending on the later of: (1) a date that is one year later, or (2) the due date for filing the return for the last taxable year and the 120-day period beginning on the date of a determination that the corporation's S corporation election had terminated for a previous taxable year.

In addition, under section 465, a shareholder of an S corporation may not deduct losses that are flowed through from the corporation to the extent the shareholder is not "at-risk" with respect to the

loss. Any loss not deductible in one taxable year because of the at-risk rules is carried forward to the next taxable year.

Reasons for Change

The Committee believes that losses suspended by the at-risk rules should be conformed to the treatment of losses suspended by the subchapter S basis rules.

Explanation of Provision

Losses of an S corporation that are suspended under the at-risk rules of section 465 are carried forward to the S corporation's post-termination period.

Effective Date

The provision applies to taxable years beginning after December 31, 1996.

13. Adjustments to basis of inherited S stock to reflect certain items of income (sec. 1313 of the bill and sec. 1367 of the Code)

Present Law

Income in respect to a decedent ("IRD") generally consists of items of gross income that accrued during the decedent's lifetime but were not includible in the decedent's income before his or her death under his or her method of accounting. IRD is includible in the income of the person acquiring the right to receive such item. A deduction for the estate tax attributable to an item of IRD is allowed to such person (sec. 691(c)). The cost or basis of property acquired from a decedent is its fair market value at the date of death (or alternate valuation date if that date is elected for estate tax purposes). This basis is often referred to as a "stepped-up basis." Property that constitutes a right to receive IRD does not receive a stepped-up basis.

The basis of a partnership interest or corporate stock acquired from a decedent generally is stepped-up at death. Under Treasury regulations, the basis of a partnership interest acquired from a decedent is reduced to the extent that its value is attributable to items constituting IRD (Treas. reg. sec. 1.742–1). This rule insures that the items of IRD held by a partnership are not later offset by a loss arising from a stepped-up basis. Although S corporation income is taxed to its shareholders in a manner similar to the taxation of a partnership and its partners, no comparable regulation requires a reduction in the basis of stock in an S corporation acquired from a decedent where the S corporation holds items of IRD.

Reasons for Change

The Committee believes that the present-law treatment of IRD items of an S corporation is unclear and that the treatment of such items should be similar to the treatment of identical items held by a partnership.

Explanation of Provision

The provision provides that a person acquiring stock in an S corporation from a decedent would treat as IRD his or her pro rata share of any item of income of the corporation that would have been IRD if that item had been acquired directly from the decedent. Where an item is treated as IRD, a deduction for the estate tax attributable to the item generally will be allowed under the provisions of section 691(c). The stepped-up basis in the stock in an S corporation acquired from a decedent is reduced by the extent to which the value of the stock is attributable to items consisting of IRD. This basis rule is comparable to the present-law partnership rule.

Effective Date

The provision applies with respect to decedents dying after the date of enactment.

14. S corporations eligible for rules applicable to real property subdivided for sale by noncorporate taxpayers (sec. 1314 of the bill and sec. 1237 of the Code)

Present Law

Under present-law section 1237, a lot or parcel of land held by a taxpayer other than a corporation generally is not treated as ordinary income property solely by reason of the land being subdivided if (1) such parcel had not previously been held as ordinary income property and if in the year of sale, the taxpayer did not hold other real property; (2) no substantial improvement has been made on the land by the taxpayer, a related party, a lessee, or a government; and (3) the land has been held by the taxpayer for five years.

Reasons for Change

The Committee believes that rules generally applicable to individuals should be applicable to S corporations.

Explanation of Provision

The provision allows the present-law capital gains presumption in the case of land held by an S corporation. It is expected that rules similar to the attribution rules for partnerships will apply to S corporation (Treas. reg. sec. 1.1237–1(b)(3)).

Effective Date

The provision is effective for sales in taxable years beginning after December 31, 1996.

15. Reelecting subchapter S status (sec. 1315 of the bill and sec. 1362 of the Code)

Present Law

A small business corporation that terminates its subchapter S election (whether by revocation or otherwise) may not make an-

other election to be an S corporation for five taxable years unless the Secretary of the Treasury consents to such election.

Reasons for Change

The Committee believes that, given the changes made by the Committee to subchapter S, it is appropriate to allow corporations that terminated their elections under subchapter S within the last five years to re-elect subchapter S status without the consent of the Secretary.

Explanation of Provision

For purposes of the five-year rule, any termination of subchapter S status in effect immediately before the date of enactment of the proposal is not to be taken into account. Thus, any small business corporation that had terminated its S corporation election within the five-year period before the date of enactment may re-elect subchapter S status upon enactment of the bill without the consent of the Secretary of the Treasury.

Effective Date

The provision is effective for terminations occurring in taxable year beginning before January 1, 1997.

PENSION SIMPLIFICATION PROVISIONS; FOREIGN SIMPLIFICATION

A. Simplified Distribution Rules (secs. 1401–1404 of the bill and secs. 72(d), 101(b), 401(a)(9), and 402(d) of the Code)

Present Law

In general, a distribution of benefits from a tax-favored retirement arrangement (i.e., a qualified plan, a qualified annuity plan, and a tax-sheltered annuity contract (sec. 403(b) annuity)) generally is includable in gross income in the year it is paid or distributed under the rules relating to the taxation of annuities.

Lump-sum distributions

Lump-sum distributions from qualified plans and qualified annuity plans are eligible for special 5-year forward averaging. In general, a lump-sum distribution is a distribution within one taxable year of the balance to the credit of an employee that becomes payable to the recipient first, on account of the death of the employee, second, after the employee attains age 59½, third, on account of the employee's separation from service, or fourth, in the case of self-employed individuals, on account of disability. Lump-sum treatment is not available for distributions from a tax-sheltered annuity.

A taxpayer is permitted to make an election with respect to a lump-sum distribution received on or after the employee attains age 59½ to use 5-year forward income averaging under the tax rates in effect for the taxable year in which the distribution is made. In general, this election allows the taxpayer to pay a separate tax on the lump-sum distribution that approximates the tax that would be due if the lump-sum distribution were received in 5

equal installments. If the election is made, the taxpayer is entitled to deduct the amount of the lump-sum distribution from gross income. Only one such election on or after age 59½ may be made with respect to any employee.

$5,000 exclusion for employer-provided death benefits

Under present law, the beneficiary or estate of a deceased employee generally can exclude up to $5,000 in benefits paid by or on behalf of an employer by reason of the employee's death (sec. 101(b)).

Recovery of basis

Amounts received as an annuity under a qualified plan generally are includible in income in the year received, except to the extent they represent the return of the recipient's investment in the contract (i.e., basis). Under present law, a pro-rata basis recovery rule generally applies, so that the portion of any annuity payment that represents nontaxable return of basis is determined by applying an exclusion ratio equal to the employee's total investment in the contract divided by the total expected payments over the term of the annuity.

Under a simplified alternative method provided by the IRS, the taxable portion of qualifying annuity payments is determined under a simplified exclusion ratio method.

In no event can the total amount excluded from income as nontaxable return of basis be greater than the recipient's total investment in the contract.

Required distributions

Present law provides uniform minimum distribution rules generally applicable to all types of tax-favored retirement vehicles, including qualified plans and annuities, IRAs, and tax- sheltered annuities.

Under present law, a qualified plan is required to provide that the entire interest of each participant will be distributed beginning no later than the participant's required beginning date (sec. 401(a)(9)). The required beginning date is generally April 1 of the calendar year following the calendar year in which the plan participant or IRA owner attains age 70½. In the case of a governmental plan or a church plan, the required beginning date is the later of first, such April 1, or second, the April 1 of the year following the year in which the participant retires.

Reasons for Change

In almost all cases, the responsibility for determining the tax liability associated with a distribution from a qualified plan, tax-sheltered annuity, or IRA rests with the individual receiving the distribution. Under present law, this task can be burdensome. Among other things, the taxpayer must consider (1) whether special tax rules apply that reduce the tax that otherwise would be paid, (2) the amount of the taxpayer's basis in the plan, annuity, or IRA and the rate at which such basis is to be recovered, and (3) whether or not a portion of the distribution is excludable from income as a death benefit.

The number of special rules for taxing pension distributions makes it difficult for taxpayers to determine which method is best for them and also increases the likelihood of error. In addition, the specifics of each of the rules create complexity. For example, the present-law rules for determining the rate at which a participant's basis in a qualified plan is recovered often entail calculations that the average participant has difficulty performing. These rules require a fairly precise estimate of the period over which benefits are expected to be paid. The IRS publication on taxation of pension distributions (Publication 939) contains over 60 pages of actuarial tables used to determine total expected payments.

The original intent of the income averaging rules for pension distributions was to prevent a bunching of taxable income because a taxpayer received all of the benefits in a qualified plan in a single taxable year. Liberalization of the rollover rules in the Unemployment Compensation Amendments of 1992 increased taxpayers' ability to determine the time of the income inclusion of pension distributions, and eliminates the need for special rules such as 5-year forward income averaging to prevent bunching of income.

It is inappropriate to require all participants to commence distributions by age 70½ without regard to whether the participant is still employed by the employer. However, the accrued benefit of employees who retire after age 70½ generally should be actuarially increased to take into account the period after age 70½ in which the employee was not receiving benefits.

Explanation of Provisions

Lump-sum distributions

The bill repeals 5-year averaging for lump-sum distributions from qualified plans. Thus, the bill repeals the separate tax paid on a lump-sum distribution and also repeals the deduction from gross income for taxpayers who elect to pay the separate tax on a lump-sum distribution. The bill preserves the transition rules adopted in the Tax Reform Act of 1986.

$5,000 exclusion for employer-provided death benefits

The bill repeals the $5,000 exclusion for employer-provided death benefits.

Recovery of basis

The bill provides that basis recovery on payments from qualified plans generally is determined under a method similar to the present-law simplified alternative method provided by the IRS. The portion of each annuity payment that represents a return of basis equals to the employee's total basis as of the annuity starting date, divided by the number of anticipated payments under the following table:

Age	*Number of payments:*
Not more than 55	360
56–60	310
61–65	260
66–70	210
More than 70	160

Required distributions

The bill modifies the rule that requires all participants in qualified plans to commence distributions by age 70½ without regard to whether the participant is still employed by the employer and generally replaces it with the rule in effect prior to the Tax Reform Act of 1986. Under the bill, distributions generally are required to begin by April 1 of the calendar year following the later of first, the calendar year in which the employee attains age 70½ or second, the calendar year in which the employee retires. However, in the case of a 5-percent owner of the employer, distributions are required to begin no later than the April 1 of the calendar year following the year in which the 5-percent owner attains age 70½.

In addition, in the case of an employee (other than a 5-percent owner) who retires in a calendar year after attaining age 70½, the bill generally requires the employee's accrued benefit to be actuarially increased to take into account the period after age 70½ in which the employee was not receiving benefits under the plan. Thus, under the bill, the employee's accrued benefit is required to reflect the value of benefits that the employee would have received if the employee had retired at age 70½ and had begun receiving benefits at that time.

The actuarial adjustment rule and the rule requiring 5-percent owners to begin distributions after attainment of age 70½ does not apply, under the bill, in the case of a governmental plan or church plan.

Effective Date

Lump-sum distributions

The provision is effective for taxable years beginning after December 31, 1998.

$5,000 exclusion for employer-provided death benefits

The provision applies with respect to decedents dying after date of enactment.

Recovery of basis

The provision is effective with respect to annuity starting dates beginning 90 days after the date of enactment.

Required distributions

The provision is effective for years beginning after December 31, 1996. Under the provision, the Committee intends that a plan (or an annuity contract) could permit, but is not required to permit participants who have already begun to receive distributions but do not have to under the provision, to stop receiving distributions until such distributions are required under the provision.

B. Increased Access to Pension Plans

1. Establish SIMPLE retirement plans (secs. 1421–1422 of the bill and secs. 401(k) and 408(p) of the Code)

Present Law

Present law does not contain rules relating to SIMPLE retirement plans. However, present law does provide a number of ways in which individuals can save for retirement on a tax-favored basis. These include employer-sponsored retirement plans that meet the requirements of the Internal Revenue Code (a "qualified plan") and individual retirement arrangements ("IRAs"). Employees can earn significant retirement benefits under employer-sponsored retirement plans. However, in order to receive tax-favored treatment, such plans must comply with a variety of rules, including complex nondiscrimination and administrative rules (including top-heavy rules). Such plans are also subject to certain requirements under the labor law provisions of the Employee Retirement Income Security Act of 1974 ("ERISA").

IRAs are not subject to the same rules as qualified plans, but the amount that can be contributed in any year is significantly less. The maximum deductible IRA contribution for a year is limited to $2,000. Distributions from IRAs and employer-sponsored retirement plans are generally taxable when made. In addition, distributions prior to age 59½ generally are subject to an additional 10-percent early withdrawal tax.

Contributions to an IRA can also be made by an employer at the election of an employee under a salary reduction simplified employee pension ("SARSEP"). Under SARSEPs, which are not qualified plans, employees can elect to have contributions made to the SARSEP or to receive the contributions in cash. The amount the employee elects to have contributed to the SARSEP is not currently includible in income. The annual amount an employee can elect to contribute to a SARSEP is limited to $9,500 for 1996. This dollar limit is indexed for inflation in $500 increments. The election to have amounts contributed to a SARSEP or received in cash is available only if at least 50 percent of the eligible employees of the employer elect to have amounts contributed to the SARSEP. In addition, such election is available for a taxable year only if the employer maintaining the SARSEP had 25 or fewer eligible employees at all times during the prior taxable year. Elective deferrals under SARSEPs are subject to a special nondiscrimination test.

Under one type of qualified plan that can be maintained by an employer, employees can elect to reduce their taxable compensation and have nontaxable contributions made to the plan. Such contributions are called elective deferrals, and the plans which allow such contributions are called qualified cash or deferred arrangements (or "401(k) plans"). Like SARSEPs, the maximum annual amount of elective deferrals that can be made by an individual is $9,500 for 1996. A special nondiscrimination test applies to elective deferrals. An employer may make contributions based on an employee's elective contributions. Such contributions are called matching contributions, and are subject to a special nondiscrimination

test similar to the special nondiscrimination test applicable to elective deferrals.

Reasons for Change

Retirement plan coverage is lower among small employers than among medium and large employers. The Committee believes that one of the reasons small employers do not establish tax-qualified retirement plans is the complexity of rules relating to such plans and the cost of complying with such rules. The Committee believes it is appropriate to encourage small employers to adopt retirement plans by providing a simplified retirement plan that is not subject to the complex rules applicable to tax-qualified plans.

Among the rules applicable to tax-qualified plans are nondiscrimination rules that help to ensure that plans cover a broad range of employees, not just an employer's highly compensated employees. The Committee believes that the goal of the nondiscrimination rules, broad pension coverage, is an important one. Unfortunately, the complicated nature of these rules may prevent small employers from establishing any plan. The Committee believes that the purposes of the nondiscrimination rules will be served in the case of small employers if all full-time employees are given the opportunity to participate in the plan, the employer is required to match employee contributions, and there are limits on the total contributions that can be made.

The Committee believes that employees should be encouraged to save for retirement, and thus believes a penalty should be imposed on amounts withdrawn within a short period after the retirement plan is adopted.

Explanation of Provision

In general

The bill creates a simplified retirement plan for small business called the savings incentive match plan for employees ("SIMPLE") retirement plan. SIMPLE plans can be adopted by employers who employ 100 or fewer employees on any day during the year and who do not maintain another employer-sponsored retirement plan. A SIMPLE plan can be either an IRA for each employee or part of a qualified cash or deferred arrangement ("401(k) plan"). If established in IRA form, a SIMPLE plan is not subject to the nondiscrimination rules generally applicable to qualified plans (including the top-heavy rules) and simplified reporting requirements apply. Within limits, contributions to a SIMPLE plan are not taxable until withdrawn.

A SIMPLE plan can also be adopted as part of a 401(k) plan. In that case, the plan does not have to satisfy the special nondiscrimination tests applicable to 401(k) plans and is not subject to the top-heavy rules. The other qualified plan rules continue to apply.

SIMPLE retirement plans in IRA form

In general

A SIMPLE retirement plan allows employees to make elective contributions to an IRA. Employee contributions have to be ex-

pressed as a percentage of the employee's compensation, and cannot exceed $6,000 per year. The $6,000 dollar limit is indexed for inflation in $500 increments.

Under the bill, the employer is required to satisfy one of two contribution formulas. Under the matching contribution formula, the employer generally is required to match employee elective contributions on a dollar-for-dollar basis up to 3 percent of the employee's compensation. Under a special rule, the employer could elect a lower percentage matching contribution for all employees (but not less than 1 percent of each employee's compensation). In order for the employer to lower the matching percentage for any year, the employer has to notify employees of the applicable match within a reasonable time before the 30-day election period for the year (described below). In addition, a lower percentage cannot be elected for more than 2 out of any 5 years.

Alternatively, for any year, an employer is permitted to elect, in lieu of making matching contributions, to make a 2 percent of compensation nonelective contribution on behalf of each eligible employee with at least $5,000 in compensation for such year. If such an election were made, the employer has to notify eligible employees of the change within a reasonable period before the 30-day election period for the year (described below). No contributions other than employee elective contributions and required employer matching contributions (or, alternatively, required employer nonelective contributions) can be made to a SIMPLE account.

Only employers who employ 100 or fewer employees on any day during the year and who do not currently maintain a qualified plan can establish SIMPLE retirement accounts for their employees.

Each employee of the employer who received at least $5,000 in compensation from the employer during any 2 prior years and who is reasonably expected to receive at least $5,000 in compensation during the year must be eligible to participate in the SIMPLE plan. Nonresident aliens and employees covered under a collective bargaining agreement do not have to be eligible to participate in the SIMPLE plan. Self-employed individuals can participate in a SIMPLE plan.

All contributions to an employee's SIMPLE account have to be fully vested.

Distributions from a SIMPLE plan generally are taxed as under the rules relating to IRAs, except that an increased early withdrawal tax (25 percent) applies to distributions within the first 2 years the employee first participates in the SIMPLE plan.

Tax treatment of SIMPLE accounts, contributions, and distributions

Contributions to a SIMPLE account generally are deductible by the employer. In the case of matching contributions, the employer will be allowed a deduction for a year only if the contributions are made by the due date (including extensions) for the employer's tax return. Contributions to a SIMPLE account are excludable from the employee's income. SIMPLE accounts, like IRAs, are not subject to tax. Distributions from a SIMPLE retirement account generally are taxed under the rules applicable to IRAs. Thus, they are includible in income when withdrawn. Tax-free rollovers can be made from

one SIMPLE account to another. A SIMPLE account can be rolled over to an IRA on a tax-free basis after a two-year period has expired since the individual first participated in the SIMPLE plan. To the extent an employee is no longer participating in a SIMPLE plan (e.g., the employee has terminated employment), the employee's SIMPLE account will be treated as an IRA.

Early withdrawals from a SIMPLE account generally are be subject to the 10-percent early withdrawal tax applicable to IRAs. However, withdrawals of contributions during the 2-year period beginning on the date the employee first participated in the SIMPLE plan are subject to a 25-percent early withdrawal tax (rather than 10 percent).

Contributions to a SIMPLE account are not subject to employment taxes or income tax withholding.

Administrative requirements

Each eligible employee can elect, within the 30-day period before the beginning of any year (or the 30-day period before first becoming eligible to participate), to participate in the SIMPLE plan (i.e., to make elective deferrals), and to modify any previous elections regarding the amount of contributions. An employer is required to contribute employees' elective deferrals to the employee's SIMPLE account within 30 days after the end of the month to which the contributions relate. Employees must be allowed to terminate participation in the SIMPLE plan at any time during the year (i.e., to stop making contributions). The plan can provide that an employee who terminates participation cannot resume participation until the following year. A plan can permit (but is not required to permit) an individual to make other changes to his or her salary reduction contribution election during the year (e.g., reduce contributions). The Committee intends that an employer is permitted to designate a SIMPLE account trustee to which contributions on behalf of eligible employees are made.

Reporting requirements

Trustee requirements.—The trustee of a SIMPLE account is required each year to prepare, and provide to the employer maintaining the SIMPLE plan, a summary description containing the following basic information about the plan: the name and address of the employer and the trustee; the requirements for eligibility; the benefits provided under the plan; the time and method of making salary reduction elections; and the procedures for and effects of, withdrawals (including rollovers) from the SIMPLE account. At least once a year, the trustee is also required to furnish an account statement to each individual maintaining a SIMPLE account. In addition, the trustee is required to file an annual report with the Secretary. A trustee who fails to provide any of such reports or descriptions will be subject to a penalty of $50 per day until such failure is corrected, unless the failure is due to reasonable cause.

Employer reports.—The employer maintaining a SIMPLE plan is required to notify each employee of the employee's opportunity to make salary reduction contributions under the plan as well as the contribution alternative chosen by the employer immediately before the employee becomes eligible to make such election. This notice

must include a copy of the summary description prepared by the trustee. An employer who fails to provide such notice will be subject to a penalty of $50 per day on which such failure continues, unless the failure is due to reasonable cause.

Definitions

For purposes of the rules relating to SIMPLE plans, compensation means compensation required to be reported by the employer on Form W–2, plus any elective deferrals of the employee. In the case of a self-employed individual, compensation means net earnings from self-employment. The term employer includes the employer and related employers. Related employers includes trades or businesses under common control (whether incorporated or not), controlled groups of corporations, and affiliated service groups. In addition, the leased employee rules apply.

For purposes of the rule prohibiting an employer from establishing a SIMPLE plan, if the employer has another qualified plan, an employer is treated as maintaining a qualified plan if the employer (or a predecessor employer) maintained a qualified plan with respect to which contributions were made, or benefits were accrued, with respect to service for any year in the period beginning with the year the SIMPLE plan became effective and ending with the year for which the determination is being made. A qualified plan includes a qualified retirement plan, a qualified annuity plan, a governmental plan, a tax-sheltered annuity, and a simplified employee pension.

SIMPLE 401(k) plans

In general, under the bill, a cash or deferred arrangement (i.e., 401(k) plan), will be deemed to satisfy the special nondiscrimination tests applicable to employee elective deferrals and employer matching contributions if the plan satisfies the contribution requirements applicable to SIMPLE plans. In addition, the plan is not subject to the top-heavy rules for any year for which this safe harbor is satisfied. The plan is subject to the other qualified plan rules.

The safe harbor is satisfied if, for the year, the employer does not maintain another qualified plan and (1) employee's elective deferrals are limited to no more than $6,000, (2) the employer matches employees' elective deferrals up to 3 percent of compensation (or, alternatively, makes a 2 percent of compensation nonelective contribution on behalf of all eligible employees with at least $5,000 in compensation), and (3) no other contributions are made to the arrangement. Contributions under the safe harbor have to be 100 percent vested. The employer cannot reduce the matching percentage below 3 percent of compensation.

Repeal of SARSEPs

Under the bill, the present-law rules permitting SARSEPs no longer apply after December 31, 1996, unless the SARSEP was established before January 1, 1997. Consequently, an employer is not permitted to establish a SARSEP after December 31, 1996. SARSEPs established before January 1, 1997, can continue to receive contributions under present-law rules, and new employees of

the employer hired after December 31, 1996, can participate in the SARSEP in accordance with such rules.

Effective Date

The provisions relating to SIMPLE plans are effective for years beginning after December 31, 1996.

2. Tax-exempt organizations eligible under section 401(k) (sec. 1426 of the bill and sec. 401(k) of the Code)

Present Law

Under present law, tax-exempt and State and local government organizations are generally prohibited from establishing qualified cash or deferred arrangements (sec. 401(k) plans). Qualified cash or deferred arrangements (1) of rural cooperatives, (2) adopted by State and local governments before May 6, 1986, or (3) adopted by tax-exempt organizations before July 2, 1986, are not subject to this prohibition.

Reasons for Change

Nongovernmental tax-exempt entities should be permitted to maintain qualified cash or deferred arrangements for their employees on the same basis as other employers.

Explanation of Provision

The bill allows tax-exempt organizations (including, for this purpose, Indian tribal governments, a subdivision of an Indian tribal government, an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of such entities) to maintain qualified cash or deferred arrangements. The bill retains the present-law prohibition against the maintenance of cash or deferred arrangements by State and local governments, except to the extent it may apply to Indian tribes.

Effective Date

The provision is effective for plan years beginning after December 31, 1996.

C. Nondiscrimination Provisions

1. Definition of highly compensated employees and repeal of family aggregation rules (sec. 1431 of the bill and secs. 401(a)(17), 404(l), and 414(g) of the Code)

Present Law

Definition of highly compensated employee

An employee, including a self-employed individual, is treated as highly compensated if, at any time during the year or the preceding year, the employee (1) was a 5-percent owner of the employer, (2) received more than $100,000 (for 1996) in annual compensation

from the employer, (3) received more than $66,000 (for 1996) in annual compensation from the employer and was one of the top-paid 20 percent of employees during the same year, or (4) was an officer of the employer who received compensation in excess of $60,000 (for 1996). If, for any year, no officer has compensation in excess of the threshold, then the highest paid officer of the employer is treated as a highly compensated employee.

Family aggregation rules

A special rule applies with respect to the treatment of family members of certain highly compensated employees for purposes of the nondiscrimination rules applicable to qualified plans. Under the special rule, if an employee is a family member of either a 5-percent owner or 1 of the top-10 highly compensated employees by compensation, then any compensation paid to such family member and any contribution or benefit under the plan on behalf of such family member is aggregated with the compensation paid and contributions or benefits on behalf of the 5-percent owner or the highly compensated employee in the top-10 employees by compensation. Therefore, such family member and employee are treated as a single highly compensated employee. An individual is considered a family member if, with respect to an employee, the individual is a spouse, lineal ascendant or descendant, or spouses of a lineal ascendant or descendant of the employee.

Similar family aggregation rules apply with respect to the $150,000 (for 1996) limit on compensation that may be taken into account under a qualified plan (sec. 401(a)(17)) and for deduction purposes (sec. 404(1)). However, under such provisions, only the spouse of the employee and lineal descendants of the employee who have not attained age 19 are taken into account.

Reasons for Change

Under present law, the administrative burden on plan sponsors to determine which employees are highly compensated can be significant. The various categories of highly compensated employees require employers to perform a number of calculations that for many employers have largely duplicative results.

The family aggregation rules impose undue restrictions on the ability of a family-owned small business to provide adequate retirement benefits for all members of the family working for the business. In addition, the complexity of the calculations required under the family aggregation rules appears to be unnecessary in light of the numerous other provisions that ensure that qualified pension plans do not disproportionately favor highly compensated employees.

Explanation of Provisions

Definition of highly compensated employee

Under the bill, an employee is treated as highly compensated if the employee (1) was a 5-percent owner of the employer at any time during the year or the preceding year or (2) had compensation for the preceding year in excess of $80,000 (indexed for inflation) and the employee was in the top 20 percent of employees by com-

pensation for such year. The bill also repeals the rule requiring the highest paid officer to be treated as a highly compensated employee.

Family aggregation rules

The bill repeals the family aggregation rules.

Effective Date

The provisions are effective for years beginning after December 31, 1996.

2. Modification of additional participation requirements (sec. 1432 of the bill and sec. 401(a)(26) of the Code)

Present Law

Under present law, a plan is not a qualified plan unless it benefits no fewer than the lesser of (a) 50 employees of the employer or (b) 40 percent of all employees of the employer (sec. 401(a)(26)). This requirement may not be satisfied by aggregating comparable plans, but may be applied separately to different lines of business of the employer. A line of business of the employer does not qualify as a separate line of business unless it has at least 50 employees.

Reasons for Change

The minimum participation rule was adopted in the Tax Reform Act of 1986 because the Congress believed that it was inappropriate to permit an employer to maintain multiple plans, each of which covered a very small number of employees. Although plans that are aggregated for nondiscrimination purposes are required to satisfy comparability requirements with respect to the amount of contributions or benefits, such an arrangement may still discriminate in favor of highly compensated employees.

However, it is appropriate to better target the minimum participation rule by limiting the scope of the rule to defined benefit pension plans and increasing the minimum number of employees required to be covered under very small plans.

Also, the arbitrary requirement that a line of business must have at least 50 employees requires application of the minimum participation rule on an employer-wide basis in some cases in which the employer truly has separate lines of business.

Explanation of Provision

The bill provides that the minimum participation rule applies only to defined benefit pension plans. In addition, the bill provides that a defined benefit pension plan does not satisfy the rule unless it benefits no fewer than the lesser of (1) 50 employees or (2) the greater of (a) 40 percent of all employees of the employer or (b) 2 employees (1 employee if there is only 1 employee).

The bill provides that the requirement that a line of business has at least 50 employees does not apply in determining whether a plan satisfies the minimum participation rule on a separate line of business basis.

Effective Date

The provision is effective for years beginning after December 31, 1996.

3. Nondiscrimination rules for qualified cash or deferred arrangements and matching contributions (sec. 1433 of the bill and secs. 401(k) and 401(m) of the Code)

Present Law

Under present law, a special nondiscrimination test applies to qualified cash or deferred arrangements (sec. 401(k) plans). The special nondiscrimination test is satisfied if the actual deferral percentage ("ADP") for eligible highly compensated employees for a plan year is equal to or less than either (1) 125 percent of the ADP of all nonhighly compensated employees eligible to defer under the arrangement or (2) the lesser of 200 percent of the ADP of all eligible nonhighly compensated employees or such ADP plus 2 percentage points.

Employer matching contributions and after-tax employee contributions under qualified defined contribution plans are subject to a special nondiscrimination test (the actual contribution percentage ("ACP") test) similar to the special nondiscrimination test applicable to qualified cash or deferred arrangements. Employer matching contributions that satisfy certain requirements can be used to satisfy the ADP test, but, to the extent so used, such contributions cannot be considered when calculating the ACP test.

A plan that would otherwise fail to meet the special nondiscrimination test for qualified cash or deferred arrangements is not treated as failing such test if excess contributions (with allocable income) are distributed to the employee or, in accordance with Treasury regulations, recharacterized as after-tax employee contributions. For purposes of this rule, in determining the amount of excess contributions and the employees to whom they are allocated, the elective deferrals of highly compensated employees are reduced in the order of their actual deferral percentage beginning with those highly compensated employees with the highest actual deferral percentages. A similar rule applies to employer matching contributions.

Reasons for Change

The sources of complexity generally associated with the nondiscrimination requirements for qualified cash or deferred arrangements and matching contributions are the recordkeeping necessary to monitor employee elections, the calculations involved in applying the tests, and the correction mechanism, i.e., what to do if the plan fails the tests.

The Committee believes that the complexity of nondiscrimination requirements, particularly after the Tax Reform Act of 1986 changes that imposed a dollar cap on elective deferrals ($9,500 in 1996), is not justified by the marginal additional participation of rank-and-file employees that might be achieved by the operation of these requirements. The result that the nondiscrimination rules are intended to produce can also be achieved by creating an incen-

tive for employers to provide certain matching contributions or nonelective contributions on behalf of rank-and-file employees. Such contributions should create a sufficient inducement to rank-and-file employee participation. Thus, the Committee believes it is appropriate to provide a design-based safe harbor for qualified cash or deferred arrangements. Plans that satisfy the safe harbors would not have to satisfy the nondiscrimination tests for cash or deferred arrangements.

In addition, the significant simplification that a design-based safe harbor test achieves may reduce the complexity of the qualified cash or deferred arrangement requirements enough to encourage additional employers to establish such plans, thereby expanding employee access to voluntary retirement savings arrangements. The adoption of a nondiscrimination safe harbor that eliminates the testing of actual plan contributions removes a significant administrative burden that may act as a deterrent to employers who would not otherwise set up such a plan. Thus, the adoption of a simpler nondiscrimination test may encourage more employers, particularly small employers, who do not now provide any tax-favored retirement plan for their employees, to set up such plans.

A design-based nondiscrimination test provides certainty to an employer and plan participants that does not exist under present law. Under such a test, an employer will know at the beginning of each plan year whether the plan satisfies the nondiscrimination requirements for the year.

Simplifying the nondiscrimination tests will also reduce administrative burdens for those plans that do not utilize the safe harbor.

Explanation of Provisions

Prior-year data

The bill modifies the special nondiscrimination tests applicable to elective deferrals and employer matching and after-tax employee contributions to provide that the maximum permitted actual deferral percentage (and actual contribution percentage) for highly compensated employees for the year is determined by reference to the actual deferral percentage (and actual contribution percentage) for nonhighly compensated employees for the preceding, rather than the current, year. A special rule applies for the first plan year.

Alternatively, under the bill, an employer is allowed to elect to use the current year actual deferral percentage (and actual contribution percentage). Such an election can be revoked only as provided by the Secretary.

Safe harbor for cash or deferred arrangements

The bill provides that a cash or deferred arrangement satisfies the special nondiscrimination tests if the plan satisfies one of two contribution requirements and satisfies a notice requirement.

A plan satisfies the contribution requirements under the safe harbor rule for qualified cash or deferred arrangements if the plan either first, satisfies a matching contribution requirement or second, the employer makes a nonelective contribution to a defined contribution plan of at least 3 percent of an employee's compensation on behalf of each nonhighly compensated employee who is eli-

gible to participate in the arrangement without regard to whether the employee makes elective contributions under the arrangement.

A plan satisfies the matching contribution requirement if, under the arrangement: first, the employer makes a matching contribution on behalf of each nonhighly compensated employee that is equal to (a) 100 percent of the employee's elective contributions up to 3 percent of compensation and (b) 50 percent of the employee's elective contributions from 3 to 5 percent of compensation; and second, the rate of match with respect to any elective contribution for highly compensated employees is not greater than the rate of match for nonhighly compensated employees.

Alternatively, if the rate of matching contribution with respect to any rate of elective contribution requirement is not equal to the percentages described in the preceding paragraph, the matching contribution requirement will be deemed to be satisfied if first, the rate of an employer's matching contribution does not increase as an employee's rate of elective contribution increases and second, the aggregate amount of matching contributions at such rate of elective contribution at least equals the aggregate amount of matching contributions that would be made if matching contributions satisfied the above percentage requirements. For example, the alternative test will be satisfied if an employer matches 125 percent of an employee's elective contributions up to the first 3 percent of compensation, 25 percent of elective deferrals from 3 to 4 percent of compensation, and provides no match thereafter. However, the alternative test will not be satisfied if an employer matches 80 percent of an employee's elective contributions up to the first 5 percent of compensation. The former example satisfies the alternative test because the employer match does not increase and the aggregate amount of matching contributions at any rate of elective contribution is at least equal to the aggregate amount of matching contributions required under the general safe harbor rule.

Employer matching and nonelective contributions used to satisfy the contribution requirements of the safe harbor rules are required to be nonforfeitable and are subject to the restrictions on withdrawals that apply to an employee's elective deferrals under a qualified cash or deferred arrangement (sec. 401(k)(2)(B) and (C)). It is intended that employer matching and nonelective contributions used to satisfy the contribution requirements of the safe harbor rules can be used to satisfy other qualified retirement plan nondiscrimination rules (except the special nondiscrimination test applicable to employer matching contributions (the ACP test)). So, for example, a cross-tested defined contribution plan that includes a qualified cash or deferred arrangement can consider such employer matching and nonelective contributions in testing. [10]

The notice requirement is satisfied if each employee eligible to participate in the arrangement is given written notice, within a reasonable period before any year, of the employee's rights and obligations under the arrangement.

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[10] The Committee intends that if two plans which include qualified cash or deferred arrangements are treated as one plan for purposes of the nondiscrimination and coverage rules, such qualified cash or deferred arrangements will be treated as one qualified cash or deferred arrangement for purposes of the safe harbor rules. In such a case, unless both qualified cash or deferred arrangements satisfied the safe harbor, both qualified cash or deferred arrangements tested together will have to satisfy the ADP and ACP tests.

Alternative method of satisfying special nondiscrimination test for matching contributions

The bill provides a safe harbor method of satisfying the special nondiscrimination test applicable to employer matching contributions (the ACP test). Under this safe harbor, a plan is treated as meeting the special nondiscrimination test if first, the plan meets the contribution and notice requirements applicable under the safe harbor method of satisfying the special nondiscrimination requirement for qualified cash or deferred arrangements, and second, the plan satisfies a special limitation on matching contributions.

The limitation on matching contributions is satisfied if: first, the employer matching contributions on behalf of any employee may not be made with respect to employee contributions or elective deferrals in excess of 6 percent of compensation; second, the rate of an employer's matching contribution does not increase as the rate of an employee's contributions or elective deferrals increases; and third, the matching contribution with respect to any highly compensated employee at any rate of employee contribution or elective deferral is not greater than that with respect to an employee who is not highly compensated.

Any after-tax employee contributions made under the qualified cash or deferred arrangement will continue to be tested under the ACP test. Employer matching and nonelective contributions used to satisfy the safe harbor rules for qualified cash or deferred arrangements cannot be considered in calculating such test. However, employer matching and nonelective contributions in excess of the amount required to satisfy the safe harbor rules for qualified cash or deferred arrangements can be taken into account in calculating such test.

Distribution of excess contributions and excess aggregate contributions

The bill provides that the total amount of excess contributions (and excess aggregate contributions) is determined as under present law, but the distribution of excess contributions (and excess aggregate contributions) are required to be made on the basis of the amount of contribution by, or on behalf of, each highly compensated employee. Thus, excess contributions (and excess aggregate contributions) are deemed attributable first to those highly compensated employees who have the greatest dollar amount of elective deferrals.

Effective Date

The provisions relating to use of prior-year data and the distribution of excess contributions and excess aggregate contributions are effective for years beginning after December 31, 1996. The provisions providing for a safe harbor for qualified cash or deferred arrangements and the alternative method of satisfying the special nondiscrimination test for matching contributions are effective for years beginning after December 31, 1998.

4. Definition of compensation for purposes of the limits on contributions and benefits (sec. 1434 of the bill and sec. 415 of the Code)

Present Law

Present law imposes limits on contributions and benefits under qualified plans based on the type of plan. For purposes of these limits, present law provides that the definition of compensation generally does not include elective employee contributions to certain employee benefit plans.

Reasons for Change

The Committee believes that not treating employee elective contributions as compensation for purposes of the limits on benefits and contributions under qualified plans unduly restricts the amount that employees, particularly employees who are not highly compensated, can earn under qualified plans.

Explanation of Provision

The bill provides that elective deferrals to section 401(k) plans and similar arrangements, elective contributions to nonqualified deferred compensation plans of tax-exempt employers and State and local governments (sec. 457 plans), and salary reduction contributions to a cafeteria plan are considered compensation for purposes of the limits on contributions and benefits.

Effective Date

The provision is effective for years beginning after December 31, 1997.

D. Miscellaneous Pension Simplification

1. Plans covering self-employed individuals (sec. 1441 of the bill and sec. 401(d) of the Code)

Present Law

Prior to the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA"), different rules applied to retirement plans maintained by incorporated employers and unincorporated employers (such as partnerships and sole proprietors). In general, plans maintained by unincorporated employers were subject to special rules in addition to the other qualification requirements of the Code. Most, but not all, of this disparity was eliminated by TEFRA. Under present law, certain special aggregation rules apply to plans maintained by owner employees of unincorporated businesses that do not apply to other qualified plans (sec. 401(d)(1) and (2)).

Reasons for Change

The remaining special aggregation rules for plans maintained by unincorporated employers are unnecessary and should be eliminated. Applying the same set of rules to all types of plans would make the qualification standards easier to apply and administer.

Explanation of Provision

The bill eliminates the special aggregation rules that apply to plans maintained by self-employed individuals that do not apply to other qualified plans.

Effective Date

The provision is effective for years beginning after December 31, 1996.

2. Elimination of special vesting rule for multiemployer plans (sec. 1442 of the bill and sec. 411(a) of the Code)

Present Law

Under present law, except in the case of multiemployer plans, a plan is not a qualified plan unless a participant's employer-provided benefit vests at least as rapidly as under one of two alternative minimum vesting schedules. A plan satisfies the first schedule if a participant acquires a nonforfeitable right to 100 percent of the participant's accrued benefit derived from employer contributions upon the participant's completion of 5 years of service. A plan satisfies the second schedule if a participant has a nonforfeitable right to at least 20 percent of the participant's accrued benefit derived from employer contributions after 3 years of service, 40 percent at the end of 4 years of service, 60 percent at the end of 5 years of service, 80 percent at the end of 6 years of service, and 100 percent at the end of 7 years of service.

In the case of a multiemployer plan, a participant's accrued benefit derived from employer contributions is required to be 100-percent vested no later than upon the participant's completion of 10 years of service. This special rule applies only to employees covered by the plan pursuant to a collective bargaining agreement.

Reasons for Change

The present-law vesting rules for multiemployer plans add to complexity because there are different vesting schedules for different types of plans, and different vesting schedules for persons within the same multiemployer plan. In addition, the present-law rule prevents some workers from earning a pension under a multiemployer plan. Conforming the multiemployer plan rules to the rules for other plans would mean that workers could earn additional benefits.

Explanation of Provision

The bill conforms the vesting rules for multiemployer plans to the rules applicable to other qualified plans.

Effective Date

The provision is effective for plan years beginning on or after the earlier of (1) the later of January 1, 1997, or the date on which the last of the collective bargaining agreements pursuant to which the plan is maintained terminates, or (2) January 1, 1999, with respect to participants with an hour of service after the effective date.

3. Distributions under rural cooperative plans (sec. 1443 of the bill and sec. 401(k)(7) of the Code)

Present Law

A qualified cash or deferred arrangement can permit withdrawals of employee elective deferrals only after the earlier of (1) the participant's separation from service, death, or disability, (2) termination of the arrangement, or (3) in the case of a profit-sharing or stock bonus plan, the attainment of age 59½ or the occurrence of a hardship of the participant. In the case of a money purchase pension plan, including a rural cooperative plan, withdrawals by participants cannot occur upon attainment of age 59½ or upon hardship.

Reasons for Change

It is appropriate to permit qualified cash or deferred arrangements of rural cooperatives to permit distributions to plan participants under the same circumstances as other qualified cash or deferred arrangements. It is also appropriate to clarify that certain public utility districts and a national association of rural cooperatives should be treated as rural cooperatives for this purpose.

Explanation of Provision

The bill provides that a rural cooperative plan that includes a cash or deferred arrangement may permit distributions to plan participants after the attainment of age 59½ or on account of hardship. In addition, the definition of a rural cooperative is expanded to include certain public utility districts and a national association of rural cooperatives.

Effective Date

The provision generally is effective for distributions after the date of enactment. The modifications to the definition of a rural cooperative apply to plan years beginning after December 31, 1996.

4. Treatment of governmental plans under section 415 (sec. 1444 of the bill and secs. 415 and 457 of the Code)

Present Law

Present law imposes limits on contributions and benefits under qualified plans based on the type of plan (sec. 415). Certain special rules apply to State and local governmental plans under which such plans may provide benefits greater than those permitted by the limits on benefits applicable to plans maintained by private employers.

In the case of defined benefit pension plans, the limit on the annual retirement benefit is the lesser of (1) 100 percent of compensation or (2) $120,000 (indexed for inflation). The dollar limit is reduced in the case of early retirement or if the employee has less than 10 years of plan participation.

Reasons for Change

The limits on contributions and benefits create unique problems for plans maintained by public employers.

Explanation of Provision

The bill makes the following modifications to the limits on contributions and benefits as applied to governmental plans:

(1) the 100 percent of compensation limitation on defined benefit pension plan benefits would not apply; and

(2) the early retirement reduction and the 10-year phase-in of the defined benefit pension plan dollar limit would not apply to certain disability and survivor benefits.

The bill also permits State and local government employers to maintain excess benefit plans without regard to the limits on unfunded deferred compensation arrangements of State and local government employers (sec. 457).

Effective Date

The provision is effective for years beginning after December 31, 1994. No inference is intended with respect to whether a governmental plan complies with the requirements of section 415 with respect to years beginning before January 1, 1995. With respect to such years, the Secretary is directed to enforce the requirements of section 415 consistent with the provision.

5. Uniform retirement age (sec. 1445 of the bill and sec. 401(a)(5) of the Code)

Present Law

A qualified plan generally must provide that payment of benefits under the plan must begin no later than 60 days after the end of the plan year in which the participant reaches age 65. Also, for purpose of the vesting and benefit accrual rules, normal retirement age generally can be no later than age 65. For purposes of applying the limits on contributions and benefits (sec. 415), Social Security retirement age is generally used as retirement age. The Social Security retirement age as used for such purposes is presently age 65, but is scheduled to gradually increase.

Reasons for Change

Many plans base benefits on social security retirement age so that the benefits under the plan complement social security. Under present law, plans that do so may fail applicable nondiscrimination tests. It is believed that the social security retirement age is an appropriate age for use under plans maintained by private employers.

Explanation of Provision

The bill provides that for purposes of the general nondiscrimination rules (sec. 401(a)(4)) the Social Security retirement age (as defined in sec. 415) is a uniform retirement age and that subsidized early retirement benefits and joint and survivor annuities are not treated as not being available to employees on the same terms

merely because they are based on an employee's Social Security retirement age (as defined in sec. 415).

Effective Date

The provision is effective for years beginning after December 31, 1996.

6. Contributions on behalf of disabled employees (sec. 1446 of the bill and sec. 415(c)(3) of the Code)

Present Law

Under present law, an employer may elect to continue deductible contributions to a defined contribution plan on behalf of an employee who is permanently and totally disabled. For purposes of the limit on annual additions (sec. 415(c)), the compensation of a disabled employee is deemed to be equal to the annualized compensation of the employee prior to the employee's becoming disabled. Contributions are not permitted on behalf of disabled employees who were officers, owners, or highly compensated before they became disabled.

Reasons for Change

It is appropriate to facilitate the provision of benefits for disabled employees, if it is done on a nondiscriminatory basis.

Explanation of Provision

The bill provides that the special rule for contributions on behalf of disabled employees is applicable without an employer election and to highly compensated employees if the defined contribution plan provides for the continuation of contributions on behalf of all participants who are permanently and totally disabled.

Effective Date

The provision is effective for years beginning after December 31, 1996.

7. Treatment of deferred compensation plans of State and local governments and tax-exempt organizations (sec. 1447 of the bill and sec. 457(e) of the Code)

Present Law

Under a section 457 plan, an employee who elects to defer the receipt of current compensation is taxed on the amounts deferred when such amounts are paid or made available. The maximum annual deferral under such a plan is the lesser of (1) $7,500 or (2) 33⅓ percent of compensation (net of the deferral).

Amounts deferred under a section 457 plan may not be made available to an employee before the earliest of (1) the calendar year in which the participant attains age 70½, (2) when the participant is separated from the service with the employer, or (3) when the participant is faced with an unforeseeable emergency.

Benefits under a section 457 plan are not treated as made available if the participant may elect to receive a lump sum payable after separation from service and within 60 days of the election. This exception is available only if the total amount payable to the participant under the plan does not exceed $3,500 and no additional amounts may be deferred under the plan with respect to the participant.

Reasons for Change

It is appropriate to index the dollar limits on deferrals under section 457 plans to maintain the value of the deferral and to provide two additional exceptions to the principle of constructive receipt with respect to distributions from such plans.

Explanation of Provision

The bill makes three changes to the rules governing section 457 plans.

The bill: (1) permits in-service distributions of accounts that do not exceed $3,500 under certain circumstances; (2) increases the number of elections that can be made with respect to the time distributions must begin under the plan, and (3) provides for indexing (in $500 increments) of the dollar limit on deferrals.

Effective Date

The provision is effective for taxable years beginning after December 31, 1996.

8. Trust requirement for deferred compensation plans of State and local governments (sec. 1448 of the bill and sec. 457 of the Code)

Present Law

Until deferrals under a section 457 plan are made available to a plan participant, such amounts deferred, all property and rights purchased with such amounts, and all income attributable to such amounts, property, or rights must remain solely the property and rights of the employer, subject only to the claims of the employer's general creditors.

Reasons for Change

The Committee is concerned about the potential for employees of certain State and local governments to lose significant portions of their retirement savings because their employer has chosen to provide benefits through an unfunded deferred compensation plan rather than a qualified pension plan. Therefore, the Committee finds it appropriate to require that benefits under a section 457 plan of a State and local government should be held in a trust (or custodial account or annuity contract) to insulate the retirement benefits of employees from the claims of the employer's creditors.

Explanation of Provision

Under the bill, all amounts deferred under a section 457 plan maintained by a State and local governmental employer have to be held in trust (or custodial account or annuity contract) for the exclusive benefit of employees. The trust (or custodial account or annuity contract) is provided tax-exempt status. Amounts will not be considered made available merely because they are held in a trust, custodial account, or annuity contract.

Effective Date

The provision generally is effective with respect to amounts held on or after the date of enactment. In the case of amounts deferred before the date of enactment, a trust will not need to be established by reason of this provision until January 1, 1999.

9. Correction of GATT interest and mortality rate provisions in the Retirement Protection Act (sec. 1449 of the bill and sec. 767 of the General Agreement on Tariffs and Trade)

Present Law

The Retirement Protection Act of 1994, enacted as part of the implementing legislation for the General Agreement on Tariffs and Trade ("GATT"), modified the actuarial assumptions that must be used in adjusting benefits and limitations. In general, in adjusting a benefit that is payable in a form other than a straight life annuity and in adjusting the dollar limitation if benefits begin before age 62, the interest rate to be used cannot be less than the greater of 5 percent or the rate specified in the plan. Under GATT, if the benefit is payable in a form subject to the requirements of section 417(e)(3), then the interest rate on 30-year Treasury securities is substituted for 5 percent. Also under GATT, for purposes of adjusting any limit or benefit, the mortality table prescribed by the Secretary must be used.

This provision of GATT is generally effective as of the first day of the first limitation year beginning in 1995.

GATT made similar changes to the interest rate and mortality assumptions used to calculate the value of lump-sum distributions for purposes of the rule permitting involuntary dispositions of certain accrued benefits. In the case of a plan adopted and in effect before December 8, 1995, those provisions do not apply before the earlier of (1) the date a plan amendment applying the new assumption is adopted or made effective (whichever is later), or (2) the first day of the first plan year beginning after December 31, 1999.

Reasons for Change

The Committee is aware that the GATT provisions enacted in the 103rd Congress had the result of reducing the benefit payments to certain pension plan beneficiaries. The Committee believes that it is appropriate to ameliorate this result by providing the same transition period for the modifications to limits on contributions and benefits to that provided under similar GATT provisions, and by providing that the interest rate to be used to reduce the dollar limit

on benefits under section 415 in cases where the participant retires before age 62 should be the same regardless of the form of benefit.

Explanation of Provision

The bill conforms the effective date of the new interest rate and mortality assumptions that must be used under section 415 to calculate the limits on benefits and contributions to the effective date of the provision relating to the calculation of lump-sum distributions. This rule applies only in the case of plans that were adopted and in effect before the date of enactment of GATT (December 8, 1994). To the extent plans have already been amended to reflect the new assumptions, plan sponsors are permitted within 1 year of the date of enactment to amend the plan to reverse retroactively such amendment. [11]

The bill also repeals the GATT provision which requires that if the benefit is payable before age 62 in a form subject to the requirements of section 417(e)(3) (e.g., lump sum), then the interest rate to be used to reduce the dollar limit on benefits under section 415 cannot be less than the greater of the rate on 30-year Treasury securities or the rate specified in the plan. Consequently, regardless of the form of benefit, the interest rate to be used cannot be less than the greater of 5 percent or the rate specified in the plan.

Effective Date

The provision is effective as if included in GATT.

10. Multiple salary reduction agreements permitted under section 403(b) (sec. 1450(a) of the bill and sec. 403(b) of the Code)

Present Law

Under Treasury regulations, a participant in a tax-sheltered annuity plan (sec. 403(b)) is not permitted to enter into more than one salary reduction agreement in any taxable year. These regulations further provide that a salary reduction agreement is effective only with respect to amounts "earned" after the agreement becomes effective, and that a salary reduction agreement must be irrevocable with respect to amounts earned while the agreement is in effect.

These restrictions do not apply to other elective deferral arrangements such as a qualified cash or deferred arrangement (sec. 401(k)). Under Treasury regulations, participants in a qualified cash or deferred arrangement may enter into more than one salary reduction agreement in a taxable year, such an agreement is effec-

[11] The Committee intends that plan sponsors will have flexibility in adopting the actuarial assumptions required under GATT. For example, plan sponsors are permitted to apply the actuarial assumptions that must be used for 415 purposes retroactively as provided under GATT. Alternatively, plan sponsors can apply such actuarial assumptions prospectively by either (1) providing a benefit equal to (i) the accrued benefit as of the effective date of the adoption of the new actuarial assumptions determined after applying section 415 using the old actuarial assumptions, plus (ii) the benefit accrued after such effective date determined after applying section 415 using the new actuarial assumptions; or (2) providing a benefit equal to the greater of (i) the accrued benefit as the effective date of the adoption of the new actuarial assumptions determined after applying section 415 using the old actuarial assumptions, or (ii) the entire accrued benefit determined after applying section 415 using the new actuarial assumptions.

tive with respect to compensation currently available to the participant after the agreement becomes effective even though previously "earned," and the agreement may be revoked by the participant.

Reasons for Change

It is appropriate to conform the treatment of salary reduction agreements under section 403(b) to the treatment of qualified cash or deferred arrangements.

Explanation of Provision

The bill provides that for participants in a tax-sheltered annuity plan, the frequency that a salary reduction agreement may be entered into, the compensation to which such agreement applies, and the ability to revoke such agreement shall be determined under the rules applicable to qualified cash or deferred arrangements.

Effective Date

The provision is effective for taxable years beginning after December 31, 1995.

11. Treatment of Indian tribal governments under section 403(b) (sec. 1450(b) of the bill and sec. 403(b) of the Code)

Present Law

Under present law, certain tax-exempt employers and certain State and local government educational organizations are permitted to maintain tax-sheltered annuity plans (sec. 403(b)). Indian tribal governments are treated as States for this purpose, so certain educational organizations associated with a tribal government are eligible to maintain tax-sheltered annuity plans.

Reasons for Change

The Committee believes that there is some uncertainty under present law about the ability of Indian tribal governments to establish 403(b) plans for all tribal government employees. Following enactment of the Indian Tribal Government Tax Status Act of 1982, several insurance companies and financial advisors marketed 403(b) plans to tribes representing that the plans could be adopted on a tribal-wide basis to cover all employees. As a result, many tribes adopted 403(b) plans for their employees that are not in compliance with the law. Given this uncertainty, the Committee believes it is appropriate to requalify such plans.

Explanation of Provision

The bill provides that any 403(b) annuity contract purchased in a plan year beginning before January 1, 1995 by an Indian tribal government shall be treated as purchased by an entity permitted to maintain a tax-sheltered annuity plan. The bill also provides that such contracts may be rolled over into a section 401(k) plan maintained by the Indian tribal government.

Effective Date

The provision is effective on the date of enactment.

12. Application of elective deferral limit to section 403(b) contracts (sec. 1450(c) of the bill and sec. 403(b) of the Code)

Present Law

A tax-sheltered annuity plan must provide that elective deferrals made under the plan on behalf of an employee may not exceed the annual limit on elective deferrals ($9,500 for 1996). Plans that do not comply with this requirement may lose their tax-favored status.

Reasons for Change

The Committee does not believe that employees participating in a tax-sheltered annuity plan should be negatively affected if other employees violate the annual limit on elective deferrals with respect to their individual tax-sheltered annuity contracts (or custodial accounts).

Explanation of Provision

Under the bill, each tax-sheltered annuity contract, not the tax-sheltered annuity plan, must provide that elective deferrals made under the contract may not exceed the annual limit on elective deferrals. The Committee intends that the contract terms be given effect in order for this requirement to be satisfied. Thus, for example, if the annuity contract issuer takes no steps to ensure that deferrals under the contract do not exceed the applicable limit, then the contract will not be treated as satisfying section 403(b). The provision is intended to make clear that the exclusion of elective deferrals from gross income by employees who have not exceeded the annual limit on elective deferrals will not be affected to the extent other employees exceed the annual limit. However, if the occurrence of an uncorrected elective deferral made by an employee is attributable to reasonable error, the contract will not fail to satisfy section 403(b), and only the portion of the elective deferral in excess of the annual limit would be includible in gross income.

Effective Date

The provision is effective for years beginning after December 31, 1995, except that an annuity contract is not required to meet any change in any requirement by reason of the provision before the 90th day after the date of enactment.

13. Waiver of minimum waiting period for qualified plan distributions (sec. 1451 of the bill and sec. 417(c) of the Code)

Present Law

Under present law, in the case of a qualified joint and survivor annuity, a written explanation of the form of benefit must generally be provided to participants no less than 30 days and no more

than 90 days before the annuity starting date. Even if a participant has elected to waive the qualified joint and survivor annuity and the spouse has consented to the distribution, the distribution from the plan cannot be made until 30 days after the written explanation was provided to the participant.[12]

Reasons for Change

The Committee believes that the notice period applicable to a QJSA should not prevent the payment of benefits if such period is waived by the plan participant and, if applicable, the participant's spouse.

Explanation of Provision

The bill provides that the minimum period between the date the explanation of the qualified joint and survivor annuity is provided and the annuity starting date does not apply if it is waived by the participant and, if applicable, the participant's spouse. For example, if the participant has not elected to waive the qualified joint and survivor annuity, only the participant needs to waive the minimum waiting period.

Effective Date

The provision is effective with respect to plan years beginning after December 31, 1996.

14. Repeal of combined plan limit (sec. 1452 of the bill and sec. 415(e) of the Code)

Present Law

Combined plan limit

Present law provides limits on contributions and benefits under qualified retirement plans based on the type of plan (i.e., based on whether the plan is a defined contribution plan or a defined benefit pension plan). An overall limit applies if an individual is a participant in both a defined benefit pension plan and a defined contribution plan (called the combined plan limit).

Excess distribution tax

Present law imposes a 15-percent excise tax on excess distributions from qualified retirement plans, tax-sheltered annuities, and IRAs. Excess distributions are generally the aggregate amount of retirement distributions from such plans during any calendar year in excess of $150,000 (or $750,000 in the case of a lump-sum distribution). An additional 15-percent estate tax is also imposed on an individual's excess retirement accumulation.

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[12] On September 15, 1995, Treasury issued temporary regulations (T.D. 8620) which provide that a plan may permit a participant to elect (with any applicable spousal consent) a distribution with an annuity starting date before 30 days have elapsed since the explanation was provided, as long as the distribution commences more than seven days after the explanation was provided. Consequently, even if the participant (and spouse, if applicable) has elected to waive the minimum waiting period for receiving a qualified plan distribution, the distribution from the plan cannot be made until seven days have elapsed since the explanation was provided to the participant.

Reasons for Change

One of the most significant sources of complexity relating to qualified pension plans is the calculation of the combined plan limit under section 415(e). Many new employers do not establish defined benefit pension plans, which provide employees with the greatest retirement income security. One of the reasons that defined benefit pension plans are not being established is because of the complex rules governing these plans and the significant administrative costs entailed in maintaining them. Section 415(e) is just one of the deterrents to the establishment and maintenance of qualified defined benefit pension plans. Thus, the Committee does not believe that the administrative costs associated with section 415(e) and the complexity of the calculations required are justified. Further, the Committee believes that section 415(e) may have the effect of discouraging employers from providing adequate retirement benefits to their employees.

The excise tax on excess distributions has a similar purpose to the combined plan limit, although it applies to all of an individual's retirement distributions, not just those from a single employer. The Committee believes that both the combined plan limit and the excise tax on excess distributions should not apply at the same time.

Explanation of Provision

Combined plan limit

The bill repeals the combined plan limit.

Excess distribution tax

Until the repeal of the combined plan limit is effective, the bill suspends the excise tax on excess distributions. The additional estate tax on excess accumulations continues to apply.

Effective Date

The provision repealing the combined plan limit is effective with respect to limitation years beginning after December 31, 1998. The provision relating to the excise tax on excess distributions is effective with respect to distributions received in 1996, 1997, and 1998.

15. Tax on prohibited transactions (sec. 1453 of the bill and sec. 4975 of the Code)

Present Law

Present law prohibits certain transactions (prohibited transactions) between a qualified plan and a disqualified person in order to prevent persons with a close relationship to the qualified plan from using that relationship to the detriment of plan participants and beneficiaries. A two-tier excise tax is imposed on prohibited transactions. The initial level tax is equal to 5 percent of the amount involved with respect to the transaction. If the transaction is not corrected within a certain period, a tax equal to 100 percent of the amount involved may be imposed.

Reasons for Change

The Committee believes it is appropriate to increase the initial level prohibited transaction tax to discourage disqualified persons from engaging in such transactions.

Explanation of Provision

The bill increases the initial-level prohibited transaction tax from 5 percent to 10 percent.

Effective Date

The provision is effective with respect to prohibited transactions occurring after the date of enactment.

16. Treatment of leased employees (sec. 1454 of the bill and sec. 414(n) of the Code)

Present Law

An individual (a leased employee) who performs services for another person (the recipient) may be required to be treated as the recipient's employee for various employee benefit provisions, if the services are performed pursuant to an agreement between the recipient and any other person (the leasing organization) who is otherwise treated as the individual's employer (sec. 414(n)). The individual is to be treated as the recipient's employee only if the individual has performed services for the recipient on a substantially full-time basis for a year, and the services are of a type historically performed by employees in the recipient's business field.

An individual who otherwise would be treated as a recipient's leased employee will not be treated as such an employee if the individual participates in a safe harbor plan maintained by the leasing organization meeting certain requirements. Each leased employee is to be treated as an employee of the recipient, regardless of the existence of a safe harbor plan, if more than 20 percent of an employer's nonhighly compensated workforce are leased.

Reasons for Change

The leased employee rules are complex and have unexpected and sometimes indefensible results, especially as interpreted under regulations proposed by the Secretary. For example, under the "historically performed" standard, the employees and partners of a law firm may be the leased employees of a client of the firm if they work a sufficient number of hours for the client and if it is not unusual for employers in that business field to have in-house counsel. While arguably meeting the present-law leased employee definition, it is believed that situations such as this are outside the intended scope of the rules.

Explanation of Provision

Under the bill, the present-law "historically performed" test is replaced with a new test under which an individual is not considered a leased employee unless the individual's services are performed under primary direction or control by the service recipient. As

under present law, the determination of whether someone is a leased employee is made after determining whether the individual is a common-law employee of the recipient. Thus, an individual who is not a common-law employee of the service recipient could nevertheless be a leased employee of the service recipient. Similarly, the fact that a person is or is not found to perform services under primary direction or control of the recipient for purposes of the employee leasing rules is not determinative of whether the person is or is not a common-law employee of the recipient.

Whether services are performed by an individual under primary direction or control by the service recipient depends on the facts and circumstances. In general, primary direction and.control means that the service recipient exercises the majority of direction and control over the individual. Factors that are relevant in determining whether primary direction or control exists include whether the individual is required to comply with instructions of the service recipient about when, where, and how he or she is to perform the services, whether the services must be performed by a particular person, whether the individual is subject to the supervision of the service recipient, and whether the individual must perform services in the order or sequence set by the service recipient. Factors that generally are not relevant in determining whether such direction or control exists include whether the service recipient has the right to hire or fire the individual and whether the individual works for others.

For example, an individual who works under the direct supervision of the service recipient would be considered to be subject to primary direction or control of the service recipient even if another company hired and trained the individual, had the ultimate (but unexercised) legal right to control the individual, paid his wages, withheld his employment and income taxes, and had the exclusive right to fire him. Thus, for example, temporary secretaries, receptionists, word processing personnel and similar office personnel who are subject to the day-to-day control of the employer in essentially the same manner as a common law employee are treated as leased employees if the period of service threshold is reached.

On the other hand, an individual who is a common-law employee of Company A who performs services for Company B on the business premises of Company B under the supervision of Company A would generally not be considered to be under primary direction or control of Company B. The supervision by Company A must be more than nominal, however, and not merely a mechanism to avoid the literal language of the direction or control test.

An example of the situation in the preceding paragraph might be a work crew that comes into a factory to install, repair, maintain, or modify equipment or machinery at the factory. The work crew includes a supervisor who is an employee of the equipment (or equipment repair) company and who has the authority to direct and control the crew, and who actually does exercise such direction and control. In this situation, the supervisor and his or her crew are required to comply with the safety and environmental precautions of the manufacturer, and the supervisor is in frequent communication with the employees of the manufacturer. As another example, certain professionals (e.g., attorneys, accountants,

actuaries, doctors, computer programmers, systems analysts, and engineers) who regularly make use of their own judgement and discretion on matters of importance in the performance of their services and are guided by professional, legal, or industry standards, are not leased employees even though the common law employer does not closely supervise the professional on a continuing basis, and the service recipient requires the services to be performed on site and according to certain stages, techniques, and timetables. In addition to the example above, outside professionals who maintain their own businesses (e.g., attorneys, accountants, actuaries, doctors, computer programmers, systems analysts, and engineers) generally would not be considered to be subject to such primary direction or control.

Under the direction or control test, clerical and similar support staff (e.g., secretaries and nurses in a doctor's office) generally would be considered to be subject to primary direction or control of the service recipient and would be leased employees provided the other requirements of section 414(n) are met.

In many cases, the "historically performed" test is overly broad, and results in the unintended treatment of individuals as leased employees. One of the principal purposes for changing the leased employee rules is to relieve the unnecessary hardship and uncertainty created for employers in these circumstances. However, it is not intended that the direction or control test enable employers to engage in abusive practices. Thus, it is intended that the Secretary interpret and apply the leased employee rules in a manner so as to prevent abuses. This ability to prevent abuses under the leasing rules is in addition to the present-law authority of the Secretary under section 414(o). For example, one potentially abusive situation exists where the benefit arrangements of the service recipient overwhelmingly favor its highly compensated employees, the employer has no or very few nonhighly compensated common-law employees, yet the employer makes substantial use of the services of nonhighly compensated individuals who are not its common-law employees.

Effective Date

The provision is effective for years beginning after December 31, 1996, except that the bill would not apply to relationships that have been previously determined by an IRS ruling not to involve leased employees. In applying the leased employee rules to years beginning before the effective date, it is intended that the Secretary use a reasonable interpretation of the statute to apply the leasing rules to prevent abuse.

17. Uniform penalty provisions to apply to certain pension reporting requirements (sec. 1455 of the bill and secs. 6652(i) and 6724(d) of the Code)

Present Law

Any person who fails to file an information report with the IRS on or before the prescribed filing date is subject to penalties for each failure. A different, flat-amount penalty applies for each failure to provide information reports to the IRS or statements to payees relating to pension payments.

Reasons for Change

Conforming the information-reporting penalties that apply with respect to pension payments to the general information-reporting penalty structure would simplify the overall penalty structure through uniformity and provide more appropriate information-reporting penalties with respect to pension payments.

Explanation of Provision

The bill incorporates into the general penalty structure the penalties for failure to provide information reports relating to pension payments to the IRS and to recipients.

Effective Date

The provision is effective with respect to returns and statements the due date for which is after December 31, 1996.

18. Retirement benefits of ministers not subject to tax on net earnings from self-employment (sec. 1456 of the bill and sec. 1402(a) of the Code)

Present Law

Under present law, certain benefits provided to ministers after they retire are subject to self-employment tax.

Reasons for Change

The Committee believes that, like retirement benefits paid from qualified plans sponsored by private employers, retirement benefits paid from church plans to ministers should not be subject to self-employment tax. The Committee believes this treatment should also apply to the rental value of any parsonage (including utilities) provided after retirement.

Explanation of Provision

The bill provides that retirement benefits received from a church plan after a minister retires, and the rental value of a parsonage (including utilities) furnished to a minister after retirement, are not subject to self-employment taxes.

Effective Date

The provision is effective for years beginning before, on, or after December 31, 1994.

19. Date for adoption of plan amendments (sec. 1457 of the bill)

Present Law

Plan amendments to reflect amendments to the law generally must be made by the time prescribed by law for filing the income tax return of the employer for the employer's taxable year in which the change in law occurs.

Reasons for Change

Plan sponsors should have adequate time to amend plan documents.

Explanation of Provision

The bill generally provides that any amendments to a plan or annuity contract required by the pension simplification bills would not be required to be made before the first plan year beginning on or after January 1, 1997. The date for amendments is extended to the first plan year beginning on or after January 1, 1999, in the case of a governmental plan.

Effective Date

The provision is effective on the date of enactment.

E. Foreign Simplification Provision

1. Repeal of excess passive assets provision (sec. 1501 of the bill and sec. 956A of the Code)

Present Law

Under the rules of subpart F (secs. 951–964), certain 10-percent U.S. shareholders of a controlled foreign corporation (CFC) are required to include in income currently for U.S. tax purposes certain earnings of the CFC, whether or not such earnings are actually distributed currently to the shareholders. The 10-percent U.S. shareholders of a CFC are subject to current U.S. tax on their shares of certain income earned by the CFC (referred to as "subpart F income"). The 10-percent U.S. shareholders are also subject to current U.S. tax on their shares of the CFC's earnings to the extent such earnings are invested by the CFC in certain U.S. property.

In addition to these current inclusion rules, the Omnibus Budget Reconciliation Act of 1993 enacted section 956A, which applies another current inclusion rule to U.S. shareholders of a CFC. Section 956A requires the 10-percent U.S. shareholders of a CFC to include in income currently their shares of the CFC's earnings to the extent such earnings are invested by the CFC in excess passive assets. A CFC generally is treated as having excess passive assets if the average of the amounts of its passive assets exceeds 25 percent of the average of the amounts of its total assets; this calculation requires a quarterly determination of the CFC's passive assets and total assets.

Reasons for Change

With the enactment of section 956A, the 1993 Act added an additional layer of complexity to the subpart F rules. In addition to determining the current inclusions with respect to a CFC's subpart F income and earnings invested in U.S. property, the U.S. shareholders must now also determine the current inclusion with respect to the CFC's earnings invested in excess passive assets. Application of section 956A requires determination and measurement of the CFC's passive assets and total assets on a quarterly basis. The

Committee understands that compliance with section 956A imposes substantial administrative burdens on both taxpayers and the IRS.

The Committee also understands that section 956A was enacted in order to restrict the benefits of tax deferral for CFCs that accumulate passive assets abroad. However, the Committee further understands that the rules of section 956A operate to provide incentives for CFCs to make investments, enter into transactions, and engage in reorganizations for the purpose of avoiding the application of such section. The Committee has been informed that CFCs acquire foreign assets that would not otherwise be attractive investments if such acquisitions reduce the CFC's percentage of passive assets below the threshold for application of section 956A. The Committee has been further informed that some U.S. shareholders of CFCs view section 956A as having the effect of an investment tax credit for foreign investments by CFCs. The Committee is concerned that section 956A provides taxpayers with incentives to engage in costly, non-economic transactions. The Committee is further concerned that section 956A provides incentives for taxpayers to make investments outside the United States that might otherwise be made in the United States. The Committee believes that the administrative burdens of compliance coupled with the costs associated with transactions undertaken to avoid its application call into question the appropriateness of section 956A.

Explanation of Provision

The bill repeals section 956A.

Effective Date

The provision applies to taxable years of foreign corporations beginning after December 31, 1996, and taxable years of U.S. shareholders with or within which such taxable years of foreign corporations end.

1. Phased-in repeal of Puerto Rico and possession tax credit (sec. 1601 of the bill and sec. 936 and new sec. 30A of the Code)

Present Law

Certain domestic corporations with business operations in the U.S. possessions (including, for this purpose, Puerto Rico and the U.S. Virgin Islands) may elect the Puerto Rico and possession tax credit which generally eliminates the U.S. tax on certain income related to their operations in the possessions. In contrast to the foreign tax credit, the possessions tax credit is a "tax sparing" credit. That is, the credit is granted whether or not the electing corporation pays income tax to the possession. Income exempt from U.S. tax under this provision falls into two broad categories: (1) possession business income, which is derived from the active conduct of a trade or business within a U.S. possession or from the sale or exchange of substantially all of the assets that were used in such a trade or business; and (2) qualified possession source investment income ("QPSII"), which is attributable to the investment in the possession or in certain Caribbean Basin countries of funds derived from the active conduct of a possession business.

In order to qualify for the Puerto Rico and possession tax credit for a taxable year, a domestic corporation must satisfy two conditions. First, the corporation must derive at least 80 percent of its gross income for the three-year period immediately preceding the close of the taxable year from sources within a possession. Second, the corporation must derive at least 75 percent of its gross income for that same period from the active conduct of a possession business.

A domestic corporation that has elected the Puerto Rico and possession tax credit and that satisfies these two conditions for a taxable year generally is entitled to a credit based on the U.S. income tax attributable to the sum of the taxpayer's possession business income and its QPSII. However, the amount of the credit attributable to possession business income is subject to the limitations enacted by the Omnibus Budget Reconciliation Act of 1993 ("1993 Act"). Under the economic activity limit, the amount of the credit with respect to such income cannot exceed the sum of a portion of the taxpayer's wage and fringe benefit expenses and depreciation allowances (plus, in certain cases, possession income taxes). In the alternative, the taxpayer may elect to apply a limit equal to the applicable percentage of the credit that would otherwise be allowable with respect to possession business income; the applicable percentage is phased down to 50 percent for 1996, 45 percent for 1997, and 40 percent for 1998 and thereafter. The amount of the Puerto Rico

and possession tax credit attributable to QPSII is not subject to these limitations.

Reasons for Change

The Committee understands that the tax benefits provided by the Puerto Rico and possession tax credit are enjoyed by only the relatively small number of U.S. corporations that operate in the possessions. Moreover, the Committee is concerned about the tax cost of the benefits provided to these possession corporations that is borne by all U.S. taxpayers. In light of current budget constraints, the Committee believes that the continuation of the tax exemption provided to corporations pursuant to the Puerto Rico and possession tax credit is no longer appropriate. However, the Committee believes that an appropriate transition period should be provided for corporations that have existing operations in the possessions. Moreover, the Committee believes that the credit computed under the economic activity limit for Puerto Rico should be moved to a new section of the Code contained in a subpart that includes other business-type credits; the credit computed under the economic activity limit operates as a credit in the traditional sense, measured by the level of employment and other economic activity engaged in by the taxpayer in the possession.

Explanation of Provision

The bill generally repeals the Puerto Rico and possession tax credit for taxable years beginning after December 31, 1995. However, the bill provides grandfather rules under which a corporation that is an existing credit claimant would be eligible to claim credits for a transition period. A special transition rule applies to the credit attributable to operations in Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.

For taxable years beginning after December 31, 1995, the Puerto Rico and possession tax credit applies only to a corporation that qualifies as an existing credit claimant (as defined below). The determination of whether a corporation is an existing credit claimant is made separately for each possession. A corporation that is an existing credit claimant with respect to a possession is entitled to the credit for income from such possession for taxable years beginning after December 31, 1995, subject to the limitations described below. The credit, subject to such limitations, is computed separately for each possession with respect to which the corporation is an existing credit claimant.

The Puerto Rico and possession tax credit attributable to QPSII is eliminated for taxable years beginning after December 31, 1995. For taxable years beginning after December 31, 1995, the Puerto Rico and possession tax credit is available only with respect to possession business income. The computation of the Puerto Rico and possession tax credit attributable to possession business income during the grandfather period depends upon whether the corporation is using the economic activity limit or the applicable percentage limit.

For corporations that are existing credit claimants with respect to a possession and that use the economic activity limit, the posses-

sion tax credit attributable to business income from the possession (determined under the economic activity limit) continues to be determined as under present law for taxable years beginning after December 31, 1995 and before January 1, 2002. For taxable years beginning after December 31, 2001 and before January 1, 2006, the corporation's possession business income that is eligible for the credit is subject to a cap computed as described below. For taxable years beginning in 2006 and thereafter, the credit attributable to possession business income (determined under the economic activity limit) is eliminated.

The bill adds to the Code a new section which provides a credit determined under the economic activity limit for business income from Puerto Rico. Such credit is computed under the rules described above with respect to the possession tax credit determined under the economic activity limit. Such section applies for taxable years beginning after December 31, 1995 and before January 1, 2006.

For corporations that are existing credit claimants with respect to a possession and that elected to use the applicable percentage limit and not to use the economic activity limit, the Puerto Rico and possession tax credit attributable to business income from the possession continues to be determined as under present law for taxable years beginning after December 31, 1995 and before January 1, 1998. For taxable years beginning after December 31, 1997 and before January 1, 2006, the corporation's possession business income that is eligible for the credit is subject to a cap computed as described below. For taxable years beginning in 2006 and thereafter, the credit attributable to possession business income (determined under the applicable percentage limit) is eliminated.

A corporation that had elected to use the applicable percentage limit is permitted to revoke that election under present law. Under the bill, such a revocation is required to be made not later than with respect to the first taxable year beginning after December 31, 1996; such revocation, if made, applies to such taxable year and to all subsequent taxable years. Accordingly, a corporation that had an election in effect to use the applicable percentage limit could revoke such election effective for its taxable year beginning in 1997 and thereafter; such corporation would continue to use the applicable percentage limit for its taxable year beginning in 1996 and would use the economic activity limit for its taxable year beginning in 1997 and thereafter.

The cap on a corporation's possession business income that is eligible for the Puerto Rico and possession tax credit is computed based on the corporation's possession business income for the base period years ("average adjusted base period possession business income"). Average adjusted base period possession business income is the average of the adjusted possession business income for each of the corporation's base period years. For the purpose of this computation, the corporation's possession business income for a base period year is adjusted by an inflation factor that reflects inflation from such year to 1995. In addition, as a proxy for real growth in income throughout the base period, the inflation factor is increased by 5 percentage points compounded for each year from such year

to the corporation's first taxable year beginning on or after October 14, 1995.

The corporation's base period years generally are three of the corporation's five most recent years ending before October 14, 1995, determined by disregarding the taxable years in which the adjusted possession business incomes were highest and lowest. For purposes of this computation, only years in which the corporation had significant possession business income are taken into account. A corporation is considered to have significant possession business income for a taxable year if such income exceeds two percent of the corporation's possession business income for the each of the six taxable years ending with the first taxable year ending on or after October 14, 1995. If the corporation has significant possession business income for only four of the five most recent taxable years ending before October 14, 1995, the base period years are determined by disregarding the year in which the corporation's possession business income was lowest. If the corporation has significant possession business income for three years or fewer of such five years, then the base period years are all such years. If there is no year of such five taxable years in which the corporation has significant possession business income, then the corporation is permitted to use as its base period its first taxable year ending on or after October 14, 1995; for this purpose, the amount of possession business income taken into account is the annualized amount of such income for the portion of the year ended September 30, 1995.

As one alternative, the corporation may elect to use its taxable year ending in 1992 as its base period (with the adjusted possession business income for such year constituting its cap). As another alternative, the corporation may elect to use as its cap the annualized amount of its possession business income for the first ten months of calendar year 1995, calculated by excluding any extraordinary items (as determined under generally accepted accounting principles) for such period. For this purpose, it is intended that transactions with a related party that are not in the ordinary course of business will be considered to be extraordinary items.

If a corporation's possession business income in a year for which the cap is applicable exceeds the cap, then the corporation's possession business income for purposes of computing its Puerto Rico and possession tax credit for the year is an amount equal to the cap. The corporation's credit continues to be subject to either the economic activity limit or the applicable percentage limit, with such limit applied to the corporation's possession business income as reduced to reflect the application of the cap.

A corporation is an existing credit claimant with respect to a possession if (1) the corporation is engaged in the active conduct of a trade or business within the possession on October 13, 1995, and (2) the corporation has elected the benefits of the Puerto Rico and possession tax credit pursuant to an election which is in effect for its taxable year that includes October 13, 1995. A corporation that adds a substantial new line of business after October 13, 1995, ceases to be an existing credit claimant as of the beginning of the taxable year during which such new line of business is added.

For purposes of these rules, a corporation is treated as engaged in the active conduct of a trade or business within a possession on

October 13, 1995, if such corporation is engaged in the active conduct of such trade or business before January 1, 1996, and such corporation has in effect on October 13, 1995, a binding contract for the acquisition of assets to be used in, or the sale of property to be produced in, such trade or business. For example, if a corporation has in effect on October 13, 1995, binding contracts for the lease of a facility and the purchase of machinery to be used in a manufacturing business in a possession and if the corporation begins actively conducting that manufacturing business in the possession before January 1, 1996, that corporation would be an existing credit claimant. A change in the ownership of a corporation will not affect its status as an existing credit claimant.

In determining whether a corporation has added a substantial new line of business, the Committee intends that principles similar to those reflected in Treas. Reg. section 1.7704–2(d) (relating to the transition rules for existing publicly traded partnerships) apply. For example, a corporation that modifies its current production methods, expands existing facilities, or adds new facilities to support the production of its current product lines and products within the same four-digit Industry Number Standard Industrial Classification Code (Industry SIC Code) will not be considered to have added a substantial new line of business. In this regard, the Committee intends that the fact that a business which is added is assigned a different four-digit Industry SIC Code than is assigned to an existing business of the corporation will not automatically cause the corporation to be considered to have added a new line of business. For example, a pharmaceutical corporation that begins manufacturing a new drug will not be considered to have added a new line of business. Moreover, a pharmaceutical corporation that begins to manufacture a complete product from the bulk active chemical through the finished dosage form, a process that may be assigned two separate four-digit Industry SIC Codes, will not be considered to have added a new line of business even though it was previously engaged in activities that involved only a portion of the entire manufacturing process from bulk chemicals to finished dosages. The Committee further intends that, in the case of a merger of affiliated possession corporations that are existing credit claimants, the corporation that survives the merger will not be considered to have added a substantial new line of business by reason of its operation of the existing business of the affiliate that was merged into it.

A special transition rule applies to the Puerto Rico and possession tax credit with respect to operations in Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands. For any taxable year beginning after December 31, 1995, and before January 1, 2006, a corporation that is an existing credit claimant with respect to one of these possessions for such year continues to determine its credit with respect to operations in such possession as under present law. For taxable years beginning in 2006 and thereafter, the Puerto Rico and possession tax credit with respect to operations in Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands is eliminated.

Effective Date

The provision is effective for taxable years beginning after December 31, 1995.

2. Repeal 50-percent interest income exclusion for financial institution loans to ESOPs (sec. 1602 of the bill and sec. 133 of the Code)

Present Law

A bank, insurance company, regulated investment company, or a corporation actively engaged in the business of lending money may generally exclude from gross income 50 percent of interest received on an ESOP loan (sec. 133). The 50-percent interest exclusion only applies if: (1) immediately after the acquisition of securities with the loan proceeds, the ESOP owns more than 50 percent of the outstanding stock or more than 50 percent of the total value of all outstanding stock of the corporation; (2) the ESOP loan term will not exceed 15 years; and (3) the ESOP provides for full pass-through voting to participants on all allocated shares acquired or transferred in connection with the loan.

Reasons for Change

The Committee believes that the 50-percent exclusion for interest with respect to ESOP loans provides an unnecessary tax benefit to financial institutions for loans they would make without regard to the interest exclusion. The Committee finds no evidence that employers that maintain ESOPs have less access to borrowing than other borrowers or that there is a need to provide an incentive to lenders to make money available to ESOPs.

Explanation of Provision

The bill repeals the 50-percent interest exclusion with respect to ESOP loans.

Effective Date

The provision is effective with respect to loans made after October 13, 1995, other than loans made pursuant to a written binding contract in effect on October 13, 1995, and at all times thereafter before such loan is made. The repeal of the 50-percent interest exclusion does not apply to the refinancing of an ESOP loan originally made on or before October 13, 1995, or pursuant to a binding contract in effect on such date, provided: (1) such refinancing loan otherwise meets the requirements of section 133 in effect on or before October 13, 1995; (2) the outstanding principal amount of the loan is not increased; and (3) the term of the refinancing loan does not extend beyond the term of the original ESOP loan.

3. Apply look-through rule for purposes of characterizing certain subpart F insurance income as unrelated business taxable income (sec. 1603 of the bill and sec. 512 of the Code)

Present Law

An organization that is exempt from tax by reason of Code section 501(a) (e.g., a charity, business league, or qualified pension trust) is nonetheless subject to tax on its unrelated business taxable income (UBTI) (sec. 511). Unrelated business taxable income generally excludes dividend income (sec. 512(b)(1)).

Special rules apply to a tax-exempt organization described in section 501(c)(3) or (c)(4) (i.e., a charity or social welfare organization) that is engaged in commercial-type insurance activities. Such activities are treated as an unrelated trade or business and the tax-exempt organization is subject to tax on the income from such insurance activities (including investment income that might otherwise be excluded from the definition of unrelated business taxable income) under subchapter L (sec. 501(m)(2)).[13] Accordingly, a tax-exempt organization described in section 501(c)(3) or (c)(4) generally is subject to tax on its income from commercial-type insurance activities in the same manner as a taxable insurance company.

A tax-exempt organization that conducts insurance activities through a foreign corporation is not subject to U.S. tax with respect to such activities. Under the subpart F rules, the United States shareholders (as defined in sec. 951(b)) of a controlled foreign corporation ("CFC") are required to include in income currently their shares of certain income of the CFC, whether or not such income is actually distributed to the shareholders. This current inclusion rule applies to certain insurance income of the CFC (sec. 953). However, income inclusions under subpart F have been characterized as dividends for unrelated business income tax purposes.[14] Accordingly, insurance income earned by the CFC that is includible in income currently under subpart F by the taxable United States shareholders of the CFC is excluded from unrelated business taxable income in the case of a shareholder that is a tax-exempt organization.

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[13] If the commercial-type insurance activities constitute a substantial part of the organization's activities, the organization will not be tax-exempt under section 501(c)(3) or (c)(4) (sec. 501(m)(1)).

[14] The Internal Revenue Service has concluded in private letter rulings, which are not to be used or cited as precedent, that subpart F inclusions are treated as dividends received by the United States shareholder (a tax-exempt entity) for purposes of computing the shareholder's UBTI (see LTRs 9407007 (November 12, 1993), 9027051 (April 13, 1990), 9024086 (March 22, 1990), 9024026 (March 15, 1990), 8922047 (March 6, 1989), 8836037 (June 14, 1988), 8819034 (February 10, 1988)). However, the IRS issued one private ruling in which it concluded that subpart F inclusions are treated as if the underlying income were realized directly by the United States shareholder (a tax-exempt entity) for purposes of computing the shareholder's UBTI (see LTR 9043039 (July 30, 1990)). This ruling gave no explanation for the IRS's departure from the position in its prior rulings, and the IRS reiterated in a subsequent ruling the position that subpart F inclusions are characterized as dividends for purposes of computing UBTI. Moreover, the application of the look-through rule in the ruling in question did not affect the ultimate result in the ruling because the income to which the subpart F inclusion was attributable was of a type that was excludible from UBTI. The Committee believes that LTR 9043039 (July 30, 1990) is incorrect in its application of a look-through rule in characterizing income inclusions under subpart F for unrelated business income tax purposes.

Reasons for Change

The unrelated business income tax rules are designed to prevent unfair competition by business operations that would otherwise be tax-favored due to their ownership by tax-exempt organizations. The rules applicable to certain tax-exempt organizations that conduct insurance activities directly are designed to ensure that such operations are taxed in the same manner as they would be taxed if conducted by a taxable entity. However, current law does not prevent unfair competition where operations involving the insurance of third-party risks are not conducted directly by such a tax-exempt organization itself, but are conducted by the organization through a controlled foreign corporation that is subject to little tax relative to competing U.S. businesses.

Explanation of Provision

The bill applies a look-through rule in characterizing certain subpart F insurance income for unrelated business income tax purposes. Under the bill, the look-through rule applies to amounts that constitute insurance income currently includible in gross income under the subpart F rules and that are not attributable to the insurance of risks of (1) the tax-exempt organization itself, (2) certain tax-exempt affiliates of such organization, or (3) an officer or director of, or an individual who (directly or indirectly) performs services for, the tax-exempt organization (or certain tax-exempt affiliates) provided that the insurance covers primarily risks associated with the individual's performance of services in connection with the tax-exempt organization (or tax-exempt affiliates). An individual who performs services for a tax-exempt organization through a partnership, for example, is indirectly performing services for such organization. The Committee intends that the determination of whether insurance covers primarily risks associated with the performance of services in connection with the tax-exempt organization or its tax-exempt affiliates will be based on all the facts and circumstances. The Committee further intends that a safe harbor be provided under which this "primarily" requirement will be considered to be satisfied where at least 80 percent of the services covered by the insurance are performed by the insured individual in connection with the tax-exempt organization or its tax-exempt affiliates. For purposes of determining whether the insurance covers risks associated with the individual's performance of services in connection with the tax-exempt organization, the Committee intends that the individual will not be considered to have performed services in connection with a tax-exempt organization solely by reason of the fact that the individual performs services at a facility leased to the individual by the tax-exempt organization.

For purposes of this bill, a tax-exempt organization is an affiliate of another tax-exempt organization if (1) the two organizations have significant common purposes and substantial common membership or (2) the two organizations have directly or indirectly substantial common direction or control.

The specified exceptions from the look-through rule apply on a shareholder by shareholder basis. Accordingly, if the subpart F insurance income allocable to a tax-exempt organization includes

both income attributable to the insurance of risks of the organization itself and income attributable to the insurance of risks of another shareholder that is not a tax-exempt affiliate of such organization, the look-through rule applies only to that portion of the income that represents income attributable to the insurance of risks of such other shareholder (and does not apply to the portion of the income that represents income attributable to the insurance of risks of the organization itself). In this regard, the Committee intends that if the CFC serves as a vehicle for the separate funding by each shareholder of its risks or liabilities for claims, without any pooling of a shareholder's risks or liabilities for claims with those of another shareholder either directly or through reinsurance, allocations that fairly reflect such arrangement will be respected for purposes of applying the look-through rule.

Effective Date

The provision applies to amounts includible in gross income in taxable years beginning after December 31, 1995.

4. Depreciation under the income forecast method (sec. 1604 of the bill and sec. 167 of the Code)

Present Law

In general

A taxpayer generally must capitalize the cost of property used in a trade or business and recover such cost over time through allowances for depreciation or amortization. Depreciation allowances for tangible property generally are determined under the modified Accelerated Cost Recovery System ("MACRS") of section 168, which provides that depreciation is computed by applying specific recovery periods, placed-in-service conventions, and depreciation methods to the cost of various types of depreciable property. Intangible property generally is amortized under section 197, which provides a 15-year recovery period and the straight-line method to the cost of applicable property.

Treatment of film, video tape, and similar property

MACRS does not apply to certain property, including any motion picture film, video tape, or sound recording or to other any property if the taxpayer elects to exclude such property from MACRS and the taxpayer applies a unit-of-production method or other method of depreciation not expressed in a term of years. Section 197 does not apply to certain intangible property, including property produced by the taxpayer or any interest in a film, sound recording, video tape, book or similar property not acquired in transaction (or a series of related transactions) involving the acquisition of assets constituting a trade or business or substantial portion thereof. Thus, the recovery of the cost of a film, video tape, or similar property that is produced by the taxpayer or is acquired on a "stand-alone" basis by the taxpayer may not be determined under either the MACRS depreciation provisions or under the section 197 amortization provisions. The cost of such property may be determined under section 167, which allows a depreciation deduction for the

reasonable allowance for the exhaustion, wear and tear, or obsolescence of the property.

The "income forecast" method is an allowable method for calculating depreciation under section 167 for certain property. Under the income forecast method, the depreciation deduction for a taxable year for a property is determined by multiplying the cost of the property [15] (less estimated salvage value) by a fraction, the numerator of which is the income generated by the property during the year and the denominator of which is the total forecasted or estimated income to be derived from the property during its useful life. The income forecast method has been held to be applicable for computing depreciation deductions for motion picture films, television films and taped shows, books, patents, master sound recordings and video games. [16] The total forecasted or estimated income to be derived from a property is to be based on the conditions known to exist at the end of the period for which depreciation is claimed. This estimate can be revised upward or downward at the end of a subsequent taxable period based on additional information that becomes available after the last prior estimate. These revisions, however, do not affect the amount of depreciation claimed in a prior taxable year.

In the case of a film, income to be taken into account under the income forecast method means income from the film less the expense of distributing the film, including estimated income from foreign distribution or other exploitation of the film. [17] In the case of a motion picture released for theatrical exhibition, income does not include estimated income from future television exhibition of the film (unless an arrangement for domestic television exhibition has been entered into before the film has been depreciated to its reasonable salvage value). In the case of a series or a motion picture produced for television exhibition, income does not include estimated income from domestic syndication of the series or the film (unless an arrangement for syndication has been entered into before the series or film has been depreciated to its reasonable salvage value). [18] The Internal Revenue Service also has ruled that income does not include net merchandising revenue received from the exploitation of film characters. [19]

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[15] In *Transamerica Corp.* v. *U.S.*, 999 F.2d 1362, (9th Cir. 1993), the Ninth Circuit overturned the District Court and held that, for purposes of applying the income forecast method to a film, "cost of a film" includes "participation" and "residual" payments (i.e., payments to producers, writers, directors, actors, guilds, and others based on a percentage of the profits from the film) even though these payments were contingent on the occurrence of future events. It is unclear to what extent, if any, the *Transamerica* decision applies to amounts incurred after the enactment of the economic performance rules of Code section 461(h), as contained in the Deficit Reduction Act of 1984.

[16] See, e.g., Rev. Rul. 60–358, 1960–2 C.B. 68; Rev. Rul. 64–273, 1964–2 C.B. 62; Rev. Rul. 79–285, 1979–2 C.B. 91; and Rev. Rul. 89–62, 1989–1 C.B. 78. Conversely, the courts have held that certain tangible personal property was not of a character to which the income forecast method was applicable. See, e.g., *ABC Rentals of San Antonio* v. *Comm.*, 68 TCM 1362 (1994) (consumer durable property subject to short-term, "rent-to-own" leases not eligible) and *Carland, Inc.* v. *Comm,*, 90 T.C. 505 (1988), aff'd. on this issue, 909 F.2d 1101 (8th Cir. 1990) (railroad rolling stock subject to a lease not eligible).

[17] Rev. Rul. 60–358, 1960–2 C.B. 68.

[18] Rev. Proc. 71–29, 1971–2 C.B. 568.

[19] Private letter ruling 7918012, January 24, 1979. Private letter rulings do not have precedential authority and may not be relied upon by any taxpayer other than the taxpayer receiving the ruling but are some indication of IRS administrative practice.

Reasons for Change

The Committee believes that, in theory, the income forecast method is an appropriate method for matching the capitalized cost of certain property with the income produced by such property. However, the Committee believes that the application of the income forecast method under present law does not meet the theoretical objective of the method. In addition, the Committee recognizes that the reliance of the operation of the income forecast method upon estimated income may result in a mismatch between income and depreciation deductions when future income is over- or under-estimated. The Committee bill attempts to address these issues.

Explanation of Provision

The bill makes several amendments to the income forecast method of determining depreciation deductions.

Determination of estimated income

First, the bill provides that income to be taken into account under the income forecast method includes all estimated income generated by the property. In applying this rule, a taxpayer generally need not take into account income expected to be generated after the close of the tenth taxable year after the year the property was placed in service. In the case of a film, television show, or similar property, such income includes, but is not necessarily limited to, income from foreign and domestic theatrical, television, and other releases and syndications; and video tape releases, sales, rentals, and syndications.

Pursuant to a special rule, in the case of television and motion picture films, the income from the property shall include income from the financial exploitation of characters, designs, scripts, scores, and other incidental income associated with such films, but only to the extent the income is earned in connection with the ultimate use of such items by, or the ultimate sale of merchandise to, persons who are not related to the taxpayer (within the meaning of sec. 267(b)). As an example of this special rule, assume a taxpayer produces a motion picture the subject of which is the adventures of a newly-created fictional character. If the taxpayer produces dolls or T-shirts using the character's image, income from the sales of these products by the taxpayer to consumers would be taken into account in determining depreciation for the motion picture under the income forecast method. Similarly, if the taxpayer enters into any licensing or similar agreement with an unrelated party with respect to the use of the image, such licensing income would be taken into account in determining depreciation for the motion picture. However, if the taxpayer uses the character's image to promote a ride at an amusement park that is wholly-owned by the taxpayer, no portion of the admission fees for the amusement park are to be taken into account under the income forecast method with respect to the motion picture.

In addition, pursuant to another special rule, if a taxpayer produces a television series and initially does not anticipate syndicating the episodes from the series, the forecasted income for the episodes of the first three years of the series need not take into ac-

count any future syndication fees (unless the taxpayer enters into an arrangement to syndicate such episodes during such period).

The 10th-taxable-year rule, the financial exploitation rule, and the syndication rule apply for purposes of the look-back method described below.

Determination of income forecast property costs

The cost of property subject to depreciation only includes amounts that satisfy the economic performance standard of section 461(h).[20] For this purpose, if the taxpayer incurs a noncontingent liability to acquire property subject to the income forecast method from another person, economic performance will be deemed to occur with respect to such noncontingent liability when the property is provided to the taxpayer. In addition, it is expected that the recurring item exception of section 461(h)(3) will apply in appropriate cases. Any costs that are taken into account after the property is placed in service are treated as a separate piece of property to the extent (1) such amounts are significant and are expected to give rise to a significant increase in the income from the property that was not included in the estimated income from the property, or (2) such costs are incurred more than 10 years after the property was placed in service. To the extent costs are incurred more than 10 years after the property was placed in service and give rise to a separate piece of property for which no income is generated, such costs may be written off and deducted they are incurred. For example, assume a taxpayer places property subject to the income forecast method in service during a taxable year and all income from the property is generated in the following four-year period. If the taxpayer incurs additional costs with respect to that property more than 10 years later (e.g., a payment pursuant to a deferred contingent compensation arrangement to a person that produced the property), such costs may be deducted in the year incurred provided no more income is generated with respect to such costs or the original property.

Any costs that are not recovered by the end of the tenth taxable year after the property was placed in service may be taken into account as depreciation in such year.

Look-back method

Finally, taxpayers that claim depreciation deductions under the income forecast method are required to pay (or would receive) interest based on the recalculation of depreciation under a "look-back" method.[21] The "look-back" method is applied in any "recomputation year" by (1) comparing depreciation deductions that had been claimed in prior periods to depreciation deductions that would have been claimed had the taxpayer used actual, rather than estimated, total income from the property; (2) determining the hypothetical overpayment or underpayment of tax based on this recalculated depreciation; and (3) applying the overpayment rate of section 6621 of the Code.

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[20] No inference is intended as to the proper application of section 461(h) to the income forecast method under present law.

[21] The "look-back" method of the provision resembles the look-back method applicable to long-term contracts accounted for under the percentage-of-completion method of present-law sec. 460.

Except as provided in Treasury regulations, a "recomputation year" is the third and tenth taxable year after the taxable year the property was placed in service, unless the actual income from the property for each taxable year ending with or before the close of such years was within 10 percent of the estimated income from the property for such years. The Secretary of the Treasury has the authority to allow a taxpayer to delay the initial application of the look-back method where the taxpayer may be expected to have significant income from the property after the third taxable year after the taxable year the property was placed in service (e.g., the Treasury Secretary may exercise such authority where the depreciable life of the property is expected to be longer than three years).

In applying the look-back method, any cost that is taken into account after the property was placed in service may be taken into account by discounting (using the Federal mid-term rate determined under sec. 1274(d) as of the time the costs were taken into account) such cost to its value as of the date the property was placed in service. Property with an adjusted basis of $100,000 or less when the property was placed in service is not subject to the look-back method. The provision provides a simplified look-back method for pass-through entities.

Effective Date

The provision is effective for property placed in service after September 13, 1995, unless placed in service pursuant to a binding written contract in effect before such date and all times thereafter.

5. Modify exclusion of damages received on account of personal injury or sickness (sec. 1605 of the bill and sec. 104(a)(2) of the Code)

Present Law

Under present law, gross income does not include any damages received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal injury or sickness (sec. 104(a)(2)).

The exclusion from gross income of damages received on account of personal injury or sickness specifically does not apply to punitive damages received in connection with a case not involving physical injury or sickness. Courts presently differ as to whether the exclusion applies to punitive damages received in connection with a case involving a physical injury or physical sickness.[22] Certain States provide that, in the case of claims under a wrongful death statute, only punitive damages may be awarded.

Courts have interpreted the exclusion from gross income of damages received on account of personal injury or sickness broadly in some cases to cover awards for personal injury that do not relate to a physical injury or sickness. For example, some courts have

[22] The Supreme Court recently agreed to decide whether punitive damages awarded in a physical injury lawsuit are excludable from gross income. *O'gilvie* v. *U.S.*, 66 F.3d 1550 (10th Cir. 1995), *cert. granted*, 64 U.S.L.W. 3639 (U.S. March 25, 1996)(No. 95-966). Also, the Tax Court recently held that if punitive damages are not of a compensatory nature, they are not excludable from income, regardless of whether the underlying claim involved a physical injury or physical sickness. *Bagley* v. *Commissioner*, 105 T.C. No. 27 (1995).

held that the exclusion applies to damages in cases involving certain forms of employment discrimination and injury to reputation where there is no physical injury or sickness. The damages received in these cases generally consist of back pay and other awards intended to compensate the claimant for lost wages or lost profits. The Supreme Court recently held that damages received based on a claim under the Age Discrimination in Employment Act could not be excluded from income.[23] In light of the Supreme Court decision, the Internal Revenue Service has suspended existing guidance on the tax treatment of damages received on account of other forms of employment discrimination.

Reasons for Change

Punitive damages are intended to punish the wrongdoer and do not compensate the claimant for lost wages or pain and suffering. Thus, they are a windfall to the taxpayer and appropriately should be included in taxable income. Further, including all punitive damages in taxable income provides a bright-line standard which avoids prospective litigation on the tax treatment of punitive damages received in connection with a case involving a physical injury or physical sickness.

Damages received on a claim not involving a physical injury or physical sickness are generally to compensate the claimant for lost profits or lost wages that would otherwise be included in taxable income. The confusion as to the tax treatment of damages received in cases not involving physical injury or physical sickness has led to substantial litigation, including two Supreme Court cases within the last four years. The taxation of damages received in cases not involving a physical injury or physical sickness should not depend on the type of claim made.

Explanation of Provisions

Include in income all punitive damages

The bill provides that the exclusion from gross income does not apply to any punitive damages received on account of personal injury or sickness whether or not related to a physical injury or physical sickness. Under the bill, present law continues to apply to punitive damages received in a wrongful death action if the applicable State law (as in effect on September 13, 1995 without regard to subsequent modification) provides, or has been construed to provide by a court decision issued on or before such date, that only punitive damages may be awarded in a wrongful death action. The Committee intends no inference as to the application of the exclusion to punitive damages prior to the effective date of the bill in connection with a case involving a physical injury or physical sickness.

Include in income damage recoveries for nonphysical injuries

The bill provides that the exclusion from gross income only applies to damages received on account of a personal physical injury or physical sickness. If an action has its origin in a physical injury

[23] *Schleier* v. *Commissioner*, 115 S. Ct. 2159 (1995).

or physical sickness, then all damages (other than punitive damages) that flow therefrom are treated as payments received on account of physical injury or physical sickness whether or not the recipient of the damages is the injured party. For example, damages (other than punitive damages) received by an individual on account of a claim for loss of consortium due to the physical injury or physical sickness of such individual's spouse are excludable from gross income. In addition, damages (other than punitive damages) received on account of a claim of wrongful death continue to be excludable from taxable income as under present law.

The bill also specifically provides that emotional distress is not considered a physical injury or physical sickness.[24] Thus, the exclusion from gross income does not apply to any damages received (other than for medical expenses as discussed below) based on a claim of employment discrimination or injury to reputation accompanied by a claim of emotional distress. Because all damages received on account of physical injury or physical sickness are excludable from gross income, the exclusion from gross income applies to any damages received based on a claim of emotional distress that is attributable to a physical injury or physical sickness. In addition, the exclusion from gross income specifically applies to the amount of damages received that is not in excess of the amount paid for medical care attributable to emotional distress.

The Committee intends no inference as to the application of the exclusion to damages prior to the effective date of the bill in connection with a case not involving a physical injury or physical sickness.

Effective Date

The provisions generally are effective with respect to amounts received after June 30, 1996. The provisions do not apply to amounts received under a written binding agreement, court decree, or mediation award in effect on (or issued on or before) September 13, 1995.

6. Repeal advance refunds of diesel fuel tax for purchasers of diesel-powered automobiles, vans, and light trucks (sec. 1606 of the bill and sec. 6427(g) of the Code)

Present Law

Excise taxes are imposed on gasoline (14 cents per gallon) and diesel fuel (20 cents per gallon) to fund the Federal Highway Trust Fund. Before 1985, the gasoline and diesel fuel tax rates were the same. The predominate highway use of diesel fuel is by trucks. In 1984, the diesel excise tax rate was increased above the gasoline tax as the revenue offset for a reduction in the annual heavy truck use tax. Because automobiles, vans, and light trucks, did not benefit from the use tax reductions, a provision was enacted allowing first purchasers of model year 1979 and later diesel-powered automobiles and light trucks a tax credit to offset this increased diesel

[24] The Committee intends that the term emotional distress includes physical symptoms (e.g., insomnia, headaches, stomach disorders) which may result from such emotional distress.

fuel tax. The credit is $102 for automobiles, and $198 for vans and light trucks.

Reasons for Change

Changed driving patterns, and vehicles currently being marketed, have resulted in fewer diesel-powered automobiles, vans, and light trucks today than was the case when this advance refund was enacted. Additionally, the highway cost allocation study on which the refund was based is now outdated. The Committee believes, therefore, that this present-law tax credit is obsolete and should be repealed.

Explanation of Provision

The tax credit for purchasers of diesel-powered automobiles and light trucks is repealed.

Effective Date

This provision is effective for vehicles purchased after the date of the bill's enactment.

TAX TECHNICAL CORRECTIONS PROVISIONS

The technical corrections subtitle contains clerical, conforming and clarifying amendments to the provisions enacted by the Revenue Reconciliation Act of 1990, the Revenue Reconciliation Act of 1993, and other recently enacted legislation. All amendments made by this title are meant to carry out the intent of Congress in enacting the original legislation. Therefore, no separate "Reasons for Change" is set forth for each individual amendment. Except as otherwise described, the amendments made by the technical corrections title take effect as if included in the original legislation to which each amendment relates.

A. Technical Corrections to the Revenue Reconciliation Act of 1990

1. Excise tax provisions

a. Application of the 2.5-cents-per-gallon tax on fuel used in rail transportation to States and local governments (sec. 1702(b)(2) of the bill, sec. 11211(b)(4) of the 1990 Act, and sec. 4093 of the Code)

Present Law

The 1990 Act increased the highway and motorboat fuels taxes by 5 cents per gallon, effective on December 1, 1990. The 1990 Act continued the exemption from these taxes for fuels used by States and local governments.

The 1990 Act further imposed a 2.5-cents-per-gallon tax on fuel used in rail transportation, also effective on December 1, 1990. Because of a drafting error, the 2.5-cents-per-gallon tax on fuel used in rail transportation incorrectly applies to fuel used by States and local governments.

Explanation of Provision

The bill clarifies that the 2.5-cents-per-gallon tax on fuel used in rail transportation does not apply to such uses by States and local governments.

b. Small winery production credit and bonding requirements (secs. 1702(b)(5), (6), and (7) of the bill, sec. 11201 of the 1990 Act, and sec. 5041 of the Code)

Present Law

A 90-cents-per-gallon credit is allowed to wine producers who produce no more than 250,000 gallons of wine in a year. The credit may be claimed against the producers' excise or income taxes.

Wine producers must post a bond in amounts determined by reference to expected excise tax liability as a condition of legally operating.

Explanation of Provision

The bill clarifies that wine produced by eligible small wineries may be transferred without payment of tax to bonded warehouses that become liable for payment of the wine excise tax without losing credit eligibility. In such cases, the bonded warehouse will be eligible for the credit to the same extent as the producer otherwise would have been.

The bill further clarifies that the Treasury Department has broad regulatory authority to prevent the benefit of the credit from accruing (directly or indirectly) to wineries producing in excess of 250,000 gallons in a calendar year.

It is intended that the Treasury regulatory authority will extend to all circumstances in which wine production is increased with a purpose of securing indirect credit eligibility for wine produced by such large producers.

The bill also clarifies that the Treasury Department may take the amount of credit expected to be claimed against a producer's wine excise tax liability into account in determining the amount of required bond.

2. Other revenue-increase provisions of the 1990 Act

a. Deposits of Railroad Retirement Tax Act taxes (sec. 1702(c)(3) of the bill, sec. 11334 of the 1990 Act, and sec. 6302(g) of the Code)

Present Law

Employers must deposit income taxes withheld from employees' wages and FICA taxes that are equal to or greater than $100,000 by the close of the next banking day. Under the Railroad Retirement Solvency Act of 1983, the deposit rules for withheld income taxes and FICA taxes automatically apply to Railroad Retirement Tax Act taxes (sec. 226 of P.L. 98–76).

Explanation of Provision

The bill conforms the Internal Revenue Code to the Railroad Retirement Solvency Act of 1983 by stating in the Code that these deposit rules for withheld income taxes and FICA taxes apply to Railroad Retirement Tax Act taxes.

b. Treatment of salvage and subrogation of property and casualty insurance companies (sec. 1702(c)(4) of the bill and sec. 11305 of the 1990 Act)

Present Law

For taxable years beginning after December 31, 1989, property and casualty insurance companies are required to reduce the deduction allowed for losses incurred (both paid and unpaid) by estimated recoveries of salvage and subrogation attributable to such losses. In the case of any property and casualty insurance company

that took into account estimated salvage and subrogation recoverable in determining losses incurred for its last taxable year beginning before January 1, 1990, 87 percent of the discounted amount of the estimated salvage and subrogation recoverable as of the close of the last taxable year beginning before January 1, 1990, is allowed as a deduction ratably over the first 4 taxable years beginning after December 31, 1989. This special deduction was enacted in order to provide such property and casualty insurance companies with substantially the same Federal income tax treatment as that provided to those property and casualty insurance companies that prior to the Revenue Reconciliation Act of 1990 did not take into account estimated salvage and subrogation recoverable in determining losses incurred.

Explanation of Provision

The bill provides that the earnings and profits of any property and casualty insurance company that took into account estimated salvage and subrogation recoverable in determining losses incurred for its last taxable year beginning before January 1, 1990, is to be determined without regard to the special deduction that is allowed over the first 4 taxable years beginning after December 31, 1989. The special deduction is to be taken into account, however, in determining earnings and profits for purposes of applying sections 56, 902, and subpart F of part III of subchapter N of chapter 1 of the Internal Revenue Code of 1986. This provision is considered necessary in order to provide those property and casualty insurance companies that took into account estimated salvage and subrogation recoverable in determining losses incurred with substantially the same Federal income tax treatment as that provided to those property and casualty insurance companies that prior to the 1990 Act did not take into account estimated salvage and subrogation recoverable in determining losses incurred.

c. Information with respect to certain foreign-owned or foreign corporations: Suspension of the statute of limitations during certain judicial proceedings (sec. 1702(c)(5) of the bill, secs. 11314 and 11315 of the 1990 Act, and secs. 6038A and 6038C of the Code)

Present Law

Any domestic corporation that is 25-percent owned by one foreign person is subject to certain information reporting and recordkeeping requirements with respect to transactions carried out directly or indirectly with certain foreign persons treated as related to the domestic corporation ("reportable transactions") (sec. 6038A(a)). In addition, the Code provides procedures whereby an IRS examination request or summons with respect to reportable transactions can be served on foreign related persons through the domestic corporation (sec. 6038A(e)). Similar provisions apply to any foreign corporation engaged in a trade or business within the United States, with respect to information, records, examination requests, and summonses pertaining to the computation of its liability for tax in the United States (sec. 6038C). Certain noncompli-

ance rules may be applied by the Internal Revenue Service in the case of the failure by a domestic corporation to comply with a summons pertaining to a reportable transaction (a "6038A summons") (sec. 6038A(e)), or the failure by a foreign corporation engaged in a U.S. trade or business to comply with a summons issued for purposes of determining the foreign corporation's liability for tax in the United States (a "6038C summons") (sec. 6038C(d)).

Any corporation that is subject to the provisions of section 6038A or 6038C has the right to petition a Federal district court to quash a 6038A or 6038C summons, or to review a determination by the IRS that the corporation did not substantially comply in a timely manner with the 6038A or 6038C summons (sec. 6038A(e)(4)(A) and (B); sec. 6038C(d)(4)). During the period that either such judicial proceeding is pending (including appeals), and for up to 90 days thereafter, the statute of limitations is suspended with respect to any transaction (or item, in the case of a foreign corporation) to which the summons relates (secs. 6038A(e)(4)(D), 6038C(d)(4)).

The legislative history of the 1989 Act amendments to section 6038A states that the suspension of the statute of limitations applies to "the taxable year(s) at issue."[25] The legislative history of the 1990 Act, which added section 6038C to the Code, uses the same language.[26]

Explanation of Provision

The bill modifies the provisions in sections 6038A and 6038C that suspend the statute of limitations to clarify that the suspension applies to any taxable year the determination of the amount of tax imposed for which is affected by the transaction or item to which the summons relates.

It is intended that, under the provision, a transaction or item would affect the determination of the amount of tax imposed for the taxable year directly at issue, as well as for any taxable year indirectly affected through, for example, net operating loss carrybacks or carryforwards. It is not intended that, under the provision, a transaction or item would affect the determination of the amount of tax imposed for any taxable year other than the taxable year directly at issue solely by reason of any similarity of issues involved. Similarly, it is not intended that, under the provision, a transaction or item would affect the determination of the amount of tax imposed on any taxpayer unrelated to the taxpayer to whom the summons is directed.

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[25] H. Rept. No. 247, 101st Cong., 1st Sess. 1301 (1989); "Explanation of Provisions Approved by the Committee on October 3, 1989," Senate Finance Committee Print, 101st Cong., 1st Sess. 118 (October 12, 1989).

[26] "Legislative History of Ways and Means Democratic Alternative," House Ways and Means Committee Print (WMCP: 101–37), 101st Cong., 2nd Sess. 58 (October 15, 1990); Report language submitted by the Senate Finance Committee to the Senate Budget Committee on S. 3299, 136 Cong. Rec. S. 15629, S. 15700 (1990).

d. Rate of interest for large corporate underpayments (secs. 1702(c)(6) and (7) of the bill, sec. 11341 of the 1990 Act, and sec. 6621(c) of the Code)

Present Law

The rate of interest otherwise applicable to underpayments of tax is increased by two percent in the case of large corporate underpayments (generally defined to exceed $100,000), applicable to periods after the 30th day following the earlier of a notice of proposed deficiency, the furnishing of a statutory notice of deficiency, or an assessment notice issued in connection with a nondeficiency procedure.

Explanation of Provision

The bill provides that an IRS notice that is later withdrawn because it was issued in error does not trigger the higher rate of interest. The bill also corrects an incorrect reference to "this subtitle".

3. Research credit provision: Effective date for repeal of special proration rule (sec. 1702(d)(1) of the bill and sec. 11402 of the 1990 Act)

Present Law

The Omnibus Budget Reconciliation Act of 1989 ("1989 Act") effectively extended the research credit for nine months by prorating certain qualified research expenses incurred before January 1, 1991. The special rule to prorate qualified research expenses applied in the case of any taxable year which began before October 1, 1990, and ended after September 30, 1990. Under this special proration rule, the amount of qualified research expenses incurred by a taxpayer prior to January 1, 1991, was multiplied by the ratio that the number of days in that taxable year before October 1, 1990, bears to the total number of days in such taxable year before January 1, 1991. The amendments made by the 1989 Act to the research credit (including the new method for calculating a taxpayer's base amount) generally were effective for taxable years beginning after December 31, 1989. However, this effective date did not apply to the special proration rule (which applied to any taxable year which began prior to October 1, 1990—including some years which began before December 31, 1989—if such taxable year ended after September 30, 1990).

Section 11402 of the Revenue Reconciliation Act of 1990 ("1990 Act") extended the research credit through December 31, 1991, and repealed the special proration rule provided for by the 1989 Act. Section 11402 of the 1990 Act was effective for taxable years beginning after December 31, 1989. Thus, in the case of taxable years beginning before December 31, 1989, and ending after September 30, 1990 (e.g., a taxable year of November 1, 1989 through October 31, 1990), the special proration rule provided by the 1989 Act would continue to apply.

Explanation of Provision

The bill repeals for all taxable years ending after December 31, 1989, the special proration rule provided for by the 1989 Act.

4. Energy tax provision: Alternative minimum tax adjustment based on energy preferences (secs. 1702(e)(1) and (4) of the bill, sec. 11531(a) of the 1990 Act, and former sec. 56(h) of the Code)

Present Law

In computing alternative minimum taxable income (and the adjusted current earnings (ACE) adjustment of the alternative minimum tax), certain adjustments are made to the taxpayer's regular tax treatment for intangible drilling costs (IDCs) and depletion. For certain taxable years, a special energy deduction is also allowed. The special energy deduction is initially determined by determining the taxpayer's (1) intangible drilling cost preference and (2) the marginal production depletion preference. The intangible drilling cost preference is the amount by which the taxpayer's alternative minimum taxable income would be reduced if it were computed without regard to the adjustments for IDCs. The marginal production depletion preference is the amount by which the taxpayer's alternative minimum taxable income would be reduced if it were computed without regard to depletion adjustments attributable to marginal production. The intangible drilling cost preference is then apportioned between (1) the portion of the preference related to qualified exploratory costs and (2) the remaining portion of the preference. The portion of the preference related to qualified exploratory costs is multiplied by 75 percent and the remaining portion is multiplied by 15 percent. The marginal production depletion preference is multiplied by 50 percent. The three products described above are added together to arrive at the taxpayer's special energy deduction (subject to certain limitations).

The special energy deduction is not allowed to the extent that it exceeds 40 percent of alternative minimum taxable income determined without regard to either this special energy deduction or the alternative tax net operating loss deduction. Any special energy deduction amount limited by the 40-percent threshold may not be carried to another taxable year. In addition, the combination of the special energy deduction, the alternative minimum tax net operating loss and the alternative minimum tax foreign tax credit cannot generally offset, in the aggregate, more than 90 percent of a taxpayer's alternative minimum tax determined without such attributes.

The special energy deduction was repealed for taxable years beginning after December 31, 1992.

Explanation of Provision

Interaction of special energy deduction with net operating loss and investment tax credit

The bill clarifies that the amount of alternative tax net operating loss that is utilized in any taxable year is to be appropriately adjusted to take into account the amount of special energy deduction

claimed for that year. This operates to preserve a portion of the alternative tax net operating loss carryover by reducing the amount of net operating loss utilized to the extent of the special energy deduction claimed, which if unused, could not be carried forward.

In addition, the bill contains a similar provision which clarifies that the limitation on the utilization of the investment tax credit for purposes of the alternative minimum tax is to be determined without regard to the special energy deduction.

Interaction of special energy deduction with adjustment based on adjusted current earnings

The bill provides that the ACE adjustment for taxable years beginning in 1991 and 1992 is to be computed without regard to the special energy deduction. Thus, the bill specifies that the ACE adjustment is equal to 75 percent of the excess of a corporation's adjusted current earnings over its alternative minimum taxable income computed without regard to either the ACE adjustment, the alternative tax net operating loss deduction, or the special energy deduction.

5. Estate tax freezes (sec. 1702(f) of the bill, sec. 11602 of the 1990 Act, and secs. 2701–2704 of the Code)

Present Law

Generally

The value of property transferred by gift or includible in the decedent's gross estate is its fair market value. Fair market value generally is the price at which the property would change hands between a willing buyer and willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts (Treas. Reg. sec. 20.2031). Chapter 14 contains rules that supersede the willing buyer, willing seller standard (Code secs. 2701–2704).

Preferred interests in corporations and partnerships

Valuation of retained interests

Scope.—Section 2701 provides special rules for valuing certain rights retained in conjunction with the transfer to a family member of an interest in a corporation or partnership. These rules apply to any applicable retained interest held by the transferor or an applicable family member immediately after the transfer of an interest in such entity. An "applicable family member" is, with respect to any transferor, the transferor's spouse, ancestors of the transferor and the spouse, and spouses of such ancestors.

An applicable retained interest is an interest with respect to which there is one of two types of rights ("affected rights"). The first type of affected right is a liquidation, put, call, or conversion right, generally defined as any liquidation, put, call, or conversion right, or similar right, the exercise or nonexercise of which affects the value of the transferred interest. The second type of affected

right is a distribution right[27] in an entity in which the transferor and applicable family members hold control immediately before the transfer. In determining control, an individual is treated as holding any interest held by the individual's brothers, sisters and lineal descendants. A distribution right does not include any right with respect to a junior equity interest.

Valuation.—Section 2701 contains two rules for valuing applicable retained interests. Under the first rule, an affected right other than a right to qualified payments is valued at zero. Under the second rule, any retained interest that confers (1) a liquidation, put, call or conversion right and (2) a distribution right that consists of the right to receive a qualified payment is valued on the assumption that each right is exercised in a manner resulting in the lowest value for all such rights (the "lowest value rule"). There is no statutory rule governing the treatment of an applicable retained interest that confers a right to receive a qualified payment, but with respect to which there is no liquidation, put, call or conversion right.

A qualified payment is a dividend payable on a periodic basis and at a fixed rate under cumulative preferred stock (or a comparable payment under a partnership agreement). A transferor or applicable family member may elect not to treat such a dividend (or comparable payment) as a qualified payment. A transferor or applicable family member also may elect to treat any other distribution right as a qualified payment to be paid in the amounts and at the times specified in the election.

Inclusion in transfer tax base.—Failure to make a qualified payment valued under the lowest value rule within four years of its due date generally results in an inclusion in the transfer tax base equal to the difference between the compounded value of the scheduled payments over the compounded value of the payments actually made. The Treasury Department has regulatory authority to make subsequent transfer tax adjustments in the transfer of an applicable retained interest to reflect the increase in a prior taxable gift by reason of section 2701.

Generally, this inclusion occurs if the holder transfers by sale or gift the applicable retained interest during life or at death. In addition, the taxpayer may, by election, treat the payment of the qualified payment as giving rise to an inclusion with respect to prior periods.

The inclusion continues to apply if the applicable retained interest is transferred to an applicable family member. There is no inclusion on a transfer of an applicable retained interest to a spouse for consideration or in a transaction qualifying for the marital deduction, but subsequent transfers by the spouse are subject to the inclusion. Other transfers to applicable family members result in an immediate inclusion as well as subjecting the transferee to subsequent inclusions.

[27] Distribution right generally is a right to a distribution from a corporation with respect to its stock, or from a partnership with respect to a partner's interest in the partnership.

Minimum value of residual interest

Section 2701 also establishes a minimum value for a junior equity interest in a corporation or partnership. For partnerships, a junior equity interest is an interest under which the rights to income and capital are junior to the rights of all other classes of equity interests.

Trusts and term interests in property

The value of a transfer in trust is the value of the entire property less the value of rights in the property retained by the grantor. Section 2702 provides that in determining the extent to which a transfer of an interest in trust to a member of the transferor's family is a gift, the value of an interest retained by the transferor or an applicable family member is zero unless such interest takes certain prescribed forms.

For a transfer with respect to a specified portion of property, section 2702 applies only to such portion. The section does not apply to the extent that the transfer is incomplete.

Options and buy-sell agreements

A restriction upon the sale or transfer of property may reduce its fair market value. Treasury regulations provide that a restriction is to be disregarded unless the agreement represents a bona fide business arrangement and not a device to pass the decedent's shares to the natural objects of his bounty for less than full and adequate consideration (Treas. Reg. sec. 20.2031–2(h)).

Section 2703 provides, that for transfer tax purposes, the value of property is determined without regard to any option, agreement or other right to acquire or use the property at less than fair market value or any restriction on the right to sell or use such property. Certain options are excepted from this rule. To fall within the exception, the option, agreement, right or restriction must (1) be a bona fide business arrangement, (2) not be a device to transfer such property to members of the decedent's family for less than full and adequate consideration in money or money's worth, and (3) have terms comparable to similar arrangements entered into by persons in an arm's length transaction.

Explanation of Provision

Preferred interests in corporations and partnerships

Valuation

The bill provides that an applicable retained interest conferring a distribution right to qualified payments with respect to which there is no liquidation, put, call, or conversion right is valued without regard to section 2701. The bill also provides that the retention of such right gives rise to potential inclusion in the transfer tax base. In making these changes, it is understood that Treasury regulations could provide, in appropriate circumstances, that a right to receive amounts on liquidation of the corporation or partnership constitutes a liquidation right within the meaning of section 2701 if the transferor, alone or with others, holds the right to cause liquidation.

The bill modifies the definition of junior equity interest by granting regulatory authority to treat a partnership interest with rights that are junior with respect to either income or capital as a junior equity interest. The bill also modifies the definition of distribution right by replacing the junior equity interest exception with an exception for a right under an interest that is junior to the rights of the transferred interest. As a result, section 2701 does not affect the valuation of a transferred interest that is senior to the retained interest, even if the retained interest is not a junior equity interest.

The bill modifies the rules for electing into or out of qualified payment treatment. A dividend payable on a periodic basis and at a fixed rate under a cumulative preferred stock held by the transferor is treated as a qualified payment unless the transferor elects otherwise. If held by an applicable family member, such stock is not treated as a qualified payment unless the holder so elects.[28] In addition, a transferor or applicable family member holding any other distribution right may treat such right as a qualified payment to be paid in the amounts and at the times specified in the election.

Inclusion in transfer tax base

The bill grants the Treasury Department regulatory authority to make subsequent transfer tax adjustments to reflect the inclusion of unpaid amounts with respect to a qualified payment. This authority, for example, would permit the Treasury Department to eliminate the double taxation that might occur if, with respect to a transfer, both the inclusion and the value of qualified payment arrearages were included in the transfer tax base. It also would permit elimination of the double taxation that might result from a transfer to a spouse, who, under the statute, is both an applicable family member and a member of the transferor's family.

The bill treats a transfer to a spouse falling under the annual exclusion the same as a transfer qualifying for the marital deduction. Thus, no inclusion would occur upon the transfer of an applicable retained interest to a spouse, but subsequent transfers by the spouse would be subject to inclusion. The bill also clarifies that the inclusion continues to apply if an applicable family member transfers a right to qualified payments to the transferor.

The provision clarifies the consequences of electing to treat a distribution as giving rise to an inclusion. Under the bill, the election gives rise to an inclusion only with respect to the payment for which the election is made. The inclusion with respect to other payments is unaffected.

Trust and term interests in property

The bill conforms section 2702 to existing regulatory terminology by substituting the term "incomplete gift" for "incomplete transfer." In addition, the bill limits the exception for incomplete gifts to instances in which the entire gift is incomplete. The Treasury Department is granted regulatory authority, however, to create additional exceptions not inconsistent with the purposes of the section.

[28] With respect to gifts made prior to the date of enactment, the provision provides that this election may be made by the due date (including extensions) of the transferor's gift tax return due for the first calendar year after the date of enactment.

This authority, for example, could be used to except a charitable remainder trust that meets the requirements of section 664 and that does not otherwise create an opportunity for transferring property to a family member free of transfer tax.

6. Miscellaneous provisions

a. Conforming amendments to the repeal of the *General Utilities* doctrine (secs. 1702(g)(1) and (2) of the bill, sec. 11702(e)(2) of the 1990 Act, and secs. 897(f) and 1248 of the Code)

Present Law

As a result of changes made by recent tax legislation, gain is generally recognized on the distribution of appreciated property by a corporation to its shareholders. The Technical Corrections subtitle of the 1990 Act and technical correction provisions in prior acts made various conforming amendments arising out of these changes. For example, the 1990 Act made a conforming change to section 355(c) to state the treatment of distributions in section 355 transactions in the affirmative rather than by reference to the provisions of section 311. In addition, the Technical and Miscellaneous Revenue Act of 1988 ("1988 Act") made a conforming change to section 1248(f) to update the references to the nonrecognition provisions contained in that subsection. One of the changes was to change the reference to "section 311(a)" from "section 311".

Explanation of Provision

The bill makes three conforming changes to the Code with respect to the repeal of the *General Utilities* doctrine.

First, section 1248(f) is amended to add a reference to section 355(c)(1), which provides generally for the nonrecognition of gain or loss on the distribution of stock or securities in certain subsidiary corporations. This retains the substance of the law as it existed before the conforming change to section 355(c) made by the 1990 Act. This provision is not intended to affect the authority of the Secretary of the Treasury to issue regulations under section 1248(f) providing exceptions to the rule recognizing gain in certain distributions (cf. Notice 87–64, 1987–2 C.B. 375).

Second, section 1248 is amended to clarify that, notwithstanding the conforming changes made by the 1988 Act, with respect to any transaction in which a U.S. person is treated as realizing gain from the sale or exchange of stock of a controlled foreign corporation, the U.S. person shall be treated as having sold or exchanged the stock for purposes of applying section 1248. Thus, if a U.S. person distributes appreciated stock of a controlled foreign corporation to its shareholders in a transaction in which gain is recognized under section 311(b), section 1248 shall be applied as if the stock had been sold or exchanged at its fair market value. Under section 1248(a), part or all of the gain may be treated as a dividend. Under the bill, the rule treating the distribution for purposes of section 1248 as a sale or exchange also applies where the U.S. person is deemed to distribute the stock under the provisions of section

1248(i). Under section 1248(i), gain will be recognized only to the extent of the amount treated as a dividend under section 1248.

Third, section 897(f), relating to the basis in a United States real property interest distributed to a foreign person, is repealed as deadwood. The basis of the distributed property is its fair market value in accordance with section 301(d).

b. Prohibited transaction rules (sec. 1702(g)(3) of the bill, sec. 11701(m) of the 1990 Act, and sec. 4975 of the Code)

Present Law

The Code and title I of the Employee Retirement Income Security Act of 1974 (ERISA) prohibit certain transactions between an employee benefit plan and certain persons related to such plan. An exemption to the prohibited transaction rules of title I of ERISA is provided in the case of sales of employer securities the plan is required to dispose of under the Pension Protection Act of 1987 (ERISA sec. 408(b)(12)). The 1990 Act amended the Code to provide that certain transactions that are exempt from the prohibited transaction rules of ERISA are automatically exempt from the prohibited transaction rules of the Code. The 1990 Act change was intended to be limited to transactions exempt under section 408(b)(12) of ERISA.

Explanation of Provision

The bill conforms the statutory language to legislative intent by providing that transactions that are exempt from the prohibited transaction rules of ERISA by reason of ERISA section 408(b)(12) are also exempt from the prohibited transaction rules of the Code.

c. Effective date of LIFO adjustment for purposes of computing adjusted current earnings (sec. 1702(g)(4) of the bill, sec. 11701 of the 1990 Act, sec. 7611(b) of the 1989 Act, and sec. 56(g) of the Code)

Present Law

For purposes of computing the adjusted current earnings (ACE) component of the corporate alternative minimum tax, taxpayers are required to make the LIFO inventory adjustments provided in section 312(n)(4) of the Code. Section 312(n)(4) generally is applicable for purposes of computing earnings and profits in taxable years beginning after September 30, 1984. The ACE adjustment generally is applicable to taxable years beginning after December 31, 1989.

Explanation of Provision

The bill clarifies that the LIFO inventory adjustment required for ACE purposes shall be computed by applying the rules of section 312(n)(4) only with respect to taxable years beginning after December 31, 1989. The effective date applicable to the determination of earnings and profits (September 30, 1984) is inapplicable for purposes of the ACE LIFO inventory adjustment. Thus, the ACE LIFO adjustment shall be computed with reference to increases

(and decreases, to the extent provided in Treasury regulations) in the ACE LIFO reserve in taxable years beginning after December 31, 1989.

d. Low-income housing tax credit (sec. 1702(g)(5) of the bill, sec. 11701(a)(11) of the 1990 Act, and sec. 42 of the Code)

Present Law

The amendments to the low-income housing tax credit contained in the Omnibus Budget Reconciliation Act of 1989 ("1989 Act") generally were effective for buildings placed in service after December 31, 1989, to the extent the buildings were financed by tax-exempt bonds ("bond-financed buildings"). This rule applied regardless of when the bonds were issued.

A technical correction enacted in the Revenue Reconciliation Act of 1990 ("1990 Act") limited this effective date to buildings financed with bonds issued after December 31, 1989. Thus, the technical correction applied pre-1989 Act law to bond-financed buildings placed in service after December 31, 1989, if the bonds were issued before January 1, 1990.

Explanation of Provision

The bill repeals the 1990 technical correction. The bill provides, however, that pre-1989 Act law will apply to a bond-financed building if the owner of the building establishes to the satisfaction of the Secretary of the Treasury reasonable reliance upon the 1990 technical correction. In the case of buildings placed in service before the date of the bill's enactment, reasonable reliance may be established by a showing of compliance with the law as in effect for those buildings before enactment of the amendments made by the bill.

7. Expired or obsolete provisions ("deadwood provisions") (secs. 1702(h)(1)–(18) of the bill and secs. 11801–11816 of the 1990 Act)

Present Law

The 1990 Act repealed and amended numerous sections of the Code by deleting obsolete provisions ("deadwood"). These amendments were not intended to make substantive changes to the tax law.

Explanation of Provision

The bill makes several amendments to restore the substance of prior law which was inadvertently changed by the deadwood provisions of the 1990 Act. These amendments include (1) a provision that clarifies that solar or wind property owned by a public utility may qualify as 5-year MACRS property (sec. 168(e)(3)(B)(vi)) and (2) a provision restoring the prior-law rule providing that if any member of an affiliated group of corporations elects the credit under section 901 for foreign taxes paid or accrued, then all members of the group paying or accruing such taxes must elect the credit in order for any dividend paid by a member of the group to

qualify for the 100-percent dividends received deduction (sec. 243(b)).

The bill also makes several nonsubstantive clerical amendments to conform the Code to the amendments made by the deadwood provisions. None of these amendments is intended to change the substance of pre-1990 law.

B. Technical Corrections to the Revenue Reconciliation Act of 1993

1. Treatment of full-time students under the low-income housing credit (sec. 1703(b)(1) of the bill, sec. 13142 of the 1993 Act and sec. 42 of the Code)

Present Law

The Revenue Reconciliation Act of 1993 ("1993 Act") codified prior law rules relating to the treatment of married students filing joint returns. Further, it provided that a housing unit occupied entirely by full-time students may qualify for the credit if the full-time students are a single parent and his or her minor children and none of the tenants is a dependent of a third party.

Explanation of Provision

The bill provides that the full-time student provision is effective on the date of enactment of the 1993 Act.

2. Indexation of threshold applicable to excise tax on luxury automobiles (sec. 1703(c) of the bill, sec. 13161 of the 1993 Act, and sec. 4001(e)(1) of the Code)

Present Law

The 1993 Act indexed the threshold above which the excise tax on luxury automobiles is to apply.

Explanation of Provision

The bill corrects the application of the indexing adjustment so that the adjustment calculated for a given calendar year applies for that calendar year rather than in the subsequent calendar year. This conforms the indexation to that described in the conference report to the 1993 Act.[29] The intent of Congress, as reflected in the conference report, was that current year indexation be effective on the date of enactment of the 1993 Act. Under the bill, the provision would, however, be effective on the date of enactment, to alleviate the difficulties that both taxpayers and the Treasury would experience in administering a retroactive refund effective to August 10, 1993.

[29] See, H. Rept. 103–213, August 4, 1993, p. 558.

(and decreases, to the extent provided in Treasury regulations) in the ACE LIFO reserve in taxable years beginning after December 31, 1989.

d. Low-income housing tax credit (sec. 1702(g)(5) of the bill, sec. 11701(a)(11) of the 1990 Act, and sec. 42 of the Code)

Present Law

The amendments to the low-income housing tax credit contained in the Omnibus Budget Reconciliation Act of 1989 ("1989 Act") generally were effective for buildings placed in service after December 31, 1989, to the extent the buildings were financed by tax-exempt bonds ("bond-financed buildings"). This rule applied regardless of when the bonds were issued.

A technical correction enacted in the Revenue Reconciliation Act of 1990 ("1990 Act") limited this effective date to buildings financed with bonds issued after December 31, 1989. Thus, the technical correction applied pre-1989 Act law to bond-financed buildings placed in service after December 31, 1989, if the bonds were issued before January 1, 1990.

Explanation of Provision

The bill repeals the 1990 technical correction. The bill provides, however, that pre-1989 Act law will apply to a bond-financed building if the owner of the building establishes to the satisfaction of the Secretary of the Treasury reasonable reliance upon the 1990 technical correction. In the case of buildings placed in service before the date of the bill's enactment, reasonable reliance may be established by a showing of compliance with the law as in effect for those buildings before enactment of the amendments made by the bill.

7. Expired or obsolete provisions ("deadwood provisions") (secs. 1702(h)(1)–(18) of the bill and secs. 11801–11816 of the 1990 Act)

Present Law

The 1990 Act repealed and amended numerous sections of the Code by deleting obsolete provisions ("deadwood"). These amendments were not intended to make substantive changes to the tax law.

Explanation of Provision

The bill makes several amendments to restore the substance of prior law which was inadvertently changed by the deadwood provisions of the 1990 Act. These amendments include (1) a provision that clarifies that solar or wind property owned by a public utility may qualify as 5-year MACRS property (sec. 168(e)(3)(B)(vi)) and (2) a provision restoring the prior-law rule providing that if any member of an affiliated group of corporations elects the credit under section 901 for foreign taxes paid or accrued, then all members of the group paying or accruing such taxes must elect the credit in order for any dividend paid by a member of the group to

qualify for the 100-percent dividends received deduction (sec. 243(b)).

The bill also makes several nonsubstantive clerical amendments to conform the Code to the amendments made by the deadwood provisions. None of these amendments is intended to change the substance of pre-1990 law.

B. Technical Corrections to the Revenue Reconciliation Act of 1993

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Present Law

The Revenue Reconciliation Act of 1993 ("1993 Act") codified prior law rules relating to the treatment of married students filing joint returns. Further, it provided that a housing unit occupied entirely by full-time students may qualify for the credit if the full-time students are a single parent and his or her minor children and none of the tenants is a dependent of a third party.

Explanation of Provision

The bill provides that the full-time student provision is effective on the date of enactment of the 1993 Act.

2. Indexation of threshold applicable to excise tax on luxury automobiles (sec. 1703(c) of the bill, sec. 13161 of the 1993 Act, and sec. 4001(e)(1) of the Code)

Present Law

The 1993 Act indexed the threshold above which the excise tax on luxury automobiles is to apply.

Explanation of Provision

The bill corrects the application of the indexing adjustment so that the adjustment calculated for a given calendar year applies for that calendar year rather than in the subsequent calendar year. This conforms the indexation to that described in the conference report to the 1993 Act.[29] The intent of Congress, as reflected in the conference report, was that current year indexation be effective on the date of enactment of the 1993 Act. Under the bill, the provision would, however, be effective on the date of enactment, to alleviate the difficulties that both taxpayers and the Treasury would experience in administering a retroactive refund effective to August 10, 1993.

[29] See, H. Rept. 103–213, August 4, 1993, p. 558.

3. Indexation of the limitation based on modified adjusted gross income for income from United States Savings bonds used to pay higher education tuition and fees (sec. 1703(d) of the bill, sec. 13201 of the 1993 Act, and sec. 135(b)(2)(B) of the Code)

Present Law

A taxpayer may exclude from gross income the proceeds from the redemption of qualified United States savings bonds if the proceeds are used to pay qualified higher education expenses and the taxpayer's modified adjusted gross income is equal to or less than $60,000 ($40,000 in the case of a single return). The exclusion is phased out for incomes above these thresholds. The $60,000 ($40,000) threshold is indexed for inflation occurring after 1992.

Explanation of Provision

The bill corrects the indexing of the $60,000 ($40,000) threshold to provide that the thresholds be indexed for inflation after 1989, as was provided prior to the 1993 Act.

4. Reporting and notification requirements for lobbying and political expenditures of tax-exempt organizations (sec. 1703(g) of the bill, sec. 13222 of the 1993 Act and sec. 6033(e) of the Code)

Present Law

Tax-exempt organizations which incur political expenditures are subject to tax under Code section 527(f). The tax is calculated by applying the highest corporate rate to the lesser of (a) the net investment income of the organization, or (b) the amount of political expenditures incurred by the organization during the taxable year. Expenditures covered by Code section 527(f) are those expended for "influencing or attempting to influence the selection, nomination, election, or appointment of any individual to any Federal, State, or local public office or office in a political organization, or the election of Presidential or Vice-Presidential electors, whether of not such individual or electors are selected, nominated, elected, or appointed."

Code section 162(e), as amended by the 1993 Act, provides a separate set of rules regarding the tax treatment of lobbying and political expenditures. Political expenditures include amounts paid or incurred in connection with "participation in, or intervention in, any political campaign on behalf of (or in opposition to) any candidate for public office." Taxpayers may not deduct the portion of dues or similar amounts paid to a tax-exempt organization which the organization notifies the taxpayer are allocable to lobbying or political expenditures.

Code section 6033(e) sets forth reporting and notification requirements applicable to tax-exempt organizations (other than charities) that incur lobbying or political expenditures within the meaning of Code section 162(e). First, the organization must report on its annual tax return both the total amount of its lobbying and political expenditures, and the total amount of dues (or similar payments) allocable to such expenditures. Second, the organization must ei-

ther provide notice to its members of the portion of dues allocable to lobbying and political expenditures (so that such amounts are not deductible by members), or may elect to pay a proxy tax (at the highest corporate rate) on its lobbying and political expenditures, up to the amount of dues receipts.

Explanation of Provision

The bill amends Code section 6033(e) to clarify that any political expenditures on which tax is paid pursuant to Code section 527(f) are not subject to the reporting and notification requirements of Code section 6033(e). In addition, the bill clarifies that the reporting and notification requirements of Code section 6033(e) apply to organizations exempt from tax under Code section 501(a), other than charities described in section 501(c)(3).

5. Estimated tax rules for certain tax-exempt organizations (sec. 1703(h) of the bill, sec. 13225 of the 1993 Act and sec. 6655(g)(3) of the Code)

Present Law

A tax-exempt organization is generally subject to an addition to tax for any underpayment of estimated tax on its unrelated business taxable income or its net investment income (as the case may be). Under the 1993 Act, for years beginning after December 31, 1993, a corporation or tax-exempt organization does not have an underpayment of estimated tax if it makes four timely estimated tax payments that total at least 100 percent of the tax liability shown on its return for the current taxable year. A corporation or tax-exempt organization may estimate its current year tax liability prior to year-end by annualizing its income. The 1993 Act also changed the method by which a corporation annualizes its current year tax liability.

Explanation of Provision

The bill clarifies that the 1993 Act did not change the method by which a tax-exempt organization annualizes its current year tax liability.

6. Current taxation of certain earnings of controlled foreign corporations—application of foreign tax credit limitation (sec. 1703(i)(1) of the bill, sec. 13231(b) of the 1993 Act, and sec. 904(d) of the Code)

Present Law

Present law requires U.S. shareholders of a controlled foreign corporation to include in income the corporation's subpart F income, certain earnings invested in U.S. property, and, as modified by the 1993 Act, certain earnings invested in excess passive assets. A U.S. shareholder's tax liability attributable to the inclusion may be offset by foreign tax credits for certain foreign taxes paid or deemed paid by the shareholder.

The foreign tax credit limitation applies separately to several categories of income. The separate limitations apply to a dividend

from a controlled foreign corporation to a U.S. shareholder of that controlled foreign corporation by reference to the character of the earnings and profits of the distributing corporation.

An inclusion of a controlled foreign corporation's earnings invested in U.S. property is treated like a dividend for purposes of the foreign tax credit limitation. Although the 1993 Act provided that inclusions of earnings invested in excess passive assets generally are determined in the same manner as inclusions of earnings invested in U.S. property, the 1993 Act did not specify how the separate limitations of the foreign tax credit should apply to inclusions of earnings invested in excess passive assets.

Some have argued that the separate limitations of the foreign tax credit do not apply to an inclusion of a controlled foreign corporation's earnings invested in excess passive assets; rather, that such an inclusion is allocated entirely to the general foreign tax credit limitation, without regard to the character of the underlying earnings and profits of the controlled foreign corporation.

Explanation of Provision

The bill clarifies that a U.S. shareholder's inclusion of a controlled foreign corporation's earnings invested in excess passive assets is treated like a dividend for purposes of the foreign tax credit limitation. Thus, the inclusion is characterized by reference to the underlying earnings and profits of the controlled foreign corporation. This treatment is consistent with present law's application of the separate limitations of the foreign tax credit to other amounts included in income with respect to a controlled foreign corporation.

7. Current taxation of certain earnings of controlled foreign corporations—measurement of accumulated earnings (sec. 1703(i)(2) of the bill, sec. 13231(b) of the 1993 Act, and sec. 956A(b) of the Code)

Present Law

Present law, as modified by the 1993 Act, limits the availability of deferral of U.S. tax on certain earnings of controlled foreign corporations by requiring U.S. shareholders of a controlled foreign corporation to include in income the corporation's accumulated[30] or current earnings invested in excess passive assets. Some have argued that the Code's definition of earnings subject to this treatment permits an accumulated deficit in earnings to eliminate positive current earnings, resulting in no income inclusion in a case where an actual distribution would be treated as a dividend out of current earnings. In addition, some have argued that the Code's definition of earnings subject to this treatment takes current-year earnings into account more than once.

Explanation of Provision

The bill clarifies that the accumulated earnings and profits of a controlled foreign corporation taken into account for purposes of determining the foreign corporation's earnings invested in excess pas-

[30] Accumulated earnings and profits are taken into account only to the extent that they were accumulated in taxable years beginning after September 30, 1993.

sive assets do not include any deficit in accumulated earnings and profits,[31] and do not include current earnings (which are taken into account separately).

8. Current taxation of certain earnings of controlled foreign corporations—aggregation and look-through rules (sec. 1703(i)(3) of the bill, sec. 13231(b) of the 1993 Act, and sec. 956A(f) of the Code)

Present Law

Present law, as modified by the 1993 Act, provides certain aggregation and look-through rules in connection with requiring U.S. shareholders of a controlled foreign corporation to include in income certain of the corporation's earnings invested in excess passive assets. Under the aggregation rule, certain groups of controlled foreign corporations that are linked by stock ownership of more than 50 percent (CFC groups) are treated as a single corporation for purposes of determining their earnings invested in excess passive assets. Look-through treatment applies to certain corporations whose stock is owned at least 25 percent by a controlled foreign corporation. Some have argued that these rules permit the assets of one foreign corporation to be taken into account more than once through a combination of CFC group treatment and look-through treatment. In addition, some have argued that these rules permit the assets of one foreign corporation to be taken into account more than once through membership of the foreign corporation in more than one CFC group.

Explanation of Provision

The bill clarifies that, within the regulatory authority provided to the Secretary of the Treasury under the 1993 Act, regulations are specifically authorized to coordinate the CFC group treatment and look-through treatment applicable for purposes of determining a foreign corporation's earnings invested in excess passive assets. Pending the promulgation of guidance by the Secretary, it is intended that taxpayers be permitted to coordinate such treatment using any reasonable method for taking assets into account only once, so long as the method is consistently applied to all controlled foreign corporations (whether or not members of any CFC group) in all taxable years.

9. Treatment of certain leased assets for PFIC purposes (sec. 1703(i)(5) of the bill, sec. 13231(d)(4) of the 1993 Act, and sec. 1297(d) of the Code)

Present Law

Under present law, as modified by the 1993 Act, certain property leased by a foreign corporation may be treated as an asset actually owned by the foreign corporation in measuring the assets of the foreign corporation for purposes of the passive foreign investment company ("PFIC") asset test of section 1296(a)(2). The 1993 Act provided a special measurement rule, under which the adjusted

[31] Incurred in taxable years beginning after September 30, 1993.

basis of the leased asset for this purpose is determined by reference to the unamortized portion of the present value of the payments under the lease for the use of the property. Some have argued, however, that the special measurement rule does not apply to PFICs that are permitted to measure their assets by fair market value, rather than by adjusted basis. Under this argument, the entire fair market value of the leased asset might be treated as owned by the foreign corporation.

Explanation of Provision

The bill clarifies that, in the case of any item of property leased by a foreign corporation and treated as an asset actually owned by the foreign corporation in measuring the assets of the foreign corporation for purposes of the PFIC asset test, the amount taken into account with respect to the leased property is the amount determined under the 1993 Act's special measurement rule, which is based on the unamortized portion of the present value of the payments under the lease for the use of the property. That is, the provision clarifies that the special measurement rule of the 1993 Act applies to all PFICs, regardless of whether they are generally permitted to measure their assets by fair market value rather than adjusted basis.

10. Amortization of goodwill and certain other intangibles (sec. 1703(k) of the bill, sec. 13261(g) of the 1993 Act, and sec. 197 of the Code)

Present Law

The 1993 Act allows amortization deductions to certain intangible assets acquired after the 1993 Act's effective date that were not amortizable under prior law. The 1993 Act contains "antichurning" rules that deny amortization to intangible assets that were not amortizable under prior law if such assets are acquired by the taxpayer after the effective date from certain related parties.

The 1993 Act also contains an election under which a taxpayer and certain related parties may elect to treat all acquisitions after July 25, 1991 as subject to the provisions of the 1993 Act.

Explanation of Provision

The bill clarifies that when a taxpayer and its related parties have made an election to apply the 1993 Act to all acquisitions after July 25, 1991, the antichurning rules will not apply when property acquired from an unrelated party after July 25, 1991 (and not subject to the antichurning rules in the hands of the acquirer) is transferred to a taxpayer related to the acquirer after the date of enactment of the 1993 Act.

11. Empowerment zones and eligibility of small farms for tax incentives (sec. 1703(l) of the bill, sec. 13301 of the 1993 Act, and sec. 1397B(d)(5)(B) of the Code)

Present Law

Pursuant to the 1993 Act, on December 21, 1994, six empowerment zones and 65 enterprise communities were designated in eligible urban areas, and three empowerment zones and 30 enterprise communities were designated in rural areas. Special tax incentives (i.e., a wage credit, additional section 179 expensing, and expanded tax-exempt financing) are available for certain business activities conducted in urban and rural empowerment zones. Expanded tax-exempt financing benefits are available for certain facilities located in urban and rural enterprise communities.

The empowerment zone wage credit is not available with respect to any individual employed by a trade or business the principal activity of which is farming (within the meaning of subparagraphs (A) and (B) of section 2032A(e)(5)) if, as of the close of the current taxable year, the sum of the aggregate unadjusted bases (or, if greater, the fair market value) of assets of the farm exceed $500,000 (sec. 1396(d)(2)(E)). In contrast, the additional section 179 expensing (available in empowerment zones) and expanded tax-exempt financing benefits (available in both empowerment zones and enterprise communities) are not allowed for any trade or business the principal activity of which is farming if, as of the close of the preceding taxable year, the sum of the aggregate bases (or, if greater, the fair market value) of the assets of the farm exceed $500,000 (sec. 1397B(d)(5)).

Explanation of Provision

The bill provides that the $500,000 asset test for determining whether a farm is eligible for additional section 179 expensing (in an empowerment zone) and expanded tax-exempt financing benefits (in an empowerment zone or enterprise community) is applied based on the assets of the farm at the end of the current taxable year. Thus, the $500,000 asset test for determining farm eligibility is based on the same taxable period (i.e., the current taxable year) for purposes of all tax incentives available in empowerment zones and enterprise communities.

C. Other Tax Technical Corrections

1. Hedge bonds (sec. 1704(b) of the bill, sec. 11701 of the 1989 Act, and sec. 149(g) of the Code)

Present Law

The 1989 Act provided generally that interest on hedge bonds is not tax-exempt unless prescribed minimum percentages of the proceeds are reasonably expected to be spent at set intervals during the five-year period after issuance of the bonds (sec. 149(g)). A hedge bond is defined generally as a bond (1) at least 85 percent of the proceeds of which is not reasonably expected to be spent within three years following issuance and (2) more than 50 percent

of the proceeds of which is invested at substantially guaranteed yields for four years or more.

This restriction does not apply, however, if at least 95 percent of the bond proceeds is invested in other tax-exempt bonds (not subject to the alternative minimum tax). The 95-percent investment requirement is not violated if investment earnings exceeding five percent of the proceeds are temporarily invested for up to 30 days pending reinvestment in taxable (including alternative minimum taxable) investments.

This provision is effective as if included in the Omnibus Budget Reconciliation Act of 1989.

Explanation of Provision

The bill clarifies that the 30-day exception for temporary investments of investment earnings applies to amounts (i.e., principal and earnings thereon) temporarily invested during the 30-day period immediately preceding redemption of the bonds as well as such periods preceding reinvestment of the proceeds.

2. Withholding on distributions from U.S. real property holding companies (sec. 1704(c) of the bill, sec. 129 of the Deficit Reduction Act of 1984, and sec. 1445 of the Code)

Present Law

In general

Under the Foreign Investment in Real Property Tax Act of 1980 ("FIRPTA"), a foreign investor that disposes of a U.S. real property interest generally is required to pay tax on any gain on the disposition. For this purpose a U.S. real property interest generally includes stock in a domestic corporation that is a U.S. real property holding corporation ("USRPHC"), or was a USRPHC at any time during the previous five years.

A sale or exchange of stock in a USRPHC is an example of a disposition of a U.S. real property interest. In addition, provisions of subchapter C of the Code treat amounts received in certain corporate distributions as amounts received in sales or exchanges, giving rise to tax liability under the FIRPTA rules when a foreign person receives such a distribution from a present or former USRPHC. Thus, amounts received by a foreign shareholder in a USRPHC in a distribution in complete liquidation of the USRPHC are treated as in full payment in exchange for the USRPHC stock, and are therefore subject to tax under FIRPTA (sec. 331; Treas. Reg. sec. 1.897–5T(b)(2)(iii)). Similarly, amounts received by a foreign shareholder in a USRPHC upon redemption of the USRPHC stock are treated as a distribution in part or full payment in exchange for the stock, and are therefore subject to tax under FIRPTA (sec. 302(a); Treas. Reg. sec. 1.897–5T(b)(2)(ii)). Third, amounts received by a foreign shareholder in a USRPHC, in a section 301 distribution from the USRPHC that exceeds the available earnings and profits of the USRPHC, are treated as gain from the sale or exchange of the shareholder's USRPHC stock to the extent that they exceed the shareholder's adjusted basis in the stock; such amounts

are therefore also subject to tax under FIRPTA (sec. 301(c)(3); Treas. Reg. sec. 1.897–5T(b)(2)(i)).

FIRPTA withholding

The Deficit Reduction Act of 1984 established a withholding system to enforce the FIRPTA tax. Unless an exception applies, a transferee of a U.S. real property interest from a foreign person generally is required to withhold the lesser of 10 percent of the amount realized (purchase price), or the maximum tax liability on disposition (as determined by the IRS) (sec. 1445). Such withholding may be reduced or eliminated pursuant to a withholding certificate issued by the Internal Revenue Service (Treas. Reg. sec. 1.1445–3).

Although the FIRPTA withholding requirement by its terms generally applies to all dispositions of U.S. real property interests, and subchapter C treats amounts received in certain distributions as amounts received in sales or exchanges, the FIRPTA withholding provisions also provide express rules for withholding on certain distributions treated as sales or exchanges. Generally, distributions in a transaction to which section 302 (redemptions) or part II of subchapter C (liquidations) applies are subject to 10-percent withholding.[32] Although a section 301 distribution in excess of earnings and profits is also treated as a disposition for purposes of computing the FIRPTA liability of a foreign recipient of the distribution, there is no corresponding withholding provision expressly addressed to the payor of such a distribution.

Explanation of Provision

The bill clarifies that FIRPTA withholding requirements apply to any section 301 distribution to a foreign person by a domestic corporation that is or was a USRPHC, which distribution is not made out of the corporation's earnings and profits and is therefore treated as an amount received in a sale or exchange of a U.S. real property interest. (The bill does not alter the withholding treatment of section 301 distributions by such a corporation that are out of earnings and profits.) Under the bill, the FIRPTA withholding requirements that apply to a section 301 distribution not out of earnings and profits are similar to the requirements applicable to redemption or liquidation distributions to a foreign person by such a corporation. It is anticipated that withholding certificates will be available to taxpayers that expect to receive section 301 distributions not out of earnings and profits.

The provision is effective for distributions made after the date of enactment of the bill. No inference is intended to be drawn from the provision as to the FIRPTA withholding requirements applicable to such a distribution under present law.

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[32] Under other rules, dividend distributions (i.e., distributions to which sec. 301(c)(1) applies) to foreign persons by U.S. corporations, including USRPHCs, are subject to 30-percent withholding under the Code. Under treaties, the withholding on a dividend may be reduced to as little as 5 or 15 percent.

3. Treatment of credits attributable to working interests in oil and gas properties (sec. 1704(d) of the bill, sec. 501 of the Tax Reform Act of 1986, and sec. 469 of the Code)

Present Law

Under present law, a working interest in an oil and gas property which does not limit the liability of the taxpayer is not a "passive activity" for purposes of the passive loss rules (sec. 469). However, if any loss from an activity is treated as not being a passive loss by reason of being from a working interest, any net income from the activity in subsequent years is not treated as income from a passive activity, notwithstanding that the activity may otherwise have become passive with respect to the taxpayer.

Explanation of Provision

The bill clarifies that any credit attributable to a working interest in an oil and gas property, in a taxable year in which the activity is no longer treated as not being a passive activity, will not be treated as attributable to a passive activity to the extent of any tax allocable to the net income from the activity for the taxable year. Any credits from the activity in excess of this amount of tax will continue to be treated as arising from a passive activity and will be treated under the rules generally applicable to the passive activity credit. The provision applies to taxable years beginning after December 31, 1986.

4. Clarification of passive loss disposition rule (sec. 1704(e) of the bill, sec. 501 of the Tax Reform Act of 1986, sec. 1005(a)(2)(A) of the Technical and Miscellaneous Revenue Act of 1988, and sec. 469(g)(1)(A) of the Code)

Present Law

The Tax Reform Act of 1986 ("1986 Act") provided that if a passive activity is disposed of in a transaction in which all gain or loss is recognized, any overall loss from the activity in the year of disposition is recognized and allowed against income (whether active or passive income).[33] The language of the 1986 Act provided that any loss was allowable, first, against income or gain from the passive activity, second, against income or gain from all passive activities, and finally, against any other income or gain. This rule was rewritten by the technical corrections portion of the Technical and Miscellaneous Revenue Act of 1988 ("1988 Act"). The statutory language (as amended by the 1988 Act) providing for the computation of the overall loss for the taxable year of disposition is not entirely clear where the activity is disposed of at a gain.

Explanation of Provision

The bill clarifies the rule relating to the computation of the overall loss allowed upon the disposition of a passive activity. The bill provides that, in a transaction in which all gain or loss is recognized on the disposition of a passive activity, any loss from the activity for the taxable year (taking into account all income, gain, and loss, including gain or loss recognized on the disposition) in excess

of any net income or gain from other passive activities for the taxable year is treated as a loss which is not from a passive activity. The provision applies to taxable years beginning after December 31, 1986.

5. Estate tax unified credit allowed nonresident aliens under treaty (sec. 1704(f)(1) of the bill, sec. 5032(b)(2) of the Technical and Miscellaneous Revenue Act of 1988, and sec. 2102(c)(3)(A) of the Code)

Present Law

Amount subject to tax

For U.S. citizens and residents, the amount subject to Federal estate and gift tax is determined by reference to all property, wherever situated. For nonresident aliens, the Code provides that the amount subject to Federal estate and gift tax is determined only by reference to property situated in the United States.

The United States has entered into bilateral treaties designed to avoid double transfer taxation. Early treaties typically did this by providing rules for determining situs and requiring that the State of domicile allow a credit for taxes paid to the situs country.[34] In contrast, treaties signed in the 1980s, and the U.S. and OECD model treaties, exempt most property, wherever situated, from taxation outside the State of domicile.[35]

Specific exemption and unified credit

Prior to the Tax Reform Act of 1976 ("1976 Act"), the Code allowed a "specific exemption" against the estate tax. The estate of a U.S. citizen or resident was allowed an exemption of $60,000, while the estate of a nonresident alien was allowed a lesser amount. A number of U.S. estate tax treaties ratified in the 1950s allowed a nonresident alien a "specific exemption" equal to the exemption allowed a U.S. citizen or resident multiplied by the percentage of the gross estate subject to U.S. estate tax (the "pro rata exemption").[36]

The 1976 Act replaced the specific exemption with a unified credit of $47,000 for the estate of U.S. citizen or resident and $3,600 for the estate of a nonresident alien. After 1976, two courts interpreted the pro rata exemption allowed in the 1950s treaties as applying to the unified credit, i.e., as allowing a unified credit no less than the unified credit allowed a U.S. citizen or resident multiplied by the percentage of the gross estate situated in the United States (and therefore subject to U.S. estate tax under those treaties).[37]

The Technical and Miscellaneous Revenue Act of 1988 ("1988 Act") increased the unified credit allowed an estate of a non-

[33] See S. Rept. 99–313, p. 725.

[34] See Staff of the Joint Committee on Taxation, 98th Cong., 2d Sess., *Explanation of Proposed Estate and Gift Tax Treaty Between the United States and Sweden* 8 (1984).

[35] See, e.g., U.S. Treasury Model Estate and Gift Tax Treaty (1980), Article 7, paragraph 1: "Transfers and deemed transfers by an individual domiciled in a Contracting State of property other an property referred to in Article 5 (Real Property) and 6 (Business Property of a Permanent Establishment and Assets Pertaining to a Fixed Base Used for the Performance of Independent Personal Services) shall be taxable only in that State."

[36] See Rev. Rul. 81–303, 1981–2 C.B. 255.

[37] See *Mudry* v. *United States*, 11 Cl. Ct. 207 (1986) (Swiss treaty); *Burghardt* v. *Commis-*

resident alien to $13,000. In so doing, the 1988 Act provided that, "to the extent required by any treaty," the estate of a nonresident alien is allowed a unified credit equal to the unified credit allowed a U.S. citizen or resident multiplied by the percentage of the gross estate situated in the United States (Code sec. 2102(c)(3)(A)). Thus, the 1988 Act did not override the "specific exemption" language of the 1950s treaties, as interpreted by the two courts, and could be interpreted as encouraging the negotiation of pro rata unified credits in future treaties.

Explanation of Provision

The bill clarifies that in determining the pro rata unified credit required by treaty, property exempted by the treaty from U.S. estate tax is not treated as situated in the United States. Under this rule, a treaty granting a pro rata unified credit would allow a nonresident alien the unified credit allowed a U.S. citizen or resident multiplied by the percentage of the gross estate subject to U.S. estate tax, as modified by treaty.

The bill is not intended to affect existing treaties that contain pro rata exemptions pursuant to which the assets reserved for situs taxation by the non-domiciliary country are specifically described. In the case of a treaty that contains pro rata exemption but does not provide rules for determining the situs for property (e.g., the treaty with Canada), the bill clarifies that property exempted by the treaty from U.S. estate tax is not treated as situated in the United States. For future treaties, it is intended that any pro rata unified credit negotiated not exceed the proportion of the gross worldwide estate subject to U.S. estate and gift tax, as modified by treaty.

The provision is effective upon the date of its enactment.

6. Limitation on deduction for certain interest paid by corporation to related persons (sec. 1704(f)(2)(A) of the bill, sec. 7210(a) of the 1989 Act, and sec. 163(j) of the Code)

Present Law

Subject to certain limitations, a taxpayer may deduct interest paid or accrued on indebtedness within a taxable year (sec. 163(a)). The 1989 Act added a so-called "earnings stripping" limitation on interest deductibility with respect to certain interest paid by corporations to related persons (sec. 163(j)). If the provision applies to a corporation for a taxable year, it disallows deductions for certain amounts of "disqualified interest" paid or accrued by the corporation during that year. If in a taxable year a deduction is disallowed, under the provision, for an amount of interest paid or accrued in that year, the disallowed amount is treated under the earnings stripping provision as disqualified interest paid or accrued in the succeeding taxable year.[38]

In order for the earnings stripping provision to apply to a corporation for a taxable year, two thresholds must be exceeded. To

[38] Disqualified interest is interest paid by a corporation to related persons that are not subject to U.S. tax on the interest received. (If, in accordance with a U.S. income tax treaty, interest income of a related person is subject to a reduced rate of U.S. tax, a portion of the interest paid to the related person is deemed to be interest on which no tax is imposed.)

exceed the first threshold, the corporation must have "excess interest expense" as that term is defined in the Code for this purpose. To exceed the second threshold, the corporation must have a ratio of debt to equity as of the close of the taxable year in question (or on any other day prescribed by the Secretary in regulations) that exceeds 1.5 to 1. Excess interest expense is the excess (if any) of the corporation's net interest expense over the sum of 50 percent of the adjusted taxable income of the corporation plus any excess limitation carryforward from a prior year. Excess limitation is the excess (if any) of 50 percent of adjusted taxable income over net interest expense.

Explanation of Provision

The bill provides that the debt-equity threshold does not apply for purposes of applying the earnings stripping provision to a carryover of excess interest expense from a prior taxable year. Thus, the bill clarifies that excess interest carried forward from a year in which the debt-equity ratio threshold is exceeded may be deducted in a subsequent year in which that threshold is not exceeded, but only to the extent that such interest would not otherwise be treated as excess interest expense in the carryforward year.

For example, assume that in year 1 $20 of a corporation's interest expense is nondeductible due to the operation of the earnings stripping provision. The corporation carries forward the $20 of interest deduction that it could not use in year 1. Assume that in year 2 the corporation has a debt-equity ratio of 1 to 1 and $50 of current net and gross interest expense, all of which is disqualified interest, and that it earns $400 of adjusted taxable income. The bill is intended to clarify that the $20 of interest carried forward from year 1 is deductible in year 2. This is because $70, the sum of the current net interest expense for year 2 ($50) plus the interest expense carried over from year 1 ($20), does not exceed one-half of adjusted taxable income in year 2.

As another example, assume that in year 2 the corporation has a debt-equity ratio of 1 to 1 and $50 of current net and gross interest expense, all of which is disqualified interest, and that it earns $80 of adjusted taxable income. The bill is intended to clarify that the $20 of interest carried forward from year 1 is not deductible in year 2. This is because the current net interest expense for year 2 ($50) exceeds by $10 one-half of adjusted taxable income in year 2 ($80 divided by 2, or $40). Therefore, treating the year 1 carryover as an interest expense in year 2 causes the corporation to have excess interest expense equal to $30. But for the debt-equity safe harbor, the corporation would have a $30 interest expense disallowance in year 2 if the carried over amount were treated as having been paid in year 2. Under the bill, no actual year 2 interest can be disallowed. However, under these facts, none of the interest carried over from year 1 can be deducted in year 2. Instead, the interest carried over from year 1 is carried forward for potential deduction (subject to the same rules that applied to the carryforward in year 2) in a year subsequent to year 2.

As a third example, assume that in year 2 the corporation has a debt-equity ratio of 1 to 1 and $50 of current net and gross interest expense, all of which is disqualified interest, and that it earns

$110 of adjusted taxable income. The bill is intended to clarify that $5 of interest carried forward from year 1 is deductible in year 2, and the other $15 of interest carried forward from year 1 is not deductible in year 2. This is because the current net interest expense for year 2 ($50) is $5 less than one-half of adjusted taxable income in year 2 (one-half of $110, or $55). Therefore, even if the debt-equity safe harbor had not been met in year 2, the corporation would have had $5 of excess limitation in year 2 had there been no carryover amount from year 1. On the other hand, treating the year 1 carryover as an interest expense in year 2 causes the corporation to have excess interest expense equal to $15. This $15 may be carried forward to a subsequent year.

The provision is effective as if included in the amendments made by section 7210(a) of the Revenue Reconciliation Act of 1989.

7. Interaction between passive activity loss rules and earnings stripping rules (secs. 1704(f)(2) (B) and (C) of the bill, sec. 7210(a) of the 1989 Act, and sec. 163(j) of the Code)

Present Law

The passive loss rules limit deductions and credits from passive trade or business activities (sec. 469). Deductions attributable to passive activities, to the extent they exceed income from passive activities, generally may not be deducted against other income, such as wages, portfolio income, or business income that is not derived from a passive activity. Deductions and credits that are suspended are carried forward and treated as deductions and credits from passive activities in the next year. Suspended losses from a passive activity are allowed in full when a taxpayer disposes of his entire interest in the passive activity to an unrelated person. The passive loss rules apply to any taxpayer that is an individual, estate, trust, closely held C corporation, or personal service corporation. In determining passive activity deductions, Treasury regulations provide that "an item of deduction arises in the taxable year in which the item would be allowable as a deduction under the taxpayer's method of accounting if taxable income for all taxable years were determined without regard to sections 469, 613A(d) and 1211" (Treas. Reg. sec. 1.469–2(d)(8)). Thus, these regulations effectively require other limitations to be applied before applying the passive loss rules.

The at-risk rules limit deductible losses from an activity to the amount that the taxpayer has at risk, in the case of an individual or a closely-held corporation (sec. 465). The amount at risk is generally the sum of (1) cash contributions, (2) the adjusted basis of contributed property, and (3) amounts borrowed for use in the activity with respect to which the taxpayer has personal liability or has pledged as security property not used in the activity. The amount at risk is increased by income from the activity and decreased by losses and withdrawals.

A taxpayer generally may deduct interest paid or accrued on indebtedness within a taxable year (sec. 163(a)). The Revenue Reconciliation Act of 1989 (the "1989 Act") added an "earnings stripping" limitation on interest deductibility with respect to certain in-

terest paid by corporations to related persons (sec. 163(j)). If the provision applies to a corporation for a taxable year, it disallows deductions for certain amounts of "disqualified interest" paid or accrued by the corporation during that year. Disqualified interest is interest paid by a corporation to related persons that are not subject to U.S. tax on the interest received. The disallowed amount is treated under the earnings stripping provision as disqualified interest paid or accrued in the succeeding taxable year. Proposed Treasury regulations would provide that "sections 465 and 469 shall be applied before applying section 163(j)" (Prop. Treas. Reg. sec. 1.163(j)–7(b)(3)).

Explanation of Provision

The provision modifies section 163(j) of the Code to clarify that the earnings stripping rules apply before the passive loss rules and the at-risk rules.

The provision is effective as if included in the 1989 Act.

8. Branch-level interest tax (sec. 1704(f)(3) of the bill, sec. 1241 of the 1986 Act, and sec. 884 of the Code)

Present Law

Interest paid (or treated as if paid) by a U.S. trade or business (i.e., a U.S. branch) of a foreign corporation is treated as if paid by a U.S. corporation and, hence, is U.S. source and subject to U.S. withholding tax of 30 percent, unless the tax is reduced or eliminated by a specific Code or treaty provision. The Treasury has regulatory authority to limit U.S. sourcing, and hence U.S. withholding, to the amount of interest reasonably expected to be deducted in arriving at the U.S. branch's effectively connected taxable income.

To the extent a U.S. branch of a foreign corporation has allocated to it under Treasury Regulation section 1.882–5 an interest deduction in excess of the interest actually paid by the branch (this generally occurs where the indebtedness of the U.S. branch is disproportionately small compared to the total indebtedness of the foreign corporation), the excess is treated as if it were interest paid on a notional loan to a U.S. subsidiary (the U.S. branch, in actuality) from its foreign corporate parent (the home office). This excess is subject to the 30-percent tax, absent a specific Code exemption or treaty reduction (sec. 884(f)(1)(B)).

These branch-level interest taxes, along with the branch profits tax, were intended to reflect the view that a foreign corporation doing business in the United States generally should be subject to the same substantive tax rules that apply to a foreign corporation operating in the United States through a U.S. subsidiary.[39] Where a U.S. corporation pays interest to its foreign corporate parent, that interest, like the interest deducted by a U.S. branch of a foreign corporation, is also generally subject to a 30-percent U.S. withholding tax unless the tax is reduced by treaty. In the case of a U.S. subsidiary of a foreign parent corporation, the withholding tax

[39] Staff of the Joint Committee on Taxation, 100th Cong., 1st Sess. *General Explanation of the Tax Reform Act of 1986,* at 1036 (1987).

applies without regard to whether the interest payment is currently deductible by the U.S. subsidiary. For example, deductions for interest may be delayed or denied under section 163, 263, 263A, 266, 267, or 469, but it is still subject (or not subject) to withholding when paid without regard to the operation of those provisions.

Explanation of Provision

The bill provides that the branch level interest tax on interest not actually paid by the branch applies to any interest which is allocable to income which is effectively connected with the conduct of a trade or business in the United States. Similarly, in the case of interest paid by the U.S. branch, the bill provides regulatory authority to limit U.S. sourcing, and hence U.S. withholding, to the amount of interest reasonably expected to be allocable to income which is effectively connected with the conduct of a trade or business in the United States. Thus, where an interest expense of a foreign corporation is allocable to U.S. effectively connected income, but that interest expense would not have been fully deductible for tax purposes under another Code provision had it been paid by a U.S. corporation, the bill clarifies that such interest is nonetheless treated for branch level interest tax purposes like a payment by a U.S. corporation to a foreign corporate parent. Similarly, with regard to the Treasury's regulatory authority to treat an interest payment by a foreign corporation's U.S. branch as though not paid by a U.S. person for source and withholding purposes, the bill clarifies that the authority extends to interest payments in excess of those reasonably expected to be allocable to U.S. effectively connected income of the foreign corporation.

These provisions are effective as if they were made by the Tax Reform Act of 1986.

9. Determination of source in case of sales of inventory property (sec. 1704(f)(4) of the bill, sec. 211 of the 1986 Act, and sec. 865(b) of the Code)

Present Law

Prior to the 1986 Act, the source of income derived from the sale of personal property generally was determined by the place of sale (commonly referred to as the "title passage" rule) (see, e.g., Treas. Reg. sec. 1.861-7, T.D. 6258, 1957-2 C.B. 368). While the 1986 Act generally replaced the place-of-sale rule for sales of personal property with a residence-of-the-seller rule (sec. 865(a)), the Act did not change the place-of-sale rule for most sales of inventory property (sec. 865(b)).

Before and after the 1986 Act, statutory rules for sourcing income from inventory sales have included those covering income from (1) purchasing inventory property outside the United States (other than within a U.S. possession) and selling it in the United States (sec. 861(a)(6)); (2) purchasing inventory property in the United States and selling it outside the United States (sec. 862(a)(6)); (3) selling outside the United States inventory property which has been produced by the taxpayer in the United States (or selling in the United States inventory property which has been produced by the taxpayer outside the United States) (sec. 863(b)(2));

and (4) purchasing inventory property in a U.S. possession and selling it in the United States (sec. 863(b)(3)). Prior to the 1986 Act, these provisions were not limited in application to income from sales of inventory property, but rather covered sales of personal property generally.

In addition to statutory rules for sourcing items of income from transactions involving inventory property specified in the Code, such as those listed above, the Code both before and after the 1986 Act has contained other sourcing rules that do not make specific reference to property sales, and includes general regulatory authority to allocate and apportion between U.S. and foreign sources items of gross income, expenses, losses, and deductions other than those specified in sections 861(a) and 862(a) (sec. 863(a)). In carving income from the sale inventory property out of the general residence-of-the-seller rule of section 865, section 865(b) makes reference to the above statutory rules making specific reference to inventory property, but not to the general grant of regulatory authority in section 863(a).

Explanation of Provision

The bill modifies the general provision relating to the sourcing of income from the sale of personal property (sec. 865) so that the cross-reference to sourcing rules applicable to inventory property includes a reference to all of section 863, rather than simply to section 863(b). The bill thus clarifies that, to the extent that the Secretary of the Treasury had general regulatory authority to provide rules for the sourcing of income from the sales of personal property prior to the 1986 Act, the Secretary of the Treasury retains that authority under present law with respect to inventory property.

The bill is not intended to increase the Treasury Secretary's regulatory authority under section 863(a) beyond the authority that he had under the law in effect prior to the enactment of the 1986 Act. It is intended that no inference be drawn from this provision either as to the correctness of, or as to the post-1986 Act implications of, any judicial decision interpreting the scope of that pre-1986 Act authority.

The provision is effective as if it were included in the Tax Reform Act of 1986.

10. Repeal of obsolete provisions (sec. 1704(f)(5) of the bill, sec. 10202 of the Revenue Act of 1987, and secs. 6038(a)(1)(F) and 6038A(b)(4) of the Code)

Present Law

A U.S. person who controls a foreign corporation must report certain information related to that foreign corporation as may be required by the Treasury Secretary (sec. 6038). Information reporting is also required with respect to certain foreign-owned domestic corporations (sec. 6038A). Included under each of these information reporting provisions is a requirement to report such information as the Treasury Secretary may require for purposes of carrying out the provisions of section 453C. Section 453C, relating to certain indebtedness treated as payment on installment obligations (the so-

called "proportional disallowance rule"), was repealed in the Revenue Act of 1987.

Explanation of Provision

The bill repeals as obsolete the information reporting requirements of sections 6038 and 6038A relating to section 453C. The provision is effective upon the date of its enactment.

11. Clarification of a certain stadium bond transition rule in Tax Reform Act of 1986 (sec. 1704(g) of the bill and sec. 1317(3)(A) of the Tax Reform Act of 1986)

Present Law

The Tax Reform Act of 1986 included a transition rule authorizing tax-exempt bonds not exceeding $200 million to be issued by or on behalf of the City of Cleveland, Ohio, to finance a stadium. The bonds were required to be issued before January 1, 1991 (and were so issued). As enacted, the rule required Cleveland to retain a residual interest in the stadium following planned private business use.

Explanation of Provision

The bill permits the residual interest in the stadium currently held by the City of Cleveland to be assigned to Cuyahoga County, Ohio (the county in which both Cleveland and the stadium are located) because of a change in Ohio State law prior to issuance of the bonds. The bill does not extend the time for issuing the bonds or otherwise affect the amount of bonds or the location or design of the stadium.

This provision is effective as if included in the Tax Reform Act of 1986.

12. Health care continuation rules (sec. 1704(h) of the bill, sec. 7862(c)(5) of the 1989 Act, sec. 4980B(f)(2)(B)(i) of the Code, sec. 602(2)(A) of ERISA, and sec. 2202(2)(A) of the Public Health Service Act)

Present Law

The Revenue Reconciliation Act of 1989 ("1989 Act") amended the health care continuation rules to provide that if a covered employee is entitled to Medicare and within 18 months of such entitlement separates from service or has a reduction in hours, the duration of continuation coverage for the spouse and dependents is 36 months from the date the covered employee became entitled to Medicare. One possible interpretation of the statutory language, however, would permit continuation coverage for up to 54 months. This extension of the coverage period was not intended.

Explanation of Provision

The bill amends the Code (sec. 4980B), title I of the Employee Retirement Income Security Act (sec. 602), and the Public Health Service Act (sec. 2202(2)(A)) to limit the continuation coverage in

such cases to no more than 36 months. The provision is effective for plan years beginning after December 31, 1989.

13. Taxation of excess inclusions of a residual interest in a REMIC for taxpayers subject to alternative minimum tax with net operating losses (sec. 1704(i) of the bill and sec. 860E(a)(6) of the Code)

Present Law

Residual interests in a REMIC

A real estate mortgage investment conduit ("REMIC") is an entity that holds real estate mortgages. All interests in a REMIC must be "regular interests" or "residual interests." A regular interest is an interest the terms of which are fixed on the start-up day, which unconditionally entitles the holder to receive a specified principal amount, and which provides that interest amounts are payable based on a fixed rate (or a variable rate to the extent provided in the Treasury regulations). A residual interest is any interest that is so designated and that is not a regular interest in a REMIC.

Generally, the holder of a residual interest in a REMIC takes into account his daily portion of the taxable income or net loss of such REMIC for each day during which he held such interest. The taxable income of any holder of a residual interest in a REMIC for any taxable year cannot be less than the excess inclusion for the year (sec. 860E). Thus, in general, income from excess inclusions cannot be offset by a net operating loss (or net operating loss carryover) in computing the taxpayer's regular tax.

Alternative minimum tax

Taxpayers are subject to an alternative minimum tax which is payable, in addition to all other tax liabilities, to the extent it exceeds the taxpayer's regular tax. The tax is imposed at rates of 26 and 28 percent (20 percent in the case of a corporation) on alternative minimum taxable income in excess of an exemption amount. Alternative minimum taxable income generally is the taxpayer's taxable income, as increased or decreased by certain adjustments and preferences. A taxpayer may offset no more than ninety percent of its alternative minimum taxable income with its alternative tax net operating loss carryover.

Because the determination of a taxpayer's alternative minimum taxable income begins with taxable income, a holder of a residual interest in a REMIC may have positive alternative minimum taxable income even where the taxpayer has a net operating loss for the year.

Explanation of Provision

The bill provides that three rules for determining the alternative minimum taxable income of a taxpayer that is not a thrift institution that holds residual interests in a REMIC.

First, the alternative minimum taxable income of such a taxpayer is computed without regard to the REMIC rule that taxable

income cannot be less than the amount of excess inclusions. This provision prevents a taxpayer from having to include in alternative minimum taxable income preference items for which it received no tax benefit.

Second, the alternative minimum taxable income of such a taxpayer for a taxable year cannot be less than the excess inclusions of the residual interests for that year. In effect, this provision prevents nonrefundable credits from reducing the taxpayer's income tax below an amount equal to what the tentative minimum tax would be if computed only on excess inclusions.

Third, the amount of any alternative minimum tax net operating loss deduction of such a taxpayer is computed without regard to any excess inclusions. This provision insures that the net operating losses will not reduce any income attributable to any excess inclusions. Thus, all such taxpayers subject to the alternative minimum tax will pay a tax on excess inclusions at the alternative minimum tax rate, regardless of whether the taxpayer has a net operating loss.

The provision is effective for all taxable years beginning after December 31, 1986, unless the taxpayer elects to apply the rules of the bill only to taxable years beginning after the date of enactment.

14. Application of harbor maintenance tax to Alaska and Hawaii ship passengers (sec. 1704(j) of the bill and sec. 4462(b) of the Code)

Present Law

A harbor maintenance excise tax ("harbor tax") of 0.125 percent of value applies generally to commercial cargo (including passenger fares) loaded or unloaded at U.S. ports (sec. 4461). The harbor tax does not apply to commercial cargo (other than crude oil with respect to Alaska) loaded or unloaded in Alaska, Hawaii, and U.S. possessions where such cargo is transported to or from the U.S. mainland (for domestic use) or where such cargo is loaded and unloaded in the same State (Alaska or Hawaii) or possession (sec. 4462(b)).

Explanation of Provision

The bill clarifies that the harbor tax does not apply to passenger fares where the passengers are transported on U.S. flag vessels operating solely within the State waters of Alaska or Hawaii and adjacent international waters (i.e., leaving and returning to a port in the same State without stopping elsewhere).

The provision applies as if included in the Harbor Maintenance Revenue Act of 1986 (April 1, 1987).

15. Modify effective date provision relating to the Energy Policy Act of 1992 (sec. 1704(k) of the bill and secs. 53 and 30 of the Code)

Present Law

The nonconventional fuels production credit (sec. 29) cannot reduce the taxpayer's tax liability to less than the amount of the tentative minimum tax. The credit for prior year minimum tax liabil-

ity (sec. 53) is increased by the amount of the nonconventional fuels credit not allowed for the taxable year solely by reason of the limitation based on the taxpayer's tentative minimum tax.

Explanation of Provision

The bill corrects a cross reference to section 29(b)(6)(B) contained in section 53(d)(1)(B)(iv), and clarifies that the correction applies to taxable years beginning after December 31, 1990. In addition, section 2(e)(5) of the bill clarifies that a correction made in the Energy Policy Act of 1992 to a similar cross reference in section 53(d)(1)(B)(iii) applies to taxable years beginning after December 31, 1990.

The bill also clarifies the relationship between the basis adjustment rules for the electric vehicle credit (sec. 30(d)(1)) and the alternative minimum tax.

16. Treat qualified football coaches plan as multiemployer pension plan for purposes of the Internal Revenue Code (sec. 1704(l) of the bill and sec. 1022 of ERISA)

Present Law

Section 3(37) of the Employee Retirement Income Security Act of 1974 ("ERISA"), as amended by Public Law 100–202 (Continuing Appropriations for Fiscal Year 1988), provides that, for purposes of Title I of ERISA, a qualified football coaches plan generally is treated as a multiemployer plan and may include a qualified cash or deferred arrangement. Under section 3(37) of ERISA, a qualified football coaches plan is defined as any defined contribution plan established and maintained by an organization described in section 501(c) of the Internal Revenue Code (the "Code"), the membership of which consists entirely of individuals who primarily coach football as full-time employees of 4-year colleges or universities, if the organization was in existence on September 18, 1986. This definition is generally intended to apply to the American Football Coaches Association.

However, section 9343(a) of the Omnibus Budget Reconciliation Act of 1987 (P.L. 100–203) provides that Titles I and IV of ERISA are not applicable in interpreting Title II of ERISA (the Code provisions relating to qualified plans), except to the extent specifically provided in the Code or as determined by the Secretary of the Treasury.

Explanation of Provision

The bill amends Title II of ERISA to provide that, for purposes of determining the qualified plan status of a qualified football coaches plan, section 3(37) of ERISA is treated as part of Title II of ERISA and a qualified football coaches plan is treated as a multiemployer collectively bargained plan.

The provision is effective for years beginning after December 22, 1987 (the date of enactment of P.L. 100–202).

17. Determination of unrecovered investment in annuity contract (sec. 1704(m) of the bill and sec. 72(b) and (c) of the Code)

Present Law

An exclusion is provided for amounts received as an annuity under an annuity, endowment, or life insurance contract, as determined under a statutory exclusion ratio (sec. 72(b)). The exclusion ratio is determined as the ratio of (1) the taxpayer's investment in the contract (as of the annuity starting date) to (2) the expected return under the contract (as of such date). In the case of a contract with a refund feature, the amount of a taxpayer's investment in the contract is reduced by the value of the refund feature (sec.72(c)).

This exclusion was modified by the Tax Reform Act of 1986 to limit the excludable amount to the taxpayer's unrecovered investment in the contract, and to provide a deduction for the unrecovered investment in the contract if payments as an annuity under the contract cease by reason of the death of an annuitant. In the case of a contract with a refund feature, the 1986 Act modifications reduce the exclusion ratio so that it is possible that less than the entire investment in the contract can be recovered tax-free.

Explanation of Provision

The bill modifies the definition of the unrecovered investment in the contract, in the case of a contract with a refund feature, so that the entire investment in the contract can be recovered tax-free.

The provision is effective as if enacted in the Tax Reform Act of 1986.

18. Election by parent to claim unearned income of certain children on parent's return (sec. 1704(n) of the bill and secs. 1 and 59(j) of the Code)

Present Law

The net unearned income of a child under 14 years of age is taxed to the child at the parent's statutory rate. Net unearned income means unearned income less the sum of $650 (for 1995) and the greater of: (1) $650 (for 1995) or, (2) if the child itemizes deductions, the amount of allowable deductions directly connected with the production of the unearned income. The dollar amounts are adjusted for inflation.

In certain circumstances, a parent may elect to include a child's unearned income on the parent's income tax return if the child's income is less than $5,000. A parent making this election must include the gross income of the child in excess of $1,000 in income for the taxable year. In addition, the parent must report an additional tax liability equal to the lesser of (1) $75 or (2) 15 percent of the excess of the child's income over $500. The dollar amounts for the election are not adjusted for inflation.

A person claimed as a dependent cannot claim a standard deduction exceeding the greater of $650 (for 1995) or such person's earned income. For alternative minimum tax purposes, the exemp-

tion of a child under 14 years of age generally cannot exceed the sum of such child's earned income plus $1,000. The $650 amount is adjusted for inflation but the $1,000 amount is not.

Explanation of Provision

The bill adjusts for inflation the dollar amounts involved in the election to claim unearned income on the parent's return. It likewise indexes the $1,000 amount used in computing the child's alternative minimum tax.

The provision is effective for taxable years beginning after December 31, 1995.

19. Treatment of certain veterans' reemployment rights (sec. 1704(o) of the bill and new sec. 414(u) of the Code)

Present Law

Under the Uniformed Services Employment and Reemployment Rights Act of 1994 ("USERRA"), Pub. L. No. 103–353, 38 U.S.C. §§4301, ff., which revised and restated the Federal law protecting veterans' reemployment rights, an employee who leaves a civilian job for qualified military service generally is entitled to be reemployed by the civilian employer if the individual returns to employment within a specified time period. In addition to reemployment rights, a returning veteran also is entitled to the restoration of certain pension, profit sharing and similar benefits that would have accrued, but for the employee's absence due to the qualified military service.

USERRA generally provides that for a reemployed veteran service in the uniformed services is considered service with the employer for retirement plan benefit accrual purposes, and the employer that reemploys the returning veteran is liable for funding any resulting obligation. USERRA also provides that the reemployed veteran is entitled to any accrued benefits that are contingent on the making of, or derived from, employee contributions or elective deferrals only to the extent the reemployed veteran makes payment to the plan with respect to such contributions or deferrals. No such payment may exceed the amount the reemployed veteran would have been permitted or required to contribute had the person remained continuously employed by the employer throughout the period of uniformed service. Under USERRA, any such payment to the plan must be made during the period beginning with the date of reemployment and whose duration is three times the reemployed veteran's period of uniform service, not to exceed five years.

Under the Internal Revenue Code, overall limits are provided on contributions and benefits under certain retirement plans. For example, the maximum amount of elective deferrals that can be made by an individual into a qualified cash or deferred arrangement in any taxable year is limited to $9,500 for 1996 (sec. 402(g)). Annual additions with respect to each participant under a qualified defined contribution plan generally are limited to the lesser of $30,000 (for 1996) or 25 percent of compensation (sec 415(c)). Annual deferrals with respect to each participant under an eligible deferred compensation plan (sec. 457) generally are limited to the lesser of

$7,500 or 33⅓ percent of includible compensation. There is no provision under present law that permits contributions or deferrals to exceed these and other annual limits in the case of contributions with respect to a reemployed veteran.

Other requirements for which there is no special provision for contributions with respect to a reemployed veteran include the limit on deductible contributions and the qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules.

Explanation of Provision

The bill provides special rules in the case of certain contributions ("make-up contributions") with respect to a reemployed veteran that are required or authorized under USERRA. The bill applies to contributions made by an employer or employee to an individual account plan or to contributions made by an employee to a defined benefit plan that provides for employee contributions.

Under the bill, if any make-up contribution is made by an employer or employee with respect to a reemployed veteran, then such contributions are not subject to the generally applicable plan contributions limits (i.e., secs. 402(g), 402(h), 403(b), 408, 415, or 457) or the limit on deductible contributions (i.e., secs. 404(a) or 404(h)) as applied with respect to the year in which the contribution is made. In addition, the make-up contribution are not taken into account in applying the plan contribution or deductible contribution limits to any other contribution made during the year. However, the amount of any make-up contribution could not exceed the aggregate amount of contributions that would have been permitted under the plan contribution and deductible contribution limits for the year to which the contribution relates had the individual continued to be employed by the employer during the period of uniformed service.

Under the bill, a plan to which a make-up contribution is made on account of a reemployed veteran is not treated as failing to meet the qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules (i.e., secs. 401(a)(4), 401(a)(26), 401(k)(3), 401(k)(11), 401(k)(12), 401(m), 403(b)(12), 408(k)(3), 408(k)(6), 408(p), 410(b), or 416) by reason of the making of such contribution. Consequently, for purposes of applying the requirements and tests associated with these rules, make-up contributions are not taken into account either for the year in which they are made or for the year to which they relate.

Under the bill, a special rule applies in the case of make-up contributions of salary reduction, employer matching, and after-tax employee amounts. A plan that provides for elective deferrals or employee contributions is treated as meeting the requirements of USERRA if the employer permits reemployed veterans to make additional elective deferrals or employee contributions under the plan during the period which begins on the date of reemployment and has the same length as the lesser of (1) the period of the individual's absence due to uniformed service multiplied by three or (2) five years.

The employer is required to match any additional elective deferrals or employee contributions at the same rate that would have

been required had the deferrals or contributions actually been made during the period of uniformed service. Additional elective deferrals, employer matching contributions, and employee contributions is treated as make-up contributions for purposes of the rule exempting such contributions from qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules as described above.

The bill clarifies that USERRA does not require (1) any earnings to be credited to an employee with respect to any contribution before such contribution is actually made or (2) any make-up allocation of any forfeiture that occurred during the period of uniformed service.

The bill also provides that the plan loan, plan qualification, and prohibited transaction rules will not be violated merely because a plan suspends the repayment of a plan loan during a period of uniformed service.

The bill also defines compensation to be used for purposes of determining make-up contributions and would conform the rules contained in the Code with certain rights of reemployed veterans contained in USERRA pertaining to employee benefit plans.

The provision is effective as of December 12, 1994, the effective date of the benefits-related provisions of USERRA.

20. Reporting of real estate transactions (sec. 1704(p) of the bill and sec. 6045(e)(3) of the Code)

Present Law

It is unlawful for any real estate reporting person to charge separately any customer for complying with the information reporting requirements with respect to real estate transactions.

Explanation of Provision

The bill clarifies that real estate reporting persons may take into account the cost of complying with the reporting requirements of Code section 6045 in establishing charges for their services, so long as a separately listed charge for such costs is not made.

The provision is effective on November 11, 1988 (as if originally enacted as part of the amendment to the Code relating to separate charges).

21. Clarification of denial of deductions for stock redemption expenses (sec. 1704(q) of the bill and sec. 162(k)(2) of the Code)

Present Law

Section 162(k), added by the Tax Reform Act of 1986, denies a deduction for any amount paid or incurred by a corporation in connection with the redemption of its stock. An exception is provided for any deduction allowable under section 163 (relating to interest). The Internal Revenue Service has taken the position that costs properly allocable to a borrowing the interest on which is deductible under the exception may not be amortized over the period of

$7,500 or 33⅓ percent of includible compensation. There is no provision under present law that permits contributions or deferrals to exceed these and other annual limits in the case of contributions with respect to a reemployed veteran.

Other requirements for which there is no special provision for contributions with respect to a reemployed veteran include the limit on deductible contributions and the qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules.

Explanation of Provision

The bill provides special rules in the case of certain contributions ("make-up contributions") with respect to a reemployed veteran that are required or authorized under USERRA. The bill applies to contributions made by an employer or employee to an individual account plan or to contributions made by an employee to a defined benefit plan that provides for employee contributions.

Under the bill, if any make-up contribution is made by an employer or employee with respect to a reemployed veteran, then such contributions are not subject to the generally applicable plan contributions limits (i.e., secs. 402(g), 402(h), 403(b), 408, 415, or 457) or the limit on deductible contributions (i.e., secs. 404(a) or 404(h)) as applied with respect to the year in which the contribution is made. In addition, the make-up contribution are not taken into account in applying the plan contribution or deductible contribution limits to any other contribution made during the year. However, the amount of any make-up contribution could not exceed the aggregate amount of contributions that would have been permitted under the plan contribution and deductible contribution limits for the year to which the contribution relates had the individual continued to be employed by the employer during the period of uniformed service.

Under the bill, a plan to which a make-up contribution is made on account of a reemployed veteran is not treated as failing to meet the qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules (i.e., secs. 401(a)(4), 401(a)(26), 401(k)(3), 401(k)(11), 401(k)(12), 401(m), 403(b)(12), 408(k)(3), 408(k)(6), 408(p), 410(b), or 416) by reason of the making of such contribution. Consequently, for purposes of applying the requirements and tests associated with these rules, make-up contributions are not taken into account either for the year in which they are made or for the year to which they relate.

Under the bill, a special rule applies in the case of make-up contributions of salary reduction, employer matching, and after-tax employee amounts. A plan that provides for elective deferrals or employee contributions is treated as meeting the requirements of USERRA if the employer permits reemployed veterans to make additional elective deferrals or employee contributions under the plan during the period which begins on the date of reemployment and has the same length as the lesser of (1) the period of the individual's absence due to uniformed service multiplied by three or (2) five years.

The employer is required to match any additional elective deferrals or employee contributions at the same rate that would have

been required had the deferrals or contributions actually been made during the period of uniformed service. Additional elective deferrals, employer matching contributions, and employee contributions is treated as make-up contributions for purposes of the rule exempting such contributions from qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules as described above.

The bill clarifies that USERRA does not require (1) any earnings to be credited to an employee with respect to any contribution before such contribution is actually made or (2) any make-up allocation of any forfeiture that occurred during the period of uniformed service.

The bill also provides that the plan loan, plan qualification, and prohibited transaction rules will not be violated merely because a plan suspends the repayment of a plan loan during a period of uniformed service.

The bill also defines compensation to be used for purposes of determining make-up contributions and would conform the rules contained in the Code with certain rights of reemployed veterans contained in USERRA pertaining to employee benefit plans.

The provision is effective as of December 12, 1994, the effective date of the benefits-related provisions of USERRA.

20. Reporting of real estate transactions (sec. 1704(p) of the bill and sec. 6045(e)(3) of the Code)

Present Law

It is unlawful for any real estate reporting person to charge separately any customer for complying with the information reporting requirements with respect to real estate transactions.

Explanation of Provision

The bill clarifies that real estate reporting persons may take into account the cost of complying with the reporting requirements of Code section 6045 in establishing charges for their services, so long as a separately listed charge for such costs is not made.

The provision is effective on November 11, 1988 (as if originally enacted as part of the amendment to the Code relating to separate charges).

21. Clarification of denial of deductions for stock redemption expenses (sec. 1704(q) of the bill and sec. 162(k)(2) of the Code)

Present Law

Section 162(k), added by the Tax Reform Act of 1986, denies a deduction for any amount paid or incurred by a corporation in connection with the redemption of its stock. An exception is provided for any deduction allowable under section 163 (relating to interest). The Internal Revenue Service has taken the position that costs properly allocable to a borrowing the interest on which is deductible under the exception may not be amortized over the period of

the loan, due to section 162(k). Different courts have reached differing conclusions when taxpayers have litigated the question. [40]

Explanation of Provision

The bill clarifies that amounts properly allocable to indebtedness on which interest is deductible and properly amortized over the term of that indebtedness are not subject to the provision of section 162(k) denying a deduction for any amount paid or incurred by a corporation in connection with the redemption of its stock.

In addition, the bill clarifies that the rules of section 162(k) apply to any acquisition of its stock by a corporation or by a party that has a relationship to the corporation described in section 465(b)(3)(C) (which applies a more than 10 percent relationship test in certain cases).

Thus, for example, it is clarified that the denial of a deduction applies to any reacquisition (i.e., any transaction that is in effect an acquisition of previously outstanding stock) regardless of whether the transaction is treated as a redemption for purposes of subchapter C of the Code, regardless of whether it is treated for tax purposes as a sale of the stock or as a dividend, and regardless of whether the transaction is a reorganization or other transaction.

Apart from the clarification relating to amounts properly allocable to indebtedness, it is not intended that application of the 1986 Act deduction denial to any amount or transaction be limited under the bill.

The provision clarifying that amounts properly allocable to indebtedness and amortized over the term of that indebtedness are not subject to the denial under section 162(k), is effective as if included in the Tax Reform Act of 1986.

The other clarifications apply to amounts paid or incurred after September 13, 1995. No inference is intended that any amounts described in these other clarifications are deductible under present law.

22. Definition of passive income in determining passive foreign investment company status (sec. 1704(s) of the bill, sec. 1235 of the 1986 Act and sec. 1296(b)(2) of the Code)

Present Law

Under the export trade corporation (ETC) provisions, a controlled foreign corporation (CFC) that qualifies as an ETC is not subject to current U.S. tax on certain export trade income. In 1971, the ETC provisions were replaced by rules applicable to domestic international sales corporations (DISCs). Only those ETCs in existence at that time are allowed to continue operating as ETCs. In 1984, the DISC provisions were largely replaced by the rules applicable to foreign sales corporations (FSCs). Certain foreign trade income of a FSC is exempt from U.S. income tax. In addition, a domestic corporation is allowed a 100-percent dividends-received deduction for dividends distributed from the FSC out of earnings attributable to certain foreign trade income.

[40] See e.g., *Fort Howard Corp.* v. *Commissioner*, 103 T.C. 345 (1994)(upholding the IRS position); compare *U.S.* v. *Kroy (Europe) Limited*, 27 F.3d 367 (9th Cir. 1994)(to the contrary).

The Tax Reform Act of 1986 established an anti-deferral regime for passive foreign investment companies (PFICs). A foreign corporation is a PFIC if (1) 75 percent or more of its gross income for the taxable year consists of passive income, or (2) 50 percent or more of the average amount of its assets consists of assets that produce, or are held for the production of passive income. Passive income for this purpose generally means income that satisfies the definition of foreign personal holding company income under subpart F. Foreign personal holding company income generally includes interest, dividends, and annuities; certain rents and royalties; related party factoring income; net commodities gains; net foreign currency gains; and net gains from sales or exchanges of certain other property. In determining whether a foreign corporation is a PFIC, passive income does not include certain active-business banking, insurance, or (in the case of the U.S. shareholders of a CFC) securities income, or certain amounts received from a related party (to the extent that the amounts are allocable to income of the related party which is not passive income).

Explanation of Provision

The bill clarifies that foreign trade income of a FSC and export trade income of an ETC do not constitute passive income for purposes of the PFIC definition.

The provision is effective as if it were included in the Tax Reform Act of 1986.

23. Exclusion from income for combat zone compensation (sec. 1704(t)(4) of the bill and sec. 112 of the Code)

Present Law

The Code provides that gross income does not include compensation received by a taxpayer for active service in the Armed Forces of the United States for any month during any part of which the taxpayer served in a combat zone (or was hospitalized as a result of injuries, wounds or disease incurred while serving in a combat zone) (limited to $500 per month for commissioned officers). The heading refers to "combat pay," although that term is no longer used to refer to special pay provisions for members of the Armed Forces, nor is the exclusion limited to those special pay provisions (hazardous duty pay (37 U.S.C. sec. 301) and hostile fire or imminent danger pay (37 U.S.C. sec. 310)).

Explanation of Provision

The bill modifies the heading of Code section 112 to refer to "combat zone compensation" instead of "combat pay." The bill also makes conforming changes to cross-references elsewhere in the Code. This provision is effective on the date of enactment.

24. Certain property not treated as section 179 property (sec. 1704(u) of the bill and sec. 179 of the Code)

Present Law

Section 179 allows a qualified taxpayer (generally, a small business) to elect to expense and deduct, rather than capitalize and depreciate, a limited amount of the cost of property placed in service in the taxpayer's trade or business.

One of the "deadwood provisions" of the Omnibus Budget Reconciliation Act of 1990 ("1990 Act") inadvertently expanded the scope of section 179 to include property described in section 50(b), air conditioning or heating units, and horses. According to legislative history, these 1990 Act provisions were "an attempt to simplify the Code by deleting 'deadwood,' without making substantive changes in the tax law."

Explanation of Provision

The bill restores pre-1990 law to deny the expensing allowance for the following property placed in service after May 14, 1996: (1) property described in section 50(b) (generally, property used outside the U.S., property used in connection with furnishing lodging, property used by tax-exempt organizations, and property used by governments and foreign persons); (2) air conditioning or heating units; and (3) horses.

III. VOTES OF THE COMMITTEE

In compliance with clause 2(l)(2)(B) of rule XI of the Rules of the House of Representatives, the following statement is made concerning the roll call votes of the Committee in its consideration of the bill.

Motion to report the bill

The bill, H.R. 3448, as amended, was ordered favorably reported on May 14, 1996, by a roll call vote of 33 yeas and 3 nays, with a quorum present. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer	X			Mr. Gibbons	X		
Mr. Crane	X			Mr. Rangel		X	
Mr. Thomas	X			Mr. Stark		X	
Mr. Shaw	X			Mr. Jacobs	X		
Mrs. Johnson	X			Mr. Ford	X		
Mr. Bunning	X			Mr. Matsui		X	
Mr. Houghton	X			Mrs. Kennelly	X		
Mr. Herger	X			Mr. Coyne	X		
Mr. McCrery	X			Mr. Levin	X		
Mr. Hancock	X			Mr. Cardin	X		
Mr. Camp	X			Mr. McDermott	X		
Mr. Ramstad	X			Mr. Kleczka	X		
Mr. Zimmer				Mr. Lewis	X		
Mr. Nussle	X			Mr. Payne	X		
Mr. Johnson	X			Mr. Neal	X		
Ms. Dunn	X			Mr. McNulty	X		
Mr. Collins	X						
Mr. Portman	X						
Mr. Hayes							
Mr. Laughlin							

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. English	X						
Mr. Ensign	X						
Mr. Christensen	X						

Votes on amendments

An amendment by Messrs. Levin and Ramstad to the Archer amendment in the nature of a substitute to strike section 1602, which would repeal the exclusion for interest on loans used to acquire employer securities, and add in subtitle F of Title I provisions regarding foreign trust tax compliance, was defeated by a roll call vote of 14 yeas to 17 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer		X		Mr. Gibbons			
Mr. Crane		X		Mr. Rangel	X		
Mr. Thomas		X		Mr. Stark	X		
Mr. Shaw		X		Mr. Jacobs			
Mrs. Johnson		X		Mr. Ford			
Mr. Bunning		X		Mr. Matsui	X		
Mr. Houghton				Mrs. Kennelly	X		
Mr. Herger		X		Mr. Coyne	X		
Mr. McCrery		X		Mr. Levin	X		
Mr. Hancock		X		Mr. Cardin	X		
Mr. Camp		X		Mr. McDermott	X		
Mr. Ramstad	X			Mr. Kleczka	X		
Mr. Zimmer				Mr. Lewis			
Mr. Nussle		X		Mr. Payne	X		
Mr. Johnson	X			Mr. Neal	X		
Ms. Dunn		X		Mr. McNulty	X		
Mr. Collins		X					
Mr. Portman		X					
Mr. Hayes							
Mr. Laughlin							
Mr. English		X					
Mr. Ensign		X					
Mr. Christensen		X					

An amendment by Mr. Matsui to the Archer amendment in the nature of a substitute to add at the end of Subtitle A of Title I a new section to extend and modify the research credit, and add at the end of Subtitle F a new section on the temporary restoration of airport and airway trust fund taxes, was defeated by a roll call vote of 14 yeas to 19 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer		X		Mr. Gibbons			
Mr. Crane		X		Mr. Rangel	X		
Mr. Thomas		X		Mr. Stark		X	
Mr. Shaw		X		Mr. Jacobs			
Mrs. Johnson	X			Mr. Ford			
Mr. Bunning		X		Mr. Matsui	X		
Mr. Houghton		X		Mrs. Kennelly	X		
Mr. Herger		X		Mr. Coyne	X		
Mr. McCrery		X		Mr. Levin	X		
Mr. Hancock		X		Mr. Cardin	X		
Mr. Camp		X		Mr. McDermott	X		
Mr. Ramstad		X		Mr. Kleczka	X		
Mr. Zimmer				Mr. Lewis	X		
Mr. Nussle		X		Mr. Payne	X		
Mr. Johnson		X		Mr. Neal	X		

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Ms. Dunn		X		Mr. McNulty	X		
Mr. Collins		X					
Mr. Portman		X					
Mr. Hayes							
Mr. Laughlin							
Mr. English	X						
Mr. Ensign		X					
Mr. Christensen		X					

An amendment by Mr. McDermott to the Archer amendment in the nature of a substitute to add at the end of Chapter 4 of Subtitle D a new section to provide that distributions from certain plans may be used without penalty during periods of unemployment, and add at the end of Subtitle F of Title I a new section on the temporary restoration of airport and airway trust fund taxes, was defeated by a roll call vote of 14 yeas to 19 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer		X		Mr. Gibbons			
Mr. Crane		X		Mr. Rangel	X		
Mr. Thomas		X		Mr. Stark	X		
Mr. Shaw		X		Mr. Jacobs			
Mrs. Johnson		X		Mr. Ford			
Mr. Bunning		X		Mr. Matsui	X		
Mr. Houghton		X		Mrs. Kennelly	X		
Mr. Herger		X		Mr. Coyne	X		
Mr. McCrery		X		Mr. Levin	X		
Mr. Hancock		X		Mr. Cardin	X		
Mr. Camp		X		Mr. McDermott	X		
Mr. Ramstad		X		Mr. Kleczka	X		
Mr. Zimmer				Mr. Lewis	X		
Mr. Nussle		X		Mr. Payne	X		
Mr. Johnson		X		Mr. Neal	X		
Ms. Dunn		X		Mr. McNulty	X		
Mr. Collins		X					
Mr. Portman		X					
Mr. Hayes							
Mr. Laughlin							
Mr. English	X						
Mr. Ensign		X					
Mr. Christensen		X					

An amendment by Mr. Neal to the Archer amendment in the nature of a substitute to add at the end of Subtitle A of Title I a new section for the deduction for higher education expenses, and at the end of Subtitle F of Title I a new section on the temporary restoration of airport and airway trust fund taxes, was defeated by a roll call vote of 13 yeas to 20 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer		X		Mr. Gibbons			
Mr. Crane		X		Mr. Rangel	X		
Mr. Thomas		X		Mr. Stark	X		
Mr. Shaw		X		Mr. Jacobs			
Mrs. Johnson		X		Mr. Ford			
Mr. Bunning		X		Mr. Matsui	X		
Mr. Houghton		X		Mrs. Kennelly	X		
Mr. Herger		X		Mr. Coyne	X		
Mr. McCrery		X		Mr. Levin	X		
Mr. Hancock		X		Mr. Cardin	X		

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Camp		X		Mr. McDermott	X		
Mr. Ramstad		X		Mr. Kleczka	X		
Mr. Zimmer				Mr. Lewis	X		
Mr. Nussle		X		Mr. Payne	X		
Mr. Johnson		X		Mr. Neal	X		
Ms. Dunn		X		Mr. McNulty	X		
Mr. Collins		X					
Mr. Portman		X					
Mr. Hayes							
Mr. Laughlin							
Mr. English		X					
Mr. Ensign		X					
Mr. Christensen		X					

An amendment by Mr. Levin to the Archer amendment in the nature of a substitute to strike subsections (b) and (c)(2) of section 1202 (relating to limitation to education below graduate level), and insert at the end of Subtitle F a new section on expansion of the requirement that involuntarily converted property be replaced with property acquired from an unrelated person, and a new section on financial asset securitization investment trusts, was agreed to by a roll call vote of 18 yeas to 15 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer		X		Mr. Gibbons			
Mr. Crane		X		Mr. Rangel	X		
Mr. Thomas		X		Mr. Stark	X		
Mr. Shaw	X			Mr. Jacobs	X		
Mrs. Johnson		X		Mr. Ford			
Mr. Bunning		X		Mr. Matsui	X		
Mr. Houghton	X			Mrs. Kennelly	X		
Mr. Herger		X		Mr. Coyne			
Mr. McCrery		X		Mr. Levin	X		
Mr. Hancock		X		Mr. Cardin	X		
Mr. Camp	X			Mr. McDermott	X		
Mr. Ramstad	X			Mr. Kleczka	X		
Mr. Zimmer				Mr. Lewis	X		
Mr. Nussle		X		Mr. Payne	X		
Mr. Johnson		X		Mr. Neal	X		
Ms. Dunn		X		Mr. McNulty	X		
Mr. Collins		X					
Mr. Portman		X					
Mr. Hayes							
Mr. Laughlin							
Mr. English		X					
Mr. Ensign	X						
Mr. Christensen		X					

An amendment by Mr. Kleczka to the Archer amendment in the nature of a substitute to strike subsection (a)(2) of section 1112 (relating to the effective date of the employer tax credit for FICA taxes paid on tip income) was defeated by a roll call vote of 13 yeas to 20 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer		X		Mr. Gibbons			
Mr. Crane		X		Mr. Rangel	X		
Mr. Thomas		X		Mr. Stark	X		
Mr. Shaw		X		Mr. Jacobs	X		
Mrs. Johnson		X		Mr. Ford			
Mr. Bunning		X		Mr. Matsui	X		

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Houghton		X		Mrs. Kennelly	X		
Mr. Herger		X		Mr. Coyne			
Mr. McCrery		X		Mr. Levin	X		
Mr. Hancock		X		Mr. Cardin	X		
Mr. Camp		X		Mr. McDermott	X		
Mr. Ramstad		X		Mr. Kleczka	X		
Mr. Zimmer				Mr. Lewis	X		
Mr. Nussle		X		Mr. Payne	X		
Mr. Johnson		X		Mr. Neal	X		
Ms. Dunn		X		Mr. McNulty	X		
Mr. Collins		X					
Mr. Portman		X					
Mr. Hayes							
Mr. Laughlin							
Mr. English		X					
Mr. Ensign		X					
Mr. Christensen		X					

Reconsideration of an amendment by Mr. Levin to the Archer amendment in the nature of a substitute to strike subsections (b) and (c)(2) of section 1202 (relating to limitation to education below graduate level), and insert at the end of Subtitle F a new section on expansion of the requirement that involuntarily converted property be replaced with property acquired from an unrelated person, and a new section on financial asset securitization investment trusts, was defeated by a roll call vote of 16 yeas to 20 nays. The vote was as follows:

Representatives	Yea	Nay	Present	Representatives	Yea	Nay	Present
Mr. Archer		X		Mr. Gibbons			
Mr. Crane		X		Mr. Rangel	X		
Mr. Thomas		X		Mr. Stark	X		
Mr. Shaw		X		Mr. Jacobs	X		
Mrs. Johnson		X		Mr. Ford	X		
Mr. Bunning		X		Mr. Matsui	X		
Mr. Houghton		X		Mrs. Kennelly	X		
Mr. Herger		X		Mr. Coyne	X		
Mr. McCrery		X		Mr. Levin	X		
Mr. Hancock		X		Mr. Cardin	X		
Mr. Camp		X		Mr. McDermott	X		
Mr. Ramstad		X		Mr. Kleczka	X		
Mr. Zimmer				Mr. Lewis	X		
Mr. Nussle		X		Mr. Payne	X		
Mr. Johnson		X		Mr. Neal	X		
Ms. Dunn		X		Mr. McNulty	X		
Mr. Collins		X					
Mr. Portman		X					
Mr. Hayes							
Mr. Laughlin							
Mr. English		X					
Mr. Ensign		X					
Mr. Christensen		X					

IV. BUDGET EFFECTS OF THE BILL

A. Committee Estimates of Budgetary Effects

In compliance with clause 7(a) of rule XIII of the Rules of the House of Representatives, the following statement is made concerning the budget effects of the bill, H.R. 3448, as reported.

The bill is estimated to have the following effects on the budget for fiscal years 1996–2003:

Estimated Budget Effects of H.R. 3448, the "Small Business Job Protection Act of 1996," As Approved by the Committee on Ways and Means

[Fiscal Years 1996–2003, in millions of dollars]

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	1996–2000	1996–2003
I. Small Business Provisions:											
1. Increase in expensing limitations for small businesses to $18,500 for 1996, $19,000 for 1997, $20,000 for 1998, $21,000 for 1999, $22,000 for 2000, $23,000 for 2001, $23,500 for 2002, $25,000 for 2003 and thereafter	tyba 12/31/95	−129	−311	−337	−479	−581	−590	−547	−625	−1,837	−3,599
2. FICA tip credit:											
a. Provided for off-premises employees	1/1/97	.....	−6	−14	−15	−16	−17	−18	−18	−51	−104
b. Clarification	.....				***Negligible Revenue Effect***						
3. Treatment of storage of product samples	tyba 12/31/95	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	−2
4. Provide that certain charitable risk pools would qualify as charitable organizations under section 501(c)(3)	tyba DOE	.....	(1)	−1	−1	−1	−1	−2	−2	−3	−8
5. Treatment of certain dues paid to agricultural or horticultural organizations	tyba 12/31/94				***Negligible Revenue Effect***						
6. Fishermen—treat "pers" payments as wages rather than self-employment income	.....	−1	−10	(1)	(1)	(1)	(1)	(1)	(1)	−11	−12
7. Require purchasers of fish in excess of $600 in cash to provide information reports	12/31/96	.....	5	9	9	10	10	11	11	33	65
Subtotal of Small Business Provisions	.....	**−130**	**−322**	**−343**	**−486**	**−588**	**−598**	**−556**	**−634**	**−1,869**	**−3,657**
II. Extension of Certain Expiring Provisions:											
1. Extend the work opportunity tax credit, with modifications through 6/30/97 [2]	7/1/96	−33	−90	−91	−48	−19	−6	−1	.....	−281	−288
2. Employer-provided educational assistance; applies to undergraduate education only after 1995; sunset after 12/31/96	1/1/95	−136	−608	.....	.....	.....	.....	.....	.....	−744	−744
3. Permanent extension of FUTA exemption for alien agricultural workers [3]	1/1/95	−5	−3	−3	−3	−3	−3	−3	−3	−17	−26
Subtotal of Expiring Provisions	.....	**−174**	**−701**	**−94**	**−51**	**−22**	**−9**	**−4**	**−3**	**−1,042**	**−1,058**
III. Provisions Relating to S Corporations:											
1. Increase number of eligible shareholders	tyba 12/31/96	.....	−5	−14	−16	−20	−22	−25	−28	−55	−130
2. Permit certain trusts to hold stock in S corporations	tyba 12/31/96	.....	−2	−2	−2	−2	−2	−2	−2	−8	−14
3. Extend holding period for certain trusts	tyba 12/31/96	.....	(4)	(4)	(4)	(4)	(4)	(4)	(4)	(5)	(6)

4. Financial institutions permitted to hold safe-harbor debt	tyba 12/31/96		(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	−1
5. Authority to validate certain invalid elections	tyba 12/31/82		(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	−1
6. Allow interim closing of the books	tyba 12/31/96					***Negligible Revenue Effect***					
7. Expand post-termination period and amend subchapter S audit procedures	tyba 12/31/96		(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	−1
8. S corporations permitted to hold S or C subsidiaries	tyba 12/31/96		−5	−9	−11	−13	−15	−17	−20	−38	−90
9. Treatment of distributions during loss years	tyba 12/31/96		(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	−1
10. Treatment of S corporations as shareholders in C corporations	tyba 12/31/96		(4)	(4)	(4)	(4)	(4)	(4)	(4)	(5)	(6)
11. Elimination of certain earnings and profits of S corporations	tyba 12/31/96		(4)	(4)	(4)	(4)	(4)	(4)	(4)	(5)	(6)
12. Treatment of certain losses carried over under at-risk rules	tyba 12/31/96		(4)	(4)	(4)	(4)	(4)	(4)	(4)	(5)	(6)
13. Adjustments to basis of inherited S stock	dda DOE		(7)	(7)	(7)	(7)	(7)	(7)	(7)	(7)	(7)
14. Treatment of certain real estate held by an S corporation	tyba 12/31/96		−1	−1	−2	−2	−2	−2	−2	−6	−12
15. Transition rule for elections after termination	tyba 12/31/96		(4)	(4)	(4)	(4)	(4)	(4)	(4)	(5)	(6)
Subtotal of Subchapter S Corporations Provisions			**−3**	**−31**	**−67**	**−78**	**−89**	**−94**	**−100**	**−107**	**−268**	**−569**
IV. Pension Simplification Provisions:											
A. Simplified Distribution Rules:											
1. Repeal of 5-year income averaging for lump-sum distributions	tyba 12/31/98		67	63	94	65	56	32	17	289	394
2. Repeal of $5,000 exclusion of employees' death benefits	dda DOE		28	49	52	54	55	55	56	183	349
3. Simplified method fo. taxing annuity distributions under certain employer plans	asda 90 da DOE		22	28	28	29	29	29	30	107	195
4. Minimum required distributions	yba 12/31/96		−1	−4	−4	−4	−4	−4	−4	−13	−25
B. Increased Access to Pension Plans:											
1. Establish SIMPLE pension plan, but repeal salary reduction SEPs	yba 12/31/96		−53	−81	−84	−87	−90	−93	−97	−305	−585
2. Tax-exempt organization eligible under section 401(k)	yba 12/31/96		−8	−22	−24	−25	−26	−28	−29	−79	−162
C. Nondiscrimination Provisions:											
1. Simplified definition of highly compensated employees [8]	yba 12/31/96		(9)	(9)		***Considered in Other Provisions***					
2. Repeal of family aggregation rules[8]	yba 12/31/96		(10)	(10)		***Considered in Other Provisions***					
3. Modification of additional participation requirements	yba 12/31/96										
4. Safe-harbor nondiscrimination rules for qualified cash or deferred arrangements and matching contributions [11]	yba 12/31/98				−42	−162	−167	−171	−176	−204	−718
5. Definition of compensation for section 415 purposes	yba 12/31/97			−1	−1	−2	−2	−2	−2	−4	−10
D. Miscellaneous Provision:											
1. Plans covering self-employed individuals	yba 12/31/96										
2. Elimination of special vesting rule for multiemployer plans	yba 12/31/96		(1)	−1	−1	−1	−1	−1	−1	−3	−4
3. Distributions under rural cooperative plans	DOE										
4. Treatment of governmental plans under section 415	yba 12/31/94										
5. Uniform retirement age[8]	yba 12/31/96		(10)	(10)		***Considered in Other Provisions***					

Estimated Budget Effects of H.R. 3448, the "Small Business Job Protection Act of 1996," As Approved by the Committee on Ways and Means—Continued

[Fiscal Years 1996–2003, in millions of dollars]

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	1996–2000	1996–2003
6. Contributions on behalf of disabled employees	yba 12/31/96	.....									
7. Treatment of deferred compensation plans of State and local governments and tax-exempt organizations	tyba 12/31/96	.....	(1)	−1	−1	−1	−2	−2	−2	−3	−9
8. Require individual ownership of section 457 plan assets	DOE	.....	−7	−21	−24	−25	−25	−26	−27	−77	−155
9. Correction of GATT interest and mortality rate provisions in the Retirement Protection Act permanent change	eaii GATT	.....	−4	−4	−4	.....	.....	.....	.....	−12	−12
10. Multiple salary reduction agreements permitted under section 403(b)	tyba 12/31/95				*Negligible Revenue Effect*						
11. Application of elective deferred limit to section 403(b) plans	tyba 12/31/95				*Negligible Revenue Effect*						
12. Treatment of Indian tribal governments under section 403(b)	pybb 1/1/95				*Negligible Revenue Effect*						
13. Repeal of combined plan limit	lyba 12/31/98	.....	.....	.....	−70	−189	−195	−201	−207	−259	−862
14. 3-year waiver of excess distribution tax	1/1/96	.....	49	43	3	.....	.....	.....	.....	95	95
15. Increase section 4975 excise tax on prohibited transactions from 5% to 10%	ptoa DOE	.....	2	4	4	4	4	4	4	14	26
16. Modify notice required of right to qualified joint and survivor annuity	pyba 12/31/96				*Negligible Revenue Effect*						
17. Treatment of leased employees	yba 12/31/96				*Negligible Revenue Effect*						
18. Uniform penalty provision to apply to certain pension reporting requirements	1/1/97				*No Revenue Effect*						
19. Clarify that SECA does not apply to certain parsonage allowance income	ybbo/a 12/31/94				*Negligible Revenue Effect*						
20. Date of adoption of plan amendments	DOE				*No Revenue Effect*						
Subtotal of Pension Simplification Provisions	.....	.....	**90**	**47**	**−74**	**−344**	**−368**	**−408**	**−438**	**−281**	**−1,495**
V. Foreign Simplification—Repeal of excess passive assets provision (section 956A)	**tyba 12/31/96**	.....	**−11**	**−22**	**−29**	**−36**	**−41**	**−45**	**−51**	**−98**	**−235**
VI. Revenue Offsets:											
1. Possessions tax credit: Wage credit companies—6 years of present law, followed by 4-year phaseout with modified base period; Income companies—2 years of present law followed by 8-year phaseout with modified base period; QPSII—repealed 1/1/96	tyba 12/31/95	255	605	552	596	498	516	746	1,116	2,506	4,884

2. Repeal 50 % interest income exclusion for financial institution loans to ESOPs	lma 10/13/95	12	68	108	148	186	223	260	295	521	1,299
3. Apply look-through rule for purposes of characterizing certain subpart F insurance income as UBTI	gira 12/31/95	7	23	24	27	30	32	34	37	111	214
4. Corporate accounting—reform of income forecast method	ppisa 9/13/95	32	69	29	13	14	16	19	22	157	214
5. Modify exclusion of damages received on account of personal injury or sickness	ara 6/30/96	5	50	55	59	61	64	68	71	230	433
6. Repeal advance refunds of diesel fuel tax for diesel cars and light trucks	vpa DOE	3	17	19	19	19	19	19	19	76	133
Subtotal of Revenue Offsets		**314**	**832**	**787**	**862**	**808**	**870**	**1,146**	**1,560**	**3,601**	**7,177**
VII. Technical Corrections—Luxury excise tax, expensing modification, and other technical corrections		**14**	**(1)**	**(1)**	**(1)**	**(1)**	**(1)**	**(1)**	**(1)**	**13**	**13**
Net Total		**21**	**−143**	**308**	**144**	**−271**	**−240**	**33**	**327**	**56**	**176**

[1] Loss of less than $500,000.
[2] Credit rate at 35% on first $6,000 of income; eligible workers expanded to include welfare cash recipients and veterans foodstamp recipients; 500 hour work requirement.
[3] Estimates provided by the Congressional Budget Office (CBO).
[4] Loss of less than $5 million.
[5] Loss of less than $15 million.
[6] Loss of less than $20 million.
[7] Gain of less than $1 million.
[8] Revenue effect after 1/1/99 included in the revenue estimate for the safe harbor provision due to interactions between this provision and item II.C.4.
[9] Loss of less than $10 million.
[10] Negligible revenue effect.
[11] This provision considers interaction effects of SIMPLE retirement plan provisions (items IV.C.1,IV.C.2, and IV.D.5).

Legend for "Effective" column: ara=amounts received after; asda=annuity starting date after; dda=decedents dying after; DOE=data of enactment; eali GATT=effective as if included in GATT; gira=gross income received in taxable years beginning after; lma=loans made after; lyba=limitation years beginning after; ppisa=property placed in service after; ptoa=prohibited transactions occurring after; pyba=plan years beginning after; pybb=plan years beginning before; tyba=taxable years beginning after; vpa DOE=vehicles purchased after date of enactment; yba=years beginning after; ybbo/a=years beginning before, on, or after; 90 da DOE=90 days after date of enactment.

Note.—Details may not add to totals due to rounding.

Source: Joint Committee on Taxation.

B. Statement Regarding New Budget Authority and Tax Expenditures

Budget authority

In compliance with subdivision (B) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, the Committee states that the provisions of the bill involve no new or increased budget authority.

Tax expenditures

In compliance with subdivision (B) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, the Committee states that the provisions involving income tax reductions generally involve increased tax expenditures and that the provisions involving increased income as revenues (see revenue table above) generally involve reduced tax expenditures. Non-income tax provisions are not classified as tax expenditures under the Budget Act. Also, certain reporting and other compliance provisions and technical corrections provisions do not involve tax expenditures.

C. Cost Estimate Prepared by the Congressional Budget Office

In compliance with subdivisions (c) of clause 2(l)(3) of rule XI of the Rules of the House of Representatives, requiring a cost estimate prepared by the Congressional Budget Office (CBO), the following statement by CBO is provided.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, May 20, 1996.

Hon. BILL ARCHER,
Chairman, Committee on Ways and Means,
House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office and the Joint Committee on Taxation (JCT) have reviewed H.R. 3448, the "Small Business Job Protection Act of 1996," as ordered reported by the House Committee on Ways and Means on May 14, 1996. The JCT estimates that this bill would increase governmental receipts by $21 million in fiscal year 1996 and by $171 million over fiscal years 1996 through 2003. CBO concurs with this estimate.

H.R. 3448 would increase the expensing limitation for small businesses, extend certain expiring provisions, simplify pension and foreign asset provisions, modify the tax treatment of Subchapter S Corporations and make technical corrections. In addition, the bill would repeal the possessions tax credit and the 50 percent interest income exclusion for financial institution loans to ESOPs, and make other changes that would increase taxes on corporations and other businesses. The revenue effects of H.R. 3448 are summarized in the table below. Please refer to the enclosed table for a more detailed estimate of the bill.

Revene Effects of H.R. 3448

[By fiscal year, in billions of dollars]

	1996	1997	1998	1999	2000	2001	2002	2003
Projected revenues under current law[1]	1,417.583	1,475.572	1,547.285	1,619.979	1,699.866	1,789.771	1,882.950	1,984.272
Proposed changes	0.021	−0.143	0.308	0.144	−0.271	−0.240	0.033	0.327
Projected revenues under H.R. 3448	1,417.604	1,475.429	1,547.593	1,620.123	1,699.595	1,789.531	1,882.983	1,984.599

[1] Includes the revenue effects of P.L. 104–7 (H.R. 831), P.L. 104–104 (S. 652), P.L. 104–117 (H.R. 2778), P.L. 104–121 (H.R. 3136), P.L. 104–132 (S. 735), and P.L. 104–134 (H.R. 3019).

In accordance with the requirements of Public Law 104–4, the Unfunded Mandates Reform Act of 1995, JCT has determined that the bill contains no intergovernmental mandates, but does contain several private sector mandates. These provisions would impose direct costs on the private sector of more than $100 million in each year from 1996–2000. The JCT estimates the direct mandate cost of tax increases in H.R. 3448 would total $314 million in 1996, and about $4.215 billion over the 1996–2000 period, as shown below:

Federal Private Sector Mandates

[By fiscal year, in millions of dollars]

	1996	1997	1998	1999	2000
Direct cost of tax increases	314	954	936	1,045	966

Please refer to the enclosed letter for a more detailed account of these provisions.

In addition to these mandates, the bill also provides for reductions in taxes. At this point, it is unclear to CBO whether these tax reductions should be viewed as offsets to the direct costs of the mandates in the bill. JCT estimates that the savings to the private sector associated with the tax reductions in H.R. 3448 would total $310 million in 1996, and about $4.477 billion over the 1996–2000 period, as shown below:

Federal Private Sector Savings

[By fiscal year, in millions of dollars]

	1996	1997	1998	1999	2000
Reductions in taxes	−310	−1,159	−722	−971	−1,315

Section 252 of the Balanced Budget and Emergency Deficit Control Act of 1985 sets up pay-as-you-go procedures for legislation affecting receipts or direct spending through 1998. Because the bill would affect receipts, pay-as-you-go procedures would apply to the bill. These effects are summarized in the table below.

Pay-as-You-Go Considerations

[By fiscal year, in millions of dollars]

	1996	1997	1998
Changes in receipts	21	−143	308
Changes in outlays	Not applicable		

If you wish further details, please feel free to contact me or your staff may wish to contact Stephanie Weiner.

Sincerely,

JAMES L. BLUM
(For June E. O'Neill, *Director*).

CONGRESS OF THE UNITED STATES,
JOINT COMMITTEE ON TAXATION,
Washington, DC, May 17, 1996.

Mrs. JUNE O'NEILL,
Director, Congressional Budget Office,
U.S. Congress, Washington, DC.

DEAR MRS. O'NEILL: We have reviewed H.R. 3448, the "Small Business Job Protection Act," as amended and ordered to be reported by the House Committee on Ways and Means on May 14, 1996. In accordance with the requirements of Public Law 104–4, the Unfunded Mandates Reform Act of 1995 (the "Unfunded Mandates Act"), we have determined that the following revenue provisions of the bill contain Federal private sector mandates: (1) the provision to repeal 5-year averaging for lump-sum distributions from qualified pension plans; (2) the provision to repeal the $5,000 exclusion for employee death benefits; (3) the provision that would provide a simplified method for taxing annuity distributions under qualified pension plans; (4) the provision relating to adjustments to basis of inherited S corporation stock; (5) the provision to phase out the section 936 credit; (6) the provision to repeal the 50 percent interest income exclusion for financial institution loans to ESOPs; (7) the provision to modify the exclusion of damages received on account of personal injury or sickness; (8) the provision to reform the income forecast method of accounting; (9) the provision to apply a look-through the rule for purposes of characterizing certain subpart F insurance income as unrelated business taxable income; (10) the provision to repeal advance refunds of diesel fuel tax for diesel cars and light trucks; and (11) the provision to lower the reporting threshold for purchasers of fish from $10,000 to $600. The attached revenue table (items I.7., III.13., IV.A. 1, 2, and 3, and VI. 1., 2., 3., 4., 5., and 6.) generally reflects amounts that are no greater than the aggregate estimated amounts that the private sector will be required to spend in order to comply with these Federal private sector mandates. [See Part IV.A of the report for a copy of the revenue table.]

The revenue provisions of the bill, as amended, contain no intergovernmental mandates.

If you would like to discuss this matter in further detail, please feel free to contact me at 225–3621. Thank you for your cooperation in this matter.

Sincerely,

KENNETH J. KIES, *Chief of Staff.*

V. OTHER MATTERS TO BE DISCUSSED UNDER RULES OF THE HOUSE

A. Committee Oversight Findings and Recommendations

With respect to subdivision (A) of clause 2(l)(3) of Rule XI of the Rules of the House of Representatives (relating to oversight findings), the Committee advises that it was the result of the Committee's oversight activities concerning the tax impact on small businesses and their workers, extension of certain expired tax provisions, tax treatment of subchapter S corporations, pension simplification, inclusion of certain earnings invested in excess passive assets, tax technical corrections, and certain revenue offsets necessary to make the bill budget neutral that the Committee concluded that it is appropriate and timely to enact the provisions contained in the bill as reported.

B. Summary of Findings and Recommendations of the Committee on Government Reform and Oversight

With respect to subdivision (D) of clause 2(l)(3) of Rule XI of the Rules of the House of Representatives, the Committee advises that no oversight findings or recommendations have been submitted to the Committee by the Committee on Government Reform and Oversight with respect to the provisions contained in the bill.

C. Inflationary Impact Statement

In compliance with clause 2(l)(4) of Rule XI of the Rules of the House of Representatives, the Committee states that the tax reductions benefiting small businesses and workers are offset by certain revenue increases over the fiscal year period 1996–2003, and therefore the bill will not add to the budget deficit. Thus, the bill will not have any inflationary impact on costs and prices in the overall national economy.

D. Information Relating to Unfunded Mandates

This information is provided in accordance with section 423 of the Unfunded Mandates Act of 1995 (P.L. 104–4).

The Committee has determined that the followings provisions of the bill contain Federal mandates on the private sector: (1) the provision to repeal 5-year averaging for lump-sum distributions from qualified pension plans; (2) the provision to repeal the $5,000 exclusion for employee death benefits; (3) the provision that would provide a simplified method for taxing annuity distributions under qualified pension plans; (4) the provision relating to adjustments to basis of inherited S corporation stock; (5) the provision to phase out the section 936 credit; (6) the provision to repeal the 50 percent interest income exclusion for financial institution loans to ESOPs; (7)

the provision to modify the exclusion of damages received on account of personal injury or sickness; (8) the provision to reform the income forecast method of accounting; (9) the provision to apply a look-through rule for purposes of characterizing certain subpart F insurance income as unrelated business taxable income; (10) the provision to repeal advance refunds of diesel fuel tax for diesel cars and light trucks; and (11) the provision to lower the reporting threshold for purchasers of fish from $10,000 to $600.

The cost required to comply with each mandate generally is no greater than the revenue estimate for the provision. Benefits from the provisions include improved administration of the Federal income tax laws, simplification for individual taxpayers, and a more accurate measurement of gross income for Federal income tax purposes. The Committee believes the benefits of the bill are greater than the costs required to comply with the Federal private sector mandates contained in the bill.

The provision to repeal five-year averaging for lump-sum distributions from qualified pension plans results in a better measurement of gross income for Federal income tax purposes and encourages taxpayers to take qualified pension plan distributions in a form other than a lump-sum distribution. The provision to repeal the $5,000 exclusion for employee death benefits results in a better measurement of gross income for Federal income tax purposes. The provision to provide a simplified method for taxing annuity distributions under qualified pension plans generally adopts an alternative method for taxing such distributions contained in Treasury regulations as the sole method for taxing such distributions and, thereby, simplifies the determination for individual taxpayers.

The provision relating to the adjustment to basis of inherited S corporation stock provides that a person acquiring stock in an S corporation from a decedent will treat as income in respect of a decedent ("IRD") his or her pro rata share of any item of income of the corporation that would have been IRD if that item had been acquired directly from the decedent, thereby improving the measurement of income for tax purposes.

The provision to phase out the section 936 credit with transition for companies that have existing operations in the possessions will result in the better measurement of gross income for Federal income tax purposes by eliminating a tax benefit enjoyed by only a small number of U.S. corporations operating in possessions.

The provision to repeal the 50-percent interest income exclusion for financial institution loans to ESOPs will result in a better measurement of the income of such financial institutions.

The provision to modify the exclusion of damages received on account of personal injury or sickness will simplify the administration of the Federal income tax laws by clarifying the taxation of damage awards and eliminating the need for additional litigation.

The provision to reform the income forecast method of accounting results in a better matching between income and depreciation deductions with respect to certain types of depreciable property.

The provision to apply a look-through rule for purposes of characterizing certain subpart F insurance income as unrelated business taxable income results in a better measurement of income by preventing unfair competition where operations involving the insur-

ance of third-party risks are conducted through a controlled foreign corporation that generally is subject to little tax relative to competing U.S. businesses.

The provision to repeal advance refunds of diesel fuel tax for diesel cars and light trucks results in a better measurement of income by repealing an obsolete credit for diesel fuel tax.

The provision to lower the reporting threshold for purchasers of fish from $10,000 to $600 will result in a better administration of the Federal tax laws by ensuring that the Internal Revenue Service has information reports with respect to more sales of fish.

The revenue-raising provisions of the bill are used to offset the cost of certain small business initiatives (including increased expensing, extension of the FICA tip credit to certain delivery persons, and pension and S corporation simplification provisions) and the extension of certain expiring provisions. These provisions are generally designed to relieve the burdens of Federal income taxation on individuals and small business and the revenue-raising provisions of the bill are critical to achieving these goals.

The revenue provisions of the bill do not contain any intergovernmental mandates.

The revenue provisions of the bill generally affect activities that are only engaged in by the private sector and, thus, do not affect the competitive balance between State, local, or tribal governments and the private sector.

E. Applicability of House Rule XXI5(c)

Rule XXI5(c) of the Rules of the House of Representatives provides that "No bill or joint resolution, amendment, or conference report carrying a Federal income tax rate increase shall be considered as passed or agreed to unless so determined by a vote of not less than three-fifths of the Members voting." The Committee has carefully reviewed the provisions of the bill to determine whether any of these provisions constitute a Federal income tax rate increase within the meaning of the House rules. It is the opinion of the Committee that there is no provision in the bill that constitutes a Federal income tax rate increase within the meaning of House rule XXI5 (c) or (d).

VI. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE CODE OF 1986

* * * * * * *

Subtitle A—Income Taxes

* * * * * * *

CHAPTER 1—NORMAL TAXES AND SURTAXES

* * * * * * *

Subchapter A—Determination of Tax Liability

* * * * * * *

PART I—TAX ON INDIVIDUALS

* * * * * * *

SEC. 1. TAX IMPOSED.

(a) * * *

* * * * * * *

(g) CERTAIN UNEARNED INCOME OF MINOR CHILDREN TAXED AS IF PARENT'S INCOME.—

(1) * * *

* * * * * * *

(7) ELECTION TO CLAIM CERTAIN UNEARNED INCOME OF CHILD ON PARENT'S RETURN.—

(A) IN GENERAL.—

If—

(i) any child to whom this subsection applies has gross income for the taxable year only from interest and dividends (including Alaska Permanent Fund dividends),

[(ii) such gross income is more than $500 and less than $5,000,]

(ii) such gross income is more than the amount described in paragraph (4)(A)(ii)(I) and less than 10 times the amount so described,

* * * * * * *

(B) INCOME INCLUDED ON PARENT'S RETURN.—In the case of a parent making the election under this paragraph—

(i) the gross income of each child to whom such election applies (to the extent the gross income of such child exceeds [$1,000] *twice the amount described in paragraph (4)(A)(ii)(I)*) shall be included in such parent's gross income for the taxable year,

(ii) the tax imposed by this section for such year with respect to such parent shall be the amount equal to the sum of—

(I) the amount determined under this section after the application of clause (i), plus

[(II) for each such child, the lesser of $75 or 15 percent of the excess of the gross income of such child over $500, and]

(II) for each such child, 15 percent of the lesser of the amount described in paragraph (4)(A)(ii)(I) or the excess of the gross income of such child over the amount so described, and

* * * * * * *

PART IV—CREDITS AGAINST TAX

Subpart A. Nonrefundable personal credits.

* * * * * * *

Subpart F. Rules for computing [targeted jobs credit] *work opportunity credit.*

* * * * * * *

PART IV—CREDITS AGAINST TAX

* * * * * * *

Subpart B—Foreign Tax Credit, Etc.

Sec. 27. Taxes of foreign countries and possessions of the United States; possession tax credit.

* * * * * * *

Sec. 30A. Puerto Rican economic activity credit.

* * * * * * *

SEC. 30. CREDIT FOR QUALIFIED ELECTRIC VEHICLES.

(a) * * *

* * * * * * *

(d) SPECIAL RULES.—

(1) BASIS REDUCTION.—The basis of any property for which a credit is allowable under subsection (a) shall be reduced by the amount of such credit *(determined without regard to subsection (b)(3))*.

* * * * * * *

(4) ELECTION TO NOT TAKE CREDIT.—No credit shall be allowed under subsection (a) for any vehicle if the taxpayer elects to not have this section apply to such vehicle.

* * * * * * *

SEC. 30A. PUERTO RICAN ECONOMIC ACTIVITY CREDIT.

(a) ALLOWANCE OF CREDIT.—

(1) IN GENERAL.—Except as otherwise provided in this section, if the conditions of both paragraph (1) and paragraph (2) of subsection (b) are satisfied with respect to a qualified domestic corporation, there shall be allowed as a credit against the tax imposed by this chapter an amount equal to the portion of the tax which is attributable to the taxable income, from sources without the United States, from—

(A) the active conduct of a trade or business within Puerto Rico, or

(B) the sale or exchange of substantially all of the assets used by the taxpayer in the active conduct of such trade or business.

In the case of any taxable year beginning after December 31, 2001, the aggregate amount of taxable income taken into account under the preceding sentence (and in applying subsection (d)) shall not exceed the adjusted base period income of such corporation, as determined in the same manner as under section 936(j).

(2) QUALIFIED DOMESTIC CORPORATION.—For purposes of paragraph (1), the term "qualified domestic corporation" means a domestic corporation—

(A) which is an existing credit claimant with respect to Puerto Rico, and

(B) with respect to which section 936(a)(4)(B) does not apply for the taxable year.

(3) SEPARATE APPLICATION.—For purposes of determining—

(A) whether a taxpayer is an existing credit claimant with respect to Puerto Rico, and

(B) the amount of the credit allowed under this section, this section (and so much of section 936 as relates to this section) shall be applied separately with respect to Puerto Rico.

(b) CONDITIONS WHICH MUST BE SATISFIED.—The conditions referred to in subsection (a) are—

(1) 3-YEAR PERIOD.—If 80 percent or more of the gross income of the qualified domestic corporation for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within a possession (determined without regard to section 904(f)).

(2) TRADE OR BUSINESS.—If 75 percent or more of the gross income of the qualified domestic corporation for such period or such part thereof was derived from the active conduct of a trade or business within a possession.

(c) CREDIT NOT ALLOWED AGAINST CERTAIN TAXES.—The credit provided by subsection (a) shall not be allowed against the tax imposed by—

(1) section 59A (relating to environmental tax),
(2) section 531 (relating to the tax on accumulated earnings),
(3) section 541 (relating to personal holding company tax), or
(4) section 1351 (relating to recoveries of foreign expropriation losses).

(d) LIMITATIONS ON CREDIT FOR ACTIVE BUSINESS INCOME.—The amount of the credit determined under subsection (a) for any taxable year shall not exceed the sum of the following amounts:

(1) 60 percent of the sum of—

(A) the aggregate amount of the qualified domestic corporation's qualified possession wages for such taxable year, plus

(B) the allocable employee fringe benefit expenses of the qualified domestic corporation for such taxable year.

(2) The sum of—

(A) 15 percent of the depreciation allowances for the taxable year with respect to short-life qualified tangible property,

(B) 40 percent of the depreciation allowances for the taxable year with respect to medium-life qualified tangible property, and

(C) 65 percent of the depreciation allowances for the taxable year with respect to long-life qualified tangible property.

(3) If the qualified domestic corporation does not have an election to use the method described in section 936(h)(5)(C)(ii) (relating to profit split) in effect for the taxable year, the amount of the qualified possession income taxes for the taxable year allocable to nonsheltered income.

(e) ADMINISTRATIVE PROVISIONS.—For purposes of this title—

(1) the provisions of section 936 (including any applicable election thereunder) shall apply in the same manner as if the credit under this section were a credit under section 936(a)(1)(A) for a domestic corporation to which section 936(a)(4)(A) applies,

(2) the credit under this section shall be treated in the same manner as the credit under section 936, and

(3) a corporation to which this section applies shall be treated in the same manner as if it were a corporation electing the application of section 936.

(f) DEFINITIONS.—For purposes of this section, any term used in this section which is also used in section 936 shall have the same meaning given such term by section 936.

(g) APPLICATION OF SECTION.—This section shall apply to taxable years beginning after December 31, 1995, and before January 1, 2006.

Subpart C—Refundable Credits

* * * * * * *

SEC. 34. CERTAIN USES OF GASOLINE AND SPECIAL FUELS.

(a) GENERAL RULE.—There shall be allowed as a credit against the tax imposed by this subtitle for the taxable year an amount equal to the sum of the amounts payable to the taxpayer—

(1) * * *

* * * * * * *

[(3) under section 6427—

[(A) with respect to fuels used for nontaxable purposes or resold, or

[(B) with respect to any qualified diesel-powered highway vehicle purchased (or deemed purchased under section 6427(g)(6)), during the taxable year (determined without regard to section 6427(k)).]

(3) under section 6427 with respect to fuels used for nontaxable purposes or resold during the taxable year (determined without regard to section 6427(k)).

* * * * * * *

Subpart D—Business Related Credits

* * * * * * *

SEC. 38. GENERAL BUSINESS CREDIT.

(a) * * *

(b) CURRENT YEAR BUSINESS CREDIT.—For purposes of this subpart, the amount of the current year business credit is the sum of the following credits determined for the taxable year:

(1) the investment credit determined under section 46,

(2) the [targeted jobs credit] *work opportunity credit* determined under section 51(a),

* * * * * * *

SEC. 39. CARRYBACK AND CARRYFORWARD OF UNUSED CREDITS.

(a) * * *

* * * * * * *

(d) TRANSITIONAL RULES.—

(1) * * *

* * * * * * *

(5) NO CARRYBACK OF SECTION [45] *45A* CREDIT BEFORE ENACTMENT.—No portion of the unused business credit for any taxable year which is attributable to the Indian employment credit determined under section 45A may be carried to a taxable year ending before the date of the enactment of section 45A.

(6) NO CARRYBACK OF SECTION [45] *45B* CREDIT BEFORE ENACTMENT.—No portion of the unused business credit for any taxable year which is attributable to the employer social security credit determined under section 45B may be carried back to a taxable year ending before the date of the enactment of section 45B.

SEC. 40. ALCOHOL USED AS FUEL.

(a) * * *

* * * * * * *

(e) TERMINATION.—

(1) IN GENERAL.—This section shall not apply to any sale or use—

(A) for any period after December 31, 2000, or

[(B) for any period before January 1, 2001, during which the Highway Trust Fund financing rate under section 4081(a)(2) is not in effect.]

(B) for any period before January 1, 2001, during which the rates of tax under section 4081(a)(2)(A) are 4.3 cents per gallon.

* * * * * * *

SEC. 42. LOW-INCOME HOUSING CREDIT.

(a) * * *

* * * * * * *

(c) QUALIFIED BASIS; QUALIFIED LOW-INCOME BUILDING.—For purposes of this section—

(1) * * *

(2) QUALIFIED LOW-INCOME BUILDING.—The term "qualified low-income building" means any building—

(A) which is part of a qualified low-income housing project at all times during the period—

(i) beginning on the 1st day in the compliance period on which such building is part of such a project, and

(ii) ending on the last day of the compliance period with respect to such building, and

(B) to which the amendments made by section 201(a) of the Tax Reform Act of 1986 apply.

Such term does not include any building with respect to which moderate rehabilitation assistance is provided, at any time during the compliance period, under section 8(e)(2) of the United States Housing Act of 1937 (other than assistance under the Stewart B. McKinney Homeless Assistance Act [of 1988] (as in effect on the date of the enactment of this sentence)).

* * * * * * *

SEC. 45B. CREDIT FOR PORTION OF EMPLOYER SOCIAL SECURITY TAXES PAID WITH RESPECT TO EMPLOYEE CASH TIPS.

(a) * * *

(b) EXCESS EMPLOYER SOCIAL SECURITY TAX—For purposes of this section—

(1) IN GENERAL.—The term "excess employer social security tax" means any tax paid by an employer under section 3111 with respect to tips received by an employee during any month, to the extent such tips—

(A) are deemed to have been paid by the employer to the employee pursuant to section 3121(q) *(without regard to whether such tips are reported under section 6053)*, and

* * * * * * *

[(2) ONLY TIPS RECEIVED AT FOOD AND BEVERAGE ESTABLISHMENTS TAKEN INTO ACCOUNT.—In applying paragraph (1), there shall be taken into account only tips received from customers in connection with the provision of food or beverages for consumption on the premises of an establishment with respect to which the tipping of employees serving food or beverages by customers is customary.]

(2) ONLY TIPS RECEIVED FOR FOOD OR BEVERAGES TAKEN INTO ACCOUNT.—In applying paragraph (1), there shall be taken into account only tips received from customers in connection with the delivering or serving of food or beverages for consumption if the tipping of employees delivering or serving food or beverages by customers is customary.

* * * * * * *

Subpart E—Rules for Computing Investment Credit

* * * * * * *

SEC. 50. OTHER SPECIAL RULES.

(a) RECAPTURE IN CASE OF DISPOSITIONS, ETC.—Under regulations prescribed by the Secretary—

(1) * * *

(2) PROPERTY CEASES TO QUALIFY FOR PROGRESS EXPENDITURES.—

(A) * * *

(C) CERTAIN SALES AND LEASEBACKS.—Under regulations prescribed by the Secretary, a sale by, and leaseback to, a taxpayer who, when the property is placed in service, will be a lessee to whom the rules referred to in [subsection (c)(4)] *subsection (d)(5)* apply shall not be treated as a cessation described in subparagraph (A) to the extent that the amount which will be passed through to the lessee under such rules with respect to such property is not less than the qualified rehabilitation expenditures properly taken into account by the lessee under section 47(d) with respect to such property.

* * * * * * *

(E) SPECIAL RULES.—Rules similar to the rules of this paragraph shall apply in cases where qualified progress expenditures were taken into account under the rules referred to in [section 48(a)(5)(A)] *section 48(a)(5)*.

* * * * * * *

Subpart F—Rules for Computing [Targeted Jobs Credit] *Work Opportunity Credit*

* * * * * * *

SEC. 51. AMOUNT OF CREDIT.

(a) DETERMINATION OF AMOUNT.—For purposes of section 38, the amount of the [targeted jobs credit] *work opportunity credit* determined under this section for the taxable year shall be equal to [40 percent] *35 percent* of the qualified first-year wages for such year.

* * * * * * *

(c) WAGES DEFINED.—For purposes of this subpart—

(1) IN GENERAL.——Except as otherwise provided in this subsection[, subsection (d)(8)(D),] and subsection (h)(2), the term "wages" has the meaning given to such term by sub-

section (b) of section 3306 (determined without regard to any dollar limitation contained in such section).

* * * * * * *

[(4) TERMINATION.—The term "wages" shall not include any amount paid or incurred to an individual who begins work for the employer after December 31, 1994.]

(4) TERMINATION.—The term "wages" shall not include any amount paid or incurred to an individual who begins work for the employer—

(A) after December 31, 1994, and before July 1, 1996, or

(B) after June 30, 1997.

[(d) MEMBERS OF TARGETED GROUPS.—For purposes of this subpart—

[(1) IN GENERAL.—An individual is a member of a targeted group if such individual is—

[(A) a vocational rehabilitation referral,

[(B) an economically disadvantaged youth,

[(C) an economically disadvantaged Vietnam-era veteran,

[(D) an SSI recipient,

[(E) a general assistance recipient,

[(F) a youth participating in a cooperative education program,

[(G) an economically disadvantaged ex-convict,

[(H) an eligible work incentive employee,

[(I) an involuntarily terminated CETA employee, or

[(J) a qualified summer youth employee.

[(2) VOCATIONAL REHABILITATION REFERRAL.—The term "vocational rehabilitation referral" means any individual who is certified by the designated local agency as—

[(A) having a physical or mental disability which, for such individual, constitutes or results in a substantial handicap to employment, and

[(B) having been referred to the employer upon completion of (or while receiving) rehabilitative services pursuant to—

[(i) an individualized written rehabilitation plan under a State plan for vocational rehabilitation services approved under the Rehabilitation Act of 1973, or

[(ii) a program of vocational rehabilitation carried out under chapter 31 of title 38, United States Code.

[(3) ECONOMICALLY DISADVANTAGED YOUTH.—

[(A) IN GENERAL.—The term "economically disadvantaged youth" means any individual who is certified by the designated local agency as—

[(i) meeting the age requirements of subparagraph (B), and

[(ii) being a member of an economically disadvantaged family (as determined under paragraph (11)).

[(B) AGE REQUIREMENTS.—An individual meets the age requirements of this subparagraph if such individual has attained age 18 but not age 23 on the hiring date.

[(4) VIETNAM VETERAN WHO IS A MEMBER OF AN ECONOMICALLY DISADVANTAGED FAMILY.—The term "Vietnam veteran

who is a member of an economically disadvantaged family" means any individual who is certified by the designated local agency as—

[(A)(i) having served on active duty (other than active duty for training) in the Armed Forces of the United States for a period of more than 180 days, any part of which occurred after August 4, 1964, and before May 8, 1975, or

[(ii) having been discharged or released from active duty in the Armed Forces of the United States for a service-connected disability if any part of such active duty was performed after August 4, 1964, and before May 8, 1975,

[(B) not having any day during the preemployment period which was a day of extended active duty in the Armed Forces of the United States, and

[(C) being a member of an economically disadvantaged family (determined under paragraph (11)).

For purposes of subparagraph (B), the term "extended active duty" means a period of more than 90 days during which the individual was on active duty (other than active duty for training).

[(5) SSI RECIPIENTS.—The term "SSI recipient" means any individual who is certified by the designated local agency as receiving supplemental security income benefits under title XVI of the Social Security Act (including supplemental security income benefits of the type described in section 1616 of such Act or section 212 of Public Law 93-66) for any month ending in the pre-employment period.

[(6) GENERAL ASSISTANCE RECIPIENTS.—

[(A) IN GENERAL.—The term "general assistance recipient" means any individual who is certified by the designated local agency as receiving assistance under a qualified general assistance program for any period of not less than 30 days ending within the preemployment period.

[(B) QUALIFIED GENERAL ASSISTANCE PROGRAM.—The term "qualified general assistance program" means any program of a State or a political subdivision of a State—

[(i) which provides general assistance or similar assistance which—

[(I) is based on need, and

[(II) consists of money payments or voucher or scrip, and

[(ii) which is designated by the Secretary (after consultation with the Secretary of Health and Human Services) as meeting the requirements of clause (i).

[(7) ECONOMICALLY DISADVANTAGED EX-CONVICT.—The term "economically disadvantaged ex-convict" means any individual who is certified by the designated local agency—

[(A) as having been convicted of a felony under any statute of the United States or any State,

[(B) as being a member of an economically disadvantaged family (as determined under paragraph (11)), and

[(C) as having a hiring date which is not more than 5 years after the last date on which such individual was so convicted or was released from prison.

[(8) YOUTH PARTICIPATING IN A QUALIFIED COOPERATIVE EDUCATION PROGRAM.—

[(A) IN GENERAL.—The term "youth participating in a qualified cooperative education program" means any individual who is certified by the school participating in the program as—

[(i) having attained age 16 and not having attained age 20,

[(ii) not having graduated from a high school or vocational school,

[(iii) being enrolled in and actively pursuing a qualified cooperative education program, and

[(iv) being a member of an economically disadvantaged family (as determined under paragraph (11)).

[(B) QUALIFIED COOPERATIVE EDUCATION PROGRAM DEFINED.—The term "qualified cooperative education program" means a program of vocational education for individuals who (through written cooperative arrangements between a qualified school and 1 or more employers) receive instruction (including required academic instruction) by alternation of study and school with a job in any occupational field (but only if these 2 experiences are planned by the school and employer so that each contributes to the student's education and employability).

[(C) QUALIFIED SCHOOL DEFINED.—The term "qualified school" means—

[(i) a specialized high school used exclusively or principally for the provision of vocational education to individuals who are available for study in preparation for entering the labor market,

[(ii) the department of a high school exclusively or principally used for providing vocational education to persons who are available for study in preparation for entering the labor market, or

[(iii) a technical or vocational school used exclusively or principally for the provision of vocational education to persons who have completed or left high school and who are available for study in preparation for entering the labor market.

A school which is not a public school shall be treated as a qualified school only if it is exempt from tax under section 501(a).

[(D) WAGES.—In the case of remuneration attributable to services performed while the individual meets the requirements of clauses (i), (ii), and (iii) of subparagraph (A), wages, and unemployment insurance wages, shall be determined without regard to section 3306(c)(10)(C).

[(9) ELIGIBLE WORK INCENTIVE EMPLOYEES.—The term "eligible work incentive employee" means an individual who has been certified by the designated local agency as—

[(A) being eligible for financial assistance under part A of title IV of the Social Security Act and as having continually received such financial assistance during the 90-day

period which immediately precedes the date on which such individual is hired by the employer, or

[(B) having been placed in employment under a work incentive program established under section 432(b)(1) or 445 of the Social Security Act.

[(10) INVOLUNTARILY TERMINATED CETA EMPLOYEE.—The term "involuntarily terminated CETA employee" means an individual who is certified by the designated local agency as having been involuntarily terminated after December 31, 1980, from employment financed in whole or in part under a program under part D of title II or title VI of the Comprehensive Employment and Training Act. This paragraph shall not apply to any individual who begins work for the employer after December 31, 1982.

[(11) MEMBERS OF ECONOMICALLY DISADVANTAGED FAMILIES.—An individual is a member of an economically disadvantaged family if the designated local agency determines that such individual was a member of a family which had an income during the 6 months immediately preceding the earlier of the month in which such determination occurs or the month in which the hiring date occurs, which, on an annual basis, would be 70 percent or less of the Bureau of Labor Statistics lower living standard. Any such determination shall be valid for the 45-day period beginning on the date such determination is made. Any such determination with respect to an individual who is a qualified summer youth employee or youth participating in a qualified cooperative education program with respect to any employer shall also apply for purposes of determining whether such individual is a member of another targeted group with respect to such employer.

[(12) QUALIFIED SUMMER YOUTH EMPLOYEE.—

[(A) IN GENERAL.—The term "qualified summer youth employee" means an individual—

[(i) who performs services for the employer between May 1 and September 15,

[(ii) who is certified by the designated local agency as having attained age 16 but not 18 on the hiring date (or if later, on May 1 of the calendar year involved),

[(iii) who has not been an employee of the employer during any period prior to the 90-day period described in subparagraph (B)(iii), and

[(iv) who is certified by the designated local agency as being a member of an economically disadvantaged family (as determined under paragraph (11)).

[(B) SPECIAL RULES FOR DETERMINING AMOUNT OF CREDIT.—For purposes of applying this subpart to wages paid or incurred to any qualified summer youth employee—

[(i) subsection (b)(2) shall be applied by substituting "any 90-day period between May 1 and September 15" for "the 1-year period beginning with the day the individual begins work for the employer", and

[(ii) subsection (b)(3) shall be applied by substituting "$3,000" for "$6,000".

[(C) as having a hiring date which is not more than 5 years after the last date on which such individual was so convicted or was released from prison.

[(8) YOUTH PARTICIPATING IN A QUALIFIED COOPERATIVE EDUCATION PROGRAM.—

[(A) IN GENERAL.—The term "youth participating in a qualified cooperative education program" means any individual who is certified by the school participating in the program as—

[(i) having attained age 16 and not having attained age 20,

[(ii) not having graduated from a high school or vocational school,

[(iii) being enrolled in and actively pursuing a qualified cooperative education program, and

[(iv) being a member of an economically disadvantaged family (as determined under paragraph (11)).

[(B) QUALIFIED COOPERATIVE EDUCATION PROGRAM DEFINED.—The term "qualified cooperative education program" means a program of vocational education for individuals who (through written cooperative arrangements between a qualified school and 1 or more employers) receive instruction (including required academic instruction) by alternation of study and school with a job in any occupational field (but only if these 2 experiences are planned by the school and employer so that each contributes to the student's education and employability).

[(C) QUALIFIED SCHOOL DEFINED.—The term "qualified school" means—

[(i) a specialized high school used exclusively or principally for the provision of vocational education to individuals who are available for study in preparation for entering the labor market,

[(ii) the department of a high school exclusively or principally used for providing vocational education to persons who are available for study in preparation for entering the labor market, or

[(iii) a technical or vocational school used exclusively or principally for the provision of vocational education to persons who have completed or left high school and who are available for study in preparation for entering the labor market.

A school which is not a public school shall be treated as a qualified school only if it is exempt from tax under section 501(a).

[(D) WAGES.—In the case of remuneration attributable to services performed while the individual meets the requirements of clauses (i), (ii), and (iii) of subparagraph (A), wages, and unemployment insurance wages, shall be determined without regard to section 3306(c)(10)(C).

[(9) ELIGIBLE WORK INCENTIVE EMPLOYEES.—The term "eligible work incentive employee" means an individual who has been certified by the designated local agency as—

[(A) being eligible for financial assistance under part A of title IV of the Social Security Act and as having continually received such financial assistance during the 90-day

period which immediately precedes the date on which such individual is hired by the employer, or

[(B) having been placed in employment under a work incentive program established under section 432(b)(1) or 445 of the Social Security Act.

[(10) INVOLUNTARILY TERMINATED CETA EMPLOYEE.—The term "involuntarily terminated CETA employee" means an individual who is certified by the designated local agency as having been involuntarily terminated after December 31, 1980, from employment financed in whole or in part under a program under part D of title II or title VI of the Comprehensive Employment and Training Act. This paragraph shall not apply to any individual who begins work for the employer after December 31, 1982.

[(11) MEMBERS OF ECONOMICALLY DISADVANTAGED FAMILIES.—An individual is a member of an economically disadvantaged family if the designated local agency determines that such individual was a member of a family which had an income during the 6 months immediately preceding the earlier of the month in which such determination occurs or the month in which the hiring date occurs, which, on an annual basis, would be 70 percent or less of the Bureau of Labor Statistics lower living standard. Any such determination shall be valid for the 45-day period beginning on the date such determination is made. Any such determination with respect to an individual who is a qualified summer youth employee or youth participating in a qualified cooperative education program with respect to any employer shall also apply for purposes of determining whether such individual is a member of another targeted group with respect to such employer.

[(12) QUALIFIED SUMMER YOUTH EMPLOYEE.—

[(A) IN GENERAL.—The term "qualified summer youth employee" means an individual—

[(i) who performs services for the employer between May 1 and September 15,

[(ii) who is certified by the designated local agency as having attained age 16 but not 18 on the hiring date (or if later, on May 1 of the calendar year involved),

[(iii) who has not been an employee of the employer during any period prior to the 90-day period described in subparagraph (B)(iii), and

[(iv) who is certified by the designated local agency as being a member of an economically disadvantaged family (as determined under paragraph (11)).

[(B) SPECIAL RULES FOR DETERMINING AMOUNT OF CREDIT.—For purposes of applying this subpart to wages paid or incurred to any qualified summer youth employee—

[(i) subsection (b)(2) shall be applied by substituting "any 90-day period between May 1 and September 15" for "the 1-year period beginning with the day the individual begins work for the employer", and

[(ii) subsection (b)(3) shall be applied by substituting "$3,000" for "$6,000".

[(C) SPECIAL RULE FOR CONTINUED EMPLOYMENT FOR SAME EMPLOYER.—In the case of an individual who, with respect to the same employer, is certified as a member of another targeted group after such individual has been a qualified summer youth employee, paragraph (14) shall be applied by substituting "certified" for "hired by the employer".

[(13) PREEMPLOYMENT PERIOD.—The term "preemployment period" means the 60-day period ending on the hiring date.

[(14) HIRING DATE.—The term "hiring date" means the day the individual is hired by the employer.

[(15) DESIGNATED LOCAL AGENCY.—The term "designated local agency" means a State employment security agency established in accordance with the Act of June 6, 1933, as amended (29 U.S.C. 49–49n).

[(16) SPECIAL RULES FOR CERTIFICATIONS.—

[(A) IN GENERAL.—An individual shall not be treated as a member of a targeted group unless, on or before the day on which such individual begins work for the employer, the employer—

[(i) has received a certification from a designated local agency that such individual is a member of a targeted group, or

[(ii) has requested in writing such certification from the designated local agency.

For purposes of the preceding sentence, if on or before the day on which such individual begins work for the employer, such individual has received from a designated local agency (or other agency or organization designated pursuant to a written agreement with such designated local agency) a written preliminary determination that such individual is a member of a targeted group, then "the fifth day" shall be substituted for "the day" in such sentence.

[(B) INCORRECT CERTIFICATIONS.—If—

[(i) an individual has been certified as a member of a targeted group, and

[(ii) such certification is incorrect because it was based on false information provided by such individual, the certification shall be revoked and wages paid by the employer after the date on which notice of revocation is received by the employer shall not be treated as qualified wages.

[(C) EMPLOYER REQUEST MUST SPECIFY POTENTIAL BASIS FOR ELIGIBILITY.—In any request for a certification of an individual as a member of a targeted group, the employer shall—

[(i) specify each subparagraph (but not more than 2) of paragraph (1) by reason of which the employer believes that such individual is such a member, and

[(ii) certify that a good faith effort was made to determine that such individual is such a member.]

(d) MEMBERS OF TARGETED GROUPS.—For purposes of this subpart—

(1) IN GENERAL.—An individual is a member of a targeted group if such individual is—

(A) a qualified IV–A recipient,

(B) a qualified veteran,

(C) a qualified ex-felon,

(D) a high-risk youth,

(E) a vocational rehabilitation referral, or

(F) a qualified summer youth employee.

(2) QUALIFIED IV–A RECIPIENT.—

(A) IN GENERAL.—The term "qualified IV–A recipient" means any individual who is certified by the designated local agency as being a member of a family receiving assistance under a IV–A program for at least a 9-month period ending during the 9-month period ending on the hiring date.

(B) IV–A PROGRAM.—For purposes of this paragraph, the term "IV–A program" means any program providing assistance under a State plan approved under part A of title IV of the Social Security Act (relating to assistance for needy families with minor children) and any successor of such program.

(3) QUALIFIED VETERAN.—

(A) IN GENERAL.—The term "qualified veteran" means any veteran who is certified by the designated local agency as being—

(i) a member of a family receiving assistance under a IV–A program (as defined in paragraph (2)(B)) for at least a 9-month period ending during the 12-month period ending on the hiring date, or

(ii) a member of a family receiving assistance under a food stamp program under the Food Stamp Act of 1977 for at least a 3-month period ending during the 12-month period ending on the hiring date.

(B) VETERAN.—For purposes of subparagraph (A), the term "veteran" means any individual who is certified by the designated local agency as—

(i)(I) having served on active duty (other than active duty for training) in the Armed Forces of the United States for a period of more than 180 days, or

(II) having been discharged or released from active duty in the Armed Forces of the United States for a service-connected disability, and

(ii) not having any day during the 60-day period ending on the hiring date which was a day of extended active duty in the Armed Forces of the United States.

For purposes of clause (ii), the term "extended active duty" means a period of more than 90 days during which the individual was on active duty (other than active duty for training).

(4) QUALIFIED EX-FELON.—The term "qualified ex-felon" means any individual who is certified by the designated local agency—

(A) as having been convicted of a felony under any statute of the United States or any State,

(B) as having a hiring date which is not more than 1 year after the last date on which such individual was so convicted or was released from prison, and

(C) as being a member of a family which had an income during the 6 months immediately preceding the earlier of the month in which such income determination occurs or the month in which the hiring date occurs, which, on an annual basis, would be 70 percent or less of the Bureau of Labor Statistics lower living standard.

Any determination under subparagraph (C) shall be valid for the 45-day period beginning on the date such determination is made.

(5) HIGH-RISK YOUTH.—

(A) IN GENERAL.—The term "high-risk youth" means any individual who is certified by the designated local agency—

(i) as having attained age 18 but not age 25 on the hiring date, and

(ii) as having his principal place of abode within an empowerment zone or enterprise community.

(B) YOUTH MUST CONTINUE TO RESIDE IN ZONE.—In the case of a high-risk youth, the term "qualified wages" shall not include wages paid or incurred for services performed while such youth's principal place of abode is outside an empowerment zone or enterprise community.

(6) VOCATIONAL REHABILITATION REFERRAL.—The term "vocational rehabilitation referral" means any individual who is certified by the designated local agency as—

(A) having a physical or mental disability which, for such individual, constitutes or results in a substantial handicap to employment, and

(B) having been referred to the employer upon completion of (or while receiving) rehabilitative services pursuant to—

(i) an individualized written rehabilitation plan under a State plan for vocational rehabilitation services approved under the Rehabilitation Act of 1973, or

(ii) a program of vocational rehabilitation carried out under chapter 31 of title 38, United States Code.

(7) QUALIFIED SUMMER YOUTH EMPLOYEE.—

(A) IN GENERAL.—The term "qualified summer youth employee" means any individual—

(i) who performs services for the employer between May 1 and September 15,

(ii) who is certified by the designated local agency as having attained age 16 but not 18 on the hiring date (or if later, on May 1 of the calendar year involved),

(iii) who has not been an employee of the employer during any period prior to the 90-day period described in subparagraph (B)(i), and

(iv) who is certified by the designated local agency as having his principal place of abode within an empowerment zone or enterprise community.

(B) SPECIAL RULES FOR DETERMINING AMOUNT OF CREDIT.—For purposes of applying this subpart to wages paid or incurred to any qualified summer youth employee—

(i) subsection (b)(2) shall be applied by substituting "any 90-day period between May 1 and September 15" for "the 1-year period beginning with the day the individual begins work for the employer", and

(ii) subsection (b)(3) shall be applied by substituting "$3,000" for "$6,000".

The preceding sentence shall not apply to an individual who, with respect to the same employer, is certified as a member of another targeted group after such individual has been a qualified summer youth employee.

(C) YOUTH MUST CONTINUE TO RESIDE IN ZONE.—Paragraph (5)(B) shall apply for purposes of this paragraph.

(8) HIRING DATE.—The term "hiring date" means the day the individual is hired by the employer.

(9) DESIGNATED LOCAL AGENCY.—The term "designated local agency" means a State employment security agency established in accordance with the Act of June 6, 1933, as amended (29 U.S.C. 49–49n).

(10) SPECIAL RULES FOR CERTIFICATIONS.—

(A) IN GENERAL.—An individual shall not be treated as a member of a targeted group unless—

(i) on or before the day on which such individual begins work for the employer, the employer has received a certification from a designated local agency that such individual is a member of a targeted group, or

(ii)(I) on or before the day the individual is offered employment with the employer, a pre-screening notice is completed by the employer with respect to such individual, and

(II) not later than the 14th day after the individual begins work for the employer, the employer submits such notice, signed by the employer and the individual under penalties of perjury, to the designated local agency as part of a written request for such a certification from such agency.

For purposes of this paragraph, the term "pre-screening notice" means a document (in such form as the Secretary shall prescribe) which contains information provided by the individual on the basis of which the employer believes that the individual is a member of a targeted group.

(B) INCORRECT CERTIFICATIONS.—If—

(i) an individual has been certified by a designated local agency as a member of a targeted group, and

(ii) such certification is incorrect because it was based on false information provided by such individual,

the certification shall be revoked and wages paid by the employer after the date on which notice of revocation is received by the employer shall not be treated as qualified wages.

(C) EXPLANATION OF DENIAL OF REQUEST.—If a designated local agency denies a request for certification of membership in a targeted group, such agency shall provide

to the person making such request a written explanation of the reasons for such denial.

* * * * * * *

(i) CERTAIN INDIVIDUALS INELIGIBLE.—

(1) * * *

* * * * * * *

[(3) INDIVIDUALS NOT MEETING MINIMUM EMPLOYMENT PERIOD.—No wages shall be taken into account under subsection (a) with respect to any individual unless such individual either—

[(A) is employed by the employer at least 90 days (14 days in the case of an individual described in subsection (d)(12)), or

[(B) has completed at least 120 hours (20 hours in the case of an individual described in subsection (d)(12)) of services performed for the employer.]

(3) INDIVIDUALS NOT MEETING MINIMUM EMPLOYMENT PERIOD.—No wages shall be taken into account under subsection (a) with respect to any individual unless such individual either—

(A) is employed by the employer at least 180 days (20 days in the case of a qualified summer youth employee), or

(B) has completed at least 500 hours (120 hours in the case of a qualified summer youth employee) of services performed for the employer.

* * * * * * *

Subpart G—Credit Against Regular Tax for Prior Year Minimum Tax Liability

* * * * * * *

SEC. 53. CREDIT FOR PRIOR YEAR MINIMUM TAX LIABILITY.

(a) * * *

* * * * * * *

(d) DEFINITIONS.—For purposes of this section—

(1) NET MINIMUM TAX.—

(A) IN GENERAL.—The term "net minimum tax" means the tax imposed by section 55.

(B) CREDIT NOT ALLOWED FOR EXCLUSION PREFERENCES.—

(i) * * *

* * * * * * *

(iv) CREDIT ALLOWABLE FOR EXCLUSION PREFERENCES OF CORPORATIONS.—In the case of a corporation—

(I) the preceding provisions of this subparagraph shall not apply, and

[(II) the adjusted net minimum tax for any taxable year is the amount of the net minimum tax for such year increased by the amount of any credit not allowed under section 29 solely by reason of the application of section 29(b)(5)(B) or not al-

lowed under section 28 solely by reason of the application of section 28(d)(2)(B).]

(II) the adjusted net minimum tax for any taxable year is the amount of the net minimum tax for such year increased in the manner provided in clause (iii).

* * * * * * *

PART VI—ALTERNATIVE MINIMUM WAGE

* * * * * * *

SEC. 55. ALTERNATIVE MINIMUM TAX IMPOSED.

(a) * * *

* * * * * * *

(c) REGULAR TAX.—

(1) IN GENERAL.—For purposes of this section, the term "regular tax" means the regular tax liability for the taxable year (as defined in section 26(b)) reduced by the foreign tax credit allowable under section 27(a) [and the section 936 credit allowable under section 27(b)], *the section 936 credit allowable under section 27(b), and the Puerto Rican economic activity credit under section 30A.* Such term [shall not include any tax imposed by section 402(d) and] shall not include any increase in tax under section 49(b) or 50(a) or subsection (j) or (k) of section 42.

* * * * * * *

SEC. 56. ADJUSTMENTS IN COMPUTING ALTERNATIVE MINIMUM TAXABLE INCOME.

(a) * * *

* * * * * * *

(d) ALTERNATIVE TAX NET OPERATING LOSS DEDUCTION DEFINED.—

(1) IN GENERAL.—For purposes of subsection (a)(4), the term "alternative tax net operating loss deduction" means the net operating loss deduction allowable for the taxable year under section 172, except that—

(A) * * *

(B) in determining the amount of such deduction—

(i) the net operating loss (within the meaning of section 172(c)) for any loss year shall be adjusted as provided in paragraph (2), and

[(ii) in the case of taxable years beginning after December 31, 1986, section 172(b)(2) shall be applied by substituting "90 percent of alternative minimum taxable income determined without regard to the alternative tax net operating loss deduction" for "taxable income" each place it appears.]

(ii) appropriate adjustments in the application of section 172(b)(2) shall be made to take into account the limitation of subparagraph (A).

* * * * * * *

to the person making such request a written explanation of the reasons for such denial.

* * * * * * *

(i) CERTAIN INDIVIDUALS INELIGIBLE.—

(1) * * *

* * * * * * *

[(3) INDIVIDUALS NOT MEETING MINIMUM EMPLOYMENT PERIOD.—No wages shall be taken into account under subsection (a) with respect to any individual unless such individual either—

[(A) is employed by the employer at least 90 days (14 days in the case of an individual described in subsection (d)(12)), or

[(B) has completed at least 120 hours (20 hours in the case of an individual described in subsection (d)(12)) of services performed for the employer.]

(3) INDIVIDUALS NOT MEETING MINIMUM EMPLOYMENT PERIOD.—No wages shall be taken into account under subsection (a) with respect to any individual unless such individual either—

(A) is employed by the employer at least 180 days (20 days in the case of a qualified summer youth employee), or

(B) has completed at least 500 hours (120 hours in the case of a qualified summer youth employee) of services performed for the employer.

* * * * * * *

Subpart G—Credit Against Regular Tax for Prior Year Minimum Tax Liability

* * * * * * *

SEC. 53. CREDIT FOR PRIOR YEAR MINIMUM TAX LIABILITY.

(a) * * *

* * * * * * *

(d) DEFINITIONS.—For purposes of this section—

(1) NET MINIMUM TAX.—

(A) IN GENERAL.—The term "net minimum tax" means the tax imposed by section 55.

(B) CREDIT NOT ALLOWED FOR EXCLUSION PREFERENCES.—

(i) * * *

* * * * * * *

(iv) CREDIT ALLOWABLE FOR EXCLUSION PREFERENCES OF CORPORATIONS.—In the case of a corporation—

(I) the preceding provisions of this subparagraph shall not apply, and

[(II) the adjusted net minimum tax for any taxable year is the amount of the net minimum tax for such year increased by the amount of any credit not allowed under section 29 solely by reason of the application of section 29(b)(5)(B) or not al-

lowed under section 28 solely by reason of the application of section 28(d)(2)(B).]

(II) the adjusted net minimum tax for any taxable year is the amount of the net minimum tax for such year increased in the manner provided in clause (iii).

* * * * * * *

PART VI—ALTERNATIVE MINIMUM WAGE

* * * * * * *

SEC. 55. ALTERNATIVE MINIMUM TAX IMPOSED.

(a) * * *

* * * * * * *

(c) REGULAR TAX.—

(1) IN GENERAL.—For purposes of this section, the term "regular tax" means the regular tax liability for the taxable year (as defined in section 26(b)) reduced by the foreign tax credit allowable under section 27(a) [and the section 936 credit allowable under section 27(b)], *the section 936 credit allowable under section 27(b), and the Puerto Rican economic activity credit under section 30A.* Such term [shall not include any tax imposed by section 402(d) and] shall not include any increase in tax under section 49(b) or 50(a) or subsection (j) or (k) of section 42.

* * * * * * *

SEC. 56. ADJUSTMENTS IN COMPUTING ALTERNATIVE MINIMUM TAXABLE INCOME.

(a) * * *

* * * * * * *

(d) ALTERNATIVE TAX NET OPERATING LOSS DEDUCTION DEFINED.—

(1) IN GENERAL.—For purposes of subsection (a)(4), the term "alternative tax net operating loss deduction" means the net operating loss deduction allowable for the taxable year under section 172, except that—

(A) * * *

(B) in determining the amount of such deduction—

(i) the net operating loss (within the meaning of section 172(c)) for any loss year shall be adjusted as provided in paragraph (2), and

[(ii) in the case of taxable years beginning after December 31, 1986, section 172(b)(2) shall be applied by substituting "90 percent of alternative minimum taxable income determined without regard to the alternative tax net operating loss deduction" for "taxable income" each place it appears.]

(ii) appropriate adjustments in the application of section 172(b)(2) shall be made to take into account the limitation of subparagraph (A).

* * * * * * *

(g) ADJUSTMENTS BASED ON ADJUSTED CURRENT EARNINGS.—
(1) * * *

* * * * * * *

(4) ADJUSTMENTS.—In determining adjusted current earnings, the following adjustments shall apply:
(A) * * *

* * * * * * *

(C) DISALLOWANCE OF ITEMS NOT DEDUCTIBLE IN COMPUTING EARNINGS AND PROFITS.—
(i) * * *
(ii) SPECIAL RULE FOR CERTAIN DIVIDENDS.—
(I) IN GENERAL.—Clause (i) shall not apply to any deduction allowable under section 243 or 245 for any dividend which is a 100-percent dividend or which is received from a 20-percent owned corporation (as defined in section 243(c)(2)), but only to the extent such dividend is attributable to income of the paying corporation which is subject to tax under this chapter determined after the application of sections *30A,* 936 (including subsections (a)(4) [and (i)]*, (i), and (j)* thereof) and 921.
(II) 100-PERCENT DIVIDEND.—For purposes [of the subclause] *of subclause* (I), the term "100 percent dividend" means any dividend if the percentage used for purposes of determining the amount allowable as a deduction under section 243 or 245 with respect to such dividend is 100 percent.
(iii) TREATMENT OF TAXES ON DIVIDENDS FROM 936 CORPORATIONS.—
(I) * * *

* * * * * * *

(VI) APPLICATION TO SECTION 30A CORPORATIONS.—References in this clause to section 936 shall be treated as including references to section 30A.

(D) CERTAIN OTHER EARNINGS AND PROFITS ADJUSTMENTS.—
(i) * * *

* * * * * * *

(iii) LIFO INVENTORY ADJUSTMENTS.—The adjustments provided in section 312(n)(4) shall apply, *but only with respect to taxable years beginning after December 31, 1989.*

* * * * * * *

[(I)] *(H)* ADJUSTED BASIS.—The adjusted basis of any property with respect to which an adjustment under this paragraph applies shall be determined by applying the treatment prescribed in this paragraph.

[(J)] *(I)* TREATMENT OF CHARITABLE CONTRIBUTIONS.—Notwithstanding subparagraphs (B) and (C), no adjustment related to the earnings and profits effects of any

charitable contribution shall be made in computing adjusted current earnings.

* * * * * * *

SEC. 59. OTHER DEFINITIONS AND SPECIAL RULES.

(a) ALTERNATIVE MINIMUM TAX FOREIGN TAX CREDIT.—For purposes of this part—

(1) IN GENERAL.—The alternative minimum tax foreign tax credit for any taxable year shall be the credit which would be determined under section 27(a) for such taxable year if—

(A) [the amount determined under section 55(b)(1)(A)] *the pre-credit tentative minimum tax* were the tax against which such credit was taken for purposes of section 904 for the taxable year and all prior taxable years beginning after December 31, 1986,

(B) section 904 were applied on the basis of alternative minimum taxable income instead of taxable income, and

(C) the determination of whether any income is high-taxed income for purposes of section 904(d)(2) were made on the basis of the applicable rate [specified in section 55(b)(1)(A)] *specified in subparagraph (A)(i) or (B)(i) of section 55(b)(1) (whichever applies)* in lieu of the highest rate of tax specified in section 1 or 11 (whichever applies).

(2) LIMITATION TO 90 PERCENT OF TAX.—

(A) IN GENERAL.—The alternative minimum tax foreign tax credit for any taxable year shall not exceed the excess (if any) of—

(i) [the amount determined under section 55(b)(1)(A)] *the pre-credit tentative minimum tax* for the taxable year, over

(ii) 10 percent of the amount [which would be determined under section 55(b)(1)(A)] *which would be the pre-credit tentative minimum tax* without regard to the alternative tax net operating loss deduction and section 57(a)(2)(E).

* * * * * * *

(3) PRE-CREDIT TENTATIVE MINIMUM TAX.—For purposes of this subsection, the term "pre-credit tentative minimum tax" means—

(A) in the case of a taxpayer other than a corporation, the amount determined under the first sentence of section 55(b)(1)(A)(i), or

(B) in the case of a corporation, the amount determined under section 55(b)(1)(B)(i).

* * * * * * *

(b) MINIMUM TAX NOT TO APPLY TO INCOME ELIGIBLE FOR SECTION 936 CREDIT.—In the case of any corporation for which a credit is allowable for the taxable year under [section 936, alternative minimum taxable income shall not include any amount with respect to which the requirements of subparagraph (A) or (B) of section 936(a)(1) are met.] *section 30A or 936, alternative minimum*

taxable income shall not include any income with respect to which a credit is determined under section 30A or 936.

* * * * * * *

(d) APPORTIONMENT OF DIFFERENTLY TREATED ITEMS IN CASE OF CERTAIN ENTITIES.—

(1) IN GENERAL. The differently treated items for the taxable year shall be apportioned (in accordance with regulations prescribed by the Secretary)—

(A) * * *

(B) COMMON TRUST FUNDS.—In the case of a common trust fund (as defined in section 584(a)), pro rata among the participants of such fund.

* * * * * * *

(j) TREATMENT OF UNEARNED INCOME OF MINOR CHILDREN.—

(1) LIMITATION ON EXEMPTION AMOUNT.—In the case of a child to whom section 1(g) applies, the exemption amount for purposes of section 55 shall not exceed the sum of—

(A) such child's earned income (as defined in section 911(d)(2)) for the taxable year, plus

(B) [$1,000] *twice the amount in effect for the taxable year under section 63(c)(5)(A)* (or, if greater, the child's share of the unused parental minimum tax exemption).

* * * * * * *

(3) UNUSED PARENTAL MINIMUM TAX EXEMPTION.—

(A) * * *

(B) CERTAIN RULES MADE APPLICABLE.—A child's share of any unused parental minimum tax exemption shall be determined under rules similar to the rules of [section 1(g)(3)(B), and rules similar to the rules of paragraphs (3)(D) and (5) of section 1(g) shall apply for purposes of this paragraph.

* * * * * * *

Subchapter B—Computation of Taxable Income

* * * * * * *

PART I—DEFINITION OF GROSS INCOME, ADJUSTED GROSS INCOME, TAXABLE INCOME, ETC.

* * * * * * *

SEC. 62. ADJUSTED GROSS INCOME DEFINED.

(a) GENERAL RULE.—For purposes of this subtitle, the term "adjusted gross income" means, in the case of an individual, gross income minus the following deductions:

(1) * * *

* * * * * * *

[(8) CERTAIN PORTION OF LUMP-SUM DISTRIBUTIONS FROM PENSION PLANS TAXED UNDER SECTION 402(d).—The deduction allowed by section 402(d)(3).]

* * * * * * *

PART II—ITEMS SPECIFICALLY INCLUDED IN GROSS INCOME

* * * * * * *

SEC. 72. ANNUITIES; CERTAIN PROCEEDS OF ENDOWMENT AND LIFE INSURANCE CONTRACTS.

(a) * * *

(b) EXCLUSION RATIO.—

(1) * * *

* * * * * * *

(4) UNRECOVERED INVESTMENT.—For purposes of this subsection, the unrecovered investment in the contract as of any date is—

(A) the investment in the contract *(determined without regard to subsection (c)(2))* as of the annuity starting date, reduced by

(B) the aggregate amount received under the contract on or after such annuity starting date and before the date as of which the determination is being made, to the extent such amount was excludable from gross income under this subtitle.

* * * * * * *

[(d) TREATMENT OF EMPLOYEE CONTRIBUTIONS UNDER DEFINED CONTRIBUTION PLANS AS SEPARATE CONTRACTS.—For purposes of this section, employee contributions (and any income allocable thereto) under a defined contribution plan may be treated as a separate contract.]

(d) SPECIAL RULES FOR QUALIFIED EMPLOYER RETIREMENT PLANS.—

(1) SIMPLIFIED METHOD OF TAXING ANNUITY PAYMENTS.—

(A) IN GENERAL.—In the case of any amount received as an annuity under a qualified employer retirement plan—

(i) subsection (b) shall not apply, and

(ii) the investment in the contract shall be recovered as provided in this paragraph.

(B) METHOD OF RECOVERING INVESTMENT IN CONTRACT.—

(i) IN GENERAL.—Gross income shall not include so much of any monthly annuity payment under a qualified employer retirement plan as does not exceed the amount obtained by dividing—

(I) the investment in the contract (as of the annuity starting date), by

(II) the number of anticipated payments determined under the table contained in clause (iii) (or, in the case of a contract to which subsection (c)(3)(B) applies, the number of monthly annuity payments under such contract).

(ii) CERTAIN RULES MADE APPLICABLE.—Rules similar to the rules of paragraphs (2) and (3) of subsection (b) shall apply for purposes of this paragraph.

(iii) NUMBER OF ANTICIPATED PAYMENTS.—

If the age of the primary annuitant on the annuity starting date is:	*The number of anticipated payments is:*
Not more than 55	*360*
More than 55 but not more than 60	*310*
More than 60 but not more than 65	*260*
More than 65 but not more than 70	*210*
More than 70	*160.*

(C) ADJUSTMENT FOR REFUND FEATURE NOT APPLICABLE.—For purposes of this paragraph, investment in the contract shall be determined under subsection (c)(1) without regard to subsection (c)(2).

(D) SPECIAL RULE WHERE LUMP SUM PAID IN CONNECTION WITH COMMENCEMENT OF ANNUITY PAYMENTS.—If, in connection with the commencement of annuity payments under any qualified employer retirement plan, the taxpayer receives a lump sum payment—

(i) such payment shall be taxable under subsection (e) as if received before the annuity starting date, and

(ii) the investment in the contract for purposes of this paragraph shall be determined as if such payment had been so received.

(E) EXCEPTION.—This paragraph shall not apply in any case where the primary annuitant has attained age 75 on the annuity starting date unless there are fewer than 5 years of guaranteed payments under the annuity.

(F) ADJUSTMENT WHERE ANNUITY PAYMENTS NOT ON MONTHLY BASIS.—In any case where the annuity payments are not made on a monthly basis, appropriate adjustments in the application of this paragraph shall be made to take into account the period on the basis of which such payments are made.

(G) QUALIFIED EMPLOYER RETIREMENT PLAN.—For purposes of this paragraph, the term "qualified employer retirement plan" means any plan or contract described in paragraph (1), (2), or (3) of section 4974(c).

(2) TREATMENT OF EMPLOYEE CONTRIBUTIONS UNDER DEFINED CONTRIBUTION PLANS.—For purposes of this section, employee contributions (and any income allocable thereto) under a defined contribution plan may be treated as a separate contract.

* * * * * * *

(m) SPECIAL RULES APPLICABLE TO EMPLOYEE ANNUITIES AND DISTRIBUTIONS UNDER EMPLOYEE PLANS.—

(2) COMPUTATION OF CONSIDERATION PAID BY THE EMPLOYEE.—In computing—

(A) the aggregate amount of premiums or other consideration paid for the contract for purposes of subsection (c)(1)(A) (relating to the investment in the contract), *and*

[(B) the consideration for the contract contributed by the employee for purposes of subsection (d)(1) (relating to employee's contributions recoverable in 3 years) and subsection (e)(7) (relating to plans where substantially all contributions are employee contributions), and]

[(C)] *(B)* the aggregate premiums or other consideration paid for purposes of subsection (e)(6) (relating to certain amounts not received as an annuity),

any amount allowed as a deduction with respect to the contract under section 404 which was paid while the employee was an employee within the meaning of section 401(c)(1) shall be treated as consideration contributed by the employer, and there shall not be taken into account any portion of the premiums or other consideration for the contract paid while the employee was an owner-employee which is properly allocable (as determined under regulations prescribed by the Secretary) to the cost of life, accident, health, or other insurance.

* * * * * * *

(p) LOANS TREATED AS DISTRIBUTIONS.—For purposes of this section—

(1) * * *

* * * * * * *

(4) QUALIFIED EMPLOYER PLAN, ETC.— For purposes of this subsection—

(A) QUALIFIED EMPLOYER PLAN.—

(i) * * *

[(ii) SPECIAL RULES.—The term "qualified employer plan"—

[(I) shall include any plan which was (or was determined to be) a qualified employer plan or a government plan, but

[(II) shall not include a plan described in subsection (e)(7).]

(ii) SPECIAL RULE.—The term "qualified employer plan" shall not include any plan which was (or was determined to be) a qualified employer plan or a government plan.

* * * * * * *

(t) 10-PERCENT ADDITIONAL TAX ON EARLY DISTRIBUTIONS FROM QUALIFIED RETIREMENT PLANS.—

(1) * * *

* * * * * * *

(6) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—In the case of any amount received from a simple retirement account (within the meaning of section 408(p)) during the 2-year period beginning on the date such individual first participated in any qualified salary reduction arrangement maintained by the individual's employer under section 408(p)(2), paragraph (1) shall be applied by substituting "25 percent" for "10 percent".

* * * * * * *

SEC. 86. SOCIAL SECURITY AND TIER 1 RAILROAD RETIREMENT BENEFITS.

(a) * * *

(b) TAXPAYERS TO WHOM SUBSECTION (a) APPLIES.—

(1) * * *

(2) MODIFIED ADJUSTED GROSS INCOME.—For purposes of this subsection, the term "modified adjusted gross income" means [adusted] *adjusted* gross income—

(A) determined without regard to this section and sections 135, *137,* 911, 931, and 933, and

(B) increased by the amount of interest received or accrued by the taxpayer during the taxable year which is exempt from tax.

* * * * * * *

PART III—ITEMS SPECIFICALLY EXCLUDED IN GROSS INCOME

Sec. 101. Certain death benefits.

* * * * * * *

Sec 112. Certain [combat pay] *combat zone compensation* of members of the armed forces.

* * * * * * *

[Sec. 133. Interest on certain loans used to acquire employer securities.]

* * * * * * *

SEC. 101. CERTAIN DEATH BENEFITS.

(a) * * *

[(b) EMPLOYEES' DEATH BENEFITS.—

[(1) GENERAL RULE.—Gross income does not include amounts received (whether in a single sum or otherwise) by the beneficiaries or the estate of an employee, if such amounts are paid by or on behalf of an employer and are paid by reason of the death of the employee.

[(2) SPECIAL RULES FOR PARAGRAPH (1).—

[(A) $5,000 LIMITATION.—The aggregate amounts excludable under paragraph (1) with respect to the death of any employee shall not exceed $5,000.

[(B) NONFORFEITABLE RIGHTS.—Paragraph (1) shall not apply to amounts with respect to which the employee possessed, immediately before his death, a nonforfeitable right to receive the amounts while living. This subparagraph shall not apply to a lump sum distribution (as defined in section 402(e)(4))—

[(i) by a stock bonus, pension, or profit-sharing trust described in section 401(a) which is exempt from tax under section 501(a),

[(ii) under an annuity contract under a plan described in section 403(a), or

[(iii) under an annuity contract purchased by an employer which is an organization referred to in section 170(b)(1)(A) (ii) or (vi) or which is a religious organization (other than a trust) and which is exempt from tax under section 501(a), but only with respect to that portion of such total distributions payable which bears the same ratio to the amount of such total distributions payable which is (without regard to this subsection) includible in gross income, as the amounts contributed by the employer for such annuity contract

which are excludable from gross income under section 403(b) bear to the total amounts contributed by the employer for such annuity contract.

[(C) JOINT AND SURVIVOR ANNUITIES.—Paragraph (1) shall not apply to amounts received by a surviving annuitant under a joint and survivor's annuity contract after the first day of the first period for which an amount was received as an annuity by the employee (or would have been received if the employee had lived).

[(D) OTHER ANNUITIES.—In the case of any amount to which section 72 (relating to annuities, etc.) applies, the amount which is excludable under paragraph (1) (as modified by the preceding subparagraphs of this paragraph) shall be determined by reference to the value of such amount as of the day on which the employee died. Any amount so excludable under paragraph (1) shall, for purposes of section 72, be treated as additional consideration paid by the employee. Paragraph (1) shall not apply in the case of an annuity under chapter 73 of title 10 of the United States Code if the member or former member of the uniformed services by reason of whose death such annuity is payable died after attaining retirement age.

[(3) TREATMENT OF SELF-EMPLOYED INDIVIDUALS.—For purposes of this subsection—

[(A) SELF-EMPLOYED INDIVIDUAL NOT CONSIDERED EMPLOYEE.—Except as provided in subparagraph (B), the term "employee" does not include a self-employed individual described in section 401(c)(1).

[(B) SPECIAL RULE FOR CERTAIN DISTRIBUTIONS.—In the case of any amount paid or distributed—

[(i) by a trust described in section 401(a) which is exempt from tax under section 501(a), or

[(ii) under a plan described in section 403(a), the term "employee" includes a self-employed individual described in section 401(c)(1).]

(c) INTEREST.—If any amount excluded from gross income by [subsection (a) or (b)] *subsection (a)* is held under an agreement to pay interest thereon, the interest payments shall be included in gross income.

* * * * * * *

SEC. 104. COMPENSATION FOR INJURIES OR SICKNESS.

(a) IN GENERAL.—Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 213 (relating to medical, etc., expenses) for any prior taxable year, gross income does not include—

(1) amounts received under workmen's compensation acts as compensation for personal injuries or sickness;

[(2) the amount of any damages received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal injuries or sickness;]

(2) the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump

sums or as periodic payments) on account of personal physical injuries or physical sickness;

(3) * * *

* * * * * * *

For purposes of paragraph (3), in the case of an individual who is, or has been, an employee within the meaning of section 401(c)(1) (relating to self-employed individuals), contributions made on behalf of such individual while he was such an employee to a trust described in section 401(a) which is exempt from tax under section 501(a), or under a plan described in section 403(a), shall, to the extent allowed as deductions under section 404, be treated as contributions by the employer which were not includible in the gross income of the employee. [Paragraph (2) shall not apply to any punitive damages in connection with a case not involving physical injury or physical sickness.] *For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. The preceding sentence shall not apply to an amount of damages not in excess of the amount paid for medical care (described in subparagraph (A) or (B) of section 213(d)(1)) attributable to emotional distress.*

* * * * * * *

(c) RESTRICTION ON PUNITIVE DAMAGES NOT TO APPLY IN CERTAIN CASES.—The restriction on the application of subsection (a)(2) to punitive damages shall not apply to punitive damages awarded in a civil action—

(1) which is a wrongful death action, and

(2) with respect to which applicable State law (as in effect on September 13, 1995 and without regard to any modification after such date) provides, or has been construed to provide by a court of competent jurisdiction pursuant to a decision issued on or before September 13, 1995, that only punitive damages may be awarded in such an action.

This subsection shall cease to apply to any civil action filed on or after the first date on which the applicable State law ceases to provide (or is no longer construed to provide) the treatment described in paragraph (2).

[(c)] *(d)* CROSS REFERENCES.—

(1) For exclusion from employee's gross income of employer contributions to accident and health plans, see section 106.

(2) For exclusion of part of disability retirement pay from the application of subsection (a)(4) of this section, see section 1403 of title 10, United States Code (relating to career compensation laws).

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SEC. 108. INCOME FROM DISCHARGE OF INDEBTEDNESS.

(a) * * *

* * * * * * *

(d) MEANING OF TERMS; SPECIAL RULES RELATING TO CERTAIN PROVISIONS.—

(1) * * *

* * * * * * *

(9) TIME FOR MAKING ELECTION, ETC.—

(A) TIME.—An election under paragraph (5) of subsection (b) or under [paragraph (3)(B)] *paragraph (3)(C)* of subsection (c) shall be made on the taxpayer's return for the taxable year in which the discharge occurs or at such other time as may be permitted in regulations prescribed by the Secretary.

* * * * * * *

SEC. 112. CERTAIN [COMBAT PAY] *COMBAT ZONE COMPENSATION* OF MEMBERS OF THE ARMED FORCES.

(a) * * *

* * * * * * *

SEC. 117. QUALIFIED SCHOLARSHIPS.

(a) * * *

* * * * * * *

(d) QUALIFIED TUITION REDUCTION.—

(1) * * *

(2) QUALIFIED TUITION REDUCTION.—For purposes of this subsection, the term "qualified tuition reduction" means the amount of any reduction in tuition provided to an employee of an organization described in section 170(b)(1)(A)(ii) for the education (below the graduate level) at such organization (or another organization described in section 170(b)(1)(A)(ii)) of—

(A) such employee, or

(B) any person treated as an employee (or whose use is treated as an employee use) under the rules of [section 132(f)] *section 132(h).*

* * * * * * *

SEC. 127. EDUCATIONAL ASSISTANCE PROGRAMS.

(a) * * *

* * * * * * *

(c) DEFINITIONS; SPECIAL RULES.—For purposes of this section—

(1) EDUCATIONAL ASSISTANCE.—The term "educational assistance" means—

(A) the payment, by an employer, of expenses incurred by or on behalf of an employee for education of the employee (including, but not limited to, tuition, fees, and similar payments, books, supplies, and equipment), and

(B) the provision, by an employer, of courses of instruction for such employee (including books, supplies, and equipment),but does not include payment for, or the provision of, tools or supplies which may be retained by the employee after completion of a course of instruction, or meals, lodging, or transportation. The term "educational assistance" also does not include any payment for, or the provision of any benefits with respect to, any course or other education involving sports, games, or hobbies *or at the graduate level.*

* * * * * * *

(d) TERMINATION.—This section shall not apply to taxable years beginning after [December 31, 1994] *December 31, 1996.*

* * * * * * *

SEC. 129. DEPENDENT CARE ASSISTANCE PROGRAMS.

(a) * * *

* * * * * * *

(d) DEPENDENT CARE ASSISTANCE PROGRAM.—

(1) * * *

* * * * * * *

(8) BENEFITS.—

(A) * * *

(B) SALARY REDUCTION AGREEMENTS.—For purposes of subparagraph (A), in the case of any benefits provided through a salary reduction agreement, a plan may disregard any employees whose compensation is less than $25,000. For purposes of this subparagraph, the term "compensation" has the meaning given such term by [section 414(q)(7)] *section 414(q)(4)*, except that, under rules prescribed by the Secretary, an employer may elect to determine compensation on any other basis which does not discriminate in favor of highly compensated employees.

* * * * * * *

[SEC. 133. INTEREST ON CERTAIN LOANS USED TO ACQUIRE EMPLOYER SECURITIES.

[(a) IN GENERAL.—Gross income does not include 50 percent of the interest received by—

[(1) a bank (within the meaning of section 581),

[(2) an insurance company to which subchapter L applies,

[(3) a corporation actively engaged in the business of lending money, or

[(4) a regulated investment company (as defined in section 851),

with respect to a securities acquisition loan.

[(b) SECURITIES ACQUISITION LOAN.—

[(1) IN GENERAL.—For purposes of this section, the term "securities acquisition loan" means—

[(A) any loan to a corporation or to an employee stock ownership plan to the extent that the proceeds are used to acquire employer securities for the plan, or

[(B) any loan to a corporation to the extent that, within 30 days, employer securities are transferred to the plan in an amount equal to the proceeds of such loan and such securities are allocable to accounts of plan participants within 1 year of the date of such loan.

For purposes of this paragraph, the term "employer securities" has the meaning given such term by section 409(l). The term "securities acquisition loan" shall not include a loan with a term greater than 15 years.

[(2) LOANS BETWEEN RELATED PERSONS.—The term "securities acquisition loan" shall not include—

[(A) any loan made between corporations which are members of the same controlled group of corporations, or

[(B) any loan made between an employee stock ownership plan and any person that is—

[(i) the employer of any employees who are covered by the plan; or

[(ii) a member of a controlled group of corporations which includes such employer.

For purposes of this paragraph, subparagraphs (A) and (B) shall not apply to any loan which, but for such subparagraphs, would be a securities acquisition loan if such loan was not originated by the employer of any employees who are covered by the plan or by any member of the controlled group of corporations which includes such employer, except that this section shall not apply to any interest received on such loan during such time as such loan is held by such employer (or any member of such controlled group).

[(3) TERMS APPLICABLE TO CERTAIN SECURITIES ACQUISITION LOANS.—A loan to a corporation shall not fail to be treated as a securities acquisition loan merely because the proceeds of such loan are lent to an employee stock ownership plan sponsored by such corporation (or by any member of the controlled group of corporations which includes such corporation) if such loan includes—

[(A) repayment terms which are substantially similar to the terms of the loan of such corporation from a lender described in subsection (a), or

[(B) repayment terms providing for more rapid repayment of principal or interest on such loan, but only if allocations under the plan attributable to such repayment do not discriminate in favor of highly compensated employees (within the meaning of section 414(q)).

[(4) CONTROLLED GROUP OF CORPORATIONS.—For purposes of this paragraph, the term "controlled group of corporations" has the meaning given such term by section 409(l)(4).

[(5) TREATMENT OF REFINANCINGS.—The term "securities acquisition loan" shall include any loan which—

[(A) is (or is part of a series of loans) used to refinance a loan described in subparagraph (A) or (B) of paragraph (1), and

[(B) meets the requirements of paragraphs (2) and (3).

[(6) PLAN MUST HOLD MORE THAN 50 PERCENT OF STOCK AFTER ACQUISITION OR TRANSFER.—

[(A) IN GENERAL.—A loan shall not be treated as a securities acquisition loan for purposes of this section unless, immediately after the acquisition or transfer referred to in subparagraph (A) or (B) of paragraph (1), respectively, the employee stock ownership plan owns more than 50 percent of—

[(i) each class of outstanding stock of the corporation issuing the employer securities, or

[(ii) the total value of all outstanding stock of the corporation.

[(B) FAILURE TO RETAIN MINIMUM STOCK INTEREST.—

[(i) IN GENERAL.—Subsection (a) shall not apply to any interest received with respect to a securities acquisition loan which is allocable to any period during which the employee stock ownership plan does not own stock meeting the requirements of subparagraph (A).

[(ii) EXCEPTION.—To the extent provided by the Secretary, clause (i) shall not apply to any period if, within 90 days of the first date on which the failure occurred (or such longer period not in excess of 180 days as the Secretary may prescribe), the plan acquires stock which results in its meeting the requirements of subparagraph (A).

[(C) STOCK.—For purposes of subparagraph (A)—

[(i) IN GENERAL.—The term "stock" means stock other than stock described in section 1504(a)(4).

[(ii) TREATMENT OF CERTAIN RIGHTS.—The Secretary may provide that warrants, options, contracts to acquire stock, convertible debt interests and other similar interests be treated as stock for 1 or more purposes under subparagraph (A).

[(D) AGGREGATION RULE.—For purposes of determining whether the requirements of subparagraph (A) are met, an employee stock ownership plan shall be treated as owning stock in the corporation issuing the employer securities which is held by any other employee stock ownership plan which is maintained by—

[(i) the employer maintaining the plan, or

[(ii) any member of a controlled group of corporations (within the meaning of section 409(l)(4)) of which the employer described in clause (i) is a member.

[(7) VOTING RIGHTS OF EMPLOYER SECURITIES.—A loan shall not be treated as a securities acquisition loan for purposes of this section unless—

[(A) the employee stock ownership plan meets the requirements of section 409(e)(2) with respect to all employer securities acquired by, or transferred to, the plan in connection with such loan (without regard to whether or not the employer has a registration-type class of securities), and

[(B) no stock described in section 409(l)(3) is acquired by, or transferred to, the plan in connection with such loan unless—

[(i) such stock has voting rights equivalent to the stock to which it may be converted, and

[(ii) the requirements of subparagraph (A) are met with respect to such voting rights.

[(c) EMPLOYEE STOCK OWNERSHIP PLAN.—For purposes of this section, the term "employee stock ownership plan" has the meaning given to such term by section 4975(e)(7).

[(d) APPLICATION WITH SECTION 483 and Original Issue Discount Rules.—In applying section 483 and subpart A of part V of subchapter P to any obligation to which this section applies, appro-

priate adjustments shall be made to the applicable Federal rate to take into account the exclusion under subsection (a).

[(e) PERIOD TO WHICH INTEREST EXCLUSION APPLIES.—

[(1) IN GENERAL.—In the case of—

[(A) an original securities acquisition loan, and

[(B) any securities acquisition loan (or series of such loans) used to refinance the original securities acquisition loan, subsection (a) shall apply only to interest accruing during the excludable period with respect to the original securities acquisition loan.

[(2) EXCLUDABLE PERIOD.—For purposes of this subsection, the term "excludable period" means, with respect to any original securities acquisition loan—

[(A) IN GENERAL.—The 7-year period beginning on the date of such loan.

[(B) LOANS DESCRIBED IN SUBSECTION (b)(1)(A).—If the term of an original securities acquisition loan described in subsection (b)(1)(A) is greater than 7 years, the term of such loan. This subparagraph shall not apply to a loan described in subsection (b)(3)(B).

[(3) ORIGINAL SECURITIES ACQUISITION LOAN.—For the purposes of this subsection, the term "original securities acquisition loan" means a securities acquisition loan described in subparagraph (A) or (B) of subsection (b)(1).]

* * * * * * *

SEC. 135. INCOME FROM UNITED STATES SAVINGS BONDS USED TO PAY HIGHER EDUCATION TUITION AND FEES.

(a) * * *

(b) LIMITATIONS.—

(1) * * *

(2) LIMITATION BASED ON MODIFIED ADJUSTED GROSS INCOME.—

(A) * * *

(B) INFLATION ADJUSTMENT.—In the case of any taxable year beginning in a calendar year after 1990, the $40,000 and $60,000 amounts contained in subparagraph (A) shall be increased by an amount equal to—

(i) such dollar amount, multiplied by

(ii) the cost-of-living adjustment under section 1(f)(3) for the calendar year in which the taxable year begins, *determined by substituting "calendar year 1989" for "calendar year 1992" in subparagraph (B) thereof.*

* * * * * * *

PART IV—TAX EXEMPTION REQUIREMENTS FOR STATE AND LOCAL BONDS

* * * * * * *

Subpart A—Private Activity Bonds

* * * * * * *

SEC. 143. MORTGAGE REVENUE BONDS: QUALIFIED MORTGAGE BOND AND QUALIFIED VETERANS' MORTGAGE BOND.

(a) * * *

* * * * * * *

(d) 3-YEAR REQUIREMENT.—

(1) * * *

(2) EXCEPTIONS.—For purposes of paragraph (1), the proceeds of an issue which are used to provide—

(A) financing with respect to targeted area residences,

(B) qualified home improvement loans and qualified rehabilitation loans, and

(C) financing with respect to land described in subsection (i)(1)(C) and the construction of any residence thereon[.],

shall be treated as used as described in paragraph (1).

* * * * * * *

(m) RECAPTURE OF PORTION OF FEDERAL SUBSIDY FROM USE OF QUALIFIED MORTGAGE BONDS AND MORTGAGE CREDIT CERTIFICATES.—

(1) * * *

* * * * * * *

(4) RECAPTURE AMOUNT.—For purposes of this subsection—

(A) * * *

* * * * * * *

(C) HOLDING PERIOD PERCENTAGE.—

(i) * * *

(ii) RETIREMENTS OF INDEBTEDNESS.—If the federally-subsidized indebtedness is completely repaid during [any month of the 10-year period] *any year of the 4-year period* beginning on the testing date, the holding period percentage for [succeeding months] *succeeding years* shall be determined by reducing ratably [over the remainder of such period (or, if lesser, 5 years)] *to zero over the succeeding 5 years* the holding period percentage which would have been determined under this subparagraph had the taxpayer disposed of his interest in the residence on the date of the repayment.

* * * * * * *

SEC. 149. BONDS MUST BE REGISTERED TO BE TAX EXEMPT; OTHER REQUIREMENTS.

(a) * * *

* * * * * * *

(g) TREATMENT OF HEDGE BONDS.—

(1) * * *

* * * * * * *

(3) HEDGE BOND.—

(A) * * *

(B) EXCEPTION FOR INVESTMENT IN TAX-EXEMPT BONDS NOT SUBJECT TO MINIMUM TAX.—

(i) * * *

* * * * * * *

[(iii) INVESTMENT EARNINGS HELD PENDING REINVESTMENT.—Investment earnings held for not more than 30 days pending reinvestment shall be treated as invested in bonds described in clause (i).]

(iii) AMOUNTS HELD PENDING REINVESTMENT OR REDEMPTION.—Amounts held for not more than 30 days pending reinvestment or bond redemption shall be treated as invested in bonds described in clause (i).

* * * * * * *

PART V—DEDUCTIONS FOR PERSONAL EXEMPTIONS

* * * * * * *

SEC. 151. ALLOWANCE OF DEDUCTIONS FOR PERSONAL EXEMPTIONS.

(a) * * *

* * * * * * *

(d) EXEMPTION AMOUNT.—For purposes of this section—

(1) * * *

* * * * * * *

(3) PHASEOUT.—

(A) * * *

* * * * * * *

(C) THRESHOLD AMOUNT.—For purposes of this paragraph, the term "threshold amount" means—

(i) $150,000 in the case of a [joint of a return] *joint return* or a surviving spouse (as defined in section 2(a)),

* * * * * * *

PART VI—ITEMIZED DEDUCTIONS FOR INDIVIDUALS AND CORPORATIONS

* * * * * * *

SEC. 162. TRADE OR BUSINESS EXPENSES.

(a) * * *

* * * * * * *

(k) STOCK [REDEMPTION] *REACQUISITION* EXPENSES.—

(1) IN GENERAL.—Except as provided in paragraph (2), no deduction otherwise allowable shall be allowed under this chapter for any amount paid or incurred by a corporation in connection with [the redemption of its stock] *the reacquisition of its stock or of the stock of any related person (as defined in section 465(b)(3)(C)).*

(2) EXCEPTIONS.—Paragraph (1) shall not apply to—

(A) CERTAIN SPECIFIC DEDUCTIONS.—Any—

(i) deduction allowable under section 163 (relating to interest), [or]

SEC. 143. MORTGAGE REVENUE BONDS: QUALIFIED MORTGAGE BOND AND QUALIFIED VETERANS' MORTGAGE BOND.

(a) * * *

* * * * * * *

(d) 3-YEAR REQUIREMENT.—

(1) * * *

(2) EXCEPTIONS.—For purposes of paragraph (1), the proceeds of an issue which are used to provide—

(A) financing with respect to targeted area residences,

(B) qualified home improvement loans and qualified rehabilitation loans, and

(C) financing with respect to land described in subsection (i)(1)(C) and the construction of any residence thereon[.],

shall be treated as used as described in paragraph (1).

* * * * * * *

(m) RECAPTURE OF PORTION OF FEDERAL SUBSIDY FROM USE OF QUALIFIED MORTGAGE BONDS AND MORTGAGE CREDIT CERTIFICATES.—

(1) * * *

* * * * * * *

(4) RECAPTURE AMOUNT.—For purposes of this subsection—

(A) * * *

* * * * * * *

(C) HOLDING PERIOD PERCENTAGE.—

(i) * * *

(ii) RETIREMENTS OF INDEBTEDNESS.—If the federally-subsidized indebtedness is completely repaid during [any month of the 10-year period] *any year of the 4-year period* beginning on the testing date, the holding period percentage for [succeeding months] *succeeding years* shall be determined by reducing ratably [over the remainder of such period (or, if lesser, 5 years)] *to zero over the succeeding 5 years* the holding period percentage which would have been determined under this subparagraph had the taxpayer disposed of his interest in the residence on the date of the repayment.

* * * * * * *

SEC. 149. BONDS MUST BE REGISTERED TO BE TAX EXEMPT; OTHER REQUIREMENTS.

(a) * * *

* * * * * * *

(g) TREATMENT OF HEDGE BONDS.—

(1) * * *

* * * * * * *

(3) HEDGE BOND.—

(A) * * *

(B) EXCEPTION FOR INVESTMENT IN TAX-EXEMPT BONDS NOT SUBJECT TO MINIMUM TAX.—

(i) * * *

* * * * * * *

[(iii) INVESTMENT EARNINGS HELD PENDING REINVESTMENT.—Investment earnings held for not more than 30 days pending reinvestment shall be treated as invested in bonds described in clause (i).]

(iii) AMOUNTS HELD PENDING REINVESTMENT OR REDEMPTION.—Amounts held for not more than 30 days pending reinvestment or bond redemption shall be treated as invested in bonds described in clause (i).

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PART V—DEDUCTIONS FOR PERSONAL EXEMPTIONS

* * * * * * *

SEC. 151. ALLOWANCE OF DEDUCTIONS FOR PERSONAL EXEMPTIONS.

(a) * * *

* * * * * * *

(d) EXEMPTION AMOUNT.—For purposes of this section—

(1) * * *

* * * * * * *

(3) PHASEOUT.—

(A) * * *

* * * * * * *

(C) THRESHOLD AMOUNT.—For purposes of this paragraph, the term "threshold amount" means—

(i) $150,000 in the case of a [joint of a return] *joint return* or a surviving spouse (as defined in section 2(a)),

* * * * * * *

PART VI—ITEMIZED DEDUCTIONS FOR INDIVIDUALS AND CORPORATIONS

* * * * * * *

SEC. 162. TRADE OR BUSINESS EXPENSES.

(a) * * *

* * * * * * *

(k) STOCK [REDEMPTION] *REACQUISITION* EXPENSES.—

(1) IN GENERAL.—Except as provided in paragraph (2), no deduction otherwise allowable shall be allowed under this chapter for any amount paid or incurred by a corporation in connection with [the redemption of its stock] *the reacquisition of its stock or of the stock of any related person (as defined in section 465(b)(3)(C)).*

(2) EXCEPTIONS.—Paragraph (1) shall not apply to—

(A) CERTAIN SPECIFIC DEDUCTIONS.—Any—

(i) deduction allowable under section 163 (relating to interest), [or]

(ii) deduction for amounts which are properly allocable to indebtedness and amortized over the term of such indebtedness, or

[(ii)] *(iii)* deduction for dividends paid (within the meaning of section 561).

(B) STOCK OF CERTAIN REGULATED INVESTMENT COMPANIES.—Any amount paid or incurred in connection with the redemption of any stock in a regulated investment company which issues only stock which is redeemable upon the demand of the shareholder.

* * * * * * *

SEC. 163. INTEREST.

(a) * * *

* * * * * * *

(j) LIMITATION OF DEDUCTION FOR INTEREST ON CERTAIN INDEBTEDNESS.—

(1) LIMITATION.—

(A) * * *

(B) DISALLOWED AMOUNT CARRIED TO SUCCEEDING TAXABLE YEAR.—Any amount disallowed under subparagraph (A) for any taxable year shall be treated as disqualified interest paid or accrued in the succeeding taxable year *(and clause (ii) of paragraph (2)(A) shall not apply for purposes of applying this subsection to the amount so treated).*

* * * * * * *

(6) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—

(A) * * *

* * * * * * *

(E) GROSS BASIS AND NET BASIS TAXATION.—

(i) GROSS BASIS TAX.—The term "gross basis tax" means any tax imposed by this subtitle which is determined by reference to the gross amount of any item of income without any reduction for any deduction allowed by this subtitle.

(ii) NET BASIS TAX.—The term "net basis tax" means any tax imposed by this subtitle which is [a] not a gross basis tax.

(7) COORDINATION WITH PASSIVE LOSS RULES, ETC.—This subsection shall be applied before sections 465 and 469.

[(7)] *(8)* REGULATIONS.—The Secretary shall prescribe such regulations as may be appropriate to carry out the purposes of this subsection, including—

(A) such regulations as may be appropriate to prevent the avoidance of the purposes of this subsection,

* * * * * * *

SEC. 164. TAXES.

(a) GENERAL RULE.—Except as otherwise provided in this section, the following taxes shall be allowed as a deduction for the taxable year within which paid or accrued:

(1) State and local, and foreign, real property taxes.

(2) State and local personal property taxes.

(3) State and local, and foreign, income, war profits, and excess profits taxes.

[(4) The environmental tax imposed by section 59A.

[(5) The GST tax imposed on income distributions.]

(4) The GST tax imposed on income distributions.

(5) The environmental tax imposed by section 59A.

In addition, there shall be allowed as a deduction State and local, and foreign, taxes not described in the preceding sentence which are paid or accrued within the taxable year in carrying on a trade or business or an activity described in section 212 (relating to expenses for production of income). Notwithstanding the preceding sentence, any tax (not described in the first sentence of this subsection) which is paid or accrued by the taxpayer in connection with an acquisition or disposition of property shall be treated as part of the cost of the acquired property or, in the case of a disposition, as a reduction in the amount realized on the disposition.

* * * * * * *

SEC. 167. DEPRECIATION.

(a) * * *

* * * * * * *

(g) DEPRECIATION UNDER INCOME FORECAST METHOD.—

(1) IN GENERAL.—If the depreciation deduction allowable under this section to any taxpayer with respect to any property is determined under the income forecast method or any similar method—

(A) the income from the property to be taken into account in determining the depreciation deduction under such method shall be equal to the amount of income earned in connection with the property before the close of the 10th taxable year following the taxable year in which the property was placed in service,

(B) the adjusted basis of the property shall only include amounts with respect to which the requirements of section 461(h) are satisfied,

(C) the depreciation deduction under such method for the 10th taxable year beginning after the taxable year in which the property was placed in service shall be equal to the adjusted basis of such property as of the beginning of such 10th taxable year, and

(D) such taxpayer shall pay (or be entitled to receive) interest computed under the look-back method of paragraph (2) for any recomputation year.

(2) LOOK-BACK METHOD.—The interest computed under the look-back method of this paragraph for any recomputation year shall be determined by—

(A) first determining the depreciation deductions under this section with respect to such property which would have been allowable for prior taxable years if the determination of the amounts so allowable had been made on the basis of the sum of the following (instead of the estimated income from such property)—

(i) the actual income earned in connection with such property for periods before the close of the recomputation year, and

(ii) an estimate of the future income to be earned in connection with such property for periods after the recomputation year and before the close of the 10th taxable year following the taxable year in which the property was placed in service,

(B) second, determining (solely for purposes of computing such interest) the overpayment or underpayment of tax for each such prior taxable year which would result solely from the application of subparagraph (A), and

(C) then using the adjusted overpayment rate (as defined in section 460(b)(7)), compounded daily, on the overpayment or underpayment determined under subparagraph (B).

For purposes of the preceding sentence, any cost incurred after the property is placed in service (which is not treated as a separate property under paragraph (5)) shall be taken into account by discounting (using the Federal mid-term rate determined under section 1274(d) as of the time such cost is incurred) such cost to its value as of the date the property is placed in service. The taxpayer may elect with respect to any property to have the preceding sentence not apply to such property.

(3) EXCEPTION FROM LOOK-BACK METHOD.—Paragraph (1)(D) shall not apply with respect to any property which, when placed in service by the taxpayer, had a basis of $100,000 or less.

(4) RECOMPUTATION YEAR.—For purposes of this subsection, except as provided in regulations, the term "recomputation year" means, with respect to any property, the 3d and the 10th taxable years beginning after the taxable year in which the property was placed in service, unless the actual income earned in connection with the property for the period before the close of such 3d or 10th taxable year is within 10 percent of the income earned in connection with the property for such period which was taken into account under paragraph (1)(A).

(5) SPECIAL RULES.—

(A) CERTAIN COSTS TREATED AS SEPARATE PROPERTY.—For purposes of this subsection, the following costs shall be treated as separate properties:

(i) Any costs incurred with respect to any property after the 10th taxable year beginning after the taxable year in which the property was placed in service.

(ii) Any costs incurred after the property is placed in service and before the close of such 10th taxable year if such costs are significant and give rise to a significant increase in the income from the property which was not included in the estimated income from the property.

(B) SYNDICATION INCOME FROM TELEVISION SERIES.—In the case of property which is an episode in a television series, income from syndicating such series shall not be required to be taken into account under this subsection before the earlier of—

(i) the 4th taxable year beginning after the date the first episode in such series is placed in service, or

(ii) the earliest taxable year in which the taxpayer has an arrangement relating to the future syndication of such series.

(C) SPECIAL RULES FOR FINANCIAL EXPLOITATION OF CHARACTERS, ETC.—For purposes of this subsection, in the case of television and motion picture films, the income from the property shall include income from the exploitation of characters, designs, scripts, scores, and other incidental income associated with such films, but only to the extent that such income is earned in connection with the ultimate use of such items by, or the ultimate sale of merchandise to, persons who are not related persons (within the meaning of section 267(b)) to the taxpayer.

(D) COLLECTION OF INTEREST.—For purposes of subtitle F (other than sections 6654 and 6655), any interest required to be paid by the taxpayer under paragraph (1) for any recomputation year shall be treated as an increase in the tax imposed by this chapter for such year.

(E) DETERMINATIONS.—For purposes of paragraph (2), determinations of the amount of income earned in connection with any property shall be made in the same manner as for purposes of applying the income forecast method; except that any income from the disposition of such property shall be taken into account.

(F) TREATMENT OF PASS-THRU ENTITIES.—Rules similar to the rules of section 460(b)(4) shall apply for purposes of this subsection.

[(g)] *(h)* CROSS REFERENCES.—

(1) * * *

* * * * * * *

SEC. 168. ACCELERATED COST RECOVERY SYSTEM.

(a) * * *

* * * * * * *

(e) CLASSIFICATION OF PROPERTY.—For purposes of this section—

(1) * * *

* * * * * * *

(3) CLASSIFICATION OF CERTAIN PROPERTY.—

(A) * * *

(B) 5-YEAR PROPERTY.—The term "5-year property" includes—

(i) any automobile or light general purpose truck,

(ii) any semi-conductor manufacturing equipment,

(iii) any computer-based telephone central office switching equipment,

(iv) any qualified technological equipment,

(v) any section 1245 property used in connection with research and experimentation, and

(vi) any property which—

(I) is described in subparagraph (A) of section 48(a)(3) (or would be so described if "solar and

wind" were substituted for "solar" in clause (i) thereof, [or]

(II) is described in paragraph (15) of section 48(l) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990) and is a qualifying small power production facility within the meaning of section 3(17)(C) of the Federal Power Act (16 U.S.C. 796(17)(C)), as in effect on September 1, 1986[.], *or*

(III) is described in section 48(l)(3)(A)(ix) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990).

Nothing in any provision of law shall be construed to treat property as not being described in clause (vi)(I) (or the corresponding provisions of prior law) by reason of being public utility property (within the meaning of section 48(a)(3)).

* * * * * * *

(g) ALTERNATIVE DEPRECIATION SYSTEM FOR CERTAIN PROPERTY

(1) * * *

* * * * * * *

(4) EXCEPTION FOR CERTAIN PROPERTY USED OUTSIDE UNITED STATES.—Subparagraph (A) of paragraph (1) shall not apply to—

(A) * * *

* * * * * * *

(K) any property described in [section 48(a)(3)(A)(iii)] *section 48(l)(3)(A)(ix) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)* which is owned by a United States person and which is used in international or territorial waters to generate energy for use in the United States; and

* * * * * * *

SEC. 172. NET OPERATING LOSS DEDUCTION.

(a) * * *

(b) NET OPERATING LOSS CARRYBACKS AND CARRYOVERS.—

(1) YEARS TO WHICH LOSS MAY BE CARRIED.—

(A) * * *

* * * * * * *

(E) EXCESS INTEREST LOSS.—

(i) * * *

(ii) LOSS LIMITATION YEAR.—For purposes of clause (i) and [subsection (m)] *subsection (h)*, the term "loss limitation year" means, with respect to any corporate equity reduction transaction, the taxable year in which such transaction occurs and each of the 2 succeeding taxable years.

* * * * * * *

(h) CORPORATE EQUITY REDUCTION INTEREST LOSSES.—For purposes of this section—

(1) * * *

* * * * * * *

(3) CORPORATE EQUITY REDUCTION TRANSACTION.—

(A) * * *

(B) MAJOR STOCK ACQUISITION.—

(i) IN GENERAL.—The term "major stock acquisition" means the acquisition by a corporation pursuant to a plan of such corporation (or any group of persons acting in concert with such corporation) of stock in another corporation representing 50 percent or more (by vote or value) of the stock in such other corporation[,].

* * * * * * *

(4) OTHER RULES.—

(A) * * *

(B) COORDINATION WITH SUBSECTION (b)(2).—[For purposes of subsection (b)(2)—] *For purposes of subsection (b)(2)—*

(i) a corporate equity reduction interest loss shall be treated in a manner similar to the manner in which a specified liability loss is treated, and

(ii) in determining the net operating loss deduction for any prior taxable year referred to in the 3rd sentence of subsection (b)(2), the portion of any net operating loss which may not be carried to such taxable year under subsection (b)(1)(E) shall not be taken into account.

(C) MEMBERS OF AFFILIATED GROUPS.—Except as provided by regulations, all members of an affiliated group filing a consolidated return under section 1501 shall be treated as 1 taxpayer for purposes of this subsection and [subsection (b)(1)(M)] *subsection (b)(1)(E).*

* * * * * * *

SEC. 179. ELECTION TO EXPENSE CERTAIN DEPRECIABLE BUSINESS ASSETS.

(a) * * *

(b) LIMITATIONS.—

[(1) DOLLAR LIMITATION.—The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed $17,500.]

(1) DOLLAR LIMITATION.—The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed the following applicable amount:

If the taxable year begins in:	*The applicable amount is:*
1996	*$18,500*
1997	*19,000*
1998	*20,000*
1999	*21,000*
2000	*22,000*
2001	*23,000*

2002	*23,500*
2003 or thereafter	*25,000.*

* * * * * * *

(d) DEFINITIONS AND SPECIAL RULES.—

(1) SECTION 179 PROPERTY.—For purposes of this section, the term "section 179 property" means any tangible property (to which section 168 applies) which is section 1245 property (as defined in section 1245(a)(3)) and which is acquired by purchase for use in the active conduct of [in a trade or business] *a trade or business. Such term shall not include any property described in section 50(b) and shall not include air conditioning or heating units and horses.*

* * * * * * *

SEC. 179A. DEDUCTION FOR CLEAN-FUEL VEHICLES AND CERTAIN REFUELING PROPERTY.

(a) * * *

* * * * * * *

[(g)] *(f)* TERMINATION.—This section shall not apply to any property placed in service after December 31, 2004.

* * * * * * *

PART VII—ADDITIONAL ITEMIZED DEDUCTIONS FOR INDIVIDUALS

* * * * * * *

SEC. 219. RETIREMENT SAVINGS.

(a) * * *

(b) MAXIMUM AMOUNT OF DEDUCTION.—

(1) * * *

* * * * * * *

(4) SPECIAL RULE FOR SIMPLE RETIREMENT ACCOUNTS.—This section shall not apply with respect to any amount contributed to a simple retirement account established under section 408(p).

* * * * * * *

(g) LIMITATION ON DEDUCTION FOR ACTIVE PARTICIPANTS IN CERTAIN PENSION PLANS.—

(1) * * *

* * * * * * *

(5) ACTIVE PARTICIPANT.—For purposes of this subsection, the term "active participant" means, with respect to any plan year, an individual—

(A) who is an active participant in—

(i) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a),

(ii) an annuity plan described in section 403(a),

(iii) a plan established for its employees by the United States, by a State or political subdivision thereof, or by an agency or instrumentality of any of the foregoing,

(iv) an annuity contract described in section 403(b), or

(v) a simplified employee pension (within the meaning of section 408(k)), [or]

(vi) any simple retirement account (within the meaning of section 408(p)), or

* * * * * * *

PART VIII—SPECIAL DEDUCTIONS FOR CORPORATIONS

* * * * * * *

SEC. 243. DIVIDENDS RECEIVED BY CORPORATIONS.

(a) * * *

(b) QUALIFYING DIVIDENDS.—

(1) * * *

[(2) AFFILIATED GROUP.—For purposes of this subsection, the term "affiliated group" has the meaning given such term by section 1504(a), except that for such purposes sections 1504(b)(2), 1504(b)(4), and 1504(c) shall not apply.]

(2) AFFILIATED GROUP.—For purposes of this subsection:

(A) IN GENERAL.—The term "affiliated group" has the meaning given such term by section 1504(a), except that for such purposes sections 1504(b)(2), 1504(b)(4), and 1504(c) shall not apply.

(B) GROUP MUST BE CONSISTENT IN FOREIGN TAX TREATMENT.—The requirements of paragraph (1)(A) shall not be treated as being met with respect to any dividend received by a corporation if, for any taxable year which includes the day on which such dividend is received—

(i) 1 or more members of the affiliated group referred to in paragraph (1)(A) choose to any extent to take the benefits of section 901, and

(ii) 1 or more other members of such group claim to any extent a deduction for taxes otherwise creditable under section 901.

* * * * * * *

(3) SPECIAL RULE FOR GROUPS WHICH INCLUDE LIFE INSURANCE COMPANIES.—

(A) IN GENERAL.—In the case *of* an affiliated group which includes 1 or more insurance companies under section 801, no dividend by any member of such group shall be treated as a qualifying dividend unless an election under this paragraph is in effect for the taxable year in which the dividend is received. The preceding sentence shall not apply in the case of a dividend described in paragraph (1)(B)(ii).

* * * * * * *

PART IX—ITEMS NOT DEDUCTIBLE

* * * * * * *

SEC. 280A. DISALLOWANCE OF CERTAIN EXPENSES IN CONNECTION WITH BUSINESS USE OF HOME, RENTAL OF VACATION HOMES, ETC.

(a) * * *

* * * * * * *

(c) EXCEPTIONS FOR CERTAIN BUSINESS OR RENTAL USE; LIMITATION ON DEDUCTIONS FOR SUCH USE.—

(1) CERTAIN BUSINESS USE.—Subsection (a) shall not apply to any item to the extent such item is allocable to a portion of the dwelling unit which is exclusively used on a regular basis—

[(A) the principal place of business for any trade or business of the taxpayer.]

(A) as the principal place of business for any trade or business of the taxpayer.

* * * * * * *

(2) CERTAIN STORAGE USE.——Subsection (a) shall not apply to any item to the extent such item is allocable to space within the dwelling unit which is used on a regular basis as a storage unit for the [inventory] *inventory or product samples* of the taxpayer held for use in the taxpayer's trade or business of selling products at retail or wholesale, but only if the dwelling unit is the sole fixed location of such trade or business.

* * * * * * *

SEC. 280F. LIMITATION ON DEPRECIATION FOR LUXURY AUTOMOBILES; LIMITATION WHERE CERTAIN PROPERTY USED FOR PERSONAL PURPOSES.

(a) LIMITATION ON AMOUNT OF [INVESTMENT TAX CREDIT AND] DEPRECIATION FOR LUXURY AUTOMOBILES.—

(1) * * *

* * * * * * *

SEC. 280G. GOLDEN PARACHUTE PAYMENTS.

(a) * * *

(b) EXCESS PARACHUTE PAYMENT.—For purposes of this section—

(1) * * *

* * * * * * *

(6) EXEMPTION FOR PAYMENTS UNDER QUALIFIED PLANS.—Notwithstanding paragraph (2), the term "parachute payment" shall not include any payment to or from—

(A) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a),

(B) an annuity plan described in section 403(a), [or]

(C) a simplified employee pension (as defined in section 408(k))[.], *or*

(D) a simple retirement account described in section 408(p).

* * * * * * *

PART XI—SPECIAL RULES RELATING TO CORPORATE PREFERENCE ITEMS

* * * * * * *

SEC. 291. SPECIAL RULES RELATING TO CORPORATE PREFERENCE ITEMS.

(a) * * *

* * * * * * *

(e) DEFINITIONS.—For purposes of this section—

(1) FINANCIAL INSTITUTION PREFERENCE ITEM.—The term "financial institution preference item" includes the following:

(B) INTEREST ON DEBT TO CARRY TAX-EXEMPT OBLIGATIONS ACQUIRED AFTER DECEMBER 31, 1982, AND BEFORE AUGUST 8, 1986.—

(i) * * *

* * * * * * *

[(iv) SPECIAL RULES FOR OBLIGATIONS TO WHICH SECTION 133 APPLIES.—In the case of an obligation to which section 133 applies, interest on such obligation shall not be treated as exempt from taxes for purposes of this subparagraph.]

[(v)] *(iv)* APPLICATION OF SUBPARAGRAPH TO CERTAIN OBLIGATIONS ISSUED AFTER AUGUST 7, 1986.—For application of this subparagraph to certain obligations issued after August 7, 1986, see section 265(b)(3).

* * * * * * *

SUBCHAPTER C—CORPORATE DISTRIBUTIONS AND ADJUSTMENTS

* * * * * * *

PART II—CORPORATE LIQUIDATIONS

* * * * * * *

Subpart C—Collapsible Corporations

* * * * * * *

SEC. 341. COLLAPSIBLE CORPORATIONS.

(a) * * *

* * * * * * *

(f) CERTAIN SALES OF STOCK OF CONSENTING CORPORATIONS.—

(1) * * *

* * * * * * *

(3) EXCEPTION FOR CERTAIN TAX-FREE TRANSACTIONS.—If the basis of a subsection (f) asset in the hands of a transferee is determined by reference to its basis in the hands of the transferor by reason of the application of section 332, [351, 361, 371(a), or 374(a)] *351, or 361*, then the amount of gain taken into account by the transferor under paragraph (2) shall not exceed the amount of gain recognized to the transferor on the transfer of such asset (determined without regard to this subsection). This paragraph shall apply only if the transferee—

(A) is not an organization which is exempt from tax imposed by this chapter, and

(B) agrees (at such time and in such manner as the Secretary may by regulations prescribe) to have the provisions of paragraph (2) apply to any disposition by it of such subsection (f) asset.

* * * * * * *

PART III—CORPORATE ORGANIZATIONS AND REORGANIZATIONS

* * * * * * *

Subpart A—Corporate Organization

* * * * * * *

SEC. 355. DISTRIBUTION OF STOCK AND SECURITIES OF A CONTROLLED CORPORATION.

(a) * * *

* * * * * * *

(d) RECOGNITION OF GAIN ON CERTAIN DISTRIBUTIONS OF STOCK OR SECURITIES IN CONTROLLED CORPORATION.—

(1) * * *

* * * * * * *

(7) AGGREGATION RULES.—

(A) IN GENERAL.—For purposes of this subsection, a person and all persons related to such person (within the meaning of *section* 267(b) or 707(b)(1)) shall be treated as one person.

* * * * * * *

Subchapter D—Deferred Compensation, Etc.

* * * * * * *

PART I—PENSION, PROFIT-SHARING, STOCK BONUS PLANS, ETC.

* * * * * * *

Subpart A—General Rule

* * * * * * *

SEC. 401. QUALIFIED PENSION, PROFIT-SHARING, AND STOCK BONUS PLANS.

(a) REQUIREMENTS FOR QUALIFICATION.—A trust created or organized in the United States and forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of his employees or their beneficiaries shall constitute a qualified trust under this section—

(1) * * *

* * * * * * *

(5) SPECIAL RULES RELATING TO NONDISCRIMINATION REQUIREMENTS.—

(A) * * *

* * * * * * *

(D) INTEGRATED DEFINED BENEFIT PLAN.—

(i) * * *

(ii) FINAL PAY.—For purposes of this subparagraph, the participant's final pay is the compensation (as defined in section [414(q)(7)] *414(q)(4)*) paid to the participant by the employer for any year—

(I) which ends during the 5-year period ending with the year in which the participant separated from service for the employer, and

(II) for which the participant's total compensation from the employer was highest.

* * * * * * *

(F) SOCIAL SECURITY RETIREMENT AGE.—For purposes of testing for discrimination under paragraph (4)—

(i) the social security retirement age (as defined in section 415(b)(8)) shall be treated as a uniform retirement age, and

(ii) subsidized early retirement benefits and joint and survivor annuities shall not be treated as being unavailable to employees on the same terms merely because such benefits or annuities are based in whole or in part on an employee's social security retirement age (as so defined).

* * * * * * *

(9) REQUIRED DISTRIBUTIONS.—

(A) * * *

* * * * * * *

[(C) REQUIRED BEGINNING DATE.—For purposes of this paragraph, the term "required beginning date" means April 1 of the calendar year following the calendar year in which the employee attains age 70-1/2. In the case of a governmental plan or church plan, the required beginning date shall be the later of the date determined under the preceding sentence or April 1 of the calendar year following the calendar year in which the employee retires. For purposes of this subparagraph, the term "church plan" means a plan maintained by a church for church employees, and the term "church" means any church (as defined in section 3121(w)(3)(A)) or qualified church controlled organization (as defined in section 3121(w)(3)(B)).]

(C) REQUIRED BEGINNING DATE.—For purposes of this paragraph—

(i) IN GENERAL.—The term "required beginning date" means April 1 of the calendar year following the later of—

(I) the calendar year in which the employee attains age 70½, or

(II) the calendar year in which the employee retires.

(ii) EXCEPTION.—Subclause (II) of clause (i) shall not apply—

(I) except as provided in section 409(d), in the case of an employee who is a 5-percent owner (as defined in section 416) with respect to the plan year ending in the calendar year in which the employee attains age 70½, or

(II) for purposes of section 408 (a)(6) or (b)(3).

(iii) ACTUARIAL ADJUSTMENT.—In the case of an employee to whom clause (i)(II) applies who retires in a calendar year after the calendar year in which the employee attains age 70½, the employee's accrued benefit shall be actuarially increased to take into account the period after age 70½ in which the employee was not receiving any benefits under the plan.

(iv) EXCEPTION FOR GOVERNMENTAL AND CHURCH PLANS.—Clauses (ii) and (iii) shall not apply in the case of a governmental plan or church plan. For purposes of this clause, the term "church plan" means a plan maintained by a church for church employees, and the term "church" means any church (as defined in section 3121(w)(3)(A)) or qualified church-controlled organization (as defined in section 3121(w)(3)(B)).

* * * * * * *

(17) COMPENSATION LIMIT.—

(A) IN GENERAL.—A trust shall not constitute a qualified trust under this section unless, under the plan of which such trust is a part, the annual compensation of each employee taken into account under the plan for any year does not exceed $150,000. [In determining the compensation of an employee, the rules of section 414(q)(6) shall apply, except that in applying such rules, the term "family" shall include only the spouse of the employee and any lineal descendants of the employee who have not attained age 19 before the close of the year.]

* * * * * * *

(20) A trust forming part of a pension plan shall not be treated as failing to constitute a qualified trust under this section merely because the pension plan of which such trust is a part makes 1 or more distributions within 1 taxable year to a distributee on account of a termination of the plan of which the trust is a part, or in the case of a profit-sharing or stock bonus plan, a complete discontinuance of contributions under such plan. This paragraph shall not apply to a defined benefit plan unless the employer maintaining such plan files a notice with the Pension Benefit Guaranty Corporation (at the time and in the manner prescribed by the Pension Benefit Guaranty Corporation) notifying the Corporation of such payment or distribution and the Corporation has approved such payment or distribution or, within 90 days after the date on which such notice was filed, has failed to disapprove such payment or distribution. For purposes of this paragraph, rules similar to the rules of section 402(a)(6)(B) (as in effect before its repeal by

section [211] *521* of the Unemployment Compensation Amendments of 1992) shall apply.

* * * * * * *

(26) ADDITIONAL PARTICIPATION REQUIREMENTS.—

[(A) IN GENERAL.—A trust shall not constitute a qualified trust under this subsection unless such trust is part of a plan which on each day of the plan year benefits the lesser of—

[(i) 50 employees of the employer, or

[(ii) 40 percent or more of all employees of the employer.]

(A) IN GENERAL.—In the case of a trust which is a part of a defined benefit plan, such trust shall not constitute a qualified trust under this subsection unless on each day of the plan year such trust benefits at least the lesser of—

(i) 50 employees of the employer, or

(ii) the greater of—

(I) 40 percent of all employees of the employer, or

(II) 2 employees (or if there is only 1 employee, such employee).

* * * * * * *

(G) SEPARATE LINES OF BUSINESS.—At the election of the employer and with the consent of the Secretary, this paragraph may be applied separately with respect to each separate line of business of the employer. For purposes of this paragraph, the term "separate line of business" has the meaning given such term by section 414(r) (without regard to [paragraph (7)] *paragraph (2)(A) or (7)* thereof).

* * * * * * *

(28) ADDITIONAL REQUIREMENTS RELATING TO EMPLOYEE STOCK OWNERSHIP PLANS.—

(A) * * *

(B) DIVERSIFICATION OF INVESTMENTS.—

(i) * * *

* * * * * * *

[(v) COORDINATION WITH DISTRIBUTION RULES.—Any distribution required by this subparagraph shall not be taken into account in determining whether a subsequent distribution is a lump sum distribution under section 402(d)(4)(A) or in determining whether section 402(c)(10) applies.]

* * * * * * *

[(d) ADDITIONAL REQUIREMENTS FOR QUALIFICATION OF TRUSTS AND PLANS BENEFITING OWNER-EMPLOYEES.—A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the following requirements of this subsection are met by the trust and by the plan of which such trust is a part:

[(1)(A) If the plan provides contributions or benefits for an owner-employee who controls, or for two or more owner-employees who together control, the trade or business with respect to which the plan is established, and who also control as an owner-employee or as owner-employees one or more other trades or businesses, such plan and the plans established with respect to such other trades or businesses, when coalesced, constitute a single plan which meets the requirements of subsection (a) (including paragraph (10) thereof) and of this subsection with respect to the employees of all such trades or businesses (including the trade or business with respect to which the plan intended to qualify under this section is established).

[(B) For purposes of subparagraph (A), an owner-employee, or two or more owner-employees, shall be considered to control a trade or business if such owner-employee, or such two or more owner-employees together—

[(i) own the entire interest in an unincorporated trade or business, or

[(ii) in the case of a partnership, own more than 50 percent of either the capital interest or the profits interest in such partnership.

For purposes of the preceding sentence, an owner-employee, or two or more owner-employees, shall be treated as owning any interest in a partnership which is owned, directly or indirectly, by a partnership which such owner-employee, or such two or more owner-employees, are considered to control within the meaning of the preceding sentence.

[(2) The plan does not provide contributions or benefits for any owner-employee who controls (within the meaning of paragraph (1)(B)), or for two or more owner-employees who together control, as an owner-employee or as owner-employees, any other trade or business, unless the employees of each trade or business which such owner-employee or such owner-employees control are included under a plan which meets the requirements of subsection (a) (including paragraph (10) thereof) and of this subsection, and provides contributions and benefits for employees which are not less favorable than contributions and benefits provided for owner-employees under the plan.

[(3) Under the plan, contributions on behalf of any owner-employee may be made only with respect to the earned income of such owner-employee which is derived from the trade or business with respect to which such plan is established.]

(d) CONTRIBUTION LIMIT ON OWNER-EMPLOYEES.—A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the plan provides that contributions on behalf of any owner-employee may be made only with respect to the earned income of such owner-employee which is derived from the trade or business with respect to which such plan is established.

* * * * * * *

(k) CASH OR DEFERRED ARRANGEMENTS.—

(1) * * *

* * * * * * *

(3) APPLICATION OF PARTICIPATION AND DISCRIMINATION STANDARDS.—

(A) A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement unless—

(i) those employees eligible to benefit under the arrangement satisfy the provisions of section 410(b)(1), and

(ii) the actual deferral percentage for eligible highly compensated employees (as defined in paragraph (5)) for [such year] *the plan year* bears a relationship to the actual deferral percentage for all other eligible employees [for such plan year] *for the preceding plan year* which meets either of the following tests:

(I) The actual deferral percentage for the group of eligible highly compensated employees is not more than the actual deferral percentage of all other eligible employees multiplied by 1.25.

(II) The excess of the actual deferral percentage for the group of eligible highly compensated employees over that of all other eligible employees is not more than 2 percentage points, and the actual deferral percentage for the group of eligible highly compensated employees is not more than the actual deferral percentage of all other eligible employees multiplied by 2.

If 2 or more plans which include cash or deferred arrangements are considered as 1 plan for purposes of section 401(a)(4) or 410(b), the cash or deferred arrangements included in such plans shall be treated as 1 arrangement for purposes of this subparagraph. *An arrangement may apply this clause by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary. .*

If any highly compensated employee is a participant under 2 or more cash or deferred arrangements of the employer, for purposes of determining the deferral percentage with respect to such employee, all such cash or deferred arrangements shall be treated as 1 cash or deferred arrangement.

* * * * * * *

(E) For purposes of this paragraph, in the case of the first plan year of any plan (other than a successor plan), the amount taken into account as the actual deferral percentage of nonhighly compensated employees for the preceding plan year shall be—

(i) 3 percent, or

(ii) if the employer makes an election under this subclause, the actual deferral percentage of nonhighly

compensated employees determined for such first plan year.

* * * * * * *

(4) OTHER REQUIREMENTS.—

(A) * * *

[(B) STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS NOT ELIGIBLE.—A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement if it is part of a plan maintained by—

[(i) a State or local government or political subdivision thereof, or any agency or instrumentality thereof, or

[(ii) any organization exempt from tax under this subtitle.

This subparagraph shall not apply to a rural cooperative plan.]

(B) ELIGIBILITY OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.—

(i) TAX-EXEMPTS ELIGIBLE.—Except as provided in clause (ii), any organization exempt from tax under this subtitle may include a qualified cash or deferred arrangement as part of a plan maintained by it.

(ii) GOVERNMENTS INELIGIBLE.—A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement if it is part of a plan maintained by a State or local government or political subdivision thereof, or any agency or instrumentality thereof. This clause shall not apply to a rural cooperative plan or to a plan of an employer described in clause (iii).

(iii) TREATMENT OF INDIAN TRIBAL GOVERNMENTS.—An employer which is an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of the foregoing shall be treated as an organization exempt from tax under this subtitle for purposes of clause (i).

* * * * * * *

(7) RURAL COOPERATIVE PLAN.—For purposes of this subsection—

(A) * * *

(B) RURAL COOPERATIVE DEFINED.—For purposes of subparagraph (A), the term "rural cooperative" means—

[(i) any organization which—

[(I) is exempt from tax under this subtitle or which is a State or local government or political subdivision thereof (or agency or instrumentality thereof), and

[(II) is engaged primarily in providing electric service on a mutual or cooperative basis,]

(i) any organization which—

(I) is engaged primarily in providing electric service on a mutual or cooperative basis, or

(II) is engaged primarily in providing electric service to the public in its area of service and which is exempt from tax under this subtitle or which is a State or local government (or an agency or instrumentality thereof), other than a municipality (or an agency or instrumentality thereof),

* * * * * * *

(C) SPECIAL RULE FOR CERTAIN DISTRIBUTIONS.—A rural cooperative plan which includes a qualified cash or deferred arrangement shall not be treated as violating the requirements of section 401(a) or of paragraph (2) merely by reason of a hardship distribution or a distribution to a participant after attainment of age 59½. For purposes of this section, the term "hardship distribution" means a distribution described in paragraph (2)(B)(i)(IV) (without regard to the limitation of its application to profit-sharing or stock bonus plans).

(8) ARRANGEMENT NOT DISQUALIFIED IF EXCESS CONTRIBUTIONS DISTRIBUTED.—

(A) * * *

* * * * * * *

(C) METHOD OF DISTRIBUTING EXCESS CONTRIBUTIONS.—Any distribution of the excess contributions for any plan year shall be made to highly compensated employees [on the basis of the respective portions of the excess contributions attributable to each of such employees] *on the basis of the amount of contributions by, or on behalf of, each of such employees.*

* * * * * * *

(10) DISTRIBUTIONS UPON TERMINATION OF PLAN OR DISPOSITION OF ASSETS OR SUBSIDIARY.—

(A) * * *

(B) DISTRIBUTIONS MUST BE LUMP SUM DISTRIBUTIONS.—

(i) IN GENERAL.—An event shall not be treated as described in subparagraph (A) with respect to any employee unless the employee receives a lump sum distribution by reason of the event.

[(ii) LUMP SUM DISTRIBUTION.—For purposes of this subparagraph, the term "lump sum distribution" has the meaning given such term by section 402(d)(4), without regard to clauses (i), (ii), (iii), and (iv) of subparagraph (A), subparagraph (B), or subparagraph (F) thereof.]

(ii) LUMP-SUM DISTRIBUTION.—For purposes of this subparagraph, the term "lump-sum distribution" has the meaning given such term by section 402(e)(4)(D) (without regard to subclauses (I), (II), (III), and (IV) of clause (i) thereof).

* * * * * * *

(11) ADOPTION OF SIMPLE PLAN TO MEET NONDISCRIMINATION TESTS.—

(A) IN GENERAL.—A cash or deferred arrangement maintained by an eligible employer shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement meets—

(i) the contribution requirements of subparagraph (B),

(ii) the exclusive benefit requirements of subparagraph (C), and

(iii) the vesting requirements of section 408(p)(3).

(B) CONTRIBUTION REQUIREMENTS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement—

(I) an employee may elect to have the employer make elective contributions for the year on behalf of the employee to a trust under the plan in an amount which is expressed as a percentage of compensation of the employee but which in no event exceeds $6,000,

(II) the employer is required to make a matching contribution to the trust for the year in an amount equal to so much of the amount the employee elects under subclause (I) as does not exceed 3 percent of compensation for the year, and

(III) no other contributions may be made other than contributions described in subclause (I) or (II).

(ii) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—An employer shall be treated as meeting the requirements of clause (i)(II) for any year if, in lieu of the contributions described in such clause, the employer elects (pursuant to the terms of the arrangement) to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 30th day before the beginning of such year.

(C) EXCLUSIVE BENEFIT.—The requirements of this subparagraph are met for any year to which this paragraph applies if no contributions were made, or benefits were accrued, for services during such year under any qualified plan of the employer on behalf of any employee eligible to participate in the cash or deferred arrangement, other than contributions described in subparagraph (B).

(D) DEFINITIONS AND SPECIAL RULE.—

(i) DEFINITIONS.—For purposes of this paragraph, any term used in this paragraph which is also used in section 408(p) shall have the meaning given such term by such section.

(ii) COORDINATION WITH TOP-HEAVY RULES.—A plan meeting the requirements of this paragraph for any year shall not be treated as a top-heavy plan under section 416 for such year.

(12) ALTERNATIVE METHODS OF MEETING NONDISCRIMINATION REQUIREMENTS.—

(A) IN GENERAL.—A cash or deferred arrangement shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement—

(i) meets the contribution requirements of subparagraph (B) or (C), and

(ii) meets the notice requirements of subparagraph (D).

(B) MATCHING CONTRIBUTIONS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement, the employer makes matching contributions on behalf of each employee who is not a highly compensated employee in an amount equal to—

(I) 100 percent of the elective contributions of the employee to the extent such elective contributions do not exceed 3 percent of the employee's compensation, and

(II) 50 percent of the elective contributions of the employee to the extent that such elective contributions exceed 3 percent but do not exceed 5 percent of the employee's compensation.

(ii) RATE FOR HIGHLY COMPENSATED EMPLOYEES.—The requirements of this subparagraph are not met if, under the arrangement, the rate of matching contribution with respect to any elective contribution of a highly compensated employee at any rate of elective contribution is greater than that with respect to an employee who is not a highly compensated employee.

(iii) ALTERNATIVE PLAN DESIGNS.—If the rate of any matching contribution with respect to any rate of elective contribution is not equal to the percentage required under clause (i), an arrangement shall not be treated as failing to meet the requirements of clause (i) if—

(I) the rate of an employer's matching contribution does not increase as an employee's rate of elective contributions increase, and

(II) the aggregate amount of matching contributions at such rate of elective contribution is at least equal to the aggregate amount of matching contributions which would be made if matching contributions were made on the basis of the percentages described in clause (i).

(C) NONELECTIVE CONTRIBUTIONS.—The requirements of this subparagraph are met if, under the arrangement, the employer is required, without regard to whether the employee makes an elective contribution or employee contribution, to make a contribution to a defined contribution plan on behalf of each employee who is not a highly com-

pensated employee and who is eligible to participate in the arrangement in an amount equal to at least 3 percent of the employee's compensation.

(D) NOTICE REQUIREMENT.—An arrangement meets the requirements of this paragraph if, under the arrangement, each employee eligible to participate is, within a reasonable period before any year, given written notice of the employee's rights and obligations under the arrangement which—

(i) is sufficiently accurate and comprehensive to appraise the employee of such rights and obligations, and

(ii) is written in a manner calculated to be understood by the average employee eligible to participate.

(E) OTHER REQUIREMENTS.—

(i) WITHDRAWAL AND VESTING RESTRICTIONS.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) of this paragraph unless the requirements of subparagraphs (B) and (C) of paragraph (2) are met with respect to all employer contributions (including matching contributions) taken into account in determining whether the requirements of subparagraphs (B) and (C) of this paragraph are met.

(ii) SOCIAL SECURITY AND SIMILAR CONTRIBUTIONS NOT TAKEN INTO ACCOUNT.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) unless such requirements are met without regard to subsection (l), and, for purposes of subsection (l), employer contributions under subparagraph (B) or (C) shall not be taken into account.

(F) OTHER PLANS.—An arrangement shall be treated as meeting the requirements under subparagraph (A)(i) if any other plan maintained by the employer meets such requirements with respect to employees eligible under the arrangement.

* * * * * * *

(m) NONDISCRIMINATION TEST FOR MATCHING CONTRIBUTIONS AND EMPLOYEE CONTRIBUTIONS.—

(1) * * *

(2) REQUIREMENTS.—

(A) CONTRIBUTION PERCENTAGE REQUIREMENT.—A plan meets the contribution percentage requirement of this paragraph for any plan year only if the contribution percentage for eligible highly compensated employees *for such plan year* does not exceed the greater of—

(i) 125 percent of such percentage for all other eligible employees *for the preceding plan year*, or

(ii) the lesser of 200 percent of such percentage for all other eligible employees *for the preceding plan year*, or such percentage for all other eligible employees *for the preceding plan year* plus 2 percentage points.

This subparagraph may be applied by using the plan year rather than the preceding plan year if the employer so

elects, except that if such an election is made, it may not be changed except as provided the Secretary.

* * * * * * *

(3) CONTRIBUTION PERCENTAGE.—For purposes of paragraph (2), the contribution percentage for a specified group of employees for a plan year shall be the average of the ratios (calculated separately for each employee in such group) of—

(A) the sum of the matching contributions and employee contributions paid under the plan on behalf of each such employee for such plan year, to

(B) the employee's compensation (within the meaning of section 414(s)) for such plan year.

Under regulations, an employer may elect to take into account (in computing the contribution percentage) elective deferrals and qualified nonelective contributions under the plan or any other plan of the employer. If matching contributions are taken into account for purposes of subsection (k)(3)(A)(ii) for any plan year, such contributions shall not be taken into account under subparagraph (A) for such year. *Rules similar to the rules of subsection (k)(3)(E) shall apply for purposes of this subsection.*

* * * * * * *

(6) PLAN NOT DISQUALIFIED IF EXCESS AGGREGATE CONTRIBUTIONS DISTRIBUTED BEFORE END OF FOLLOWING PLAN YEAR.—

(A) * * *

* * * * * * *

(C) METHOD OF DISTRIBUTING EXCESS AGGREGATE CONTRIBUTIONS.—Any distribution of the excess aggregate contributions for any plan year shall be made to highly compensated employees [on the basis of the respective portions of such amounts attributable to each of such employees] *on the basis of the amount of contributions on behalf of, or by, each such employee.* Forfeitures of excess aggregate contributions may not be allocated to participants whose contributions are reduced under this paragraph.

* * * * * * *

(10) ALTERNATIVE METHOD OF SATISFYING TESTS.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

(A) meets the contribution requirements of subparagraph (B) of subsection (k)(11),

(B) meets the exclusive benefit requirements of subsection (k)(11)(C), and

(C) meets the vesting requirements of section 408(p)(3).

(11) ALTERNATIVE METHOD OF SATISFYING TESTS.—

(A) IN GENERAL.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

(i) meets the contribution requirements of subparagraph (B) or (C) of subsection (k)(12),

(ii) meets the notice requirements of subsection (k)(12)(D), and

(iii) meets the requirements of subparagraph (B).

(B) LIMITATION ON MATCHING CONTRIBUTIONS.—The requirements of this subparagraph are met if—

(i) matching contributions on behalf of any employee may not be made with respect to an employee's contributions or elective deferrals in excess of 6 percent of the employee's compensation,

(ii) the rate of an employer's matching contribution does not increase as the rate of an employee's contributions or elective deferrals increase, and

(iii) the matching contribution with respect to any highly compensated employee at any rate of an employee contribution or rate of elective deferral is not greater than that with respect to an employee who is not a highly compensated employee.

[(10)] *(12)* CROSS REFERENCE.—

For excise tax on certain excess contributions, see section 4979.

* * * * * * *

SEC. 402. TAXABILITY OF BENEFICIARY OF EMPLOYEES' TRUST.

(a) * * *

* * * * * * *

(c) RULES APPLICABLE TO ROLLOVERS FROM EXEMPT TRUSTS.—

(1) * * *

* * * * * * *

[(10) DENIAL OF AVERAGING FOR SUBSEQUENT DISTRIBUTIONS.—If paragraph (1) applies to any distribution paid to any employee, paragraphs (1) and (3) of subsection (d) shall not apply to any distribution (paid after such distribution) of the balance to the credit of the employee under the plan under which the preceding distribution was made (or under any other plan which, under subsection (d)(4)(C), would be aggregated with such plan).]

* * * * * * *

[(d) TAX ON LUMP SUM DISTRIBUTIONS.—

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

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

[(B) AMOUNT OF TAX.—The amount of tax imposed by subparagraph (A) for any taxable year is an amount equal to 5 times the tax which would be imposed by subsection (c) of section 1 if the recipient were an individual referred to in such subsection and the taxable income were an amount equal to ⅕ of the excess of—

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

[(ii) the minimum distribution allowance.

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

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

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

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

[(2) DISTRIBUTIONS OF ANNUITY CONTRACTS.—

[(A) IN GENERAL.—In the case of any recipient of a lump sum distribution for any taxable year, if the distribution (or any part thereof) is an annuity contract, the total taxable amount of the distribution shall be aggregated for purposes of computing the tax imposed by paragraph (1)(A), except that the amount of tax so computed shall be reduced (but not below zero) by that portion of the tax on the aggregate total taxable amount which is attributable to annuity contracts.

[(B) BENEFICIARIES.—For purposes of this paragraph, a beneficiary of a trust to which a lump sum distribution is made shall be treated as the recipient of such distribution if the beneficiary is an employee (including an employee within the meaning of section 401(c)(1)) with respect to the plan under which the distribution is made or if the beneficiary is treated as the owner of such trust for purposes of subpart E of part I of subchapter J.

[(C) ANNUITY CONTRACTS.—For purposes of this paragraph, in the case of the distribution of an annuity contract, the taxable amount of such distribution shall be deemed to be the current actuarial value of the contract, determined on the date of such distribution.

[(D) TRUSTS.—In the case of a lump sum distribution with respect to any individual which is made only to 2 or more trusts, the tax imposed by paragraph (1)(A) shall be computed as if such distribution was made to a single trust, but the liability for such tax shall be apportioned among such trusts according to the relative amounts received by each.

[(E) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this paragraph.

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

[(4) DEFINITIONS AND SPECIAL RULES.—

[(A) LUMP SUM DISTRIBUTION.—For purposes of this section and section 403, the term "lump sum distribution" means the distribution or payment within 1 taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient—

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

[(ii) after the employee attains age 59½,

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

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

from a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501 or from a plan described in section 403(a). Clause (iii) of this subparagraph shall be applied only with respect to an 401(c)(1), and clause (iv) shall be applied only with respect to an employee within the meaning of section 401(c)(1). A distribution of an annuity contract from a trust or annuity plan referred to in the first sentence of this subparagraph shall be treated as a lump sum distribution. For purposes of this subparagraph, a distribution to 2 or more trusts shall be treated as a distribution to 1 recipient. For purposes of this subsection, the balance to the credit of the employee does not include the accumulated deductible employee contributions under the plan (within the meaning of section 72(o)(5)).

[(B) AVERAGING TO APPLY TO 1 LUMP SUM DISTRIBUTION AFTER AGE 59½.—Paragraph (1) shall apply to a lump sum distribution with respect to an employee under subparagraph (A) only if—

[(i) such amount is received on or after the date on which the employee has attained age 59½, and

[(ii) the taxpayer elects for the taxable year to have all such amounts received during such taxable year so treated.

Not more than 1 election may be made under this subparagraph by any taxpayer with respect to any employee. No election may be made under this subparagraph by any taxpayer other than an individual, an estate, or a trust. In the case of a lump sum distribution made with respect to an employee to 2 or more trusts, the election under this subparagraph shall be made by the personal representative of the taxpayer.

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

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

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

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

[(i) the amounts considered contributed by the employee (determined by applying section 72(f)), reduced by any amounts previously distributed which were not includible in gross income, and

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

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

[(F) MINIMUM PERIOD OF SERVICE.—For purposes of this subsection, no amount distributed to an employee from or under a plan may be treated as a lump sum distribution under subparagraph (A) unless the employee has been a participant in the plan for 5 or more taxable years before the taxable year in which such amounts are distributed.

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

[(H) BALANCE TO CREDIT OF EMPLOYEE NOT TO INCLUDE AMOUNTS PAYABLE UNDER QUALIFIED DOMESTIC RELATIONS ORDER.—For purpose of this subsection, the balance to the credit of an employee shall not include any amount payable to an alternate payee under a qualified domestic relations order (within the meaning of section 414(p)).

[(I) TRANSFERS TO COST-OF-LIVING ARRANGEMENT NOT TREATED AS DISTRIBUTION.—For purposes of this subsection, the balance to the credit of an employee under a defined contribution plan shall not include any amount transferred from such defined contribution plan to a qualified cost-of- living arrangement (within the meaning of section 415(k)(2)) under a defined benefit plan.

[(J) LUMP SUM DISTRIBUTIONS OF ALTERNATE PAYEES.—If any distribution or payment of the balance to the credit of an employee would be treated as a lump sum distribution, then, for purposes of this subsection, the payment under a qualified domestic relations order (within the meaning of section 414(p)) of the balance to the credit of an alternate payee who is the spouse or former spouse of the employee shall be treated as a lump sum distribution. For purposes of this subparagraph, the balance to the credit of the alternate payee shall not include any amount payable to the employee.

[(K) TREATMENT OF PORTION NOT ROLLED OVER.—If any portion of a lump sum distribution is transferred in a transfer to which subsection (c) applies, paragraphs (1) and (3) shall not apply with respect to the distribution.

[(L) SECURITIES.—For purposes of this subsection, the terms "securities" and "securities of the employer corporation" have the respective meanings provided by subsection (e)(4)(E).

[(5) SPECIAL RULE WHERE PORTIONS OF LUMP SUM DISTRIBUTION ATTRIBUTABLE TO ROLLOVER OF BOND PURCHASED UNDER

QUALIFIED BOND PURCHASE PLAN.—If any portion of a lump sum distribution is attributable to a transfer described in section 405(d)(3)(A)(ii) (as in effect before its repeal by the Tax Reform Act of 1984), paragraphs (1) and (3) of this subsection shall not apply to such portion.

[(6) TREATMENT OF POTENTIAL FUTURE VESTING.—

[(A) IN GENERAL.—For purposes of determining whether any distribution which becomes payable to the recipient on account of the employee's separation from service is a lump sum distribution, the balance to the credit of the employee shall be determined without regard to any increase in vesting which may occur if the employee is reemployed by the employer.

[(B) RECAPTURE IN CERTAIN CASES.—If—

[(i) an amount is treated as a lump sum distribution by reason of subparagraph (A),

[(ii) special lump sum treatment applies to such distribution,

[(iii) the employee is subsequently reemployed by the employer, and

[(iv) as a result of services performed after being so reemployed, there is an increase in the employee's vesting for benefits accrued before the separation referred to in subparagraph (A),

under regulations prescribed by the Secretary, the tax imposed by this chapter for the taxable year (in which the increase in vesting first occurs) shall be increased by the reduction in tax which resulted from the special lump treatment (and any election under paragraph 4(B) shall not be taken into account for purposes of determining whether the employee may make another election under paragraph (4)(B)).

[(C) SPECIAL LUMP SUM TREATMENT.—For purposes of this paragraph, special lump treatment applies to any distribution if any portion of such distribution is taxed under the subsection by reason of any election under paragraph (4)(B).

[(D) VESTING.—For purposes of this paragraph, the term "vesting" means the portion of the accrued benefits derived from employer contributions to which the participant has a nonforfeitable right.

[(7) COORDINATION WITH FOREIGN TAX CREDIT LIMITATIONS.—Subsections (a), (b), and (c) of section 904 shall be applied separately with respect to any lump sum distribution on which tax is imposed under paragraph (1), and the amount of such distribution shall be treated as the taxable income for purposes of such separate application.]

(d) TAXABILITY OF BENEFICIARY OF CERTAIN FOREIGN SITUS TRUSTS.—For purposes of subsections (a), (b), and (c), a stock bonus, pension, or profit-sharing trust which would qualify for exemption from tax under section 501(a) except for the fact that it is a trust created or organized outside the United States shall be treated as if it were a trust exempt from tax under section 501(a).

(e) OTHER RULES APPLICABLE TO EXEMPT TRUSTS.—

(1) * * *

* * * * * * *

(4) NET UNREALIZED APPRECIATION.—

(A) * * *

* * * * * * *

[(D) LUMP SUM DISTRIBUTION.—For purposes of this paragraph, the term "lump sum distribution" has the meaning given such term by subsection (d)(4)(A) (without regard to subsection (d)(4)(F)).]

(D) LUMP-SUM DISTRIBUTION.—For purposes of this paragraph—

(i) IN GENERAL.—The term "lump sum distribution" means the distribution or payment within one taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient—

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

(II) after the employee attains age 59½,

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

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

from a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501 or from a plan described in section 403(a). Subclause (III) of this clause shall be applied only with respect to an individual who is an employee without regard to section 401(c)(1), and subclause (IV) shall be applied only with respect to an employee within the meaning of section 401(c)(1). For purposes of this clause, a distribution to two or more trusts shall be treated as a distribution to one recipient. For purposes of this paragraph, the balance to the credit of the employee does not include the accumulated deductible employee contributions under the plan (within the meaning of section 72(o)(5)).

(ii) AGGREGATION OF CERTAIN TRUSTS AND PLANS.—For purposes of determining the balance to the credit of an employee under clause (i)—

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

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

(iii) COMMUNITY PROPERTY LAWS.—The provisions of this paragraph shall be applied without regard to community property laws.

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

(v) BALANCE TO CREDIT OF EMPLOYEE NOT TO INCLUDE AMOUNTS PAYABLE UNDER QUALIFIED DOMESTIC RELATIONS ORDER.—For purposes of this paragraph, the balance to the credit of an employee shall not include any amount payable to an alternate payee under a qualified domestic relations order (within the meaning of section 414(p)).

(vi) TRANSFERS TO COST-OF-LIVING ARRANGEMENT NOT TREATED AS DISTRIBUTION.—For purposes of this paragraph, the balance to the credit of an employee under a defined contribution plan shall not include any amount transferred from such defined contribution plan to a qualified cost-of-living arrangement (within the meaning of section 415(k)(2)) under a defined benefit plan.

(vii) LUMP-SUM DISTRIBUTIONS OF ALTERNATE PAYEES.—If any distribution or payment of the balance to the credit of an employee would be treated as a lump-sum distribution, then, for purposes of this paragraph, the payment under a qualified domestic relations order (within the meaning of section 414(p)) of the balance to the credit of an alternate payee who is the spouse or former spouse of the employee shall be treated as a lump-sum distribution. For purposes of this clause, the balance to the credit of the alternate payee shall not include any amount payable to the employee.

[(5) TAXABILITY OF BENEFICIARY OF CERTAIN FOREIGN SITUS TRUSTS.—For purposes of subsections (a), (b), and (c), a stock bonus, pension, or profit-sharing trust which would qualify for exemption from tax under section 501(a) except for the fact that it is a trust created or organized outside the United States shall be treated as if it were a trust exempt from tax under section 501(a).]

* * * * * * *

(g) LIMITATION ON EXCLUSION FOR ELECTIVE DEFERRALS.—

(1) * * *

* * * * * * *

(3) ELECTIVE DEFERRALS.—For purposes of this subsection, the term "elective deferrals" means, with respect to any taxable year, the sum of—

(A) any employer contribution under a qualified cash or deferred arrangement (as defined in section 401(k)) to the extent not includible in gross income for the taxable year under subsection [(a)(8)] *(e)(3)* (determined without regard to this subsection),

(B) any employer contribution to the extent not includible in gross income for the taxable year under subsection (h)(1)(B) (determined without regard to this subsection), [and]

(C) any employer contribution to purchase an annuity contract under section 403(b) under a salary reduction agreement (within the meaning of section 3121(a)(5)(D))[.], *and*

(D) any elective employer contribution under section 408(p)(2)(A)(i).

An employer contribution shall not be treated as an elective deferral described in subparagraph (C) if under the salary reduction agreement such contribution is made pursuant to a one-time irrevocable election made by the employee at the time of initial eligibility to participate in the agreement or is made pursuant to a similar arrangement involving a one-time irrevocable election specified in regulations.

* * * * * * *

(k) TREATMENT OF SIMPLE RETIREMENT ACCOUNTS.—Rules similar to the rules of paragraphs (1) and (3) of subsection (h) shall apply to contributions and distributions with respect to a simple retirement account under section 408(p).

SEC. 403. TAXATION OF EMPLOYEE ANNUITIES.

(a) * * *

(b) TAXABILITY OF BENEFICIARY UNDER ANNUITY PURCHASED BY SECTION 501(c)(3) ORGANIZATION OR PUBLIC SCHOOL.—

(1) GENERAL RULE.—If—

(A) * * *

* * * * * * *

[(E) in the case of a contract purchased under a plan which provides a salary reduction agreement, the plan meets the requirements of section 401(a)(30),]

(E) in the case of a contract purchased under a salary reduction agreement, the contract meets the requirements of section 401(a)(30),

then amounts contributed by such employer for such annuity contract on or after such rights become nonforfeitable shall be excluded from the gross income of the employee for the taxable year to the extent that the aggregate of such amounts does not exceed the exclusion allowance for such taxable year. The amount actually distributed to any distributee under such contract shall be taxable to the distributee (in the year in which so distributed) under section 72 (relating to annuities). For purposes of applying the rules of this subsection to amounts contributed by an employer for a taxable year, amounts transferred to a contract described in this paragraph by reason of a rollover contribution described in paragraph (8) of this subsection or section 408(d)(3)(A)(iii) shall not be considered contributed by such employer.

* * * * * * *

(10) DISTRIBUTION REQUIREMENTS.—Under regulations prescribed by the Secretary, this subsection shall not apply to any annuity contract (or to any custodial account described in paragraph (7) or retirement income account described in paragraph (9)) unless requirements similar to the requirements of section 401(a)(9) and 401(a)(31) are met (and requirements similar to

the incidental death benefit requirements of section 401(a) are met) with respect to such annuity contract (or custodial account or retirement income account). Any amount transferred in [an] *a* direct trustee-to-trustee transfer in accordance with section 401(a)(31) shall not be includible in gross income for the taxable year of the transfer.

* * * * * * *

SEC. 404. DEDUCTION FOR CONTRIBUTIONS OF AN EMPLOYER TO AN EMPLOYEES' TRUST OR ANNUITY PLAN AND COMPENSATION UNDER A DEFERRED PAYMENT PLAN.

(a) GENERAL RULE.—If contributions are paid by an employer to or under a stock bonus, pension, profit-sharing, or annuity plan, or if compensation is paid or accrued on account of any employee under a plan deferring the receipt of such compensation, such contributions or compensation shall not be deductible under this chapter; but, if they would otherwise be deductible, they shall be deductible under this section, subject, however, to the following limitations as to the amounts deductible in any year:

(1) * * *

(2) EMPLOYEES' ANNUITIES.—In the taxable year when paid, in an amount determined in accordance with paragraph (1), if the contributions are paid toward the purchase of retirement annuities, or retirement annuities and medical benefits as described in section 401(h), and such purchase is part of a plan which meets the requirements of section 401(a) (3), (4), (5), (6), (7), (8), (9), (11), (12), (13), (14), (15), (16), (17), [(18),] (19), (20), (22), (26), (27) and (31) and, if applicable, the requirements of section 401(a)(10) and of section 401(d), and if refunds of premiums, if any, are applied within the current taxable year or next succeeding taxable year toward the purchase of such retirement annuities, or such retirement annuities and medical benefits.

* * * * * * *

(j) SPECIAL RULES RELATING TO APPLICATION WITH SECTION 415.—

(1) NO DEDUCTION IN EXCESS OF SECTION 415 LIMITATION.—In computing the amount of any deduction allowable under paragraph (1), (2), (3), (4), (7), or [(10)] *(9)* of subsection (a) for any year—

(A) in the case of a defined benefit plan, there shall not be taken into account any benefits for any year in excess of any limitation on such benefits under section 415 for such year, or

(B) in the case of a defined contribution plan, the amount of any contributions otherwise taken into account shall be reduced by any annual additions in excess of the limitation under section 415 for such year.

* * * * * * *

(l) LIMITATION ON AMOUNT OF ANNUAL COMPENSATION TAKEN INTO ACCOUNT.—For purposes of applying the limitations of this section, the amount of annual compensation of each employee taken into account under the plan for any year shall not exceed

$150,000. The Secretary shall adjust the $150,000 amount at the same time, and by the same amount, as any adjustment under section 401(a)(17)(B). For purposes of clause (i), (ii), or (iii) of subsection (a)(1)(A), and in computing the full funding limitation, any adjustment under the preceding sentence shall not be taken into account for any year before the year for which such adjustment first takes effect. [In determining the compensation of an employee, the rules of section 414(q)(6) shall apply, except that in applying such rules, the term "family" shall include only the spouse of the employee and any lineal descendants of the employee who have not attained age 19 before the close of the year.]

(m) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—

(1) IN GENERAL.—Employer contributions to a simple retirement account shall be treated as if they are made to a plan subject to the requirements of this section.

(2) TIMING.—

(A) DEDUCTION.—Contributions described in paragraph (1) shall be deductible in the taxable year of the employer with or within which the calendar year for which the contributions were made ends.

(B) CONTRIBUTIONS AFTER END OF YEAR.—For purposes of this subsection, contributions shall be treated as made for a taxable year if they are made on account of the taxable year and are made not later than the time prescribed by law for filing the return for the taxable year (including extensions thereof).

* * * * * * *

SEC. 406. EMPLOYEES OF FOREIGN AFFILIATES COVERED BY SECTION 3121(l) AGREEMENTS.

(a) * * *

* * * * * * *

[(c) TERMINATION OF STATUS AS DEEMED EMPLOYEE NOT TO BE TREATED AS SEPARATION FROM SERVICE FOR PURPOSES OF LIMITATION OF TAX.—For purposes of applying section 402(d) with respect to an individual who is treated as an employee of an American employer under subsection (a), such individual shall not be considered as separated from the service of such American employer solely by reason of the fact that—

[(1) the agreement entered into by such American employer under section 3121(l) which covers the employment of such individual is terminated under the provisions of such section,

[(2) such individual becomes an employee of a foreign affiliate with respect to which such agreement does not apply,

[(3) such individual ceases to be an employee of the foreign affiliate by reason of which he is treated as an employee of such American employer, if he becomes an employee of another entity in which such American employer has not less than a 10-percent interest (within the meaning of section 3121(l)(8)(B)), or

[(4) the provision of the plan described in subsection (a)(2) is terminated.]

* * * * * * *

(e) TREATMENT AS EMPLOYEE UNDER RELATED PROVISIONS.—An individual who is treated as an employee of an American employer under subsection (a) shall also be treated as an employee of such American employer, with respect to the plan described in subsection (a)(2), for purposes of applying the following provisions of this title:

(1) Section 72(f) (relating to special rules for computing employees' contributions).

[(2) Section 101(b) (relating to employees' death benefits).]

[(3)] *(2)* Section 2039 (relating to annuities).

* * * * * * *

SEC. 407. CERTAIN EMPLOYEES OF DOMESTIC SUBSIDIARIES ENGAGED IN BUSINESS OUTSIDE THE UNITED STATES.

(a) * * *

* * * * * * *

[(c) TERMINATION OF STATUS AS DEEMED EMPLOYEE NOT TO BE TREATED AS SEPARATION FROM SERVICE FOR PURPOSES OF LIMITATIONS OF TAX.—For purposes of applying section 402(d) with respect to an individual who is treated as an employee of a domestic parent corporation under subsection (a), such individual shall not be considered as separated from the service of such domestic parent corporation solely by reason of the fact that—

[(1) the corporation of which such individual is an employee ceases, for any taxable year, to be a domestic subsidiary within the meaning of subsection (a)(2)(A),

[(2) such individual ceases to be an employee of a domestic subsidiary of such domestic parent corporation, if he becomes an employee of another corporation controlled by such domestic parent corporation, or

[(3) the provision of the plan described in subsection (a)(1)(A) is terminated.]

* * * * * * *

(e) TREATMENT AS EMPLOYEE UNDER RELATED PROVISIONS.—An individual who is treated as an employee of a domestic parent corporation under subsection (a) shall also be treated as an employee of such domestic parent corporation, with respect to the plan described in subsection (a)(1)(A), for purposes of applying the following provisions of this title:

(1) Section 72(f) (relating to special rules for computing employees' contributions).

[(2) Section 101(b) (relating to employees' death benefits).]

[(3)] *(2)* Section 2039 (relating to annuities).

* * * * * * *

SEC. 408. INDIVIDUAL RETIREMENT ACCOUNTS.

(a) * * *

* * * * * * *

(d) TAX TREATMENT OF DISTRIBUTIONS.—

(1) * * *

* * * * * * *

(3) ROLLOVER CONTRIBUTION.—An amount is described in this paragraph as a rollover contribution if it meets the requirements of subparagraphs (A) and (B).

(A) * * *

* * * * * * *

(G) SIMPLE RETIREMENT ACCOUNTS.—This paragraph shall not apply to any amount paid or distributed out of a simple retirement account (as defined in section 408(p)) unless—

(i) it is paid into another simple retirement account, or

(ii) in the case of any payment or distribution to which section 72(t)(8) does not apply, it is paid into an individual retirement plan.

* * * * * * *

(i) REPORTS.—The trustee of an individual retirement account and the issuer of an endowment contract described in subsection (b) or an individual retirement annuity shall make such reports regarding such account, contract, or annuity to the Secretary and to the individuals for whom the account, contract, or annuity is, or is to be, maintained with respect to contributions (and the years to which they relate), distributions *aggregating $10 or more in any calendar year*, and such other matters as the Secretary may require under regulations. The reports required by this subsection—

(1) shall be filed at such time and in such manner as the Secretary prescribes in such regulations, and

(2) shall be furnished to individuals—

(A) not later than January 31 of the calendar year following the calendar year to which such reports relate, and

(B) in such manner as the Secretary prescribes in such regulations.

In the case of a simple retirement account under subsection (p), only one report under this subsection shall be required to be submitted each calendar year to the Secretary (at the time provided under paragraph (2)) but, in addition to the report under this subsection, there shall be furnished, within 30 days after each calendar year, to the individual on whose behalf the account is maintained a statement with respect to the account balance as of the close of, and the account activity during, such calendar year.

* * * * * * *

(k) SIMPLIFIED EMPLOYEE PENSION DEFINED.—

(1) * * *

(2) PARTICIPATION REQUIREMENTS.—This paragraph is satisfied with respect to a simplified employee pension for a year only if for such year the employer contributes to the simplified employee pension of each employee who—

(A) has attained age 21,

(B) has performed service for the employer during at least 3 of the immediately preceding 5 years, and

(C) received at least $300 in compensation (within the meaning of section [414(q)(7)] *414(q)(4)*) from the employer for the year.

For purposes of this paragraph, there shall be excluded from consideration employees described in subparagraph (A) or (C) of section 410(b)(3). For purposes of any arrangement described in subsection (k)(6), any employee who is eligible to have employer contributions made on the employee's behalf under such arrangement shall be treated as if such a contribution was made.

* * * * * * *

(6) EMPLOYEE MAY ELECT SALARY REDUCTION ARRANGEMENT.—

(A) * * *

* * * * * * *

(H) TERMINATION.—This paragraph shall not apply to years beginning after December 31, 1996. The preceding sentence shall not apply to a simplified employee pension if the terms of such pension, as in effect on December 31, 1996, provide that an employee may make the election described in subparagraph (A).

(l) SIMPLIFIED EMPLOYER REPORTS.—[An employer]

(1) IN GENERAL.—An employer who makes a contribution on behalf of an employee to a simplified employee pension shall provide such simplified reports with respect to such contributions as the Secretary may require by regulations. The reports required by this subsection shall be filed at such time and in such manner, and information with respect to such contributions shall be furnished to the employee at such time and in such manner, as may be required by regulations.

(2) SIMPLE RETIREMENT ACCOUNTS.—

(A) NO EMPLOYER REPORTS.—Except as provided in this paragraph, no report shall be required under this section by an employer maintaining a qualified salary reduction arrangement under subsection (p).

(B) SUMMARY DESCRIPTION.—The trustee of any simple retirement account established pursuant to a qualified salary reduction arrangement under subsection (p) shall provide to the employer maintaining the arrangement, each year a description containing the following information:

(i) The name and address of the employer and the trustee.

(ii) The requirements for eligibility for participation.

(iii) The benefits provided with respect to the arrangement.

(iv) The time and method of making elections with respect to the arrangement.

(v) The procedures for, and effects of, withdrawals (including rollovers) from the arrangement.

(C) EMPLOYEE NOTIFICATION.—The employer shall notify each employee immediately before the period for which an election described in subsection (p)(5)(C) may be made of the employee's opportunity to make such election. Such notice shall include a copy of the description described in subparagraph (B).

* * * * * * *

(p) SIMPLE RETIREMENT ACCOUNTS.—

(1) IN GENERAL.—For purposes of this title, the term "simple retirement account" means an individual retirement plan (as defined in section 7701(a)(37))—

(A) with respect to which the requirements of paragraphs (3), (4), and (5) are met; and

(B) with respect to which the only contributions allowed are contributions under a qualified salary reduction arrangement.

(2) QUALIFIED SALARY REDUCTION ARRANGEMENT.—

(A) IN GENERAL.—For purposes of this subsection, the term "qualified salary reduction arrangement" means a written arrangement of an eligible employer under which—

(i) an employee eligible to participate in the arrangement may elect to have the employer make payments—

(I) as elective employer contributions to a simple retirement account on behalf of the employee, or

(II) to the employee directly in cash,

(ii) the amount which an employee may elect under clause (i) for any year is required to be expressed as a percentage of compensation and may not exceed a total of $6,000 for any year,

(iii) the employer is required to make a matching contribution to the simple retirement account for any year in an amount equal to so much of the amount the employee elects under clause (i)(I) as does not exceed the applicable percentage of compensation for the year, and

(iv) no contributions may be made other than contributions described in clause (i) or (iii).

(B) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—An employer shall be treated as meeting the requirements of subparagraph (A)(iii) for any year if, in lieu of the contributions described in such clause, the employer elects to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 30-day period for such year under paragraph (5)(C).

(C) DEFINITIONS.—For purposes of this subsection—

(i) ELIGIBLE EMPLOYER.—The term "eligible employer" means an employer who employs 100 or fewer employees on any day during the year.

(ii) APPLICABLE PERCENTAGE.—

(I) IN GENERAL.—The term "applicable percentage" means 3 percent.

(II) ELECTION OF LOWER PERCENTAGE.—An employer may elect to apply a lower percentage (not less than 1 percent) for any year for all employees eligible to participate in the plan for such year if the employer notifies the employees of such lower

percentage within a reasonable period of time before the 30-day election period for such year under paragraph (5)(C). An employer may not elect a lower percentage under this subclause for any year if that election would result in the applicable percentage being lower than 3 percent in more than 2 of the years in the 5-year period ending with such year.

(III) SPECIAL RULE FOR YEARS ARRANGEMENT NOT IN EFFECT.—If any year in the 5-year period described in subclause (II) is a year prior to the first year for which any qualified salary reduction arrangement is in effect with respect to the employer (or any predecessor), the employer shall be treated as if the level of the employer matching contribution was at 3 percent of compensation for such prior year.

(D) ARRANGEMENT MAY BE ONLY PLAN OF EMPLOYER.—

(i) IN GENERAL.—An arrangement shall not be treated as a qualified salary reduction arrangement for any year if the employer (or any predecessor employer) maintained a qualified plan with respect to which contributions were made, or benefits were accrued, for service in any year in the period beginning with the year such arrangement became effective and ending with the year for which the determination is being made.

(ii) QUALIFIED PLAN.—For purposes of this subparagraph, the term "qualified plan" means a plan, contract, pension, or trust described in subparagraph (A) or (B) of section 219(g)(5).

(E) COST-OF-LIVING ADJUSTMENT.—The Secretary shall adjust the $6,000 amount under subparagraph (A)(ii) at the same time and in the same manner as under section 415(d), except that the base period taken into account shall be the calendar quarter ending September 30, 1995, and any increase under this subparagraph which is not a multiple of $500 shall be rounded to the next lower multiple of $500.

(3) VESTING REQUIREMENTS.—The requirements of this paragraph are met with respect to a simple retirement account if the employee's rights to any contribution to the simple retirement account are nonforfeitable. For purposes of this paragraph, rules similar to the rules of subsection (k)(4) shall apply.

(4) PARTICIPATION REQUIREMENTS.—

(A) IN GENERAL.—The requirements of this paragraph are met with respect to any simple retirement account for a year only if, under the qualified salary reduction arrangement, all employees of the employer who—

(i) received at least $5,000 in compensation from the employer during any 2 preceding years, and

(ii) are reasonably expected to receive at least $5,000 in compensation during the year,

are eligible to make the election under paragraph (2)(A)(i) or receive the nonelective contribution described in paragraph (2)(B).

(B) EXCLUDABLE EMPLOYEES.—An employer may elect to exclude from the requirement under subparagraph (A) employees described in section 410(b)(3).

(5) ADMINISTRATIVE REQUIREMENTS.—The requirements of this paragraph are met with respect to any simplified retirement account if, under the qualified salary reduction arrangement—

(A) an employer must—

(i) make the elective employer contributions under paragraph (2)(A)(i) not later than the close of the 30-day period following the last day of the month with respect to which the contributions are to be made, and

(ii) make the matching contributions under paragraph (2)(A)(iii) or the nonelective contributions under paragraph (2)(B) not later than the date described in section 404(m)(2)(B),

(B) an employee may elect to terminate participation in such arrangement at any time during the year, except that if an employee so terminates, the arrangement may provide that the employee may not elect to resume participation until the beginning of the next year, and

(C) each employee eligible to participate may elect, during the 30-day period before the beginning of any year (and the 30-day period before the first day such employee is eligible to participate), to participate in the arrangement, or to modify the amounts subject to such arrangement, for such year.

(6) DEFINITIONS.—For purposes of this subsection—

(A) COMPENSATION.—

(i) IN GENERAL.—The term "compensation" means amounts described in paragraphs (3) and (8) of section 6051(a).

(ii) SELF-EMPLOYED.—In the case of an employee described in subparagraph (B), the term "compensation" means net earnings from self-employment determined under section 1402(a) without regard to any contribution under this subsection.

(B) EMPLOYEE.—The term "employee" includes an employee as defined in section 401(c)(1).

(C) YEAR.—The term "year" means the calendar year.

[(p)] *(q)* CROSS REFERENCES.—

(1) * * *

* * * * * * *

Subpart B—Special Rules

* * * * * * *

SEC. 411. MINIMUM VESTING STANDARDS.

(a) GENERAL RULE.—A trust shall not constitute a qualified trust under section 401(a) unless the plan of which such trust is a part provides that an employee's right to his normal retirement benefit

is nonforfeitable upon the attainment of normal retirement age (as defined in paragraph (8)) and in addition satisfies the requirements of paragraphs (1), (2), and (11) of this subsection and the requirements of subsection (b)(3), and also satisfies, in the case of a defined benefit plan, the requirements of subsection (b)(1) and, in the case of a defined contribution plan, the requirements of subsection (b)(2).

(1) * * *

(2) EMPLOYER CONTRIBUTIONS.—A plan satisfies the requirements of this paragraph if it satisfies the requirements of [subparagraph (A), (B), or (C)] *subparagraph (A) or (B).*

(A) 5-YEAR VESTING.—A plan satisfies the requirements of this subparagraph if an employee who has completed at least 5 years of service has a nonforfeitable right to 100 percent of the employee's accrued benefit derived from employer contributions.

* * * * * * *

[(C) MULTIEMPLOYER PLANS.—A plan satisfies the requirements of this subparagraph if—

[(i) the plan is a multiemployer plan (within the meaning of section 414(f)), and

[(ii) under the plan—

[(I) an employee who is covered pursuant to a collective bargaining agreement described in section 414(f)(1)(B) and who has completed at least 10 years of service has a nonforfeitable right to 100 percent of the employee's accrued benefit derived from employer contributions, and

[(II) the requirements of subparagraph (A) or (B) are met with respect to employees not described in subclause (I).]

* * * * * * *

SEC. 414. DEFINITIONS AND SPECIAL RULES.

(a) * * *

(b) EMPLOYEES OF CONTROLLED GROUP OF CORPORATIONS.—For purposes of sections 401, 408(k), *408(p),* 410, 411, 415, and 416, all employees of all corporations which are members of a controlled group of corporations (within the meaning of section 1563(a), determined without regard to section 1563(a)(4) and (e)(3)(C)) shall be treated as employed by a single employer. With respect to a plan adopted by more than one such corporation, the applicable limitations provided by section 404(a) shall be determined as if all such employers were a single employer, and allocated to each employer in accordance with regulations prescribed by the Secretary.

(c) EMPLOYEES OF PARTNERSHIPS, PROPRIETORSHIPS, ETC., WHICH ARE UNDER COMMON CONTROL.—For purposes of sections 401, 408(k), *408(p),* 410, 411, 415, and 416, under regulations prescribed by the Secretary, all employees of trades or businesses (whether or not incorporated) which are under common control shall be treated as employed by a single employer. The regulations prescribed

under this subsection shall be based on principles similar to the principles which apply in the case of subsection (b).

* * * * * * *

(m) EMPLOYEES OF AN AFFILIATED SERVICE GROUP.—

(1) * * *

* * * * * * *

(4) EMPLOYEE BENEFIT REQUIREMENTS.—For purposes of this subsection, the employee benefit requirements listed in this paragraph are—

(A) paragraphs (3), (4), (7), (16), (17), and (26) of section 401(a), and

(B) sections 408(k), *408(p),* 410, 411, 415, and 416.

* * * * * * *

(n) EMPLOYEE LEASING.—

(1) * * *

(2) LEASED EMPLOYEE.—For purposes of paragraph (1), the term "leased employee" means any person who is not an employee of the recipient and who provides services to the recipient if—

(A) * * *

* * * * * * *

[(C) such services are of a type historically performed, in the business field of the recipient, by employees.]

(C) such services are performed under primary direction or control by the recipient.

(3) REQUIREMENTS.—For purposes of this subsection, the requirements listed in this paragraph are—

(A) paragraphs (3), (4), (7), (16), (17), and (26) of section 401(a),

(B) sections 408(k), *408(p),* 410, 411, 415, and 416, and

(C) sections 79, 106, 117(d), 120, 125, 127, 129, 132, 274(j), 505, and 4980B.

* * * * * * *

(q) HIGHLY COMPENSATED EMPLOYEE.—

[(1) IN GENERAL.—The term "highly compensated employee" means any employee who, during the year or the preceding year—

[(A) was at any time a 5-percent owner,

[(B) received compensation from the employer in excess of $75,000,

[(C) received compensation from the employer in excess of $50,000 and was in the top-paid group of employees for such year, or

[(D) was at any time an officer and received compensation greater than 50 percent of the amount in effect under section 415(b)(1)(A) for such year.

The Secretary shall adjust the $75,000 and $50,000 amounts under this paragraph at the same time and in the same manner as under section 415(d).

[(2) SPECIAL RULE FOR CURRENT YEAR.—In the case of the year for which the relevant determination is being made, an

employee not described in subparagraph (B), (C), or (D) of paragraph (1) for the preceding year (without regard to this paragraph) shall not be treated as described in subparagraph (B), (C), or (D) of paragraph (1) unless such employee is a member of the group consisting of the 100 employees paid the greatest compensation during the year for which such determination is being made.]

(1) IN GENERAL.—The term "highly compensated employee" means any employee who—

(A) was a 5-percent owner at any time during the year or the preceding year, or

(B) for the preceding year—

(i) had compensation from the employer in excess of $80,000, and

(ii) was in the top-paid group of the employer.

The Secretary shall adjust the $80,000 amount under subparagraph (B) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1996.

[(3)] *(2)* 5-PERCENT OWNER.—An employee shall be treated as a 5-percent owner for any year if at any time during such year such employee was a 5-percent owner (as defined in section 416(i)(1)) of the employer.

[(4)] *(3)* TOP-PAID GROUP.—An employee is in the top-paid group of employees for any year if such employee is in the group consisting of the top 20 percent of the employees when ranked on the basis of compensation paid during such year.

[(5) SPECIAL RULES FOR TREATMENT OF OFFICERS.—

[(A) NOT MORE THAN 50 OFFICERS TAKEN INTO ACCOUNT.—For purposes of paragraph (1)(D), no more than 50 employees (or, if lesser, the greater of 3 employees or 10 percent of the employees) shall be treated as officers.

[(B) AT LEAST 1 OFFICER TAKEN INTO ACCOUNT.—If for any year no officer of the employer is described in paragraph (1)(D), the highest paid officer of the employer for such year shall be treated as described in such paragraph.

[(6) TREATMENT OF CERTAIN FAMILY MEMBERS.—

[(A) IN GENERAL.—If any individual is a member of the family of a 5-percent owner or of a highly compensated employee in the group consisting of the 10 highly compensated employees paid the greatest compensation during the year, then—

[(i) such individual shall not be considered a separate employee, and

[(ii) any compensation paid to such individual (and any applicable contribution or benefit on behalf of such individual) shall be treated as if it were paid to (or on behalf of) the 5-percent owner or highly compensated employee.

[(B) FAMILY.—For purposes of subparagraph (A), the term "family" means, with respect to any employee, such employee's spouse and lineal ascendants or descendants and the spouses of such lineal ascendants or descendants.

[(C) RULES TO APPLY TO OTHER PROVISIONS.—

[(i) IN GENERAL.—Except as provided in regulations and in clause (ii), the rules of subparagraph (A) shall be applied in determining the compensation of (or any contributions or benefits on behalf of) any employee for purposes of any section with respect to which a highly compensated employee is defined by reference to this subsection.

[(ii) EXCEPTION FOR DETERMINING INTEGRATION LEVELS.—Clause (i) shall not apply in determining the portion of the compensation of a participant which is under the integration level for purposes of section 401(l).

[(7) COMPENSATION.—For purposes of this subsection—

[(A) IN GENERAL.—The term "compensation" means compensation within the meaning of section 415(c)(3).

[(B) CERTAIN PROVISIONS NOT TAKEN INTO ACCOUNT.—The determination under subparagraph (A) shall be made—

[(i) without regard to sections 125, 402(e)(3), and 402(h)(1)(B), and

[(ii) in the case of employer contributions made pursuant to a salary reduction agreement, without regard to section 403(b).

[(8) EXCLUDED EMPLOYEES.—For purposes of subsection (r) and for purposes of determining the number of employees in the top-paid group under paragraph (4) or the number of officers taken into account under paragraph (5), the following employees shall be excluded—

[(A) employees who have not completed 6 months of service,

[(B) employees who normally work less than 17-1/2 hours per week,

[(C) employees who normally work during not more than 6 months during any year,

[(D) employees who have not attained age 21, and

[(E) except to the extent provided in regulations, employees who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and the employer.

Except as provided by the Secretary, the employer may elect to apply subparagraph (A), (B), (C), or (D) by substituting a shorter period of service, smaller number of hours or months, or lower age for the period of service, number of hours or months, or age (as the case may be) than that specified in such subparagraph.]

(4) COMPENSATION.—For purposes of this subsection, the term "compensation" has the meaning given such term by section 415(c)(3).

[(9)] *(5)* FORMER EMPLOYEES.—A former employee shall be treated as a highly compensated employee if—

(A) such employee was a highly compensated employee when such employee separated from service, or

(B) such employee was a highly compensated employee at any time after attaining age 55.

[(10)] *(6)* COORDINATION WITH OTHER PROVISIONS.—Subsections (b), (c), (m), (n), and (o) shall be applied before the application of this section.

[(11)] *(7)* SPECIAL RULE FOR NONRESIDENT ALIENS.—For purposes of this subsection and subsection (r), employees who are nonresident aliens and who receive no earned income (within the meaning of section 911(d)(2)) from the employer which constitutes income from sources within the United States (within the meaning of section 861(a)(3)) shall not be treated as employees.

[(12) SIMPLIFIED METHOD FOR DETERMINING HIGHLY COMPENSATED EMPLOYEES.—

[(A) IN GENERAL.—If an election by the employer under this paragraph applies to any year, in determining whether an employee is a highly compensated employee for such year—

[(i) subparagraph (B) of paragraph (1) shall be applied by substituting "$50,000" for "$75,000", and

[(ii) subparagraph (C) of paragraph (1) shall not apply.

[(B) REQUIREMENT FOR ELECTION.—An election under this paragraph shall not apply to any year unless—

[(i) at all times during such year, the employer maintained significant business activities (and employed employees) in at least 2 significantly separate geographic areas, and

[(ii) the employer satisfies such other conditions as the Secretary may prescribe.]

(r) SPECIAL RULES FOR SEPARATE LINE OF BUSINESS.—

(1) * * *

(2) LINE OF BUSINESS MUST HAVE 50 EMPLOYEES, ETC.—A line of business shall not be treated as separate under paragraph (1) unless—

(A) such line of business has at least 50 employees who are not excluded under [subsection (q)(8)] *paragraph (9)*,

* * * * * * *

(9) EXCLUDED EMPLOYEES.—For purposes of this subsection, the following employees shall be excluded:

(A) Employees who have not completed 6 months of service.

(B) Employees who normally work less than 17½ hours per week.

(C) Employees who normally work not more than 6 months during any year.

(D) Employees who have not attained the age of 21.

(E) Except to the extent provided in regulations, employees who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and the employer.

Except as provided by the Secretary, the employer may elect to apply subparagraph (A), (B), (C), or (D) by substituting a short-

er period of service, smaller number of hours or months, or lower age for the period of service, number of hours or months, or age (as the case may be) specified in such subparagraph.

(s) COMPENSATION.—For purposes of any applicable provision—

(1) * * *

(2) EMPLOYER MAY ELECT *NOT* TO TREAT CERTAIN DEFERRALS AS COMPENSATION.—An employer may elect *not* to include as compensation any amount which is contributed by the employer pursuant to a salary reduction agreement and which is not includible in the gross income of an employee under section 125, 402(e)(3), 402(h), or 403(b).

* * * * * * *

(u) SPECIAL RULES RELATING TO VETERANS' REEMPLOYMENT RIGHTS UNDER USERRA.—

(1) TREATMENT OF CERTAIN CONTRIBUTIONS MADE PURSUANT TO VETERANS' REEMPLOYMENT RIGHTS.—If any contribution is made by an employer or an employee under an individual account plan with respect to an employee, or by an employee to a defined benefit plan that provides for employee contributions, and such contribution is required by reason of such employee's rights under chapter 43 of title 38, United States Code, resulting from qualified military service, then—

(A) such contribution shall not be subject to any otherwise applicable limitation contained in section 402(g), 402(h), 403(b), 404(a), 404(h), 408, 415, or 457, and shall not be taken into account in applying such limitations to other contributions or benefits under such plan or any other plan, with respect to the year in which the contribution is made,

(B) such contribution shall be subject to the limitations referred to in subparagraph (A) with respect to the year to which the contribution relates (in accordance with rules prescribed by the Secretary), and

(C) such plan shall not be treated as failing to meet the requirements of section 401(a)(4), 401(a)(26), 401(k)(3), 401(k)(11), 401(k)(12), 401(m), 403(b)(12), 408(k)(3), 408(k)(6), 408(p), 410(b), or 416 by reason of the making of (or the right to make) such contribution.

For purposes of the preceding sentence, any elective deferral or employee contribution made under paragraph (2) shall be treated as required by reason of the employee's rights under such chapter 43.

(2) REEMPLOYMENT RIGHTS UNDER USERRA WITH RESPECT TO ELECTIVE DEFERRALS.—

(A) IN GENERAL.—For purposes of this subchapter and section 457, if an employee is entitled to the benefits of chapter 43 of title 38, United States Code, with respect to any plan which provides for elective deferrals, the employer sponsoring the plan shall be treated as meeting the requirements of such chapter 43 with respect to such elective deferrals only if such employer—

(i) permits such employee to make additional elective deferrals under such plan (in the amount determined under subparagraph (B) or such lesser amount as is

elected by the employee) during the period which begins on the date of the reemployment of such employee with such employer and has the same length as the lesser of—

(I) the product of 3 and the period of qualified military service which resulted in such rights, and

(II) 5 years, and

(ii) makes a matching contribution with respect to any additional elective deferral made pursuant to clause (i) which would have been required had such deferral actually been made during the period of such qualified military service.

(B) AMOUNT OF MAKEUP REQUIRED.—The amount determined under this subparagraph with respect to any plan is the maximum amount of the elective deferrals that the individual would have been permitted to make under the plan in accordance with the limitations referred to in paragraph (1)(A) during the period of qualified military service if the individual had continued to be employed by the employer during such period and received compensation as determined under paragraph (7). Proper adjustment shall be made to the amount determined under the preceding sentence for any elective deferrals actually made during the period of such qualified military service.

(C) ELECTIVE DEFERRAL.—For purposes of this paragraph, the term "elective deferral" has the meaning given such term by section 402(g)(3); except that such term shall include any deferral of compensation under an eligible deferred compensation plan (as defined in section 457(b)).

(D) AFTER-TAX EMPLOYEE CONTRIBUTIONS.—References in subparagraphs (A) and (B) to elective deferrals shall be treated as including references to employee contributions.

(3) CERTAIN RETROACTIVE ADJUSTMENTS NOT REQUIRED.—For purposes of this subchapter and subchapter E, no provision of chapter 43 of title 38, United States Code, shall be construed as requiring—

(A) any crediting of earnings to an employee with respect to any contribution before such contribution is actually made, or

(B) any allocation of any forfeiture with respect to the period of qualified military service.

(4) LOAN REPAYMENT SUSPENSIONS PERMITTED.—If any plan suspends the obligation to repay any loan made to an employee from such plan for any part of any period during which such employee is performing service in the uniformed services (as defined in chapter 43 of title 38, United States Code), whether or not qualified military service, such suspension shall not be taken into account for purposes of section 72(p), 401(a), or 4975(d)(1).

(5) QUALIFIED MILITARY SERVICE.—For purposes of this subsection, the term "qualified military service" means any service in the uniformed services (as defined in chapter 43 of title 38, United States Code) by any individual if such individual is en-

titled to reemployment rights under such chapter with respect to such service.

(6) INDIVIDUAL ACCOUNT PLAN.—For purposes of this subsection, the term "individual account plan" means any defined contribution plan (including any tax-sheltered annuity plan under section 403(b), any simplified employee pension under section 408(k), any qualified salary reduction arrangement under section 408(p), and any eligible deferred compensation plan (as defined in section 457(b)).

(7) COMPENSATION.—For purposes of sections 403(b)(3), 415(c)(3), and 457(e)(5), an employee who is in qualified military service shall be treated as receiving compensation from the employer during such period of qualified military service equal to—

(A) the compensation the employee would have received during such period if the employee were not in qualified military service, determined based on the rate of pay the employee would have received from the employer but for absence during the period of qualified military service, or

(B) if the compensation the employee would have received during such period was not reasonably certain, the employee's average compensation from the employer during the 12-month period immediately preceding the qualified military service (or, if shorter, the period of employment immediately preceding the qualified military service).

(8) USERRA REQUIREMENTS FOR QUALIFIED RETIREMENT PLANS.—For purposes of this subchapter and section 457, an employer sponsoring a retirement plan shall be treated as meeting the requirements of chapter 43 of title 38, United States Code, only if each of the following requirements is met:

(A) An individual reemployed under such chapter is treated with respect to such plan as not having incurred a break in service with the employer maintaining the plan by reason of such individual's period of qualified military service.

(B) Each period of qualified military service served by an individual is, upon reemployment under such chapter, deemed with respect to such plan to constitute service with the employer maintaining the plan for the purpose of determining the nonforfeitability of the individual's accrued benefits under such plan and for the purpose of determining the accrual of benefits under such plan.

(C) An individual reemployed under such chapter is entitled to accrued benefits that are contingent on the making of, or derived from, employee contributions or elective deferrals only to the extent the individual makes payment to the plan with respect to such contributions or deferrals. No such payment may exceed the amount the individual would have been permitted or required to contribute had the individual remained continuously employed by the employer throughout the period of qualified military service. Any payment to such plan shall be made during the period beginning with the date of reemployment and whose duration

is 3 times the period of the qualified military service (but not greater than 5 years).

(9) PLANS NOT SUBJECT TO TITLE 38.—This subsection shall not apply to any retirement plan to which chapter 43 of title 38, United States Code, does not apply.

(10) REFERENCES.—For purposes of this section, any reference to chapter 43 of title 38, United States Code, shall be treated as a reference to such chapter as in effect on December 12, 1994 (without regard to any subsequent amendment).

SEC. 415. LIMITATIONS ON BENEFITS AND CONTRIBUTION UNDER QUALIFIED PLANS.

(a) GENERAL RULE.—

(1) TRUSTS.—A trust which is a part of a pension, profitsharing, or stock bonus plan shall not constitute a qualified trust under section 401(a) if—

(A) in the case of a defined benefit plan, the plan provides for the payment of benefits with respect to a participant which exceed the limitation of subsection (b), *or*

(B) in the case of a defined contribution plan, contributions and other additions under the plan with respect to any participant for any taxable year exceed the limitation of subsection (c)[, or].

[(C) in any case in which an individual is a participant in both a defined benefit plan and a defined contribution plan maintained by the employer, the trust has been disqualified under subsection (g).]

* * * * * * *

(b) LIMITATION FOR DEFINED BENEFIT PLANS.—

(1) * * *

(2) ANNUAL BENEFIT.—

(A) * * *

* * * * * * *

(E) LIMITATION ON CERTAIN ASSUMPTIONS.—

(i) [Except as provided in clause (ii), for purposes of adjusting any benefit or limitation under subparagraph (B) or (C),] *For purposes of adjusting any limitation under subparagraph (C) and, except as provided in clause (ii), for purposes of adjusting any benefit under subparagraph (B),* the interest rate assumption shall not be less than the greater of 5 percent or the rate specified in the plan.

(ii) [For purposes of adjusting the benefit or limitation of any form of benefit subject to section 417(e)(3),] *For purposes of adjusting any benefit under subparagraph (B) for any form of benefit subject to section 417(e)(3),* the applicable interest rate (as defined in section 417(e)(3)) shall be substituted for "5 percent" in clause (i).

* * * * * * *

(I) EXEMPTION FOR SURVIVOR AND DISABILITY BENEFITS PROVIDED UNDER GOVERNMENTAL PLANS.—Subparagraph

(C) of this paragraph and paragraph (5) shall not apply to—

(i) income received from a governmental plan (as defined in section 414(d)) as a pension, annuity, or similar allowance as the result of the recipient becoming disabled by reason of personal injuries or sickness, or

(ii) amounts received from a governmental plan by the beneficiaries, survivors, or the estate of an employee as the result of the death of the employee.

* * * * * * *

(5) REDUCTION FOR PARTICIPATION OR SERVICE OF LESS THAN 10 YEARS.—

(A) * * *

(B) COMPENSATION AND BENEFITS LIMITATIONS.—The provisions of subparagraph (A) shall apply to the limitations under paragraphs (1)(B) and (4) [and subsection (e)], except that such subparagraph shall be applied with respect to years of service with an employer rather than years of participation in a plan.

* * * * * * *

(10) SPECIAL RULE FOR STATE AND LOCAL GOVERNMENT PLANS.—

(A) * * *

* * * * * * *

(C) ELECTION.—[This]

(i) IN GENERAL.—This paragraph shall not apply to any plan unless each employer maintaining the plan elects before the close of the 1st plan year beginning after December 31, 1989, to have this subsection (other than paragraph (2)(G)) applied without regard to paragraph (2)(F).

(ii) REVOCATION OF ELECTION.—An election under clause (i) may be revoked not later than the last day of the third plan year beginning after the date of the enactment of this clause. The revocation shall apply to all plan years to which the election applied and to all subsequent plan years. Any amount paid by a plan in a taxable year ending after the revocation shall be includible in income in such taxable year under the rules of this chapter in effect for such taxable year, except that, for purposes of applying the limitations imposed by this section, any portion of such amount which is attributable to any taxable year during which the election was in effect shall be treated as received in such taxable year.

(11) SPECIAL LIMITATION RULE FOR GOVERNMENTAL PLANS.—In the case of a governmental plan (as defined in section 414(d)), subparagraph (B) of paragraph (1) shall not apply.

(c) LIMITATION FOR DEFINED CONTRIBUTION PLANS.—

(1) * * *

* * * * * * *

(3) PARTICIPANT'S COMPENSATION.—For purposes of paragraph (1)—

(A) * * *

* * * * * * *

(C) SPECIAL RULES FOR PERMANENT AND TOTAL DISABILITY.—In the case of a participant in any defined contribution plan—

(i) who is permanently and totally disabled (as defined in section 22(e)(3)),

(ii) who is not a highly compensated employee (within the meaning of section 414(q)), and

(iii) with respect to whom the employer elects, at such time and in such manner as the Secretary may prescribe, to have this subparagraph apply,

the term "participant's compensation" means the compensation the participant would have received for the year if the participant was paid at the rate of compensation paid immediately before becoming permanently and totally disabled. This subparagraph shall apply only if contributions made with respect to amounts treated as compensation under this subparagraph are nonforfeitable when made. *If a defined contribution plan provides for the continuation of contributions on behalf of all participants described in clause (i) for a fixed or determinable period, this subparagraph shall be applied without regard to clauses (ii) and (iii).*

(D) CERTAIN DEFERRALS INCLUDED.—The term "participant's compensation" shall include—

(i) any elective deferral (as defined in section 402(g)(3)), and

(ii) any amount which is contributed by the employer at the election of the employee and which is not includible in the gross income of the employee under section 125 or 457.

* * * * * * *

[(e) LIMITATION IN CASE OF DEFINED BENEFIT PLAN AND DEFINED CONTRIBUTION PLAN FOR SAME EMPLOYEE.—

[(1) IN GENERAL.—In any case in which an individual is a participant in both a defined benefit plan and a defined contribution plan maintained by the same employer, the sum of the defined benefit plan fraction and the defined contribution plan fraction for any year may not exceed 1.0.

[(2) DEFINED BENEFIT PLAN FRACTION.—For purposes of this subsection, the defined benefit plan fraction for any year is a fraction—

[(A) the numerator of which is the projected annual benefit of the participant under the plan (determined as of the close of the year), and

[(B) the denominator of which is the lesser of—

[(i) the product of 1.25, multiplied by the dollar limitation in effect under subsection (b)(1)(A) for such year, or

[(ii) the product of—

[(I) 1.4, multiplied by

[(II) the amount which may be taken into account under subsection (b)(1)(B) with respect to such individual under the plan for such year.

[(3) DEFINED CONTRIBUTION PLAN FRACTION.—For purposes of this subsection, the defined contribution plan fraction for any year is a fraction—

[(A) the numerator of which is the sum of the annual additions to the participant's account as of the close of the year, and

[(B) the denominator of which is the sum of the lesser of the following amounts determined for such year and for each prior year of service with the employer:

[(i) the product of 1.25, multiplied by the dollar limitation in effect under subsection (c)(1)(A) for such year (determined without regard to subsection (c)(6)), or

[(ii) the product of—

[(I) 1.4, multiplied by—

[(II) the amount which may be taken into account under subsection (c)(1)(B) (or subsection (c)(7), if applicable) with respect to such individual under such plan for such year.

[(4) SPECIAL TRANSITION RULES FOR DEFINED CONTRIBUTION FRACTION.—In applying paragraph (3) with respect to years beginning before January 1, 1976—

[(A) the aggregate amount taken into account under paragraph (3)(A) may not exceed the aggregate amount taken into account under paragraph (3)(B), and

[(B) the amount taken into account under subsection (c)(2)(B)(i) for any year concerned is an amount equal to—

[(i) the excess of the aggregate amount of employee contributions for all years beginning before January 1, 1976, during which the employee was an active participant of the plan, over 10 percent of the employee's aggregate compensation for all such years, multiplied by

[(ii) a fraction the numerator of which is 1 and the denominator of which is the number of years beginning before January 1, 1976, during which the employee was an active participant in the plan.

Employee contributions made on or after October 2, 1973, shall be taken into account under subparagraph (B) of the preceding sentence only to the extent that the amount of such contributions does not exceed the maximum amount of contributions permissible under the plan as in effect on October 2, 1973.

[(5) SPECIAL RULES FOR SECTIONS 403(b) AND 408.—For purposes of this section, any annuity contract described in section 403(b) (except in the case of a participant who has elected under subsection (c)(4)(D) to have the provisions of subsection (c)(4)(C) apply) for the benefit of a participant shall be treated as a defined contribution plan maintained by each employer with respect to which the participant has the control required under subsection (b) or (c) of section 414 (as modified by subsection (h)). For purposes of this section, any contribution by

an employer to a simplified employee pension for an individual for a taxable year shall be treated as an employer contribution to a defined contribution plan for such individual for such year. In the case of any annuity contract described in section 403(b), the amount of the contribution disqualified by reason of subsection (g) shall reduce the exclusion allowance as provided in section 403(b)(2).

[(6) SPECIAL TRANSITION RULE FOR DEFINED CONTRIBUTION FRACTION FOR YEARS ENDING AFTER DECEMBER 31, 1982.—

[(A) IN GENERAL.—At the election of the plan administrator, in applying paragraph (3) with respect to any year ending after December 31, 1982, the amount taken into account under paragraph (3)(B) with respect to each participant for all years ending before January 1, 1983, shall be an amount equal to the product of—

[(i) the amount determined under paragraph (3)(B) (as in effect for the year ending in 1982) for the year ending in 1982, multiplied by

[(ii) the transition fraction.

[(B) TRANSITION FRACTION.—The term "transition fraction" means a fraction—

[(i) the numerator of which is the lesser of—

[(I) $51,875, or

[(II) 1.4, multiplied by 25 percent of the compensation of the participant for the year ending in 1981, and

[(ii) the denominator of which is the lesser of—

[(I) $41,500, or

[(II) 25 percent of the compensation of the participant for the year ending in 1981.

[(C) PLAN MUST HAVE BEEN IN EXISTENCE ON OR BEFORE JULY 1, 1982.—This paragraph shall apply only to plans which were in existence on or before July 1, 1982.]

(f) COMBINING OF PLANS.—

(1) IN GENERAL.—For purposes of applying the limitations of [subsections (b), (c), and (e)] *subsections (b) and (c)*—

(A) all defined benefit plans (whether or not terminated) of an employer are to be treated as one defined benefit plan, and

(B) all defined contribution plans (whether or not terminated) of an employer are to be treated as one defined contribution plan.

* * * * * * *

(g) AGGREGATION OF PLANS.—The Secretary, in applying the provisions of this section to benefits or contributions under more than one plan maintained by the same employer, and to any trusts, contracts, accounts, or bonds referred to in subsection (a)(2), with respect to which the participant has the control required under section 414(b) or (c), as modified by subsection (h), shall, under regulations prescribed by the Secretary, disqualify one or more trusts, plans, contracts, accounts, or bonds, or any combination thereof until such benefits or contributions do not exceed the limitations contained in this section. In addition to taking into account such other factors as may be necessary to carry out the purposes of

[subsections (e) and (f)] *subsection (f)*, the regulations prescribed under this paragraph shall provide that no plan which has been terminated shall be disqualified until all other trusts, plans, contracts, accounts, or bonds have been disqualified.

* * * * * * *

(k) SPECIAL RULES.—

(1) DEFINED BENEFIT PLAN AND DEFINED CONTRIBUTION PLAN.—For purposes of this title, the term "defined contribution plan" or "defined benefit plan" means a defined contribution plan (within the meaning of section 414(i)) or a defined benefit plan (within the meaning of section 414(j)), whichever applies, which is—

(A) a plan described in section 401(a) which includes a trust which is exempt from tax under section 501(a),

(B) an annuity plan described in section 403(a),

(C) an annuity contract described in section 403(b), *or*

[(D) an individual retirement account described in section 408(a),

[(E) an individual retirement annuity described in section 408(b), or]

[(F)] *(D)* a simplified employee pension.

(2) CONTRIBUTIONS TO PROVIDE COST-OF-LIVING PROTECTION UNDER DEFINED BENEFIT PLANS.—

(A) IN GENERAL.—In the case of a defined benefit plan which maintains a qualified cost-of-living arrangement—

[(i) any contribution made directly by an employee under such arrangement—

[(I) shall not be treated as an annual addition for purposes of subsection (c), but

[(II) shall be so treated for purposes of subsection (e), and]

(i) any contribution made directly by an employee under such an arrangement shall not be treated as an annual addition for purposes of subsection (c), and

(ii) any benefit under such arrangement which is allocable to an employer contribution which was transferred from a defined contribution plan and to which the requirements of subsection (c) were applied shall, for purposes of subsection (b), be treated as a benefit derived from an employee contribution (and [subsections (c) and (e)] *subsection (c)* shall not again apply to such contribution by reason of such transfer).

* * * * * * *

(m) TREATMENT OF QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENTS.—

(1) GOVERNMENTAL PLAN NOT AFFECTED.—In determining whether a governmental plan (as defined in section 414(d)) meets the requirements of this section, benefits provided under a qualified governmental excess benefit arrangement shall not be taken into account. Income accruing to a governmental plan (or to a trust that is maintained solely for the purpose of providing benefits under a qualified governmental excess benefit arrangement) in respect of a qualified governmental excess ben-

efit arrangement shall constitute income derived from the exercise of an essential governmental function upon which such governmental plan (or trust) shall be exempt from tax under section 115.

(2) TAXATION OF PARTICIPANT. —For purposes of this chapter—

(A) the taxable year or years for which amounts in respect of a qualified governmental excess benefit arrangement are includible in gross income by a participant, and

(B) the treatment of such amounts when so includible by the participant,

shall be determined as if such qualified governmental excess benefit arrangement were treated as a plan for the deferral of compensation which is maintained by a corporation not exempt from tax under this chapter and which does not meet the requirements for qualification under section 401.

(3) QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENT.—For purposes of this subsection, the term "qualified governmental excess benefit arrangement" means a portion of a governmental plan if—

(A) such portion is maintained solely for the purpose of providing to participants in the plan that part of the participant's annual benefit otherwise payable under the terms of the plan that exceeds the limitations on benefits imposed by this section,

(B) under such portion no election is provided at any time to the participant (directly or indirectly) to defer compensation, and

(C) benefits described in subparagraph (A) are not paid from a trust forming a part of such governmental plan unless such trust is maintained solely for the purpose of providing such benefits.

SEC. 416. SPECIAL RULES FOR TOP-HEAVY PLANS.

(a) * * *

* * * * * * *

(g) TOP-HEAVY PLAN DEFINED.—For purposes of this section—

(1) * * *

* * * * * * *

(4) OTHER SPECIAL RULES.—For purposes of this subsection—

(A) * * *

* * * * * * *

(G) SIMPLE RETIREMENT ACCOUNTS.—The term "top-heavy plan" shall not include a simple retirement account under section 408(p).

[(h) ADJUSTMENTS IN SECTION 415 LIMITS FOR TOP-HEAVY PLANS.—

[(1) IN GENERAL.—In the case of any top-heavy plan, paragraphs (2)(B) and (3)(B) of section 415(e) shall be applied by substituting "1.0" for "1.25".

[(2) EXCEPTION WHERE BENEFITS FOR KEY EMPLOYEES DO NOT EXCEED 90 PERCENT OF TOTAL BENEFITS AND ADDITIONAL CONTRIBUTIONS ARE MADE FOR NON-KEY EMPLOYEES.—Paragraph

(1) shall not apply with respect to any top-heavy plan if the requirements of subparagraphs (A) and (B) of this paragraph are met with respect to such plan.

[(A) MINIMUM BENEFIT REQUIREMENTS.—

[(i) IN GENERAL.—The requirements of this subparagraph are met with respect to any top-heavy plan if such plan (and any plan required to be included in an aggregation group with such plan) meets the requirements of subsection (c) as modified by clause (ii).

[(ii) MODIFICATIONS.—For purposes of clause (i)—

[(I) paragraph (1)(B) of subsection (c) shall be applied by substituting "3 percent" for "2 percent", and by increasing (but not by more than 10 percentage points) 20 percent by 1 percentage point for each year for which such plan was taken into account under this subsection, and

[(II) paragraph (2)(A) shall be applied by substituting "4 percent" for "3 percent".

[(B) BENEFITS FOR KEY EMPLOYEES CANNOT EXCEED 90 PERCENT OF TOTAL BENEFITS.—A plan meets the requirements of this subparagraph if such plan would not be a top-heavy plan if "90 percent" were substituted for "60 percent" each place it appears in paragraphs (1)(A) and (2)(B) of subsection (g).

[(3) TRANSITION RULE.—If, but for this paragraph, paragraph (1) would begin to apply with respect to any top-heavy plan, the application of paragraph (1) shall be suspended with respect to any individual so long as there are no—

[(A) employer contributions, forfeitures, or voluntary nondeductible contributions allocated to such individual, or

[(B) accruals for such individual under the defined benefit plan.

[(4) COORDINATION WITH TRANSITIONAL RULE UNDER SECTION 415.—In the case of any top-heavy plan to which paragraph (1) applies, section 415(e)(6)(B)(i) shall be applied by substituting "$41,500" for "$51,875".]

(i) DEFINITIONS.—For purposes of this section—

(1) KEY EMPLOYEE.—

(A) IN GENERAL.—The term "key employee" means an employee who, at any time during the plan year or any of the 4 preceding plan years, is—

(i) * * *

* * * * * * *

For purposes of clause (i), no more than 50 employees (or, if lesser, the greater of 3 or 10 percent of the employees) shall be treated as officers. For purposes of clause (ii), if 2 employees have the same interest in the employer, the employee having greater annual compensation from the employer shall be treated as having a larger interest. Such term shall not include any officer or employee of an entity referred to in section 414(d) (relating to governmental plans). For purposes of determining the

number of officers taken into account under clause (i), employees described in section [414(q)(8)] *414(r)(9)* shall be excluded.

* * * * * * *

(D) COMPENSATION.—For purposes of this paragraph, the term "compensation" has the meaning given such term by section [414(q)(7)] *414(q)(4)*.

* * * * * * *

Subpart D—Treatment of Welfare Benefit Funds

* * * * * * *

SEC. 419A. QUALIFIED ASSET ACCOUNT; LIMITATION ON ADDITIONS TO ACCOUNT.

(a) * * *

* * * * * * *

(c) ACCOUNT LIMIT.—For purposes of this section—

(1) * * *

* * * * * * *

(3) AMOUNT TAKEN INTO ACCOUNT FOR SUB OR [SEVERENCE] *SEVERANCE* PAY BENEFITS.—

(A) IN GENERAL.—The account limit for any taxable year with respect to SUB or severance pay benefits is 75 percent of the average annual qualified direct costs for SUB or severance pay benefits for any 2 of the immediately preceding 7 taxable years (as selected by the fund).

* * * * * * *

Subpart E—Treatment of Transfers to Retiree Health Accounts

* * * * * * *

SEC. 420. TRANSFERS OF EXCESS PENSION ASSETS TO RETIREE HEALTH ACCOUNTS.

(a) * * *

* * * * * * *

(e) DEFINITION AND SPECIAL RULES.—For purposes of this section—

(1) QUALIFIED CURRENT RETIREE HEALTH LIABILITIES.—For purposes of this section—

(A) * * *

* * * * * * *

(C) APPLICABLE HEALTH BENEFITS.—The term "applicable health benefits" [mean] *means* health benefits or coverage which are provided to—

(i) * * *

* * * * * * *

PART II—CERTAIN STOCK OPTIONS

* * * * * * *

SEC. 424. DEFINITIONS AND SPECIAL RULES.

(a) * * *

* * * * * * *

(c) DISPOSITION.—

(1) * * *

* * * * * * *

(3) SPECIAL RULE WHERE INCENTIVE STOCK IS ACQUIRED THROUGH USE OF OTHER STATUTORY OPTION STOCK.—

(A) * * *

(B) STATUTORY OPTION STOCK.—For purpose of subparagraph (A), the term "statutory option stock" means any stock acquired through the exercise of [a qualified stock option, an incentive stock option, an option granted under an employee stock purchase plan, or a restricted stock option] *an incentive stock option or an option granted under an employee stock purchase plan.*

* * * * * * *

Subchapter E—Accounting Periods and Methods of Accounting

* * * * * * *

PART II—METHODS OF ACCOUNTING

* * * * * * *

Subpart B—Taxable Year for Which Items of Gross Income Included

* * * * * * *

SEC. 457. DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.

(a) * * *

(b) ELIGIBLE DEFERRED COMPENSATION PLAN DEFINED.—For purposes of this section, the term "eligible deferred compensation plan" means a plan established and maintained by an eligible employer—

(1) * * *

* * * * * * *

(6) *except as provided in subsection (g),* which provides that—

(A) * * *

* * * * * * *

(c) INDIVIDUALS WHO ARE PARTICIPANTS IN MORE THAN 1 PLAN.—

(1) * * *

(2) COORDINATION WITH CERTAIN OTHER DEFERRALS.—In applying paragraph (1) of this subsection—

(A) * * *

(B) any amount—

(i) excluded from gross income under section 402(e)(3) or section [402(h)(1)(B)] *402(h)(1)(B) or (k)* for the taxable year, or

* * * * * * *

(e) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) * * *

* * * * * * *

[(9) BENEFITS NOT TREATED AS MADE AVAILABLE BY REASON OF CERTAIN ELECTIONS.—If—

[(A) the total amount payable to a participant under the plan does not exceed $3,500, and

[(B) no additional amounts may be deferred under the plan with respect to the participant, the amount payable to the participant under the plan shall not be treated as made available merely because such participant may elect to receive a lump sum payable after separation from service and within 60 days of the election.]

(9) BENEFITS NOT TREATED AS MADE AVAILABLE BY REASON OF CERTAIN ELECTIONS, ETC.—

(A) TOTAL AMOUNT PAYABLE IS $3,500 OR LESS.—The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to receive such amount (or the plan may distribute such amount without the participant's consent) if—

(i) such amount does not exceed $3,500, and

(ii) such amount may be distributed only if—

(I) no amount has been deferred under the plan with respect to such participant during the 2-year period ending on the date of the distribution, and

(II) there has been no prior distribution under the plan to such participant to which this subparagraph applied.

A plan shall not be treated as failing to meet the distribution requirements of subsection (d) by reason of a distribution to which this subparagraph applies.

(B) ELECTION TO DEFER COMMENCEMENT OF DISTRIBUTIONS.—The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to defer commencement of distributions under the plan if—

(i) such election is made after amounts may be available under the plan in accordance with subsection (d)(1)(A) and before commencement of such distributions, and

(ii) the participant may make only 1 such election.

* * * * * * *

(14) TREATMENT OF QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENTS.—Subsections (b)(2) and (c)(1) shall not apply to any qualified governmental excess benefit arrangement (as defined in section 415(m)(3)), and benefits provided under such an arrangement shall not be taken into account in determining whether any other plan is an eligible deferred compensation plan.

(15) COST-OF-LIVING ADJUSTMENT OF MAXIMUM DEFERRAL AMOUNT.—The Secretary shall adjust the $7,500 amount specified in subsections (b)(2) and (c)(1) at the same time and in the

same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1994, and any increase under this paragraph which is not a multiple of $500 shall be rounded to the next lowest multiple of $500.

(f) TAX TREATMENT OF PARTICIPANTS WHERE PLAN OR ARRANGEMENT OF EMPLOYER IS NOT ELIGIBLE.—

(1) * * *

(2) EXCEPTIONS.—Paragraph (1) shall not apply to—

(A) * * *

* * * * * * *

(C) that portion of any plan which consists of a transfer of property described in section 83, **[**and**]**

(D) that portion of any plan which consists of a trust to which section 402(b) applies**[**.**]**, *and*

(E) a qualified governmental excess benefit arrangement described in section 415(m).

* * * * * * *

(g) GOVERNMENTAL PLANS MUST MAINTAIN SET-ASIDES FOR EXCLUSIVE BENEFIT OF PARTICIPANTS.—

(1) IN GENERAL.—A plan maintained by an eligible employer described in subsection (e)(1)(A) shall not be treated as an eligible deferred compensation plan unless all assets and income of the plan described in subsection (b)(6) are held in trust for the exclusive benefit of participants and their beneficiaries.

(2) TAXABILITY OF TRUSTS AND PARTICIPANTS.—For purposes of this title—

(A) a trust described in paragraph (1) shall be treated as an organization exempt from taxation under section 501(a), and

(B) notwithstanding any other provision of this title, amounts in the trust shall be includible in the gross income of participants and beneficiaries only to the extent, and at the time, provided in this section.

(3) CUSTODIAL ACCOUNTS AND CONTRACTS.—For purposes of this subsection, custodial accounts and contracts described in section 401(f) shall be treated as trusts under rules similar to the rules under section 401(f).

* * * * * * *

SEC. 460. SPECIAL RULES FOR LONG-TERM CONTRACTS.

(a) * * *

* * * * * * *

(b) PERCENTAGE OF COMPLETION METHOD.—

(1) * * *

* * * * * * *

In the case of any long-term contract with respect to which the percentage of completion method is used, except for purposes of applying **[**the look-back method of paragraph (3)**]** *the look-back method of paragraph (2)*, any income under the contract (to the extent not previously includible in gross income) shall be included in gross in-

come for the taxable year following the taxable year in which the contract was completed.

* * * * * * *

(e) EXCEPTION FOR CERTAIN CONSTRUCTION CONTRACTS.—

(1) * * *

* * * * * * *

(6) DEFINITIONS RELATING TO RESIDENTIAL CONSTRUCTION CONTRACTS.—For purposes of this subsection—

(A) * * *

(B) RESIDENTIAL CONSTRUCTION CONTRACT.—The term "residential construction contract" means any contract which would be described in subparagraph (A) if clause (i) of such subparagraph reads as follows:

"(i) dwelling units (as defined in section [167(k)] *168(e)(2)(A)(ii)*), and".

* * * * * * *

Subpart C—Taxable Year for Which Deductions Taken

* * * * * * *

SEC. 461. GENERAL RULE FOR TAXABLE YEAR OF DEDUCTION.

(a) * * *

* * * * * * *

(i) SPECIAL RULES FOR TAX SHELTERS.—

(1) * * *

* * * * * * *

(3) TAX SHELTER DEFINED.—For purposes of this subsection, the term "tax shelter" means—

(A) * * *

* * * * * * *

(C) any tax shelter (as defined in [section 6662(d)(2)(C)(ii)] *section 6662(d)(2)(C)(iii)*).

* * * * * * *

SEC. 469. PASSIVE ACTIVITY LOSSES AND CREDITS LIMITED.

(a) * * *

* * * * * * *

(c) PASSIVE ACTIVITY DEFINED.—For purposes of this section—

(1) * * *

* * * * * * *

(3) WORKING INTERESTS IN OIL AND GAS PROPERTY.—

(A) * * *

(B) INCOME IN SUBSEQUENT YEARS.—If any taxpayer has any loss for any taxable year from a working interest in any oil or gas property which is treated as a loss which is not from a passive activity, then any net income from such property (or any property the basis of which is determined in whole or in part by reference to the basis of such property) for any succeeding taxable year shall be treated as income of the taxpayer which is not from a passive activ-

ity. *If the preceding sentence applies to the net income from any property for any taxable year, any credits allowable under subpart B (other than section 27(a)) or D of part IV of subchapter A for such taxable year which are attributable to such property shall be treated as credits not from a passive activity to the extent the amount of such credits does not exceed the regular tax liability of the taxpayer for the taxable year which is allocable to such net income.*

* * * * * * *

(g) DISPOSITIONS OF ENTIRE INTEREST IN PASSIVE ACTIVITY.—If during the taxable year a taxpayer disposes of his entire interest in any passive activity (or former passive activity), the following rules shall apply:

(1) FULLY TAXABLE TRANSACTION.—

[(A) IN GENERAL.—If all gain or loss realized on such disposition is recognized, the excess of—

[(i) the sum of—

[(I) any loss from such activity for such taxable year (determined after application of subsection (b)), plus

[(II) any loss realized on such disposition, over

[(ii) net income or gain for such taxable year from all passive activities (determined without regard to losses described in clause (i)), shall be treated as a loss which is not from a passive activity.]

(A) IN GENERAL.—If all gain or loss realized on such disposition is recognized, the excess of—

(i) any loss from such activity for such taxable year (determined after the application of subsection (b)), over

(ii) any net income or gain for such taxable year from all other passive activities (determined after the application of subsection (b)),

shall be treated as a loss which is not from a passive activity.

* * * * * * *

Subchapter F—Exempt Organizations

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PART I—GENERAL RULE

* * * * * * *

SEC. 501. EXEMPTION FROM TAX ON CORPORATIONS, CERTAIN TRUSTS, ETC.

(a) * * *

* * * * * * *

(c) LIST OF EXEMPT ORGANIZATIONS.—The following organizations are referred to in subsection (a):

(1) * * *

* * * * * * *

(21)(A) * * *

* * * * * * *

(D) For purposes of this paragraph:

(i) * * *

(ii) The term "qualified investments" means—

(I) * * *

* * * * * * *

(III) time or demand deposits in a bank (as defined in section 581) or an insured credit union (within the meaning of section [101(6)] *101(7)* of the Federal Credit Union Act, 12 U.S.C. [1752(6)] *1752(7)*) located in the United States.

* * * * * * *

(n) CHARITABLE RISK POOLS.—

(1) IN GENERAL.—For purposes of this title—

(A) a qualified charitable risk pool shall be treated as an organization organized and operated exclusively for charitable purposes, and

(B) subsection (m) shall not apply to a qualified charitable risk pool.

(2) QUALIFIED CHARITABLE RISK POOL.—For purposes of this subsection, the term "qualified charitable risk pool" means any organization—

(A) which is organized and operated solely to pool insurable risks of its members (other than risks related to medical malpractice) and to provide information to its members with respect to loss control and risk management,

(B) which is comprised solely of members that are organizations described in subsection (c)(3) and exempt from tax under subsection (a), and

(C) which meets the organizational requirements of paragraph (3).

(3) ORGANIZATIONAL REQUIREMENTS.—An organization (hereinafter in this subsection referred to as the "risk pool") meets the organizational requirements of this paragraph if—

(A) such risk pool is organized as a nonprofit organization under State law provisions authorizing risk pooling arrangements for charitable organizations,

(B) such risk pool is exempt from any income tax imposed by the State (or will be so exempt after such pool qualifies as an organization exempt from tax under this title),

(C) such risk pool has obtained at least $1,000,000 in startup capital from nonmember charitable organizations,

(D) such risk pool is controlled by a board of directors elected by its members, and

(E) the organizational documents of such risk pool require that—

(i) each member of such pool shall at all times be an organization described in subsection (c)(3) and exempt from tax under subsection (a),

(ii) any member which receives a final determination that it no longer qualifies as an organization described

in subsection (c)(3) shall immediately notify the pool of such determination and the effective date of such determination, and

(iii) each policy of insurance issued by the risk pool shall provide that such policy will not cover the insured with respect to events occurring after the date such final determination was issued to the insured.

An organization shall not cease to qualify as a qualified charitable risk pool solely by reason of the failure of any of its members to continue to be an organization described in subsection (c)(3) if, within a reasonable period of time after such pool is notified as required under subparagraph (C)(ii), such pool takes such action as may be reasonably necessary to remove such member from such pool.

(4) OTHER DEFINITIONS.—For purposes of this subsection—

(A) STARTUP CAPITAL.—The term "startup capital" means any capital contributed to, and any program-related investments (within the meaning of section 4944(c)) made in, the risk pool before such pool commences operations.

(B) NONMEMBER CHARITABLE ORGANIZATION.—The term "nonmember charitable organization" means any organization which is described in subsection (c)(3) and exempt from tax under subsection (a) and which is not a member of the risk pool and does not benefit (directly or indirectly) from the insurance coverage provided by the pool to its members.

[(n)] *(o)* CROSS REFERENCE.—

For nonexemption of Communist-controlled organizations, see section 11(b) of the Internal Security Act of 1950 (64 Stat. 997; 50 U.S.C. 790(b)).

* * * * * * *

PART III—TAXATION OF BUSINESS INCOME OF CERTAIN EXEMPT ORGANIZATIONS

* * * * * * *

SEC. 512. UNRELATED BUSINESS TAXABLE INCOME.

(a) * * *

(b) MODIFICATIONS.—The modifications referred to in subsection (a) are the following:

(1) * * *

* * * * * * *

(17) TREATMENT OF CERTAIN AMOUNTS DERIVED FROM FOREIGN CORPORATIONS.—

(A) IN GENERAL.—Notwithstanding paragraph (1), any amount included in gross income under section 951(a)(1)(A) shall be included as an item of gross income derived from an unrelated trade or business to the extent the amount so included is attributable to insurance income (as defined in section 953) which, if derived directly by the organization, would be treated as gross income from an unrelated trade or business. There shall be allowed all deductions directly connected with amounts included in gross income under the preceding sentence.

(B) EXCEPTION.—Subparagraph (A) shall not apply to income attributable to a policy of insurance or reinsurance with respect to which the person (directly or indirectly) insured is—

(i) such organization,

(ii) an affiliate of such organization which is exempt from tax under section 501(a), or

(iii) a director or officer of, or an individual who (directly or indirectly) performs services for, such organization or affiliate but only if the insurance covers primarily risks associated with the performance of services in connection with such organization or affiliate.

For purposes of this subparagraph, the determination as to whether an entity is an affiliate of an organization shall be made under rules similar to the rules of section 168(h)(4)(B).

(C) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this paragraph, including regulations for the application of this paragraph in the case of income paid through 1 or more entities or between 2 or more chains of entities.

* * * * * * *

(d) TREATMENT OF DUES OF AGRICULTURAL OR HORTICULTURAL ORGANIZATIONS.—

(1) IN GENERAL.—If—

(A) an agricultural or horticultural organization described in section 501(c)(5) requires annual dues to be paid in order to be a member of such organization, and

(B) the amount of such required annual dues does not exceed $100,

in no event shall any portion of such dues be treated as derived by such organization from an unrelated trade or business by reason of any benefits or privileges to which members of such organization are entitled.

(2) INDEXATION OF $100 AMOUNT.—In the case of any taxable year beginning in a calendar year after 1995, the $100 amount in paragraph (1) shall be increased by an amount equal to—

(A) $100, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting "calendar year 1994" for "calendar year 1992" in subparagraph (B) thereof.

(3) DUES.—For purposes of this subsection, the term "dues" includes any payment required to be made in order to be recognized by the organization as a member of the organization.

Subchapter G—Corporations Used to Avoid Income tax on Shareholders

* * * * * * *

PART I—CORPORATIONS IMPROPERLY ACCUMULATING SURPLUS

* * * * * * *

SEC. 537. REASONABLE NEEDS OF THE BUSINESS.

(a) * * *

(b) SPECIAL RULES.—For purposes of subsection (a)—

(1) * * *

* * * * * * *

(4) PRODUCT LIABILITY LOSS RESERVES.—The accumulation of reasonable amounts for the payment of reasonably anticipated product liability losses (as defined in section [172(i)] *172(f)*), as determined under regulations prescribed by the Secretary, shall be treated as accumulated for the reasonably anticipated needs of the business.

* * * * * * *

PART II—PERSONAL HOLDING COMPANIES

* * * * * * *

SEC. 543. PERSONAL HOLDING COMPANY INCOME.

(a) GENERAL RULE.—For purposes of this subtitle, the term "personal holding company income" means the portion of the adjusted ordinary gross income which consists of:

(1) * * *

(2) RENTS.—The adjusted income from rents; except that such adjusted income shall not be included if—

(A) such adjusted income constitutes 50 percent or more of the adjusted ordinary gross income, and

(B) the sum of—

(i) the dividends paid during the taxable year (determined under section 562),

(ii) the dividends considered as paid on the last day of the taxable year under section [563(c)] *563(d)* (as limited by the second sentence of section 563(b)), and

* * * * * * *

Subchapter I—Natural Resources

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PART I—DEDUCTIONS

* * * * * * *

SEC. 613. PERCENTAGE DEPLETION.

(a) * * *

* * * * * * *

(e) PERCENTAGE DEPLETION FOR GEOTHERMAL DEPOSITS.—

(1) IN GENERAL.—In the case of geothermal deposits located in the United States or in a possession of the United States, for purposes of subsection (a)—

(A) such deposits shall be treated as listed in subsection (b), and

(B) 15 percent shall be deemed to be the percentage specified in paragraph (b)[.],

* * * * * * *

SEC. 613A. LIMITATIONS ON PERCENTAGE DEPLETION IN CASE OF OIL AND GAS WELLS.

(a) * * *

* * * * * * *

(c) EXEMPTION FOR INDEPENDENT PRODUCERS AND ROYALTY OWNERS.—

(1) * * *

* * * * * * *

(3) DEPLETABLE OIL QUANTITY.—

(A) IN GENERAL.—For purposes of paragraph (1), the taxpayer's depletable oil quantity shall be equal to—

(i) the tentative quantity determined under [the table contained in] subparagraph (B), reduced (but not below zero) by

(ii) except in the case of a taxpayer making an election under paragraph (6)(B), the taxpayer's average daily marginal production for the taxable year.

* * * * * * *

Subchapter J—Estates, Trusts, Beneficiaries, and Decedents

* * * * * * *

PART I—ESTATES, TRUSTS, AND BENEFICIARIES

* * * * * * *

Subpart A—General Rules for Taxation of Estates and Trusts

* * * * * * *

SEC. 641. IMPOSITION OF TAX.

(a) * * *

* * * * * * *

(d) SPECIAL RULES FOR TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—

(1) IN GENERAL.—For purposes of this chapter—

(A) the portion of any electing small business trust which consists of stock in 1 or more S corporations shall be treated as a separate trust, and

(B) the amount of the tax imposed by this chapter on such separate trust shall be determined with the modifications of paragraph (2).

(2) MODIFICATIONS.—For purposes of paragraph (1), the modifications of this paragraph are the following:

(A) Except as provided in section 1(h), the amount of the tax imposed by section 1(e) shall be determined by using the highest rate of tax set forth in section 1(e).

(B) The exemption amount under section 55(d) shall be zero.

(C) The only items of income, loss, deduction, or credit to be taken into account are the following:

(i) The items required to be taken into account under section 1366.

(ii) Any gain or loss from the disposition of stock in an S corporation.

(iii) To the extent provided in regulations, State or local income taxes or administrative expenses to the extent allocable to items described in clauses (i) and (ii).

No deduction or credit shall be allowed for any amount not described in this paragraph, and no item described in this paragraph shall be apportioned to any beneficiary.

(D) No amount shall be allowed under paragraph (1) or (2) of section 1211(b).

(3) TREATMENT OF REMAINDER OF TRUST AND DISTRIBUTIONS.—For purposes of determining—

(A) the amount of the tax imposed by this chapter on the portion of any electing small business trust not treated as a separate trust under paragraph (1), and

(B) the distributable net income of the entire trust,

the items referred to in paragraph (2)(C) shall be excluded. Except as provided in the preceding sentence, this subsection shall not affect the taxation of any distribution from the trust.

(4) TREATMENT OF UNUSED DEDUCTIONS WHERE TERMINATION OF SEPARATE TRUST.—If a portion of an electing small business trust ceases to be treated as a separate trust under paragraph (1), any carryover or excess deduction of the separate trust which is referred to in section 642(h) shall be taken into account by the entire trust.

(5) ELECTING SMALL BUSINESS TRUST.—For purposes of this subsection, the term "electing small business trust" has the meaning given such term by section 1361(e)(1).

SEC. 642. SPECIAL RULES FOR CREDITS AND DEDUCTIONS.

(a) * * *

* * * * * * *

(g) DISALLOWANCE OF DOUBLE DEDUCTIONS.—Amounts allowable under section 2053 or 2054 as a deduction in computing the taxable estate of a decedent shall not be allowed as a deduction (or as an offset against the sales price of property in determining gain or loss) in computing the taxable income of the estate or of any other person, unless there is filed, within the time and in the manner and form prescribed by the Secretary, a statement that the amounts have not been allowed as deductions under section 2053 or 2054 and a waiver of the right to have such amounts allowed at any time as deductions under section 2053 or 2054. Rules similar to the rules of the preceding sentence shall apply to amounts which may be taken into account under *section* 2621(a)(2) or

2622(b). This subsection shall not apply with respect to deductions allowed under part II (relating to income in respect of decedents).

* * * * * * *

PART II—INCOME IN RESPECT OF DECEDENTS

* * * * * * *

SEC. 691. RECIPIENTS OF INCOME IN RESPECT OF DECEDENTS.

(a) * * *

* * * * * * *

(c) DEDUCTION FOR ESTATE TAX.—

(1) * * *

* * * * * * *

[(5) COORDINATION WITH SECTION 402(d).—For purposes of section 402(d) (other than paragraph (1)(C) thereof), the total taxable amount of any lump sum distribution shall be reduced by the amount of the deduction allowable under paragraph (1) of this subsection which is attributable to the total taxable amount (determined without regard to this paragraph).]

* * * * * * *

Subchapter K—Partners and Partnerships

* * * * * * *

PART II—CONTRIBUTIONS, DISTRIBUTIONS, AND TRANSFERS

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Subpart A—Contributions to a Partnership

* * * * * * *

SEC. 724. CHARACTER OF GAIN OR LOSS ON CONTRIBUTED UNREALIZED RECEIVABLES, INVENTORY ITEMS, AND CAPITAL LOSS PROPERTY.

(a) * * *

* * * * * * *

(d) DEFINITIONS.—For purposes of this section—

(1) * * *

* * * * * * *

(3) SUBSTITUTED BASIS PROPERTY.—

(A) IN GENERAL.—If any property described in subsection (a), (b), or (c) is disposed of in a nonrecognition transaction, the tax treatment which applies to such property under such subsection shall also apply to any substituted basis property resulting from such transaction. A similar rule shall also apply in the case of a series of non-recognition transactions.

(B) EXCEPTION FOR STOCK IN C CORPORATION.—[Subparagaph] *Subparagraph* (A) shall not apply to any

stock in a C corporation received in an exchange described in section 351.

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Subchapter L—Insurance Companies

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PART I—LIFE INSURANCE COMPANIES

* * * * * * *

Subpart C—Life Insurance Deductions

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SEC. 805. GENERAL DEDUCTIONS.

(a) GENERAL RULE.—For purposes of this part, there shall be allowed the following deductions:

(1) * * *

* * * * * * *

(4) DIVIDENDS RECEIVED BY COMPANY.—

(A) * * *

* * * * * * *

(E) CERTAIN DIVIDENDS RECEIVED BY FOREIGN CORPORATIONS.—Subparagraph (A)(i) (and not subparagraph (A)(ii)) shall apply to any dividend received by a foreign corporation from a domestic corporation which would be a 100 percent dividend if section 1504(b)(3) did not apply for purposes of applying section [243(b)(5)] *243(b)(2).*

* * * * * * *

SEC. 807. RULES FOR CERTAIN RESERVES.

(a) * * *

* * * * * * *

(d) METHOD OF COMPUTING RESERVES FOR PURPOSES OF DETERMINING INCOME.—

(1) * * *

* * * * * * *

(3) TAX RESERVE METHOD.—For purposes of this subsection—

(A) * * *

(B) DEFINITION OF CRVM AND CARVM.—For purposes of this paragraph—

(i) CRVM.—The term "CRVM" means the Commissioners' Reserve Valuation Method prescribed by the National Association of Insurance Commissioners which is in effect on the date of the issuance of the contract.

(ii) CARVM.—The term "CARVM" means the [Commissoners'] *Commissioners'* Annuities Reserve Valuation Method prescribed by the National Associa-

tion of Insurance Commissioners which is in effect on the date of the issuance of the contract.

* * * * * * *

Subpart D—Accounting, Allocation, and Foreign Provisions

* * * * * * *

SEC. 812. DEFINITION OF COMPANY'S SHARE AND POLICYHOLDERS' SHARE.

(a) * * *

* * * * * * *

[(g) TREATMENT OF INTEREST PARTIALLY TAX-EXEMPT UNDER SECTION 133.—For purposes of this section and subsections (a) and (b) of section 807, the terms "gross investment income" and "tax-exempt interest" shall not include any interest received with respect to a securities acquisition loan (as defined in section 133(b)). Such interest shall not be included in life insurance gross income for purposes of subsection (b)(3).]

* * * * * * *

PART II—OTHER INSURANCE COMPANIES

* * * * * * *

SEC. 832. INSURANCE COMPANY TAXABLE INCOME.

(a) * * *

(b) DEFINITIONS.—In the case of an insurance company subject to the tax imposed by section 831—

(1) * * *

* * * * * * *

(5) LOSSES INCURRED.—

(A) * * *

* * * * * * *

(C) EXCEPTION FOR INVESTMENTS MADE BEFORE AUGUST 8, 1986.—

(i) IN GENERAL.—Except as provided in clause (ii), subparagraph (B) shall not apply to any dividend or interest received or accrued on any stock or obligation acquired before August 8, 1986.

(ii) SPECIAL RULE FOR 100 PERCENT DIVIDENDS.—For purposes of clause (i), the portion of any 100 percent dividend which is attributable to prorated amounts shall be treated as received with respect to stock acquired on the later of—

(I) the date the payor acquired the stock or obligation to which the prorated amounts are attributable, or

(II) the 1st day on which the payor and payee were members of the same affiliated group (as defined in section [243(b)(5)] *243(b)(2)*).

(D) DEFINITIONS.—For purposes of this paragraph—

(i) PRORATED AMOUNTS.—The term "prorated amounts" means tax-exempt interest and dividends

with respect to which a deduction is allowable under section 243, 244, or 245 (other than 100 percent dividends).

(ii) 100 PERCENT DIVIDEND.—

(I) IN GENERAL.—The term "100 percent dividend" means any dividend if the percentage used for purposes of determining the deduction allowable under section 243, 244, or 245(b) is 100 percent.

(II) CERTAIN DIVIDENDS RECEIVED BY FOREIGN CORPORATIONS.—A dividend received by a foreign corporation from a domestic corporation which would be a 100 percent dividend if section 1504(b)(3) did not apply for purposes of applying section [243(b)(5)] *243(b)(2)* shall be treated as a 100 percent dividend.

* * * * * * *

Subchapter M—Regulated Investment Companies and Real Estate Investment Trusts

* * * * * * *

PART I—REGULATED INVESTMENT COMPANIES

* * * * * * *

SEC. 852. TAXATION OF REGULATED INVESTMENT COMPANIES AND THEIR SHAREHOLDERS.

(a) * * *

* * * * * * *

(b) METHOD OF TAXATION OF COMPANIES AND SHAREHOLDERS.—

(1) * * *

* * * * * * *

(5) EXEMPT-INTEREST DIVIDENDS.—If, at the close of each quarter of its taxable year, at least 50 percent of the value (as defined in section 851(c)(4)) of the total assets of the regulated investment company consists of obligations described in section 103(a), such company shall be qualified to pay exempt-interest dividends, as defined herein, to its shareholders.

(A) * * *

* * * * * * *

[(C) INTEREST ON CERTAIN LOANS USED TO ACQUIRE EMPLOYER SECURITIES.—For purposes of this section—

[(i) 50 percent of the amount of any loan of the regulated investment company which qualifies as a securities acquisition loan (as defined in section 133) shall be treated as an obligation described in section 103(a), and

[(ii) 50 percent of the interest received on such loan shall be treated as interest excludable from gross income under section 103.]

* * * * * * *

PART II—REAL ESTATE INVESTMENT TRUSTS

* * * * * * *

SEC. 856. DEFINITION OF REAL ESTATE INVESTMENT TRUST.

(a) IN GENERAL.—For purposes of this title, the term "real estate investment trust" means a corporation, trust, or association—

(1) * * *

* * * * * * *

(4) which is neither (A) a financial institution referred to in section [582(c)(5)] *582(c)(2)*, nor (B) an insurance company to which subchapter L applies;

* * * * * * *

PART IV—REAL ESTATE MORTGAGE INVESTMENT CONDUITS

* * * * * * *

SEC. 860E. TREATMENT OF INCOME IN EXCESS OF DAILY ACCRUALS ON RESIDUAL INTERESTS.

(a) EXCESS INCLUSIONS MAY NOT BE OFFSET BY NET OPERATING LOSSES.—

(1) * * *

* * * * * * *

(6) COORDINATION WITH MINIMUM TAX.—For purposes of part VI of subchapter A of this chapter—

(A) the reference in section 55(b)(2) to taxable income shall be treated as a reference to taxable income determined without regard to this subsection,

(B) the alternative minimum taxable income of any holder of a residual interest in a REMIC for any taxable year shall in no event be less than the excess inclusion for such taxable year, and

(C) any excess inclusion shall be disregarded for purposes of computing the alternative tax net operating loss deduction.

The preceding sentence shall not apply to any organization to which section 593 applies, except to the extent provided in regulations prescribed by the Secretary under paragraph (2).

* * * * * * *

SEC. 860F. OTHER RULES.

(a) 100 PERCENT TAX ON PROHIBITED TRANSACTIONS.—

(1) * * *

* * * * * * *

(5) EXCEPTIONS.—Notwithstanding subparagraphs (A) and (D) of paragraph [(1)] *(2)*, the term "prohibited transaction" shall not include any disposition—

(A) required to prevent default on a regular interest where the threatened default resulted from a default on 1 or more qualified mortgages, or

(B) to facilitate a clean-up call (as defined in regulations).

* * * * * * *

Subchapter N—Tax Bases on Income from Sources Within or Without the United States

* * * * * * *

PART I—DETERMINATION OF SOURCES OF INCOME

* * * * * * *

SEC. 865. SOURCE RULES FOR PERSONAL PROPERTY SALES.

(a) * * *

(b) EXCEPTION FOR INVENTORY PROPERTY.—In the case of income derived from the sale of inventory property—

(1) this section shall not apply, and

(2) such income shall be sourced under the rules of sections 861(a)(6), 862(a)(6), and 863(b).

Notwithstanding the preceding sentence, any income from the sale of any unprocessed timber which is a softwood and was cut from an area in the United States shall be sourced in the United States and the rules of sections 862(a)(6) and 863[(b)] shall not apply to any such income. For purposes of the preceding sentence, the term "unprocessed timber" means any log, cant, or similar form of timber.

* * * * * * *

PART II—NONRESIDENT ALIENS AND FOREIGN CORPORATIONS

* * * * * * *

Subpart A—Nonresident Alien Individuals

* * * * * * *

SEC. 871. TAX ON NONRESIDENT ALIEN INDIVIDUALS.

(a) * * *

(b) INCOME CONNECTED WITH UNITED STATES BUSINESS—GRADUATED RATE OF TAX.—

(1) IMPOSITION OF TAX.—A nonresident alien individual engaged in trade or business within the United States during the taxable year shall be taxable as provided in [section 1, 55, or 402(d)(1)] *section 1 or 55* on his taxable income which is effectively connected with the conduct of a trade or business within the United States.

* * * * * * *

SEC. 877. EXPATRIATION TO AVOID TAX.

(a) * * *

(b) ALTERNATIVE TAX.—A nonresident alien individual described in subsection (a) shall be taxable for the taxable year as provided in [section 1, 55, or 402(d)(1)] *section 1 or 55*, except that—

(1) * * *

* * * * * * *

Subpart B—Foreign Corporations

* * * * * * *

SEC. 884. BRANCH PROFITS TAX.

(a) * * *

* * * * * * *

(f) TREATMENT OF INTEREST ALLOCABLE TO EFFECTIVELY CONNECTED INCOME.—

(1) IN GENERAL.—In the case of a foreign corporation engaged in a trade or business in the United States (or having gross income treated as effectively connected with the conduct of a trade or business in the United States), for purposes of this subtitle—

(A) any interest paid by such trade or business in the United States shall be treated as if it were paid by a domestic corporation, and

(B) [to the extent the amount of interest allowable as a deduction under section 882 in computing the effectively connected taxable income of such foreign corporation exceeds the interest described in subparagraph (A)] *to the extent that the allocable interest exceeds the interest described in subparagraph (A)*, such foreign corporation shall be liable for tax under section 881(a) in the same manner as if such excess were interest paid to such foreign corporation by a wholly owned domestic corporation on the last day of such foreign corporation's taxable year.

To the extent provided in regulations, subparagraph (A) shall not apply to interest in excess of the amounts [reasonably expected to be deductible under section 882 in computing the effectively connected taxable income of such foreign corporation.] *reasonably expected to be allocable interest.*

[(2) EFFECTIVELY CONNECTED TAXABLE INCOME.—For purposes of this subsection, the term "effectively connected taxable income" means taxable income which is effectively connected (or treated as effectively connected) with the conduct of a trade or business within the United States.]

(2) ALLOCABLE INTEREST.—For purposes of this subsection, the term "allocable interest" means any interest which is allocable to income which is effectively connected (or treated as effectively connected) with the conduct of a trade or business in the United States.

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Subpart D—Miscellaneous Provisions

* * * * * * *

SEC. 897. DISPOSITION OF INVESTMENT IN UNITED STATES REAL PROPERTY.

(a) * * *

* * * * * * *

[(f) DISTRIBUTIONS BY DOMESTIC CORPORATIONS TO FOREIGN SHAREHOLDERS.—If a domestic corporation distributes a United States real property interest to a nonresident alien individual or a foreign corporation in a distribution to which section 301 applies, notwithstanding any other provision of this chapter, the basis of such United States real property interest in the hands of such nonresident alien individual or foreign corporation shall not exceed—

[(1) the adjusted basis of such property before the distribution, increased by

[(2) the sum of—

[(A) any gain recognized by the distributing corporation on the distribution, and

[(B) any tax paid under this chapter by the distributee on such distribution.]

* * * * * * *

PART III—INCOME FROM SOURCES WITHOUT THE UNITED STATES

* * * * * * *

Subpart A—Foreign Tax Credit

* * * * * * *

SEC. 904. LIMITATION ON CREDIT.

(a) * * *

* * * * * * *

(d) SEPARATE APPLICATION OF SECTION WITH RESPECT TO CERTAIN CATEGORIES OF INCOME.—

(1) * * *

* * * * * * *

(3) LOOK-THRU IN CASE OF CONTROLLED FOREIGN CORPORATIONS.—

(A) * * *

* * * * * * *

(G) DIVIDEND.—For purposes of this paragraph, the term "dividend" includes any amount included in gross income in [section 951(a)(1)(B)] *subparagraph (B) or (C) of section 951(a)(1).* Any amount included in gross income under section 78 to the extent attributable to amounts included in gross income in section 951(a)(1)(A) shall not be treated as a dividend but shall be treated as included in gross income under section 951(a)(1)(A).

* * * * * * *

(f) RECAPTURE OF OVERALL FOREIGN LOSS.—

(1) * * *

(2) OVERALL FOREIGN LOSS DEFINED.—For purposes of this subsection, the term "overall foreign loss" means the amount

by which the gross income for the taxable year from sources without the United States (whether or not the taxpayer chooses the benefits of this subpart for such taxable year) for such year is exceeded by the sum of the deductions properly apportioned or allocated thereto, except that there shall not be taken into account—

(A) any net operating loss deduction allowable for such year under section 172(a), and

(B) any—

(i) foreign expropriation loss for such year, as defined in section 172(h) *(as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)*, or

(ii) loss for such year which arises from fire, storm, shipwreck, or other casualty, or from theft,

to the extent such loss is not compensated for by insurance or otherwise.

* * * * * * *

SEC. 907. SPECIAL RULES IN CASE OF FOREIGN OIL AND GAS INCOME. * * *

* * * * * * *

(c) FOREIGN INCOME DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) * * *

* * * * * * *

(4) RECAPTURE OF FOREIGN OIL AND GAS EXTRACTION LOSSES BY RECHARACTERIZING LATER EXTRACTION INCOME.—

(A) * * *

(B) FOREIGN OIL EXTRACTION LOSS DEFINED.—

(i) * * *

* * * * * * *

(iii) EXPROPRIATION AND CASUALTY LOSSES NOT TAKEN INTO ACCOUNT.—For purposes of clause (i), there shall not be taken into account—

(I) any foreign expropriation loss (as defined in section 172(h) *(as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)*) for the taxable year, or

(II) any loss for the taxable year which arises from fire, storm, shipwreck, or other casualty, or from theft,

to the extent such loss is not compensated for by insurance or otherwise.

Subpart D—Possessions of the United States

* * * * * * *

SEC. 936. PUERTO RICO AND POSSESSION TAX CREDIT.

(a) * * *

(b) AMOUNTS RECEIVED IN UNITED STATES.—In determining taxable income for purposes of subsection (a), there shall not be taken into account as income from sources without the United States any

gross income which was received by such domestic corporation within the United States, whether derived from sources within or without the United States. This subsection shall not apply to any amount described in subsection (a)(1)(A)(i) received from a person who is not a related person (within the meaning of subsection (h)(3) but without regard to subparagraphs (D)(ii)[(I)] and (E)(i) thereof) with respect to the domestic corporation.

* * * * * * *

(j) TERMINATION.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, this section shall not apply to any taxable year beginning after December 31, 1995.

(2) TRANSITION RULES FOR ACTIVE BUSINESS INCOME CREDIT.—Except as provided in paragraph (3)—

(A) ECONOMIC ACTIVITY CREDIT.—In the case of an existing credit claimant—

(i) with respect to a possession other than Puerto Rico, and

(ii) to which subsection (a)(4)(B) does not apply,

the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 2002.

(B) SPECIAL RULE FOR REDUCED CREDIT.—

(i) IN GENERAL.—In the case of an existing credit claimant to which subsection (a)(4)(B) applies, the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 1998.

(ii) ELECTION IRREVOCABLE AFTER 1997.—An election under subsection (a)(4)(B)(iii) which is in effect for the taxpayer's last taxable year beginning before 1997 may not be revoked unless it is revoked for the taxpayer's first taxable year beginning in 1997 and all subsequent taxable years.

(C) ECONOMIC ACTIVITY CREDIT FOR PUERTO RICO.—

For economic activity credit for Puerto Rico, see section 30A.

(3) ADDITIONAL RESTRICTED CREDIT.—

(A) IN GENERAL.—In the case of an existing credit claimant—

(i) the credit under subsection (a)(1)(A) shall be allowed for the period beginning with the first taxable year after the last taxable year to which subparagraph (A) or (B) of paragraph (2), whichever is appropriate, applied and ending with the last taxable year beginning before January 1, 2006, except that

(ii) the aggregate amount of taxable income taken into account under subsection (a)(1)(A) for any such taxable year shall not exceed the adjusted base period income of such claimant.

(B) COORDINATION WITH SUBSECTION (a)(4).—The amount of income described in subsection (a)(1)(A) which is taken into account in applying subsection (a)(4) shall be such income as reduced under this paragraph.

(4) ADJUSTED BASE PERIOD INCOME.—For purposes of paragraph (3)—

(A) IN GENERAL.—The term "adjusted base period income" means the average of the inflation-adjusted possession incomes of the corporation for each base period year.

(B) INFLATION-ADJUSTED POSSESSION INCOME.—For purposes of subparagraph (A), the inflation-adjusted possession income of any corporation for any base period year shall be an amount equal to the sum of—

(i) the possession income of such corporation for such base period year, plus

(ii) such possession income multiplied by the inflation adjustment percentage for such base period year.

(C) INFLATION ADJUSTMENT PERCENTAGE.—For purposes of subparagraph (B), the inflation adjustment percentage for any base period year means the percentage (if any) by which—

(i) the CPI for 1995, exceeds

(ii) the CPI for the calendar year in which the base period year for which the determination is being made ends.

For purposes of the preceding sentence, the CPI for any calendar year is the CPI (as defined in section 1(f)(5)) for such year under section 1(f)(4).

(D) INCREASE IN INFLATION ADJUSTMENT PERCENTAGE FOR GROWTH DURING BASE YEARS.—The inflation adjustment percentage (determined under subparagraph (C) without regard to this subparagraph) for each of the 5 taxable years referred to in paragraph (5)(A) shall be increased by—

(i) 5 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1995;

(ii) 10.25 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1994;

(iii) 15.76 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1993;

(iv) 21.55 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1992; and

(v) 27.63 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1991.

(5) BASE PERIOD YEAR.—For purposes of this subsection—

(A) IN GENERAL.—The term "base period year" means each of 3 taxable years which are among the 5 most recent taxable years of the corporation ending before October 14, 1995, determined by disregarding—

(i) one taxable year for which the corporation had the largest inflation-adjusted possession income, and

(ii) one taxable year for which the corporation had the smallest inflation-adjusted possession income.

(B) CORPORATIONS NOT HAVING SIGNIFICANT POSSESSION INCOME THROUGHOUT 5-YEAR PERIOD.—

(i) IN GENERAL.—If a corporation does not have significant possession income for each of the most recent 5 taxable years ending before October 14, 1995, then, in lieu of applying subparagraph (A), the term "base period year" means only those taxable years (of such 5 taxable years) for which the corporation has significant possession income; except that, if such corporation has significant possession income for 4 of such 5 taxable years, the rule of subparagraph (A)(ii) shall apply.

(ii) SPECIAL RULE.—If there is no year (of such 5 taxable years) for which a corporation has significant possession income—

(I) the term "base period year" means the first taxable year ending on or after October 14, 1995, but

(II) the amount of possession income for such year which is taken into account under paragraph (4) shall be the amount which would be determined if such year were a short taxable year ending on September 30, 1995.

(iii) SIGNIFICANT POSSESSION INCOME.—For purposes of this subparagraph, the term "significant possession income" means possession income which exceeds 2 percent of the possession income of the taxpayer for the taxable year (of the period of 6 taxable years ending with the first taxable year ending on or after October 14, 1995) having the greatest possession income.

(C) ELECTION TO USE ONE BASE PERIOD YEAR.—

(i) IN GENERAL.—At the election of the taxpayer, the term "base period year" means—

(I) only the last taxable year of the corporation ending in calendar year 1992, or

(II) a deemed taxable year which includes the first ten months of calendar year 1995.

(ii) BASE PERIOD INCOME FOR 1995.—In determining the adjusted base period income of the corporation for the deemed taxable year under clause (i)(II), the possession income shall be annualized and shall be determined without regard to any extraordinary item.

(iii) ELECTION.—An election under this subparagraph by any possession corporation may be made only for the corporation's first taxable year beginning after December 31, 1995, for which it is a possession corporation. The rules of subclauses (II) and (III) of subsection (a)(4)(B)(iii) shall apply to the election under this subparagraph.

(D) ACQUISITIONS AND DISPOSITIONS.—Rules similar to the rules of subparagraphs (A) and (B) of section 41(f)(3) shall apply for purposes of this subsection.

(6) POSSESSION INCOME.—For purposes of this subsection, the term "possession income" means, with respect to any possession, the income referred to in subsection (a)(1)(A) determined with

respect to that possession. In no event shall possession income be treated as being less than zero.

(7) SHORT YEARS.—If the current year or a base period year is a short taxable year, the application of this subsection shall be made with such annualizations as the Secretary shall prescribe.

(8) SPECIAL RULES FOR CERTAIN POSSESSIONS.—

(A) IN GENERAL.—In the case of an existing credit claimant with respect to an applicable possession, this section (other than the preceding paragraphs of this subsection) shall apply to such claimant with respect to such applicable possession for taxable years beginning after December 31, 1995, and before January 1, 2006.

(B) APPLICABLE POSSESSION.—For purposes of this paragraph, the term "applicable possession" means Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.

(9) EXISTING CREDIT CLAIMANT.—For purposes of this subsection—

(A) IN GENERAL.—The term "existing credit claimant" means a corporation—

(i) which was actively conducting a trade or business in a possession on October 13, 1995, and

(ii) with respect to which an election under this section is in effect for the corporation's taxable year which includes October 13, 1995.

(B) NEW LINES OF BUSINESS PROHIBITED.—If, after October 13, 1995, a corporation which would (but for this subparagraph) be an existing credit claimant adds a substantial new line of business, such corporation shall cease to be treated as an existing credit claimant as of the close of the taxable year ending before the date of such addition.

(C) BINDING CONTRACT EXCEPTION.—If, on October 13, 1995, and at all times thereafter, there is in effect with respect to a corporation a binding contract for the acquisition of assets to be used in, or for the sale of assets to be produced from, a trade or business, the corporation shall be treated for purposes of this paragraph as actively conducting such trade or business on October 13, 1995. The preceding sentence shall not apply if such trade or business is not actively conducted before January 1, 1996.

(10) SEPARATE APPLICATION TO EACH POSSESSION.—In the case of any taxpayer, this subsection (and so much of this section as relates to this subsection) shall be applied separately with respect to each possession.

* * * * * * *

Subpart F—Controlled Foreign Corporations

Sec. 951. Amounts included in gross income of United States shareholders.

* * * * * * *

[Sec. 956A. Earnings invested in excess passive assets.]

* * * * * * *

SEC. 951. AMOUNTS INCLUDED IN GROSS INCOME OF UNITED STATES SHAREHOLDERS.

(a) AMOUNTS INCLUDED.—

(1) IN GENERAL.—If a foreign corporation is a controlled foreign corporation for an uninterrupted period of 30 days or more during any taxable year, every person who is a United States shareholder (as defined in subsection (b)) of such corporation and who owns (within the meaning of section 958(a)) stock in such corporation on the last day, in such year, on which such corporation is a controlled foreign corporation shall include in his gross income, for his taxable year in which or with which such taxable year of the corporation ends—

(A) the sum of—

(i) his pro rata share (determined under paragraph (2)) of the corporation's subpart F income for such year,

(ii) his pro rata share (determined under section 955(a)(3) as in effect before the enactment of the Tax Reduction Act of 1975) of the corporation's previously excluded subpart F income withdrawn from investment in less developed countries for such year, and

(iii) his pro rata share (determined under section 955(a)(3)) of the corporation's previously excluded subpart F income withdrawn from foreign base company shipping operations for such year, *and*

(B) the amount determined under section 956 with respect to such shareholder for such year (but only to the extent not excluded from gross income under section 959(a)(2))[; and].

[(C) the amount determined under section 956A with respect to such shareholder for such year (but only to the extent not excluded from gross income under section 959(a)(3)).]

* * * * * * *

[SEC. 956A. EARNINGS INVESTED IN EXCESS PASSIVE ASSETS.

[(a) GENERAL RULE.—In the case of any controlled foreign corporation, the amount determined under this section with respect to any United States shareholder for any taxable year is the lesser of—

[(1) the excess (if any) of—

[(A) such shareholder's pro rata share of the amount of the controlled foreign corporation's excess passive assets for such taxable year, over

[(B) the amount of earnings and profits described in section 959(c)(1)(B) with respect to such shareholder, or

[(2) such shareholder's pro rata share of the applicable earnings of such controlled foreign corporation determined after the application of section 951(a)(1)(B).

[(b) Applicable Earnings.—For purposes of this section, the term "applicable earnings" means, with respect to any controlled foreign corporation, the sum of—

[(1) the amount (not including a deficit) referred to in section 316(a)(1) to the extent such amount was accumulated in prior taxable years beginning after September 30, 1993, and

[(2) the amount referred to in section 316(a)(2),

but reduced by distributions made during the taxable year and reduced by the earnings and profits described in section 959(c)(1) to the extent that the earnings and profits so described were accumulated in taxable years beginning after September 30, 1993.

[(c) EXCESS PASSIVE ASSETS.—For purposes of this section—

[(1) IN GENERAL.—The excess passive assets of any controlled foreign corporation for any taxable year is the excess (if any) of—

[(A) the average of the amounts of passive assets held by such corporation as of the close of each quarter of such taxable year, over

[(B) 25 percent of the average of the amounts of total assets held by such corporation as of the close of each quarter of such taxable year.

For purposes of the preceding sentence, the amount taken into account with respect to any asset shall be its adjusted basis as determined for purposes of computing earnings and profits.

[(2) PASSIVE ASSET.—

[(A) IN GENERAL.—Except as otherwise provided in this section, the term "passive asset" means any asset held by the controlled foreign corporation which produces passive income (as defined in section 1296(b)) or is held for the production of such income.

[(B) COORDINATION WITH SECTION 956.—The term "passive asset" shall not include any United States property (as defined in section 956).

[(3) CERTAIN RULES TO APPLY.—For purposes of this subsection, the rules of the following provisions shall apply:

[(A) Section 1296(c) (relating to look-thru rules).

[(B) Section 1297(d) (relating to leasing rules).

[(C) Section 1297(e) (relating to intangible property).

[(d) TREATMENT OF CERTAIN GROUPS OF CONTROLLED FOREIGN CORPORATIONS.—

[(1) IN GENERAL.—For purposes of applying subsection (c)—

[(A) all controlled foreign corporations which are members of the same CFC group shall be treated as 1 controlled foreign corporation, and

[(B) the amount of the excess passive assets determined with respect to such 1 corporation shall be allocated among the controlled foreign corporations which are members of such group in proportion to their respective amounts of applicable earnings.

[(2) CFC GROUP.—For purposes of paragraph (1), the term "CFC group" means 1 or more chains of controlled foreign corporations connected through stock ownership with a top tier corporation which is a controlled foreign corporation, but only if—

[(A) the top tier corporation owns directly more than 50 percent (by vote or value) of the stock of at least 1 of the other controlled foreign corporations, and

[(B) more than 50 percent (by vote or value) of the stock of each of the controlled foreign corporations (other than the top tier corporation) is owned (directly or indirectly) by one or more other members of the group.

[(e) SPECIAL RULE WHERE CORPORATION CEASES TO BE CONTROLLED FOREIGN CORPORATION DURING TAXABLE YEAR.—If any foreign corporation ceases to be a controlled foreign corporation during any taxable year—

[(1) the determination of any United States shareholder's pro rata share shall be made on the basis of stock owned (within the meaning of section 958(a)) by such shareholder on the last day during the taxable year on which the foreign corporation is a controlled foreign corporation, and

[(2) the amount of such corporation's excess passive assets for such taxable year shall be determined by only taking into account quarters ending on or before such last day, and

[(3) in determining applicable earnings, the amount taken into account by reason of being described in paragraph (2) of section 316(a) shall be the portion of the amount so described which is allocable (on a pro rata basis) to the part of such year during which the corporation is a controlled foreign corporation.

[(f) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this section, including regulations to prevent the avoidance of the provisions of this section through reorganizations or otherwise and regulations coordinating the provisions of subsections (c)(3)(A) and (d).]

SEC. 958. RULES FOR DETERMINING STOCK OWNERSHIP.

(a) DIRECT AND INDIRECT OWNERSHIP.—

(1) GENERAL RULE.—For purposes of this subpart (other than [sections 955(b)(1)(A) and (B), 955(c)(2)(A)(ii), and 960(a)(1)] *section 960(a)(1)*), stock owned means—

(A) stock owned directly, and

(B) stock owned with the application of paragraph (2).

* * * * * * *

(b) CONSTRUCTIVE OWNERSHIP.—For purposes of sections 951(b), 954(d)(3), [956(b)(2)] *956(c)(2)*, and 957, section 318(a) (relating to constructive ownership of stock) shall apply to the extent that the effect is to treat any United States person as a United States shareholder within the meaning of section 951(b), to treat a person as a related person within the meaning of section 954(d)(3), to treat the stock of a domestic corporation as owned by a United States shareholder of the controlled foreign corporation for purposes of section [956(b)(2)] *956(c)(2)*, or to treat a foreign corporation as a controlled foreign corporation under section 957, except that—

(1) In applying paragraph (1)(A) of section 318(a), stock owned by a nonresident alien individual (other than a foreign trust or foreign estate) shall not be considered as owned by a citizen or by a resident alien individual.

(2) In applying subparagraphs (A), (B), and (C) of section 318(a)(2), if a partnership, estate, trust, or corporation owns, directly or indirectly, more than 50 percent of the total combined voting power of all classes of stock entitled to vote of a

corporation, it shall be considered as owning all the stock entitled to vote.

(3) In applying subparagraph (C) of section 318(a)(2), the phrase "10 percent" shall be substituted for the phrase "50 percent" used in subparagraph (C).

(4) Subparagraph (A), (B), and (C) of section 318(a)(3) shall not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person.

Paragraphs (1) and (4) shall not apply for purposes of section [956(b)(2)] *956(c)(2)* to treat stock of a domestic corporation as not owned by a United States shareholder.

* * * * * * *

SEC. 959. EXCLUSION FROM GROSS INCOME OF PREVIOUSLY TAXED EARNINGS AND PROFITS.

(a) EXCLUSION FROM GROSS INCOME OF UNITED STATES PERSONS.—For purposes of this chapter, the earnings and profits of a foreign corporation attributable to amounts which are, or have been, included in the gross income of a United States shareholder under section 951(a) shall not, when—

(1) such amounts are distributed to, *or*

(2) such amounts would, but for this subsection, be included under section 951(a)(1)(B) in the gross income of, [or]

[(3) such amounts would, but for this subsection, be included under section 951(a)(1)(C) in the gross income of,]

such shareholder (or any other United States person who acquires from any person any portion of the interest of such United States shareholder in such foreign corporation, but only to the extent of such portion, and subject to such proof of the identity of such interest as the Secretary may by regulations prescribe) directly or indirectly through a chain of ownership described under section 958(a), be again included in the gross income of such United States shareholder (or of such other United States person). The rules of subsection (c) shall apply for purposes of paragraph (1) of this subsection and the rules of subsection (f) shall apply for purposes of [paragraphs (2) and (3)] *paragraph (2)* of this subsection.

* * * * * * *

(c) ALLOCATION OF DISTRIBUTIONS.—For purposes of subsections (a) and (b), section 316(a) shall be applied by applying paragraph (2) thereof, and then paragraph (1) thereof—

(1) * * *

* * * * * * *

(3) then to other earnings and profits.

References in this subsection to section 951(a)(1)(C) and subsection (a)(3) shall be treated as references to such provisions as in effect on the day before the date of the enactment of the Small Business Job Protection Act of 1996.

* * * * * * *

(f) ALLOCATION RULES FOR CERTAIN INCLUSIONS.—

[(1) IN GENERAL.—For purposes of this section—

[(A) amounts that would be included under subparagraph (B) of section 951(a)(1) (determined without regard

to this section) shall be treated as attributable first to earnings described in subsection (c)(2), and then to earnings described in subsection (c)(3), and

[(B) amounts that would be included under subparagraph (C) of section 951(a)(1) (determined without regard to this section) shall be treated as attributable first to earnings described in subsection (c)(2) to the extent the earnings so described were accumulated in taxable years beginning after September 30, 1993, and then to earnings described in subsection (c)(3).]

(1) IN GENERAL.—For purposes of this section, amounts that would be included under subparagraph (B) of section 951(a)(1) (determined without regard to this section) shall be treated as attributable first to earnings described in subsection (c)(2), and then to earnings described in subsection (c)(3).

(2) TREATMENT OF DISTRIBUTIONS.—In applying this section, actual distributions shall be taken into account before amounts that would be included under [subparagraphs (B) and (C) of section 951(a)(1)] *section 951(a)(1)(B)* (determined without regard to this section).

* * * * * * *

Subpart J—Foreign Currency Transactions

* * * * * * *

SEC. 989. OTHER DEFINITIONS AND SPECIAL RULES.

(a) * * *

(b) APPROPRIATE EXCHANGE RATE.—Except as provided in regulations, for purposes of this subpart, the term "appropriate exchange rate" means—

(1) * * *

* * * * * * *

(4) in the case of any other qualified business unit of a taxpayer, the weighted average exchange rate for the taxable year of such qualified business unit.

For purposes of the preceding sentence, any amount included in income under [subparagraph (B) or (C) of section 951(a)(1)] *section 951(a)(1)(B)* shall be treated as an actual distribution made on the last day of the taxable year for which such amount was so included.

* * * * * * *

Subchapter O—Gain or Loss on Disposition of Property

* * * * * * *

PART II—BASIS RULES OF GENERAL APPLICATION

* * * * * * *

SEC. 1017. DISCHARGE OF INDEBTEDNESS.

(a) * * *

(b) AMOUNT AND PROPERTIES DETERMINED UNDER REGULATIONS.—
(1) * * *

* * * * * * *

(4) SPECIAL RULES FOR QUALIFIED FARM INDEBTEDNESS.—
(A) IN GENERAL.—Any amount which under subsection [(b)(2)(D)] *(b)(2)(E)* of section 108 is to be applied to reduce basis and which is attributable to an amount excluded under subsection (a)(1)(C) of section 108—
(i) * * *

* * * * * * *

PART III—COMMON NONTAXABLE EXCHANGE

* * * * * * *

SEC. 1042. SALES OF STOCK TO EMPLOYEE STOCK OWNERSHIP PLANS OR CERTAIN COOPERATIVES.

(a) * * *

* * * * * * *

(c) DEFINITIONS; SPECIAL RULES.—
For purposes of this section—
(1) * * *

* * * * * * *

(4) QUALIFIED REPLACEMENT PROPERTY.—
(A) IN GENERAL.—The term "qualified replacement property" means any security issued by a domestic operating corporation which—
(i) did not, for the taxable year preceding the taxable year in which such security was purchased, have passive investment income (as defined in section [1362(d)(3)(D)] *1362(d)(3)(C)*) in excess of 25 percent of the gross receipts of such corporation for such preceding taxable year, and

* * * * * * *

SEC. 1044. ROLLOVER OF PUBLICLY TRADED SECURITIES GAIN INTO SPECIALIZED SMALL BUSINESS INVESTMENT COMPANIES.

(a) * * *

* * * * * * *

(c) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—
(1) * * *
[(2) PURCHASE.—The term "purchase" has the meaning given such term by section 1043(b)(4).]
(2) PURCHASE.—The taxpayer shall be considered to have purchased any property if, but for subsection (d), the unadjusted basis of such property would be its cost within the meaning of section 1012.

* * * * * * *

Subchapter P—Capital Gains and Losses

PART I—TREATMENT OF CAPITAL GAINS

* * * * * * *

SEC. 1201. ALTERNATIVE TAX FOR CORPORATIONS.

(a) GENERAL RULE.—If for any taxable year a corporation has a net capital gain and any rate of tax imposed by section 11, 511, or 831(a) or (b) (whichever is applicable) exceeds 35 percent (determined without regard to the [last sentence] *last 2 sentences* of section 11(b)(1)), then, in lieu of any such tax, there is hereby imposed a tax (if such tax is less than the tax imposed by such sections) which shall consist of the sum of—

(1) a tax computed on the taxable income reduced by the amount of the net capital gain, at the rates and in the manner as if this subsection had not been enacted, plus

(2) a tax of 34 percent of the net capital gain.

* * * * * * *

PART IV—SPECIAL RULES FOR DETERMINING CAPITAL GAINS AND LOSSES

* * * * * * *

SEC. 1237. REAL PROPERTY SUBDIVIDED FOR SALE.

(a) GENERAL.—Any lot or parcel which is part of a tract of real property in the hands of a taxpayer [other than a corporation] *other than a C corporation* shall not be deemed to be held primarily for sale to customers in the ordinary course of trade or business at the time of sale solely because of the taxpayer having subdivided such tract for purposes of sale or because of any activity incident to such subdivision or sale, if—

(1) such tract, or any lot or parcel thereof, had not previously been held by such taxpayer primarily for sale to customers in the ordinary course of trade or business (unless such tract at such previous time would have been covered by this section) and, in the same taxable year in which the sale occurs, such taxpayer does not so hold any other real property; and

(2) no substantial improvement that substantially enhances the value of the lot or parcel sold is made by the taxpayer on such tract while held by the taxpayer or is made pursuant to a contract of sale entered into between the taxpayer and the buyer. For purposes of this paragraph, an improvement shall be deemed to be made by the taxpayer if such improvement was made by—

(A) the taxpayer or members of his family (as defined in section 267(c)(4)), by a corporation controlled by the taxpayer, *an S corporation which included the taxpayer as a shareholder,* or by a partnership which included the taxpayer as a partner; or

* * * * * * *

SEC. 1245. GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE PROPERTY.

(a) GENERAL RULE.—

(1) * * *

* * * * * * *

[(3) SECTION 1245 PROPERTY.—For purposes of this section, the term "section 1245 property" means any property which is or has been property of a character subject to the allowance for depreciation provided in section 167 (or subject to the allowance of amortization provided in) and is either—]

(3) SECTION 1245 PROPERTY.—For purposes of this section, the term "section 1245 property" means any property which is or has been property of a character subject to the allowance for depreciation provided in section 167 and is either—

(A) * * *

* * * * * * *

SEC. 1248. GAIN FROM CERTAIN SALES OR EXCHANGES OF STOCK IN CERTAIN FOREIGN CORPORATIONS.

(a) GENERAL RULE.—If—

(1) a United States person sells or exchanges stock in a foreign corporation[, or if a United States person receives a distribution from a foreign corporation which, under section 302 or 331, is treated as an exchange of stock], and

* * * * * * *

then the gain recognized on the sale or exchange of such stock shall be included in the gross income of such person as a dividend, to the extent of the earnings and profits of the foreign corporation attributable (under regulations prescribed by the Secretary) to such stock which were accumulated in taxable years of such foreign corporation beginning after December 31, 1962, and during the period or periods the stock sold or exchanged was held by such person while such foreign corporation was a controlled foreign corporation. *For purposes of this section, a United States person shall be treated as having sold or exchanged any stock if, under any provision of this subtitle, such person is treated as realizing gain from the sale or exchange of such stock.*

* * * * * * *

(e) SALES OR EXCHANGES OF STOCK IN CERTAIN DOMESTIC CORPORATIONS.—Except as provided in regulations prescribed by the Secretary, if—

(1) a United States person sells or exchanges stock of a domestic corporation[, or receives a distribution from a domestic corporation which, under section 302 or 331, is treated as an exchange of stock], and

* * * * * * *

(f) CERTAIN NONRECOGNITION TRANSACTIONS.—Except as provided in regulations prescribed by the Secretary—

(1) IN GENERAL.—If—

(A) a domestic corporation satisfies the stock ownership requirements of subsection (a)(2) with respect to a foreign corporation, and

(B) such domestic corporation distributes stock of such foreign corporation in a distribution to which section 311(a), 337, [or 361(c)(1)] *355(c)(1), or 361(c)(1)* applies,

then, notwithstanding any other provision of this subtitle, an amount equal to the excess of the fair market value of such stock over its adjusted basis in the hands of the domestic corporation shall be included in the gross income of the domestic corporation as a dividend to the extent of the earnings and profits of the foreign corporation attributable (under regulations prescribed by the Secretary) to such stock which were accumulated in taxable years of such foreign corporation beginning after December 31, 1962, and during the period or periods the stock was held by such domestic corporation while such foreign corporation was a controlled foreign corporation. For purposes of subsections (c)(2), (d), and (h), a distribution of stock to which this subsection applies shall be treated as a sale of stock to which subsection (a) applies.

* * * * * * *

(i) TREATMENT OF CERTAIN INDIRECT TRANSFERS.—

[(1) IN GENERAL.—If any shareholder of a 10-percent corporate shareholder of a foreign corporation exchanges stock of the 10-percent corporate shareholder for stock of the foreign corporation, for purposes of this section, the stock of the foreign corporation received in such exchange shall be treated as if it had been—

[(A) issued to the 10-percent corporate shareholder, and

[(B) then distributed by the 10-percent corporate shareholder to such shareholder in redemption or liquidation (whichever is appropriate).]

(1) IN GENERAL.—If any shareholder of a 10-percent corporate shareholder of a foreign corporation exchanges stock of the 10-percent corporate shareholder for stock of the foreign corporation, such 10-percent corporate shareholder shall recognize gain in the same manner as if the stock of the foreign corporation received in such exchange had been—

(A) issued to the 10-percent corporate shareholder, and

(B) then distributed by the 10-percent corporate shareholder to such shareholder in redemption or liquidation (whichever is appropriate).

The amount of gain recognized by such 10-percent corporate shareholder under the preceding sentence shall not exceed the amount treated as a dividend under this section.

* * * * * * *

SEC. 1250. GAIN FROM DISPOSITIONS OF CERTAIN DEPRECIABLE REALTY.

(a) * * *

* * * * * * *

(e) HOLDING PERIOD.—For purposes of determining the applicable percentage under this section, the provisions of section 1223 shall not apply, and the holding period of section 1250 property shall be determined under the following rules:

(1) * * *

* * * * * * *

[(4) QUALIFIED LOW-INCOME HOUSING.—The holding period of any section 1250 property acquired which is described in sub-

section (d)(8)(E)(i) shall include the holding period of the corresponding element of section 1250 property disposed of.]

* * * * * * *

PART V—SPECIAL RULES FOR BONDS AND OTHER DEBT INSTRUMENTS

* * * * * * *

Subpart A—Original Issue Discount

* * * * * * *

SEC. 1274. DETERMINATION OF ISSUE PRICE IN THE CASE OF CERTAIN DEBT INSTRUMENTS ISSUED FOR PROPERTY.

(a) * * *

(b) IMPUTED PRINCIPAL AMOUNT.—For purposes of this section—

(1) * * *

* * * * * * *

(3) FAIR MARKET VALUE RULE IN POTENTIALLY ABUSIVE SITUATIONS.—

(A) * * *

(B) POTENTIALLY ABUSIVE SITUATION DEFINED.— For purposes of subparagraph (A), the term "potentially abusive situation" means—

(i) a tax shelter (as defined in section [6662(d)(2)(C)(ii)] *6662(d)(2)(C)(iii)*), and

* * * * * * *

SEC. 1274A. SPECIAL RULES FOR CERTAIN TRANSACTIONS WHERE STATED PRINCIPAL AMOUNT DOES NOT EXCEED $2,800,000.

(a) * * *

* * * * * * *

(c) ELECTION TO USE CASH METHOD WHERE STATED PRINCIPAL AMOUNT DOES NOT EXCEED $2,000,000.—

(1) IN GENERAL.—In the case of any cash method debt instrument—

(A) section 1274 shall not apply, and

(B) interest on such debt [instument] *instrument* shall be taken into account by both the borrower and the lender under the cash receipts and disbursements method of accounting.

* * * * * * *

PART VI—TREATMENT OF CERTAIN PASSIVE FOREIGN INVESTMENT COMPANIES

* * * * * * *

Subpart C—General Provisions

* * * * * * *

SEC. 1296. PASSIVE FOREIGN INVESTMENT COMPANY.

(a) * * *

(b) PASSIVE INCOME.—For purposes of this section—

(1) * * *

(2) EXCEPTIONS.—Except as provided in regulations, the term "passive income" does not include any income—

(A) derived in the active conduct of a banking business by an institution licensed to do business as a bank in the United States (or, to the extent provided in regulations, by any other corporation),

(B) derived in the active conduct of an insurance business by a corporation which is predominantly engaged in an insurance business and which would be subject to tax under subchapter L if it were a domestic corporation, [or]

(C) which is interest, a dividend, or a rent or royalty, which is received or accrued from a related person (within the meaning of section 954(d)(3)) to the extent such amount is properly allocable (under regulations prescribed by the Secretary) to income of such related person which is not passive income[.], *or*

(D) which is foreign trade income of a FSC or export trade income of an export trade corporation (as defined in section 971).

For purposes of subparagraph (C), the term "related person" has the meaning given such term by section 954(d)(3) determined by substituting "foreign corporation" for "controlled foreign corporation" each place it appears in section 954(d)(3).

* * * * * * *

SEC. 1297. SPECIAL RULES.

(a) * * *

* * * * * * *

(d) TREATMENT OF CERTAIN LEASED PROPERTY.—For purposes of this part—

(1) * * *

[(2) DETERMINATION OF ADJUSTED BASIS.—]

(2) AMOUNT TAKEN INTO ACCOUNT.—

(A) IN GENERAL.—[The adjusted basis of any asset] *The amount taken into account under section 1296(a)(2) with respect to any asset* to which paragraph (1) applies shall be the unamortized portion (as determined under regulations prescribed by the Secretary) of the present value of the payments under the lease for the use of such property.

* * * * * * *

(e) SPECIAL RULES FOR CERTAIN INTANGIBLES.—*For purposes of this part—*

(1) * * *

* * * * * * *

Subchapter S—Tax Treatment of S Corporations

* * * * * * *

PART I—IN GENERAL

* * * * * * *

SEC. 1361. S CORPORATION DEFINED.

(a) * * *

(b) SMALL BUSINESS CORPORATION.—

(1) IN GENERAL.—For purposes of this subchapter, the term "small business corporation" means a domestic corporation which is not an ineligible corporation and which does not—

(A) have more than [35] *75* shareholders,

* * * * * * *

(2) INELIGIBLE CORPORATION DEFINED.—For purposes of paragraph (1), the term "ineligible corporation" means any corporation which is—

[(A) a member of an affiliated group (determined under section 1504 without regard to the exceptions contained in subsection (b) thereof),]

[(B)] *(A)* a financial institution to which section 585 applies (or would apply but for subsection (c) thereof) or to which section 593 applies,

[(C)] *(B)* an insurance company subject to tax under subchapter L,

[(D)] *(C)* a corporation to which an election under section 936 applies, or

[(E)] *(D)* a DISC or former DISC.

(3) TREATMENT OF CERTAIN WHOLLY OWNED SUBSIDIARIES.—

(A) IN GENERAL.—For purposes of this title—

(i) a corporation which is a qualified subchapter S subsidiary shall not be treated as a separate corporation, and

(ii) all assets, liabilities, and items of income, deduction, and credit of a qualified subchapter S subsidiary shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

(B) QUALIFIED SUBCHAPTER S SUBSIDIARY.—For purposes of this paragraph, the term 'qualified subchapter S subsidiary' means any domestic corporation which is not an ineligible corporation (as defined in paragraph (2)), if—

(i) 100 percent of the stock of such corporation is held by the S corporation, and

(ii) the S corporation elects to treat such corporation as a qualified subchapter S subsidiary.

(C) TREATMENT OF TERMINATIONS OF QUALIFIED SUBCHAPTER S SUBSIDIARY STATUS.—For purposes of this title, if any corporation which was a qualified subchapter S subsidiary ceases to meet the requirements of subparagraph (B), such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the S corporation in exchange for its stock.

(c) SPECIAL RULES FOR APPLYING SUBSECTION (b).—

(1) * * *

(2) CERTAIN TRUSTS PERMITTED AS SHAREHOLDERS.—

(A) IN GENERAL.—For purposes of subsection (b)(1)(B), the following trusts may be shareholders:

(i) A trust all of which is treated (under subpart E of part I of subchapter J of this chapter) as owned by an individual who is a citizen or resident of the United States.

(ii) A trust which was described in clause (i) immediately before the death of the deemed owner and which continues in existence after such death, but only for the [60-day period] *2-year period* beginning on the day of the deemed owner's death. [If a trust is described in the preceding sentence and if the entire corpus of the trust is includible in the gross estate of the deemed owner, the preceding sentence shall be applied by substituting "2-year period" for "60-day period".]

(iii) A trust with respect to stock transferred to it pursuant to the terms of a will, but only for the [60-day period] *2-year period* beginning on the day on which such stock is transferred to it.

(iv) A trust created primarily to exercise the voting power of stock transferred to it.

(v) An electing small business trust.

This subparagraph shall not apply to any foreign trust.

(B) TREATMENT AS SHAREHOLDERS.—For purposes of subsection (b)(1)—

(i) In the case of a trust described in clause (i) of subparagraph (A), the deemed owner shall be treated as the shareholder.

(ii) In the case of a trust described in clause (ii) of subparagraph (A), the estate of the deemed owner shall be treated as the shareholder.

(iii) In the case of a trust described in clause (iii) of subparagraph (A), the estate of the testator shall be treated as the shareholder.

(iv) In the case of a trust described in clause (iv) of subparagraph (A), each beneficiary of the trust shall be treated as a shareholder.

(v) In the case of a trust described in clause (v) of subparagraph (A), each potential current beneficiary of such trust shall be treated as a shareholder; except that, if for any period there is no potential current beneficiary of such trust, such trust shall be treated as the shareholder during such period.

* * * * * * *

(5) STRAIGHT DEBT SAFE HARBOR.—

(A) * * *

(B) STRAIGHT DEBT DEFINED.—For purposes of this paragraph, the term "straight debt" means any written unconditional promise to pay on demand or on a specified date a sum certain in money if—

(i) * * *

* * * * * * *

(iii) the creditor is an individual (other than a nonresident alien), an estate, [or a trust described in paragraph (2)] *a trust described in paragraph (2), or a person which is actively and regularly engaged in the business of lending money.*

[(6) OWNERSHIP OF STOCK IN CERTAIN INACTIVE CORPORATIONS.—For purposes of subsection (b)(2)(A), a corporation shall not be treated as a member of an affiliated group during any period within a taxable year by reason of the ownership of stock in another corporation if such other corporation—

[(A) has not begun business at any time on or before the close of such period, and

[(B) does not have gross income for such period.]

* * * * * * *

(e) ELECTING SMALL BUSINESS TRUST DEFINED.—

(1) ELECTING SMALL BUSINESS TRUST.—For purposes of this section—

(A) IN GENERAL.—Except as provided in subparagraph (B), the term "electing small business trust" means any trust if—

(i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, or (III) an organization described in paragraph (2), (3), (4), or (5) of section 170(c) which holds a contingent interest and is not a potential current beneficiary,

(ii) no interest in such trust was acquired by purchase, and

(iii) an election under this subsection applies to such trust.

(B) CERTAIN TRUSTS NOT ELIGIBLE.—The term "electing small business trust" shall not include—

(i) any qualified subchapter S trust (as defined in subsection (d)(3)) if an election under subsection (d)(2) applies to any corporation the stock of which is held by such trust, and

(ii) any trust exempt from tax under this subtitle.

(C) PURCHASE.—For purposes of subparagraph (A), the term "purchase" means any acquisition if the basis of the property acquired is determined under section 1012.

(2) POTENTIAL CURRENT BENEFICIARY.—For purposes of this section, the term "potential current beneficiary" means, with respect to any period, any person who at any time during such period is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust. If a trust disposes of all of the stock which it holds in an S corporation, then, with respect to such corporation, the term "potential current beneficiary" does not include any person who first met the requirements of the preceding sentence during the 60-day period ending on the date of such disposition.

(3) ELECTION.—An election under this subsection shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent taxable years of such trust unless revoked with the consent of the Secretary.

(4) CROSS REFERENCE.—

For special treatment of electing small business trusts, see section 641(d).

* * * * * * *

SEC. 1362. ELECTION; REVOCATION; TERMINATION.

(a) * * *

(b) WHEN MADE.—

(1) * * *

* * * * * * *

(5) AUTHORITY TO TREAT LATE ELECTIONS, ETC., AS TIMELY.—If—

(A) an election under subsection (a) is made for any taxable year (determined without regard to paragraph (3)) after the date prescribed by this subsection for making such election for such taxable year or no such election is made for any taxable year, and

(B) the Secretary determines that there was reasonable cause for the failure to timely make such election,

the Secretary may treat such an election as timely made for such taxable year (and paragraph (3) shall not apply).

* * * * * * *

(d) TERMINATION.—

(1) * * *

* * * * * * *

(3) WHERE PASSIVE INVESTMENT INCOME EXCEEDS 25 PERCENT OF GROSS RECEIPTS FOR 3 CONSECUTIVE TAXABLE YEARS AND CORPORATION HAS [SUBCHAPTER C] *ACCUMULATED* EARNINGS AND PROFITS.—

(A) TERMINATION.—

(i) IN GENERAL.—An election under subsection (a) shall be terminated whenever the corporation—

(I) has [subchapter C] *accumulated* earnings and profits at the close of each of 3 consecutive taxable years, and

[(B) SUBCHAPTER C EARNINGS AND PROFITS.—For purposes of subparagraph (A), the term "subchapter C earnings and profits" means earnings and profits of any corporation for any taxable year with respect to which an election under section 1362(a) (or under section 1372 of prior law) was not in effect.]

[(C)] *(B)* GROSS RECEIPTS FROM SALES OF CAPITAL ASSETS (OTHER THAN STOCK AND SECURITIES).—For purposes of this paragraph, in the case of dispositions of capital assets (other than stock and securities), gross receipts from such dispositions shall be taken into account only to the extent of the capital gain net income therefrom.

[(D)] *(C)* PASSIVE INVESTMENT INCOME DEFINED.—For purposes of this paragraph—

(i) * * *

* * * * * * *

[(E)] *(D)* SPECIAL RULE FOR OPTIONS AND COMMODITY DEALINGS.—

(i) * * *

* * * * * * *

(F) TREATMENT OF CERTAIN DIVIDENDS.—If an S corporation holds stock in a C corporation meeting the requirements of section 1504(a)(2), the term "passive investment income" shall not include dividends from such C corporation to the extent such dividends are attributable to the earnings and profits of such C corporation derived from the active conduct of a trade or business.

* * * * * * *

[(f) INADVERTENT TERMINATIONS.—If—

[(1) an election under subsection (a) by any corporation was terminated under paragraph (2) or (3) of subsection (d),

[(2) the Secretary determines that the termination was inadvertent,

[(3) no later than a reasonable period of time after discovery of the event resulting in such termination, steps were taken so that the corporation is once more a small business corporation, and

[(4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period,

then, notwithstanding the terminating event, such corporation shall be treated as continuing to be an S corporation during the period specified by the Secretary.]

(f) INADVERTENT INVALID ELECTIONS OR TERMINATIONS.—If—

(1) an election under subsection (a) by any corporation—

(A) was not effective for the taxable year for which made (determined without regard to subsection (b)(2)) by reason of a failure to meet the requirements of section 1361(b) or to obtain shareholder consents, or

(B) was terminated under paragraph (2) or (3) of subsection (d),

(2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent,

(3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken—

(A) so that the corporation is a small business corporation, or

(B) to acquire the required shareholder consents, and

(4) the corporation, and each person who was a shareholder in the corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period,

then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.

* * * * * * *

PART II—TAX TREATMENT OF SHAREHOLDERS

* * * * * * *

SEC. 1366. PASS-THRU OF ITEMS TO SHAREHOLDERS.

(a) DETERMINATION OF SHAREHOLDER'S TAX LIABILITY.—

(1) IN GENERAL.—In determining the tax under this chapter of a shareholder for the shareholder's taxable year in which the taxable year of the S corporation ends (or for the final taxable year of a shareholder who dies, *or of a trust or estate which terminates,* before the end of the corporation's taxable year), there shall be taken into account the shareholder's pro rata share of the corporation's—

(A) * * *

* * * * * * *

(d) SPECIAL RULES FOR LOSSES AND DEDUCTIONS.—

(1) CANNOT EXCEED SHAREHOLDER'S BASIS IN STOCK AND DEBT.—The aggregate amount of losses and deductions taken into account by a shareholder under subsection (a) for any taxable year shall not exceed the sum of—

(A) the adjusted basis of the shareholder's stock in the S corporation (determined with regard to [paragraph (1)] *paragraphs (1) and (2)(A)* of section 1367(a) for the taxable year), and

* * * * * * *

(3) CARRYOVER OF DISALLOWED LOSSES AND DEDUCTIONS TO POST-TERMINATION TRANSITION PERIOD.—

(A) * * *

* * * * * * *

(D) AT-RISK LIMITATIONS.—To the extent that any increase in adjusted basis described in subparagraph (B) would have increased the shareholder's amount at risk under section 465 if such increase had occurred on the day preceding the commencement of the post-termination transition period, rules similar to the rules described in subparagraphs (A) through (C) shall apply to any losses disallowed by reason of section 465(a).

* * * * * * *

[(g) CROSS REFERENCE.—

[For rules relating to procedures for determining the tax treatment of subchapter S items, see subchapter D of chapter 63.]

* * * * * * *

SEC. 1367. ADJUSTMENTS TO BASIS OF STOCK OF SHAREHOLDERS, ETC.

(a) GENERAL RULE.—

(1) * * *

(2) DECREASES IN BASIS.—The basis of each shareholder's stock in an S corporation shall be decreased for any period (but not below zero) by the sum of the following items determined with respect to the shareholder for such period:

(A) * * *

* * * * * * *

(E) the amount of the shareholder's deduction for depletion for any oil and gas property held by the S corporation to the extent such deduction does not exceed the proportionate share of the adjusted basis of such property allocated to such shareholder under [section 613A(c)(13)(B)] *section 613A(c)(11)(B).*

(b) SPECIAL RULES.—

(1) * * *

* * * * * * *

(4) ADJUSTMENTS IN CASE OF INHERITED STOCK.—

(A) IN GENERAL.—If any person acquires stock in an S corporation by reason of the death of a decedent or by bequest, devise, or inheritance, section 691 shall be applied with respect to any item of income of the S corporation in the same manner as if the decedent had held directly his pro rata share of such item.

(B) ADJUSTMENTS TO BASIS.—The basis determined under section 1014 of any stock in an S corporation shall be reduced by the portion of the value of the stock which is attributable to items constituting income in respect of the decedent.

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SEC. 1368. DISTRIBUTIONS.

(a) * * *

* * * * * * *

(d) CERTAIN ADJUSTMENTS TAKEN INTO ACCOUNT.—Subsections (b) and (c) shall be applied by taking into account (to the extent proper)—

(1) the adjustments to the basis of the shareholder's stock described in section 1367, and

(2) the adjustments to the accumulated adjustments account which are required by subsection (e)(1).

In the case of any distribution made during any taxable year, the adjusted basis of the stock shall be determined with regard to the adjustments provided in paragraph (1) of section 1367(a) for the taxable year.

(e) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) ACCUMULATED ADJUSTMENTS ACCOUNT.—

(A) IN GENERAL.—Except [as provided in subparagraph (B)] *as otherwise provided in this paragraph,* the term "accumulated adjustments account" means an account of the S corporation which is adjusted for the S period in a manner similar to the adjustments under section 1367 (except that no adjustment shall be made for income (and related

expenses) which is exempt from tax under this title and the phrase "(but not below zero)" shall be disregarded in [section 1367(b)(2)(A)] *section 1367(a)(2)*) and no adjustment shall be made for Federal taxes attributable to any taxable year in which the corporation was a C corporation.

* * * * * * *

(C) NET LOSS FOR YEAR DISREGARDED.—

(i) IN GENERAL.—In applying this section to distributions made during any taxable year, the amount in the accumulated adjustments account as of the close of such taxable year shall be determined without regard to any net negative adjustment for such taxable year.

(ii) NET NEGATIVE ADJUSTMENT.—For purposes of clause (i), the term "net negative adjustment" means, with respect to any taxable year, the excess (if any) of—

(I) the reductions in the account for the taxable year (other than for distributions), over

(II) the increases in such account for such taxable year.

* * * * * * *

PART III—SPECIAL RULES

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SEC. 1371. COORDINATION WITH SUBCHAPTER C.

[(a) APPLICATION OF SUBCHAPTER C RULES.—

[(1) IN GENERAL.—Except as otherwise provided in this title, and except to the extent inconsistent with this subchapter, subchapter C shall apply to an S corporation and its shareholders.

[(2) S CORPORATION AS SHAREHOLDER TREATED LIKE INDIVIDUAL.—For purposes of subchapter C, an S corporation in its capacity as a shareholder of another corporation shall be treated as an individual.]

(a) APPLICATION OF SUBCHAPTER C RULES.—Except as otherwise provided in this title, and except to the extent inconsistent with this subchapter, subchapter C shall apply to an S corporation and its shareholders.

* * * * * * *

SEC. 1375. TAX IMPOSED WHEN PASSIVE INVESTMENT INCOME OF CORPORATION HAVING [SUBCHAPTER C] *ACCUMULATED* EARNINGS AND PROFITS EXCEEDS 25 PERCENT OF GROSS RECEIPTS.

(a) GENERAL RULE.—If for the taxable year an S corporation has—

(1) [subchapter C] *accumulated* earnings and profits at the close of such taxable year, and

* * * * * * *

(b) DEFINITIONS.—For purposes of this section—

(1) * * *

* * * * * * *

[(3) PASSIVE INVESTMENT INCOME; ETC.—The terms "subchapter C earnings and profits", "passive investment income", and "gross receipts" shall have the same respective meanings as when used in paragraph (3) of section 1362(d).]

(3) PASSIVE INVESTMENT INCOME, ETC.—The terms "passive investment income" and "gross receipts" have the same respective meanings as when used in paragraph (3) of section 1362(d).

* * * * * * *

PART IV—DEFINITIONS; MISCELLANEOUS

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SEC. 1377. DEFINITIONS AND SPECIAL RULE.

(a) PRO RATA SHARE.—For purposes of this subchapter—

(1) * * *

[(2) ELECTION TO TERMINATE YEAR.—Under regulations prescribed by the Secretary, if any shareholder terminates his interest in the corporation during the taxable year and all persons who are shareholders during the taxable year agree to the application of this paragraph, paragraph (1) shall be applied as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination.]

(2) ELECTION TO TERMINATE YEAR.—

(A) IN GENERAL.—Under regulations prescribed by the Secretary, if any shareholder terminates the shareholder's interest in the corporation during the taxable year and all affected shareholders and the corporation agree to the application of this paragraph, paragraph (1) shall be applied to the affected shareholders as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination.

(B) AFFECTED SHAREHOLDERS.—For purposes of subparagraph (A), the term "affected shareholders" means the shareholder whose interest is terminated and all shareholders to whom such shareholder has transferred shares during the taxable year. If such shareholder has transferred shares to the corporation, the term "affected shareholders" shall include all persons who are shareholders during the taxable year.

(b) POST-TERMINATION TRANSITION PERIOD.—

(1) IN GENERAL.—For purposes of this subchapter, the term "post-termination transition period" means—

(A) the period beginning on the day after the last day of the corporation's last taxable year as an S corporation and ending on the later of—

(i) the day which is 1 year after such last day, or

(ii) the due date for filing the return for such last year as an S corporation (including extensions), [and]

(B) the 120-day period beginning on the date of any determination pursuant to an audit of the taxpayer which follows the termination of the corporation's election and which adjusts a subchapter S item of income, loss, or deduction of the corporation arising during the S period (as defined in section 1368(e)(2)), and

[(B)] *(C)* the 120-day period beginning on the date of a determination that the corporation's election under section 1362(a) had terminated for a previous taxable year.

(2) DETERMINATION DEFINED.—For purposes of paragraph (1), the term "determination" means—

[(A) a court decision which becomes final,

[(B) a closing agreement, or]

(A) a determination as defined in section 1313(a), or

[(C)] *(B)* an agreement between the corporation and the Secretary that the corporation failed to qualify as an S corporation.

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Subchapter U—Designation and Treatment of Empowerment Zones, Enterprise Communities, and Rural Development Investment Areas

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PART II—TAX-EXEMPT FACILITY BONDS FOR EMPOWERMENT ZONES AND ENTERPRISE COMMUNITIES

* * * * * * *

SEC. 1394. TAX-EXEMPT ENTERPRISE ZONE FACILITY BONDS.

(a) * * *

* * * * * * *

(e) PENALTY FOR CEASING TO MEET REQUIREMENTS.—

(1) * * *

(2) LOSS OF DEDUCTIONS WHERE FACILITY CEASES TO BE QUALIFIED.—No deduction shall be allowed under this chapter for interest on any financing provided from any bond to which subsection (a) applies with respect to any facility to the extent such interest accrues during the period beginning on the first day of the calendar year which includes the date on which—

[(i)] *(A)* substantially all of the facility with respect to which the financing was provided ceases to be used in an empowerment zone or enterprise community, or

[(ii)] *(B)* the principal user of such facility ceases to be an enterprise zone business (as defined in subsection (b)).

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PART III—ADDITIONAL INCENTIVIES FOR EMPOWERMENT ZONES

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Subpart A—Empowerment Zone Employment Credit

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SEC. 1396. EMPOWERMENT ZONE EMPLOYMENT CREDIT.

(a) * * *

* * * * * * *

(c) QUALIFIED ZONE WAGES.—

(1) * * *

* * * * * * *

(3) COORDINATION WITH [TARGETED JOBS CREDIT] *WORK OPPORTUNITY CREDIT.*—

(A) IN GENERAL.—The term "qualified zone wages" shall not include wages taken into account in determining the credit under section 51.

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Subpart B—Additional Expensing

* * * * * * *

SEC. 1397B. ENTERPRISE ZONE BUSINESS DEFINED.

(a) * * *

* * * * * * *

(d) QUALIFIED BUSINESS.—For purposes of this section—

(1) * * *

* * * * * * *

(5) CERTAIN BUSINESSES EXCLUDED.—The term "qualified business" shall not include—

(A) any trade or business consisting of the operation of any facility described in section 144(c)(6)(B), and

(B) any trade or business the principal activity of which is farming (within the meaning of subparagraphs (A) or (B) of section 2032A(e)(5)), but only if, as of the close of the [preceding] taxable year, the sum of—

(i) the aggregate unadjusted bases (or, if greater, the fair market value) of the assets owned by the taxpayer which are used in such a trade or business, and

(ii) the aggregate value of assets leased by the taxpayer which are used in such a trade or business,exceeds $500,000.

For purposes of subparagraph (B), rules similar to the rules of section 1397(b) shall apply.

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CHAPTER 2—TAX ON SELF-EMPLOYMENT INCOME

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SEC. 1402. DEFINITIONS.

(a) NET EARNINGS FROM SELF-EMPLOYMENT.—The term "net earnings from self-employment" means the gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed by this subtitle which are attributable to such trade or business, plus his distributive share (whether or not distributed) of income or loss described in section 702(a)(8) from any trade or business carried on by a partnership of which he is a member; except that in computing such gross income and deductions and such distributive share of partnership ordinary income or loss—

(1) * * *

* * * * * * *

(8) an individual who is a duly ordained, commissioned, or licensed minister of a church or a member of a religious order shall compute his net earnings from self-employment derived from the performance of service described in subsection (c)(4) without regard to section 107 (relating to rental value of parsonages), section 119 (relating to meals and lodging furnished for the convenience of the employer), and section 911 (relating to citizens or residents of the United States living abroad), *but shall not include in such net earnings from self-employment the rental value of any parsonage (whether or not excludable under section 107) provided after the individual retires, or any other retirement benefit received by such individual from a church plan (as defined in section 414(e)) after the individual retires*;

* * * * * * *

CHAPTER 3—WITHHOLDING OF TAX ON NONRESIDENT ALIENS AND FOREIGN CORPORATIONS

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Subchapter A—Nonresident Aliens and Foreign Corporations

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SEC. 1445. WITHHOLDING OF TAX ON DISPOSITIONS OF UNITED STATES REAL PROPERTY INTERESTS.

(a) * * *

* * * * * * *

(e) SPECIAL RULES RELATING TO DISTRIBUTIONS, ETC., BY CORPORATIONS, PARTNERSHIPS, TRUSTS, OR ESTATES.—

(1) * * *

* * * * * * *

(3) DISTRIBUTIONS BY CERTAIN DOMESTIC CORPORATIONS TO FOREIGN SHAREHOLDERS.—If a domestic corporation which is or has been a United States real property holding corporation (as defined in section 897(c)(2)) during the applicable period specified in section 897(c)(1)(A)(ii) distributes property to a foreign person in a transaction to which section 302 or part II of subchapter C applies, such corporation shall deduct and withhold under subsection (a) a tax equal to 10 percent of the amount realized by the foreign shareholder. The preceding sentence shall not apply if, as of the date of the distribution, interests in such corporation are not United States real property interests by reason of section 897(c)(1)(B). *Rules similar to the rules of the preceding provisions of this paragraph shall apply in the case of any distribution to which section 301 applies and which is not made out of the earnings and profits of such a domestic corporation.*

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Subchapter B—Application of Withholding Provisions

* * * * * * *

SEC. 1463. TAX PAID BY RECIPIENT OF INCOME.

If—

(1) any person, in violation of the provisions of this chapter, fails to deduct and withhold any tax under this chapter, and

(2) thereafter the tax against which such tax may be credited is paid,

the tax so required to be deducted and withheld shall not be collected from such person; but this [subsection] *section* shall in no case relieve such person from liability for interest or any penalties or additions to the tax otherwise applicable in respect of such failure to deduct and withhold.

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CHAPTER 6—CONSOLIDATED RETURNS

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Subchapter A—Returns and Payment of Tax

* * * * * * *

SEC. 1504. DEFINITIONS.

(a) * * *

(b) DEFINITION OF "INCLUDIBLE CORPORATION".—As used in this chapter, the term "includible corporation" means any corporation except—

(1) * * *

* * * * * * *

(8) An S corporation.

(c) INCLUDIBLE INSURANCE COMPANIES.—Notwithstanding the provisions of paragraph (2) of subsection (b)—

(1) * * *

(2)(A) * * *

(B) IF AN ELECTION UNDER THIS PARAGRAPH IS IN EFFECT FOR A TAXABLE YEAR.—

(i) section 243(b)(3) and the exception provided under *section* 243(b)(2) with respect to subsections (b)(2) and (c) of this section,

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Subchapter B—Related Rules

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PART II—CERTAIN CONTROLLED CORPORATIONS

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SEC. 1561. LIMITATIONS ON CERTAIN MULTIPLE TAX BENEFITS IN THE CASE OF CERTAIN CONTROLLED CORPORATIONS.

(a) GENERAL RULE.—The component members of a controlled group of corporations on a December 31 shall, for their taxable years which include such December 31, be limited for purposes of this subtitle to—

(1) amounts in each taxable income bracket in the tax table in section 11(b)(1) which do not aggregate more than the maximum amount in such bracket to which a corporation which is not a component member of a controlled group is entitled,

(2) one $250,000 ($150,000 if any component member is a corporation described in section 535(c)(2)(B)) amount for purposes of computing the accumulated earnings credit under section 535(c)(2) and (3),

(3) one $40,000 exemption amount for purposes of computing the amount of the minimum tax, and

(4) one $2,000,000 amount for purposes of computing the tax imposed by section 59A.

The amounts specified in paragraph (1), the amount specified in paragraph (3), and the amount specified in paragraph (4) shall be divided equally among the component members of such group on such December 31 unless all of such component members consent (at such time and in such manner as the Secretary shall by regulations prescribe) to an apportionment plan providing for an unequal allocation of such amounts. The amounts specified in paragraph (2) shall be divided equally among the component members of such group on such December 31 unless the Secretary prescribes regulations permitting an unequal allocation of such amounts. Notwithstanding paragraph (1), in applying the [last sentence] *last 2 sentences* of section 11(b)(1) to such component members, the taxable income of all such component members shall be taken into account and any increase in tax under such [last sentence] *last 2 sentences* shall be divided among such component members in the same manner as amounts under paragraph (1). In applying section 55(d)(3), the alternative minimum taxable income of all component members shall be taken into account and any decrease in the exemption

amount shall be allocated to the component members in the same manner as under paragraph (3).

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Subtitle B—Estate and Gift Taxes

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CHAPTER 11—ESTATE TAX

* * * * * * *

Subchapter B—Estates of Nonresidents Not Citizens

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SEC. 2102. CREDITS AGAINST TAX.

(a) * * *

* * * * * * *

(c) UNIFIED CREDIT.—

(1) * * *

* * * * * * *

(3) SPECIAL RULES.—

(A) COORDINATION WITH TREATIES.—To the extent required under any treaty obligation of the United States, the credit allowed under this subsection shall be equal to the amount which bears the same ratio to $192,800 as the value of the part of the decedent's gross estate which at the time of his death is situated in the United States bears to the value of his entire gross estate wherever situated. *For purposes of the preceding sentence, property shall not be treated as situated in the United States if such property is exempt from the tax imposed by this subchapter under any treaty obligation of the United States.*

* * * * * * *

SEC. 2104. PROPERTY WITHIN THE UNITED STATES.

(a) * * *

* * * * * * *

(c) DEBT OBLIGATIONS.—For purposes of this subchapter, debt obligations of—

(1) a United States person, or

(2) the United States, a State or any political subdivision thereof, or the District of Columbia,

owned and held by a nonresident not a citizen of the United States shall be deemed property within the United States. With respect to estates of decedents dying after December 31, 1969, deposits with a domestic branch of a foreign corporation, if such branch is engaged in the commercial banking business, shall, for purposes of this subchapter, be deemed property within the United States. This

subsection shall not apply to a debt obligation to which section 2105(b) applies or to a debt obligation of a domestic corporation if any interest on such obligation, were such interest received by the decedent at the time of his death, would be treated by reason of [subparagraph (A), (C), or (D) of section 861(a)(1)] *section 861(a)(1)(A)* as income from sources without the United States.

* * * * * * *

CHAPTER 14—SPECIAL VALUATION RULES

* * * * * * *

SEC. 2701. SPECIAL VALUATION RULES IN CASE OF TRANSFERS OF CERTAIN INTERESTS IN CORPORATIONS OR PARTNERSHIPS.

(a) VALUATION RULES.—

(1) * * *

* * * * * * *

(3) VALUATION OF RIGHTS TO WHICH PARAGRAPH APPLIES.—

(A) IN GENERAL.—The value of any right described in paragraph (1), other than a distribution right which consists of a right to receive a qualified payment, shall be treated as being zero.

(B) VALUATION OF *CERTAIN* QUALIFIED PAYMENTS.—If—

(i) any applicable retained interest confers a distribution right which consists of the right to a qualified payment, and

(ii) there are 1 or more liquidation, put, call, or conversion rights with respect to such interest, the value of all such rights shall be determined as if each liquidation, put, call, or conversion right were exercised in the manner resulting in the lowest value being determined for all such rights.

(C) VALUATION OF QUALIFIED PAYMENTS WHERE NO LIQUIDATION, ETC. RIGHTS.—In the case of an applicable retained interest which is described in subparagraph (B)(i) but not subparagraph (B)(ii), the value of the distribution right shall be determined without regard to this section.

(4) MINIMUM VALUATION OF JUNIOR EQUITY.—

(A) IN GENERAL.—In the case of a transfer described in paragraph (1) of a junior equity interest in a corporation or partnership, such interest shall in no event be valued at an amount less than the value which would be determined if the total value of all of the junior equity interests in the entity were equal to 10 percent of the sum of—

(i) the total value of all of the equity interests in such entity, plus

(ii) the total amount of indebtedness of such entity to the transferor (or an applicable family member).

(B) DEFINITIONS.—For purposes of this paragraph—

(i) JUNIOR EQUITY INTEREST.—The term "junior equity interest" means common stock or, in the case of a partnership, any partnership interest under which the rights as to income and capital *(or, to the extent*

provided in regulations, the rights as to either income or capital) are junior to the rights of all other classes of equity interests.

(ii) EQUITY INTEREST.—The term "equity interest" means stock or any interest as a partner, as the case may be.

(b) APPLICABLE RETAINED INTERESTS.—For purposes of this section—

(1) IN GENERAL.—The term "applicable retained interest" means any interest in an entity with respect to which there is—

(A) a distribution right, but only if, immediately before the transfer described in subsection (a)(1), the transferor and applicable family members hold (after application of subsection (e)(3)) control of the entity, or

(B) a liquidation, put, call, or conversion right.

(2) CONTROL.—For purposes of paragraph (1)—

(A) CORPORATIONS.—In the case of a corporation, the term "control" means the holding of at least 50 percent (by vote or value) of the stock of the corporation.

(B) PARTNERSHIPS.—In the case of a partnership, the term "control" means—

(i) the holding of at least 50 percent of the capital or profits interests in the partnership, or

(ii) in the case of a limited partnership, the holding of any interest as a general partner.

(C) APPLICABLE FAMILY MEMBER.—For purposes of this subsection, the term "applicable family member" includes any lineal descendant of any parent of the transferor or the transferor's spouse.

(c) DISTRIBUTION AND OTHER RIGHTS; QUALIFIED PAYMENTS.—For purposes of this section—

(1) DISTRIBUTION RIGHT.—

(A) IN GENERAL.—The term "distribution right" means—

(i) a right to distributions from a corporation with respect to its stock, and

(ii) a right to distributions from a partnership with respect to a partner's interest in the partnership.

(B) EXCEPTIONS.—The term "distribution right" does not include—

[(i) a right to distributions with respect to any junior equity interest (as defined in subsection (a)(4)(B)(i)),]

(i) a right to distributions with respect to any interest which is junior to the rights of the transferred interest,

(ii) any liquidation, put, call, or conversion right, or

(iii) any right to receive any guaranteed payment described in section 707(c) of a fixed amount.

* * * * * * *

(3) QUALIFIED PAYMENT.—

(A) IN GENERAL.—Except as otherwise provided in this paragraph, the term "qualified payment" means any dividend payable on a periodic basis under any cumulative preferred stock (or a comparable payment under any part-

nership interest) to the extent that such dividend (or comparable payment) is determined at a fixed rate.

(B) TREATMENT OF VARIABLE RATE PAYMENTS.—For purposes of subparagraph (A), a payment shall be treated as fixed as to rate if such payment is determined at a rate which bears a fixed relationship to a specified market interest rate.

(C) ELECTIONS.—

[(i) WAIVER OF QUALIFIED PAYMENT TREATMENT.—A transferor or applicable family member may elect with respect to payments under any interest specified in such election to treat such payments as payments which are not qualified payments.]

(i) IN GENERAL.—Payments under any interest held by a transferor which (without regard to this subparagraph) are qualified payments shall be treated as qualified payments unless the transferor elects not to treat such payments as qualified payments. Payments described in the preceding sentence which are held by an applicable family member shall be treated as qualified payments only if such member elects to treat such payments as qualified payments.

(ii) ELECTION TO HAVE INTEREST TREATED AS QUALIFIED PAYMENT.—[A transferor or any applicable family member may elect to treat any distribution right as a qualified payment, to be paid in the amounts and at the times specified in such election.] *A transferor or applicable family member holding any distribution right which (without regard to this subparagraph) is not a qualified payment may elect to treat such right as a qualified payment, to be paid in the amounts and at the times specified in such election.* The preceding sentence shall apply only to the extent that the amounts and times so specified are not inconsistent with the underlying legal instrument giving rise to such right.

(iii) ELECTIONS IRREVOCABLE.—Any election under this subparagraph with respect to an interest shall, once made, be irrevocable.

(d) TRANSFER TAX TREATMENT OF CUMULATIVE BUT UNPAID DISTRIBUTIONS.—

(1) IN GENERAL.—If a taxable event occurs with respect to any distribution right to which [subsection (a)(3)(B)] *subsection (a)(3) (B) or (C)* applied, the following shall be increased by the amount determined under paragraph (2):

* * * * * * *

(3) TAXABLE EVENTS.—For purposes of this subsection—

(A) IN GENERAL.—The term "taxable event" means any of the following:

(i) The death of the transferor if the applicable retained interest conferring the distribution right is includible in the estate of the transferor.

(ii) The transfer of such applicable retained interest.

(iii) At the election of the taxpayer, the payment of any qualified payment after the period described in paragraph (2)(C), but only with respect to [the period ending on the date of] such payment.

(B) EXCEPTION WHERE SPOUSE IS TRANSFEREE.—

(i) DEATHTIME TRANSFERS.—Subparagraph (A)(i) shall not apply to any interest includible in the gross estate of the transferor if a deduction with respect to such interest is allowable under section 2056 or 2106(a)(3).

(ii) LIFETIME TRANSFERS.—A transfer to the spouse of the transferor shall not be treated as a taxable event under subparagraph (A)(ii) if such transfer does not result in a taxable gift by reason of—

(I) any deduction allowed under section 2523, *or the exclusion under section 2503(b),* or

(II) consideration for the transfer provided by the spouse.

(iii) SPOUSE SUCCEEDS TO TREATMENT OF TRANSFEROR.—If an event is not treated as a taxable event by reason of this subparagraph, the transferee spouse or surviving spouse (as the case may be) shall be treated in the same manner as the transferor in applying this subsection with respect to the interest involved.

(4) SPECIAL RULES FOR APPLICABLE FAMILY MEMBERS.—

(A) FAMILY MEMBER TREATED IN SAME MANNER AS TRANSFEROR.—For purposes of this subsection, an applicable family member shall be treated in the same manner as the transferor with respect to any distribution right retained by such family member to which [subsection (a)(3)(B)] *subsection (a)(3) (B) or (C)* applied.

(B) TRANSFER TO APPLICABLE FAMILY MEMBER.—In the case of a taxable event described in paragraph (3)(A)(ii) involving the transfer of an applicable retained interest to an applicable family member (other than the spouse of the transferor), the applicable family member shall be treated in the same manner as the transferor in applying this subsection to distributions accumulating with respect to such interest after such taxable event.

(C) TRANSFER TO TRANSFERORS.—In the case of a taxable event described in paragraph (3)(A)(ii) involving a transfer of an applicable retained interest from an applicable family member to a transferor, this subsection shall continue to apply to the transferor during any period the transferor holds such interest.

(5) TRANSFER TO INCLUDE TERMINATION.—For purposes of this subsection, any termination of an interest shall be treated as a transfer.

(e) OTHER DEFINITIONS AND RULES.—For purposes of this section—

(1) * * *

* * * * * * *

[(3) ATTRIBUTION RULES.—

[(A) INDIRECT HOLDINGS AND TRANSFERS.—AN INDIVIDUAL]

(3) ATTRIBUTION OF INDIRECT HOLDINGS AND TRANSFERS.—An individual shall be treated as holding any interest to the extent such interest is held indirectly by such individual through a corporation, partnership, trust, or other entity. If any individual is treated as holding any interest by reason of the preceding sentence, any transfer which results in such interest being treated as no longer held by such individual shall be treated as a transfer of such interest.

[(B) CONTROL.—For purposes of subsections (b)(1), an individual shall be treated as holding any interest held by the individual's brothers, sisters, or lineal descendants.]

(4) EFFECT OF ADOPTION.—A relationship by legal adoption shall be treated as a relationship by blood.

(5) CERTAIN CHANGES TREATED AS TRANSFERS.—Except as provided in regulations, a contribution to capital or a redemption, recapitalization, or other change in the capital structure of a corporation or partnership shall be treated as a transfer of an interest in such entity to which this section applies if the taxpayer or an applicable family member—

(A) receives an applicable retained interest in such entity pursuant to [such contribution to capital or such redemption, recapitalization, or other change] *such transaction*, or

(B) under regulations, otherwise holds, immediately after [the transfer] *such transaction*, an applicable retained interest in such entity.

This paragraph shall not apply to any transaction (other than a contribution to capital) if the interests in the entity held by the transferor, applicable family members, and members of the transferor's family before and after the transaction are substantially identical.

(6) ADJUSTMENTS.—Under regulations prescribed by the Secretary, if there is any subsequent transfer, or inclusion in the gross estate, of any applicable retained interest which was valued under the rules of subsection (a), appropriate adjustments shall be made for purposes of chapter 11, 12, or 13 to reflect the increase in the amount of any prior taxable gift made by the transferor or decedent by reason of such valuation *or to reflect the application of subsection (d).*

(7) TREATMENT AS SEPARATE INTERESTS.—The Secretary may by regulation provide that any applicable retained interest shall be treated as 2 or more separate interests for purposes of this section.

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SEC. 2702. SPECIAL VALUATION RULES IN CASE OF TRANSFERS OF INTERESTS IN TRUSTS.

(a) VALUATION RULES.—

(1) * * *

* * * * * * *

(3) EXCEPTIONS.—

(A) IN GENERAL.—This subsection shall not apply to any transfer—

(i) [to the extent] *if* such transfer is an [incomplete transfer] *incomplete gift*, [or]

(ii) if such transfer involves the transfer of aninterest in trust all the property in which consists of a residence to be used as a personal residence by persons holding term interests in such trust[.], *or*

(iii) to the extent that regulations provide that such transfer is not inconsistent with the purposes of this section.

(B) [INCOMPLETE TRANSFER] *INCOMPLETE GIFT.*—For purposes of subparagraph (A), the term "[incomplete transfer] *incomplete gift*" means any transfer which would not be treated as a gift whether or not consideration was received for such transfer.

* * * * * * *

SEC. 2704. TREATMENT OF CERTAIN LAPSING RIGHTS AND RESTRICTIONS.

(a) * * *

* * * * * * *

(c) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) * * *

* * * * * * *

(3) ATTRIBUTION.—The rule of section [2701(e)(3)(A)] *2701(e)(3)* shall apply for purposes of determining the interests held by any individual.

* * * * * * *

Subtitle C—Employment Taxes

* * * * * * *

CHAPTER 21—FEDERAL INSURANCE CONTRIBUTIONS ACT

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Subchapter C—General Provisions

* * * * * * *

SEC. 3121. DEFINITIONS.

(a) WAGES.—For purposes of this chapter, the term "wages" means all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash; except that such term shall not include—

(1) * * *

* * * * * * *

(5) any payment made to, or on behalf of, an employee or his beneficiary—

(A) * * *

* * * * * * *

(F) to supplement pension benefits under a plan or trust described in any of the foregoing provisions of this paragraph to take into account some portion or all of the increase in the cost of living (as determined by the Secretary of Labor) since retirement but only if such supplemental payments are under a plan which is treated as a welfare plan under section 3(2)(B)(ii) of the Employee Retirement Income Security Act of 1974, [or]

(G) under a cafeteria plan (within the meaning of section 125) if such payment would not be treated as wages without regard to such plan and it is reasonable to believe that (if section 125 applied for purposes of this section) section 125 would not treat any wages as constructively received; *or*

(H) under an arrangement to which section 408(p) applies, other than any elective contributions under paragraph (2)(A)(i) thereof,

* * * * * * *

(b) EMPLOYMENT.—For purposes of this chapter, the term "employment" means any service, of whatever nature, performed (A) by an employee for the person employing him, irrespective of the citizenship or residence of either, (i) within the United States, or (ii) on or in connection with an American vessel or American aircraft under a contract of service which is entered into within the United States or during the performance of which and while the employee is employed on the vessel or aircraft it touches at a port in the United States, if the employee is employed on and in connection with such vessel or aircraft when outside the United States, or (B) outside the United States by a citizen or resident of the United States as an employee for an American employer (as defined in subsection (h)), or (C) if it is service, regardless of where or by whom performed, which is designated as employment or recognized as equivalent to employment under an agreement entered into under section 233 of the Social Security Act; except that such term shall not include—

(1) * * *

* * * * * * *

(20) service (other than service described in paragraph (3)(A)) performed by an individual on a boat engaged in catching fish or other forms of aquatic animal life under an arrangement with the owner or operator of such boat pursuant to which—

[(A) such individual does not receive any cash remuneration (other than as provided in subparagraph (B)),]

(A) such individual does not receive any cash remuneration other than as provided in subparagraph (B) and other than cash remuneration—

(i) which does not exceed $100 per trip;

(ii) which is contingent on a minimum catch; and

(iii) which is paid solely for additional duties (such as mate, engineer, or cook) for which additional cash remuneration is traditional in the industry,

* * * * * * *

For purposes of paragraph (20), the operating crew of a boat shall be treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals.

* * * * * * *

CHAPTER 23—FEDERAL UNEMPLOYMENT TAX ACT

* * * * * * *

SEC. 3306. DEFINITIONS.

(a) * * *

(b) WAGES.—For purposes of this chapter, the term "wages" means all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash; except that such term shall not include—

(1) * * *

* * * * * * *

(5) any payment made to, or on behalf of, an employee or his beneficiary—

(A) * * *

* * * * * * *

(F) to supplement pension benefits under a plan or trust described in any of the foregoing provisions of this paragraph to take into account some portion or all of the increase in the cost of living (as determined by the Secretary of Labor) since retirement but only if such supplemental payments are under a plan which is treated as a welfare plan under section 3(2)(B)(ii) of the Employee Retirement Income Security Act of 1974; **[**or**]**

(G) under a cafeteria plan (within the meaning of section 125) if such payment would not be treated as wages without regard to such plan and it is reasonable to believe that (if section 125 applied for purposes of this section) section 125 would not treat any wages as constructively received, *or*

(H) under an arrangement to which section 408(p) applies, other than any elective contributions under paragraph (2)(A)(i) thereof,

* * * * * * *

(c) EMPLOYMENT.—For purposes of this chapter, the term "employment" means any service performed prior to 1955, which was employment for purposes of subchapter C of chapter 9 of the Internal Revenue Code of 1939 under the law applicable to the period in which such service was performed, and (A) any service, of whatever nature, performed after 1954 by an employee for the person

employing him, irrespective of the citizenship or residence of either, (i) within the United States, or (ii) on or in connection with an American vessel or American aircraft under a contract of service which is entered into within the United States or during the performance of which and while the employee is employed on the vessel or aircraft it touches at a port in the United States, if the employee is employed on and in connection with such vessel or aircraft when outside the United States, and (B) any service, of whatever nature, performed after 1971 outside the United States (except in a contiguous country with which the United States has an agreement relating to unemployment compensation) by a citizen of the United States as an employee of an American employer (as defined in subsection (j)(3)), except—

(1) agricultural labor (as defined in subsection (k)) unless—

(A) * * *

(B) such labor is not agricultural labor performed [before January 1, 1995,] by an individual who is an alien admitted to the United States to perform agricultural labor pursuant to sections 214(c) and 101(a)(15)(H) of the Immigration and Nationality Act;

* * * * * * *

(k) AGRICULTURAL LABOR.—For purposes of this chapter, the term "agricultural labor" has the meaning assigned to such term by subsection (g) of section 3121, except that for purposes of this chapter subparagraph (B) of paragraph (4) of such subsection (g) shall be treated as reading:

"(B) in the employ of a group of operators of farms (or a cooperative organization of which such operators are members) in the performance of service described in subparagraph (A), but only if such if such operators produced more than one-half of the commodity with respect to which such service is performed;".

* * * * * * *

CHAPTER 24—COLLECTION OF INCOME TAX AT SOURCE ON WAGES

* * * * * * *

SEC. 3401. DEFINITIONS.

(a) WAGES.—For purposes of this chapter, the term "wages" means all remuneration (other than fees paid to a public official) for services performed by an employee for his employer, including the cash value of all remuneration (including benefits) paid in any medium other than cash; except that such term shall not include remuneration paid—

(1) for active service performed in a month for which such employee is entitled to the benefits of section 112 (relating to certain [combat pay] *combat zone compensation* of members of the Armed Forces of the United States) to the extent remuneration for such service is excludable from gross income under such section; or

* * * * * * *

(12) to, or on behalf of, an employee or his beneficiary—

(A) from or to a trust described in section 401(a) which is exempt from tax under section 501(a) at the time of such payment unless such payment is made to an employee of the trust as remuneration for services rendered as such employee and not as a beneficiary of the trust; or

(B) under or to an annuity plan which, at the time of such payment, is a plan described in section 403(a); or

(C) for a payment described in section 402(h)(1) and (2) if, at the time of such payment, it is reasonable to believe that the employee will be entitled to an exclusion under such section for payment; or

(D) under an arrangement to which section 408(p) applies; or

* * * * * * *

SEC. 3405. SPECIAL RULES FOR PENSIONS, ANNUITIES, AND CERTAIN OTHER DEFERRED INCOME.

(a) * * *

* * * * * * *

(e) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) * * *

* * * * * * *

(12) FAILURE TO PROVIDE CORRECT TIN.—If—

(A) a payee fails to furnish his TIN to the payor in the manner required by the Secretary, or

(B) the Secretary notifies the payor before any payment or distribution that the TIN furnished by the payee is incorrect, no election under subsection (a)(2) or [(b)(3)] *(b)(2)* shall be treated as in effect and subsection (a)(4) shall not apply to such payee.

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Subtitle D—Miscellaneous Excise Taxes

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CHAPTER 31—RETAIL EXCISE TAXES

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Subchapter A—Luxury Passenger Automobiles

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SEC. 4001. IMPOSITION OF TAX.

(a) * * *

* * * * * * *

[(e) INFLATION ADJUSTMENT.—

[(1) IN GENERAL.—If, for any calendar year, the excess (if any) of—

[(A) $30,000, increased by the cost-of-living adjustment for the calendar year, over

[(B) the dollar amount in effect under subsection (a) for the calendar year,

is equal to or greater than $2,000, then the $30,000 amount in subsection (a) and section 4003(a) (as previously adjusted under this subsection) for any subsequent calendar year shall be increased by the amount of such excess rounded to the next lowest multiple of $2,000.

[(2) COST-OF-LIVING ADJUSTMENT.—For purposes of paragraph (1), the cost-of-living adjustment for any calendar year shall be the cost-of-living adjustment under section 1(f)(3) for such calendar year, determined by substituting "calendar year 1990" for "calendar year 1992" in subparagraph (B) thereof.]

(e) INFLATION ADJUSTMENT.—

(1) IN GENERAL.—The $30,000 amount in subsection (a) and section 4003(a) shall be increased by an amount equal to—

(A) $30,000, multiplied by

(B) the cost-of-living adjustment under section 1(f)(3) for the calendar year in which the vehicle is sold, determined by substituting "calendar year 1990" for "calendar year 1992" in subparagraph (B) thereof.

(2) ROUNDING.—If any amount as adjusted under paragraph (1) is not a multiple of $2,000, such amount shall be rounded to the next lowest multiple of $2,000.

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CHAPTER 36—FACILITIES AND SERVICES

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Subchapter A—Harbor Maintenance Tax

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SEC. 4462. DEFINITIONS AND SPECIAL RULES.

(a) * * *

(b) SPECIAL RULE FOR ALASKA, HAWAII, AND POSSESSIONS.—

(1) IN GENERAL.—No tax shall be imposed under section 4461(a) with respect to—

(A) * * *

* * * * * * *

(D) cargo loaded on a vessel in Alaska, Hawaii, or a possession of the United States and unloaded in the State or possession in which loaded, *or passengers transported on United States flag vessels operating solely within the State waters of Alaska or Hawaii and adjacent international waters.*

* * * * * * *

Subchapter B—Transportation by Water

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Sec. 4472. Definitions [and special rules].

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CHAPTER 43—QUALIFIED PENSION, ETC., PLANS

* * * * * * *

[Sec. 4978B. Tax on disposition of employer securities to which section 133 applied.]

* * * * * * *

SEC. 4972. TAX ON NONDEDUCTIBLE CONTRIBUTIONS TO QUALIFIED EMPLOYER PLANS.

(a) * * *

* * * * * * *

(d) DEFINITIONS.—For purposes of this section—

(1) QUALIFIED EMPLOYER PLAN.—

(A) IN GENERAL.—The term "qualified employer plan" means—

(i) any plan meeting the requirements of section 401(a) which includes a trust exempt from tax under section 501(a),

(ii) an annuity plan described in section 403(a), [and]

(iii) any simplified employee pension (within the meaning of section 408(k))[.], *and*

(iv) any simple retirement account (within the meaning of section 408(p)).

* * * * * * *

SEC. 4973. TAX ON EXCESS CONTRIBUTIONS TO INDIVIDUAL RETIREMENT ACCOUNTS, CERTAIN SECTION 403(B) CONTRACTS, AND CERTAIN INDIVIDUAL RETIREMENT ANNUITIES.

(a) * * *

(b) EXCESS CONTRIBUTIONS.—For purposes of this section, in the case of individual retirement accounts or individual retirement annuities, the term "excess contributions" means the sum of—

(1) the excess (if any) of—

(A) the amount contributed for the taxable year to the accounts or for the annuities (other than a rollover contribution described in [sections 402(c)] *section 402(c)*, 403(a)(4), 403(b)(8), or 408(d)(3)), over

* * * * * * *

SEC. 4975. TAX ON PROHIBITED TRANSACTIONS.

(a) INITIAL TAXES ON DISQUALIFIED PERSON.—There is hereby imposed a tax on each prohibited transaction. The rate of tax shall be equal to [5] *10* percent of the amount involved with respect to the prohibited transaction for each year (or part thereof) in the taxable period. The tax imposed by this subsection shall be paid by

any disqualified person who participates in the prohibited transaction (other than a fiduciary acting only as such).

* * * * * * *

(d) EXEMPTIONS.—The prohibitions provided in subsection (c) shall not apply to—

(1) * * *

* * * * * * *

(13) any transaction which is exempt from section 406 of such Act by reason of section 408(e) of such Act (or which would be so exempt if such section 406 applied to such transaction) or which is exempt from section 406 of such Act by reason of section [408(b)] *408(b)(12)* of such Act;

* * * * * * *

SEC. 4977. TAX ON CERTAIN FRINGE BENEFITS PROVIDED BY AN EMPLOYER.

(a) * * *

* * * * * * *

(c) EFFECT OF ELECTION ON SECTION 132(a).—If—

(1) an election under this section is in effect with respect to an employer for any calendar year, and

(2) at all times on or after January 1, 1984, and before the close of the calendar year involved, substantially all of the employees of the employer were entitled to employee discounts on goods or services provided by the employer in 1 line of business,

for purposes of paragraphs (1) and (2) of section 132(a) (but not for purposes of [section 132(i)(2)] *section 132(h)*), all employees of any line of business of the employer which was in existence on January 1, 1984, shall be treated as employees of the line of business referred to in paragraph (2).

* * * * * * *

SEC. 4978. TAX ON CERTAIN DISPOSITIONS BY EMPLOYEE STOCK OWNERSHIP PLANS AND CERTAIN COOPERATIVES.

(a) * * *

(b) AMOUNT OF TAX.—

(1) * * *

(2) LIMITATION.—The amount realized taken into account under paragraph (1) shall not exceed that portion allocable to qualified securities acquired in the sale to which section 1042 applied determined as if such securities were disposed of—

[(A) first, from section 133 securities (as defined in section 4978B(e)(2)) acquired during the 3-year period ending on the date of such disposition, beginning with the securities first so acquired.

[(B) second, from section 133 securities (as so defined) acquired before such 3-year period unless such securities (or proceeds from the disposition) have been allocated to accounts of participants or beneficiaries."

[(C) third, from qualified securities to which section 1042 applied acquired during the 3-year period ending on

the date of the disposition, beginning with the securities first so acquired, and

[(D) then from any other employer securities.

[If subsection (d) or section 4978B(d) applies to a disposition, the disposition shall be treated as made from employer securities in the opposite order of the preceding sentence.]

(A) first from qualified securities to which section 1042 applied acquired during the 3-year period ending on the date of the disposition, beginning with the securities first so acquired, and

(B) then from any other employer securities.

If subsection (d) applies to a disposition, the disposition shall be treated as made from employer securities in the opposite order of the preceding sentence.

* * * * * * *

[SEC. 4978B. TAX ON DISPOSITION OF EMPLOYER SECURITIES TO WHICH SECTION 133 APPLIED.

[(a) IMPOSITION OF TAX.—In the case of an employee stockownership plan which has acquired section 133 securities, there is hereby imposed a tax on each taxable event in an amount equal to the amount determined under subsection (b).

[(b) AMOUNT OF TAX.—

[(1) IN GENERAL.—The amount of the tax imposed by subsection (a) shall be equal to 10 percent of the amount realized on the disposition to the extent allocable to section 133 securities under section 4978(b)(2).

[(2) DISPOSITIONS OTHER THAN SALES OR EXCHANGES.—For purposes of paragraph (1), in the case of a disposition of employer securities which is not a sale or exchange, the amount realized on such disposition shall be the fair market value of such securities at the time of disposition.

[(c) TAXABLE EVENT.—For purposes of this section, the term "taxable event" means any of the following dispositions:

[(1) DISPOSITIONS WITHIN 3 YEARS.—Any disposition of any employer securities by an employee stock ownership plan within 3 years after such plan acquired section 133 securities if—

[(A) the total number of employer securities held by such plan after such disposition is less than the total number of employer securities held after such acquisition, or

[(B) except to the extent provided in regulations, the value of employer securities held by such plan after the disposition is 50 percent or less of the total value of all employer securities as of the time of the disposition.

For purposes of subparagraph (B), the aggregation rule of section 133(b)(6)(D) shall apply.

[(2) STOCK DISPOSED OF BEFORE ALLOCATION.—Any disposition of section 133 securities to which paragraph (1) does not apply if—

[(A) such disposition occurs before such securities are allocated to accounts of participants or their beneficiaries, and

[(B) the proceeds from such disposition are not so allocated.

[(d) SECTION NOT TO APPLY TO CERTAIN DISPOSITIONS.—

[(1) IN GENERAL.—This section shall not apply to any disposition described in paragraph (1), (3), or (4) of section 4978(d).

[(2) CERTAIN REORGANIZATIONS.—For purposes of this section, any exchange of section 133 securities for employer securities of another corporation in any reorganization described in section 368(a)(1) shall not be treated as a disposition, but the employer securities received shall be treated as section 133 securities and as having been held by the plan during the period the securities which were exchanged were held.

[(3) FORCED DISPOSITION OCCURRING BY OPERATION OF STATE LAW.—Any forced disposition of section 133 securities by an employee stock ownership plan occurring by operation of a State law shall not be treated as a disposition. This paragraph shall only apply to securities which, at the time the securities were acquired by the plan, were regularly traded on an established securities market.

[(4) COORDINATION WITH OTHER TAXES.—This section shall not apply to any disposition which is subject to tax under section 4978 or section 4978A (as in effect on the day before the date of enactment of this section).

[(e) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

[(1) LIABILITY FOR PAYMENT OF TAXES.—The tax imposed by this section shall be paid by the employer.

[(2) SECTION 133 SECURITIES.—The term "section 133 securities" means employer securities acquired by an employee stock ownership plan in a transaction to which section 133 applied.

[(3) DISPOSITION.—The term "disposition" includes any distribution.

[(4) ORDERING RULES.—For ordering rules for dispositions of employer securities, see section 4978(b)(2).]

* * * * * * *

SEC. 4980A. TAX ON EXCESS DISTRIBUTIONS FROM QUALIFIED RETIREMENT PLANS.

(a) * * *

* * * * * * *

(c) EXCESS DISTRIBUTIONS.—For purposes of this section—

(1) * * *

* * * * * * *

[(4) SPECIAL RULE WHERE TAXPAYER ELECTS INCOME AVERAGING.—]

(4) SPECIAL ONE-TIME ELECTION.—If the retirement distributions with respect to any individual during any calendar year include a lump sum distribution [to which an election under section 402(d)(4)(B) applies] *(as defined in section 402(e)(4)(D)) with respect to which the individual elects to have this paragraph apply*—

(A) paragraph (1) shall be applied separately with respect to such lump sum distribution and other retirement distributions, and

(B) the limitation under paragraph (1) with respect to such lump sum distribution shall be equal to 5 times the amount of such limitation determined without regard to this subparagraph.

An individual may elect to have this paragraph apply to only one lump-sum distribution.

* * * * * * *

(g) LIMITATION ON APPLICATION.—This section shall not apply to distributions during years beginning after December 31, 1995, and before January 1, 1999, and such distributions shall be treated as made first from amounts not described in subsection (f).

SEC. 4980B. FAILURE TO SATISFY CONTINUATION COVERAGE REQUIREMENTS OF GROUP HEALTH PLANS.

(a) * * *

* * * * * * *

(f) CONTINUATION COVERAGE REQUIREMENTS OF GROUP HEALTH PLANS.—

(1) * * *

(2) CONTINUATION COVERAGE.—For purposes of paragraph (1), the term "continuation coverage" means coverage under the plan which meets the following requirements:

(A) * * *

(B) PERIOD OF COVERAGE.—The coverage must extend for at least the period beginning on the date of the qualifying event and ending not earlier than the earliest of the following:

(i) MAXIMUM REQUIRED PERIOD.—

(I) * * *

* * * * * * *

[(V) QUALIFYING EVENT INVOLVING MEDICARE ENTITLEMENT.—In the case of an event described in paragraph (3)(D) (without regard to whether such event is a qualifying event), the period of coverage for qualified beneficiaries other than the covered employee for such event or any subsequent qualifying event shall not terminate before the close of the 36-month period beginning on the date the covered employee becomes entitled to benefits under title XVIII of the Social Security Act.]

(V) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in paragraph (3)(B) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this clause before the close of the 36-month period beginning on the date the covered employee became so entitled.

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Subtitle E—Alcohol, Tobacco, and Certain Other Excise Taxes

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CHAPTER 51—DISTILLED SPIRITS, WINES, AND BEER

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PART I—GALLONAGE TAXES

* * * * * * *

Subpart C—Wines

* * * * * * *

SEC. 5041. IMPOSITION AND RATE OF TAX.

(a) * * *

* * * * * * *

(c) CREDIT FOR SMALL DOMESTIC PRODUCERS.—

(1) * * *

* * * * * * *

[(6) REGULATIONS.—The Secretary may prescribe such regulations as may be necessary to prevent the credit provided in this subsection from benefiting any person who produces more than 250,000 wine gallons of wine during a calendar year and to assure proper reduction of such credit for persons producing more than 150,000 wine gallons of wine during a calendar year.]

(6) CREDIT FOR TRANSFEREE IN BOND.—If—

(A) wine produced by any person would be eligible for any credit under paragraph (1) if removed by such person during the calendar year,

(B) wine produced by such person is removed during such calendar year by any other person (hereafter in this paragraph referred to as the "transferee") to whom such wine was transferred in bond and who is liable for the tax imposed by this section with respect to such wine, and

(C) such producer holds title to such wine at the time of its removal and provides to the transferee such information as is necessary to properly determine the transferee's credit under this paragraph,

then, the transferee (and not the producer) shall be allowed the credit under paragraph (1) which would be allowed to the producer if the wine removed by the transferee had been removed by the producer on that date.

(7) REGULATIONS.—The Secretary may prescribe such regulations as may be necessary to carry out the purposes of this subsection, including regulations—

(A) to prevent the credit provided in this subsection from benefiting any person who produces more than 250,000 wine gallons during a calendar year, and

(B) to assure proper reduction of such credit for persons producing more than 150,000 wine gallons of wine during a calendar year.

* * * * * * *

Subpart E—General Provisions

* * * * * * *

SEC. 5061. METHOD OF COLLECTING TAX.

(a) * * *

(b) EXCEPTIONS.—Notwithstanding the provisions of subsection (a), any taxes imposed on, or amounts to be paid or collected in respect of, distilled spirits, wines, and beer under—

(1) * * *

* * * * * * *

[(3) section 5041(e),]

(3) section 5041(f),

* * * * * * *

PART II—OCCUPATIONAL TAX

* * * * * * *

Subpart F—Nonbeverage Domestic Drawback Claimants

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SEC. 5134. DRAWBACK.

(a) * * *

* * * * * * *

(c) ALLOWANCE OF DRAWBACK EVEN WHERE CERTAIN REQUIREMENTS NOT MET.—

(1) * * *

* * * * * * *

(3) PENALTY TREATED AS TAX.—The penalty imposed by paragraph (2) shall be assessed, collected, and paid in the same manner as taxes, as provided in section [6662(a)] *6665(a).*

* * * * * * *

Subchapter C—Operation of Distalled Spirits Plants

* * * * * * *

PART I—GENERAL PROVISIONS

* * * * * * *

SEC. 5206. CONTAINERS.

(a) * * *

* * * * * * *

(f) CROSS REFERENCES.—

(1) * * *

(2) For provisions relating to labeling containers of distilled spirits of one gallon or less for nonindustrial uses, see section [5(e)] *105(e)* of the Federal Alcohol Administration Act (27 U.S.C. 205(e)).

* * * * * * *

Subchapter F—Bonded and Taxpaid Wine Premises

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SEC. 5354. BOND.

The bond for a bonded wine cellar shall be in such form, on such conditions, and with such adequate surety, as regulations issued by the Secretary shall prescribe, and shall be in a penal sum not less than the tax on any wine or distilled spirits possessed or in transit at any one time *(taking into account the appropriate amount of credit with respect to such wine under section 5041(c))*, but not less than $1,000 nor more than $50,000; except that where the tax on such wine and on such distilled spirits exceeds $250,000, the penal sum of the bond shall be not more than $100,000. Where additional liability arises as a result of deferral of payment of tax payable on any return, the Secretary may require the proprietor to file a supplemental bond in such amount as may be necessary to protect the revenue. The liability of any person on any such bond shall apply whether the transaction or operation on which the liability of the proprietor is based occurred on or off the proprietor's premises.

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Subtitle F—Procedure and Administration

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CHAPTER 61—INFORMATION AND RETURNS

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Subchapter A—Returns and records

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PART III—INFORMATION RETURNS

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Subpart A—Information Concerning Persons Subject to Special Provisions

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SEC. 6033. RETURNS BY EXEMPT ORGANIZATIONS.

(a) * * *

* * * * * * *

(e) SPECIAL RULES RELATING TO LOBBYING ACTIVITIES.—

(1) REPORTING REQUIREMENTS.—

(A) * * *

(B) ORGANIZATIONS TO WHICH SUBSECTION APPLIES.—

(i) IN GENERAL.—This subsection shall apply to any organization which is exempt from taxation under [this subtitle] *section 501* other than an organization described in section 501(c)(3).

* * * * * * *

(iii) COORDINATION WITH SECTION 527(f).—This subsection shall not apply to any amount on which tax is imposed by reason of section 527(f).

* * * * * * *

SEC. 6037. RETURN OF S CORPORATION.

(a) * * *

* * * * * * *

(c) SHAREHOLDER'S RETURN MUST BE CONSISTENT WITH CORPORATE RETURN OR SECRETARY NOTIFIED OF INCONSISTENCY.—

(1) IN GENERAL.—A shareholder of an S corporation shall, on such shareholder's return, treat a subchapter S item in a manner which is consistent with the treatment of such item on the corporate return.

(2) NOTIFICATION OF INCONSISTENT TREATMENT.—

(A) IN GENERAL.—In the case of any subchapter S item, if—

(i)(I) the corporation has filed a return but the shareholder's treatment on his return is (or may be) inconsistent with the treatment of the item on the corporate return, or

(II) the corporation has not filed a return, and

(ii) the shareholder files with the Secretary a statement identifying the inconsistency,

paragraph (1) shall not apply to such item.

(B) SHAREHOLDER RECEIVING INCORRECT INFORMATION.—A shareholder shall be treated as having complied with clause (ii) of subparagraph (A) with respect to a subchapter S item if the shareholder—

(i) demonstrates to the satisfaction of the Secretary that the treatment of the subchapter S item on the shareholder's return is consistent with the treatment of the item on the schedule furnished to the shareholder by the corporation, and

(ii) elects to have this paragraph apply with respect to that item.

(3) EFFECT OF FAILURE TO NOTIFY.—In any case—

(A) described in subparagraph (A)(i)(I) of paragraph (2), and

(B) in which the shareholder does not comply with subparagraph (A)(ii) of paragraph (2),

any adjustment required to make the treatment of the items by such shareholder consistent with the treatment of the items on the corporate return shall be treated as arising out of mathematical or clerical errors and assessed according to section 6213(b)(1). Paragraph (2) of section 6213(b) shall not apply to any assessment referred to in the preceding sentence.

(4) SUBCHAPTER S ITEM.—For purposes of this subsection, the term "subchapter S item" means any item of an S corporation to the extent that regulations prescribed by the Secretary provide that, for purposes of this subtitle, such item is more appropriately determined at the corporation level than at the shareholder level.

(5) ADDITION TO TAX FOR FAILURE TO COMPLY WITH SECTION.—

For addition to tax in the case of a shareholder's negligence in connection with, or disregard of, the requirements of this section, see part II of subchapter A of chapter 68.

SEC. 6038. INFORMATION WITH RESPECT TO CERTAIN FOREIGN CORPORATIONS.

(a) REQUIREMENT.—

(1) IN GENERAL.—Every United States person shall furnish, with respect to any foreign corporation which such person controls (within the meaning of subsection (e)(1)), such information as the Secretary may prescribe by regulations relating to—

(A) * * *

* * * * * * *

(E) a description of the varoius classes of stock outstanding, and a list showing the name and address of, and number of shares held by, each United States person who is a shareholder of record owning at any time during the annual accounting period 5 percent or more in value of any class of stock outstanding of such foreign corporation[, and].

[(F) such information as the Secretary may require for purposes of carrying out the provisions of section 453C.]

* * * * * * *

[(e)] *(f)* CROSS REFERENCES.—

(1) For provisions relating to penalties for violations of this section, see section 7203.

(2) For definition of the term "United States person", see section 7701(a)(30).

* * * * * * *

SEC. 6038A. INFORMATION WITH RESPECT TO CERTAIN FOREIGN-OWNED CORPORATIONS.

(a) * * *

(b) REQUIRED INFORMATION.—For purposes of subsection (a), the information described in this subsection is such information as the Secretary may prescribe by regulations relating to—

(1) * * *

* * * * * * *

(2) the manner in which the reporting corporation is related to each person referred to in paragraph (1), *and*

(3) transactions between the reporting corporation and each foreign person which is a related party to the reporting corporation[, and].

[(4) such information as the Secretary may require for purposes of carrying out the provisions of section 453C.]

* * * * * * *

(e) ENFORCEMENT OF REQUESTS FOR CERTAIN RECORDS.—

(1) * * *

* * * * * * *

(4) JUDICIAL PROCEEDINGS.—

(A) * * *

* * * * * * *

(D) SUSPENSION OF STATUTE OF LIMITATIONS.—If the reporting corporation brings an action under subparagraph (A) or (B), the running of any period of limitations under section 6501 (relating to assessment and collection of tax) or under section 6531 (relating to criminal prosecutions) with respect to [any transaction to which the summons relates] *any affected taxable year* shall be suspended for the period during which such proceeding, and appeals therein are pending. In no event shall any such period expire before the 90th day after the day on which there is a final determination in such proceeding. *For purposes of this subparagraph, the term "affected taxable year" means any taxable year if the determination of the amount of tax imposed for such taxable year is affected by the treatment of the transaction to which the summons relates.*

* * * * * * *

Subpart B—Information Concerning Tranactions With Other Persons

Sec. 6041. Information at source.

* * * * * * *

Sec. 6043. Liquidating[;], etc., transactions.

* * * * * * *

Sec. 6050Q. Returns relating to certain purchases of fish.

* * * * * * *

SEC. 6043. LIQUIDATING[;], ETC., TRANSACTIONS.

(a) * * *

* * * * * * *

SEC. 6045. RETURNS OF BROKERS.

(a) * * *

(e) RETURN REQUIRED IN THE CASE OF REAL ESTATE TRANSACTIONS.—

(1) * * *

* * * * * * *

(3) PROHIBITION OF SEPARATE CHARGE FOR FILING RETURN.—It shall be unlawful for any real estate reporting person to separately charge any customer for complying with any requirement of paragraph (1). *Nothing in this paragraph shall be construed to prohibit the real estate reporting person from taking into account its cost of complying with such requirement in establishing its charge (other than a separate charge for complying with such requirement) to any customer for performing services in the case of a real estate transaction.*

* * * * * * *

SEC. 6047. INFORMATION RELATING TO CERTAIN TRUSTS AND ANNUITY PLANS.

(a) * * *

* * * * * * *

(d) REPORTS BY EMPLOYERS, PLAN ADMINISTRATORS, ETC.—

(1) IN GENERAL.—The Secretary shall by forms or regulations require that—

(A) the employer maintaining, or the plan administrator (within the meaning of section 414(g)) of, a plan from which designated distributions (as defined in section 3405(e)(1)) may be made, and

(B) any person issuing any contract under which designated distributions (as so defined) may be made,

make returns and reports regarding such plan (or contract) to the Secretary, to the participants and beneficiaries of such plan (or contract), and to such other persons as the Secretary may by regulations prescribe. *No return or report may be required under the preceding sentence with respect to distributions to any person during any year unless such distributions aggregate $10 or more.*

* * * * * * *

(e) EMPLOYEE STOCK OWNERSHIP PLANS.—The Secretary shall require—

[(1) any employer maintaining, or the plan administrator (within the meaning of section 414(g)) of, an employee stock ownership plan—

[(A) which acquired stock in a transaction to which section 133 applies, or

[(B) which holds stock with respect to which section 404(k) applies to dividends paid on such stock,

[(2) any person making or holding a loan to which section 133 applies, or

[(3) both such employer or plan administrator and such person,]

(1) any employer maintaining, or the plan administrator (within the meaning of section 414(g)) of, an employee stock ownership plan which holds stock with respect to which section 404(k) applies to dividends paid on such stock, or

(2) both such employer or plan administrator,

make returns and reports regarding such plan, transaction, or ıan to the Secretary and to such other persons as the Secretary ıy prescribe. Such returns and reports shall be made in such

form, shall be made at such time, and shall contain such information as the Secretary may prescribe.

(f) CROSS REFERENCES.—

[(1) For provisions relating to penalties for failure to file a return required by this section, see section 6652(e).]

(1) For provisions relating to penalties for failures to file returns and reports required under this section, see sections 6652(e), 6721, and 6722.

(2) For criminal penalty for furnishing fraudulent information, see section 7207.

(3) For provisions relating to penalty for failure to comply with the provisions of subsection (d), see section 6704.

* * * * * * *

SEC. 6050A. REPORTING REQUIREMENTS OF CERTAIN FISHING BOAT OPERATORS.

(a) REPORTS.—The operator of a boat on which one or more individuals, during a calendar year, perform services described in section 3121(b)(20) shall submit to the Secretary (at such time, and in such manner and form, as the Secretary shall by regulations prescribe) information respecting—

(1) * * *

* * * * * * *

(3) if such individual receives his share in kind, the type and weight of such share, together with such other information as the Secretary may prescribe by regulations reasonably necessary to determine the value of such share; **[**and**]**

(4) if such individual receives a share of the proceeds of such catches, the amount so received**[**.**]**; *and*

(5) any cash remuneration described in section 3121(b)(20)(A).

* * * * * * *

SEC. 6050B. RETURNS RELATING TO UNEMPLOYMENT COMPENSATION.

(a) * * *

* * * * * * *

(c) DEFINITIONS.—For purposes of this section—

(1) UNEMPLOYMENT COMPENSATION.—The term "unemployment compensation" has the meaning given to such term by section **[**85(c)**]** *85(b).*

(2) PERSON.——The term "person" means the officer or employee having control of the payment of the unemployment compensation, or the person appropriately designated for purposes of this section.

* * * * * * *

SEC. 6050Q. RETURNS RELATING TO CERTAIN PURCHASES OF FISH.

(a) REQUIREMENT OF REPORTING.—Every person—

(1) who is engaged in the trade or business of purchasing fish for resale from any person engaged in the trade or business of catching fish; and

(2) who makes payments in cash in the course of such trade or business to such a person of $600 or more during any calendar year for the purchase of fish,

shall make a return (at such times as the Secretary may prescribe) described in subsection (b) with respect to each person to whom such a payment was made during such calendar year.

(b) RETURN.—A return is described in this subsection if such return—

(1) is in such form as the Secretary may prescribe, and

(2) contains—

(A) the name, address, and TIN of each person to whom a payment described in subsection (a)(2) was made during the calendar year;

(B) the aggregate amount of such payments made to such person during such calendar year and the date and amount of each such payment, and

(C) such other information as the Secretary may require.

(c) STATEMENT TO BE FURNISHED WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

(1) the name and address of the person required to make such a return, and

(2) the aggregate amount of payments to the person required to be shown on the return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) is required to be made.

(d) DEFINITIONS.—For purposes of this section:

(1) CASH.—The term "cash" has the meaning given such term by section 6050I(d).

(2) FISH.—The term "fish" includes other forms of aquatic life.

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Subchapter B—Miscellaneous Provisions

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SEC. 6103. CONFIDENTIALITY AND DISCLOSURE OF RETURNS AND RETURN INFORMATION.

(a) * * *

* * * * * * *

(e) DISCLOSURE TO PERSONS HAVING MATERIAL INTEREST.—

(1) IN GENERAL.—The return of a person shall, upon written request, be open to inspection by or disclosure to—

(A) in the case of the return of an individual—

(i) * * *

* * * * * * *

(iv) the child of that individual (or such child's legal representative) to the extent necessary to comply with the provisions of [section 1(i) or 59(j);] *section 1(g) or 59(j);*

* * * * * * *

SEC. 6109. IDENTIFYING NUMBERS.

(a) * * *

* * * * * * *

[(f)] *(g)* ACCESS TO EMPLOYER IDENTIFICATION NUMBERS BY FEDERAL CROP INSURANCE CORPORATION FOR PURPOSES OF THE FEDERAL CROP INSURANCE ACT.—

(1) * * *

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CHAPTER 62—TIME AND PLACE FOR PAYING TAX

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Subchapter B—Extensions of Time for Payment

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SEC. 6166. EXTENSION OF TIME FOR PAYMENT OF ESTATE TAX WHERE ESTATE CONSISTS LARGELY OF INTEREST IN CLOSELY HELD BUSINESS.

(a) * * *

* * * * * * *

(k) CROSS REFERENCES.—

(1) * * *

* * * * * * *

[(6) Payment of estate tax by employee stock ownership plan or eligible worker-owned cooperative.—For provision allowing plan administrator or eligible worker-owned cooperative to elect to pay a certain portion of the estate tax in installments under the provisions of this section, see section 2210(c).]

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CHAPTER 63—ASSESSMENT

SUBCHAPTER A. In general.

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[SUBCHAPTER D. Tax Treatment of subchapter S items.]

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Subchapter B—Deficiency Procedures in the Case of Income, Estate, Gift, and Certain Excise Taxes

* * * * * * *

SEC. 6214. DETERMINATIONS BY TAX COURT.

(a) * * *

* * * * * * *

[(e) CROSS REFERENCES.—

[(1) For provision giving Tax Court jurisdiction to determine whether any portion of deficiency is a substantial underpayment attributable to tax motivated transactions, see section 6621(c)(4).

[(2) For provision giving Tax Court jurisdiction to order a refund of an overpayment and to award sanctions, see section 6512(b)(2).]

(e) CROSS REFERENCE.—

For provision giving Tax Court jurisdiction to order a refund of an overpayment and to award sanctions, see section 6512(b)(2).

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Subchapter C—Tax Treatment of Partnership Items

* * * * * * *

SEC. 6233. EXTENSION TO ENTITIES FILING PARTNERSHIP RETURNS, ETC.

(a) * * *

[(b) SIMILAR RULES IN CERTAIN CASES.—If for any taxable year——

[(1) an entity files a return as an S corporation but it is determined that the entity was not an S corporation for such year, or

[(2) a partnership return or S corporation return is filed but it is determined that there is no entity for such taxable year, then, to the extent provided in regulations, rules similar to the rules of subsection (a) shall apply.]

(b) SIMILAR RULES IN CERTAIN CASES.—If a partnership return is filed for any taxable year but it is determined that there is no entity for such taxable year, to the extent provided in regulations, rules similar to the rules of subsection (a) shall apply.

* * * * * * *

[Subchapter D—Tax Treatment of Subchapter S Items

[SEC. 6241. TAX TREATMENT DETERMINED AT CORPORATE LEVEL.

[Except as otherwise provided in regulations prescribed by the Secretary, the tax treatment of any subchapter S item shall be determined at the corporate level.

[SEC. 6242. SHAREHOLDER'S RETURN MUST BE CONSISTENT WITH CORPORATE RETURN OR SECRETARY NOTIFIED OF INCONSISTENCY.

[A shareholder of an S corporation shall, on such shareholder's return, treat a subchapter S item in a manner which is consistent with the treatment of such item on the corporate return unless the shareholder notifies the Secretary (at the time and in the manner prescribed by regulations) of the inconsistency.

[SEC. 6243. ALL SHAREHOLDERS TO BE NOTIFIED OF PROCEEDINGS AND GIVEN OPPORTUNITY TO PARTICIPATE.

[In the manner and at the time prescribed in regulations, each shareholder in a corporation shall be given notice of, and the right to participate in, any administrative or judicial proceeding for the determination at the corporate level of any subchapter S item.

[SEC. 6244. CERTAIN PARTNERSHIP PROVISIONS MADE APPLICABLE.

[The provisions of—

[(1) subchapter C which relate to—

[(A) assessing deficiencies, and filing claims for credit or refund, with respect to partnership items, and

[(B) judicial determination of partnership items, and

[(2) so much of the other provisions of this subtitle as relate to partnership items,

are (except to the extent modified or made inapplicable in regulations) hereby extended to and made applicable to subchapter S items.

[SEC. 6245. SUBCHAPTER S ITEM DEFINED.

[For purposes of this subchapter, the term "subchapter S item" means any item of an S corporation to the extent regulations prescribed by the Secretary provide that, for purposes of this subtitle, such item is more appropriately determined at the corporate level than at the shareholder level.]

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CHAPTER 64—COLLECTION

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Subchapter A—General Provisions

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SEC. 6302. MODE OR TIME OF COLLECTION.

(a) * * *

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(g) DEPOSITS OF SOCIAL SECURITY TAXES AND WITHHELD INCOME TAXES.—If, under regulations prescribed by the Secretary, a person is required to make deposits of taxes imposed by chapters 21, *22,* and 24 on the basis of eight-month periods, such person shall make deposits of such taxes on the 1st banking day after any day on which such person has $100,000 or more of such taxes for deposit.

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CHAPTER 65—ABATEMENTS, CREDITS, AND REFUNDS

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Subchapter B—Rules of Special Application

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SEC. 6416. CERTAIN TAXES ON SALES AND SERVICES.

(a) * * *

(b) SPECIAL CASES IN WHICH TAX PAYMENTS CONSIDERED OVERPAYMENTS.—Under regulations prescribed by the Secretary, credit or refund (without interest) shall be allowed or made in respect of the overpayments determined under the following paragraphs:

(1) PRICE READJUSTMENTS.—

(A) IN GENERAL.—Except as provided in subparagraph (B) or (C), if the price of any article in respect of which a tax, based on such price, is imposed by [chapter 32 or by section 4051] *chapter 31 or 32*, is readjusted by reason of the return or repossession of the article or a covering or container, or by a bona fide discount, rebate, or allowance, including a readjustment for local advertising (but only to the extent provided in section 4216(e)(2) and (3)), the part of the tax proportionate to the part of the price repaid or credited to the purchaser shall be deemed to be an overpayment.

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SEC. 6427. FUELS NOT USED FOR TAXABLE PURPOSES.

(a) * * *

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[(g) ADVANCE REPAYMENT OF INCREASED DIESEL FUEL TAX TO ORIGINAL PURCHASERS OF DIESEL.—Upowered Automobiles and Light Trucks.—

[(1) IN GENERAL.—Except as provided in subsection (k), the Secretary shall pay (without interest) to the original purchaser of any qualified diesel-powered highway vehicle an amount equal to the diesel fuel differential amount.

[(2) QUALIFIED DIESEL-POWERED HIGHWAY VEHICLE.—For purposes of this subsection, the term "qualified diesel-powered highway vehicle" means any diesel-powered highway vehicle which—

[(A) has at least 4 wheels,

[(B) has a gross vehicle weight rating of 10,000 pounds or less, and

[(C) is registered for highway use in the United States under the laws of any State.

[(3) DIESEL FUEL DIFFERENTIAL AMOUNT.—For purposes of this subsection, the term "diesel fuel differential amount" means—

[(A) except as provided in subparagraph (B), $102, or

[(B) in the case of a truck or van, $198.

[(4) Original purchaser.—For purposes of this subsection—

[(A) IN GENERAL.— Except as provided in subparagraph (B), the term "original purchaser" means the first person to purchase the qualified diesel-powered vehicle for use other than resale.

[(B) EXCEPTION FOR CERTAIN PERSONS NOT SUBJECT TO FUELS TAX.—The term "original purchaser" shall not include any State or local government (as defined in section 4221(d)(4)) or any nonprofit educational organization (as defined in section 4221(d)(5)).

[(C) TREATMENT OF DEMONSTRATION USE BY DEALER.—For purposes of subparagraph (A), use as a demonstrator by a dealer shall not be taken into account.

[(5) VEHICLES TO WHICH SUBSECTION APPLIES.—Except as provided in paragraph (6), this subsection shall only apply to qualified diesel-powered highway vehicles originally purchased after January 1, 1985, and before January 1, 1999.

[(6) SPECIAL RULE FOR CERTAIN VEHICLES HELD ON JANUARY 1, 1985.—

[(A) IN GENERAL.—In the case of any person holding a qualified diesel-powered highway vehicle on January 1, 1985—

[(i) such person shall be treated as if he originally purchased such vehicle on December 31, 1984, but

[(ii) the amount payable under paragraph (1) to such person for such vehicle shall be the applicable fraction of the diesel fuel differential amount.

[(B) APPLICABLE FRACTION.—For purposes of subparagraph (A), the applicable fraction is the fraction determined in accordance with the following table:

[If the model year of the vehicle is:	The applicable fraction is:
1984 or 1985	1
1983	5/6
1982	4/6
1981	3/6
1980	2/6
1979	1/6

In the case of a 1978 or earlier model year vehicle, the applicable fraction shall be zero.

[(7) BASIS REDUCTION.—For the purposes of subtitle A, the basis of any qualified diesel-powered highway vehicle shall be reduced by the amount payable under this subsection with respect to such vehicle.]

* * * * * * *

(i) TIME FOR FILING CLAIMS; PERIOD COVERED.—

(1) GENERAL RULE.—Except as otherwise provided in this subsection, not more than one claim may be filed under subsection (a), (b), (c), (d), [(g),] (h), (l) or (q) by any person with respect to fuel used [(or a qualified diesel powered highway vehicle purchased)] during his taxable year; and no claim shall be allowed under this paragraph with respect to fuel used [(or a qualified diesel powered highway vehicle purchased)] during any taxable year unless filed by the purchaser not later than the time prescribed by law for filing a claim for credit or refund of overpayment of income tax for such taxable year. For purposes of this paragraph, a person's taxable year shall be his taxable year for purposes of subtitle A.

(2) EXCEPTIONS.—

(A) IN GENERAL.—If $1,000 or more is payable under subsections (a), (b), (d), [(g),] (h), and (q) to any person with respect to fuel used [(or a qualified diesel powered highway vehicle purchased)] during any of the first 3 quarters of his taxable year, a claim may be filed under

this section by the purchaser with respect to fuel used [(or a qualified diesel powered highway vehicle purchased)], during such quarter.

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CHAPTER 66—LIMITATIONS

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Subchapter A—Procedure in General

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SEC. 6501. LIMITATIONS ON ASSESSMENT AND COLLECTION.

(a) * * *

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[(m) DEFICIENCY ATTRIBUTABLE TO ELECTION UNDER SECTION 44B.—The period for assessing a deficiency attributable to any election under section 44B (or any revocation thereof) shall not expire before the date 1 year after the date on which the Secretary is notified of such election (or revocation).]

[(n)] *(m)* DEFICIENCIES ATTRIBUTABLE TO ELECTION OF CERTAIN CREDITS.—The period for assessing a deficiency attributable to any election under [section 40(f) or 51(j)] *section 30(d)(4), 40(f), 43, 45B, or 51(j)* (or any revocation thereof) shall not expire before the date 1 year after the date on which the Secretary is notified of such election (or revocation).

[(o)] *(n)* CROSS REFERENCES.—

(1) For period of limitations for assessment and collection in the case of a joint income return filed after separate returns have been filed, see section 6013(b)(3) and (4).

(2) For extension of period in the case of partnership items (as defined in section 6231(a)(3)), see section 6229.

* * * * * * *

SEC. 6503. SUSPENSION OF RUNNING OF PERIOD OF LIMITATION.

(a) * * *

* * * * * * *

[(k)] *(j)* EXTENSION IN CASE OF CERTAIN SUMMONSES.—

(1) IN GENERAL.—If any designated summons is issued by the Secretary with respect to any return of tax by a corporation, the running of any period of limitations provided in section 6501 on the assessment of such tax shall be suspended—

(A) * * *

* * * * * * *

[(l)] *(k)* CROSS REFERENCES.—

For suspension in case of—

* * * * * * *

CHAPTER 67—INTEREST

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Subchapter C—Determination of Interest Rate; Compounding of Interest

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SEC. 6621. DETERMINATION OF RATE OF INTEREST.

(a) * * *

* * * * * * *

(c) INCREASE IN UNDERPAYMENT RATE FOR LARGE CORPORATE UNDERPAYMENTS.—

(1) * * *

(2) APPLICABLE RATE.—For purposes of this subsection—

(A) IN GENERAL.—The applicable date is the 30th day after the earlier of—

(i) the date on which the 1st letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the Internal Revenue Service Office of Appeals is sent, or

(ii) the date on which the deficiency notice under section 6212 is sent.

The preceding sentence shall be applied without regard to any such letter or notice which is withdrawn by the Secretary.

(B) SPECIAL RULES.—

(i) NONDEFICIENCY PROCEDURES.—In the case of any underpayment of any tax imposed by this [subtitle] *title* to which the deficiency procedures do not apply, subparagraph (A) shall be applied by taking into account any letter or notice provided by the Secretary which notifies the taxpayer of the assessment or proposed assessment of the tax.

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CHAPTER 68—ADDITIONS TO THE TAX, ADDITIONAL AMOUNTS, ANS ASSESSABLE PENALTIES

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Subchapter A—Additions to the Tax and Additional Amounts

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PART I—GENERAL PROVISIONS

Sec. 6651. Failure to file tax return or to pay tax.

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[Sec. 6662. Applicable rules.]

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SEC. 6652. FAILURE TO FILE CERTAIN INFORMATION RETURNS, REGISTRATION STATEMENTS, ETC.

(a) * * *

(e) INFORMATION REQUIRED IN CONNECTION WITH CERTAIN PLANS OF DEFERRED COMPENSATION, ETC.—In the case of failure to file a return or statement required under section 6058 (relating to information required in connection with certain plans of deferred compensation), 6047 (relating to information relating to certain trusts and annuity and bond purchase plans), or 6039D (relating to returns and records with respect to certain fringe benefit plans) on the date and in the manner prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause, there shall be paid (on notice and demand by the Secretary and in the same manner as tax) by the person failing so to file, $25 for each day during which such failure continues, but the total amount imposed under this subsection on any person for failure to file any return shall not exceed $15,000. *This subsection shall not apply to any return or statement which is an information return described in section 6724(d)(1)(C)(ii) or a payee statement described in section 6724(d)(2)(W).*

* * * * * * *

(i) FAILURE TO GIVE WRITTEN EXPLANATION TO RECIPIENTS OF CERTAIN QUALIFYING ROLLOVER DISTRIBUTIONS.—In the case of each failure to provide a written explanation as required by section 402(f), at the time prescribed therefor, unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid, on notice and demand of the Secretary and in the same manner as tax, by the person failing to provide such written explanation, an amount equal to [the $10] *$100* for each such failure, but the total amount imposed on such person for all such failures during any calendar year shall not exceed [$5,000] *$50,000*.

* * * * * * *

SEC. 6655. FAILURE BY CORPORATION TO PAY ESTIMATED INCOME TAX.

(a) * * *

* * * * * * *

(g) DEFINITIONS AND SPECIAL RULES.—

(1) * * *

* * * * * * *

(3) CERTAIN TAX-EXEMPT ORGANIZATIONS.—For purposes of this section—

(A) * * *

* * * * * * *

(C) Any reference to taxable income shall be treated as including a reference to unrelated business taxable income or net investment income (as the case may be).

In the case of any organization described in subparagraph (A), subsection (b)(2)(A) shall be applied by substituting "5th month" for "3rd month"[, and, except in the case of an election under subsection (e)(2)(C), subsection (e)(2)(A) shall be applied by substituting "2 months" for "3 months" and in clause (i)(I),

by substituting "4 months" for "5 months" in clause (i)(II), by substituting "7 months" for "8 months" in clause (i)(III), and by substituting "10 months" for "11 months" in clause (i)(IV).], *subsection (e)(2)(A) shall be applied by substituting "2 months" for "3 months" in clause (i)(I), the election under clause (i) of subsection (e)(2)(C) may be made separately for each installment, and clause (ii) of subsection (e)(2)(C) shall not apply.*

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Subchapter B—Assessable Penalties

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PART I—GENERAL PROVISIONS

Sec. 6671. Rules for application of assessable penalties.

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Sec. [6714.] 6715. Dyed fuel sold for use in or used in taxable use, etc.

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SEC. 6693. FAILURE TO PROVIDE REPORTS ON INDIVIDUAL RETIREMENT ACCOUNTS OR ANNUITIES; PENALTIES RELATING TO DESIGNATED NONDEDUCTIBLE CONTRIBUTIONS.

(a) The person required by subsection (i) or (l) of section 408 to file a report regarding an individual retirement account or individual retirement annuity at the time and in the manner required by such subsection shall pay a penalty of $50 for each failure unless it is shown that such failure is due to reasonable cause. *This subsection shall not apply to any report which is an information return described in section 6724(d)(1)(C)(i) or a payee statement described in section 6724(d)(2)(V).*

* * * * * * *

(c) PENALTIES RELATING TO SIMPLE RETIREMENT ACCOUNTS.—

(1) EMPLOYER PENALTIES.—An employer who fails to provide 1 or more notices required by section 408(l)(2)(C) shall pay a penalty of $50 for each day on which such failures continue.

(2) TRUSTEE PENALTIES.—A trustee who fails—

(A) to provide 1 or more statements required by the last sentence of section 408(i) shall pay a penalty of $50 for each day on which such failures continue, or

(B) to provide 1 or more summary descriptions required by section 408(l)(2)(B) shall pay a penalty of $50 for each day on which such failures continue.

(3) REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed under this subsection with respect to any failure which the taxpayer shows was due to reasonable cause.

[(c)] *(d)* DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) does not apply to the assessment or collection of any penalty imposed by this section.

SEC. 6714. FAILURE TO MEET DISCLOSURE REQUIREMENTS APPLICABLE TO QUID PRO QUO CONTRIBUTIONS.

(a) IMPOSITION OF PENALTY.—If an organization fails to meet the disclosure requirement of section 6115 with respect to a quid pro quo contribution, such organization shall pay a penalty of $10 for each contribution in respect of which the organization fails to make the required disclosure, except that the total penalty imposed by this subsection with respect to a particular fundraising event or mailing shall not exceed $5,000.

(b) REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed under this section with respect to any failure if it is shown that such failure is due to reasonable cause.

SEC. [6714.] *6715.* DYED FUEL SOLD FOR USE OR USED IN TAXABLE USE, ETC.

(a) IMPOSITION OF PENALTY.—If—

(1) any dyed fuel is sold or held for sale by any person for any use which such person knows or has reason to know is not a nontaxable use of such fuel,

(2) * * *

* * * * * * *

PART II—FAILURE TO COMPLY WITH CERTAIN INFORMATION REPORTING REQUIREMENTS

* * * * * * *

SEC. 6724. WAIVER; DEFINITIONS AND SPECIAL RULES.

(a) * * *

* * * * * * *

(d) DEFINITIONS.—For purposes of this part—

(1) INFORMATION RETURN.—The term "information return" means—

(A) any statement of the amount of payments to another person required by—

(i) * * *

* * * * * * *

(vi) section 6050N(a) (relating to payments of royalties), **[**or**]**

(vii) section 6051(d) (relating to information returns with respect to income tax withheld), **[**and**]** *or*

(viii) section 6050Q (relating to returns relating to certain purchases of fish), and

(B) any return required by—

(i) * * *

* * * * * * *

(xii) subparagraph (A) or (C) of subsection (c)(4), or section 4093 (relating to information reporting with respect to tax on diesel and aviation fuels), **[**or**]**

(xiii) section 4101(d) (relating to information reporting with respect to fuels taxes)**[**.**]**, *or*

(xiv) subparagraph (C) of section 338(h)(10)(relating to information required to be furnished to the Sec-

retary in case of elective recognition of gain or loss)[.], *and*

(C) any statement of the amount of payments to another person required to be made to the Secretary under—

(i) section 408(i) (relating to reports with respect to individual retirement accounts or annuities), or

(ii) section 6047(d) (relating to reports by employers, plan administrators, etc.).

Such term also includes any form, statement, or schedule required to be filed with the Secretary with respect to any amount from which tax was required to be deducted and withheld under chapter 3 (or from which tax would be required to be so deducted and withheld but for an exemption under this title or any treaty obligation of the United States).

(2) PAYEE STATEMENT.—The term "payee statement" means any statement required to be furnished under—

(A) section 6031 (b) or (c), 6034A, or 6037(b) (relating to statements furnished by certain pass-thru entities),

* * * * * * *

(Q) section 6050Q(c) (relating to returns relating to certain purchases of fish),

[(Q)] *(R)* section 6051 (relating to receipts for employees),

[(R)] *(S)* section 6052(b) (relating to returns regarding payment of wages in the form of group-term life insurance),

[(S)] *(T)* section 6053 (b) or (c) (relating to reports of tips), [or]

[(T)] *(U)* section 4093(c)(4)(B) (relating to certain purchasers of diesel and aviation fuels)[.],

(V) section 408(i) (relating to reports with respect to individual retirement plans) to any person other than the Secretary with respect to the amount of payments made to such person, or

(W) section 6047(d) (relating to reports by plan administrators) to any person other than the Secretary with respect to the amount of payments made to such person.

Such term also includes any form, statement, or schedule required to be furnished to the recipient of any amount from which tax was required to be deducted and withheld under chapter 3 (or from which tax would be required to be so deducted and withheld but for an exemption under this title or any treaty obligation of the United States).

(3) Specified information reporting requirement.—The term "specified information reporting requirement" means—

(A) * * *

* * * * * * *

(E) any requirement under section [6109(f)] *6109(h)* that—

(i) a person include on his return the name, address, and TIN of another person, or

(ii) a person furnish his TIN to another person.

* * * * * * *

SEC. 7012. CROSS REFERENCES.

(1) * * *

* * * * * * *

(3) For provisions relating to registration in relation to the [production or importation of gasoline] *taxes on gasoline and diesel fuel*, see section 4101.

[(4) For provisions relating to registration in relation to the manufacture or production of lubricating oils, see section 4101.]

[(5)] *(4)* For penalty for failure to register, see section 7272.

[(6)] *(5)* For other penalties for failure to register with respect to wagering, see section 7262.

* * * * * * *

CHAPTER 75—CRIMES, OTHER OFFENSES, AND FIREARMS

* * * * * * *

Subchapter A—Crimes

* * * * * * *

PART II—PENALTIES APPLICABLE TO CERTAIN TAXES

* * * * * * *

SEC. 7232. FAILURE TO REGISTER, OR FALSE STATEMENT BY MANUFACTURER OR PRODUCER OF GASOLINE, [LUBRICATING OIL,] DIESEL FUEL, OR AVIATION FUEL.

Every person who fails to register as required by section 4101, or who in connection with any purchase of gasoline, [lubricating oil,] diesel fuel, or aviation fuel falsely represents himself to be registered as provided by section 4101, or who willfully makes any false statement in an application for registration under section 4101, shall, upon conviction thereof, be fined not more than $5,000, or imprisoned not more than 5 years, or both, together with the costs of prosecution.

* * * * * * *

CHAPTER 76—JUDICIAL PROCEEDINGS

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Subchapter C—The Tax Court

* * * * * * *

PART II—PROCEDURE

* * * * * * *

SEC. 7454. BURDEN OF PROOF IN FRAUD, FOUNDATION MANAGER, AND TRANSFEREE CASES.

(a) * * *

(b) FOUNDATION MANAGERS.—In any proceeding involving the issue whether a foundation manager (as defined in section 4946(b)) has "knowingly" participated in an act of self-dealing (within the meaning of section 4941), participated in an investment which jeopardizes the carrying out of exempt purposes (within the meaning of section 4944), or agreed to the making of a taxable expenditure (within the meaning of section 4945), or whether the trustee of a trust described in section 501(c)(21) has "knowingly" participated in an act of self-dealing (within the meaning of section 4951) or agreed to the making of a taxable expenditure (within the meaning of section 4952), or whether an organization manager (as defined in [section 4955(e)(2)] *section 4955(f)(2)*) has "knowingly" agreed to the making of a political expenditure (within the meaning of section 4955),, or whether an organization manager (as defined in section 4912(d)(2)) has "knowingly" agreed to the making of disqualifying lobbying expenditures within the meaning of section 4912(b), the burden of proof in respect of such issue shall be upon the Secretary.

* * * * * * *

CHAPTER 78—DISCOVERY OF LIABILITY AND ENFORCEMENT OF TITLE

* * * * * * *

Subchapter A—Examination and Inspection

* * * * * * *

SEC. 7611. RESTRICTIONS ON CHURCH TAX INQUIRIES AND EXAMINATIONS.

(a) * * *

* * * * * * *

(h) DEFINITIONS.—For purposes of this section—

(1) * * *

* * * * * * *

(7) APPROPRIATE HIGH-LEVEL TREASURY OFFICIAL.—The term "[approporiate] *appropriate* high-level Treasury official" means the Secretary of the Treasury or any delegate of the Secretary whose rank is no lower than that of a principal Internal Revenue officer for an internal revenue region.

* * * * * * *

CHAPTER 79—DEFINITIONS

* * * * * * *

SEC. 7701. DEFINITIONS.

(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—

(1) * * *

* * * * * * *

(20) EMPLOYEE.—For the purpose of applying the provisions of section 79 with respect to group-term life insurance purchased for employees, for the purpose of applying the provisions of sections 104, 105, and 106 with respect to accident and health insurance or accident and health plans[, for the purpose of applying the provisions of section 101(b) with respect to employees' death benefits], and for the purpose of applying the provisions of subtitle A with respect to contributions to or under a stock bonus, pension, profit-sharing, or annuity plan, and with respect to distributions under such a plan, or by a trust forming part of such a plan, and for purposes of applying section 125 with respect to cafeteria plans, the term "employee" shall include a full-time life insurance salesman who is considered an employee for the purpose of chapter 21, or in the case of services performed before January 1, 1951, who would be considered an employee if his services were performed during 1951.

* * * * * * *

CHAPTER 80—GENERAL RULES

* * * * * * *

Subchapter C—Provisions Affecting More Than One Subtitle

* * * * * * *

SEC. 7872. TREATMENT OF LOANS WITH BELOW-MARKET INTEREST RATES.

(a) TREATMENT OF GIFT LOANS AND DEMAND LOANS.—

(1) IN GENERAL.—For purposes of this title, in the case of any below-market loan to which this section applies and which is a gift loan or a demand loan, the [foregone] *forgone* interest shall be treated as—

(A) transferred from the lender to the borrower, and

(B) retransferred by the borrower to the lender as interest.

(2) TIME WHEN TRANSFERS MADE.—Except as otherwise provided in regulations prescribed by the Secretary, any [foregone] *forgone* interest attributable to periods during any calendar year shall be treated as transferred (and retransferred) under paragraph (1) on the last day of such calendar year.

* * * * * * *

(e) DEFINITIONS OF BELOW-MARKET LOAN AND [FOREGONE] *FORGONE* INTEREST.—For purposes of this section—

(1) * * *

(2) [FOREGONE] *FORGONE* INTEREST.—The term "[foregone] *forgone* interest" means, with respect to any period during which the loan is outstanding, the excess of—

(A) the amount of interest which would have been payable on the loan for the period if interest accrued on the loan at the applicable Federal rate and were payable annually on the day referred to in subsection (a)(2), over

(B) any interest payable on the loan properly allocable to such period.

(f) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) * * *

* * * * * * *

[(12) SPECIAL RULE FOR CERTAIN EMPLOYER SECURITY LOANS.—This section shall not apply to any loan between a corporation (or any member of the controlled group of corporations which includes such corporation) and an employee stock ownership plan described in section 4975(e)(7) to the extent that the interest rate on such loan is equal to the interest rate paid on a related securities acquisition loan (as described in section 133(b)) to such corporation.]

* * * * * * *

Subtitle I—Trust Fund Code

* * * * * * *

CHAPTER 98 TRUST FUND CODE

* * * * * * *

Subchapter A—Establishment of Trust Funds

* * * * * * *

SEC. 9502. AIRPORT AND AIRWAY TRUST FUND.

(a) * * *

(b) TRANSFER TO AIRPORT AND AIRWAY TRUST FUND OF AMOUNTS EQUIVALENT TO CERTAIN TAXES.—There is hereby appropriated to the Airport and Airway Trust Fund—

(1) * * *

(2) amounts determined by the Secretary of the Treasury to be equivalent to the taxes received in the Treasury after August 31, 1982, *and before* January 1, 1996, under section 4081 (to the extent of 14 cents per gallon), with respect to gasoline used in aircraft;

* * * * * * *

Subtitle J—Coal Industry Health Benefits

* * * * * * *

CHAPTER 99—COAL INDUSTRY HEALTH BENEFITS

* * * * * * *

Subchapter B—Combined Benefit Fund

* * * * * * *

PART III—ENFORCEMENT

* * * * * * *

SEC. 9707. FAILURE TO PAY PREMIUM.

(a) * * *

* * * * * * *

(d) LIMITATIONS ON A OF PENALTY.—

(1) IN GENERAL.—No penalty shall be imposed by subsection (a) on any failure during any period for which it is established to the satisfaction of the Secretary of the Treasury that none of the persons responsible for such failure knew, or exercising reasonable [diligence,] *diligence* would have known, that such failure existed.

* * * * * * *

REVENUE RECONCILIATION ACT OF 1993

TITLE XIII—REVENUE, HEALTH CARE, HUMAN RESOURCES, INCOME SECURITY, CUSTOMS AND TRADE, FOOD STAMP PROGRAM, AND TIMBER SALE PROVISIONS

CHAPTER 1—REVENUE PROVISIONS

SEC. 13001. SHORT TITLE; ETC.

(a) SHORT TITLE.—This chapter may be cited as the "Revenue Reconciliation Act of 1993".

* * * * * * *

Subchapter A—Training and Investment Incentives

* * * * * * *

PART IV—INCENTIVES FOR INVESTMENT IN REAL ESTATE

Subpart A—Extension of Qualified Mortgage Bonds and Low-Income Housing Credit

* * * * * * *

SEC. 13142. LOW-INCOME HOUSING CREDIT.

(a) * * *

(b) MODIFICATIONS.—

(1) * * *

* * * * * * *

(6) EFFECTIVE DATES.—

(A) * * *

[(B) WAIVER AUTHORITY AND PROHIBITED DISCRIMINATION.—The amendments made by paragraphs (3) and (4) shall take effect on the date of the enactment of this Act.]

(B) FULL-TIME STUDENTS, WAIVER AUTHORITY, AND PROHIBITED DISCRIMINATION.—The amendments made by paragraphs (2), (3), and (4) shall take effect on the date of the enactment of this Act.

(C) HOME ASSISTANCE.—The amendment made by paragraph [(2)] *(5)* shall apply to periods after the date of the enactment of this Act.

* * * * * * *

Subchapter B—Revenue Increases

PART I—PROVISIONS AFFECTING INDIVIDUALS

Subpart A—Rate Increases

* * * * * * *

SEC. 13206. PROVISIONS TO PREVENT CONVERSION OF ORDINARY INCOME TO CAPITAL GAIN.

(a) INTEREST EMBEDDED IN FINANCIAL TRANSACTIONS.—

(1) * * *

* * * * * * *

(3) EFFECTIVE DATE.—The amendments made by this [section] *subsection* shall apply to conversion transactions entered into after April 30, 1993.

* * * * * * *

Subpart B—Other Provisions

* * * * * * *

SEC. 13215. SOCIAL SECURITY AND TIER 1 RAILROAD RETIREMENT BENEFITS.

(a) * * *

* * * * * * *

(c) TRANSFERS TO THE HOSPITAL INSURANCE TRUST FUND.—

(1) IN GENERAL.—Paragraph (1) of section 121(e) of the Social Security Amendments of 1983 ([Public Law 92–21] *Public Law 98–21*) is amended by—

(A) * * *

* * * * * * *

PART VI—TREATMENT OF INTANGIBLES

SEC. 13261. AMORTIZATION OF GOODWILL AND CERTAIN OTHER INTANGIBLES.

(a) * * *

* * * * * * *

(g) EFFECTIVE DATE.—

(1) * * *

(2) ELECTION TO HAVE AMENDMENTS APPLY TO PROPERTY ACQUIRED AFTER JULY 25, 1991.—

(A) IN GENERAL.—If an election under this paragraph applies to the taxpayer—

(i) * * *

* * * * * * *

(iii) in applying subsection (f)(9) of such section, with respect to any property acquired [by the taxpayer] *by the taxpayer or a related person* on or before the date of the enactment of this Act, only holding or use on July 25, 1991, shall be taken into account.

* * * * * * *

Subchapter C—Empowerment Zones, Enterprise Communities, Rural Development Investment Areas, Etc.

* * * * * * *

PART II—CREDIT FOR CONTRIBUTIONS TO CERTAIN COMMUNITY DEVELOPMENT CORPORATIONS

SEC. 13311. CREDIT FOR CONTRIBUTIONS TO CERTAIN COMMUNITY DEVELOPMENT CORPORATIONS.

(a) * * *

* * * * * * *

(e) SELECTED COMMUNITY DEVELOPMENT CORPORATIONS.—

(1) * * *

(2) ONLY 20 CORPORATIONS MAY BE SELECTED.—The Secretary of Housing and Urban Development may select 20 corporations for purposes of this section, subject to the availability of eligible corporations. Such selections may be made only before July

1, 1994. At least 8 of the operational areas of the corporations selected must be rural areas (as defined by section [1393(a)(3)] *1393(a)(2)* of such Code).

* * * * * * *

Part V—Miscellaneous Provisions

* * * * * * *

SEC. 13443. CREDIT FOR PORTION OF EMPLOYER SOCIAL SECURITY TAXES PAID WITH RESPECT TO EMPLOYEE CASH TIPS.

(a) * * *

* * * * * * *

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to taxes paid after December 31, 1993, *with respect to services performed before, on, or after such date.*

* * * * * * *

SOCIAL SECURITY ACT

* * * * * * *

TITLE II—FEDERAL OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE BENEFITS

* * * * * * *

DEFINITION OF WAGES

SEC. 209. (a) For the purposes of this title, the term "wages" means remuneration paid prior to 1951 which was wages for the purposes of this title under the law applicable to the payment of such remuneration, and remuneration paid after 1950 for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash; except that, in the case of remuneration paid after 1950, such term shall not include—

(1) * * *

* * * * * * *

(4) Any payment made to, or on behalf of, an employee or his beneficiary (A) from or to a trust exempt from tax under section 165(a) of the Internal Revenue Code of 1939 at the time of such payment or, in the case of a payment after 1954, under sections 401 and 501(a) of the Internal Revenue Code of 1954 or the Internal Revenue Code of 1986, unless such payment is made to an employee of the trust as remuneration for services rendered as such employee and not as a beneficiary of the trust, or (B) under or to an annuity plan which, at the time of such payment, meets the requirements of section 165(a)(3), (4), (5), and (6) of the Internal Revenue Code of 1939 or, in the case of a payment after 1954 and prior to 1963, the requirements of section 401(a)(3), (4), (5), and (6) of the Internal Revenue Code of 1954, or (C) under or to an annuity plan which, at the time of any such payment after 1962, is a plan described

in section 403(a) of the Internal Revenue Code of 1986, or (D) under or to a bond purchase plan which, at the time of any such payment after 1962, is a qualified bond purchase plan described in section 405(a) of the Internal Revenue Code of 1954 (as in effect before the enactment of the Tax Reform Act of 1984), or (E) under or to an annuity contract described in section 403(b) of the Internal Revenue Code of 1986, other than a payment for the purchase of such contract which is made by reason of a salary reduction agreement (whether evidenced by a written instrument or otherwise), or (F) under or to an exempt governmental deferred compensation plan (as defined in section 3121(v)(3) of such Code), or (G) to supplement pension benefits under a plan or trust described in any of the foregoing provisions of this subsection to take into account some portion or all of the increase in the cost of living (as determined by the Secretary of Labor) since retirement but only if such supplemental payments are under a plan which is treated as a welfare plan under section 3(2)(B)(ii) of the Employee Retirement Income Security Act of 1974, or (H) under a simplified employee pension (as defined in section 408(k)(1) of such Code), other than any contributions described in section 408(k)(6) of such Code, (I) under a cafeteria plan (within the meaning of section 125 of the Internal Revenue Code of 1986) if such payment would not be treated as wages without regard to such plan and it is reasonable to believe that (if section 125 applied for purposes of this section) section 125 would not treat any wages as constructively received, *or (J) under an arrangement to which section 408(p) of such Code applies, other than any elective contributions under paragraph (2)(A)(i) thereof*;

* * * * * * *

DEFINITION OF EMPLOYMENT

SEC. 210. For the purposes of this title—

Employment

(a) The term "employment" means any service performed after 1936 and prior to 1951 which was employment for the purposes of this title under the law applicable to the period in which such service was performed, and any service, of whatever nature, performed after 1950 (A) by an employee for the person employing him, irrespective of the citizenship or residence of either, (i) within the United States, or (ii) on or in connection with an American vessel or American aircraft under a contract of service which is entered into within the United States or during the performance of which and while the employee is employed on the vessel or aircraft it touches at a port in the United States, if the employee is employed on and in connection with such vessel or aircraft when outside the United States, or (B) outside the United States by a citizen or resident of the United States as an employee (i) of an American employer (as defined in subsection (e) of this section), or (ii) of a foreign affiliate (as defined in section 3121(l)(6) of the Internal Revenue Code of 1986 of an American employer during any period for which there is in effect an agreement, entered into pursuant to sec-

tion 3121(l) of such Code, with respect to such affiliate, or (C) if it is service, regardless of where or by whom performed, which is designated as employment or recognized as equivalent to employment under an agreement entered into under section 233; except that, in the case of service performed after 1950, such term shall not include—

(1) * * *

* * * * * * *

(20) Service (other than service described in paragraph (3)(A)) performed by an individual on a boat engaged in catching fish or other forms of aquatic animal life under an arrangement with the owner or operator of such boat pursuant to which—

[(A) such individual does not receive any cash remuneration (other than as provided in subparagraph (B)),]

(A) such individual does not receive any additional compensation other than as provided in subparagraph (B) and other than cash remuneration—

(i) which does not exceed $100 per trip;

(ii) which is contingent on a minimum catch; and

(iii) which is paid solely for additional duties (such as mate, engineer, or cook) for which additional cash remuneration is traditional in the industry,

* * * * * * *

For purposes of paragraph (20), the operating crew of a boat shall be treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals.

* * * * * * *

TAX REFORM ACT OF 1986

* * * * * * *

TITLE XI—PENSIONS AND DEFERRED COMPENSATION; EMPLOYEE BENEFITS; EMPLOYEE STOCK OWNERSHIP PLANS

Subtitle A—Pensions and Deferred Compensation

* * * * * * *

PART II—NONDISCRIMINATION REQUIREMENTS

* * * * * * *

SEC. 1114. DEFINITION OF HIGHLY COMPENSATED EMPLOYEE.

(a) * * *

* * * * * * *

(c) EFFECTIVE DATE.—

(1) * * *

* * * * * * *

(4) SPECIAL RULE FOR DETERMINING HIGHLY COMPENSATED EMPLOYEES.—For purposes of sections 401(k) and 401(m) of the Internal Revenue Code of 1986, in the case of an employer incorporated on December 15, 1924, if more than 50 percent of its employees in the top-paid group (within the meaning of section 414(q)(4) of such Code) earn less than $25,000 (indexed at the same time and in the same manner as under section 415(d) of such Code), then the highly compensated employees shall include employees described in section 414(q)(1)(C) of such Code determined without regard to the level of compensation of such employees. *Any reference in this paragraph to section 414(q) shall be treated as a reference to such section as in effect on the day before the date of the enactment of the Small Business Job Protection Act of 1996.*

* * * * * * *

TITLE XIII—TAX-EXEMPT BONDS

* * * * * * *

Subtitle B—Effective Dates and Transitional Rules

* * * * * * *

SEC. 1317. TRANSITIONAL RULES FOR SPECIFIC FACILITIES.

(1) * * *

* * * * * * *

(3) SPORTS FACILITIES.—A bond issued as part of an issue 95 percent or more of the net proceeds of which are to be used to provide sports facilities (within the meaning of section 103(b)(4)(B) of the 1954 Code) shall be treated as an exempt facility bond for purposes of part IV of subchapter B of chapter 1 of the 1986 Code if such facilities are described in any of the following subparagraphs:

(A) A facility is described in this subparagraph if it is a stadium—

(i) * * *

* * * * * * *

The aggregate face amount of bonds to which this subparagraph applies shall not exceed $200,000,000. *A facility shall not fail to be treated as described in this subparagraph by reason of an assignment (or an agreement to an assignment) by the governmental unit on whose behalf the*

bonds are issued of any part of its interest in the property financed by such bonds to another governmental unit.

* * * * * * *

SECTION 767 OF THE URUGUAY ROUND AGREEMENTS ACT

SEC. 767. SINGLE SUM DISTRIBUTIONS.

(a) * * *

* * * * * * *

(d) EFFECTIVE DATE.—

(1) * * *

* * * * * * *

(3) SECTION 415.—

[(A) NO REDUCTION REQUIRED.—An accrued benefit shall not be required to be reduced below the accrued benefit as of the last day of the last plan year beginning before January 1, 1995, merely because of the amendments made by subsection (b).]

(A) EXCEPTION.—A plan that was adopted and in effect before December 8, 1994, shall not be required to apply the amendments made by subsection (b) with respect to benefits accrued before the earlier of—

(i) the later of the date a plan amendment applying such amendment is adopted or made effective, or

(ii) the first day of the first limitation year beginning after December 31, 1999.

Determinations under section 415(b)(2)(E) of the Internal Revenue Code of 1986 before such earlier date shall be made with respect to such benefits on the basis of such section as in effect on December 7, 1994 (except that the modification made by section 1449(b) of the Small Business Job Protection Act of 1996 shall be taken into account), and the provisions of the plan as in effect on December 7, 1994, but only if such provisions of the plan meet the requirements of such section (as so in effect).

* * * * * * *

REVENUE RECONCILIATION ACT OF 1990

TITLE XI—REVENUE PROVISIONS

SEC. 11001. SHORT TITLE; ETC.

(a) SHORT TITLE.—This title may be cited as the "Revenue Reconciliation Act of 1990".

* * * * * * *

Subtitle B—Excise Taxes

* * * * * * *

PART II—USER-RELATED TAXES

* * * * * * *

SEC. 11212. IMPROVEMENTS IN ADMINISTRATION OF GASOLINE EXCISE TAX.

(a) * * *

* * * * * * *

(e) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) [Paragraph (1) of section 6724(d)] *Subparagraph (B) of section 6724(d)(1)* is amended by striking "or" at the end of clause (x), by striking ", or subsection (e)," in clause (xi), by striking the period at the end of clause (xi) and inserting ", or", and by inserting after clause (xi) the following new clause:

"(xii) section 4101(d) (relating to information reporting with respect to fuels taxes)."

* * * * * * *

Subtitle G—Tax Technical Corrections

* * * * * * *

SEC. 11701. AMENDMENTS RELATED TO REVENUE RECONCILIATION ACT OF 1989.

(a) AMENDMENTS RELATED TO SECTION 7108.—

(1) * * *

* * * * * * *

[(11) Paragraph (2) of section 7108(r) of the Revenue Reconciliation Act of 1989 is amended by inserting before the period "but only with respect to bonds issued after such date".]

* * * * * * *

(f) AMENDMENT RELATED TO SECTION 7401.—Paragraph (2) of section 6038(e) *(relating to definitions)* is amended by adding at the end thereof the following new sentence: "In the case of a specified foreign corporation (as defined in section 898), the taxable year of such corporation shall be treated as its annual accounting period."

* * * * * * *

EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974

* * * * * * *

TITLE I—PROTECTION OF EMPLOYEE BENEFIT RIGHTS

SUBTITLE A—GENERAL PROVISIONS

* * * * * * *

DEFINITIONS

SEC. 3. For purposes of this title:
(1) * * *

* * * * * * *

(37)(A) * * *

* * * * * * *

(F)(i) * * *

(ii) For purposes of the Internal Revenue Code of 1986—

(I) clause (i) shall apply, and

(II) a qualified football coaches plan shall be treated as a multiemployer collectively bargained plan.

[(ii)] *(iii)* For purposes of this subparagraph, the term "qualified football coaches plan" means any defined contribution plan which is established and maintained by an organization—

(I) which is described in section 501(c) of such Code;

(II) the membership of which consists entirely of individuals who primarily coach football as full-time employees of 4-year colleges or universities described in section 170(b)(1)(A)(ii) of such Code; and

(III) which was in existence on September 18, 1986.

* * * * * * *

PART 6—GROUP HEALTH PLANS

GROUP HEALTH PLANS

* * * * * * *

SEC. 602. CONTINUATION COVERAGE.

For purposes of section 601, the term "continuation coverage" means coverage under the plan which meets the following requirements:

(1) * * *

(2) PERIOD OF COVERAGE.—The coverage must extend for at least the period beginning on the date of the qualifying event and ending not earlier than the earliest of the following:

(A) MAXIMUM REQUIRED PERIOD.—

(i) * * *

* * * * * * *

[(v) QUALIFYING EVENT INVOLVING MEDICARE ENTITLEMENT.—In the case of an event described in section 603(4) (without regard to whether such event is a qualifying event), the period of coverage for qualified beneficiaries other than the covered employee for such event or any subsequent qualifying event shall not terminate before the close of the 36-month period beginning on the date the covered employee becomes enti-

tled to benefits under title XVIII of the Social Security Act.]

(v) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in section 603(2) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this subparagraph before the close of the 36-month period beginning on the date the covered employee became so entitled.

In the case of an individual who is determined, under title II or XVI of the Social Security Act, to have been disabled at the time of a qualifying event described in section 603(2), any reference in clause (i) or (ii) to 18 months with respect to such event is deemed a reference to 29 months, but only if the qualified beneficiary has provided notice of such determination under section 606(3) before the end of such 18 months.

* * * * * * *

SECTION 2202 OF THE PUBLIC HEALTH SERVICE ACT

SEC. 2202. CONTINUATION COVERAGE.

For purposes of section 2201, the term "continuation coverage" means coverage under the plan which meets the following requirements:

(1) * * *

(2) PERIOD OF COVERAGE.—The coverage must extend for at least the period beginning on the date of the qualifying event and ending not earlier than the earliest of the following:

(A) MAXIMUM REQUIRED PERIOD.—

(i) * * *

* * * * * * *

[(iv) QUALIFYING EVENT INVOLVING MEDICARE ENTITLEMENT.—In the case of an event described in section 2203(4) (without regard to whether such event is a qualifying event), the period of coverage for qualified beneficiaries other than the covered employee for such event or any subsequent qualifying event shall not terminate before the close of the 36-month period beginning on the date the covered employee becomes entitled to benefits under title XVIII of the Social Security Act.]

(iv) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in section 2203(2) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than

the covered employee shall not terminate under this subparagraph before the close of the 36-month period beginning on the date the covered employee became so entitled.

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OMNIBUS BUDGET RECONCILIATION ACT OF 1989

* * * * * * *

TITLE VI—MEDICARE, MEDICAID, MATERNAL AND CHILD HEALTH, AND OTHER HEALTH PROVISIONS

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Subtitle E—Provisions With Respect to COBRA Continuation Coverage

PART 1—EXTENSION OF COVERAGE FOR DISABLED EMPLOYEES

* * * * * * *

SEC. 6701. EXTENSION, UNDER INTERNAL REVENUE CODE, OF COVERAGE FROM 18 TO 29 MONTHS FOR THOSE WITH A DISABILITY AT TIME OF TERMINATION OF EMPLOYMENT.

(a) IN GENERAL.—Paragraph (2)(B) of section 4980B(f) of the Internal Revenue Code of 1986, as added by section 3011(a) of the Technical and Miscellaneous Revenue Act of 1988 (Public Law 100–647), (relating to maximum required period of continuation coverage), is amended—

(1) in clause (i) by adding after and below subclause [(IV)] *(V)* the following new sentence:

"In the case of a qualified beneficiary who is determined, under title II or XVI of the Social Security Act, to have been disabled at the time of a qualifying event described in paragraph (3)(B), any reference in subclause (I) or (II) to 18 months with respect to such event is deemed a reference to 29 months, but only if the qualified beneficiary has provided notice of such determination under paragraph (6)(C) before the end of such 18 months."; and

* * * * * * *

TITLE VII—REVENUE MEASURES

* * * * * * *

Subtitle C—Employee Benefit Provisions

PART I—EMPLOYEE STOCK OWNERSHIP PLANS

* * * * * * *

SEC. 7304. REPEAL OF CERTAIN PROVISIONS RELATING TO EMPLOYEE STOCK OWNERSHIP PLANS.

(a) ESTATE TAX DEDUCTION.—

(1) * * *

(2) CONFORMING AMENDMENTS.—

(A) * * *

* * * * * * *

(D) Section 4979A is amended—

(i) by striking "or section 2057" in subsection (b)(1), and

(ii) by striking "or section 2057(d)" in subsection [(c)(2)] *(c)*.

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Subtitle F—Miscellaneous Provisions

* * * * * * *

PART V—OTHER PROVISIONS

* * * * * * *

SEC. 7646. REPORTING OF POINTS ON MORTGAGE LOANS.

(a) * * *

(b) TECHNICAL AMENDMENTS.—

(1) Subparagraph (B) of section [6050H(b)(1)] *6050H(b)(2)* is amended by inserting "(other than points)" after "such interest".

* * * * * * *

Subtitle G—Revision of Civil Penalties

* * * * * * *

PART II—REVISION OF ACCURACY-RELATED PENALTIES

SEC. 7721. REVISION OF ACCURACY-RELATED PENALTIES.

(a) * * *

* * * * * * *

(c) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) * * *

* * * * * * *

(10) Subparagraph (C) of section 461(i)(3) is amended by striking "section [6662(b)(2)(C)(ii)] *6661(b)(2)(C)(ii)*" and inserting "section 6662(d)(2)(C)(ii)".

* * * * * * *

Subtitle H—Technical Corrections

* * * * * * *

PART I—AMENDMENTS RELATED TO TECHNICAL AND MISCELLANEOUS REVENUE ACT OF 1988

SEC. 7811. AMENDMENTS RELATED TO TITLE I OF THE 1988 ACT.

(a) * * *

* * * * * * *

(i) AMENDMENTS RELATED TO SECTION 1012 OF THE 1988 ACT.—

(1) * * *

* * * * * * *

(3) Subparagraph (A) of section 954(c)(3) is amended—

(A) by striking "is created" *the first place it appears* in clause (i) and inserting "is a corporation created",

* * * * * * *

PART IV—MISCELLANEOUS CHANGES

SEC. 7841. MISCELLANEOUS CHANGES.

(a) * * *

* * * * * * *

(d) MISCELLANEOUS CLERICAL CHANGES.—

(1) * * *

* * * * * * *

(10) Paragraph (27) of section [381(a)] *381(c)* (relating to credit under section 53) is redesignated as paragraph (26).

* * * * * * *

PART V—AMENDMENTS RELATED TO PENSION PROVISIONS

* * * * * * *

Subpart A—Amendments Related To Tax Reform Act of 1986

SEC. 7861. AMENDMENTS RELATED TO TITLE XI OF THE REFORM ACT.

(a) * * *

* * * * * * *

(c) AMENDMENTS RELATED TO SECTION 1140 OF THE REFORM ACT.—

(1) * * *

(2) Section 1140(c) of the Reform Act is amended by striking all after "the first plan year beginning" *the second place it appears* and inserting "after the later of—

"(1) December 31, 1988, or

"(2) the earlier of—

"(A) December 31, 1990, or

"(B) the date on which the last of such collective bargaining agreements terminate (without regard to any extension after February 28, 1986)."

* * * * * * *

VII. SUPPLEMENTAL VIEWS OF DEMOCRATIC MEMBERS OF THE COMMITTEE ON WAYS AND MEANS ON H.R. 3448

After many months of strong opposition to legislation that would increase the minimum hourly wage from $4.25 to $5.15 over two years, Republicans have indicated they will consider wage legislation only if they are allowed to include tax benefits for business. Even though we favor expanded investment incentives and simplified rules for small business, we prefer not to endanger the passage of an increase in the minimum wage by linking it to unrelated issues.

Some Republicans have argued that minimum wage concerns should not be taken seriously since workers living on these low wages do not exist.We know differently; these workers are real people; they do exist; many of them have families; many of them are struggling to make ends meet. These people are not seeking government hand-outs. They merely seek a way to keep their heads above water, food on the table, and shelter. They also seek an opportunity to improve their status in life.

However, our major regret over most of the tax provisions contained in the bill is that we were not permitted to reach a bipartisan consensus on the details of the provisions that we all support. We think this bill should help the workers and their families as well as business owners.

During Committee consideration of this bill, we attempted to improve the bill for workers and their families. Our Republican Members rejected amendments which would have (1) improved educational opportunities for American workers and low- and middle-income families and (2) enhanced financial stability for the long-term unemployed.

Improved educational opportunity needs more than lip service to become a reality

Under the bill, the provision to provide tax-free employer-provided educational assistance would be extended from January 1, 1995, through December 31, 1996. However educational expenses for graduate studies would not receive the exclusion after December 31, 1995. We question the intelligence of this decision. The Republicans argue that their primary concern here is to provide more Americans with the opportunity to obtain a basic education at the undergraduate level before resources can be committed for graduate studies. Given the advanced knowledge of technology that is required by many of today's jobs, it is more important than ever that our American workers receive higher education. If employers are willing to foot the bill, can we as a national fail to encourage the effort?

During consideration of H.R. 3448, Republicans were given the opportunity to approve an amendment, originally proposed by

President Clinton, that would have allowed taxpayers with income below $70,000 (single return) and $120,000 (joint return) to deduct up to $5,000 of educational expenses. Republicans argued that because the benefit would not be available to taxpayers at all income levels, they could not support the amendment. We cannot endorse such policies. In a time of limited Resources, our Republican colleagues have refused to set priorities based on areas of greatest need. Republicans continue to demonstrate that any tax benefits they support for low- and middle-income taxpayers must trickle down from benefits bestowed upon the high-income taxpayers.

In addition, the fallacy of the argument espoused by Republicans in support of the repeal of the benefit for graduate studies must be questioned. If the true reason for this repeal is to give priority to providing a basic undergraduate education to a greater number of workers and families, what happened to this commitment when the Republicans were presented with the perfect opportunity to lend credence to this claim? How do they explain their failure to provide approximately 17 million students with a modest deduction for educational expenses incurred in obtaining the basic undergraduate education? What alternative do they offer? Let us remind ourselves that this bill is intended to include benefits for "small" businesses and the employees of those businesses. In the area of education, it fails.

The need for continuing education has never been more real and evident in our country than today. Technological advances outpace the ability of employers and workers to maintain a leading competitive edge in the world today. The world economy mandates that substantial resources be committed to the continuing training and education of our workers. This effort cannot be executed efficiently if it must be undertaken solely by employers.

Data on the employer-provided educational assistance benefit indicate that most employees who are receiving employer-provided graduate education are studying business education; health-related courses are second; and engineering is third. We have been unable to uncover any evidence to support the Republican claim that graduate level benefits should not be allowed because they are used primarily by individuals who become doctors and lawyers. We cannot argue that this does not occur occasionally, but are we prepared to "throw the baby out with the bath water" at a time when this benefit is needed more than ever? We implore our Republican colleagues to reconsider their position on this issue.

It was argued that the employer-provided educational assistance benefit must be modified because it gives an unfair advantage to the worker whose employer offers this benefit over the worker whose employer does not offer the benefit. We must ask, if this is truly a concern why not support the effort to provide these workers with the benefit of a $5,000 deduction for their educational expense? Moreover, should we be concerned over the total elimination of this benefit the next time around? At one point during consideration of this bill, five Republicans joined us in adding back graduate education benefits to the exclusion. For one fleeting moment, we delighted in the fact that this Committee had set aside partisanship and accomplished good policy. However, our pride in the Committee was short-lived for within an hour of the first vote

every Republican Member voted to reconsider the earlier vote and then voted against the graduate education benefit.

Where is the concern for the long-term unemployed?

We were also disappointed when our Republican colleagues turned their backs on a golden opportunity to permit long-term unemployed individuals, during periods of unemployment, to withdraw funds from their pension plans without paying the additional 10-percent tax.

The urgency of this provision confronts us every day as we hear from people who were once gainfully employed, saving for retirement, and providing adequately for the needs of their families. Then their employment was terminated. At the beginning of this process, the worker is optimistic because he or she has some small savings to cover short-term emergencies. A few months go by and the reality of job hunting in today's market catches up with the individual. Unemployment benefits begin but at a level substantially below the worker's former salary. However, the rent or mortgage continue to be due every month, the utilities charges begin to fall into arrears; even with modification, the food bill becomes impossible for the family. This family is desperate and the only other available funds are invested in retirement savings. The family is now faced with the difficult choice of depleting some portion of its resources set aside for retirement. Under present law, withdrawals before age 59½ are not only subject to income tax on the withdrawn amount but also an additional 10-percent tax. This policy can become self-defeating. It must be evaluated in more realistic terms.

Our Republican colleagues have argued that this is not the time to support such a provision. We ask, if not now, when? How many more large-scale corporate restructuring deals must we read about before we hear the pleas of desperate individuals and families? Another argument raised by the Republicans in their defense of their position is that the provision would permit individuals to withdraw retirement funds for lavish Christmas shopping. We must strongly state our disagreement. We believe that if an employee has been conscientious enough to save for retirement, such an employee is not likely to deplete these resources willy-nilly.

In summary, we wish we had been allowed to help craft a bill to assist both businesses and workers. We believe a better product would have been reported from this Committee if such bipartisanship had prevailed.

SAM M. GIBBONS.
CHARLES B. RANGEL.
FORTNEY PETE STARK.
HAROLD E. FORD.
ROBERT T. MATSUI.
BARBARA B. KENNELLY.
WILLIAM J. COYNE.
SANDER M. LEVIN.
JIM MCDERMOTT.
GERALD D. KLECZKA.
JOHN LEWIS.
L.F. PAYNE.
RICHARD E. NEAL.
MICHAEL R. MCNULTY.

VIII. DISSENTING VIEWS ON H.R. 3448 BY: REP. CHARLES B. RANGEL (D–NY)

Although I may differ over some of the details, I support most of the provisions contained in the bill reported by the Committee. I do regret that the Committee was not permitted to reach a bipartisan consensus over the details of tax provisions that we all support. However, that is not the reason for my opposition to the bill. I oppose the bill reported by the Committee because the tax benefits it provides for small businesses and others are largely funded through revenues raised by modifications to the section 936 credit. I believe that those modifications will have an adverse impact on the economy of Puerto Rico and other possessions.

Section 936 has long been an important part of the economic development programs of Puerto Rico and the other possessions. We made substantial revisions to the section 936 credit in the 1993 Reconciliation Act with the purpose of focusing the benefits of that credit on companies with substantial economic activities in Puerto Rico. Before we have had an opportunity to analyze the impact of those changes on the economy of Puerto Rico and the other possessions, we are again considering substantial changes to section 936.

When one examines the details of the Committee bill, it becomes apparent that great care was taken to accommodate the interests of the companies currently operating in Puerto Rico. I only wish that similar care had been taken in assessing its impact on the economies of Puerto Rico and the other possessions. The fact that the individuals who could be directly and adversely affected by the Committee bill do not have voting representation in Congress requires us to be particularly sensitive to their interests.

For U.S. companies operating in Puerto Rico, section 936 generally eliminates the U.S. tax on their active business income in Puerto Rico (referred to as the active business credit) and on their income derived from certain passive investments in Puerto Rico (referred to as the QPSII credit).

The bill reported by Committee immediately terminates the QPSII credit without any serious examination of the adverse impact of such a change. Currently over one-third of the total bank deposits in Puerto Rico consists of investments eligible for the QPSII credit. Many of these deposits have short maturities and will likely be quickly withdrawn if the Committee bill becomes law. One can only speculate on the impact of such withdrawals on the banking system of Puerto Rico. The termination of the QPSII credit may have a dramatic impact on the Puerto Rican banking system but is a small inconvenience for the companies operating there. That inconvenience is offset by other provisions of the Committee bill that facilitate the accumulation of passive investment assets in foreign tax haven countries.

The Committee bill immediately terminates the section 936 active business credit for new investments in Puerto Rico. Under the committee bill, there will be no tax incentives for new business investments in Puerto Rico but there will be very generous transition rules for those companies who have claimed section 936 benefits in the past. Opponents of section 936 have argued that it provides overly generous tax benefits to a relatively small number of companies operating in Puerto Rico. Ironically, the companies currently enjoying those "over generous" benefits are generally supportive of the Committee bill because it provides them a generous ten-year transition period during which they will continue to enjoy most of those benefits.

I believe that we should consider modifications to the section 936 credit and other tax benefits to ensure that they are accomplishing their intended purpose. The Administration has a proposal that would continue the effort started in 1993 to focus the credit on companies with substantial economic activities in Puerto Rico. I believe that such an approach would eliminate the alleged abuses under the section 936 credit and would continue positive tax incentives for future business investments in Puerto Rico.

CHARLES B. RANGEL.

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104TH CONGRESS
2d Session
HOUSE OF REPRESENTATIVES
REPORT
104–737

SMALL BUSINESS JOB PROTECTION ACT OF 1996

AUGUST 1, 1996.—Ordered to be printed

Mr. ARCHER, from the committee of conference, submitted the following

CONFERENCE REPORT

[To accompany H.R. 3448]

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 3448), to provide tax relief for small businesses, to protect jobs, to create opportunities, to increase the take home pay of workers, to amend the Portal-to-Portal Act of 1947 relating to the payment of wages to employees who use employer owned vehicles, and to amend the Fair Labor Standards Act of 1938 to increase the minimum wage rate and to prevent job loss by providing flexibility to employers in complying with minimum wage and overtime requirements under that Act, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

TITLE I

That the House recede from its disagreement to the amendment of the Senate numbered 1, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment, insert the following:

(b) TABLE OF CONTENTS.—

26–253

TITLE I—SMALL BUSINESS AND OTHER TAX PROVISIONS

SEC. 1101. AMENDMENT OF 1986 CODE.

Except as otherwise expressly provided, whenever in this title an amendment or repeal is expressed in terms of an amendment to, or

repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

SEC. 1102. UNDERPAYMENTS OF ESTIMATED TAX.

No addition to the tax shall be made under section 6654 or 6655 of the Internal Revenue Code of 1986 (relating to failure to pay estimated tax) with respect to any underpayment of an installment required to be paid before the date of the enactment of this Act to the extent such underpayment was created or increased by any provision of this title.

Subtitle A—Expensing; Etc.

SEC. 1111. INCREASE IN EXPENSE TREATMENT FOR SMALL BUSINESSES.

(a) GENERAL RULE.—Paragraph (1) of section 179(b) (relating to dollar limitation) is amended to read as follows:

"(1) DOLLAR LIMITATION.—The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed the following applicable amount:

"If the taxable year begins in:	*The applicable amount is:*
1997	*18,000*
1998	*18,500*
1999	*19,000*
2000	*20,000*
2001 or 2002	*24,000*
2003 or thereafter	*25,000.".*

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1996.

SEC. 1112. TREATMENT OF EMPLOYEE TIPS.

(a) EMPLOYEE CASH TIPS.—

(1) REPORTING REQUIREMENT NOT CONSIDERED.—Subparagraph (A) of section 45B(b)(1) (relating to excess employer social security tax) is amended by inserting "(without regard to whether such tips are reported under section 6053)" after "section 3121(q)".

(2) TAXES PAID.—Subsection (d) of section 13443 of the Revenue Reconciliation Act of 1993 is amended by inserting ", with respect to services performed before, on, or after such date" after "1993".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall take effect as if included in the amendments made by, and the provisions of, section 13443 of the Revenue Reconciliation Act of 1993.

(b) TIPS FOR EMPLOYEES DELIVERING FOOD OR BEVERAGES.—

(1) IN GENERAL.—Paragraph (2) of section 45B(b) is amended to read as follows:

"(2) ONLY TIPS RECEIVED FOR FOOD OR BEVERAGES TAKEN INTO ACCOUNT.—In applying paragraph (1), there shall be taken into account only tips received from customers in connection with the providing, delivering, or serving of food or beverages for consumption if the tipping of employees delivering or serving food or beverages by customers is customary.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to tips received for services performed after December 31, 1996.

SEC. 1113. TREATMENT OF STORAGE OF PRODUCT SAMPLES.

(a) IN GENERAL.—Paragraph (2) of section 280A(c) is amended by striking "inventory" and inserting "inventory or product samples".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1995.

SEC. 1114. TREATMENT OF CERTAIN CHARITABLE RISK POOLS.

(a) GENERAL RULE.—Section 501 (relating to exemption from tax on corporations, certain trusts, etc.) is amended by redesignating subsection (n) as subsection (o) and by inserting after subsection (m) the following new subsection:

"(n) CHARITABLE RISK POOLS.—

"(1) IN GENERAL.—For purposes of this title—

"(A) a qualified charitable risk pool shall be treated as an organization organized and operated exclusively for charitable purposes, and

"(B) subsection (m) shall not apply to a qualified charitable risk pool.

"(2) QUALIFIED CHARITABLE RISK POOL.—For purposes of this subsection, the term 'qualified charitable risk pool' means any organization—

"(A) which is organized and operated solely to pool insurable risks of its members (other than risks related to medical malpractice) and to provide information to its members with respect to loss control and risk management,

"(B) which is comprised solely of members that are organizations described in subsection (c)(3) and exempt from tax under subsection (a), and

"(C) which meets the organizational requirements of paragraph (3).

"(3) ORGANIZATIONAL REQUIREMENTS.—An organization (hereinafter in this subsection referred to as the 'risk pool') meets the organizational requirements of this paragraph if—

"(A) such risk pool is organized as a nonprofit organization under State law provisions authorizing risk pooling arrangements for charitable organizations,

"(B) such risk pool is exempt from any income tax imposed by the State (or will be so exempt after such pool qualifies as an organization exempt from tax under this title),

"(C) such risk pool has obtained at least $1,000,000 in startup capital from nonmember charitable organizations,

"(D) such risk pool is controlled by a board of directors elected by its members, and

"(E) the organizational documents of such risk pool require that—

"(i) each member of such pool shall at all times be an organization described in subsection (c)(3) and exempt from tax under subsection (a),

"(ii) any member which receives a final determination that it no longer qualifies as an organization described in subsection (c)(3) shall immediately notify the pool of such determination and the effective date of such determination, and

"(iii) each policy of insurance issued by the risk pool shall provide that such policy will not cover the insured with respect to events occurring after the date such final determination was issued to the insured.

An organization shall not cease to qualify as a qualified charitable risk pool solely by reason of the failure of any of its members to continue to be an organization described in subsection (c)(3) if, within a reasonable period of time after such pool is notified as required under subparagraph (C)(ii), such pool takes such action as may be reasonably necessary to remove such member from such pool.

"(4) OTHER DEFINITIONS.—For purposes of this subsection—

"(A) STARTUP CAPITAL.—The term 'startup capital' means any capital contributed to, and any program-related investments (within the meaning of section 4944(c)) made in, the risk pool before such pool commences operations.

"(B) NONMEMBER CHARITABLE ORGANIZATION.—The term 'nonmember charitable organization' means any organization which is described in subsection (c)(3) and exempt from tax under subsection (a) and which is not a member of the risk pool and does not benefit (directly or indirectly) from the insurance coverage provided by the pool to its members."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after the date of the enactment of this Act.

SEC. 1115. TREATMENT OF DUES PAID TO AGRICULTURAL OR HORTICULTURAL ORGANIZATIONS.

(a) GENERAL RULE.—Section 512 (defining unrelated business taxable income) is amended by adding at the end the following new subsection:

"(d) TREATMENT OF DUES OF AGRICULTURAL OR HORTICULTURAL ORGANIZATIONS.—

"(1) IN GENERAL.—If—

"(A) an agricultural or horticultural organization described in section 501(c)(5) requires annual dues to be paid in order to be a member of such organization, and

"(B) the amount of such required annual dues does not exceed $100,

in no event shall any portion of such dues be treated as derived by such organization from an unrelated trade or business by reason of any benefits or privileges to which members of such organization are entitled.

"(2) INDEXATION OF $100 AMOUNT.—In the case of any taxable year beginning in a calendar year after 1995, the $100 amount in paragraph (1) shall be increased by an amount equal to—

"(A) $100, multiplied by

"(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting 'calendar year 1994' for 'calendar year 1992' in subparagraph (B) thereof.

"(3) DUES.—For purposes of this subsection, the term 'dues' means any payment (whether or not designated as dues) which is required to be made in order to be recognized by the organization as a member of the organization.".

(b) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendment made by this section shall apply to taxable years beginning after December 31, 1986.

(2) TRANSITIONAL RULE.—If—

(A) for purposes of applying part III of subchapter F of chapter 1 of the Internal Revenue Code of 1986 to any taxable year beginning before January 1, 1987, an agricultural or horticultural organization did not treat any portion of membership dues received by it as income derived in an unrelated trade or business, and

(B) such organization had a reasonable basis for not treating such dues as income derived in an unrelated trade or business,

then, for purposes of applying such part III to any such taxable year, in no event shall any portion of such dues be treated as derived in an unrelated trade or business.

(3) REASONABLE BASIS.—For purposes of paragraph (2), an organization shall be treated as having a reasonable basis for not treating membership dues as income derived in an unrelated trade or business if the taxpayer's treatment of such dues was in reasonable reliance on any of the following:

(A) Judicial precedent, published rulings, technical advice with respect to the organization, or a letter ruling to the organization.

(B) A past Internal Revenue Service audit of the organization in which there was no assessment attributable to the reclassification of membership dues for purposes of the tax on unrelated business income.

(C) Long-standing recognized practice of agricultural or horticultural organizations.

SEC. 1116. CLARIFICATION OF EMPLOYMENT TAX STATUS OF CERTAIN FISHERMEN.

(a) CLARIFICATION OF EMPLOYMENT TAX STATUS.—

(1) AMENDMENTS OF INTERNAL REVENUE CODE OF 1986.—

(A) DETERMINATION OF SIZE OF CREW.—Subsection (b) of section 3121 (defining employment) is amended by adding at the end the following new sentence:

"For purposes of paragraph (20), the operating crew of a boat shall be treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals.".

(B) CERTAIN CASH REMUNERATION PERMITTED.—Subparagraph (A) of section 3121(b)(20) is amended to read as follows:

"(A) such individual does not receive any cash remuneration other than as provided in subparagraph (B) and other than cash remuneration—

"(i) which does not exceed $100 per trip;

"(ii) which is contingent on a minimum catch; and

"(iii) which is paid solely for additional duties (such as mate, engineer, or cook) for which additional cash remuneration is traditional in the industry,".

(C) CONFORMING AMENDMENT.—Section 6050A(a) is amended by striking "and" at the end of paragraph (3), by striking the period at the end of paragraph (4) and inserting "; and", and by adding at the end the following new paragraph:

"(5) any cash remuneration described in section 3121(b)(20)(A).".

(2) AMENDMENT OF SOCIAL SECURITY ACT.—

(A) DETERMINATION OF SIZE OF CREW.—Subsection (a) of section 210 of the Social Security Act is amended by adding at the end the following new sentence:

"For purposes of paragraph (20), the operating crew of a boat shall be treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals.".

(B) CERTAIN CASH REMUNERATION PERMITTED.—Subparagraph (A) of section 210(a)(20) of such Act is amended to read as follows:

"(A) such individual does not receive any additional compensation other than as provided in subparagraph (B) and other than cash remuneration—

"(i) which does not exceed $100 per trip;

"(ii) which is contingent on a minimum catch; and

"(iii) which is paid solely for additional duties (such as mate, engineer, or cook) for which additional cash remuneration is traditional in the industry,".

(3) EFFECTIVE DATES.—

(A) IN GENERAL.—The amendments made by this subsection shall apply to remuneration paid—

(i) after December 31, 1994, and

(ii) after December 31, 1984, and before January 1, 1995, unless the payor treated such remuneration (when paid) as being subject to tax under chapter 21 of the Internal Revenue Code of 1986.

(B) REPORTING REQUIREMENT.—The amendment made by paragraph (1)(C) shall apply to remuneration paid after December 31, 1996.

(b) INFORMATION REPORTING.—

(1) IN GENERAL.—Subpart B of part III of subchapter A of chapter 68 (relating to information concerning transactions with other persons) is amended by inserting after section 6050Q the following new section:

"SEC. 6050R. RETURNS RELATING TO CERTAIN PURCHASES OF FISH.

"(a) REQUIREMENT OF REPORTING.—Every person—

"(1) who is engaged in the trade or business of purchasing fish for resale from any person engaged in the trade or business of catching fish; and

"(2) who makes payments in cash in the course of such trade or business to such a person of $600 or more during any calendar year for the purchase of fish,

shall make a return (at such times as the Secretary may prescribe) described in subsection (b) with respect to each person to whom such a payment was made during such calendar year.

"(b) RETURN.—A return is described in this subsection if such return—

"(1) is in such form as the Secretary may prescribe, and

"(2) contains—

"(A) the name, address, and TIN of each person to whom a payment described in subsection (a)(2) was made during the calendar year;

"(B) the aggregate amount of such payments made to such person during such calendar year and the date and amount of each such payment, and

"(C) such other information as the Secretary may require.

"(c) STATEMENT TO BE FURNISHED WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

"(1) the name and address of the person required to make such a return, and

"(2) the aggregate amount of payments to the person required to be shown on the return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) is required to be made.

"(d) DEFINITIONS.—For purposes of this section:

"(1) CASH.—The term 'cash' has the meaning given such term by section 6050I(d).

"(2) FISH.—The term 'fish' includes other forms of aquatic life.".

(2) TECHNICAL AMENDMENTS.—

(A) Subparagraph (A) of section 6724(d)(1) is amended by striking "or" at the end of clause (vi), by striking "and" at the end of clause (vii) and inserting "or", and by adding at the end the following new clause:

"(viii) section 6050R (relating to returns relating to certain purchases of fish), and".

(B) Paragraph (2) of section 6724(d) is amended by redesignating subparagraphs (R) through (U) as subparagraphs (S) through (V), respectively, and by inserting after subparagraph (Q) the following new subparagraph:

"(R) section 6050R(c) (relating to returns relating to certain purchases of fish),".

(C) The table of sections for subpart B of part III of subchapter A of chapter 68 is amended by inserting after the item relating to 6050Q the following new item:

"Sec. 6050R. Returns relating to certain purchases of fish.".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to payments made after December 31, 1997.

SEC. 1117. MODIFICATIONS OF TAX-EXEMPT BOND RULES FOR FIRST-TIME FARMERS.

(a) ACQUISITION FROM RELATED PERSON ALLOWED.—Section 147(c)(2) (relating to exception for first-time farmers) is amended by adding at the end the following new subparagraph:

"(G) ACQUISITION FROM RELATED PERSON.—For purposes of this paragraph and section 144(a), the acquisition by a first-time farmer of land or personal property from a related person (within the meaning of section 144(a)(3)) shall not be treated as an acquisition from a related person, if—

"(i) the acquisition price is for the fair market value of such land or property, and

"(ii) subsequent to such acquisition, the related person does not have a financial interest in the farming operation with respect to which the bond proceeds are to be used.".

(b) SUBSTANTIAL FARMLAND AMOUNT DOUBLED.—Clause (i) of section 147(c)(2)(E) (defining substantial farmland) is amended by striking "15 percent" and inserting "30 percent".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to bonds issued after the date of the enactment of this Act.

SEC. 1118. NEWSPAPER DISTRIBUTORS TREATED AS DIRECT SELLERS.

(a) IN GENERAL.—Section 3508(b)(2)(A) is amended by striking "or" at the end of clause (i), by inserting "or" at the end of clause (ii), and by inserting after clause (ii) the following new clause:

"(iii) is engaged in the trade or business of the delivering or distribution of newspapers or shopping news (including any services directly related to such trade or business),".

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to services performed after December 31, 1995.

SEC. 1119. APPLICATION OF INVOLUNTARY CONVERSION RULES TO PRESIDENTIALLY DECLARED DISASTERS.

(a) IN GENERAL.—Section 1033(h) is amended by redesignating paragraphs (2) and (3) as paragraphs (3) and (4), respectively, and by inserting after paragraph (1) the following new paragraph:

"(2) TRADE OR BUSINESS AND INVESTMENT PROPERTY.—If a taxpayer's property held for productive use in a trade or business or for investment is compulsorily or involuntarily converted as a result of a Presidentially declared disaster, tangible property of a type held for productive use in a trade or business shall be treated for purposes of subsection (a) as property similar or related in service or use to the property so converted.".

(b) CONFORMING AMENDMENTS.—Section 1033(h) is amended—

(1) by striking "residence" in paragraph (3) (as redesignated by subsection (a)) and inserting "property",

(2) by striking "PRINCIPAL RESIDENCES" in the heading and inserting "PROPERTY", and

(3) by striking "(1) IN GENERAL.—" and inserting "(1) PRINCIPAL RESIDENCES.—".

(c) EXPANSION OF OKLAHOMA CITY ENTERPRISE COMMUNITY.—Notwithstanding sections 1391 and 1392(a)(3)(D) of the Internal Revenue Code of 1986, the boundaries of the enterprise community for Oklahoma City, Oklahoma, designated by the Secretary of Housing and Urban Development on December 21, 1994, may be extended with respect to census tracts located in the area damaged due to the bombing of the Alfred P. Murrah Federal Building in Oklahoma City on April 19, 1995, primarily in the area bounded on the south by Robert S. Kerr Avenue, on the north by North 13th Street, on the east by Oklahoma Avenue, and on the west by Shartel Avenue.

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to disasters declared after December 31, 1994, in taxable years ending after such date.

(2) SUBSECTION (c).—Subsection (c) shall take effect on the date of the enactment of this Act.

SEC. 1120. CLASS LIFE FOR GAS STATION CONVENIENCE STORES AND SIMILAR STRUCTURES.

(a) IN GENERAL.—Section 168(e)(3)(E) (classifying certain property as 15-year property) is amended by striking "and" at the end of clause (i), by striking the period at the end of clause (ii) and inserting ", and", and by adding at the end the following new clause:

"(iii) any section 1250 property which is a retail motor fuels outlet (whether or not food or other convenience items are sold at the outlet).".

(b) CONFORMING AMENDMENT.—Subparagraph (B) of section 168(g)(3) is amended by inserting after the item relating to subparagraph (E)(ii) in the table contained therein the following new item:

"(E)(iii) ..... 20".

(c)EFFECTIVE DATE.—The amendments made by this section shall apply to property which is placed in service on or after the date of the enactment of this Act and to which section 168 of the Internal Revenue Code of 1986 applies after the amendment made by section 201 of the Tax Reform Act of 1986. A taxpayer may elect (in such form and manner as the Secretary of the Treasury may prescribe) to have such amendments apply with respect to any property placed in service before such date and to which such section so applies.

SEC. 1121 TREATMENT OF ABANDONMENT OF LESSOR IMPROVEMENTS AT TERMINATION OF LEASE.

(a) IN GENERAL.—Paragraph (8) of section 168(i) is amended to read as follows:

"(8) TREATMENT OF LEASEHOLD IMPROVEMENTS.—

"(A) IN GENERAL.—In the case of any building erected (or improvements made) on leased property, if such building or improvement is property to which this section ap-

plies, the depreciation deduction shall be determined under the provisions of this section.

"(B) TREATMENT OF LESSOR IMPROVEMENTS WHICH ARE ABANDONED AT TERMINATION OF LEASE.—An improvement—

"(i) which is made by the lessor of leased property for the lessee of such property, and

"(ii) which is irrevocably disposed of or abandoned by the lessor at the termination of the lease by such lessee,

shall be treated for purposes of determining gain or loss under this title as disposed of by the lessor when so disposed of or abandoned.".

(b) EFFECTIVE DATE.—Subparagraph (B) of section 168(i)(8) of the Internal Revenue Code of 1986, as added by the amendment made by subsection (a), shall apply to improvements disposed of or abandoned after June 12, 1996.

SEC. 1122. SPECIAL RULES RELATING TO DETERMINATION WHETHER INDIVIDUALS ARE EMPLOYEES FOR PURPOSES OF EMPLOYMENT TAXES.

(a) IN GENERAL.—Section 530 of the Revenue Act of 1978 is amended by adding at the end the following new subsection:

"(e) SPECIAL RULES FOR APPLICATION OF SECTION.—

"(1) NOTICE OF AVAILABILITY OF SECTION.—An officer or employee of the Internal Revenue Service shall, before or at the commencement of any audit inquiry relating to the employment status of one or more individuals who perform services for the taxpayer, provide the taxpayer with a written notice of the provisions of this section.

"(2) RULES RELATING TO STATUTORY STANDARDS.—For purposes of subsection (a)(2)—

"(A) a taxpayer may not rely on an audit commenced after December 31, 1996, for purposes of subparagraph (B) thereof unless such audit included an examination for employment tax purposes of whether the individual involved (or any individual holding a position substantially similar to the position held by the individual involved) should be treated as an employee of the taxpayer,

"(B) in no event shall the significant segment requirement of subparagraph (C) thereof be construed to require a reasonable showing of the practice of more than 25 percent of the industry (determined by not taking into account the taxpayer), and

"(C) in applying the long-standing recognized practice requirement of subparagraph (C) thereof—

"(i) such requirement shall not be construed as requiring the practice to have continued for more than 10 years, and

"(ii) a practice shall not fail to be treated as long-standing merely because such practice began after 1978.

"(3) AVAILABILITY OF SAFE HARBORS.—Nothing in this section shall be construed to provide that subsection (a) only ap-

plies where the individual involved is otherwise an employee of the taxpayer.

"(4) BURDEN OF PROOF.—

"(A) IN GENERAL.—If—

"(i) a taxpayer establishes a prima facie case that it was reasonable not to treat an individual as an employee for purposes of this section, and

"(ii) the taxpayer has fully cooperated with reasonable requests from the Secretary of the Treasury or his delegate,

then the burden of proof with respect to such treatment shall be on the Secretary.

"(B) EXCEPTION FOR OTHER REASONABLE BASIS.—In the case of any issue involving whether the taxpayer had a reasonable basis not to treat an individual as an employee for purposes of this section, subparagraph (A) shall only apply for purposes of determining whether the taxpayer meets the requirements of subparagraph (A), (B), or (C) of subsection (a)(2).

"(5) PRESERVATION OF PRIOR PERIOD SAFE HARBOR.—If—

"(A) an individual would (but for the treatment referred to in subparagraph (B)) be deemed not to be an employee of the taxpayer under subsection (a) for any prior period, and

"(B) such individual is treated by the taxpayer as an employee for employment tax purposes for any subsequent period,

then, for purposes of applying such taxes for such prior period with respect to the taxpayer, the individual shall be deemed not to be an employee.

"(6) SUBSTANTIALLY SIMILAR POSITION.—For purposes of this section, the determination as to whether an individual holds a position substantially similar to a position held by another individual shall include consideration of the relationship between the taxpayer and such individuals.".

(b) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendment made by this section shall apply to periods after December 31, 1996.

(2) NOTICE BY INTERNAL REVENUE SERVICE.—Section 530(e)(1) of the Revenue Act of 1978 (as added by subsection (a)) shall apply to audits which commence after December 31, 1996.

(3) BURDEN OF PROOF.—

(A) IN GENERAL.—Section 530(e)(4) of the Revenue Act of 1978 (as added by subsection (a)) shall apply to disputes involving periods after December 31, 1996.

(B) NO INFERENCE.—Nothing in the amendments made by this section shall be construed to infer the proper treatment of the burden of proof with respect to disputes involving periods before January 1, 1997.

SEC. 1123. TREATMENT OF HOUSING PROVIDED TO EMPLOYEES BY ACADEMIC HEALTH CENTERS.

(a) IN GENERAL.—Paragraph (4) of section 119(d) (relating to lodging furnished by certain educational institutions to employees) is amended to read as follows:

"(4) EDUCATIONAL INSTITUTION, ETC.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'educational institution' means—

"(i) an institution described in section 170(b)(1)(A)(ii) (or an entity organized under State law and composed of public institutions so described), or

"(ii) an academic health center.

"(B) ACADEMIC HEALTH CENTER.—For purposes of subparagraph (A), the term 'academic health center' means an entity—

"(i) which is described in section 170(b)(1)(A)(iii),

"(ii) which receives (during the calendar year in which the taxable year of the taxpayer begins) payments under subsection (d)(5)(B) or (h) of section 1886 of the Social Security Act (relating to graduate medical education), and

"(iii) which has as one of its principal purposes or functions the providing and teaching of basic and clinical medical science and research with the entity's own faculty.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 1995.

Subtitle B—Extension of Certain Expiring Provisions

SEC. 1201. WORK OPPORTUNITY TAX CREDIT.

(a) AMOUNT OF CREDIT.—Subsection (a) of section 51 (relating to amount of credit) is amended by striking "40 percent" and inserting "35 percent".

(b) MEMBERS OF TARGETED GROUPS.—Subsection (d) of section 51 is amended to read as follows:

"(d) MEMBERS OF TARGETED GROUPS.—For purposes of this subpart—

"(1) IN GENERAL.—An individual is a member of a targeted group if such individual is—

"(A) a qualified IV–A recipient,

"(B) a qualified veteran,

"(C) a qualified ex-felon,

"(D) a high-risk youth,

"(E) a vocational rehabilitation referral,

"(F) a qualified summer youth employee, or

"(G) a qualified food stamp recipient.

"(2) QUALIFIED IV–A RECIPIENT.—

"(A) IN GENERAL.—The term 'qualified IV–A recipient' means any individual who is certified by the designated local agency as being a member of a family receiving assist-

ance under a IV–A program for at least a 9-month period ending during the 9-month period ending on the hiring date.

"(B) IV–A PROGRAM.—For purposes of this paragraph, the term 'IV–A program' means any program providing assistance under a State plan approved under part A of title IV of the Social Security Act (relating to assistance for needy families with minor children) and any successor of such program.

"(3) QUALIFIED VETERAN.—

"(A) IN GENERAL.—The term 'qualified veteran' means any veteran who is certified by the designated local agency as being—

"(i) a member of a family receiving assistance under a IV–A program (as defined in paragraph (2)(B)) for at least a 9-month period ending during the 12-month period ending on the hiring date, or

"(ii) a member of a family receiving assistance under a food stamp program under the Food Stamp Act of 1977 for at least a 3-month period ending during the 12-month period ending on the hiring date.

"(B) VETERAN.—For purposes of subparagraph (A), the term 'veteran' means any individual who is certified by the designated local agency as—

"(i)(I) having served on active duty (other than active duty for training) in the Armed Forces of the United States for a period of more than 180 days, or

"(II) having been discharged or released from active duty in the Armed Forces of the United States for a service-connected disability, and

"(ii) not having any day during the 60-day period ending on the hiring date which was a day of extended active duty in the Armed Forces of the United States.

For purposes of clause (ii), the term 'extended active duty' means a period of more than 90 days during which the individual was on active duty (other than active duty for training).

"(4) QUALIFIED EX-FELON.—The term 'qualified ex-felon' means any individual who is certified by the designated local agency—

"(A) as having been convicted of a felony under any statute of the United States or any State,

"(B) as having a hiring date which is not more than 1 year after the last date on which such individual was so convicted or was released from prison, and

"(C) as being a member of a family which had an income during the 6 months immediately preceding the earlier of the month in which such income determination occurs or the month in which the hiring date occurs, which, on an annual basis, would be 70 percent or less of the Bureau of Labor Statistics lower living standard.

Any determination under subparagraph (C) shall be valid for the 45-day period beginning on the date such determination is made.

"(5) HIGH-RISK YOUTH.—

"(A) IN GENERAL.—The term 'high-risk youth' means any individual who is certified by the designated local agency—

"(i) as having attained age 18 but not age 25 on the hiring date, and

"(ii) as having his principal place of abode within an empowerment zone or enterprise community.

"(B) YOUTH MUST CONTINUE TO RESIDE IN ZONE.—In the case of a high-risk youth, the term 'qualified wages' shall not include wages paid or incurred for services performed while such youth's principal place of abode is outside an empowerment zone or enterprise community.

"(6) VOCATIONAL REHABILITATION REFERRAL.—The term 'vocational rehabilitation referral' means any individual who is certified by the designated local agency as—

"(A) having a physical or mental disability which, for such individual, constitutes or results in a substantial handicap to employment, and

"(B) having been referred to the employer upon completion of (or while receiving) rehabilitative services pursuant to—

"(i) an individualized written rehabilitation plan under a State plan for vocational rehabilitation services approved under the Rehabilitation Act of 1973, or

"(ii) a program of vocational rehabilitation carried out under chapter 31 of title 38, United States Code.

"(7) QUALIFIED SUMMER YOUTH EMPLOYEE.—

"(A) IN GENERAL.—The term 'qualified summer youth employee' means any individual—

"(i) who performs services for the employer between May 1 and September 15,

"(ii) who is certified by the designated local agency as having attained age 16 but not 18 on the hiring date (or if later, on May 1 of the calendar year involved),

"(iii) who has not been an employee of the employer during any period prior to the 90-day period described in subparagraph (B)(i), and

"(iv) who is certified by the designated local agency as having his principal place of abode within an empowerment zone or enterprise community.

"(B) SPECIAL RULES FOR DETERMINING AMOUNT OF CREDIT.—For purposes of applying this subpart to wages paid or incurred to any qualified summer youth employee—

"(i) subsection (b)(2) shall be applied by substituting 'any 90-day period between May 1 and September 15' for 'the 1-year period beginning with the day the individual begins work for the employer', and

"(ii) subsection (b)(3) shall be applied by substituting '$3,000' for '$6,000'.

The preceding sentence shall not apply to an individual who, with respect to the same employer, is certified as a

member of another targeted group after such individual has been a qualified summer youth employee.

"(C) YOUTH MUST CONTINUE TO RESIDE IN ZONE.—Paragraph (5)(B) shall apply for purposes of subparagraph (A)(iv).

"(8) QUALIFIED FOOD STAMP RECIPIENT.—

"(A) IN GENERAL.—The term 'qualified food stamp recipient' means any individual who is certified by the designated local agency—

"(i) as having attained age 18 but not age 25 on the hiring date, and

"(ii) as being a member of a family—

"(I) receiving assistance under a food stamp program under the Food Stamp Act of 1977 for the 6-month period ending on the hiring date, or

"(II) receiving such assistance for at least 3 months of the 5-month period ending on the hiring date, in the case of a member of a family who ceases to be eligible for such assistance under section 6(o) of the Food Stamp Act of 1977.

"(B) PARTICIPATION INFORMATION.—Notwithstanding any other provision of law, the Secretary of the Treasury and the Secretary of Agriculture shall enter into an agreement to provide information to designated local agencies with respect to participation in the food stamp program.

"(9) HIRING DATE.—The term 'hiring date' means the day the individual is hired by the employer.

"(10) DESIGNATED LOCAL AGENCY.—The term 'designated local agency' means a State employment security agency established in accordance with the Act of June 6, 1933, as amended (29 U.S.C. 4949n).

"(11) SPECIAL RULES FOR CERTIFICATIONS.—

"(A) IN GENERAL.—An individual shall not be treated as a member of a targeted group unless—

"(i) on or before the day on which such individual begins work for the employer, the employer has received a certification from a designated local agency that such individual is a member of a targeted group, or

"(ii)(I) on or before the day the individual is offered employment with the employer, a pre-screening notice is completed by the employer with respect to such individual, and

"(II) not later than the 21st day after the individual begins work for the employer, the employer submits such notice, signed by the employer and the individual under penalties of perjury, to the designated local agency as part of a written request for such a certification from such agency.

For purposes of this paragraph, the term 'pre-screening notice' means a document (in such form as the Secretary shall prescribe) which contains information provided by the individual on the basis of which the employer believes that the individual is a member of a targeted group.

"(B) INCORRECT CERTIFICATIONS.—If—

"(i) an individual has been certified by a designated local agency as a member of a targeted group, and

"(ii) such certification is incorrect because it was based on false information provided by such individual,

the certification shall be revoked and wages paid by the employer after the date on which notice of revocation is received by the employer shall not be treated as qualified wages.

"(C) EXPLANATION OF DENIAL OF REQUEST.—If a designated local agency denies a request for certification of membership in a targeted group, such agency shall provide to the person making such request a written explanation of the reasons for such denial.".

(c) MINIMUM EMPLOYMENT PERIOD.—Paragraph (3) of section 51(i) (relating to certain individuals ineligible) is amended to read as follows:

"(3) INDIVIDUALS NOT MEETING MINIMUM EMPLOYMENT PERIOD.—No wages shall be taken into account under subsection (a) with respect to any individual unless such individual either—

"(A) is employed by the employer at least 180 days (20 days in the case of a qualified summer youth employee), or

"(B) has completed at least 400 hours (120 hours in the case of a qualified summer youth employee) of services performed for the employer.".

(d) TERMINATION.—Paragraph (4) of section 51(c) (relating to wages defined) is amended to read as follows:

"(4) TERMINATION.—The term 'wages' shall not include any amount paid or incurred to an individual who begins work for the employer—

"(A) after December 31, 1994, and before October 1, 1996, or

"(B) after September 30, 1997.".

(e) REDESIGNATION OF CREDIT.—

(1) Sections 38(b)(2), 41(b)(2)(D)(iii), 45A(b)(1)(B), 51 (a) and (g), and 196(c) are each amended in the text by striking "targeted jobs credit" each place it appears and inserting "work opportunity credit".

*(2) The subpart heading for subpart F of part IV of subchapter A of chapter 1 is amended by striking **"Targeted Jobs Credit"** and inserting **"Work Opportunity Credit"**.*

(3) The table of subparts for such part IV is amended by striking "targeted jobs credit" and inserting "work opportunity credit".

(4) The headings for sections 41(b)(2)(D)(iii) and 1396(c)(3) are each amended by striking "TARGETED JOBS CREDIT" and inserting "WORK OPPORTUNITY CREDIT".

(5) The heading for subsection (j) of section 51 is amended by striking "TARGETED JOBS CREDIT" and inserting "WORK OPPORTUNITY CREDIT".

(f) TECHNICAL AMENDMENT.—Paragraph (1) of section 51(c) is amended by striking ", subsection (d)(8)(D),".

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to individuals who begin work for the employer after September 30, 1996.

SEC. 1202. EMPLOYER-PROVIDED EDUCATIONAL ASSISTANCE PROGRAMS.

(a) EXTENSION.—Subsection (d) of section 127 (relating to educational assistance programs) is amended by striking "December 31, 1994." and inserting "May 31, 1997. In the case of any taxable year beginning in 1997, only expenses paid with respect to courses beginning before July 1, 1997, shall be taken into account in determining the amount excluded under this section.".

(b) LIMITATION TO EDUCATION BELOW GRADUATE LEVEL.—The last sentence of section 127(c)(1) is amended by inserting before the period the following: ", and such term also does not include any payment for, or the provision of any benefits with respect to, any graduate level course of a kind normally taken by an individual pursuing a program leading to a law, business, medical, or other advanced academic or professional degree".

(c) EFFECTIVE DATES.—

(1) EXTENSION.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1994.

(2) GRADUATE EDUCATION.—The amendment made by subsection (b) shall apply with respect to expenses relating to courses beginning after June 30, 1996.

(3) EXPEDITED PROCEDURES.—The Secretary of the Treasury shall establish expedited procedures for the refund of any overpayment of taxes imposed by the Internal Revenue Code of 1986 which is attributable to amounts excluded from gross income during 1995 or 1996 under section 127 of such Code, including procedures waiving the requirement that an employer obtain an employee's signature where the employer demonstrates to the satisfaction of the Secretary that any refund collected by the employer on behalf of the employee will be paid to the employee.

SEC. 1203. FUTA EXEMPTION FOR ALIEN AGRICULTURAL WORKERS.

(a) IN GENERAL.—Subparagraph (B) of section 3306(c)(1) (defining employment) is amended by striking "before January 1, 1995,".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to services performed after December 31, 1994.

SEC. 1204. RESEARCH CREDIT.

(a) IN GENERAL.—Subsection (h) of section 41 (relating to credit for research activities) is amended to read as follows:

"(h) TERMINATION.—

"(1) IN GENERAL.—This section shall not apply to any amount paid or incurred—

"(A) after June 30, 1995, and before July 1, 1996, or

"(B) after May 31, 1997.

Notwithstanding the preceding sentence, in the case of a taxpayer making an election under subsection (c)(4) for its first taxable year beginning after June 30, 1996, and before July 1, 1997, this section shall apply to amounts paid or incurred during the first 11 months of such taxable year.

"(2) COMPUTATION OF BASE AMOUNT.—In the case of any taxable year with respect to which this section applies to a number of days which is less than the total number of days in such taxable year, the base amount with respect to such taxable year shall be the amount which bears the same ratio to the base amount for such year (determined without regard to this paragraph) as the number of days in such taxable year to which this section applies bears to the total number of days in such taxable year.".

(b) BASE AMOUNT FOR START-UP COMPANIES.—Clause (i) of section 41(c)(3)(B) (relating to start-up companies) is amended to read as follows:

"(i) TAXPAYERS TO WHICH SUBPARAGRAPH APPLIES.—The fixed-base percentage shall be determined under this subparagraph if—

"(I) the first taxable year in which a taxpayer had both gross receipts and qualified research expenses begins after December 31, 1983, or

"(II) there are fewer than 3 taxable years beginning after December 31, 1983, and before January 1, 1989, in which the taxpayer had both gross receipts and qualified research expenses.".

(c) ELECTION OF ALTERNATIVE INCREMENTAL CREDIT.—Subsection (c) of section 41 is amended by redesignating paragraphs (4) and (5) as paragraphs (5) and (6), respectively, and by inserting after paragraph (3) the following new paragraph:

"(4) ELECTION OF ALTERNATIVE INCREMENTAL CREDIT.—

"(A) IN GENERAL.—At the election of the taxpayer, the credit determined under subsection (a)(1) shall be equal to the sum of—

"(i) 1.65 percent of so much of the qualified research expenses for the taxable year as exceeds 1 percent of the average described in subsection (c)(1)(B) but does not exceed 1.5 percent of such average,

"(ii) 2.2 percent of so much of such expenses as exceeds 1.5 percent of such average but does not exceed 2 percent of such average, and

"(iii) 2.75 percent of so much of such expenses as exceeds 2 percent of such average.

"(B) ELECTION.—An election under this paragraph may be made only for the first taxable year of the taxpayer beginning after June 30, 1996. Such an election shall apply to the taxable year for which made and all succeeding taxable years unless revoked with the consent of the Secretary.".

(d) INCREASED CREDIT FOR CONTRACT RESEARCH EXPENSES WITH RESPECT TO CERTAIN RESEARCH CONSORTIA.—Paragraph (3) of section 41(b) is amended by adding at the end the following new subparagraph:

"(C) AMOUNTS PAID TO CERTAIN RESEARCH CONSORTIA.—

"(i) IN GENERAL.—Subparagraph (A) shall be applied by substituting '75 percent' for '65 percent' with respect to amounts paid or incurred by the taxpayer to

a qualified research consortium for qualified research on behalf of the taxpayer and 1 or more unrelated taxpayers. For purposes of the preceding sentence, all persons treated as a single employer under subsection (a) or (b) of section 52 shall be treated as related taxpayers.

"(ii) QUALIFIED RESEARCH CONSORTIUM.—The term 'qualified research consortium' means any organization which—

"(I) is described in section 501(c)(3) or 501(c)(6) and is exempt from tax under section 501(a),

"(II) is organized and operated primarily to conduct scientific research, and

"(III) is not a private foundation.".

(e) CONFORMING AMENDMENT.—Subparagraph (D) of section 28(b)(1) is amended by inserting ", and before July 1, 1996, and periods after May 31, 1997" after "June 30, 1995".

(f) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years ending after June 30, 1996.

(2) SUBSECTIONS (c) AND (d).—The amendments made by subsections (c) and (d) shall apply to taxable years beginning after June 30, 1996.

(3) ESTIMATED TAX.—The amendments made by this section shall not be taken into account under section 6654 or 6655 of the Internal Revenue Code of 1986 (relating to failure to pay estimated tax) in determining the amount of any installment required to be paid for a taxable year beginning in 1997.

SEC. 1205. ORPHAN DRUG TAX CREDIT.

(a) RECATEGORIZED AS A BUSINESS CREDIT.—

(1) IN GENERAL.—Section 28 (relating to clinical testing expenses for certain drugs for rare diseases or conditions) is transferred to subpart D of part IV of subchapter A of chapter 1, inserted after section 45B, and redesignated as section 45C.

(2) CONFORMING AMENDMENT.—Subsection (b) of section 38 (relating to general business credit) is amended by striking "plus" at the end of paragraph (10), by striking the period at the end of paragraph (11) and inserting ", plus", and by adding at the end the following new paragraph:

"(12) the orphan drug credit determined under section 45C(a).".

(3) CLERICAL AMENDMENTS.—

(A) The table of sections for subpart B of such part IV is amended by striking the item relating to section 28.

(B) The table of sections for subpart D of such part IV is amended by adding at the end the following new item:

"Sec. 45C. Clinical testing expenses for certain drugs for rare diseases or conditions.".

(b) CREDIT TERMINATION.—Subsection (e) of section 45C, as redesignated by subsection (a)(1), is amended to read as follows:

"(e) TERMINATION.—This section shall not apply to any amount paid or incurred—

"(1) after December 31, 1994, and before July 1, 1996, or

"(2) after May 31, 1997.".

(c) NO PRE-JULY 1, 1996 CARRYBACKS.—Subsection (d) of section 39 (relating to carryback and carryforward of unused credits) is amended by adding at the end the following new paragraph:

"(7) NO CARRYBACK OF SECTION 45C CREDIT BEFORE JULY 1, 1996.—No portion of the unused business credit for any taxable year which is attributable to the orphan drug credit determined under section 45C may be carried back to a taxable year ending before July 1, 1996.".

(d) ADDITIONAL CONFORMING AMENDMENTS.—

(1) Section 45C(a), as redesignated by subsection (a)(1), is amended by striking "There shall be allowed as a credit against the tax imposed by this chapter for the taxable year" and inserting "For purposes of section 38, the credit determined under this section for the taxable year is".

(2) Section 45C(d), as so redesignated, is amended by striking paragraph (2) and by redesignating paragraphs (3), (4), and (5) as paragraphs (2), (3), and (4).

(3) Section 29(b)(6)(A) is amended by striking "sections 27 and 28" and inserting "section 27".

(4) Section 30(b)(3)(A) is amended by striking "sections 27, 28, and 29" and inserting "sections 27 and 29".

(5) Section 53(d)(1)(B) is amended—

(A) by striking "or not allowed under section 28 solely by reason of the application of section 28(d)(2)(B)," in clause (iii), and

(B) by striking "or not allowed under section 28 solely by reason of the application of section 28(d)(2)(B)" in clause (iv)(II).

(6) Section 55(c)(2) is amended by striking "28(d)(2),".

(7) Section 280C(b) is amended—

(A) by striking "section 28(b)" in paragraph (1) and inserting "section 45C(b)",

(B) by striking "section 28" in paragraphs (1) and (2)(A) and inserting "section 45C", and

(C) by striking "subsection (d)(2) thereof" in paragraphs (1) and (2)(A) and inserting "section 38(c)".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts paid or incurred in taxable years ending after June 30, 1996.

SEC. 1206. CONTRIBUTIONS OF STOCK TO PRIVATE FOUNDATIONS.

(a) IN GENERAL.—Subparagraph (D) of section 170(e)(5) (relating to special rule for contributions of stock for which market quotations are readily available) is amended to read as follows:

"(D) TERMINATION.—This paragraph shall not apply to contributions made—

"(i) after December 31, 1994, and before July 1, 1996, or

"(ii) after May 31, 1997.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to contributions made after June 30, 1996.

SEC. 1207. EXTENSION OF BINDING CONTRACT DATE FOR BIOMASS AND COAL FACILITIES.

(a) IN GENERAL.—Subparagraph (A) of section 29(g)(1) (relating to extension of certain facilities) is amended by striking "January 1, 1997" and inserting "July 1, 1998" and by striking "January 1, 1996" and inserting "January 1, 1997".

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act.

SEC. 1208. MORATORIUM FOR EXCISE TAX ON DIESEL FUEL SOLD FOR USE OR USED IN DIESEL-POWERED MOTORBOATS.

Subparagraph (D) of section 4041(a)(1) (relating to the imposition of tax on diesel fuel and special motor fuels) is amended by redesignating clauses (i) and (ii) as clauses (ii) and (iii), respectively, and by inserting before clause (ii) (as redesignated) the following new clause:

> *"(i) no tax shall be imposed by subsection (a) or (d)(1) during the period beginning on the date which is 7 days after the date of the enactment of the Small Business Job Protection Act of 1996 and ending on December 31, 1997,".*

Subtitle C—Provisions Relating to S Corporations

SEC. 1301. S CORPORATIONS PERMITTED TO HAVE 75 SHAREHOLDERS.

Subparagraph (A) of section 1361(b)(1) (defining small business corporation) is amended by striking "35 shareholders" and inserting "75 shareholders".

SEC. 1302. ELECTING SMALL BUSINESS TRUSTS.

(a) GENERAL RULE.—Subparagraph (A) of section 1361(c)(2) (relating to certain trusts permitted as shareholders) is amended by inserting after clause (iv) the following new clause:

> *"(v) An electing small business trust.".*

(b) CURRENT BENEFICIARIES TREATED AS SHAREHOLDERS.—Subparagraph (B) of section 1361(c)(2) is amended by adding at the end the following new clause:

> *"(v) In the case of a trust described in clause (v) of subparagraph (A), each potential current beneficiary of such trust shall be treated as a shareholder; except that, if for any period there is no potential current beneficiary of such trust, such trust shall be treated as the shareholder during such period.".*

(c) ELECTING SMALL BUSINESS TRUST DEFINED.—Section 1361 (defining S corporation) is amended by adding at the end the following new subsection:

"(e) ELECTING SMALL BUSINESS TRUST DEFINED.—

"(1) ELECTING SMALL BUSINESS TRUST.—For purposes of this section—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'electing small business trust' means any trust if—

"(i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, or

(III) an organization described in paragraph (2), (3), (4), or (5) of section 170(c) which holds a contingent interest and is not a potential current beneficiary,

"(ii) no interest in such trust was acquired by purchase, and

"(iii) an election under this subsection applies to such trust.

"(B) CERTAIN TRUSTS NOT ELIGIBLE.—The term 'electing small business trust' shall not include—

"(i) any qualified subchapter S trust (as defined in subsection (d)(3)) if an election under subsection (d)(2) applies to any corporation the stock of which is held by such trust, and

"(ii) any trust exempt from tax under this subtitle.

"(C) PURCHASE.—For purposes of subparagraph (A), the term 'purchase' means any acquisition if the basis of the property acquired is determined under section 1012.

"(2) POTENTIAL CURRENT BENEFICIARY.—For purposes of this section, the term 'potential current beneficiary' means, with respect to any period, any person who at any time during such period is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust. If a trust disposes of all of the stock which it holds in an S corporation, then, with respect to such corporation, the term 'potential current beneficiary' does not include any person who first met the requirements of the preceding sentence during the 60-day period ending on the date of such disposition.

"(3) ELECTION.—An election under this subsection shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent taxable years of such trust unless revoked with the consent of the Secretary.

"(4) CROSS REFERENCE.—

"For special treatment of electing small business trusts, see section 641(d).".

(d) TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—Section 641 (relating to imposition of tax on trusts) is amended by adding at the end the following new subsection:

"(d) SPECIAL RULES FOR TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—

"(1) IN GENERAL.—For purposes of this chapter—

"(A) the portion of any electing small business trust which consists of stock in 1 or more S corporations shall be treated as a separate trust, and

"(B) the amount of the tax imposed by this chapter on such separate trust shall be determined with the modifications of paragraph (2).

"(2) MODIFICATIONS.—For purposes of paragraph (1), the modifications of this paragraph are the following:

"(A) Except as provided in section 1(h), the amount of the tax imposed by section 1(e) shall be determined by using the highest rate of tax set forth in section 1(e).

"(B) The exemption amount under section 55(d) shall be zero.

"(C) The only items of income, loss, deduction, or credit to be taken into account are the following:

"(i) The items required to be taken into account under section 1366.

"(ii) Any gain or loss from the disposition of stock in an S corporation.

"(iii) To the extent provided in regulations, State or local income taxes or administrative expenses to the extent allocable to items described in clauses (i) and (ii).

No deduction or credit shall be allowed for any amount not described in this paragraph, and no item described in this paragraph shall be apportioned to any beneficiary.

"(D) No amount shall be allowed under paragraph (1) or (2) of section 1211(b).

"(3) TREATMENT OF REMAINDER OF TRUST AND DISTRIBUTIONS.—For purposes of determining—

"(A) the amount of the tax imposed by this chapter on the portion of any electing small business trust not treated as a separate trust under paragraph (1), and

"(B) the distributable net income of the entire trust,

the items referred to in paragraph (2)(C) shall be excluded. Except as provided in the preceding sentence, this subsection shall not affect the taxation of any distribution from the trust.

"(4) TREATMENT OF UNUSED DEDUCTIONS WHERE TERMINATION OF SEPARATE TRUST.—If a portion of an electing small business trust ceases to be treated as a separate trust under paragraph (1), any carryover or excess deduction of the separate trust which is referred to in section 642(h) shall be taken into account by the entire trust.

"(5) ELECTING SMALL BUSINESS TRUST.—For purposes of this subsection, the term 'electing small business trust' has the meaning given such term by section 1361(e)(1).".

(e) TECHNICAL AMENDMENT.—Paragraph (1) of section 1366(a) is amended by inserting ", or of a trust or estate which terminates," after "who dies".

SEC. 1303. EXPANSION OF POST-DEATH QUALIFICATION FOR CERTAIN TRUSTS.

Subparagraph (A) of section 1361(c)(2) (relating to certain trusts permitted as shareholders) is amended—

(1) by striking "60-day period" each place it appears in clauses (ii) and (iii) and inserting "2-year period", and

(2) by striking the last sentence in clause (ii).

SEC. 1304. FINANCIAL INSTITUTIONS PERMITTED TO HOLD SAFE HARBOR DEBT.

Clause (iii) of section 1361(c)(5)(B) (defining straight debt) is amended by striking "or a trust described in paragraph (2)" and inserting "a trust described in paragraph (2), or a person which is actively and regularly engaged in the business of lending money".

SEC. 1305. RULES RELATING TO INADVERTENT TERMINATIONS AND INVALID ELECTIONS.

(a) GENERAL RULE.—Subsection (f) of section 1362 (relating to inadvertent terminations) is amended to read as follows:

"(f) INADVERTENT INVALID ELECTIONS OR TERMINATIONS.—If—

"(1) an election under subsection (a) by any corporation—

"(A) was not effective for the taxable year for which made (determined without regard to subsection (b)(2)) by reason of a failure to meet the requirements of section 1361(b) or to obtain shareholder consents, or

"(B) was terminated under paragraph (2) or (3) of subsection (d),

"(2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent,

"(3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken—

"(A) so that the corporation is a small business corporation, or

"(B) to acquire the required shareholder consents, and

"(4) the corporation, and each person who was a shareholder in the corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period,

then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.".

(b) LATE ELECTIONS, ETC.—Subsection (b) of section 1362 is amended by adding at the end the following new paragraph:

"(5) AUTHORITY TO TREAT LATE ELECTIONS, ETC., AS TIMELY.—If—

"(A) an election under subsection (a) is made for any taxable year (determined without regard to paragraph (3)) after the date prescribed by this subsection for making such election for such taxable year or no such election is made for any taxable year, and

"(B) the Secretary determines that there was reasonable cause for the failure to timely make such election,

the Secretary may treat such an election as timely made for such taxable year (and paragraph (3) shall not apply).".

(c) EFFECTIVE DATE.—The amendments made by subsection (a) and (b) shall apply with respect to elections for taxable years beginning after December 31, 1982.

SEC. 1306. AGREEMENT TO TERMINATE YEAR.

Paragraph (2) of section 1377(a) (relating to pro rata share) is amended to read as follows:

"(2) ELECTION TO TERMINATE YEAR.—

"(A) IN GENERAL.—Under regulations prescribed by the Secretary, if any shareholder terminates the shareholder's interest in the corporation during the taxable year and all affected shareholders and the corporation agree to the application of this paragraph, paragraph (1) shall be applied to the affected shareholders as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination.

"(B) AFFECTED SHAREHOLDERS.—For purposes of subparagraph (A), the term 'affected shareholders' means the

shareholder whose interest is terminated and all shareholders to whom such shareholder has transferred shares during the taxable year. If such shareholder has transferred shares to the corporation, the term 'affected shareholders' shall include all persons who are shareholders during the taxable year.".

SEC. 1307. EXPANSION OF POST-TERMINATION TRANSITION PERIOD.

(a) IN GENERAL.—Paragraph (1) of section 1377(b) (relating to post-termination transition period) is amended by striking "and" at the end of subparagraph (A), by redesignating subparagraph (B) as subparagraph (C), and by inserting after subparagraph (A) the following new subparagraph:

"(B) the 120-day period beginning on the date of any determination pursuant to an audit of the taxpayer which follows the termination of the corporation's election and which adjusts a subchapter S item of income, loss, or deduction of the corporation arising during the S period (as defined in section 1368(e)(2)), and".

(b) DETERMINATION DEFINED.—Paragraph (2) of section 1377(b) is amended by striking subparagraphs (A) and (B), by redesignating subparagraph (C) as subparagraph (B), and by inserting before subparagraph (B) (as so redesignated) the following new subparagraph:

"(A) a determination as defined in section 1313(a), or".

(c) REPEAL OF SPECIAL AUDIT PROVISIONS FOR SUBCHAPTER S ITEMS.—

(1) GENERAL RULE.—Subchapter D of chapter 63 (relating to tax treatment of subchapter S items) is hereby repealed.

(2) CONSISTENT TREATMENT REQUIRED.—Section 6037 (relating to return of S corporation) is amended by adding at the end the following new subsection:

"(c) SHAREHOLDER'S RETURN MUST BE CONSISTENT WITH CORPORATE RETURN OR SECRETARY NOTIFIED OF INCONSISTENCY.—

"(1) IN GENERAL.—A shareholder of an S corporation shall, on such shareholder's return, treat a subchapter S item in a manner which is consistent with the treatment of such item on the corporate return.

"(2) NOTIFICATION OF INCONSISTENT TREATMENT.—

"(A) IN GENERAL.—In the case of any subchapter S item, if—

"(i)(I) the corporation has filed a return but the shareholder's treatment on his return is (or may be) inconsistent with the treatment of the item on the corporate return, or

"(II) the corporation has not filed a return, and

"(ii) the shareholder files with the Secretary a statement identifying the inconsistency,

paragraph (1) shall not apply to such item.

"(B) SHAREHOLDER RECEIVING INCORRECT INFORMATION.—A shareholder shall be treated as having complied with clause (ii) of subparagraph (A) with respect to a subchapter S item if the shareholder—

"(i) demonstrates to the satisfaction of the Secretary that the treatment of the subchapter S item on the shareholder's return is consistent with the treat-

ment of the item on the schedule furnished to the shareholder by the corporation, and

"(ii) elects to have this paragraph apply with respect to that item.

"(3) EFFECT OF FAILURE TO NOTIFY.—In any case—

"(A) described in subparagraph (A)(i)(I) of paragraph (2), and

"(B) in which the shareholder does not comply with subparagraph (A)(ii) of paragraph (2),

any adjustment required to make the treatment of the items by such shareholder consistent with the treatment of the items on the corporate return shall be treated as arising out of mathematical or clerical errors and assessed according to section 6213(b)(1). Paragraph (2) of section 6213(b) shall not apply to any assessment referred to in the preceding sentence.

"(4) SUBCHAPTER S ITEM.—For purposes of this subsection, the term 'subchapter S item' means any item of an S corporation to the extent that regulations prescribed by the Secretary provide that, for purposes of this subtitle, such item is more appropriately determined at the corporation level than at the shareholder level.

"(5) ADDITION TO TAX FOR FAILURE TO COMPLY WITH SECTION.—

"For addition to tax in the case of a shareholder's negligence in connection with, or disregard of, the requirements of this section, see part II of subchapter A of chapter 68.".

(3) CONFORMING AMENDMENTS.—

(A) Section 1366 is amended by striking subsection (g).

(B) Subsection (b) of section 6233 is amended to read as follows:

"(b) SIMILAR RULES IN CERTAIN CASES.—If a partnership return is filed for any taxable year but it is determined that there is no entity for such taxable year, to the extent provided in regulations, rules similar to the rules of subsection (a) shall apply.".

(C) The table of subchapters for chapter 63 is amended by striking the item relating to subchapter D.

SEC. 1308. S CORPORATIONS PERMITTED TO HOLD SUBSIDIARIES.

(a) IN GENERAL.—Paragraph (2) of section 1361(b) (defining ineligible corporation) is amended by striking subparagraph (A) and by redesignating subparagraphs (B), (C), (D), and (E) as subparagraphs (A), (B), (C), and (D), respectively.

(b) TREATMENT OF CERTAIN WHOLLY OWNED S CORPORATION SUBSIDIARIES.—Section 1361(b) (defining small business corporation) is amended by adding at the end the following new paragraph:

"(3) TREATMENT OF CERTAIN WHOLLY OWNED SUBSIDIARIES.—

"(A) IN GENERAL.—For purposes of this title—

"(i) a corporation which is a qualified subchapter S subsidiary shall not be treated as a separate corporation, and

"(ii) all assets, liabilities, and items of income, deduction, and credit of a qualified subchapter S subsidi-

ary shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

"(B) QUALIFIED SUBCHAPTER S SUBSIDIARY.—For purposes of this paragraph, the term 'qualified subchapter S subsidiary' means any domestic corporation which is not an ineligible corporation (as defined in paragraph (2)), if—

"(i) 100 percent of the stock of such corporation is held by the S corporation, and

"(ii) the S corporation elects to treat such corporation as a qualified subchapter S subsidiary.

"(C) TREATMENT OF TERMINATIONS OF QUALIFIED SUBCHAPTER S SUBSIDIARY STATUS.—For purposes of this title, if any corporation which was a qualified subchapter S subsidiary ceases to meet the requirements of subparagraph (B), such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the S corporation in exchange for its stock.

"(D) ELECTION AFTER TERMINATION.—If a corporation's status as a qualified subchapter S subsidiary terminates, such corporation (and any successor corporation) shall not be eligible to make—

"(i) an election under subparagraph (B)(ii) to be treated as a qualified subchapter S subsidiary, or

"(ii) an election under section 1362(a) to be treated as an S corporation,

before its 5th taxable year which begins after the 1st taxable year for which such termination was effective, unless the Secretary consents to such election.".

(c) CERTAIN DIVIDENDS NOT TREATED AS PASSIVE INVESTMENT INCOME.—Paragraph (3) of section 1362(d) is amended by adding at the end the following new subparagraph:

"(F) TREATMENT OF CERTAIN DIVIDENDS.—If an S corporation holds stock in a C corporation meeting the requirements of section 1504(a)(2), the term 'passive investment income' shall not include dividends from such C corporation to the extent such dividends are attributable to the earnings and profits of such C corporation derived from the active conduct of a trade or business.".

(d) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 1361 is amended by striking paragraph (6).

(2) Subsection (b) of section 1504 (defining includible corporation) is amended by adding at the end the following new paragraph:

"(8) An S corporation.".

SEC. 1309. TREATMENT OF DISTRIBUTIONS DURING LOSS YEARS.

(a) ADJUSTMENTS FOR DISTRIBUTIONS TAKEN INTO ACCOUNT BEFORE LOSSES.—

(1) Subparagraph (A) of section 1366(d)(1) (relating to losses and deductions cannot exceed shareholder's basis in stock and debt) is amended by striking "paragraph (1)" and inserting "paragraphs (1) and (2)(A)".

(2) Subsection (d) of section 1368 (relating to certain adjustments taken into account) is amended by adding at the end the following new sentence:

"In the case of any distribution made during any taxable year, the adjusted basis of the stock shall be determined with regard to the adjustments provided in paragraph (1) of section 1367(a) for the taxable year.".

(b) ACCUMULATED ADJUSTMENTS ACCOUNT.—Paragraph (1) of section 1368(e) (relating to accumulated adjustments account) is amended by adding at the end the following new subparagraph:

"(C) NET LOSS FOR YEAR DISREGARDED.—

"(i) IN GENERAL.—In applying this section to distributions made during any taxable year, the amount in the accumulated adjustments account as of the close of such taxable year shall be determined without regard to any net negative adjustment for such taxable year.

"(ii) NET NEGATIVE ADJUSTMENT.—For purposes of clause (i), the term 'net negative adjustment' means, with respect to any taxable year, the excess (if any) of—

"(I) the reductions in the account for the taxable year (other than for distributions), over

"(II) the increases in such account for such taxable year.".

(c) CONFORMING AMENDMENTS.—Subparagraph (A) of section 1368(e)(1) is amended—

(1) by striking "as provided in subparagraph (B)" and inserting "as otherwise provided in this paragraph", and

(2) by striking "section 1367(b)(2)(A)" and inserting "section 1367(a)(2)".

SEC. 1310. TREATMENT OF S CORPORATIONS UNDER SUBCHAPTER C.

Subsection (a) of section 1371 (relating to application of subchapter C rules) is amended to read as follows:

"(a) APPLICATION OF SUBCHAPTER C RULES.—Except as otherwise provided in this title, and except to the extent inconsistent with this subchapter, subchapter C shall apply to an S corporation and its shareholders.".

SEC. 1311. ELIMINATION OF CERTAIN EARNINGS AND PROFITS.

(a) IN GENERAL.—If—

(1) a corporation was an electing small business corporation under subchapter S of chapter 1 of the Internal Revenue Code of 1986 for any taxable year beginning before January 1, 1983, and

(2) such corporation is an S corporation under subchapter S of chapter 1 of such Code for its first taxable year beginning after December 31, 1996,

the amount of such corporation's accumulated earnings and profits (as of the beginning of such first taxable year) shall be reduced by an amount equal to the portion (if any) of such accumulated earnings and profits which were accumulated in any taxable year beginning before January 1, 1983, for which such corporation was an electing small business corporation under such subchapter S.

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (3) of section 1362(d), as amended by section 1308, is amended—

(A) by striking "SUBCHAPTER C" in the paragraph heading and inserting "ACCUMULATED",

(B) by striking "subchapter C" in subparagraph (A)(i)(I) and inserting "accumulated", and

(C) by striking subparagraph (B) and redesignating the following subparagraphs accordingly.

(2)(A) Subsection (a) of section 1375 is amended by striking "subchapter C" in paragraph (1) and inserting "accumulated".

(B) Paragraph (3) of section 1375(b) is amended to read as follows:

"(3) PASSIVE INVESTMENT INCOME, ETC.—The terms 'passive investment income' and 'gross receipts' have the same respective meanings as when used in paragraph (3) of section 1362(d).".

*(C) The section heading for section 1375 is amended by striking "**SUBCHAPTER C**" and inserting "**ACCUMULATED**".*

(D) The table of sections for part III of subchapter S of chapter 1 is amended by striking "subchapter C" in the item relating to section 1375 and inserting "accumulated".

(3) Clause (i) of section 1042(c)(4)(A) is amended by striking "section 1362(d)(3)(D)" and inserting "section 1362(d)(3)(C)".

SEC. 1312. CARRYOVER OF DISALLOWED LOSSES AND DEDUCTIONS UNDER AT-RISK RULES ALLOWED.

Paragraph (3) of section 1366(d) (relating to carryover of disallowed losses and deductions to post-termination transition period) is amended by adding at the end the following new subparagraph:

"(D) AT-RISK LIMITATIONS.—To the extent that any increase in adjusted basis described in subparagraph (B) would have increased the shareholder's amount at risk under section 465 if such increase had occurred on the day preceding the commencement of the post-termination transition period, rules similar to the rules described in subparagraphs (A) through (C) shall apply to any losses disallowed by reason of section 465(a).".

SEC. 1313. ADJUSTMENTS TO BASIS OF INHERITED S STOCK TO REFLECT CERTAIN ITEMS OF INCOME.

(a) IN GENERAL.—Subsection (b) of section 1367 (relating to adjustments to basis of stock of shareholders, etc.) is amended by adding at the end the following new paragraph:

"(4) ADJUSTMENTS IN CASE OF INHERITED STOCK.—

"(A) IN GENERAL.—If any person acquires stock in an S corporation by reason of the death of a decedent or by bequest, devise, or inheritance, section 691 shall be applied with respect to any item of income of the S corporation in the same manner as if the decedent had held directly his pro rata share of such item.

"(B) ADJUSTMENTS TO BASIS.—The basis determined under section 1014 of any stock in an S corporation shall be reduced by the portion of the value of the stock which is attributable to items constituting income in respect of the decedent.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply in the case of decedents dying after the date of the enactment of this Act.

SEC. 1314. S CORPORATIONS ELIGIBLE FOR RULES APPLICABLE TO REAL PROPERTY SUBDIVIDED FOR SALE BY NONCORPORATE TAXPAYERS.

(a) IN GENERAL.—Subsection (a) of section 1237 (relating to real property subdivided for sale) is amended by striking "other than a corporation" in the material preceding paragraph (1) and inserting "other than a C corporation".

(b) CONFORMING AMENDMENT.—Subparagraph (A) of section 1237(a)(2) is amended by inserting "an S corporation which included the taxpayer as a shareholder," after "controlled by the taxpayer,".

SEC. 1315. FINANCIAL INSTITUTIONS.

Subparagraph (A) of section 1361(b)(2) (defining ineligible corporation), as redesignated by section 1308(a), is amended to read as follows:

> *"(A) a financial institution which uses the reserve method of accounting for bad debts described in section 585,".*

SEC. 1316. CERTAIN EXEMPT ORGANIZATIONS ALLOWED TO BE SHAREHOLDERS.

(a) ELIGIBILITY TO BE SHAREHOLDERS.—

(1) IN GENERAL.—Subparagraph (B) of section 1361(b)(1) (defining small business corporation) is amended to read as follows:

> *"(B) have as a shareholder a person (other than an estate, a trust described in subsection (c)(2), or an organization described in subsection (c)(7)) who is not an individual,".*

(2) ELIGIBLE EXEMPT ORGANIZATIONS.—Section 1361(c) (relating to special rules for applying subsection (b)) is amended by adding at the end the following new paragraph:

"(7) CERTAIN EXEMPT ORGANIZATIONS PERMITTED AS SHAREHOLDERS.—For purposes of subsection (b)(1)(B), an organization which is—

> *"(A) described in section 401(a) or 501(c)(3), and*
>
> *"(B) exempt from taxation under section 501(a),*

may be a shareholder in an S corporation.".

(b) CONTRIBUTIONS OF S CORPORATION STOCK.—Section 170(e)(1) (relating to certain contributions of ordinary income and capital gain property) is amended by adding at the end the following new sentence: "For purposes of applying this paragraph in the case of a charitable contribution of stock in an S corporation, rules similar to the rules of section 751 shall apply in determining whether gain on such stock would have been long-term capital gain if such stock were sold by the taxpayer.".

(c) TREATMENT OF INCOME.—Section 512 (relating to unrelated business taxable income), as amended by section 1113, is amended by adding at the end the following new subsection:

"(e) SPECIAL RULES APPLICABLE TO S CORPORATIONS.—

"(1) IN GENERAL.—If an organization described in section 1361(c)(7) holds stock in an S corporation—

"(A) such interest shall be treated as an interest in an unrelated trade or business; and

"(B) notwithstanding any other provision of this part—

"(i) all items of income, loss, or deduction taken into account under section 1366(a), and

"(ii) any gain or loss on the disposition of the stock in the S corporation

shall be taken into account in computing the unrelated business taxable income of such organization.

"(2) BASIS REDUCTION.—Except as provided in regulations, for purposes of paragraph (1), the basis of any stock acquired by purchase (within the meaning of section 1012) shall be reduced by the amount of any dividends received by the organization with respect to the stock.".

(d) CERTAIN BENEFITS NOT APPLICABLE TO S CORPORATIONS.—

(1) CONTRIBUTION TO ESOPS.—Paragraph (9) of section 404(a) (relating to certain contributions to employee ownership plans) is amended by inserting at the end the following new subparagraph:

"(C) S CORPORATIONS.—This paragraph shall not apply to an S corporation.".

(2) DIVIDENDS ON EMPLOYER SECURITIES.—Paragraph (1) of section 404(k) (relating to deduction for dividends on certain employer securities) is amended by striking "a corporation" and inserting "a C corporation".

(3) EXCHANGE TREATMENT.—Subparagraph (A) of section 1042(c)(1) (defining qualified securities) is amended by striking "domestic corporation" and inserting "domestic C corporation".

(e) CONFORMING AMENDMENT.—Clause (i) of section 1361(e)(1)(A), as added by section 1302, is amended by striking "which holds a contingent interest and is not a potential current beneficiary".

(f) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1997.

SEC. 1317. EFFECTIVE DATE.

(a) IN GENERAL.—Except as otherwise provided in this subtitle, the amendments made by this subtitle shall apply to taxable years beginning after December 31, 1996.

(b) TREATMENT OF CERTAIN ELECTIONS UNDER PRIOR LAW.—For purposes of section 1362(g) of the Internal Revenue Code of 1986 (relating to election after termination), any termination under section 1362(d) of such Code in a taxable year beginning before January 1, 1997, shall not be taken into account.

Subtitle D—Pension Simplification

CHAPTER 1—SIMPLIFIED DISTRIBUTION RULES

SEC. 1401. REPEAL OF 5-YEAR INCOME AVERAGING FOR LUMP-SUM DISTRIBUTIONS.

(a) IN GENERAL.—Subsection (d) of section 402 (relating to taxability of beneficiary of employees' trust) is amended to read as follows:

"(d) TAXABILITY OF BENEFICIARY OF CERTAIN FOREIGN SITUS TRUSTS.—For purposes of subsections (a), (b), and (c), a stock bonus, pension, or profit-sharing trust which would qualify for exemption from tax under section 501(a) except for the fact that it is a trust created or organized outside the United States shall be treated as if it were a trust exempt from tax under section 501(a).".

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (D) of section 402(e)(4) (relating to other rules applicable to exempt trusts) is amended to read as follows:

"(D) LUMP-SUM DISTRIBUTION.—For purposes of this paragraph—

"(i) IN GENERAL.—The term 'lump sum distribution' means the distribution or payment within one taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient—

"(I) on account of the employee's death,

"(II) after the employee attains age 59½,

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

"(IV) after the employee has become disabled (within the meaning of section 72(m)(7)),

from a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501 or from a plan described in section 403(a). Subclause (III) of this clause shall be applied only with respect to an individual who is an employee without regard to section 401(c)(1), and subclause (IV) shall be applied only with respect to an employee within the meaning of section 401(c)(1). For purposes of this clause, a distribution to two or more trusts shall be treated as a distribution to one recipient. For purposes of this paragraph, the balance to the credit of the employee does not include the accumulated deductible employee contributions under the plan (within the meaning of section 72(o)(5)).

"(ii) AGGREGATION OF CERTAIN TRUSTS AND PLANS.—For purposes of determining the balance to the credit of an employee under clause (i)—

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

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

"(iii) COMMUNITY PROPERTY LAWS.—The provisions of this paragraph shall be applied without regard to community property laws.

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

"(v) BALANCE TO CREDIT OF EMPLOYEE NOT TO INCLUDE AMOUNTS PAYABLE UNDER QUALIFIED DOMESTIC RELATIONS ORDER.—For purposes of this paragraph, the balance to the credit of an employee shall not include any amount payable to an alternate payee under a qualified domestic relations order (within the meaning of section 414(p)).

"(vi) TRANSFERS TO COST-OF-LIVING ARRANGEMENT NOT TREATED AS DISTRIBUTION.—For purposes of this paragraph, the balance to the credit of an employee under a defined contribution plan shall not include any amount transferred from such defined contribution plan to a qualified cost-of-living arrangement (within the meaning of section 415(k)(2)) under a defined benefit plan.

"(vii) LUMP-SUM DISTRIBUTIONS OF ALTERNATE PAYEES.—If any distribution or payment of the balance to the credit of an employee would be treated as a lump-sum distribution, then, for purposes of this paragraph, the payment under a qualified domestic relations order (within the meaning of section 414(p)) of the balance to the credit of an alternate payee who is the spouse or former spouse of the employee shall be treated as a lump-sum distribution. For purposes of this clause, the balance to the credit of the alternate payee shall not include any amount payable to the employee.".

(2) Section 402(c) (relating to rules applicable to rollovers from exempt trusts) is amended by striking paragraph (10).

(3) Paragraph (1) of section 55(c) (defining regular tax) is amended by striking "shall not include any tax imposed by section 402(d) and".

(4) Paragraph (8) of section 62(a) (relating to certain portion of lump-sum distributions from pension plans taxed under section 402(d)) is hereby repealed.

(5) Section 401(a)(28)(B) (relating to coordination with distribution rules) is amended by striking clause (v).

(6) Subparagraph (B)(ii) of section 401(k)(10) (relating to distributions that must be lump-sum distributions) is amended to read as follows:

"(ii) LUMP-SUM DISTRIBUTION.—For purposes of this subparagraph, the term 'lump-sum distribution' has the meaning given such term by section

402(e)(4)(D) (without regard to subclauses (I), (II), (III), and (IV) of clause (i) thereof).".

(7) Section 406(c) (relating to termination of status as deemed employee not to be treated as separation from service for purposes of limitation of tax) is hereby repealed.

(8) Section 407(c) (relating to termination of status as deemed employee not to be treated as separation from service for purposes of limitation of tax) is hereby repealed.

(9) Section 691(c) (relating to deduction for estate tax) is amended by striking paragraph (5).

(10) Paragraph (1) of section 871(b) (relating to imposition of tax) is amended by striking "section 1, 55, or 402(d)(1)" and inserting "section 1 or 55".

(11) Subsection (b) of section 877 (relating to alternative tax) is amended by striking "section 1, 55, or 402(d)(1)" and inserting "section 1 or 55".

(12) Section 4980A(c)(4) is amended—

(A) by striking "to which an election under section 402(d)(4)(B) applies" and inserting "(as defined in section 402(e)(4)(D)) with respect to which the individual elects to have this paragraph apply",

(B) by adding at the end the following new flush sentence:

"An individual may elect to have this paragraph apply to only one lump-sum distribution.", and

(C) by striking the heading and inserting:

"(4) SPECIAL ONE-TIME ELECTION.—".

(13) Section 402(e) is amended by striking paragraph (5).

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1999.

(2) RETENTION OF CERTAIN TRANSITION RULES.—The amendments made by this section shall not apply to any distribution for which the taxpayer is eligible to elect the benefits of section 1122 (h)(3) or (h)(5) of the Tax Reform Act of 1986. Notwithstanding the preceding sentence, individuals who elect such benefits after December 31, 1999, shall not be eligible for 5-year averaging under section 402(d) of the Internal Revenue Code of 1986 (as in effect immediately before such amendments).

SEC. 1402. REPEAL OF $5,000 EXCLUSION OF EMPLOYEES' DEATH BENEFITS.

(a) IN GENERAL.—Subsection (b) of section 101 is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 101 is amended by striking "subsection (a) or (b)" and inserting "subsection (a)".

(2) Sections 406(e) and 407(e) are each amended by striking paragraph (2) and by redesignating paragraph (3) as paragraph (2).

(3) Section 7701(a)(20) is amended by striking ", for the purpose of applying the provisions of section 101(b) with respect to employees' death benefits".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to decedents dying after the date of the enactment of this Act.

SEC. 1403. SIMPLIFIED METHOD FOR TAXING ANNUITY DISTRIBUTIONS UNDER CERTAIN EMPLOYER PLANS.

(a) GENERAL RULE.—Subsection (d) of section 72 (relating to annuities; certain proceeds of endowment and life insurance contracts) is amended to read as follows:

"(d) SPECIAL RULES FOR QUALIFIED EMPLOYER RETIREMENT PLANS.—

"(1) SIMPLIFIED METHOD OF TAXING ANNUITY PAYMENTS.—

"(A) IN GENERAL.—In the case of any amount received as an annuity under a qualified employer retirement plan—

"(i) subsection (b) shall not apply, and

"(ii) the investment in the contract shall be recovered as provided in this paragraph.

"(B) METHOD OF RECOVERING INVESTMENT IN CONTRACT.—

"(i) IN GENERAL.—Gross income shall not include so much of any monthly annuity payment under a qualified employer retirement plan as does not exceed the amount obtained by dividing—

"(I) the investment in the contract (as of the annuity starting date), by

"(II) the number of anticipated payments determined under the table contained in clause (iii) (or, in the case of a contract to which subsection (c)(3)(B) applies, the number of monthly annuity payments under such contract).

"(ii) CERTAIN RULES MADE APPLICABLE.—Rules similar to the rules of paragraphs (2) and (3) of subsection (b) shall apply for purposes of this paragraph.

"(iii) NUMBER OF ANTICIPATED PAYMENTS.—

"If the age of the primary annuitant on the annuity starting date is:	*The number of anticipated payments is:*
Not more than 55	*360*
More than 55 but not more than 60	*310*
More than 60 but not more than 65	*260*
More than 65 but not more than 70	*210*
More than 70	*160.*

"(C) ADJUSTMENT FOR REFUND FEATURE NOT APPLICABLE.—For purposes of this paragraph, investment in the contract shall be determined under subsection (c)(1) without regard to subsection (c)(2).

"(D) SPECIAL RULE WHERE LUMP SUM PAID IN CONNECTION WITH COMMENCEMENT OF ANNUITY PAYMENTS.—If, in connection with the commencement of annuity payments under any qualified employer retirement plan, the taxpayer receives a lump sum payment—

"(i) such payment shall be taxable under subsection (e) as if received before the annuity starting date, and

"(ii) the investment in the contract for purposes of this paragraph shall be determined as if such payment had been so received.

"(E) EXCEPTION.—This paragraph shall not apply in any case where the primary annuitant has attained age 75 on the annuity starting date unless there are fewer than 5 years of guaranteed payments under the annuity.

"(F) ADJUSTMENT WHERE ANNUITY PAYMENTS NOT ON MONTHLY BASIS.—In any case where the annuity payments are not made on a monthly basis, appropriate adjustments in the application of this paragraph shall be made to take into account the period on the basis of which such payments are made.

"(G) QUALIFIED EMPLOYER RETIREMENT PLAN.—For purposes of this paragraph, the term 'qualified employer retirement plan' means any plan or contract described in paragraph (1), (2), or (3) of section 4974(c).

"(2) TREATMENT OF EMPLOYEE CONTRIBUTIONS UNDER DEFINED CONTRIBUTION PLANS.—For purposes of this section, employee contributions (and any income allocable thereto) under a defined contribution plan may be treated as a separate contract.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply in cases where the annuity starting date is after the 90th day after the date of the enactment of this Act.

SEC. 1404. REQUIRED DISTRIBUTIONS.

(a) IN GENERAL.—Section 401(a)(9)(C) (defining required beginning date) is amended to read as follows:

"(C) REQUIRED BEGINNING DATE.—For purposes of this paragraph—

"(i) IN GENERAL.—The term 'required beginning date' means April 1 of the calendar year following the later of—

"(I) the calendar year in which the employee attains age 70½, or

"(II) the calendar year in which the employee retires.

"(ii) EXCEPTION.—Subclause (II) of clause (i) shall not apply—

"(I) except as provided in section 409(d), in the case of an employee who is a 5-percent owner (as defined in section 416) with respect to the plan year ending in the calendar year in which the employee attains age 70½, or

"(II) for purposes of section 408 (a)(6) or (b)(3).

"(iii) ACTUARIAL ADJUSTMENT.—In the case of an employee to whom clause (i)(II) applies who retires in a calendar year after the calendar year in which the employee attains age 70½, the employee's accrued benefit shall be actuarially increased to take into account the period after age 70½ in which the employee was not receiving any benefits under the plan.

"(iv) EXCEPTION FOR GOVERNMENTAL AND CHURCH PLANS.—Clauses (ii) and (iii) shall not apply in the

case of a governmental plan or church plan. For purposes of this clause, the term 'church plan' means a plan maintained by a church for church employees, and the term 'church' means any church (as defined in section 3121(w)(3)(A)) or qualified church-controlled organization (as defined in section 3121(w)(3)(B)).".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to years beginning after December 31, 1996.

CHAPTER 2—INCREASED ACCESS TO RETIREMENT PLANS

Subchapter A—Simple Savings Plans

SEC. 1421. ESTABLISHMENT OF SAVINGS INCENTIVE MATCH PLANS FOR EMPLOYEES OF SMALL EMPLOYERS.

(a) IN GENERAL.—Section 408 (relating to individual retirement accounts) is amended by redesignating subsection (p) as subsection (q) and by inserting after subsection (o) the following new subsection:

"(p) SIMPLE RETIREMENT ACCOUNTS.—

"(1) IN GENERAL.—For purposes of this title, the term 'simple retirement account' means an individual retirement plan (as defined in section 7701(a)(37))—

"(A) with respect to which the requirements of paragraphs (3), (4), and (5) are met; and

"(B) with respect to which the only contributions allowed are contributions under a qualified salary reduction arrangement.

"(2) QUALIFIED SALARY REDUCTION ARRANGEMENT.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'qualified salary reduction arrangement' means a written arrangement of an eligible employer under which—

"(i) an employee eligible to participate in the arrangement may elect to have the employer make payments—

"(I) as elective employer contributions to a simple retirement account on behalf of the employee, or

"(II) to the employee directly in cash,

"(ii) the amount which an employee may elect under clause (i) for any year is required to be expressed as a percentage of compensation and may not exceed a total of $6,000 for any year,

"(iii) the employer is required to make a matching contribution to the simple retirement account for any year in an amount equal to so much of the amount the employee elects under clause (i)(I) as does not exceed the applicable percentage of compensation for the year, and

"(iv) no contributions may be made other than contributions described in clause (i) or (iii).

"(B) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—

"(i) IN GENERAL.—An employer shall be treated as meeting the requirements of subparagraph (A)(iii) for any year if, in lieu of the contributions described in such clause, the employer elects to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 60-day period for such year under paragraph (5)(C).

"(ii) COMPENSATION LIMITATION.—The compensation taken into account under clause (i) for any year shall not exceed the limitation in effect for such year under section 401(a)(17).

"(C) DEFINITIONS.—For purposes of this subsection—

"(i) ELIGIBLE EMPLOYER.—

"(I) IN GENERAL.—The term 'eligible employer' means, with respect to any year, an employer which had no more than 100 employees who received at least $5,000 of compensation from the employer for the preceding year.

"(II) 2-YEAR GRACE PERIOD.—An eligible employer who establishes and maintains a plan under this subsection for 1 or more years and who fails to be an eligible employer for any subsequent year shall be treated as an eligible employer for the 2 years following the last year the employer was an eligible employer. If such failure is due to any acquisition, disposition, or similar transaction involving an eligible employer, the preceding sentence shall apply only in accordance with rules similar to the rules of section 410(b)(6)(C)(i).

"(ii) APPLICABLE PERCENTAGE.—

"(I) IN GENERAL.—The term 'applicable percentage' means 3 percent.

"(II) ELECTION OF LOWER PERCENTAGE.—An employer may elect to apply a lower percentage (not less than 1 percent) for any year for all employees eligible to participate in the plan for such year if the employer notifies the employees of such lower percentage within a reasonable period of time before the 60-day election period for such year under paragraph (5)(C). An employer may not elect a lower percentage under this subclause for any year if that election would result in the applicable percentage being lower than 3 percent in more than 2 of the years in the 5-year period ending with such year.

"(III) SPECIAL RULE FOR YEARS ARRANGEMENT NOT IN EFFECT.—If any year in the 5-year period described in subclause (II) is a year prior to the first year for which any qualified salary reduction

arrangement is in effect with respect to the employer (or any predecessor), the employer shall be treated as if the level of the employer matching contribution was at 3 percent of compensation for such prior year.

"(D) ARRANGEMENT MAY BE ONLY PLAN OF EMPLOYER.—

"(i) IN GENERAL.—An arrangement shall not be treated as a qualified salary reduction arrangement for any year if the employer (or any predecessor employer) maintained a qualified plan with respect to which contributions were made, or benefits were accrued, for service in any year in the period beginning with the year such arrangement became effective and ending with the year for which the determination is being made.

"(ii) QUALIFIED PLAN.—For purposes of this subparagraph, the term 'qualified plan' means a plan, contract, pension, or trust described in subparagraph (A) or (B) of section 219(g)(5).

"(E) COST-OF-LIVING ADJUSTMENT.—The Secretary shall adjust the $6,000 amount under subparagraph (A)(ii) at the same time and in the same manner as under section 415(d), except that the base period taken into account shall be the calendar quarter ending September 30, 1996, and any increase under this subparagraph which is not a multiple of $500 shall be rounded to the next lower multiple of $500.

"(3) VESTING REQUIREMENTS.—The requirements of this paragraph are met with respect to a simple retirement account if the employee's rights to any contribution to the simple retirement account are nonforfeitable. For purposes of this paragraph, rules similar to the rules of subsection (k)(4) shall apply.

"(4) PARTICIPATION REQUIREMENTS.—

"(A) IN GENERAL.—The requirements of this paragraph are met with respect to any simple retirement account for a year only if, under the qualified salary reduction arrangement, all employees of the employer who—

"(i) received at least $5,000 in compensation from the employer during any 2 preceding years, and

"(ii) are reasonably expected to receive at least $5,000 in compensation during the year,

are eligible to make the election under paragraph (2)(A)(i) or receive the nonelective contribution described in paragraph (2)(B).

"(B) EXCLUDABLE EMPLOYEES.—An employer may elect to exclude from the requirement under subparagraph (A) employees described in section 410(b)(3).

"(5) ADMINISTRATIVE REQUIREMENTS.—The requirements of this paragraph are met with respect to any simplified retirement account if, under the qualified salary reduction arrangement—

"(A) an employer must—

"(i) make the elective employer contributions under paragraph (2)(A)(i) not later than the close of the 30-day period following the last day of the month with respect to which the contributions are to be made, and

"(ii) make the matching contributions under paragraph (2)(A)(iii) or the nonelective contributions under paragraph (2)(B) not later than the date described in section 404(m)(2)(B),

"(B) an employee may elect to terminate participation in such arrangement at any time during the year, except that if an employee so terminates, the arrangement may provide that the employee may not elect to resume participation until the beginning of the next year, and

"(C) each employee eligible to participate may elect, during the 60-day period before the beginning of any year (and the 60-day period before the first day such employee is eligible to participate), to participate in the arrangement, or to modify the amounts subject to such arrangement, for such year.

"(6) DEFINITIONS.—For purposes of this subsection—

"(A) COMPENSATION.—

"(i) IN GENERAL.—The term 'compensation' means amounts described in paragraphs (3) and (8) of section 6051(a).

"(ii) SELF-EMPLOYED.—In the case of an employee described in subparagraph (B), the term 'compensation' means net earnings from self-employment determined under section 1402(a) without regard to any contribution under this subsection.

"(B) EMPLOYEE.—The term 'employee' includes an employee as defined in section 401(c)(1).

"(C) YEAR.—The term 'year' means the calendar year.

"(7) USE OF DESIGNATED FINANCIAL INSTITUTION.—A plan shall not be treated as failing to satisfy the requirements of this subsection or any other provision of this title merely because the employer makes all contributions to the individual retirement accounts or annuities of a designated trustee or issuer. The preceding sentence shall not apply unless each plan participant is notified in writing (either separately or as part of the notice under subsection (l)(2)(C)) that the participant's balance may be transferred without cost or penalty to another individual account or annuity in accordance with subsection (d)(3)(G).".

(b) TAX TREATMENT OF SIMPLE RETIREMENT ACCOUNTS.—

(1) DEDUCTIBILITY OF CONTRIBUTIONS BY EMPLOYEES.—

(A) Section 219(b) (relating to maximum amount of deduction) is amended by adding at the end the following new paragraph:

"(4) SPECIAL RULE FOR SIMPLE RETIREMENT ACCOUNTS.—This section shall not apply with respect to any amount contributed to a simple retirement account established under section 408(p).".

(B) Section 219(g)(5)(A) (defining active participant) is amended by striking "or" at the end of clause (iv) and by adding at the end the following new clause:

"(vi) any simple retirement account (within the meaning of section 408(p)), or".

(2) DEDUCTIBILITY OF EMPLOYER CONTRIBUTIONS.—Section 404 (relating to deductions for contributions of an employer to pension, etc. plans) is amended by adding at the end the following new subsection:

"(m) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—

"(1) IN GENERAL.—Employer contributions to a simple retirement account shall be treated as if they are made to a plan subject to the requirements of this section.

"(2) TIMING.—

"(A) DEDUCTION.—Contributions described in paragraph (1) shall be deductible in the taxable year of the employer with or within which the calendar year for which the contributions were made ends.

"(B) CONTRIBUTIONS AFTER END OF YEAR.—For purposes of this subsection, contributions shall be treated as made for a taxable year if they are made on account of the taxable year and are made not later than the time prescribed by law for filing the return for the taxable year (including extensions thereof).".

(3) CONTRIBUTIONS AND DISTRIBUTIONS.—

(A) Section 402 (relating to taxability of beneficiary of employees' trust) is amended by adding at the end the following new subsection:

"(k) TREATMENT OF SIMPLE RETIREMENT ACCOUNTS.—Rules similar to the rules of paragraphs (1) and (3) of subsection (h) shall apply to contributions and distributions with respect to a simple retirement account under section 408(p).".

(B) Section 408(d)(3) is amended by adding at the end the following new subparagraph:

"(G) SIMPLE RETIREMENT ACCOUNTS.—This paragraph shall not apply to any amount paid or distributed out of a simple retirement account (as defined in subsection (p)) unless—

"(i) it is paid into another simple retirement account, or

"(ii) in the case of any payment or distribution to which section 72(t)(6) does not apply, it is paid into an individual retirement plan.".

(C) Clause (i) of section 457(c)(2)(B) is amended by striking "section 402(h)(1)(B)" and inserting "section 402(h)(1)(B) or (k)".

(4) PENALTIES.—

(A) EARLY WITHDRAWALS.—Section 72(t) (relating to additional tax in early distributions) is amended by adding at the end the following new paragraph:

"(6) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—In the case of any amount received from a simple retirement account (within the meaning of section 408(p)) during the 2-year period beginning on the date such individual first participated in any qualified salary reduction arrangement maintained by the individual's employer under section 408(p)(2), paragraph (1) shall be applied by substituting '25 percent' for '10 percent'.".

(B) FAILURE TO REPORT.—Section 6693 is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

"(c) PENALTIES RELATING TO SIMPLE RETIREMENT ACCOUNTS.—

"(1) EMPLOYER PENALTIES.—An employer who fails to provide 1 or more notices required by section 408(l)(2)(C) shall pay a penalty of $50 for each day on which such failures continue.

"(2) TRUSTEE PENALTIES.—A trustee who fails—

"(A) to provide 1 or more statements required by the last sentence of section 408(i) shall pay a penalty of $50 for each day on which such failures continue, or

"(B) to provide 1 or more summary descriptions required by section 408(l)(2)(B) shall pay a penalty of $50 for each day on which such failures continue.

"(3) REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed under this subsection with respect to any failure which the taxpayer shows was due to reasonable cause.".

(5) REPORTING REQUIREMENTS.—

(A) Section 408(l) is amended by adding at the end the following new paragraph:

"(2) SIMPLE RETIREMENT ACCOUNTS.—

"(A) NO EMPLOYER REPORTS.—Except as provided in this paragraph, no report shall be required under this section by an employer maintaining a qualified salary reduction arrangement under subsection (p).

"(B) SUMMARY DESCRIPTION.—The trustee of any simple retirement account established pursuant to a qualified salary reduction arrangement under subsection (p) shall provide to the employer maintaining the arrangement, each year a description containing the following information:

"(i) The name and address of the employer and the trustee.

"(ii) The requirements for eligibility for participation.

"(iii) The benefits provided with respect to the arrangement.

"(iv) The time and method of making elections with respect to the arrangement.

"(v) The procedures for, and effects of, withdrawals (including rollovers) from the arrangement.

"(C) EMPLOYEE NOTIFICATION.—The employer shall notify each employee immediately before the period for which an election described in subsection (p)(5)(C) may be made of the employee's opportunity to make such election. Such notice shall include a copy of the description described in subparagraph (B).".

(B) Section 408(l) is amended by striking "An employer" and inserting the following:

"(1) IN GENERAL.—An employer".

(6) REPORTING REQUIREMENTS.—Section 408(i) is amended by adding at the end the following new flush sentence:

"In the case of a simple retirement account under subsection (p), only one report under this subsection shall be required to be submitted each calendar year to the Secretary (at the time provided under

paragraph (2)) but, in addition to the report under this subsection, there shall be furnished, within 30 days after each calendar year, to the individual on whose behalf the account is maintained a statement with respect to the account balance as of the close of, and the account activity during, such calendar year.".

(7) EXEMPTION FROM TOP-HEAVY PLAN RULES.—Section 416(g)(4) (relating to special rules for top-heavy plans) is amended by adding at the end the following new subparagraph:

"(G) SIMPLE RETIREMENT ACCOUNTS.—The term 'top-heavy plan' shall not include a simple retirement account under section 408(p).".

(8) EMPLOYMENT TAXES.—

(A) Paragraph (5) of section 3121(a) is amended by striking "or" at the end of subparagraph (F), by inserting "or" at the end of subparagraph (G), and by adding at the end the following new subparagraph:

"(H) under an arrangement to which section 408(p) applies, other than any elective contributions under paragraph (2)(A)(i) thereof,".

(B) Section 209(a)(4) of the Social Security Act is amended by inserting "; or (J) under an arrangement to which section 408(p) of such Code applies, other than any elective contributions under paragraph (2)(A)(i) thereof" before the semicolon at the end thereof.

(C) Paragraph (5) of section 3306(b) is amended by striking "or" at the end of subparagraph (F), by inserting "or" at the end of subparagraph (G), and by adding at the end the following new subparagraph:

"(H) under an arrangement to which section 408(p) applies, other than any elective contributions under paragraph (2)(A)(i) thereof,".

(D) Paragraph (12) of section 3401(a) is amended by adding the following new subparagraph:

"(D) under an arrangement to which section 408(p) applies; or".

(9) CONFORMING AMENDMENTS.—

(A) Section 280G(b)(6) is amended by striking "or" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", or" and by adding after subparagraph (C) the following new subparagraph:

"(D) a simple retirement account described in section 408(p).".

(B) Section 402(g)(3) is amended by striking "and" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", and", and by adding after subparagraph (C) the following new subparagraph:

"(D) any elective employer contribution under section 408(p)(2)(A)(i).".

(C) Subsections (b), (c), (m)(4)(B), and (n)(3)(B) of section 414 are each amended by inserting "408(p)," after "408(k),".

(D) Section 4972(d)(1)(A) is amended by striking "and" at the end of clause (ii), by striking the period at the end

of clause (iii) and inserting ", and", and by adding after clause (iii) the following new clause:

"(iv) any simple retirement account (within the meaning of section 408(p)).".

(c) REPEAL OF SALARY REDUCTION SIMPLIFIED EMPLOYEE PENSIONS.—Section 408(k)(6) is amended by adding at the end the following new subparagraph:

"(H) TERMINATION.—This paragraph shall not apply to years beginning after December 31, 1996. The preceding sentence shall not apply to a simplified employee pension if the terms of such pension, as in effect on December 31, 1996, provide that an employee may make the election described in subparagraph (A).".

(d) MODIFICATIONS OF ERISA.—

(1) REPORTING REQUIREMENTS.—Section 101 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1021) is amended by redesignating subsection (g) as subsection (h) and by inserting after subsection (f) the following new subsection:

"(g) SIMPLE RETIREMENT ACCOUNTS.—

"(1) NO EMPLOYER REPORTS.—Except as provided in this subsection, no report shall be required under this section by an employer maintaining a qualified salary reduction arrangement under section 408(p) of the Internal Revenue Code of 1986.

"(2) SUMMARY DESCRIPTION.—The trustee of any simple retirement account established pursuant to a qualified salary reduction arrangement under section 408(p) of such Code shall provide to the employer maintaining the arrangement each year a description containing the following information:

"(A) The name and address of the employer and the trustee.

"(B) The requirements for eligibility for participation.

"(C) The benefits provided with respect to the arrangement.

"(D) The time and method of making elections with respect to the arrangement.

"(E) The procedures for, and effects of, withdrawals (including rollovers) from the arrangement.

"(3) EMPLOYEE NOTIFICATION.—The employer shall notify each employee immediately before the period for which an election described in section 408(p)(5)(C) of such Code may be made of the employee's opportunity to make such election. Such notice shall include a copy of the description described in paragraph (2)."

(2) FIDUCIARY DUTIES.—Section 404(c) of such Act (29 U.S.C. 1104(c)) is amended by inserting "(1)" after "(c)", by redesignating paragraphs (1) and (2) as subparagraphs (A) and (B), respectively, and by adding at the end the following new paragraph:

"(2) In the case of a simple retirement account established pursuant to a qualified salary reduction arrangement under section 408(p) of the Internal Revenue Code of 1986, a participant or beneficiary shall, for purposes of paragraph (1), be

treated as exercising control over the assets in the account upon the earliest of—

"(A) an affirmative election among investment options with respect to the initial investment of any contribution,

"(B) a rollover to any other simple retirement account or individual retirement plan, or

"(C) one year after the simple retirement account is established.

No reports, other than those required under section 101(g), shall be required with respect to a simple retirement account established pursuant to such a qualified salary reduction arrangement.".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1422. EXTENSION OF SIMPLE PLAN TO 401(k) ARRANGEMENTS.

(a) ALTERNATIVE METHOD OF SATISFYING SECTION 401(k) NONDISCRIMINATION TESTS.—Section 401(k) (relating to cash or deferred arrangements) is amended by adding at the end the following new paragraph:

"(11) ADOPTION OF SIMPLE PLAN TO MEET NONDISCRIMINATION TESTS.—

"(A) IN GENERAL.—A cash or deferred arrangement maintained by an eligible employer shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement meets—

"(i) the contribution requirements of subparagraph (B),

"(ii) the exclusive plan requirements of subparagraph (C), and

"(iii) the vesting requirements of section 408(p)(3).

"(B) CONTRIBUTION REQUIREMENTS.—

"(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement—

"(I) an employee may elect to have the employer make elective contributions for the year on behalf of the employee to a trust under the plan in an amount which is expressed as a percentage of compensation of the employee but which in no event exceeds $6,000,

"(II) the employer is required to make a matching contribution to the trust for the year in an amount equal to so much of the amount the employee elects under subclause (I) as does not exceed 3 percent of compensation for the year, and

"(III) no other contributions may be made other than contributions described in subclause (I) or (II).

"(ii) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—An employer shall be treated as meeting the requirements of clause (i)(II) for any year if, in lieu of the contributions described in such clause, the employer elects (pursuant to the terms of the arrangement) to make nonelective contributions of 2 percent of compensation for each employee who is eligible

to participate in the arrangement and who has at least $5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 60th day before the beginning of such year.

"(C) EXCLUSIVE PLAN REQUIREMENT.—The requirements of this subparagraph are met for any year to which this paragraph applies if no contributions were made, or benefits were accrued, for services during such year under any qualified plan of the employer on behalf of any employee eligible to participate in the cash or deferred arrangement, other than contributions described in subparagraph (B).

"(D) DEFINITIONS AND SPECIAL RULE.—

"(i) DEFINITIONS.—For purposes of this paragraph, any term used in this paragraph which is also used in section 408(p) shall have the meaning given such term by such section.

"(ii) COORDINATION WITH TOP-HEAVY RULES.—A plan meeting the requirements of this paragraph for any year shall not be treated as a top-heavy plan under section 416 for such year.".

(b) ALTERNATIVE METHODS OF SATISFYING SECTION 401(m) NONDISCRIMINATION TESTS.—Section 401(m) (relating to nondiscrimination test for matching contributions and employee contributions) is amended by redesignating paragraph (10) as paragraph (11) and by adding after paragraph (9) the following new paragraph:

"(10) ALTERNATIVE METHOD OF SATISFYING TESTS.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

"(A) meets the contribution requirements of subparagraph (B) of subsection (k)(11),

"(B) meets the exclusive plan requirements of subsection (k)(11)(C), and

"(C) meets the vesting requirements of section 408(p)(3).".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning after December 31, 1996.

Subchapter B—Other Provisions

SEC. 1426. TAX-EXEMPT ORGANIZATIONS ELIGIBLE UNDER SECTION 401(k).

(a) IN GENERAL.—Subparagraph (B) of section 401(k)(4) is amended to read as follows:

"(B) ELIGIBILITY OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.—

"(i) TAX-EXEMPTS ELIGIBLE.—Except as provided in clause (ii), any organization exempt from tax under this subtitle may include a qualified cash or deferred arrangement as part of a plan maintained by it.

"(ii) GOVERNMENTS INELIGIBLE.—A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement if it is part of a plan maintained by a State or local government or political subdivision thereof, or any agency or instrumentality thereof. This clause shall not apply to a rural cooperative plan or to a plan of an employer described in clause (iii).

"(iii) TREATMENT OF INDIAN TRIBAL GOVERNMENTS.—An employer which is an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of the foregoing may include a qualified cash or deferred arrangement as part of a plan maintained by the employer.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to plan years beginning after December 31, 1996, but shall not apply to any cash or deferred arrangement to which clause (i) of section 1116(f)(2)(B) of the Tax Reform Act of 1986 applies.

SEC. 1427. HOMEMAKERS ELIGIBLE FOR FULL IRA DEDUCTION.

(a) SPOUSAL IRA COMPUTED ON BASIS OF COMPENSATION OF BOTH SPOUSES.—Subsection (c) of section 219 (relating to special rules for certain married individuals) is amended to read as follows:

"(c) SPECIAL RULES FOR CERTAIN MARRIED INDIVIDUALS.—

"(1) IN GENERAL.—In the case of an individual to whom this paragraph applies for the taxable year, the limitation of paragraph (1) of subsection (b) shall be equal to the lesser of—

"(A) the dollar amount in effect under subsection (b)(1)(A) for the taxable year, or

"(B) the sum of—

"(i) the compensation includible in such individual's gross income for the taxable year, plus

"(ii) the compensation includible in the gross income of such individual's spouse for the taxable year reduced by the amount allowed as a deduction under subsection (a) to such spouse for such taxable year.

"(2) INDIVIDUALS TO WHOM PARAGRAPH (1) APPLIES.—Paragraph (1) shall apply to any individual if—

"(A) such individual files a joint return for the taxable year, and

"(B) the amount of compensation (if any) includible in such individual's gross income for the taxable year is less than the compensation includible in the gross income of such individual's spouse for the taxable year.".

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (2) of section 219(f) (relating to other definitions and special rules) is amended by striking "subsections (b) and (c)" and inserting "subsection (b)".

(2) Section 219(g)(1) is amended by striking "(c)(2)" and inserting "(c)(1)(A)".

(3) Section 408(d)(5) is amended by striking "$2,250" and inserting "the dollar amount in effect under section 219(b)(1)(A)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

CHAPTER 3—NONDISCRIMINATION PROVISIONS

SEC. 1431. DEFINITION OF HIGHLY COMPENSATED EMPLOYEES; REPEAL OF FAMILY AGGREGATION.

(a) IN GENERAL.—Paragraph (1) of section 414(q) (defining highly compensated employee) is amended to read as follows:

"(1) IN GENERAL.—The term 'highly compensated employee' means any employee who—

"(A) was a 5-percent owner at any time during the year or the preceding year, or

"(B) for the preceding year—

"(i) had compensation from the employer in excess of $80,000, and

"(ii) if the employer elects the application of this clause for such preceding year, was in the top-paid group of employees for such preceding year.

The Secretary shall adjust the $80,000 amount under subparagraph (B) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1996.".

(b) REPEAL OF FAMILY AGGREGATION RULES.—

(1) IN GENERAL.—Paragraph (6) of section 414(q) is hereby repealed.

(2) COMPENSATION LIMIT.—Paragraph (17)(A) of section 401(a) is amended by striking the last sentence.

(3) DEDUCTION.—Subsection (l) of section 404 is amended by striking the last sentence.

(c) CONFORMING AMENDMENTS.—

(1)(A) Subsection (q) of section 414 is amended by striking paragraphs (2), (5), and (12) and by redesignating paragraphs (3), (4), (7), (8), (9), (10), and (11) as paragraphs (2) through (8), respectively.

(B) Sections 129(d)(8)(B), 401(a)(5)(D)(ii), 408(k)(2)(C), and 416(i)(1)(D) are each amended by striking "section 414(q)(7)" and inserting "section 414(q)(4)".

(C) Section 416(i)(1)(A) is amended by striking "section 414(q)(8)" and inserting "section 414(q)(5)".

(D) Subparagraph (A) of section 414(r)(2) is amended by striking "subsection (q)(8)" and inserting "subsection (q)(5)".

(E) Section 414(q)(5), as redesignated by subparagraph (A), is amended by striking "under paragraph (4), or the number of officers taken into account under paragraph (5)".

(2) Section 1114(c)(4) of the Tax Reform Act of 1986 is amended by adding at the end the following new sentence: "Any reference in this paragraph to section 414(q) shall be treated as a reference to such section as in effect on the day before the date

of the enactment of the Small Business Job Protection Act of 1996.".

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to years beginning after December 31, 1996, except that in determining whether an employee is a highly compensated employee for years beginning in 1997, such amendments shall be treated as having been in effect for years beginning in 1996.

(2) FAMILY AGGREGATION.—The amendments made by subsection (b) shall apply to years beginning after December 31, 1996.

SEC. 1432. MODIFICATION OF ADDITIONAL PARTICIPATION REQUIREMENTS.

(a) GENERAL RULE.—Section 401(a)(26)(A) (relating to additional participation requirements) is amended to read as follows:

"(A) IN GENERAL.—In the case of a trust which is a part of a defined benefit plan, such trust shall not constitute a qualified trust under this subsection unless on each day of the plan year such trust benefits at least the lesser of—

"(i) 50 employees of the employer, or

"(ii) the greater of—

"(I) 40 percent of all employees of the employer, or

"(II) 2 employees (or if there is only 1 employee, such employee).".

(b) SEPARATE LINE OF BUSINESS TEST.—Section 401(a)(26)(G) (relating to separate line of business) is amended by striking "paragraph (7)" and inserting "paragraph (2)(A) or (7)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1996.

SEC. 1433. NONDISCRIMINATION RULES FOR QUALIFIED CASH OR DEFERRED ARRANGEMENTS AND MATCHING CONTRIBUTIONS.

(a) ALTERNATIVE METHODS OF SATISFYING SECTION 401(k) NONDISCRIMINATION TESTS.—Section 401(k) (relating to cash or deferred arrangements), as amended by section 1422, is amended by adding at the end the following new paragraph:

"(12) ALTERNATIVE METHODS OF MEETING NONDISCRIMINATION REQUIREMENTS.—

"(A) IN GENERAL.—A cash or deferred arrangement shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement—

"(i) meets the contribution requirements of subparagraph (B) or (C), and

"(ii) meets the notice requirements of subparagraph (D).

"(B) MATCHING CONTRIBUTIONS.—

"(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement, the employer makes matching contributions on behalf of each employee who is not a highly compensated employee in an amount equal to—

"(I) 100 percent of the elective contributions of the employee to the extent such elective contributions do not exceed 3 percent of the employee's compensation, and

"(II) 50 percent of the elective contributions of the employee to the extent that such elective contributions exceed 3 percent but do not exceed 5 percent of the employee's compensation.

"(ii) RATE FOR HIGHLY COMPENSATED EMPLOYEES.—The requirements of this subparagraph are not met if, under the arrangement, the rate of matching contribution with respect to any elective contribution of a highly compensated employee at any rate of elective contribution is greater than that with respect to an employee who is not a highly compensated employee.

"(iii) ALTERNATIVE PLAN DESIGNS.—If the rate of any matching contribution with respect to any rate of elective contribution is not equal to the percentage required under clause (i), an arrangement shall not be treated as failing to meet the requirements of clause (i) if—

"(I) the rate of an employer's matching contribution does not increase as an employee's rate of elective contributions increase, and

"(II) the aggregate amount of matching contributions at such rate of elective contribution is at least equal to the aggregate amount of matching contributions which would be made if matching contributions were made on the basis of the percentages described in clause (i).

"(C) NONELECTIVE CONTRIBUTIONS.—The requirements of this subparagraph are met if, under the arrangement, the employer is required, without regard to whether the employee makes an elective contribution or employee contribution, to make a contribution to a defined contribution plan on behalf of each employee who is not a highly compensated employee and who is eligible to participate in the arrangement in an amount equal to at least 3 percent of the employee's compensation.

"(D) NOTICE REQUIREMENT.—An arrangement meets the requirements of this paragraph if, under the arrangement, each employee eligible to participate is, within a reasonable period before any year, given written notice of the employee's rights and obligations under the arrangement which—

"(i) is sufficiently accurate and comprehensive to appraise the employee of such rights and obligations, and

"(ii) is written in a manner calculated to be understood by the average employee eligible to participate.

"(E) OTHER REQUIREMENTS.—

"(i) WITHDRAWAL AND VESTING RESTRICTIONS.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) of this para-

graph unless the requirements of subparagraphs (B) and (C) of paragraph (2) are met with respect to all employer contributions (including matching contributions) taken into account in determining whether the requirements of subparagraphs (B) and (C) of this paragraph are met.

"(ii) SOCIAL SECURITY AND SIMILAR CONTRIBUTIONS NOT TAKEN INTO ACCOUNT.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) unless such requirements are met without regard to subsection (l), and, for purposes of subsection (l), employer contributions under subparagraph (B) or (C) shall not be taken into account.

"(F) OTHER PLANS.—An arrangement shall be treated as meeting the requirements under subparagraph (A)(i) if any other plan maintained by the employer meets such requirements with respect to employees eligible under the arrangement.".

(b) ALTERNATIVE METHODS OF SATISFYING SECTION 401(m) NONDISCRIMINATION TESTS.—Section 401(m) (relating to nondiscrimination test for matching contributions and employee contributions), as amended by section 1422(b), is amended by redesignating paragraph (11) as paragraph (12) and by adding after paragraph (10) the following new paragraph:

"(11) ALTERNATIVE METHOD OF SATISFYING TESTS.—

"(A) IN GENERAL.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

"(i) meets the contribution requirements of subparagraph (B) or (C) of subsection (k)(12),

"(ii) meets the notice requirements of subsection (k)(12)(D), and

"(iii) meets the requirements of subparagraph (B).

"(B) LIMITATION ON MATCHING CONTRIBUTIONS.—The requirements of this subparagraph are met if—

"(i) matching contributions on behalf of any employee may not be made with respect to an employee's contributions or elective deferrals in excess of 6 percent of the employee's compensation,

"(ii) the rate of an employer's matching contribution does not increase as the rate of an employee's contributions or elective deferrals increase, and

"(iii) the matching contribution with respect to any highly compensated employee at any rate of an employee contribution or rate of elective deferral is not greater than that with respect to an employee who is not a highly compensated employee.".

(c) YEAR FOR COMPUTING NONHIGHLY COMPENSATED EMPLOYEE PERCENTAGE.—

(1) CASH OR DEFERRED ARRANGEMENTS.—Section 401(k)(3)(A) is amended—

(A) by striking "such year" in clause (ii) and inserting "the plan year",

(B) by striking "for such plan year" in clause (ii) and inserting "for the preceding plan year", and

(C) by adding at the end the following new sentence: "An arrangement may apply clause (ii) by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary.".

(2) MATCHING AND EMPLOYEE CONTRIBUTIONS.—Section 401(m)(2)(A) is amended—

(A) by inserting "for such plan year" after "highly compensated employees",

(B) by inserting "for the preceding plan year" after "eligible employees" each place it appears in clause (i) and clause (ii), and

(C) by adding at the end the following flush sentence: "This subparagraph may be applied by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided the Secretary.".

(d) SPECIAL RULE FOR DETERMINING AVERAGE DEFERRAL PERCENTAGE FOR FIRST PLAN YEAR, ETC.—

(1) Paragraph (3) of section 401(k) is amended by adding at the end the following new subparagraph:

"(E) For purposes of this paragraph, in the case of the first plan year of any plan (other than a successor plan), the amount taken into account as the actual deferral percentage of nonhighly compensated employees for the preceding plan year shall be—

"(i) 3 percent, or

"(ii) if the employer makes an election under this subclause, the actual deferral percentage of nonhighly compensated employees determined for such first plan year.".

(2) Paragraph (3) of section 401(m) is amended by adding at the end the following: "Rules similar to the rules of subsection (k)(3)(E) shall apply for purposes of this subsection.".

(e) DISTRIBUTION OF EXCESS CONTRIBUTIONS AND EXCESS AGGREGATE CONTRIBUTIONS.—

(1) Subparagraph (C) of section 401(k)(8) (relating to arrangement not disqualified if excess contributions distributed) is amended by striking "on the basis of the respective portions of the excess contributions attributable to each of such employees" and inserting "on the basis of the amount of contributions by, or on behalf of, each of such employees".

(2) Subparagraph (C) of section 401(m)(6) (relating to method of distributing excess aggregate contributions) is amended by striking "on the basis of the respective portions of such amounts attributable to each of such employees" and inserting "on the basis of the amount of contributions on behalf of, or by, each such employee".

(f) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to years beginning after December 31, 1998.

(2) EXCEPTIONS.—The amendments made by subsections (c), (d), and (e) shall apply to years beginning after December 31, 1996.

SEC. 1434. DEFINITION OF COMPENSATION FOR SECTION 415 PURPOSES.

(a) GENERAL RULE.—Section 415(c)(3) (defining participant's compensation) is amended by adding at the end the following new subparagraph:

"(D) CERTAIN DEFERRALS INCLUDED.—The term 'participant's compensation' shall include—

"(i) any elective deferral (as defined in section 402(g)(3)), and

"(ii) any amount which is contributed or deferred by the employer at the election of the employee and which is not includible in the gross income of the employee by reason of section 125 or 457.".

(b) CONFORMING AMENDMENTS.—

(1) Section 414(q)(4), as redesignated by section 1431, is amended to read as follows:

"(4) COMPENSATION.—For purposes of this subsection, the term 'compensation' has the meaning given such term by section 415(c)(3).".

(2) Section 414(s)(2) is amended by inserting "not" after "elect" in the text and heading thereof.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1997.

CHAPTER 4—MISCELLANEOUS PROVISIONS

SEC. 1441. PLANS COVERING SELF-EMPLOYED INDIVIDUALS.

(a) AGGREGATION RULES.—Section 401(d) (relating to additional requirements for qualification of trusts and plans benefiting owner-employees) is amended to read as follows:

"(d) CONTRIBUTION LIMIT ON OWNER-EMPLOYEES.—A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the plan provides that contributions on behalf of any owner-employee may be made only with respect to the earned income of such owner-employee which is derived from the trade or business with respect to which such plan is established.".

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1996.

SEC. 1442. ELIMINATION OF SPECIAL VESTING RULE FOR MULTIEMPLOYER PLANS.

(a) AMENDMENTS TO 1986 CODE.—Paragraph (2) of section 411(a) (relating to minimum vesting standards) is amended—

(1) by striking "subparagraph (A), (B), or (C)" and inserting "subparagraph (A) or (B)"; and

(2) by striking subparagraph (C).

(b) AMENDMENTS TO ERISA.—Paragraph (2) of section 203(a) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1053(a)) is amended—

(1) by striking "subparagraph (A), (B), or (C)" and inserting "subparagraph (A) or (B)"; and

(2) by striking subparagraph (C).

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning on or after the earlier of—

(1) the later of—

(A) January 1, 1997, or

(B) the date on which the last of the collective bargaining agreements pursuant to which the plan is maintained terminates (determined without regard to any extension thereof after the date of the enactment of this Act), or

(2) January 1, 1999.

Such amendments shall not apply to any individual who does not have more than 1 hour of service under the plan on or after the 1st day of the 1st plan year to which such amendments apply.

SEC. 1443. DISTRIBUTIONS UNDER RURAL COOPERATIVE PLANS.

(a) DISTRIBUTIONS FOR HARDSHIP OR AFTER A CERTAIN AGE.—Section 401(k)(7) is amended by adding at the end the following new subparagraph:

"(C) SPECIAL RULE FOR CERTAIN DISTRIBUTIONS.—A rural cooperative plan which includes a qualified cash or deferred arrangement shall not be treated as violating the requirements of section 401(a) or of paragraph (2) merely by reason of a hardship distribution or a distribution to a participant after attainment of age 59½. For purposes of this section, the term 'hardship distribution' means a distribution described in paragraph (2)(B)(i)(IV) (without regard to the limitation of its application to profit-sharing or stock bonus plans).".

(b) PUBLIC UTILITY DISTRICTS.—Clause (i) of section 401(k)(7)(B) (defining rural cooperative) is amended to read as follows:

"(i) any organization which—

"(I) is engaged primarily in providing electric service on a mutual or cooperative basis, or

"(II) is engaged primarily in providing electric service to the public in its area of service and which is exempt from tax under this subtitle or which is a State or local government (or an agency or instrumentality thereof), other than a municipality (or an agency or instrumentality thereof),".

(c) EFFECTIVE DATES.—

(1) DISTRIBUTIONS.—The amendments made by subsection (a) shall apply to distributions after the date of the enactment of this Act.

(2) PUBLIC UTILITY DISTRICTS.—The amendments made by subsection (b) shall apply to plan years beginning after December 31, 1996.

SEC. 1444. TREATMENT OF GOVERNMENTAL PLANS UNDER SECTION 415.

(a) COMPENSATION LIMIT.—Subsection (b) of section 415 is amended by adding immediately after paragraph (10) the following new paragraph:

"(11) SPECIAL LIMITATION RULE FOR GOVERNMENTAL PLANS.—In the case of a governmental plan (as defined in section 414(d)), subparagraph (B) of paragraph (1) shall not apply.".

(b) TREATMENT OF CERTAIN EXCESS BENEFIT PLANS.—

(1) IN GENERAL.—Section 415 is amended by adding at the end the following new subsection:

"(m) TREATMENT OF QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENTS.—

"(1) GOVERNMENTAL PLAN NOT AFFECTED.—In determining whether a governmental plan (as defined in section 414(d)) meets the requirements of this section, benefits provided under a qualified governmental excess benefit arrangement shall not be taken into account. Income accruing to a governmental plan (or to a trust that is maintained solely for the purpose of providing benefits under a qualified governmental excess benefit arrangement) in respect of a qualified governmental excess benefit arrangement shall constitute income derived from the exercise of an essential governmental function upon which such governmental plan (or trust) shall be exempt from tax under section 115.

"(2) TAXATION OF PARTICIPANT.—For purposes of this chapter—

"(A) the taxable year or years for which amounts in respect of a qualified governmental excess benefit arrangement are includible in gross income by a participant, and

"(B) the treatment of such amounts when so includible by the participant,

shall be determined as if such qualified governmental excess benefit arrangement were treated as a plan for the deferral of compensation which is maintained by a corporation not exempt from tax under this chapter and which does not meet the requirements for qualification under section 401.

"(3) QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENT.—For purposes of this subsection, the term 'qualified governmental excess benefit arrangement' means a portion of a governmental plan if—

"(A) such portion is maintained solely for the purpose of providing to participants in the plan that part of the participant's annual benefit otherwise payable under the terms of the plan that exceeds the limitations on benefits imposed by this section,

"(B) under such portion no election is provided at any time to the participant (directly or indirectly) to defer compensation, and

"(C) benefits described in subparagraph (A) are not paid from a trust forming a part of such governmental plan unless such trust is maintained solely for the purpose of providing such benefits.".

(2) COORDINATION WITH SECTION 457.—Subsection (e) of section 457 is amended by adding at the end the following new paragraph:

"(14) TREATMENT OF QUALIFIED GOVERNMENTAL EXCESS BENEFIT ARRANGEMENTS.—Subsections (b)(2) and (c)(1) shall

not apply to any qualified governmental excess benefit arrangement (as defined in section 415(m)(3)), and benefits provided under such an arrangement shall not be taken into account in determining whether any other plan is an eligible deferred compensation plan.".

(3) CONFORMING AMENDMENT.—Paragraph (2) of section 457(f) is amended by striking "and" at the end of subparagraph (C), by striking the period at the end of subparagraph (D) and inserting ", and", and by inserting immediately thereafter the following new subparagraph:

"(E) a qualified governmental excess benefit arrangement described in section 415(m).".

(c) EXEMPTION FOR SURVIVOR AND DISABILITY BENEFITS.—Paragraph (2) of section 415(b) is amended by adding at the end the following new subparagraph:

"(I) EXEMPTION FOR SURVIVOR AND DISABILITY BENEFITS PROVIDED UNDER GOVERNMENTAL PLANS.—Subparagraph (C) of this paragraph and paragraph (5) shall not apply to—

"(i) income received from a governmental plan (as defined in section 414(d)) as a pension, annuity, or similar allowance as the result of the recipient becoming disabled by reason of personal injuries or sickness, or

"(ii) amounts received from a governmental plan by the beneficiaries, survivors, or the estate of an employee as the result of the death of the employee.".

(d) REVOCATION OF GRANDFATHER ELECTION.—

(1) IN GENERAL.—Subparagraph (C) of section 415(b)(10) is amended by adding at the end the following new clause:

"(ii) REVOCATION OF ELECTION.—An election under clause (i) may be revoked not later than the last day of the third plan year beginning after the date of the enactment of this clause. The revocation shall apply to all plan years to which the election applied and to all subsequent plan years. Any amount paid by a plan in a taxable year ending after the revocation shall be includible in income in such taxable year under the rules of this chapter in effect for such taxable year, except that, for purposes of applying the limitations imposed by this section, any portion of such amount which is attributable to any taxable year during which the election was in effect shall be treated as received in such taxable year.".

(2) CONFORMING AMENDMENT.—Subparagraph (C) of section 415(b)(10) is amended by striking "This" and inserting:

"(i) IN GENERAL.—This".

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by subsections (a), (b), and (c) shall apply to years beginning after December 31, 1994. The amendments made by subsection (d) shall apply with respect to revocations adopted after the date of the enactment of this Act.

(2) TREATMENT FOR YEARS BEGINNING BEFORE JANUARY 1, 1995.—Nothing in the amendments made by this section shall be construed to imply that a governmental plan (as defined in section 414(d) of the Internal Revenue Code of 1986) fails to satisfy the requirements of section 415 of such Code for any taxable year beginning before January 1, 1995.

SEC. 1445. UNIFORM RETIREMENT AGE.

(a) DISCRIMINATION TESTING.—Paragraph (5) of section 401(a) (relating to special rules relating to nondiscrimination requirements) is amended by adding at the end the following new subparagraph:

"(F) SOCIAL SECURITY RETIREMENT AGE.—For purposes of testing for discrimination under paragraph (4)—

"(i) the social security retirement age (as defined in section 415(b)(8)) shall be treated as a uniform retirement age, and

"(ii) subsidized early retirement benefits and joint and survivor annuities shall not be treated as being unavailable to employees on the same terms merely because such benefits or annuities are based in whole or in part on an employee's social security retirement age (as so defined).".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to years beginning after December 31, 1996.

SEC. 1446. CONTRIBUTIONS ON BEHALF OF DISABLED EMPLOYEES.

(a) ALL DISABLED PARTICIPANTS RECEIVING CONTRIBUTIONS.—Section 415(c)(3)(C) is amended by adding at the end the following: "If a defined contribution plan provides for the continuation of contributions on behalf of all participants described in clause (i) for a fixed or determinable period, this subparagraph shall be applied without regard to clauses (ii) and (iii).".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to years beginning after December 31, 1996.

SEC. 1447. TREATMENT OF DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.

(a) SPECIAL RULES FOR PLAN DISTRIBUTIONS.—Paragraph (9) of section 457(e) (relating to other definitions and special rules) is amended to read as follows:

"(9) BENEFITS NOT TREATED AS MADE AVAILABLE BY REASON OF CERTAIN ELECTIONS, ETC.—

"(A) TOTAL AMOUNT PAYABLE IS $3,500 OR LESS.—The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to receive such amount (or the plan may distribute such amount without the participant's consent) if—

"(i) such amount does not exceed $3,500, and

"(ii) such amount may be distributed only if—

"(I) no amount has been deferred under the plan with respect to such participant during the 2-year period ending on the date of the distribution, and

"(II) there has been no prior distribution under the plan to such participant to which this subparagraph applied.

A plan shall not be treated as failing to meet the distribution requirements of subsection (d) by reason of a distribution to which this subparagraph applies.

"(B) ELECTION TO DEFER COMMENCEMENT OF DISTRIBUTIONS.—The total amount payable to a participant under the plan shall not be treated as made available merely because the participant may elect to defer commencement of distributions under the plan if—

"(i) such election is made after amounts may be available under the plan in accordance with subsection (d)(1)(A) and before commencement of such distributions, and

"(ii) the participant may make only 1 such election.".

(b) COST-OF-LIVING ADJUSTMENT OF MAXIMUM DEFERRAL AMOUNT.—Subsection (e) of section 457, as amended by section 1444(b)(2) (relating to governmental plans), is amended by adding at the end the following new paragraph:

"(15) COST-OF-LIVING ADJUSTMENT OF MAXIMUM DEFERRAL AMOUNT.—The Secretary shall adjust the $7,500 amount specified in subsections (b)(2) and (c)(1) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter ending September 30, 1994, and any increase under this paragraph which is not a multiple of $500 shall be rounded to the next lowest multiple of $500.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1448. TRUST REQUIREMENT FOR DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS.

(a) IN GENERAL.—Section 457 is amended by adding at the end the following new subsection:

"(g) GOVERNMENTAL PLANS MUST MAINTAIN SET-ASIDES FOR EXCLUSIVE BENEFIT OF PARTICIPANTS.—

"(1) IN GENERAL.—A plan maintained by an eligible employer described in subsection (e)(1)(A) shall not be treated as an eligible deferred compensation plan unless all assets and income of the plan described in subsection (b)(6) are held in trust for the exclusive benefit of participants and their beneficiaries.

"(2) TAXABILITY OF TRUSTS AND PARTICIPANTS.—For purposes of this title—

"(A) a trust described in paragraph (1) shall be treated as an organization exempt from taxation under section 501(a), and

"(B) notwithstanding any other provision of this title, amounts in the trust shall be includible in the gross income of participants and beneficiaries only to the extent, and at the time, provided in this section.

"(3) CUSTODIAL ACCOUNTS AND CONTRACTS.—For purposes of this subsection, custodial accounts and contracts described in section 401(f) shall be treated as trusts under rules similar to the rules under section 401(f).".

(b) CONFORMING AMENDMENT.—Paragraph (6) of section 457(b) is amended by inserting "except as provided in subsection (g)," before "which provides that".

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to assets and income described in section 457(b)(6) of the Internal Revenue Code of 1986 held by a plan on and after the date of the enactment of this Act.

(2) TRANSITION RULE.—In the case of a plan in existence on the date of the enactment of this Act, a trust need not be established by reason of the amendments made by this section before January 1, 1999.

SEC. 1449. TRANSITION RULE FOR COMPUTING MAXIMUM BENEFITS UNDER SECTION 415 LIMITATIONS.

(a) IN GENERAL.—Subparagraph (A) of section 767(d)(3) of the Uruguay Round Agreements Act is amended to read as follows:

> *"(A) EXCEPTION.—A plan that was adopted and in effect before December 8, 1994, shall not be required to apply the amendments made by subsection (b) with respect to benefits accrued before the earlier of—*
>
> *"(i) the later of the date a plan amendment applying the amendments made by subsection (b) is adopted or made effective, or*
>
> *"(ii) the first day of the first limitation year beginning after December 31, 1999.*
>
> *Determinations under section 415(b)(2)(E) of the Internal Revenue Code of 1986 before such earlier date shall be made with respect to such benefits on the basis of such section as in effect on December 7, 1994 (except that the modification made by section 1449(b) of the Small Business Job Protection Act of 1996 shall be taken into account), and the provisions of the plan as in effect on December 7, 1994, but only if such provisions of the plan meet the requirements of such section (as so in effect).".*

(b) MODIFICATION OF CERTAIN ASSUMPTIONS FOR ADJUSTING BENEFITS OF DEFINED BENEFIT PLANS FOR EARLY RETIREES.—Subparagraph (E) of section 415(b)(2) (relating to limitation on certain assumptions) is amended—

(1) by striking "Except as provided in clause (ii), for purposes of adjusting any benefit or limitation under subparagraph (B) or (C)," in clause (i) and inserting "For purposes of adjusting any limitation under subparagraph (C) and, except as provided in clause (ii), for purposes of adjusting any benefit under subparagraph (B),", and

(2) by striking "For purposes of adjusting the benefit or limitation of any form of benefit subject to section 417(e)(3)," in clause (ii) and inserting "For purposes of adjusting any benefit under subparagraph (B) for any form of benefit subject to section 417(e)(3),".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect as if included in the provisions of section 767 of the Uruguay Round Agreements Act.

(d) TRANSITIONAL RULE.—In the case of a plan that was adopted and in effect before December 8, 1994, if—

(1) a plan amendment was adopted or made effective on or before the date of the enactment of this Act applying the amendments made by section 767 of the Uruguay Round Agreements Act, and

(2) within 1 year after the date of the enactment of this Act, a plan amendment is adopted which repeals the amendment referred to in paragraph (1),

the amendment referred to in paragraph (1) shall not be taken into account in applying section 767(d)(3)(A) of the Uruguay Round Agreements Act, as amended by subsection (a).

SEC. 1450. MODIFICATIONS OF SECTION 403(b).

(a) MULTIPLE SALARY REDUCTION AGREEMENTS PERMITTED.—

(1) GENERAL RULE.—For purposes of section 403(b) of the Internal Revenue Code of 1986, the frequency that an employee is permitted to enter into a salary reduction agreement, the salary to which such an agreement may apply, and the ability to revoke such an agreement shall be determined under the rules applicable to cash or deferred elections under section 401(k) of such Code.

(2) CONSTRUCTIVE RECEIPT.—Section 402(e)(3) is amended by inserting "or which is part of a salary reduction agreement under section 403(b)" after "section 401(k)(2))".

(3) EFFECTIVE DATE.—This subsection shall apply to taxable years beginning after December 31, 1995.

(b) TREATMENT OF INDIAN TRIBAL GOVERNMENTS.—

(1) IN GENERAL.—In the case of any contract purchased in a plan year beginning before January 1, 1995, section 403(b) of the Internal Revenue Code of 1986 shall be applied as if any reference to an employer described in section 501(c)(3) of the Internal Revenue Code of 1986 which is exempt from tax under section 501 of such Code included a reference to an employer which is an Indian tribal government (as defined by section 7701(a)(40) of such Code), a subdivision of an Indian tribal government (determined in accordance with section 7871(d) of such Code), an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of the foregoing.

(2) ROLLOVERS.—Solely for purposes of applying section 403(b)(8) of such Code to a contract to which paragraph (1) applies, a qualified cash or deferred arrangement under section 401(k) of such Code shall be treated as if it were a plan or contract described in clause (ii) of section 403(b)(8)(A) of such Code.

(c) ELECTIVE DEFERRALS.—

(1) IN GENERAL.—Subparagraph (E) of section 403(b)(1) is amended to read as follows:

"(E) in the case of a contract purchased under a salary reduction agreement, the contract meets the requirements of section 401(a)(30),".

(2) EFFECTIVE DATE.—The amendment made by this subsection shall apply to years beginning after December 31, 1995,

except a contract shall not be required to meet any change in any requirement by reason of such amendment before the 90th day after the date of the enactment of this Act.

SEC. 1451. SPECIAL RULES RELATING TO JOINT AND SURVIVOR ANNUITY EXPLANATIONS.

(a) AMENDMENT TO INTERNAL REVENUE CODE.—Section 417(a) is amended by adding at the end the following new paragraph:

"(7) SPECIAL RULES RELATING TO TIME FOR WRITTEN EXPLANATION.—Notwithstanding any other provision of this subsection—

"(A) EXPLANATION MAY BE PROVIDED AFTER ANNUITY STARTING DATE.—

"(i) IN GENERAL.—A plan may provide the written explanation described in paragraph (3)(A) after the annuity starting date. In any case to which this subparagraph applies, the applicable election period under paragraph (6) shall not end before the 30th day after the date on which such explanation is provided.

"(ii) REGULATORY AUTHORITY.—The Secretary may by regulations limit the application of clause (i), except that such regulations may not limit the period of time by which the annuity starting date precedes the provision of the written explanation other than by providing that the annuity starting date may not be earlier than termination of employment.

"(B) WAIVER OF 30-DAY PERIOD.—A plan may permit a participant to elect (with any applicable spousal consent) to waive any requirement that the written explanation be provided at least 30 days before the annuity starting date (or to waive the 30-day requirement under subparagraph (A)) if the distribution commences more than 7 days after such explanation is provided."

(b) AMENDMENT TO ERISA.—Section 205(c) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1055(c)) is amended by adding at the end the following new paragraph:

"(8) Notwithstanding any other provision of this subsection—

"(A)(i) A plan may provide the written explanation described in paragraph (3)(A) after the annuity starting date. In any case to which this subparagraph applies, the applicable election period under paragraph (7) shall not end before the 30th day after the date on which such explanation is provided.

"(ii) The Secretary may by regulations limit the application of clause (i), except that such regulations may not limit the period of time by which the annuity starting date precedes the provision of the written explanation other than by providing that the annuity starting date may not be earlier than termination of employment.

"(B) A plan may permit a participant to elect (with any applicable spousal consent) to waive any requirement that the written explanation be provided at least 30 days before the annuity starting date (or to waive the 30-day requirement under subparagraph (A)) if the distribution com-

mences more than 7 days after such explanation is provided."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning after December 31, 1996.

SEC. 1452. REPEAL OF LIMITATION IN CASE OF DEFINED BENEFIT PLAN AND DEFINED CONTRIBUTION PLAN FOR SAME EMPLOYEE; EXCESS DISTRIBUTIONS.

(a) IN GENERAL.—Section 415(e) is repealed.

(b) EXCESS DISTRIBUTIONS.—Section 4980A is amended by adding at the end the following new subsection:

"(g) LIMITATION ON APPLICATION.—This section shall not apply to distributions during years beginning after December 31, 1996, and before January 1, 2000, and such distributions shall be treated as made first from amounts not described in subsection (f).".

(c) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 415(a) is amended—

(A) by adding "or" at the end of subparagraph (A),

(B) by striking ", or" at the end of subparagraph (B) and inserting a period, and

(C) by striking subparagraph (C).

(2) Subparagraph (B) of section 415(b)(5) is amended by striking "and subsection (e)".

(3) Paragraph (1) of section 415(f) is amended by striking "subsections (b), (c), and (e)" and inserting "subsections (b) and (c)".

(4) Subsection (g) of section 415 is amended by striking "subsections (e) and (f)" in the last sentence and inserting "subsection (f)".

(5) Clause (i) of section 415(k)(2)(A) is amended to read as follows:

> *"(i) any contribution made directly by an employee under such an arrangement shall not be treated as an annual addition for purposes of subsection (c), and".*

(6) Clause (ii) of section 415(k)(2)(A) is amended by striking "subsections (c) and (e)" and inserting "subsection (c)".

(7) Section 416 is amended by striking subsection (h).

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to limitation years beginning after December 31, 1999.

(2) EXCESS DISTRIBUTIONS.—The amendment made by subsection (b) shall apply to years beginning after December 31, 1996.

SEC. 1453. TAX ON PROHIBITED TRANSACTIONS.

(a) IN GENERAL.—Section 4975(a) is amended by striking "5 percent" and inserting "10 percent".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to prohibited transactions occurring after the date of the enactment of this Act.

SEC. 1454. TREATMENT OF LEASED EMPLOYEES.

(a) GENERAL RULE.—Subparagraph (C) of section 414(n)(2) (defining leased employee) is amended to read as follows:

"(C) such services are performed under primary direction or control by the recipient.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to years beginning after December 31, 1996, but shall not apply to any relationship determined under an Internal Revenue Service ruling issued before the date of the enactment of this Act pursuant to section 414(n)(2)(C) of the Internal Revenue Code of 1986 (as in effect on the day before such date) not to involve a leased employee.

SEC. 1455. UNIFORM PENALTY PROVISIONS TO APPLY TO CERTAIN PENSION REPORTING REQUIREMENTS.

(a) PENALTIES.—

(1) STATEMENTS.—Paragraph (1) of section 6724(d) is amended by striking "and" at the end of subparagraph (A), by striking the period at the end of subparagraph (B) and inserting ", and", and by inserting after subparagraph (B) the following new subparagraph:

"(C) any statement of the amount of payments to another person required to be made to the Secretary under—

"(i) section 408(i) (relating to reports with respect to individual retirement accounts or annuities), or

"(ii) section 6047(d) (relating to reports by employers, plan administrators, etc.).".

(2) REPORTS.—Paragraph (2) of section 6724(d) is amended by striking "or" at the end of subparagraph (U), by striking the period at the end of subparagraph (V) and inserting a comma, and by inserting after subparagraph (V) the following new subparagraphs:

"(W) section 408(i) (relating to reports with respect to individual retirement plans) to any person other than the Secretary with respect to the amount of payments made to such person, or

"(X) section 6047(d) (relating to reports by plan administrators) to any person other than the Secretary with respect to the amount of payments made to such person.".

(b) MODIFICATION OF REPORTABLE DESIGNATED DISTRIBUTIONS.—

(1) SECTION 408.—Subsection (i) of section 408 (relating to individual retirement account reports) is amended by inserting "aggregating $10 or more in any calendar year" after "distributions".

(2) SECTION 6047.—Paragraph (1) of section 6047(d) (relating to reports by employers, plan administrators, etc.) is amended by adding at the end the following new sentence: "No return or report may be required under the preceding sentence with respect to distributions to any person during any year unless such distributions aggregate $10 or more.".

(c) QUALIFYING ROLLOVER DISTRIBUTIONS.—Section 6652(i) is amended—

(1) by striking "the $10" and inserting "$100", and

(2) by striking "$5,000" and inserting "$50,000".

(d) CONFORMING AMENDMENTS.—

(1) Paragraph (1) of section 6047(f) is amended to read as follows:

"(1) For provisions relating to penalties for failures to file returns and reports required under this section, see sections 6652(e), 6721, and 6722.".

(2) Subsection (e) of section 6652 is amended by adding at the end the following new sentence: "This subsection shall not apply to any return or statement which is an information return described in section 6724(d)(1)(C)(ii) or a payee statement described in section 6724(d)(2)(X).".

(3) Subsection (a) of section 6693 is amended by adding at the end the following new sentence: "This subsection shall not apply to any report which is an information return described in section 6724(d)(1)(C)(i) or a payee statement described in section 6724(d)(2)(W).".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to returns, reports, and other statements the due date for which (determined without regard to extensions) is after December 31, 1996.

SEC. 1456. RETIREMENT BENEFITS OF MINISTERS NOT SUBJECT TO TAX ON NET EARNINGS FROM SELF-EMPLOYMENT.

(a) IN GENERAL.—Section 1402(a)(8) (defining net earning from self-employment) is amended by inserting ", but shall not include in such net earnings from self-employment the rental value of any parsonage or any parsonage allowance (whether or not excludable under section 107) provided after the individual retires, or any other retirement benefit received by such individual from a church plan (as defined in section 414(e)) after the individual retires" before the semicolon at the end.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning before, on, or after December 31, 1994.

SEC. 1457. SAMPLE LANGUAGE FOR SPOUSAL CONSENT AND QUALIFIED DOMESTIC RELATIONS FORMS.

(a) DEVELOPMENT OF SAMPLE LANGUAGE.—Not later than January 1, 1997, the Secretary of the Treasury shall develop—

(1) sample language for inclusion in a form for the spousal consent required under section 417(a)(2) of the Internal Revenue Code of 1986 and section 205(c)(2) of the Employee Retirement Income Security Act of 1974 which—

(A) is written in a manner calculated to be understood by the average person, and

(B) discloses in plain form—

(i) whether the waiver to which the spouse consents is irrevocable, and

(ii) whether such waiver may be revoked by a qualified domestic relations order, and

(2) sample language for inclusion in a form for a qualified domestic relations order described in section 414(p)(1)(A) of such Code and section 206(d)(3)(B)(i) of such Act which—

(A) meets the requirements contained in such sections, and

(B) the provisions of which focus attention on the need to consider the treatment of any lump sum payment, qualified joint and survivor annuity, or qualified preretirement survivor annuity.

(b) PUBLICITY.—The Secretary of the Treasury shall include publicity for the sample language developed under subsection (a) in the pension outreach efforts undertaken by the Secretary.

SEC. 1458. TREATMENT OF LENGTH OF SERVICE AWARDS TO VOLUNTEERS PERFORMING FIRE FIGHTING OR PREVENTION SERVICES, EMERGENCY MEDICAL SERVICES, OR AMBULANCE SERVICES.

(a) IN GENERAL.—Paragraph (11) of section 457(e) (relating to deferred compensation plans of State and local governments and tax-exempt organizations) is amended to read as follows:

"(11) CERTAIN PLANS EXCLUDED.—

"(A) IN GENERAL.—The following plans shall be treated as not providing for the deferral of compensation:

"(i) Any bona fide vacation leave, sick leave, compensatory time, severance pay, disability pay, or death benefit plan.

"(ii) Any plan paying solely length of service awards to bona fide volunteers (or their beneficiaries) on account of qualified services performed by such volunteers.

"(B) SPECIAL RULES APPLICABLE TO LENGTH OF SERVICE AWARD PLANS.—

"(i) BONA FIDE VOLUNTEER.—An individual shall be treated as a bona fide volunteer for purposes of subparagraph (A)(ii) if the only compensation received by such individual for performing qualified services is in the form of—

"(I) reimbursement for (or a reasonable allowance for) reasonable expenses incurred in the performance of such services, or

"(II) reasonable benefits (including length of service awards), and nominal fees for such services, customarily paid by eligible employers in connection with the performance of such services by volunteers.

"(ii) LIMITATION ON ACCRUALS.—A plan shall not be treated as described in subparagraph (A)(ii) if the aggregate amount of length of service awards accruing with respect to any year of service for any bona fide volunteer exceeds $3,000.

"(C) QUALIFIED SERVICES.—For purposes of this paragraph, the term 'qualified services' means fire fighting and prevention services, emergency medical services, and ambulance services.".

(b) EXEMPTION FROM SOCIAL SECURITY TAXES.—

(1) Subsection (a)(5) of section 3121, as amended by section 1421, is amended by striking "(or)" at the end of subparagraph (G), by inserting "or" at the end of subparagraph (H), and by adding at the end the following new subparagraph:

"(I) under a plan described in section 457(e)(11)(A)(ii) and maintained by an eligible employer (as defined in section 457(e)(1)).".

(2) Section 209(a)(4) of the Social Security Act is amended by inserting "; or (K) under a plan described in section

457(e)(11)(A)(ii) of the Internal Revenue Code of 1986 and maintained by an eligible employer (as defined in section 457(e)(1) of such Code)" before the semicolon at the end thereof.

(c) EFFECTIVE DATE.—

(1) SUBSECTION (a).—The amendment made by subsection (a) shall apply to accruals of length of service awards after December 31, 1996.

(2) SUBSECTION (b).—The amendments made by subsection (b) shall apply to remuneration paid after December 31, 1996.

SEC. 1459. ALTERNATIVE NONDISCRIMINATION RULES FOR CERTAIN PLANS THAT PROVIDE FOR EARLY PARTICIPATION.

(a) CASH OR DEFERRED ARRANGEMENTS.—Paragraph (3) of section 401(k) (relating to application of participation and discrimination standards), as amended by section 1433(d)(1) of this Act, is amended by adding at the end the following new subparagraph:

"(F) SPECIAL RULE FOR EARLY PARTICIPATION.—If an employer elects to apply section 410(b)(4)(B) in determining whether a cash or deferred arrangement meets the requirements of subparagraph (A)(i), the employer may, in determining whether the arrangement meets the requirements of subparagraph (A)(ii), exclude from consideration all eligible employees (other than highly compensated employees) who have not met the minimum age and service requirements of section 410(a)(1)(A).".

(b) MATCHING CONTRIBUTIONS.—Paragraph (5) of section 401(m) (relating to employees taken into consideration) is amended by adding at the end the following new subparagraph:

"(C) SPECIAL RULE FOR EARLY PARTICIPATION.—If an employer elects to apply section 410(b)(4)(B) in determining whether a plan meets the requirements of section 410(b), the employer may, in determining whether the plan meets the requirements of paragraph (2), exclude from consideration all eligible employees (other than highly compensated employees) who have not met the minimum age and service requirements of section 410(a)(1)(A).".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning after December 31, 1998.

SEC. 1460. CLARIFICATION OF APPLICATION OF ERISA TO INSURANCE COMPANY GENERAL ACCOUNTS.

(a) IN GENERAL.—Section 401 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1101) is amended by adding at the end the following new subsection:

"(c)(1)(A) Not later than June 30, 1997, the Secretary shall issue proposed regulations to provide guidance for the purpose of determining, in cases where an insurer issues 1 or more policies to or for the benefit of an employee benefit plan (and such policies are supported by assets of such insurer's general account), which assets held by the insurer (other than plan assets held in its separate accounts) constitute assets of the plan for purposes of this part and section 4975 of the Internal Revenue Code of 1986 and to provide guidance with respect to the application of this title to the general account assets of insurers.

"(B) The proposed regulations under subparagraph (A) shall be subject to public notice and comment until September 30, 1997.

"(C) The Secretary shall issue final regulations providing the guidance described in subparagraph (A) not later than December 31, 1997.

"(D) Such regulations shall only apply with respect to policies which are issued by an insurer on or before December 31, 1998, to or for the benefit of an employee benefit plan which is supported by assets of such insurer's general account. With respect to policies issued on or before December 31, 1998, such regulations shall take effect at the end of the 18-month period following the date on which such regulations become final.

"(2) The Secretary shall ensure that the regulations issued under paragraph (1)—

"(A) are administratively feasible, and

"(B) protect the interests and rights of the plan and of its participants and beneficiaries (including meeting the requirements of paragraph (3)).

"(3) The regulations prescribed by the Secretary pursuant to paragraph (1) shall require, in connection with any policy issued by an insurer to or for the benefit of an employee benefit plan to the extent that the policy is not a guaranteed benefit policy (as defined in subsection (b)(2)(B))—

"(A) that a plan fiduciary totally independent of the insurer authorize the purchase of such policy (unless such purchase is a transaction exempt under section 408(b)(5)),

"(B) that the insurer describe (in such form and manner as shall be prescribed in such regulations), in annual reports and in policies issued to the policyholder after the date on which such regulations are issued in final form pursuant to paragraph (1)(C) —

"(i) a description of the method by which any income and expenses of the insurer's general account are allocated to the policy during the term of the policy and upon the termination of the policy, and

"(ii) for each report, the actual return to the plan under the policy and such other financial information as the Secretary may deem appropriate for the period covered by each such annual report,

"(C) that the insurer disclose to the plan fiduciary the extent to which alternative arrangements supported by assets of separate accounts of the insurer (which generally hold plan assets) are available, whether there is a right under the policy to transfer funds to a separate account and the terms governing any such right, and the extent to which support by assets of the insurer's general account and support by assets of separate accounts of the insurer might pose differing risks to the plan, and

"(D) that the insurer manage those assets of the insurer which are assets of such insurer's general account (irrespective of whether any such assets are plan assets) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, taking into account all obligations supported by such enterprise.

"(4) Compliance by the insurer with all requirements of the regulations issued by the Secretary pursuant to paragraph (1) shall be deemed compliance by such insurer with sections 404, 406, and 407 with respect to those assets of the insurer's general account which support a policy described in paragraph (3).

"(5)(A) Subject to subparagraph (B), any regulations issued under paragraph (1) shall not take effect before the date on which such regulations become final.

"(B) No person shall be subject to liability under this part or section 4975 of the Internal Revenue Code of 1986 for conduct which occurred before the date which is 18 months following the date described in subparagraph (A) on the basis of a claim that the assets of an insurer (other than plan assets held in a separate account) constitute assets of the plan, except—

"(i) as otherwise provided by the Secretary in regulations intended to prevent avoidance of the regulations issued under paragraph (1), or

"(ii) as provided in an action brought by the Secretary pursuant to paragraph (2) or (5) of section 502(a) for a breach of fiduciary responsibilities which would also constitute a violation of Federal or State criminal law.

The Secretary shall bring a cause of action described in clause (ii) if a participant, beneficiary, or fiduciary demonstrates to the satisfaction of the Secretary that a breach described in clause (ii) has occurred.

"(6) Nothing in this subsection shall preclude the application of any Federal criminal law.

"(7) For purposes of this subsection, the term 'policy' includes a contract.".

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendment made by this section shall take effect on January 1, 1975.

(2) CIVIL ACTIONS.—The amendment made by this section shall not apply to any civil action commenced before November 7, 1995.

SEC. 1461. SPECIAL RULES FOR CHAPLAINS AND SELF-EMPLOYED MINISTERS.

(a) IN GENERAL.—Section 414(e) (defining church plan) is amended by adding at the end the following new paragraph:

"(5) SPECIAL RULES FOR CHAPLAINS AND SELF-EMPLOYED MINISTERS.—

"(A) CERTAIN MINISTERS MAY PARTICIPATE.—For purposes of this part—

"(i) IN GENERAL.—An employee of a church or a convention or association of churches shall include a duly ordained, commissioned, or licensed minister of a church who, in connection with the exercise of his or her ministry—

"(I) is a self-employed individual (within the meaning of section 401(c)(1)(B)), or

"(II) is employed by an organization other than an organization described in section 501(c)(3).

"(ii) TREATMENT AS EMPLOYER AND EMPLOYEE.—

"(I) SELF-EMPLOYED.—A minister described in clause (i)(I) shall be treated as his or her own employer which is an organization described in section 501(c)(3) and which is exempt from tax under section 501(a).

"(II) OTHERS.—A minister described in clause (i)(II) shall be treated as employed by an organization described in section 501(c)(3) and exempt from tax under section 501(a).

"(B) SPECIAL RULES FOR APPLYING SECTION 403(b) TO SELF-EMPLOYED MINISTERS.—In the case of a minister described in subparagraph (A)(i)(I)—

"(i) the minister's includible compensation under section 403(b)(3) shall be determined by reference to the minister's earned income (within the meaning of section 401(c)(2)) from such ministry rather than the amount of compensation which is received from an employer, and

"(ii) the years (and portions of years) in which such minister was a self-employed individual (within the meaning of section 401(c)(1)(B)) with respect to such ministry shall be included for purposes of section 403(b)(4).

"(C) EFFECT ON NON-DENOMINATIONAL PLANS.—If a duly ordained, commissioned, or licensed minister of a church in the exercise of his or her ministry participates in a church plan (within the meaning of this section) and in the exercise of such ministry is employed by an employer not eligible to participate in such church plan, then such employer may exclude such minister from being treated as an employee of such employer for purposes of applying sections 401(a)(3), 401(a)(4), and 401(a)(5), as in effect on September 1, 1974, and sections 401(a)(4), 401(a)(5), 401(a)(26), 401(k)(3), 401(m), 403(b)(1)(D) (including section 403(b)(12)), and 410 to any stock bonus, pension, profit-sharing, or annuity plan (including an annuity described in section 403(b) or a retirement income account described in section 403(b)(9)). The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purpose of, and prevent the abuse of, this subparagraph.

"(D) COMPENSATION TAKEN INTO ACCOUNT ONLY ONCE.—If any compensation is taken into account in determining the amount of any contributions made to, or benefits to be provided under, any church plan, such compensation shall not also be taken into account in determining the amount of any contributions made to, or benefits to be provided under, any other stock bonus, pension, profit-sharing, or annuity plan which is not a church plan."

(b) CONTRIBUTIONS BY CERTAIN MINISTERS TO RETIREMENT INCOME ACCOUNTS.—Section 404(a) (relating to deduction for contributions of an employer to an employees' trust or annuity plan and

compensation under a deferred-payment plan) is amended by adding at the end the following new paragraph:

"(10) CONTRIBUTIONS BY CERTAIN MINISTERS TO RETIREMENT INCOME ACCOUNTS.—In the case of contributions made by a minister described in section 414(e)(5) to a retirement income account described in section 403(b)(9) and not by a person other than such minister, such contributions—

"(A) shall be treated as made to a trust which is exempt from tax under section 501(a) and which is part of a plan which is described in section 401(a), and

"(B) shall be deductible under this subsection to the extent such contributions do not exceed the limit on elective deferrals under section 402(g), the exclusion allowance under section 403(b)(2), or the limit on annual additions under section 415.

For purposes of this paragraph, all plans in which the minister is a participant shall be treated as one plan.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to years beginning after December 31, 1996.

SEC. 1462. DEFINITION OF HIGHLY COMPENSATED EMPLOYEE FOR PRE-ERISA RULES FOR CHURCH PLANS.

(a) IN GENERAL.—Section 414(q) (defining highly compensated employee), as amended by section 1431(c)(1)(A) of this Act, is amended by adding at the end the following new paragraph:

"(7) CERTAIN EMPLOYEES NOT CONSIDERED HIGHLY COMPENSATED AND EXCLUDED EMPLOYEES UNDER PRE-ERISA RULES FOR CHURCH PLANS.—In the case of a church plan (as defined in subsection (e)), no employee shall be considered an officer, a person whose principal duties consist of supervising the work of other employees, or a highly compensated employee for any year unless such employee is a highly compensated employee under paragraph (1) for such year.".

(b) SAFEHARBOR AUTHORITY.—The Secretary of the Treasury may design nondiscrimination and coverage safe harbors for church plans.

(c) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to years beginning after December 31, 1996.

SEC. 1463. RULE RELATING TO INVESTMENT IN CONTRACT NOT TO APPLY TO FOREIGN MISSIONARIES.

(a) IN GENERAL.—The last sentence of section 72(f) is amended by inserting ", or to the extent such credits are attributable to services performed as a foreign missionary (within the meaning of section 403(b)(2)(D)(iii))" before the end period.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1464. WAIVER OF EXCISE TAX ON FAILURE TO PAY LIQUIDITY SHORTFALL.

(a) IN GENERAL.—Section 4971(f) (relating to failure to pay liquidity shortfall) is amended by adding at the end the following new paragraph:

"(4) WAIVER BY SECRETARY.—If the taxpayer establishes to the satisfaction of the Secretary that—

"(A) the liquidity shortfall described in paragraph (1) was due to reasonable cause and not willful neglect, and

"(B) reasonable steps have been taken to remedy such liquidity shortfall,

the Secretary may waive all or part of the tax imposed by this subsection.".

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect as if included in the amendment made by clause (ii) of section 751(a)(9)(B) of the Retirement Protection Act of 1994 (108 Stat. 5020).

SEC. 1465. DATE FOR ADOPTION OF PLAN AMENDMENTS.

If any amendment made by this subtitle requires an amendment to any plan or annuity contract, such amendment shall not be required to be made before the first day of the first plan year beginning on or after January 1, 1998, if—

(1) during the period after such amendment takes effect and before such first plan year, the plan or contract is operated in accordance with the requirements of such amendment, and

(2) such amendment applies retroactively to such period.

In the case of a governmental plan (as defined in section 414(d) of the Internal Revenue Code of 1986), this section shall be applied by substituting "2000" for "1998".

Subtitle E—Foreign Simplification

SEC. 1501. REPEAL OF INCLUSION OF CERTAIN EARNINGS INVESTED IN EXCESS PASSIVE ASSETS.

(a) IN GENERAL.—

(1) REPEAL OF INCLUSION.—Paragraph (1) of section 951(a) (relating to amounts included in gross income of United States shareholders) is amended by striking subparagraph (C), by striking "; and" at the end of subparagraph (B) and inserting a period, and by adding "and" at the end of subparagraph (A).

(2) REPEAL OF INCLUSION AMOUNT.—Section 956A (relating to earnings invested in excess passive assets) is repealed.

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (G) of section 904(d)(3), as amended by section 1703(i)(1), is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(1) Paragraph (1) of section 956(b) is amended to read as follows:

"(1) APPLICABLE EARNINGS.—For purposes of this section, the term 'applicable earnings' means, with respect to any controlled foreign corporation, the sum of—

"(A) the amount (not including a deficit) referred to in section 316(a)(1), and

"(B) the amount referred to in section 316(a)(2),

but reduced by distributions made during the taxable year and by earnings and profits described in section 959(c)(1).".

(2) Paragraph (3) of section 956(b) is amended to read as follows:

"(3) SPECIAL RULE WHERE CORPORATION CEASES TO BE CONTROLLED FOREIGN CORPORATION.—If any foreign corporation

ceases to be a controlled foreign corporation during any taxable year—

"(A) the determination of any United States shareholder's pro rata share shall be made on the basis of stock owned (within the meaning of section 958(a)) by such shareholder on the last day during the taxable year on which the foreign corporation is a controlled foreign corporation,

"(B) the average referred to in subsection (a)(1)(A) for such taxable year shall be determined by only taking into account quarters ending on or before such last day, and

"(C) in determining applicable earnings, the amount taken into account by reason of being described in paragraph (2) of section 316(a) shall be the portion of the amount so described which is allocable (on a pro rata basis) to the part of such year during which the corporation is a controlled foreign corporation."..

(3) Subsection (a) of section 959 (relating to exclusion from gross income of previously taxed earnings and profits) is amended by adding "or" at the end of paragraph (1), by striking "or" at the end of paragraph (2), and by striking paragraph (3).

(4) Subsection (a) of section 959 is amended by striking "paragraphs (2) and (3)" in the last sentence and inserting "paragraph (2)".

(5) Subsection (c) of section 959 is amended by adding at the end the following flush sentence:

"References in this subsection to section 951(a)(1)(C) and subsection (a)(3) shall be treated as references to such provisions as in effect on the day before the date of the enactment of the Small Business Job Protection Act of 1996.".

(6) Paragraph (1) of section 959(f) is amended to read as follows:

"(1) IN GENERAL.—For purposes of this section, amounts that would be included under subparagraph (B) of section 951(a)(1) (determined without regard to this section) shall be treated as attributable first to earnings described in subsection (c)(2), and then to earnings described in subsection (c)(3).".

(7) Paragraph (2) of section 959(f) is amended by striking "subparagraphs (B) and (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(8) Subsection (b) of section 989 is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(9) Paragraph (9) of section 1297(b) is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(10) Subsections (d)(3)(B) and (e)(2)(B)(ii) of section 1297 are each amended by striking "or section 956A".

(11) Subparagraph (G) of section 904(d)(3) is amended by striking "subparagraph (B) or (C) of section 951(a)(1)" and inserting "section 951(a)(1)(B)".

(c) CLERICAL AMENDMENT.—The table of sections for subpart F of part III of subchapter N of chapter 1 is amended by striking the item relating to section 956A.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years of foreign corporations beginning after December 31, 1996, and to taxable years of United States shareholders within which or with which such taxable years of foreign corporations end.

Subtitle F—Revenue Offsets

PART I—GENERAL PROVISIONS

SEC. 1601. TERMINATION OF PUERTO RICO AND POSSESSION TAX CREDIT.

(a) IN GENERAL.—Section 936 is amended by adding at the end the following new subsection:

"(j) TERMINATION.—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, this section shall not apply to any taxable year beginning after December 31, 1995.

"(2) TRANSITION RULES FOR ACTIVE BUSINESS INCOME CREDIT.—Except as provided in paragraph (3)—

"(A) ECONOMIC ACTIVITY CREDIT.—In the case of an existing credit claimant—

"(i) with respect to a possession other than Puerto Rico, and

"(ii) to which subsection (a)(4)(B) does not apply,

the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 2002.

"(B) SPECIAL RULE FOR REDUCED CREDIT.—

"(i) IN GENERAL.—In the case of an existing credit claimant to which subsection (a)(4)(B) applies, the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 1998.

"(ii) ELECTION IRREVOCABLE AFTER 1997.—An election under subsection (a)(4)(B)(iii) which is in effect for the taxpayer's last taxable year beginning before 1997 may not be revoked unless it is revoked for the taxpayer's first taxable year beginning in 1997 and all subsequent taxable years.

"(C) ECONOMIC ACTIVITY CREDIT FOR PUERTO RICO.—

"For economic activity credit for Puerto Rico, see section 30A.

"(3) ADDITIONAL RESTRICTED CREDIT.—

"(A) IN GENERAL.—In the case of an existing credit claimant—

"(i) the credit under subsection (a)(1)(A) shall be allowed for the period beginning with the first taxable year after the last taxable year to which subparagraph (A) or (B) of paragraph (2), whichever is appropriate,

applied and ending with the last taxable year beginning before January 1, 2006, except that

"(ii) the aggregate amount of taxable income taken into account under subsection (a)(1)(A) for any such taxable year shall not exceed the adjusted base period income of such claimant.

"(B) COORDINATION WITH SUBSECTION (a)(4).—The amount of income described in subsection (a)(1)(A) which is taken into account in applying subsection (a)(4) shall be such income as reduced under this paragraph.

"(4) ADJUSTED BASE PERIOD INCOME.—For purposes of paragraph (3)—

"(A) IN GENERAL.—The term 'adjusted base period income' means the average of the inflation-adjusted possession incomes of the corporation for each base period year.

"(B) INFLATION-ADJUSTED POSSESSION INCOME.—For purposes of subparagraph (A), the inflation-adjusted possession income of any corporation for any base period year shall be an amount equal to the sum of—

"(i) the possession income of such corporation for such base period year, plus

"(ii) such possession income multiplied by the inflation adjustment percentage for such base period year.

"(C) INFLATION ADJUSTMENT PERCENTAGE.—For purposes of subparagraph (B), the inflation adjustment percentage for any base period year means the percentage (if any) by which—

"(i) the CPI for 1995, exceeds

"(ii) the CPI for the calendar year in which the base period year for which the determination is being made ends.

For purposes of the preceding sentence, the CPI for any calendar year is the CPI (as defined in section 1(f)(5)) for such year under section 1(f)(4).

"(D) INCREASE IN INFLATION ADJUSTMENT PERCENTAGE FOR GROWTH DURING BASE YEARS.—The inflation adjustment percentage (determined under subparagraph (C) without regard to this subparagraph) for each of the 5 taxable years referred to in paragraph (5)(A) shall be increased by—

"(i) 5 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1995;

"(ii) 10.25 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1994;

"(iii) 15.76 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1993;

"(iv) 21.55 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1992; and

"(v) 27.63 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1991.

"(5) BASE PERIOD YEAR.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'base period year' means each of 3 taxable years which are among the 5 most recent taxable years of the corporation ending before October 14, 1995, determined by disregarding—

"(i) one taxable year for which the corporation had the largest inflation-adjusted possession income, and

"(ii) one taxable year for which the corporation had the smallest inflation-adjusted possession income.

"(B) CORPORATIONS NOT HAVING SIGNIFICANT POSSESSION INCOME THROUGHOUT 5-YEAR PERIOD.—

"(i) IN GENERAL.—If a corporation does not have significant possession income for each of the most recent 5 taxable years ending before October 14, 1995, then, in lieu of applying subparagraph (A), the term 'base period year' means only those taxable years (of such 5 taxable years) for which the corporation has significant possession income; except that, if such corporation has significant possession income for 4 of such 5 taxable years, the rule of subparagraph (A)(ii) shall apply.

"(ii) SPECIAL RULE.—If there is no year (of such 5 taxable years) for which a corporation has significant possession income—

"(I) the term 'base period year' means the first taxable year ending on or after October 14, 1995, but

"(II) the amount of possession income for such year which is taken into account under paragraph (4) shall be the amount which would be determined if such year were a short taxable year ending on September 30, 1995.

"(iii) SIGNIFICANT POSSESSION INCOME.—For purposes of this subparagraph, the term 'significant possession income' means possession income which exceeds 2 percent of the possession income of the taxpayer for the taxable year (of the period of 6 taxable years ending with the first taxable year ending on or after October 14, 1995) having the greatest possession income.

"(C) ELECTION TO USE ONE BASE PERIOD YEAR.—

"(i) IN GENERAL.—At the election of the taxpayer, the term 'base period year' means—

"(I) only the last taxable year of the corporation ending in calendar year 1992, or

"(II) a deemed taxable year which includes the first ten months of calendar year 1995.

"(ii) BASE PERIOD INCOME FOR 1995.—In determining the adjusted base period income of the corporation for the deemed taxable year under clause (i)(II), the possession income shall be annualized and shall be determined without regard to any extraordinary item.

"(iii) ELECTION.—An election under this subparagraph by any possession corporation may be made only for the corporation's first taxable year beginning after December 31, 1995, for which it is a possession corporation. The rules of subclauses (II) and (III) of subsection (a)(4)(B)(iii) shall apply to the election under this subparagraph.

"(D) ACQUISITIONS AND DISPOSITIONS.—Rules similar to the rules of subparagraphs (A) and (B) of section 41(f)(3) shall apply for purposes of this subsection.

"(6) POSSESSION INCOME.—For purposes of this subsection, the term 'possession income' means, with respect to any possession, the income referred to in subsection (a)(1)(A) determined with respect to that possession. In no event shall possession income be treated as being less than zero.

"(7) SHORT YEARS.—If the current year or a base period year is a short taxable year, the application of this subsection shall be made with such annualizations as the Secretary shall prescribe.

"(8) SPECIAL RULES FOR CERTAIN POSSESSIONS.—

"(A) IN GENERAL.—In the case of an existing credit claimant with respect to an applicable possession, this section (other than the preceding paragraphs of this subsection) shall apply to such claimant with respect to such applicable possession for taxable years beginning after December 31, 1995, and before January 1, 2006.

"(B) APPLICABLE POSSESSION.—For purposes of this paragraph, the term 'applicable possession' means Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.

"(9) EXISTING CREDIT CLAIMANT.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'existing credit claimant' means a corporation—

"(i)(I) which was actively conducting a trade or business in a possession on October 13, 1995, and

"(II) with respect to which an election under this section is in effect for the corporation's taxable year which includes October 13, 1995, or

"(ii) which acquired all of the assets of a trade or business of a corporation which—

"(I) satisfied the requirements of subclause (I) of clause (i) with respect to such trade or business, and

"(II) satisfied the requirements of subclause (II) of clause (i).

"(B) NEW LINES OF BUSINESS PROHIBITED.—If, after October 13, 1995, a corporation which would (but for this subparagraph) be an existing credit claimant adds a substantial new line of business (other than in an acquisition described in subparagraph (A)(ii)), such corporation shall cease to be treated as an existing credit claimant as of the close of the taxable year ending before the date of such addition.

"(C) BINDING CONTRACT EXCEPTION.—If, on October 13, 1995, and at all times thereafter, there is in effect with respect to a corporation a binding contract for the acquisition of assets to be used in, or for the sale of assets to be produced from, a trade or business, the corporation shall be treated for purposes of this paragraph as actively conducting such trade or business on October 13, 1995. The preceding sentence shall not apply if such trade or business is not actively conducted before January 1, 1996.

"(10) SEPARATE APPLICATION TO EACH POSSESSION.—For purposes of determining—

"(A) whether a taxpayer is an existing credit claimant, and

"(B) the amount of the credit allowed under this section,

this subsection (and so much of this section as relates to this subsection) shall be applied separately with respect to each possession.".

(b) ECONOMIC ACTIVITY CREDIT FOR PUERTO RICO.—

(1) IN GENERAL.—Subpart B of part IV of subchapter A of chapter 1 is amended by adding at the end the following new section:

"SEC. 30A. PUERTO RICAN ECONOMIC ACTIVITY CREDIT.

"(a) ALLOWANCE OF CREDIT.—

"(1) IN GENERAL.—Except as otherwise provided in this section, if the conditions of both paragraph (1) and paragraph (2) of subsection (b) are satisfied with respect to a qualified domestic corporation, there shall be allowed as a credit against the tax imposed by this chapter an amount equal to the portion of the tax which is attributable to the taxable income, from sources without the United States, from—

"(A) the active conduct of a trade or business within Puerto Rico, or

"(B) the sale or exchange of substantially all of the assets used by the taxpayer in the active conduct of such trade or business.

In the case of any taxable year beginning after December 31, 2001, the aggregate amount of taxable income taken into account under the preceding sentence (and in applying subsection (d)) shall not exceed the adjusted base period income of such corporation, as determined in the same manner as under section 936(j).

"(2) QUALIFIED DOMESTIC CORPORATION.—For purposes of paragraph (1), the term 'qualified domestic corporation' means a domestic corporation—

"(A) which is an existing credit claimant with respect to Puerto Rico, and

"(B) with respect to which section 936(a)(4)(B) does not apply for the taxable year.

"(3) SEPARATE APPLICATION.—For purposes of determining—

"(A) whether a taxpayer is an existing credit claimant with respect to Puerto Rico, and

"(B) the amount of the credit allowed under this section,

this section (and so much of section 936 as relates to this section) shall be applied separately with respect to Puerto Rico.

"(b) CONDITIONS WHICH MUST BE SATISFIED.—The conditions referred to in subsection (a) are—

"(1) 3-YEAR PERIOD.—If 80 percent or more of the gross income of the qualified domestic corporation for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within a possession (determined without regard to section 904(f)).

"(2) TRADE OR BUSINESS.—If 75 percent or more of the gross income of the qualified domestic corporation for such period or such part thereof was derived from the active conduct of a trade or business within a possession.

"(c) CREDIT NOT ALLOWED AGAINST CERTAIN TAXES.—The credit provided by subsection (a) shall not be allowed against the tax imposed by—

"(1) section 59A (relating to environmental tax),

"(2) section 531 (relating to the tax on accumulated earnings),

"(3) section 541 (relating to personal holding company tax), or

"(4) section 1351 (relating to recoveries of foreign expropriation losses).

"(d) LIMITATIONS ON CREDIT FOR ACTIVE BUSINESS INCOME.—The amount of the credit determined under subsection (a) for any taxable year shall not exceed the sum of the following amounts:

"(1) 60 percent of the sum of—

"(A) the aggregate amount of the qualified domestic corporation's qualified possession wages for such taxable year, plus

"(B) the allocable employee fringe benefit expenses of the qualified domestic corporation for such taxable year.

"(2) The sum of—

"(A) 15 percent of the depreciation allowances for the taxable year with respect to short-life qualified tangible property,

"(B) 40 percent of the depreciation allowances for the taxable year with respect to medium-life qualified tangible property, and

"(C) 65 percent of the depreciation allowances for the taxable year with respect to long-life qualified tangible property.

"(3) If the qualified domestic corporation does not have an election to use the method described in section 936(h)(5)(C)(ii) (relating to profit split) in effect for the taxable year, the amount of the qualified possession income taxes for the taxable year allocable to nonsheltered income.

"(e) ADMINISTRATIVE PROVISIONS.—For purposes of this title—

"(1) the provisions of section 936 (including any applicable election thereunder) shall apply in the same manner as if the credit under this section were a credit under section

936(a)(1)(A) for a domestic corporation to which section 936(a)(4)(A) applies,

"(2) the credit under this section shall be treated in the same manner as the credit under section 936, and

"(3) a corporation to which this section applies shall be treated in the same manner as if it were a corporation electing the application of section 936.

"(f) DEFINITIONS.—For purposes of this section, any term used in this section which is also used in section 936 shall have the same meaning given such term by section 936.

"(g) APPLICATION OF SECTION.—This section shall apply to taxable years beginning after December 31, 1995, and before January 1, 2006.".

(2) CONFORMING AMENDMENTS.—

(A) Paragraph (1) of section 55(c) is amended by striking "and the section 936 credit allowable under section 27(b)" and inserting ", the section 936 credit allowable under section 27(b), and the Puerto Rican economic activity credit under section 30A".

(B) Subclause (I) of section 56(g)(4)(C)(ii) is amended—

(i) by inserting "30A," before "936", and

(ii) by striking "and (i)" and inserting ", (i), and (j)".

(C) Clause (iii) of section 56(g)(4)(C) is amended by adding at the end the following new subclause:

"(VI) APPLICATION TO SECTION 30A CORPORATIONS.—References in this clause to section 936 shall be treated as including references to section 30A.".

(D) Subsection (b) of section 59 is amended by striking "section 936," and all that follows and inserting "section 30A or 936, alternative minimum taxable income shall not include any income with respect to which a credit is determined under section 30A or 936.".

(E) The table of sections for subpart B of part IV of subchapter A of chapter 1 is amended by adding at the end the following new item:

"Sec. 30A. Puerto Rican economic activity credit.".

(F)(i) The heading for subpart B of part IV of subchapter A of chapter 1 is amended to read as follows:

"Subpart B—Other Credits".

(ii) The table of subparts for part IV of subchapter A of chapter 1 is amended by striking the item relating to subpart B and inserting the following new item:

"Subpart B. Other credits.".

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1995.

(2) SPECIAL RULE FOR QUALIFIED POSSESSION SOURCE INVESTMENT INCOME.—The amendments made by this section

shall not apply to qualified possession source investment income received or accrued before July 1, 1996, without regard to the taxable year in which received or accrued.

(3) SPECIAL TRANSITION RULE FOR PAYMENT OF ESTIMATED TAX INSTALLMENT.—In determining the amount of any installment due under section 6655 of the Internal Revenue Code of 1986 after the date of the enactment of this Act and before October 1, 1996, only ½ of any increase in tax (for the taxable year for which such installment is made) by reason of the amendments made by subsections (a) and (b) shall be taken into account. Any reduction in such installment by reason of the preceding sentence shall be recaptured by increasing the next required installment for such year by the amount of such reduction.

SEC. 1602. REPEAL OF EXCLUSION FOR INTEREST ON LOANS USED TO ACQUIRE EMPLOYER SECURITIES.

(a) IN GENERAL.—Section 133 (relating to interest on certain loans used to acquire employer securities) is hereby repealed.

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (B) of section 291(e)(1) is amended by striking clause (iv) and by redesignating clause (v) as clause (iv).

(2) Section 812 is amended by striking subsection (g).

(3) Paragraph (5) of section 852(b) is amended by striking subparagraph (C).

(4) Paragraph (2) of section 4978(b) is amended by striking subparagraph (A) and all that follows and inserting the following:

> *"(A) first from qualified securities to which section 1042 applied acquired during the 3-year period ending on the date of the disposition, beginning with the securities first so acquired, and*
>
> *"(B) then from any other employer securities.*

If subsection (d) applies to a disposition, the disposition shall be treated as made from employer securities in the opposite order of the preceding sentence.".

(5)(A) Section 4978B (relating to tax on disposition of employer securities to which section 133 applied) is hereby repealed.

(B) The table of sections for chapter 43 is amended by striking the item relating to section 4978B.

(6) Subsection (e) of section 6047 is amended by striking paragraphs (1), (2), and (3) and inserting the following new paragraphs:

"(1) any employer maintaining, or the plan administrator (within the meaning of section 414(g)) of, an employee stock ownership plan which holds stock with respect to which section 404(k) applies to dividends paid on such stock, or

"(2) both such employer or plan administrator,".

(7) Subsection (f) of section 7872 is amended by striking paragraph (12).

(8) The table of sections for part III of subchapter B of chapter 1 is amended by striking the item relating to section 133.

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to loans made after the date of the enactment of this Act.

(2) REFINANCINGS.—The amendments made by this section shall not apply to loans made after the date of the enactment of this Act to refinance securities acquisition loans (determined without regard to section 133(b)(1)(B) of the Internal Revenue Code of 1986, as in effect on the day before the date of the enactment of this Act) made on or before such date or to refinance loans described in this paragraph if—

(A) the refinancing loans meet the requirements of section 133 of such Code (as so in effect),

(B) immediately after the refinancing the principal amount of the loan resulting from the refinancing does not exceed the principal amount of the refinanced loan (immediately before the refinancing), and

(C) the term of such refinancing loan does not extend beyond the last day of the term of the original securities acquisition loan.

For purposes of this paragraph, the term "securities acquisition loan" includes a loan from a corporation to an employee stock ownership plan described in section 133(b)(3) of such Code (as so in effect).

(3) EXCEPTION.—Any loan made pursuant to a binding written contract in effect before June 10, 1996, and at all times thereafter before such loan is made, shall be treated for purposes of paragraphs (1) and (2) as a loan made on or before the date of the enactment of this Act.

SEC. 1603. CERTAIN AMOUNTS DERIVED FROM FOREIGN CORPORATIONS TREATED AS UNRELATED BUSINESS TAXABLE INCOME.

(a) GENERAL RULE.—Subsection (b) of section 512 (relating to modifications) is amended by adding at the end the following new paragraph:

"(17) TREATMENT OF CERTAIN AMOUNTS DERIVED FROM FOREIGN CORPORATIONS.—

"(A) IN GENERAL.—Notwithstanding paragraph (1), any amount included in gross income under section 951(a)(1)(A) shall be included as an item of gross income derived from an unrelated trade or business to the extent the amount so included is attributable to insurance income (as defined in section 953) which, if derived directly by the organization, would be treated as gross income from an unrelated trade or business. There shall be allowed all deductions directly connected with amounts included in gross income under the preceding sentence.

"(B) EXCEPTION.—

"(i) IN GENERAL.—Subparagraph (A) shall not apply to income attributable to a policy of insurance or reinsurance with respect to which the person (directly or indirectly) insured is—

"(I) such organization,

"(II) an affiliate of such organization which is exempt from tax under section 501(a), or

"(III) a director or officer of, or an individual who (directly or indirectly) performs services for, such organization or affiliate but only if the insurance covers primarily risks associated with the performance of services in connection with such organization or affiliate.

"(ii) AFFILIATE.—For purposes of this subparagraph—

"(I) IN GENERAL.—The determination as to whether an entity is an affiliate of an organization shall be made under rules similar to the rules of section 168(h)(4)(B).

"(II) SPECIAL RULE.—Two or more organizations (and any affiliates of such organizations) shall be treated as affiliates if such organizations are colleges or universities described in section 170(b)(1)(A)(ii) or organizations described in section 170(b)(1)(A)(iii) and participate in an insurance arrangement that provides for any profits from such arrangement to be returned to the policyholders in their capacity as such.

"(C) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this paragraph, including regulations for the application of this paragraph in the case of income paid through 1 or more entities or between 2 or more chains of entities.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to amounts included in gross income in any taxable year beginning after December 31, 1995.

SEC. 1604. DEPRECIATION UNDER INCOME FORECAST METHOD.

(a) GENERAL RULE.—Section 167 (relating to depreciation) is amended by redesignating subsection (g) as subsection (h) and by inserting after subsection (f) the following new subsection:

"(g) DEPRECIATION UNDER INCOME FORECAST METHOD.—

"(1) IN GENERAL.—If the depreciation deduction allowable under this section to any taxpayer with respect to any property is determined under the income forecast method or any similar method—

"(A) the income from the property to be taken into account in determining the depreciation deduction under such method shall be equal to the amount of income earned in connection with the property before the close of the 10th taxable year following the taxable year in which the property was placed in service,

"(B) the adjusted basis of the property shall only include amounts with respect to which the requirements of section 461(h) are satisfied,

"(C) the depreciation deduction under such method for the 10th taxable year beginning after the taxable year in which the property was placed in service shall be equal to

the adjusted basis of such property as of the beginning of such 10th taxable year, and

"(D) such taxpayer shall pay (or be entitled to receive) interest computed under the look-back method of paragraph (2) for any recomputation year.

"(2) LOOK-BACK METHOD.—The interest computed under the look-back method of this paragraph for any recomputation year shall be determined by—

"(A) first determining the depreciation deductions under this section with respect to such property which would have been allowable for prior taxable years if the determination of the amounts so allowable had been made on the basis of the sum of the following (instead of the estimated income from such property)—

"(i) the actual income earned in connection with such property for periods before the close of the recomputation year, and

"(ii) an estimate of the future income to be earned in connection with such property for periods after the recomputation year and before the close of the 10th taxable year following the taxable year in which the property was placed in service,

"(B) second, determining (solely for purposes of computing such interest) the overpayment or underpayment of tax for each such prior taxable year which would result solely from the application of subparagraph (A), and

"(C) then using the adjusted overpayment rate (as defined in section 460(b)(7)), compounded daily, on the overpayment or underpayment determined under subparagraph (B).

For purposes of the preceding sentence, any cost incurred after the property is placed in service (which is not treated as a separate property under paragraph (5)) shall be taken into account by discounting (using the Federal mid-term rate determined under section 1274(d) as of the time such cost is incurred) such cost to its value as of the date the property is placed in service. The taxpayer may elect with respect to any property to have the preceding sentence not apply to such property.

"(3) EXCEPTION FROM LOOK-BACK METHOD.—Paragraph (1)(D) shall not apply with respect to any property which had a cost basis of $100,000 or less.

"(4) RECOMPUTATION YEAR.—For purposes of this subsection, except as provided in regulations, the term 'recomputation year' means, with respect to any property, the 3d and the 10th taxable years beginning after the taxable year in which the property was placed in service, unless the actual income earned in connection with the property for the period before the close of such 3d or 10th taxable year is within 10 percent of the income earned in connection with the property for such period which was taken into account under paragraph (1)(A).

"(5) SPECIAL RULES.—

"(A) CERTAIN COSTS TREATED AS SEPARATE PROPERTY.—For purposes of this subsection, the following costs shall be treated as separate properties:

"(i) Any costs incurred with respect to any property after the 10th taxable year beginning after the taxable year in which the property was placed in service.

"(ii) Any costs incurred after the property is placed in service and before the close of such 10th taxable year if such costs are significant and give rise to a significant increase in the income from the property which was not included in the estimated income from the property.

"(B) SYNDICATION INCOME FROM TELEVISION SERIES.—In the case of property which is 1 or more episodes in a television series, income from syndicating such series shall not be required to be taken into account under this subsection before the earlier of—

"(i) the 4th taxable year beginning after the date the first episode in such series is placed in service, or

"(ii) the earliest taxable year in which the taxpayer has an arrangement relating to the future syndication of such series.

"(C) SPECIAL RULES FOR FINANCIAL EXPLOITATION OF CHARACTERS, ETC.—For purposes of this subsection, in the case of television and motion picture films, the income from the property shall include income from the exploitation of characters, designs, scripts, scores, and other incidental income associated with such films, but only to the extent that such income is earned in connection with the ultimate use of such items by, or the ultimate sale of merchandise to, persons who are not related persons (within the meaning of section 267(b)) to the taxpayer.

"(D) COLLECTION OF INTEREST.—For purposes of subtitle F (other than sections 6654 and 6655), any interest required to be paid by the taxpayer under paragraph (1) for any recomputation year shall be treated as an increase in the tax imposed by this chapter for such year.

"(E) DETERMINATIONS.—For purposes of paragraph (2), determinations of the amount of income earned in connection with any property shall be made in the same manner as for purposes of applying the income forecast method; except that any income from the disposition of such property shall be taken into account.

"(F) TREATMENT OF PASS-THRU ENTITIES.—Rules similar to the rules of section 460(b)(4) shall apply for purposes of this subsection."

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendment made by subsection (a) shall apply to property placed in service after September 13, 1995.

(2) BINDING CONTRACTS.—The amendment made by subsection (a) shall not apply to any property produced or acquired by the taxpayer pursuant to a written contract which was binding on September 13, 1995, and at all times thereafter before such production or acquisition.

(3) UNDERPAYMENTS OF INCOME TAX.—No addition to tax shall be made under section 6662 of such Code as a result of

the application of subsection (d) of that section (relating to substantial understatements of income tax) with respect to any underpayment of income tax for any taxable year ending before such date of enactment, to the extent such underpayment was created or increased by the amendments made by subsection (a).

SEC. 1605. REPEAL OF EXCLUSION FOR PUNITIVE DAMAGES AND FOR DAMAGES NOT ATTRIBUTABLE TO PHYSICAL INJURIES OR SICKNESS.

(a) IN GENERAL.—Paragraph (2) of section 104(a) (relating to compensation for injuries or sickness) is amended to read as follows:

"(2) the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness;".

(b) EMOTIONAL DISTRESS AS SUCH TREATED AS NOT PHYSICAL INJURY OR PHYSICAL SICKNESS.—Section 104(a) is amended by striking the last sentence and inserting the following new sentence: "For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. The preceding sentence shall not apply to an amount of damages not in excess of the amount paid for medical care (described in subparagraph (A) or (B) of section 213(d)(1)) attributable to emotional distress.".

(c) APPLICATION OF PRIOR LAW FOR STATES IN WHICH ONLY PUNITIVE DAMAGES MAY BE AWARDED IN WRONGFUL DEATH ACTIONS.—Section 104 is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

"(c) APPLICATION OF PRIOR LAW IN CERTAIN CASES.—The phrase '(other than punitive damages)' shall not apply to punitive damages awarded in a civil action—

"(1) which is a wrongful death action, and

"(2) with respect to which applicable State law (as in effect on September 13, 1995 and without regard to any modification after such date) provides, or has been construed to provide by a court of competent jurisdiction pursuant to a decision issued on or before September 13, 1995, that only punitive damages may be awarded in such an action.

This subsection shall cease to apply to any civil action filed on or after the first date on which the applicable State law ceases to provide (or is no longer construed to provide) the treatment described in paragraph (2).".

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to amounts received after the date of the enactment of this Act, in taxable years ending after such date.

(2) EXCEPTION.—The amendments made by this section shall not apply to any amount received under a written binding agreement, court decree, or mediation award in effect on (or issued on or before) September 13, 1995.

SEC. 1606. REPEAL OF DIESEL FUEL TAX REBATE TO PURCHASERS OF DIESEL-POWERED AUTOMOBILES AND LIGHT TRUCKS.

(a) IN GENERAL.—Section 6427 (relating to fuels not used for taxable purposes) is amended by striking subsection (g).

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (3) of section 34(a) is amended to read as follows:

"(3) under section 6427 with respect to fuels used for nontaxable purposes or resold during the taxable year (determined without regard to section 6427(k)).".

(2) Paragraphs (1) and (2)(A) of section 6427(i) are each amended—

(A) by striking "(g),", and

(B) by striking "(or a qualified diesel powered highway vehicle purchased)" each place it appears.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to vehicles purchased after the date of the enactment of this Act.

SEC. 1607. EXTENSION AND PHASEDOWN OF LUXURY PASSENGER AUTOMOBILE TAX.

(a) EXTENSION.—Subsection (f) of section 4001 is amended by striking "1999" and inserting "2002".

(b) PHASEDOWN.—Section 4001 is amended by redesignating subsection (f) (as amended by subsection (a) of this section) as subsection (g) and by inserting after subsection (e) the following new subsection:

"(f) PHASEDOWN.—For sales occurring in calendar years after 1995 and before 2003, subsection (a) shall be applied by substituting for '10 percent' the percentage determined in accordance with the following table:

"If the calendar year is:	*The percentage is:*
1996	*9 percent*
1997	*8 percent*
1998	*7 percent*
1999	*6 percent*
2000	*5 percent*
2001	*4 percent*
2002	*3 percent.".*

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to sales occurring after the date which is 7 days after the date of the enactment of this Act.

SEC. 1608. TERMINATION OF FUTURE TAX-EXEMPT BOND FINANCING FOR LOCAL FURNISHERS OF ELECTRICITY AND GAS.

(a) IN GENERAL.—Section 142(f) (relating to local furnishing of electric energy or gas) is amended by adding at the end the following new paragraphs:

"(3) TERMINATION OF FUTURE FINANCING.—For purposes of this section, no bond may be issued as part of an issue described in subsection (a)(8) with respect to a facility for the local furnishing of electric energy or gas on or after the date of the enactment of this paragraph unless—

"(A) the facility will—

"(i) be used by a person who is engaged in the local furnishing of that energy source on January 1, 1997, and

"(ii) be used to provide service within the area served by such person on January 1, 1997, (or within

a county or city any portion of which is within such area), or

"(B) the facility will be used by a successor in interest to such person for the same use and within the same service area as described in subparagraph (A).

"(4) ELECTION TO TERMINATE TAX-EXEMPT BOND FINANCING BY CERTAIN FURNISHERS.—

"(A) IN GENERAL.—In the case of a facility financed with bonds issued before the date of the enactment of this paragraph which would cease to be tax-exempt by reason of the failure to meet the local furnishing requirement of subsection (a)(8) as a result of a service area expansion, such bonds shall not cease to be tax-exempt bonds (and section 150(b)(4) shall not apply) if the person engaged in such local furnishing by such facility makes an election described in subparagraph (B).

"(B) ELECTION.—An election is described in this subparagraph if it is an election made in such manner as the Secretary prescribes, and such person (or its predecessor in interest) agrees that—

"(i) such election is made with respect to all facilities for the local furnishing of electric energy or gas, or both, by such person,

"(ii) no bond exempt from tax under section 103 and described in subsection (a)(8) may be issued on or after the date of the enactment of this paragraph with respect to all such facilities of such person,

"(iii) any expansion of the service area—

"(I) is not financed with the proceeds of any exempt facility bond described in subsection (a)(8), and

"(II) is not treated as a nonqualifying use under the rules of paragraph (2), and

"(iv) all outstanding bonds used to finance the facilities for such person are redeemed not later than 6 months after the later of—

"(I) the earliest date on which such bonds may be redeemed, or

"(II) the date of the election.

"(C) RELATED PERSONS.—For purposes of this paragraph, the term 'person' includes a group of related persons (within the meaning of section 144(a)(3)) which includes such person.".

(b) NO INFERENCE WITH RESPECT TO OUTSTANDING BONDS.—The use of the term "person" in section 142(f)(3) of the Internal Revenue Code of 1986, as added by subsection (a), shall not be construed to affect the tax-exempt status of interest on any bonds issued before the date of the enactment of this Act.

SEC. 1609. EXTENSION OF AIRPORT AND AIRWAY TRUST FUND EXCISE TAXES.

(a) FUEL TAX.—

(1) Subparagraph (A) of section 4091(b)(3) is amended to read as follows:

"(A) The rate of tax specified in paragraph (1) shall be 4.3 cents per gallon—

"(i) after December 31, 1995, and before the date which is 7 calendar days after the date of the enactment of the Small Business Job Protection Act of 1996, and

"(ii) after December 31, 1996.".

(2) Section 4081(d) is amended—

(A) by adding at the end the following new paragraph:

"(3) AVIATION GASOLINE.—After December 31, 1996, the rate of tax specified in subsection (a)(2)(A)(i) on aviation gasoline shall be 4.3 cents per gallon.", and

(B) by inserting "(other than the tax on aviation gasoline)" after "subsection (a)(2)(A)".

(3) Section 4041(c)(5) is amended by inserting ", and during the period beginning on the date which is 7 calendar days after the date of the enactment of the Small Business Job Protection Act of 1996 and ending on December 31, 1996" after "December 31, 1995".

(b) TICKET TAXES.—Sections 4261(g) and 4271(d) are each amended by striking "January 1, 1996" and inserting "January 1, 1996, and to transportation beginning on or after the date which is 7 calendar days after the date of the enactment of the Small Business Job Protection Act of 1996 and before January 1, 1997".

(c) TRANSFERS TO AIRPORT AND AIRWAY TRUST FUND.—

(1) Subsection (b) of section 9502 is amended by striking "January 1, 1996" each place it appears and inserting "January 1, 1997".

(2) Paragraph (3) of section 9502(f) is amended to read as follows:

"(3) TERMINATION.—Notwithstanding the preceding provisions of this subsection, the Airport and Airway Trust Fund financing rate shall be zero with respect to—

"(A) taxes imposed after December 31, 1995, and before the date which is 7 calendar days after the date of the enactment of the Small Business Job Protection Act of 1996, and

"(B) taxes imposed after December 31, 1996.".

(3) Subsection (d) of section 9502 is amended by adding at the end the following new paragraph:

"(5) TRANSFERS FROM AIRPORT AND AIRWAY TRUST FUND ON ACCOUNT OF REFUNDS OF TAXES ON TRANSPORTATION BY AIR.—The Secretary of the Treasury shall pay from time to time from the Airport and Airway Trust Fund into the general fund of the Treasury amounts equivalent to the amounts paid after December 31, 1995, under section 6402 (relating to authority to make credits or refunds) or section 6415 (relating to credits or refunds to persons who collected certain taxes) in respect of taxes under sections 4261 and 4271.".

(d) EXCISE TAX EXEMPTION FOR CERTAIN EMERGENCY MEDICAL TRANSPORTATION BY AIR AMBULANCE.—Subsection (f) of section 4261 (relating to imposition of tax on transportation by air) is amended to read as follows:

"(f) EXEMPTION FOR AIR AMBULANCES PROVIDING CERTAIN EMERGENCY MEDICAL TRANSPORTATION.—No tax shall be imposed under this section or section 4271 on any air transportation for the purpose of providing emergency medical services—

"(1) by helicopter, or

"(2) by a fixed-wing aircraft equipped for and exclusively dedicated to acute care emergency medical services.".

(e) EXEMPTION FOR CERTAIN HELICOPTER USES.—Subsection (e) of section 4261 is amended by adding at the end the following new sentence: "In the case of helicopter transportation described in paragraph (1), this subsection shall be applied by treating each flight segment as a distinct flight.".

(f) FLIGHT-BY-FLIGHT DETERMINATION OF AVAILABILITY FOR HIRE FOR AFFILIATED GROUPS.—Section 4282 is amended by redesignating subsection (b) as subsection (c) and by inserting after subsection (a) the following new subsection:

"(b) AVAILABILITY FOR HIRE.—For purposes of subsection (a), the determination of whether an aircraft is available for hire by persons who are not members of an affiliated group shall be made on a flight-by-flight basis."

(g) CONSOLIDATION OF TAXES ON AVIATION GASOLINE.—

(1) IN GENERAL.—Subparagraph (A) of section 4081(a)(2) (relating to imposition of tax on gasoline and diesel fuel) is amended by redesignating clause (ii) as clause (iii) and by striking clause (i) and inserting the following:

"(i) in the case of gasoline other than aviation gasoline, 18.3 cents per gallon,

"(ii) in the case of aviation gasoline, 19.3 cents per gallon, and".

(2) TERMINATION.—Subsection (d) of section 4081 is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following new paragraph:

"(2) AVIATION GASOLINE.—On and after January 1, 1997, the rate specified in subsection (a)(2)(A)(ii) shall be 4.3 cents per gallon."

(3) REPEAL OF RETAIL LEVEL TAX.—

(A) Subsection (c) of section 4041 is amended by striking paragraphs (2) and (3) and by redesignating paragraphs (4) and (5) as paragraphs (2) and (3), respectively.

(B) Paragraph (3) of section 4041(c), as redesignated by paragraph (1), is amended by striking "paragraphs (1) and (2)" and inserting "paragraph (1)".

(4) CONFORMING AMENDMENTS.—

(A) Paragraph (1) of section 4041(k) is amended by adding "and" at the end of subparagraph (A), by striking ", and" at the end of subparagraph (B) and inserting a period, and by striking subparagraph (C).

(B) Paragraph (1) of section 4081(d) is amended by striking "each rate of tax specified in subsection (a)(2)(A)" and inserting "the rates of tax specified in clauses (i) and (iii) of subsection (a)(2)(A)".

(C) Sections 6421(f)(2)(A) and 9502(f)(1)(A) are each amended by striking "section 4041(c)(4)" and inserting "section 4041(c)(2)".

(D) Paragraph (2) of section 9502(b) is amended by striking "14 cents" and inserting "15 cents".

(h) FLOOR STOCKS TAXES ON AVIATION FUEL.—

(1) IMPOSITION OF TAX.—In the case of aviation fuel on which tax was imposed under section 4091 of the Internal Revenue Code of 1986 before the tax-increase date described in paragraph (3)(A)(i) and which is held on such date by any person, there is hereby imposed a floor stocks tax of 17.5 cents per gallon.

(2) LIABILITY FOR TAX AND METHOD OF PAYMENT.—

(A) LIABILITY FOR TAX.—A person holding aviation fuel on a tax-increase date to which the tax imposed by paragraph (1) applies shall be liable for such tax.

(B) METHOD OF PAYMENT.—The tax imposed by paragraph (1) shall be paid in such manner as the Secretary shall prescribe.

(C) TIME FOR PAYMENT.—The tax imposed by paragraph (1) with respect to any tax-increase date shall be paid on or before the first day of the 7th month beginning after such tax-increase date.

(3) DEFINITIONS.—For purposes of this subsection—

(A) TAX INCREASE DATE.—The term "tax-increase date" means the date which is 7 calendar days after the date of the enactment of this Act.

(B) AVIATION FUEL.—The term "aviation fuel" has the meaning given such term by section 4093 of such Code.

(C) HELD BY A PERSON.—Aviation fuel shall be considered as "held by a person" if title thereto has passed to such person (whether or not delivery to the person has been made).

(D) SECRETARY.—The term "Secretary" means the Secretary of the Treasury or his delegate.

(4) EXCEPTION FOR EXEMPT USES.—The tax imposed by paragraph (1) shall not apply to aviation fuel held by any person on any tax-increase date exclusively for any use for which a credit or refund of the entire tax imposed by section 4091 of such Code is allowable for aviation fuel purchased on or after such tax-increase date for such use.

(5) EXCEPTION FOR CERTAIN AMOUNTS OF FUEL.—

(A) IN GENERAL.—No tax shall be imposed by paragraph (1) on aviation fuel held on any tax-increase date by any person if the aggregate amount of aviation fuel held by such person on such date does not exceed 2,000 gallons. The preceding sentence shall apply only if such person submits to the Secretary (at the time and in the manner required by the Secretary) such information as the Secretary shall require for purposes of this paragraph.

(B) EXEMPT FUEL.—For purposes of subparagraph (A), there shall not be taken into account fuel held by any person which is exempt from the tax imposed by paragraph (1) by reason of paragraph (4).

(C) CONTROLLED GROUPS.—For purposes of this paragraph—

(i) CORPORATIONS.—

(I) IN GENERAL.—All persons treated as a controlled group shall be treated as 1 person.

(II) CONTROLLED GROUP.—The term "controlled group" has the meaning given to such term by subsection (a) of section 1563 of such Code; except that for such purposes the phrase "more than 50 percent" shall be substituted for the phrase "at least 80 percent" each place it appears in such subsection.

(ii) NONINCORPORATED PERSONS UNDER COMMON CONTROL.—Under regulations prescribed by the Secretary, principles similar to the principles of clause (i) shall apply to a group of persons under common control where 1 or more of such persons is not a corporation.

(6) OTHER LAW APPLICABLE.—All provisions of law, including penalties, applicable with respect to the taxes imposed by section 4091 of such Code shall, insofar as applicable and not inconsistent with the provisions of this subsection, apply with respect to the floor stock taxes imposed by paragraph (1) to the same extent as if such taxes were imposed by such section 4091.

(i) EFFECTIVE DATE.—The amendments made by this section shall take effect on the 7th calendar day after the date of the enactment of this Act, except that the amendments made by subsection (b) shall not apply to any amount paid before such date.

SEC. 1610. BASIS ADJUSTMENT TO PROPERTY HELD BY CORPORATION WHERE STOCK IN CORPORATION IS REPLACEMENT PROPERTY UNDER INVOLUNTARY CONVERSION RULES.

(a) IN GENERAL.—Subsection (b) of section 1033 is amended to read as follows:

"(b) BASIS OF PROPERTY ACQUIRED THROUGH INVOLUNTARY CONVERSION.—

"(1) CONVERSIONS DESCRIBED IN SUBSECTION (a)(1).—If the property was acquired as the result of a compulsory or involuntary conversion described in subsection (a)(1), the basis shall be the same as in the case of the property so converted—

"(A) decreased in the amount of any money received by the taxpayer which was not expended in accordance with the provisions of law (applicable to the year in which such conversion was made) determining the taxable status of the gain or loss upon such conversion, and

"(B) increased in the amount of gain or decreased in the amount of loss to the taxpayer recognized upon such conversion under the law applicable to the year in which such conversion was made.

"(2) CONVERSIONS DESCRIBED IN SUBSECTION (a)(2).—In the case of property purchased by the taxpayer in a transaction described in subsection (a)(2) which resulted in the nonrecognition of any part of the gain realized as the result of a compulsory or involuntary conversion, the basis shall be the cost of such property decreased in the amount of the gain not so recognized; and if the property purchased consists of more than 1 piece of property, the basis determined under this sentence shall be allo-

cated to the purchased properties in proportion to their respective costs.

"(3) PROPERTY HELD BY CORPORATION THE STOCK OF WHICH IS REPLACEMENT PROPERTY.—

"(A) IN GENERAL.—If the basis of stock in a corporation is decreased under paragraph (2), an amount equal to such decrease shall also be applied to reduce the basis of property held by the corporation at the time the taxpayer acquired control (as defined in subsection (a)(2)(E)) of such corporation.

"(B) LIMITATION.—Subparagraph (A) shall not apply to the extent that it would (but for this subparagraph) require a reduction in the aggregate adjusted bases of the property of the corporation below the taxpayer's adjusted basis of the stock in the corporation (determined immediately after such basis is decreased under paragraph (2)).

"(C) ALLOCATION OF BASIS REDUCTION.—The decrease required under subparagraph (A) shall be allocated—

"(i) first to property which is similar or related in service or use to the converted property,

"(ii) second to depreciable property (as defined in section 1017(b)(3)(B)) not described in clause (i), and

"(iii) then to other property.

"(D) SPECIAL RULES.—

"(i) REDUCTION NOT TO EXCEED ADJUSTED BASIS OF PROPERTY.—No reduction in the basis of any property under this paragraph shall exceed the adjusted basis of such property (determined without regard to such reduction).

"(ii) ALLOCATION OF REDUCTION AMONG PROPERTIES.—If more than 1 property is described in a clause of subparagraph (C), the reduction under this paragraph shall be allocated among such property in proportion to the adjusted bases of such property (as so determined).".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to involuntary conversions occurring after the date of the enactment of this Act.

SEC. 1611. TREATMENT OF CERTAIN INSURANCE CONTRACTS ON RETIRED LIVES.

(a) GENERAL RULE.—

(1) Paragraph (2) of section 817(d) (defining variable contract) is amended by striking "or" at the end of subparagraph (A), by striking "and" at the end of subparagraph (B) and inserting "or", and by inserting after subparagraph (B) the following new subparagraph:

"(C) provides for funding of insurance on retired lives as described in section 807(c)(6), and".

(2) Paragraph (3) of section 817(d) is amended by striking "or" at the end of subparagraph (A), by striking the period at the end of subparagraph (B) and inserting ", or", and by inserting after subparagraph (B) the following new subparagraph:

"(C) in the case of funds held under a contract described in paragraph (2)(C), the amounts paid in, or the

amounts paid out, reflect the investment return and the market value of the segregated asset account.".

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1995.

SEC. 1612. TREATMENT OF MODIFIED GUARANTEED CONTRACTS.

(a) GENERAL RULE.—Subpart E of part I of subchapter L of chapter 1 (relating to definitions and special rules) is amended by inserting after section 817 the following new section:

"SEC. 817A. SPECIAL RULES FOR MODIFIED GUARANTEED CONTRACTS.

"(a) COMPUTATION OF RESERVES.—In the case of a modified guaranteed contract, clause (ii) of section 807(e)(1)(A) shall not apply.

"(b) SEGREGATED ASSETS UNDER MODIFIED GUARANTEED CONTRACTS MARKED TO MARKET.—

"(1) IN GENERAL.—In the case of any life insurance company, for purposes of this subtitle—

"(A) Any gain or loss with respect to a segregated asset shall be treated as ordinary income or loss, as the case may be.

"(B) If any segregated asset is held by such company as of the close of any taxable year—

"(i) such company shall recognize gain or loss as if such asset were sold for its fair market value on the last business day of such taxable year, and

"(ii) any such gain or loss shall be taken into account for such taxable year.

Proper adjustment shall be made in the amount of any gain or loss subsequently realized for gain or loss taken into account under the preceding sentence. The Secretary may provide by regulations for the application of this subparagraph at times other than the times provided in this subparagraph.

"(2) SEGREGATED ASSET.—For purposes of paragraph (1), the term 'segregated asset' means any asset held as part of a segregated account referred to in subsection (d)(1) under a modified guaranteed contract.

"(c) SPECIAL RULE IN COMPUTING LIFE INSURANCE RESERVES.—For purposes of applying section 816(b)(1)(A) to any modified guaranteed contract, an assumed rate of interest shall include a rate of interest determined, from time to time, with reference to a market rate of interest.

"(d) MODIFIED GUARANTEED CONTRACT DEFINED.—For purposes of this section, the term 'modified guaranteed contract' means a contract not described in section 817—

"(1) all or part of the amounts received under which are allocated to an account which, pursuant to State law or regulation, is segregated from the general asset accounts of the company and is valued from time to time with reference to market values,

"(2) which—

"(A) provides for the payment of annuities,

"(B) is a life insurance contract, or

"(C) is a pension plan contract which is not a life, accident, or health, property, casualty, or liability contract,

"(3) for which reserves are valued at market for annual statement purposes, and

"(4) which provides for a net surrender value or a policyholder's fund (as defined in section 807(e)(1)).

If only a portion of a contract is not described in section 817, such portion shall be treated for purposes of this section as a separate contract.

"(e) REGULATIONS.—The Secretary may prescribe regulations—

"(1) to provide for the treatment of market value adjustments under sections 72, 7702, 7702A, and 807(e)(1)(B),

"(2) to determine the interest rates applicable under sections 807(c)(3), 807(d)(2)(B), and 812 with respect to a modified guaranteed contract annually, in a manner appropriate for modified guaranteed contracts and, to the extent appropriate for such a contract, to modify or waive the applicability of section 811(d),

"(3) to provide rules to limit ordinary gain or loss treatment to assets constituting reserves for modified guaranteed contracts (and not other assets) of the company,

"(4) to provide appropriate treatment of transfers of assets to and from the segregated account, and

"(5) as may be necessary or appropriate to carry out the purposes of this section.".

(b) CLERICAL AMENDMENT.—The table of sections for subpart E of part I of subchapter L of chapter 1 is amended by inserting after the item relating to section 817 the following new item:

"Sec. 817A. Special rules for modified guaranteed contracts.".

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1995.

(2) TREATMENT OF NET ADJUSTMENTS.—Except as provided in paragraph (3), in the case of any taxpayer required by the amendments made by this section to change its calculation of reserves to take into account market value adjustments and to mark segregated assets to market for any taxable year—

(A) such changes shall be treated as a change in method of accounting initiated by the taxpayer,

(B) such changes shall be treated as made with the consent of the Secretary, and

(C) the adjustments required by reason of section 481 of the Internal Revenue Code of 1986, shall be taken into account as ordinary income by the taxpayer for the taxpayer's first taxable year beginning after December 31, 1995.

(3) LIMITATION ON LOSS RECOGNITION AND ON DEDUCTION FOR RESERVE INCREASES.—

(A) LIMITATION ON LOSS RECOGNITION.—

(i) IN GENERAL.—The aggregate loss recognized by reason of the application of section 481 of the Internal Revenue Code of 1986 with respect to section 817A(b) of such Code (as added by this section) for the first tax-

able year of the taxpayer beginning after December 31, 1995, shall not exceed the amount included in the taxpayer's gross income for such year by reason of the excess (if any) of—

(I) the amount of life insurance reserves as of the close of the prior taxable year, over

(II) the amount of such reserves as of the beginning of such first taxable year,

to the extent such excess is attributable to subsection (a) of such section 817A. Notwithstanding the preceding sentence, the adjusted basis of each segregated asset shall be determined as if all such losses were recognized.

(ii) DISALLOWED LOSS ALLOWED OVER PERIOD.—The amount of the loss which is not allowed under clause (i) shall be allowed ratably over the period of 7 taxable years beginning with the taxpayer's first taxable year beginning after December 31, 1995.

(B) LIMITATION ON DEDUCTION FOR INCREASE IN RESERVES.—

(i) IN GENERAL.—The deduction allowed for the first taxable year of the taxpayer beginning after December 31, 1995, by reason of the application of section 481 of such Code with respect to section 817A(a) of such Code (as added by this section) shall not exceed the aggregate built-in gain recognized by reason of the application of such section 481 with respect to section 817A(b) of such Code (as added by this section) for such first taxable year.

(ii) DISALLOWED DEDUCTION ALLOWED OVER PERIOD.—The amount of the deduction which is disallowed under clause (i) shall be allowed ratably over the period of 7 taxable years beginning with the taxpayer's first taxable year beginning after December 31, 1995.

(iii) BUILT-IN GAIN.—For purposes of this subparagraph, the built-in gain on an asset is the amount equal to the excess of—

(I) the fair market value of the asset as of the beginning of the first taxable year of the taxpayer beginning after December 31, 1995, over

(II) the adjusted basis of such asset as of such time.

SEC. 1613. TREATMENT OF CONTRIBUTIONS IN AID OF CONSTRUCTION.

(a) TREATMENT OF CONTRIBUTIONS IN AID OF CONSTRUCTION.—

(1) IN GENERAL.—Section 118 (relating to contributions to the capital of a corporation) is amended—

(A) by redesignating subsection (c) as subsection (e), and

(B) by inserting after subsection (b) the following new subsections:

"(c) SPECIAL RULES FOR WATER AND SEWERAGE DISPOSAL UTILITIES.—

"(1) GENERAL RULE.—For purposes of this section, the term 'contribution to the capital of the taxpayer' includes any amount of money or other property received from any person (whether or not a shareholder) by a regulated public utility which provides water or sewerage disposal services if—

"(A) such amount is a contribution in aid of construction,

"(B) in the case of contribution of property other than water or sewerage disposal facilities, such amount meets the requirements of the expenditure rule of paragraph (2), and

"(C) such amount (or any property acquired or constructed with such amount) is not included in the taxpayer's rate base for ratemaking purposes.

"(2) EXPENDITURE RULE.—An amount meets the requirements of this paragraph if—

"(A) an amount equal to such amount is expended for the acquisition or construction of tangible property described in section 1231(b)—

"(i) which is the property for which the contribution was made or is of the same type as such property, and

"(ii) which is used predominantly in the trade or business of furnishing water or sewerage disposal services,

"(B) the expenditure referred to in subparagraph (A) occurs before the end of the second taxable year after the year in which such amount was received, and

"(C) accurate records are kept of the amounts contributed and expenditures made, the expenditures to which contributions are allocated, and the year in which the contributions and expenditures are received and made.

"(3) DEFINITIONS.—For purposes of this subsection—

"(A) CONTRIBUTION IN AID OF CONSTRUCTION.—The term 'contribution in aid of construction' shall be defined by regulations prescribed by the Secretary, except that such term shall not include amounts paid as service charges for starting or stopping services.

"(B) PREDOMINANTLY.—The term 'predominantly' means 80 percent or more.

"(C) REGULATED PUBLIC UTILITY.—The term 'regulated public utility' has the meaning given such term by section 7701(a)(33), except that such term shall not include any utility which is not required to provide water or sewerage disposal services to members of the general public in its service area.

"(4) DISALLOWANCE OF DEDUCTIONS AND CREDITS; ADJUSTED BASIS.—Notwithstanding any other provision of this subtitle, no deduction or credit shall be allowed for, or by reason of, any expenditure which constitutes a contribution in aid of construction to which this subsection applies. The adjusted basis of any property acquired with contributions in aid of construction to which this subsection applies shall be zero.

"(d) STATUTE OF LIMITATIONS.—If the taxpayer for any taxable year treats an amount as a contribution to the capital of the taxpayer described in subsection (c), then—

"(1) the statutory period for the assessment of any deficiency attributable to any part of such amount shall not expire before the expiration of 3 years from the date the Secretary is notified by the taxpayer (in such manner as the Secretary may prescribe) of—

"(A) the amount of the expenditure referred to in subparagraph (A) of subsection (c)(2),

"(B) the taxpayer's intention not to make the expenditures referred to in such subparagraph, or

"(C) a failure to make such expenditure within the period described in subparagraph (B) of subsection (c)(2), and

"(2) such deficiency may be assessed before the expiration of such 3-year period notwithstanding the provisions of any other law or rule of law which would otherwise prevent such assessment.".

(2) CONFORMING AMENDMENT.—Section 118(b) is amended by inserting "except as provided in subsection (c)," before "the term".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to amounts received after June 12, 1996.

(b) RECOVERY METHOD AND PERIOD FOR WATER UTILITY PROPERTY.—

(1) REQUIREMENT TO USE STRAIGHT LINE METHOD.—Section 168(b)(3) is amended by adding at the end the following new subparagraph:

"(F) Water utility property described in subsection (e)(5).".

(2) 25-YEAR RECOVERY PERIOD.—The table contained in section 168(c)(1) is amended by inserting the following item after the item relating to 20-year property:

"Water utility property	*25 years".*

(3) WATER UTILITY PROPERTY.—

(A) IN GENERAL.—Section 168(e) is amended by adding at the end the following new paragraph:

"(5) WATER UTILITY PROPERTY.—The term 'water utility property' means property—

"(A) which is an integral part of the gathering, treatment, or commercial distribution of water, and which, without regard to this paragraph, would be 20-year property, and

"(B) any municipal sewer.".

(B) CONFORMING AMENDMENTS.—Section 168 is amended—

(i) by striking subparagraph (F) of subsection (e)(3), and

(ii) by striking the item relating to subparagraph (F) in the table in subsection (g)(3).

(4) ALTERNATIVE SYSTEM.—Clause (iv) of section 168(g)(2)(C) is amended by inserting "or water utility property" after "tunnel bore".

(5) EFFECTIVE DATE.—The amendments made by this subsection shall apply to property placed in service after June 12, 1996, other than property placed in service pursuant to a binding contract in effect before June 10, 1996, and at all times thereafter before the property is placed in service.

SEC. 1614. ELECTION TO CEASE STATUS AS QUALIFIED SCHOLARSHIP FUNDING CORPORATION.

(a) IN GENERAL.—Subsection (d) of section 150 (relating to definitions and special rules) is amended by adding at the end the following new paragraph:

"(3) ELECTION TO CEASE STATUS AS QUALIFIED SCHOLARSHIP FUNDING CORPORATION.—

"(A) IN GENERAL.—Any qualified scholarship funding bond, and qualified student loan bond, outstanding on the date of the issuer's election under this paragraph (and any bond (or series of bonds) issued to refund such a bond) shall not fail to be a tax-exempt bond solely because the issuer ceases to be described in subparagraphs (A) and (B) of paragraph (2) if the issuer meets the requirements of subparagraphs (B) and (C) of this paragraph.

"(B) ASSETS AND LIABILITIES OF ISSUER TRANSFERRED TO TAXABLE SUBSIDIARY.—The requirements of this subparagraph are met by an issuer if—

"(i) all of the student loan notes of the issuer and other assets pledged to secure the repayment of qualified scholarship funding bond indebtedness of the issuer are transferred to another corporation within a reasonable period after the election is made under this paragraph;

"(ii) such transferee corporation assumes or otherwise provides for the payment of all of the qualified scholarship funding bond indebtedness of the issuer within a reasonable period after the election is made under this paragraph;

"(iii) to the extent permitted by law, such transferee corporation assumes all of the responsibilities, and succeeds to all of the rights, of the issuer under the issuer's agreements with the Secretary of Education in respect of student loans;

"(iv) immediately after such transfer, the issuer, together with any other issuer which has made an election under this paragraph in respect of such transferee, hold all of the senior stock in such transferee corporation; and

"(v) such transferee corporation is not exempt from tax under this chapter.

"(C) ISSUER TO OPERATE AS INDEPENDENT ORGANIZATION DESCRIBED IN SECTION 501(C)(3).—The requirements of this subparagraph are met by an issuer if, within a reasonable period after the transfer referred to in subparagraph (B)—

"(i) the issuer is described in section 501(c)(3) and exempt from tax under section 501(a);

"(ii) the issuer no longer is described in subparagraphs (A) and (B) of paragraph (2); and

"(iii) at least 80 percent of the members of the board of directors of the issuer are independent members.

"(D) SENIOR STOCK.—For purposes of this paragraph, the term 'senior stock' means stock—

"(i) which participates pro rata and fully in the equity value of the corporation with all other common stock of the corporation but which has the right to payment of liquidation proceeds prior to payment of liquidation proceeds in respect of other common stock of the corporation;

"(ii) which has a fixed right upon liquidation and upon redemption to an amount equal to the greater of—

"(I) the fair market value of such stock on the date of liquidation or redemption (whichever is applicable); or

"(II) the fair market value of all assets transferred in exchange for such stock and reduced by the amount of all liabilities of the corporation which has made an election under this paragraph assumed by the transferee corporation in such transfer;

"(iii) the holder of which has the right to require the transferee corporation to redeem on a date that is not later than 10 years after the date on which an election under this paragraph was made and pursuant to such election such stock was issued; and

"(iv) in respect of which, during the time such stock is outstanding, there is not outstanding any equity interest in the corporation having any liquidation, redemption or dividend rights in the corporation which are superior to those of such stock.

"(E) INDEPENDENT MEMBER.—The term 'independent member' means a member of the board of directors of the issuer who (except for services as a member of such board) receives no compensation directly or indirectly—

"(i) for services performed in connection with such transferee corporation, or

"(ii) for services as a member of the board of directors or as an officer of such transferee corporation.

For purposes of clause (ii), the term 'officer' includes any individual having powers or responsibilities similar to those of officers.

"(F) COORDINATION WITH CERTAIN PRIVATE FOUNDATION TAXES.—For purposes of sections 4942 (relating to the excise tax on a failure to distribute income) and 4943 (relating to the excise tax on excess business holdings), the transferee corporation referred to in subparagraph (B) shall be treated as a functionally related business (within the meaning of section 4942(j)(4)) with respect to the issuer during the period commencing with the date on which an

election is made under this paragraph and ending on the date that is the earlier of—

"(i) the last day of the last taxable year for which more than 50 percent of the gross income of such transferee corporation is derived from, or more than 50 percent of the assets (by value) of such transferee corporation consists of, student loan notes incurred under the Higher Education Act of 1965; or

"(ii) the last day of the taxable year of the issuer during which occurs the date which is 10 years after the date on which the election under this paragraph is made.

"(G) ELECTION.—An election under this paragraph may be revoked only with the consent of the Secretary.".

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act.

SEC. 1615. CERTAIN TAX BENEFITS DENIED TO INDIVIDUALS FAILING TO PROVIDE TAXPAYER IDENTIFICATION NUMBERS.

(a) PERSONAL EXEMPTION.—

(1) IN GENERAL.—Section 151 (relating to allowance of deductions for personal exemptions) is amended by adding at the end the following new subsection:

"(e) IDENTIFYING INFORMATION REQUIRED.—No exemption shall be allowed under this section with respect to any individual unless the TIN of such individual is included on the return claiming the exemption.".

(2) CONFORMING AMENDMENTS.—

(A) Subsection (e) of section 6109 is repealed.

(B) Section 6724(d)(3) is amended by adding "and" at the end of subparagraph (C), by striking subparagraph (D), and by redesignating subparagraph (E) as subparagraph (D).

(b) DEPENDENT CARE CREDIT.—Subsection (e) of section 21 (relating to expenses for household and dependent care services necessary for gainful employment) is amended by adding at the end the following new paragraph:

"(10) IDENTIFYING INFORMATION REQUIRED WITH RESPECT TO QUALIFYING INDIVIDUALS.—No credit shall be allowed under this section with respect to any qualifying individual unless the TIN of such individual is included on the return claiming the credit.".

(c) EXTENSION OF PROCEDURES APPLICABLE TO MATHEMATICAL OR CLERICAL ERRORS.—Section 6213(g)(2) (relating to the definition of mathematical or clerical errors), as amended by the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, is amended by striking "and' at the end of subparagraph (F), by striking the period at the end of subparagraph (G) and inserting ", and", and by inserting at the end the following new subparagraph:

"(H) an omission of a correct TIN required under section 21 (relating to expenses for household and dependent care services necessary for gainful employment) or section 151 (relating to allowance of deductions for personal exemptions).".

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply with respect to returns the due date for which (without regard to extensions) is on or after the 30th day after the date of the enactment of this Act.

(2) SPECIAL RULE FOR 1995 AND 1996.—In the case of returns for taxable years beginning in 1995 or 1996, a taxpayer shall not be required by the amendments made by this section to provide a taxpayer identification number for a child who is born after October 31, 1995, in the case of a taxable year beginning in 1995 or November 30, 1996, in the case of a taxable year beginning in 1996.

SEC. 1616. REPEAL OF BAD DEBT RESERVE METHOD FOR THRIFT SAVINGS ASSOCIATIONS.

(a) IN GENERAL.—Section 593 (relating to reserves for losses on loans) is amended by adding at the end the following new subsections:

"(f) TERMINATION OF RESERVE METHOD.—Subsections (a), (b), (c), and (d) shall not apply to any taxable year beginning after December 31, 1995.

"(g) 6-YEAR SPREAD OF ADJUSTMENTS.—

"(1) IN GENERAL.—In the case of any taxpayer who is required by reason of subsection (f) to change its method of computing reserves for bad debts—

"(A) such change shall be treated as a change in a method of accounting,

"(B) such change shall be treated as initiated by the taxpayer and as having been made with the consent of the Secretary, and

"(C) the net amount of the adjustments required to be taken into account by the taxpayer under section 481(a)—

"(i) shall be determined by taking into account only applicable excess reserves, and

"(ii) as so determined, shall be taken into account ratably over the 6-taxable year period beginning with the first taxable year beginning after December 31, 1995.

"(2) APPLICABLE EXCESS RESERVES.—

"(A) IN GENERAL.—For purposes of paragraph (1), the term 'applicable excess reserves' means the excess (if any) of—

"(i) the balance of the reserves described in subsection (c)(1) (other than the supplemental reserve) as of the close of the taxpayer's last taxable year beginning before January 1, 1996, over

"(ii) the lesser of—

"(I) the balance of such reserves as of the close of the taxpayer's last taxable year beginning before January 1, 1988, or

"(II) the balance of the reserves described in subclause (I), reduced in the same manner as under section 585(b)(2)(B)(ii) on the basis of the taxable years described in clause (i) and this clause.

"(B) SPECIAL RULE FOR THRIFTS WHICH BECOME SMALL BANKS.—In the case of a bank (as defined in section 581) which was not a large bank (as defined in section 585(c)(2)) for its first taxable year beginning after December 31, 1995—

"(i) the balance taken into account under subparagraph (A)(ii) shall not be less than the amount which would be the balance of such reserves as of the close of its last taxable year beginning before such date if the additions to such reserves for all taxable years had been determined under section 585(b)(2)(A), and

"(ii) the opening balance of the reserve for bad debts as of the beginning of such first taxable year shall be the balance taken into account under subparagraph (A)(ii) (determined after the application of clause (i) of this subparagraph).

The preceding sentence shall not apply for purposes of paragraphs (5) and (6) or subsection (e)(1).

"(3) RECAPTURE OF PRE-1988 RESERVES WHERE TAXPAYER CEASES TO BE BANK.—If, during any taxable year beginning after December 31, 1995, a taxpayer to which paragraph (1) applied is not a bank (as defined in section 581), paragraph (1) shall apply to the reserves described in paragraph (2)(A)(ii) and the supplemental reserve; except that such reserves shall be taken into account ratably over the 6-taxable year period beginning with such taxable year.

"(4) SUSPENSION OF RECAPTURE IF RESIDENTIAL LOAN REQUIREMENT MET.—

"(A) IN GENERAL.—In the case of a bank which meets the residential loan requirement of subparagraph (B) for the first taxable year beginning after December 31, 1995, or for the following taxable year—

"(i) no adjustment shall be taken into account under paragraph (1) for such taxable year, and

"(ii) such taxable year shall be disregarded in determining—

"(I) whether any other taxable year is a taxable year for which an adjustment is required to be taken into account under paragraph (1), and

"(II) the amount of such adjustment.

"(B) RESIDENTIAL LOAN REQUIREMENT.—A taxpayer meets the residential loan requirement of this subparagraph for any taxable year if the principal amount of the residential loans made by the taxpayer during such year is not less than the base amount for such year.

"(C) RESIDENTIAL LOAN.—For purposes of this paragraph, the term 'residential loan' means any loan described in clause (v) of section 7701(a)(19)(C) but only if such loan is incurred in acquiring, constructing, or improving the property described in such clause.

"(D) BASE AMOUNT.—For purposes of subparagraph (B), the base amount is the average of the principal amounts of the residential loans made by the taxpayer during the 6 most recent taxable years beginning on or before

December 31, 1995. At the election of the taxpayer who made such loans during each of such 6 taxable years, the preceding sentence shall be applied without regard to the taxable year in which such principal amount was the highest and the taxable year in such principal amount was the lowest. Such an election may be made only for the first taxable year beginning after such date, and, if made for such taxable year, shall apply to the succeeding taxable year unless revoked with the consent of the Secretary.

"(E) CONTROLLED GROUPS.—In the case of a taxpayer which is a member of any controlled group of corporations described in section 1563(a)(1), subparagraph (B) shall be applied with respect to such group.

"(5) CONTINUED APPLICATION OF FRESH START UNDER SECTION 585 TRANSITIONAL RULES.—In the case of a taxpayer to which paragraph (1) applied and which was not a large bank (as defined in section 585(c)(2)) for its first taxable year beginning after December 31, 1995:

"(A) IN GENERAL.—For purposes of determining the net amount of adjustments referred to in section 585(c)(3)(A)(iii), there shall be taken into account only the excess (if any) of the reserve for bad debts as of the close of the last taxable year before the disqualification year over the balance taken into account by such taxpayer under paragraph (2)(A)(ii) of this subsection.

"(B) TREATMENT UNDER ELECTIVE CUT-OFF METHOD.—For purposes of applying section 585(c)(4)—

"(i) the balance of the reserve taken into account under subparagraph (B) thereof shall be reduced by the balance taken into account by such taxpayer under paragraph (2)(A)(ii) of this subsection, and

"(ii) no amount shall be includible in gross income by reason of such reduction.

"(6) SUSPENDED RESERVE INCLUDED AS SECTION 381(c) ITEMS.—The balance taken into account by a taxpayer under paragraph (2)(A)(ii) of this subsection and the supplemental reserve shall be treated as items described in section 381(c).

"(7) CONVERSIONS TO CREDIT UNIONS.—In the case of a taxpayer to which paragraph (1) applied which becomes a credit union described in section 501(c) and exempt from taxation under section 501(a)—

"(A) any amount required to be included in the gross income of the credit union by reason of this subsection shall be treated as derived from an unrelated trade or business (as defined in section 513), and

"(B) for purposes of paragraph (3), the credit union shall not be treated as if it were a bank.

"(8) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out this subsection and subsection (e), including regulations providing for the application of such subsections in the case of acquisitions, mergers, spin-offs, and other reorganizations."

(b) CONFORMING AMENDMENTS.—

(1) Subsection (d) of section 50 is amended by adding at the end the following new sentence:

"Paragraphs (1)(A), (2)(A), and (4) of the section 46(e) referred to in paragraph (1) of this subsection shall not apply to any taxable year beginning after December 31, 1995."

(2) Subsection (e) of section 52 is amended by striking paragraph (1) and by redesignating paragraphs (2) and (3) as paragraphs (1) and (2), respectively.

(3) Subsection (a) of section 57 is amended by striking paragraph (4).

(4) Section 246 is amended by striking subsection (f).

(5) Clause (i) of section 291(e)(1)(B) is amended by striking "or to which section 593 applies".

(6) Subparagraph (A) of section 585(a)(2) is amended by striking "other than an organization to which section 593 applies".

(7)(A) The material preceding subparagraph (A) of section 593(e)(1) is amended by striking "by a domestic building and loan association or an institution that is treated as a mutual savings bank under section 591(b)" and inserting "by a taxpayer having a balance described in subsection (g)(2)(A)(ii)".

(B) Subparagraph (B) of section 593(e)(1) is amended to read as follows:

"(B) then out of the balance taken into account under subsection (g)(2)(A)(ii) (properly adjusted for amounts charged against such reserves for taxable years beginning after December 31, 1987),".

(C) The second sentence of section 593(e)(1) is amended by striking "the association or an institution that is treated as a mutual savings bank under section 591(b)" and inserting "a taxpayer having a balance described in subsection (g)(2)(A)(ii)".

(D) The third sentence of section 593(e)(1) is amended by striking "an association" and inserting "a taxpayer having a balance described in subsection (g)(2)(A)(ii)".

(E) Paragraph (1) of section 593(e) is amended by adding at the end the following new sentence: "This paragraph shall not apply to any distribution of all of the stock of a bank (as defined in section 581) to another corporation if, immediately after the distribution, such bank and such other corporation are members of the same affiliated group (as defined in section 1504) and the provisions of section 5(e) of the Federal Deposit Insurance Act (as in effect on December 31, 1995) or similar provisions are in effect."

(8) Section 595 is hereby repealed.

(9) Section 596 is hereby repealed.

(10) Subsection (a) of section 860E is amended—

(A) by striking "Except as provided in paragraph (2), the" in paragraph (1) and inserting "The",

(B) by striking paragraphs (2) and (4) and redesignating paragraphs (3), (5), and (6) as paragraphs (2), (3), and (4), respectively,

(C) by striking in paragraph (2) (as so redesignated) all that follows "subsection" and inserting a period, and

(D) by striking the last sentence of paragraph (4) (as so redesignated).

(11) Paragraph (3) of section 992(d) is amended by striking "or 593".

(12) Section 1038 is amended by striking subsection (f).

(13) Clause (ii) of section 1042(c)(4)(B) is amended by striking "or 593".

(14) Subsection (c) of section 1277 is amended by striking "or to which section 593 applies".

(15) Subparagraph (B) of section 1361(b)(2) is amended by striking "or to which section 593 applies".

(16) The table of sections for part II of subchapter H of chapter 1 is amended by striking the items relating to sections 595 and 596.

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall apply to taxable years beginning after December 31, 1995.

(2) SUBSECTION (b)(7)(B).—The amendments made by subsection (b)(7)(B) shall not apply to any distribution with respect to preferred stock if—

(A) such stock is outstanding at all times after October 31, 1995, and before the distribution, and

(B) such distribution is made before the date which is 1 year after the date of the enactment of this Act (or, in the case of stock which may be redeemed, if later, the date which is 30 days after the earliest date that such stock may be redeemed).

(3) SUBSECTION (b)(8).—The amendment made by subsection (b)(8) shall apply to property acquired in taxable years beginning after December 31, 1995.

(4) SUBSECTION (b)(10).—The amendments made by subsection (b)(10) shall not apply to any residual interest held by a taxpayer if such interest has been held by such taxpayer at all times after October 31, 1995.

SEC. 1617. EXCLUSION FOR ENERGY CONSERVATION SUBSIDIES LIMITED TO SUBSIDIES WITH RESPECT TO DWELLING UNITS.

(a) IN GENERAL.—Paragraph (1) of section 136(c) (defining energy conservation measure) is amended by striking "energy demand—" and all that follows and inserting "energy demand with respect to a dwelling unit."

(b) CONFORMING AMENDMENTS.—

(1) Subsection (a) of section 136 is amended to read as follows:

"(a) EXCLUSION.—Gross income shall not include the value of any subsidy provided (directly or indirectly) by a public utility to a customer for the purchase or installation of any energy conservation measure."

(2) Paragraph (2) of section 136(c) is amended—

(A) by striking subparagraph (A) and by redesignating subparagraphs (B) and (C) as subparagraphs (A) and (B), respectively, and

(B) by striking "AND SPECIAL RULES" in the paragraph heading.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts received after December 31, 1996, unless received pursuant to a written binding contract in effect on September 13, 1995, and at all times thereafter.

PART II—FINANCIAL ASSET SECURITIZATION INVESTMENTS

SEC. 1621. FINANCIAL ASSET SECURITIZATION INVESTMENT TRUSTS.

(a) IN GENERAL.—Subchapter M of chapter 1 is amended by adding at the end the following new part:

"PART V—FINANCIAL ASSET SECURITIZATION INVESTMENT TRUSTS

"SEC. 860H. TAXATION OF A FASIT; OTHER GENERAL RULES.

"(a) TAXATION OF FASIT.—A FASIT as such shall not be subject to taxation under this subtitle (and shall not be treated as a trust, partnership, corporation, or taxable mortgage pool).

"(b) TAXATION OF HOLDER OF OWNERSHIP INTEREST.—In determining the taxable income of the holder of the ownership interest in a FASIT—

"(1) all assets, liabilities, and items of income, gain, deduction, loss, and credit of a FASIT shall be treated as assets, liabilities, and such items (as the case may be) of such holder,

"(2) the constant yield method (including the rules of section 1272(a)(6)) shall be applied under an accrual method of accounting in determining all interest, acquisition discount, original issue discount, and market discount and all premium deductions or adjustments with respect to each debt instrument of the FASIT,

"(3) there shall not be taken into account any item of income, gain, or deduction allocable to a prohibited transaction, and

"(4) interest accrued by the FASIT which is exempt from tax imposed by this subtitle shall, when taken into account by such holder, be treated as ordinary income.

"(c) TREATMENT OF REGULAR INTERESTS.—For purposes of this title—

"(1) a regular interest in a FASIT, if not otherwise a debt instrument, shall be treated as a debt instrument,

"(2) section 163(e)(5) shall not apply to such an interest, and

"(3) amounts includible in gross income with respect to such an interest shall be determined under an accrual method of accounting.

"SEC. 860I. GAIN RECOGNITION ON CONTRIBUTIONS TO A FASIT AND IN OTHER CASES.

"(a) TREATMENT OF PROPERTY ACQUIRED BY FASIT.—

"(1) PROPERTY ACQUIRED FROM HOLDER OF OWNERSHIP INTEREST OR RELATED PERSON.—If property is sold or contributed to a FASIT by the holder of the ownership interest in such FASIT (or by a related person) gain (if any) shall be recognized to such holder (or person) in an amount equal to the excess (if any) of such property's value under subsection (d) on the date of such sale or contribution over its adjusted basis on such date.

"(2) PROPERTY ACQUIRED OTHER THAN FROM HOLDER OF OWNERSHIP INTEREST OR RELATED PERSON.—Property which is acquired by a FASIT other than in a transaction to which paragraph (1) applies shall be treated—

"(A) as having been acquired by the holder of the ownership interest in the FASIT for an amount equal to the FASIT's cost of acquiring such property, and

"(B) as having been sold by such holder to the FASIT at its value under subsection (d) on such date.

"(b) GAIN RECOGNITION ON PROPERTY OUTSIDE FASIT WHICH SUPPORTS REGULAR INTERESTS.—If property held by the holder of the ownership interest in a FASIT (or by any person related to such holder) supports any regular interest in such FASIT—

"(1) gain shall be recognized to such holder (or person) in the same manner as if such holder (or person) had sold such property at its value under subsection (d) on the earliest date such property supports such an interest, and

"(2) such property shall be treated as held by such FASIT for purposes of this part.

"(c) DEFERRAL OF GAIN RECOGNITION.—The Secretary may prescribe regulations which—

"(1) provide that gain otherwise recognized under subsection (a) or (b) shall not be recognized before the earliest date on which such property supports any regular interest in such FASIT or any indebtedness of the holder of the ownership interest (or of any person related to such holder), and

"(2) provide such adjustments to the other provisions of this part to the extent appropriate in the context of the treatment provided under paragraph (1).

"(d) VALUATION.—For purposes of this section—

"(1) IN GENERAL.—The value of any property under this subsection shall be—

"(A) in the case of a debt instrument which is not traded on an established securities market, the sum of the present values of the reasonably expected payments under such instrument determined (in the manner provided by regulations prescribed by the Secretary)—

"(i) as of the date of the event resulting in the gain recognition under this section, and

"(ii) by using a discount rate equal to 120 percent of the applicable Federal rate (as defined in section 1274(d)), or such other discount rate specified in such regulations, compounded semiannually, and

"(B) in the case of any other property, its fair market value.

"(2) SPECIAL RULE FOR REVOLVING LOAN ACCOUNTS.—For purposes of paragraph (1)—

"(A) each extension of credit (other than the accrual of interest) on a revolving loan account shall be treated as a separate debt instrument, and

"(B) payments on such extensions of credit having substantially the same terms shall be applied to such extensions beginning with the earliest such extension.

"(e) SPECIAL RULES.—

"(1) NONRECOGNITION RULES NOT TO APPLY.—Gain required to be recognized under this section shall be recognized notwithstanding any other provision of this subtitle.

"(2) BASIS ADJUSTMENTS.—The basis of any property on which gain is recognized under this section shall be increased by the amount of gain so recognized.

"SEC. 860J. NON-FASIT LOSSES NOT TO OFFSET CERTAIN FASIT INCLUSIONS.

"(a) IN GENERAL.—The taxable income of the holder of the ownership interest or any high-yield interest in a FASIT for any taxable year shall in no event be less than the sum of—

"(1) such holder's taxable income determined solely with respect to such interests (including gains and losses from sales and exchanges of such interests), and

"(2) the excess inclusion (if any) under section 860E(a)(1) for such taxable year.

"(b) COORDINATION WITH SECTION 172.—Any increase in the taxable income of any holder of the ownership interest or a high-yield interest in a FASIT for any taxable year by reason of subsection (a) shall be disregarded—

"(1) in determining under section 172 the amount of any net operating loss for such taxable year, and

"(2) in determining taxable income for such taxable year for purposes of the 2nd sentence of section 172(b)(2).

"(c) COORDINATION WITH MINIMUM TAX.—For purposes of part VI of subchapter A of this chapter—

"(1) the reference in section 55(b)(2) to taxable income shall be treated as a reference to taxable income determined without regard to this section,

"(2) the alternative minimum taxable income of any holder of the ownership interest or a high-yield interest in a FASIT for any taxable year shall in no event be less than such holder's taxable income determined solely with respect to such interests, and

"(3) any increase in taxable income under this section shall be disregarded for purposes of computing the alternative tax net operating loss deduction.

"(d) AFFILIATED GROUPS.—All members of an affiliated group filing a consolidated return shall be treated as 1 taxpayer for purposes of this section.

"SEC. 860K. TREATMENT OF TRANSFERS OF HIGH-YIELD INTERESTS TO DISQUALIFIED HOLDERS.

"(a) GENERAL RULE.—In the case of any high-yield interest which is held by a disqualified holder—

"(1) the gross income of such holder shall not include any income (other than gain) attributable to such interest, and

"(2) amounts not includible in the gross income of such holder by reason of paragraph (1) shall be included (at the time otherwise includible under paragraph (1)) in the gross income of the most recent holder of such interest which is not a disqualified holder.

"(b) EXCEPTIONS.—Rules similar to the rules of paragraphs (4) and (7) of section 860E(e) shall apply to the tax imposed by reason of the inclusion in gross income under subsection (a).

"(c) DISQUALIFIED HOLDER.—For purposes of this section, the term 'disqualified holder' means any holder other than—

"(1) an eligible corporation (as defined in section 860L(a)(2)), or

"(2) a FASIT.

"(d) TREATMENT OF INTERESTS HELD BY SECURITIES DEALERS.—

"(1) IN GENERAL.—Subsection (a) shall not apply to any high-yield interest held by a disqualified holder if such holder is a dealer in securities who acquired such interest exclusively for sale to customers in the ordinary course of business (and not for investment).

"(2) CHANGE IN DEALER STATUS.—

"(A) IN GENERAL.—In the case of a dealer in securities which is not an eligible corporation (as defined in section 860L(a)(2)), if—

"(i) such dealer ceases to be a dealer in securities, or

"(ii) such dealer commences holding the high-yield interest for investment,

there is hereby imposed (in addition to other taxes) an excise tax equal to the product of the highest rate of tax specified in section 11(b)(1) and the income of such dealer attributable to such interest for periods after the date of such cessation or commencement.

"(B) HOLDING FOR 31 DAYS OR LESS.—For purposes of subparagraph (A)(ii), a dealer shall not be treated as holding an interest for investment before the 32d day after the date such dealer acquired such interest unless such interest is so held as part of a plan to avoid the purposes of this paragraph.

"(C) ADMINISTRATIVE PROVISIONS.—The deficiency procedures of subtitle F shall apply to the tax imposed by this paragraph.

"(e) TREATMENT OF HIGH-YIELD INTERESTS IN PASS-THRU ENTITIES.—

"(1) IN GENERAL.—If a pass-thru entity (as defined in section 860E(e)(6)) issues a debt or equity interest—

"(A) which is supported by any regular interest in a FASIT, and

"(B) which has an original yield to maturity which is greater than each of—

"(i) the sum determined under clauses (i) and (ii) of section 163(i)(1)(B) with respect to such debt or equity interest, and

"(ii) the yield to maturity to such entity on such regular interest (determined as of the date such entity acquired such interest),

there is hereby imposed on the pass-thru entity a tax (in addition to other taxes) equal to the product of the highest rate of tax specified in section 11(b)(1) and the income of the holder of such debt or equity interest which is properly attributable to such regular interest. For purposes of the preceding sentence, the yield to maturity of any equity interest shall be determined under regulations prescribed by the Secretary.

"(2) EXCEPTION.—Paragraph (1) shall not apply to arrangements not having as a principal purpose the avoidance of the purposes of this subsection.

"SEC. 860L. DEFINITIONS AND OTHER SPECIAL RULES.

"(a) FASIT.—

"(1) IN GENERAL.—For purposes of this title, the terms 'financial asset securitization investment trust' and 'FASIT' mean any entity—

"(A) for which an election to be treated as a FASIT applies for the taxable year,

"(B) all of the interests in which are regular interests or the ownership interest,

"(C) which has only 1 ownership interest and such ownership interest is held directly by an eligible corporation,

"(D) as of the close of the 3rd month beginning after the day of its formation and at all times thereafter, substantially all of the assets of which (including assets treated as held by the entity under section 860I(b)(2)) consist of permitted assets, and

"(E) which is not described in section 851(a).

A rule similar to the rule of the last sentence of section 860D(a) shall apply for purposes of this paragraph.

"(2) ELIGIBLE CORPORATION.—For purposes of paragraph (1)(C), the term 'eligible corporation' means any domestic C corporation other than—

"(A) a corporation which is exempt from, or is not subject to, tax under this chapter,

"(B) an entity described in section 851(a) or 856(a),

"(C) a REMIC, and

"(D) an organization to which part I of subchapter T applies.

"(3) ELECTION.—An entity (otherwise meeting the requirements of paragraph (1)) may elect to be treated as a FASIT. Except as provided in paragraph (5), such an election shall apply to the taxable year for which made and all subsequent taxable years unless revoked with the consent of the Secretary.

"(4) TERMINATION.—If any entity ceases to be a FASIT at any time during the taxable year, such entity shall not be treated as a FASIT after the date of such ceasation.

"(5) INADVERTENT TERMINATIONS, ETC.—Rules similar to the rules of section 860D(b)(2)(B) shall apply to inadvertent failures to qualify or remain qualified as a FASIT.

"(6) PERMITTED ASSETS NOT TREATED AS INTEREST IN FASIT.—Except as provided in regulations prescribed by the Secretary, any asset which is a permitted asset at the time acquired by a FASIT shall not be treated at any time as an interest in such FASIT.

"(b) INTERESTS IN FASIT.—For purposes of this part—

"(1) REGULAR INTEREST.—

"(A) IN GENERAL.—The term 'regular interest' means any interest which is issued by a FASIT after the startup date with fixed terms and which is designated as a regular interest if—

"(i) such interest unconditionally entitles the holder to receive a specified principal amount (or other similar amount),

"(ii) interest payments (or other similar amounts), if any, with respect to such interest are determined based on a fixed rate, or, except as otherwise provided by the Secretary, at a variable rate permitted under section 860G(a)(1)(B)(i),

"(iii) such interest does not have a stated maturity (including options to renew) greater than 30 years (or such longer period as may be permitted by regulations),

"(iv) the issue price of such interest does not exceed 125 percent of its stated principal amount, and

"(v) the yield to maturity on such interest is less than the sum determined under section 163(i)(1)(B) with respect to such interest.

An interest shall not fail to meet the requirements of clause (i) merely because the timing (but not the amount) of the principal payments (or other similar amounts) may be contingent on the extent that payments on debt instruments held by the FASIT are made in advance of anticipated payments and on the amount of income from permitted assets.

"(B) HIGH-YIELD INTERESTS.—

"(i) IN GENERAL.—The term 'regular interest' includes any high-yield interest.

"(ii) HIGH-YIELD INTEREST.—The term 'high-yield interest' means any interest which would be described in subparagraph (A) but for—

"(I) failing to meet the requirements of one or more of clauses (i), (iv), or (v) thereof, or

"(II) failing to meet the requirement of clause (ii) thereof but only if interest payments (or other similar amounts), if any, with respect to such interest consist of a specified portion of the interest payments on permitted assets and such portion does not vary during the period such interest is outstanding.

"(2) OWNERSHIP INTEREST.—The term 'ownership interest' means the interest issued by a FASIT after the startup day which is designated as an ownership interest and which is not a regular interest.

"(c) PERMITTED ASSETS.—For purposes of this part—

"(1) IN GENERAL.—The term 'permitted asset' means—

"(A) cash or cash equivalents,

"(B) any debt instrument (as defined in section 1275(a)(1)) under which interest payments (or other similar amounts), if any, at or before maturity meet the requirements applicable under clause (i) or (ii) of section 860G(a)(1)(B),

"(C) foreclosure property,

"(D) any asset—

"(i) which is an interest rate or foreign currency notional principal contract, letter of credit, insurance, guarantee against payment defaults, or other similar instrument permitted by the Secretary, and

"(ii) which is reasonably required to guarantee or hedge against the FASIT's risks associated with being the obligor on interests issued by the FASIT,

"(E) contract rights to acquire debt instruments described in subparagraph (B) or assets described in subparagraph (D),

"(F) any regular interest in another FASIT, and

"(G) any regular interest in a REMIC.

"(2) DEBT ISSUED BY HOLDER OF OWNERSHIP INTEREST NOT PERMITTED ASSET.—The term 'permitted asset' shall not include any debt instrument issued by the holder of the ownership interest in the FASIT or by any person related to such holder or any direct or indirect interest in such a debt instrument. The preceding sentence shall not apply to cash equivalents and to any other investment specified in regulations prescribed by the Secretary.

"(3) FORECLOSURE PROPERTY.—

"(A) IN GENERAL.—The term 'foreclosure property' means property—

"(i) which would be foreclosure property under section 856(e) (determined without regard to paragraph (5) thereof) if such property were real property acquired by a real estate investment trust, and

"(ii) which is acquired in connection with the default or imminent default of a debt instrument held by the FASIT unless the security interest in such property was created for the principal purpose of permitting the FASIT to invest in such property.

Solely for purposes of subsection (a)(1), the determination of whether any property is foreclosure property shall be made without regard to section 856(e)(4).

"(B) AUTHORITY TO REDUCE GRACE PERIOD.—In the case of property other than real property and other than personal property incident to real property, the Secretary may by regulation reduce for purposes of subparagraph (A)

the periods otherwise applicable under paragraphs (2) and (3) of section 856(e).

"(d) STARTUP DAY.—For purposes of this part—

"(1) IN GENERAL.—The term 'startup day' means the date designated in the election under subsection (a)(3) as the startup day of the FASIT. Such day shall be the beginning of the first taxable year of the FASIT.

"(2) TREATMENT OF PROPERTY HELD ON STARTUP DAY.—All property held (or treated as held under section 860I(c)(2)) by an entity as of the startup day shall be treated as contributed to such entity on such day by the holder of the ownership interest in such entity.

"(e) TAX ON PROHIBITED TRANSACTIONS.—

"(1) IN GENERAL.—There is hereby imposed for each taxable year of a FASIT a tax equal to 100 percent of the net income derived from prohibited transactions. Such tax shall be paid by the holder of the ownership interest in the FASIT.

"(2) PROHIBITED TRANSACTIONS.—For purposes of this part, the term 'prohibited transaction' means—

"(A) the receipt of any income derived from any asset that is not a permitted asset,

"(B) except as provided in paragraph (3), the disposition of any permitted asset,

"(C) the receipt of any income derived from any loan originated by the FASIT, and

"(D) the receipt of any income representing a fee or other compensation for services (other than any fee received as compensation for a waiver, amendment, or consent under permitted assets (other than foreclosure property) held by the FASIT).

"(3) EXCEPTION FOR INCOME FROM CERTAIN DISPOSITIONS.—

"(A) IN GENERAL.—Paragraph (2)(B) shall not apply to a disposition which would not be a prohibited transaction (as defined in section 860F(a)(2)) by reason of—

"(i) clause (ii), (iii), or (iv) of section 860F(a)(2)(A), or

"(ii) section 860F(a)(5),

if the FASIT were treated as a REMIC and debt instruments described in subsection (c)(1)(B) were treated as qualified mortgages.

"(B) SUBSTITUTION OF DEBT INSTRUMENTS; REDUCTION OF OVER-COLLATERALIZATION.—Paragraph (2)(B) shall not apply to—

"(i) the substitution of a debt instrument described in subsection (c)(1)(B) for another debt instrument which is a permitted asset, or

"(ii) the distribution of a debt instrument contributed by the holder of the ownership interest to such holder in order to reduce over-collateralization of the FASIT,

but only if a principal purpose of acquiring the debt instrument which is disposed of was not the recognition of gain (or the reduction of a loss) as a result of an increase in the

market value of the debt instrument after its acquisition by the FASIT.

"(C) LIQUIDATION OF CLASS OF REGULAR INTERESTS.—Paragraph (2)(B) shall not apply to the complete liquidation of any class of regular interests.

"(4) NET INCOME.—For purposes of this subsection, net income shall be determined in accordance with section 860F(a)(3).

"(f) COORDINATION WITH OTHER PROVISIONS.—

"(1) WASH SALES RULES.—Rules similar to the rules of section 860F(d) shall apply to the ownership interest in a FASIT.

"(2) SECTION 475.—Except as provided by the Secretary by regulations, if any security which is sold or contributed to a FASIT by the holder of the ownership interest in such FASIT was required to be marked-to-market under section 475 by such holder, section 475 shall continue to apply to such security; except that in applying section 475 while such security is held by the FASIT, the fair market value of such security for purposes of section 475 shall not be less than its value under section 860I(d).

"(g) RELATED PERSON.—For purposes of this part, a person (hereinafter in this subsection referred to as the 'related person') is related to any person if—

"(1) the related person bears a relationship to such person specified in section 267(b) or section 707(b)(1), or

"(2) the related person and such person are engaged in trades or businesses under common control (within the meaning of subsections (a) and (b) of section 52).

For purposes of paragraph (1), in applying section 267(b) or 707(b)(1), '20 percent' shall be substituted for '50 percent'.

"(h) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this part, including regulations to prevent the abuse of the purposes of this part through transactions which are not primarily related to securitization of debt instruments by a FASIT.".

(b) TECHNICAL AMENDMENTS.—

(1) Paragraph (2) of section 26(b) is amended by striking "and" at the end of subparagraph (M), by striking the period at the end of subparagraph (N) and inserting ", and", and by adding at the end the following new subparagraph:

"(O) section 860K (relating to treatment of transfers of high-yield interests to disqualified holders).".

(2) Paragraph (6) of section 56(g) is amended by striking "or REMIC" and inserting "REMIC, or FASIT".

(3) Clause (ii) of section 382(l)(4)(B) is amended by striking "or a REMIC to which part IV of subchapter M applies" and inserting "a REMIC to which part IV of subchapter M applies, or a FASIT to which part V of subchapter M applies".

(4) Paragraph (1) of section 582(c) is amended by inserting ", and any regular interest in a FASIT," after "REMIC".

(5) Subparagraph (E) of section 856(c)(6) is amended by adding at the end the following new sentence: "The principles of the preceding provisions of this subparagraph shall apply to regular interests in a FASIT.".

(6) Paragraph (3) of section 860G(a) is amended by striking "and" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", and", and by inserting after subparagraph (C) the following new subparagraph:

"(D) any regular interest in a FASIT which is transferred to, or purchased by, the REMIC as described in clauses (i) and (ii) of subparagraph (A) but only if 95 percent or more of the value of the assets of such FASIT is at all times attributable to obligations described in subparagraph (A) (without regard to such clauses).".

(7) Subparagraph (C) of section 1202(e)(4) is amended by striking "or REMIC" and inserting "REMIC, or FASIT".

(8) Clause (xi) of section 7701(a)(19)(C) is amended to read as follows:

"(xi) any regular or residual interest in a REMIC, and any regular interest in a FASIT, but only in the proportion which the assets of such REMIC or FASIT consist of property described in any of the preceding clauses of this subparagraph; except that if 95 percent or more of the assets of such REMIC or FASIT are assets described in clauses (i) through (x), the entire interest in the REMIC or FASIT shall qualify.".

(9) Subparagraph (A) of section 7701(i)(2) is amended by inserting "or a FASIT" after "a REMIC".

(c) CLERICAL AMENDMENT.—The table of parts for subchapter M of chapter 1 is amended by adding at the end the following new item:

"Part V. Financial asset securitization investment trusts.".

(d) EFFECTIVE DATE.—The amendments made by this section shall take effect on September 1, 1997.

(e) TREATMENT OF EXISTING SECURITIZATION ENTITIES.—

(1) IN GENERAL.—In the case of the holder of the ownership interest in a pre-effective date FASIT—

(A) gain shall not be recognized under section 860L(d)(2) of the Internal Revenue Code of 1986 on property deemed contributed to the FASIT, and

(B) gain shall not be recognized under section 860I of such Code on property contributed to such FASIT,

until such property (or portion thereof) ceases to be properly allocable to a pre-FASIT interest.

(2) ALLOCATION OF PROPERTY TO PRE-FASIT INTEREST.—For purposes of paragraph (1), property shall be allocated to a pre-FASIT interest in such manner as the Secretary of the Treasury may prescribe, except that all property in a FASIT shall be treated as properly allocable to pre-FASIT interests if the fair market value of all such property does not exceed 107 percent of the aggregate principal amount of all outstanding pre-FASIT interests.

(3) DEFINITIONS.—For purposes of this subsection—

(A) PRE-EFFECTIVE DATE FASIT.—The term "pre-effective date FASIT" means any FASIT if the entity (with re-

spect to which the election under section 860L(a)(3) of such Code was made) is in existence on August 31, 1997.

(B) PRE-FASIT INTEREST.—The term "pre-FASIT interest" means any interest in the entity referred to in subparagraph (A) which was issued before the startup day (other than any interest held by the holder of the ownership interest in the FASIT).

Subtitle G—Technical Corrections

SEC. 1701. COORDINATION WITH OTHER SUBTITLES.

For purposes of applying the amendments made by any subtitle of this title other than this subtitle, the provisions of this subtitle shall be treated as having been enacted immediately before the provisions of such other subtitles.

SEC. 1702. AMENDMENTS RELATED TO REVENUE RECONCILIATION ACT OF 1990.

(a) AMENDMENTS RELATED TO SUBTITLE A.—

(1) Subparagraph (B) of section 59(j)(3) is amended by striking "section 1(i)(3)(B)" and inserting "section 1(g)(3)(B)".

(2) Clause (i) of section 151(d)(3)(C) is amended by striking "joint of a return" and inserting "joint return".

(b) AMENDMENTS RELATED TO SUBTITLE B.—

(1) Paragraph (1) of section 11212(e) of the Revenue Reconciliation Act of 1990 is amended by striking "Paragraph (1) of section 6724(d)" and inserting "Subparagraph (B) of section 6724(d)(1)".

(2)(A) Subparagraph (B) of section 4093(c)(2), as in effect before the amendments made by the Revenue Reconciliation Act of 1993, is amended by inserting before the period "unless such fuel is sold for exclusive use by a State or any political subdivision thereof".

(B) Paragraph (4) of section 6427(l), as in effect before the amendments made by the Revenue Reconciliation Act of 1993, is amended by inserting before the period "unless such fuel was used by a State or any political subdivision thereof".

(3) Paragraph (1) of section 6416(b) is amended by striking "chapter 32 or by section 4051" and inserting "chapter 31 or 32".

(4) Section 7012 is amended—

(A) by striking "production or importation of gasoline" in paragraph (3) and inserting "taxes on gasoline and diesel fuel", and

(B) by striking paragraph (4) and redesignating paragraphs (5) and (6) as paragraphs (4) and (5), respectively.

(5) Subsection (c) of section 5041 is amended by striking paragraph (6) and by inserting the following new paragraphs:

"(6) CREDIT FOR TRANSFEREE IN BOND.—If—

"(A) wine produced by any person would be eligible for any credit under paragraph (1) if removed by such person during the calendar year,

"(B) wine produced by such person is removed during such calendar year by any other person (hereafter in this

paragraph referred to as the 'transferee') to whom such wine was transferred in bond and who is liable for the tax imposed by this section with respect to such wine, and

"(C) such producer holds title to such wine at the time of its removal and provides to the transferee such information as is necessary to properly determine the transferee's credit under this paragraph,

then, the transferee (and not the producer) shall be allowed the credit under paragraph (1) which would be allowed to the producer if the wine removed by the transferee had been removed by the producer on that date.

"(7) REGULATIONS.—The Secretary may prescribe such regulations as may be necessary to carry out the purposes of this subsection, including regulations—

"(A) to prevent the credit provided in this subsection from benefiting any person who produces more than 250,000 wine gallons of wine during a calendar year, and

"(B) to assure proper reduction of such credit for persons producing more than 150,000 wine gallons of wine during a calendar year.".

(6) Paragraph (3) of section 5061(b) is amended to read as follows:

"(3) section 5041(f),".

(7) Section 5354 is amended by inserting "(taking into account the appropriate amount of credit with respect to such wine under section 5041(c))" after "any one time".

(c) AMENDMENTS RELATED TO SUBTITLE C.—

(1) Paragraph (4) of section 56(g) is amended by redesignating subparagraphs (I) and (J) as subparagraphs (H) and (I), respectively.

(2) Subparagraph (B) of section 6724(d)(1) is amended—

(A) by striking "or" at the end of clause (xii), and

(B) by striking the period at the end of clause (xiii) and inserting ", or".

(3) Subsection (g) of section 6302 is amended by inserting ", 22," after "chapters 21".

(4) The earnings and profits of any insurance company to which section 11305(c)(3) of the Revenue Reconciliation Act of 1990 applies shall be determined without regard to any deduction allowed under such section; except that, for purposes of applying sections 56 and 902, and subpart F of part III of subchapter N of chapter 1 of the Internal Revenue Code of 1986, such deduction shall be taken into account.

(5) Subparagraph (D) of section 6038A(e)(4) is amended—

(A) by striking "any transaction to which the summons relates" and inserting "any affected taxable year", and

(B) by adding at the end thereof the following new sentence: "For purposes of this subparagraph, the term 'affected taxable year' means any taxable year if the determination of the amount of tax imposed for such taxable year is affected by the treatment of the transaction to which the summons relates.".

(6) Subparagraph (A) of section 6621(c)(2) is amended by adding at the end thereof the following new flush sentence:

"The preceding sentence shall be applied without regard to any such letter or notice which is withdrawn by the Secretary.".

(7) Clause (i) of section 6621(c)(2)(B) is amended by striking "this subtitle" and inserting "this title".

(d) AMENDMENTS RELATED TO SUBTITLE D.—

(1) Notwithstanding section 11402(c) of the Revenue Reconciliation Act of 1990, the amendment made by section 11402(b)(1) of such Act shall apply to taxable years ending after December 31, 1989.

(2) Clause (ii) of section 143(m)(4)(C) is amended—

(A) by striking "any month of the 10-year period" and inserting "any year of the 4-year period",

(B) by striking "succeeding months" and inserting "succeeding years", and

(C) by striking "over the remainder of such period (or, if lesser, 5 years)" and inserting "to zero over the succeeding 5 years".

(e) AMENDMENTS RELATED TO SUBTITLE E.—

(1)(A) Clause (ii) of section 56(d)(1)(B) is amended to read as follows:

"(ii) appropriate adjustments in the application of section 172(b)(2) shall be made to take into account the limitation of subparagraph (A).".

(B) For purposes of applying sections 56(g)(1) and 56(g)(3) of the Internal Revenue Code of 1986 with respect to taxable years beginning in 1991 and 1992, the reference in such sections to the alternative tax net operating loss deduction shall be treated as including a reference to the deduction under section 56(h) of such Code as in effect before the amendments made by section 1915 of the Energy Policy Act of 1992.

(2) Clause (i) of section 613A(c)(3)(A) is amended by striking "the table contained in".

(3) Section 6501 is amended—

(A) by striking subsection (m) (relating to deficiency attributable to election under section 44B) and by redesignating subsections (n) and (o) as subsections (m) and (n), respectively, and

(B) by striking "section 40(f) or 51(j)" in subsection (m) (as redesignated by subparagraph (A)) and inserting "section 40(f), 43, or 51(j)".

(4) Subparagraph (C) of section 38(c)(2) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990) is amended by inserting before the period at the end of the first sentence the following: "and without regard to the deduction under section 56(h)".

(5) The amendment made by section 1913(b)(2)(C)(i) of the Energy Policy Act of 1992 shall apply to taxable years beginning after December 31, 1990.

(f) AMENDMENTS RELATED TO SUBTITLE F.—

(1)(A) Section 2701(a)(3) is amended by adding at the end thereof the following new subparagraph:

"(C) VALUATION OF QUALIFIED PAYMENTS WHERE NO LIQUIDATION, ETC. RIGHTS.—In the case of an applicable re-

tained interest which is described in subparagraph (B)(i) but not subparagraph (B)(ii), the value of the distribution right shall be determined without regard to this section.".

(B) Section 2701(a)(3)(B) is amended by inserting "CERTAIN" before "QUALIFIED" in the heading thereof.

(C) Sections 2701 (d)(1) and (d)(4) are each amended by striking "subsection (a)(3)(B)" and inserting "subsection (a)(3)(B) or (C)".

(2) Clause (i) of section 2701(a)(4)(B) is amended by inserting "(or, to the extent provided in regulations, the rights as to either income or capital)" after "income and capital".

(3)(A) Section 2701(b)(2) is amended by adding at the end thereof the following new subparagraph:

"(C) APPLICABLE FAMILY MEMBER.—For purposes of this subsection, the term 'applicable family member' includes any lineal descendant of any parent of the transferor or the transferor's spouse.".

(B) Section 2701(e)(3) is amended—

(i) by striking subparagraph (B), and

(ii) by striking so much of paragraph (3) as precedes "shall be treated as holding" and inserting:

"(3) ATTRIBUTION OF INDIRECT HOLDINGS AND TRANSFERS.—An individual".

(C) Section 2704(c)(3) is amended by striking "section 2701(e)(3)(A)" and inserting "section 2701(e)(3)".

(4) Clause (i) of section 2701(c)(1)(B) is amended to read as follows:

"(i) a right to distributions with respect to any interest which is junior to the rights of the transferred interest,".

(5)(A) Clause (i) of section 2701(c)(3)(C) is amended to read as follows:

"(i) IN GENERAL.—Payments under any interest held by a transferor which (without regard to this subparagraph) are qualified payments shall be treated as qualified payments unless the transferor elects not to treat such payments as qualified payments. Payments described in the preceding sentence which are held by an applicable family member shall be treated as qualified payments only if such member elects to treat such payments as qualified payments.".

(B) The first sentence of section 2701(c)(3)(C)(ii) is amended to read as follows: "A transferor or applicable family member holding any distribution right which (without regard to this subparagraph) is not a qualified payment may elect to treat such right as a qualified payment, to be paid in the amounts and at the times specified in such election.".

(C) The time for making an election under the second sentence of section 2701(c)(3)(C)(i) of the Internal Revenue Code of 1986 (as amended by subparagraph (A)) shall not expire before the due date (including extensions) for filing the transferor's return of the tax imposed by section 2501 of such Code for the first calendar year ending after the date of enactment.

(6) Section 2701(d)(3)(A)(iii) is amended by striking "the period ending on the date of".

(7) Subclause (I) of section 2701(d)(3)(B)(ii) is amended by inserting "or the exclusion under section 2503(b)," after "section 2523,".

(8) Section 2701(e)(5) is amended—

(A) by striking "such contribution to capital or such redemption, recapitalization, or other change" in subparagraph (A) and inserting "such transaction", and

(B) by striking "the transfer" in subparagraph (B) and inserting "such transaction".

(9) Section 2701(d)(4) is amended by adding at the end thereof the following new subparagraph:

"(C) TRANSFER TO TRANSFERORS.—In the case of a taxable event described in paragraph (3)(A)(ii) involving a transfer of an applicable retained interest from an applicable family member to a transferor, this subsection shall continue to apply to the transferor during any period the transferor holds such interest.".

(10) Section 2701(e)(6) is amended by inserting "or to reflect the application of subsection (d)" before the period at the end thereof.

(11)(A) Section 2702(a)(3)(A) is amended—

(i) by striking "to the extent" and inserting "if" in clause (i),

(ii) by striking "or" at the end of clause (i),

(iii) by striking the period at the end of clause (ii) and inserting ", or", and

(iv) by adding at the end thereof the following new clause:

"(iii) to the extent that regulations provide that such transfer is not inconsistent with the purposes of this section.".

(B)(i) Section 2702(a)(3) is amended by striking "incomplete transfer" each place it appears and inserting "incomplete gift".

(ii) The heading for section 2702(a)(3)(B) is amended by striking "INCOMPLETE TRANSFER" and inserting "INCOMPLETE GIFT".

(g) AMENDMENTS RELATED TO SUBTITLE G.—

(1)(A) Subsection (a) of section 1248 is amended—

(i) by striking ", or if a United States person receives a distribution from a foreign corporation which, under section 302 or 331, is treated as an exchange of stock" in paragraph (1), and

(ii) by adding at the end thereof the following new sentence: "For purposes of this section, a United States person shall be treated as having sold or exchanged any stock if, under any provision of this subtitle, such person is treated as realizing gain from the sale or exchange of such stock.".

(B) Paragraph (1) of section 1248(e) is amended by striking ", or receives a distribution from a domestic corporation which, under section 302 or 331, is treated as an exchange of stock".

(C) Subparagraph (B) of section 1248(f)(1) is amended by striking "or 361(c)(1)" and inserting "355(c)(1), or 361(c)(1)".

(D) Paragraph (1) of section 1248(i) is amended to read as follows:

"(1) IN GENERAL.—If any shareholder of a 10-percent corporate shareholder of a foreign corporation exchanges stock of the 10-percent corporate shareholder for stock of the foreign corporation, such 10-percent corporate shareholder shall recognize gain in the same manner as if the stock of the foreign corporation received in such exchange had been—

"(A) issued to the 10-percent corporate shareholder, and

"(B) then distributed by the 10-percent corporate shareholder to such shareholder in redemption or liquidation (whichever is appropriate).

The amount of gain recognized by such 10-percent corporate shareholder under the preceding sentence shall not exceed the amount treated as a dividend under this section.".

(2) Section 897 is amended by striking subsection (f).

(3) Paragraph (13) of section 4975(d) is amended by striking "section 408(b)" and inserting "section 408(b)(12)".

(4) Clause (iii) of section 56(g)(4)(D) is amended by inserting ", but only with respect to taxable years beginning after December 31, 1989" before the period at the end thereof.

(5)(A) Paragraph (11) of section 11701(a) of the Revenue Reconciliation Act of 1990 (and the amendment made by such paragraph) are hereby repealed, and section 7108(r)(2) of the Revenue Reconciliation Act of 1989 shall be applied as if such paragraph (and amendment) had never been enacted.

(B) Subparagraph (A) shall not apply to any building if the owner of such building establishes to the satisfaction of the Secretary of the Treasury or his delegate that such owner reasonably relied on the amendment made by such paragraph (11).

(h) AMENDMENTS RELATED TO SUBTITLE H.—

(1)(A) Clause (vi) of section 168(e)(3)(B) is amended by striking "or" at the end of subclause (I), by striking the period at the end of subclause (II) and inserting ", or", and by adding at the end thereof the following new subclause:

"(III) is described in section 48(l)(3)(A)(ix) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990).".

(B) Subparagraph (B) of section 168(e)(3) (relating to 5-year property) is amended by adding at the end the following flush sentence:

"Nothing in any provision of law shall be construed to treat property as not being described in clause (vi)(I) (or the corresponding provisions of prior law) by reason of being public utility property (within the meaning of section 48(a)(3)).".

(C) Subparagraph (K) of section 168(g)(4) is amended by striking "section 48(a)(3)(A)(iii)" and inserting "section 48(l)(3)(A)(ix) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)".

(2) Clause (ii) of section 172(b)(1)(E) is amended by striking "subsection (m)" and inserting "subsection (h)".

(3) Sections 805(a)(4)(E), 832(b)(5)(C)(ii)(II), and 832(b)(5)(D)(ii)(II) are each amended by striking "243(b)(5)" and inserting "243(b)(2)".

(4) Subparagraph (A) of section 243(b)(3) is amended by inserting "of" after "In the case".

(5) The subsection heading for subsection (a) of section 280F is amended by striking "INVESTMENT TAX CREDIT AND".

(6) Clause (i) of section 1504(c)(2)(B) is amended by inserting "section" before "243(b)(2)".

(7) Paragraph (3) of section 341(f) is amended by striking "351, 361, 371(a), or 374(a)" and inserting "351, or 361".

(8) Paragraph (2) of section 243(b) is amended to read as follows:

"(2) AFFILIATED GROUP.—For purposes of this subsection:

"(A) IN GENERAL.—The term 'affiliated group' has the meaning given such term by section 1504(a), except that for such purposes sections 1504(b)(2), 1504(b)(4), and 1504(c) shall not apply.

"(B) GROUP MUST BE CONSISTENT IN FOREIGN TAX TREATMENT.—The requirements of paragraph (1)(A) shall not be treated as being met with respect to any dividend received by a corporation if, for any taxable year which includes the day on which such dividend is received—

"(i) 1 or more members of the affiliated group referred to in paragraph (1)(A) choose to any extent to take the benefits of section 901, and

"(ii) 1 or more other members of such group claim to any extent a deduction for taxes otherwise creditable under section 901.".

(9) The amendment made by section 11813(b)(17) of the Revenue Reconciliation Act of 1990 shall be applied as if the material stricken by such amendment included the closing parenthesis after "section 48(a)(5)".

(10) Paragraph (1) of section 179(d) is amended by striking "in a trade or business" and inserting "a trade or business".

(11) Subparagraph (E) of section 50(a)(2) is amended by striking "section 48(a)(5)(A)" and inserting "section 48(a)(5)".

(12) The amendment made by section 11801(c)(9)(G)(ii) of the Revenue Reconciliation Act of 1990 shall be applied as if it struck "Section 422A(c)(2)" and inserted "Section 422(c)(2)".

(13) Subparagraph (B) of section 424(c)(3) is amended by striking "a qualified stock option, an incentive stock option, an option granted under an employee stock purchase plan, or a restricted stock option" and inserting "an incentive stock option or an option granted under an employee stock purchase plan".

(14) Subparagraph (E) of section 1367(a)(2) is amended by striking "section 613A(c)(13)(B)" and inserting "section 613A(c)(11)(B)".

(15) Subparagraph (B) of section 460(e)(6) is amended by striking "section 167(k)" and inserting "section 168(e)(2)(A)(ii)".

(16) Subparagraph (C) of section 172(h)(4) is amended by striking "subsection (b)(1)(M)" and inserting "subsection (b)(1)(E)".

(17) Section 6503 is amended—

(A) by redesignating the subsection relating to extension in case of certain summonses as subsection (j), and

(B) by redesignating the subsection relating to cross references as subsection (k).

(18) Paragraph (4) of section 1250(e) is hereby repealed.

(19) Paragraph (1) of section 179(d) is amended by adding at the end the following new sentence: "Such term shall not include any property described in section 50(b) and shall not include air conditioning or heating units.".

"(i) EFFECTIVE DATE.—Except as otherwise expressly provided, any amendment made by this section shall take effect as if included in the provision of the Revenue Reconciliation Act of 1990 to which such amendment relates.".

SEC. 1703. AMENDMENTS RELATED TO REVENUE RECONCILIATION ACT OF 1993.

(a) AMENDMENT RELATED TO SECTION 13114.—Paragraph (2) of section 1044(c) is amended to read as follows:

"(2) PURCHASE.—The taxpayer shall be considered to have purchased any property if, but for subsection (d), the unadjusted basis of such property would be its cost within the meaning of section 1012.".

(b) AMENDMENTS RELATED TO SECTION 13142.—

(1) Subparagraph (B) of section 13142(b)(6) of the Revenue Reconciliation Act of 1993 is amended to read as follows:

"(B) FULL-TIME STUDENTS, WAIVER AUTHORITY, AND PROHIBITED DISCRIMINATION.—The amendments made by paragraphs (2), (3), and (4) shall take effect on the date of the enactment of this Act.".

(2) Subparagraph (C) of section 13142(b)(6) of such Act is amended by striking "paragraph (2)" and inserting "paragraph (5)".

(c) AMENDMENT RELATED TO SECTION 13161.—

(1) IN GENERAL.—Subsection (e) of section 4001 (relating to inflation adjustment) is amended to read as follows:

"(e) INFLATION ADJUSTMENT.—

"(1) IN GENERAL.—The $30,000 amount in subsection (a) and section 4003(a) shall be increased by an amount equal to—

"(A) $30,000, multiplied by

"(B) the cost-of-living adjustment under section 1(f)(3) for the calendar year in which the vehicle is sold, determined by substituting 'calendar year 1990' for 'calendar year 1992' in subparagraph (B) thereof.

"(2) ROUNDING.—If any amount as adjusted under paragraph (1) is not a multiple of $2,000, such amount shall be rounded to the next lowest multiple of $2,000.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect on the date of the enactment of this Act.

(d) AMENDMENT RELATED TO SECTION 13201.—Clause (ii) of section 135(b)(2)(B) is amended by inserting before the period at the end thereof the following: ", determined by substituting 'calendar year 1989' for 'calendar year 1992' in subparagraph (B) thereof".

(e) AMENDMENTS RELATED TO SECTION 13203.—Subsection (a) of section 59 is amended—

(1) by striking "the amount determined under section 55(b)(1)(A)" in paragraph (1)(A) and (2)(A)(i) and inserting "the pre-credit tentative minimum tax",

(2) by striking "specified in section 55(b)(1)(A)" in paragraph (1)(C) and inserting "specified in subparagraph (A)(i) or (B)(i) of section 55(b)(1) (whichever applies)",

(3) by striking "which would be determined under section 55(b)(1)(A)" in paragraph (2)(A)(ii) and inserting "which would be the pre-credit tentative minimum tax", and

(4) by adding at the end thereof the following new paragraph:

"(3) PRE-CREDIT TENTATIVE MINIMUM TAX.—For purposes of this subsection, the term 'pre-credit tentative minimum tax' means—

"(A) in the case of a taxpayer other than a corporation, the amount determined under the first sentence of section 55(b)(1)(A)(i), or

"(B) in the case of a corporation, the amount determined under section 55(b)(1)(B)(i).".

(f) AMENDMENT RELATED TO SECTION 13221.—Sections 1201(a) and 1561(a) are each amended by striking "last sentence" each place it appears and inserting "last 2 sentences".

(g) AMENDMENTS RELATED TO SECTION 13222.—

(1) Subparagraph (B) of section 6033(e)(1) is amended by adding at the end thereof the following new clause:

"(iii) COORDINATION WITH SECTION 527(f).—This subsection shall not apply to any amount on which tax is imposed by reason of section 527(f).".

(2) Clause (i) of section 6033(e)(1)(B) is amended by striking "this subtitle" and inserting "section 501".

(h) AMENDMENT RELATED TO SECTION 13225.—Paragraph (3) of section 6655(g) is amended by striking all that follows "'3rd month'" in the sentence following subparagraph (C) and inserting ", subsection (e)(2)(A) shall be applied by substituting '2 months' for '3 months' in clause (i)(I), the election under clause (i) of subsection (e)(2)(C) may be made separately for each installment, and clause (ii) of subsection (e)(2)(C) shall not apply.".

(i) AMENDMENTS RELATED TO SECTION 13231.—

(1) Subparagraph (G) of section 904(d)(3) is amended by striking "section 951(a)(1)(B)" and inserting "subparagraph (B) or (C) of section 951(a)(1)".

(2) Paragraph (1) of section 956A(b) is amended to read as follows:

"(1) the amount (not including a deficit) referred to in section 316(a)(1) to the extent such amount was accumulated in prior taxable years beginning after September 30, 1993, and".

(3) Subsection (f) of section 956A is amended by inserting before the period at the end thereof: "and regulations coordinating the provisions of subsections (c)(3)(A) and (d)".

(4) Subsection (b) of section 958 is amended by striking "956(b)(2)" each place it appears and inserting "956(c)(2)".

(5)(A) Subparagraph (A) of section 1297(d)(2) is amended by striking "The adjusted basis of any asset" and inserting "The

amount taken into account under section 1296(a)(2) with respect to any asset".

(B) The paragraph heading of paragraph (2) of section 1297(d) is amended to read as follows:

"(2) AMOUNT TAKEN INTO ACCOUNT.—".

(6) Subsection (e) of section 1297 is amended by inserting "For purposes of this part—" after the subsection heading.

(j) AMENDMENT RELATED TO SECTION 13241.—Subparagraph (B) of section 40(e)(1) is amended to read as follows:

> *"(B) for any period before January 1, 2001, during which the rates of tax under section 4081(a)(2)(A) are 4.3 cents per gallon.".*

(k) AMENDMENT RELATED TO SECTION 13242.—Paragraph (4) of section 6427(f) is amended by striking "1995" and inserting "1999".

(l) AMENDMENT RELATED TO SECTION 13261.—Clause (iii) of section 13261(g)(2)(A) of the Revenue Reconciliation Act of 1993 is amended by striking "by the taxpayer" and inserting "by the taxpayer or a related person".

(m) AMENDMENT RELATED TO SECTION 13301.—Subparagraph (B) of section 1397B(d)(5) is amended by striking "preceding".

(n) CLERICAL AMENDMENTS.—

(1) Subsection (d) of section 39 is amended—

(A) by striking "45" in the heading of paragraph (5) and inserting "45A", and

(B) by striking "45" in the heading of paragraph (6) and inserting "45B".

(2) Subparagraph (A) of section 108(d)(9) is amended by striking "paragraph (3)(B)" and inserting "paragraph (3)(C)".

(3) Subparagraph (C) of section 143(d)(2) is amended by striking the period at the end thereof and inserting a comma.

(4) Clause (ii) of section 163(j)(6)(E) is amended by striking "which is a" and inserting "which is".

(5) Subparagraph (A) of section 1017(b)(4) is amended by striking "subsection (b)(2)(D)" and inserting "subsection (b)(2)(E)".

(6) So much of section 1245(a)(3) as precedes subparagraph (A) thereof is amended to read as follows:

"(3) SECTION 1245 PROPERTY.—For purposes of this section, the term 'section 1245 property' means any property which is or has been property of a character subject to the allowance for depreciation provided in section 167 and is either—".

(7) Paragraph (2) of section 1394(e) is amended—

(A) by striking "(i)" and inserting "(A)", and

(B) by striking "(ii)" and inserting "(B)".

(8) Subsection (m) of section 6501 (as redesignated by section 1602) is amended by striking "or 51(j)" and inserting "45B, or 51(j)".

(9)(A) The section 6714 added by section 13242(b)(1) of the Revenue Reconciliation Act of 1993 is hereby redesignated as section 6715.

(B) The table of sections for part I of subchapter B of chapter 68 is amended by striking "6714" in the item added by such section 13242(b)(2) of such Act and inserting "6715".

(10) Paragraph (2) of section 9502(b) is amended by inserting "and before" after "1982,".

(11) Subsection (a)(3) of section 13206 of the Revenue Reconciliation Act of 1993 is amended by striking "this section" and inserting "this subsection".

(12) Paragraph (1) of section 13215(c) of the Revenue Reconciliation Act of 1993 is amended by striking "Public Law 92–21" and inserting "Public Law 98–21".

(13) Paragraph (2) of section 13311(e) of the Revenue Reconciliation Act of 1993 is amended by striking "section 1393(a)(3)" and inserting "section 1393(a)(2)".

(14) Subparagraph (B) of section 117(d)(2) is amended by striking "section 132(f)" and inserting "section 132(h)".

(o) EFFECTIVE DATE.—Any amendment made by this section shall take effect as if included in the provision of the Revenue Reconciliation Act of 1993 to which such amendment relates.

SEC. 1704. MISCELLANEOUS PROVISIONS.

(a) APPLICATION OF AMENDMENTS MADE BY TITLE XII OF OMNIBUS BUDGET RECONCILIATION ACT OF 1990.—Except as otherwise expressly provided, whenever in title XII of the Omnibus Budget Reconciliation Act of 1990 an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

(b) TREATMENT OF CERTAIN AMOUNTS UNDER HEDGE BOND RULES.—

(1) IN GENERAL.—Clause (iii) of section 149(g)(3)(B) is amended to read as follows:

> *"(iii) AMOUNTS HELD PENDING REINVESTMENT OR REDEMPTION.—Amounts held for not more than 30 days pending reinvestment or bond redemption shall be treated as invested in bonds described in clause (i).".*

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 7651 of the Omnibus Budget Reconciliation Act of 1989.

(c) TREATMENT OF CERTAIN DISTRIBUTIONS UNDER SECTION 1445.—

(1) IN GENERAL.—Paragraph (3) of section 1445(e) is amended by adding at the end thereof the following new sentence: "Rules similar to the rules of the preceding provisions of this paragraph shall apply in the case of any distribution to which section 301 applies and which is not made out of the earnings and profits of such a domestic corporation.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to distributions after the date of the enactment of this Act.

(d) TREATMENT OF CERTAIN CREDITS UNDER SECTION 469.—

(1) IN GENERAL.—Subparagraph (B) of section 469(c)(3) is amended by adding at the end thereof the following new sentence: "If the preceding sentence applies to the net income from any property for any taxable year, any credits allowable under subpart B (other than section 27(a)) or D of part IV of subchapter A for such taxable year which are attributable to such property shall be treated as credits not from a passive activity

to the extent the amount of such credits does not exceed the regular tax liability of the taxpayer for the taxable year which is allocable to such net income.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1986.

(e) TREATMENT OF DISPOSITIONS UNDER PASSIVE LOSS RULES.—

(1) IN GENERAL.—Subparagraph (A) of section 469(g)(1) is amended to read as follows:

"(A) IN GENERAL.—If all gain or loss realized on such disposition is recognized, the excess of—

"(i) any loss from such activity for such taxable year (determined after the application of subsection (b)), over

"(ii) any net income or gain for such taxable year from all other passive activities (determined after the application of subsection (b)),

shall be treated as a loss which is not from a passive activity.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1986.

(f) MISCELLANEOUS AMENDMENTS TO FOREIGN PROVISIONS.—

(1) COORDINATION OF UNIFIED ESTATE TAX CREDIT WITH TREATIES.—Subparagraph (A) of section 2102(c)(3) is amended by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, property shall not be treated as situated in the United States if such property is exempt from the tax imposed by this subchapter under any treaty obligation of the United States.".

(2) TREATMENT OF CERTAIN INTEREST PAID TO RELATED PERSON.—

(A) Subparagraph (B) of section 163(j)(1) is amended by inserting before the period at the end thereof the following: "(and clause (ii) of paragraph (2)(A) shall not apply for purposes of applying this subsection to the amount so treated)".

(B) Subsection (j) of section 163 is amended by redesignating paragraph (7) as paragraph (8) and by inserting after paragraph (6) the following new paragraph:

"(7) COORDINATION WITH PASSIVE LOSS RULES, ETC.—This subsection shall be applied before sections 465 and 469.".

(C) The amendments made by this paragraph shall apply as if included in the amendments made by section 7210(a) of the Revenue Reconciliation Act of 1989.

(3) TREATMENT OF INTEREST ALLOCABLE TO EFFECTIVELY CONNECTED INCOME.—

(A) IN GENERAL.—

(i) Subparagraph (B) of section 884(f)(1) is amended by striking "to the extent" and all that follows down through "subparagraph (A)" and inserting "to the extent that the allocable interest exceeds the interest described in subparagraph (A)".

(ii) The second sentence of section 884(f)(1) is amended by striking "reasonably expected" and all that follows down through the period at the end thereof and inserting "reasonably expected to be allocable interest.".

(iii) Paragraph (2) of section 884(f) is amended to read as follows:

"(2) ALLOCABLE INTEREST.—For purposes of this subsection, the term 'allocable interest' means any interest which is allocable to income which is effectively connected (or treated as effectively connected) with the conduct of a trade or business in the United States.".

(B) EFFECTIVE DATE.—The amendments made by subparagraph (A) shall take effect as if included in the amendments made by section 1241(a) of the Tax Reform Act of 1986.

(4) CLARIFICATION OF SOURCE RULE.—

(A) IN GENERAL.—Paragraph (2) of section 865(b) is amended by striking "863(b)" and inserting "863".

(B) EFFECTIVE DATE.—The amendment made by subparagraph (A) shall take effect as if included in the amendments made by section 1211 of the Tax Reform Act of 1986.

(5) REPEAL OF OBSOLETE PROVISIONS.—

(A) Paragraph (1) of section 6038(a) is amended by striking ", and" at the end of subparagraph (E) and inserting a period, and by striking subparagraph (F).

(B) Subsection (b) of section 6038A is amended by adding "and" at the end of paragraph (2), by striking ", and" at the end of paragraph (3) and inserting a period, and by striking paragraph (4).

(g) CLARIFICATION OF TREATMENT OF MEDICARE ENTITLEMENT UNDER COBRA PROVISIONS.—

(1) IN GENERAL.—

(A) Subclause (V) of section 4980B(f)(2)(B)(i) is amended to read as follows:

"(V) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in paragraph (3)(B) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this clause before the close of the 36-month period beginning on the date the covered employee became so entitled.".

(B) Clause (v) of section 602(2)(A) of the Employee Retirement Income Security Act of 1974 is amended to read as follows:

"(v) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in section 603(2) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not ter-

minate under this subparagraph before the close of the 36-month period beginning on the date the covered employee became so entitled.".

(C) Clause (iv) of section 2202(2)(A) of the Public Health Service Act is amended to read as follows:

"(iv) MEDICARE ENTITLEMENT FOLLOWED BY QUALIFYING EVENT.—In the case of a qualifying event described in section 2203(2) that occurs less than 18 months after the date the covered employee became entitled to benefits under title XVIII of the Social Security Act, the period of coverage for qualified beneficiaries other than the covered employee shall not terminate under this subparagraph before the close of the 36-month period beginning on the date the covered employee became so entitled.".

(2) EFFECTIVE DATE.—The amendments made by this subsection shall apply to plan years beginning after December 31, 1989.

(h) TREATMENT OF CERTAIN REMIC INCLUSIONS.—

(1) IN GENERAL.—Subsection (a) of section 860E is amended by adding at the end thereof the following new paragraph:

"(6) COORDINATION WITH MINIMUM TAX.—For purposes of part VI of subchapter A of this chapter—

"(A) the reference in section 55(b)(2) to taxable income shall be treated as a reference to taxable income determined without regard to this subsection,

"(B) the alternative minimum taxable income of any holder of a residual interest in a REMIC for any taxable year shall in no event be less than the excess inclusion for such taxable year, and

"(C) any excess inclusion shall be disregarded for purposes of computing the alternative tax net operating loss deduction.

The preceding sentence shall not apply to any organization to which section 593 applies, except to the extent provided in regulations prescribed by the Secretary under paragraph (2).".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 671 of the Tax Reform Act of 1986 unless the taxpayer elects to apply such amendment only to taxable years beginning after the date of the enactment of this Act.

(i) EXEMPTION FROM HARBOR MAINTENANCE TAX FOR CERTAIN PASSENGERS.—

(1) IN GENERAL.—Subparagraph (D) of section 4462(b)(1) (relating to special rule for Alaska, Hawaii, and possessions) is amended by inserting before the period the following: ", or passengers transported on United States flag vessels operating solely within the State waters of Alaska or Hawaii and adjacent international waters".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 1402(a) of the Harbor Maintenance Revenue Act of 1986.

(j) AMENDMENTS RELATED TO REVENUE PROVISIONS OF ENERGY POLICY ACT OF 1992.—

(1) Effective with respect to taxable years beginning after December 31, 1990, subclause (II) of section 53(d)(1)(B)(iv) is amended to read as follows:

> *"(II) the adjusted net minimum tax for any taxable year is the amount of the net minimum tax for such year increased in the manner provided in clause (iii).".*

(2) Subsection (g) of section 179A is redesignated as subsection (f).

(3) Subparagraph (E) of section 6724(d)(3) is amended by striking "section 6109(f)" and inserting "section 6109(h)".

(4)(A) Subsection (d) of section 30 is amended—

(i) by inserting "(determined without regard to subsection (b)(3))" before the period at the end of paragraph (1) thereof, and

(ii) by adding at the end thereof the following new paragraph:

"(4) ELECTION TO NOT TAKE CREDIT.—No credit shall be allowed under subsection (a) for any vehicle if the taxpayer elects to not have this section apply to such vehicle.".

(B) Subsection (m) of section 6501 (as redesignated by section 1602) is amended by striking "section 40(f)" and inserting "section 30(d)(4), 40(f)".

(5) Subclause (III) of section 501(c)(21)(D)(ii) is amended by striking "section 101(6)" and inserting "section 101(7)" and by striking "1752(6)" and inserting "1752(7)".

(6) Paragraph (1) of section 1917(b) of the Energy Policy Act of 1992 shall be applied as if "at a rate" appeared instead of "at the rate" in the material proposed to be stricken.

(7) Paragraph (2) of section 1921(b) of the Energy Policy Act of 1992 shall be applied as if a comma appeared after "(2)" in the material proposed to be stricken.

(8) Subsection (a) of section 1937 of the Energy Policy Act of 1992 shall be applied as if "Subpart B" appeared instead of "Subpart C".

(k) TREATMENT OF QUALIFIED FOOTBALL COACHES PLAN.—

(1) IN GENERAL.—For purposes of the Internal Revenue Code of 1986, a qualified football coaches plan—

(A) shall be treated as a multiemployer collectively bargained plan, and

(B) notwithstanding section 401(k)(4)(B) of such Code, may include a qualified cash and deferred arrangement under section 401(k) of such Code.

(2) QUALIFIED FOOTBALL COACHES PLAN.—For purposes of this subsection, the term "qualified football coaches plan" means any defined contribution plan which is established and maintained by an organization—

(A) which is described in section 501(c) of such Code,

(B) the membership of which consists entirely of individuals who primarily coach football as full-time employees of 4-year colleges or universities described in section 170(b)(1)(A)(ii) of such Code, and

(C) which was in existence on September 18, 1986.

(3) EFFECTIVE DATE.—This subsection shall apply to years beginning after December 22, 1987.

(l) DETERMINATION OF UNRECOVERED INVESTMENT IN ANNUITY CONTRACT.—

(1) IN GENERAL.—Subparagraph (A) of section 72(b)(4) is amended by inserting "(determined without regard to subsection (c)(2))" after "contract".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 1122(c) of the Tax Reform Act of 1986.

(m) MODIFICATIONS TO ELECTION TO INCLUDE CHILD'S INCOME ON PARENT'S RETURN.—

(1) ELIGIBILITY FOR ELECTION.—Clause (ii) of section 1(g)(7)(A) (relating to election to include certain unearned income of child on parent's return) is amended to read as follows:

> *"(ii) such gross income is more than the amount described in paragraph (4)(A)(ii)(I) and less than 10 times the amount so described,".*

(2) COMPUTATION OF TAX.—Subparagraph (B) of section 1(g)(7) (relating to income included on parent's return) is amended—

(A) by striking "$1,000" in clause (i) and inserting "twice the amount described in paragraph (4)(A)(ii)(I)", and

(B) by amending subclause (II) of clause (ii) to read as follows:

> *"(II) for each such child, 15 percent of the lesser of the amount described in paragraph (4)(A)(ii)(I) or the excess of the gross income of such child over the amount so described, and".*

(3) MINIMUM TAX.—Subparagraph (B) of section 59(j)(1) is amended by striking "$1,000" and inserting "twice the amount in effect for the taxable year under section 63(c)(5)(A)".

(4) EFFECTIVE DATE.—The amendments made by this subsection shall apply to taxable years beginning after December 31, 1995.

(n) TREATMENT OF CERTAIN VETERANS' REEMPLOYMENT RIGHTS.—

(1) IN GENERAL.—Section 414 is amended by adding at the end the following new subsection:

"(u) SPECIAL RULES RELATING TO VETERANS' REEMPLOYMENT RIGHTS UNDER USERRA.—

"(1) TREATMENT OF CERTAIN CONTRIBUTIONS MADE PURSUANT TO VETERANS' REEMPLOYMENT RIGHTS.—If any contribution is made by an employer or an employee under an individual account plan with respect to an employee, or by an employee to a defined benefit plan that provides for employee contributions, and such contribution is required by reason of such employee's rights under chapter 43 of title 38, United States Code, resulting from qualified military service, then—

> *"(A) such contribution shall not be subject to any otherwise applicable limitation contained in section 402(g), 402(h), 403(b), 404(a), 404(h), 408, 415, or 457, and shall not be taken into account in applying such limitations to other contributions or benefits under such plan or any other*

plan, with respect to the year in which the contribution is made,

"(B) such contribution shall be subject to the limitations referred to in subparagraph (A) with respect to the year to which the contribution relates (in accordance with rules prescribed by the Secretary), and

"(C) such plan shall not be treated as failing to meet the requirements of section 401(a)(4), 401(a)(26), 401(k)(3), 401(k)(11), 401(k)(12), 401(m), 403(b)(12), 408(k)(3), 408(k)(6), 408(p), 410(b), or 416 by reason of the making of (or the right to make) such contribution.

For purposes of the preceding sentence, any elective deferral or employee contribution made under paragraph (2) shall be treated as required by reason of the employee's rights under such chapter 43.

"(2) REEMPLOYMENT RIGHTS UNDER USERRA WITH RESPECT TO ELECTIVE DEFERRALS.—

"(A) IN GENERAL.—For purposes of this subchapter and section 457, if an employee is entitled to the benefits of chapter 43 of title 38, United States Code, with respect to any plan which provides for elective deferrals, the employer sponsoring the plan shall be treated as meeting the requirements of such chapter 43 with respect to such elective deferrals only if such employer—

"(i) permits such employee to make additional elective deferrals under such plan (in the amount determined under subparagraph (B) or such lesser amount as is elected by the employee) during the period which begins on the date of the reemployment of such employee with such employer and has the same length as the lesser of—

"(I) the product of 3 and the period of qualified military service which resulted in such rights, and

"(II) 5 years, and

"(ii) makes a matching contribution with respect to any additional elective deferral made pursuant to clause (i) which would have been required had such deferral actually been made during the period of such qualified military service.

"(B) AMOUNT OF MAKEUP REQUIRED.—The amount determined under this subparagraph with respect to any plan is the maximum amount of the elective deferrals that the individual would have been permitted to make under the plan in accordance with the limitations referred to in paragraph (1)(A) during the period of qualified military service if the individual had continued to be employed by the employer during such period and received compensation as determined under paragraph (7). Proper adjustment shall be made to the amount determined under the preceding sentence for any elective deferrals actually made during the period of such qualified military service.

"(C) ELECTIVE DEFERRAL.—For purposes of this paragraph, the term 'elective deferral' has the meaning given

such term by section 402(g)(3); except that such term shall include any deferral of compensation under an eligible deferred compensation plan (as defined in section 457(b)).

"(D) AFTER-TAX EMPLOYEE CONTRIBUTIONS.—References in subparagraphs (A) and (B) to elective deferrals shall be treated as including references to employee contributions.

"(3) CERTAIN RETROACTIVE ADJUSTMENTS NOT REQUIRED.—For purposes of this subchapter and subchapter E, no provision of chapter 43 of title 38, United States Code, shall be construed as requiring—

"(A) any crediting of earnings to an employee with respect to any contribution before such contribution is actually made, or

"(B) any allocation of any forfeiture with respect to the period of qualified military service.

"(4) LOAN REPAYMENT SUSPENSIONS PERMITTED.—If any plan suspends the obligation to repay any loan made to an employee from such plan for any part of any period during which such employee is performing service in the uniformed services (as defined in chapter 43 of title 38, United States Code), whether or not qualified military service, such suspension shall not be taken into account for purposes of section 72(p), 401(a), or 4975(d)(1).

"(5) QUALIFIED MILITARY SERVICE.—For purposes of this subsection, the term 'qualified military service' means any service in the uniformed services (as defined in chapter 43 of title 38, United States Code) by any individual if such individual is entitled to reemployment rights under such chapter with respect to such service.

"(6) INDIVIDUAL ACCOUNT PLAN.—For purposes of this subsection, the term 'individual account plan' means any defined contribution plan (including any tax-sheltered annuity plan under section 403(b), any simplified employee pension under section 408(k), any qualified salary reduction arrangement under section 408(p), and any eligible deferred compensation plan (as defined in section 457(b)).

"(7) COMPENSATION.—For purposes of sections 403(b)(3), 415(c)(3), and 457(e)(5), an employee who is in qualified military service shall be treated as receiving compensation from the employer during such period of qualified military service equal to—

"(A) the compensation the employee would have received during such period if the employee were not in qualified military service, determined based on the rate of pay the employee would have received from the employer but for absence during the period of qualified military service, or

"(B) if the compensation the employee would have received during such period was not reasonably certain, the employee's average compensation from the employer during the 12-month period immediately preceding the qualified military service (or, if shorter, the period of employment immediately preceding the qualified military service).

"(8) USERRA REQUIREMENTS FOR QUALIFIED RETIREMENT PLANS.—For purposes of this subchapter and section 457, an employer sponsoring a retirement plan shall be treated as meeting the requirements of chapter 43 of title 38, United States Code, only if each of the following requirements is met:

"(A) An individual reemployed under such chapter is treated with respect to such plan as not having incurred a break in service with the employer maintaining the plan by reason of such individual's period of qualified military service.

"(B) Each period of qualified military service served by an individual is, upon reemployment under such chapter, deemed with respect to such plan to constitute service with the employer maintaining the plan for the purpose of determining the nonforfeitability of the individual's accrued benefits under such plan and for the purpose of determining the accrual of benefits under such plan.

"(C) An individual reemployed under such chapter is entitled to accrued benefits that are contingent on the making of, or derived from, employee contributions or elective deferrals only to the extent the individual makes payment to the plan with respect to such contributions or deferrals. No such payment may exceed the amount the individual would have been permitted or required to contribute had the individual remained continuously employed by the employer throughout the period of qualified military service. Any payment to such plan shall be made during the period beginning with the date of reemployment and whose duration is 3 times the period of the qualified military service (but not greater than 5 years).

"(9) PLANS NOT SUBJECT TO TITLE 38.—This subsection shall not apply to any retirement plan to which chapter 43 of title 38, United States Code, does not apply.

"(10) REFERENCES.—For purposes of this section, any reference to chapter 43 of title 38, United States Code, shall be treated as a reference to such chapter as in effect on December 12, 1994 (without regard to any subsequent amendment).".

(2) AMENDMENT TO ERISA.—Section 408(b)(1) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1148(b)) is amended by adding at the end the following new sentence: "A loan made by a plan shall not fail to meet the requirements of the preceding sentence by reason of a loan repayment suspension described under section 414(u)(4) of the Internal Revenue Code of 1986."

(3) EFFECTIVE DATE.—The amendments made by this subsection shall be effective as of December 12, 1994.

(o) REPORTING OF REAL ESTATE TRANSACTIONS.—

(1) IN GENERAL.—Paragraph (3) of section 6045(e) (relating to prohibition of separate charge for filing return) is amended by adding at the end the following new sentence: "Nothing in this paragraph shall be construed to prohibit the real estate reporting person from taking into account its cost of complying with such requirement in establishing its charge (other than a separate charge for complying with such requirement) to any

customer for performing services in the case of a real estate transaction.".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in section 1015(e)(2)(A) of the Technical and Miscellaneous Revenue Act of 1988.

(p) CLARIFICATION OF DENIAL OF DEDUCTION FOR STOCK REDEMPTION EXPENSES.

(1) IN GENERAL.—Paragraph (1) of section 162(k) is amended by striking "the redemption of its stock" and inserting "the reacquisition of its stock or of the stock of any related person (as defined in section 465(b)(3)(C))".

(2) CERTAIN DEDUCTIONS PERMITTED.—Subparagraph (A) of section 162(k)(2) is amended by striking "or" at the end of clause (i), by redesignating clause (ii) as clause (iii), and by inserting after clause (i) the following new clause:

"(ii) deduction for amounts which are properly allocable to indebtedness and amortized over the term of such indebtedness, or".

(3) CLERICAL AMENDMENT.—The subsection heading for subsection (k) of section 162 is amended by striking "REDEMPTION" and inserting "REACQUISITION".

(4) EFFECTIVE DATE.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by this subsection shall apply to amounts paid or incurred after September 13, 1995, in taxable years ending after such date.

(B) PARAGRAPH (2).—The amendment made by paragraph (2) shall take effect as if included in the amendment made by section 613 of the Tax Reform Act of 1986.

(q) CLERICAL AMENDMENT TO SECTION 404.—

(1) IN GENERAL.—Paragraph (1) of section 404(j) is amended by striking "(10)" and inserting "(9)".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 713(d)(4)(A) of the Deficit Reduction Act of 1984.

(r) PASSIVE INCOME NOT TO INCLUDE FSC INCOME, ETC.—

(1) IN GENERAL.—Paragraph (2) of section 1296(b) is amended by striking "or" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", or", and by inserting after subparagraph (C) the following new subparagraph:

"(D) which is foreign trade income of a FSC or export trade income of an export trade corporation (as defined in section 971).".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall take effect as if included in the amendments made by section 1235 of the Tax Reform Act of 1986.

(s) TECHNICAL CORRECTION OF INTERMEDIATE SANCTIONS PROVISIONS.—

(1) Subparagraph (C) of section 6652(c)(1) is amended by striking "$10" and inserting "$20", and by striking "$5,000" and inserting "$10,000".

(2) Subparagraph (D) of section 6652(c)(1) is amended by striking "$10" and inserting "$20".

(t) MISCELLANEOUS CLERICAL AMENDMENTS.—

(1) Subclause (II) of section 56(g)(4)(C)(ii) is amended by striking "of the subclause" and inserting "of subclause".

(2) Paragraph (2) of section 72(m) is amended by inserting "and" at the end of subparagraph (A), by striking subparagraph (B), and by redesignating subparagraph (C) as subparagraph (B).

(3) Paragraph (2) of section 86(b) is amended by striking "adusted" and inserting "adjusted".

*(4)(A) The heading for section 112 is amended by striking "**COMBAT PAY**" and inserting "**COMBAT ZONE COMPENSATION**".*

(B) The item relating to section 112 in the table of sections for part III of subchapter B of chapter 1 is amended by striking "combat pay" and inserting "combat zone compensation".

(C) Paragraph (1) of section 3401(a) is amended by striking "combat pay" and inserting "combat zone compensation".

(5) Clause (i) of section 172(h)(3)(B) is amended by striking the comma at the end thereof and inserting a period.

(6) Clause (ii) of section 543(a)(2)(B) is amended by striking "section 563(c)" and inserting "section 563(d)".

(7) Paragraph (1) of section 958(a) is amended by striking "sections 955(b)(1) (A) and (B), 955(c)(2)(A)(ii), and 960(a)(1)" and inserting "section 960(a)(1)".

(8) Subsection (g) of section 642 is amended by striking "under 2621(a)(2)" and inserting "under section 2621(a)(2)".

(9) Section 1463 is amended by striking "this subsection" and inserting "this section".

(10) Subsection (k) of section 3306 is amended by inserting a period at the end thereof.

(11) The item relating to section 4472 in the table of sections for subchapter B of chapter 36 is amended by striking "and special rules".

(12) Paragraph (3) of section 5134(c) is amended by striking "section 6662(a)" and inserting "section 6665(a)".

(13) Paragraph (2) of section 5206(f) is amended by striking "section 5(e)" and inserting "section 105(e)".

(14) Paragraph (1) of section 6050B(c) is amended by striking "section 85(c)" and inserting "section 85(b)".

(15) Subsection (k) of section 6166 is amended by striking paragraph (6).

(16) Subsection (e) of section 6214 is amended to read as follows:

"(e) CROSS REFERENCE.—

"For provision giving Tax Court jurisdiction to order a refund of an overpayment and to award sanctions, see section 6512(b)(2).".

(17) The section heading for section 6043 is amended by striking the semicolon and inserting a comma.

(18) The item relating to section 6043 in the table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking the semicolon and inserting a comma.

(19) The table of sections for part I of subchapter A of chapter 68 is amended by striking the item relating to section 6662.

(20)(A) Section 7232 is amended—

*(i) by striking "**LUBRICATING OIL**," in the heading, and*

(ii) by striking "lubricating oil," in the text.

(B) The table of sections for part II of subchapter A of chapter 75 is amended by striking "lubricating oil," in the item relating to section 7232.

(21) Paragraph (1) of section 6701(a) of the Omnibus Budget Reconciliation Act of 1989 is amended by striking "subclause (IV)" and inserting "subclause (V)".

(22) Clause (ii) of section 7304(a)(2)(D) of such Act is amended by striking "subsection (c)(2)" and inserting "subsection (c)".

(23) Paragraph (1) of section 7646(b) of such Act is amended by striking "section 6050H(b)(1)" and inserting "section 6050H(b)(2)".

(24) Paragraph (10) of section 7721(c) of such Act is amended by striking "section 6662(b)(2)(C)(ii)" and inserting "section 6661(b)(2)(C)(ii)".

(25) Subparagraph (A) of section 7811(i)(3) of such Act is amended by inserting "the first place it appears" before "in clause (i)".

(26) Paragraph (10) of section 7841(d) of such Act is amended by striking "section 381(a)" and inserting "section 381(c)".

(27) Paragraph (2) of section 7861(c) of such Act is amended by inserting "the second place it appears" before "and inserting".

(28) Paragraph (1) of section 460(b) is amended by striking "the look-back method of paragraph (3)" and inserting "the look-back method of paragraph (2)".

(29) Subparagraph (C) of section 50(a)(2) is amended by striking "subsection (c)(4)" and inserting "subsection (d)(5)".

(30) Subparagraph (B) of section 172(h)(4) is amended by striking the material following the heading and preceding clause (i) and inserting "For purposes of subsection (b)(2)—".

(31) Subparagraph (A) of section 355(d)(7) is amended by inserting "section" before "267(b)".

(32) Subparagraph (C) of section 420(e)(1) is amended by striking "mean" and inserting "means".

(33) Paragraph (4) of section 537(b) is amended by striking "section 172(i)" and inserting "section 172(f)".

(34) Subparagraph (B) of section 613(e)(1) is amended by striking the comma at the end thereof and inserting a period.

(35) Paragraph (4) of section 856(a) is amended by striking "section 582(c)(5)" and inserting "section 582(c)(2)".

(36) Sections 904(f)(2)(B)(i) and 907(c)(4)(B)(iii) are each amended by inserting "(as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990)" after "section 172(h)".

(37) Subsection (b) of section 936 is amended by striking "subparagraphs (D)(ii)(I)" and inserting "subparagraphs (D)(ii)".

(38) Subsection (c) of section 2104 is amended by striking "subparagraph (A), (C), or (D) of section 861(a)(1)" and inserting "section 861(a)(1)(A)".

(39) Subparagraph (A) of section 280A(c)(1) is amended to read as follows:

"(A) as the principal place of business for any trade or business of the taxpayer,".

(40) Section 6038 is amended by redesignating the subsection relating to cross references as subsection (f).

(41) Clause (iv) of section 6103(e)(1)(A) is amended by striking all that follows "provisions of" and inserting "section 1(g) or 59(j);".

(42) The subsection (f) of section 6109 of the Internal Revenue Code of 1986 which was added by section 2201(d) of Public Law 101–624 is redesignated as subsection (g).

(43) Subsection (b) of section 7454 is amended by striking "section 4955(e)(2)" and inserting "section 4955(f)(2)".

(44) Subsection (d) of section 11231 of the Revenue Reconciliation Act of 1990 shall be applied as if "comma" appeared instead of "period" and as if the paragraph (9) proposed to be added ended with a comma.

(45) Paragraph (1) of section 11303(b) of the Revenue Reconciliation Act of 1990 shall be applied as if "paragraph" appeared instead of "subparagraph" in the material proposed to be stricken.

(46) Subsection (f) of section 11701 of the Revenue Reconciliation Act of 1990 is amended by inserting "(relating to definitions)" after "section 6038(e)".

(47) Subsection (i) of section 11701 of the Revenue Reconciliation Act of 1990 shall be applied as if "subsection" appeared instead of "section" in the material proposed to be stricken.

(48) Subparagraph (B) of section 11801(c)(2) of the Revenue Reconciliation Act of 1990 shall be applied as if "section 56(g)" appeared instead of "section 59(g)".

(49) Subparagraph (C) of section 11801(c)(8) of the Revenue Reconciliation Act of 1990 shall be applied as if "reorganizations" appeared instead of "reorganization" in the material proposed to be stricken.

(50) Subparagraph (H) of section 11801(c)(9) of the Revenue Reconciliation Act of 1990 shall be applied as if "section 1042(c)(1)(B)" appeared instead of "section 1042(c)(2)(B)".

(51) Subparagraph (F) of section 11801(c)(12) of the Revenue Reconciliation Act of 1990 shall be applied as if "and (3)" appeared instead of "and (E)".

(52) Subparagraph (A) of section 11801(c)(22) of the Revenue Reconciliation Act of 1990 shall be applied as if "chapters 21" appeared instead of "chapter 21" in the material proposed to be stricken.

(53) Paragraph (3) of section 11812(b) of the Revenue Reconciliation Act of 1990 shall be applied by not executing the amendment therein to the heading of section 42(d)(5)(B).

(54) Clause (i) of section 11813(b)(9)(A) of the Revenue Reconciliation Act of 1990 shall be applied as if a comma appeared after "(3)(A)(ix)" in the material proposed to be stricken.

(55) Subparagraph (F) of section 11813(b)(13) of the Revenue Reconciliation Act of 1990 shall be applied as if "tax" appeared after "investment" in the material proposed to be stricken.

(56) Paragraph (19) of section 11813(b) of the Revenue Reconciliation Act of 1990 shall be applied as if "Paragraph (20) of section 1016(a), as redesignated by section 11801," appeared instead of "Paragraph (21) of section 1016(a)".

(57) Paragraph (5) section 8002(a) of the Surface Transportation Revenue Act of 1991 shall be applied as if "4481(e)" appeared instead of "4481(c)".

(58) Section 7872 is amended—

(A) by striking "foregone" each place it appears in subsections (a) and (e)(2) and inserting "forgone", and

(B) by striking "FOREGONE" in the heading for subsection (e) and the heading for paragraph (2) of subsection (e) and inserting "FORGONE".

(59) Paragraph (7) of section 7611(h) is amended by striking "approporiate" and inserting "appropriate".

(60) The heading of paragraph (3) of section 419A(c) is amended by striking "SEVERENCE" and inserting "SEVERANCE".

(61) Clause (ii) of section 807(d)(3)(B) is amended by striking "Commissoners' " and inserting "Commissioners' ".

(62) Subparagraph (B) of section 1274A(c)(1) is amended by striking "instument" and inserting "instrument".

(63) Subparagraph (B) of section 724(d)(3) by striking "Subparagaph" and inserting "Subparagraph".

(64) The last sentence of paragraph (2) of section 42(c) is amended by striking "of 1988".

(65) Paragraph (1) of section 9707(d) is amended by striking "diligence," and inserting "diligence".

(66) Subsection (c) of section 4977 is amended by striking "section 132(i)(2)" and inserting "section 132(h)".

(67) The last sentence of section 401(a)(20) is amended by striking "section 211" and inserting "section 521".

(68) Subparagraph (A) of section 402(g)(3) is amended by striking "subsection (a)(8)" and inserting "subsection (e)(3)".

(69) The last sentence of section 403(b)(10) is amended by striking "an direct" and inserting "a direct".

(70) Subparagraph (A) of section 4973(b)(1) is amended by striking "sections 402(c)" and inserting "section 402(c)".

(71) Paragraph (12) of section 3405(e) is amended by striking "(b)(3)" and inserting "(b)(2)".

(72) Paragraph (41) of section 521(b) of the Unemployment Compensation Amendments of 1992 shall be applied as if "section" appeared instead of "sections" in the material proposed to be stricken.

(73) Paragraph (27) of section 521(b) of the Unemployment Compensation Amendments of 1992 shall be applied as if "Section 691(c)(5)" appeared instead of "Section 691(c)".

(74) Paragraph (5) of section 860F(a) is amended by striking "paragraph (1)" and inserting "paragraph (2)".

(75) Paragraph (1) of section 415(k) is amended by adding "or" at the end of subparagraph (C), by striking subparagraphs (D) and (E), and by redesignating subparagraph (F) as subparagraph (D).

(76) Paragraph (2) of section 404(a) is amended by striking "(18),".

(77) Clause (ii) of section 72(p)(4)(A) is amended to read as follows:

> *"(ii) SPECIAL RULE.—The term 'qualified employer plan' shall include any plan which was (or was determined to be) a qualified employer plan or a government plan.".*

(78) Sections 461(i)(3)(C) and 1274(b)(3)(B)(i) are each amended by striking "section 6662(d)(2)(C)(ii)" and inserting "section 6662(d)(2)(C)(iii)".

(79) Subsection (a) of section 164 is amended by striking the paragraphs relating to the generation-skipping tax and the environmental tax imposed by section 59A and by inserting after paragraph (3) the following new paragraphs:

"(4) The GST tax imposed on income distributions.

"(5) The environmental tax imposed by section 59A.".

(80) Subclause (I) of section 936(a)(4)(A)(ii) is amended by striking "deprecation" and inserting "depreciation".

Subtitle H—Other Provisions

SEC. 1801. EXEMPTION FROM DIESEL FUEL DYEING REQUIREMENTS WITH RESPECT TO CERTAIN STATES.

(a) IN GENERAL.—Section 4082 (relating to exemptions for diesel fuel) is amended by redesignating subsections (c) and (d) as subsections (d) and (e), respectively, and by inserting after subsection (b) the following new subsection:

"(c) EXCEPTION TO DYEING REQUIREMENTS.—Paragraph (2) of subsection (a) shall not apply with respect to any diesel fuel—

> *"(1) removed, entered, or sold in a State for ultimate sale or use in an area of such State during the period such area is exempted from the fuel dyeing requirements under subsection (i) of section 211 of the Clean Air Act (as in effect on the date of the enactment of this subsection) by the Administrator of the Environmental Protection Agency under paragraph (4) of such subsection (i) (as so in effect), and*
>
> *"(2) the use of which is certified pursuant to regulations issued by the Secretary."*

(b) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to fuel removed, entered, or sold on or after the first day of the first calendar quarter beginning after the date of the enactment of this Act.

SEC. 1802. TREATMENT OF CERTAIN UNIVERSITY ACCOUNTS.

(a) IN GENERAL.—For purposes of subsection (s) of section 3121 of the Internal Revenue Code of 1986 (relating to concurrent employment by 2 or more employers)—

(1) the following entities shall be deemed to be related corporations that concurrently employ the same individual:

(A) a State university which employs health professionals as faculty members at a medical school, and

(B) an agency account of a State university which is described in subparagraph (A) and from which there is distributed to such faculty members payments forming a part of the compensation that the State, or such State university, as the case may be, agrees to pay to such faculty members, but only if—

(i) such agency account is authorized by State law and receives the funds for such payments from a faculty practice plan described in section 501(c)(3) of such Code and exempt from tax under section 501(a) of such Code,

(ii) such payments are distributed by such agency account to such faculty members who render patient care at such medical school, and

(iii) such faculty members comprise at least 30 percent of the membership of such faculty practice plan, and

(2) remuneration which is disbursed by such agency account to any such faculty member of the medical school described in paragraph (1)(A) shall be deemed to have been actually disbursed by the State, or such State university, as the case may be, as a common paymaster and not to have been actually disbursed by such agency account.

(b) EFFECTIVE DATE.—The provisions of subsection (a) shall apply to remuneration paid after December 31, 1996.

SEC. 1803. MODIFICATIONS TO EXCISE TAX ON OZONE-DEPLETING CHEMICALS.

(a) RECYCLED HALON.—

(1) IN GENERAL.—Section 4682(d)(1) (relating to recycling) is amended by inserting ", or on any recycled halon imported from any country which is a signatory to the Montreal Protocol on Substances that Deplete the Ozone Layer" before the period at the end.

(2) CERTIFICATION SYSTEM.—The Secretary of the Treasury, after consultation with the Administrator of the Environmental Protection Agency, shall develop a certification system to ensure compliance with the recycling requirement for imported halon under section 4682(d)(1) of the Internal Revenue Code of 1986, as amended by paragraph (1).

(b) CHEMICALS USED AS PROPELLANTS IN METERED-DOSE INHALERS TAX-EXEMPT.—Paragraph (4) of section 4682(g) (relating to phase-in of tax on certain substances) is amended to read as follows:

"(4) CHEMICALS USED AS PROPELLANTS IN METERED-DOSE INHALERS.—

"(A) TAX-EXEMPT.—

"(i) IN GENERAL.—No tax shall be imposed by section 4681 on—

"(I) any use of any substance as a propellant in metered-dose inhalers, or

"(II) any qualified sale by the manufacturer, producer, or importer of any substance.

"(ii) QUALIFIED SALE.—For purposes of clause (i), the term 'qualified sale' means any sale by the manufacturer, producer, or importer of any substance—

"(I) for use by the purchaser as a propellant in metered-dose inhalers, or

"(II) for resale by the purchaser to a 2d purchaser for such use by the 2d purchaser.

The preceding sentence shall apply only if the manufacturer, producer, and importer, and the 1st and 2d purchasers (if any) meet such registration requirements as may be prescribed by the Secretary.

"(B) OVERPAYMENTS.—If any substance on which tax was paid under this subchapter is used by any person as a propellant in metered-dose inhalers, credit or refund without interest shall be allowed to such person in an amount equal to the tax so paid. Amounts payable under the preceding sentence with respect to uses during the taxable year shall be treated as described in section 34(a) for such year unless claim thereof has been timely filed under this subparagraph."

(c) EFFECTIVE DATES.—

(1) RECYCLED HALON.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the amendment made by subsection (a)(1) shall take effect on January 1, 1997.

(B) HALON-1211.—In the case of Halon-1211, the amendment made by subsection (a)(1) shall take effect on January 1, 1998.

(2) METERED-DOSE INHALERS.—The amendment made by subsection (b) shall take effect on the 7th day after the date of the enactment of this Act.

SEC. 1804. TAX-EXEMPT BONDS FOR SALE OF ALASKA POWER ADMINISTRATION FACILITY.

Sections 142(f)(3) (as added by section 1608) and 147(d) of the Internal Revenue Code of 1986 shall not apply in determining whether any private activity bond issued after the date of the enactment of this Act and used to finance the acquisition of the Snettisham hydroelectric project from the Alaska Power Administration is a qualified bond for purposes of such Code.

SEC. 1805. NONRECOGNITION TREATMENT FOR CERTAIN TRANSFERS BY COMMON TRUST FUNDS TO REGULATED INVESTMENT COMPANIES.

(a) GENERAL RULE.—Section 584 (relating to common trust funds) is amended by redesignating subsection (h) as subsection (i) and by inserting after subsection (g) the following new subsection:

"(h) NONRECOGNITION TREATMENT FOR CERTAIN TRANSFERS TO REGULATED INVESTMENT COMPANIES.—

"(1) IN GENERAL.—If—

"(A) a common trust fund transfers substantially all of its assets to one or more regulated investment companies in exchange solely for stock in the company or companies to which such assets are so transferred, and

"(B) such stock is distributed by such common trust fund to participants in such common trust fund in exchange solely for their interests in such common trust fund, no gain or loss shall be recognized by such common trust fund by reason of such transfer or distribution, and no gain or loss shall be recognized by any participant in such common trust fund by reason of such exchange.

"(2) BASIS RULES.—

"(A) REGULATED INVESTMENT COMPANY.—The basis of any asset received by a regulated investment company in a transfer referred to in paragraph (1)(A) shall be the same as it would be in the hands of the common trust fund.

"(B) PARTICIPANTS.—The basis of the stock which is received in an exchange referred to in paragraph (1)(B) shall be the same as that of the property exchanged. If stock in more than one regulated investment company is received in such exchange, the basis determined under the preceding sentence shall be allocated among the stock in each such company on the basis of respective fair market values.

"(3) TREATMENT OF ASSUMPTIONS OF LIABILITY.—

"(A) IN GENERAL.—In determining whether the transfer referred to in paragraph (1)(A) is in exchange solely for stock in one or more regulated investment companies, the assumption by any such company of a liability of the common trust fund, and the fact that any property transferred by the common trust fund is subject to a liability, shall be disregarded.

"(B) SPECIAL RULE WHERE ASSUMED LIABILITIES EXCEED BASIS.—

"(i) IN GENERAL.—If, in any transfer referred to in paragraph (1)(A), the assumed liabilities exceed the aggregate adjusted bases (in the hands of the common trust fund) of the assets transferred to the regulated investment company or companies—

"(I) notwithstanding paragraph (1), gain shall be recognized to the common trust fund on such transfer in an amount equal to such excess,

"(II) the basis of the assets received by the regulated investment company or companies in such transfer shall be increased by the amount so recognized, and

"(III) any adjustment to the basis of a participant's interest in the common trust fund as a result of the gain so recognized shall be treated as occurring immediately before the exchange referred to in paragraph (1)(B).

If the transfer referred to in paragraph (1)(A) is to two or more regulated investment companies, the basis increase under subclause (II) shall be allocated among such companies on the basis of the respective fair market values of the assets received by each of such companies.

"(ii) ASSUMED LIABILITIES.—For purposes of clause (i), the term 'assumed liabilities' means the aggregate of—

"(I) any liability of the common trust fund assumed by any regulated investment company in connection with the transfer referred to in paragraph (1)(A), and

"(II) any liability to which property so transferred is subject.

"(4) COMMON TRUST FUND MUST MEET DIVERSIFICATION RULES.—This subsection shall not apply to any common trust fund which would not meet the requirements of section 368(a)(2)(F)(ii) if it were a corporation. For purposes of the preceding sentence, Government securities shall not be treated as securities of an issuer in applying the 25-percent and 50-percent test and such securities shall not be excluded for purposes of determining total assets under clause (iv) of section 368(a)(2)(F).".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to transfers after December 31, 1995.

SEC. 1806. QUALIFIED STATE TUITION PROGRAMS.

(a) IN GENERAL.—Subchapter F of chapter 1 (relating to exempt organizations) is amended by adding at the end the following new part:

"PART VIII—QUALIFIED STATE TUITION PROGRAMS

"Sec. 529. Qualified State tuition programs.

"SEC. 529. QUALIFIED STATE TUITION PROGRAMS.

"(a) GENERAL RULE.—A qualified State tuition program shall be exempt from taxation under this subtitle. Notwithstanding the preceding sentence, such program shall be subject to the taxes imposed by section 511 (relating to imposition of tax on unrelated business income of charitable organizations).

"(b) QUALIFIED STATE TUITION PROGRAM.—For purposes of this section—

"(1) IN GENERAL.—The term 'qualified State tuition program' means a program established and maintained by a State or agency or instrumentality thereof—

"(A) under which a person—

"(i) may purchase tuition credits or certificates on behalf of a designated beneficiary which entitle the beneficiary to the waiver or payment of qualified higher education expenses of the beneficiary, or

"(ii) may make contributions to an account which is established for the purpose of meeting the qualified higher education expenses of the designated beneficiary of the account, and

"(B) which meets the other requirements of this subsection.

"(2) CASH CONTRIBUTIONS.—A program shall not be treated as a qualified State tuition program unless it provides that purchases or contributions may only be made in cash.

"(3) REFUNDS.—A program shall not be treated as a qualified State tuition program unless it imposes a more than de minimis penalty on any refund of earnings from the account which are not—

"(A) used for qualified higher education expenses of the designated beneficiary,

"(B) made on account of the death or disability of the designated beneficiary, or

"(C) made on account of a scholarship (or allowance or payment described in section 135(d)(1) (B) or (C)) received by the designated beneficiary to the extent the amount of the refund does not exceed the amount of the scholarship, allowance, or payment.

"(4) SEPARATE ACCOUNTING.—A program shall not be treated as a qualified State tuition program unless it provides separate accounting for each designated beneficiary.

"(5) NO INVESTMENT DIRECTION.—A program shall not be treated as a qualified State tuition program unless it provides that any contributor to, or designated beneficiary under, such program may not direct the investment of any contributions to the program (or any earnings thereon).

"(6) NO PLEDGING OF INTEREST AS SECURITY.—A program shall not be treated as a qualified State tuition program if it allows any interest in the program or any portion thereof to be used as security for a loan.

"(7) PROHIBITION ON EXCESS CONTRIBUTIONS.—A program shall not be treated as a qualified State tuition program unless it provides adequate safeguards to prevent contributions on behalf of a designated beneficiary in excess of those necessary to provide for the qualified higher education expenses of the beneficiary.

"(c) TAX TREATMENT OF DESIGNATED BENEFICIARIES AND CONTRIBUTORS.—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, no amount shall be includible in gross income of—

"(A) a designated beneficiary under a qualified State tuition program, or

"(B) a contributor to such program on behalf of a designated beneficiary,

with respect to any distribution or earnings under such program.

"(2) CONTRIBUTIONS.—In no event shall a contribution to a qualified State tuition program on behalf of a designated beneficiary be treated as a taxable gift for purposes of chapter 12.

"(3) DISTRIBUTIONS.—

"(A) IN GENERAL.—Any distribution under a qualified State tuition program shall be includible in the gross income of the distributee in the manner as provided under section 72 to the extent not excluded from gross income under any other provision of this chapter.

"(B) IN-KIND DISTRIBUTIONS.—Any benefit furnished to a designated beneficiary under a qualified State tuition program shall be treated as a distribution to the beneficiary.

"(C) CHANGE IN BENEFICIARIES.—

"(i) ROLLOVERS.—Subparagraph (A) shall not apply to that portion of any distribution which, within 60 days of such distribution, is transferred to the credit of another designated beneficiary under a qualified State tuition program who is a member of the family of the designated beneficiary with respect to which the distribution was made.

"(ii) CHANGE IN DESIGNATED BENEFICIARIES.—Any change in the designated beneficiary of an interest in a qualified State tuition program shall not be treated as a distribution for purposes of subparagraph (A) if the new beneficiary is a member of the family of the old beneficiary.

"(D) OPERATING RULES.—For purposes of applying section 72—

"(i) to the extent provided by the Secretary, all qualified State tuition programs of which an individual is a designated beneficiary shall be treated as one program,

"(ii) all distributions during a taxable year shall be treated as one distribution, and

"(iii) the value of the contract, income on the contract, and investment in the contract shall be computed as of the close of the calendar year in which the taxable year begins.

"(4) ESTATE TAX INCLUSION.—The value of any interest in any qualified State tuition program which is attributable to contributions made by an individual to such program on behalf of any designated beneficiary shall be includible in the gross estate of the contributor for purposes of chapter 11.

"(5) SPECIAL RULE FOR APPLYING SECTION 2503(e).—For purposes of section 2503(e), the waiver (or payment to an educational institution) of qualified higher education expenses of a designated beneficiary under a qualified State tuition program shall be treated as a qualified transfer.

"(d) REPORTING REQUIREMENTS.—

"(1) IN GENERAL.—If there is a distribution to any individual with respect to an interest in a qualified State tuition program during any calendar year, each officer or employee having control of the qualified State tuition program or their designee shall make such reports as the Secretary may require regarding such distribution to the Secretary and to the designated beneficiary or the individual to whom the distribution was made. Any such report shall include such information as the Secretary may prescribe.

"(2) TIMING OF REPORTS.—Any report required by this subsection—

"(A) shall be filed at such time and in such matter as the Secretary prescribes, and

"(B) shall be furnished to individuals not later than January 31 of the calendar year following the calendar year to which such report relates.

"(e) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) DESIGNATED BENEFICIARY.—The term 'designated beneficiary' means—

"(A) the individual designated at the commencement of participation in the qualified State tuition program as the beneficiary of amounts paid (or to be paid) to the program,

"(B) in the case of a change in beneficiaries described in subsection (c)(2)(C), the individual who is the new beneficiary, and

"(C) in the case of an interest in a qualified State tuition program purchased by a State or local government or an organization described in section 501(c)(3) and exempt from taxation under section 501(a) as part of a scholarship program operated by such government or organization, the individual receiving such interest as a scholarship.

"(2) MEMBER OF FAMILY.—The term 'member of the family' has the same meaning given such term as section 2032A(e)(2).

"(3) QUALIFIED HIGHER EDUCATION EXPENSES.—The term 'qualified higher education expenses' means tuition, fees, books, supplies, and equipment required for the enrollment or attendance of a designated beneficiary at an eligible educational institution (as defined in section 135(c)(3)).

"(4) APPLICATION OF SECTION 514.—An interest in a qualified State tuition program shall not be treated as debt for purposes of section 514.".

(b) CONFORMING AMENDMENTS.—

(1) Section 135(d)(1) is amended by striking "or" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting ", or", and by adding at the end the following new subparagraph:

"(D) a payment, waiver, or reimbursement of qualified higher education expenses under a qualified State tuition program (within the meaning of section 529(b))."

(2) The table of parts for subchapter F of chapter 1 is amended by adding at the end the following new item:

"Part VIII. Qualified State tuition programs."

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years ending after the date of the enactment of this Act.

(2) TRANSITION RULE.—If—

(A) a State or agency or instrumentality thereof maintains, on the date of the enactment of this Act, a program under which persons may purchase tuition credits or certificates on behalf of, or make contributions for education expenses of, a designated beneficiary, and

(B) such program meets the requirements of a qualified State tuition program before the later of—

(i) the date which is 1 year after such date of enactment, or

(ii) the first day of the first calendar quarter after the close of the first regular session of the State legislature that begins after such date of enactment,

the amendments made by this section shall apply to contributions (and earnings allocable thereto) made before the date such program meets the requirements of such amendments without regard to whether any requirements of such amendments are met with respect to such contributions and earnings.

For purposes of subparagraph (B)(ii), if a State has a 2-year legislative session, each year of such session shall be deemed to be a separate regular session of the State legislature.

SEC. 1807. ADOPTION ASSISTANCE.

(a) IN GENERAL.—Subpart A of part IV of subchapter A of chapter 1 (relating to nonrefundable personal credits) is amended by inserting after section 22 the following new section:

"SEC. 23. ADOPTION EXPENSES.

"(a) ALLOWANCE OF CREDIT.—

"(1) IN GENERAL.—In the case of an individual, there shall be allowed as a credit against the tax imposed by this chapter the amount of the qualified adoption expenses paid or incurred by the taxpayer.

"(2) YEAR CREDIT ALLOWED.—The credit under paragraph (1) with respect to any expense shall be allowed—

"(A) for the taxable year following the taxable year during which such expense is paid or incurred, or

"(B) in the case of an expense which is paid or incurred during the taxable year in which the adoption becomes final, for such taxable year.

"(b) LIMITATIONS.—

"(1) DOLLAR LIMITATION.—The aggregate amount of qualified adoption expenses which may be taken into account under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed $5,000 ($6,000, in the case of a child with special needs).

"(2) INCOME LIMITATION.—

"(A) IN GENERAL.—The amount allowable as a credit under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so allowable (determined without regard to this paragraph but with regard to paragraph (1)) as—

"(i) the amount (if any) by which the taxpayer's adjusted gross income exceeds $75,000, bears to

"(ii) $40,000.

"(B) DETERMINATION OF ADJUSTED GROSS INCOME.—For purposes of subparagraph (A), adjusted gross income shall be determined—

"(i) without regard to sections 911, 931, and 933, and

"(ii) after the application of sections 86, 135, 137, 219, and 469.

"(3) DENIAL OF DOUBLE BENEFIT.—

"(A) IN GENERAL.—No credit shall be allowed under subsection (a) for any expense for which a deduction or credit is allowed under any other provision of this chapter.

"(B) GRANTS.—No credit shall be allowed under subsection (a) for any expense to the extent that funds for such expense are received under any Federal, State, or local program.

"(c) CARRYFORWARDS OF UNUSED CREDIT.—If the credit allowable under subsection (a) for any taxable year exceeds the limitation imposed by section 26(a) for such taxable year reduced by the sum of the credits allowable under this subpart (other than this section), such excess shall be carried to the succeeding taxable year and added to the credit allowable under subsection (a) for such taxable year. No credit may be carried forward under this subsection to any taxable year following the fifth taxable year after the taxable year in which the credit arose. For purposes of the preceding sentence, credits shall be treated as used on a first-in first-out basis.

"(d) DEFINITIONS.—For purposes of this section—

"(1) QUALIFIED ADOPTION EXPENSES.—The term 'qualified adoption expenses' means reasonable and necessary adoption fees, court costs, attorney fees, and other expenses—

"(A) which are directly related to, and the principal purpose of which is for, the legal adoption of an eligible child by the taxpayer,

"(B) which are not incurred in violation of State or Federal law or in carrying out any surrogate parenting arrangement,

"(C) which are not expenses in connection with the adoption by an individual of a child who is the child of such individual's spouse, and

"(D) which are not reimbursed under an employer program or otherwise.

"(2) ELIGIBLE CHILD.—The term 'eligible child' means any individual—

"(A) who—

"(i) has not attained age 18, or

"(ii) is physically or mentally incapable of caring for himself, and

"(B) in the case of qualified adoption expenses paid or incurred after December 31, 2001, who is a child with special needs.

"(3) CHILD WITH SPECIAL NEEDS.—The term 'child with special needs' means any child if—

"(A) a State has determined that the child cannot or should not be returned to the home of his parents,

"(B) such State has determined that there exists with respect to the child a specific factor or condition (such as his ethnic background, age, or membership in a minority or sibling group, or the presence of factors such as medical conditions or physical, mental, or emotional handicaps) because of which it is reasonable to conclude that such child cannot be placed with adoptive parents without providing adoption assistance, and

"(C) such child is a citizen or resident of the United States (as defined in section 217(h)(3)).

"(e) SPECIAL RULES FOR FOREIGN ADOPTIONS.—In the case of an adoption of a child who is not a citizen or resident of the United States (as defined in section 217(h)(3))—

"(1) subsection (a) shall not apply to any qualified adoption expense with respect to such adoption unless such adoption becomes final, and

"(2) any such expense which is paid or incurred before the taxable year in which such adoption becomes final shall be taken into account under this section as if such expense were paid or incurred during such year.

"(f) FILING REQUIREMENTS.—

"(1) MARRIED COUPLES MUST FILE JOINT RETURNS.—Rules similar to the rules of paragraphs (2), (3), and (4) of section 21(e) shall apply for purposes of this section.

"(2) TAXPAYER MUST INCLUDE TIN.—

"(A) In general.—No credit shall be allowed under this section with respect to any eligible child unless the taxpayer includes (if known) the name, age, and TIN of such child on the return of tax for the taxable year.

"(B) OTHER METHODS.—The Secretary may, in lieu of the information referred to in subparagraph (A), require other information meeting the purposes of subparagraph (A), including identification of an agent assisting with the adoption.

"(g) BASIS ADJUSTMENTS.—For purposes of this subtitle, if a credit is allowed under this section for any expenditure with respect to any property, the increase in the basis of such property which would (but for this subsection) result from such expenditure shall be reduced by the amount of the credit so allowed.

"(h) REGULATIONS.—The Secretary shall prescribe such regulations as may be appropriate to carry out this section and section 137, including regulations which treat unmarried individuals who pay or incur qualified adoption expenses with respect to the same child as 1 taxpayer for purposes of applying the dollar limitation in subsection (b)(1) of this section and in section 137(b)(1)."

(b) EXCLUSION OF AMOUNTS RECEIVED UNDER EMPLOYER'S ADOPTION ASSISTANCE PROGRAMS.—Part III of subchapter B of chapter 1 (relating to items specifically excluded from gross income) is amended by redesignating section 137 as section 138 and by inserting after section 136 the following new section:

"SEC. 137. ADOPTION ASSISTANCE PROGRAMS.

"(a) IN GENERAL.—Gross income of an employee does not include amounts paid or expenses incurred by the employer for qualified adoption expenses in connection with the adoption of a child by an employee if such amounts are furnished pursuant to an adoption assistance program.

"(b) LIMITATIONS.—

"(1) DOLLAR LIMITATION.—The aggregate amount excludable from gross income under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed $5,000 ($6,000, in the case of a child with special needs).

"(2) INCOME LIMITATION.—The amount excludable from gross income under subsection (a) for any taxable year shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so excludable (determined without regard to this paragraph but with regard to paragraph (1)) as—

"(A) the amount (if any) by which the taxpayer's adjusted gross income exceeds $75,000, bears to

"(B) $40,000.

"(3) DETERMINATION OF ADJUSTED GROSS INCOME.—For purposes of paragraph (2), adjusted gross income shall be determined—

"(A) without regard to this section and sections 911, 931, and 933, and

"(B) after the application of sections 86, 135, 219, and 469.

"(c) ADOPTION ASSISTANCE PROGRAM.—For purposes of this section, an adoption assistance program is a separate written plan of an employer for the exclusive benefit of such employer's employees—

"(1) under which the employer provides such employees with adoption assistance, and

"(2) which meets requirements similar to the requirements of paragraphs (2), (3), (5), and (6) of section 127(b).

An adoption reimbursement program operated under section 1052 of title 10, United States Code (relating to armed forces) or section 514 of title 14, United States Code (relating to members of the Coast Guard) shall be treated as an adoption assistance program for purposes of this section.

"(d) QUALIFIED ADOPTION EXPENSES.—For purposes of this section, the term 'qualified adoption expenses' has the meaning given such term by section 23(d) (determined without regard to reimbursements under this section).

"(e) CERTAIN RULES TO APPLY.—Rules similar to the rules of subsections (e), (f), and (g) of section 23 shall apply for purposes of this section.

"(f) TERMINATION.—This section shall not apply to amounts paid or expenses incurred after December 31, 2001."

(c) CONFORMING AMENDMENTS.—

(1) Subparagraph (C) of section 25(e)(1) is amended by inserting "and section 23" after "this section".

(2) Sections 86(b)(2)(A) and 135(c)(4)(A) are each amended by inserting "137," before "911".

(3) Clause (i) of section 219(g)(3)(A) is amended by inserting ", 137," before "and 911".

(4) Clause (ii) of section 469(i)(3)(E) is amended to read as follows:

"(ii) the amounts excludable from gross income under sections 135 and 137,".

(5) Subsection (a) of section 1016 is amended by striking "and" at the end of paragraph (24), by striking the period at the end of paragraph (25) and inserting ", and", and by adding at the end the following new paragraph:

"(26) to the extent provided in sections 23(g) and 137(e)."

(6) The table of sections for subpart A of part IV of subchapter A of chapter 1 is amended by inserting after the item relating to section 22 the following new item:

"Sec. 23. Adoption expenses."

(7) The table of sections for part III of subchapter B of chapter 1 is amended by striking the item relating to section 137 and inserting the following:

"Sec. 137. Adoption assistance programs.
"Sec. 138. Cross reference to other Acts."

(d) STUDY AND REPORT.—The Secretary of the Treasury shall study the effect on adoptions of the tax credit and gross income exclusion established by the amendments made by this section and shall submit a report regarding the study to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives not later than January 1, 2000.

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 1808. REMOVAL OF BARRIERS TO INTERETHNIC ADOPTION.

(a) STATE PLAN REQUIREMENTS.—Section 471(a) of the Social Security Act (42 U.S.C 671(a)) is amended—

(1) by striking "and" at the end of paragraph (16);

(2) by striking the period at the end of paragraph (17) and inserting "; and"; and

(3) by adding at the end the following:

"(18) not later than January 1, 1997, provides that neither the State nor any other entity in the State that receives funds from the Federal Government and is involved in adoption or foster care placements may—

"(A) deny to any person the opportunity to become an adoptive or a foster parent, on the basis of the race, color, or national origin of the person, or of the child, involved; or

"(B) delay or deny the placement of a child for adoption or into foster care, on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved.".

(b) ENFORCEMENT.—Section 474 of such Act (42 U.S.C. 674) is amended by adding at the end the following:

"(d)(1) If, during any quarter of a fiscal year, a State's program operated under this part is found, as a result of a review conducted under section 1123A, or otherwise, to have violated section 471(a)(18) with respect to a person or to have failed to implement a corrective action plan within a period of time not to exceed 6 months with respect to such violation, then, notwithstanding subsection (a) of this section and any regulations promulgated under section 1123A(b)(3), the Secretary shall reduce the amount otherwise payable to the State under this part, for that fiscal year quarter and for any subsequent quarter of such fiscal year, until the State program is found, as a result of a subsequent review under section 1123A, to have implemented a corrective action plan with respect to such violation, by—

"(A) 2 percent of such otherwise payable amount, in the case of the 1st such finding for the fiscal year with respect to the State;

"(B) 3 percent of such otherwise payable amount, in the case of the 2d such finding for the fiscal year with respect to the State; or

"(C) 5 percent of such otherwise payable amount, in the case of the 3d or subsequent such finding for the fiscal year with respect to the State.

In imposing the penalties described in this paragraph, the Secretary shall not reduce any fiscal year payment to a State by more than 5 percent.

"(2) Any other entity which is in a State that receives funds under this part and which violates section 471(a)(18) during a fiscal year quarter with respect to any person shall remit to the Secretary all funds that were paid by the State to the entity during the quarter from such funds.

"(3)(A) Any individual who is aggrieved by a violation of section 471(a)(18) by a State or other entity may bring an action seeking relief from the State or other entity in any United States district court.

"(B) An action under this paragraph may not be brought more than 2 years after the date the alleged violation occurred.

"(4) This subsection shall not be construed to affect the application of the Indian Child Welfare Act of 1978.".

(c) CIVIL RIGHTS.—

(1) PROHIBITED CONDUCT.—A person or government that is involved in adoption or foster care placements may not—

(A) deny to any individual the opportunity to become an adoptive or a foster parent, on the basis of the race, color, or national origin of the individual, or of the child, involved; or

(B) delay or deny the placement of a child for adoption or into foster care, on the basis of the race, color, or national origin of the adoptive or foster parent, or the child, involved.

(2) ENFORCEMENT.—Noncompliance with paragraph (1) is deemed a violation of title VI of the Civil Rights Act of 1964.

(3) NO EFFECT ON THE INDIAN CHILD WELFARE ACT OF 1978.—This subsection shall not be construed to affect the application of the Indian Child Welfare Act of 1978.

(d) CONFORMING AMENDMENT.—Section 553 of the Howard M. Metzenbaum Multiethnic Placement Act of 1994 (42 U.S.C. 5115a) is repealed.

SEC. 1809. 6-MONTH DELAY OF ELECTRONIC FUND TRANSFER REQUIREMENT.

Notwithstanding any other provision of law, the increase in the applicable required percentages for fiscal year 1997 in clauses (i)(IV) and (ii)(IV) of section 6302(h)(2)(C) of the Internal Revenue Code of 1986 shall not take effect before July 1, 1997.

Subtitle I—Foreign Trust Tax Compliance

SEC. 1901. IMPROVED INFORMATION REPORTING ON FOREIGN TRUSTS.

(a) IN GENERAL.—Section 6048 (relating to returns as to certain foreign trusts) is amended to read as follows:

"SEC. 6048. INFORMATION WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

"(a) NOTICE OF CERTAIN EVENTS.—

"(1) GENERAL RULE.—On or before the 90th day (or such later day as the Secretary may prescribe) after any reportable event, the responsible party shall provide written notice of such event to the Secretary in accordance with paragraph (2).

"(2) CONTENTS OF NOTICE.—The notice required by paragraph (1) shall contain such information as the Secretary may prescribe, including—

"(A) the amount of money or other property (if any) transferred to the trust in connection with the reportable event, and

"(B) the identity of the trust and of each trustee and beneficiary (or class of beneficiaries) of the trust.

"(3) REPORTABLE EVENT.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'reportable event' means—

"(i) the creation of any foreign trust by a United States person,

"(ii) the transfer of any money or property (directly or indirectly) to a foreign trust by a United States person, including a transfer by reason of death, and

"(iii) the death of a citizen or resident of the United States if—

"(I) the decedent was treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, or

"(II) any portion of a foreign trust was included in the gross estate of the decedent.

"(B) EXCEPTIONS.—

"(i) FAIR MARKET VALUE SALES.—Subparagraph (A)(ii) shall not apply to any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value and the rules of section 679(a)(3) shall apply.

"(ii) DEFERRED COMPENSATION AND CHARITABLE TRUSTS.—Subparagraph (A) shall not apply with respect to a trust which is—

"(I) described in section 402(b), 404(a)(4), or 404A, or

"(II) determined by the Secretary to be described in section 501(c)(3).

"(4) RESPONSIBLE PARTY.—For purposes of this subsection, the term 'responsible party' means—

"(A) the grantor in the case of the creation of an inter vivos trust,

"(B) the transferor in the case of a reportable event described in paragraph (3)(A)(ii) other than a transfer by reason of death, and

"(C) the executor of the decedent's estate in any other case.

"(b) UNITED STATES GRANTOR OF FOREIGN TRUST.—

"(1) IN GENERAL.—If, at any time during any taxable year of a United States person, such person is treated as the owner of any portion of a foreign trust under the rules of subpart E of part I of subchapter J of chapter 1, such person shall be responsible to ensure that—

"(A) such trust makes a return for such year which sets forth a full and complete accounting of all trust activities and operations for the year, the name of the United States agent for such trust, and such other information as the Secretary may prescribe, and

"(B) such trust furnishes such information as the Secretary may prescribe to each United States person (i) who is treated as the owner of any portion of such trust or (ii) who receives (directly or indirectly) any distribution from the trust.

"(2) TRUSTS NOT HAVING UNITED STATES AGENT.—

"(A) IN GENERAL.—If the rules of this paragraph apply to any foreign trust, the determination of amounts required to be taken into account with respect to such trust by a United States person under the rules of subpart E of part I of subchapter J of chapter 1 shall be determined by the Secretary.

"(B) UNITED STATES AGENT REQUIRED.—The rules of this paragraph shall apply to any foreign trust to which paragraph (1) applies unless such trust agrees (in such manner, subject to such conditions, and at such time as the Secretary shall prescribe) to authorize a United States person to act as such trust's limited agent solely for purposes of applying sections 7602, 7603, and 7604 with respect to—

"(i) any request by the Secretary to examine records or produce testimony related to the proper treatment of amounts required to be taken into account under the rules referred to in subparagraph (A), or

"(ii) any summons by the Secretary for such records or testimony.

The appearance of persons or production of records by reason of a United States person being such an agent shall not subject such persons or records to legal process for any purpose other than determining the correct treatment under this title of the amounts required to be taken into account under the rules referred to in subparagraph (A). A foreign trust which appoints and described in this subparagraph shall not be considered to have an office or a permanent establishment in the United States, or to be engaged in a trade or business in the United States, solely because of the activities of such agent pursuant to this subsection.

"(C) OTHER RULES TO APPLY.—Rules similar to the rules of paragraphs (2) and (4) of section 6038A(e) shall apply for purposes of this paragraph.

"(c) REPORTING BY UNITED STATES BENEFICIARIES OF FOREIGN TRUSTS.—

"(1) IN GENERAL.—If any United States person receives (directly or indirectly) during any taxable year of such person any distribution from a foreign trust, such person shall make a return with respect to such trust for such year which includes—

"(A) the name of such trust,

"(B) the aggregate amount of the distributions so received from such trust during such taxable year, and

"(C) such other information as the Secretary may prescribe.

"(2) INCLUSION IN INCOME IF RECORDS NOT PROVIDED.—

"(A) IN GENERAL.—If adequate records are not provided to the Secretary to determine the proper treatment of any distribution from a foreign trust, such distribution shall be treated as an accumulation distribution includible in the gross income of the distributee under chapter 1. To the extent provided in regulations, the preceding sentence shall not apply if the foreign trust elects to be subject to rules similar to the rules of subsection (b)(2)(B).

"(B) APPLICATION OF ACCUMULATION DISTRIBUTION RULES.—For purposes of applying section 668 in a case to which subparagraph (A) applies, the applicable number of years for purposes of section 668(a) shall be ½ of the number of years the trust has been in existence.

"(d) SPECIAL RULES.—

"(1) DETERMINATION OF WHETHER UNITED STATES PERSON MAKES TRANSFER OR RECEIVES DISTRIBUTION.—For purposes of this section, in determining whether a United States person makes a transfer to, or receives a distribution from, a foreign trust, the fact that a portion of such trust is treated as owned by another person under the rules of subpart E of part I of subchapter J of chapter 1 shall be disregarded.

"(2) DOMESTIC TRUSTS WITH FOREIGN ACTIVITIES.—To the extent provided in regulations, a trust which is a United States person shall be treated as a foreign trust for purposes of this section and section 6677 if such trust has substantial activities, or holds substantial property, outside the United States.

"(3) TIME AND MANNER OF FILING INFORMATION.—Any notice or return required under this section shall be made at such time and in such manner as the Secretary shall prescribe.

"(4) MODIFICATION OF RETURN REQUIREMENTS.—The Secretary is authorized to suspend or modify any requirement of this section if the Secretary determines that the United States has no significant tax interest in obtaining the required information.".

(b) INCREASED PENALTIES.—Section 6677 (relating to failure to file information returns with respect to certain foreign trusts) is amended to read as follows:

"SEC. 6677. FAILURE TO FILE INFORMATION WITH RESPECT TO CERTAIN FOREIGN TRUSTS.

"(a) CIVIL PENALTY.—In addition to any criminal penalty provided by law, if any notice or return required to be filed by section 6048—

"(1) is not filed on or before the time provided in such section, or

"(2) does not include all the information required pursuant to such section or includes incorrect information,

the person required to file such notice or return shall pay a penalty equal to 35 percent of the gross reportable amount. If any failure described in the preceding sentence continues for more than 90 days after the day on which the Secretary mails notice of such failure to the person required to pay such penalty, such person shall pay a penalty (in addition to the amount determined under the preceding sentence) of $10,000 for each 30-day period (or fraction thereof) during which such failure continues after the expiration of such 90-day period. In no event shall the penalty under this subsection with respect to any failure exceed the gross reportable amount.

"(b) SPECIAL RULES FOR RETURNS UNDER SECTION 6048(b).—In the case of a return required under section 6048(b)—

"(1) the United States person referred to in such section shall be liable for the penalty imposed by subsection (a), and

"(2) subsection (a) shall be applied by substituting '5 percent' for '35 percent'.

"(c) GROSS REPORTABLE AMOUNT.—For purposes of subsection (a), the term 'gross reportable amount' means—

"(1) the gross value of the property involved in the event (determined as of the date of the event) in the case of a failure relating to section 6048(a),

"(2) the gross value of the portion of the trust's assets at the close of the year treated as owned by the United States person in the case of a failure relating to section 6048(b)(1), and

"(3) the gross amount of the distributions in the case of a failure relating to section 6048(c).

"(d) REASONABLE CAUSE EXCEPTION.—No penalty shall be imposed by this section on any failure which is shown to be due to reasonable cause and not due to willful neglect. The fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the required information is not reasonable cause.

"(e) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a).".

(c) CONFORMING AMENDMENTS.—

(1) Paragraph (2) of section 6724(d) is amended by striking "or" at the end of subparagraph (S), by striking the period at the end of subparagraph (T) and inserting ", or", and by inserting after subparagraph (T) the following new subparagraph:

"(U) section 6048(b)(1)(B) (relating to foreign trust reporting requirements).".

(2) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking the item relating to section 6048 and inserting the following new item:

"Sec. 6048. Information with respect to certain foreign trusts.".

(3) The table of sections for part I of subchapter B of chapter 68 is amended by striking the item relating to section 6677 and inserting the following new item:

"Sec. 6677. Failure to file information with respect to certain foreign trusts.".

(d) EFFECTIVE DATES.—

(1) REPORTABLE EVENTS.—To the extent related to subsection (a) of section 6048 of the Internal Revenue Code of 1986, as amended by this section, the amendments made by this section shall apply to reportable events (as defined in such section 6048) occurring after the date of the enactment of this Act.

(2) GRANTOR TRUST REPORTING.—To the extent related to subsection (b) of such section 6048, the amendments made by this section shall apply to taxable years of United States persons beginning after December 31, 1995.

(3) REPORTING BY UNITED STATES BENEFICIARIES.—To the extent related to subsection (c) of such section 6048, the amendments made by this section shall apply to distributions received after the date of the enactment of this Act.

SEC. 1902. COMPARABLE PENALTIES FOR FAILURE TO FILE RETURN RELATING TO TRANSFERS TO FOREIGN ENTITIES.

(a) IN GENERAL.—Section 1494 is amended by adding at the end the following new subsection:

"(c) PENALTY.—In the case of any failure to file a return required by the Secretary with respect to any transfer described in section 1491, the person required to file such return shall be liable for the penalties provided in section 6677 in the same manner as if such failure were a failure to file a notice under section 6048(a).".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to transfers after the date of the enactment of this Act.

SEC. 1903. MODIFICATIONS OF RULES RELATING TO FOREIGN TRUSTS HAVING ONE OR MORE UNITED STATES BENEFICIARIES.

(a) TREATMENT OF TRUST OBLIGATIONS, ETC.—

(1) Paragraph (2) of section 679(a) is amended by striking subparagraph (B) and inserting the following:

"(B) TRANSFERS AT FAIR MARKET VALUE.—To any transfer of property to a trust in exchange for consideration of at least the fair market value of the transferred property. For purposes of the preceding sentence, consideration other than cash shall be taken into account at its fair market value.".

(2) Subsection (a) of section 679 (relating to foreign trusts having one or more United States beneficiaries) is amended by adding at the end the following new paragraph:

"(3) CERTAIN OBLIGATIONS NOT TAKEN INTO ACCOUNT UNDER FAIR MARKET VALUE EXCEPTION.—

"(A) IN GENERAL.—In determining whether paragraph (2)(B) applies to any transfer by a person described in

clause (ii) or (iii) of subparagraph (C), there shall not be taken into account—

"(i) except as provided in regulations, any obligation of a person described in subparagraph (C), and

"(ii) to the extent provided in regulations, any obligation which is guaranteed by a person described in subparagraph (C).

"(B) TREATMENT OF PRINCIPAL PAYMENTS ON OBLIGATION.—Principal payments by the trust on any obligation referred to in subparagraph (A) shall be taken into account on and after the date of the payment in determining the portion of the trust attributable to the property transferred.

"(C) PERSONS DESCRIBED.—The persons described in this subparagraph are—

"(i) the trust,

"(ii) any grantor or beneficiary of the trust, and

"(iii) any person who is related (within the meaning of section 643(i)(2)(B)) to any grantor or beneficiary of the trust.".

(b) EXEMPTION OF TRANSFERS TO CHARITABLE TRUSTS.—Subsection (a) of section 679 is amended by striking "section 404(a)(4) or 404A" and inserting "section 6048(a)(3)(B)(ii)".

(c) OTHER MODIFICATIONS.—Subsection (a) of section 679 is amended by adding at the end the following new paragraphs:

"(4) SPECIAL RULES APPLICABLE TO FOREIGN GRANTOR WHO LATER BECOMES A UNITED STATES PERSON.—

"(A) IN GENERAL.—If a nonresident alien individual has a residency starting date within 5 years after directly or indirectly transferring property to a foreign trust, this section and section 6048 shall be applied as if such individual transferred to such trust on the residency starting date an amount equal to the portion of such trust attributable to the property transferred by such individual to such trust in such transfer.

"(B) TREATMENT OF UNDISTRIBUTED INCOME.—For purposes of this section, undistributed net income for periods before such individual's residency starting date shall be taken into account in determining the portion of the trust which is attributable to property transferred by such individual to such trust but shall not otherwise be taken into account.

"(C) RESIDENCY STARTING DATE.—For purposes of this paragraph, an individual's residency starting date is the residency starting date determined under section 7701(b)(2)(A).

"(5) OUTBOUND TRUST MIGRATIONS.—If—

"(A) an individual who is a citizen or resident of the United States transferred property to a trust which was not a foreign trust, and

"(B) such trust becomes a foreign trust while such individual is alive,

then this section and section 6048 shall be applied as if such individual transferred to such trust on the date such trust becomes a foreign trust an amount equal to the portion of such

trust attributable to the property previously transferred by such individual to such trust. A rule similar to the rule of paragraph (4)(B) shall apply for purposes of this paragraph.".

(d) MODIFICATIONS RELATING TO WHETHER TRUST HAS UNITED STATES BENEFICIARIES.—Subsection (c) of section 679 is amended by adding at the end the following new paragraph:

"(3) CERTAIN UNITED STATES BENEFICIARIES DISREGARDED.—A beneficiary shall not be treated as a United States person in applying this section with respect to any transfer of property to foreign trust if such beneficiary first became a United States person more than 5 years after the date of such transfer.".

(e) TECHNICAL AMENDMENT.—Subparagraph (A) of section 679(c)(2) is amended to read as follows:

"(A) in the case of a foreign corporation, such corporation is a controlled foreign corporation (as defined in section 957(a)),".

(f) REGULATIONS.—Section 679 is amended by adding at the end the following new subsection:

"(d) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.".

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to transfers of property after February 6, 1995.

SEC. 1904. FOREIGN PERSONS NOT TO BE TREATED AS OWNERS UNDER GRANTOR TRUST RULES.

(a) GENERAL RULE.—

(1) Subsection (f) of section 672 (relating to special rule where grantor is foreign person) is amended to read as follows:

"(f) SUBPART NOT TO RESULT IN FOREIGN OWNERSHIP.—

"(1) IN GENERAL.—Notwithstanding any other provision of this subpart, this subpart shall apply only to the extent such application results in an amount (if any) being currently taken into account (directly or through 1 or more entities) under this chapter in computing the income of a citizen or resident of the United States or a domestic corporation.

"(2) EXCEPTIONS.—

"(A) CERTAIN REVOCABLE AND IRREVOCABLE TRUSTS.—Paragraph (1) shall not apply to any portion of a trust if—

"(i) the power to revest absolutely in the grantor title to the trust property to which such portion is attributable is exercisable solely by the grantor without the approval or consent of any other person or with the consent of a related or subordinate party who is subservient to the grantor, or

"(ii) the only amounts distributable from such portion (whether income or corpus) during the lifetime of the grantor are amounts distributable to the grantor or the spouse of the grantor.

"(B) COMPENSATORY TRUSTS.—Except as provided in regulations, paragraph (1) shall not apply to any portion of a trust distributions from which are taxable as compensation for services rendered.

"(3) SPECIAL RULES.—Except as otherwise provided in regulations prescribed by the Secretary—

"(A) a controlled foreign corporation (as defined in section 957) shall be treated as a domestic corporation for purposes of paragraph (1), and

"(B) paragraph (1) shall not apply for purposes of applying section 1296.

"(4) RECHARACTERIZATION OF PURPORTED GIFTS.—In the case of any transfer directly or indirectly from a partnership or foreign corporation which the transferee treats as a gift or bequest, the Secretary may recharacterize such transfer in such circumstances as the Secretary determines to be appropriate to prevent the avoidance of the purposes of this subsection.

"(5) SPECIAL RULE WHERE GRANTOR IS FOREIGN PERSON.—If—

"(A) but for this subsection, a foreign person would be treated as the owner of any portion of a trust, and

"(B) such trust has a beneficiary who is a United States person,

such beneficiary shall be treated as the grantor of such portion to the extent such beneficiary has made (directly or indirectly) transfers of property (other than in a sale for full and adequate consideration) to such foreign person. For purposes of the preceding sentence, any gift shall not be taken into account to the extent such gift would be excluded from taxable gifts under section 2503(b).

"(6) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subsection, including regulations providing that paragraph (1) shall not apply in appropriate cases.".

(2) The last sentence of subsection (c) of section 672 is amended by inserting "subsection (f) and" before "sections 674".

(b) CREDIT FOR CERTAIN TAXES.—

(1) Paragraph (2) of section 665(d) is amended by adding at the end the following new sentence: "Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust under subpart E but for section 672(f), the term 'taxes imposed on the trust' includes the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on the settlor or such other person in respect of trust income.".

(2) Paragraph (5) of section 901(b) is amended by adding at the end the following new sentence: "Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust under subpart E but for section 672(f), the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on the settlor or such other person in respect of trust income.".

(c) DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS THROUGH NOMINEES.—

(1) Section 643 is amended by adding at the end the following new subsection:

"(h) DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS THROUGH NOMINEES.—For purposes of this part, any amount paid to a United States person which is derived directly or indirectly from a foreign trust of which the payor is not the grantor shall be deemed in the year of payment to have been directly paid by the foreign trust to such United States person.".

(2) Section 665 is amended by striking subsection (c).

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided by paragraph (2), the amendments made by this section shall take effect on the date of the enactment of this Act.

(2) EXCEPTION FOR CERTAIN TRUSTS.—The amendments made by this section shall not apply to any trust—

(A) which is treated as owned by the grantor under section 676 or 677 (other than subsection (a)(3) thereof) of the Internal Revenue Code of 1986, and

(B) which is in existence on September 19, 1995.

The preceding sentence shall not apply to the portion of any such trust attributable to any transfer to such trust after September 19, 1995.

(e) TRANSITIONAL RULE.—If—

(1) by reason of the amendments made by this section, any person other than a United States person ceases to be treated as the owner of a portion of a domestic trust, and

(2) before January 1, 1997, such trust becomes a foreign trust, or the assets of such trust are transferred to a foreign trust,

no tax shall be imposed by section 1491 of the Internal Revenue Code of 1986 by reason of such trust becoming a foreign trust or the assets of such trust being transferred to a foreign trust.

SEC. 1905. INFORMATION REPORTING REGARDING FOREIGN GIFTS.

(a) IN GENERAL.—Subpart A of part III of subchapter A of chapter 61 is amended by inserting after section 6039E the following new section:

"SEC. 6039F. NOTICE OF LARGE GIFTS RECEIVED FROM FOREIGN PERSONS.

"(a) IN GENERAL.—If the value of the aggregate foreign gifts received by a United States person (other than an organization described in section 501(c) and exempt from tax under section 501(a)) during any taxable year exceeds $10,000, such United States person shall furnish (at such time and in such manner as the Secretary shall prescribe) such information as the Secretary may prescribe regarding each foreign gift received during such year.

"(b) FOREIGN GIFT.—For purposes of this section, the term 'foreign gift' means any amount received from a person other than a United States person which the recipient treats as a gift or bequest. Such term shall not include any qualified transfer (within the meaning of section 2503(e)(2)) or any distribution properly disclosed in a return under section 6048(c).

"(c) PENALTY FOR FAILURE TO FILE INFORMATION.—

"(1) IN GENERAL.—If a United States person fails to furnish the information required by subsection (a) with respect to any foreign gift within the time prescribed therefor (including extensions)—

"(A) the tax consequences of the receipt of such gift shall be determined by the Secretary, and

"(B) such United States person shall pay (upon notice and demand by the Secretary and in the same manner as tax) an amount equal to 5 percent of the amount of such foreign gift for each month for which the failure continues (not to exceed 25 percent of such amount in the aggregate).

"(2) REASONABLE CAUSE EXCEPTION.—Paragraph (1) shall not apply to any failure to report a foreign gift if the United States person shows that the failure is due to reasonable cause and not due to willful neglect.

"(d) COST-OF-LIVING ADJUSTMENT.—In the case of any taxable year beginning after December 31, 1996, the $10,000 amount under subsection (a) shall be increased by an amount equal to the product of such amount and the cost-of-living adjustment for such taxable year under section 1(f)(3), except that subparagraph (B) thereof shall be applied by substituting '1995' for '1992'.

"(e) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.".

(b) CLERICAL AMENDMENT.—The table of sections for such subpart is amended by inserting after the item relating to section 6039E the following new item:

"Sec. 6039F. Notice of large gifts received from foreign persons.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts received after the date of the enactment of this Act in taxable years ending after such date.

SEC. 1906. MODIFICATION OF RULES RELATING TO FOREIGN TRUSTS WHICH ARE NOT GRANTOR TRUSTS.

(a) MODIFICATION OF INTEREST CHARGE ON ACCUMULATION DISTRIBUTIONS.—Subsection (a) of section 668 (relating to interest charge on accumulation distributions from foreign trusts) is amended to read as follows:

"(a) GENERAL RULE.—For purposes of the tax determined under section 667(a)—

"(1) INTEREST DETERMINED USING UNDERPAYMENT RATES.—The interest charge determined under this section with respect to any distribution is the amount of interest which would be determined on the partial tax computed under section 667(b) for the period described in paragraph (2) using the rates and the method under section 6621 applicable to underpayments of tax.

"(2) PERIOD.—For purposes of paragraph (1), the period described in this paragraph is the period which begins on the date which is the applicable number of years before the date of the distribution and which ends on the date of the distribution.

"(3) APPLICABLE NUMBER OF YEARS.—For purposes of paragraph (2)—

"(A) IN GENERAL.—The applicable number of years with respect to a distribution is the number determined by dividing—

"(i) the sum of the products described in subparagraph (B) with respect to each undistributed income year, by

"(ii) the aggregate undistributed net income.

The quotient determined under the preceding sentence shall be rounded under procedures prescribed by the Secretary.

"(B) PRODUCT DESCRIBED.—For purposes of subparagraph (A), the product described in this subparagraph with respect to any undistributed income year is the product of—

"(i) the undistributed net income for such year, and

"(ii) the sum of the number of taxable years between such year and the taxable year of the distribution (counting in each case the undistributed income year but not counting the taxable year of the distribution).

"(4) UNDISTRIBUTED INCOME YEAR.—For purposes of this subsection, the term 'undistributed income year' means any prior taxable year of the trust for which there is undistributed net income, other than a taxable year during all of which the beneficiary receiving the distribution was not a citizen or resident of the United States.

"(5) DETERMINATION OF UNDISTRIBUTED NET INCOME.—Notwithstanding section 666, for purposes of this subsection, an accumulation distribution from the trust shall be treated as reducing proportionately the undistributed net income for undistributed income years.

"(6) PERIODS BEFORE 1996.—Interest for the portion of the period described in paragraph (2) which occurs before January 1, 1996, shall be determined—

"(A) by using an interest rate of 6 percent, and

"(B) without compounding until January 1, 1996.".

(b) ABUSIVE TRANSACTIONS.—Section 643(a) is amended by inserting after paragraph (6) the following new paragraph:

"(7) ABUSIVE TRANSACTIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this part, including regulations to prevent avoidance of such purposes.".

(c) TREATMENT OF LOANS FROM TRUSTS.—

(1) IN GENERAL.—Section 643 (relating to definitions applicable to subparts A, B, C, and D) is amended by adding at the end the following new subsection:

"(i) LOANS FROM FOREIGN TRUSTS.—For purposes of subparts B, C, and D—

"(1) GENERAL RULE.—Except as provided in regulations, if a foreign trust makes a loan of cash or marketable securities directly or indirectly to—

"(A) any grantor or beneficiary of such trust who is a United States person, or

"(B) any United States person not described in subparagraph (A) who is related to such grantor or beneficiary,

the amount of such loan shall be treated as a distribution by such trust to such grantor or beneficiary (as the case may be).

"(2) DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—

"(A) CASH.—The term 'cash' includes foreign currencies and cash equivalents.

"(B) RELATED PERSON.—

"(i) IN GENERAL.—A person is related to another person if the relationship between such persons would result in a disallowance of losses under section 267 or 707(b). In applying section 267 for purposes of the preceding sentence, section 267(c)(4) shall be applied as if the family of an individual includes the spouses of the members of the family.

"(ii) ALLOCATION.—If any person described in paragraph (1)(B) is related to more than one person, the grantor or beneficiary to whom the treatment under this subsection applies shall be determined under regulations prescribed by the Secretary.

"(C) EXCLUSION OF TAX-EXEMPTS.—The term 'United States person' does not include any entity exempt from tax under this chapter.

"(D) TRUST NOT TREATED AS SIMPLE TRUST.—Any trust which is treated under this subsection as making a distribution shall be treated as described in section 651.

"(3) SUBSEQUENT TRANSACTIONS REGARDING LOAN PRINCIPAL.—If any loan is taken into account under paragraph (1), any subsequent transaction between the trust and the original borrower regarding the principal of the loan (by way of complete or partial repayment, satisfaction, cancellation, discharge, or otherwise) shall be disregarded for purposes of this title.".

(2) TECHNICAL AMENDMENT.—Paragraph (8) of section 7872(f) is amended by inserting ", 643(i)," before "or 1274" each place it appears.

(d) EFFECTIVE DATES.—

(1) INTEREST CHARGE.—The amendment made by subsection (a) shall apply to distributions after the date of the enactment of this Act.

(2) ABUSIVE TRANSACTIONS.—The amendment made by subsection (b) shall take effect on the date of the enactment of this Act.

(3) LOANS FROM TRUSTS.—The amendment made by subsection (c) shall apply to loans of cash or marketable securities made after September 19, 1995.

SEC. 1907. RESIDENCE OF TRUSTS, ETC.

(a) TREATMENT AS UNITED STATES PERSON.—

(1) IN GENERAL.—Paragraph (30) of section 7701(a) is amended by striking "and" at the end of subparagraph (C) and by striking subparagraph (D) and by inserting the following new subparagraphs:

"(D) any estate (other than a foreign estate, within the meaning of paragraph (31)), and

"(E) any trust if—

"(i) a court within the United States is able to exercise primary supervision over the administration of the trust, and

"(ii) one or more United States fiduciaries have the authority to control all substantial decisions of the trust.".

(2) CONFORMING AMENDMENT.—Paragraph (31) of section 7701(a) is amended to read as follows:

"(31) FOREIGN ESTATE OR TRUST.—

"(A) FOREIGN ESTATE.—The term 'foreign estate' means an estate the income of which, from sources without the United States which is not effectively connected with the conduct of a trade or business within the United States, is not includible in gross income under subtitle A.

"(B) FOREIGN TRUST.—The term 'foreign trust' means any trust other than a trust described in subparagraph (E) of paragraph (30).".

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply—

(A) to taxable years beginning after December 31, 1996, or

(B) at the election of the trustee of a trust, to taxable years ending after the date of the enactment of this Act.

Such an election, once made, shall be irrevocable.

(b) DOMESTIC TRUSTS WHICH BECOME FOREIGN TRUSTS.—

(1) IN GENERAL.—Section 1491 (relating to imposition of tax on transfers to avoid income tax) is amended by adding at the end the following new flush sentence:

"If a trust which is not a foreign trust becomes a foreign trust, such trust shall be treated for purposes of this section as having transferred, immediately before becoming a foreign trust, all of its assets to a foreign trust.".

(2) EFFECTIVE DATE.—The amendment made by this subsection shall take effect on the date of the enactment of this Act.

Subtitle J—Generalized System of Preferences

SEC. 1951. SHORT TITLE.

This subtitle may be cited as the "GSP Renewal Act of 1996".

SEC. 1952. GENERALIZED SYSTEM OF PREFERENCES.

(a) IN GENERAL.—Title V of the Trade Act of 1974 is amended to read as follows:

"TITLE V—GENERALIZED SYSTEM OF PREFERENCES

"SEC. 501. AUTHORITY TO EXTEND PREFERENCES.

"The President may provide duty-free treatment for any eligible article from any beneficiary developing country in accordance with

the provisions of this title. In taking any such action, the President shall have due regard for—

"(1) the effect such action will have on furthering the economic development of developing countries through the expansion of their exports;

"(2) the extent to which other major developed countries are undertaking a comparable effort to assist developing countries by granting generalized preferences with respect to imports of products of such countries;

"(3) the anticipated impact of such action on United States producers of like or directly competitive products; and

"(4) the extent of the beneficiary developing country's competitiveness with respect to eligible articles.

"SEC. 502. DESIGNATION OF BENEFICIARY DEVELOPING COUNTRIES.

"(a) AUTHORITY TO DESIGNATE COUNTRIES.—

"(1) BENEFICIARY DEVELOPING COUNTRIES.—The President is authorized to designate countries as beneficiary developing countries for purposes of this title.

"(2) LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRIES.—The President is authorized to designate any beneficiary developing country as a least-developed beneficiary developing country for purposes of this title, based on the considerations in section 501 and subsection (c) of this section.

"(b) COUNTRIES INELIGIBLE FOR DESIGNATION.—

"(1) SPECIFIC COUNTRIES.—The following countries may not be designated as beneficiary developing countries for purposes of this title:

"(A) Australia.
"(B) Canada.
"(C) European Union member states.
"(D) Iceland.
"(E) Japan.
"(F) Monaco.
"(G) New Zealand.
"(H) Norway.
"(I) Switzerland.

"(2) OTHER BASES FOR INELIGIBILITY.—The President shall not designate any country a beneficiary developing country under this title if any of the following applies:

"(A) Such country is a Communist country, unless—

"(i) the products of such country receive nondiscriminatory treatment,

"(ii) such country is a WTO Member (as such term is defined in section 2(10) of the Uruguay Round Agreements Act) (19 U.S.C. 3501(10)) and a member of the International Monetary Fund, and

"(iii) such country is not dominated or controlled by international communism.

"(B) Such country is a party to an arrangement of countries and participates in any action pursuant to such arrangement, the effect of which is—

"(i) to withhold supplies of vital commodity resources from international trade or to raise the price of such commodities to an unreasonable level, and

"(ii) to cause serious disruption of the world economy.

"(C) Such country affords preferential treatment to the products of a developed country, other than the United States, which has, or is likely to have, a significant adverse effect on United States commerce.

"(D)(i) Such country—

"(I) has nationalized, expropriated, or otherwise seized ownership or control of property, including patents, trademarks, or copyrights, owned by a United States citizen or by a corporation, partnership, or association which is 50 percent or more beneficially owned by United States citizens,

"(II) has taken steps to repudiate or nullify an existing contract or agreement with a United States citizen or a corporation, partnership, or association which is 50 percent or more beneficially owned by United States citizens, the effect of which is to nationalize, expropriate, or otherwise seize ownership or control of property, including patents, trademarks, or copyrights, so owned, or

"(III) has imposed or enforced taxes or other exactions, restrictive maintenance or operational conditions, or other measures with respect to property, including patents, trademarks, or copyrights, so owned, the effect of which is to nationalize, expropriate, or otherwise seize ownership or control of such property,

unless clause (ii) applies.

"(ii) This clause applies if the President determines that—

"(I) prompt, adequate, and effective compensation has been or is being made to the citizen, corporation, partnership, or association referred to in clause (i),

"(II) good faith negotiations to provide prompt, adequate, and effective compensation under the applicable provisions of international law are in progress, or the country described in clause (i) is otherwise taking steps to discharge its obligations under international law with respect to such citizen, corporation, partnership, or association, or

"(III) a dispute involving such citizen, corporation, partnership, or association over compensation for such a seizure has been submitted to arbitration under the provisions of the Convention for the Settlement of Investment Disputes, or in another mutually agreed upon forum,

and the President promptly furnishes a copy of such determination to the Senate and House of Representatives.

"(E) Such country fails to act in good faith in recognizing as binding or in enforcing arbitral awards in favor of United States citizens or a corporation, partnership, or association which is 50 percent or more beneficially owned by United States citizens, which have been made by arbitrators appointed for each case or by permanent arbitral bod-

ies to which the parties involved have submitted their dispute.

"(F) Such country aids or abets, by granting sanctuary from prosecution to, any individual or group which has committed an act of international terrorism.

"(G) Such country has not taken or is not taking steps to afford internationally recognized worker rights to workers in the country (including any designated zone in that country).

Subparagraphs (D), (E), (F), and (G) shall not prevent the designation of any country as a beneficiary developing country under this title if the President determines that such designation will be in the national economic interest of the United States and reports such determination to the Congress with the reasons therefor.

"(c) FACTORS AFFECTING COUNTRY DESIGNATION.—In determining whether to designate any country as a beneficiary developing country under this title, the President shall take into account—

"(1) an expression by such country of its desire to be so designated;

"(2) the level of economic development of such country, including its per capita gross national product, the living standards of its inhabitants, and any other economic factors which the President deems appropriate;

"(3) whether or not other major developed countries are extending generalized preferential tariff treatment to such country;

"(4) the extent to which such country has assured the United States that it will provide equitable and reasonable access to the markets and basic commodity resources of such country and the extent to which such country has assured the United States that it will refrain from engaging in unreasonable export practices;

"(5) the extent to which such country is providing adequate and effective protection of intellectual property rights;

"(6) the extent to which such country has taken action to—

"(A) reduce trade distorting investment practices and policies (including export performance requirements); and

"(B) reduce or eliminate barriers to trade in services; and

"(7) whether or not such country has taken or is taking steps to afford to workers in that country (including any designated zone in that country) internationally recognized worker rights.

"(d) WITHDRAWAL, SUSPENSION, OR LIMITATION OF COUNTRY DESIGNATION.—

"(1) IN GENERAL.—The President may withdraw, suspend, or limit the application of the duty-free treatment accorded under this title with respect to any country. In taking any action under this subsection, the President shall consider the factors set forth in section 501 and subsection (c) of this section.

"(2) CHANGED CIRCUMSTANCES.—The President shall, after complying with the requirements of subsection (f)(2), withdraw or suspend the designation of any country as a beneficiary de-

veloping country if, after such designation, the President determines that as the result of changed circumstances such country would be barred from designation as a beneficiary developing country under subsection (b)(2). Such country shall cease to be a beneficiary developing country on the day on which the President issues an Executive order or Presidential proclamation revoking the designation of such country under this title.

"(3) ADVICE TO CONGRESS.—The President shall, as necessary, advise the Congress on the application of section 501 and subsection (c) of this section, and the actions the President has taken to withdraw, to suspend, or to limit the application of duty-free treatment with respect to any country which has failed to adequately take the actions described in subsection (c).

"(e) MANDATORY GRADUATION OF BENEFICIARY DEVELOPING COUNTRIES.—If the President determines that a beneficiary developing country has become a 'high income' country, as defined by the official statistics of the International Bank for Reconstruction and Development, then the President shall terminate the designation of such country as a beneficiary developing country for purposes of this title, effective on January 1 of the second year following the year in which such determination is made.

"(f) CONGRESSIONAL NOTIFICATION.—

"(1) NOTIFICATION OF DESIGNATION.—

"(A) IN GENERAL.—Before the President designates any country as a beneficiary developing country under this title, the President shall notify the Congress of the President's intention to make such designation, together with the considerations entering into such decision.

"(B) DESIGNATION AS LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRY.—At least 60 days before the President designates any country as a least-developed beneficiary developing country, the President shall notify the Congress of the President's intention to make such designation.

"(2) NOTIFICATION OF TERMINATION.—If the President has designated any country as a beneficiary developing country under this title, the President shall not terminate such designation unless, at least 60 days before such termination, the President has notified the Congress and has notified such country of the President's intention to terminate such designation, together with the considerations entering into such decision.

"SEC. 503. DESIGNATION OF ELIGIBLE ARTICLES.

"(a) ELIGIBLE ARTICLES.—

"(1) DESIGNATION.—

"(A) IN GENERAL.—Except as provided in subsection (b), the President is authorized to designate articles as eligible articles from all beneficiary developing countries for purposes of this title by Executive order or Presidential proclamation after receiving the advice of the International Trade Commission in accordance with subsection (e).

"(B) LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRIES.—Except for articles described in subparagraphs (A), (B), and (E) of subsection (b)(1) and articles described in paragraphs (2) and (3) of subsection (b), the

President may, in carrying out section 502(d)(1) and subsection (c)(1) of this section, designate articles as eligible articles only for countries designated as least-developed beneficiary developing countries under section 502(a)(2) if, after receiving the advice of the International Trade Commission in accordance with subsection (e) of this section, the President determines that such articles are not import-sensitive in the context of imports from least-developed beneficiary developing countries.

"(C) THREE-YEAR RULE.—If, after receiving the advice of the International Trade Commission under subsection (e), an article has been formally considered for designation as an eligible article under this title and denied such designation, such article may not be reconsidered for such designation for a period of 3 years after such denial.

"(2) RULE OF ORIGIN.—

"(A) GENERAL RULE.—The duty-free treatment provided under this title shall apply to any eligible article which is the growth, product, or manufacture of a beneficiary developing country if—

"(i) that article is imported directly from a beneficiary developing country into the customs territory of the United States; and

"(ii) the sum of—

"(I) the cost or value of the materials produced in the beneficiary developing country or any two or more such countries that are members of the same association of countries and are treated as one country under section 507(2), plus

"(II) the direct costs of processing operations performed in such beneficiary developing country or such member countries,

is not less than 35 percent of the appraised value of such article at the time it is entered.

"(B) EXCLUSIONS.—An article shall not be treated as the growth, product, or manufacture of a beneficiary developing country by virtue of having merely undergone—

"(i) simple combining or packaging operations, or

"(ii) mere dilution with water or mere dilution with another substance that does not materially alter the characteristics of the article.

"(3) REGULATIONS.—The Secretary of the Treasury, after consulting with the United States Trade Representative, shall prescribe such regulations as may be necessary to carry out paragraph (2), including, but not limited to, regulations providing that, in order to be eligible for duty-free treatment under this title, an article—

"(A) must be wholly the growth, product, or manufacture of a beneficiary developing country, or

"(B) must be a new or different article of commerce which has been grown, produced, or manufactured in the beneficiary developing country.

"(b) ARTICLES THAT MAY NOT BE DESIGNATED AS ELIGIBLE ARTICLES.—

"(1) IMPORT SENSITIVE ARTICLES.—The President may not designate any article as an eligible article under subsection (a) if such article is within one of the following categories of import-sensitive articles:

"(A) Textile and apparel articles which were not eligible articles for purposes of this title on January 1, 1994, as this title was in effect on such date.

"(B) Watches, except those watches entered after June 30, 1989, that the President specifically determines, after public notice and comment, will not cause material injury to watch or watch band, strap, or bracelet manufacturing and assembly operations in the United States or the United States insular possessions.

"(C) Import-sensitive electronic articles.

"(D) Import-sensitive steel articles.

"(E) Footwear, handbags, luggage, flat goods, work gloves, and leather wearing apparel which were not eligible articles for purposes of this title on January 1, 1995, as this title was in effect on such date.

"(F) Import-sensitive semimanufactured and manufactured glass products.

"(G) Any other articles which the President determines to be import-sensitive in the context of the Generalized System of Preferences.

"(2) ARTICLES AGAINST WHICH OTHER ACTIONS TAKEN.—An article shall not be an eligible article for purposes of this title for any period during which such article is the subject of any action proclaimed pursuant to section 203 of this Act (19 U.S.C. 2253) or section 232 or 351 of the Trade Expansion Act of 1962 (19 U.S.C. 1862, 1981).

"(3) AGRICULTURAL PRODUCTS.—No quantity of an agricultural product subject to a tariff-rate quota that exceeds the in-quota quantity shall be eligible for duty-free treatment under this title.

"(c) WITHDRAWAL, SUSPENSION, OR LIMITATION OF DUTY-FREE TREATMENT; COMPETITIVE NEED LIMITATION.—

"(1) IN GENERAL.—The President may withdraw, suspend, or limit the application of the duty-free treatment accorded under this title with respect to any article, except that no rate of duty may be established with respect to any article pursuant to this subsection other than the rate which would apply but for this title. In taking any action under this subsection, the President shall consider the factors set forth in sections 501 and 502(c).

"(2) COMPETITIVE NEED LIMITATION.—

"(A) BASIS FOR WITHDRAWAL OF DUTY-FREE TREATMENT.—

"(i) IN GENERAL.—Except as provided in clause (ii) and subject to subsection (d), whenever the President determines that a beneficiary developing country has exported (directly or indirectly) to the United States during any calendar year beginning after December 31, 1995—

"(I) a quantity of an eligible article having an appraised value in excess of the applicable amount for the calendar year, or

"(II) a quantity of an eligible article equal to or exceeding 50 percent of the appraised value of the total imports of that article into the United States during any calendar year,

the President shall, not later than July 1 of the next calendar year, terminate the duty-free treatment for that article from that beneficiary developing country.

"(ii) ANNUAL ADJUSTMENT OF APPLICABLE AMOUNT.—For purposes of applying clause (i), the applicable amount is—

"(I) for 1996, $75,000,000, and

"(II) for each calendar year thereafter, a amount equal to the applicable amount in effect for the preceding calendar year plus $5,000,000.

"(B) COUNTRY DEFINED.—For purposes of this paragraph, the term 'country' does not include an association of countries which is treated as one country under section 507(2), but does include a country which is a member of any such association.

"(C) REDESIGNATIONS.—A country which is no longer treated as a beneficiary developing country with respect to an eligible article by reason of subparagraph (A) may, subject to the considerations set forth in sections 501 and 502, be redesignated a beneficiary developing country with respect to such article if imports of such article from such country did not exceed the limitations in subparagraph (A) during the preceding calendar year.

"(D) LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRIES.—Subparagraph (A) shall not apply to any least-developed beneficiary developing country.

"(E) ARTICLES NOT PRODUCED IN THE UNITED STATES EXCLUDED.—Subparagraph (A)(i)(II) shall not apply with respect to any eligible article if a like or directly competitive article was not produced in the United States on January 1, 1995.

"(F) DE MINIMIS WAIVERS.—

"(i) IN GENERAL.—The President may disregard subparagraph (A)(i)(II) with respect to any eligible article from any beneficiary developing country if the aggregate appraised value of the imports of such article into the United States during the preceding calendar year does not exceed the applicable amount for such preceding calendar year.

"(ii) APPLICABLE AMOUNT.—For purposes of applying clause (i), the applicable amount is—

"(I) for calendar year 1996, $13,000,000, and

"(II) for each calendar year thereafter, an amount equal to the applicable amount in effect for the preceding calendar year plus $500,000.

"(d) WAIVER OF COMPETITIVE NEED LIMITATION.—

"(1) IN GENERAL.—The President may waive the application of subsection (c)(2) with respect to any eligible article of any beneficiary developing country if, before July 1 of the calendar year beginning after the calendar year for which a determination described in subsection (c)(2)(A) was made with respect to such eligible article, the President—

"(A) receives the advice of the International Trade Commission under section 332 of the Tariff Act of 1930 on whether any industry in the United States is likely to be adversely affected by such waiver,

"(B) determines, based on the considerations described in sections 501 and 502(c) and the advice described in subparagraph (A), that such waiver is in the national economic interest of the United States, and

"(C) publishes the determination described in subparagraph (B) in the Federal Register.

"(2) CONSIDERATIONS BY THE PRESIDENT.—In making any determination under paragraph (1), the President shall give great weight to—

"(A) the extent to which the beneficiary developing country has assured the United States that such country will provide equitable and reasonable access to the markets and basic commodity resources of such country, and

"(B) the extent to which such country provides adequate and effective protection of intellectual property rights.

"(3) OTHER BASES FOR WAIVER.—The President may waive the application of subsection (c)(2) if, before July 1 of the calendar year beginning after the calendar year for which a determination described in subsection (c)(2) was made with respect to a beneficiary developing country, the President determines that—

"(A) there has been a historical preferential trade relationship between the United States and such country,

"(B) there is a treaty or trade agreement in force covering economic relations between such country and the United States, and

"(C) such country does not discriminate against, or impose unjustifiable or unreasonable barriers to, United States commerce,

and the President publishes that determination in the Federal Register.

"(4) LIMITATIONS ON WAIVERS.—

"(A) IN GENERAL.—The President may not exercise the waiver authority under this subsection with respect to a quantity of an eligible article entered during any calendar year beginning after 1995, the aggregate appraised value of which equals or exceeds 30 percent of the aggregate appraised value of all articles that entered duty-free under this title during the preceding calendar year.

"(B) OTHER WAIVER LIMITS.—The President may not exercise the waiver authority provided under this subsection with respect to a quantity of an eligible article entered during any calendar year beginning after 1995, the aggregate appraised value of which exceeds 15 percent of the aggre-

gate appraised value of all articles that have entered duty-free under this title during the preceding calendar year from those beneficiary developing countries which for the preceding calendar year—

"(i) had a per capita gross national product (calculated on the basis of the best available information, including that of the International Bank for Reconstruction and Development) of $5,000 or more; or

"(ii) had exported (either directly or indirectly) to the United States a quantity of articles that was duty-free under this title that had an aggregate appraised value of more than 10 percent of the aggregate appraised value of all articles that entered duty-free under this title during that year.

"(C) CALCULATION OF LIMITATIONS.—There shall be counted against the limitations imposed under subparagraphs (A) and (B) for any calendar year only that value of any eligible article of any country that—

"(i) entered duty-free under this title during such calendar year; and

"(ii) is in excess of the value of that article that would have been so entered during such calendar year if the limitations under subsection (c)(2)(A) applied.

"(5) EFFECTIVE PERIOD OF WAIVER.—Any waiver granted under this subsection shall remain in effect until the President determines that such waiver is no longer warranted due to changed circumstances.

"(e) INTERNATIONAL TRADE COMMISSION ADVICE.—Before designating articles as eligible articles under subsection (a)(1), the President shall publish and furnish the International Trade Commission with lists of articles which may be considered for designation as eligible articles for purposes of this title. The provisions of sections 131, 132, 133, and 134 shall be complied with as though action under section 501 and this section were action under section 123 to carry out a trade agreement entered into under section 123.

"(f) SPECIAL RULE CONCERNING PUERTO RICO.—No action under this title may affect any tariff duty imposed by the Legislature of Puerto Rico pursuant to section 319 of the Tariff Act of 1930 on coffee imported into Puerto Rico.

"SEC. 504. REVIEW AND REPORT TO CONGRESS.

The President shall submit an annual report to the Congress on the status of internationally recognized worker rights within each beneficiary developing country.

"SEC. 505. DATE OF TERMINATION.

"No duty-free treatment provided under this title shall remain in effect after May 31, 1997.

"SEC. 506. AGRICULTURAL EXPORTS OF BENEFICIARY DEVELOPING COUNTRIES.

"The appropriate agencies of the United States shall assist beneficiary developing countries to develop and implement measures designed to assure that the agricultural sectors of their economies are not directed to export markets to the detriment of the production of foodstuffs for their citizenry.

"SEC. 507. DEFINITIONS.

"For purposes of this title:

"(1) BENEFICIARY DEVELOPING COUNTRY.—The term 'beneficiary developing country' means any country with respect to which there is in effect an Executive order or Presidential proclamation by the President designating such country as a beneficiary developing country for purposes of this title.

"(2) COUNTRY.—The term 'country' means any foreign country or territory, including any overseas dependent territory or possession of a foreign country, or the Trust Territory of the Pacific Islands. In the case of an association of countries which is a free trade area or customs union, or which is contributing to comprehensive regional economic integration among its members through appropriate means, including, but not limited to, the reduction of duties, the President may by Executive order or Presidential proclamation provide that all members of such association other than members which are barred from designation under section 502(b) shall be treated as one country for purposes of this title.

"(3) ENTERED.—The term 'entered' means entered, or withdrawn from warehouse for consumption, in the customs territory of the United States.

"(4) INTERNATIONALLY RECOGNIZED WORKER RIGHTS.—The term 'internationally recognized worker rights' includes—

"(A) the right of association;

"(B) the right to organize and bargain collectively;

"(C) a prohibition on the use of any form of forced or compulsory labor;

"(D) a minimum age for the employment of children; and

"(E) acceptable conditions of work with respect to minimum wages, hours of work, and occupational safety and health.

"(5) LEAST-DEVELOPED BENEFICIARY DEVELOPING COUNTRY.—The term 'least-developed beneficiary developing country' means a beneficiary developing country that is designated as a least-developed beneficiary developing country under section 502(a)(2).".

(b) TABLE OF CONTENTS.—The items relating to title V in the table of contents of the Trade Act of 1974 are amended to read as follows:

"TITLE V—GENERALIZED SYSTEM OF PREFERENCES

SEC. 1953. EFFECTIVE DATE.

(a) IN GENERAL.—The amendments made by this subtitle apply to articles entered on or after October 1, 1996.

(b) RETROACTIVE APPLICATION.—

(1) GENERAL RULE.—Notwithstanding section 514 of the Tariff Act of 1930 or any other provision of law and subject to subsection (c)—

(A) any article that was entered—

(i) after July 31, 1995, and

(ii) before January 1, 1996, and

to which duty-free treatment under title V of the Trade Act of 1974 would have applied if the entry had been made on July 31, 1995, shall be liquidated or reliquidated as free of duty, and the Secretary of the Treasury shall refund any duty paid with respect to such entry, and

(B) any article that was entered—

(i) after December 31, 1995, and

(ii) before October 1, 1996, and

to which duty-free treatment under title V of the Trade Act of 1974 (as amended by this subtitle) would have applied if the entry had been made on or after October 1, 1996, shall be liquidated or reliquidated as free of duty, and the Secretary of the Treasury shall refund any duty paid with respect to such entry.

(2) LIMITATION ON REFUNDS.—No refund shall be made pursuant to this subsection before October 1, 1996.

(3) ENTRY.—As used in this subsection, the term "entry" includes a withdrawal from warehouse for consumption.

(c) REQUESTS.—Liquidation or reliquidation may be made under subsection (b) with respect to an entry only if a request therefor is filed with the Customs Service, within 180 days after the date of the enactment of this Act, that contains sufficient information to enable the Customs Service—

(1) to locate the entry; or

(2) to reconstruct the entry if it cannot be located.

SEC. 1954. CONFORMING AMENDMENTS.

(a) TRADE LAWS.—

(1) Section 1211(b) of the Omnibus Trade and Competitiveness Act of 1988 (19 U.S.C. 3011(b)) is amended—

(A) in paragraph (1), by striking "(19 U.S.C. 2463(a), 2464(c)(3))" and inserting "(as in effect on July 31, 1995)"; and

(B) in paragraph (2), by striking "(19 U.S.C. 2464(c)(1))" and inserting the following: "(as in effect on July 31, 1995)".

(2) Section 203(c)(7) of the Andean Trade Preference Act (19 U.S.C. 3202(c)(7)) is amended by striking "502(a)(4)" and inserting "507(4)".

(3) Section 212(b)(7) of the Caribbean Basin Economic Recovery Act (19 U.S.C. 2702(b)(7)) is amended by striking "502(a)(4)" and inserting "507(4)".

(4) General note 3(a)(iv)(C) of the Harmonized Tariff Schedule of the United States is amended by striking "sections 503(b) and 504(c)" and inserting "subsections (a), (c), and (d) of section 503".

(5) Section 201(a)(2) of the North American Free Trade Agreement Implementation Act (19 U.S.C. 3331(a)(2)) is amend-

ed by striking "502(a)(2) of the Trade Act of 1974 (19 U.S.C. 2462(a)(2))" and inserting "502(f)(2) of the Trade Act of 1974".

(6) Section 131 of the Uruguay Round Agreements Act (19 U.S.C. 3551) is amended in subsections (a) and (b)(1) by striking "502(a)(4)" and inserting "507(4)".

(b) OTHER LAWS.—

(1) Section 871(f)(2)(B) of the Internal Revenue Code of 1986 is amended by striking "within the meaning of section 502" and inserting "under title V".

(2) Section 2202(8) of the Export Enhancement Act of 1988 (15 U.S.C. 4711(8)) is amended by striking "502(a)(4)" and inserting "507(4)".

(3) Section 231A(a) of the Foreign Assistance Act of 1961 (22 U.S.C. 2191a(a)) is amended—

(A) in paragraph (1) by striking "502(a)(4) of the Trade Act of 1974 (19 U.S.C. 2462(a)(4))" and inserting "507(4) of the Trade Act of 1974";

(B) in paragraph (2) by striking "505(c) of the Trade Act of 1974 (19 U.S.C. 2465(c))" and inserting "504 of the Trade Act of 1974"; and

(C) in paragraph (4) by striking "502(a)(4)" and inserting "507(4)".

(4) Section 1621(a)(1) of the International Financial Institutions Act (22 U.S.C. 262p–4p(a)(1)) is amended by striking "502(a)(4)" and inserting "507(4)".

(5) Section 103B of the Agricultural Act of 1949 (7 U.S.C. 1444–2) is amended in subsections (a)(5)(F)(v) and (n)(1)(C) by striking "503(d) of the Trade Act of 1974 (19 U.S.C. 2463(d))" and inserting "503(b)(3) of the Trade Act of 1974".

And the Senate agree to the same.

TITLE II

That the House recede from its disagreement to the amendments of the Senate numbered 2 and 3 and agree to the same.

That the House recede from its disagreement to the amendment of the Senate numbered 4 and agree to the same with an amendment as follows:

On page 236, line 12 of the House engrossed bill, strike "Act" and insert "This section and sections 2102 and 2103"; and on page 237, line 4 of the House engrossed bill, strike "section 1" and insert "section 2102"; and the Senate agree to the same.

That the House recede from its disagreement to the amendment of the Senate numbered 5 and agree to the same with an amendment as follows:

On page 237, line 18 of the House engrossed bill, strike "June 30, 1996" and insert "September 30, 1996"; on line 19, strike "July 1, 1996" and insert "October 1, 1996"; beginning in line 20 strike "after the expiration of such year" and insert "beginning September 1, 1997"; and after line 21, insert the following:

(c) CONFORMING AMENDMENT.—Section 6 of such Act (29 U.S.C. 206) is amended by striking subsection (c).

And the Senate agree to the same.

That the House recede from its disagreement to the amendment of the Senate numbered 6 and agree to the same with an amendment as follows:

On page 239, line 1 of the House engrossed bill, strike "next to"; in line 3 of such page strike "to read as follows" and insert "by striking 'previous sentence' and inserting 'preceding 2 sentences' and by striking '(1)' and '(2)' and such section is amended by striking the next to last sentence and inserting the following"; and in line 15 of such page strike "cash"; and the Senate agree to the same.

From the Committee on Ways and Means, for consideration of the House bill (except for title II) and the Senate amendment numbered 1, and modifications committed to conference:

BILL ARCHER,
PHIL CRANE,
BILL THOMAS,
SAM GIBBONS,
CHARLES B. RANGEL,

As additional conferees from the Committee on Economic and Educational Opportunities, for consideration of secs. 1704(h)(1)(B) and 1704(l) of the House bill and secs. 1421(d), 1442(b), 1442(c), 1451, 1457, 1460(b), 1460(c), 1461, 1465, and 1704(h)(1)(B) of the Senate amendment numbered 1, and modifications committed to conference:

WILLIAM F. GOODLING,
CASS BALLENGER,

As additional conferees from the Committee on Economic and Educational Opportunities, for consideration of title II of the House bill and the Senate amendments numbered 2–6, and modifications committed to conference:

WILLIAM F. GOODLING,
H.W. FAWELL,
FRANK RIGGS,
WILLIAM L. CLAY,
MAJOR R. OWENS,
MAURICE HINCHEY,
Managers on the Part of the House.

From the Committee on Labor and Human Resources:
NANCY LANDON KASSEBAUM,
EDWARD M. KENNEDY,
JIM JEFFORDS,
From the Committee on Finance:
BILL ROTH,
JOHN H. CHAFEE,
CHUCK GRASSLEY,
ORIN G. HATCH,
AL SIMPSON,
LARRY PRESSLER,
DANIEL P. MOYNIHAN,
MAX BAUCUS,
DAVID PRYOR,
JOHN D. ROCKEFELLER IV,
Managers on the Part of the Senate.

JOINT EXPLANATORY STATEMENT OF THE COMMITTEE OF CONFERENCE

The managers on the part of the House and the Senate at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 3448) to provide tax relief for small businesses, to protect jobs, to create opportunities, to increase the take home pay of workers, to amend the Portal-to-Portal Act of 1947 relating to the payment of wages to employees who use employer owned vehicles, and to amend the Fair Labor Standards Act of 1938 to increase the minimum wage rate and to prevent job loss by providing flexibility to employers in complying with minimum wage and overtime requirements under that Act, submit the following joint statement to the House and the Senate in explanation of the effect of the action agreed upon by the managers and recommended in the accompanying conference report:

I. SMALL BUSINESS AND OTHER TAX PROVISIONS

A. Small Business Provisions

1. INCREASE IN EXPENSING FOR SMALL BUSINESSES

(Sec. 1111 of the House bill and the Senate amendment.)

Present law

In lieu of depreciation, a taxpayer with a sufficiently small amount of annual investment may elect to deduct up to $17,500 of the cost of qualifying property placed in service for the taxable year (sec. 179).[1] In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. The $17,500 amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable year exceeds $200,000. In addition, the amount eligible to be expensed for a taxable year may not exceed the taxable income of the taxpayer for the year that is derived from the active conduct of a trade or business (determined without regard to this provision). Any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding taxable years (subject to similar limitations).

House bill

The House bill increases the $17,500 amount allowed to be expensed under Code section 179 to $25,000. The increase is phased in as follows:

[1] The amount permitted to be expensed under Code section 179 is increased by up to an additional $20,000 for certain property placed in service by a business located in an empowerment zone (sec. 1397A).

Taxable year beginning in—	Maximum expensing
1996	$18,500
1997	19,000
1998	20,000
1999	21,000
2000	22,000
2001	23,000
2002	23,500
2003 and thereafter	25,000

Effective date.—The provision is effective for property placed in service in taxable years beginning after December 31, 1995, subject to the phase-in schedule set forth above.

Senate amendment[2]

The Senate amendment increases the $17,500 amount allowed to be expensed under Code section 179 to $25,000. The increase is phased in as follows:

Taxable year beginning in—	Maximum expensing
1997	$18,000
1998	18,500
1999	19,000
2000	20,000
2001	24,000
2002	24,000
2003 and thereafter	25,000

Effective date.—The provision is effective for property placed in service in taxable years beginning after December 31, 1996, subject to the phase-in schedule set forth above.

Conference agreement

The conference agreement follows the Senate amendment.

2. TAX CREDIT FOR SOCIAL SECURITY TAXES PAID WITH RESPECT TO EMPLOYEE CASH TIPS

(Sec. 1112 of the House bill and the Senate amendment.)

Present law

Employee tip income is treated as employer-provided wages for purposes of the Federal Insurance Contributions Act ("FICA"). Employees are required to report to the employer the amount of tips received. The Omnibus Budget Reconciliation Act of 1993 ("OBRA 1993") provided a business tax credit with respect to certain employer FICA taxes paid with respect to tips treated as paid by the employer. The credit applies to tips received from customers in connection with the provision of food or beverages for consumption on the premises of an establishment with respect to which the tipping of employees is customary. OBRA 1993 provided that the FICA tip credit is effective for taxes paid after December 31, 1993. Temporary Treasury regulations provide that the tax credit is available only with respect to tips reported by the employee. The temporary regulations also provide that the credit is effective for FICA taxes paid by an employer after December 31, 1993, with respect to tips received for services performed after December 31, 1993.

[2] See discussion in Part VII (Tax Technical Corrections Provisions) below, regarding the Senate amendment clarification of the present-law provision that horses are qualified property for purposes of section 179.

House bill

The provision clarifies the credit with respect to employer FICA taxes paid on tips by providing that the credit is (1) available whether or not the employee reported the tips on which the employer FICA taxes were paid pursuant to section 6053(a), and (2) effective with respect to taxes paid after December 31, 1993, regardless of when the services with respect to which the tips are received were performed.

The provision also modifies the credit so that it applies with respect to tips received from customers in connection with the delivery or serving of food or beverages, regardless of whether the food or beverages are for consumption on the premises of the establishment.

Effective date.—The clarifications relating to the effective date and nonreported tips are effective as if included in OBRA 1993. The provision expanding the tip credit to the provision of food or beverages not for consumption on the premises of the establishment is effective with respect to FICA taxes paid on tips received with respect to services performed after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

3. HOME OFFICE DEDUCTION: TREATMENT OF STORAGE OF PRODUCT SAMPLES

(Sec. 1113 of the House bill.)

Present law

A taxpayer's business use of his or her home may give rise to a deduction for the business portion of expenses related to operating the home (e.g., a portion of rent or depreciation and repairs). Code section 280A(c)(1) provides, however, that business deductions generally are allowed only with respect to a portion of a home that is used exclusively and regularly in one of the following ways: (1) as the principal place of business for a trade or business; (2) as a place of business used to meet with patients, clients, or customers in the normal course of the taxpayer's trade or business; or (3) in connection with the taxpayer's trade or business, if the portion so used constitutes a separate structure not attached to the dwelling unit. In the case of an employee, the Code further requires that the business use of the home must be for the convenience of the employer (sec. 280A(c)(1)). These rules apply to houses, apartments, condominiums, mobile homes, boats, and other similar property used as the taxpayer's home (sec. 280A(f)(1)).

Section 280A(c)(2) contains a special rule that allows a home office deduction for business expenses related to a space within a home that is used on a regular (even if not exclusive) basis as a storage unit for the inventory of the taxpayer's trade or business

of selling products at retail or wholesale, but only if the home is the sole fixed location of such trade or business.

Home office deductions may not be claimed if they create (or increase) a net loss from a business activity, although such deductions may be carried over to subsequent taxable years (sec. 280A(c)(5)).

House bill

The House bill clarifies that the special rule contained in present-law section 280A(c)(2) permits deductions for expenses related to a storage unit in a taxpayer's home regularly used for inventory or product samples (or both) of the taxpayer's trade or business of selling products at retail or wholesale, provided that the home is the sole fixed location of such trade or business.

Effective date—The provision applies to taxable years beginning after December 31, 1995.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill.

4. TREATMENT OF CERTAIN CHARITABLE RISK POOLS

(Sec. 1114 of the House bill.)

Present law

Organizations described in section 501(c)(3) (which are referred to as "charities") generally are exempt from Federal income tax and are eligible to receive tax-deductible contributions and to use the proceeds of tax-exempt financing. Section 501(c)(3) requires that an organization be organized and operated exclusively for a charitable or other specifically enumerated exempt purpose in order to qualify for tax-exempt status under that section.

Section 501(c)(3) requires that an organization that is organized and operated exclusively for charitable purposes is entitled to tax-exempt status under that section only if the organization satisfies the additional requirements that no part of its net earnings inures to the benefit of any private individual or shareholder (referred to as the "private inurement test") and only if the organization does not engage in political campaign activity on behalf of (or in opposition to) any candidate for public office and does not engage in substantial lobbying activities.

Section 501(m) provides that an organization described in section 501(c)(3) or 501(c)(4) of the Code is exempt from tax only if no substantial part of its activities consists of providing commercial-type insurance. For purposes of this rule, commercial-type insurance does not include insurance provided at substantially below cost to a class of charitable recipients.

Present law does not specifically accord tax-exempt status to an organization that pools insurable risks of a group of tax-exempt organizations described in section 501(c)(3).

House bill

Under the House bill, a qualified charitable risk pool is treated as organized and operated exclusively for charitable purposes. The provision make inapplicable to a qualified charitable risk pool the present-law rule under section 501(m) that a charitable organization described in section 501(c)(3) is exempt from tax only if no substantial part of its activities consists of providing commercial-type insurance.

The House bill defines a qualified charitable risk pool as an organization organized and operated solely to pool insurable risks of its members (other than medical malpractice risks) and to provide information to its members with respect to loss control and risk management. Because a qualified charitable risk pool must be organized and operated solely to pool insurable risks of its members and to provide information to members with respect to loss control and risk management, no profit may be accorded to any member of the organization other than through providing members with insurance coverage below the cost of comparable commercial coverage and through providing members with loss control and risk management information. Only charitable tax-exempt organizations described in section 501(c)(3) may be members of a qualified charitable risk pool.

The House bill further requires that a qualified risk pool is required to (1) be organized as a nonprofit organization under State law authorizing risk pooling for charitable organizations; (2) be exempt from State income tax; (3) obtain at least $1 million in start-up capital from nonmember charitable organizations; (4) be controlled by a board of directors elected by its members; and (5) provide in its organizational documents that members must be tax-exempt charitable organizations at all times, and if a member loses that status it must immediately notify the organization, and that no insurance coverage applies to a member after the date of any final determination that the member no longer qualifies as a tax-exempt charitable organization.

To be entitled to tax-exempt status under section 501(c)(3), a qualified charitable risk pool described in the provision also must satisfy the other requirements of that section (i.e., the private inurement test and the prohibition of political campaign activities and substantial lobbying).

Effective date.—The provision applies to taxable years beginning after the date of enactment.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill.

5. TREATMENT OF DUES PAID TO AGRICULTURAL OR HORTICULTURAL ORGANIZATIONS

(Sec. 1115 of the House bill and sec. 1113 of the Senate amendments.)

Present law

Tax-exempt organizations generally are subject to the unrelated business income tax ("UBIT") on income derived from a trade or business regularly carried on that is not substantially related to the performance of the organization's tax-exempt functions (secs. 511–514). Dues payments made to a membership organization generally are not subject to the UBIT. However, several courts have held that, with respect to postal labor organizations, dues payments were subject to the UBIT when received from individuals who were not postal workers, but who became "associate" members for the purpose of obtaining health insurance available to members of the organization. See *National League of Postmasters of the United States* v. *Commissioner,* No. 95–2646 (4th Cir. 1996), *American Postal Workers Union, AFL–CIO* v. *United States,* 925 F.2d 480 (D.C. Cir. 1991), *National Association of Postal Supervisors* v. *United States,* 944 F.2d 859 (Fed. Cir. 1991).

In Rev. Proc. 95–21 (issued March 23, 1995), the IRS set forth its position regarding when associate member dues payments received by an organization described in section 501(c)(5) will be treated as subject to the UBIT. The IRS stated that dues payments from associate members will not be treated as subject to UBIT unless, for the relevant period, "the associate member category has been formed or availed of for the principal purpose of producing unrelated business income." Thus, under Rev. Proc. 95–21, the focus of the inquiry is upon the organization's purposes in forming the associate member category (and whether the purposes of that category of membership are substantially related to the organization's exempt purposes other than through the production of income) rather than upon the motive of the individuals who join as associate members.

House bill

Under the House bill, if an agricultural or horticultural organization described in section 501(c)(5) requires annual dues not exceeding $100 to be paid in order to be a member of such organization, then in no event will any portion of such dues be subject to the UBIT by reason of any benefits or privileges to which members of such organization are entitled. For taxable years beginning after 1995, the $100 amount will be indexed for inflation. The term "dues" is defined as "any payment required to be made in order to be recognized by the organization as a member of the organization." Thus, if a person is recognized as a member of an organization by virtue of having paid annual dues for his or her membership, then any subsequent payments made by that person during the year to purchase another membership in the same organization (covering the same period) would not be within the scope of the provision.

Effective date.—The provision applies to taxable years beginning after December 31, 1994.

Senate amendment

Same as the House bill, except that the Senate amendment applies to taxable years beginning after December 31, 1986. The Senate amendment also provides transitional relief to agricultural or

horticultural organizations that had a reasonable basis for not treating membership dues received prior to January 1, 1987, as unrelated business income. In such cases, no portion of such dues will be treated as derived from an unrelated trade or business.

Conference agreement

The conference agreement follows the Senate amendment. The conferees intend that, if a person makes a single payment that entitles the person to be recognized as a member of the organization for more than twelve months, then such payment may be prorated to determine whether annual dues exceed the $100 cap (as adjusted for inflation).

6. CLARIFY EMPLOYMENT TAX STATUS OF CERTAIN FISHERMEN

(Sec. 1116(a) of the House bill and sec. 1114 of the Senate amendment.)

Present law

Under present law, service as a crew member on a fishing vessel is generally excluded from the definition of employment for purposes of income tax withholding on wages and for purposes of the Federal Insurance Contributions Act (FICA) and the Federal Unemployment Tax Act (FUTA) taxes if the operating crew of the boat normally consists of fewer than 10 individuals, the individual receives a share of the catch based on the total catch, and the individual does not receive cash remuneration other than proceeds from the sale of the individual's share of the catch. If a crew member receives any other cash, e.g., payment for services as an engineer, the exemption from FICA and FUTA taxes does not apply. Crew members to which the exemption applies are subject to self-employment taxes. Special reporting requirements apply to the operators of boats on which exempt crew members serve.

House bill

The operating crew of a boat is treated as normally made up of fewer than 10 individuals if the average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of fewer than 10 individuals. In addition, the exemption applies if the crew member receives certain cash payments. The cash payments cannot exceed $100 per trip, is contingent on a minimum catch, and is paid solely for additional duties (e.g., as mate, engineer, or cook) for which additional cash remuneration is customary.

Effective date.—The provision applies to remuneration paid after December 31, 1996. In addition, the provision applies to remuneration paid after December 31, 1984, and before January 1, 1997, unless the payor treated such remuneration when paid as subject to FICA taxes.

Senate amendment

The Senate amendment is the same as the House bill.

Effective date.—The provision applies to remuneration paid after December 31, 1994. In addition, the provision applies to remuneration paid after December 31, 1984, and before January 1,

1995, unless the payer treated such remuneration when paid as subject to FICA taxes.

Conference agreement

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

Effective date.—The conference agreement follows the Senate amendment.

7. REPORTING REQUIREMENTS FOR PURCHASERS OF FISH

(Sec. 1116(b) of the House bill.)

Present law

Under present law, a person engaged in a trade or business who makes payments during the calendar year of $600 or more to a person for "rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable gains, profits, or other income" must file an information return with the Internal Revenue Service reporting the amount of such payments, as well as the name, address, and taxpayer identification number of the person to whom such payments were made (Code sec. 6041). A similar statement must also be furnished to the person to whom such payments were made. Treasury regulations provide that payments for "merchandise" are not required to be reported under this provision (Treas. reg. sec. 1.6041–3(d)). Consequently, information reporting is generally not required with respect to purchases of fish or other forms of aquatic life. Information reporting is required by a person engaged in a trade or business who, in the course of that trade or business, receives more than $10,000 in cash in one transaction (or several related transactions) (Code sec. 6050I).

House bill

The provision requires persons engaged in the trade or business of purchasing fish for resale who pay more than $600 in cash in a calendar year for fish or other forms of aquatic life from any seller engaged in the trade or business of catching fish to file information reports with the Secretary regarding such purchases. A copy of the report must be provided to the seller.

Effective date.—The provision is effective for purchases made after December 31, 1996.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill.

Effective date.—The provision is effective for purchases made after December 31, 1997.

8. MODIFY RULES GOVERNING ISSUANCE OF TAX-EXEMPT BONDS FOR FIRST-TIME FARMERS

(Sec. 1115 of the Senate amendment.)

Present law

Interest on bonds issued by State and local governments to provide financing to private persons is taxable unless an exception is provided in the Internal Revenue Code. One such exception allows State and local governments to issue bonds to finance loans to first-time farmers for the acquisition of land (and limited amounts of related depreciable farm property) if the purchasers will be the principal user of the property and will materially participate in the farming operation in which the property is to be used.

A first-time farmer is defined as an individual who has at no time owned farm land in excess of 15 percent of the median size of the farm in the county in which such land is located, and the fair market value of the land has not at any time when held by the individual exceeded $125,000.

Under general rules governing issuance of tax-exempt bonds, working capital financing (including purchases from related parties) is precluded.

House bill

No provision.

Senate amendment

The Senate amendment makes two modifications to the rules governing issuance of tax-exempt bonds for first-time farmers. First, the definition of first-time farmer is broadened to include an individual who has at no time owned farm land in excess of 30 percent of the median size farm in the county. Second, these bonds may be used to finance purchases between related parties provided that: (1) the price paid reflects the fair market value of the property and, (2) the seller has no financial interest in the farming operation conducted on the land after the bond-financed sale occurs.

Effective date.—For financing provided with bonds issued after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment with a clarification relating to the circumstances in which a related seller is treated as having a continuing financial interest in bond-financed farmland. In general, the conferees intend that such a seller will not be treated as having a financial interest if the seller:

(a) has no more than a ten-percent interest in the capital or profits in a partnership comprising the farm;

(b) has no more than a ten-percent stock interest in a corporation comprising the farm;

(c) has no more than ten-percent of the beneficial interest in a trust comprising the farm;

(d) is not a principal user of the farm; or

(e) has no other direct or indirect ownership or use of the farm which has as a principal purposes, the avoidance of this provision.

The conferees further intend that issuers making loans to finance related party sales provide appropriate notice to borrowers of these restrictions and of the fact that bond-proceeds may not be

re-transferred from sellers to purchasers as part of efforts (e.g., step-transactions) to transfer both property financed with the bond proceeds and the bond proceeds received by the seller.

9. CLARIFY TREATMENT OF NEWSPAPER DISTRIBUTORS AND CARRIERS AS DIRECT SELLERS

(Sec. 1116 of the Senate amendment.)

Present law

For Federal tax purposes, there are two classifications of workers: a worker is either an employee of the service recipient or an independent contractor. Significant tax consequences result from the classification of a worker as an employee or independent contractor. These differences relate to withholding and employment tax requirements, as well as the ability to exclude certain types of compensation from income or take tax deductions for certain expenses. Some of these consequences favor employee status, while others favor independent contractor status. For example, an employee may exclude from gross income employer-provided benefits such as pension, health, and group-term life insurance benefits. On the other hand, an independent contractor can establish his or her own pension plan and deduct contributions to the plan. An independent contractor also has greater ability to deduct work-related expenses.

Under present law, the determination of whether a worker is an employee or an independent contractor is generally made under a common-law facts and circumstances test that seeks to determine whether the service provider is subject to the control of the service recipient, not only as to the nature of the work performed, but the circumstances under which it is performed. Under a special safe harbor rule (sec. 530 of the Revenue Act of 1978), a service recipient may treat a worker as an independent contractor for employment tax purposes even though the worker is an employee under the common-law test if the service recipient has a reasonable basis for treating the worker as an independent contractor and certain other requirements are met.

In addition to the common-law test, there are also some persons who are treated by statute as either employees or independent contractors. For example, "direct sellers" are deemed to be independent contractors. A direct seller is a person engaged in the trade or business of selling consumer products in the home or otherwise than in a permanent retail establishment, if substantially all the remuneration for the performance of the services is directly related to sales or other output rather than to the number of hours worked, and the services performed by the person are performed pursuant to a written contract between such person and the service recipient and such contract provides that the person will not be treated as an employee for Federal tax purposes.

The newspaper industry has generally taken the position that newspaper distributors and carriers should be treated as direct sellers for income and employment tax purposes. The Internal Revenue Service has generally taken the position that the direct seller rules do not apply to newspaper distributors and carriers operating

under an agency distribution system (i.e., where the publisher retains title to the newspapers).

House bill

No provision.

Senate amendment

The Senate amendment clarifies the treatment of qualifying newspaper distributors and carriers as direct sellers. Under the Senate amendment, a person engaged in the trade or business of the delivery or distribution of newspapers or shopping news (including any services that are directly related to such trade or business such as solicitation of customers of collection of receipts) qualifies as a direct seller, provided substantially all the remuneration for the performance of the services is directly related to sales or other output rather than to the number of hours worked, and the services performed by the person are performed pursuant to a written contract between such person and the service recipient and such contract provides that the person will not be treated as an employee for Federal tax purposes. The Senate amendment is intended to apply to newspaper distributors and carriers whether or not they hire others to assist in the delivery of newspapers. The Senate amendment also applies to newspaper distributors and carriers operating under either a buy-sell distribution system (i.e., where the newspaper distributors or carriers purchase the newspapers from the publisher) or an agency distribution system. For example, newspaper distributors and carriers operating under an agency distribution system who are paid based on the number of papers delivered and have an appropriate written agreement qualify as direct sellers. The status of newspaper distributors and carriers who do not qualify as direct sellers under the Senate amendment continue to be determined under present-law rules. No inference is intended with respect to the employment status of newspaper distributors and carriers prior to the effective date of the Senate amendment. Further, the provision is intended to clarify the worker classification issue for income and employment taxes only. The provision is not intended to have any impact whatsoever on the interpretation or applicability of Federal, State, or local labor laws.

Effective date.—The provision is effective with respect to services performed after December 31, 1995.

Conference agreement

The conference agreement follows the Senate amendment.

10. APPLICATION OF INVOLUNTARY CONVERSION RULES TO PROPERTY DAMAGED AS A RESULT OF PRESIDENTIALLY DECLARED DISASTERS

(Sec. 1117 of the Senate amendment.)

Present law

A taxpayer may elect not to recognize gain with respect to property that is involuntarily converted if the taxpayer acquires within an applicable period property similar or related in service or use. If the taxpayer does not replace the converted property with

property similar or related in service or use, then gain generally is recognized.

House bill

No provision.

Senate amendment

Any tangible property acquired and held for productive use in a business is treated as similar or related in service or use to property that (1) was held for investment or for productive use in a business and (2) was involuntarily converted as a result of a Presidentially declared disaster.

Effective date.—The Senate amendment is effective for disasters for which a Presidential declaration is made after December 31, 1994, in taxable years ending after that date.

Conference agreement

The conference agreement follows the Senate amendment, with the modification that the boundaries of the enterprise community for Oklahoma City designated by the Secretary of Housing and Urban Development on December 21, 1994, may be extended with respect to the census tracts located in the area damaged by the bombing of the Alfred P. Murrah Federal Building in Oklahoma City on April 19, 1995. The modification is effective on the date of enactment.

11. ESTABLISH 15-YEAR RECOVERY PERIOD FOR RETAIL MOTOR FUELS OUTLET STORES

(Sec. 1118 of the Senate amendment.)

Present law

Under present law, depreciation for property used in the retail gasoline trade is calculated under section 168 using a 15-year recovery period and the 150-percent declining balance method. Nonresidential real property is depreciated using a 39-year recovery period and the straight-line method. It is understood that taxpayers generally have taken the position that convenience stores and other buildings installed at retail motor fuels outlets have a 15-year recovery period. The IRS, in a position described in a recent Coordinated Issues Paper, generally limits the application of the 15-year recovery period to instances where the structure: (1) is 1,400 square feet or less or (2) meets a 50-percent test. The 50-percent test is met if: (1) 50 percent or more of the gross revenues that are generated from the building are derived from petroleum sales and (2) 50 percent or more of the floor space in the building is devoted to petroleum marketing sales.

House bill

No provision.

Senate amendment

The Senate amendment provides that 15-year property includes any section 1250 property (generally, depreciable real property) that is a retail motor fuels outlet (whether or not food or

other convenience items are sold at the outlet). A retail motor fuels outlet does not include any facility related to petroleum or natural gas trunk pipelines or to any section 1250 property used only to an insubstantial extent in the retail marketing of petroleum or petroleum products.

Effective date.—The provision is effective for property placed in service on or after the date of enactment and to which the amendments made by section 201 of the Tax Reform Act of 1986 apply (i.e., property subject to the modified Accelerated Cost Recovery System of sec. 168). The taxpayer may elect the application of the provision for property placed in service prior to the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

A taxpayer may elect the application of the provision for qualified property placed in service prior to the date of enactment. The conferees clarify that if a taxpayer has already treated qualified property that was placed in service before the date of enactment as 15-year property, the taxpayer will be deemed to have made the election with respect to such property.

12. TREATMENT OF LEASEHOLD IMPROVEMENTS

(Sec. 1119 of the Senate amendment.)

Present law

A taxpayer generally recovers the adjusted basis of property for purposes of determining gain or loss upon the disposition of the property. Upon the termination of a lease, the adjusted basis of leasehold improvements that were made, but are not retained, by a lessee are taken into account to compute gain or loss by the lessee. The proper treatment of the adjusted basis of improvements made by a lessor upon termination of a lease is less clear. It appears that it is the position of the Internal Revenue Service that leasehold improvements made by a lessor that constitute structural components of a building must be continued to be depreciated in the same manner as the underlying real property, even if such improvements are retired at the end of the lease term. Some lessors, on the other hand, may be taking the position that a leasehold improvement is a property separate and distinct from the underlying building and that an abandonment loss under section 165 is allowable at the end of the lease term for the adjusted basis of the property.

House bill

No provision.

Senate amendment

A lessor of leased property that disposes of a leasehold improvement which was made by the lessor for the lessee of the property may take the adjusted basis of the improvement into account for purposes of determining gain or loss, if the improvement is irrevocably disposed of or abandoned by the lessee at the termination of the lease.

Effective date.—The provision is effective for leasehold improvements disposed of after June 12, 1996. No inference is intended as to the proper treatment of such dispositions before June 13, 1996.

Conference agreement

The conference agreement follows the Senate amendment. The conferees wish to clarify that the provision does not apply to the extent section 280B of present law applies to the demolition of a structure, a portion of which may include leasehold improvements.

13. INCREASE DEDUCTIBILITY OF BUSINESS MEAL EXPENSES OF CERTAIN SEAFOOD PROCESSING FACILITIES

(Sec. 1120 of the Senate amendment.)

Present law

In general, 50 percent of meal and entertainment expenses incurred in connection with a trade or business that are ordinary and necessary (and not lavish or extravagant) are deductive (sec. 274). Food or beverage expenses are fully deductible provided that they are (1) required by Federal law to be provided to crew members of a commercial vessel, (2) provided to crew members of similar commercial vessels not operated on the oceans, or (3) provided on certain oil or gas platforms or drilling rigs.

House bill

No provision.

Senate amendment

The Senate amendment adds remote seafood processing facilities located in the United States north of 53 degrees north latitude to the present-law list of entities not subject to the 50 percent limitation on the deductibility of business meals. Consequently, these expenses are fully deductible. A seafood processing facility is remote when there are insufficient eating facilities in the vicinity of the employer's premises.[3]

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Conference agreement

The conference agreement does not include the Senate amendment provision.

14. PROVIDE A LOWER RATE OF TAX ON CERTAIN HARD CIDERS

(Sec. 1121 of the Senate amendment.)

Present law

Distilled spirits are taxed at a rate of $13.50 per proof gallon; beer is taxed at a rate of $18 per barrel (approximately 58 cents per gallon); and still wines of 14 percent alcohol or less are taxed at a rate of $1.07 per wine gallon. Higher rates of tax are applied to wines with great alcohol content and sparkling wines.

[3] See Treas. Reg. sec. 1.119–1(a)(2)(ii)(c) and 1.119–1(f) (Example 7).

Certain small wineries may claim a credit against the excise tax on wine of 90 cents per wine gallon on the first 100,000 gallons on wine produced annually. Certain small breweries pay a reduced tax of $7.00 per barrel (approximately 22.6 cents per gallon) on the first 60,000 barrels of beer produced annually.

Apple cider containing alcohol is classified and taxed as wine.

House bill

No provision.

Senate amendment

The Senate amendment adjusts the tax rate on apple cider having an alcohol content of no more than seven percent to 22.6 cents per gallon.

Effective date.—The provision is effective for apple cider removed after December 31, 1996.

Conference agreement

The conference agreement does not include the Senate amendment.

15. MODIFICATIONS TO SECTION 530 OF THE REVENUE ACT OF 1978

(Sec. 1122 of the Senate amendment.)

Present law

In general

For Federal tax purposes, there are two classifications of workers: a worker is either an employee of the service recipient or an independent contractor. In general, the determination of whether an employer-employee relationship exists for Federal tax purposes is made under a common-law test. Treasury regulations provide that an employer-employee relationship generally exists if the person contracting for services has the right to control not only the result of the services, but also the means by which that result is accomplished.[4]

Section 530

With increased enforcement of the employment tax laws beginning in the late 1960s, controversies developed between the IRS and taxpayers as to whether businesses had correctly classified certain workers as self employed rather than as employees. In response to this problem, the Congress enacted section 530 of the Revenue Act of 1978 ("section 530"). That provision generally allows a taxpayer to treat a worker as not being an employee for employment tax purposes (but not income tax purposes), regardless of the individual's actual status under the common-law test, unless the taxpayer has no reasonable basis for such treatment.

It is the position of the IRS, based on legislative history, that section 530 can only apply after a determination has been made

[4]The Internal Revenue Service ("IRS") has developed a list of 20 factors that may be examined in determining whether an employer-employee relationship exists. Rev. Rul. 87-41, 1987-1 C.B. 296.

that a worker is an employee under the common-law test.[5] The IRS does not require the taxpayer to concede or agree to a determination that the worker is an employee.[6] However, several courts that have explicitly considered the question have held that section 530 relief is available irrespective of whether there has been an initial determination of worker classification under the common law.[7]

Under section 530, a reasonable basis for treating a worker as an independent contractor is considered to exist if the taxpayer (1) reasonably relied on published rulings or judicial precedent, (2) reasonably relied on past IRS audit practice with respect to the taxpayer, (3) reasonably relief on long-standing recognized practice of a significant segment of the industry of which the taxpayer is a member, or (4) has any other reasonable basis for treating a worker as an independent contractor. The legislative history states that section 530 is to be "construed liberally in favor of taxpayers."[8]

Under section 530, reliance on judicial precedent, published rulings, technical advice with respect to the taxpayer, or a letter ruling to the taxpayer is deemed a reasonable basis for treating a worker as an independent contractor. If a taxpayer relies on this safe harbor, the IRS will look to see whether the facts of the judicial precedent or published ruling are sufficiently similar to the taxpayer's facts.[9]

Under the prior-audit safe harbor, reasonable reliance is generally found to exist if the IRS failed to raise an employment tax issue on audit, even though the audit was not related to employment tax matters. A taxpayer can also rely on a prior audit in which an employment tax issue was raised, but was resolved in favor of the taxpayer. According to the IRS, an "audit" must involve an examination of the taxpayer's books and records; mere inquiries from an IRS service center or a "compliance check" to determine whether a taxpayer has filed all returns will not suffice.[10] In order to rely on a prior audit, the IRS requires that the taxpayer must have treated the workers at issue as independent contractors during the period covered by the prior audit.[11]

A taxpayer is also treated as having a reasonable basis for treating a worker as an independent contractor under section 530 if the taxpayer reasonably relied on long-standing recognized practice of a significant segment of the industry in which the taxpayer is engaged.

Section 530 does not specify a period of time in order for a practice to be long standing. The IRS Training Guide provides that

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[5] Employee or Independent Contractor?, at 3–4 (July 15, 1996) (hereinafter the "IRS Training Guide").

[6] IRS Training Guide, at 3–6; TAM 9443002 (December 3, 1993).

[7] See e.g., *Lambert's Nursery and Landscaping, Inc.* v. *U.S.*, 894 F.2d 154 (5th Cir. 1990) ("It is not necessary to determine whether [taxpayer's] workers were independent contractors or employees for employment tax purposes.") *J & J Cab Service, Inc.* v. *U.S.*, 75 AFTR2d No. 95–618 (W.D. N.C. 1995) ("Section 530 relief may be granted irrespective of whether individuals were incorrectly treated as other than employees"); *Queensgate Dental Family Practice, Inc.* v. *U.S.*, 91–2 USTC No. 50,536 (M.D. Pa. 1991) (disagreeing with the IRS' contention that the court must first determine worker classification before applying section 530).

[8] H. Rept. No. 1748 (95th Cong., 2d Sess., 5 (1978)). The conference agreement to the Revenue Act of 1978 adopted the provisions of the House bill and therefore incorporates this legislative history.

[9] See e.g., TAM 9443002 (December 3, 1993); TAM 9330007 (April 28, 1993).

[10] IRS Training Guide, at 3–19.

[11] IRS Training Guide, at 3–20.

a practice is presumed to be long standing if it existed for 10 years or more.[12] the IRS Training Guide recognizes that a taxpayer may use the industry practice safe harbor even if it began business after 1978 or the industry came into existence after 1978.[13] However, the IRS Training Guide provides that if the industry practice changed by the time the taxpayer joined the industry, the taxpayer cannot rely on the former practice.

Neither section 530, nor the legislative history, provides a clear standard as to what constitutes a significant segment of a taxpayer's industry. The IRS Training Guide provides that the determination will be based on the facts and circumstances.[14] A few courts have addressed this issue. In one case, the IRS argued that a significant segment of the industry means more than 50 percent of the industry.[15] However, that court held that a significant segment is less than a majority of the firms in an industry. Another court held that 15 out of 84 industry respondents (18 percent) treating workers as independent contractors would constitute a significant segment of an industry.[16]

Even if a taxpayer is unable to rely on one of the three safe harbors described above, a taxpayer may still be entitled to relief under section 530 if the taxpayer has any other reasonable basis for treating a worker as an independent contractor.

The relief under section 530 is available with respect to an individual only if certain additional requirements are satisfied. The taxpayer must not have treated the individual as an employee for any period, and for periods since 1978 all Federal tax returns, including information returns, must have been filed on a basis consistent with treating such individual as an independent contractor. Further, the taxpayer (or a predecessor) must not have treated any individual holding a substantially similar position as an employee for purposes of employment taxes for any period beginning after 1977.

Whether workers are similarly situated is dependent on the facts and circumstances. The IRS Training Guide states that a "substantially similar position exists if the job functions, duties, and responsibilities are substantially similar and the control and supervision of those duties and responsibilities is substantially similar."[17]

There have been a few court decisions addressing this issue. For example, in *REAG, Inc.* v. *U.S.*,[18] the court held that the position of appraisers who were owner-officers of the business was not substantially similar to appraisers who were not owners since the owner-officers had managerial responsibilities. By contrast, in *Lowen Corp.* v. *U.S.*,[19] the court found that all workers engaged in the business of selling real estate signs had substantially similar positions even though some were salaried and had to file daily re-

[12] IRS Training Guide, at 3–24.
[13] IRS Training Guide, at 3–24.
[14] IRS Training Guide, at 3–25.
[15] In re Bentley, 73 AFTR2d No. 94–667 (Bkrtcy. E.D. Tenn. 1994).
[16] *REAG, Inc.* v. *U.S.*, 801 F.Supp. 494 (W.D. Okla. 1992).
[17] IRS Training Guide, at 3–11.
[18] 801 F.Supp. 494 (W.D. Okla. 1992).
[19] 785 F.Supp. 913 (D. Kan. 1992).

ports while others were paid by commission and did not have to file such reports.

The IRS Training Guide states that the burden of proof is on the taxpayer to demonstrate that it had a reasonable basis for treating a worker as an independent contractor.[20] However, in light of the Congressional instruction in the legislative history to construe section 530 liberally,[21] courts appear to be split as to how stringent a burden to apply.

In *McClellan* v. *U.S.*,[22] the court held that section 530 requires the "taxpayer to come forward with an explanation and enough evidence to establish prima facie grounds for a finding of reasonableness. . . . [T]his threshold burden is relatively low, and can be met with any reasonableness showing. Once the taxpayer has made this prima facie showing, the burden then shifts to the IRS to verify or refute the taxpayer's explanation." By contrast, in *Boles Trucking, Inc.,* v. *U.S.*,[23] the court held that the burden is on the taxpayer to show, based on a preponderance of the evidence, that it had a reasonable basis for treating workers as independent contractors.

Under section 1706 of the Tax Reform Act of 1986, section 530 does not apply in the case of an individual who, pursuant to an arrangement between the taxpayer and another person, provides services for such other person as an engineer; designer, drafter, computer programmer, systems analyst, or other similarly skilled worker engaged in a similar line of work. Thus, the determination of whether such individuals are employees or self employed is made in accordance with the common-law test.

House bill

No provision.

Senate amendment

The Senate amendment makes several clarifications of and modifications to section 530.

First, under the Senate amendment, a worker does not have to otherwise be an employee of the taxpayer in order for section 530 to apply. The provision is intended to reverse the IRS position, as stated in the IRS Training Guide, that there first must be a determination that the worker is an employee under the common law standards before application of section 530.

The Senate amendment modifies the prior audit safe harbor so that taxpayers may not rely on an audit commencing after December 31, 1996, unless such audit included an examination for employment tax purposes of whether the worker involved (or any worker holding a position substantially similar to the position held by the worker involved) should be treated as an employee of the

[20] IRS Training Guide, at 3–6.

[21] H. Rept. No. 1748 (95th Cong., 2d Sess., 5 (1978)). The conference agreement to the Revenue Act of 1978 adopted the provisions of the House bill and therefore incorporates this legislative history.

[22] 900 F.Supp. 101 (E.D. Mich. 1995). See also *REAG. Inc.* v. *U.S.*, 801 F.Supp. 494 (W.D. Okla. 1992) (a taxpayer need only show a substantial rational basis for its decision to treat the workers as independent contractors).

[23] 77 F.3d 236 (8th Cir. 1996) See also *Springfield* v. *U.S.*, 1996 U.S. App. LEXIS 15879 (9th Cir. 1996) (taxpayer has the burden to show it satisfies the requirements of section 530 by a preponderance of the evidence).

taxpayer. The provision does not affect the ability of taxpayers to rely on prior audits that commenced before January 1, 1997, even though the audit was not related to employment tax matters, as under present law.

Under the Senate amendment, section 530 does not apply with respect to a worker unless the taxpayer and the worker sign a statement (at such time and in such manner as the Secretary may prescribe) which provides that the worker will not be treated as an employee for employment tax purposes. Also, the Senate amendment provides that an officer or employee of the IRS must, at (or before) the commencement of an audit involving worker classification issues, provide the taxpayer with written notice of the provisions of section 530.

The Senate amendment makes a number of changes to the industry practice safe harbor. First, the Senate amendment provides that a significant segment of the taxpayer's industry under the industry practice safe harbor does not require a reasonable showing of the practice of more than 25 percent of an industry (determined without taking into account the taxpayer). The provision is intended to be a safe harbor; a lower percentage may constitute a significant segment of the taxpayer's industry based on the particular facts and circumstances.

The Senate amendment also provides that an industry practice need not have continued for more than 10 years in order for the industry practice to be considered long standing. As with the significant segment safe harbor, this provision is intended to be a safe harbor; an industry practice in existence for a shorter period of time may be considered long standing based on the particular facts and circumstances. In addition, the Senate amendment clarifies that an industry practice will not fail to be treated as long standing merely because such practice began after 1978. Consequently, the provision clarifies that new industries can take advantage of section 530.

The Senate amendment modifies the burden of proof in section 530 cases by providing that if a taxpayer establishes a prima facie case that it was reasonable not to treat a worker as an employee for purposes of section 530,[24] the burden of proof shifts to the IRS with respect to such treatment.[25] In order for the shift in burden of proof to occur, the taxpayer must fully cooperate with reasonable requests by the IRS for information relevant to the taxpayer's treatment of the worker as an independent contractor under section 530. It is intended that a request by the IRS will not be treated as reasonable if complying with the request would be impracticable given the particular circumstances and the relative costs involved. The shift in the burden of proof does not apply for purposes of determining whether the taxpayer had any other reasonable basis for treating the worker as an independent contractor, but does apply to all other aspects of section 530. So, for example, pro-

[24] For example, the taxpayer must establish a prima facie case that it reasonably satisfies the requirements of section 530 for not treating the worker as an employee, including the reporting consistency and consistency among workers with substantially similar positions requirements, and the requirement that the taxpayer have a reasonable basis for not treating the worker as an employee.

[25] The provision is generally intended to codify the holding in *McClellan* v. *U.S.*, discussed above, with respect to the burden of proof in section 530 cases.

vided the taxpayer establishes its prima facie case and fully cooperates with the IRS' reasonable requests, the burden of proof shifts to the IRS with respect to all other aspects of section 530, including whether the taxpayer had a reasonable basis for treating the worker as an independent contractor under the judicial or administrative precedent, prior audit, or long-standing industry practice safe harbors, whether the taxpayer filed all Federal tax returns on a basis consistent with treating the worker as an independent contractor, and whether the taxpayer treated any worker holding a substantially similar position as an employee. No inference is intended with respect to the application of the burden of proof in section 530 cases prior to the effective date of this provision.

The Senate amendment also provides that if a taxpayer prospectively changes its treatment of workers from independent contractors to employees for employment tax purposes, such a change will not affect the applicability of section 530 with respect to such workers for prior periods.

Finally, the Senate amendment provides that, in determining whether a worker holds a substantially similar position to another worker, the relationship of the parties must be one of the factors taken into account.

Effective date.—The provisions generally apply to periods after December 31, 1996. The provision regarding the burden of proof applies to disputes with respect to periods after December 31, 1996. In the case of workers engaged to perform services for a taxpayer before January 1, 1997, the provision requiring a written statement that such workers are not employees for employment tax purposes is effective for periods after December 31, 1997 (unless the taxpayer elects to apply the provision earlier). The provision requiring the IRS to notify taxpayers of the provisions of section 530 applies to audits commencing after December 31, 1996.

Conference agreement

The conference agreement follows the Senate amendment, with the following modifications:

The conference agreement deletes the written statement requirement in the Senate amendment.

The conferees wish to clarify the notice that the IRS must provide to taxpayers at (or before) the commencement of an audit inquiry involving worker classification issues. The conferees recognize that, in many cases, the portion of an audit involving worker classification issues will not arise until after the examination of the taxpayer begins. In that case, the notice need only be given at the time the worker classification issue is first raised with the taxpayer.

With respect to the burden of proof in section 530 cases, the conferees intend that a request for information by the IRS will not be treated as reasonable if (1) it does not relate to the particular basis on which the taxpayer relied for establishing its reasonable basis, or (2) complying with the request would be impracticable given the particular circumstances and the relative costs involved.

With respect to the substantially similar position provision, the conferees clarify that consideration of the relationship between a

taxpayer and a worker includes consideration of the degree of supervision and control of the worker by the taxpayer.

16. EMPLOYEE HOUSING FOR CERTAIN MEDICAL RESEARCH INSTITUTIONS

(Sec. 1123 of the Senate amendment.)

Present law

Under Code section 119(d), employees of an educational institution described in Code section 170(b)(1)(A)(ii) do not have to include in income the fair market value of campus housing as long as the rent is at least five percent of the appraised value of the housing. If the rent is less than the five-percent safe harbor, there is inclusion into income to the extent that the rent that was charged falls short of the lesser of five percent of the appraised value or the average of rents paid by individuals (other than employees or students of the educational institution) for similar lodging provided by the institution.

House bill

No provision.

Senate amendment

The Senate amendment treats as "educational institutions" for purposes of Code section 119(d) certain medical research institutions ("academic health centers") that engage in basic and clinical research, have a regular faculty and teach a curriculum in basic and clinical research to students in attendance at the institution.

Effective date.—The provision is effective for taxable years beginning after December 31, 1995.

Conference agreement

The conference agreement follows the Senate amendment, with a further modification that treats as "educational institutions" for purposes of Code section 119(d) certain entities ("university systems") organized under State law composed of public institutions described in Code section 170(b)(1)(A)(ii). The conferees intend that, for purposes of the present-law requirement of Code section 119(d)(3)(A) that the employee housing be provided on (or in the proximity of) a campus of the employer, a campus of one of the component educational institutions of a university system should be considered to be a campus of the university system.

B. Extension of Certain Expiring Provisions

1. WORK OPPORTUNITY TAX CREDIT

(Sec. 1201 of House bill and the Senate amendment.)

Present law

Prior to January 1, 1995, the targeted jobs tax credit was available on an elective basis for employers hiring individuals from one or more of nine targeted groups. The credit generally was equal to 40 percent of qualified first-year wages (up to $6,000) for maximum credit of $2,400.

House bill

General rules.—The House bill replaces the targeted jobs tax credit with the "work opportunity tax credit". The new credit is available on an elective basis for employers hiring individuals from one or more of seven targeted groups. The credit generally is equal to 35 percent of qualified first-year wages.

Minimum employment period.—Under the House bill, no credit is allowed for wages paid unless the eligible individual is employed by the employer for at least 180 days (20 days in the case of a qualified summer youth employee) or 500 hours (120 hours in the case of a qualified summer youth employee).

Certification of members of targeted groups.—In general, under the House bill, an individual is not treated as a member of a targeted group unless: (1) on or before the day the individual begins work for the employer, the employer received in writing a certification from the designated local agency that the individual is a member of a specific targeted group, or (2) on or before the day the individual is offered work with the employer, a pre-screening notice is completed with respect to that individual by the employer and within 14 days after the individual begins work for the employer, the employer submits such notice, signed by the employer and the individual under penalties of perjury, to the designated local agency as part of a written request for certification. The pre-screening notice will contain the information provided to the employer by the individual that forms the basis of the employer's belief that the individual is a member of a targeted group.

Effective date.—Wages paid or incurred to a qualified individual who begins work for an employer after June 30, 1996, and before July 1, 1997.

Senate amendment

General rules.—Same as the House bill with the addition of an eighth targeted group, individuals 18 to 24 who are in families that have been receiving food stamps for at least a three-month period ending on the date of hire.

Minimum employment period.—Under the Senate amendment, no credit is allowed for wages paid unless the eligible individual is employed by the employer for at least 180 days (20 in the case of a qualified summer youth employee) or 375 hours (120 hours in the case of a qualified summer youth employee).

Certification of members of targeted groups.—Same as House bill except that it replaces the 14-day rule with a 21-day rule for submission of pre-screening notice.

Effective date.—Wages paid or incurred to a qualified individual who begins work for an employer after September 30, 1996, and before October 1, 1997.

Conference agreement

General rules.—The conference agreement generally follows the Senate amendment with one modification to the food stamps category. Under the modification, members of the eighth targeted group are individuals aged 18–24 who are in families that have been receiving food stamps for at least a six-month (rather than a three-month) period ending on the date of hire. In the case of fami-

lies that cease to be eligible for food stamps under section 6(o) of the Food Stamp Act of 1977, the six-month requirement is replaced with a requirement that the family has been receiving food stamps for at least three of the five months ending on the date of hire.

Minimum employment period.—Under the conference agreement, no credit is allowed for wages paid unless the eligible individual is employed by the employer for at least 180 days (20 in the case of a qualified summer youth employee) or 400 hours (120 hours in the case of a qualified summer youth employee).

Certification of members of targeted groups.—The conference agreement follows the Senate amendment.

Effective date.—The conference agreement follows the Senate amendment.

2. EMPLOYER-PROVIDED EDUCATIONAL ASSISTANCE

(Sec. 1202 of the House bill and the Senate amendment.)

Present and prior law

For taxable years beginning before January 1, 1995, an employee's gross income and wages did not include amounts paid or incurred by the employer for educational assistance provided to the employee if such amounts were paid or incurred pursuant to an educational assistance program that met certain requirements. This exclusion, which expired for taxable years beginning after December 31, 1994, was limited to $5,250 of educational assistance with respect to an individual during a calendar year. The exclusion applied whether or not the education was job related. In the absence of this exclusion, educational assistance is excludable from income only if it is related to the employee's current job.

House bill

The provision extends the exclusion for employer-provided educational assistance for taxable years beginning after December 31, 1994, and before January 1, 1997. After December 31, 1995, the exclusion would not apply with respect to graduate education.

To the extent employers have previously filed Forms W–2 reporting the amount of educational assistance provided as taxable wages, present Treasury regulations require the employer to file Forms W–2c (i.e., corrected Forms W–2) with the Internal Revenue Service.[26] It is intended that employers also be required to provide copies of Form W–2c to affected employees.

The Secretary is directed to establish expedited procedures for the refund of any overpayment of taxes paid on excludable educational assistance provided in 1995 and 1996, including procedures for waiving the requirement that an employer obtain an employee's signature if the employer demonstrates to the satisfaction of the Secretary that any refund collected by the employer on behalf of the employee will be paid to the employee.

Because the exclusion is extended, no interest and penalties should be imposed if an employer failed to withhold income and employment taxes on excludable educational assistance or failed to report such educational assistance. Further, it is intended that the

[26] Treasury regulation section 31.6051–1(c).

Secretary establish expedited procedures for refunding any interest and penalties relating to educational assistance previously paid.

Effective date.—The provision is effective with respect to taxable years beginning after December 31, 1994, and before January 1, 1997.

Senate amendment

The provision is the same as the House bill, except that the exclusion is extended for an additional year, through December 31, 1997, and the Senate amendment does not preclude application of the exclusion to graduate courses.

Effective date.—The provision is effective for taxable years beginning after December 31, 1994, and before January 1, 1998.

Conference agreement

The conference agreement follows the House bill, with the following modifications. The exclusion expires with respect to courses beginning after May 31, 1997. The exclusion for graduate courses applies in 1995. In 1996, the exclusion for graduate courses does not apply to courses beginning after June 30, 1996.

3. PERMANENT EXTENSION OF FUTA EXEMPTION FOR ALIEN AGRICULTURAL WORKERS

(Sec. 1203 of the House bill.)

Present law

Generally, the Federal unemployment tax ("FUTA") is imposed on farm operators who (1) employ 10 or more agricultural workers for some portion of 20 different days, each beginning in a different calendar week or (2) have a quarterly payroll for agricultural services of at least $20,000. An exclusion from FUTA was provided, however, for labor performed by an alien admitted to the United States to perform agricultural labor under section 214(c) and 101(a)(15)(H) of the Immigration and Nationality Act. This exclusion was effective for labor performed before January 1, 1995.

House bill

The House bill permanently extends the FUTA exemption for alien agricultural workers.

Effective date.—Labor performed on or after January 1, 1995.

Senate amendment

No provision.

Conference agreement

The conference agreement includes the House bill provision.

4. RESEARCH AND EXPERIMENTAL TAX CREDIT

(Sec. 1203 of the Senate amendment.)

Present and prior law

General rule

Prior to July 1, 1995, section 41 of the Internal Revenue Code provided for a research tax credit equal to 20 percent of the amount by which a taxpayer's qualified research expenditures for a taxable year exceeded its base amount for that year. The research tax credit expired and does not apply to amounts paid or incurred after June 30, 1995.

A 20-percent research tax credit also applied to the excess of (1) 100 percent of corporate cash expenditures (including grants or contributions) paid for basic research conducted by universities (and certain nonprofit scientific research organizations) over (2) the sum of (a) the greater of two minimum basic research floors plus (b) an amount reflecting any decrease in nonresearch giving to universities by the corporation as compared to such giving during a fixed-base period, as adjusted for inflation. This separate credit computation is commonly referred to as the "university basic research credit" (see sec. 41(e)).

Computation of allowable credit

Except for certain university basic research payments made by corporations, the research tax credit applies only to the extent that the taxpayers' qualified research expenditures for the current taxable year exceed its base amount. The base amount for the current year generally is computed by multiplying the taxpayer's "fixed-base percentage" by the average amount of the taxpayer's gross receipts for the four preceding years. If a taxpayer both incurred qualified research expenditures and had gross receipts during each of at least three years from 1984 through 1988, then its "fixed-base percentage" is the ratio that its total qualified research expenditures for the 1984–1988 period bears to its total gross receipts for that period (subject to a maximum ratio of .16). All other taxpayers (so-called "start-up firms") are assigned a fixed-base percentage of 3 percent.[27]

In computing the credit, a taxpayer's base amount may not be less than 50 percent of its current-year qualified research expenditures.

To prevent artificial increases in research expenditures among commonly controlled or otherwise related entities, research expenditures and gross receipts of the taxpayer are aggregated with research expenditures and gross receipts of certain related persons for purposes of computing any allowable credit (sec. 41(f)(1)). Special rules apply for computing the credit when a major portion of

[27] The Omnibus Budget Reconciliation Act of 1993 included a special rule designed to gradually recompute a start-up firm's fixed-base percentage based on its actual research experience. Under this special rule, a start-up firm (i.e., any taxpayer that did not have gross receipts in at least three years during the 1984–1988 period) will be assigned a fixed-base percentage of 3 percent for each of its first five taxable years after 1993 in which it incurs qualified research expenditures. In the event that the research credit is extended beyond the scheduled June 30, 1995 expiration date, a start-up firm's fixed-base percentage for its sixth through tenth taxable years after 1993 in which it incurs qualified research expenditures will be a phased-in ratio based on its actual research experience. For all subsequent taxable years, the taxpayer's fixed-base percentage will be its actual ratio of qualified research expenditures to gross receipts for any five years selected by the taxpayer from its fifth through tenth taxable years after 1993 (sec. 41(c)(3)(B)).

a business changes hands, under which qualified research expenditures and gross receipts for periods prior to the change or ownership of a trade or business are treated as transferred with the trade or business that gave rise to those expenditures and receipts for purposes of recomputing a taxpayer's fixed-base percentage (sec. 41(f)(3)).

Eligible expenditures

Qualified research expenditures eligible for the research tax credit consist of (1) "in-house" expenses of the taxpayer for wages and supplies attributable to qualified research; (2) certain time-sharing costs for computer use in qualified research; and (3) 65 percent of amounts paid by the taxpayer for qualified research conducted on the taxpayer's behalf (so-called "contract research expenses").

To be eligible for the credit, the research must not only satisfy the requirements of present-law section 174 but must be undertaken for the purpose of discovering information that is technological in nature, the application of which is intended to be useful in the development of a new or improved business component of the taxpayer, and must pertain to functional aspects, performance, reliability, or quality of a business component. Research does not qualify for the credit if substantially all of the activities relate to style, taste, cosmetic, or seasonal design factors (sec. 41(d)(3)). In addition, research does not qualify for the credit if conducted after the beginning of commercial production of the business component, if related to the adaptation of an existing business component to a particular customer's requirements, if related to the duplication of an existing business component from a physical examination of the component itself or certain other information, or if related to certain efficiency surveys, market research or development, or routine quality control (sec. 41(d)(4)).

Expenditures attributable to research that is conducted outside the United States do not enter into the credit computation. In addition, the credit is not available for research in the social sciences, arts, or humanities, nor is it available for research to the extent funded by any grant, contract, or otherwise by another person (or governmental entity).

House bill

No provision.

Senate amendment

The Senate amendment extends the research tax credit for 18 months—i.e., for the period July 1, 1996, through December 31, 1997 (with a special rule for taxpayers who elect the alternative incremental research credit regime, as described below).

The Senate amendment also expand the definition of "start-up firms" under section 41(c)(3)(B)(I) to include any firm if the first taxable year in which such firm had both gross receipts and qualified research expenses began after 1983.[28]

[28] In applying the start-up firm rules, the test is whether a taxpayer, in fact, both incurred research expenses (which under the present-law rules would be qualified research expenses) and

In addition, the Senate amendment allows taxpayers to elect an alternative incremental research credit regime. If a taxpayer elects to be subject to this alternative regime, the taxpayer is assigned a three-tiered fixed-base percentage (that is lower than the fixed-base percentage otherwise applicable under present law) and the credit rate likewise is reduced. Under the alternative credit regime, a credit rate of 1.65 percent applies to the extent that a taxpayer's current-year research expenses exceed a base amount computed by using a fixed-base percentage of 1 percent (i.e., the base amount equals 1 percent of the taxpayer's average gross receipts for the four preceding years) but do not exceed a base amount computed by using a fixed-base percentage of 1.5 percent. A credit rate of 2.2 percent applies to the extent that a taxpayer's current-year research expenses exceed a base amount computed by using a fix-base percentage of 1.5 percent but do not exceed a base amount computed by using a fixed-base percentage of 2 percent. A credit rate of 2.75 percent applies to the extent that a taxpayer's current-year research expenses exceed a base amount computed by using a fixed-base percentage of 2 percent. An election to be subject to this alternative incremental credit regime may be made only for a taxpayer's first taxable year beginning after June 30, 1996, and such an election applies to that taxable year and all subsequent years unless revoked with the consent of the Secretary of the Treasury. Under the amendment, if a taxpayer elects the alternative incremental credit regime for its first taxable year beginning after June 30, 1996, and before July 1, 1997, then all qualified research expenses paid or incurred during such taxable year and the first six months of the following taxable year are treated as qualified research expenses for purposes of computing the taxpayer's credit under the alternative incremental credit regime.

The Senate amendment also provide for a special rule for payments made to certain nonprofit research consortia. Under this special rule, 75 percent of amounts paid to a research consortium for qualified research is treated as qualified research expenses eligible for the research credit (rather than 65 percent under the present-law section 41(b)(3) rule governing contract research expenses) if (1) such research consortium is a tax-exempt organization that is described in section 501(c)(3) (other than a private foundation) or section 501(c)(6) and is organized and operated primarily to conduct scientific research, and (2) such qualified research is conducted by the consortium on behalf of the taxpayer and one or more persons not related to the taxpayer.

Effective date.—Under the Senate amendment, extension of the research tax credit is effective for expenditures paid or incurred during the period July 1, 1996, through December 31, 1997 (with a special rule for taxpayers who elect the alternative incremental research credit regime). The modification to the definition of "start-up firms" is effective for taxable years ending after June 30, 1996. Taxpayers may elect the alternative research credit regime (with lower fixed-base percentages and lower credit rates) for the first taxable year beginning after June 30, 1996, and before July 1,

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had gross receipts in a particular year, not whether the taxpayer claimed a research tax credit for that year.

1997, and the credit is available with respect to all qualified research expenses incurred during such taxable year and during the first six months of the following taxable year. The rule that treats 75 percent of qualified research consortium payments as qualified research expenses is effective for taxable years beginning after June 30, 1996.

Conference agreement

The conference agreement extends the research tax credit for 11 months—i.e., for the period July 1, 1996, through May 31, 1997 (with a special rule for taxpayers who elect the alternative incremental research credit regime, as described below).

The conference agreement includes the provision in the Senate amendment to expand the definition of "start-up firms" under section 41(c)(3)(B)(I).

The conference agreement includes the provision in the Senate amendment to allow taxpayers to elect an alternative incremental research credit regime, with the modification that, if a taxpayer elects the alternative incremental credit regime for its first taxable year beginning after June 30, 1996, and before July 1, 1997, then all qualified research expenses paid or incurred during the first 11 months of such taxable year are treated as qualified research expenses for purposes of computing the taxpayers's credit under the alternative incremental credit regime.

The conference agreement includes the special rule of the Senate amendment that treats 75 percent (rather than 65 percent) of payments made to certain nonprofit research consortia as qualified research expenses.

In addition, the conference agreement provides that research credit amounts earned under the conference agreement may not be taken into account in computing estimated tax payments required to be paid for taxable years beginning in 1997.

Effective date.—Under the conference agreement, extension of the research tax credit is effective for expenditures paid or incurred during the period July 1, 1996, through May 31, 1997 (with a special rule for taxpayers who elect the alternative incremental research credit regime). The modification to the definition of "start-up firms" is effective for taxable years ending after June 30, 1996. Taxpayers may elect the alternative research credit regime (with lower fixed-base percentages and lower credit rates) for the first taxable year beginning after June 30, 1996, and before July 1, 1997, and the credit is available with respect to all qualified research expenses incurred during the first 11 months of such taxable year. The rule that treats 75 percent of qualified research consortium payments as qualified research expenses is effective for taxable years beginning after June 30, 1996.

5. ORPHAN DRUG TAX CREDIT

(Sec. 1204 of the Senate amendment.)

Present and prior law

Prior to January 1, 1995, a 50-percent nonrefundable tax credit was allowed for qualified clinical testing expenses incurred in testing of certain drugs for rare diseases or conditions, generally re-

ferred to as "orphan drugs." Qualified testing expenses are costs incurred to test an orphan drug after the drug has been approved for human testing by the Food and Drug Administration (FDA) but before the drug has been approved for sale by the FDA. A rare disease or condition is defined as one that (1) affects less than 200,000 persons in the United States, or (2) affects more than 200,000 persons, but for which there is no reasonable expectation that businesses could recoup the costs of developing a drug for such disease or condition from U.S. sales of the drug. These rare diseases and conditions include Huntington's disease, myoclonus, ALS (Lou Gehrig's disease), Tourette's syndrome, and Duchenne's dystrophy (a form of muscular dystrophy).

Under prior law, the orphan drug tax credit could be claimed by a taxpayer only to the extent that its regular tax liability for the year the credit was earned exceeded its tentative minimum tax for the year, after regular tax was reduced by nonrefundable personal credits and the foreign tax credit.[29] Unused credits could not be carried back or carried forward to reduce taxes in other years.

The orphan drug tax credit expired after December 31, 1994.

House bill

No provision.

Senate amendment

The Senate amendment extends the orphan drug tax credit for 18 months—i.e., for the period July 1, 1996, through December 31, 1997.

In addition, the Senate amendment allows taxpayers to carry back unused credits to three years preceding the year the credit is earned and to carry forward unused credits to 15 years following the year the credit is earned.

Effective date.—The Senate amendment applies to qualified clinical testing expenses paid or incurred during the period July 1, 1996, through December 31, 1997. The provision allowing for the carry back and carry forward of unused credits is effective for taxable years ending after June 30, 1996. No portion of the unused business credit that is attributable to the orphan drug credit could be carried back under section 39 to a taxable year ending before July 1, 1996.

Conference agreement

The conference agreement extends the orphan drug tax credit for 11 months—i.e., for the period July 1, 1996, through May 31, 1997.

In addition, the conference agreement includes the provision of the Senate amendment that allows taxpayers to carry back unused credits to three years preceding the year the credit is earned and to carry forward unused credits to 15 years following the year the credit is earned.

Effective date.—The conference agreement applies to qualified clinical testing expenses paid or incurred during the period July 1,

[29] To the extent that the orphan drug tax credit could not be used by reason of the minimum tax limitation, the taxpayer's minimum tax credit was increased (sec. 53(d)(1)(B)(iii)).

1996, through May 31, 1997. The provision allowing for the carry back and carry forward of unused credits is effective for taxable years ending after June 30, 1996. No portion of the unused business credit that is attributable to the orphan drug credit could be carried back under section 39 to a taxable year ending before July 1, 1996.

6. CONTRIBUTIONS OF STOCK TO PRIVATE FOUNDATIONS

(Sec. 1205 of the Senate amendment.)

Present and prior law

In computing taxable income, a taxpayer who itemizes deductions generally is allowed to deduct the fair market value of property contributed to a charitable organization.[30] However, in the case of a charitable contribution of short-term gain, inventory, or other ordinary income property, the amount of the deduction generally is limited to the taxpayer's basis in the property. In the case of a charitable contribution of tangible personal property, the deduction is limited to the taxpayer's basis in such property if the use by the recipient charitable organization is unrelated to the organization's tax-exempt purpose.[31]

In cases involving contributions to a private foundation (other than certain private operating foundations), the amount of the deduction is limited to the taxpayer's basis in the property. However, under a special rule contained in section 170(e)(5), taxpayers were allowed a deduction equal to the fair market value of "qualified appreciated stock" contributed to a private foundation prior to January 1, 1995. Qualified appreciated stock was defined as publicly traded stock which is capital gain property. The fair-market-value deduction for qualified appreciated stock donations applied only to the extent that total donations made by the donor to private foundations of stock in a particular corporation did not exceed 10 percent of the outstanding stock of that corporation. For this purpose, an individual was treated as making all contributions that were made by any member of the individual's family. This special rule contained in section 170(e)(5) expired after December 31, 1994.

House bill

No provision.

Senate amendment

The Senate amendment extends the special rule contained in section 170(e)(5) for 18 months—i.e., for contributions of qualified

[30] The amount of the deduction allowable for a taxable year with respect to a charitable contribution may be reduced depending on the type of property contributed, the type of charitable organization to which the property is contributed, and the income of the taxpayer (secs. 170(b) and 170(e)).

[31] As part of the Omnibus Budget Reconciliation Act of 1993, Congress eliminated the treatment of contributions of appreciated property (real, personal, and intangible) as a tax preference for alternative minimum tax (AMT) purposes. Thus, if a taxpayer makes a gift to charity of property (other than short-term gain, inventory, or other ordinary income property, or gifts to private foundations) that is real property, intangible property, or tangible personal property the use of which is related to the donee's tax-exempt purpose, the taxpayer is allowed to claim the same fair-market-value deduction for both regular tax and AMT purposes (subject to present-law percentage limitations).

appreciated stock made to private foundations during the period July 1, 1996, through December 31, 1997.

Effective date.—The provision is effective for contributions of qualified appreciated stock to private foundations made during the period July 1, 1996, through December 31, 1997.

Conference agreement

The conference agreement extends the special rule contained in section 170(e)(5) for 11 months—i.e., for contributions of qualified appreciated stock made to private foundations during the period July 1, 1996, through May 31, 1997.[32]

Effective date.—The provision is effective for contributions of qualified appreciated stock to private foundations made during the period July 1, 1996, through May 31, 1997.

7. TAX CREDIT FOR PRODUCING FUEL FROM A NONCONVENTIONAL SOURCE

(Sec. 1206 of the Senate amendment.)

Present law

Certain fuels produced from "nonconventional sources" and sold to unrelated parties are eligible for an income tax credit equal to $3 (generally adjusted for inflation) per barrel or BTU oil barrel equivalent (sec. 29). Qualified fuels must be produced within the United States.

Qualified fuels include: (1) oil produced from shale and tar sands; (2) gas produced from geopressured brine, Devonian shale, coal seams, tight formations ("tight sands"), or biomass; and (3) liquid, gaseous, or solid synthetic fuels produced from coal (including lignite).

In general, the credit is available only with respect to fuels produced from wells drilled or facilities placed in service after December 31, 1979, and before January 1, 1993. An exception extends the January 1, 1993 expiration date for facilities producing gas from biomass and synthetic fuel from coal if the facility producing the fuel is placed in service before January 1, 1997, pursuant to a binding contract entered into before January 1, 1996.

The credit may be claimed for qualified fuels produced and sold before January 1, 2003 (in the case of nonconventional sources subject to the January 1, 1993 expiration date) or January 1, 2008 (in the case of biomass gas and synthetic fuel facilities eligible for the extension period).

House bill

No provision.

Senate amendment

The Senate amendment extends the binding contract date for facilities producing synthetic fuels from coal and gas from biomass until the date which is six months after the date of the provision's

[32] If, during this period, a taxpayer contributes qualified appreciated stock as defined in section 170(e)(5) and the amount of such contribution exceeds the percentage limitation under section 170(b)(1)(D), the excess may be carried over to succeeding taxable years. See, e.g., LTR 9444029, LTR 9424020.

enactment, and then placed in service date for two years. The present sunset on producing qualifying for the credit is not changed.

Therefore, under the provision, synthetic fuels from coal and gas from biomass produced from a facility placed in service before January 1, 1999, pursuant to a binding contract entered into before the date which is six months after the date of the provision's enactment, will be eligible for the tax credit if produced before January 1, 2008.

Effective date.—The provision is effective on the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment with two modifications. First, the conference agreement extends the binding contract date for facilities producing synthetic fuels from coal and gas from biomass through December 31, 1996, rather than for six months after the date of enactment as would have been provided in the Senate amendment. Second, the conference agreement extends the placed in service date for eighteen months, rather than for two years as would have been provided in the Senate amendment. The conference agreement does not change the present-law sunset on production qualifying for the credit.

Therefore, under the conference agreement, synthetic fuels from coal and gas from biomass produced from a facility placed in service before July 1, 1998, pursuant to a binding contract entered into before January 1, 1997, will be eligible for the tax credit if produced before January 1, 2008.

Effective date.—The provision is effective on the date of enactment.

8. SUSPEND IMPOSITION OF DIESEL FUEL TAX ON RECREATIONAL MOTORBOATS

(Sec. 1207 of the Senate amendment.)

Present law

Diesel fuel used in recreational motorboats is subject to a 24.4 cents-per-gallon excise tax through December 31, 1999. This tax was enacted by the Omnibus Budget Reconciliation Act of 1993 as a revenue offset for repeal of the excise tax on certain luxury boats. Revenues from this tax are retained in the General Fund.

The diesel fuel tax is imposed on removal of the fuel from a registered terminal facility (i.e., at the "terminal rack"). Present law provides that tax is imposed on all diesel fuel removed from terminal facilities unless the fuel is destined for a nontaxable use and is indelibly dyed pursuant to Treasury Department regulations. If fuel on which tax is paid at the terminal rack (i.e., undyed diesel fuel) ultimately is used in a nontaxable use, a refund is allowed. Depending on the aggregate amount of tax to be refunded, this refund may be claimed either by a direct filing with the Internal Revenue Service or as a credit against income tax.

Dyed diesel fuel (fuel on which no tax is paid) may not be used in a taxable use. Present law imposes a penalty equal to the great-

er of $10 per gallon or $1,000 on persons found to be violating this prohibition.

House bill

No provision.

Senate amendment

The Senate amendment provides that no tax will be imposed on diesel fuel used in recreational motorboats during the period beginning seven days after the date of enactment through December 31, 1997.

In addition, the Senate Finance Committee requested that the Treasury Department study possible alternatives to the current collection regime for motoboat diesel fuel that will provide comparable compliance with the law, and report to the House Committee on Ways and Means and the Senate Committee on Finance no later than April 1, 1997.

Effective date.—The provision is effective on the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

9. EXTENSION OF TRANSITION RULE FOR CERTAIN PUBLICLY TRADED PARTNERSHIPS

(Sec. 1208 of the Senate amendment.)

Present law

Present law provides that, in general, a publicly traded partnership is treated as a corporation for Federal income tax purposes. An exception is provided for certain partnerships, 90 percent or more of whose gross income is passive-type income (as defined for purposes of the provision). A publicly traded partnership is any partnership if (1) partnership interests are traded on an established securities market, or (2) partnership interests are readily tradable on a secondary market (or the substantial equivalent). This provision was added by the Omnibus Budget Reconciliation Act of 1987 (the "1987 Act"), and applied generally to taxable years beginning after December 31, 1987.

The 1987 Act provided a 10-year grandfather rule for certain existing partnerships. Thus, the provision becomes effective for such existing partnerships for taxable years beginning after December 31, 1997. The 1987 Act provides that an existing partnership is one: (1) which was a publicly traded partnership on December 17, 1987; (2) with respect to which a registration statement indicating that such partnership was to be a publicly traded partnership was filed with the Securities and Exchange Commission on or before December 17, 1987; or (3) with respect to which an application was filed with a State regulatory commission on or before December 17, 1987 seeking permission to restructure a portion of a corporation as a publicly traded partnership. A partnership ceases to be treated as an existing partnership if it adds a substantial new line of business after December 17, 1987.

House bill

No provision.

Senate amendment

The Senate amendment provides a two-year extension of the ten-year grandfather rule for existing partnerships. Thus, under the Senate amendment, the present-law provision treating publicly traded partnerships as corporations applies to existing partnerships for taxable years beginning after December 31, 1999.

Effective date.—The provision takes effect as if included in the 1987 Act.

Conference agreement

The conference agreement does not include the Senate amendment provision.

C. Provisions Relating to S Corporations

1. S CORPORATIONS PERMITTED TO HAVE 75 SHAREHOLDERS

(Sec. 1301 of the House bill and the Senate amendment.)

Present law

The taxable income or loss of an S corporation is taken into account by the corporation's shareholders, rather than by the entity, whether or not such income is distributed. A small business corporation may elect to be treated as an S corporation. A "small business corporation" is defined as a domestic corporation which is not an ineligible corporation and which does not have (1) more than 35 shareholders, (2) as a shareholder, a person (other than certain trusts or estates) who is not an individual, (3) a nonresident alien as a shareholder, and (4) more than one class of stock. For purposes of the 35-shareholder limitation, a husband and wife are treated as one shareholder.

House bill

The House bill increases maximum number of eligible shareholders from 35 to 75.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

2. ELECTING SMALL BUSINESS TRUSTS

(Sec. 1302 of the House bill and the Senate amendment.)

Present law

Under present law, trusts other than grantor trusts, voting trusts, certain testamentary trusts and "qualified subchapter S

trusts" may not be shareholders in an S corporation. A "qualified subchapter S trust" is a trust which, under its terms, (1) is required to have only one current income beneficiary (for life), (2) any corpus distributed during the life of the beneficiary must be distributed to the beneficiary, (3) the beneficiary's income interest must terminate at the earlier of the beneficiary's death or the termination of the trust, and (4) if the trust terminates during the beneficiary's life, the trust assets must be distributed to the beneficiary. All the income (as defined for local law purposes) must be currently distributed to that beneficiary. The beneficiary is treated as the owner of the portion of the trust consisting of the stock in the S corporation.

House bill

In general

The House bill allows stock in an S corporation to be held by certain trusts ("electing small business trusts"). In order to qualify for this treatment, all beneficiaries of the trust must be individuals or estates eligible to be S corporation shareholders, except that charitable organizations may hold contingent remainder interests. No interest in the trust may be acquired by purchase. For this purpose, "purchase" means any acquisition of property with a cost basis (determined under sec. 1012). Thus, interests in the trust must be acquired by reason of gift, bequest, etc. A trust must elect to be treated as an electing small business trust.

Each potential current beneficiary of the trust is counted as a shareholder for purposes of the proposed 75 shareholder limitation (or if there were no potential current beneficiaries, the trust would be treated as the shareholder). A potential current income beneficiary means any person, with respect to the applicable period, who is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust.

Treatment of items relating to S corporation stock

The portion of the trust which consists of stock in one or more S corporations is treated as a separate trust for purposes of computing the income tax attributable to the S corporation stock held by the trust. The trust is taxed at the highest individual rate (currently, 39.6 percent on ordinary income and 28 percent on net capital gain) on this portion of the trust's income. The taxable income attributable to this portion includes (1) the items of income, loss, or deduction allocated to it as an S corporation shareholder under the rules of subchapter S, (2) gain or loss from the sale of the S corporation stock, and (3) to the extent provided in regulations, any state or local income taxes and administrative expenses of the trust properly allocable to the S corporation stock. Otherwise allowable capital losses are allowed only to the extent of capital gains.

In computing the trust's income tax on this portion of the trust, no deduction is allowed for amounts distributed to beneficiaries, and no deduction or credit is allowed for any item other than the items described above. This income is not included in the distributable net income of the trust, and thus is not included in

the beneficiaries' income. No item relating to the S corporation stock could be apportioned to any beneficiary.

On the termination of all or any portion of an electing small business trust the loss carryovers or excess deductions referred to in section 642(h) is taken into account by the entire trust, subject to the usual rules on termination of the entire trust.

Treatment of remainder of items held by trust

In determining the tax liability with regard to the remaining portion of the trust, the items taken into account by the subchapter S portion of the trust are disregarded. Although distributions from the trust are deductible in computing the taxable income on this portion of the trust, under the usual rules of subchapter J, the trust's distributable net income does not include any income attributable to the S corporation stock.

Termination of trust and conforming amendment applicable to all trusts

Where the trust terminates before the end of the S corporation's taxable year, the trust takes into account its pro rata share of S corporation items for its final year. The bill makes a conforming amendment applicable to all trusts and estates clarifying that this is the present-law treatment of trusts and estates that terminate before the end of the S corporation's taxable year.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

3. EXPANSION OF POST-DEATH QUALIFICATION FOR CERTAIN TRUSTS

(Sec. 1303 of the House bill and the Senate amendment.)

Present law

Under present law, trusts other than grantor trusts, voting trusts, certain testamentary trusts and "qualified subchapter S trusts" may not be shareholders in a S corporation. A grantor trust may remain an S corporation shareholder for 60 days after the death of the grantor. The 60-day period is extended to two years if the entire corpus of the trust is includible in the gross estate of the deemed owner. In addition, a trust may be an S corporation shareholder for 60 days after the transfer of S corporation pursuant to a will.

House bill

The House bill expands the post-death holding period to two years for all testamentary trusts.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

4. FINANCIAL INSTITUTIONS PERMITTED TO HOLD SAFE HARBOR DEBT

(Sec. 1304 of the House bill and the Senate amendment.)

Present law

A small business corporation eligible to be an S corporation may not have more than one class of stock. Certain debt ("straight debt") is not treated as a second class of stock so long as such debt is an unconditional promise to pay on demand or on a specified date a sum certain in money if: (1) the interest rate (and interest payment dates) are not contingent on profits, the borrower's discretion, or similar factors; (2) there is no convertibility (directly or indirectly) into stock, and (3) the creditor is an individual (other than a nonresident alien), an estate, or certain qualified trusts.

House bill

The definition of "straight debt" is expanded to include debt held by creditors, other than individuals, that are actively and regularly engaged in the business of lending money.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

5. RULES RELATING TO INADVERTENT TERMINATIONS AND INVALID ELECTIONS

(Sec. 1305 of the House bill and the Senate amendment.)

Present law

Under present law, if the Internal Revenue Service ("IRS") determines that a corporation's Subchapter S election is inadvertently terminated, the IRS can waive the effect of the terminating event for any period if the corporation timely corrects the event and if the corporation and shareholders agree to be treated as if the election had been in effect for that period. Such waivers generally are obtained through the issuance of a private letter ruling. Present law does not grant the IRS the ability to waive the effect of an inadvertent invalid Subchapter S election.

In addition, under present law, a small business corporation must elect to be an S corporation no later than the 15th day of the third month of the taxable year for which the election is effective. The IRS may not validate a late election.

House bill

Under the House bill, the authority of the IRS to waive the effect of an inadvertent termination is extended to allow the Service to waive the effect of an invalid election caused by an inadvertent failure to qualify as a small business corporation or to obtain the required shareholder consents (including elections regarding qualified subchapter S trusts), or both. The House bill also allows the IRS to treat a late Subchapter S election as timely where the Service determines that there was reasonable cause for the failure to make the election timely. It is intended that the IRS be reasonable in exercising this authority and apply standards that are similar to those applied under present law to inadvertent subchapter S terminations and other late or invalid elections.

Effective date.—The provision applies to taxable years beginning after December 31, 1982.

Senate amendment

Same as the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment. The conferees wish to clarify that in exercising the authority provided under the provision, the IRS may consider relevant information provided by any affected shareholder (including a person who became a shareholder in a subsequent year) before determining the validity of the S election for the taxable year in question.

6. AGREEMENT TO TERMINATE YEAR

(Sec. 1306 of the House bill and the Senate amendment.)

Present law

In general, each item of S corporation income, deduction and loss is allocated to shareholders on a per-share, per-day basis. However, if any shareholder terminates his or her interest in an S corporation during a taxable year, the S corporation, with the consent of all its shareholders, may elect to allocate S corporation items by closing its books as of the date of such termination rather than apply the per-share, per-day rule.

House bill

The House bill provides that, under regulations to be prescribed by the Secretary of the Treasury, the election to close the books of the S corporation upon the termination of a shareholder's interest is made by all affected shareholders and the corporation, rather than by all shareholders. The closing of the books applies only to the affected shareholders. For this purpose, "affected shareholders" means any shareholder whose interest is terminated and all shareholders to whom such shareholder has transferred shares during the year. If a shareholder transferred shares to the corporation, "affected shareholders" includes all persons who were shareholders during the year.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

7. EXPANSION OF POST-TERMINATION TRANSITION PERIOD

(Sec. 1307 of the House bill and the Senate amendment.)

Present law

Distributions made by a former S corporation during its post-termination period are treated in the same manner as if the distributions were made by an S corporation (e.g., treated by shareholders as nontaxable distributions to the extent of the accumulated adjustment account). Distributions made after the post-termination period are generally treated as made by a C corporation (i.e., treated by shareholders as taxable dividends to the extent of earnings and profits).

The "post-termination period" is the period beginning on the day after the last day of the last taxable year of the S corporation and ending on the later of: (1) a date that is one year later, or (2) the due date for filing the return for the last taxable year and the 120-day period beginning on the date of a determination that the corporation's S corporation election had terminated for a previous taxable year.

In addition, the audit procedures adopted by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") with respect to partnerships also apply to S corporations. Thus, the tax treatment of items is determined at the corporate, rather than individual level.

House bill

The present-law definition of post-termination period is expanded to include the 120-day period beginning on the date of any determination pursuant to an audit of the taxpayer that follows the termination of the S corporation's election and that adjusts a subchapter S item of income, loss or deduction of the S corporation during the S period. In addition, the definition of "determination" is expanded to include a final disposition of the Secretary of the Treasury of a claim for refund and, under regulations, certain agreements between the Secretary and any person, relating to the tax liability of the person.

In addition, the House bill repeals the TEFRA audit provisions applicable to S corporations and would provide other rules to require consistency between the returns of the S corporation and its shareholders.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

8. S CORPORATIONS PERMITTED TO HOLD SUBSIDIARIES

(Sec. 1308 of the House bill and the Senate amendment.)

Present law

A small business corporation may not be a member of an affiliated group of corporations (other than by reason of ownership in certain inactive corporations). Thus, an S corporation may not own 80 percent or more of the stock of another corporation (whether an S corporation or a C corporation).

In addition, a small business corporation may not have as a shareholder another corporation (whether an S corporation or a C corporation).

House bill

An S corporation is allowed to own 80 percent or more of the stock of a C corporation. The C corporation subsidiary could elect to join in the filing of a consolidated return with its affiliated C corporations. An S corporation is not allowed to join in such election. Dividends received by an S corporation from a C corporation in which the S corporation has an 80 percent or greater ownership stake is not treated as passive investment income for purposes of sections 1362 and 1375 to the extent the dividends are attributable to the earnings and profits of the C corporation derived from the active conduct of a trade or business.

In addition, an S corporation is allowed to own a qualified subchapter S subsidiary. The term "qualified subchapter S subsidiary" means a domestic corporation that is not an ineligible corporation (i.e., a corporation that would be eligible to be an S corporation if the stock of the corporation were held directly by the shareholders of its parent S corporation) if (1) 100 percent of the stock of the subsidiary were held by its S corporation parent and (2) for which the parent elects to treat as a qualified subchapter S subsidiary. Under the election, the qualified subchapter S subsidiary is not treated as a separate corporation and all the assets, liabilities, and items of income, deduction, and credit of the subsidiary are treated as the assets, liabilities, and items of income, deduction, and credit of the parent S corporation.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

9. TREATMENT OF DISTRIBUTIONS DURING LOSS YEARS

(Sec. 1309 of the House bill and the Senate amendment.)

Present law

Under present law, the amount of loss an S corporation shareholder may take into account for a taxable year cannot exceed the sum of the shareholder's adjusted basis in his or her stock of the corporation and the adjusted basis in any indebtedness of the corporation to the shareholder. Any excess loss is carried forward.

Any distribution to a shareholder by an S corporation generally is tax-free to the shareholder to the extent of the shareholder's adjusted basis of his or her stock. The shareholder's adjusted basis is reduced by the tax-free amount of the distribution. Any distribution in excess of the shareholder's adjusted basis is treated as gain from the sale or exchange of property.

Under present law, income (whether or not taxable) and expenses (whether or not deductible) serve, respectively, to increase and decrease an S corporation shareholder's basis in the stock of the corporation. These rules require that the adjustments to basis for items of both income and loss for any taxable year apply before the adjustment for distributions applies.

These rules limiting losses and allowing tax-free distributions up to the amount of the shareholder's adjusted basis are similar in certain respects to the rules governing the treatment of losses and cash distributions by partnerships. Under the partnership rules (unlike the S corporation rules), for any taxable year, a partner's basis is first increased by items of income, then decreased by distributions, and finally is decreased by losses for that year.

In addition, if the S corporation has accumulated earnings and profits, any distribution in excess of the amount in an "accumulated adjustments account" will be treated as a dividend (to the extent of the accumulated earnings and profits). A dividend distribution does not reduce the adjusted basis of the shareholder's stock. The "accumulated adjustments account" generally is the amount of the accumulated undistributed post-1982 gross income less deductions.

House bill

The House bill provides that the adjustments for distributions made by an S corporation during a taxable year are taken into account before applying the loss limitation for the year. Thus, distributions during a year reduce the adjusted basis for purposes of determining the allowable loss for the year, but the loss for a year does not reduce the adjusted basis for purposes of determining the tax status of the distributions made during that year.

The House bill also provides that in determining the amount in the accumulated adjustment account for purposes of determining the tax treatment of distributions made during a taxable year by an S corporation having accumulated earnings and profits, net negative adjustments (i.e., the excess of losses and deductions over income) for that taxable year are disregarded.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

10. TREATMENT OF S CORPORATIONS UNDER SUBCHAPTER C

(Sec. 1310 of the House bill and the Senate amendment.)

Present law

Present law contains several provisions relating to the treatment of S corporations as corporations generally for purpose of the Internal Revenue Code.

First, under present law, the taxable income of an S corporation is computed in the same manner as in the case of an individual (sec. 1363(b)). Under this rule, the provisions of the Code governing the computation of taxable income which are applicable only to corporations, such as the dividends received deduction, do not apply to S corporations.

Second, except as otherwise provided by the Internal Revenue Code and except to the extent inconsistent with subchapter S, subchapter C (i.e., the rules relating to corporate distributions and adjustments) applies to an S corporation and its shareholders (sec. 1371(a)(1)). Under this second rule, provisions such as the corporate reorganization provisions apply to S corporations. Thus, a C corporation may merge into an S corporation tax-free.

Finally, an S corporation in its capacity as a shareholder of another corporation is treated as an individual for purposes of subchapter C (sec. 1371(a)(2)). In 1988, the Internal Revenue Service took the position that this rule prevents the tax-free liquidation of a C corporation into an S corporation because a C corporation cannot liquidate tax-free when owned by an individual shareholder.[33] In 1992, the Internal Revenue Service reversed its position, stating that the prior ruling was incorrect.[34]

House bill

The House bill repeals the rule that treats an S corporation in its capacity as a shareholder of another corporation as an individual. Thus, the provision clarifies that the liquidation of a C corporation into an S corporation will be governed by the generally applicable subchapter C rules, including the provisions of sections 332 and 337 allowing the tax-free liquidation of a corporation into its parent corporation. Following a tax-free liquidation, the built-in gains of the liquidating corporation may later be subject to tax under section 1374 upon a subsequent disposition. An S corporation also will be eligible to make a section 338 election (assuming all the requirements are otherwise met), resulting in immediate recognition of all the acquired C corporation's gains and losses (and the resulting imposition of a tax).

[33] PLR 8818049, (Feb. 10, 1988).
[34] PLR 9245004, (July 28, 1992).

The repeal of this rule does not change the general rule governing the computation of income of an S corporation. For example, it does not allow an S corporation, or its shareholders, to claim a dividends received deduction with respect to dividends received by the S corporation, or to treat any item of income or deduction in a manner inconsistent with the treatment accorded to individual taxpayers.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

11. ELIMINATION OF CERTAIN EARNINGS AND PROFITS

(Sec. 1311 of the House bill and the Senate amendment.)

Present law

Under present law, the accumulated earnings and profits of a corporation are not increased for any year in which an election to be treated as an S corporation is in effect. However, under the subchapter S rules in effect before revision in 1982, a corporation electing subchapter S for a taxable year increased its accumulated earnings and profits if its earnings and profits for the year exceeded both its taxable income for the year and its distributions out of that year's earnings and profits. As a result of this rule, a shareholder may later be required to include in his or her income the accumulated earnings and profits when it is distributed by the corporation. The 1982 revision to subchapter S repealed this rule for earnings attributable to taxable years beginning after 1982 but did not do so for previously accumulated S corporation earnings and profits.

House bill

The House bill provides that if a corporation is an S corporation for its first taxable year beginning after December 31, 1995, the accumulated earnings and profits of the corporation as of the beginning of that year is reduced by the accumulated earnings and profits (if any) accumulated in any taxable year beginning before January 1, 1983, for which the corporation was an electing small business corporation under subchapter S. Thus, such a corporation's accumulated earnings and profits are solely attributable to taxable years for which an S election was not in effect. This rule is generally consistent with the change adopted in 1982 limiting the S shareholder's taxable income attributable to S corporation earnings to his or her share of the taxable income of the S corporation.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

12. CARRYOVER OF DISALLOWED LOSSES AND DEDUCTIONS UNDER THE AT-RISK RULES

(Sec. 1312 of the House bill and the Senate amendment.)

Present law

Under section 1366, the amount of loss an S corporation shareholder may take into account cannot exceed the sum of the shareholder's adjusted basis in his or her stock of the corporation and the unadjusted basis in any indebtedness of the corporation to the shareholder. Any disallowed loss is carried forward to the next taxable year. Any loss that is disallowed for the last taxable year of the S corporation may be carried forward to the post-termination period. The "post-termination period" is the period beginning on the day after the last day of the last taxable year of the S corporation and ending on the later of: (1) a date that is one year later, or (2) the due date for filing the return for the last taxable year and the 120-day period beginning on the date of a determination that the corporation's S corporation election had terminated for a previous taxable year.

In addition, under section 465, a shareholder of an S corporation may not deduct losses that are flowed through from the corporation to the extent the shareholder is not "at-risk" with respect to the loss. Any loss not deductible in one taxable year because of the at-risk rules is carried forward to the next taxable year.

House bill

Losses of an S corporation that are suspended under the at-risk rules of section 465 are carried forward to the S corporation's post-termination period.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

13. ADJUSTMENTS TO BASIS OF INHERITED S STOCK TO REFLECT CERTAIN ITEMS OF INCOME

(Sec. 1313 of the House bill and the Senate amendment.)

Present law

Income in respect to a decedent ("IRD") generally consists of items of gross income that accrued during the decedent's lifetime but were not includible in the decedent's income before his or her death under his or her method of accounting. IRD is includible in the income of the person acquiring the right to receive such item.

A deduction for the estate tax attributable to an item of IRD is allowed to such person (sec. 681(c)). The cost or basis of property acquired from a decedent is its fair market value at the date of death (or alternate valuation date if that date is elected for estate tax purposes). This basis is often referred to as "stepped-up basis." Property that constitutes a right to receive IRD does not receive a stepped-up basis.

The basis of a partnership interest or corporate stock acquired from a decedent generally is stepped-up at death. Under Treasury regulations, the basis of a partnership interest acquired from a decedent is reduced to the extent that its value is attributable to items constituting IRD (Treas. reg. sec. 1.742–1). This rule insures that the items of IRD held by a partnership are not later offset by a loss arising from a stepped-up basis. Although S corporation income is taxed to its shareholders in a manner similar to the taxation of a partnership and its partners, no comparable regulation require a reduction in the basis of stock in an S corporation acquired from a decedent where the S corporation holds items of IRD.

House bill

The House bill provides that a person acquiring stock in an S corporation from a decedent would treat as IRD his or her pro rata share of any item of income of the corporation that would have been IRD if that item had been acquired directly from the decedent. Where an item is treated as IRD, a deduction for the estate tax attributable to the item generally will be allowed under the provisions of section 691(c). The stepped-up basis in the stock in an S corporation acquired from a decedent is reduced by the extent to which the value of the stock is attributable to items consisting of IRD. This basis rule is comparable to the present-law partnership rule.

Effective date.—The provision applies with respect to decedent dying after the date of enactment.

Senate amendment

Same as the House bill.

Conference agreement

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

14. S CORPORATIONS ELIGIBLE FOR RULES APPLICABLE TO REAL PROPERTY SUBDIVIDED FOR SALE BY NONCORPORATE TAXPAYERS

(Sec. 1314 of the House bill and the Senate amendment.)

Present law

Under present-law section 1237, a lot or parcel of land held by a taxpayer other than a corporation generally is not treated as ordinary income property solely by reason of the land being subdivided if: (1) such parcel had not previously been held as ordinary income property and if in the year of sale, the taxpayer did not hold other real property; (2) no substantial improvement has been made on the land by the taxpayer, a related party, a lessee, or a

government; and (3) the land has been held by the taxpayer for five years.

House bill

The House bill allows the present-law capital gains presumption in the case of land held by an S corporation. It is expected that rules similar to the attribution rules for partnerships will apply to S corporation (Treas. reg. sec. 1. 1237–1(b)(3)).

Effective date.—The provision is effective for sales in taxable years beginning after December 31, 1996.

Senate amendment

Same as the House bill.

Conference agreement

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

15. CERTAIN FINANCIAL INSTITUTIONS AS ELIGIBLE CORPORATIONS

(Sec. 1315 of the Senate amendment.)

Present law

A small business corporation may elect to be treated as an S corporation. A "small business corporation" is defined as a domestic corporation which is not an ineligible corporation and which meets certain other requirements. An "ineligible corporation" means any corporation which is a member of an affiliated group, certain depository financial institutions (i.e., banks, domestic savings and loan associations, mutual savings banks, and certain cooperative banks), certain insurance companies, a section 936 corporation, or a DISC or former DISC.

House bill

No provision.

Senate amendment

A bank (as defined in sec. 581) is allowed to be an eligible small business corporation unless such institution uses a reserve method of accounting for bad debts.

Effective date.—The provision applies to taxable years beginning after December 31, 1996.

Conference agreement

The conference agreement follows the Senate amendment.

16. CERTAIN TAX-EXEMPT ENTITIES ALLOWED TO BE SHAREHOLDERS

(Sec. 1316 of the Senate amendment.)

Present law

A tax-exempt organization described in section 401(a) (relating to qualified retirement plan trusts) or section 501(c)(3) (relating to certain charitable organizations) cannot be a shareholder in an S corporation.

House bill

No provision.

Senate amendment

Tax-exempt organizations described in Code sections 401(a) and 501(c)(3) ("qualified tax-exempt shareholders") are allowed to be shareholders in S corporations. For purposes of determining the number of shareholders of an S corporation, a qualified tax-exempt shareholder will count as one shareholder.

Items of income or loss of an S corporation will flow-through to qualified tax-exempt shareholders as unrelated business taxable income ("UBTI"), regardless of the source or nature of such income (e.g., passive income of an S corporation will flow through to the qualified tax-exempt shareholders as UBTI.) In addition, gain or loss on the sale or other disposition of stock of an S corporation by a qualified tax-exempt shareholder will be treated as UBTI.

In addition, certain special tax rules relating to employee stock ownership plans ("ESOPs") will not apply with respect to S corporation stock held by the ESOP.

Effective date.—The provision applies to taxable years beginning after December 31, 1997.

Conference agreement

The conference agreement generally follows the Senate amendment. In addition, the conference agreement provides that if a qualified tax-exempt shareholder acquired, by purchase, stock in an S corporation (whether such stock was acquired when the corporation was a C or an S corporation) and receives a dividend distribution with respect to such S corporation stock (i.e., a distribution of subchapter C earnings and profits), except as provided in regulations the shareholder must reduce its basis in the stock by the amount of the dividend. Regulations may provide that the basis reduction only would apply to the extent the dividend is deemed to be allocable to subchapter C earnings and profits that accrued on or before the date of acquisition.

17. REELECTING SUBCHAPTER S STATUS

(Sec. 1315(b) of the House bill and sec. 1317(b) of the Senate amendment.)

Present law

A small business corporation that terminates its subchapter S election (whether by revocation or otherwise) may not make another election to be an S corporation for five taxable years unless the Secretary of the Treasury consents to such election.

House bill

For purposes of the five-year rule, any termination of subchapter S status in effect immediately before the date of enactment of the proposal is not to be taken into account. Thus, any small business corporation that had terminated its S corporation election within the five-year period before the date of enactment may re-

elect subchapter S status upon enactment of the bill without the consent of the Secretary of the Treasury.

Effective date.—The provision is effective for terminations occurring in a taxable year beginning before January 1, 1997.

Senate amendment

Same as the House bill.

Conference agreement

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

II. PENSION SIMPLIFICATION PROVISIONS

A. Simplified Distribution Rules

(Secs. 1401–1404 of the House bill and the Senate amendment.)

Present law

In general, a distribution of benefits from a tax-favored retirement arrangement (i.e., a qualified plan, a qualified annuity plan, and a tax-sheltered annuity contract (sec. 403(b) annuity)) generally is includable in gross income in the year it is paid or distributed under the rules relating to the taxation of annuities.

Lump-sum distributions

Lump-sum distributions from qualified plans and qualified annuity plans are eligible for special 5-year forward averaging. In general, a lump-sum distribution is a distribution within one taxable year of the balance to the credit of an employee that becomes payable to the recipient first, on account of the death of the employee, second, after the employee attains age 59½, third, on account of the employee's separation from service, or fourth, in the case of self-employed individuals, on account of disability. Lump-sum treatment is not available for distributions from a tax-sheltered annuity.

A taxpayer is permitted to make an election with respect to a lump-sum distribution received on or after the employee attains age 59½ to use 5-year forward income averaging under the tax rates in effect for the taxable year in which the distribution is made. In general, this election allows the taxpayer to pay a separate tax on the lump-sum distribution that approximates the tax that would be due if the lump-sum distribution were received in 5 equal installments. If the election is made, the taxpayer is entitled to deduct the amount of the lump-sum distribution from gross income. Only one such election on or after 59½ may be made with respect to any employee.

Under the Tax Reform Act of 1986 (the "1986 Act"), individuals who attained age 50 by January 1, 1986, can elect to use 10-year averaging (under the rates in effect prior to the 1986 Act) in lieu of 5-year averaging. In addition, such individuals may elect to retain capital gains treatment with respect to the pre-1974 portion of a lump sum distribution.

Exclusion of $5,000 for employer-provided death benefits

Under present law, the beneficiary or estate of a deceased employee generally can exclude up to $5,000 in benefits paid by or on behalf of an employer by reason of the employee's death (sec. 101(b)).

Recovery of basis

Amounts received as an annuity under a qualified plan generally are includable in income in the year received, except to the extent they represent the return of the recipient's investment in the contract (i.e., basis). Under present law, a pro-rata basis recovery rule generally applies, so that the portion of any annuity payment that represents nontaxable return of basis is determined by applying an exclusion ratio equal to the employee's total investment in the contract divided by the total expected payments over the term of the annuity.

Under a simplified alternative method provided by the IRS, the taxable portion of qualifying annuity payments is determined under a simplified exclusion ratio method.

In no event can the total amount excluded from income as nontaxable return of basis be greater than the recipient's total investment in the contract.

Required distributions

Present law provides uniform minimum distribution rules generally applicable to all types of tax-favored retirement vehicles, including qualified plans and annuities, IRAs, and tax-sheltered annuities.

Under present law, a qualified plan is required to provide that the entire interest of each participant will be distributed beginning no later than the participant's required beginning date (sec. 401(a)(9)). The required beginning date is generally April 1 of the calendar year following the calendar year in which the plan participant or IRA owner attains age 70½. In the case of a governmental plan or a church plan, the required beginning date is the later of first, such April 1, or second, the April 1 of the year following the year in which the participant retires.

House bill

Lump-sum distributions

The House bill repeals 5-year averaging for lump-sum distributions from qualified plans. Thus, the House bill repeals the separate tax paid on a lump-sum distribution and also repeals the deduction from gross income for taxpayers who elect to pay the separate tax on a lump-sum distribution.

Effective date.—The provision is effective for taxable years beginning after December 31, 1998. The House bill preserves the ability of certain individuals to elect 10-year averaging and capital gains treatment as provided under the Tax Reform Act of 1986.

Exclusion of $5,000 for employer-provided death benefits

The House bill repeals the $5,000 exclusion for employer-provided death benefits.

Effective date.—The provision applies with respect to decedents dying after date of enactment.

Recovery of basis

The House bill provides that basis recovery on payments from qualified plans generally is determined under a method similar to the present-law simplified alternative method provided by the IRS. The portion of each annuity payment that represents a return of basis equals to the employee's total basis as of the annuity starting date, divided by the number of anticipated payments under the following table:

Age	*Number of payments:*
Not more than 55	360
56–60	310
61–65	260
66–70	210
More than 70	160

Effective date.—The provision is effective with respect to annuity starting dates beginning 90 days after the date of enactment.

Required distributions

The House bill modifies the rule that requires all participants in qualified plans to commence distributions by age 70½ without regard to whether the participant is still employed by the employer and generally replaces it with the rule in effect prior to the Tax Reform Act of 1986. Under the House bill, distributions generally are required to begin by April 1 of the calendar year following the later of first, the calendar year in which the employee attains age 70½ or second, the calendar year in which the employee retires. However, in the case of a 5-percent owner of the employer, distributions are required to begin no later than the April 1 of the calendar year following the year in which the 5-percent owner attains age 70½.

In addition, in the case of an employee (other than a 5-percent owner) who retires in a calendar year after attaining age 70½, the House bill generally requires the employee's accrued benefit to be actuarially increased to take into account the period after age 70½ in which the employee was not receiving benefits under the plan. Thus, under the House bill, the employee's accrued benefit is required to reflect the value of benefits that the employee would have received if the employee had retired at age 70½ and had begun receiving benefits at that time.

The actuarial adjustment rule and the rule requiring 5-percent owners to begin distributions after attainment of age 70½ does not apply, under the House bill, in the case of a governmental plan or church plan.

Effective date.—The provision is effective for years beginning after December 31, 1996. If a participant is currently receiving distributions, but does not have to under the provision, it is intended that a plan (or annuity contract) could (but would not be required to) permit the participant, with his or her consent, with his or her consent to stop receiving distributions until such distributions are required under the provision.

Senate amendment

Lump-sum distributions

The Senate amendment is the same as the House bill.

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

Exclusion of $5,000 for employer-provided death benefits

The Senate amendment is the same as the House bill.

Recovery of basis

The Senate amendment is the same as the House bill.

Required distributions

The Senate amendment is the same as the House bill.

Conference agreement

Lump-sum distributions

The conference agreement follows the Senate amendment.

Exclusion of $5,000 for employer-provided death benefits

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

Recovery of basis

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

Required distributions

The conference agreement follows the House bill and the Senate amendment. The conferees intend that the actuarial adjustment rule does not apply in the case of a defined contribution plan.

B. Increased Access to Retirement Savings Plans

1. ESTABLISH SIMPLE RETIREMENT PLANS FOR EMPLOYEES OF SMALL EMPLOYERS

(Secs. 1421–1422 of the House bill and the Senate amendment.)

Present law

Present law does not contain rules relating to SIMPLE retirement plans. However, present law does provide a number of ways in which individuals can save for retirement on a tax-favored basis. These include employer-sponsored retirement plans that meet the requirements of the Internal Revenue Code (a "qualified plan") and individual retirement arrangements ("IRAs"). Employees can earn significant retirement benefits under employer-sponsored retirement plans. However, in order to receive tax-favored treatment, such plans must comply with a variety of rules, including complex nondiscrimination and administrative rules (including top-heavy rules). Such plans are also subject to certain requirements under

the labor law provisions of the Employee Retirement Income Security Act of 1974 ("ERISA").

Contributions to an IRA can also be made by an employer at the election of an employee under a salary reduction simplified employee pension ("SARSEP"). Under SARSEPs, which are not qualified plans, employees can elect to have contributions made to the SARSEP or to receive the contributions in cash. The amount the employee elects to have contributed to the SARSEP is not currently includible in income.

House bill

In general

The House bill creates a simplified retirement plan for small business called the savings incentive match plan for employees ("SIMPLE") retirement plan. SIMPLE plans can be adopted by employers who employ 100 or fewer employees on any day during the year and who do not maintain another employer-sponsored retirement plan. A SIMPLE plan can be either an IRA for each employee or part of a qualified cash or deferred arrangement ("401(k) plan"). If established in IRA form, a SIMPLE plan is not subject to the nondiscrimination rules generally applicable to qualified plans (including the top-heavy rules) and simplified reporting requirements apply. Within limits, contributions to a SIMPLE plan are not taxable until withdrawn.

A SIMPLE plan can also be adopted as part of a 401(k) plan. In that case, the plan does not have to satisfy the special nondiscrimination tests applicable to 401(k) plans and is not subject to the top-heavy rules. The other qualified plan rules continue to apply.

SIMPLE retirement plans in IRA form.

In general.—A SIMPLE retirement plan allows employees to make elective contributions to an IRA. Employee contributions have to be expressed as a percentage of the employee's compensation, and cannot exceed $6,000 per year. The $6,000 dollar limit is indexed for inflation in $500 increments.

Under the House bill, the employer is required to satisfy one of two contribution formulas. Under the matching contribution formula, the employer generally is required to match employee elective contributions on a dollar-for-dollar basis up to 3 percent of the employee's compensation. Under a special rule, the employer can elect a lower percentage matching contribution for all employees (but not less than 1 percent of each employee's compensation). A lower percentage cannot be elected for more than 2 out of any 5 years.

Alternatively, for any year, in lieu of making matching contributions, an employer may elect to make a 2 percent of compensation nonelective contribution on behalf of each eligible employee with at least $5,000 in compensation for such year. No contributions other than employee elective contributions and required employer matching contributions (or, alternatively, required employer nonelective contributions) can be made to a SIMPLE account.

Each employee of the employer who received at least $5,000 in compensation from the employer during any 2 prior years and who is reasonably expected to receive at least $5,000 in compensation during the year generally must be eligible to participate in the SIMPLE plan. Self-employed individuals can participate in a SIMPLE plan.

All contributions to an employee's SIMPLE account have to be fully vested.

Tax treatment of SIMPLE accounts, contributions, and distributions.—Contributions to a SIMPLE account generally are deductible by the employer. In the case of matching contributions, the employer is allowed a deduction for a year only if the contributions are made by the due date (including extensions) for the employer's tax return. Contributions to a SIMPLE account are excludable from the employee's income. SIMPLE accounts, like IRAs, are not subject to tax. Distributions from a SIMPLE retirement account generally are taxed under the rules applicable to IRAs. Thus, they are includable in income when withdrawn. Tax-free rollovers can be made from one SIMPLE account to another. A SIMPLE account can be rolled over to an IRA on a tax-free basis after a two-year period has expired since the individual first participated in the SIMPLE plan. To the extent an employee is no longer participating in a SIMPLE plan (e.g., the employee has terminated employment) and 2 years have expired since the employee first participated in the SIMPLE plan, the employee's SIMPLE account is treated as an IRA.

Early withdrawals from a SIMPLE account generally are subject to the 10-percent early withdrawal tax applicable to IRAs. However, withdrawals of contributions during the 2-year period beginning on the date the employee first participated in the SIMPLE plan are subject to a 25-percent early withdrawal tax (rather than 10 percent).

Employer matching or nonelective contributions to a SIMPLE account are not treated as wages for employment tax purposes.

Administrative requirements.—Each eligible employee can elect, with the 30-day period before the beginning of any year (or the 30-day period before first becoming eligible to participate), to participate in the SIMPLE plan (i.e., to make elective deferrals), and to modify any previous elections regarding the amount of contributions. An employer is required to contribute employees' elective deferrals to the employee's SIMPLE account within 30 days after the end of the month to which the contributions relate. Employees must be allowed to terminate participation in the SIMPLE plan at any time during the year (i.e., to stop making contributions). The plan can provide that an employee who terminates participation cannot resume participation until the following year. A plan can permit (but is not required to permit) an individual to make other changes to his or her salary reduction contribution election during the year (e.g., reduce contributions). It is intended that an employer is permitted to designate a SIMPLE account trustee to which contributions on behalf of eligible employees are made.

Definitions.—For purposes of the rules relating to SIMPLE plans, compensation means compensation required to be reported

by the employer on Form W–2, plus any elective deferrals of the employee. In the case of a self-employed individual, compensation means net earnings from self-employment. The term employer includes the employer and related employers. Related employers include trades or businesses under common control (whether incorporated or not), controlled groups of corporations, and affiliated service groups. In addition, the leased employee rules apply.

SIMPLE 401(k) plans

In general, under the House bill, a cash or deferred arrangement (i.e., 401(k) plan), is deemed to satisfy the special nondiscrimination tests applicable to employee elective deferrals and employer matching contributions if the plan satisfies the contribution requirements applicable to SIMPLE plans. In addition, the plan is not subject to the top-heavy rules for any year for which this safe harbor is satisfied. The plan is subject to the other qualified plan rules.

The safe harbor is satisfied if, for the year, the employer does not maintain another qualified plan and (1) employees' elective deferrals are limited to no more than $6,000, (2) the employer matches employees' elective deferrals up to 3 percent of compensation (or, alternatively, makes a 2 percent of compensation nonelective contribution on behalf of all eligible employees with at least $5,000 in compensation), and (3) no other contributions are made to the arrangement. Contributions under the safe harbor have to be 100 percent vested. The employer cannot reduce the matching percentage below 3 percent of compensation.

Repeal of SARSEPs

Under the House bill, SARSEPs are repealed.

Effective date

The provision relating to SIMPLE plans are effective for years beginning after December 31, 1996. The repeal of SARSEPs applies to years beginning after December 31, 1996, unless the SARSEP was established before January 1, 1997. Consequently, an employer is not permitted to establish a SARSEP after December 31, 1996. SARSEPs established before January 1, 1997, can continue to receive contributions under present-law rules, and new employees of the employer hired after December 31, 1996, can participate in the SARSEP in accordance with such rules.

Senate amendment

The Senate amendment is the same as the House bill, except for the following modifications.

Under the Senate amendment, a SIMPLE plan can be adopted by employers who employed 100 employees or less with at least $5,000 in compensation for the preceding year. Employers who no longer qualify are given a 2-year grace period to continue to maintain the plan.

Under the Senate amendment, eligible employees are given 60 days before the beginning of any year (or the 60-day period before first becoming eligible to participate in the plan) to elect to participate in the SIMPLE plan.

For purposes of the 2 percent of compensation nonelective contribution formula, no more than $150,000 of compensation can be taken into account in any year with respect to any eligible employee.

The Senate amendment clarifies that an employer is permitted to designate a SIMPLE account trustee to which contributions on behalf of eligible employees are made. The Senate amendment also amends title I of ERISA to provide that only simplified reporting requirements apply to SIMPLE plans and so that the employer (and any other plan fiduciary) will not be subject to fiduciary liability resulting from the employee (or beneficiary) exercising control over the assets in the SIMPLE account. For this purpose, an employee (or beneficiary) is treated as exercising control over the assets in his or her account upon the earlier of (1) an affirmative election with respect to the initial investment of any contributions, (2) a rollover contribution (including a trustee-to-trustee transfer) to another SIMPLE account or IRA, or (3) one year after the SIMPLE account is established.

Conference agreement

The conference agreement follows the Senate amendment.

2. TAX-EXEMPT ORGANIZATIONS ELIGIBLE UNDER SECTION 401(K)

(Sec. 1426 of the House bill and the Senate amendment.)

Present law

Under present law, tax-exempt and State and local government organizations are generally prohibited from establishing qualified cash or deferred arrangements (sec. 401(k) plans). Qualified cash or deferred arrangements (1) of rural cooperatives, (2) adopted by State and local governments before May 6, 1986, or (3) adopted by tax-exempt organizations before July 2, 1986, are not subject to this prohibition.

House bill

The House bill allows tax-exempt organizations (including, for this purpose, Indian tribal governments, a subdivision of an Indian tribal government, an agency or instrumentality of an Indian tribal government or subdivision thereof, or a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of such entities) to maintain qualified cash or deferred arrangements. The House bill retains the present-law prohibition against the maintenance of cash or deferred arrangements by State and local governments except to the extent it may apply to Indian tribal governments.

Effective date.—The provision is effective for plan years beginning after December 31, 1996.

Senate amendment

The Senate amendment is the same as the House bill, except that the legislative history to the Senate amendment provides that no inference is intended with respect to whether Indian tribal governments are permitted to maintain qualified cash or deferred arrangements under present law.

Conference agreement

The conference agreement follows the Senate amendment. Thus, under the conference agreement, no inference is intended with respect to whether Indian tribal governments are permitted to maintain qualified cash or deferred arrangements under present law.

3. SPOUSAL IRAS

(Sec. 1427 of the Senate amendment.)

Present law

Within limits, an individual is allowed a deduction for contributions to an individual retirement account or an individual retirement annuity (an "IRA"). An individual generally is not subject to income tax on amounts held in an IRA, including earnings on contributions, until the amounts are withdrawn from the IRA.

Under present law, the maximum deductible contribution that can be made to an IRA generally is the lesser of $2,000 or 100 percent of an individual's compensation (earned income in the case of a self-employed individual). In the case of a married individual whose spouse has no compensation (or elects to be treated as having no compensation), the $2,000 maximum limit on IRA contributions is increased to $2,250.

House bill

No provision.

Senate amendment

The Senate amendment permits deductible IRA contributions of up to $2,000 to be made for each spouse (including, for example, a homemaker who does not work outside the home) if the combined compensation of both spouses is at least equal to the contributed amount.

Effective date.—The provision is effective for taxable years beginning after December 31, 1996.

Conference agreement

The conference agreement follows the Senate amendment.

C. NONDISCRIMINATION PROVISIONS

1. DEFINITION OF HIGHLY COMPENSATED EMPLOYEES AND REPEAL OF FAMILY AGGREGATION RULES

(Sec. 1431 of the House bill and the Senate amendment.)

Present law

Definition of highly compensated employee

An employee, including a self-employed individual, is treated as highly compensated if, at any time during the year or the preceding year, the employee (1) was a 5-percent owner of the employer, (2) received more than $100,000 (for 1996) in annual compensation from the employer, (3) received more than $66,000 (for 1996) in annual compensation from the employer and was one of

the top-paid 20 percent of employees during the same year, or (4) was an officer of the employer who received compensation in excess of $60,000 (for 1996). If, for any year, no officer has compensation in excess of the threshold, then the highest paid officer of the employer is treated as a highly compensated employee.

Family aggregation rules

A special rule applies with respect to the treatment of family members of certain highly compensated employees for purposes of the nondiscrimination rules applicable to qualified plans. Under the special rule, if an employee is a family member of either a 5-percent owner or 1 of the top-10 highly compensated employees by compensation, then any compensation paid to such family member and any contribution or benefit under the plan on behalf of such family member is aggregated with the compensation paid and contributions or benefits on behalf of the 5-percent owner or the highly compensated employee in the top-10 employees by compensation.

Similar family aggregation rules apply with respect to the $150,000 (for 1996) limit on compensation that may be taken into account under a qualified plan (sec. 401(a)(17)) and for deduction purposes (sec. 404(1)).

House bill

Definition of highly compensated employee

Under the House bill, an employee is treated as highly compensated if the employee (1) was a 5-percent owner of the employer at any time during the year or the preceding year or (2) had compensation for the preceding year in excess of $80,000 (indexed for inflation) and the employee was in the top 20 percent employees by compensation for such year. The House bill also repeals the rule requiring the highest paid officer to be treated as a highly compensated employee.

Effective date.—The provision is effective for years beginning after December 31, 1996.

Family aggregation rules

The House bill repeals the family aggregation rules.

Effective date.—The provision is effective for years beginning after December 31, 1996.

Senate amendment

Definition of highly compensated employee

The Senate amendment is the same as the House bill, except an employee who had compensation for the preceding year in excess of $80,000 is treated as highly compensated without regard to whether the employee was in the top 20 percent of employees by compensation.

Family aggregation rules

The Senate amendment is the same as the House bill.

Conference agreement

Definition of highly compensated employee

The conference agreement follows the House bill and the Senate amendment. Thus, under the conference agreement, a plan may elect for a plan year to use either the definition of highly compensated employee in the House bill or the Senate amendment.

Family aggregation rules

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

2. MODIFICATION OF ADDITIONAL PARTICIPATION REQUIREMENTS

(Sec. 1432 of the House bill and the Senate amendment.)

Present law

Under present law, a plan is not a qualified plan unless it benefits no fewer than the lesser of (a) 50 employees of the employer or (b) 40 percent of all employees of the employer (sec. 401(a)(26)). This requirement may not be satisfied by aggregating comparable plans, but may be applied separately to different lines of business of the employer. A line of business of the employer does not qualify as a separate line of business unless it has at least 50 employees.

House bill

The House bill provides that the minimum participation rule applies only to defined benefit pension plans. In addition, the House bill provides that a defined benefit pension plan does not satisfy the rule unless it benefits no fewer than the lesser of (1) 50 employees or (2) the greater of (a) 40 percent of all employees of the employer or (b) 2 employees (1 employee if there is only 1 employee).

The House bill provides that the requirement that a line of business has at least 50 employees does not apply in determining whether a plan satisfies the minimum participation rule on a separate line of business basis.

Effective date.—The provision is effective for years beginning after December 31, 1996.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

3. NONDISCRIMINATION RULES FOR QUALIFIED CASH OR DEFERRED ARRANGEMENTS AND MATCHING CONTRIBUTIONS

(Sec. 1433 of the House bill and the Senate amendment.)

Present law

Under present law, a special nondiscrimination test applies to qualified cash or deferred arrangements (sec. 401(k) plans). The special nondiscrimination test is satisfied if the actual deferral per-

centage ("ADP") for eligible highly compensated employees for a plan year is equal to or less than either (1) 125 percent of the ADP of all nonhighly compensated employees eligible to defer under the arrangement or (2) the lesser of 200 percent of the ADP of all eligible nonhighly compensated employees or such ADP plus 2 percentage points.

Employer matching contributions and after-tax employee contributions under qualified defined contribution plans are subject to a special nondiscrimination test (the actual contribution percentage ("ACP") test) similar to the special nondiscrimination test applicable to qualified cash or deferred arrangements. Employer matching contributions that satisfy certain requirements can be used to satisfy the ADP test, but, to the extent so used, such contributions cannot be considered when calculating the ACP test.

A plan that would otherwise fail to meet the special nondiscrimination test for qualified cash or deferred arrangements is not treated as failing such test if excess contributions (with allocable income) are distributed to the employee or, in accordance with Treasury regulations, recharacterized as after-tax employee contributions. For purposes of this rule, in determining the amount of excess contributions and the employees to whom they are allocated, the elective deferrals of highly compensated employees are reduced in the order of their actual deferral percentage beginning with those highly compensated employees with the highest actual deferral percentages. A similar rule applies to employer matching contributions.

House bill

Prior-year data

The House bill modifies the special nondiscrimination tests applicable to elective deferrals and employer matching and after-tax employee contributions to provide that the maximum permitted actual deferral percentage (and actual contribution percentage) for highly compensated employees for the year is determined by reference to the actual deferral percentage (and actual contribution percentage) for nonhighly compensated employees for the preceding, rather than the current, year. A special rule applies for the first plan year.

Alternatively, under the House bill, an employer is allowed to elect to use the current year actual deferral percentage (and actual contribution percentage). Such an election can be revoked only as provided by the Secretary.

Safe harbor for cash or deferred arrangements

The House bill provides that a cash or deferred arrangement satisfies the special nondiscrimination tests if the plan satisfies one of two contribution requirements and satisfies a notice requirement.

A plan satisfies the contribution requirements under the safe harbor rule for qualified cash or deferred arrangements if the plan either first, satisfies a matching contribution requirement or second, the employer makes a nonelective contribution to a defined contribution plan of at least 3 percent of an employee's compensa-

tion on behalf of each nonhighly compensated employee who is eligible to participate in the arrangement without regard to whether the employee makes elective contributions under the arrangement.

A plan satisfies the matching contribution requirement if, under the arrangement: first, the employer makes a matching contribution on behalf of each nonhighly compensated employee that is equal to (a) 100 percent of the employee's elective contributions up to 3 percent of compensation and (b) 50 percent of the employee's elective contributions from 3 to 5 percent of compensation; and second, the rate of match with respect to any elective contribution for highly compensated employees is not greater than the rate of match for nonhighly compensated employees.

Alternatively, if the rate of matching contribution with respect to any rate of elective contribution requirement is not equal to the percentages described in the preceding paragraph, the matching contribution requirement will be deemed to be satisfied if first, the rate of an employer's matching contribution does not increase as an employer's rate of elective contribution increases and second, the aggregate amount of matching contributions at such rate of elective contribution at least equals the aggregate amount of matching contributions that would be made if matching contributions satisfied the above percentage requirements.

Employer matching and nonelective contributions used to satisfy the contribution requirements of the safe harbor rules are required to be nonforfeitable and are subject to the restrictions on withdrawals that apply to an employee's elective deferrals under a qualified cash or deferred arrangement (sec. 401(k)(2) (B) and (C)). It is intended that employer matching and nonelective contributions used to satisfy the contribution requirements of the safe harbor rules can be used to satisfy other qualified retirement plan nondiscrimination rules (except the special nondiscrimination test applicable to employer matching contributions (the ACP test)). So, for example, a cross-tested defined contribution plan that includes a qualified cash or deferred arrangement can consider such employer matching and nonelective contributions in testing.

The notice requirement is satisfied if each employee eligible to participate in the arrangement is given written notice, within a reasonable period before any year, of the employee's rights and obligations under the arrangement.

Alternative method of satisfying special nondiscrimination test for matching contributions

The House bill provides a safe harbor method of satisfying the special nondiscrimination test applicable to employer matching contributions (the ACP test). Under this safe harbor, a plan is treated as meeting the special nondiscrimination test if first, the plan meets the contribution and notice requirements applicable under the safe harbor method of satisfying the special nondiscrimination requirement for qualified cash or deferred arrangements, and second, the plan satisfies a special limitation on matching contributions.

The limitation on matching contributions is satisfied if: first, the employer matching contributions on behalf of any employee may not be made with respect to employee contributions or elective

deferrals in excess of 6 percent of compensation; second, the rate of an employer's matching contribution does not increase as the rate of an employee's contributions or elective deferrals increases; and third, the matching contribution with respect to any highly compensated employee at any rate of employee contribution or elective deferral is not greater than that with respect to an employee who is not highly compensated.

Any after-tax employee contributions made under the qualified cash or deferred arrangement will continue to be tested under the ACP test. Employer matching and nonelective contributions used to satisfy the safe harbor rules for qualified cash or deferred arrangements cannot be considered in calculating such test. However, employer matching and nonelective contributions in excess of the amount required to satisfy the safe harbor rules for qualified cash or deferred arrangements can be taken into account in calculating such test.

Distribution of excess contributions and excess aggressive contributions

The House bill provides that the total amount of excess contributions (and excess aggregate contributions) is determined as under present law, but the distribution of excess contributions (and excess aggregate contributions) are required to be made on the basis of the amount of contribution by, or on behalf of, each highly compensated employee. Thus, excess contributions (and excess aggregate contributions) are deemed attributable first to those highly compensated employees who have the greatest dollar amount of elective deferrals.

Effective date

The provisions relating to use of prior-year data and the distribution of excess contributions and excess aggregate contributions are effective for years beginning after December 31, 1996. The provisions providing for a safe harbor for qualified cash or deferred arrangements and the alternative method of satisfying the special nondiscrimination test for matching contributions are effective for years beginning after December 31, 1998.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

4. DEFINITION OF COMPENSATION FOR PURPOSES OF THE LIMITS ON CONTRIBUTIONS AND BENEFITS

(Sec. 1434 of the House bill and the Senate amendment.)

Present law

Present law imposes limits on contributions and benefits under qualified plans based on the type of plan. For purposes of these limits, present law provides that the definition of compensation

generally does not include elective employee contributions to certain employee benefit plans.

House bill

The House bill provides that elective deferrals to section 401(k) plans and similar arrangements, elective contributions to nonqualified deferred compensation plans of tax-exempt employers and State and local governments (sec. 457 plans), and salary reduction contributions to a cafeteria plan are considered compensation for purposes of the limits on contributions and benefits.

Effective date.—The provision is effective for years beginning after December 31, 1997.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

D. Miscellaneous Pension Simplification

1. Plans covering self-employed individuals

(Sec. 1441 of the House bill and the Senate amendment.)

Present law

Under present law, certain special aggregation rules apply to plans maintained by owner employees of unincorporated businesses that do not apply to other qualified plans (sec. 401(d)(1) and (2)).

House bill

The House bill eliminates the special aggregation rules that apply to plans maintained by self-employed individuals that do not apply to other qualified plans.

Effective date.—The provision is effective for years beginning after December 31, 1996.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

2. Elimination of special vesting rule for multiemployer plans

(Sec. 1442 of the House bill and the Senate amendment.)

Present law

Under present law, except in the case of multiemployer plans, a plan is not a qualified plan unless a participant's employer-provided benefit vests at least as rapidly as under one of two alternative minimum vesting schedules. A plan satisfies the first schedule if a participant acquires a nonforfeitable right to 100 percent

of the participant's accrued benefit derived from employer contributions upon the participant's completion of 5 years of service. A plan satisfies the second schedule if a participant has a nonforfeitable right to at least 10 percent of the participant's accrued benefit derived from employer contributions after 3 years of service, 40 percent at the end of 4 years of service, 60 percent at the end of 5 years of service, 80 percent at the end of 6 years of service, and 100 percent at the end of 7 years of service.

In the case of a multiemployer plan, a participant's accrued benefit derived from employer contributions is required to be 100-percent vested no later than upon the participant's completion of 10 years of service. This special rule applies only to employees covered by the plan pursuant to a collective bargaining agreement.

House bill

The House bill conforms the vesting rules for multiemployer plans to the rules applicable to other qualified plans.

Effective date.—The provision is effective for plan years beginning on or after the earlier of (1) the later of January 1, 1997, or the date on which the last of the collective bargaining agreements pursuant to which the plan is maintained terminates, or (2) January 1, 1999, with respect to participants with an hour of service after the effective date.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

3. DISTRIBUTIONS UNDER RURAL COOPERATIVE PLANS

(Sec. 1443 of the House bill and the Senate amendment.)

Present law

A qualified cash or deferred arrangement can permit withdrawals of employee elective deferrals only after the earlier of (1) the participant's separation from service, death, or disability, (2) termination of the arrangement, or (3) in the case of a profit-sharing or stock bonus plan, the attainment of age 59½ or the occurrence of a hardship of the participant. In the case of a money purchase pension plan, including a rural cooperative plan, withdrawals by participants cannot occur upon attainment of age 59½ or upon hardship.

House bill

The House bill provides that a rural cooperative plan that includes a cash or deferred arrangement may permit distributions to plan participants after the attainment of age 59½ or on account of hardship. In addition, the definition of a rural cooperative is expanded to include certain public utility districts.

Effective date.—The provision generally is effective for distributions after the date of enactment. The modifications to the defini-

tion of a rural cooperative apply to plan years beginning after December 31, 1996.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

4. TREATMENT OF GOVERNMENTAL PLANS UNDER SECTION 415

(Sec. 1444 of the House bill and the Senate amendment.)

Present law

Present law imposes limits on contributions and benefits under qualified plans based on the type of plan (sec. 415). Certain special rules apply to State and local governmental plans under which such plans may provide benefits greater than those permitted by the limits on benefits applicable to plans maintained by private employers.

In the case of defined benefit pension plans, the limit on the annual retirement benefit is the lesser of (1) 100 percent of compensation or (2) $120,000 (indexed for inflation). The dollar limit is reduced in the case of early retirement or if the employee has less than 10 years of plan participation.

House bill

The House bill makes the following modifications to the limits on contributions and benefits as applied to governmental plans: (1) the 100 percent of compensation limitation on defined benefit pension plan benefits would not apply; and (2) the early retirement reduction and the 10-year phase-in of the defined benefit pension plan dollar limit would not apply to certain disability and survivor benefits.

The House bill also permits State and local government employers to maintain excess benefit plans without regard to the limits on unfunded deferred compensation arrangements of State and local government employers (sec. 457).

Effective date—The provision is effective for years beginning after December 31, 1994. No inference is intended with respect to whether a governmental plan complies with the requirements of section 415 with respect to years beginning before January 1, 1995. With respect to such years, the Secretary is directed to enforce the requirements of section 415 consistent with the provision.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

5. UNIFORM RETIREMENT AGE

(Sec. 1445 of the House bill and the Senate amendment.)

Present law

A qualified plan generally must provide that payment of benefits under the plan must begin no later than 60 days after the end of the plan year in which the participant reaches age 65. Also, for purpose of the vesting and benefit accrual rules, normal retirement age generally can be no later than age 65. For purposes of applying the limits on contributions and benefits (sec. 415), Social Security retirement age is generally used as retirement age. The Social Security retirement age as used for such purposes is presently age 65, but is scheduled to gradually increase.

House bill

The House bill provides that for purposes of the general nondiscrimination rules (sec. 401(a)(4)) the Social Security retirement age (as defined in sec. 415) is a uniform retirement age and that subsidized early retirement benefits and joint and survivor annuities are not treated as not being available to employees on the same terms merely because they are based on an employee's Social Security retirement age (as defined in sec. 415).

Effective date.—The provision is effective for years beginning after December 31, 1996.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

6. CONTRIBUTIONS ON BEHALF OF DISABLED EMPLOYEES

(Sec. 1446 of the House bill and the Senate amendment.)

Present law

Under present law, an employer may elect to continue deductible contributions to a defined contribution plan on behalf of an employee who is permanently and totally disabled. For purposes of the limit on annual additions (sec. 415(c)), the compensation of a disabled employee is deemed to be equal to the annualized compensation of the employee prior to the employee's becoming disabled. Contributions are not permitted on behalf of disabled employees who were officers, owners, or highly compensated before they become disabled.

House bill

The House bill provides that the special rule for contributions on behalf of disabled employees is applicable without an employer election and to highly compensated employees if the defined contribution plan provides for the continuation of contributions on behalf of all participants who are permanently and totally disabled

Effective date.—The provision is effective for years beginning after December 31, 1996.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

7. TREATMENT OF DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS

(Sec. 1447 of the House bill and the Senate amendment.)

Present law

Under an unfunded deferred compensation plan of a State or local government or a tax-exempt organization (a "sec. 457 plan"), an employee who elects to defer the receipt of current compensation is taxed on the amounts deferred when such amounts are paid or made available. The maximum annual deferral under such a plan is the lesser of (1) $7,500 or (2) 33⅓ percent of compensation (net of the deferral).

Amounts deferred under a section 457 plan may not be made available to an employee before the earliest of (1) the calendar year in which the participant attains age 70½, (2) when the participant is separated from the service with the employer, or (3) when the participant is faced with an unforeseeable emergency.

Benefits under a section 457 plan are not treated as made available if the participant may elect to receive a lump sum payable after separation from service and within 60 days of the election. This exception is available only if the total amount payable to the participant under the plan does not exceed $3,500 and no additional amounts may be deferred under the plan with respect to the participant.

House bill

The House bill makes three changes to the rules governing section 457 plans.

The House bill: (1) permits in-service distributions of accounts that do not exceed $3,500 under certain circumstances; (2) increases the number of elections that can be made with respect to the time distributions must begin under the plan; and (3) provides for indexing (in $500 increments) of the dollar limit on deferrals.

Effective date.—The provision is effective for taxable years beginning after December 31, 1996.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

8. TRUST REQUIREMENT FOR DEFERRED COMPENSATION PLANS OF STATE AND LOCAL GOVERNMENTS

(Sec. 1448 of the House bill and the Senate amendment.)

Present law

Until deferrals under an unfunded deferred compensation plan of a State or local government or a tax-exempt organization (a "sec. 457 plan") are made available to a plan participant, the amounts deferred, all property and rights purchased with such amounts, and all income attributable to such amounts, property, or rights must remain solely the property and rights of the employer, subject only to the claims of the employer's general creditors.

House bill

Under the House bill, all amounts deferred under a section 457 plan maintained by a State and local governmental employer have to be held in trust (or custodial account or annuity contract) for the exclusive benefit of employees. The trust (or custodial account or annuity contract) is provided tax-exempt status. Amounts are not considered made available merely because they are held in a trust, custodial account, or annuity contract.

Effective date.—The provision generally is effective with respect to amounts held on or after the date of enactment. In the case of amounts deferred before the date of enactment (and income thereon), the trust requirement does not have to be satisfied until January 1, 1999.

Senate amendment

The Senate amendment is the same as the House bill.

Effective date.—The Senate amendment is the same as the House bill, except that in the case of plans in existence on the date of enactment, the trust requirement does not have to be satisfied until January 1, 1999. Thus, deferrals prior to and after the date of enactment (and earnings thereon) do not have to be held in trust (or custodial account or annuity contract) until January 1, 1999.

Conference agreement

The conference agreement follows the House bill and the Senate amendment. The conference agreement clarifies that amounts held in trust (or custodial account or annuity contract), may be loaned to plan participants (or beneficiaries) pursuant to rules applicable to loans from qualified plans (sec. 72(p)).[35] A section 457 plan is not required to permit loans. The conferees intend that the income inclusion rules in the Code (secs. 83 and 402(b), do not apply to amounts deferred under the section 457 plan (and income thereon) merely because such amounts are contributed to the trust (or custodial account or annuity contract).

Effective date.—The conference agreement follows the House bill and the Senate amendment. Under the conference agreement, in the case of plans in existence on the date of enactment, the trust requirement does not have to be satisfied until January 1, 1999. Thus, deferrals prior to and after the date of enactment (and earnings thereon) do not have to be held in trust (or custodial account or annuity contract) until January 1, 1999.

[35] Under section 72(p), a loan from a plan is treated as a distribution unless the loan generally (1) does not exceed certain limits (generally, the lesser of $50,000 or one-half of the participant's vested plan benefit; (2) must be repaid within 5 years; and (3) must be amortized on a substantially level basis with payments at least quarterly.

9. CORRECTION OF GATT INTEREST AND MORTALITY RATE PROVISIONS IN THE RETIREMENT PROTECTION ACT

(Sec. 1449 of the House bill and the Senate amendment.)

Present law

The Retirement Protection Act of 1994, enacted as part of the implementing legislation for the General Agreement on Tariffs and Trade ("GATT"), modified the actuarial assumptions that must be used in adjusting benefits and limitations. In general, in adjusting a benefit that is payable in a form other than a straight life annuity and in adjusting the dollar limitation if benefits begin before age 62, the interest rate to be used cannot be less than the greater of 5 percent or the rate specified in the plan. Under GATT, if the benefit is payable in a form subject to the requirements of section 417(e)(3), then the interest rate on 30-year Treasury securities is substituted for 5 percent. Also under GATT, for purposes of adjusting any limit or benefit, the mortality table prescribed by the Secretary must be used.

This provision of GATT is generally effective as of the first day of the first limitation year beginning in 1995.

GATT made similar changes to the interest rate and mortality assumptions used to calculate the value of lump-sum distributions for purposes of the rule permitting involuntary dispositions of certain accrued benefits. In the case of a plan adopted and in effect before December 8, 1995, those provisions do not apply before the earlier of (1) the date a plan amendment applying the new assumption is adopted or made effective (whichever is later), or (2) the first day of the first plan year beginning after December 31, 1999.

House bill

The House bill conforms the effective date of the new interest rate and mortality assumptions that must be used under section 415 to calculate the limits on benefits and contributions to the effective date of the provision relating to the calculation of lump-sum distributions. This rule applies only in the case of plans that were adopted and in effect before the date of enactment of GATT (December 8, 1994). To the extent plans have already been amended to reflect the new assumptions, plan sponsors are permitted within 1 year of the date of enactment to amend the plan to reverse retroactively such amendment.

The House bill also repeals the GATT provision which requires that if the benefit is payable before age 62 in a form subject to the requirements of section 417(e)(3) (e.g., lump sum), then the interest rate to be used to reduce the dollar limit on benefits under section 415 cannot be less than the greater of the rate on 30-year Treasury securities or the rate specified in the plan. Consequently, regardless of the form of benefit, the interest rate to be used cannot be less than the greater of 5 percent or the rate specified in the plan.

Effective date.—The provision is effective as if included in GATT.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

10. MULTIPLE SALARY REDUCTION AGREEMENTS PERMITTED UNDER SECTION 403(B)

(Sec. 1450(a) of the House bill and the Senate amendment.)

Present law

Under Treasury regulations, a participant in a tax-sheltered annuity plan (sec. 403(b)) is not permitted to enter into more than one salary reduction agreement in any taxable year.

These restrictions do not apply to other elective deferral arrangements such as a qualified cash or deferred arrangement (sec. 401(k)).

House bill

Under the House bill, for participants in a tax-sheltered annuity plan, the frequency that a salary reduction agreement may be entered into the compensation to which such agreement applies, and the ability to revoke such agreement shall be determined under the rules applicable to qualified cash or deferred arrangements.

Effective date.—The provision is effective for taxable years beginning after December 31, 1995.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

11. TREATMENT OF INDIAN TRIBAL GOVERNMENTS UNDER SECTION 403(B)

(Sec. 1450(b) of the House bill and the Senate amendment.)

Present law

Under present law, certain tax-exempt employers and certain State and local government educational organizations are permitted to maintain tax-sheltered annuity plans (sec. 403(b)). Indian tribal governments are treated as States for this purpose, so certain educational organizations associated with a tribal government are eligible to maintain tax-sheltered annuity plans.

House bill

The House bill provides that any section 403(b) annuity contract purchased in a plan year beginning before January 1, 1995, by an Indian tribal government will be treated as purchased by an entity permitted to maintain a tax-sheltered annuity plan. The House bill also provides that such contracts may be rolled over into a section 401(k) plan maintained by the Indian tribal government.

Effective date.—The provision is effective on the date of enactment.

Senate amendment

The Senate amendment provides that any section 403(b) annuity contract purchased in a plan year beginning before January 1, 1997, by an Indian tribal government will be treated as purchased by an entity permitted to maintain a tax-sheltered annuity plan. The Senate amendment also provides that such contracts may be rolled over into a section 401(k) plan maintained by the Indian tribal government.

In addition, beginning January 1, 1997, Indian tribal governments are permitted to maintain tax-sheltered annuity plans.

Effective date.—The provision generally is effective on the date of enactment, except that the provision permitting Indian tribal governments to maintain tax-sheltered annuity plans is effective for taxable years beginning after December 31, 1996.

Conference agreement

The conference agreement follows the House bill.

12. APPLICATION OF ELECTIVE DEFERRAL LIMIT TO SECTION 403(B) CONTRACTS

(Sec. 1450(c) of the House bill and the Senate amendment.)

Present law

A tax-sheltered annuity plan must provide that elective deferrals made under the plan on behalf of an employee may not exceed the annual limit on elective deferrals ($9,500 for 1996). Plans that do not comply with this requirement may lose their tax-favored status.

House bill

Under the House bill, each tax-sheltered annuity contract, not the tax-sheltered annuity plan, must provide that elective deferrals made under the contract may not exceed the annual limit on elective deferrals. It is intended that the contract terms be given effect in order for this requirement to be satisfied.

Effective date.—The provision is effective for years beginning after December 31, 1995, except that an annuity contract is not required to meet any change in any requirement by reason of the provision before the 90th day after the date of enactment. No inference is intended as to whether the exclusion of elective deferrals from gross income by employees who have not exceeded the annual limit on elective deferrals is affected to the extent other employees exceed the annual limit prior to the effective date of this provision.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

13. WAIVER OF MINIMUM WAITING PERIOD FOR QUALIFIED PLAN DISTRIBUTIONS

(Sec. 1451 of the House bill.)

Present law

Under present law, in the case of a qualified joint and survivor annuity ("QJSA"), a written explanation of the form of benefit must generally be provided to participants no less than 30 days and no more than 90 days before the annuity starting date. Temporary Treasury regulations provide that a plan may permit a participant to elect (with any applicable spousal consent) a distribution with an annuity starting date before 30 days have elapsed since the explanation was provided, as long as the distribution commences more than seven days after the explanation was provided.

House bill

The House bill provides that the minimum period between the date the explanation of the qualified joint and survivor annuity is provided and the annuity starting date does not apply if it is waived by the participant and, if applicable, the participant's spouse.

Effective date.—The provision is effective with respect to plan years beginning after December 31, 1996.

Senate amendment

No provision.

Conference agreement

The conference agreement codifies the provision in the temporary Treasury regulations which provides that a plan may permit a participant to elect (with any applicable spousal consent) a distribution with an annuity starting date before 30 days have elapsed since the explanation was provided, as long as the distribution commences more than seven days after the explanation was provided. The conference agreement also provides that a plan is permitted to provide the explanation after the annuity starting date if the distribution commences at least 30 days after such explanation was provided, subject to the same waiver of the 30-day minimum waiting period as described above. This is intended to allow retroactive payments of benefits which are attributable to the period before the explanation was provided.

14. EXPANSION OF PBGC MISSING PARTICIPANT PROGRAM

(Sec. 1451 of the Senate amendment.)

Present law

The Retirement Protection Act ("RPA"), enacted as part of the legislation implementing the General Agreement on Tariffs and Trade ("GATT") in 1994, provided special rules for the payment of benefits with respect to missing participants under a terminating single-employer defined benefit plan covered by the Pension Benefit Guaranty Corporation ("PBFC"). These rules generally required the plan administrator to (1) transfer the missing participant's des-

ignated benefit to the PBGC or purchase an annuity from an insurer to satisfy the benefit liability, and (2) provide the PBGC with such information and certifications with respect to the benefits or annuity as the PBGC may specify. The missing participant program does not apply to multiemployer defined benefit plans, defined contribution plans, and defined benefit plans not covered by the PBGC (generally governmental plans, church plans, and plans sponsored by professional service employers with less than 25 employees).

House bill

No provision.

Senate amendment

The missing participant program is generally expanded to be available to multiemployer defined benefit plans, defined contribution plans, and defend benefit plans not covered by the PBGC (other than governmental and church plans). Under the Senate amendment, the present law missing participant program applicable to single-employer defined benefits plans applies to a terminating muiltiemployer defined benefit plan under rules prescribed by the PBGC.

In the case of a terminating defined contribution plan or a terminating defined benefit plan not covered by the PBGC, the missing participant program does not apply unless the plan elects to transfer a missing participant's benefits to the PBGC. To the extent provided in regulations issued by the PBGC, the administrator of the plan making such an election is required to provide the PBGC with information with respect to the benefits of a missing participant. Upon location of the missing participant, the missing participant's benefits would be paid by the PBGC in a lump sum or in such other form as specified in regulations.

Effective date.—The provision is effective with respect to distributions made on or after the date final regulations implementing the provision are issued by the PBGC.

Conference agreement

The conference agreement does not include the Senate amendment provision.

15. REPEAL OF COMBINED PLAN LIMIT

(Sec. 1452 of the House bill and the Senate amendment.)

Present law

Combined plan limit

Present law provides limits on contributions and benefits under qualified retirement plans based on the type of plan (i.e., based on whether the plan is a defined contribution plan or a defined benefit pension plan). In the case of a defined contribution plan, annual contributions are generally limited to the lesser of $30,000 (for 1996) and 25 percent of compensation. In the case of a defined benefit pension plan, the annual benefit is generally limited to the lesser of $120,000 (for 1996) and 100 percent of the par-

ticipant's average compensation for the highest 3 years. An overall limit applies if an individual is a participant in both a defined benefit pension plan and a defined contribution plan (called the combined plan limit).

Excess distribution tax

Present law imposes a 15-percent excise tax on excess distributions from qualified retirement plans, tax-sheltered annuities, and IRAs. Excess distributions are generally the aggregate amount of retirement distributions from such plans during any calendar year in excess of $150,000 (or $750,000 in the case of a lump-sum distribution). An additional 15-percent estate tax is also imposed on an individual's excess retirement accumulation.

House bill

Combined plan limit

The House bill repeals the combined plan limit.

Effective date.—The provision repealing the combined plan limit is effective with respect to limitation years beginning after December 31, 1998.

Excess distribution tax

Until the repeal of the combined plan limit is effective, the House bill suspends the excise tax on excess distributions. The additional estate tax on excess accumulations continues to apply.

Effective date.—The provision relating to the excise tax on excess distributions is effective with respect to distributions received in 1996, 1997, and 1998.

Senate amendment

Combined plan limit

The Senate amendment is the same as the House bill.

Effective date.—The provision repealing the combined plan limit is effective with respect to limitation years beginning after December 31, 1999.

Excess distribution tax

The Senate amendment is the same as the House bill.

Effective date.—The provision relating to the excise tax on excess distribution is effective with respect to distributions received in 1997, 1998, and 1999.

Conference agreement

Combined plan limit

The conference agreement follows the Senate amendment.

Excess distribution tax

The conference agreement follows the Senate amendment.

16. TAX ON PROHIBITED TRANSACTIONS

(Sec. 1453 of the House bill and the Senate amendment.)

Present law

Present law prohibits certain transactions (prohibited transactions) between a qualified plan and a disqualified person in order to prevent with a close relationship to the qualified plan from using that relationship to the detriment of plan participants and beneficiaries. A two-tier excise tax is imposed on prohibited transactions. The initial level tax is equal to 5 percent of the amount involved with respect to the transaction. If the transaction is not corrected within a certain period, a tax equal to 100 percent of the amount involved may be imposed.

House bill

The House bill increases the initial-level prohibited transaction tax from 5 percent to 10 percent.

Effective date.—The provision is effective with respect to prohibited transactions occurring after the date of enactment.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

17. TREATMENT OF LEASED EMPLOYEES

(Sec. 1454 of the House bill and the Senate amendment.)

Present law

An individual (a leased employee) who performs services for another person (the recipient) may be required to be treated as the recipient's employee for various employee benefit provisions, if the services are performed pursuant to an agreement between the recipient and any other person (the leasing organization) who is otherwise treated as the individual's employer (sec. 414(n)). The individual is to be treated as the recipient's employee only if the individual has performed services for the recipient on a substantially full-time basis for a year, and the services are of a type historically performed by employees in the recipient's business field.

An individual who otherwise would be treated as a recipient's leased employee will not be treated as such an employee if the individual participates in a safe harbor plan maintained by the leasing organization meeting certain requirements. Each leased employee is to be treated as an employee of the recipient, regardless of the existence of a safe harbor plan, if more than 20 percent of an employer's nonhighly compensated workforce are leased.

House bill

Under the House bill, the present-law "historically performed" test is replaced with a new test under which an individual is not considered a leased employee unless the individual's services are performed under primary direction or control by the service recipient. As under present law, the determination of whether someone is a leased employee is made after determining whether the indi-

vidual is a common-law employee of the recipient. Thus, an individual who is not a common-law employee of the service recipient could nevertheless be a leased employee of the service recipient. Similarly, the fact that a person is or is not found to perform services under primary direction or control of the recipient for purposes of the employee leasing rules is not determinative of whether the person is or is not a common-law employee of the recipient.

Whether services are performed by an individual under primary direction or control by the service recipient depends on the facts and circumstances. In general, primary direction and control means that the service recipient exercises the majority of direction and control over the individual. Factors that are relevant in determining whether primary direction or control exists include whether the individual is required to comply with instructions of the service recipient about when, where, and how he or she is to perform the services, whether the services must be performed by a particular person, whether the individual is subject to the supervision of the service recipient, and whether the individual must perform services in the order or sequence set by the service recipient. Factors that generally are not relevant in determining whether such direction or control exists include whether the service recipient has the right to hire or fire the individual and whether the individual works for others.

For example, an individual who works under the direct supervision of the service recipient would be considered to be subject to primary direction or control of the service recipient even if another company hired and trained the individual, had the ultimate (but unexercised) legal right to control the individual, paid his wages, withheld his employment and income taxes, and had the exclusive right to fire him. Thus, for example, temporary secretaries, receptionists, word processing personnel and similar office personnel who are subject to the day-to-day control of the employer in essentially the same manner as a common-law employee are treated as leased employees if the period of service threshold is reached.

On the other hand, an individual who is a common-law employee of Company A who performs services for Company B on the business premises of Company B under the supervision of Company A would generally not be considered to be under primary direction or control of Company B. The supervision by Company A must be more than nominal, however, and not merely a mechanism to avoid the literal language of the direction or control test.

An example of the situation in the preceding paragraph might be a work crew that comes into a factory to install, repair, maintain, or modify equipment or machinery at the factory. The work crew includes a supervisor who is an employee of the equipment (or equipment repair) company and who has the authority to direct and control the crew, and who actually does exercise such direction and control. In this situation, the supervisor and his or her crew are required to comply with the safety and environmental precautions of the manufacturer, and the supervisor is in frequent communication with the employees of the manufacturer. As another example, certain professionals (e.g., attorneys, accountants, actuaries, doctors, computer programmers, systems analysts, and engineers) who regularly make use of their own judgment and dis-

cretion on matters of importance in the performance of their services and are guided by professional, legal, or industry standards, are not leased employees even though the common law employer does not closely supervise the professional on a continuing basis, and the service recipient requires the services to be performed on site and according to certain stages, techniques, and timetables. In addition to the example above, outside professionals who maintain their own businesses (e.g., attorneys, accountants, actuaries, doctors, computer programmers, systems analysts, and engineers) generally would not be considered to be subject to such primary direction or control.

Under the direction or control test, clerical and similar support staff (e.g., secretaries and nurses in a doctor's office), generally would be considered to be subject to primary direction or control of the service recipient and would be leased employees provided the other requirements of section 414(n) are met.

In many cases, the "historically performed" test is overly broad, and results in the unintended treatment of individuals as leased employees. One of the principal purposes for changing the leased employee rules is to relieve the unnecessary hardship and uncertainty created for employers in these circumstances. However, it is not intended that the direction or control test enable employers to engage in abusive practices. Thus, it is intended that the Secretary interpret and apply the leased employee rules in a manner so as to prevent abuses. This ability to prevent abuses under the leasing rules is in addition to the present-law authority of the Secretary under section 414(o). For example, one potentially abusive situation exists where the benefit arrangements of the service recipient overwhelmingly favor its highly compensated employees, the employer has no or very few nonhighly compensated common-law employees, yet the employer makes substantial use of the services of nonhighly compensated individuals who are not its common-law employees.

Effective date.—The provision is effective for years beginning after December 31, 1996, except that the House bill would not apply to relationships that have been previously determined by an IRS ruling not to involve leased employees. In applying the leased employee rules to years beginning before the effective date, it is intended that the Secretary use a reasonable interpretation of the statute to apply the leasing rules to prevent abuse.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

18. UNIFORM PENALTY PROVISIONS TO APPLY TO CERTAIN PENSION REPORTING REQUIREMENTS

(Sec. 1455 of the House bill and the Senate amendment.)

Present law

Any person who fails to file an information report with the IRS on or before the prescribed filing date is subject to penalties for each failure. A different, flat-amount penalty applies for each failure to provide information reports to the IRS or statements to payees relating to pension payments.

House bill

The House bill incorporates into the general penalty structure the penalties for failure to provide information reports relating to pension payments to the IRS and to recipients.

Effective date.—The provision is effective with respect to returns and statements the due date for which is after December 31, 1996.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

19. RETIREMENT BENEFITS OF MINISTERS NOT SUBJECT TO TAX ON NET EARNINGS FROM SELF-EMPLOYMENT

(Sec. 1456 of the House bill and the Senate amendment.)

Present law

Under present law, certain benefits provided to ministers after they retire are subject to self-employment tax.

House bill

The House bill provides that retirement benefits received from a church plan after a minister retires, and the rental value or allowance of a parsonage (including utilities) furnished to a minister after retirement, are not subject to self-employment taxes.

Effective date.—The provision is effective for years beginning before, on, or after December 31, 1994.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

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

20. TREASURY TO PROVIDE MODEL FORMS FOR SPOUSAL CONSENT AND QUALIFIED DOMESTIC RELATIONS ORDERS

(Sec. 1457 of the Senate amendment.)

Present law

Present law contains a number of rules designed to provide income to the surviving spouse of a deceased employee. Under these spousal protection rules, defined benefit pension plans and money

purchase pension plans are required to provide that vested retirement benefits with a present value in excess of $3,500 are payable in the form of a qualified joint and survivor annuity ("QJSA") or, in the case of a participant who dies before the annuity starting date, a qualified preretirement survivor annuity ("QPSA"). Benefits from a plan subject to the survivor benefit rules may be paid in a form other than a QJSA or QPSA if the participant waives the QJSA or QPSA (or both) and the applicable notice, election, and spousal consent requirements are satisfied.

Also, under present law, benefits under a qualified retirement plan are subject to prohibitions against assignment or alienation of benefits. An exception to this rule generally applies in the case of plan benefits paid to a former spouse pursuant to a qualified domestic relations order ("QDRO").

House bill

No provision.

Senate amendment

Model spousal consent form

The Secretary is required to develop a model spousal consent from, no later than January 1, 1997, waving the QJSA and QPSA forms of benefit. Such form must be written in a manner calculated to be understood by the average person, and must disclose in plain form whether the waiver is irrevocable and that it may be revoked by a QDRO.

Model QDRO

The Secretary is required to develop a model QDRO, no later than January 1, 1997, which satisfies the requirements of a QDRO under present law, and the provisions of which focus attention on the need to consider the treatment of any lump sum payment, QJSA, or QPSA.

Effective date

The provisions are effective on the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment, except that instead of developing a model spousal consent form and a model QDRO, the Secretary must develop sample language for inclusion in a spousal consent form and QDRO.

21. TREATMENT OF LENGTH OF SERVICE AWARDS FOR CERTAIN VOLUNTEERS UNDER SECTION 457

(Sec. 1458 of the Senate amendment.)

Present law

Compensation deferred under an eligible deferred compensation plan of a tax-exempt or governmental employer that meets certain requirements (a "sec. 457 plan") is not includible in gross income until paid or made available. One of the requirements for a section 457 plan is that the maximum annual amount that can be

deferred is the lesser of $7,500 or 33⅓ percent of the individual's taxable compensation.

Amounts deferred under plans of tax-exempt and governmental employers that do not meet the requirements of section 457 (other than amounts deferred under tax-qualified retirement plans, section 403(b) annuities and certain other plans) are includible in gross income in the first year in which there is no substantial risk of forfeiture of such amounts.

House bill

No provision.

Senate amendment

Under the Senate amendment, the requirements of section 457 do not apply to any plan paying solely length of service awards to bona fide volunteers (or their beneficiaries) on account of fire fighting and prevention, emergency medical, and ambulance services performed by such volunteers. An individual is considered a "bona fide volunteer" if the only compensation received by such individual for performing such services is reimbursement (or a reasonable allowance) for expenses incurred in the performance of such services, or reasonable benefits (including length of service awards) and nominal fees for such services customarily paid by tax-exempt or governmental employers in connection with the performance of such services by volunteers. Under the Senate amendment, a length of service award plan will not qualify for this special treatment under section 457 if the aggregate amount of length of service awards accruing with respect to any year of service for any bona fide volunteer exceeds $3,000.

In addition, any amounts exempt from the requirements of section 457 under the Senate amendment are not considered wages for purposes of the Federal Insurance Contribution Act ("FICA") taxes.

Effective date.—The provision applies to accruals of length of service awards after December 31, 1996.

Conference agreement

The conference agreement follows the Senate amendment.

22. ALTERNATIVE NONDISCRIMINATION RULES FOR CERTAIN PLANS THAT PROVIDE FOR EARLY PARTICIPATION

(Sec. 1459 of the Senate amendment.)

Present law

Under present law, a special nondiscrimination test applies to qualified cash or deferred arrangements (sec. 401(k) plans). The special nondiscrimination test is satisfied if the actual deferral percentage ("ADP") for eligible highly compensated employees for a plan year is equal to or less than either (1) 125 percent of the ADP of all nonhighly compensated employees eligible to defer under the arrangement or (2) the lesser of 200 percent of the ADP of all eligible nonhighly compensated employees or such ADP plus 2 percentage points. Employer matching contributions and after-tax employee contributions under qualified defined contribution plans are subject to a special nondiscrimination test (the actual contribution

percentage ("ACP") test) similar to the special nondiscrimination test applicable to qualified cash or deferred arrangements.

In general, a plan need not permit employees to enter a plan prior to the attainment of age 21 and the completion of 1 year service. For purposes of the nondiscrimination rules (including the ADP and ACP tests), an employer that chooses less restrictive entry conditions (e.g., age 18 rather than age 21) may choose "separate testing" under which all employees who have not met the statutory age and service entry maximums are disregarded, provided that the plan satisfies the nondiscrimination rules taking into account only those employees whose age and service are less than the statutory age and service maximums. Thus, for example, such a plan would apply one ADP test for employees who are over age 21 with 1 year of service, under which the plan would disregard elective contributions for other employees, and a second ADP test looking solely at elective contribution for employees under age 21 or who have not completed 1 year of service.

House bill

No provision.

Senate amendment

Under the Senate amendment, for purposes of the ADP test, a section 401(k) plan may elect to disregard employees (other than highly compensated employees) eligible to participate before they have completed 1 year of service and reached age 21, provided the plan separately satisfies the minimum coverage rules (sec. 410(b)) taking into account only those employees who have not completed 1 year of service or are under age 21. Instead of applying two separate ADP tests, such a plan could apply a single ADP test that compares the ADP for all highly compensated employees who are eligible to make elective contributions with the ADP for those nonhighly compensated employees who are eligible to make elective contributions and who have completed one year of service and reached age 21. A similar rule applies for purposes of the ACP test.

Effective date.—The provision is effective for plan years beginning after December 31, 1998.

Conference agreement

The conference agreement follows the Senate amendment.

23. MODIFICATIONS OF JOINT AND SURVIVOR ANNUITY REQUIREMENTS

(Sec. 1460 of the Senate amendment.)

Present law

Present law contains a number of rules designed to provide income to the surviving spouse of a deceased employee. These rules are in both the Internal Revenue Code and title I of the Employee Retirement Income Security Act of 1974, as amended.

Under the spousal protection rules, defined benefit pension plans and money purchase pension plans are required to provide that vested retirement benefits with a present value in excess of $3,500 are payable in the form of a qualified joint and survivor annuity ("QJSA") or, in the case of a participant who dies before the

annuity starting date, a qualified preretirement survivor annuity ("QPSA"). A QJSA is generally defined as an annuity for the life of the participant with a survivor annuity for the life of the spouse which is not less than 50 percent of (and not greater than 100 percent of) the amount of the participant's annuity, and which is the actuarial equivalent of a single life annuity for the life of the participant. A QPSA is generally defined as an annuity for the life of the surviving spouse of the participant, the payments of which are not less than the amount which would be payable as a survivor annuity under the plan's QJSA.

The survivor benefit rules do not apply to defined contribution plans other than money purchase pension plans if (1) the plan provides that, upon the death of the participant, the participant's accrued benefit is payable to the participant's surviving spouse, (2) the participant does not elect payment of benefits in the form of an annuity, and (3) the plan is not a transferee plan of a plan subject to the joint and survivor rules.

Benefits from a plan subject to the survivor benefit rules may be paid in a form other than a QJSA or QPSA if the participant waives the QJSA or QPSA and the applicable notice, election, and spousal consent requirements are satisfied. Similarly, under a defined contribution plan not subject to the survivor benefit rules, the spouse can consent to have benefits paid to another beneficiary.

House bill

No provision.

Senate amendment

Under the Senate amendment, if a plan provides as its QJSA a benefit which provides a survivor annuity for the life of the spouse which is not equal to 66⅔ percent of the amount of the participant's annuity, the plan is required to provide the participant with an election to receive an annuity for the life of the participant with a survivor annuity for the life of the spouse which is 66⅔ percent of the amount of the participant's annuity.[36] If the participant makes such an election the benefit received is treated as a QJSA for purposes of the qualified plan requirements; however the fact that such an election is offered does not affect how the QPSA is calculated. In other words, the QPSA continues to be based on the regular QJSA provided under the plan.

Effective date.—The provision is effective for plan years beginning after December 31, 1996. However, plans in existence on the date of enactment do not have to comply with the requirements of the amendment before the plan year immediately following the first plan year in which any amendment to the plan that is otherwise made becomes effective.

Conference agreement

The conference agreement does not include the Senate amendment provision.

[36] As with the QJSA, this benefit would be the actuarial equivalent of a single life annuity for the life of the participant.

24. CLARIFICATION OF APPLICATION OF ERISA TO INSURANCE COMPANY GENERAL ACCOUNTS

(Sec. 1461 of the Senate amendment.)

Present law

The Employee Retirement Income Security Act of 1974 ("ERISA") imposes certain fiduciary requirements (including restrictions on certain prohibited transactions) with respect to the assets of an employee benefit plan ("plan assets"). The International Revenue Code of 1986 (the "Code") imposes an excise tax in the case of certain prohibited transactions involving plan assets.

In 1975, the Department of Labor issued guidance providing that if an insurance company issues a contract or policy of insurance to an employee benefit plan and places the consideration for such contract or policy in its general asset account, the assets in such account are not considered to be plan assets.[37] In 1993, the Supreme Court[38] ruled that certain assets held in an insurance company's general account should be considered plan assets.

House bill

No provision.

Senate amendment

Under the Senate amendment, not later than December 31, 1996, the Secretary of Labor is required to issue proposed regulations providing guidance for the purpose of determining, in cases where an insurer issues 1 or more policies (supported by the assets of the insurer's general account) to or for the benefit of an employee benefit plan, which assets of the insurer (other than plan assets held in its separate account) constitute plan assets for purposes of the fiduciary rules of ERISA and the prohibited transaction provisions of the Code. Such proposed regulations must be subject to public notice and comment until March 31, 1997, and the Secretary of Labor is required to issue final regulations by June 30, 1997. Any regulations issued by the Secretary of Labor in accordance with the Senate amendment generally could not take effect before the date on which such regulations became final.

In issuing regulations, the Secretary of Labor would have to ensure that such regulations are administratively feasible and are designed to protect the interests and rights of the plan and of the plans participants and beneficiaries. In issuing regulations, the Secretary of Labor may exclude any assets of the insurer with respect to its operations, products, or services from treatment as plan assets. Further, the regulations would have to provide that plan assets do not include assets which are not treated as plan assets under present law because they are (1) assets of an investment company registered under the Investment Company Act of 1940, or

[37] Interpretive Bulletin 1975–2, 29 CFR section 2509.75–2(b) (1992). The term "general account" refers to all assets of an insurance company which are not legally segregated and allocated to separate accounts. The assets in a general account are derived from all classes of business and support the insurer's obligations on an unsegregated basis, with no particular assets being specifically committed to meet the obligations under any particular contract or policy.

[38] *John Hancock Mutual Life Insurance Company* v. *Harris Trust and Savings Bank,* 510 U.S. 86 (1993).

(2) assets of an insurer with respect to a guaranteed benefit policy issued by such insurer.

Under the Senate amendment, no person is liable under ERISA or the Code for conduct which occurred prior to the date which is 18 months following the effective date of the final regulations on the basis of a claim that the assets of the insurer (other than plan assets held in a separate account) constituted plan assets, except as otherwise provided by the Secretary of Labor in order to prevent avoidance of the guidance in the regulations or as provided in an action brought by the Secretary of Labor under ERISA's enforcement provisions for a breach of fiduciary responsibility which would also constitute a violation of Federal criminal law or constitute a felony under applicable State law.[39]

The Senate amendment does not preclude the application of any Federal criminal law.

Effective date.—The provision generally would be effective on January 1, 1975. However, the provision would not apply to any civil action commenced before January 7, 1995.

Conference agreement

The conference agreement follows the Senate amendment with the following modifications.

Proposed regulations need not be issued by the Secretary of Labor until June 30, 1997. Such proposed regulations will be subject to public notice and comment until September 30, 1997. Final regulations need not be issued until December 31, 1997.

Such regulations will only apply with respect to a policy issued by an insurer on or before December 31, 1998. In the case of such a policy, the regulations will take effect at the end of the 18 month period following the date such regulations become final. New policies issued after December 31, 1998, will be subject to the fiduciary obligations under ERISA.

In issuing regulations, the Secretary of Labor must ensure that such regulations protect the interests and rights of the plan and of its participants and beneficiaries as opposed to ensuring that such regulations are designed to protect the interests and rights of the plan and of its participants and beneficiaries.

Under the conference agreement, in connection with any policy (other than a guaranteed benefit policy) issued by an insurer to or for the benefit of an employee benefit plan, the regulations issued by the Secretary of Labor must require (1) that a plan fiduciary totally independent of the insurer authorize the purchase of such policy (unless it is the purchase of a life insurance, health insurance, or annuity contract exempt from ERISA's prohibited transaction rules); (2) that after the date final regulations are issued the insurer provide periodic reports to the policyholder disclosing the method by which any income or expenses of the insurer's general account are allocated to the policy and disclosing the actual return to the plan under the policy and such other financial information the Secretary may deem appropriate; and (3) that the insurer disclose to the plan fiduciary the extent to which alternative arrangements supported by assets of separate accounts of the insurer are

[39] The Senate amendment provides that the term policy includes a contract.

available, whether there is a right under the policy to transfer funds to a separate account and the terms governing any such right, and the extent to which support by assets of the insurer's general account and support by assets of separate accounts of the insurer might pose differing risks to the plan; and (4) that the insurer must manage general account assets with the level of care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims, taking into account all obligations supported by such enterprise.

Under the Conference agreement, compliance by the insurer with all the requirements of the regulations issued by the Secretary of Labor will be deemed compliance by such insurer with ERISA's fiduciary duties, prohibited transactions, and limitations on holding employer securities and employer real property provisions (ERISA secs. 404, 406, and 407).

25. CHURCH PENSION PLAN SIMPLIFICATION

(Secs. 1462–1464 of the Senate amendment.)

Present law

In general, a church plan is a plan established and maintained for employees (or their beneficiaries) by a church or a church convention or association of churches that is exempt from tax (sec. 414(e)). Church plans include plans maintained by an organization, whether a corporation or otherwise, that has as its principal purpose or function the administration or funding of a plan or program for providing retirement or welfare benefits for the employees of the church or convention or association of churches. Employees of a church include any minister, regardless of the source of his or her compensation, and an employee of an organization which is exempt from tax and which is controlled by or associated with a church or a convention or association of churches.[40]

Plans maintained by churches and certain church-controlled organizations are exempt from certain of the requirements applicable to pension plans under the Code pursuant to the Employee Retirement Income Security Act of 1974 (as amended) ("ERISA"). For example, such plans are not subject to ERISA's vesting, coverage, and funding requirements. In some cases, such plans are subject to provisions in effect before the enactment of ERISA. Under the rules in effect before ERISA, a plan cannot discriminate in favor of officers, shareholders, persons whose principal duties consist in supervising the work of other employees, or highly compensated employees. Church plans may elect to waive the exemption from the qualification rules (sec. 410(d)). Electing plans become subject to all the tax Code (sec. 401(a)) qualification requirements, Title I of ERISA, the excise tax on prohibited transactions, and participation in the pension plan termination insurance program administered by the Pension Benefit Guaranty Corporation.

[40] With respect to certain provisions (e.g., the exemption for church plans from nondiscrimination requirements applicable to tax-sheltered annuities), the more limited definition of church under the employment tax rules applies (secs. 3121(w)(3) (A) and (B)).

Certain eligible employers may maintain tax-sheltered annuity plans (sec. 403(b)). These plans provide tax-deferred retirement savings for employees of public education institutions and employees of certain tax-exempt organizations (including churches and certain organizations associated with churches). In addition to tax-sheltered annuities, alternative funding mechanisms that provide similar tax benefits include church-maintained retirement income accounts (sec. 403(b)(9)).

For purposes of determining an employee's investment in the contract under the rules relating to taxation of annuities, amounts contributed by the employer are included as investment in the contract, but only to the extent that such amounts were includible in the gross income of the employee or, if such amounts had been paid directly to the employee, would not have been includible in income. However, amounts contributed by the employer which, if they had been paid directly to the employee, would have been excludable under section 911 are not treated as investment in the contract, except to the extent attributable to services performed before January 1, 1963.

House bill

No provision.

Senate amendment

The Senate amendment allows self-employed ministers to participate in a church plan. For purposes of the definition of a church plan, a self-employed minister is treated as his or her own employer and as if the employer were a tax-exempt organization under section 501(c)(3). The earned income of the self-employed minister is treated as his or her compensation. Self-employed ministers are able to deduct their contributions.

In addition, ministers employed by an organization other than a church are treated as if employed by a church. Thus, such ministers can also participate in a church plan.

The Senate amendment provides that if a minister is employed by an employer that is not eligible to maintain a church plan, the minister is not taken into account by that employer in applying nondiscrimination rules.

The Senate amendment permits retirement income accounts to be established for self-employed ministers.

The Senate amendment provides that church plans subject to the pre-ERISA nondiscrimination rules are to apply the same definition of highly compensated employee as other pension plans, rather than the pre-ERISA rule relating to employees who are officers, shareholders, persons whose principal duties consist of supervising the work of other employees or highly compensated employees.

The Senate amendment provides that the Secretary of the Treasury may develop safe harbor rules for church plans under the applicable coverage and nondiscrimination rules.

The Senate amendment provides that, in the case of foreign missionaries, amounts contributed to a plan by the employer are investment in the contract even though the amounts, if paid di-

rectly to the employee would have been excludable under section 911.

Effective date.—The provision is effective for years beginning after December 31, 1996.

Conference agreement

The conference agreement follows the Senate amendment with technical modifications.

26. INCREASE IN MULTIEMPLOYER PLAN BENEFITS GUARANTEED

(Sec. 1465 of the Senate amendment.)

Present law

The Pension Benefit Guaranty Corporation ("PBGC") guarantees benefits of workers under multiemployer plans. The monthly guarantee is equal to the participant's years of service multiplied by the sum of (1) 100 percent of the first $5 of the monthly benefit accrual rate, and (2) 75 percent of the next $15 of the accrual rate.

House bill

No provision.

Senate amendment

The Senate amendment generally adjusts the amount guaranteed under multiemployer plans to account for changes in the Social Security wage index since 1980. Under the Senate amendment, the monthly benefit guaranteed by the PBGC is generally increased to the participant's years of service multiplied by the sum of (1) 100 percent of the first $11 of the monthly benefit accrual rate, and (2) 75 percent of the next $33 of the accrual rate. The maximum annual guarantee for a retiree with 30 years of service is generally increased to $12,870.

The increase in guaranteed multiemployer plan benefits only applies in the case of multiemployer plans which first receive financial assistance from the PBGC during the applicable period. The applicable period is the period beginning on the date of enactment and ending on the last day of the first fiscal year in which the surplus in the PBGC's multiemployer insurance program is less than half of the surplus for the fiscal year ending September 30, 1995, as reflected in the Statement of Financial Condition in the PBGC's 1995 Annual Report. In determining the surplus in the multiemployer insurance program in any fiscal year, the PBGC is required to use the same actuarial assumptions that it used in determining the surplus for the fiscal year ending September 30, 1995. If the PBGC surplus declines by more than 50 percent, benefits of participants in multiemployer plans that first received financial assistance from the PBGC during the applicable period would continue to be guaranteed at the increased level; however, other benefits would be guaranteed at the present-law levels. The guaranteed benefit level would not automatically increase if the surplus increases.

Effective date.—The provision is effective on the date of enactment.

Conference agreement

The conference agreement does not include the Senate amendment provision.

27. WAIVER OF EXCISE TAX ON FAILURE TO PAY LIQUIDITY SHORTFALL

(Sec. 1466 of the Senate amendment.)

Present law

A provision in the Retirement Protection Act of 1994, enacted as part of the implementing legislation for the General Agreement on Tariffs and Trade ("GATT"), generally requires certain underfunded single-employer defined benefit plans to make quarterly contributions sufficient to maintain liquid plan assets, i.e., cash and marketable securities, at an amount approximately equal to three times the total trust disbursements for the preceding 12-month period. This liquidity requirement only applies to underfunded single-employer defined benefit plans (other than small plans)[41] that (1) are required to make quarterly installments of their estimated minimum funding contribution for the plan year, and (2) have a liquidity shortfall for any quarter during the plan year.

A plan has a liquidity shortfall if its liquid assets as of the last day of the quarter are less than the base amount for the quarter. Liquid assets are cash, marketable securities and such other assets as specified by the Secretary. The base amount for the quarter is an amount equal to the product of three times the adjusted disbursements from the plan for the 12 months ending on the last day of the last month preceding the quarterly installment due date. If the base amount exceeds the product of two times the sum of adjusted disbursements for the 36 months ending on the last day of the last month preceding the quarterly installment due date, and an enrolled actuary certifies to the satisfaction of the Secretary that the excess is the result of nonrecurring circumstances, such nonrecurring circumstances are not included in the base amount. For purposes of determining the base amount, adjusted disbursements mean the amount of all disbursements from the plan's trust, including purchases of annuities, payments of single sums, other benefit payments, and administrative expenses reduced by the product of the plan's funded current liability percentage for the plan year and the sum of the purchases of annuities, payments of single sums, and such other disbursements as the Secretary provides in regulations.

The amount of the required quarterly installment for defined benefit plans that have a liquidity shortfall for any quarter is the greater of the quarterly installment or the liquidity shortfall. The amount of the liquidity shortfall must be paid in the form of liquid assets. It may not be paid by the application of credit balances in the funding standard account. The amount of any liquidity shortfall payment when added to prior installments for the plan year cannot exceed the amount necessary to increase the funded current liability percentage of the plan to 100 percent taking into account the

[41] A plan is a small plan if it had 100 or fewer participants on each day during the plan year (as determined in Code sec. 412(l)(6)).

expected increase in current liability due to benefits accruing during the plan year.

If a liquidity shortfall payment is not made, then the plan sponsor is subject to a nondeductible excise tax equal to 10 percent of the amount of the outstanding liquidity shortfall. A liquidity shortfall payment is no longer considered outstanding on the earlier of (1) the last day of a later quarter for which the plan does not have a liquidity shortfall or (2) the date on which the liquidity shortfall for a later quarter is timely paid. If the liquidity shortfall remains outstanding after four quarters, the excise tax increases to 100 percent.

House bill

No provision.

Senate amendment

The Senate amendment gives the Secretary authority to waive all or part of the excise tax imposed for a failure to make a liquidity shortfall payment if the plan sponsor establishes to the satisfaction of the Secretary that the liquidity shortfall was due to reasonable cause and not willful neglect and reasonable steps have been taken to remedy such shortfall.

Effective date.—The provision is effective as if included in GATT.

Conference agreement

The conference agreement follows the Senate amendment.

28. TREATMENT OF MULTIEMPLOYER PLANS UNDER SECTION 415

(Sec. 1467 of the Senate amendment.)

Present law

Present law imposes limits on contributions and benefits under qualified plans based on the type of plan. In the case of defined benefit pension plans, the limit on the annual retirement benefit is the lesser of (1) 100 percent of compensation or (2) $120,000 (indexed for inflation). The dollar limit is reduced in the case of early retirement or if the employee has less than 10 years of plan participation.

House bill

No provision.

Senate amendment

The Senate amendment makes the following modifications to the limits on contributions and benefits as applied to multiemployer plans:

(1) the 100 percent of compensation limitation on defined benefit pension plan benefits does not apply; and

(2) the early retirement reduction and the 10-year phase-in of the defined benefit pension plan dollar limit does not apply to certain disability and survivor benefits.

Effective date.—The provision applies to multiemployer plans for years beginning after December 31, 1996.

Conference agreement

The conference agreement does not include the Senate amendment provision.

29. PAYMENT OF LUMP-SUM CREDIT FOR FORMER SPOUSES OF FEDERAL EMPLOYEES

(Sec. 1468 of the Senate amendment.)

Present law

When a Federal employee or former Federal employee dies, any contribution to his or her credit in the Civil Service Retirement and Disability Fund must be paid to whomever the employee designated to receive that contribution. If no designation was made, there is a statutory order of precedence beginning with the surviving spouse. There is no provision in law that permits a domestic relations order to interfere with these arrangements. Thus, if an employee agreed in a divorce settlement to designate a former spouse to receive these funds, and later designated another individual, present law would require payment of the funds to the other individual. By contrast, under present law, an employee's annuity and survivor benefits are subject to the provisions of a domestic relations order.

House bill

No provision.

Senate amendment

The payment of contributions to the employee's credit in the Civil Service Retirement and Disability Fund is subject to the provisions of a domestic relations order, in the same way as the employee's annuity and survivor benefits. Thus, a domestic relations order on file with the Office of Personnel Management supersedes any designation of beneficiary by the employee.

Effective date.—The provision is effective with respect to deaths occurring after the 90th day after the date of enactment.

Conference agreement

The conference agreement does not include the Senate amendment.

30. DATE FOR ADOPTION OF PLAN AMENDMENTS

(Sec. 1459 of the House bill and sec. 1469 of the Senate amendment.)

Present law

Plan amendments to reflect amendments to the law generally must be made by the time prescribed by law for filing the income tax return of the employer for the employer's taxable year in which the change in law occurs.

House bill

The House bill generally provides that any amendments to a plan or annuity contract required by the pension simplification

amendments would not be required to be made before the first plan year beginning on or after January 1, 1997. The date for amendments is extended to the first plan year beginning on or after January 1, 1999, in the case of a governmental plan.

Effective date.—The provision is effective on the date of enactment.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

Under the conference agreement, any amendments to a plan or annuity contract required by the pension simplification amendments would not be required to be made before the first plan year beginning on or after January 1, 1998. The date for amendments is extended to the first plan year beginning on or after January 1, 2000, in the case of a governmental plan.

Effective date.—The provision is effective on the date of enactment.

IV. FOREIGN SIMPLIFICATION PROVISION

1. REPEAL OF EXCESS PASSIVE ASSETS PROVISION

(Sec. 1501 of the House bill.)

Present law

Under the rules of subpart F (secs. 951–964), certain 10-percent U.S. shareholders of a controlled foreign corporation (CFC) are required to include in income currently for U.S. tax purposes certain earnings of the CFC, whether or not such earnings are actually distributed currently to the shareholders. The 10-percent U.S. shareholders of a CFC are subject to current U.S. tax on their shares of certain income earned by the CFC (referred to as "subpart F income"). The 10-percent U.S. shareholders are also subject to current U.S. tax on their shares of the CFC's earnings to the extent such earnings are invested by the CFC in certain U.S. property.

In addition to these current inclusion rules, the Omnibus Budget Reconciliation Act of 1993 enacted section 956A, which applies another current inclusion rule to U.S. shareholders of a CFC. Section 956A requires the 10-percent U.S. shareholder of a CFC to include in income currently their shares of the CFC's earnings to the extent such earnings are invested by the CFC in excess passive assets. A CFC generally is treated as having excess passive assets if the average of the amounts of its passive assets exceeds 25 percent of the average of the amounts of its total assets; this calculation requires a quarterly determination of the CFC's passive assets and total assets.

House bill

The House bill repeals section 956A.

Effective date.—The provision applies to taxable years of foreign corporations beginning after December 31, 1996, and taxable

years of U.S. shareholders with or within which such taxable years of foreign corporations end.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill.

V. OTHER PROVISIONS

1. EXEMPT ALASKA FROM DIESEL DYEING REQUIREMENT WHILE ALASKA IS EXEMPT FROM SIMILAR CLEAN AIR ACT DYEING REQUIREMENT

(Sec. 1801 of the Senate amendment.)

Present law

An excise tax totaling 24.3 cents per gallon is imposed on diesel fuel. In the case of fuel used in highway transportation, 20 cents per gallon is dedicated to the Highway Trust Fund. The remaining portion of this tax is imposed on transportation generally and is retained in the General Fund.

The diesel fuel tax is imposed on removal of the fuel from a pipeline or barge terminal facility (i.e., at the "terminal rack"). Present law provides that tax is imposed on all diesel fuel removed from terminal facilities unless the fuel is destined for a nontaxable use and is indelibly dyed pursuant to Treasury Department regulations.

In general, the diesel fuel tax does not apply to non-transportation uses of the fuel. A specific exemption is provided for off-highway business uses (e.g., use as fuel powering off-highway equipment). Use as heating oil also is exempt. (Most fuel commonly referred to as heating oil is diesel fuel.) The tax also does not apply to fuel used on a farm for farming purposes or by State and local governments, to exported fuels, and to fuel used in commercial shipping. Fuel used by intercity buses and trains is partially exempt from the diesel fuel tax.

A similar dyeing regime exists for diesel fuel under the Clean Air Act. That Act prohibits the use on highways of diesel fuel with a sulfur content exceeding prescribed levels. This "high sulfur" diesel fuel is required to be dyed by the EPA. The State of Alaska generally was exempted from the Clean Air Act, but not the excise tax, dyeing regime for three years (until October 1, 1996) (urban areas) or permanently (remote areas).

House bill

No provision.

Senate amendment

The Senate amendment provides that diesel fuel sold in the State of Alaska will be exempt from the diesel dyeing requirement during the period when that State is exempt from the Clean Air Act dyeing requirements. Thus, subject to a certification procedure to be developed by the Treasury Department, undyed diesel fuel which is destined for a nontaxable use may be removed from termi-

nals without payment of tax through September 30, 1996 (urban areas, unless extended by the Environmental Protection Agency) or permanently (remote areas).

Effective date.—Effective beginning with the first calendar quarter after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

2. APPLICATION OF COMMON PAYMASTER RULES TO CERTAIN AGENCY ACCOUNTS AT STATE UNIVERSITIES

(Sec. 1802 of the Senate amendment.)

Present law

In general, the OASDI portion of FICA taxes are payable with respect to employee remuneration not in excess of a contribution base. If an employee works for more than one employer during a year, these taxes are payable for each employer up to the contribution base. Under the common paymaster rule if an individual works for two or more related corporations, the remuneration may be treated as being from one employer and therefore taxable for one contribution base.

Section 125 of Social Security Amendments of 1983 provided a common paymaster rule for certain State universities that employ health care professionals as faculty members at a medical school and at a tax-exempt faculty practice plan. This rule does not explicitly apply to situations where compensation is made through a university agency account and not directly by a medical school faculty practice plan.

House bill

No provision.

Senate amendment

The Senate amendment establishes a common paymaster rule in cases where: (1) a State or State university provides remuneration pursuant to a single contract of employment to certain health care professionals as members of its medical school faculty; and (2) as agency account at such institution also provides remuneration to such health care professionals. The agency account must receive funds for the remuneration from a faculty practice plan described in section 501(c)(3) of the Code. The payments may only be distributed by the agency account to faculty members who render patient care at the medical school. The faculty members receiving payments must comprise at least 30 percent of the membership of the faculty practice plan.

Effective date.—Remuneration paid after December 31, 1996. It is intended that, with respect to years before the effective date, the Secretary apply present law in a manner consistent with the proposal.

Conference agreement

The conference agreement includes the Senate amendment provision.

3. MODIFICATIONS TO EXCISE TAX ON OZONE-DEPLETING CHEMICALS

a. Exempt imported recycled halons from the excise tax on ozone-depleting chemicals

(Sec. 1803(a) of the bill.)

Present law

An excise tax is imposed on the sale or use by the manufacturer or importer of certain ozone-depleting chemicals (Code sec. 4681). The amount of tax generally is determined by multiplying the base tax amount applicable for the calendar year by an ozone-depleting factor assigned to each taxable chemical. The base tax amount is $5.80 per pound in 1996 and will increase by 45 cents per pound per year thereafter. The ozone-depleting factors for taxable halons are 3 for halon-1211, 10 for halon-1301, and 6 for halon-2402.

Taxable chemicals that are recovered and recycled within the United States are exempt from tax.

House bill

No provision.

Senate amendment

The Senate amendment extends the exemption from tax for domestically recovered and recycled ozone-depleting chemicals to imported recycled halons. The exemption for imported recycled halons applies only to such chemicals imported from countries that are signatories to the Montreal Protocol on Substances that Deplete the Ozone Layer.

Effective date.—The provision is effective for chemicals imported after December 31, 1996.

Conference agreement

The conference agreement follows the Senate amendment with a modification to the effective date.

Effective date.—The provision is effective for halon-1301 and halon-2402 imported after December 31, 1996, and for halon-1211 imported after December 31, 1997.

b. Exempt chemicals used in metered-dose inhalers from the excise tax on ozone-depleting chemicals

(Sec. 1803(b) of the bill.)

Present law

An excise tax is imposed on the sale or use by the manufacturer or importer of certain ozone-depleting chemicals (Code sec. 4681). The amount of tax generally is determined by multiplying the base tax amount applicable for the calendar year by an ozone-depleting factor assigned to each taxable chemical. The base tax amount is $5.80 per pound in 1996 and will increase by 45 cents per pound per year thereafter.

A reduced rate of tax of $1.67 per pound applies to chemicals used as propellants in metered-dose inhalers (sec. 4682(g)(4)).

House bill

No provision.

Senate amendment

The Senate amendment exempts chemicals used as propellants in metered-dose inhalers from the excise tax on ozone-depleting chemicals.

Effective date.—The provision is effective for chemicals sold or used seven days after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

4. TAX-EXEMPT BONDS FOR THE SALE OF THE ALASKA POWER ADMINISTRATION FACILITY

(Sec. 1804 of the Senate amendment.)

Present law

Interest on State and local government bonds to provide financing to private parties (private activity bonds) is taxable unless an exception is provided in the Internal Revenue Code. One such exception relates to the financing of facilities for the furnishing of electricity and gas.

Most private activity bonds are subject to annual State volume limits of the greater of $50 per resident of the State or $150 million. Additionally, persons acquiring existing property financed with most private activity bonds must satisfy a rehabilitation requirement as a condition of the financing.

House bill

No provision.

Senate amendment

Provides an exception from the general rehabilitation requirement for private activity bonds used to acquire existing property for certain bonds to finance the acquisition of the Snettisham hydroelectric project for the Alaska Power Administration pursuant to legislation that has been enacted authorizing that transaction. These bonds are subject to the State of Alaska's private activity bond volume limit.

Effective date.—Bonds issued after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

5. ALLOW BANK COMMON TRUST FUNDS TO TRANSFER ASSETS TO REGULATED INVESTMENT COMPANIES WITHOUT TAXATION

(Sec. 1805 of the Senate amendment.)

Present law

Common trust funds

A common trust fund is a fund maintained by a bank exclusively for the collective investment and reinvestment of monies

contributed by the bank in its capacity as a trustee, executor, administrator, guardian, or custodian of certain accounts and in conformity with rules and regulations of the Board of Governors of the Federal Reserve System or the Comptroller of the Currency pertaining to the collective investment of trust funds by national banks (sec. 584(a)).

The common trust fund is not subject to tax and is not treated as a corporation (sec. 584(b)). Each participant in a common trust fund includes his proportional share of common trust fund income, whether or not the income is distributed or distributable (sec. 584(c)).

No gain or loss is realized by the fund upon admission or withdrawal of a participant. Participants generally treat their admission to the fund as the purchase of an interest. Withdrawals from the fund generally are treated as the sale of an interest by the participant (sec. 584(e)).

Regulated investment companies ("RICs")

A RIC also is treated as a conduit for Federal income tax purposes. Conduit treatment is accorded by allowing the RIC a deduction for dividend distributions to its shareholders. Present law is unclear as to the tax consequences when a common trust fund transfers its assets to one or more RICs.

House bill

No provision.

Senate amendment

In general, the Senate amendment permits a common trust fund to transfer substantially all of its assets to one or more RICs without gain or loss being recognized by the fund or its participants. The fund must transfer its assets to the RICs solely in exchange for shares of the RICs, and the fund must then distribute the RIC shares to the fund's participants in exchange for the participants' interests in the fund.

The basis of any asset received by a RIC will be the basis of the asset in the hands of the fund prior to transfer (increased by the amount of gain recognized by reason of the rule regarding the assumption of liabilities). In addition, the basis of any RIC shares that are received by a fund participant will be an allocable portion of the participant's basis in the interests exchanged. If stock in more than one RIC is received in exchange for assets of a common trust fund, the basis of the shares in each RIC shall be determined by allocating the basis of common fund assets used in the exchange among the shares of each RIC received in the exchange on the basis of the respective fair market values of the RICs.

The tax-free transfer is not available to a common trust fund with assets that are not diversified under the requirements of section 368(a)(2)(F)(ii), except that the diversification test is modified so that Government securities are not to be included as securities of an issuer and are to be included in determining total assets for purposes of the 25- and 50-percent tests.

Effective date.—The provision is effective for transfers after December 31, 1995.

Conference agreement

The conference agreement follows the Senate amendment. In order to qualify for the provision, the transfer by the common trust fund to the RIC must occur after December 31, 1995. The conferees intend that there is no requirement for qualification that the transfer of assets by the common trust fund to one or more RICs and the distribution of RIC shares to participants in the common trust fund be made contemporaneously or pursuant to a single plan.

6. TREATMENT OF QUALIFIED STATE TUITION PROGRAMS

(Sec. 1806 of the Senate amendment.)

Present law

In *Michigan* v. *United States,* 40 F.3d 817 (6th Cir. 1994), the Sixth Circuit held that the Michigan Education Trust, an entity created by the State of Michigan to operate a prepaid tuition payment program, is an integral part of the State, and, thus, the investment income realized by the Trust is not currently subject to Federal income tax. The Trust was established to receive advance payments of college tuition, invest the money, and ultimately make disbursements under a program that allows beneficiaries to attend any of the State's public colleges or universities without further tuition costs for a year or more (depending on the terms of the contract).

Section 115 of the Code provides that gross income does not include income derived from any public utility or the exercise of any essential governmental function and accruing to a State or any political subdivision thereof, or the District of Columbia.

Section 2501 imposes a Federal gift tax on certain transfers of property by gift. Section 2503(e) specifically excludes from gifts subject to tax under section 2501 any "qualified transfer," which includes any amount paid on behalf of an individual as tuition to an educational institution (as described in sec. 170(b)(1)(A)(ii)) for the education or training of such individual.

On June 11, 1996, the Treasury Department issued final regulations under the original issue discount ("OID") provisions of the Code (secs. 163(e) and 1271 through 1275), including regulations relating to debt instruments that provide for contingent payments (see TD 8674). These regulations specifically provide that they do not apply to contracts issued pursuant to State-sponsored prepaid tuition programs, whether or not the contracts are debt instruments. In addition, the IRS announced in Rev. Proc. 96–34 that it will not issue advance rulings or determination letters regarding State-sponsored prepaid tuition plans because issues that arise under such plans are being studied.

House bill

No provision.

Senate amendment

The Senate amendment provides tax-exempt status to "qualified State tuition programs," meaning programs established and maintained by a State (or agency or instrumentality thereof) under

which persons may (1) purchase tuition credits or certificates on behalf of a designated beneficiary that entitle the beneficiary to a waiver or payment of qualified higher education expenses of the beneficiary, or (2) make contributions to an account that is established for the sole purpose of meeting qualified higher education expenses of the designated beneficiary of the account. "Qualified higher education expenses" are defined as tuition, fees, books, and equipment required for enrollment or attendance at a college or university (or certain vocational schools). The Senate amendment specifically provides that, although a qualified State tuition program generally is exempt from Federal income tax, such a program is subject to the unrelated business income tax (UBIT).[42]

A qualified State tuition program is required to provide that purchases or contributions only be made in cash. Contributors and beneficiaries are not allowed to direct any investments made on their behalf by the program. The program is required to maintain a separate accounting for each designated beneficiary. A specified individual must be designated as the beneficiary at the commencement of participation in a qualified State tuition program (i.e., when contributions are first made to purchase an interest in such a program[43]), unless interests in such a program are purchased by a State or local government or a tax-exempt charity described in section 501(c)(3) as part of a scholarship program operated by such government or charity under which beneficiaries to be named in the future will receive such interests as scholarships. A transfer of credits (or other amounts) from one account benefiting one designated beneficiary to another account benefiting a different beneficiary will be considered a distribution (as will a change in the designated beneficiary of an interest in a qualified State tuition program) unless the beneficiaries are members of the same family.[44] Earnings on an account may be refunded to a contributor or beneficiary, but the State or instrumentality must impose a more than de minimis monetary penalty unless the refund is (1) used for qualified higher education expenses of the beneficiary, (2) made on account of the death or disability of the beneficiary,[45] or (3) made on account of a scholarship received by the designated beneficiary to the extent the amount refunded does not exceed the amount of the scholarship used for higher education expenses. A qualified State tuition program may not allow any interest in the program or any portion thereof to be used as security for a loan.

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[42] The bill specifically provides that an interest in a qualified State tuition program will not be treated as debt for purposes of the UBIT debt-financed property rules (sec. 514). Consequently, a qualified State tuition program's investment income will not constitute debt-financed property income subject to the UBIT merely because the program accepts contributions and is obligated to pay out (or refund) such contributions and certain earnings thereon to designated beneficiaries or to contributors. However, investment income of a qualified State tuition program could be subject to the UBIT as debt-financed property income to the extent the program acquires indebtedness when investing the contributions made on behalf of designated beneficiaries.

[43] The bill allows for a change in designated beneficiaries, so long as the new beneficiary is a member of the family of the old beneficiary.

[44] For this purpose, the term "member of the family" is defined under present-law section 2032A(e)(2).

[45] Thus, a State need not impose a monetary penalty when a refund is made from a qualified State tuition program in order to cover medical expenses incurred by (or on behalf of) a designated beneficiary who suffers a disabling illness (and who could be any member of the same family of the originally designated beneficiary).

In addition, the Senate amendment provides that no amount shall be included in the gross income of a contributor to, or beneficiary of, a qualified State tuition program with respect to any distribution from, or earnings under, such program, except that (1) amounts distributed or educational benefits provided to a beneficiary (e.g., when the beneficiary attends college) will be included in the beneficiary's gross income (unless excludable under another Code section) to the extent such amount or the value of the educational benefits exceeds contributions made on behalf of the beneficiary, and (2) amounts distributed to a contributor (e.g., when a parent or other relative receives a refund) will be included in the contributor's gross income to the extent such amounts exceed contributions made by that person.[46]

The Senate amendment further provides that, for purposes of present-law section 2503(e), contributions made by an individual to a qualified State tuition program are treated as a qualified transfer and, thus, not subject to Federal gift tax.

Effective date.—The provision is effective for taxable years ending after the date of enactment. The bill also includes a transition rule providing that if (1) a State maintains (on the date of enactment) a program under which persons may purchase tuition credits on behalf of, or make contributions for educational expenses of, a designated beneficiary, and (2) such program meets the requirements of a qualified State tuition program before the later of (a) one year after the date of enactment, or (b) the first day of the first calendar quarter after the close of the first regular session of the State legislature that begins after the date of enactment, then the provisions of the bill will apply to contributions (and earnings allocable thereto) made before the date the program meets the requirements of a qualified State tuition program, without regard to whether the requirements of a qualified State tuition program are satisfied with respect to such contributions and earnings (e.g., even if the interest in the tuition or educational savings program covers not only qualified higher education expenses but also room and board expenses).

Conference agreement

The conference agreement generally follows the Senate amendment, with the following modifications:

(1) A program will not be treated as a qualified State tuition program unless it provides adequate safeguards to prevent contributions on behalf of a designated beneficiary in excess of those necessary to provide for the qualified higher education expenses of the beneficiary.

(2) Contributions made to a qualified State tuition program will be treated as incomplete gifts for Federal gift tax purposes. Thus, any Federal gift tax consequences will be determined at the time that a distribution is made from an account under the program.

[46] Specifically, the bill provides that any distribution under a qualified State tuition program shall be includible in the gross income of the distributee in the same manner as provided under present-law section 72 to the extent not excluded from gross income under any other provision of the Code.

(3) The waiver (or payment) of qualified higher education expenses of a designated beneficiary by (or to) an educational institution under a qualified State tuition program will be treated as a qualified transfer for purposes of present-law section 2503(e).[47]

(4) Amounts contributed to a qualified State tuition program (and earnings thereon) will be included in the contributor's estate for Federal estate tax purposes in the event that the contributor dies before such amounts are distributed under the program.

The conference agreement provides that any distribution under a qualified State tuition program shall be includible in the gross income of the distributee in the manner as provided under section 72 to the extent not excluded from gross income under any other provision of the Internal Revenue Code. Thus, the conferees understand that if matching-grant amounts are distributed to (or on behalf of) a beneficiary as part of a qualified State tuition program, then such matching-grant amounts still may be excluded from the gross income of the beneficiary as a scholarship under present-law section 117.

Effective date.—The conference agreement follows the Senate amendment.

7. ADOPTION ASSISTANCE

(Sec. 101 of H.R. 3286.)

Present law

Present law does not provide a tax credit for adoption expenses. Also, present law does not provide an exclusion from gross income for employer-provided adoption assistance. The Federal Adoption Assistance program (a Federal outlay program) provides financial assistance for the adoption of certain special needs children. In general, a special needs child is defined as a child who (1) according to a State determination, could not or should not be returned to the home of the birth parents and (2) on account of a specific factor or condition (such as ethnic background, age, membership in a minority or sibling group, medical condition, or physical, mental or emotional handicap), could not reasonably be expected to be adopted unless adoption assistance is provided. Specifically, the program provides assistance for adoption expenses for those special needs children receiving Federally assisted adoption assistance payments as well as special needs children in private and State-funded programs. The maximum Federal reimbursement is $1,000 per special needs child. Reimbursable expenses include those nonrecurring costs directly associated with the adoption process such as legal costs, social service review, and transportation costs.

[47] In this regard, the conferees intend that if a qualified State tuition program issues a check in the names of both the designated beneficiary and an educational institution at which the beneficiary incurs (or will incur) qualified higher education expenses, then the issuance of the check will be considered a payment of qualified higher education expenses to an educational institution if the check (after endorsement by the beneficiary) is deposited in the institution's bank account.

House bill

Tax credit

No provision. However, H.R. 3286 provides taxpayers with a maximum nonrefundable credit against income tax liability of $5,000 per child for qualified adoption expenses paid or incurred by the taxpayer. Any unused adoption credit may be carried forward by the taxpayer for up to five years. Qualified adoption expenses are reasonable and necessary adoption fees, court costs, attorneys' fees and other expenses that are directly related to the legal adoption of an eligible child. In the case of an international adoption, the credit is not available unless the adoption is finalized. An eligible child is an individual (1) who has not attained age 18 as of the time of the adoption, or (2) who is physically or mentally incapable of caring for himself or herself. No credit is allowed for expenses incurred (1) in violation of State or Federal law, (2) in carrying out any surrogate parenting arrangement, or (3) in connection with the adoption of a child of the taxpayer's spouse. The credit is phased out ratably for taxpayers with modified adjusted gross income (AGI) above $75,000, and is fully phased out at $115,000 of modified AGI.

The credit is not allowed for any expenses for which a grant is received under any Federal, State, or local program. This limit, however, does not apply in the case of special needs adoptions.

Exclusion from income

The proposal provides a maximum $5,000 exclusion from the gross income of an employee for specified certain adoption expenses paid by the employer. The $5,000 limit is a per child limit, not an annual limitation. The exclusion is phased out ratably for taxpayers with modified AGI above $75,000 and is fully phased out at $115,000 of modified AGI.

No credit is allowed for adoption expenses paid or reimbursed under an adoption assistance program.

Effective date

The House bill is effective for taxable years beginning after December 31, 1996.

Senate amendment

Tax credit

The Senate amendment to H.R. 3286 is the same as the House bill, with three changes:

(1) The maximum credit is increased from $5,000 to $6,000 in the case of special needs adoptions.

(2) The credit for non-special needs adoptions is repealed for expenses paid or incurred after December 31, 2000.

(3) No credit is allowed in the case of special needs adoptions for expenses for which a grant is received under any Federal, State or local program.

Exclusion from income

The Senate amendment to H.R. 3286 is the same as the House bill except:

(1) The maximum exclusion is increased from $5,000 to $6,000 in the case of special needs adoptions.

(2) The exclusion is repealed after December 31, 2000.

Effective date

The Senate amendment to H.R. 3286 is the same as the House bill.

Conference agreement

Tax credit

The conference agreement follows the Senate amendment provision of H.R. 3286 with four modifications:

(1) The repeal of the credit for non-special needs adoptions is delayed for one year. Therefore, the credit for non-special needs adoptions is not available for expenses paid or incurred after December 31, 2001.

(2) Special needs foreign adoptions are limited to a maximum credit of $5,000 (rather than $6,000) for qualified adoption expenses until December 31, 2001, at which time the credit for special needs foreign adoptions is also repealed.

(3) The taxpayer is required to provide available information about the name, age, and taxpayer identification number of each adopted child.

(4) Otherwise, qualified adoption expenses paid in one taxable year are not taken into account for purposes of the credit until the next taxable year unless the expenses are incurred in the year the adoption becomes final.

Exclusion from income

The conference agreement follows the Senate amendment provision of H.R. 3286 with three modifications:

(1) The repeal of the exclusion is delayed for one year. Therefore, the exclusion is not available for expenses paid or incurred after December 31, 2001.

(2) Special needs foreign adoptions are limited to a maximum exclusion of $5,000 (rather than $6,000) for qualified adoption expenses until December 31, 2001, at which time the exclusion is repealed.

(3) The taxpayer is required to provide available information about the name, age, and taxpayer identification number of each adopted child.

Taxpayer identification numbers

The conference committee is concerned that problems may arise in processing tax returns of adopting parents because of unavoidable delays involved in obtaining a social security number of a child who is being adopted. The conference understands that the Internal Revenue Service recognizes these concerns and is committed to working with the Congress to develop as soon as possible an administrative solution that minimizes the burdens imposed on

adopting parents while balancing processing and potential compliance considerations.

Effective date

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

The conferees wish to clarify the operation of the effective date by way of an example. Suppose that, in the course of attempting to adopt a child, a taxpayer incurs $1,000 in qualified adoption expenses in November, 1996, and an additional $3,000 in qualified adoption expenses in February, 1997, when the adoption becomes final. The taxpayer is entitled to claim a credit for tax year 1997 only with respect to the $3,000 of qualified adoption expenses in February, 1997. The taxpayer is never entitled to claim a credit with respect to the $1,000 in qualified adoption expenses in November, 1996, because those expenses were incurred prior to the effective date of this provision.

8. SIX-MONTH DELAY IN IMPLEMENTATION OF ELECTRONIC FUND TRANSFER SYSTEM FOR COLLECTION OF CERTAIN TAXES

Present law

Employers are required to withhold income taxes and FICA taxes from wages paid to their employees. Employers also are liable for their portion of FICA taxes, excise taxes, and estimated payments of their corporate income tax liability.

The Code requires the development and implementation of an electronic fund transfer system to remit these taxes and convey deposit information directly to the Treasury (Code sec. 6302(h)). The Electronic Federal Tax Payment System ("EFTPS") was developed by Treasury in response to this requirement.[48] Employers must enroll with one of two private contractors hired by the Treasury. After enrollment, employers generally initiate deposits either by telephone or by computer.

The new system is phased in over a period of years by increasing each year the percentage of total taxes subject to the new EFTPS system. For fiscal year 1994, 3 percent of the total taxes are required to be made by electronic fund transfer. These percentages increased gradually for fiscal years 1995 and 1996. For fiscal year 1996, the percentage was 20.1 percent (30 percent for excise taxes and corporate estimated tax payments). For fiscal year 1997, these percentages increased significantly, to 58.3 percent (60 percent for excise taxes and corporate estimated tax payments). The specific implementation method required to achieve the target percentages is set forth in Treasury regulations. Implementation began with the largest depositors. Treasury has implemented the 1997 percentages by requiring that all employers who deposit more than $50,000 in 1995 must begin using EFTPS by January 1, 1997.

House bill

No provision.

[48] Treasury had earlier developed TAXLINK as the prototype for EFTPS. TAXLINK has been operational for several years; EFTPS is currently becoming operational. Employers currently using TAXLINK will ultimately be required to participate in EFTPS.

Senate amendment

No provision.

Conference agreement

The conferees are concerned that the initial mailing by IRS to employers that informed them of the 1997 requirements confused many of these employers. The conferees believe that it is necessary to provide additional time prior to implementation of the 1997 requirements so that employers may be better informed about their responsibilities. Accordingly, the conference agreement provides that the increase in the required percentages for fiscal year 1997 (which, pursuant to Treasury regulations, was to take effect on January 1, 1997) shall not take effect until July 1, 1997.

Effective date.—The provision is effective on the date of enactment.

VI. REVENUE OFFSETS

1. MODIFICATIONS OF THE PUERTO RICO AND POSSESSION TAX CREDIT

(Sec. 1601 of the bill and the Senate amendment.)

Present law

Certain domestic corporations with business operations in the U.S. possessions (including, for this purpose, Puerto Rico and the U.S. Virgin Islands) may elect the Puerto Rico and possession tax credit which generally eliminates the U.S. tax on certain income related to their operations in the possessions. In contrast to the foreign tax credit, the Puerto Rico and possession tax credit is a "tax sparing" credit. That is, the credit is granted whether or not the electing corporation pays income tax to the possession. Income eligible for the credit under this provision falls into two broad categories: (1) possession business income, which is derived from the active conduct of a trade or business within a U.S. possession or from the sale or exchange of substantially all of the assets that were used in such a trade or business; and (2) qualified possession source investment income ("QPSII"), which is attributable to the investment in the possession or in certain Caribbean Basin countries of funds derived from the active conduct of a possession business.

In order to qualify for the Puerto Rico and possession tax credit for a taxable year, a domestic corporation must satisfy two conditions. First, the corporation must derive at least 80 percent of its gross income for the three-year period immediately preceding the close of the taxable year from sources within a possession. Second, the corporation must derive at least 75 percent of its gross income for that same period from the active conduct of a possession business.

A domestic corporation that has elected the Puerto Rico and possession tax credit and that satisfies these two conditions for a taxable year generally is entitled to a credit based on the U.S. tax attributable to the sum of the taxpayer's possession business income and its QPSII. However, the amount of the credit attributable to possession business income is subject to the limitations enacted by the Omnibus Budget Reconciliation Act of 1993. Under the economic activity limit, the amount of the credit with respect to such

income cannot exceed an amount equal to the sum of (i) 60 percent of the taxpayer's qualifying wage and fringe benefit expenses, (ii) specified percentages of the taxpayer's depreciation allowances with respect to qualifying tangible property, and (iii) in certain cases, the taxpayer's qualifying possession income taxes. The credit calculated under the economic activity limit is referred to herein as the "wage credit." In the alternative, the taxpayer may elect to apply a limit equal to the applicable percentage of the credit that would otherwise be allowable with respect to possession business income; the applicable percentage is phased down to 50 percent for 1995, 45 percent for 1997, and 40 percent for 1998 and thereafter. The credit calculated under the applicable percentage limit is referred to herein as the "income credit." The amount of the Puerto Rico and possession tax

House bill

In general.—The House bill generally repeals the Puerto Rico and possession tax credit for taxable years beginning after December 31, 1995. However, the House bill provides grandfather rules under which a corporation that is an existing credit claimant would be eligible to claim credits for a transition period. A special transition rule applies to the credit attributable to operations in Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.

For taxable years beginning after December 31, 1995, the Puerto Rico and possession tax credit applies only to a corporation that qualifies as an existing credit claimant (as defined below). The determination of whether a corporation is an existing credit claimant is made separately for each possession. A corporation that is an existing credit claimant with respect to a possession is entitled to the credit for income from such possession for taxable years beginning after December 31, 1995, subject to the limitations described below. The credit, subject to such limitations, is computed separately for each possession with respect to which the corporation is an existing credit claimant.

The Puerto Rico and possession tax credit attributable to QPSII is eliminated for taxable years beginning after December 31, 1995. For taxable years beginning after December 31, 1995, the Puerto Rico and possession tax credit is available only with respect to possession business income. The computation of the Puerto Rico and possession tax credit attributable to possession business income during the grandfather period depends upon whether the corporation is using the economic activity limit or the applicable percentage limit.

Wage credit.—For corporations that are existing credit claimants with respect to a possession and that use the wage credit method, the possession tax credit attributable to business income from the possession (determined under the wage credit method) continues to be determined as under present law for taxable years beginning after December 31, 1995 and before January 1, 2002. For taxable years beginning after December 31, 2001 and before January 1, 2006, the corporation's possession business income that is eligible for the wage credit is subject to a cap computed as described below. For taxable years beginning in 2006 and thereafter, the

credit attributable to possession business income (determined under the wage credit method) is eliminated.

The House bill adds to the Code a new section which provides a credit determined under the wage credit method for business income from Puerto Rico. Such credit is computed under the rules described above with respect to the possession tax credit determined under the wage credit method. Such section applies for taxable years beginning after December 31, 1995 and before January 1, 2006.

Income credit.—For corporations that are existing credit claimants with respect to a possession and that elected to use the income credit method and not to use the wage credit method, the Puerto Rico and possession tax credit attributable to business income from the possession continues to be determined as under present law for taxable years beginning after December 31, 1995 and before January 1, 1998. For taxable years beginning after December 31, 1997 and before January 1, 2006, the corporation's possession business income tax that is eligible for the credit is subject to a cap computed as described below. For taxable years beginning in 2006 and thereafter, the credit attributable to possession business income (determined under the income credit method) is eliminated.

A corporation that had elected to use the income credit method is permitted to revoke that election under present law. Under the House bill, such a revocation is required to be made not later than with respect to the first taxable year beginning after December 31, 1996; such revocation, if made, applies to such taxable year and to all subsequent taxable years. Accordingly, a corporation that had an election in effect to use the income credit method could revoke such election effective for its taxable year beginning in 1997 and thereafter; such corporation would continue to use the income credit method for its taxable year beginning in 1996 and would use the wage credit method for its taxable year beginning in 1997 and thereafter.

Computation of income cap.—The cap on a corporation's possession business income that is eligible for the Puerto Rico and possession tax credit is computed based on the corporation's possession business income for the base period years ("average adjusted base period possession business income"). Average adjusted base period possession business income is the average of the adjusted possession business income for each of the corporation's base period years. For the purpose of this computation, the corporation's possession business income for a base period year is adjusted by an inflation factor that reflects inflation from such year to 1995. In addition, as a proxy for real growth in income throughout the base period, the inflation factor is increased by 5 percentage points compounded for each year from such year to the corporation's first taxable year beginning on or after October 14, 1995.

The corporation's base period years generally are three of the corporation's five most recent years ending before October 14, 1995, determined by disregarding the taxable years in which the adjusted possession business incomes were highest and lowest. For purposes of this computation, only years in which the corporation had significant possession business income are taken into account. A cor-

poration is considered to have significant possession business income for a taxable year if such income exceeds two percent of the corporation's possession business income for each of the six taxable years ending with the first taxable year ending on or after October 14, 1995. If the corporation has significant possession business income for only four of the five most recent taxable years ending before October 14, 1995, the base period years are determined by disregarding the year in which the corporation's possession business income was lowest. If the corporation has significant possession business income for three years or fewer of such five years, then the base period years are all such years. If there is no year of such five taxable years in which the corporation has significant possession business income, then the corporation is permitted to use as its base period its first taxable year ending on or after October 14, 1995; for this purpose, the amount of possession business income taken into account is the annualized amount of such income for the portion of the year ended September 30, 1995.

As one alternative, the corporation may elect to use its taxable year ending in 1992 as its base period (with the adjusted possession business income for such year constituting its cap). As another alternative, the corporation may elect to use as its cap the annualized amount of its possession business income for the first ten months of calendar year 1995, calculated by excluding any extraordinary items (as determined under generally accepted accounting principles) for such period. For this purpose, it is intended that transactions with a related party that are not in the ordinary course of business will be considered to be extraordinary items.

If a corporation's possession business income in a year for which the cap is applicable exceeds the cap, then the corporation's possession business income for purposes of computing its Puerto Rico and possession tax credit for the year is an amount equal to the cap. The corporation's credit continues to be subject to either the economic activity limit or the applicable percentage limit, with such limit applied to the corporation's possession business income as reduced to reflect the application of the cap.

Qualification as existing credit claimant.—A corporation is an existing credit claimant with respect to a possession if (1) the corporation is engaged in the active conduct of a trade or business within the possession on October 13, 1995, and (2) the corporation has elected the benefits of the Puerto Rico and possession tax credit pursuant to an election which is in effect for its taxable year that includes October 13, 1995. A corporation that adds a substantial new line of business after October 13, 1995, ceases to be an existing credit claimant as of the beginning of the taxable year during which such new line of business is added.

For purposes of these rules, a corporation is treated as engaged in the active conduct of a trade or business within a possession on October 13, 1995, if such corporation is engaged in the active conduct of such trade or business before January 1, 1996, and such corporation has in effect on October 13, 1995, a binding contract for the acquisition of assets to be used in, or the sale of property to be produced in, such trade or business. For example, if a corporation has in effect on October 13, 1995, binding contracts for the lease of a facility and the purchase of machinery to be used in

manufacturing business in a possession and if the corporation begins actively conducting that manufacturing business in the possession before January 1, 1996, that corporation would be an existing credit claimant. A change in the ownership of a corporation will not affect its status as an existing credit claimant.

In determining whether a corporation has added a substantial new line of business, the Committee intends that principles similar to those reflected in Treas. Reg. section 1.7704–2(d) (relating to the transition rules for existing publicly traded partnerships) apply. For example, a corporation that modifies its current production methods, expands existing facilities, or adds new facilities to support the production of its current product lines and products within the same four-digit Industry Number Standard Industrial Classification Code (Industry SIC Code) will not be considered to have added a substantial new line of business. In this regard, the Committee intends that the fact that a business which is added is assigned a different four-digit Industry SIC Code than is assigned to an existing business of the corporation will not automatically cause the corporation to be considered to have added a new line of business. For example, a pharmaceutical corporation that begins manufacturing a new drug will not be considered to have added a new line of business. Moreover, a pharmaceutical corporation that begins to manufacture a complete product from the bulk active chemical through the finished dosage form, a process that may be assigned two separate four-digit Industry SIC Codes, will not be considered to have added a new line of business even though it was previously engaged in activities that involved only a portion of the entire manufacturing process from bulk chemicals to finished dosages. The Committee further intends that, in the case of a merger of affiliated possession corporations that are existing credit claimants, the corporation that survives the merger will not be considered to have added a substantial new line of business by reason of its operation of the existing business of the affiliate that was merged into it.

Special rules for certain possessions.—A special transition rule applies to the Puerto Rico and possession tax credit with respect to operations in Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands. For any taxable year beginning after December 31, 1995, and before January 1, 2006, a corporation that is an existing credit claimant with respect to one of these possessions for such year continues to determine its credit with respect to operations in such possession as under present law. For taxable years beginning in 2006 and thereafter, the Puerto Rico and possession tax credit with respect to operations in Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands is eliminated.

Effective date.—The House bill is effective for taxable years beginning after December 31, 1995.

Senate amendment

The Senate amendment is the same as the House bill with three modifications.

Under the Senate amendment, the Puerto Rico and possession tax credit attributable to QPSII continues to be allowed for QPSII earned before July 1, 1996.

Under the Senate amendment, a corporation that is an existing credit claimant continues to be eligible to claim credits under the wage credit method for taxable years beginning after December 31, 2005. For taxable years beginning in 2006 and thereafter, in computing the economic activity limit on the wage credit, the percentage of the corporation's qualifying wage and fringe benefit expenses that is taken into account is reduced from 60 percent of 40 percent. The corporation's business income that is eligible for the wage credit continues to be subject to the income cap. For taxable years beginning in 2006 and thereafter, a corporation that is an existing credit claimant with respect to Guam, American Samoa, or the Commonwealth of the Northern Mariana Islands continues to be eligible to claim credits under the wage credit method, determined under the foregoing rules, with respect to its operations in such possession.

Under the Senate amendment, the Treasury Department is directed to study the effect on the economy of Puerto Rico of the wage credit (under present law and as amended), including an analysis of the impact of such credit on unemployment rates and economic growth. The Treasury Department is directed to submit to the House Committee on Ways and Means and the Senate Committee on Finance reports on its findings with respect to the impact of the wage credit within two years of the date of enactment and every four years thereafter.

Effective date.—Same as the House bill.

Conference agreement

The conference agreement follows the House bill with modifications.

Under the conference agreement, as under the Senate amendment, the Puerto Rico and possession tax credit attributable to QPSII continues to be allowed for QPSII earned before July 1, 1996. The conferees note that the repeal of the credit for QPSII will have the effect of eliminating a provision that has supported economic development and trade-related growth in the Caribbean Basin and served U.S. interests in the region. The loss of this program should not be interpreted as a loss of U.S. interest in the region. The conferees continue to support efforts furthering stable commercial and economic relations in that region.

Under the conference agreement, a corporation that acquires all the assets of a trade or business of an existing credit claimant will qualify as an existing credit claimant. The adjusted base period income of the existing credit claimant from which the assets are acquired is divided between such corporation and the corporation that acquires such assets. It is intended that regulations or other guidance will prevent taxpayers from abusing this rule through transactions that manipulate base period income amounts.

Under the conference agreement, for purposes of estimated tax payments due before October 1, 1996, a taxpayer whose tax liability is increased by reason of the modifications of the Puerto Rico and possession tax credit is not required to make a deposit with re-

spect to more than 50 percent of such increase; any amount not deposited by such date will be required to be deposited, without penalty or interest, on the next estimated tax payment due date.

2. REPEAL 50-PERCENT INTEREST INCOME EXCLUSION FOR FINANCIAL INSTITUTION LOANS TO ESOP'S

(Sec. 1602 of the House bill and the Senate amendment.)

Present law

A bank, insurance company, regulated investment company, or a corporation actively engaged in the business of lending money may generally exclude from gross income 50 percent of interest received on an ESOP loan (sec. 133). The 50-percent interest exclusion only applies if: (1) immediately after the acquisition of securities with the loan proceeds, the ESOP owns more than 50 percent of the outstanding stock or more than 50 percent of the total value of all outstanding stock of the corporation; (2) the ESOP loan term will not exceed 15 years; and (3) the ESOP provides for full pass-through voting to participants on all allocated shares acquired or transferred in connection with the loan.

House bill

The provision repeals the 50-percent interest exclusion with respect to ESOP's.

Effective date.—The provision generally is effective with respect to loans made after October 13, 1995. The repeal of the exclusion does not apply to the refinancing of an ESOP loan originally made on or before October 13, 1995, provided: (1) such refinancing loan otherwise meets the requirements of section 133 in effect on or before October 13, 1993; (2) the outstanding principal amount of the loan is not increased; and (3) the term of the refinancing loan does not extend beyond the term of the original ESOP loan.

Senate amendment

Same as the House bill.

Effective date.—The provision is effective with respect to loans made after the date of enactment, other than loans made pursuant to a written binding contract in effect before June 10, 1996, and at all times thereafter before such loan is made. The repeal of the 50-percent interest exclusion does not apply to the refinancing of an ESOP loan originally made on or before the date of enactment or pursuant to a binding contract in effect before June 10, 1996, provided: (1) such refinancing loan otherwise meets the requirements of section 133 in effect on the day before the date of enactment; (2) the outstanding principal amount of the loan is not increased; and (3) the term of the refinancing loan does not extend beyond the term of the original ESOP loan.

Conference agreement

The conference agreement follows the Senate amendment.

3. APPLY LOOK-THROUGH RULE FOR PURPOSES OF CHARACTERIZING CERTAIN SUBPART F INSURANCE INCOME AS UNRELATED BUSINESS TAXABLE INCOME

(Sec. 1602 of the House bill.)

Present law

An organization that is exempt from tax by reason of Code section 501(a) (e.g., a charity, business league, or qualified pension trust) is nonetheless subject to tax on its unrelated business taxable income (UBTI) (sec. 511). Unrelated business taxable income generally excludes dividend income (sec. 512(b)(1)).

Special rules apply to a tax-exempt organization described in section 501(c)(3) or (c)(4) (i.e., a charity or social welfare or organization) that is engaged in commercial-type insurance activities. Such activities are treated as an unrelated trade or business and the tax-exempt organization is subject to tax on the income from such insurance activities (including investment income that might otherwise be excluded from the definition of unrelated business taxable income) under subchapter L (sec. 501(m)(2)).[49] Accordingly, a tax-exempt organization described in section 501(c)(3) or (c)(4) generally is subject to tax on its income from commercial-type insurance activities in the same manner as a taxable insurance company.

A tax-exempt organization that conducts insurance activities through a foreign corporation is not subject to U.S. tax with respect to such activities. Under the subpart F rules, the United States shareholders (as defined in sec. 951(b)) of a controlled foreign corporation (CFC) are required to include in income currently their shares of certain income of the CFC, whether or not such income is actually distributed to the shareholders. This current inclusion rule applies to certain insurance income of the CFC (sec. 953). However, income inclusions under subpart F have been characterized as dividends for unrelated business income tax purposes.[50] Accordingly, insurance income earned by the CFC that is includible in income currently under subpart F by the taxable United States shareholders of the CFC is excluded from unrelated business taxable income in the case of a shareholder that is a tax-exempt organization.

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[49] If the commercial-type insurance activities constitute a substantial part of the organization's activities, the organization will not be tax-exempt under section 501(c)(3) or (c)(4) (sec. 501(m)(1)).

[50] The Internal Revenue Service has concluded in private letter rulings, which are not to be used or cited as precedent, that subpart F inclusions are treated as dividends received by the United States shareholders (a tax-exempt entity) for purposes of computing the shareholder's UBTI (see LTRs 9407007 (November 12, 1993), 9027051 (April 13, 1990), 9024086 (March 22, 1990), 9024026 (March 15, 1990), 8922047 (March 6, 1989), 8836037 (June 14, 1988), 8819034 (February 10, 1988)). However, the IRS issued one private ruling in which it concluded that subpart F inclusions are treated as if the underlying income were realized directly by the United States shareholder (a tax-exempt entity) for purposes of computing the shareholder's UBTI (see LTR 9043039 (July 30, 1990)). This ruling gave no explanation for the IRS's departure from the position in its prior rulings, and the IRS reiterated in a subsequent ruling the position that subpart F inclusions are characterized as dividends for purposes of computing UBTI. Moreover, the application of the look-through rule in the ruling in question did not affect the ultimate result in the ruling because the income to which the subpart F inclusion was attributable was of a type that was excludible from UBTI. The conferees believe that LTR 9043039 (July 30, 1990) is incorrect in its application of a look-through rule in characterizing income inclusions under subpart F for unrelated business income tax purposes.

House bill

The House bill applies a look-through rule in characterizing certain subpart F insurance income for unrelated business income tax purposes. Under the House bill, the look-through rule applies to amounts that constitute insurance income currently includible in gross income under the subpart F rules and that are not attributable to the insurance of risks of (1) the tax-exempt organization itself, (2) certain tax-exempt affiliates of such organization, or (3) an officer or director of, or an individual who (directly or indirectly) performs services for, the tax-exempt organization (or certain tax-exempt affiliates) provided that the insurance covers primarily risks associated with the individual's performance of services in connection with the tax-exempt organization (or tax-exempt affiliates). For purposes of this provision, a tax-exempt organization is an affiliate of another tax-exempt organization if (1) the two organizations have significant common purposes and substantial common membership or (2) the two organizations have directly or indirectly substantial common direction or control.

Effective date.—The provision applies to amounts includible in gross income in taxable years beginning after December 31, 1995.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill with one modification. For purposes of the provision, two or more organizations generally are treated as affiliates if such organizations are colleges or universities described in section 170(b)(1)(A)(ii) or hospitals or other medical entities described in section 170(b)(1)(A)(iii). Accordingly, in applying the provision to two or more such organizations that are the shareholders of a CFC, the exceptions from the look-through rule apply to each shareholder's share of the income attributable to insurance of risks of all such shareholders; the look-through rule applies to a shareholder's share of any income attributable to insurance of risks of a third party.

4. DEPRECIATION UNDER THE INCOME FORECAST METHOD

(Sec. 1604 of the House bill.)

Present law

In general

A taxpayer generally must capitalize the cost of property used in a trade or business and is allowed to recover such cost over time through allowances for depreciation or amortization.

The "income forecast" method is an allowable method for calculating depreciation for certain property. Under the income forecast method, the depreciation deduction for a taxable year for a property is determined by multiplying the cost of the property[51]

[51] In *Transamerica Corp.* v. *U.S.*, 999 F.2d 1362, (9th Cir. 1993), the Ninth Circuit overturned the District Court and held that, for purposes of applying the income forecast method to a film, the "cost of a film" includes "participation" and "residual" payments (i.e., payments to producers,

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(less estimated salvage value) by a fraction, the numerator of which is the income generated by the property during the year and the denominator of which is the total forecasted or estimated income to be derived from the property during its useful life. The income forecast method has been held to be applicable for computing depreciation deductions for motion picture films, television films and taped shows, books, patents, master sound recordings and video games. The total forecasted or estimated income to be derived from a property is to be based on the conditions known to exist at the end of the period for which depreciation is claimed.

House bill

The House bill makes several amendments to the income forecast method of determining depreciation deductions.

First, the bill provides that income to be taken into account under the income forecast method includes all estimated income generated by the property. In applying this rule, a taxpayer generally need not take into account income expected to be generated after the close of the tenth taxable year after the year the property was placed in service. Pursuant to a special rule, in the case of television and motion picture films, the income from the property shall include income from the financial exploitation of characters, designs, scripts, scores, and other incidental income associated with such films, but only to the extent the income is earned in connection with the ultimate use of such items by, or the ultimate sale of merchandise to, persons who are not related to the taxpayer (within the meaning of sec. 267(b)). In addition, pursuant to another special rule, if a taxpayer produces a television series and initially does not anticipate syndicating the episodes from the series, the forecasted income for the episodes of the first three years of the series need not take into account any future syndication fees (unless the taxpayer enters into an arrangement to syndicate such episodes during such period). The 10th-taxable-year rule, the financial exploitation rule, and the syndication rule apply for purposes of the lookback method described below.

Second, the adjusted basis of property that may be taken into account under the income forecast method only will include amounts that satisfy the economic performance standard of section 461(h).

Finally, taxpayers that claim depreciation deductions under the income forecast method are required to pay (or would receive) interest based on the recalculation of depreciation under a "look-back" method. The "look-back" method is applied in any "recomputation year" by (1) comparing depreciation deductions that had been claimed in prior periods to depreciation deductions that would have been claimed had the taxpayer used actual, rather than estimated, total income from the property; (2) determining the hypothetical overpayment or underpayment of tax based on this recalculated depreciation; and (3) applying the overpayment rate of sec-

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writers, directors, actors, guilds, and others based on a percentage of the profits from the film) even though these payments were contingent on the occurrence of future events. It is unclear to what extent, if any, the *Transamerica* decision applies to amounts incurred after the enactment of the economic performance rules of Code section 461(h), as contained in the Deficit Reduction Act of 1984.

tion 6621 of the Code. Except as provided in Treasury regulations, a "recomputation year" is the third and tenth taxable year after the taxable year the property was placed in service, unless the actual income from the property for each taxable year ending with or before the close of such years was within 10 percent of the estimated income from the property for such years. Property that had a basis of $100,000 or less when placed in service is not subject to the look-back method.

Effective date.—The provision is effective for property placed in service after September 13, 1995, unless placed in service pursuant to a binding written contract in effect on such date and all times thereafter.

Senate amendment

No provision. A similar provision was contained in section 402 of the Senate amendment to H.R. 3286, the "Adoption, Promotion and Stability Act of 1996," as favorably reported by the Senate Finance Committee on June 12, 1996.

Conference agreement

The conference agreement follows the provision that was contained in section 402 of the Senate amendment to H.R. 3286, the "Adoption, Promotion and Stability Act of 1996," as favorably reported by the Senate Finance Committee on June 12, 1996. Thus, the conference agreement provides the following modifications to the income forecast method of present law.

Determination of estimated income

First, the agreement provides that income to be taken into account under the income forecast method includes all estimated income generated by the property. In applying this rule, a taxpayer generally need not take into account income expected to be generated after the close of the tenth taxable year after the year the property was placed in service. In the case of a film, television show, or similar property, such income includes, but is not necessarily limited to, income form foreign and domestic theatrical, television, and other releases and syndications; and video tape releases, sales, rentals, and syndications.

Pursuant to a special rule, in the case of television and motion picture films, the income from the property shall include income from the financial exploitation of characters, designs, scripts, scores, and other incidental income associated with such films, but only to the extent the income is earned in connection with the ultimate use of such items by, or the ultimate sale of merchandise to, persons who are not related to the taxpayer (within the meaning of sec. 267(b)). As an example of this special rule, assume a taxpayer produces a motion picture the subject of which is the adventures of a newly-created fictional character. If the taxpayer produces dolls or T-shirts using the character's image, income from the sales of these products by the taxpayer to consumers would be taken into account in determining depreciation for the motion picture under the income forecast method. Similarly, if the taxpayer enters into any licensing or similar agreement with an unrelated party with respect to the use of the image, such licensing income

would be taken into account in determining depreciation for the motion picture. However, if the taxpayer uses the character's image to promote a ride at an amusement park that is wholly-owned by the taxpayer, no portion of the admission fees for the amusement park are to be taken into account under the income forecast method with respect to the motion picture.

In addition, pursuant to another special rule, if a taxpayer produces a television series and initially does not anticipate syndicating the episodes from the series, the forecasted income for the episodes of the first three years of the series need not take into account any future syndication fees (unless the taxpayer enters into an arrangement to syndicate such episodes during such period).

The 10th-taxable-year rule, the financial exploitation rule, and the syndication rule apply for purposes of the look-back method described below.

Determination and treatment of costs of property

The adjusted basis of property that may be taken into account under the income forecast method only will include amounts that satisfy the economic performance standard of section 461(h).[52] For this purpose, if the taxpayer incurs a noncontingent liability to acquire property subject to the income forecast method from another person, economic performance will be deemed to occur with respect to such noncontingent liability when the property is provided to the taxpayer. In addition, the recurring item exception of section 461(h)(3) will apply in a manner similar to the way such exception applies under present law. Thus, expenditures that relate to an item of property that are incurred in the taxable year following the taxable year in which the property is placed in service may be taken into account in the year the property is placed in service to the extent such expenditures meet the recurring item exception for such year.

Any costs that are taken into account after the property is placed in service are treated as a separate piece of property to the extent (1) such amounts are significant and are expected to give rise to a significant increase in the income from the property that was not included in the estimated income from the property, or (2) such costs are incurred more than 10 years after the property was placed in service. To the extent costs are incurred more than 10 years after the property was placed in service and give rise to a separate piece of property for which no income is generated, such costs may be written off and deducted as they are incurred. For example, assume a taxpayer places property subject to the income forecast method in service during a taxable year and all income from the property is generated in the following four-year period. If the taxpayer incurs additional costs with respect to that property more than 10 years later (e.g., a payment pursuant to a deferred contingent compensation arrangement to a person that produced the property), such costs may be deducted in the year incurred provided no more income is generated with respect to such costs or the original property.

[52] No inference is intended as to the proper application of section 461(h) to the income forecast method under present law.

Any costs that are not recovered by the end of the tenth taxable year after the property was placed in service may be taken into account as depreciation in such year.

Look-back method

Finally, taxpayers that claim depreciation deductions under the income forecast method are required to pay (or would receive) interest based on the recalculation of depreciation under a "look-back" method.[53] The "look-back" method is applied in any "recomputation year" by (1) comparing depreciation deductions that had been claimed in prior periods of depreciation deductions that would have been claimed had the taxpayer used actual, rather than estimated, total income from the property; (2) determining the hypothetical overpayment or underpayment of tax based on this recalculated depreciation; and (3) applying the overpayment rate of section 6621 of the Code.

Except as provided in Treasury regulations, a "recomputation year" is the third and tenth taxable year after the taxable year the property was placed in service, unless the actual income from the property for each taxable year ending with or before the close of such years was within 10 percent of the estimated income from the property for such years. The Secretary of the Treasury has the authority to allow a taxpayer to delay the initial application of the look-back method where the taxpayer may be expected to have significant income from the property after the third taxable year after the taxable year the property was placed in service (e.g., the Treasury Secretary may exercise such authority where the depreciable life of the property is expected to be longer than three years).

In applying the look-back method, any cost that is taken into account after the property was placed in service may be taken into account by discounting (using the Federal mid-term rate determined under sec. 1274(d) as of the time the costs were taken into account) such cost to its value as of the date the property was placed in service.

Property that had an unadjusted basis of $100,000 or less is not subject to the look-back method. For this purpose, "unadjusted basis" means the total capitalized cost of a property as of the close of a recomputation year.

The agreement provides a simplified look-back method for pass-through entities.

Effective date

The agreement is effective for property placed in service after September 13, 1995, unless produced or acquired pursuant to a binding written contract in effect on such date and all times thereafter. For this purpose, the binding contract exception may apply to a written contract in effect on the relevant dates if that contract binds a taxpayer to produce, license or deliver property that will be used by the other party to the contract once the property is produced.

[53] The "look-back" method of the provision resembles the look-back method applicable to long-term contracts accounted for under the percentage-of-completion method of present-law sec. 460.

The agreement may apply to property placed in service in taxable years that ended before the date of enactment of this Act. The agreement waives additions to tax imposed under sections 6654, 6655, and 6662(d) for any underpayments of tax or estimated tax for any taxable year ending before the date of enactment of this Act to the extent the underpayment was created or increased by the changes made to the income forecast method of depreciation by the provision. The application of the agreement (including the look-back method) is not waived for any taxable year that ends after the date of enactment of this Act.

5. MODIFY EXCLUSION OF DAMAGES RECEIVED ON ACCOUNT OF PERSONAL INJURY OR SICKNESS

(Sec. 1605 of the House bill and sec. 1603 of the Senate amendment.)

Present law

Under present law, gross income does not include any damages received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal injury or sickness (sec. 104(a)(2)).

The exclusion from gross income of damages received on account of personal injury or sickness specifically does not apply to punitive damages received in connection with a case not involving physical injury or sickness. Courts presently differ as to whether the exclusion applies to punitive damages received in connection with a case involving a physical injury or physical sickness.[54] Certain States provide that, in the case of claims under a wrongful death statute, only punitive damages may be awarded.

Courts have interpreted the exclusion from gross income of damages received on account of personal injury or sickness broadly in some cases to cover awards for personal injury that do not relate to a physical injury or sickness. For example, some courts have held that the exclusion applies to damages in cases involving certain forms of employment discrimination and injury to reputation where there is no physical injury or sickness. The damages received in these cases generally consist of back pay and other awards intended to compensate the claimant for lost wages or lost profits. The Supreme Court recently held that damages received based on a claim under the Age Discrimination in Employment Act could not be excluded from income.[55] In light of the Supreme Court decision, the Internal Revenue Service has suspended existing guidance on the tax treatment of damages received on account of other forms of employment discrimination.

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[54] The Supreme Court recently agreed to decide whether punitive damages awarded in a physical injury lawsuit are excludable from gross income. *O'gilvie* v. *U.S.*, 66 F.3d 1550 (10th Cir. 1995), cert. granted, 64 U.S.L.W. 3639 (U.S. March 25, 1996) (No. 95–966). Also, the Tax Court recently held that if punitive damages are not of a compensatory nature, they are not excludable from income, regardless of whether the underlying claim involved a physical injury or physical sickness. *Bagley* v. *Commissioner*, 105 T.C. No. 27 (1995).

[55] *Schleier* v. *Commissioner*, 115 S. Ct. 2159 (1995).

House bill

Include in income all punitive damages

The House bill provides that the exclusion from gross income does not apply to any punitive damages received on account of personal injury or sickness whether or not related to a physical injury or physical sickness. Under the House bill, present law continues to apply to punitive damages received in a wrongful death action if the applicable State law (as in effect on September 13, 1995 without regard to subsequent modification) provides, or has been construed to provide by a court decision issued on or before such date, that only punitive damages may be awarded in a wrongful death action. No inference is intended as to the application of the exclusion to punitive damages prior to the effective date of the House bill in connection with a case involving a physical injury or physical sickness.

Include in income damage recoveries for nonphysical injuries

The House bill provides that the exclusion from gross income only applies to damages received on account of a personal physical injury or physical sickness. If an action has its origin in a physical injury or physical sickness, then all damages (other than punitive damages) that flow therefrom are treated as payments received on account of physical injury or physical sickness whether or not the recipient of the damages is the injured party. For example, damages (other than punitive damages) received by an individual on account of a claim for loss of consortium due to the physical injury or physical sickness of such individual's spouse are excludable from gross income. In addition, damages (other than punitive damages) received on account of a claim of wrongful death continue to be excludable from taxable income as under present law.

The House bill also specifically provides that emotional distress is not considered a physical injury or physical sickness.[56] Thus, the exclusion from gross income does not apply to any damages received (other than for medical expenses as discussed below) based on a claim of employment discrimination or injury to reputation accompanied by a claim of emotional distress. Because all damages received on account of physical injury or physical sickness are excludable from gross income, the exclusion from gross income applies to any damages received based on a claim of emotional distress that is attributable to a physical injury or physical sickness. In addition, the exclusion from gross income specifically applies to the amount of damages received that is not in excess of the amount paid for medical care attributable to emotional distress.

No inference is intended as to the application of the exclusion to damages prior to the effective date of the House bill in connection with a case not involving a physical injury or physical sickness.

Effective date.—The provisions generally are effective with respect to amounts received after June 30, 1996. The provisions do not apply to amounts received under a written binding agreement,

[56] It is intended that the term emotional distress includes symptoms (e.g., insomnia, headaches, stomach disorders) which may result from such emotional distress.

court decree, or mediation award in effect on (or issued on or before) September 13, 1995.

Senate amendment

Include in income all punitive damages

The Senate amendment is the same as the House bill.

Include in income damage recoveries for nonphysical injuries

No provision.

Conference agreement

Include in income all punitive damages

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

Include in income damage recoveries for nonphysical injuries

The conference agreement follows the House bill.

Effective date.—The provisions generally are effective with respect to amounts received after date of enactment. The provisions do not apply to amounts received under a written binding agreement, court decree, or mediation award in effect on (or issued on or before) September 13, 1995.

6. REPEAL ADVANCE REFUNDS OF DIESEL FUEL TAX FOR PURCHASERS OF DIESEL-POWERED AUTOMOBILES, VANS AND LIGHT TRUCKS

(Sec. 1606 of the House bill.)

Present Law

Excise taxes are imposed on gasoline (14 cents per gallon) and diesel fuel (20 cents per gallon) to fund the Federal Highway Trust Fund. Before 1985, the gasoline and diesel fuel tax rates were the same. The predominate highway use of diesel fuel is by trucks. In 1984, the diesel excise tax rate was increased above the gasoline tax as the revenue offset for a reduction in the annual heavy truck use tax. Because automobiles, vans, and light trucks did not benefit from the use tax reductions, a provision was enacted allowing first purchasers of model year 1979 and later diesel-powered automobiles and light trucks a tax credit to offset this increased diesel fuel tax. The credit is $102 for automobiles and $198 for vans and light trucks.

House bill

The House bill repeals the tax credit for purchasers of diesel-powered automobiles, vans and light trucks.

Effective date.—Vehicles purchased after the date of enactment.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill.

7. EXTENSION AND PHASEOUT OF EXCISE TAX ON LUXURY AUTOMOBILES

(Sec. 1604 of the bill and sec. 4001 of the Code.)

Present law

Present law imposes an excise tax on the sale of an automobile whose price exceeds a designated threshold, currently $34,000. The excise tax is imposed at a rate of 10-percent on the excess of the sales price above the designated threshold. The $34,000 threshold is indexed for inflation.

The tax applies to sales before January 1, 2000.

House bill

No provision.

Senate amendment

The Senate amendment extends and phases out the luxury tax on automobiles. The tax rate is reduced by one percentage point per year beginning in 1996. The tax rate for sales (on or after the date of enactment plus seven days) in 1996 is 9 percent. The tax rate for sales in 1997 is 8 percent. The tax rate for sales in 1998 is 7 percent. The tax rate for sales in 1999 is 6 percent. The tax rate for sales in 2000 is 5 percent. The tax rate for sales in 2001 is 4 percent. The tax rate for sales in 2002 is 3 percent. The tax will expire after December 31, 2002.

Effective date.—The provision is effective for sales on or after date of enactment plus seven days.

Conference agreement

The conference agreement follows the Senate amendment.

8. ALLOW CERTAIN PERSONS ENGAGED IN THE LOCAL FURNISHING OF ELECTRICITY OR GAS TO ELECT NOT TO BE ELIGIBLE FOR FUTURE TAX-EXEMPT BOND FINANCING

(Sec. 1605 of the amendment.)

Present law

Interest on State and local government bonds generally is excluded from income except where the bonds are issued to provide financing for private parties. Present law includes several exceptions, however, that allow tax-exempt bonds to be used to provide financing for certain specifically identified private parties. One such exception allows tax-exempt bonds to be issued to finance facilities for the furnishing of electricity or gas by private parties if the area served by the facilities does not exceed (1) two contiguous counties or (2) a city and a contiguous county (commonly referred to as the "local furnishing" of electricity or gas).

Most private activity tax-exempt bonds are subject to general State private activity bond volume limits of $50 per resident of the State ($150 million, if greater) per year. Tax-exempt bonds for facilities used in the local furnishing of electricity or gas are subject to this limit. Like most other private beneficiaries of tax-exempt bonds, borrowers using tax-exempt bonds to finance these facilities

are denied interest deductions on the debt underlying the bonds if the facilities cease to be used in qualified local furnishing activities. Additionally, as with all tax-exempt bonds, if the use of facilities financed with the bonds changes to a use a not qualified for tax-exempt financing after the debt is incurred, interest on the bonds becomes taxable unless certain safe harbor standards are satisfied.

House bill

No provision.

Senate amendment

The Senate amendment allows persons that have received tax-exempt financing of facilities that currently qualify as used in the local furnishing of electricity or gas to elect to terminate their qualification for this tax-exempt financing and to expand their service areas without incurring the present-law loss of interest deductions and loss of tax-exemption penalties if—

(1) no additional bonds are issued for facilities of the person making the election (or were issued for any predecessor) after the date of the provision's enactment;

(2) the expansion of the person's service area is not financed with any tax-exempt bond proceeds; and

(3) all outstanding tax-exempt bounds of the person making the election (and any predecessor) are redeemed no later than six months after the earliest date on which redemption is not prohibited under the terms of the bonds, as issued, (or six months after the election, if later).

Except as described below, the provision further limits the local furnishing exception to bonds for facilities of (1) of persons that qualified as engaged in that activity on the date of the provision's enactment and (2) that serve areas served by those persons on that date. The area which is considered to be served on the date of the provision's enactment consists of the geographic area in which service actually is being provided on that date. Service initially provided after the date of enactment to a new customer within that area (e.g., as a result of new construction or of a change in heating fuel type) is not treated as a service area expansion.

For purposes of this requirement, a change in the identity of a person serving an area is disregarded if the change is the result of a corporate reorganization where the area served remains unchanged and there is common ownership of both the predecessor and successor entities. To facilitate compliance with electric and gas industry restructuring now in progress, the Senate amendment further permits continued qualification of successor entities under a "step-in-the-shoes" rule without regard to common ownership if the service provided remains unchanged and the area served after the facilities are transferred does not exceed the service area before the transfer. For example, if facilities of a person engaged in local furnishing are sold to another person, the purchaser (when it engages in otherwise qualified local furnishing activities) is eligible for continued tax-exempt financing to the same extent that the seller would have been had the sale not occurred if the service provided and the area served by the facilities do not change.

Similarly, a purchaser "steps into the shoes" of its seller with regard to eligibility (or the lack thereof) for making the election to terminate its status as engaged in local furnishing without imposition of certain penalties on outstanding tax-exempt bonds. For example, if a person engaged in local furnishing activities on the date of the provision's enactment receives financing from tax-exempt bonds issued after the date of the provision's enactment (and is thereby ineligible to make the election), any purchaser from that person likewise is ineligible.

Effective date.—The Senate amendment is effective on the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment, with two modifications to the portion of the provision that generally limits the benefit of tax-exempt financing to persons engaged in local furnishing activities on the date of the provision's enactment. First, the conference agreement allows certain expansions of existing local furnishing service areas to occur after the effective date of the provision without affecting continued qualification under the local furnishing exception, both within the existing service area and in the expansion area. Under this modification, a qualified local furnishing service area which includes a portion of a city or a county on the effective date of the provision may be expanded after that date to include other portions of the same city or county. For example, if a gas utility's service area on the effective date of the provision includes only an urban section of a county, a subsequent expansion of the utility's service area to include rural portions of the same county (e.g., as a result of population growth), does not in itself preclude qualification of the entire, expanded service area as a local furnishing area. This exception does not, however, allow expansion of local furnishing service areas beyond the borders of a city or county where service is being provided on the effective date of the provision or interconnection of facilities serving those areas with other facilities or persons in a manner not permitted under present law.

Second, the date by which an entity must be engaged in local furnishing activities (i.e., have facilities for local furnishing placed in service in that activity) as a condition of receiving future tax-exempt financing is delayed until January 1, 1997 (rather than the date of the provision's enactment).

The conferees also wish to clarify several questions that have arisen since passage of the Senate amendment with respect to the limitation on future eligibility under the local furnishing exception. First, because the conference agreement precludes issuance of tax-exempt bonds except for local furnishers engaged in that activity on January 1, 1997 (and successors in interest), the statutory wording of the provision differs from the traditional focus of the local furnishing exception on a two county (or city and contiguous county) area without regard to the entity providing the service. The statutory references to "persons" engaged in the local furnishing of electricity or gas contained in the conference agreement are intended to prevent new entities (other than successors in interest) from qualifying for tax-exempt financing under the local furnishing

exception. They are not to be construed in a manner affecting the tax-exempt status of interest on any outstanding bonds or the receipt of additional tax-exempt financing by an existing local furnisher, provided that the facilities financed with those bonds are used at all times in qualified local furnishing activities (defined under present law as modified by the conference agreement) and the bonds comply otherwise with the Internal Revenue Code's requirements for tax-exemption.

Second, the conferees are aware that present-law disregards certain transmission of electricity pursuant to FERC orders in determining whether a facility is used in the local furnishing of electricity. The conference agreement retains the relevant statutory rule to that effect, and the conferees intend no change in that rule.

Third, the conferees wish to clarify, by example, the application of the restriction on qualified local furnishing activities contained in this portion of the conference agreement to certain utility transactions such as those that may be expected to occur as a result of deregulation of the electric and gas industries.

Example (1).—As part of a corporate reorganization, an existing local furnishing utility sells a portion of its service area to a third party. The retained portion of the utility's service territory continues to qualify for tax-exempt financing under the local furnishing exception provided that no violations of that exception such as an impermissible interconnection with facilities outside the area occur. The determination of whether the portion of the service territory that is sold to a third party continues to qualify under the local furnishing exception depends on the manner in which the purchaser provides service in the area it acquires. If, for example, the purchaser operates in the area which it purchases in a manner that otherwise qualifies under the local furnishing exception, the purchaser is treated as a successor in interest to the seller and facilities for the area that is sold continue to be treated as used in local furnishing. However, if that area is merged into, or impermissibly (under present-law rules) interconnected with, another service area that does not qualify as a local furnishing area after the transaction, the successor in interest rule does not preserve the status as a local furnishing area of the area sold.

Example (2).—Two independent utilities, both qualifying as engaged in local furnishing on the effective date of the provision, serve adjoining areas. The utilities decide to adjust their common service area boundary line to eliminate irregular geographic patterns. The parties to this transaction may be treated as successors in interest with respect to the area each acquires if the resulting service areas each qualify under the local furnishing exception (as modified by the conference agreement).

Example (3).—Assume the facts of Example (2), except the area acquired by one of the utilities is in a county where it did not provide service before the boundary line adjustments, and the utility's resulting service area includes all or part of three counties. That utility would no longer qualify as engaged in local furnishing under present law. The result is the same under the conference agreement.

Example (4).—Assume the facts of Example (2), except the utilities merge into a single company with a single service area. If the

resulting combined service area of the new company does not exceed two counties (or a city and a contiguous county), the new company continues to be eligible for tax-exempt financing as a successor in interest.

Example (5).—Assume that a local furnishing utility decides to contract with a newly-formed independent power generating venture to construct a generating plant that will sell electricity to it exclusively for use in its service area. Tax-exempt bonds may not be issued under the local furnishing exception for construction of the generating plant. The independent power producer was neither engaged in the local furnishing of electricity to the service area involved on the effective date of the conference agreement's restriction nor is it a successor in interest under the agreement.

Effective date.—These provisions are effective on the date of the conference agreement's enactment.

9. REPEAL OF FINANCIAL INSTITUTION TRANSITION RULE TO INTEREST ALLOCATION RULES

Present law

For foreign tax credit purposes, taxpayers generally are required to allocate and apportion interest expense between U.S. and foreign source income based on the proportion of the taxpayer's total assets in each location. Such allocation and apportionment is required to be made for affiliated groups (as defined in sec. 864(e)(5)) as a whole rather than on a subsidiary-by-subsidiary basis. However, certain types of financial institutions that are members of an affiliated group are treated as members of a separate affiliated group for purposes of allocating and apportioning their interest expense. Section 1215(c)(5) of the Tax Reform Act of 1986 (P.L. 99–514, 100 Stat. 2548) includes a targeted rule which treats a certain corporation as a financial institution for this purpose.

House bill

No provision.

Senate amendment

No provision. However section 1606 of the Senate amendment to H.R. 3448 (Small Business Job Protection Act of 1996) contained a provision that repeals section 1215(c)(5) of the Tax Reform Act of 1986.

Effective date.—Taxable years beginning after December 31, 1995.

Conference agreement

The conference agreement does not include the Senate amendment provision.

10. EXTENSION OF AIRPORT AND AIRWAY TRUST FUND EXCISE TAXES

(Sec. 1607 of the Senate amendment and secs. 4041, 4081, 4261, and 4271 of the Code.)

Present law

Extension of aviation taxes

Before January 1, 1996, the following excise taxes were imposed to fund the Airport and Airway Trust Fund: (1) a 10-percent tax on domestic air passenger tickets; (2) a 6.25-percent tax on domestic air freight waybills; (3) a $6-per-person tax on international air departures; (4) a 17.5 cents-per-gallon tax on jet fuel used in noncommercial aviation; and (5) a 15-cents-per-gallon tax on gasoline used in noncommercial aviation (14 cents per gallon of this tax continues, with the revenues being deposited in the Highway Trust Fund). In addition, jet fuel and gasoline used in noncommercial aviation are subject to a tax of 4.3 cents per gallon, the revenues of which are deposited in the General Fund of the Treasury. Prior to January 1, 1996, of the total tax of 19.3 cents per gallon imposed on gasoline used in noncommercial aviation, 18.3 cents per gallon was collected when the gasoline was removed from a pipeline or barge terminal. The remaining 1 cent per gallon was imposed at the retail level.

Exemption for certain medical air transportation

An exemption is provided from the air passenger and air freight taxes for emergency medical helicopter transportation if the helicopter does not take off from or land at Federally assisted airports or otherwise use Federal aviation facilities or services.

Exemption for helicopters used in exploration or development of hard minerals or oil or gas

An exemption is provided from the air passenger tax for helicopter transportation for exploration, development, or removal of hard minerals or oil or gas if the helicopter does not take off from or land at Federally assisted airports or otherwise use Federal aviation facilities or services.

Transportation of employees of affiliated companies

Generally, when employees fly on their employer's aircraft, the fuel tax applies, but when a company flies other passengers for compensation or hire, the passenger ticket tax applies. Employees of affiliated corporations do not cause the air ticket tax to apply. The Internal Revenue Service has interpreted the use limitation of present-law section 4282 on an all-or nothing basis relating to aircraft of affiliated groups. That is, if an aircraft is available for hire by persons outside the affiliated group, all amounts paid for transportation, including charges among members of an affiliated group, are subject to the passenger ticket tax rather than the fuels tax.[57]

House bill

No provision.

[57] Rev. Rul. 770405, 1977–2 C.B. 381; Rev. Rul. 76–394, 1976–2 C.B. 355.

Senate amendment

Extension of aviation taxes

The five Airport and Airway Trust Fund excise taxes are reinstated at the pre-1996 rates for the period beginning seven days after the date of enactment through April 15, 1997.

Exemption for certain medical air transportation

The Senate amendment: (1) expands the exemption for emergency medical helicopters to also include fixed-wing aircraft equipped for and exclusively dedicated to acute care emergency medical services; and (2) removes the reference to non-use of Federally assisted airports or other Federal aviation facilities or services for such medical aircraft to qualify for the exemption.

Exemption for helicopters used in exploration or development of hard minerals or oil or gas

The Senate amendment provides that the exemption for such helicopter transportation applies on a flight segment basis.

Effective date.—The Senate amendment applies for transportation or fuel sold beginning seven days after the date of enactment. The air passenger and air freight taxes do not apply to any amount paid before that date, even if for transportation occurring during the reinstatement period.

Conference agreement

The conference agreement follows the Senate amendment with three modifications. First, the conference agreement reinstates the five Airport and Airway Trust Fund excise taxes at the pre-1996 rates for the period beginning seven calendar days after the date of enactment and through December 1, 1996 (rather than through April 15, 1997).

Second, the conference agreement consolidates imposition of the aviation gasoline excise tax, with the entire 19.3-cents-per-gallon rate being imposed when the gasoline is removed from a pipeline or barge terminal facility.

Third, the conference agreement provides that the determination of which tax, the passenger ticket tax or the fuels tax, applies to flights of aircraft of affiliated groups of corporations will be made on a flight-by-flight basis.

Effective date.—Same as Senate amendment.

11. MODIFY BASIS ADJUSTMENT RULES UNDER SECTION 1033

(Sec. 1608 of the Senate amendment.)

Present law

Under section 1033, gain realized by a taxpayer from certain involuntary conversions of property is deferred to the extent the taxpayer purchases property similar or related in service of use to the converted property within a specified replacement period of time. The replacement property may be acquired directly or by acquiring control of a corporation (generally, 80 percent of the stock of the corporation) that owns replacement property. The taxpayer's basis in the replacement property generally is the same as the tax-

payer's basis in the converted property, decreased by the amount of any money or loss recognized on the conversion, and increased by the amount of any gain recognized on the conversion. In cases in which a taxpayer purchases stock as replacement property, the taxpayer generally reduces the basis of the stock, but does not reduce the basis of the underlying assets. Thus, the reduction in the basis of the stock generally does not result in reduced depreciation deductions where the corporation holds depreciable property, and may result in the taxpayer having more aggregate depreciable basis after the acquisition of replacement property than before the involuntary conversion.

House bill

No provision.

Senate amendment

The Senate amendment provides that where the taxpayer satisfies the replacement property requirement of section 1033 by acquiring stock in a corporation, the corporation generally will reduce its adjusted bases in its assets by the amount by which the taxpayer reduces its basis in the stock. The corporation's adjusted bases in its assets will not be reduced, in the aggregate, below the taxpayer's basis is its stock (determined after the appropriate basis adjustment for the stock). In addition, the basis of any individual asset will not be reduced below zero. The basis reduction first is applied to: (1) property that is similar or related in service or use to the converted property, then (2) to other depreciable property, then (3) to other property.

Effective date.—The provision applies to involuntary conversions occurring after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

12. EXTENSION OF WITHHOLDING TO CERTAIN GAMBLING WINNINGS

(Sec. 1609 of the Senate amendment.)

Present law

In general, proceeds from a wagering transaction are subject to withholding at a rate of 28 percent if the proceeds exceed $5,000 and are at least 300 times as large as the amount wagered. No withholding tax is imposed on winnings from bingo or keno.

House bill

No provision.

Senate amendment

The Senate amendment imposes withholding on proceeds from bingo or keno wagering transactions at a rate of 28 percent if such proceeds exceed $5,000, regardless of the odds of the wager.

Effective date.—The provision is effective 30 days after the date of enactment.

Conference agreement

The conference agreement does not include the Senate amendment provision.

13. TREATMENT OF CERTAIN INSURANCE CONTRACTS ON RETIRED LIVES

(Sec. 1610 of the Senate amendment.)

Present law

Life insurance companies are allowed a deduction for any net increase in reserves and are required to include in income any net decrease in reserves. The reserve of a life insurance company for any contract is the greater of the net surrender value of the contract or the reserve determined under Federally prescribed rules. In no event, however, may the amount of the reserve for tax purposes for any contract at any time exceed the amount of the reserve for annual statement purposes.

Special rules are provided in the case of a variable contract. Under these rules, the reserve for a variable contract is adjusted by (1) subtracting any amount that has been added to the reserve by reason of appreciation in the value of assets underlying such contract, and (2) adding any amount that has been subtracted from the reserve by reason of depreciation in the value of assets underlying such contract. In addition, the basis of each asset underlying a variable contract is adjusted for appreciation or depreciation to the extent the reserve is adjusted.

A variable contract generally is defined as any annuity or life insurance contract (1) that provides for the allocation of all or part of the amounts received under the contract to an account that is segregated from the general asset accounts of the company, and (2) under which, in the case of an annuity contract, the amounts paid in, or the amounts paid out, reflect the investment return and the market value of the segregated asset account, or, in the case of a life insurance contract, the amount of the death benefit (or the period of coverage) is adjusted on the basis of the investment return and the market value of the segregated asset account. A pension plan contract that is not a life, accident, or health, property, casualty, or liability insurance contract is treated as an annuity contract for purposes of this definition.

House bill

No provision.

Senate amendment

The Senate amendment provides that a variable contract is to include a contract that provides for the funding of group term life or group accident and health insurance on retired lives if: (1) the contract provides for the allocation of all or part of the amounts received under the contract to an account that is segregated from the general asset account of the company; and (2) the amounts paid in, or the amounts paid out, under the contract reflect the investment return and the market value of the segregated asset account underlying the contract.

Thus, the reserve for such a contract is to be adjusted by (1) subtracting any amount that has been added to the reserve by reason of appreciation in the value of assets underlying such contract, and (2) adding any amount that has been subtracted from the reserve by reason of depreciation in the value of assets underlying such contract. In addition, the basis of each asset underlying the contract is to be adjusted for appreciation or depreciation to the extent that the reserve is adjusted.

Effective date.—The provision applies to taxable years beginning after December 31, 1995.

Conference agreement

The conference agreement follows the Senate amendment.

14. TREATMENT OF MODIFIED GUARANTEED CONTRACTS

Present law

Life insurance companies are allowed a deduction for any net increase in reserves and are required to include in income any net decrease in reserves. The reserve of a life insurance company for any contract is the greater of the net surrender value of the contract or the reserve determined under Federally prescribed rules. The net surrender value of a contract is the cash surrender value reduced by any surrender penalty, except that any market value adjustment required on surrender is not taken into account. In no event, however, may the amount of the reserve for tax purposes for any contract at any time exceed the amount of the reserve for annual statement purposes.

In general, assets held for investment are treated as capital assets. Any gain or loss from the sale or exchange of a capital asset is treated as a capital gain or loss and is taken into account for the taxable year in which the asset is sold or exchanged.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement generally applies a mark-to-market regime to assets held as part of a segregated account under a modified guaranteed contract issued by a life insurance company. Gain or loss with respect to such assets held as of the close of any taxable year are taken into account for that year (even though the assets have not been sold or exchanged),[58] and are treated as ordinary. If gain or loss is taken into account by reason of the mark-to-market requirement, then the amount of gain or loss subsequently realized as a result of sale, exchange, or other disposition of the asset, or as a result of the application of the mark-to-market requirement is appropriately adjusted to reflect such gain or loss. In addition, the reserve for a modified guaranteed contract is deter-

[58] The wash sale rules of section 1091 of the Code are not to apply to any loss that is required to be taken into account solely by reason of the mark-to-market requirement.

mined by taking into account the market value adjustment required on surrender of the contract.

A modified guaranteed contract is defined as any life insurance contract, annuity contract or pension plan contract[59] that is not a variable contract (within the meaning of Code section 817), and that satisfies the following requirements. All or part of the amounts received under the contract must be allocated to an account which, pursuant to State law or regulation, is segregated from the general asset accounts of the company and is valued from time to time by reference to market values.

The reserves for the contract must be valued at market for annual statement purposes and the Federally prescribed reserve for the contract under section 807(d)(2) must be valued at market. Further, a modified guaranteed contract includes only a contract that provides either for a net surrender value or for a policyholder's fund (within the meaning of section 807(e)(1)). It is intended that a policyholder's fund be more than de minimis. For example, Treasury regulations could provide that a policyholder's fund that represents 15 percent or less of the insurer's reserve for the contract under section 807, and that is attributable to employee contributions, would be considered de minimis.

If only a portion of the contract is not described in section 817, that portion is treated as a separate contract for purposes of the provision.

The Treasury Department is authorized to issue regulations that provide for the application of the mark-to-market requirement at times other than the close of a taxable year or the last business day of a taxable year. The Treasury Department is also authorized to issue such regulations as may be necessary or appropriate to carry out the purposes of the provision and to provide for treatment of modified guaranteed contracts under sections 72, 7702, and 7702A. In addition, the Treasury Department is authorized to determine the interest rates applicable under section 807(c)(3), 807(d)(2)(B) and 812 with respect to modified guaranteed contracts annually, calculating such rates as appropriate for modified guaranteed contracts. The Treasury Department has discretion to determine an appropriate rate that is a current market rate, which could be determined, for example, either by using a rate that is appropriate for the obligations under the contract to which the reserve relates, or by taking into account the yield on the assets underlying the contract. The Treasury Department may exercise this authority by issuing a periodic announcement of the appropriate market interest rates or formula for determining such rates. The Treasury Department is also authorized, to the extent appropriate for such a contract, to modify or waive section 811(d).

The Treasury Department is also authorized to provide rules limiting the ordinary treatment provided under the provision to gain or loss on those assets properly taken into account in calculating the reserve for Federal tax purposes (and necessary to support such reserves) for modified guaranteed contracts, and to provide rules for limiting such treatment with respect to other assets (such

[59] The provision applies only to a pension plan contract that is not a life, accident or health, property, casualty, or liability contract.

as assets representing surplus of the company). Particular concern has been expressed about characterization of gain or loss as ordinary under the provision in transactions that would otherwise either (1) have to meet the requirements of the hedging exception to the straddle rules to receive this treatment, or (2) by treated as capital transactions under present law. It is intended that the mark-to-market treatment apply to all assets held as part of a segregated account established under the provision, even though ordinary treatment may not apply (pursuant to Treasury regulatory authority) to assets held as part of the segregated account that are not necessary to support the reserve for modified guaranteed contracts.

The conference agreement authorizes the Treasury Department to prescribe regulations that provide for the treatment of assets transferred to or from a segregated account. This regulatory authority is provided because of concern that taxpayers may exercise selective ordinary loss (or income or gain) recognition by virtue of the ordinary treatment under the provision. One example of selective ordinary loss recognition could arise if assets are always marked to market when transferred out of the segregated account. For example, if at the beginning of the taxable year an asset in the segregated account is worth $1,000, but declines to $900 in July, the taxpayer might choose to recognize $100 of ordinary loss while continuing to own the asset, simply by transferring it out of the segregated account in July and replacing $1,000 of cash (for example) in the segregated account.

It is intended that the regulations relating to asset transfers will forestall opportunities for selective recognition of ordinary items. Prior to the issuance of these regulations, the following rules shall apply.

If an asset is transferred to a segregated account, gain or loss attributable to the period during which the asset was not in the segregated account is taken into account when the asset is actually sold, and retains the character (as ordinary or capital) properly attributable to that period. Appropriate adjustments are made to the basis of the asset to reflect gain or loss attributable to that period.

If an asset is transferred out of a segregated account, the transfer is deemed to occur on the last business day of the taxable year and gain or loss with respect to the transferred asset is taken into account as of that day. Loss with respect to such transferred asset is treated as ordinary to the extent of the lesser of (1) the loss (if any) that would have been recognized if the asset had been sold for its fair market value on the last business day of the taxable year (or the date the asset was actually sold by the taxpayer, if earlier) or (2) the loss (if any) that would have been recognized if the asset had been sold for its fair market value on the date of the transfer. A similar rule applies for gains. Proper adjustment is made in the amount of any gain or loss subsequently realized to reflect gain or loss under the provision.

For example, assume that a capital asset in the segregated account that is worth $1,000 at the beginning of the year is transferred out of the segregated account in July at a value of $900, is retained by the company and is worth $950 on the last business day of the taxable year. A $50 ordinary loss is taken into account

with respect to the asset for the taxable year (the difference Between $1,000 and $950). The asset is not marked to market in any subsequent year under the provision, provide that it is not transferred back to the segregated account.

As an additional example, assume that a capital asset in the segregated account that is worth $1,000 at the beginning of the year is transferred out of the segregated accounted in July at a value of $900, is retained by the company and continues to decline in value to $850 on the last business day of the taxable year. A $100 ordinary loss ($1,000 less $900) and a $50 capital loss ($900 less $850) is taken into account with respect to the asset for the taxable year.

Effective date.—The provision applies to taxable years beginning after December 31, 1995. A taxpayer that is required to (1) change its calculation of reserves to take into account market value adjustments and (2) mark to market its segregated assets in order to comply with the requirements of the provision is treated as having initiated changes in methods of accounting and as having received the consent of the Treasury Department to make such changes.

Except as otherwise provided in special rules (described below), the section 481(a) adjustments required by reason of the changes in method of accounting are to be taken into account as ordinary income for the taxpayer's first taxable year beginning after December 31, 1995.

Special rules providing for a seven-year spread apply in the case of certain losses (if any), and in the case of certain reserve increases (if any), in order to limit selective loss recognition or selective minimization of gain recognition. Thus, the seven-year spread rule applies when the taxpayer's section 481(a) adjustment is negative.

First, if, for the taxpayer's first taxable year beginning after December 31, 1995, (1) the aggregate amount of the loss recognized by reason of the change in method of accounting with respect to segregated assets under modified guaranteed contracts (i.e., the switch to a mark-to-market regime for such assets) exceeds (2) the amount included in income by reason of the change in method of accounting with respect to reserves (i.e., the change permitting a market value adjustment to be taken into account with respect to a modified guaranteed contract), then the excess is not allowed as a deduction in the taxpayer's first taxable year beginning after December 31, 1995. Rather, such excess is allowed ratably over the period of seven taxable years beginning with the taxpayer's first taxable year beginning after December 31, 1995. The adjusted basis of each such segregated asset is nevertheless determined as if such losses were realized in the taxpayer's first taxable year beginning after December 31, 1995.

Second, if, for the taxpayer's first taxable year beginning after December 31, 1995, (1) the aggregate amount the taxpayer's deduction that arises by reason of the change in method of accounting with respect to reserves (i.e., the change permitting a market value adjustment to be taken into account with respect to a modified guaranteed contract), exceeds (2) the aggregate amount of the gain recognized by reason of the change in method of accounting with

respect to segregated assets under modified guaranteed contracts (i.e., the switch to a mark-to-market regime for such assets), then the excess is not allowed as a deduction in the taxpayer's first taxable year beginning after December 31, 1995. Rather, such excess is allowed ratably over the period of seven taxable years beginning with the taxpayer's first taxable year beginning after December 31, 1995.

15. TREATMENT OF CONTRIBUTIONS IN AID OF CONSTRUCTION FOR WATER UTILITIES

(Sec. 1611(a) of the Senate amendment.)

Present and prior law

The gross income of a corporation does not include contributions to its capital. A contribution to the capital of a corporation does not include any contribution in aid of construction or any other contribution as a customer or potential customer.

Prior to the enactment of the Tax Reform Act of 1986 ("1986 Act"), a regulated public utility that provided electric energy, gas water, or sewage disposal services was allowed to treat any amount of money or property received from any person as a tax-free contribution to its capital so long as such amount: (1) was a contribution in aid of construction; and (2) was not included in the taxpayer's rate base for rate-making purposes. A contribution in aid of construction did not include a connection fee. The basis of any property acquired with a contribution in aid of construction was zero.

If the contribution was in property other than electric energy, gas, steam, water, or sewerage disposal facilities, such contribution was not includible in the utility's gross income so long as: (1) an amount at least equal to the amount of the contribution was expended for the acquisition or construction of tangible property that was used predominantly in the trade or business of furnishing utility services; (2) the expenditure occurred before the end of the second taxable year after the year that the contribution was received; and (3) certain records were kept with respect to the contribution and the expenditure. In addition, the status of limitations for the assessment of deficiencies was extended in the case of these contributions.

These rules were repealed by the 1986 Act. Thus, after the 1986 Act, the receipt by a utility of a contribution in aid of construction is includible in the gross income of the utility, and the basis of property received or constructed pursuant to the contribution is not reduced.

House bill

No provision.

Senate amendment

The Senate amendment restores the contributions in aid of construction provisions that were repealed by the 1986 Act for regulated public utilities that provide water or sewerage disposal services.

Effective date.—The provision is effective for amounts received after June 12, 1996.

Conference agreement

The conference agreement follows the Senate amendment.

16. REQUIRE WATER UTILITY PROPERTY TO BE DEPRECIATED OVER 25 YEARS

(Sec. 1611(b) of the Senate amendment.)

Present law

Property used by a water utility in the gathering, treatment, and commercial distribution of water and municipal sewers are depreciated over a 20-year period for regular tax purposes. The depreciation method generally applicable to property with a recovery period of 20 years is the 150-percent declining balance method (switching to the straight-line method in the year that maximizes the depreciation deduction). The straight-line method applies to property with a recovery period over 20 years.

House bill

No provision.

Senate amendment

The Senate amendment provides that water utility property will be depreciated using a 25-year recovery period and the straight-line method for regular tax purposes. For this purpose, "water utility property" means (1) property that is an integral part of the gathering, treatment, or commercial distribution of water, and that, without regard to the proposal, would have had a recovery period of 20 years and (2) any municipal sewer. Such property generally is described in Asset Classes 49.3 and 51 of Revenue Procedure 87–56, 1987–2 C.B. 674. The Senate amendment does not change the class lives of water utility property for purposes of the alternative depreciation system of section 168(g).

Effective date.—The provision is effective for property placed in service after June 12, 1996, other than property placed in service pursuant to a binding contract in effect before June 10, 1996, and at all times thereafter before the property is placed in service.

Conference agreement

The conference agreement follows the Senate amendment.

17. ALLOW CONVERSION OF SCHOLARSHIP FUNDING CORPORATION TO TAXABLE CORPORATION

(Sec. 1621 of the Senate amendment.)

Present law

Qualified scholarship funding corporations are nonprofit corporations established and operated exclusively for the purpose of acquiring student loan notes incurred under the Higher Education Act of 1965 (sec. 150(d)). In addition, a qualified scholarship funding corporation must be required by its corporate charter and bylaws, or under State law, to devote any income (after payment of

expenses, debt service and the creation of reserves for the same) to the purchase of additional student loan notes or to pay over any income to the United States.

In general, State and local government bonds issued to finance private loans (e.g., student loans) are taxable private activity bonds. However, interest on qualified student loan bonds is tax-exempt. Qualified scholarship funding corporations are eligible issuers of qualified student loan bonds.

The Internal Revenue Code restricts the direct and indirect investment of bond proceeds in higher yielding investments and requires that profits on investments that are unrelated to the government purpose for which the bonds are issued be rebated to the United States. Special allowance payments (SAP) made by the Department of Education are treated as interest on notes and, therefore, are permitted arbitrage that need not be rebated to the United States.

Generally, a private foundation and disqualified persons may, in the aggregate, own 20 percent of the voting stock of a functionally unrelated corporation.

House bill

No provision.

Senate amendment

In general.—The amendment would provide that a nonprofit student loan funding corporation may elect to cease its status as a qualified scholarship funding corporation. If the corporation meets the requirements outlined below, such an election would not cause any bond outstanding as of the date of the issuer's election and any bond issued to refund such a bond to fail to be a qualified student loan bond. Once made, an election could be revoked only with the consent of the Secretary of the Treasury. After making the election, the issuer would not be authorized to issue any new bonds.

Requirements.—First, upon making the election, the issuer would be required to transfer all of the student loan notes to another, taxable, corporation in exchange for senior stock of such corporation within a reasonable period of time after the election is made. Immediately after the transfer, the issuer, and any other issuer who made the election, would be required to hold all of the senior stock of the corporation. Senior stock is stock whose rights to dividends, liquidation or redemption rights are not inferior to those of any other class of stock and that (1) participates pro rata and fully in the equity value of any other common stock of the corporation, (2) has the right to payments receivable in liquidation prior to any other stock in the corporation, (3) upon liquidation or redemption, has a fixed right to receive the greater of (a) the fair market value of the stock at the date of liquidation or redemption or (b) the net fair market value of all assets transferred to the corporation by the issuer, and (4) has a right to require its redemption by a date which is not later than 10 years after the date that the election is made.

Second, the transferee corporation would be required to assume or otherwise provide for the payment of all the qualified

scholarship funding bond indebtedness of the issuer within a reasonable period after the election.

Third, immediately after the transfer, the issuer (i.e., the nonprofit student loan funding corporation) would be required to become a charitable organization (described in section 501(c)(3) that is exempt from tax under section 501(a)), at least 80 percent of the members of its board of directors must be independent members, and it must hold all of the senior stock of the corporation.

Excess business holdings.—For purposes of the excess business holding restrictions imposed on a private foundation, the charity would not be required to divest its ownership in a corporation most of whose assets are student loan notes incurred under the Higher Education Act of 1965.

Effective date.—The amendment would be effective on the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

18. APPLY MATHEMATICAL OR CLERICAL ERROR PROCEDURES FOR DEPENDENCY EXEMPTIONS AND FILING STATUS WHEN CORRECT TAXPAYER IDENTIFICATION NUMBERS ARE NOT PROVIDED

(Sec. 1613 of the Senate amendment.)

Present law

In general

Individuals who claim personal exemptions for dependents must include on their tax return the name and taxpayer identification number (TIN) of each dependent. For returns filed with respect to tax year 1996, individuals must provide a TIN for all dependents born on or before November 30, 1996. For returns filed with respect to tax year 1997 and all subsequent years, individuals must provide TINs for all dependents, regardless of their age. An individual's TIN is generally that individual's social security number.

If the individual fails to provide a correct TIN for a dependent, the Internal Revenue Service may impose a $50 penalty.

Mathematical or clerical errors

The IRS may summarily assess additional tax due as a result of a mathematical or clerical error without sending the taxpayer a notice of deficiency and giving the taxpayer an opportunity to petition the Tax Court. Where the IRS uses the summary assessment procedure for mathematical or clerical errors, the taxpayer must be given an explanation of the asserted error and a period of 60 days to request that the IRS abate its assessment. The IRS may not proceed to collect the amount of the assessment until the taxpayer has agreed to it or has allowed the 60-day period for objecting to expire. If the taxpayer files a request for abatement of the assessment specified in the notice, the IRS must abate the assessment. Any reassessment of the abated amount is subject to the ordinary deficiency procedures. The request for abatement of the assessment is the only procedure a taxpayer may use prior to paying the assessed

amount in order to contest an assessment arising out of a mathematical or clerical error. Once the assessment is satisfied, however, the taxpayer may file a claim for refund if he or she believes the assessment was made in error.

House bill

No provision.

Senate amendment

If an individual fails to provide a correct TIN for a dependent, the IRS is authorized to deny the dependency exemption. Such a change also has indirect consequences for other tax benefits currently conditioned on being able to claim a dependency exemption (e.g., head of household filing status and the dependent care credit). In addition, the failure to provide a correct TIN for a dependent will be treated as a mathematical or clerical error and thus any notification that the taxpayer owes additional tax because of that failure will not be treated as a notice of deficiency.

Effective date.—The provision is effective for tax returns for which the due date (without regard to extensions) is 30 days or more after the date of enactment. For taxable years beginning in 1995, no requirement to obtain a TIN applies in the case of dependents born after October 31, 1995. For taxable years beginning in 1996, no requirement to obtain a TIN applies in the case of dependents born after November 30, 1996.

Conference agreement

The conference agreement follows the Senate amendment.

19. TREATMENT OF FINANCIAL ASSET SECURITIZATION INVESTMENT TRUSTS ("FASITS")

(Sec. 1621 of the Senate amendment.)

Present law

An individual can own income-producing assets directly, or indirectly through an entity (i.e., a corporation, partnership, or trust). Where an individual owns assets through an entity (e.g., a corporation), the nature of the interest in the entity (e.g., stock of a corporation) is different than the nature of the assets held by the entity (e.g., assets of the corporation).

Securitization is the process of converting one type of asset into another and generally involves the use of an entity separate from the underlying assets. In the case of securitization of debt instruments, the instruments created in the securitization typically have different maturities and characteristics than the debt instruments that are securitized.

Entities used in securitization include entities that are subject to tax (e.g., a corporation), conduit entities that generally are not subject to tax (e.g., a partnership, grantor trust, or real estate mortgage investment conduit ("REMIC")), or partial-conduit entities that generally are subject to tax only to the extent income is not distributed to owners (e.g., a trust, real estate investment trust ("REIT"), or regulated investment company ("RIC")).

There is no statutory entity that facilitates the securitization of revolving, non-mortgage debt obligations.

House bill

No provision.

Senate amendment

In general

The Senate amendment would create a new type of statutory entity called a "financial asset securitization investment trust" ("FASIT") that facilitates the securitization of debt obligations such as credit card receivables, home equity loans, and auto loans. A FASIT generally will not be taxable; the FASIT's taxable income or net loss will flow through to the owner of the FASIT.

The ownership interest of a FASIT generally will be required to be entirely held by a single domestic C corporation. The Finance Committee expected that the Treasury Department will issue guidance on how this rule would apply to cases in which the entity that owns the FASIT joins in the filing of a consolidated return with other members of the group that wish to hold an ownership interest in the FASIT. In addition, a FASIT generally may hold only qualified debt obligations, and certain other specified assets, and will be subject to certain restrictions on its activities. An entity that qualifies as a FASIT can issue instruments that meet certain specified requirements and treat those instruments as debt for Federal income tax purposes. Instruments issued by a FASIT bearing yields to maturity over five percentage points above the yield to maturity on specified United States government obligations (i.e., "high-yield interests") must be held, directly or indirectly, only by domestic C corporations that are not exempt from income tax.

Qualification as a FASIT

In general.—To qualify as a FASIT, an entity must: (1) make an election to be treated as a FASIT for the year of the election and all subsequent years; (2) have assets substantially all of which (including assets that the FASIT is treated as owning because they support regular interests) are specified types called "permitted assets;" (3) have non-ownership interests be certain specified types of debt instruments called "regular interests"; (4) have a single ownership interest which is held by an "eligible holder"; and (5) not qualify as a RIC. Any entity, including a corporation, partnership, or trust may be treated as a FASIT. In addition, a segregated pool of assets may qualify as a FASIT.

Election to be a FASIT.—Once an election to be a FASIT is made, the election applies from the date specified in the election and all subsequent years until the entity ceases to be a FASIT. The manner of making the election to be a FASIT is to be determined by the Secretary of the Treasury. If an election to be a FASIT is made after the initial year of an entity, all of the assets in the entity at the time of the FASIT election are deemed contributed to

the FASIT at that time and, accordingly, any gain (but not loss) on such assets will be recognized at that time.[60]

Ceasing to be a FASIT.—Once an entity ceases to be a FASIT, it is not a FASIT for that year or any subsequent year. Nonetheless, an entity can continue to be a FASIT where the Treasury Department determines that the entity inadvertently ceases to be a FASIT, steps are taken reasonably soon after it is discovered that the entity ceased being a FASIT so that it again qualifies as a FASIT, and the FASIT and its owner take those steps that the Treasury Department deems necessary. An entity will cease qualifying as a FASIT if the entity's owner ceases being an eligible corporation. Loss of FASIT status is to be treated as if all of the regular interests of the FASIT were retired and then reissued without the application of the rule which deems regular interests of a FASIT to be debt. The Finance Committee understood that this treatment could result in the creation of cancellation of indebtedness income where the new instruments deemed to be issued are treated as stock under general tax principles.

Permitted assets

In general.—For an entity or arrangement to qualify as a FASIT, substantially all of its assets must consist of the following "permitted assets": (1) cash and cash equivalents; (2) certain permitted debt instruments; (3) certain foreclosure property; (4) certain instruments or contracts that represent a hedge or guarantee of debt held or issued by the FASIT; (5) contract rights to acquire permitted debt instruments or hedges; and (6) a regular interest in another FASIT. A FASIT must meet the asset test at the 90th day after its formation and at all times thereafter. Permitted assets may be acquired at any time by a FASIT, including any time after its formation.

Permitted debt instruments.—A debt instrument will be a permitted asset only if the instrument is indebtedness for Federal income tax purposes including trade receivables, regular interests in a real estate mortgage investment conduit (REMIC), or regular interests issued by another FASIT and it bears (1) fixed interest or (2) variable interest of a type that relates to qualified variable rate debt (as defined in Treasury regulations prescribed under sec. 860G(a)(1)(B)). Except for cash equivalents, permitted debt obligations cannot be obligations issued, directly or indirectly, by the owner of the FASIT or a related person.

Foreclosure property.—Permitted assets include property acquired on default (or imminent default) of debt instruments, swap contracts, forward contracts, or similar contracts held by the FASIT that would be foreclosure property to a REIT (under sec. 856(e)) if the property that was acquired by foreclosure by the FASIT was real property or would be foreclosure property to a REIT but for certain leases entered into or construction performed (as described in sec. 856(e)(4)) while held by the FASIT.

Hedges.—Permitted assets include interest rate or foreign currency notional principal contracts, letters of credit, insurance, guar-

[60] The Senate amendment provided transitional relief under which gain in pre-effective date entities that make a FASIT election may be deferred.

antees against payment defaults, notional principal contracts that are "in the money," or other similar instruments as permitted under Treasury regulations, which are reasonably required to guarantee or hedge against the FASIT's risks associated with being the obligor of regular interests. An instrument is a hedge if it results in risk reduction as described in Treasury regulation section 1.1221–2.

"Regular interests" of a FASIT.—Under the Senate amendment, "regular interests" of a FASIT, including "high-yield interests," are treated as debt for Federal income tax purposes regardless of whether instruments with similar terms issued by non-FASITs might be characterized as equity under general tax principles. To be treated as a "regular interest," an instrument must have fixed terms and must: (1) unconditionally entitle the holder to receive a specified principal amount; (2) pay interest that is based on (a) one or more rates that are fixed, (b) rates that measure contemporaneous variations in the cost of newly borrowed funds,[61] or (c) to the extent permitted by Treasury regulations, variable rates allowed to regular interests of a REMIC if the FASIT would otherwise qualify as a REMIC; (3) have a term to maturity of no more than 30 years, except as permitted by Treasury regulations; (4) be issued to the public with a premium of not more than 25 percent of its stated principal amount; and (5) have a yield to maturity determined on the date of issue of no more than five percentage points above the applicable Federal rate (AFR) for the calendar month in which the instrument is issued.

A FASIT also may issue high-yield debt instruments, which includes any debt instrument issued by a FASIT that meets the second and third conditions described above, so long as such interests are not held by a disqualified holder. A "disqualified holder" generally is any holder other than (1) a domestic C corporation that does not qualify as a RIC, REIT, REMIC, or cooperative[62] or (2) a dealer who acquires FASIT debt for resale to customers in the ordinary course of business. An excise tax is imposed at the highest corporate rate on a dealer if there is a change in dealer status or if the holding of the instrument is for investment purposes. A 31-day grace period is granted before ownership of an interest held by a dealer generally could be treated as held by the FASIT owner for investment purposes.

Permitted ownership holder.—A permitted holder of the ownership interest in a FASIT generally is a non-exempt domestic C corporation, other than a corporation that qualifies as a RIC, REIT, REMIC, or cooperative.

Transfers to non-permitted holders of high-yield interests

A transfer of a high-yield interest to a disqualified holder is to be ignored for Federal income tax purposes. Thus, such a transferor will continue to be liable for any taxes due with respect to the transferred interest.

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[61] Variable interest rates that would meet this standard include variable interest rates described in Treasury Income Tax Regulations 1.860G–1(a)(3).

[62] The Senate amendment treats cooperatives as disqualified holders since cooperatives, like RICs and REITs, are treated as pass-through entities and, also like the owners of RICs and REITs, the cooperative's members and patrons need not be C corporations.

Taxation of a FASIT

In general.—A FASIT generally is not subject to tax. Instead, all of the FASIT's assets and liabilities are treated as assets and liabilities of the FASIT's owner and any income, gain, deduction or loss of the FASIT is allocable directly to its owner. Accordingly, income tax rules applicable to a FASIT (e.g., related party rules, sec. 871(h), sec. 165(g)(2)) are to be applied in the same manner as they apply to the FASIT's owner. Any securities held by the FASIT that are treated as held by its owner are treated as held for investment. The taxable income of a FASIT is calculated using an accrual method of accounting. The constant yield method and principles that apply for purposes of determining OID accrual on debt obligations whose principal is subject to acceleration apply to all debt obligations held by a FASIT to calculate the FASIT's interest and discount income and premium deductions or adjustments. For this purpose, a FASIT's income does not include any income subject to the 100-percent penalty excise tax on prohibited transactions.

Income from prohibited transactions.—The owner of a FASIT is required to pay a penalty excise tax equal to 100 percent of net income derived from (1) an asset that is not a permitted asset, (2) any disposition of an asset other than a permitted disposition, (3) any income attributable to loans originated by the FASIT, and (4) compensation for services (other than fees for a waiver, amendment, or consent under permitted assets not acquired through foreclosure). A permitted disposition is any disposition of any permitted asset (1) arising from complete liquidation of a class of regular interests (i.e., a qualified liquidation[63]), (2) incident to the foreclosure, default, or imminent default of the asset, (3) incident to the bankruptcy or insolvency of the FASIT, (4) necessary to avoid a default on any indebtedness of the FASIT attributable to a default (or imminent default) on an asset of the FASIT, (5) to facilitate a clean-up call, (6) to substitute a permitted debt instrument for another such instrument, or (7) in order to reduce overcollateralization where a principal purpose of the disposition was not to avoid recognition of gain arising from an increase in its market value after its acquisition by the FASIT. Notwithstanding this rule, the owner of a FASIT may currently deduct its losses incurred in prohibited transactions in computing its taxable income for the year of the loss.

Taxation of interests in the FASIT

Taxation of holders of regular interests.—In general.—A holder of a regular interest, including a high-yield interest, is taxed in the same manner as a holder of any other debt instrument, except that the regular interest holder is required to account for income relating to the interest on an accrual method of accounting, regardless of the method of accounting otherwise used by the holder.[64]

High-yield interests.—Holders of high-yield interests are not allowed to use net operating losses to offset any income derived from the high-yield debt. Any net operating loss carryover shall be com-

[63] For this purpose, a "qualified liquidation" has the same meaning as it does purposes of the exemption from the tax on prohibited transactions of a REMIC in section 860F(a)(4).

[64] Regular interests in a FASIT 95 percent or more of whose assets are real estate mortgages are treated as real estate assets where relevant (e.g., secs. 856, 593, 7701(a)(19)).

puted by disregarding any income arising by reason of the disallowed loss.

In addition, a transfer of a high-yield interest to a disqualified holder is not recognized for Federal income tax purposes such that the transferor will continue to be taxed on the income from the high-yield interest unless the transferee provides the transferor with an affidavit that the transferee is not a disqualified person or the Treasury Secretary determines that the high-yield interest is no longer held by a disqualified person and a corporate tax has been paid on the income from the high-yield interest while it was held by a disqualified person.[65] High-yield interests may be held without a corporate tax being imposed on the income from the high-yield interest where the interest is held by a dealer in securities who acquired such high-yield interest for sale in the ordinary course of his business as a securities dealer. In such a case, a corporate tax is imposed on such a dealer if his reason for holding the high-yield interest changes to investment. There is a presumption that the dealer has not changed his intent for holding high-yield instruments to investment for the first 31 days he holds such interests unless such holding is part of a plan to avoid the restriction on holding of high-yield interests by disqualified persons.

Where a pass-through entity (other than a FASIT) issues either debt or equity instruments that are secured by regular interests in a FASIT and such instruments bear a yield to maturity greater than the yield on the regular iterests and the applicable Federal rate plus five percentage points (determined on date that the pass-through entity acquires the regular interests in the FASIT) and the pass-through entity issued such debt or equity with a principal purpose of avoiding the rule that high-yield interests be held by corporations, then an excise tax is imposed on the pass-through entity at a rate equal to the highest corporate rate on the income of any holder of such instrument attributable to the regular interests.

Taxation of holder of ownership interest.—All of the FASIT's assets and liabilities are treated as assets and liabilities of the holder of a FASIT ownership interest and that owner takes into account all of the FASIT's income, gain, deduction, or loss in computing its taxable income or net loss for the taxable year. The character of the income to the holder of an ownership interest is the same as its character to the FASIT, except tax-exempt interest is taken into income of the holder as ordinary income.[66]

Losses on assets contributed to the FASIT are not allowed upon their contribution, but may be allowed to the FASIT owner upon their disposition by the FASIT. A special rule provides that the holder of a FASIT ownership interest cannot offset income or gain from the FASIT ownership interest with any other losses. Any net operating loss carryover of the FASIT owner shall be computed by disregarding any income arising by reason arising by reason of a disallowed loss.

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[65] Under this rule, no high-yield interests will be treated as issued where the FASIT directly issues such interests to a disqualified holder.

[66] Ownership interests in a FASIT 95 percent or more of whose assets are real estate mortgages are treated as real estate assets where relevant (e.g., secs. 856, 593, 7701(a)(19)).

For purposes of the alternative minimum tax, the owner's taxable income is determined without regard to the minimum FASIT income. The alternative minimum taxable income of the FASIT owner cannot be less than the FASIT income for that year, and the alternative minimum tax net operating loss deduction is computed without regard to the minimum FASIT income.

Transfers to FASITs

Gain generally is recognized immediately by the owner of the FASIT upon the transfer of assets to a FASIT. Assets that are acquired by the FASIT from someone other than its owner are treated as if they were acquired by the owner and then contributed to the FASIT. In addition, any assets of the FASIT owner or a related person that are used to support[67] FASIT regular interests are treated as contributed to the FASIT and, thus, any gain on any such assets also will be recognized at the earliest date that such assets support any FASIT's regular interests.[68] To the extent provided by Treasury regulations, gain recognition on the contributed assets may be deferred until such assets support regular interests issued by the FASIT or any indebtedness of the owner or related person. These regulations may adjust other statutory FASIT provisions to the extent such provisions are inconsistent with such regulations. For example, such regulations may disqualify certain assets as permitted assets. The basis of any FASIT assets is increased by the amount of the taxable gain recognized on the contribution of the assets to the FASIT.

Valuation rules

In general, except in the case of debt instruments, the value of FASIT assets is their fair market value. In the case of debt instruments that are traded on an established securities market, then the market price will be used for purposes of determining the amount of gain realized upon contribution of such assets to a FASIT. Nonetheless, the Senate amendment contained special rules for valuing other debt instruments for purposes of computing gain on the transfer to a FASIT. Under these rules, the value of such debt instruments is the sum of the present values of the reasonably expected cash flows from such obligations discounted over the weighted average life of such assets. The discount rate is 120 percent of the applicable Federal rate, compounded semiannually, or such other rate that the Treasury Secretary shall prescribe by regulations. For purposes of determining the value of a pool of revolving loan accounts having substantially the same terms, each extension of credit (other than the accrual of interest) is treated as a separate debt instrument and the maturity of the instruments is determined using the reasonably anticipated periodic payment rate at which principal payments will be made as a proportion of their

[67] For this purpose, supporting assets includes any assets that are reasonably expected to directly or indirectly pay regular interests or to otherwise secure or collateralize regular interests. In the case where there is a commitment to make additional contributions to a FASIT, any such assets will not be treated as supporting the FASIT until they are transferred to the FASIT or set aside for such use.

[68] In the case of a securities dealer which may be an eligible holder, the Finance Committee understood that the mark-to-market rule of section 475 will not apply to an ownership interest in a FASIT or assets held in the FASIT.

aggregate outstanding principal assuming that payments are applied to the earliest credit extensions. The Finance Committee understood that reasonably expected cash flows from loans will reflect nonpayment (i.e., losses), early payments (i.e., prepayments), and reasonable costs of servicing the loans. This value shall be used in determining the amount of gain realized upon the contribution of assets to a FASIT even though that value may be different than the value of such assets would be applying a willing buyer/willing seller standard.

Related person

For purposes of the FASIT rules, a person is related to another person if that person bears a relationship to the other person specified in sections 267(b) or 707(b)(1), using a 20-percent ownership test instead of the 50-percent test, or such persons are engaged in trades or businesses under common control as determined under sections 52 (a) or (b).

Related amendments

For purposes of the wash sale rule (sec. 1091), an ownership interest of a FASIT is treated as a "security." In addition, an ownership interest in a FASIT and a residual interest in a pool of debt obligations that are substantially similar to the debt obligations in the FASIT shall be treated as "substantially identical stock or securities". Finally, the wash sale period begins six months before, and ends six months after, the sale of the ownership interest of the FASIT.

Effective date

The Senate amendment would take effect on the date of enactment. The Senate amendment provided a special transition rule for entities (e.g., a trust whose interests are taxed like a partnership) that were in existence on June 10, 1996, that subsequently elect to be a FASIT (called a "pre-effective date FASIT"). Under the special transitional rule, gain is not recognized on property contributed, or deemed contributed, to the FASIT to the extent that any such property is allocable to interests issued by a "pre-effective date FASIT" (called a "pre-FASIT interest"). The portion of such property that is allocable to pre-FASIT interests is to be determined by the Treasury Secretary, except that the property of the entity allocable to "pre-FASIT interests" shall not be less than 107 percent of the aggregate principal amounts of outstanding "pre-FASIT interests."

Conference agreement

The conference agreement follows the Senate amendment with the following changes and clarifications:

The conference agreement modifies the rule under which property that is acquired by a FASIT from someone other than the FASIT's owner or a person related to the FASIT's owner is treated as being first acquired by the FASIT's owner who then transfers that asset to the FASIT. The conference modification would clarify that the deemed acquisition by the FASIT's owner would be for the FASIT's cost in acquiring that asset from the non-owner or related person.

The conference agreement makes a technical modification to the rule which deems gain to be recognized on assets held by the owner of the FASIT or a related person that support any regular interest of the FASIT to clarify that the gain will be deemed realized to the related person when the assets which support a regular interest in the FASIT is held by that related person.

The conference agreement clarifies that the taxable income of the holder of the ownership interest or a high-yield interest, that may not be offset by non-FASIT losses, includes gain and loss from the sale of the ownership interest or high-yield interest. In addition, the conference agreement coordinates the rule that limits a taxpayer's ability to offset REMIC excess inclusion income against net operating losses with this similar rule under the FASIT provisions.

The conference agreement provides that the taxable income of a holder of a FASIT ownership interest cannot be less than the taxable income with respect to the FASIT interest applies to any consolidated group of corporations of which the holder is a member as if the group were a single taxpayer.

The conference agreement makes a technical modification to the wording of a waiver of the rule that treats transfers of high-yield interest to disqualified persons as being ineffective such that the income for such high-yield interests will remain includible in the gross income of the transferor in computing its tax.

The conference agreement limits the rule of the Senate amendment that imposes a corporate tax on a pass-thru entity that issues a debt or equity interest that is supported by a regular interest in a FASIT and has high yield to cases where a principal purpose of such arrangement is the avoidance of the restriction that high-yield interests be held only by qualified holders.

The conference agreement modifies the rule of the Senate amendment which deals with terminations of a FASIT to provide that such terminations become effective on the date of the termination, instead of the beginning of the FASIT's taxable year in which the termination occurs.

The conference agreement provides that an asset which was a permitted asset at the time that it was acquired by the FASIT shall not be treated as an interest in the FASIT, except to the extent provided by regulation issued by the Treasury Secretary. Thus, an instrument acquired by the FASIT as a hedge (e.g., an interest rate swap) will not later become an interest in the FASIT when there is later an obligation by the FASIT to make payments to the counterparty under that hedge instrument.

The conference agreement clarifies that a FASIT may issue regular instruments with fixed rates or, except as provided by regulations issued by the Treasury Secretary, variable rates permitted to be issued by real estate mortgage investment conduits ("REMICs").

The conference agreement clarifies that "interest-only instruments" ("IOs") may be issued by a FASIT as high-yield instruments if the instrument makes payments which consist of a specified portion of the interest payments in permitted assets and that portion does not vary throughout the life of that instrument.

The conference agreement clarifies that foreclosure property, which may be a permitted asset of a FASIT, includes property acquired by foreclosure even though the acquired property is not real property. The conference agreement also grants the Treasury Secretary the power to reduce by regulations the two-year period that foreclosure property may be held as a permitted asset of the FASIT.

The conference agreement clarifies the application of section 475 to a securities dealer that holds an ownership interest in a FASIT. Under this clarification, except as provided in Treasury regulations, if section 475 applies to securities before their transfer to the FASIT, section 475 will continue to apply to securities that have been transferred (or deemed transferred) to the FASIT, except that the amount realized under the mark-to-market rule of section 475 shall be the greater of the securities' value under present law or their value determined under the special valuation rules applicable to FASITs.

The conference agreement deletes in technical amendments the rules that treat an ownership interests in a FASIT (a) as a noncapital asset of a bank or (b) as a permitted asset of a real estate investment trust ("REIT").

The conference agreement provides that a regular interest, but not an ownership interest, in a FASIT is treated as a qualified mortgage of a real estate mortgage investment conduit ("REMIC") if 95 percent or more of the value of the FASIT's assets consists, at all times, of real estate mortgages.

The conference agreement clarifies that a regular interest, but not an ownership interest, in a FASIT is treated as a qualifying asset for purposes of the definition of a domestic building and loan association so long as at least 95 percent of the assets of the FASIT are, at all times, qualified assets.

The conference agreement delays the effective date of the provision from the date of enactment of the provision to September 1, 1997, and extends the special transitional rule to any entity created before that date. The conferees expect that, prior to September 1, 1997, Treasury will issue guidance on how the ownership rule would apply to cases in which the entity that owns the FASIT joins in the filing of a consolidated return with other members of the group that wish to hold an ownership interest in the FASIT.

20. REVISION OF EXPATRIATION TAX RULES

(Secs. 1631–1633 of the Senate amendment.)

Present law

Individuals who relinquish U.S. citizenship with a principal purpose of avoiding U.S. taxes are subject to special tax provisions for 10 years after expatriation. The determination of who is a U.S. citizen for tax purposes, and when such citizenship is lost, is governed by the provisions of the Immigration and Nationality Act, 8 U.S.C. section 1401, et. seq.

An individual who relinquishes his U.S. citizenship with a principal purpose of avoiding U.S. taxes is subject to tax on his or her U.S. source income at the rates applicable to U.S. citizens, rather than the rates applicable to other non-resident aliens, for 10

years after expatriation. In addition, the scope of items treated as U.S. source income for this purpose is broader than those items generally considered to be U.S. source income. For example, gains on the sale of personal property located in the United States and gains on the sale or exchange of stock or securities issued by U.S. persons are treated as U.S. source income. This alternative method of income taxation applies only if it results in a higher U.S. tax liability.

Rules applicable in the estate and gift tax contexts expand the categories of items that are subject to the gift and estate taxes in the case of a U.S. citizen who relinquished citizenship with a principal purpose of avoiding U.S. taxes within the 10-year period ending on the date of the transfer. For example, U.S. property held through a foreign corporation controlled by such individual and related persons is included in his or her estate and gifts of U.S.-situs intangible property by such individual are subject to the gift tax.

House bill

No provision.

Senate amendment

The Senate amendment replaces the present-law expatriation income tax rules with rules that generally subject certain U.S. citizens who relinquish their U.S. citizenship and certain long-term U.S. residents who relinquish their U.S. residency to tax on the net unrealized gain in their property as if such property were sold for fair market value on the expatriation date. The Senate amendment modifies the present-law expatriation estate and gift tax rules to apply to certain long-term U.S. residents and to provide that, for purposes of applying such rules, certain persons would be treated as having relinquished citizenship or residency for a principal purpose of avoiding U.S. taxes. The Senate amendment also imposes information reporting and sharing obligations with respect to U.S. citizens who relinquish their citizenship and long-term residents whose U.S. residency is terminated.

Effective date.—The provision generally is effective for U.S. citizens whose date of relinquishment of citizenship occurs on or after February 6, 1995 and for long-term residents who terminate their U.S. residency on or after such date.

Conference agreement

The conference agreement does not include the Senate amendment provision.

21. MODIFY TREATMENT OF FOREIGN TRUSTS

(Secs. 411–417 of H.R. 3286.)

Present law

Inbound grantor trusts with foreign grantors

Under the grantor trust rules (secs. 671–679), a grantor that retains certain rights or powers generally is treated as the owner of the trust's assets without regard to whether the grantor is a domestic or foreign person. Under these rules, U.S. trust beneficiaries

are not subject to U.S. tax on distributions from a trust where a foreign grantor is treated as owner of the trust, even though no tax may be imposed on the trust income by any jurisdiction. In addition, a special rule provides that if a U.S. beneficiary of an inbound grantor trust transfers property to the foreign grantor by gift, that U.S. beneficiary is treated as the grantor of the trust to the extent of the transfer.

Foreign trusts that are no grantor trusts

Under the accumulation distribution rules (which generally apply to distributions from a trust in excess of the trust's distributable net income for the taxable year), a distribution by a foreign nongrantor trust of previously accumulated income generally is taxed at the U.S. beneficiary's average marginal rate for the prior 5 years, plus interest (secs. 666 and 667). Interest is computed at a fixed annual rate of 6 percent, with no compounding (sec. 668). If adequate records of the trust are not available to determine the proper application of the rules relating to accumulation distributions to any distribution from a trust, the distribution is treated as an accumulation distribution out of income earned during the first year of the trust (sec. 666(d)).

If a foreign nongrantor trust makes a loan to one of its beneficiaries, the principal of such a loan generally is not taxable as income to the beneficiary.

Outbound foreign grantor trusts with U.S. grantors

Under the grantor trust rules, a U.S. person that transfers property to a foreign trust generally is treated as the owner of the portion of the trust comprising that property for any taxable year in which there is a U.S. beneficiary of any portion of the trust (sec. 679(a)). This treatment generally does not apply, however, to transfers by reason of death, to transfers made before the transferor became a U.S. person, or to transfers that represent sales or exchanges of property at fair market value where gain is recognized to the transferor.

Residence of trusts

A trust is treated as foreign if it is not subject to U.S. income taxation on its income that is neither derived from U.S. sources nor effectively connected with the conduct of a U.S. trade or business. Thus, if a trust is taxed in a manner similar to a nonresident alien individual, it is considered to be a foreign trust. Any other trust is treated as domestic.

Section 1491 generally imposes a 35-percent excise tax on a U.S. person that transfers appreciated property to certain foreign entities, including a foreign trust. In the case of a domestic trust that changes its situs and becomes a foreign trust, it is unclear whether property has been transferred from a U.S. person to a foreign entity and, thus, whether the transfer is subject to the excise tax.

Information reporting and penalties related to foreign trusts

Any U.S. person that creates a foreign trust or transfers money or property to a foreign trust is required to report that event to the

Treasury Department without regard to whether the trust is a grantor or a nongrantor trust. Similarly, any U.S. person that transfers property to a foreign trust that has one or more U.S. beneficiaries is required to report annually to the Treasury Department. In addition, any U.S. person that makes a transfer described in section 1491 is required to report the transfer to the Treasury Department.

Any person that fails to file a required report with respect to the creation of, or a transfer to, a foreign trust may be subject to a penalty of 5 percent of the amount transferred to the foreign trust. Similarly, any person that fails to file a required annual report with respect to a foreign trust with U.S. beneficiaries may be subject to a penalty of 5 percent of the value of the corpus of the trust at the close of the taxable year. The maximum amount of the penalty imposed under either case may not exceed $1,000. A reasonable cause exception is available.

Reporting of foreign gifts

There is no requirement to report gifts or bequests from foreign sources.

House bill

No provision. However, sections 411–417 of H.R. 3286 (Adoption Promotion and Stability Act of 1996) contains the following provisions:

Inbound grantor trusts with foreign grantors

The House bill generally applies only to the extent it results, directly or indirectly, in income or other amounts (if any) being currently taken into account in computing the income of a U.S. citizen or resident or a domestic corporation. Certain exceptions apply to this rule. Under one exception, the grantor trust rules continue to apply to the portion of a trust where that portion of the trust is revocable by the grantor either without approval of another person or with the consent of a related or subordinate party who is subservient to the grantor. Under another exception, the grantor trust rules continue to apply to the portion of a trust where the only amounts distributable from that portion during the lifetime of the grantor are to the grantor or the grantor's spouse. The general rule denying grantor trust status does not apply to trusts established to pay compensation, and certain trusts in existence as of September 19, 1995 provided that such trust is treated as owned by the grantor under section 676 or 677 (other than sec. 677(a)(3)).[69] In addition, the grantor trust rules generally apply where the grantor is a controlled foreign corporation (as defined in sec. 957). Finally, the grantor trust rules continue to apply in determining whether a foreign corporation is characterized as a passive foreign investment company ("PFIC"). Thus, a foreign corporation cannot avoid PFIC status by transferring its assets to a grantor trust.

[69] The exception does not apply to the portion of any such trust attributable to any transfers made after September 19, 1995.

If a U.S. beneficiary, or a family member of such a beneficiary,[70] of an inbound grantor trust transfers property to the foreign grantor, such beneficiary generally is treated as a grantor of a portion of the trust to the extent of the transfer. This rule applies without regard to whether the foreign grantor is otherwise treated as the owner of any portion of such trust. However, this rule does not apply if the transfer is a sale of the property for full and adequate consideration or if the transfer is a gift that qualifies for the annual exclusion described in section 2503(b).

The House bill provides a special rule that allows the Secretary of the Treasury to recharacterize a transfer, directly or indirectly, from a partnership or foreign corporation which the transferee treats as a gift or bequest, to prevent the avoidance of the purpose of section 672(f).[71] In a case where a foreign person (that would be treated as the owner of a trust but for the above rule) actually pays tax on the income of the trust to a foreign country, it is anticipated that Treasury regulations will provide that, for foreign tax credit purposes, U.S. beneficiaries that are subject to U.S. income tax on the same income will be treated as having paid the foreign taxes that are paid by the foreign grantor. Any resulting foreign tax credits would be subject to applicable foreign tax credit limitations.

The House bill provides a transition rule for any domestic trust that has a foreign grantor that is treated as the owner of the trust under present law, but becomes a nongrantor trust under the bill. If such a trust becomes a foreign trust before January 1, 1997, or if the assets of such a trust are transferred to a foreign trust before that date, such trust is exempt from the excise tax on transfers to a foreign trust otherwise imposed by section 1491. However, the House bill's new reporting requirements and penalties are applicable to such a trust and its beneficiaries. In addition, the assets of such a trust will be treated as if they were recontributed to a nongrantor trust by the foreign grantor, with no recognition of gain or loss, on the date the trust ceases to be treated as a grantor trust. The nongrantor trust will have the same basis in such assets as did the grantor on the date the trust ceases to be treated as a grantor trust.

Effective date.—The provisions described in this part are effective on the date of enactment.

Foreign trusts that are not grantor trusts

The House bill changes the interest rate applicable to accumulation distributions from foreign trusts from simple interest at a fixed rate of 6 percent to compound interest determined in the same manner as interest imposed on underpayments of tax under section 6621(a)(2). Simple interest is accrued at the rate of 6 percent through 1995. Beginning on January 1, 1996, however, compound interest based on the underpayment rate is imposed not only on tax amounts determined under the accumulation distribution rules but also on the total simple interest for pre-1996 periods, if any. For purposes of computing the interest charge, the accumu-

[70] For this purpose, a family member is generally defined as a brother, sister, spouse, ancestor or lineal descendant.

[71] See discussion below for reporting requirements under the House bill with respect to certain foreign gifts and bequests received by a U.S. person.

lation distribution is allocated proportionately to prior trust years in which the trust has undistributed net income (and the beneficiary receiving the distribution was a U.S. citizen or resident), rather than to the earliest of such years. An accumulation distribution is treated as reducing proportionately the undistributed net income from prior years.

In the case of a loan of cash or marketable securities by the foreign trust to a U.S. grantor or a U.S. beneficiary (or a U.S. person related to such grantor or beneficiary[72]), except, to the extent provided by Treasury regulations, the House bill treats the full amount of the loan as distributed to the grantor or beneficiary. It is expected that Treasury regulations will provide an exception from this treatment for loans with arm's-length terms. In applying this exception, it is further expected that consideration be given to whether there is a reasonable expectation that a loan will be repaid. In addition, any subsequent transaction between the trust and the original borrower regarding the principal of the loan (e.g., repayment) is disregarded for all purposes of the Code. This provision does not apply to loans made to persons that are exempt from U.S. income tax.

Effective date.—The provision to modify the interest charge on accumulation distributions applies to distributions after the date of enactment. The provision with respect to loans to U.S. grantors, U.S. beneficiaries or a related U.S. person related to such a grantor or beneficiary applies to loans made after September 19, 1995.

Outbound foreign grantor trusts with U.S. grantors

The House bill makes several modifications to the general rule of section 679(a)(1) under which a U.S. person who transfer property to a foreign trust generally is treated as the owner of the portion of the trust comprising that property for any taxable year in which there is a U.S. beneficiary of the trust. The House bill also contains an amendment to conform the definition of certain foreign corporations the income of which is deemed to be accumulated for the benefit of a U.S. beneficiary to the definition controlled foreign corporations (as defined in sec. 957(a)).

Sale or exchange at market value.—Present law contains several exceptions to grantor trust treatment under section 679(a)(1) described above. Under one of the exceptions, grantor trust treatment does not result from a transfer of property by a U.S. person to a foreign trust in the form of a sale or exchange at fair market value where gain is recognized to the transferor. In determining whether the trust paid fair markets value to the transferor, the House bill provides that obligations issued (or, to the extent provided by regulations, guaranteed) by the trust, by any grantor or beneficiary of the trust, or by any person related to any grantor or beneficiary[73] (referred to as "trust obligations") generally are not

[72] For this purpose, a person generally would be treated as related to the grantor or beneficiary if the relationship between such person and the grantor or beneficiary would result in a disallowance of losses under section 267 or 707(b), except that in applying section 267(c)(4) an individual's family includes the spouses of the members of the family.

[73] For this purpose, a person is treated as related to the grantor or beneficiary if the relationship between such person and the grantor or beneficiary would result in a disallowance of losses under section 267 or 707(b), except that in applying section 267(c)(4) an individual's family includes the spouses of the members of the family.

taken into account except as provided in Treasury regulations. It is expected that Treasury regulations will provide an exception from this treatment for loans with arm's-length terms. In applying this exception, it is further expected that consideration be given to whether there is a reasonable expectation that a loan will be repaid. Principal payments by the trust on any such trust obligations generally will reduce the portion of the trust attributable to the property transferred (i.e., the portion of which the transferor is treated as the grantor).

Other transfers.—The House bill adds new exception to the general rule of section 679(a)(1) described above. Under the House bill, a transfer of property to certain charitable trusts is exempt from the application of the rules treating foreign trusts with U.S. grantors and U.S. beneficiaries as grantor trusts.

Transferors or beneficiaries who become U.S. persons.—The House bill applies the rule of section 679(a)(1) to certain foreign persons who transfer property to a foreign trust and subsequently become U.S. persons. A nonresident alien individual who transfers property, directly or indirectly, to a foreign trust and then becomes a resident of the United States within 5 years after the transfer generally is treated as making a transfer to the foreign trust on the individual's U.S. residency starting date (as defined in sec. 7701(b)(2)(A)). The amount of the deemed transfer is the portion of the trust (including undistributed earnings) attributable to the property previously transferred. Consequently, the individual generally is treated under section 679(a)(1) as the owner of that portion of the trust in any taxable year in which the trust has U.S. beneficiaries.

Outbound trust migrations.—The House bill applies the rules of section 679(a)(1) to a U.S. person who transferred property to a domestic trust if the trust subsequently becomes a foreign trust while the transferor is still alive. Such a person is deemed to make a transfer to the foreign trust on the date of the migration. The amount of the deemed transfer is the portion of the trust (including undistributed earnings) attributable to the property previously transferred. Consequently, the individual generally is treated under the rules of section 679(a)(1) as the owner of that portion of the trust in any taxable year in which the trust has U.S. beneficiaries.

Effective date.—The provisions to amend section 679 apply to transfers of property after February 6, 1995.

Anti-abuse regulatory authority

The House bill includes an anti-abuse rule which authorizes the Secretary of the Treasury to issue regulations, on or after the date of enactment, that may be necessary or appropriate to carry out the purposes of the rules applicable to estates, trusts and beneficiaries, including regulations to prevent the avoidance of those purposes.

Effective date.—The provision is effective on the date of enactment.

Residence of trusts

The House bill establishes a two-part objective test for determining for tax purposes whether a trust is foreign or domestic. If both parts of the test are satisfied, the trust is treated as domestic. Under the first part of the proposed test, if a U.S. court (i.e., Federal, State, or local) exercises primary supervision over the administration of the trust, the trust is treated as domestic. Under the second part of the proposed test, in order for a trust to be treated as domestic, one or more U.S. fiduciaries must have the authority to control all substantial decisions of the trust.

Under the House bill, if a domestic trust changes its situs and becomes a foreign trust, the trust is treated as having made a transfer of its assets to a foreign trust and is subject to the 35-percent excise tax imposed by present-law section 1491 unless one of the exceptions to this excise tax is applicable.

Effective date.—The provision to modify the treatment of a trust as a U.S. person applies to taxable years beginning after December 31, 1996. In addition, if the trustee of a trust so elects, the provision would apply to taxable years ending after the date of enactment. The amendment to section 1491 is effective on the date of enactment.

Information reporting and penalties relating to foreign trusts

The House bill generally requires the grantor, transferor or executor (i.e., the "responsible party") to file information returns with the Treasury Department upon the occurrence of certain events. The term "reportable event" generally means the creation of any foreign trust by a U.S. person, the direct and indirect transfer of any money or property to a foreign trust, including a transfer by reason of death, and the death of a U.S. citizen or resident if any portion of a foreign trust was included in the gross estate of the decedent. In addition, a U.S. owner of any portion of a foreign trust generally is required to ensure that the trust files an annual return to provide full accounting of all the trust activities for the taxable year. Finally, any U.S. person that receives (directly or indirectly) any distribution from a foreign trust generally is required to file a return to report the name of the trust, the aggregate amount of the distributions received, and other information that the Secretary of the Treasury may prescribe.

Under the House bill, a person that fails to provide the required notice or return in cases involving the transfer of property to a new or existing foreign trust, or a distribution by a foreign trust to a U.S. person, is subject to an initial penalty equal to 35 percent of the gross reportable amount. A failure to provide an annual reporting of trust activities will result in an initial penalty equal to 5 percent of the gross reportable amount.

The House bill provides that if a U.S. owner of any portion of a foreign trust fails to appoint a limited U.S. agent to accept service of process with respect to any requests and summons by the Secretary of the Treasury in connection with the tax treatment of any items related to the trust, the Secretary may determine the tax consequences of amounts to be taken into account under the grantor trust rules. In cases where adequate records are not provided to the Secretary to determine the proper treatment of any distribu-

tions from a foreign trust, the distribution is includible in the gross income of the U.S. distributee and is treated as an accumulation distribution from the middle year of a foreign trust (i.e., computed by taking the number of years that the trust has been in existence divided by 2) for purposes of computing the interest charge applicable to such distribution, unless the foreign trust elects to have a U.S. agent for the limited purpose of accepting service of process (as described above).

Under the House bill, a person that fails to provide the required notice or return in cases involving the transfer of property to a new or existing foreign trust, or a distribution by a foreign trust to a U.S. person, is subject to an initial penalty equal to 35 percent of the gross reportable amount (generally the value of the property involved in the transaction). A failure to provide an annual reporting of trust activities will result in an initial penalty equal to 5 percent of the gross reportable amount. An additional $10,000 penalty is imposed for continued failure for each 30-day period (or fraction thereof) beginning 90 days after the Treasury Department notifies the responsible party of such failure. Such penalties are subject to a reasonable cause exception. In no event will the total amount of penalties exceed the gross reportable amount.

Effective date.—The reporting requirements and applicable penalties generally apply to reportable events occurring or distributions received after the date of enactment. The annual reporting requirement and penalties applicable to U.S. grantors apply to taxable years of such persons beginning after December 31, 1995.

Reporting of foreign gifts

The House bill generally requires any U.S. person (other than certain tax-exempt organizations) that receives purported gifts or bequests from foreign sources total more than $10,000 during the taxable year to report them to the Treasury Department. The threshold for this reporting requirement is indexed for inflation. The definition of a gift to a U.S. person for this purpose excludes amounts that are qualified tuition or medical payments made on behalf of the U.S. person, as defined for gift tax purposes (sec. 2503(e)(2)), and amounts that are distributions to a U.S. beneficiary of a foreign trust if such amounts are properly disclosed under the reporting requirements of the House bill. If the U.S. person fails, without reasonable cause, to report foreign gifts as required, the Secretary of the Treasury is authorized to determine the tax treatment of the unreported gifts. It is intended that the Treasury Secretary's exercise of its authority to make such a determination will be subject to judicial review under a arbitrary or capricious standard, which provides a high degree of deference to such determination. In addition, the U.S. person is subject to a penalty equal to 5 percent of the amount of the gift for each month that the failure continues, with the total penalty not to exceed 25 percent of such amount.

Effective date.—The provision applies to amounts received after the date of enactment.

Senate amendment

No provision.

Conference agreement

The conference agreement adopts the House bill provision of H.R. 3286 with one modification and two clarifications.

If a U.S. beneficiary of an inbound grantor trust transfers property to a foreign grantor, such beneficiary generally is treated as a grantor of a portion of the trust to the extent of the transfer. Under the conference agreement, this provision generally does not apply transfers by a family member of such a beneficiary.

The conferees wish to clarify that in exercising its regulatory authority to treat a U.S. trust as a foreign trust for purposes of information reporting purposes, the Secretary of the Treasury will take into account the information that such a trust reported under the domestic trust reporting rules.

Under the House bill, the section 1491 excise tax applies when a domestic trust changes its situs and becomes a foreign trust after the date of enactment. In addition, under the House bill, a trustee may elect to apply the new objective test for determining the residence of a trust to the taxable year of the trust ending after the date of enactment. The conferees wish to clarify that when a trustee makes this election, and thereby changes the situs of a trust from domestic to foreign, the trust is treated as having made an outbound transfer of its assets on the date of such election. Consequently, the section 1491 excise tax will apply to such a transfer.

22. TREATMENT OF BAD DEBT DEDUCTIONS OF THRIFT INSTITUTIONS

(Sec. 401 of the H.R. 3103 and sec. 611 of the Senate amendment to H.R. 3103.)

Present law

Generally, a taxpayer engaged in a trade or business may deduct the amount of any debt that becomes wholly or partially worthless during the year (the "specific charge-off" method of sec. 166). Certain thrift institutions (building and loan associations, mutual savings banks, or cooperative banks) are allowed deductions for bad debts under rules more favorable than those granted to other taxpayers (and more favorable than the rules applicable to other financial institutions). Qualified thrift institutions may compute deductions for bad debts using either the specific charge-off method or the reserve method of section 593. To qualify for this reserve method, a thrift institution must meet an asset test, requiring that 60 percent of its assets consist of "qualifying assets" (generally cash, government obligations, and loans secured by residential real property). This percentage must be computed at the close of the taxable year, or at the option of the taxpayer, as the annual average of monthly, quarterly, or semiannual computations of similar percentages.

If a thrift institution uses the reserve method of accounting, it must establish and maintain a reserve for bad debts and charge actual losses against the reserve, and is allowed a deduction for annual additions to restore the reserve to its permitted balance. Under section 593, a thrift institution annually may elect to calculate its addition to its bad debt reserve under either (1) the "percentage of taxable income" method applicable only to thrift institu-

tions, or (2) the "experience" method that also is available to small banks.

Under the "percentage of taxable income" method, a thrift institution generally is allowed a deduction for an addition to its bad debt reserve equal to 8 percent of its taxable income (determined without regard to this deduction and with additional adjustments). Under the experience method, a thrift institution generally is allowed a deduction for an addition to its bad debt reserve equal to the greater of: (1) an amount based on its actual average experience for losses in the current and five preceding taxable years, or (2) an amount necessary to restore the reserve to its balance as of the close of the base year. For taxable years beginning before 1988, the "base year" was the last taxable year before the most recent adoption of the experience method (i.e., generally, the last year the taxpayer was on the percentage of taxable income method). For taxable years beginning after 1987, the base year is the last taxable year beginning before 1988. Prior to 1988, computing bad debts under a "base year" rule allowed a thrift institution to claim a deduction for bad debts for an amount at least equal to the institution's actual losses that were charged off during the taxable year.

If a thrift institution becomes a commercial bank, or if the institution fails to satisfy the 60-percent qualified asset test, it is required to change its method of accounting for bad debts and, under proposed Treasury regulations, is required to recapture its bad debt reserve. The percentage-of-taxable-income portion of the reserve generally is included in income ratably over a 6-taxable year period. The experience method portion of the reserve is not restored to income if the former thrift institution qualifies as a small bank. If the former thrift institution is treated as a large bank, the experience method portion of the reserve is restored to income ratably over a 6-taxable year period, or under the 4-year recapture method or the cut-off method described above.

In addition, a thrift institution may be subject to a form of reserve recapture even if the institution continues to qualify for the percentage of taxable income method. Specifically, if a thrift institution distributes to its shareholders an amount in excess of its post-1951 earnings and profits, such excess is deemed to be distributed from the nonexperience potion of the institution's bad debt reserve and is restored to income. In the case of any distribution in redemption of stock or in partial or complete liquidation of an institution, the distribution is treated as first coming from the nonexperience potion of the bad debt reserves of the institution (sec. 593(e)).

House bill

No provision in H.R. 3448. Section 401 of H.R. 3103, the "Health Coverage Availability and Affordability Act of 1996," as passed by the House of Representatives on March 28, 1996, contained the following provision.

Repeal of section 593

The bill repeals the section 593 reserve method of account for bad debts by thrift institutions, effective for taxable years beginning after 1995. Thrift institutions that would be treated as small

banks (as determined under sec. 585(c)(2)) are allowed to utilize the experience method applicable to such institutions, while thrift institutions that are treated as large banks are required to use only the specific charge-off method.

Treatment of recapture of bad debt reserves

In general.—A thrift institution required to change its method of computing reserves for bad debts will treat such change as a change in a method of accounting, initiated by the taxpayer, and having been made with the consent of the Secretary of the Treasury. Any section 481(a) adjustment required to be taken into account with respect to such change generally will be determined solely with respect to the "applicable excess reserves" of the taxpayer. The amount of applicable excess reserves shall be taken into account ratably over a six-taxable year period, beginning with the first taxable year beginning after 1995, subject to the residential loan requirement described below. In the case of a thrift institution that becomes a large bank, the amount of the institution's applicable excess reserves generally is the excess of (1) the balance of its reserves described in section 593(c)(1) other than its supplemental reserve for losses on loans (i.e., its reserve for losses on qualifying real property loans and its reserve for losses on nonqualifying loans) as of the close of its last taxable year beginning before January 1, 1996, over (2) the balance of such reserves (i.e., its reserve for losses on qualifying real property loans and its reserve for losses on nonqualifying loans) as of the close of its last taxable year beginning before January 1, 1988 (i.e., the "pre-1988 reserves"). Similar rules would apply to small banks.

The balance of the pre-1988 reserves is subject to the provisions of section 593(e) (requiring recapture in the case of certain excess distributions to, and redemptions of, shareholders). In addition, the balances of the pre-1988 reserve and the supplemental reserve will be treated as tax attributes to which section 381 applies. Certain internal reorganizations of a group of thrift institutions will not be treated as distributions to shareholders for purposes of section 593(e). Further, if a taxpayer no longer qualifies as a bank (as defined by sec. 581), the balances of the taxpayer's pre-1988 reserve and supplement reserves are restored to income ratably over a six-year period, beginning in the taxable year the taxpayer no longer qualifies as a bank.

Residential loan requirement.—Under a special rule, if the taxpayer meets the "residential loan requirement" for a taxable year, the recapture of the applicable excess reserves otherwise required to be taken into account as a section 481(a) adjustment for such year will be suspended. A taxpayer meets the residential loan requirement if, for the taxable year, the principal amount of residential loans made by the taxpayer during the year is not less than its base amount. The residential loan requirement is applicable only for taxable years that begin after December 31, 1995, and before January 1, 1998, and must be applied separately with respect to each such year.

Treatment of conversions to credit unions

The bill provides that if a thrift institution to which the repeal of section 593 applies becomes a credit union, the credit union will be treated as a institution that is not a bank and any section 481(a) adjustment required to be included in gross income will be treated as derived from an unrelated trade or business.

Effective date

The provision general is effective for taxable years beginning after December 31, 1995. The amendments to section 593(e) do not apply to certain distributions with respect to preferred stock.

Senate amendment

No provision in the Senate amendment to H.R. 3448. Section 611 of the Senate amendment to H.R. 3103, the "Health Coverage Availability and Affordability Act of 1996," as passed by the Senate on April 23, 1996, contained a provision similar to the provision in the House-passed version of H.R. 3103.

Conference agreement

The conference agreement generally follows the provision in the House-and Senate-passed versions of H.R. 3103, with modifications. The following describes the provisions of the conference agreement.

Repeal of section 593

The conference agreement repeals the section 593 reserve method of accounting for bad debts by thrift institutions, effective for taxable years beginning after 1995. Thrift institutions that would be treated as small banks[74] are allowed to utilize the experience method applicable to such institutions, while thrift institutions that are treated as large banks are required to use only the specific charge-off method. Thus, the percentage of taxable income method of accounting for bad debts is no longer available for any financial institution. The conference agreement also repeals the following present-law provisions that only apply to thrift institutions to which section 593 applies: (1) the denial of a portion of certain tax credits to a thrift institution (sec. 50(d)(1)); (2) the special rules with respect to the foreclosure of property securing loans of a thrift institution (sec. 595); (3) the reduction in the dividends received reduction of a thrift institution (sec. 596); and (4) the ability of a thrift institution to use a net operating loss to offset its income from a residual interest in REMIC (sec. 860E(a)(2)).

Treatment of recapture of bad debt reserves

In general.—A thrift institution required to change its method of computing reserves for bad debts will treat such change as a change in a method of accounting initiated by the taxpayer, and having been made with the consent of the Secretary of the Treas-

[74] Under present-law section 581, the definition of a "bank" includes a thrift institution.

ury.[75] Any section 481(a) adjustment required to be taken into account with respect to such change generally will be determined solely with respect to the "applicable excess reserves" of the taxpayer. The amount of applicable excess reserves shall be taken into account ratably over a six-taxable year period, beginning with the first taxable year beginning after 1995, subject to the residential loan requirement described below. In the case of a thrift institution that becomes a "large bank" (as determined under sec. 585(c)(2)), the amount of the institution's applicable excess reserves generally is the excess of (1) the balance of its reserves described in section 593(c)(1) other than its supplemental reserve for losses on loans (i.e., its reserve for losses on qualifying real property loans and its reserve for losses on nonqualifying loans) as of the close of its last taxable year beginning before January 1, 1996, over (2) the balance of such reserves (i.e., its reserve for losses on qualifying real property loans and its reserve for losses on nonqualifying loans) as of the close of its last taxable year beginning before January 1, 1988 (i.e., the "pre-1988 reserves").[76] Thus, a thrift institution that is treated as a large bank generally is required to recapture its post-1987 additions to its bad debt reserves, whether such additions are made pursuant to the percentage of taxable income method or the experience method. The timing of this recapture may be delayed for a one- or two-year period to the extent the residential loan requirement described below applies.

In the case of a thrift institution that becomes a "small bank" (as determined under sec. 585(c)(2)), the amount of the institution's applicable excess reserves will be the excess of (1) the balance of its reserves described in section 593(c)(1) as of the close of its last taxable year beginning before January 1, 1996, over (2) the greater of the balance of: (a) its pre-1988 reserves or (b) what the institution's reserves would have been at the close of its last taxable year beginning before January 1, 1996, had the institution always used the experience method described in section 585(b)(2)(A) (i.e., the six-year average method). For purposes of the future application of section 585, the beginning balance of the small bank's reserve for its first taxable year beginning after December 31, 1995, will be the greater of the two amounts described in (2) in the preceding sentence, and the balance of the reserve at the close of the base year (for purposes of sec. 585(b)(2)(B)) will be the amount of its pre-1988 reserves. The residential loan requirement described below also applies to small banks. If such small bank later becomes a large bank, any section 481(a) adjustment amount required to be taken

[75] The provisions of the conference agreement will apply to a thrift institution that has a taxable year that begins after December 31, 1995, even if such taxable year is a short taxable year that comes to a close because the thrift institution is acquired by a non-thrift institution.

In addition, a thrift institution that uses a reserve method described in section 593 will be deemed to have changed its method of computing reserves for bad debts even though such institution will be allowed to use the reserve method of section 585. Similarly, a large thrift institution will be deemed to have changed its method of computing reserves for bad debts even through such institution used the experience-method portion of section 593 in lieu of the percentage-of-taxable-income method of section 593.

[76] The balance of a taxpayer's pre-1988 reserves is reduced if the taxpayer's loan portfolio had decreased since 1988. The permitted balance of a taxpayer's pre-1988 reserves is reduced by multiplying such balance by the ratio of the balance of the taxpayer's loans outstanding at the close of the last taxable beginning before 1996, to the balance of the taxpayer's loans outstanding at the close of the last taxable beginning before 1988. This reduction is required for both large and small banks.

into account under section 585(c)(3) will not include any portion of the bank's pre-1988 reserve. Similarly, if the bank elects the cut-off method to implement its conversion to large bank status, the amount of the reserve against which the bank charges its actual losses will not include any portion of the bank's pre-1988 reserve and the amount by which the pre-1988 reserve exceeds actual losses will not be included in gross income.

The balance of the pre-1988 reserves is subject to the provisions of section 593(e), as modified by the conference agreement (requiring recapture in the case of certain excess distributions to, and redemptions of, shareholders). Thus, section 593(e) will apply to an institution regardless of whether the institution becomes a commercial bank or remains a thrift institution. In addition, the balances of the pre-1988 reserve and the supplemental reserve will be treated as tax attributes to which section 381 applies. The conferees expect that Treasury regulations will provide rules for the application of section 593(e) in the case of mergers, acquisitions, spin-offs, and other reorganizations of thrift and other institutions.[77] The conferees believe that any such regulations should provide that, if the stock of an institution with a pre-1988 reserve is acquired by another depository institution, the pre-1988 reserve will not be restored to income by reason of the acquisition. Similarly, if an institution with a pre-1988 reserve is merged or liquidated tax-free into a bank, the pre-1988 reserve should not be restored to income by reason of the merger or liquidation. Rather, the bank will inherit the pre-1988 reserve and the post-1951 earnings and profits of the former thrift institution and section 593(e) will apply to the bank as if it were a thrift institution. That is, the pre-1988 reserve will be restored into income in the case of any distribution in redemption of the stock of the bank or in partial or complete liquidation of the bank following the merger or liquidation. In the case of any other distribution, the pre-1988 reserve will not be restored to income unless the distribution is in excess of the sum of the post-1951 earnings and profits inherited from the thrift institution and the post-1913 earnings and profits of the acquiring bank.[78] The conferees expect that Treasury regulations will address the case where the shareholders of an institution with a pre-1988 reserve are "cashed out" in a taxable merger of the institution and a bank. Such regulations may provide that the pre-1988 reserve may be restored to income if such redemption represents a concealed distribution from the former thrift institution. For example, cash received by former thrift shareholders pursuant to a taxable reverse merger may represent a concealed distribution if, im-

[77] The conferees expect that in the case of the merger, acquisition, spin-off, or other reorganization involving only thrift institutions, section 593(e) as modified by the conference agreement, will continue to be applied in a manner similar to the way section 593(e) is applied under present law.

However, guidance will be needed in the case of transactions where one of the parties to the transaction is not a thrift institution. Guidance may be needed because the issue of whether section 593(e) applies in the case where a thrift institution is merged into a bank generally does not arise under present law because such merger results in a charter change and, under proposed Treasury regulations, requires full bad debt reserve recapture.

[78] If the acquiring bank is a former thrift institution itself and the pre-1988 reserves of neither institution are restored to income pursuant to the merger, the conferees expect that the pre-1988 reserves and the post-1951 earnings and profits of the two institutions will be combined for purposes of the continued application of section 593(e) with respect to the combined institution.

mediately preceding the merger, the acquiring bank had no available resources to distribute and its existing debt structure, indenture restriction, financial condition, or regulatory capital requirements precluded it from borrowing money for purposes of making the cash payment to the former thrift shareholders. No inference is intended by the conferees as to the application of section 593(e) to these and similar transactions under present law.

Further, if a taxpayer no longer qualifies as a bank (as defined by sec. 581), the balances of the taxpayer's pre-1988 reserve and supplemental reserves are restored to income ratably over a six-year period, beginning in the taxable year the taxpayer no longer qualifies as a bank.

Residential loan requirement.—Under a special rule, if the taxpayer meets the "residential loan requirement" for a taxable year, the recapture of the applicable excess reserve otherwise required to be taken into account as a section 481(a) adjustment for such year will be suspended. A taxpayer meets the residential loan requirement if, for the taxable year, the principal amount of residential loans made by the taxpayer during the year is not less than its base amount. The residential loan requirement is applicable only for taxable years that begin after December 31, 1995, and before January 1, 1998, and must be applied separately with respect to each such year. Thus, all taxpayers are required to recapture their applicable excess reserves within six, seven, or eight years after the effective date of the provision.

The "base amount" of a taxpayer means the average of the principal amounts of the residential loans made by the taxpayer during the six most recent taxable years beginning before January 1, 1996. At the election of the taxpayer, the base amount may be computed by disregarding the taxable years within that six-year period in which the principal amounts of loans made during such years were highest and lowest. This election must be made for the first taxable year beginning after December 31, 1995, and applies to the succeeding taxable year unless revoked with the consent of the Secretary of the Treasury or his delegate.

For purposes of the residential loan requirement, a loan will be deemed to be "made" by a financial institution to the extent the institution is, in fact, the principal source of the loan financing. Thus, any loan only can be "made" once. The conferees expect that loans "made" by a financial institution may include, but are not limited to, loans (1) originated directly by the institution through its place of business or its employees, (2) closed in the name of the institution, (3) originated by a broker that acts as an agent for the institution, and (4) originated by another person (other than a financial institution) and that are acquired by the institution pursuant to a pre-existing, enforceable agreement to acquire such loans. In addition, Treasury regulations also may provide that loans "made" by a financial institution may include loans originated by another person (other than a financial institution) acquired by the institution soon after origination if such acquisition is pursuant to a customary practice of acquiring such loans from such person. A loan acquired by a financial institution from another financial institution generally will be considered to be made by the transferor rather than the transferee of the loan; however, such loan may be com-

pletely disregarded if a principal purpose of the transfer was to allow the transferor to meet the residential loan requirement. A loan may be considered to be made by a financial institution even if such institution has an arrangement to transfer such loan to the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation.

For purposes of the residential loan requirement, a "residential loan" is a loan described in section 7701(a)(19)(C)(v) (generally, loans secured by residential real and church property and certain mobile homes),[79] but only to the extent the loan is made to the owner of the property to acquire, construct, or improve the property. Thus, mortgage refinancings and home equity loans are not considered to be residential loans, except to the extent the proceeds of the loan are used to acquire, construct, or improve qualified residential real property. The conferees understand that pursuant to the Home Mortgage Disclosure Act, financial institutions are required to disclose the purpose for which loans are made. The conferees further understand that for purposes of this disclosure, institutions are required to classify loans as home purchase loans, home improvement loans, refinancings, and multifamily dwelling loans (whether for purchase, improvement or refinancing of such property). The conferees expect that taxpayers (and the Secretary of the Treasury in promulgating guidance) may take such reporting into account, and make such adjustments as are appropriate,[80] in determining: (1) whether or not a loan qualifies as a "residential loan" and (2) whether the institution "made" the loan. A taxpayer must use consistent standards for determining whether loans qualify as residential loans made by the institution both for purposes of determining its base amount and for purposes of determining whether it met the residential loan requirement for a taxable year.

The residential loan requirement is determined on a controlled group basis. Thus, for example, if a controlled group consists of two thrift institutions with applicable excess reserves that are wholly-owned by a bank, the residential loan requirement will be met (or not met) with respect to both thrift institutions by comparing the principal amount of the residential loans made by all three members of the group during the taxable year to the group's base amount. The group's base amount will be the average principal amount of residential loans made by all three members of the group during the base period. The election to disregard the high and low taxable years during the 6-year base period also would be applied on a controlled group basis (i.e., generally by treating the members of the group as one taxpayer so that all members of the group must join in the election, and the same corresponding years of each member would be so disregarded).

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[79] For this purpose, as under present law, if a multifamily structure securing a loan is used in part for nonresidential purposes, the entire loan will be deemed a residential real property loan if the planned residential use exceeds 80 percent of the property's planned use (determined as of the time the loan is made). In addition, loans made to finance the acquisition or development of land will be deemed to be loans secured by an interest in residential real property if, under regulations prescribed by the Secretary of the Treasury, there is a reasonable assurance that the property will become residential real property within a period of three years from the date of acquisition of the land.

[80] For example, adjustments will be required with respect to the reporting of multifamily dwellings in order to distinguish home purchase, home improvement, and refinancing loans.

Treasury regulations may provide rules for the application of the residential loan requirement in the case of mergers, acquisitions, and other reorganizations of thrift and other institutions. For example, the balance of a taxpayer's applicable excess reserve will be treated as a tax attribute to which section 381 applies. Thus, if an institution with an applicable excess reserve is acquired in a tax-free reorganization, the conferees expect that balance of such reserve will not be immediately restored to income but will continue to be subject to the residential loan requirement in the hands of the acquirer. The conferees further expect that if a financial institution joins or merges into (or leaves) a group of financial institutions, the base amount of the acquiring (or remaining) group will be appropriately adjusted to reflect the base amount of the acquired (or departing) institution for purposes of determining whether the group meets the residential loan requirement for the year of the acquisition (or departure) and subsequent years. Similarly, if a controlled group of institutions had made an election to disregard its high and low years in computing its base amount, it is anticipated that such election shall be binding on any institution that subsequently joins the group and the election shall be applied to the new member by disregarding the high and low years of the new member even if such years do not correspond to the years applicable to the other members of the group.

Treatment of conversions to credit unions

The conference agreement provides that if a thrift institution to which the repeal of section 593 applies becomes a credit union, the credit union will be treated as an institution that is not a bank and any section 481(a) adjustment required to be included in gross income will be treated as derived from an unrelated trade or business. Thus, if a thrift institution becomes a credit union in its first taxable year beginning after December 31, 1995, the entire balance of the institution's bad debt reserve will be included in income, and subject to tax, over a six-year period beginning with such taxable year. No inference is intended as to the Federal income tax treatment of any other aspect of the conversion of a financial institution to a credit union.

Effective date.—The repeal of section 593 is effective for taxable years beginning after December 31, 1995. The repeal of section 595 is effective for property acquired in taxable years beginning after December 31, 1995. The amendment to section 860E does not apply to any residual interest in a REMIC held by the taxpayer on October 31, 1995, and at all times thereafter.

The amendment to section 593(e)(1)(B) does not apply to any distributions with respect to preferred stock (including redemptions of such stock) if: (1) such stock was issued and outstanding as of November 1, 1995, and at all times thereafter before the distribution and (2) such distribution is made within the later of (a) one year after the date of enactment of this Act or (b) if the stock is redeemable by the issuer or a related party, 30 days after the date such stock first may be redeemed. For this purpose, the first date a preferred stock may be redeemed is the day upon which the issuer or a related party has the right to call the stock, regardless of the amount of call premium.

23. REMOVE BUSINESS EXCLUSION FOR ENERGY SUBSIDIES PROVIDED BY PUBLIC UTILITIES

(Sec. 401 of H.R. 3286.)

Present law

Internal Revenue Code section 136, as added by the Energy Policy Act of 1992, provides an exclusion from the gross income of a customer of a public utility for the value of any subsidy provided by the utility for the purchase or installation of an energy conservation measure with respect to a dwelling unit (as defined by sec. 280A(f)(1)). In addition, for subsidies received after 1994, section 136 provides a partial exclusion from gross income for the value of any subsidy provided by a utility for the purchase or installation of an energy conservation measure with respect to property that is not a dwelling unit. The amount of the exclusion is 40 percent of the value for subsidies received in 1995, 50 percent of the value for subsidies received in 1996, and 65 percent of the value for subsidies received after 1996.

For this purpose, an energy conservation measure is any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to property. With respect to property other than a dwelling unit, an energy conservation measure includes "specially defined energy property" (generally, property described in sec. 48(l)(5) of the Code as in effect on the day before the date of enactment of the Revenue Reconciliation Act of 1990).

The exclusion does not apply to payments made to or from a qualified cogeneration facility or a qualifying small power production facility pursuant to section 210 of the Public Utility Regulatory Policy Act of 1978.

Section 136 denies a deduction or credit to a taxpayer (or in appropriate cases requires a reduction in the adjusted basis of property of a taxpayer) for any expenditure to the extent that a subsidy related to the expenditure was excluded from the gross income of the taxpayer.

House bill

No provision in H.R. 3448. Section 401 of H.R. 3286, the "Adoption Promotion and Stability Act of 1996," as passed by the House, repeals the partial exclusion for any subsidy provided by a utility for the purchase or installation of an energy conservation measure with respect to property that is not a dwelling unit.

Effective date.—The provision is effective for subsidies received after December 31, 1996, unless received pursuant to a binding written contract in effect on September 13, 1995, and all times thereafter.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the provision in H.R. 3286.

VII. TAX TECHNICAL CORRECTIONS PROVISIONS

House bill

The House bill contains technical, clerical, and conforming amendments to the Revenue Reconciliation Act of 1990, the Revenue Reconciliation Act of 1993, and other recently enacted tax legislation.

Senate amendment

The Senate amendment is the same as the House bill, except as follows:

(a) Expiration date of special ethanol blender refund (sec. 1703(k) of the Senate amendment)

The Senate amendment corrects a 1990 drafting error by conforming the expiration date for an excise tax expedited refund provision for gasohol blenders to that for gasoline tax provisions generally.

(b) Estate tax freezes (sec. 1702(f) of the House bill and the Senate amendment)

The House bill includes a provision (also contained in prior technical corrections bills) to provide a special definition of "applicable family member" for purposes of determining control under section 2701 of the Code (relating to special valuation rules in case of transfers of certain interests in corporations or partnerships). The Senate amendment does not include this provision.

(c) Certain property not treated as section 179 property (sec. 1704(u) of the House bill and sec. 1702(h)(19) of the Senate amendment)

The House bill includes a provision denying the section 179 expensing allowance to (1) property described in section 50(b) (generally property used outside the United States, property used in connection with furnishing lodging, property used by tax exempt organizations, governments and foreign persons); (2) air conditioning or heating units; and (3) horses. The provision is effective for property placed in service after May 14, 1996.

The Senate amendment does not deny the expensing allowance for horses. The provision in the Senate amendment is effective as if included in the Revenue Reconciliation Act of 1990.

Conference agreement

The conference agreement follows the House bill and the Senate amendment with respect to identical provisions, with one modification. That modification deletes the technical correction related to a Tax Reform Act of 1986 transition rule allowing tax-exempt bonds to be issued for certain facilities. The 1986 provision to which that technical correction relates expired after December 31, 1990, and the correction has been rendered moot by passage of time.

With regard to the differing provisions, the conference agreement includes the following:

(a) Expiration date of special ethanol blender refund

The conference agreement follows the Senate amendment.

(b) Estate tax freezes

The conference agreement follows the House bill.

(c) Certain property not treated as section 179 property

The conference agreement follows the Senate amendment.

(d) Intermediate sanctions penalty provisions

The conference agreement corrects a drafting error in the Taxpayer Bill of Rights II (H.R. 2337) with respect to the additional filing and disclosure rules imposed on certain tax-exempt organizations as part of the intermediate sanctions provisions. The conference agreement increases (from $10 to $20 per each day of failure) present-law penalties that apply when a tax-exempt organization fails to allow public inspection of its annual returns (sec. 6652(c)(1)(C)) or fails to allow public inspection of its application for recognition of tax-exempt status (sec. 6652(c)(1)(D)). In addition, the conference agreement increases the section 6652(c)(1)(C) maximum penalty with respect to any one return from $5,000 to $10,000.

TRADE PROVISIONS

GENERALIZED SYSTEM OF PREFERENCES

Subtitle J of Title I of the conference agreement, the Generalized System of Preferences (GSP) Renewal Act of 1996, is a substitute amendment to Title V of the Trade Act of 1974, which expired on July 31, 1995. As indicated below, the conference agreement reinstates several provisions of expired law without change.

1. BASIC AUTHORITY

Expired law

Section 501 of the Trade Act of 1974, as amended, (Generalized System of Preferences) grants authority to the President to provide duty-free treatment to imports of eligible articles from designated Beneficiary Developing Countries (BDCs), subject to certain conditions and limitations.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reinstates the expired section 501 of Title V, without change.

2. DESIGNATION OF BENEFICIARY DEVELOPING COUNTRIES

Expired law

Section 502 of the Trade Act of 1974 sets forth both the procedures for designating countries as Beneficiary Developing Countries (BDCs) and the conditions for such designation. This section establishes conditions for designation which are mandatory and others which are discretionary. With regard to mandatory conditions, the President is prohibited from designating any country for GSP benefits which is a developed country listed in section 502(b). Further, the term "country" is defined as any foreign country, any overseas dependent territory or possession of a foreign country, or the Trust Territory of the Pacific Islands.

Under Section 502(b), the President is prohibited from designating specific developed countries as BDCs: Australia, Austria, Canada, European Union member states, Finland, Iceland, Japan, Monaco, New Zealand, Norway, Sweden, and Switzerland.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement amends the definition of country to include "any territory" and deletes the reference in section 502(b) to Austria, Finland, and Sweden which are now European Union member states.

3. MANDATORY CONDITIONS

Expired law

Under section 502(c) the President is prohibited from designating as a BDC a country which:

(a) is a Communist country, unless (i) its products receive non-discriminatory most-favored-nation (MFN) treatment, (ii) it is a GATT Contracting Party and a member of the International Monetary Fund (IMF), and (iii) it is not dominated or controlled by international communism;

(b) is an OPEC member, or a party to another arrangement, and participates in an action the effect of which is to withhold supplies of vital commodity resources from international trade or raise their price to an unreasonable level and to cause disruption of the world economy, subject to trade agreement exemptions consistent with objectives under the Trade Act of 1974;

(c) affords "reverse preferences" having or likely to have a significant adverse effect on U.S. commerce, unless the President receives satisfactory assurances of elimination before January 1, 1976;

(d) has nationalized or expropriated U.S. property, or taken similar actions, unless compensation is made, being negotiated, or in arbitration;

(e) fails to recognize as binding or enforce arbitral awards in favor of U.S. citizens;

(f) aids or abets, by granting sanctuary from prosecution to, any individual or group which has committed an act of international terrorism; and

(g) has not taken or is not taking steps to afford internationally recognized worker rights to its workers.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reinstates expired law, except, with respect to mandatory conditions: in (a)(ii), replaces "is a GATT contracting party" with "is a Member of the World Trade Organization."; in (b), deletes the reference to OPEC member and the exemption authority; in (c), deletes the satisfactory assurances exemption for reverse preferences.

4. DISCRETIONARY CRITERIA

Expired law

Under section 502(c) of the Trade Act of 1974 the President must take into account a list of factors in determining whether to designate a country a BDC, including whether or not other major developed countries are granting GSP to the country, whether or not the country has taken or is taking steps to afford its workers internationally recognized workers rights, and the extent to which the country is providing adequate and effective intellectual property protection.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement makes no substantive change to the expired provision, but makes a technical change to the intellectual property rights criterion.

5. GRADUATION OF BDC'S

Expired law

Countries are graduated from GSP eligibility if the per capita GNP of any BDC for any year exceeds a dollar limit ($11,800 in 1994), indexed annually under a formula starting with the base amount of $500 in 1984. When the income level reaches this amount, such country is subject to a 25, rather than 50, percent competitive need import share limit on all eligible articles for up

to the following two years. After that time, the country is no longer treated as a BDC.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement substitutes "high income" country as designated by the World Bank (approximately $8,600 per capita GNP in 1994), for the per capita GNP indexing formula in current law. Thus, if the President determines that a BDC has become a "high income" country as designated by the World Bank, the President is required to remove the country from eligibility under the program. Although the Conference agreement would reinstate a transition period of up to two years for country graduation from the GSP program, it would eliminate application of the 25 percent competitive need limit during this phase-out period.

6. DESIGNATION OF ELIGIBLE ARTICLES

a. Exempted products

Expired law

Under Section 503 of the Trade Act of 1974 the President may not designate any article as GSP eligible within the following categories of import-sensitive articles:

(a) textile and apparel articles which are subject to textile agreements;

(b) watches, except watches entered after June 30, 1989 that the President determines will not cause material injury to watch or watch band, strap, or bracelet manufacturing and assembly operations in the United States or U.S. insular possessions;

(c) import-sensitive electronic articles;

(d) import-sensitive steel articles;

(e) footwear, handbags, luggage, flat goods, work gloves, and leather wearing apparel which were not GSP eligible articles on April 1, 1984;

(f) import-sensitive semi-manufactured and manufactured glass products; and

(g) any other articles the President determines to be import-sensitive in the context of GSP.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reinstates provisions of expired law, except, with respect to changes in the following statutory exemp-

tions: in (a), it replaces the expired provision with exemption of textile and apparel articles which were not GSP eligible on January 1, 1994 and; in (e) it applies exemption to footwear and related articles which were not GSP eligible on January 1, 1995.

b. Three-year rule

Expired law

Each year the U.S. Trade Representative (USTR) conducts an interagency review process in which products can be added to or removed from the GSP program, or in which a country's compliance with eligibility requirements can be reviewed. The reviews are normally based on petitions filed by interested parties, but may also be self-initiated by USTR.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement prohibits consideration of an article for designation of eligibility for three years following formal consideration and denial of that article.

c. Least developed developing countries (LDDCs)

Expired law

No provision.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement provides specific authority for the President to designate any article that is the growth, product, or manufacture of a least-developed developing country (LDDC) as an eligible article with respect to imports from LDDCs, if, after receiving advice from the International Trade Commission, the President determines such an article is not import-sensitive in the context of imports from LDDCs. This authority does not apply to statutorily exempt articles—textiles and apparel, footwear and related articles, and watches. The President shall notify Congress at least 60 days in advance of LDDC designations. LDDC designations will be based on overall economic and discretionary criteria for country designation under the GSP program.

7. LIMITS ON PREFERENTIAL AUTHORITY

Expired law

Under Section 504 of the Trade Act of 1974, the President may withdraw, suspend, or limit GSP duty-free treatment with respect to any article or any country, except that no duty may be established other than the rate of duty which would otherwise apply (the MFN rate), after considering both the policy objectives and the discretionary BDC designation factors of the GSP program. The President shall withdraw or suspend the BDC designation of any country if he determines that, as a result of changed circumstances, the country would be barred from designation.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reinstates expired law.

8. COMPETITIVE NEED LIMITS

Expired law

Whenever the President determines that exports by any BDC to the United States of a GSP eligible article during any year—

(a) exceed a dollar limit ($122 million in 1995) based on $25 million adjusted annually relative to changes in the U.S. GNP since 1974, or

(b) equal or exceed a 50 percent share of the total value of U.S. imports of the article,

then, no later than July 1 of the next year, such country is not treated as a BDC with respect to such article.

Not later than January 4, 1987, and periodically thereafter, the President must conduct a general review of eligible articles and, if he determines that a BDC has demonstrated a sufficient degree of competitiveness relative to other BDCs on any eligible article, then a lower competitive need dollar limit ($41.9 million in 1993, indexed annually from 1984 base) and 25 percent total import share limit apply.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reduces the basic competitive need limit to $75 million for any year beginning January 1, 1996, and substitutes a standard annual increase of $5 million for the indexing formula in expired law. The 50 percent import share limit is

reinstated. The conference agreement deletes the general review requirements and the lower competitive need limits.

9. AUTHORITY TO WAIVE COMPETITIVE NEED LIMITS

Expired law

The President may waive the dollar and import share competitive need limits on any eligible article of any BDC if he (1) receives ITC advice on the likely effect of the waiver on any U.S. industry; (2) determines, based on the overall GSP and discretionary country designation considerations and the ITC advice, that the waiver is in the U.S. national economic interest; and (3) publishes the determination in the Federal Register.

The import share competitive need limit may be disregarded if total U.S. imports of the eligible article during the preceding year do not exceed a de minimis amount of $5 million adjusted annually ($13.4 million in 1994) according to changes in U.S. GNP since 1979. The import share competitive need limit does not apply to any eligible article if a like or directly competitive article was not produced in the United States as of January 3, 1985.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reinstates the expired waiver authority. Under the conference Agreement the import share competitive need limit does not apply if the article is not produced in the United States as of January 1, 1995. The conference Agreement also reinstates the de minimis import provision, but substitutes $13 million in 1996 and a standard annual increase of $500,000 beginning January 1, 1996 for the indexing formula in expired law.

10. OTHER PROVISIONS REGARDING WAIVER AUTHORITY, REPORTS, AND AGRICULTURE EXPORTS

a. Waiver trade limits

Expired law

Under section 504(c)(3)(D) of the Trade Act of 1974, the President may not exercise the competitive need waiver authority in any year on imports of eligible articles exceeding:

(a) 30 percent of total GSP duty-free imports during the preceding year, or

(b) 15 percent of total GSP duty-free imports during the preceding year from BDCs which had (i) a per capita GNP of $5,000 or more, or (ii) exported to the United States more than 10 percent of total GSP duty-free imports during that year.

The President may waive competitive need limits in certain cases where there has been a historical preferential trade relationship between the United States and that country.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reinstates provisions in expired law regarding waiver trade limits, and historical preferences.

b. Report on workers rights

Expired law

The President must submit an annual report to the Congress on the status of internationally recognized workers' rights within each BDC.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reinstates expired law.

c. Agriculture exports

Expired law

Section 506 requires that appropriate U.S. agencies assist BDCs in developing and implementing measures designed to ensure that the production of agricultural sectors of their economies is not directed to export markets, to the detriment of the foodstuff production for their citizens.

House bill

No provision.

Senate bill

No provision.

Conference agreement

The conference agreement reinstates expired law.

11. PROVISIONS REGARDING TERMINATION AND EFFECTIVE DATES

Expired law

No duty-free treatment shall remain in effect after July 31, 1995.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement reauthorizes the program for one year, ten months, to terminate on May 31, 1997. The effective date of the extension of the GSP program is October 1, 1996. However, the conference agreement also provides that, notwithstanding section 514 of the Tariff Act of 1930 or any other provision of law, the entry (1) of any article to which duty-free treatment under Title V of the Trade Act of 1974 would have applied if the entry had been made on July 31, 1995, and (2) that was made after July 31, 1995, and before January 1, 1996, shall be liquidated or reliquidated as free of duty and the Secretary of the Treasury shall refund any duty paid, upon proper request filed with the appropriate customs officer, within 180 days after the date of enactment. Further, the conference agreement provides that notwithstanding section 514 of the Tariff Act of 1930 or any other provision of law, the entry (1) of any article to which duty-free treatment under Title V of 1974 (as amended by this Title) would have applied if the entry had been made on or after October 1, 1996, and (2) that was made after December 31, 1995, and before October 1, 1996, shall be liquidated or reliquidated as free of duty and the Secretary of the Treasury shall refund any duty paid, upon proper request filed with the appropriate customs officer, within 180 days after the date of enactment. Although importers would be entitled to request such refunds after the date of enactment of the bill, reimbursement of duties would occur only after the beginning of fiscal year 1997 (October 1, 1996).

REMOVAL OF BARRIERS TO INTERETHNIC ADOPTION

Present law

State law governs adoption and foster care placement. Many States permit race matching of foster and adoptive parents with children either in regulation, statute, policy, or practice. The Howard M. Metzenbaum Multiethnic Placement Act of 1994 ("Metzenbaum Act", Public Law 103–382) permits States to consider race and ethnicity in selecting a foster care or adoptive home, but States cannot delay or deny the placement of the child solely on the basis of race, color, or national origin.

Noncompliance with the Metzenbaum Act is deemed a violation of Title VI of the Civil Rights Act of 1964.

House bill

Section 553 of the Metzenbaum Act is repealed. In addition, Section 471 of the Social Security Act is amended to prohibit a State or other entity that receives Federal assistance from denying to any person the opportunity to become an adoptive or a foster parent on the basis of the race, color, or national origin of the person or of the child involved. Similarly, so State or other entity receiving Federal funds can delay or deny the placement of a child for adoption or foster care in making a placement, on the basis of

the race, color, or national origin of the adoptive or foster parent or the child involved.

Section 474 of the Social Security Act is amended to require the Secretary of the Department of Health and Human Services (HHS) to reduce the amount of Federal foster care and adoption funds provided to the State through Title IV–E if the State program is found in violation of this provision as a result of a review conducted under Section 1123 of the Social Security Act. States found to be in violation would have their quarterly funds reduced by 2 percent for the first violation, by 5 percent for the second violation, and by 10 percent for the third or subsequent violation.

Private entities found to be in violation of this provision for a quarter are required to return to the Secretary all federal funds received from the State during the quarter. Any individual who is harmed by a violation of this provision may seek redress in any United States district court. An action under this provision may not be brought more than two years after the alleged violation occurred.

Noncompliance with this provision constitutes a violation of Title VI of the Civil Rights Act of 1964. The Indian Child Welfare Act of 1978 is not affected by changes made in this title.

Effective date.—This provision applies upon enactment (except States must meet the State plan requirement provision of bill section 201(a) not later than January 1, 1997).

Senate amendment

The Senate amendment is the same as the House bill, except that the Senate amendment clarifies that the Secretary of HHS shall apply penalties in conformance with section 1123 procedures to include an opportunity for the State to adopt and implement a corrective action plan. The provision clarifies that penalties will be assessed on a fiscal year basis. The amendment limits to 25 percent the maximum amount the Secretary of HHS can reduce a State's grant in a quarter.

Conference agreement

The conference agreement follows the House bill and the Senate amendment with modifications. If the State has failed to correct the violation within six months (or less, at the Secretary's discretion), the Secretary shall impose penalties. The amount of the graduated penalties or set at 2, 3, and 5 percent respectively. The total amount of penalties which can be applied in a fiscal year cannot exceed 5 percent of a State's total IV–E grant.

The Indian Child Welfare Act of 1978 is not affected by changes made in this title.

Effective date.—The provisions related to civil rights enforcement are effective upon enactment. The provisions related to State plan requirements are effective on January 1, 1997.

TITLE II

Senate Amendments 2 through 6: Senate amendments 2 through 6 made technical corrections in the section numbering in title II of the House bill. The House receded from its disagreement

to Senate amendments 2 through 6 with technical changes to the House bill and other changes described in this statement.

1. EMPLOYEE COMMUTING FLEXIBILITY ACT

House bill

The House bill would clarify the Portal-to-Portal Act of 1947 to allow employers and employees to agree on the use of employer-provided vehicles to commute to and from work at the beginning and end of the workday, without the commuting time being treated as hours of work.

Senate amendment

Same.

Conference agreement

Follow House and Senate language.

2. MINIMUM WAGE INCREASE

House bill

The House bill would increase the minimum wage in two increments. Beginning July 1, 1996 the minimum wage would increase from $4.25 to $4.75, and beginning July 1, 1997 the minimum wage would increase from $4.75 to $5.15.

Senate amendment

Same.

Conference agreement

Beginning October 1, 1996, the minimum wage would increase from $4.25 to $4.75, and beginning September 1, 1997, the minimum wage would increase from $4.75 to $5.15. The conference agreement also makes a technical change to avoid retroactively increasing the minimum wage in Puerto Rico by also striking section 6(c) of the Fair Labor Standards Act.

3. COMPUTER PROFESSIONALS EXEMPTION

House bill

The House bill specifies that computer professionals who are paid at least $27.63 per hour (maintaining current law) are exempt from overtime wages.

Senate amendment

Same.

Conference agreement

Follow House and Senate language.

4. TIP CREDIT

House bill

The Fair Labor Standards Act (FLSA) currently contains a tip credit system whereby employers of tipped employees may count tips received by the worker for up to 50 percent of the employer's

minimum wage obligation. In the event that an employee's cash wages and tips do not meet the statutory minimum wage, the employer must contribute the amount of wages necessary for the employee to make at least the minimum wage.

The House bill sets the cash wage paid by employers to tipped employees at $2.13 and allows tips to be counted toward the remainder of the minimum wage obligation. The employer would be required to make up any difference between the minimum wage and the combination of $2.13 plus tips to ensure that each employee makes at least the minimum wage.

Senate amendment

Same.

Conference agreement

Follows House and Senate language except makes technical changes including the technical change of deleting the word "cash" before "wage" where it appears in paragraph (2).

5. OPPORTUNITY WAGE

House bill

The House bill allows employers to pay new hires under 20 years of age not less than $4.25 per hour for the first 90 days (calendar days—not days of work) after the employee is hired. The House bill contains protections for current workers by prohibiting employers from taking any action to displace any employee in order to hire a worker at the opportunity wage.

Senate amendment

Same.

Conference agreement

Follow House and Senate language.

ESTIMATED BUDGET EFFECTS OF THE CONFERENCE AGREEMENT RELATING TO THE REVENUE PROVISIONS OF H.R. 3448, THE "SMALL BUSINESS JOB PROTECTION ACT OF 1996,"

Fiscal Years 1996-2006

[Millions of Dollars]

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	1996-00	1997-01	1996-06
I. IDENTICAL PROVISIONS															
Small Business and Other Tax Provisions															
A. Small Business Provisions															
1. FICA tip credit:															
a. Provided for off-premises employees	1/1/97	---	-6	-14	-15	-16	-17	-18	-18	-19	-20	-21	-51	-68	-165
b. Clarification of effective date	[1]	*Negligible Revenue Effect*													
2. Clarify exemption from FICA taxes for certain fishermen and provide that exemption applies even if crew member receives de minimis amounts of cash payments	[2]	-1	-10	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	-11	-11	-13
B. Provisions Relating to S Corporations															
1. Increase number of eligible shareholders	tyba 12/31/96	---	-5	-14	-16	-20	-22	-25	-28	-31	-35	-39	-55	-77	-235
2. Permit certain trusts to hold stock in S corporations	tyba 12/31/96	---	-2	-2	-2	-2	-2	-2	-2	-3	-3	-3	-8	-10	-23
3. Extend holding period for certain trusts	tyba 12/31/96	---	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[5]	[6]	[7]
4. Financial institutions permitted to hold safe-harbor debt	tyba 12/31/96	---	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	-1
5. Authority to validate certain invalid elections	tyba 12/31/82	---	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	-1
6. Allow interim closing of the books	tyba 12/31/96	*Negligible Revenue Effect*													
7. Expand post-termination period and amend subchapter S audit procedures	tyba 12/31/96	---	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	-1
8. S corporations permitted to hold S or C subsidiaries	tyba 12/31/96	---	-5	-9	-11	-13	-15	-17	-20	-23	-26	-29	-38	-53	-168
9. Treatment of distributions during loss years	tyba 12/31/96	---	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	-1
10. Treatment of S corporations as shareholders in C corporations	tyba 12/31/96	---	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[5]	[6]	[7]
11. Elimination of certain earnings and profits of S corporations	tyba 12/31/96	---	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[5]	[6]	[7]
12. Treatment of certain losses carried over under at-risk rules	tyba 12/31/96	---	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[5]	[6]	[7]
13. Adjustments to basis of inherited S stock	dda DOE	---	[8]	[8]	[8]	[8]	[8]	[8]	[8]	[8]	[8]	[8]	[8]	[8]	[8]
14. Treatment of certain real estate held by an S corporation	tyba 12/31/96	---	-1	-1	-2	-2	-2	-2	-2	-2	-2	-2	-6	-8	-18
15. Transition rule for elections after termination	tyba 12/31/96	---	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[4]	[5]	[6]	[7]
16. Interaction of subchapter S changes except for ESOP and financial institution proposals	---	--	-3	-26	-32	-37	-38	-39	-40	-40	-40	-40	-98	-136	-335

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	1996-00	1997-01	1996-06
Pension Simplification Provisions															
A. Simplified Distribution Rules															
1. Repeal of $5,000 exclusion of employees' death benefits	dda DOE	---	28	49	52	54	55	55	56	57	57	58	183	238	521
2. Simplified method for taxing annuity distributions under certain employer plans	asda 90 da DOE	---	22	28	28	29	29	29	30	30	31	31	107	136	287
3. Minimum required distributions	yba 12/31/96	---	-1	-4	-4	-4	-4	-4	-4	-4	-4	-4	-13	-17	-37
B. Increased Access to Retirement Savings Plans -															
1. Tax-exempt organizations eligible under section 401(k)	yba 12/31/96	---	-8	-22	-24	-25	-26	-28	-29	-30	-31	-31	-79	-105	-254
C. Nondiscrimination Provisions															
1. Repeal of family aggregation rules [9]	yba 12/31/96	---	[10]	[10]	*Considered in Other Provisions*								[10]	[10]	[10]
2. Modification of additional participation requirements	yba 12/31/96	*Negligible Revenue Effect*													
3. Definition of compensation for section 415 purposes	yba 12/31/97	---	---	-1	-1	-2	-2	-2	-2	-2	-3	-3	-4	-6	-18
4. Safe-harbor nondiscrimination rules for qualified cash or deferred arrangements and matching contributions [11]	yba 12/31/98	---	---	---	-46	-166	-171	-175	-180	-186	-191	-196	-211	-382	-1,309
D. Miscellaneous Provisions															
1. Plans covering self-employed individuals	yba 12/31/96	*Negligible Revenue Effect*													
2. Elimination of special vesting rule for multiemployer plans	yba 12/31/96	---	[3]	-1	-1	-1	-1	-1	-1	-1	-1	-1	-3	-4	-9
3. Distributions under rural cooperative plans	DOE	*Negligible Revenue Effect*													
4. Treatment of governmental plans under section 415	yba 12/31/94	*Negligible Revenue Effect*													
5. Uniform retirement age [9]	yba 12/31/96	---	[10]	[10]	*Considered in Other Provisions*								[10]	[10]	[10]
6. Contributions on behalf of disabled employees	yba 12/31/96	*Negligible Revenue Effect*													
7. Treatment of deferred compensation plans of State and local governments and tax-exempt organizations	tyba 12/31/96	---	[3]	-1	-1	-1	-2	-2	-2	-2	-2	-2	-3	-5	-15
8. Correction of GATT interest and mortality rate provisions in the Retirement Protection Act	[12]	---	-4	-4	-4	---	---	---	---	---	---	---	-12	-12	-12
9. Application of elective deferral limit to section 403(b) plans	tyba 12/31/95	*Negligible Revenue Effect*													
10. Increase section 4975 excise tax on prohibited transactions from 5% to 10%	ptoa DOE	---	2	4	4	4	4	4	4	4	4	4	14	18	38
11. Treatment of leased employees	yba 12/31/96	*Negligible Revenue Effect*													
12. Uniform penalty provision to apply to certain pension reporting requirements	1/1/97	*No Revenue Effect*													
13. Clarify that SECA does not apply to certain parsonage allowance income	ybboia 12/31/94	*Negligible Revenue Effect*													
14. Date of adoption of plan amendments	DOE	*No Revenue Effect*													
15. Require section 457 plan assets to be held in trust; transition rule for existing plans	DOE	--	-7	-21	-24	-25	-25	-26	-27	-28	-29	-30	-77	-102	-242

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	1996-00	1997-01	1996-06
16. Multiple salary reduction agreements permitted under section 403(b)	tyba 12/31/95	*Negligible Revenue Effect*													
SUBTOTAL: Identical Provisions		—	-16	-64	-113	-242	-264	-268	-280	-295	-310	-323	-425	-679	-2,161
II. PROVISIONS AGREED UPON															
Small Business and Other Tax Provisions															
A. Small Business Provisions															
1. Increase in expensing limitation for small businesses to $18,000 for 1997, $18,500 for 1998, $19,000 for 1999, $20,000 for 2000, $24,000 for 2001, $24,000 for 2002, $25,000 for 2003 and thereafter [13]	tyba 12/31/96	—	-67	-180	-261	-331	-763	-938	-786	-646	-439	-265	-839	-1,602	-4,676
2. Treatment of storage of product samples	tyba 12/31/95	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	-2
3. Provide that certain charitable risk pools would qualify as charitable organizations under section 501(c)(3)	tyba DOE	—	[3]	-1	-1	-1	-1	-2	-2	-2	-3	-3	-3	-4	-16
4. Treatment of certain dues paid to agricultural or horticultural organizations	tyba 12/31/86	*Negligible Revenue Effect*													
5. Require purchasers of fish in excess of $600 in cash to provide information reports	12/31/97	—	—	5	9	10	10	11	11	11	12	12	24	34	91
6. Change related-party and maximum size requirements for first-time farmer industrial development bonds	bia DOE	—	-1	-6	-12	-17	-21	-26	-30	-34	-37	-40	-36	-57	-224
7. Clarify that newspaper carriers and distributors are independent contractors	spa 12/31/95	*Negligible Revenue Effect*													
8. Provide involuntary conversion treatment for Presidentially declared disaster areas	DDA 12/31/94	-6	-14	-10	-10	-10	-10	-10	-10	-10	-10	-10	-50	-54	-110
9. Provide 15-year depreciation for gas station/convenience stores	ppiso/a/b DOE	-7	-24	-37	-45	-50	-53	-53	-55	-61	-42	-25	-163	-209	-452
10. Leasehold improvements provision	lida 6/12/96	-12	-22	-19	-16	-13	-11	-7	-4	-2	1	4	-82	-81	-101
11. Worker classification:															
a. Clarification of Section 530 safe harbor	spa 12/31/96	—	[3]	[3]	[3]	[3]	[3]	-1	-1	-1	-1	-1	-1	-1	-6
b. Provide that if the taxpayer reclassifies independent contractors as employees, this change does not alter the application of the safe harbor for prior periods	pa 12/31/96	—	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[4]	[4]	[4]
c. Clarify "substantially similar position"	pa 12/31/96	*Negligible Revenue Effect*													
12. Allow certain teaching hospitals to provide tax-free housing to medical faculty	tyba 12/31/95	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[4]	[4]	[15]
B. Extension of Certain Expiring Provisions															
1. Extend the work opportunity tax credit, with modifications through 9/30/97 [16]	10/1/96	—	-116	-141	-82	-32	-12	-2	—	—	—	—	-371	-383	-385

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	1996-00	1997-01	1996-06
2. Employer-provided educational assistance; extend for graduate education through 6/30/96; undergraduate education sunset 5/31/97	1/1/95	-68	-934	-103	---	---	---	---	---	---	---	---	-1,105	-1,037	-1,105
3. Permanent extension of FUTA exemption for alien agricultural workers [17]	1/1/95	-5	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-17	-15	-35
4. R&E credit, with modifications through 5/31/97	7/1/96	-101	-331	-872	-208	-148	-77	-17	---	---	---	---	-1,660	-1,636	-1,754
5. Orphan drug tax credit through 5/31/97 with section 39 benefits	7/1/96	-6	-16	-1	-1	-1	-1	[3]	[3]	[3]	[3]	[3]	-25	-20	-26
6. Contribution of appreciated stock to private foundations through 5/31/97	7/1/96	-14	-104	-10	-4	---	---	---	---	---	---	---	-132	-118	-132
7. Extend section 29 binding contract date to 12/31/96 and placed-in-service date to 6/30/98 for biomass and coal	---	---	---	-8	-34	-60	-69	-65	-57	-55	-56	-58	-59	-171	-236	-522
8. Suspend excise tax on motorboat diesel through 12/31/97	DOE + 7 days	-4	-34	-9	---	---	---	---	---	---	---	---	---	-47	-43	-47
C. Provisions Relating to S Corporations																
1. Treat financial institutions that do not use the reserve method as eligible corporations	tyba 12/31/96	---	-1	-3	-5	-6	-8	-10	-12	-14	-15	-16	-15	-23	-90	
2. Permit tax-exempts to be subchapter S shareholders with UBTI inclusion and ESOP benefit restriction	tyba 12/31/97	---	---	-3	-9	-11	-13	-15	-17	-19	-21	-23	-23	-36	-131	
Pension Simplification Provisions																
A. Simplified Distribution Rules																
1. Repeal of 5-year income averaging for lump-sum distributions	tyba 12/31/99	---	74	77	108	78	70	44	17	15	---	---	337	407	483	
B. Increased Access to Retirement Savings Plans -																
1. Establish SIMPLE pension plan	yba 12/31/96	---	-50	-76	-79	-81	-84	-87	-91	-94	-97	-101	-286	-370	-840	
2. Increase availability of spousal IRAs	yba 12/31/96	---	-57	-168	-184	-195	-206	-219	-233	-248	-264	-281	-604	-810	-2,055	
C. Nondiscrimination Provisions																
1. Simplified definition of highly compensated employees; employers can elect whether or not to apply a top 20% test [9]	yba 12/31/96	---	[15]	[15]	*Considered in Other Provisions*								[4]	[4]	[4]	
D. Miscellaneous Provisions																
1. Treatment of Indian tribal governments under section 403(b)	cpb 1/1/95	*Negligible Revenue Effect*														
2. Allow waiver of 30-day waiting period for qualified plan distributions	pyba 12/31/96	*Negligible Revenue Effect*														
3. Repeal of combined plan limit	lyba 12/31/99	---	---	---	---	-72	-195	-201	-207	-213	-219	-226	-72	-267	-1,333	
4. 3-year waiver of excess distribution tax	1/1/97	---	42	44	47	32	---	---	---	---	---	---	165	165	165	
5. Direct IRS to develop model forms for																

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	1996-00	1997-01	1996-06
qualified domestic relations orders ("QDRO") and reputable consent provisions	DOE	*Negligible Revenue Effect*													
6. Permit volunteer firefighters to make deferrals under section 457 (limited to $3,000 per year)	do/a 1/1/97	---	-2	-5	-7	-9	-11	-13	-16	-18	-20	-23	-23	-34	-124
7. Alternative nondiscrimination rules for certain plans that provide for early participation	1/1/99	---	---	---	-6	-17	-18	-19	-19	-20	-20	-20	-23	-41	-139
8. Clarify definition of plan assets	1/1/75	*Negligible Revenue Effect*													
9. Church pension plan simplification:															
a. Allow pension plan coverage for self-employed clergy	yba 12/31/96	*Negligible Revenue Effect*													
b. Allow church pension plans to use the new definition of highly compensated employee in the bill - Treasury safe harbor	yba 12/31/96	*Negligible Revenue Effect*													
c. Allow payroll deduction of pension contributions for clergy on foreign missions	tyba 12/31/96	*Negligible Revenue Effect*													
10. Grant IRS the discretion to waive pension liquidity shortfall excise tax	[12]	---	-4	-3	-2	-1	[3]	[3]	[3]	[3]	[3]	[3]	-11	-11	-11
Foreign Simplification															
1. Repeal of excess passive assets provision (section 956A)	---	---	-11	-22	-29	-36	-41	-45	-51	-57	-64	-71	-98	-139	-427
Other Provisions															
1. Exempt from diesel dyeing requirement any States exempt from Clean Air Act dyeing requirement	fcqa DOE	---	[3]	-1	-1	-1	-1	-1	-1	-1	-1	-1	-2	-3	-6
2. Application of common paymaster rules to certain agency accounts at State universities [17]	rpa 12/31/96	---	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]	[14]
3. Exempt imported recycled halons from ozone-depleting chemicals tax	cia 12/31/96	---	-1	-1	-1	-1	-1	-1	-1	-1	-1	-1	-4	-4	-9
4. Suspend excise tax on ozone depleting chemicals used in metered dose inhalers	DOE + 7 days	---	-12	-8	-8	-2	---	---	---	---	---	---	-30	-30	-30
5. Alaska Power Authority:															
a. Authorize tax-exempt bonds for purchase of Alaska Power Authority	bia DOE	---	-1	-1	-1	-1	-1	-1	-1	-1	-1	-1	-4	-5	-10
b. Proceeds from asset sale; foregone receipts from electricity sale [18]	DOE	---	76	-7	-7	-7	-7	-7	-7	-7	-7	-7	55	48	13
6. Allow for tax-free conversion of common trust funds to mutual funds	ta 12/31/95	-4	-9	-8	-8	-8	-8	-8	-9	-9	-9	-9	-37	-41	-89
7. Clarify that State prepaid tuition plans are tax-exempt entities; clarify OID rules	tyba 12/31/95	*Negligible Revenue Effect*													

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	1996-00	1997-01	1996-06
Revenue Offsets															
1. Possessions tax credit: Wage credit companies - 6 years of present law, thereafter subject to income cap, followed by 4-year phaseout with modified base period, then repealed; income companies - 2 years of present law followed by 8 years subject to income cap, then repealed; QPSII - repealed later of taxable years beginning after 12/31/95 or earnings after 6/30/96 with estimated payment adjustment; permit base adjustment for asset acquisition	tyba 12/31/95	111	697	586	589	490	507	736	1,105	1,378	1,678	2,686	2,473	2,869	10,563
2. Repeal 50% interest income exclusion for financial institution loans to ESOPs [19]	lma DOE	10	64	105	144	182	220	256	292	327	360	327	505	715	2,287
3. Apply look-through rule for purposes of characterizing certain subpart F insurance income as UBTI, with amendment	---	1	3	4	4	5	5	5	6	6	7	8	17	21	54
4. Corporate accounting - reform of income forecast method	ppisa 9/13/95	32	69	29	13	14	16	19	22	28	31	35	157	141	308
5. Modify exclusion of damages received on account of personal injury or sickness	ara DOE	3	50	55	59	61	64	68	71	74	77	80	228	289	662
6. Repeal advance refunds of diesel fuel tax for diesel cars and light trucks	vpa DOE	1	15	19	19	19	19	19	19	19	19	19	73	91	187
7. Phase out and extend luxury automobile excise tax through 12/31/02	soa DOE + 7 days	-4	-56	-105	-132	124	183	140	32	---	---	---	-173	14	182
8. Modify two county tax-exempt bond rule for local furnishers of electricity or gas; prohibit new local furnishers (with current service areas grandfathered)	[20]	---	---	3	-3	-6	-4	-3	[3]	7	13	15	-5	-9	23
9. Reinstate Airport and Airway Trust Fund excise taxes through 12/31/96, with (1) exemption for fixed-wing emergency medical aircraft, and mining, oil, and gas industry helicopters for flights not using FAA services; (2) clarification of collection point; and (3) clarification of tax treatment of travel on corporate aircraft in affiliated groups	tp7data DOE	28	1,528	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	1,556	1,528	1,555
10. Modify basis adjustment rules under section 1033	lca DOE	---	1	5	9	14	20	29	37	46	56	64	29	49	281
11. Treatment of certain insurance on retired lives	tyba 12/31/95	---	2	1	-2	5	2	[3]	10	-5	2	-3	6	8	12
12. Modified guaranteed contracts	tyba 12/31/95	---	-3	3	2	2	-1	-1	[3]	[3]	[3]	[3]	5	4	1
13. Tax-free treatment of contributions in aid of construction for water utilities; change depreciation for water utilities	[21]	---	-21	-9	-3	11	24	35	45	55	64	73	-22	2	274

Provision	Effective	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	1996-00	1997-01	1996-06
14. Permit scholarship funding corporation to convert to taxable corporation	1/1/97	---	3	6	8	10	10	9	7	6	5	4	26	36	68
15. Apply math error rules for dependency exemptions and filing status when correct taxpayer identification numbers are not provided	rd 30 da DOE	---	133	272	262	249	242	234	226	217	209	201	916	1,158	2,245
16. Provide for flow through treatment for Financial Asset Securitization Investment Trusts (FASITs)	9/1/97	---	---	92	48	8	-3	-9	-14	-19	-25	-32	148	146	47
Technical Corrections															
1. Luxury excise tax, and other technical corrections [13]	---	14	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	14	[3]	13
Additional Provisions															
1. Extend GSP through 5/31/97 [17] [22]	---	---	-817	---	---	---	---	---	---	---	---	---	-817	-817	-817
2. $5,000 nonrefundable adoption credit and employer-provided assistance exclusion;$6,000 special needs; non-special needs sunset after 2001; AGI phaseout beginning at $75,000	tyba 12/31/96	---	-19	-204	-332	-355	-366	-348	-222	-139	-129	-119	-910	-1,276	-2,234
3. 6 month delay of electronic funds transfer	---	---	---	---	---	---	---	---	---	---	---	---	---	---	---
4. Remove business exclusion for energy subsidies provided by public utilities	tyba 12/31/96	---	63	100	104	107	109	111	113	115	116	117	374	483	1,055
5. Repeal bad debt reserve deduction for thrift institutions, with residential loan test for 1996 and 1997	tyba 12/31/95	47	111	216	280	277	272	260	247	111	36	29	931	1,156	1,886
6. Modify treatment of foreign trusts	[23]	52	143	171	180	188	197	206	214	223	245	260	734	879	2,079
NET TOTALS		**67**	**316**	**-316**	**250**	**160**	**-269**	**-190**	**347**	**663**	**1,135**	**2,271**	**471**	**136**	**4,413**

Joint Committee on Taxation

NOTE: Details may not add to totals due to rounding.
Enactment date is assumed to be August 1, 1996.

Legend for "Effective" column: ara = amounts received after
asda = annuity starting date after
bia = bonds issued after
cia = chemicals imported after
cpb = contracts purchased before
dda = decedents dying after
DDA = disasters declared after
do/a = deferrals on or after
DOE = date of enactment
fcqa = first calendar quarter after

[Footnotes for Table #96-0 218 appear on the following page]

Footnotes continued:

ica = involuntary conversions after
lida = leasehold improvements disposed of after
lma = loans made after
lyba = limitation years beginning after
pa = periods after
ppisa = property placed in service after
ppiso/a/b = property placed in service on, after, or before
ptoa = prohibited transactions occurring after
pyba = plan years beginning after
rd 30 da = returns due 30 days after
rpa = remuneration paid after
•o/a = sales on or after
spa = services performed after
ta = transfers after
tyba = taxable years beginning after
tp7data DOE = tickets purchased 7 days after date of enactment for travel 7 days after date of enactment
yba = years beginning after
ybbo/a = years beginning before, on, or after
vpa = vehicles purchased after
90 da DOE = 90 days after date of enactment

[1] Effective as if included in the Omnibus Reconciliation Act of 1993.
[2] The provision applies to remuneration paid after 12/31/94, and also is effective with respect to remuneration paid after 12/31/84, and before 1/1/85, unless the payor treated such remuneration (when paid) as being subject to FICA taxes.
[3] Loss of less than $500,000.
[4] Loss of less than $5 million.
[5] Loss of less than $15 million.
[6] Loss of less than $20 million.
[7] Loss of less than $30 million.
[8] Gain of less than $1 million.
[9] Revenue effect after 1/1/99 included in the revenue estimate for the safe harbor provision due to interactions between this provision and Item II. Pension C.4.
[10] Negligible revenue effect.
[11] This provision considers interaction effects of SIMPLE retirement plan provisions (Items I. Pension C.1, I. Pension D.5, and II. Pension C.1).
[12] Effective as if included in the General Agreement on Tariffs and Trade of 1994.
[13] The technical correction relating to expensing is included in the increase in expensing limitation provision (Item II. Small Business A.1).
[14] Loss of less than $1 million.
[15] Loss of less than $10 million.
[16] Credit rate at 35% on first $6,000 of income; eligible workers expanded to include enterprise zone/community youth, welfare cash recipients, veteran foodstamp recipients, and 18 - 24 year olds living in a household receiving food stamps for a period of at least 6 months on the date of hire without pre-certification; 400 hour work requirement; 21 day certification requirement.
[17] Estimates provided by the Congressional Budget Office.
[18] Estimate provided by the Congressional Budget Office. Negative numbers indicate that Federal outlays will increase; positive numbers indicate that Federal outlays will decrease.
[19] The repeal would not apply to loans made pursuant to a binding contract entered into before 6/10/96.
[20] Effective generally date of enactment; placed in service before 1/1/97 for limitation on new local furnishers.
[21] Effective for amounts received after 6/12/96 and property placed in service after 6/12/96 with the exception of certain property subject to a binding contract before 6/10/96.
[22] Amounts are payable after 9/30/96.
[23] Various effective dates depending on provisions.

From the Committee on Ways and Means, for consideration of the House bill (except for title II) and the Senate amendment numbered 1, and modifications committed to conference:

BILL ARCHER,
PHIL CRANE,
BILL THOMAS,
SAM GIBBONS,
CHARLES B. RANGEL,

As additional conferees from the Committee on Economic and Educational Opportunities, for consideration of secs. 1704(h)(1)(B) and 1704(l) of the House bill and secs. 1421(d), 1442(b), 1442(c), 1451, 1457, 1460(b), 1460(c), 1461, 1465, and 1704(h)(1)(B) of the Senate amendment numbered 1, and modifications committed to conference:

WILLIAM F. GOODLING,
CASS BALLENGER,

As additional conferees from the Committee on Economic and Educational Opportunities, for consideration of title II of the House bill and the Senate amendments numbered 2–6, and modifications committed to conference:

WILLIAM F. GOODLING,
H.W. FAWELL,
FRANK RIGGS,
WILLIAM L. CLAY,
MAJOR R. OWENS,
MAURICE HINCHEY,
Managers on the Part of the House.

From the Committee on Labor and Human Resources:

NANCY LANDON KASSEBAUM,
EDWARD M. KENNEDY,
JIM JEFFORDS,

From the Committee on Finance:

BILL ROTH,
JOHN H. CHAFEE,
CHUCK GRASSLEY,
ORRIN G. HATCH,
AL SIMPSON,
LARRY PRESSLER,
DANIEL P. MOYNIHAN,
MAX BAUCUS,
DAVID PRYOR,
JOHN D. ROCKEFELLER IV,
Managers on the Part of the Senate.

Public Law 104–191
104th Congress, H.R. 3103[1]
August 21, 1996

An Act to amend the Internal Revenue Code of 1986 to improve portability and continuity of health insurance coverage in the group and individual markets, to combat waste, fraud, and abuse in health insurance and health care delivery, to promote the use of medical savings accounts, to improve access to long-term care services and coverage, to simplify the administration of health insurance, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

* * * * * *

TITLE III—TAX-RELATED HEALTH PROVISIONS

SEC. 300. AMENDMENT OF 1986 CODE.

Except as otherwise expressly provided, whenever in this title an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

Subtitle A—Medical Savings Accounts

SEC. 301. MEDICAL SAVINGS ACCOUNTS.

(a) IN GENERAL.—Part VII of subchapter B of chapter 1 (relating to additional itemized deductions for individuals) is amended by redesignating section 220 as section 221 and by inserting after section 219 the following new section:

"SEC. 220. MEDICAL SAVINGS ACCOUNTS.

"(a) DEDUCTION ALLOWED.—In the case of an individual who is an eligible individual for any month during the taxable year, there shall be allowed as a deduction for the taxable year an amount equal to the aggregate amount paid in cash during such taxable year by such individual to a medical savings account of such individual.

"(b) LIMITATIONS.—

"(1) IN GENERAL.—The amount allowable as a deduction under subsection (a) to an individual for the taxable year shall not exceed the sum of the monthly limitations for months during such taxable year that the individual is an eligible individual.

"(2) MONTHLY LIMITATION.—The monthly limitation for any month is the amount equal to 1/12 of—

"(A) in the case of an individual who has self-only coverage under the high deductible health plan as of the first day of such month, 65 percent of the annual deductible under such coverage, and

"(B) in the case of an individual who has family coverage under the high deductible health plan as of the

[1]This publication of the law is restricted to excerpts involving tax matters.

first day of such month, 75 percent of the annual deductible under such coverage.

"(3) SPECIAL RULE FOR MARRIED INDIVIDUALS.—In the case of individuals who are married to each other, if either spouse has family coverage—

"(A) both spouses shall be treated as having only such family coverage (and if such spouses each have family coverage under different plans, as having the family coverage with the lowest annual deductible), and

"(B) the limitation under paragraph (1) (after the application of subparagraph (A) of this paragraph) shall be divided equally between them unless they agree on a different division.

"(4) DEDUCTION NOT TO EXCEED COMPENSATION.—

"(A) EMPLOYEES.—The deduction allowed under subsection (a) for contributions as an eligible individual described in subclause (I) of subsection (c)(1)(A)(iii) shall not exceed such individual's wages, salaries, tips, and other employee compensation which are attributable to such individual's employment by the employer referred to in such subclause.

"(B) SELF-EMPLOYED INDIVIDUALS.—The deduction allowed under subsection (a) for contributions as an eligible individual described in subclause (II) of subsection (c)(1)(A)(iii) shall not exceed such individual's earned income (as defined in section 401(c)(1)) derived by the taxpayer from the trade or business with respect to which the high deductible health plan is established.

"(C) COMMUNITY PROPERTY LAWS NOT TO APPLY.—The limitations under this paragraph shall be determined without regard to community property laws.

"(5) COORDINATION WITH EXCLUSION FOR EMPLOYER CONTRIBUTIONS.—No deduction shall be allowed under this section for any amount paid for any taxable year to a medical savings account of an individual if—

"(A) any amount is contributed to any medical savings account of such individual for such year which is excludable from gross income under section 106(b), or

"(B) if such individual's spouse is covered under the high deductible health plan covering such individual, any amount is contributed for such year to any medical savings account of such spouse which is so excludable.

"(6) DENIAL OF DEDUCTION TO DEPENDENTS.—No deduction shall be allowed under this section to any individual with respect to whom a deduction under section 151 is allowable to another taxpayer for a taxable year beginning in the calendar year in which such individual's taxable year begins.

"(c) DEFINITIONS.—For purposes of this section—

"(1) ELIGIBLE INDIVIDUAL.—

"(A) IN GENERAL.—The term 'eligible individual' means, with respect to any month, any individual if—

"(i) such individual is covered under a high deductible health plan as of the 1st day of such month,

"(ii) such individual is not, while covered under a high deductible health plan, covered under any health plan—

"(I) which is not a high deductible health plan, and

"(II) which provides coverage for any benefit which is covered under the high deductible health plan, and

"(iii)(I) the high deductible health plan covering such individual is established and maintained by the employer of such individual or of the spouse of such individual and such employer is a small employer, or

"(II) such individual is an employee (within the meaning of section 401(c)(1)) or the spouse of such an employee and the high deductible health plan covering such individual is not established or maintained by any employer of such individual or spouse.

"(B) CERTAIN COVERAGE DISREGARDED.—Subparagraph (A)(ii) shall be applied without regard to—

"(i) coverage for any benefit provided by permitted insurance, and

"(ii) coverage (whether through insurance or otherwise) for accidents, disability, dental care, vision care, or long-term care.

"(C) CONTINUED ELIGIBILITY OF EMPLOYEE AND SPOUSE ESTABLISHING MEDICAL SAVINGS ACCOUNTS.—If, while an employer is a small employer—

"(i) any amount is contributed to a medical savings account of an individual who is an employee of such employer or the spouse of such an employee, and

"(ii) such amount is excludable from gross income under section 106(b) or allowable as a deduction under this section,

such individual shall not cease to meet the requirement of subparagraph (A)(iii)(I) by reason of such employer ceasing to be a small employer so long as such employee continues to be an employee of such employer.

"(D) LIMITATIONS ON ELIGIBILITY.—

"For limitations on number of taxpayers who are eligible to have medical savings accounts, see subsection (i).

"(2) HIGH DEDUCTIBLE HEALTH PLAN.—

"(A) IN GENERAL.—The term 'high deductible health plan' means a health plan—

"(i) in the case of self-only coverage, which has an annual deductible which is not less than $1,500 and not more than $2,250,

"(ii) in the case of family coverage, which has an annual deductible which is not less than $3,000 and not more than $4,500, and

"(iii) the annual out-of-pocket expenses required to be paid under the plan (other than for premiums) for covered benefits does not exceed—

"(I) $3,000 for self-only coverage, and

"(II) $5,500 for family coverage.

"(B) SPECIAL RULES.—

"(i) EXCLUSION OF CERTAIN PLANS.—Such term does not include a health plan if substantially all of its coverage is coverage described in paragraph (1)(B).

"(ii) SAFE HARBOR FOR ABSENCE OF PREVENTIVE CARE DEDUCTIBLE.—A plan shall not fail to be treated as a high deductible health plan by reason of failing to have a deductible for preventive care if the absence of a deductible for such care is required by State law.

"(3) PERMITTED INSURANCE.—The term 'permitted insurance' means—

"(A) Medicare supplemental insurance,

"(B) insurance if substantially all of the coverage provided under such insurance relates to—

"(i) liabilities incurred under workers' compensation laws,

"(ii) tort liabilities,

"(iii) liabilities relating to ownership or use of property, or

"(iv) such other similar liabilities as the Secretary may specify by regulations,

"(C) insurance for a specified disease or illness, and

"(D) insurance paying a fixed amount per day (or other period) of hospitalization.

"(4) SMALL EMPLOYER.—

"(A) IN GENERAL.—The term 'small employer' means, with respect to any calendar year, any employer if such employer employed an average of 50 or fewer employees on business days during either of the 2 preceding calendar years. For purposes of the preceding sentence, a preceding calendar year may be taken into account only if the employer was in existence throughout such year.

"(B) EMPLOYERS NOT IN EXISTENCE IN PRECEDING YEAR.—In the case of an employer which was not in existence throughout the 1st preceding calendar year, the determination under subparagraph (A) shall be based on the average number of employees that it is reasonably expected such employer will employ on business days in the current calendar year.

"(C) CERTAIN GROWING EMPLOYERS RETAIN TREATMENT AS SMALL EMPLOYER.—The term 'small employer' includes, with respect to any calendar year, any employer if—

"(i) such employer met the requirement of subparagraph (A) (determined without regard to subparagraph (B)) for any preceding calendar year after 1996,

"(ii) any amount was contributed to the medical savings account of any employee of such employer with respect to coverage of such employee under a high deductible health plan of such employer during such preceding calendar year and such amount was excludable from gross income under section 106(b) or allowable as a deduction under this section, and

"(iii) such employer employed an average of 200 or fewer employees on business days during each preceding calendar year after 1996.

"(D) SPECIAL RULES.—

"(i) CONTROLLED GROUPS.—For purposes of this paragraph, all persons treated as a single employer under subsection (b), (c), (m), or (o) of section 414 shall be treated as 1 employer.

"(ii) PREDECESSORS.—Any reference in this paragraph to an employer shall include a reference to any predecessor of such employer.

"(5) FAMILY COVERAGE.—The term 'family coverage' means any coverage other than self-only coverage.

"(d) MEDICAL SAVINGS ACCOUNT.—For purposes of this section—

"(1) MEDICAL SAVINGS ACCOUNT.—The term 'medical savings account' means a trust created or organized in the United States exclusively for the purpose of paying the qualified medical expenses of the account holder, but only if the written governing instrument creating the trust meets the following requirements:

"(A) Except in the case of a rollover contribution described in subsection (f)(5), no contribution will be accepted—

"(i) unless it is in cash, or

"(ii) to the extent such contribution, when added to previous contributions to the trust for the calendar year, exceeds 75 percent of the highest annual limit deductible permitted under subsection (c)(2)(A)(ii) for such calendar year.

"(B) The trustee is a bank (as defined in section 408(n)), an insurance company (as defined in section 816), or another person who demonstrates to the satisfaction of the Secretary that the manner in which such person will administer the trust will be consistent with the requirements of this section.

"(C) No part of the trust assets will be invested in life insurance contracts.

"(D) The assets of the trust will not be commingled with other property except in a common trust fund or common investment fund.

"(E) The interest of an individual in the balance in his account is nonforfeitable.

"(2) QUALIFIED MEDICAL EXPENSES.—

"(A) IN GENERAL.—The term 'qualified medical expenses' means, with respect to an account holder, amounts paid by such holder for medical care (as defined in section 213(d)) for such individual, the spouse of such individual, and any dependent (as defined in section 152) of such individual, but only to the extent such amounts are not compensated for by insurance or otherwise.

"(B) HEALTH INSURANCE MAY NOT BE PURCHASED FROM ACCOUNT.—

"(i) IN GENERAL.—Subparagraph (A) shall not apply to any payment for insurance.

"(ii) EXCEPTIONS.—Clause (i) shall not apply to any expense for coverage under—

"(I) a health plan during any period of continuation coverage required under any Federal law,

"(II) a qualified long-term care insurance contract (as defined in section 7702B(b)), or

"(III) a health plan during a period in which the individual is receiving unemployment compensation under any Federal or State law.

"(C) MEDICAL EXPENSES OF INDIVIDUALS WHO ARE NOT ELIGIBLE INDIVIDUALS.—Subparagraph (A) shall apply to an amount paid by an account holder for medical care of an individual who is not an eligible individual for the month in which the expense for such care is incurred only if no amount is contributed (other than a rollover contribution) to any medical savings account of such account holder for the taxable year which includes such month. This subparagraph shall not apply to any expense for coverage described in subclause (I) or (III) of subparagraph (B)(ii).

"(3) ACCOUNT HOLDER.—The term 'account holder' means the individual on whose behalf the medical savings account was established.

"(4) CERTAIN RULES TO APPLY.—Rules similar to the following rules shall apply for purposes of this section:

"(A) Section 219(d)(2) (relating to no deduction for rollovers).

"(B) Section 219(f)(3) (relating to time when contributions deemed made).

"(C) Except as provided in section 106(b), section 219(f)(5) (relating to employer payments).

"(D) Section 408(g) (relating to community property laws).

"(E) Section 408(h) (relating to custodial accounts).

"(e) TAX TREATMENT OF ACCOUNTS.—

"(1) IN GENERAL.—A medical savings account is exempt from taxation under this subtitle unless such account has ceased to be a medical savings account. Notwithstanding the preceding sentence, any such account is subject to the taxes imposed by section 511 (relating to imposition of tax on unrelated business income of charitable, etc. organizations).

"(2) ACCOUNT TERMINATIONS.—Rules similar to the rules of paragraphs (2) and (4) of section 408(e) shall apply to medical savings accounts, and any amount treated as distributed under such rules shall be treated as not used to pay qualified medical expenses.

"(f) TAX TREATMENT OF DISTRIBUTIONS.—

"(1) AMOUNTS USED FOR QUALIFIED MEDICAL EXPENSES.—Any amount paid or distributed out of a medical savings account which is used exclusively to pay qualified medical expenses of any account holder shall not be includible in gross income.

"(2) INCLUSION OF AMOUNTS NOT USED FOR QUALIFIED MEDICAL EXPENSES.—Any amount paid or distributed out of a medical savings account which is not used exclusively to pay the qualified medical expenses of the account holder shall be included in the gross income of such holder.

"(3) EXCESS CONTRIBUTIONS RETURNED BEFORE DUE DATE OF RETURN.—

"(A) IN GENERAL.—If any excess contribution is contributed for a taxable year to any medical savings account of an individual, paragraph (2) shall not apply to distributions from the medical savings accounts of such individual (to the extent such distributions do not exceed the aggregate excess contributions to all such accounts of such individual for such year) if—

"(i) such distribution is received by the individual on or before the last day prescribed by law (including extensions of time) for filing such individual's return for such taxable year, and

"(ii) such distribution is accompanied by the amount of net income attributable to such excess contribution.

Any net income described in clause (ii) shall be included in the gross income of the individual for the taxable year in which it is received.

"(B) EXCESS CONTRIBUTION.—For purposes of subparagraph (A), the term 'excess contribution' means any contribution (other than a rollover contribution) which is neither excludable from gross income under section 106(b) nor deductible under this section.

"(4) ADDITIONAL TAX ON DISTRIBUTIONS NOT USED FOR QUALIFIED MEDICAL EXPENSES.—

"(A) IN GENERAL.—The tax imposed by this chapter on the account holder for any taxable year in which there is a payment or distribution from a medical savings account of such holder which is includible in gross income under paragraph (2) shall be increased by 15 percent of the amount which is so includible.

"(B) EXCEPTION FOR DISABILITY OR DEATH.—Subparagraph (A) shall not apply if the payment or distribution is made after the account holder becomes disabled within the meaning of section 72(m)(7) or dies.

"(C) EXCEPTION FOR DISTRIBUTIONS AFTER MEDICARE ELIGIBILITY.—Subparagraph (A) shall not apply to any payment or distribution after the date on which the account holder attains the age specified in section 1811 of the Social Security Act.

"(5) ROLLOVER CONTRIBUTION.—An amount is described in this paragraph as a rollover contribution if it meets the requirements of subparagraphs (A) and (B).

"(A) IN GENERAL.—Paragraph (2) shall not apply to any amount paid or distributed from a medical savings account to the account holder to the extent the amount received is paid into a medical savings account for the benefit of such holder not later than the 60th day after the day on which the holder receives the payment or distribution.

"(B) LIMITATION.—This paragraph shall not apply to any amount described in subparagraph (A) received by an individual from a medical savings account if, at any time during the 1-year period ending on the day of such receipt, such individual received any other amount described in subparagraph (A) from a medical savings account which was not includible in the individual's gross income because of the application of this paragraph.

"(6) COORDINATION WITH MEDICAL EXPENSE DEDUCTION.—For purposes of determining the amount of the deduction under section 213, any payment or distribution out of a medical savings account for qualified medical expenses shall not be treated as an expense paid for medical care.

"(7) TRANSFER OF ACCOUNT INCIDENT TO DIVORCE.—The transfer of an individual's interest in a medical savings account

to an individual's spouse or former spouse under a divorce or separation instrument described in subparagraph (A) of section 71(b)(2) shall not be considered a taxable transfer made by such individual notwithstanding any other provision of this subtitle, and such interest shall, after such transfer, be treated as a medical savings account with respect to which such spouse is the account holder.

"(8) TREATMENT AFTER DEATH OF ACCOUNT HOLDER.—

"(A) TREATMENT IF DESIGNATED BENEFICIARY IS SPOUSE.—If the account holder's surviving spouse acquires such holder's interest in a medical savings account by reason of being the designated beneficiary of such account at the death of the account holder, such medical savings account shall be treated as if the spouse were the account holder.

"(B) OTHER CASES.—

"(i) IN GENERAL.—If, by reason of the death of the account holder, any person acquires the account holder's interest in a medical savings account in a case to which subparagraph (A) does not apply—

"(I) such account shall cease to be a medical savings account as of the date of death, and

"(II) an amount equal to the fair market value of the assets in such account on such date shall be includible if such person is not the estate of such holder, in such person's gross income for the taxable year which includes such date, or if such person is the estate of such holder, in such holder's gross income for the last taxable year of such holder.

"(ii) SPECIAL RULES.—

"(I) REDUCTION OF INCLUSION FOR PRE-DEATH EXPENSES.—The amount includible in gross income under clause (i) by any person (other than the estate) shall be reduced by the amount of qualified medical expenses which were incurred by the decedent before the date of the decedent's death and paid by such person within 1 year after such date.

"(II) DEDUCTION FOR ESTATE TAXES.—An appropriate deduction shall be allowed under section 691(c) to any person (other than the decedent or the decedent's spouse) with respect to amounts included in gross income under clause (i) by such person.

"(g) COST-OF-LIVING ADJUSTMENT.—In the case of any taxable year beginning in a calendar year after 1998, each dollar amount in subsection (c)(2) shall be increased by an amount equal to—

"(1) such dollar amount, multiplied by

"(2) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which such taxable year begins by substituting 'calendar year 1997' for 'calendar year 1992' in subparagraph (B) thereof.

If any increase under the preceding sentence is not a multiple of $50, such increase shall be rounded to the nearest multiple of $50.

"(h) REPORTS.—The Secretary may require the trustee of a medical savings account to make such reports regarding such account to the Secretary and to the account holder with respect to contributions, distributions, and such other matters as the Secretary determines appropriate. The reports required by this subsection shall be filed at such time and in such manner and furnished to such individuals at such time and in such manner as may be required by the Secretary.

"(i) LIMITATION ON NUMBER OF TAXPAYERS HAVING MEDICAL SAVINGS ACCOUNTS.—

"(1) IN GENERAL.—Except as provided in paragraph (5), no individual shall be treated as an eligible individual for any taxable year beginning after the cut-off year unless—

"(A) such individual was an active MSA participant for any taxable year ending on or before the close of the cut-off year, or

"(B) such individual first became an active MSA participant for a taxable year ending after the cut-off year by reason of coverage under a high deductible health plan of an MSA–participating employer.

"(2) CUT-OFF YEAR.—For purposes of paragraph (1), the term 'cut-off year' means the earlier of—

"(A) calendar year 2000, or

"(B) the first calendar year before 2000 for which the Secretary determines under subsection (j) that the numerical limitation for such year has been exceeded.

"(3) ACTIVE MSA PARTICIPANT.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'active MSA participant' means, with respect to any taxable year, any individual who is the account holder of any medical savings account into which any contribution was made which was excludable from gross income under section 106(b), or allowable as a deduction under this section, for such taxable year.

"(B) SPECIAL RULE FOR CUT-OFF YEARS BEFORE 2000.—In the case of a cut-off year before 2000—

"(i) an individual shall not be treated as an eligible individual for any month of such year or an active MSA participant under paragraph (1)(A) unless such individual is, on or before the cut-off date, covered under a high deductible health plan, and

"(ii) an employer shall not be treated as an MSA-participating employer unless the employer, on or before the cut-off date, offered coverage under a high deductible health plan to any employee.

"(C) CUT-OFF DATE.—For purposes of subparagraph (B)—

"(i) IN GENERAL.—Except as otherwise provided in this subparagraph, the cut-off date is October 1 of the cut-off year.

"(ii) EMPLOYEES WITH ENROLLMENT PERIODS AFTER OCTOBER 1.—In the case of an individual described in subclause (I) of subsection (c)(1)(A)(iii), if the regularly scheduled enrollment period for health plans of the individual's employer occurs during the last 3 months of the cut-off year, the cut-off date is December 31 of the cut-off year.

"(iii) SELF-EMPLOYED INDIVIDUALS.—In the case of an individual described in subclause (II) of subsection (c)(1)(A)(iii), the cut-off date is November 1 of the cut-off year.

"(iv) SPECIAL RULES FOR 1997.—If 1997 is a cut-off year by reason of subsection (j)(1)(A)—

"(I) each of the cut-off dates under clauses (i) and (iii) shall be 1 month earlier than the date determined without regard to this clause, and

"(II) clause (ii) shall be applied by substituting '4 months' for '3 months'.

"(4) MSA-PARTICIPATING EMPLOYER.—For purposes of this subsection, the term 'MSA-participating employer' means any small employer if—

"(A) such employer made any contribution to the medical savings account of any employee during the cut-off year or any preceding calendar year which was excludable from gross income under section 106(b), or

"(B) at least 20 percent of the employees of such employer who are eligible individuals for any month of the cut-off year by reason of coverage under a high deductible health plan of such employer each made a contribution of at least $100 to their medical savings accounts for any taxable year ending with or within the cut-off year which was allowable as a deduction under this section.

"(5) ADDITIONAL ELIGIBILITY AFTER CUT-OFF YEAR.—If the Secretary determines under subsection (j)(2)(A) that the numerical limit for the calendar year following a cut-off year described in paragraph (2)(B) has not been exceeded—

"(A) this subsection shall not apply to any otherwise eligible individual who is covered under a high deductible health plan during the first 6 months of the second calendar year following the cut-off year (and such individual shall be treated as an active MSA participant for purposes of this subsection if a contribution is made to any medical savings account with respect to such coverage), and

"(B) any employer who offers coverage under a high deductible health plan to any employee during such 6-month period shall be treated as an MSA-participating employer for purposes of this subsection if the requirements of paragraph (4) are met with respect to such coverage.

For purposes of this paragraph, subsection (j)(2)(A) shall be applied for 1998 by substituting '750,000' for '600,000'.

"(j) DETERMINATION OF WHETHER NUMERICAL LIMITS ARE EXCEEDED.—

"(1) DETERMINATION OF WHETHER LIMIT EXCEEDED FOR 1997.—The numerical limitation for 1997 is exceeded if, based on the reports required under paragraph (4), the number of medical savings accounts established as of—

"(A) April 30, 1997, exceeds 375,000, or

"(B) June 30, 1997, exceeds 525,000.

"(2) DETERMINATION OF WHETHER LIMIT EXCEEDED FOR 1998 OR 1999.—

"(A) IN GENERAL.—The numerical limitation for 1998 or 1999 is exceeded if the sum of—

"(i) the number of MSA returns filed on or before April 15 of such calendar year for taxable years ending with or within the preceding calendar year, plus

"(ii) the Secretary's estimate (determined on the basis of the returns described in clause (i)) of the number of MSA returns for such taxable years which will be filed after such date,

exceeds 600,000 (750,000 in the case of 1999). For purposes of the preceding sentence, the term 'MSA return' means any return on which any exclusion is claimed under section 106(b) or any deduction is claimed under this section.

"(B) ALTERNATIVE COMPUTATION OF LIMITATION.—The numerical limitation for 1998 or 1999 is also exceeded if the sum of—

"(i) 90 percent of the sum determined under subparagraph (A) for such calendar year, plus

"(ii) the product of 2.5 and the number of medical savings accounts established during the portion of such year preceding July 1 (based on the reports required under paragraph (4)) for taxable years beginning in such year,

exceeds 750,000.

"(3) PREVIOUSLY UNINSURED INDIVIDUALS NOT INCLUDED IN DETERMINATION.—

"(A) IN GENERAL.—The determination of whether any calendar year is a cut-off year shall be made by not counting the medical savings account of any previously uninsured individual.

"(B) PREVIOUSLY UNINSURED INDIVIDUAL.—For purposes of this subsection, the term 'previously uninsured individual' means, with respect to any medical savings account, any individual who had no health plan coverage (other than coverage referred to in subsection (c)(1)(B)) at any time during the 6-month period before the date such individual's coverage under the high deductible health plan commences.

"(4) REPORTING BY MSA TRUSTEES.—

"(A) IN GENERAL.—Not later than August 1 of 1997, 1998, and 1999, each person who is the trustee of a medical savings account established before July 1 of such calendar year shall make a report to the Secretary (in such form and manner as the Secretary shall specify) which specifies—

"(i) the number of medical savings accounts established before such July 1 (for taxable years beginning in such calendar year) of which such person is the trustee,

"(ii) the name and TIN of the account holder of each such account, and

"(iii) the number of such accounts which are accounts of previously uninsured individuals.

"(B) ADDITIONAL REPORT FOR 1997.—Not later than June 1, 1997, each person who is the trustee of a medical savings account established before May 1, 1997, shall make an additional report described in subparagraph (A) but only with respect to accounts established before May 1, 1997.

"(C) PENALTY FOR FAILURE TO FILE REPORT.—The penalty provided in section 6693(a) shall apply to any report required by this paragraph, except that—

"(i) such section shall be applied by substituting '$25' for '$50', and

"(ii) the maximum penalty imposed on any trustee shall not exceed $5,000.

"(D) AGGREGATION OF ACCOUNTS.—To the extent practicable, in determining the number of medical savings accounts on the basis of the reports under this paragraph, all medical savings accounts of an individual shall be treated as 1 account and all accounts of individuals who are married to each other shall be treated as 1 account.

"(5) DATE OF MAKING DETERMINATIONS.—Any determination under this subsection that a calendar year is a cut-off year shall be made by the Secretary and shall be published not later than October 1 of such year.".

(b) DEDUCTION ALLOWED WHETHER OR NOT INDIVIDUAL ITEMIZES OTHER DEDUCTIONS.—Subsection (a) of section 62 is amended by inserting after paragraph (15) the following new paragraph:

"(16) MEDICAL SAVINGS ACCOUNTS.—The deduction allowed by section 220.".

(c) EXCLUSIONS FOR EMPLOYER CONTRIBUTIONS TO MEDICAL SAVINGS ACCOUNTS.—

(1) EXCLUSION FROM INCOME TAX.—The text of section 106 (relating to contributions by employer to accident and health plans) is amended to read as follows:

"(a) GENERAL RULE.—Except as otherwise provided in this section, gross income of an employee does not include employer-provided coverage under an accident or health plan.

"(b) CONTRIBUTIONS TO MEDICAL SAVINGS ACCOUNTS.—

"(1) IN GENERAL.—In the case of an employee who is an eligible individual, amounts contributed by such employee's employer to any medical savings account of such employee shall be treated as employer-provided coverage for medical expenses under an accident or health plan to the extent such amounts do not exceed the limitation under section 220(b)(1) (determined without regard to this subsection) which is applicable to such employee for such taxable year.

"(2) NO CONSTRUCTIVE RECEIPT.—No amount shall be included in the gross income of any employee solely because the employee may choose between the contributions referred to in paragraph (1) and employer contributions to another health plan of the employer.

"(3) SPECIAL RULE FOR DEDUCTION OF EMPLOYER CONTRIBUTIONS.—Any employer contribution to a medical savings account, if otherwise allowable as a deduction under this chapter, shall be allowed only for the taxable year in which paid.

"(4) EMPLOYER MSA CONTRIBUTIONS REQUIRED TO BE SHOWN ON RETURN.—Every individual required to file a return under section 6012 for the taxable year shall include on such return the aggregate amount contributed by employers to the medical savings accounts of such individual or such individual's spouse for such taxable year.

"(5) MSA CONTRIBUTIONS NOT PART OF COBRA COVERAGE.—Paragraph (1) shall not apply for purposes of section 4980B.

"(6) DEFINITIONS.—For purposes of this subsection, the terms 'eligible individual' and 'medical savings account' have the respective meanings given to such terms by section 220.

"(7) CROSS REFERENCE.—

"For penalty on failure by employer to make comparable contributions to the medical savings accounts of comparable employees, see section 4980E.".

(2) EXCLUSION FROM EMPLOYMENT TAXES.—

(A) RAILROAD RETIREMENT TAX.—Subsection (e) of section 3231 is amended by adding at the end the following new paragraph:

"(10) MEDICAL SAVINGS ACCOUNT CONTRIBUTIONS.—The term 'compensation' shall not include any payment made to or for the benefit of an employee if at the time of such payment it is reasonable to believe that the employee will be able to exclude such payment from income under section 106(b).".

(B) UNEMPLOYMENT TAX.—Subsection (b) of section 3306 is amended by striking "or" at the end of paragraph (15), by striking the period at the end of paragraph (16) and inserting "; or", and by inserting after paragraph (16) the following new paragraph:

"(17) any payment made to or for the benefit of an employee if at the time of such payment it is reasonable to believe that the employee will be able to exclude such payment from income under section 106(b).".

(C) WITHHOLDING TAX.—Subsection (a) of section 3401 is amended by striking "or" at the end of paragraph (19), by striking the period at the end of paragraph (20) and inserting "; or", and by inserting after paragraph (20) the following new paragraph:

"(21) any payment made to or for the benefit of an employee if at the time of such payment it is reasonable to believe that the employee will be able to exclude such payment from income under section 106(b)."

(3) EMPLOYER CONTRIBUTIONS REQUIRED TO BE SHOWN ON W–2.—Subsection (a) of section 6051 is amended by striking "and" at the end of paragraph (9), by striking the period at the end of paragraph (10) and inserting ", and", and by inserting after paragraph (10) the following new paragraph:

"(11) the amount contributed to any medical savings account (as defined in section 220(d)) of such employee or such employee's spouse.".

(4) PENALTY FOR FAILURE OF EMPLOYER TO MAKE COMPARABLE MSA CONTRIBUTIONS.—

(A) IN GENERAL.—Chapter 43 is amended by adding after section 4980D the following new section:

"SEC. 4980E. FAILURE OF EMPLOYER TO MAKE COMPARABLE MEDICAL SAVINGS ACCOUNT CONTRIBUTIONS.

"(a) GENERAL RULE.—In the case of an employer who makes a contribution to the medical savings account of any employee with respect to coverage under a high deductible health plan of the employer during a calendar year, there is hereby imposed a tax on the failure of such employer to meet the requirements of subsection (d) for such calendar year.

"(b) AMOUNT OF TAX.—The amount of the tax imposed by subsection (a) on any failure for any calendar year is the amount

equal to 35 percent of the aggregate amount contributed by the employer to medical savings accounts of employees for taxable years of such employees ending with or within such calendar year.

"(c) WAIVER BY SECRETARY.—In the case of a failure which is due to reasonable cause and not to willful neglect, the Secretary may waive part or all of the tax imposed by subsection (a) to the extent that the payment of such tax would be excessive relative to the failure involved.

"(d) EMPLOYER REQUIRED TO MAKE COMPARABLE MSA CONTRIBUTIONS FOR ALL PARTICIPATING EMPLOYEES.—

"(1) IN GENERAL.—An employer meets the requirements of this subsection for any calendar year if the employer makes available comparable contributions to the medical savings accounts of all comparable participating employees for each coverage period during such calendar year.

"(2) COMPARABLE CONTRIBUTIONS.—

"(A) IN GENERAL.—For purposes of paragraph (1), the term 'comparable contributions' means contributions—

"(i) which are the same amount, or

"(ii) which are the same percentage of the annual deductible limit under the high deductible health plan covering the employees.

"(B) PART-YEAR EMPLOYEES.—In the case of an employee who is employed by the employer for only a portion of the calendar year, a contribution to the medical savings account of such employee shall be treated as comparable if it is an amount which bears the same ratio to the comparable amount (determined without regard to this subparagraph) as such portion bears to the entire calendar year.

"(3) COMPARABLE PARTICIPATING EMPLOYEES.—For purposes of paragraph (1), the term 'comparable participating employees' means all employees—

"(A) who are eligible individuals covered under any high deductible health plan of the employer, and

"(B) who have the same category of coverage.

For purposes of subparagraph (B), the categories of coverage are self-only and family coverage.

"(4) PART-TIME EMPLOYEES.—

"(A) IN GENERAL.—Paragraph (3) shall be applied separately with respect to part-time employees and other employees.

"(B) PART-TIME EMPLOYEE.—For purposes of subparagraph (A), the term 'part-time employee' means any employee who is customarily employed for fewer than 30 hours per week.

"(e) CONTROLLED GROUPS.—For purposes of this section, all persons treated as a single employer under subsection (b), (c), (m), or (o) of section 414 shall be treated as 1 employer.

"(f) DEFINITIONS.—Terms used in this section which are also used in section 220 have the respective meanings given such terms in section 220.".

(B) CLERICAL AMENDMENT.—The table of sections for chapter 43 is amended by adding after the item relating to section 4980D the following new item:

"Sec. 4980E. Failure of employer to make comparable medical savings account contributions.".

(d) MEDICAL SAVINGS ACCOUNT CONTRIBUTIONS NOT AVAILABLE UNDER CAFETERIA PLANS.—Subsection (f) of section 125 of such Code is amended by inserting "106(b)," before "117".

(e) TAX ON EXCESS CONTRIBUTIONS.—Section 4973 (relating to tax on excess contributions to individual retirement accounts, certain section 403(b) contracts, and certain individual retirement annuities) is amended—

(1) by inserting "**MEDICAL SAVINGS ACCOUNTS,**" after "**ACCOUNTS,**" in the heading of such section,

(2) by striking "or" at the end of paragraph (1) of subsection (a),

(3) by redesignating paragraph (2) of subsection (a) as paragraph (3) and by inserting after paragraph (1) the following:

"(2) a medical savings account (within the meaning of section 220(d)), or", and

(4) by adding at the end the following new subsection:

"(d) EXCESS CONTRIBUTIONS TO MEDICAL SAVINGS ACCOUNTS.—For purposes of this section, in the case of medical savings accounts (within the meaning of section 220(d)), the term 'excess contributions' means the sum of—

"(1) the aggregate amount contributed for the taxable year to the accounts (other than rollover contributions described in section 220(f)(5)) which is neither excludable from gross income under section 106(b) nor allowable as a deduction under section 220 for such year, and

"(2) the amount determined under this subsection for the preceding taxable year, reduced by the sum of—

"(A) the distributions out of the accounts which were included in gross income under section 220(f)(2), and

"(B) the excess (if any) of—

"(i) the maximum amount allowable as a deduction under section 220(b)(1) (determined without regard to section 106(b)) for the taxable year, over

"(ii) the amount contributed to the accounts for the taxable year.

For purposes of this subsection, any contribution which is distributed out of the medical savings account in a distribution to which section 220(f)(3) applies shall be treated as an amount not contributed.".

(f) TAX ON PROHIBITED TRANSACTIONS.—

(1) Section 4975 (relating to tax on prohibited transactions) is amended by adding at the end of subsection (c) the following new paragraph:

"(4) SPECIAL RULE FOR MEDICAL SAVINGS ACCOUNTS.—An individual for whose benefit a medical savings account (within the meaning of section 220(d)) is established shall be exempt from the tax imposed by this section with respect to any transaction concerning such account (which would otherwise be taxable under this section) if, with respect to such transaction, the account ceases to be a medical savings account by reason of the application of section 220(e)(2) to such account.".

(2) Paragraph (1) of section 4975(e) is amended to read as follows:

"(1) PLAN.—For purposes of this section, the term 'plan' means—

"(A) a trust described in section 401(a) which forms a part of a plan, or a plan described in section 403(a), which trust or plan is exempt from tax under section 501(a),

"(B) an individual retirement account described in section 408(a),

"(C) an individual retirement annuity described in section 408(b),

"(D) a medical savings account described in section 220(d), or

"(E) a trust, plan, account, or annuity which, at any time, has been determined by the Secretary to be described in any preceding subparagraph of this paragraph.".

(g) FAILURE TO PROVIDE REPORTS ON MEDICAL SAVINGS ACCOUNTS.—

(1) Subsection (a) of section 6693 (relating to failure to provide reports on individual retirement accounts or annuities) is amended to read as follows:

"(a) REPORTS.—

"(1) IN GENERAL.—If a person required to file a report under a provision referred to in paragraph (2) fails to file such report at the time and in the manner required by such provision, such person shall pay a penalty of $50 for each failure unless it is shown that such failure is due to reasonable cause.

"(2) PROVISIONS.—The provisions referred to in this paragraph are—

"(A) subsections (i) and (l) of section 408 (relating to individual retirement plans), and

"(B) section 220(h) (relating to medical savings accounts).".

(h) EXCEPTION FROM CAPITALIZATION OF POLICY ACQUISITION EXPENSES.—Subparagraph (B) of section 848(e)(1) (defining specified insurance contract) is amended by striking "and" at the end of clause (ii), by striking the period at the end of clause (iii) and inserting ", and", and by adding at the end the following new clause:

"(iv) any contract which is a medical savings account (as defined in section 220(d)).".

(i) CLERICAL AMENDMENT.—The table of sections for part VII of subchapter B of chapter 1 is amended by striking the last item and inserting the following:

"Sec. 220. Medical savings accounts.
"Sec. 221. Cross reference.".

26 USC 62 note.

(j) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

26 USC 220 note.

(k) MONITORING OF PARTICIPATION IN MEDICAL SAVINGS ACCOUNTS.—The Secretary of the Treasury or his delegate shall—

(1) during 1997, 1998, 1999, and 2000, regularly evaluate the number of individuals who are maintaining medical savings accounts and the reduction in revenues to the United States by reason of such accounts, and

(2) provide such reports of such evaluations to Congress as such Secretary determines appropriate.

26 USC 220 note.

(l) STUDY OF EFFECTS OF MEDICAL SAVINGS ACCOUNTS ON SMALL GROUP MARKET.—The Comptroller General of the United States shall enter into a contract with an organization with expertise in health economics, health insurance markets, and actuarial

science to conduct a comprehensive study regarding the effects of medical savings accounts in the small group market on—

(1) selection, including adverse selection,

(2) health costs, including any impact on premiums of individuals with comprehensive coverage,

(3) use of preventive care,

(4) consumer choice,

(5) the scope of coverage of high deductible plans purchased in conjunction with such accounts, and

(6) other relevant items.

A report on the results of the study conducted under this subsection shall be submitted to the Congress no later than January 1, 1999. Reports.

Subtitle B—Increase in Deduction for Health Insurance Costs of Self-Employed Individuals

SEC. 311. INCREASE IN DEDUCTION FOR HEALTH INSURANCE COSTS OF SELF-EMPLOYED INDIVIDUALS.

(a) IN GENERAL.—Paragraph (1) of section 162(l) is amended to read as follows:

"(1) ALLOWANCE OF DEDUCTION.—

"(A) IN GENERAL.—In the case of an individual who is an employee within the meaning of section 401(c)(1), there shall be allowed as a deduction under this section an amount equal to the applicable percentage of the amount paid during the taxable year for insurance which constitutes medical care for the taxpayer, his spouse, and dependents.

"(B) APPLICABLE PERCENTAGE.—For purposes of subparagraph (A), the applicable percentage shall be determined under the following table:

"For taxable years beginning in calendar year—	The applicable percentage is—
1997	40 percent
1998 through 2002	45 percent
2003	50 percent
2004	60 percent
2005	70 percent
2006 or thereafter	80 percent.".

(b) EXCLUSION FOR AMOUNTS RECEIVED UNDER CERTAIN SELF-INSURED PLANS.—Paragraph (3) of section 104(a) is amended by inserting "(or through an arrangement having the effect of accident or health insurance)" after "health insurance".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996. 26 USC 104 note.

Subtitle C—Long-Term Care Services and Contracts

PART I—GENERAL PROVISIONS

SEC. 321. TREATMENT OF LONG-TERM CARE INSURANCE.

(a) GENERAL RULE.—Chapter 79 (relating to definitions) is amended by inserting after section 7702A the following new section:

"SEC. 7702B. TREATMENT OF QUALIFIED LONG-TERM CARE INSURANCE.

"(a) IN GENERAL.—For purposes of this title—

"(1) a qualified long-term care insurance contract shall be treated as an accident and health insurance contract,

"(2) amounts (other than policyholder dividends, as defined in section 808, or premium refunds) received under a qualified long-term care insurance contract shall be treated as amounts received for personal injuries and sickness and shall be treated as reimbursement for expenses actually incurred for medical care (as defined in section 213(d)),

"(3) any plan of an employer providing coverage under a qualified long-term care insurance contract shall be treated as an accident and health plan with respect to such coverage,

"(4) except as provided in subsection (e)(3), amounts paid for a qualified long-term care insurance contract providing the benefits described in subsection (b)(2)(A) shall be treated as payments made for insurance for purposes of section 213(d)(1)(D), and

"(5) a qualified long-term care insurance contract shall be treated as a guaranteed renewable contract subject to the rules of section 816(e).

"(b) QUALIFIED LONG-TERM CARE INSURANCE CONTRACT.—For purposes of this title—

"(1) IN GENERAL.—The term 'qualified long-term care insurance contract' means any insurance contract if—

"(A) the only insurance protection provided under such contract is coverage of qualified long-term care services,

"(B) such contract does not pay or reimburse expenses incurred for services or items to the extent that such expenses are reimbursable under title XVIII of the Social Security Act or would be so reimbursable but for the application of a deductible or coinsurance amount,

"(C) such contract is guaranteed renewable,

"(D) such contract does not provide for a cash surrender value or other money that can be—

"(i) paid, assigned, or pledged as collateral for a loan, or

"(ii) borrowed,

other than as provided in subparagraph (E) or paragraph (2)(C),

"(E) all refunds of premiums, and all policyholder dividends or similar amounts, under such contract are to be applied as a reduction in future premiums or to increase future benefits, and

"(F) such contract meets the requirements of subsection (g).

"(2) SPECIAL RULES.—

"(A) PER DIEM, ETC. PAYMENTS PERMITTED.—A contract shall not fail to be described in subparagraph (A) or (B) of paragraph (1) by reason of payments being made on a per diem or other periodic basis without regard to the expenses incurred during the period to which the payments relate.

"(B) SPECIAL RULES RELATING TO MEDICARE.—

"(i) Paragraph (1)(B) shall not apply to expenses which are reimbursable under title XVIII of the Social Security Act only as a secondary payor.

"(ii) No provision of law shall be construed or applied so as to prohibit the offering of a qualified long-term care insurance contract on the basis that the contract coordinates its benefits with those provided under such title.

"(C) REFUNDS OF PREMIUMS.—Paragraph (1)(E) shall not apply to any refund on the death of the insured, or on a complete surrender or cancellation of the contract, which cannot exceed the aggregate premiums paid under the contract. Any refund on a complete surrender or cancellation of the contract shall be includible in gross income to the extent that any deduction or exclusion was allowable with respect to the premiums.

"(c) QUALIFIED LONG-TERM CARE SERVICES.—For purposes of this section—

"(1) IN GENERAL.—The term 'qualified long-term care services' means necessary diagnostic, preventive, therapeutic, curing, treating, mitigating, and rehabilitative services, and maintenance or personal care services, which—

"(A) are required by a chronically ill individual, and

"(B) are provided pursuant to a plan of care prescribed by a licensed health care practitioner.

"(2) CHRONICALLY ILL INDIVIDUAL.—

"(A) IN GENERAL.—The term 'chronically ill individual' means any individual who has been certified by a licensed health care practitioner as—

"(i) being unable to perform (without substantial assistance from another individual) at least 2 activities of daily living for a period of at least 90 days due to a loss of functional capacity,

"(ii) having a level of disability similar (as determined under regulations prescribed by the Secretary in consultation with the Secretary of Health and Human Services) to the level of disability described in clause (i), or

"(iii) requiring substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment.

Such term shall not include any individual otherwise meeting the requirements of the preceding sentence unless within the preceding 12-month period a licensed health care practitioner has certified that such individual meets such requirements.

"(B) ACTIVITIES OF DAILY LIVING.—For purposes of subparagraph (A), each of the following is an activity of daily living:

"(i) Eating.
"(ii) Toileting.
"(iii) Transferring.
"(iv) Bathing.
"(v) Dressing.
"(vi) Continence.

A contract shall not be treated as a qualified long-term care insurance contract unless the determination of whether an individual is a chronically ill individual takes into account at least 5 of such activities.

"(3) MAINTENANCE OR PERSONAL CARE SERVICES.—The term 'maintenance or personal care services' means any care the primary purpose of which is the provision of needed assistance with any of the disabilities as a result of which the individual is a chronically ill individual (including the protection from threats to health and safety due to severe cognitive impairment).

"(4) LICENSED HEALTH CARE PRACTITIONER.—The term 'licensed health care practitioner' means any physician (as defined in section 1861(r)(1) of the Social Security Act) and any registered professional nurse, licensed social worker, or other individual who meets such requirements as may be prescribed by the Secretary.

"(d) AGGREGATE PAYMENTS IN EXCESS OF LIMITS.—

"(1) IN GENERAL.—If the aggregate of—

"(A) the periodic payments received for any period under all qualified long-term care insurance contracts which are treated as made for qualified long-term care services for an insured, and

"(B) the periodic payments received for such period which are treated under section 101(g) as paid by reason of the death of such insured,

exceeds the per diem limitation for such period, such excess shall be includible in gross income without regard to section 72. A payment shall not be taken into account under subparagraph (B) if the insured is a terminally ill individual (as defined in section 101(g)) at the time the payment is received.

"(2) PER DIEM LIMITATION.—For purposes of paragraph (1), the per diem limitation for any period is an amount equal to the excess (if any) of—

"(A) the greater of—

"(i) the dollar amount in effect for such period under paragraph (4), or

"(ii) the costs incurred for qualified long-term care services provided for the insured for such period, over

"(B) the aggregate payments received as reimbursements (through insurance or otherwise) for qualified long-term care services provided for the insured during such period.

"(3) AGGREGATION RULES.—For purposes of this subsection—

"(A) all persons receiving periodic payments described in paragraph (1) with respect to the same insured shall be treated as 1 person, and

"(B) the per diem limitation determined under paragraph (2) shall be allocated first to the insured and any remaining limitation shall be allocated among the other

such persons in such manner as the Secretary shall prescribe.

"(4) DOLLAR AMOUNT.—The dollar amount in effect under this subsection shall be $175 per day (or the equivalent amount in the case of payments on another periodic basis).

"(5) INFLATION ADJUSTMENT.—In the case of a calendar year after 1997, the dollar amount contained in paragraph (4) shall be increased at the same time and in the same manner as amounts are increased pursuant to section 213(d)(10).

"(6) PERIODIC PAYMENTS.—For purposes of this subsection, the term 'periodic payment' means any payment (whether on a periodic basis or otherwise) made without regard to the extent of the costs incurred by the payee for qualified long-term care services.

"(e) TREATMENT OF COVERAGE PROVIDED AS PART OF A LIFE INSURANCE CONTRACT.—Except as otherwise provided in regulations prescribed by the Secretary, in the case of any long-term care insurance coverage (whether or not qualified) provided by a rider on or as part of a life insurance contract—

"(1) IN GENERAL.—This section shall apply as if the portion of the contract providing such coverage is a separate contract.

"(2) APPLICATION OF 7702.—Section 7702(c)(2) (relating to the guideline premium limitation) shall be applied by increasing the guideline premium limitation with respect to a life insurance contract, as of any date—

"(A) by the sum of any charges (but not premium payments) against the life insurance contract's cash surrender value (within the meaning of section 7702(f)(2)(A)) for such coverage made to that date under the contract, less

"(B) any such charges the imposition of which reduces the premiums paid for the contract (within the meaning of section 7702(f)(1)).

"(3) APPLICATION OF SECTION 213.—No deduction shall be allowed under section 213(a) for charges against the life insurance contract's cash surrender value described in paragraph (2), unless such charges are includible in income as a result of the application of section 72(e)(10) and the rider is a qualified long-term care insurance contract under subsection (b).

"(4) PORTION DEFINED.—For purposes of this subsection, the term 'portion' means only the terms and benefits under a life insurance contract that are in addition to the terms and benefits under the contract without regard to long-term care insurance coverage.

"(f) TREATMENT OF CERTAIN STATE-MAINTAINED PLANS.—

"(1) IN GENERAL.—If—

"(A) an individual receives coverage for qualified long-term care services under a State long-term care plan, and

"(B) the terms of such plan would satisfy the requirements of subsection (b) were such plan an insurance contract,

such plan shall be treated as a qualified long-term care insurance contract for purposes of this title.

"(2) STATE LONG-TERM CARE PLAN.—For purposes of paragraph (1), the term 'State long-term care plan' means any plan—

"(A) which is established and maintained by a State or an instrumentality of a State,

"(B) which provides coverage only for qualified long-term care services, and

"(C) under which such coverage is provided only to—

"(i) employees and former employees of a State (or any political subdivision or instrumentality of a State),

"(ii) the spouses of such employees, and

"(iii) individuals bearing a relationship to such employees or spouses which is described in any of paragraphs (1) through (8) of section 152(a).".

(b) RESERVE METHOD.—Clause (iii) of section 807(d)(3)(A) is amended by inserting "(other than a qualified long-term care insurance contract, as defined in section 7702B(b))" after "insurance contract".

(c) LONG-TERM CARE INSURANCE NOT PERMITTED UNDER CAFETERIA PLANS OR FLEXIBLE SPENDING ARRANGEMENTS.—

(1) CAFETERIA PLANS.—Section 125(f) is amended by adding at the end the following new sentence: "Such term shall not include any product which is advertised, marketed, or offered as long-term care insurance.".

(2) FLEXIBLE SPENDING ARRANGEMENTS.—Section 106 (relating to contributions by employer to accident and health plans), as amended by section 301(c), is amended by adding at the end the following new subsection:

"(c) INCLUSION OF LONG-TERM CARE BENEFITS PROVIDED THROUGH FLEXIBLE SPENDING ARRANGEMENTS.—

"(1) IN GENERAL.—Effective on and after January 1, 1997, gross income of an employee shall include employer-provided coverage for qualified long-term care services (as defined in section 7702B(c)) to the extent that such coverage is provided through a flexible spending or similar arrangement.

"(2) FLEXIBLE SPENDING ARRANGEMENT.—For purposes of this subsection, a flexible spending arrangement is a benefit program which provides employees with coverage under which—

"(A) specified incurred expenses may be reimbursed (subject to reimbursement maximums and other reasonable conditions), and

"(B) the maximum amount of reimbursement which is reasonably available to a participant for such coverage is less than 500 percent of the value of such coverage.

In the case of an insured plan, the maximum amount reasonably available shall be determined on the basis of the underlying coverage."

(d) CONTINUATION COVERAGE RULES NOT TO APPLY.—

(1) Paragraph (2) of section 4980B(g) is amended by adding at the end the following new sentence: "Such term shall not include any plan substantially all of the coverage under which is for qualified long-term care services (as defined in section 7702B(c))."

* * * * * *

(e) CLERICAL AMENDMENT.—The table of sections for chapter 79 is amended by inserting after the item relating to section 7702A the following new item:

"Sec. 7702B. Treatment of qualified long-term care insurance.".

(f) EFFECTIVE DATES.— 26 USC 1702B note.

(1) GENERAL EFFECTIVE DATE.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by this section shall apply to contracts issued after December 31, 1996.

(B) RESERVE METHOD.—The amendment made by subsection (b) shall apply to contracts issued after December 31, 1997.

(2) CONTINUATION OF EXISTING POLICIES.—In the case of any contract issued before January 1, 1997, which met the long-term care insurance requirements of the State in which the contract was situsued at the time the contract was issued—

(A) such contract shall be treated for purposes of the Internal Revenue Code of 1986 as a qualified long-term care insurance contract (as defined in section 7702B(b) of such Code), and

(B) services provided under, or reimbursed by, such contract shall be treated for such purposes as qualified long-term care services (as defined in section 7702B(c) of such Code).

In the case of an individual who is covered on December 31, 1996, under a State long-term care plan (as defined in section 7702B(f)(2) of such Code), the terms of such plan on such date shall be treated for purposes of the preceding sentence as a contract issued on such date which met the long-term care insurance requirements of such State.

(3) EXCHANGES OF EXISTING POLICIES.—If, after the date of enactment of this Act and before January 1, 1998, a contract providing for long-term care insurance coverage is exchanged solely for a qualified long-term care insurance contract (as defined in section 7702B(b) of such Code), no gain or loss shall be recognized on the exchange. If, in addition to a qualified long-term care insurance contract, money or other property is received in the exchange, then any gain shall be recognized to the extent of the sum of the money and the fair market value of the other property received. For purposes of this paragraph, the cancellation of a contract providing for long-term care insurance coverage and reinvestment of the cancellation proceeds in a qualified long-term care insurance contract within 60 days thereafter shall be treated as an exchange.

(4) ISSUANCE OF CERTAIN RIDERS PERMITTED.—For purposes of applying sections 101(f), 7702, and 7702A of the Internal Revenue Code of 1986 to any contract—

(A) the issuance of a rider which is treated as a qualified long-term care insurance contract under section 7702B, and

(B) the addition of any provision required to conform any other long-term care rider to be so treated,

shall not be treated as a modification or material change of such contract.

(5) APPLICATION OF PER DIEM LIMITATION TO EXISTING CONTRACTS.—The amount of per diem payments made under a contract issued on or before July 31, 1996, with respect to an insured which are excludable from gross income by reason of section 7702B of the Internal Revenue Code of 1986 (as added by this section) shall not be reduced under subsection (d)(2)(B) thereof by reason of reimbursements received under a contract issued on or before such date. The preceding sentence shall cease to apply as of the date (after July 31, 1996) such contract is exchanged or there is any contract modification which results in an increase in the amount of such per diem payments or the amount of such reimbursements.

26 USC 7702B note.

(g) LONG-TERM CARE STUDY REQUEST.—The Chairman of the Committee on Ways and Means of the House of Representatives and the Chairman of the Committee on Finance of the Senate shall jointly request the National Association of Insurance Commissioners, in consultation with representatives of the insurance industry and consumer organizations, to formulate, develop, and conduct a study to determine the marketing and other effects of per diem limits on certain types of long-term care policies. If the National Association of Insurance Commissioners agrees to the study request, the National Association of Insurance Commissioners shall report the results of its study to such committees not later than 2 years after accepting the request.

Reports.

SEC. 322. QUALIFIED LONG-TERM CARE SERVICES TREATED AS MEDICAL CARE.

(a) GENERAL RULE.—Paragraph (1) of section 213(d) (defining medical care) is amended by striking "or" at the end of subparagraph (B), by redesignating subparagraph (C) as subparagraph (D), and by inserting after subparagraph (B) the following new subparagraph:

"(C) for qualified long-term care services (as defined in section 7702B(c)), or".

(b) TECHNICAL AMENDMENTS.—

(1) Subparagraph (D) of section 213(d)(1) (as redesignated by subsection (a)) is amended by inserting before the period "or for any qualified long-term care insurance contract (as defined in section 7702B(b))".

(2)(A) Paragraph (1) of section 213(d) is amended by adding at the end the following new flush sentence:

"In the case of a qualified long-term care insurance contract (as defined in section 7702B(b)), only eligible long-term care premiums (as defined in paragraph (10)) shall be taken into account under subparagraph (D)."

(B) Paragraph (2) of section 162(l) is amended by adding at the end the following new subparagraph:

"(C) LONG-TERM CARE PREMIUMS.—In the case of a qualified long-term care insurance contract (as defined in section 7702B(b)), only eligible long-term care premiums (as defined in section 213(d)(10)) shall be taken into account under paragraph (1)."

(C) Subsection (d) of section 213 is amended by adding at the end the following new paragraphs:

"(10) ELIGIBLE LONG-TERM CARE PREMIUMS.—

"(A) IN GENERAL.—For purposes of this section, the term 'eligible long-term care premiums' means the amount paid during a taxable year for any qualified long-term care insurance contract (as defined in section 7702B(b)) covering an individual, to the extent such amount does not exceed the limitation determined under the following table:

"In the case of an individual with an attained age before the close of the taxable year of:	The limitation is:
40 or less	$ 200
More than 40 but not more than 50	375
More than 50 but not more than 60	750
More than 60 but not more than 70	2,000
More than 70	2,500

"(B) INDEXING.—

"(i) IN GENERAL.—In the case of any taxable year beginning in a calendar year after 1997, each dollar amount contained in subparagraph (A) shall be increased by the medical care cost adjustment of such amount for such calendar year. If any increase determined under the preceding sentence is not a multiple of $10, such increase shall be rounded to the nearest multiple of $10.

"(ii) MEDICAL CARE COST ADJUSTMENT.—For purposes of clause (i), the medical care cost adjustment for any calendar year is the percentage (if any) by which—

"(I) the medical care component of the Consumer Price Index (as defined in section 1(f)(5)) for August of the preceding calendar year, exceeds

"(II) such component for August of 1996.

The Secretary shall, in consultation with the Secretary of Health and Human Services, prescribe an adjustment which the Secretary determines is more appropriate for purposes of this paragraph than the adjustment described in the preceding sentence, and the adjustment so prescribed shall apply in lieu of the adjustment described in the preceding sentence.

"(11) CERTAIN PAYMENTS TO RELATIVES TREATED AS NOT PAID FOR MEDICAL CARE.—An amount paid for a qualified long-term care service (as defined in section 7702B(c)) provided to an individual shall be treated as not paid for medical care if such service is provided—

"(A) by the spouse of the individual or by a relative (directly or through a partnership, corporation, or other entity) unless the service is provided by a licensed professional with respect to such service, or

"(B) by a corporation or partnership which is related (within the meaning of section 267(b) or 707(b)) to the individual.

For purposes of this paragraph, the term 'relative' means an individual bearing a relationship to the individual which is described in any of paragraphs (1) through (8) of section 152(a).

This paragraph shall not apply for purposes of section 105(b) with respect to reimbursements through insurance.".

(3) Paragraph (6) of section 213(d) is amended—

(A) by striking "subparagraphs (A) and (B)" and inserting "subparagraphs (A), (B), and (C)", and

(B) by striking "paragraph (1)(C)" in subparagraph (A) and inserting "paragraph (1)(D)".

(4) Paragraph (7) of section 213(d) is amended by striking "subparagraphs (A) and (B)" and inserting "subparagraphs (A), (B), and (C)".

26 USC 162 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 323. REPORTING REQUIREMENTS.

(a) IN GENERAL.—Subpart B of part III of subchapter A of chapter 61 is amended by adding at the end the following new section:

"SEC. 6050Q. CERTAIN LONG-TERM CARE BENEFITS.

"(a) REQUIREMENT OF REPORTING.—Any person who pays long-term care benefits shall make a return, according to the forms or regulations prescribed by the Secretary, setting forth—

"(1) the aggregate amount of such benefits paid by such person to any individual during any calendar year,

"(2) whether or not such benefits are paid in whole or in part on a per diem or other periodic basis without regard to the expenses incurred during the period to which the payments relate,

"(3) the name, address, and TIN of such individual, and

"(4) the name, address, and TIN of the chronically ill or terminally ill individual on account of whose condition such benefits are paid.

"(b) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS REQUIRED.—Every person required to make a return under subsection (a) shall furnish to each individual whose name is required to be set forth in such return a written statement showing—

"(1) the name of the person making the payments, and

"(2) the aggregate amount of long-term care benefits paid to the individual which are required to be shown on such return.

The written statement required under the preceding sentence shall be furnished to the individual on or before January 31 of the year following the calendar year for which the return under subsection (a) was required to be made.

"(c) LONG-TERM CARE BENEFITS.—For purposes of this section, the term 'long-term care benefit' means—

"(1) any payment under a product which is advertised, marketed, or offered as long-term care insurance, and

"(2) any payment which is excludable from gross income by reason of section 101(g).".

(b) PENALTIES.—

(1) Subparagraph (B) of section 6724(d)(1) is amended by redesignating clauses (ix) through (xiv) as clauses (x) through (xv), respectively, and by inserting after clause (viii) the following new clause:

"(ix) section 6050Q (relating to certain long-term care benefits),".

(2) Paragraph (2) of section 6724(d) is amended by redesignating subparagraphs (Q) through (T) as subparagraphs (R) through (U), respectively, and by inserting after subparagraph (P) the following new subparagraph:

"(Q) section 6050Q(b) (relating to certain long-term care benefits),".

(c) CLERICAL AMENDMENT.—The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by adding at the end the following new item:

"Sec. 6050Q. Certain long-term care benefits.".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to benefits paid after December 31, 1996. 26 USC 6050Q note.

PART II—CONSUMER PROTECTION PROVISIONS

SEC. 325. POLICY REQUIREMENTS.

Section 7702B (as added by section 321) is amended by adding at the end the following new subsection:

"(g) CONSUMER PROTECTION PROVISIONS.—

"(1) IN GENERAL.—The requirements of this subsection are met with respect to any contract if the contract meets—

"(A) the requirements of the model regulation and model Act described in paragraph (2),

"(B) the disclosure requirement of paragraph (3), and

"(C) the requirements relating to nonforfeitability under paragraph (4).

"(2) REQUIREMENTS OF MODEL REGULATION AND ACT.—

"(A) IN GENERAL.—The requirements of this paragraph are met with respect to any contract if such contract meets—

"(i) MODEL REGULATION.—The following requirements of the model regulation:

"(I) Section 7A (relating to guaranteed renewal or noncancellability), and the requirements of section 6B of the model Act relating to such section 7A.

"(II) Section 7B (relating to prohibitions on limitations and exclusions).

"(III) Section 7C (relating to extension of benefits).

"(IV) Section 7D (relating to continuation or conversion of coverage).

"(V) Section 7E (relating to discontinuance and replacement of policies).

"(VI) Section 8 (relating to unintentional lapse).

"(VII) Section 9 (relating to disclosure), other than section 9F thereof.

"(VIII) Section 10 (relating to prohibitions against post-claims underwriting).

"(IX) Section 11 (relating to minimum standards).

"(X) Section 12 (relating to requirement to offer inflation protection), except that any requirement for a signature on a rejection of inflation

protection shall permit the signature to be on an application or on a separate form.

"(XI) Section 23 (relating to prohibition against preexisting conditions and probationary periods in replacement policies or certificates).

"(ii) MODEL ACT.—The following requirements of the model Act:

"(I) Section 6C (relating to preexisting conditions).

"(II) Section 6D (relating to prior hospitalization).

"(B) DEFINITIONS.—For purposes of this paragraph—

"(i) MODEL PROVISIONS.—The terms 'model regulation' and 'model Act' mean the long-term care insurance model regulation, and the long-term care insurance model Act, respectively, promulgated by the National Association of Insurance Commissioners (as adopted as of January 1993).

"(ii) COORDINATION.—Any provision of the model regulation or model Act listed under clause (i) or (ii) of subparagraph (A) shall be treated as including any other provision of such regulation or Act necessary to implement the provision.

"(iii) DETERMINATION.—For purposes of this section and section 4980C, the determination of whether any requirement of a model regulation or the model Act has been met shall be made by the Secretary.

"(3) DISCLOSURE REQUIREMENT.—The requirement of this paragraph is met with respect to any contract if such contract meets the requirements of section 4980C(d).

"(4) NONFORFEITURE REQUIREMENTS.—

"(A) IN GENERAL.—The requirements of this paragraph are met with respect to any level premium contract, if the issuer of such contract offers to the policyholder, including any group policyholder, a nonforfeiture provision meeting the requirements of subparagraph (B).

"(B) REQUIREMENTS OF PROVISION.—The nonforfeiture provision required under subparagraph (A) shall meet the following requirements:

"(i) The nonforfeiture provision shall be appropriately captioned.

"(ii) The nonforfeiture provision shall provide for a benefit available in the event of a default in the payment of any premiums and the amount of the benefit may be adjusted subsequent to being initially granted only as necessary to reflect changes in claims, persistency, and interest as reflected in changes in rates for premium paying contracts approved by the Secretary for the same contract form.

"(iii) The nonforfeiture provision shall provide at least one of the following:

"(I) Reduced paid-up insurance.

"(II) Extended term insurance.

"(III) Shortened benefit period.

"(IV) Other similar offerings approved by the Secretary.

"(5) CROSS REFERENCE.—

"For coordination of the requirements of this subsection with State requirements, see section 4980C(f).".

SEC. 326. REQUIREMENTS FOR ISSUERS OF QUALIFIED LONG-TERM CARE INSURANCE CONTRACTS.

(a) IN GENERAL.—Chapter 43 is amended by adding at the end the following new section:

"SEC. 4980C. REQUIREMENTS FOR ISSUERS OF QUALIFIED LONG-TERM CARE INSURANCE CONTRACTS.

"(a) GENERAL RULE.—There is hereby imposed on any person failing to meet the requirements of subsection (c) or (d) a tax in the amount determined under subsection (b).

"(b) AMOUNT.—

"(1) IN GENERAL.—The amount of the tax imposed by subsection (a) shall be $100 per insured for each day any requirement of subsection (c) or (d) is not met with respect to each qualified long-term care insurance contract.

"(2) WAIVER.—In the case of a failure which is due to reasonable cause and not to willful neglect, the Secretary may waive part or all of the tax imposed by subsection (a) to the extent that payment of the tax would be excessive relative to the failure involved.

"(c) RESPONSIBILITIES.—The requirements of this subsection are as follows:

"(1) REQUIREMENTS OF MODEL PROVISIONS.—

"(A) MODEL REGULATION.—The following requirements of the model regulation must be met:

"(i) Section 13 (relating to application forms and replacement coverage).

"(ii) Section 14 (relating to reporting requirements), except that the issuer shall also report at least annually the number of claims denied during the reporting period for each class of business (expressed as a percentage of claims denied), other than claims denied for failure to meet the waiting period or because of any applicable preexisting condition.

"(iii) Section 20 (relating to filing requirements for marketing).

"(iv) Section 21 (relating to standards for marketing), including inaccurate completion of medical histories, other than sections 21C(1) and 21C(6) thereof, except that—

"(I) in addition to such requirements, no person shall, in selling or offering to sell a qualified long-term care insurance contract, misrepresent a material fact; and

"(II) no such requirements shall include a requirement to inquire or identify whether a prospective applicant or enrollee for long-term care insurance has accident and sickness insurance.

"(v) Section 22 (relating to appropriateness of recommended purchase).

"(vi) Section 24 (relating to standard format outline of coverage).

"(vii) Section 25 (relating to requirement to deliver shopper's guide).

"(B) MODEL ACT.—The following requirements of the model Act must be met:

"(i) Section 6F (relating to right to return), except that such section shall also apply to denials of applications and any refund shall be made within 30 days of the return or denial.

"(ii) Section 6G (relating to outline of coverage).

"(iii) Section 6H (relating to requirements for certificates under group plans).

"(iv) Section 6I (relating to policy summary).

"(v) Section 6J (relating to monthly reports on accelerated death benefits).

"(vi) Section 7 (relating to incontestability period).

"(C) DEFINITIONS.—For purposes of this paragraph, the terms 'model regulation' and 'model Act' have the meanings given such terms by section 7702B(g)(2)(B).

"(2) DELIVERY OF POLICY.—If an application for a qualified long-term care insurance contract (or for a certificate under such a contract for a group) is approved, the issuer shall deliver to the applicant (or policyholder or certificateholder) the contract (or certificate) of insurance not later than 30 days after the date of the approval.

"(3) INFORMATION ON DENIALS OF CLAIMS.—If a claim under a qualified long-term care insurance contract is denied, the issuer shall, within 60 days of the date of a written request by the policyholder or certificateholder (or representative)—

"(A) provide a written explanation of the reasons for the denial, and

"(B) make available all information directly relating to such denial.

"(d) DISCLOSURE.—The requirements of this subsection are met if the issuer of a long-term care insurance policy discloses in such policy and in the outline of coverage required under subsection (c)(1)(B)(ii) that the policy is intended to be a qualified long-term care insurance contract under section 7702B(b).

"(e) QUALIFIED LONG-TERM CARE INSURANCE CONTRACT DEFINED.—For purposes of this section, the term 'qualified long-term care insurance contract' has the meaning given such term by section 7702B.

"(f) COORDINATION WITH STATE REQUIREMENTS.—If a State imposes any requirement which is more stringent than the analogous requirement imposed by this section or section 7702B(g), the requirement imposed by this section or section 7702B(g) shall be treated as met if the more stringent State requirement is met.".

(b) CONFORMING AMENDMENT.—The table of sections for chapter 43 is amended by adding at the end the following new item:

"Sec. 4980C. Requirements for issuers of qualified long-term care insurance contracts.".

26 USC 4980C note.

SEC. 327. EFFECTIVE DATES.

(a) IN GENERAL.—The provisions of, and amendments made by, this part shall apply to contracts issued after December 31, 1996. The provisions of section 321(f) (relating to transition rule) shall apply to such contracts.

(b) ISSUERS.—The amendments made by section 326 shall apply to actions taken after December 31, 1996.

Subtitle D—Treatment of Accelerated Death Benefits

SEC. 331. TREATMENT OF ACCELERATED DEATH BENEFITS BY RECIPIENT.

(a) IN GENERAL.—Section 101 (relating to certain death benefits) is amended by adding at the end the following new subsection:

"(g) TREATMENT OF CERTAIN ACCELERATED DEATH BENEFITS.—

"(1) IN GENERAL.—For purposes of this section, the following amounts shall be treated as an amount paid by reason of the death of an insured:

"(A) Any amount received under a life insurance contract on the life of an insured who is a terminally ill individual.

"(B) Any amount received under a life insurance contract on the life of an insured who is a chronically ill individual.

"(2) TREATMENT OF VIATICAL SETTLEMENTS.—

"(A) IN GENERAL.—If any portion of the death benefit under a life insurance contract on the life of an insured described in paragraph (1) is sold or assigned to a viatical settlement provider, the amount paid for the sale or assignment of such portion shall be treated as an amount paid under the life insurance contract by reason of the death of such insured.

"(B) VIATICAL SETTLEMENT PROVIDER.—

"(i) IN GENERAL.—The term 'viatical settlement provider' means any person regularly engaged in the trade or business of purchasing, or taking assignments of, life insurance contracts on the lives of insureds described in paragraph (1) if—

"(I) such person is licensed for such purposes (with respect to insureds described in the same subparagraph of paragraph (1) as the insured) in the State in which the insured resides, or

"(II) in the case of an insured who resides in a State not requiring the licensing of such persons for such purposes with respect to such insured, such person meets the requirements of clause (ii) or (iii), whichever applies to such insured.

"(ii) TERMINALLY ILL INSUREDS.—A person meets the requirements of this clause with respect to an insured who is a terminally ill individual if such person—

"(I) meets the requirements of sections 8 and 9 of the Viatical Settlements Model Act of the National Association of Insurance Commissioners, and

"(II) meets the requirements of the Model Regulations of the National Association of Insurance Commissioners (relating to standards for evaluation of reasonable payments) in determining

amounts paid by such person in connection with such purchases or assignments.

"(iii) CHRONICALLY ILL INSUREDS.—A person meets the requirements of this clause with respect to an insured who is a chronically ill individual if such person—

"(I) meets requirements similar to the requirements referred to in clause (ii)(I), and

"(II) meets the standards (if any) of the National Association of Insurance Commissioners for evaluating the reasonableness of amounts paid by such person in connection with such purchases or assignments with respect to chronically ill individuals.

"(3) SPECIAL RULES FOR CHRONICALLY ILL INSUREDS.—In the case of an insured who is a chronically ill individual—

"(A) IN GENERAL.—Paragraphs (1) and (2) shall not apply to any payment received for any period unless—

"(i) such payment is for costs incurred by the payee (not compensated for by insurance or otherwise) for qualified long-term care services provided for the insured for such period, and

"(ii) the terms of the contract giving rise to such payment satisfy—

"(I) the requirements of section 7702B(b)(1)(B), and

"(II) the requirements (if any) applicable under subparagraph (B).

For purposes of the preceding sentence, the rule of section 7702B(b)(2)(B) shall apply.

"(B) OTHER REQUIREMENTS.—The requirements applicable under this subparagraph are—

"(i) those requirements of section 7702B(g) and section 4980C which the Secretary specifies as applying to such a purchase, assignment, or other arrangement,

"(ii) standards adopted by the National Association of Insurance Commissioners which specifically apply to chronically ill individuals (and, if such standards are adopted, the analogous requirements specified under clause (i) shall cease to apply), and

"(iii) standards adopted by the State in which the policyholder resides (and if such standards are adopted, the analogous requirements specified under clause (i) and (subject to section 4980C(f)) standards under clause (ii), shall cease to apply).

"(C) PER DIEM PAYMENTS.—A payment shall not fail to be described in subparagraph (A) by reason of being made on a per diem or other periodic basis without regard to the expenses incurred during the period to which the payment relates.

"(D) LIMITATION ON EXCLUSION FOR PERIODIC PAYMENTS.—

"For limitation on amount of periodic payments which are treated as described in paragraph (1), see section 7702B(d).".

"(4) DEFINITIONS.—For purposes of this subsection—

"(A) TERMINALLY ILL INDIVIDUAL.—The term 'terminally ill individual' means an individual who has been

certified by a physician as having an illness or physical condition which can reasonably be expected to result in death in 24 months or less after the date of the certification.

"(B) CHRONICALLY ILL INDIVIDUAL.—The term 'chronically ill individual' has the meaning given such term by section 7702B(c)(2); except that such term shall not include a terminally ill individual.

"(C) QUALIFIED LONG-TERM CARE SERVICES.—The term 'qualified long-term care services' has the meaning given such term by section 7702B(c).

"(D) PHYSICIAN.—The term 'physician' has the meaning given to such term by section 1861(r)(1) of the Social Security Act (42 U.S.C. 1395x(r)(1)).

"(5) EXCEPTION FOR BUSINESS-RELATED POLICIES.—This subsection shall not apply in the case of any amount paid to any taxpayer other than the insured if such taxpayer has an insurable interest with respect to the life of the insured by reason of the insured being a director, officer, or employee of the taxpayer or by reason of the insured being financially interested in any trade or business carried on by the taxpayer.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to amounts received after December 31, 1996. 26 USC 101 note.

SEC. 332. TAX TREATMENT OF COMPANIES ISSUING QUALIFIED ACCELERATED DEATH BENEFIT RIDERS.

(a) QUALIFIED ACCELERATED DEATH BENEFIT RIDERS TREATED AS LIFE INSURANCE.—Section 818 (relating to other definitions and special rules) is amended by adding at the end the following new subsection:

"(g) QUALIFIED ACCELERATED DEATH BENEFIT RIDERS TREATED AS LIFE INSURANCE.—For purposes of this part—

"(1) IN GENERAL.—Any reference to a life insurance contract shall be treated as including a reference to a qualified accelerated death benefit rider on such contract.

"(2) QUALIFIED ACCELERATED DEATH BENEFIT RIDERS.—For purposes of this subsection, the term 'qualified accelerated death benefit rider' means any rider on a life insurance contract if the only payments under the rider are payments meeting the requirements of section 101(g).

"(3) EXCEPTION FOR LONG-TERM CARE RIDERS.—Paragraph (1) shall not apply to any rider which is treated as a long-term care insurance contract under section 7702B.".

(b) EFFECTIVE DATE.— 26 USC 818 note.

(1) IN GENERAL.—The amendment made by this section shall take effect on January 1, 1997.

(2) ISSUANCE OF RIDER NOT TREATED AS MATERIAL CHANGE.—For purposes of applying sections 101(f), 7702, and 7702A of the Internal Revenue Code of 1986 to any contract—

(A) the issuance of a qualified accelerated death benefit rider (as defined in section 818(g) of such Code (as added by this Act)), and

(B) the addition of any provision required to conform an accelerated death benefit rider to the requirements of such section 818(g),

shall not be treated as a modification or material change of such contract.

Subtitle E—State Insurance Pools

SEC. 341. EXEMPTION FROM INCOME TAX FOR STATE-SPONSORED ORGANIZATIONS PROVIDING HEALTH COVERAGE FOR HIGH-RISK INDIVIDUALS.

(a) IN GENERAL.—Subsection (c) of section 501 (relating to list of exempt organizations) is amended by adding at the end the following new paragraph:

"(26) Any membership organization if—

"(A) such organization is established by a State exclusively to provide coverage for medical care (as defined in section 213(d)) on a not-for-profit basis to individuals described in subparagraph (B) through—

"(i) insurance issued by the organization, or

"(ii) a health maintenance organization under an arrangement with the organization,

"(B) the only individuals receiving such coverage through the organization are individuals—

"(i) who are residents of such State, and

"(ii) who, by reason of the existence or history of a medical condition—

"(I) are unable to acquire medical care coverage for such condition through insurance or from a health maintenance organization, or

"(II) are able to acquire such coverage only at a rate which is substantially in excess of the rate for such coverage through the membership organization,

"(C) the composition of the membership in such organization is specified by such State, and

"(D) no part of the net earnings of the organization inures to the benefit of any private shareholder or individual.".

26 USC 501 note.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 342. EXEMPTION FROM INCOME TAX FOR STATE-SPONSORED WORKMEN'S COMPENSATION REINSURANCE ORGANIZATIONS.

(a) IN GENERAL.—Subsection (c) of section 501 (relating to list of exempt organizations), as amended by section 341, is amended by adding at the end the following new paragraph:

"(27) Any membership organization if—

"(A) such organization is established before June 1, 1996, by a State exclusively to reimburse its members for losses arising under workmen's compensation acts,

"(B) such State requires that the membership of such organization consist of—

"(i) all persons who issue insurance covering workmen's compensation losses in such State, and

"(ii) all persons and governmental entities who self-insure against such losses, and

"(C) such organization operates as a non-profit organization by—

"(i) returning surplus income to its members or workmen's compensation policyholders on a periodic basis, and

"(ii) reducing initial premiums in anticipation of investment income.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years ending after the date of the enactment of this Act. 26 USC 501 note.

Subtitle F—Organizations Subject to Section 833

SEC. 351. ORGANIZATIONS SUBJECT TO SECTION 833.

(a) IN GENERAL.—Section 833(c) (relating to organization to which section applies) is amended by adding at the end the following new paragraph:

"(4) TREATMENT AS EXISTING BLUE CROSS OR BLUE SHIELD ORGANIZATION.—

"(A) IN GENERAL.—Paragraph (2) shall be applied to an organization described in subparagraph (B) as if it were a Blue Cross or Blue Shield organization.

"(B) APPLICABLE ORGANIZATION.—An organization is described in this subparagraph if it—

"(i) is organized under, and governed by, State laws which are specifically and exclusively applicable to not-for-profit health insurance or health service type organizations, and

"(ii) is not a Blue Cross or Blue Shield organization or health maintenance organization.".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years ending after December 31, 1996. 26 USC 833 note.

Subtitle G—IRA Distributions to the Unemployed

SEC. 361. DISTRIBUTIONS FROM CERTAIN PLANS MAY BE USED WITHOUT ADDITIONAL TAX TO PAY FINANCIALLY DEVASTATING MEDICAL EXPENSES.

(a) IN GENERAL.—Section 72(t)(3)(A) is amended by striking "(B),".

(b) DISTRIBUTIONS FOR PAYMENT OF HEALTH INSURANCE PREMIUMS OF CERTAIN UNEMPLOYED INDIVIDUALS.—Paragraph (2) of section 72(t) is amended by adding at the end the following new subparagraph:

"(D) DISTRIBUTIONS TO UNEMPLOYED INDIVIDUALS FOR HEALTH INSURANCE PREMIUMS.—

"(i) IN GENERAL.—Distributions from an individual retirement plan to an individual after separation from employment—

"(I) if such individual has received unemployment compensation for 12 consecutive weeks under any Federal or State unemployment compensation law by reason of such separation,

"(II) if such distributions are made during any taxable year during which such unemployment compensation is paid or the succeeding taxable year, and

"(III) to the extent such distributions do not exceed the amount paid during the taxable year for insurance described in section 213(d)(1)(D) with respect to the individual and the individual's spouse and dependents (as defined in section 152).

"(ii) DISTRIBUTIONS AFTER REEMPLOYMENT.—Clause (i) shall not apply to any distribution made after the individual has been employed for at least 60 days after the separation from employment to which clause (i) applies.

"(iii) SELF-EMPLOYED INDIVIDUALS.—To the extent provided in regulations, a self-employed individual shall be treated as meeting the requirements of clause (i)(I) if, under Federal or State law, the individual would have received unemployment compensation but for the fact the individual was self-employed.".

(c) CONFORMING AMENDMENT.—Subparagraph (B) of section 72(t)(2) is amended by striking "or (C)" and inserting ", (C), or (D)".

26 USC 72 note.

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to distributions after December 31, 1996.

Subtitle H—Organ and Tissue Donation Information Included With Income Tax Refund Payments

26 USC 6042 note.

SEC. 371. ORGAN AND TISSUE DONATION INFORMATION INCLUDED WITH INCOME TAXREFUND PAYMENTS.

(a) IN GENERAL.—The Secretary of the Treasury shall, to the extent practicable, include with the mailing of any payment of a refund of individual income tax made during the period beginning on February 1, 1997, and ending on June 30, 1997, a copy of the document described in subsection (b).

(b) TEXT OF DOCUMENT.—The Secretary of the Treasury shall, after consultation with the Secretary of Health and Human Services and organizations promoting organ and tissue (including eye) donation, prepare a document suitable for inclusion with individual income tax refund payments which—

(1) encourages organ and tissue donation;

(2) includes a detachable organ and tissue donor card; and

(3) urges recipients to—

(A) sign the organ and tissue donor card;

(B) discuss organ and tissue donation with family members and tell family members about the recipient's desire to be an organ and tissue donor if the occasion arises; and

(C) encourage family members to request or authorize organ and tissue donation if the occasion arises.

TITLE IV—APPLICATION AND ENFORCEMENT OF GROUP HEALTH PLAN REQUIREMENTS

Subtitle A—Application and Enforcement of Group Health Plan Requirements

SEC. 401. GROUP HEALTH PLAN PORTABILITY, ACCESS, AND RENEWABILITY REQUIREMENTS.

(a) IN GENERAL.—The Internal Revenue Code of 1986 is amended by adding at the end the following new subtitle:

"Subtitle K—Group Health Plan Portability, Access, and Renewability Requirements

"CHAPTER 100—GROUP HEALTH PLAN PORTABILITY, ACCESS, AND RENEWABILITY REQUIREMENTS

"SEC. 9801. INCREASED PORTABILITY THROUGH LIMITATION ON PREEXISTING CONDITION EXCLUSIONS.

"(a) LIMITATION ON PREEXISTING CONDITION EXCLUSION PERIOD; CREDITING FOR PERIODS OF PREVIOUS COVERAGE.—Subject to subsection (d), a group health plan may, with respect to a participant or beneficiary, impose a preexisting condition exclusion only if—

"(1) such exclusion relates to a condition (whether physical or mental), regardless of the cause of the condition, for which medical advice, diagnosis, care, or treatment was recommended or received within the 6-month period ending on the enrollment date;

"(2) such exclusion extends for a period of not more than 12 months (or 18 months in the case of a late enrollee) after the enrollment date; and

"(3) the period of any such preexisting condition exclusion is reduced by the length of the aggregate of the periods of creditable coverage (if any) applicable to the participant or beneficiary as of the enrollment date.

"(b) DEFINITIONS.—For purposes of this section—

"(1) PREEXISTING CONDITION EXCLUSION.—

"(A) IN GENERAL.—The term 'preexisting condition exclusion' means, with respect to coverage, a limitation or exclusion of benefits relating to a condition based on

the fact that the condition was present before the date of enrollment for such coverage, whether or not any medical advice, diagnosis, care, or treatment was recommended or received before such date.

"(B) TREATMENT OF GENETIC INFORMATION.—For purposes of this section, genetic information shall not be treated as a condition described in subsection (a)(1) in the absence of a diagnosis of the condition related to such information.

"(2) ENROLLMENT DATE.—The term 'enrollment date' means, with respect to an individual covered under a group health plan, the date of enrollment of the individual in the plan or, if earlier, the first day of the waiting period for such enrollment.

"(3) LATE ENROLLEE.—The term 'late enrollee' means, with respect to coverage under a group health plan, a participant or beneficiary who enrolls under the plan other than during—

"(A) the first period in which the individual is eligible to enroll under the plan, or

"(B) a special enrollment period under subsection (f).

"(4) WAITING PERIOD.—The term 'waiting period' means, with respect to a group health plan and an individual who is a potential participant or beneficiary in the plan, the period that must pass with respect to the individual before the individual is eligible to be covered for benefits under the terms of the plan.

"(c) RULES RELATING TO CREDITING PREVIOUS COVERAGE.—

"(1) CREDITABLE COVERAGE DEFINED.—For purposes of this part, the term 'creditable coverage' means, with respect to an individual, coverage of the individual under any of the following:

"(A) A group health plan.

"(B) Health insurance coverage.

"(C) Part A or part B of title XVIII of the Social Security Act.

"(D) Title XIX of the Social Security Act, other than coverage consisting solely of benefits under section 1928.

"(E) Chapter 55 of title 10, United States Code.

"(F) A medical care program of the Indian Health Service or of a tribal organization.

"(G) A State health benefits risk pool.

"(H) A health plan offered under chapter 89 of title 5, United States Code.

"(I) A public health plan (as defined in regulations).

"(J) A health benefit plan under section 5(e) of the Peace Corps Act (22 U.S.C. 2504(e)).

Such term does not include coverage consisting solely of coverage of excepted benefits (as defined in section 9805(c)).

"(2) NOT COUNTING PERIODS BEFORE SIGNIFICANT BREAKS IN COVERAGE.—

"(A) IN GENERAL.—A period of creditable coverage shall not be counted, with respect to enrollment of an individual under a group health plan, if, after such period and before the enrollment date, there was a 63-day period during all of which the individual was not covered under any creditable coverage.

"(B) WAITING PERIOD NOT TREATED AS A BREAK IN COVERAGE.—For purposes of subparagraph (A) and subsection (d)(4), any period that an individual is in a waiting period for any coverage under a group health plan or is in an affiliation period shall not be taken into account in determining the continuous period under subparagraph (A).

"(C) AFFILIATION PERIOD.—

"(i) IN GENERAL.—For purposes of this section, the term 'affiliation period' means a period which, under the terms of the health insurance coverage offered by the health maintenance organization, must expire before the health insurance coverage becomes effective. During such an affiliation period, the organization is not required to provide health care services or benefits and no premium shall be charged to the participant or beneficiary.

"(ii) BEGINNING.—Such period shall begin on the enrollment date.

"(iii) RUNS CONCURRENTLY WITH WAITING PERIODS.—Any such affiliation period shall run concurrently with any waiting period under the plan.

"(3) METHOD OF CREDITING COVERAGE.—

"(A) STANDARD METHOD.—Except as otherwise provided under subparagraph (B), for purposes of applying subsection (a)(3), a group health plan shall count a period of creditable coverage without regard to the specific benefits for which coverage is offered during the period.

"(B) ELECTION OF ALTERNATIVE METHOD.—A group health plan may elect to apply subsection (a)(3) based on coverage of any benefits within each of several classes or categories of benefits specified in regulations rather than as provided under subparagraph (A). Such election shall be made on a uniform basis for all participants and beneficiaries. Under such election a group health plan shall count a period of creditable coverage with respect to any class or category of benefits if any level of benefits is covered within such class or category.

"(C) PLAN NOTICE.—In the case of an election with respect to a group health plan under subparagraph (B), the plan shall—

"(i) prominently state in any disclosure statements concerning the plan, and state to each enrollee at the time of enrollment under the plan, that the plan has made such election, and

"(ii) include in such statements a description of the effect of this election.

"(4) ESTABLISHMENT OF PERIOD.—Periods of creditable coverage with respect to an individual shall be established through presentation of certifications described in subsection (e) or in such other manner as may be specified in regulations.

"(d) EXCEPTIONS.—

"(1) EXCLUSION NOT APPLICABLE TO CERTAIN NEWBORNS.—Subject to paragraph (4), a group health plan may not impose any preexisting condition exclusion in the case of an individual who, as of the last day of the 30-day period beginning with the date of birth, is covered under creditable coverage.

"(2) EXCLUSION NOT APPLICABLE TO CERTAIN ADOPTED CHILDREN.—Subject to paragraph (4), a group health plan may not impose any preexisting condition exclusion in the case of a child who is adopted or placed for adoption before attaining 18 years of age and who, as of the last day of the 30-day period beginning on the date of the adoption or placement for adoption, is covered under creditable coverage. The previous sentence shall not apply to coverage before the date of such adoption or placement for adoption.

"(3) EXCLUSION NOT APPLICABLE TO PREGNANCY.—For purposes of this section, a group health plan may not impose any preexisting condition exclusion relating to pregnancy as a preexisting condition.

"(4) LOSS IF BREAK IN COVERAGE.—Paragraphs (1) and (2) shall no longer apply to an individual after the end of the first 63-day period during all of which the individual was not covered under any creditable coverage.

"(e) CERTIFICATIONS AND DISCLOSURE OF COVERAGE.—

"(1) REQUIREMENT FOR CERTIFICATION OF PERIOD OF CREDITABLE COVERAGE.—

"(A) IN GENERAL.—A group health plan shall provide the certification described in subparagraph (B)—

"(i) at the time an individual ceases to be covered under the plan or otherwise becomes covered under a COBRA continuation provision,

"(ii) in the case of an individual becoming covered under such a provision, at the time the individual ceases to be covered under such provision, and

"(iii) on the request on behalf of an individual made not later than 24 months after the date of cessation of the coverage described in clause (i) or (ii), whichever is later.

The certification under clause (i) may be provided, to the extent practicable, at a time consistent with notices required under any applicable COBRA continuation provision.

"(B) CERTIFICATION.—The certification described in this subparagraph is a written certification of—

"(i) the period of creditable coverage of the individual under such plan and the coverage under such COBRA continuation provision, and

"(ii) the waiting period (if any) (and affiliation period, if applicable) imposed with respect to the individual for any coverage under such plan.

"(C) ISSUER COMPLIANCE.—To the extent that medical care under a group health plan consists of health insurance coverage offered in connection with the plan, the plan is deemed to have satisfied the certification requirement under this paragraph if the issuer provides for such certification in accordance with this paragraph.

"(2) DISCLOSURE OF INFORMATION ON PREVIOUS BENEFITS.—

"(A) IN GENERAL.—In the case of an election described in subsection (c)(3)(B) by a group health plan, if the plan enrolls an individual for coverage under the plan and the individual provides a certification of coverage of the individual under paragraph (1)—

"(i) upon request of such plan, the entity which issued the certification provided by the individual shall promptly disclose to such requesting plan information on coverage of classes and categories of health benefits available under such entity's plan, and

"(ii) such entity may charge the requesting plan or issuer for the reasonable cost of disclosing such information.

"(3) REGULATIONS.—The Secretary shall establish rules to prevent an entity's failure to provide information under paragraph (1) or (2) with respect to previous coverage of an individual from adversely affecting any subsequent coverage of the individual under another group health plan or health insurance coverage.

"(f) SPECIAL ENROLLMENT PERIODS.—

"(1) INDIVIDUALS LOSING OTHER COVERAGE.—A group health plan shall permit an employee who is eligible, but not enrolled, for coverage under the terms of the plan (or a dependent of such an employee if the dependent is eligible, but not enrolled, for coverage under such terms) to enroll for coverage under the terms of the plan if each of the following conditions is met:

"(A) The employee or dependent was covered under a group health plan or had health insurance coverage at the time coverage was previously offered to the employee or individual.

"(B) The employee stated in writing at such time that coverage under a group health plan or health insurance coverage was the reason for declining enrollment, but only if the plan sponsor (or the health insurance issuer offering health insurance coverage in connection with the plan) required such a statement at such time and provided the employee with notice of such requirement (and the consequences of such requirement) at such time.

"(C) The employee's or dependent's coverage described in subparagraph (A)—

"(i) was under a COBRA continuation provision and the coverage under such provision was exhausted; or

"(ii) was not under such a provision and either the coverage was terminated as a result of loss of eligibility for the coverage (including as a result of legal separation, divorce, death, termination of employment, or reduction in the number of hours of employment) or employer contributions toward such coverage were terminated.

"(D) Under the terms of the plan, the employee requests such enrollment not later than 30 days after the date of exhaustion of coverage described in subparagraph (C)(i) or termination of coverage or employer contribution described in subparagraph (C)(ii).

"(2) FOR DEPENDENT BENEFICIARIES.—

"(A) IN GENERAL.—If—

"(i) a group health plan makes coverage available with respect to a dependent of an individual,

"(ii) the individual is a participant under the plan (or has met any waiting period applicable to becoming

a participant under the plan and is eligible to be enrolled under the plan but for a failure to enroll during a previous enrollment period), and

"(iii) a person becomes such a dependent of the individual through marriage, birth, or adoption or placement for adoption,

the group health plan shall provide for a dependent special enrollment period described in subparagraph (B) during which the person (or, if not otherwise enrolled, the individual) may be enrolled under the plan as a dependent of the individual, and in the case of the birth or adoption of a child, the spouse of the individual may be enrolled as a dependent of the individual if such spouse is otherwise eligible for coverage.

"(B) DEPENDENT SPECIAL ENROLLMENT PERIOD.—The dependent special enrollment period under this subparagraph shall be a period of not less than 30 days and shall begin on the later of—

"(i) the date dependent coverage is made available, or

"(ii) the date of the marriage, birth, or adoption or placement for adoption (as the case may be) described in subparagraph (A)(iii).

"(C) NO WAITING PERIOD.—If an individual seeks coverage of a dependent during the first 30 days of such a dependent special enrollment period, the coverage of the dependent shall become effective—

"(i) in the case of marriage, not later than the first day of the first month beginning after the date the completed request for enrollment is received;

"(ii) in the case of a dependent's birth, as of the date of such birth; or

"(iii) in the case of a dependent's adoption or placement for adoption, the date of such adoption or placement for adoption.

"SEC. 9802. PROHIBITING DISCRIMINATION AGAINST INDIVIDUAL PARTICIPANTS AND BENEFICIARIES BASED ON HEALTH STATUS.

"(a) IN ELIGIBILITY TO ENROLL.—

"(1) IN GENERAL.—Subject to paragraph (2), a group health plan may not establish rules for eligibility (including continued eligibility) of any individual to enroll under the terms of the plan based on any of the following factors in relation to the individual or a dependent of the individual:

"(A) Health status.

"(B) Medical condition (including both physical and mental illnesses).

"(C) Claims experience.

"(D) Receipt of health care.

"(E) Medical history.

"(F) Genetic information.

"(G) Evidence of insurability (including conditions arising out of acts of domestic violence).

"(H) Disability.

"(2) NO APPLICATION TO BENEFITS OR EXCLUSIONS.—To the extent consistent with section 9801, paragraph (1) shall not be construed—

"(A) to require a group health plan to provide particular benefits (or benefits with respect to a specific procedure, treatment, or service) other than those provided under the terms of such plan; or

"(B) to prevent such a plan from establishing limitations or restrictions on the amount, level, extent, or nature of the benefits or coverage for similarly situated individuals enrolled in the plan or coverage.

"(3) CONSTRUCTION.—For purposes of paragraph (1), rules for eligibility to enroll under a plan include rules defining any applicable waiting periods for such enrollment.

"(b) IN PREMIUM CONTRIBUTIONS.—

"(1) IN GENERAL.—A group health plan may not require any individual (as a condition of enrollment or continued enrollment under the plan) to pay a premium or contribution which is greater than such premium or contribution for a similarly situated individual enrolled in the plan on the basis of any factor described in subsection (a)(1) in relation to the individual or to an individual enrolled under the plan as a dependent of the individual.

"(2) CONSTRUCTION.—Nothing in paragraph (1) shall be construed—

"(A) to restrict the amount that an employer may be charged for coverage under a group health plan; or

"(B) to prevent a group health plan from establishing premium discounts or rebates or modifying otherwise applicable copayments or deductibles in return for adherence to programs of health promotion and disease prevention.

"SEC. 9803. GUARANTEED RENEWABILITY IN MULTIEMPLOYER PLANS AND CERTAIN MULTIPLE EMPLOYER WELFARE ARRANGEMENTS.

"(a) IN GENERAL.—A group health plan which is a multiemployer plan (as defined in section 414(f)) or which is a multiple employer welfare arrangement may not deny an employer continued access to the same or different coverage under such plan, other than—

"(1) for nonpayment of contributions;

"(2) for fraud or other intentional misrepresentation of material fact by the employer;

"(3) for noncompliance with material plan provisions;

"(4) because the plan is ceasing to offer any coverage in a geographic area;

"(5) in the case of a plan that offers benefits through a network plan, because there is no longer any individual enrolled through the employer who lives, resides, or works in the service area of the network plan and the plan applies this paragraph uniformly without regard to the claims experience of employers or a factor described in section 9802(a)(1) in relation to such individuals or their dependents; or

"(6) for failure to meet the terms of an applicable collective bargaining agreement, to renew a collective bargaining or other

agreement requiring or authorizing contributions to the plan, or to employ employees covered by such an agreement.

"(b) MULTIPLE EMPLOYER WELFARE ARRANGEMENT.—For purposes of subsection (a), the term 'multiple employer welfare arrangement' has the meaning given such term by section 3(40) of the Employee Retirement Income Security Act of 1974, as in effect on the date of the enactment of this section.

"SEC. 9804. GENERAL EXCEPTIONS.

"(a) EXCEPTION FOR CERTAIN PLANS.—The requirements of this chapter shall not apply to—

"(1) any governmental plan, and

"(2) any group health plan for any plan year if, on the first day of such plan year, such plan has less than 2 participants who are current employees.

"(b) EXCEPTION FOR CERTAIN BENEFITS.—The requirements of this chapter shall not apply to any group health plan in relation to its provision of excepted benefits described in section 9805(c)(1).

"(c) EXCEPTION FOR CERTAIN BENEFITS IF CERTAIN CONDITIONS MET.—

"(1) LIMITED, EXCEPTED BENEFITS.—The requirements of this chapter shall not apply to any group health plan in relation to its provision of excepted benefits described in section 9805(c)(2) if the benefits—

"(A) are provided under a separate policy, certificate, or contract of insurance; or

"(B) are otherwise not an integral part of the plan.

"(2) NONCOORDINATED, EXCEPTED BENEFITS.—The requirements of this chapter shall not apply to any group health plan in relation to its provision of excepted benefits described in section 9805(c)(3) if all of the following conditions are met:

"(A) The benefits are provided under a separate policy, certificate, or contract of insurance.

"(B) There is no coordination between the provision of such benefits and any exclusion of benefits under any group health plan maintained by the same plan sponsor.

"(C) Such benefits are paid with respect to an event without regard to whether benefits are provided with respect to such an event under any group health plan maintained by the same plan sponsor.

"(3) SUPPLEMENTAL EXCEPTED BENEFITS.—The requirements of this chapter shall not apply to any group health plan in relation to its provision of excepted benefits described in section 9805(c)(4) if the benefits are provided under a separate policy, certificate, or contract of insurance.

"SEC. 9805. DEFINITIONS.

"(a) GROUP HEALTH PLAN.—For purposes of this chapter, the term 'group health plan' has the meaning given to such term by section 5000(b)(1).

"(b) DEFINITIONS RELATING TO HEALTH INSURANCE.—For purposes of this chapter—

"(1) HEALTH INSURANCE COVERAGE.—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'health insurance coverage' means benefits consisting of medical care (provided directly, through insurance or reimbursement, or otherwise) under any hospital or medical service policy or certificate, hospital or medical

service plan contract, or health maintenance organization contract offered by a health insurance issuer.

"(B) NO APPLICATION TO CERTAIN EXCEPTED BENEFITS.—In applying subparagraph (A), excepted benefits described in subsection (c)(1) shall not be treated as benefits consisting of medical care.

"(2) HEALTH INSURANCE ISSUER.—The term 'health insurance issuer' means an insurance company, insurance service, or insurance organization (including a health maintenance organization, as defined in paragraph (3)) which is licensed to engage in the business of insurance in a State and which is subject to State law which regulates insurance (within the meaning of section 514(b)(2) of the Employee Retirement Income Security Act of 1974, as in effect on the date of the enactment of this section). Such term does not include a group health plan.

"(3) HEALTH MAINTENANCE ORGANIZATION.—The term 'health maintenance organization' means—

"(A) a federally qualified health maintenance organization (as defined in section 1301(a) of the Public Health Service Act (42 U.S.C. 300e(a))),

"(B) an organization recognized under State law as a health maintenance organization, or

"(C) a similar organization regulated under State law for solvency in the same manner and to the same extent as such a health maintenance organization.

"(c) EXCEPTED BENEFITS.—For purposes of this chapter, the term 'excepted benefits' means benefits under one or more (or any combination thereof) of the following:

"(1) BENEFITS NOT SUBJECT TO REQUIREMENTS.—

"(A) Coverage only for accident, or disability income insurance, or any combination thereof.

"(B) Coverage issued as a supplement to liability insurance.

"(C) Liability insurance, including general liability insurance and automobile liability insurance.

"(D) Workers' compensation or similar insurance.

"(E) Automobile medical payment insurance.

"(F) Credit-only insurance.

"(G) Coverage for on-site medical clinics.

"(H) Other similar insurance coverage, specified in regulations, under which benefits for medical care are secondary or incidental to other insurance benefits.

"(2) BENEFITS NOT SUBJECT TO REQUIREMENTS IF OFFERED SEPARATELY.—

"(A) Limited scope dental or vision benefits.

"(B) Benefits for long-term care, nursing home care, home health care, community-based care, or any combination thereof.

"(C) Such other similar, limited benefits as are specified in regulations.

"(3) BENEFITS NOT SUBJECT TO REQUIREMENTS IF OFFERED AS INDEPENDENT, NONCOORDINATED BENEFITS.—

"(A) Coverage only for a specified disease or illness.

"(B) Hospital indemnity or other fixed indemnity insurance.

"(4) BENEFITS NOT SUBJECT TO REQUIREMENTS IF OFFERED AS SEPARATE INSURANCE POLICY.—Medicare supplemental health insurance (as defined under section 1882(g)(1) of the Social Security Act), coverage supplemental to the coverage provided under chapter 55 of title 10, United States Code, and similar supplemental coverage provided to coverage under a group health plan.

"(d) OTHER DEFINITIONS.—For purposes of this chapter—

"(1) COBRA CONTINUATION PROVISION.—The term 'COBRA continuation provision' means any of the following:

"(A) Section 4980B, other than subsection (f)(1) thereof insofar as it relates to pediatric vaccines.

"(B) Part 6 of subtitle B of title I of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1161 et seq.), other than section 609 of such Act.

"(C) Title XXII of the Public Health Service Act.

"(2) GOVERNMENTAL PLAN.—The term 'governmental plan' has the meaning given such term by section 414(d).

"(3) MEDICAL CARE.—The term 'medical care' has the meaning given such term by section 213(d) determined without regard to—

"(A) paragraph (1)(C) thereof, and

"(B) so much of paragraph (1)(D) thereof as relates to qualified long-term care insurance.

"(4) NETWORK PLAN.—The term 'network plan' means health insurance coverage of a health insurance issuer under which the financing and delivery of medical care are provided, in whole or in part, through a defined set of providers under contract with the issuer.

"(5) PLACED FOR ADOPTION DEFINED.—The term 'placement', or being 'placed', for adoption, in connection with any placement for adoption of a child with any person, means the assumption and retention by such person of a legal obligation for total or partial support of such child in anticipation of adoption of such child. The child's placement with such person terminates upon the termination of such legal obligation.

"SEC. 9806. REGULATIONS.

"The Secretary, consistent with section 104 of the Health Care Portability and Accountability Act of 1996, may promulgate such regulations as may be necessary or appropriate to carry out the provisions of this chapter. The Secretary may promulgate any interim final rules as the Secretary determines are appropriate to carry out this chapter.".

(b) CLERICAL AMENDMENT.—The table of subtitles of such Code is amended by adding at the end the following new item:

"Subtitle K. Group health plan portability, access, and renewability requirements.".

26 USC 9801 note.

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to plan years beginning after June 30, 1997.

(2) DETERMINATION OF CREDITABLE COVERAGE.—

(A) PERIOD OF COVERAGE.—

(i) IN GENERAL.—Subject to clause (ii), no period before July 1, 1996, shall be taken into account under chapter 100 of the Internal Revenue Code of 1986 (as added by this section) in determining creditable coverage.

(ii) SPECIAL RULE FOR CERTAIN PERIODS.—The Secretary of the Treasury, consistent with section 104, shall provide for a process whereby individuals who need to establish creditable coverage for periods before July 1, 1996, and who would have such coverage credited but for clause (i) may be given credit for creditable coverage for such periods through the presentation of documents or other means.

(B) CERTIFICATIONS, ETC.—

(i) IN GENERAL.—Subject to clauses (ii) and (iii), subsection (e) of section 9801 of the Internal Revenue Code of 1986 (as added by this section) shall apply to events occurring after June 30, 1996.

(ii) NO CERTIFICATION REQUIRED TO BE PROVIDED BEFORE JUNE 1, 1997.—In no case is a certification required to be provided under such subsection before June 1, 1997.

(iii) CERTIFICATION ONLY ON WRITTEN REQUEST FOR EVENTS OCCURRING BEFORE OCTOBER 1, 1996.—In the case of an event occurring after June 30, 1996, and before October 1, 1996, a certification is not required to be provided under such subsection unless an individual (with respect to whom the certification is otherwise required to be made) requests such certification in writing.

(C) TRANSITIONAL RULE.—In the case of an individual who seeks to establish creditable coverage for any period for which certification is not required because it relates to an event occurring before June 30, 1996—

(i) the individual may present other credible evidence of such coverage in order to establish the period of creditable coverage; and

(ii) a group health plan and a health insurance issuer shall not be subject to any penalty or enforcement action with respect to the plan's or issuer's crediting (or not crediting) such coverage if the plan or issuer has sought to comply in good faith with the applicable requirements under the amendments made by this section.

(3) SPECIAL RULE FOR COLLECTIVE BARGAINING AGREEMENTS.—Except as provided in paragraph (2), in the case of a group health plan maintained pursuant to 1 or more collective bargaining agreements between employee representatives and one or more employers ratified before the date of the enactment of this Act, the amendments made by this section shall not apply to plan years beginning before the later of—

(A) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension thereof agreed to after the date of the enactment of this Act), or

(B) July 1, 1997.

For purposes of subparagraph (A), any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added by this section shall not be treated as a termination of such collective bargaining agreement.

(4) TIMELY REGULATIONS.—The Secretary of the Treasury, consistent with section 104, shall first issue by not later than April 1, 1997, such regulations as may be necessary to carry out the amendments made by this section.

(5) LIMITATION ON ACTIONS.—No enforcement action shall be taken, pursuant to the amendments made by this section, against a group health plan or health insurance issuer with respect to a violation of a requirement imposed by such amendments before January 1, 1998, or, if later, the date of issuance of regulations referred to in paragraph (4), if the plan or issuer has sought to comply in good faith with such requirements.

SEC. 402. PENALTY ON FAILURE TO MEET CERTAIN GROUP HEALTH PLAN REQUIREMENTS.

(a) IN GENERAL.—Chapter 43 of the Internal Revenue Code of 1986 (relating to qualified pension, etc., plans) is amended by adding after section 4980C the following new section:

"SEC. 4980D. FAILURE TO MEET CERTAIN GROUP HEALTH PLAN REQUIREMENTS.

"(a) GENERAL RULE.—There is hereby imposed a tax on any failure of a group health plan to meet the requirements of chapter 100 (relating to group health plan portability, access, and renewability requirements).

"(b) AMOUNT OF TAX.—

"(1) IN GENERAL.—The amount of the tax imposed by subsection (a) on any failure shall be $100 for each day in the noncompliance period with respect to each individual to whom such failure relates.

"(2) NONCOMPLIANCE PERIOD.—For purposes of this section, the term 'noncompliance period' means, with respect to any failure, the period—

"(A) beginning on the date such failure first occurs, and

"(B) ending on the date such failure is corrected.

"(3) MINIMUM TAX FOR NONCOMPLIANCE PERIOD WHERE FAILURE DISCOVERED AFTER NOTICE OF EXAMINATION.—Notwithstanding paragraphs (1) and (2) of subsection (c)—

"(A) IN GENERAL.—In the case of 1 or more failures with respect to an individual—

"(i) which are not corrected before the date a notice of examination of income tax liability is sent to the employer, and

"(ii) which occurred or continued during the period under examination,

the amount of tax imposed by subsection (a) by reason of such failures with respect to such individual shall not be less than the lesser of $2,500 or the amount of tax which would be imposed by subsection (a) without regard to such paragraphs.

"(B) HIGHER MINIMUM TAX WHERE VIOLATIONS ARE MORE THAN DE MINIMIS.—To the extent violations for which any person is liable under subsection (e) for any year are more than de minimis, subparagraph (A) shall be applied by substituting '$15,000' for '$2,500' with respect to such person.

"(C) EXCEPTION FOR CHURCH PLANS.—This paragraph shall not apply to any failure under a church plan (as defined in section 414(e)).

"(c) LIMITATIONS ON AMOUNT OF TAX.—

"(1) TAX NOT TO APPLY WHERE FAILURE NOT DISCOVERED EXERCISING REASONABLE DILIGENCE.—No tax shall be imposed by subsection (a) on any failure during any period for which it is established to the satisfaction of the Secretary that the person otherwise liable for such tax did not know, and exercising reasonable diligence would not have known, that such failure existed.

"(2) TAX NOT TO APPLY TO FAILURES CORRECTED WITHIN CERTAIN PERIODS.—No tax shall be imposed by subsection (a) on any failure if—

"(A) such failure was due to reasonable cause and not to willful neglect, and

"(B)(i) in the case of a plan other than a church plan (as defined in section 414(e)), such failure is corrected during the 30-day period beginning on the first date the person otherwise liable for such tax knew, or exercising reasonable diligence would have known, that such failure existed, and

"(ii) in the case of a church plan (as so defined), such failure is corrected before the close of the correction period (determined under the rules of section 414(e)(4)(C)).

"(3) OVERALL LIMITATION FOR UNINTENTIONAL FAILURES.—In the case of failures which are due to reasonable cause and not to willful neglect—

"(A) SINGLE EMPLOYER PLANS.—

"(i) IN GENERAL.—In the case of failures with respect to plans other than specified multiple employer health plans, the tax imposed by subsection (a) for failures during the taxable year of the employer shall not exceed the amount equal to the lesser of—

"(I) 10 percent of the aggregate amount paid or incurred by the employer (or predecessor employer) during the preceding taxable year for group health plans, or

"(II) $500,000.

"(ii) TAXABLE YEARS IN THE CASE OF CERTAIN CONTROLLED GROUPS.—For purposes of this subparagraph, if not all persons who are treated as a single employer for purposes of this section have the same taxable year, the taxable years taken into account shall be determined under principles similar to the principles of section 1561.

"(B) SPECIFIED MULTIPLE EMPLOYER HEALTH PLANS.—

"(i) IN GENERAL.—In the case of failures with respect to a specified multiple employer health plan, the tax imposed by subsection (a) for failures during the taxable year of the trust forming part of such plan shall not exceed the amount equal to the lesser of—

"(I) 10 percent of the amount paid or incurred by such trust during such taxable year to provide medical care (as defined in section 9805(d)(3))

directly or through insurance, reimbursement, or otherwise, or

"(II) $500,000.

For purposes of the preceding sentence, all plans of which the same trust forms a part shall be treated as one plan.

"(ii) SPECIAL RULE FOR EMPLOYERS REQUIRED TO PAY TAX.—If an employer is assessed a tax imposed by subsection (a) by reason of a failure with respect to a specified multiple employer health plan, the limit shall be determined under subparagraph (A) (and not under this subparagraph) and as if such plan were not a specified multiple employer health plan.

"(4) WAIVER BY SECRETARY.—In the case of a failure which is due to reasonable cause and not to willful neglect, the Secretary may waive part or all of the tax imposed by subsection (a) to the extent that the payment of such tax would be excessive relative to the failure involved.

"(d) TAX NOT TO APPLY TO CERTAIN INSURED SMALL EMPLOYER PLANS.—

"(1) IN GENERAL.—In the case of a group health plan of a small employer which provides health insurance coverage solely through a contract with a health insurance issuer, no tax shall be imposed by this section on the employer on any failure which is solely because of the health insurance coverage offered by such issuer.

"(2) SMALL EMPLOYER.—

"(A) IN GENERAL.—For purposes of paragraph (1), the term 'small employer' means, with respect to a calendar year and a plan year, an employer who employed an average of at least 2 but not more than 50 employees on business days during the preceding calendar year and who employs at least 2 employees on the first day of the plan year. For purposes of the preceding sentence, all persons treated as a single employer under subsection (b), (c), (m), or (o) of section 414 shall be treated as one employer.

"(B) EMPLOYERS NOT IN EXISTENCE IN PRECEDING YEAR.—In the case of an employer which was not in existence throughout the preceding calendar year, the determination of whether such employer is a small employer shall be based on the average number of employees that it is reasonably expected such employer will employ on business days in the current calendar year.

"(C) PREDECESSORS.—Any reference in this paragraph to an employer shall include a reference to any predecessor of such employer.

"(3) HEALTH INSURANCE COVERAGE; HEALTH INSURANCE ISSUER.—For purposes of paragraph (1), the terms 'health insurance coverage' and 'health insurance issuer' have the respective meanings given such terms by section 9805.

"(e) LIABILITY FOR TAX.—The following shall be liable for the tax imposed by subsection (a) on a failure:

"(1) Except as otherwise provided in this subsection, the employer.

"(2) In the case of a multiemployer plan, the plan.

"(3) In the case of a failure under section 9803 (relating to guaranteed renewability) with respect to a plan described in subsection (f)(2)(B), the plan.

"(f) DEFINITIONS.—For purposes of this section—

"(1) GROUP HEALTH PLAN.—The term 'group health plan' has the meaning given such term by section 9805(a).

"(2) SPECIFIED MULTIPLE EMPLOYER HEALTH PLAN.—The term 'specified multiple employer health plan' means a group health plan which is—

"(A) any multiemployer plan, or

"(B) any multiple employer welfare arrangement (as defined in section 3(40) of the Employee Retirement Income Security Act of 1974, as in effect on the date of the enactment of this section).

"(3) CORRECTION.—A failure of a group health plan shall be treated as corrected if—

"(A) such failure is retroactively undone to the extent possible, and

"(B) the person to whom the failure relates is placed in a financial position which is as good as such person would have been in had such failure not occurred.".

(b) CLERICAL AMENDMENT.—The table of sections for chapter 43 of such Code is amended by adding after the item relating to section 4980C the following new item:

"Sec. 4980D. Failure to meet certain group health plan requirements.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to failures under chapter 100 of the Internal Revenue Code of 1986 (as added by section 401 of this Act). 26 USC 4980D note.

Subtitle B—Clarification of Certain Continuation Coverage Requirements

SEC. 421. COBRA CLARIFICATIONS.

(a) PUBLIC HEALTH SERVICE ACT.—

(1) PERIOD OF COVERAGE.—Section 2202(2) of the Public Health Service Act (42 U.S.C. 300bb–2(2)) is amended—

(A) in subparagraph (A)—

(i) by transferring the sentence immediately preceding clause (iv) so as to appear immediately following such clause (iv); and

(ii) in the last sentence (as so transferred)—

(I) by striking "an individual" and inserting "a qualified beneficiary";

(II) by striking "at the time of a qualifying event described in section 2203(2)" and inserting "at any time during the first 60 days of continuation coverage under this title";

(III) by striking "with respect to such event,"; and

(IV) by inserting "(with respect to all qualified beneficiaries)" after "29 months";

(B) in subparagraph (D)(i), by inserting before ", or" the following: "(other than such an exclusion or limitation which does not apply to (or is satisfied by) such beneficiary by reason of chapter 100 of the Internal Revenue Code

of 1986, part 7 of subtitle B of title I of the Employee Retirement Income Security Act of 1974, or title XXVII of this Act)"; and

(C) in subparagraph (E), by striking "at the time of a qualifying event described in section 2203(2)" and inserting "at any time during the first 60 days of continuation coverage under this title".

(2) NOTICES.—Section 2206(3) of the Public Health Service Act (42 U.S.C. 300bb–6(3)) is amended by striking "at the time of a qualifying event described in section 2203(2)" and inserting "at any time during the first 60 days of continuation coverage under this title".

(3) BIRTH OR ADOPTION OF A CHILD.—Section 2208(3)(A) of the Public Health Service Act (42 U.S.C. 300bb–8(3)(A)) is amended by adding at the end thereof the following new flush sentence:

"Such term shall also include a child who is born to or placed for adoption with the covered employee during the period of continuation coverage under this title.".

(b) EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974.—

(1) PERIOD OF COVERAGE.—Section 602(2) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1162(2)) is amended—

(A) in the last sentence of subparagraph (A)—

(i) by striking "an individual" and inserting "a qualified beneficiary";

(ii) by striking "at the time of a qualifying event described in section 603(2)" and inserting "at any time during the first 60 days of continuation coverage under this part";

(iii) by striking "with respect to such event"; and

(iv) by inserting "(with respect to all qualified beneficiaries)" after "29 months";

(B) in subparagraph (D)(i), by inserting before ", or" the following: "(other than such an exclusion or limitation which does not apply to (or is satisfied by) such beneficiary by reason of chapter 100 of the Internal Revenue Code of 1986, part 7 of this subtitle, or title XXVII of the Public Health Service Act)"; and

(C) in subparagraph (E), by striking "at the time of a qualifying event described in section 603(2)" and inserting "at any time during the first 60 days of continuation coverage under this part".

(2) NOTICES.—Section 606(a)(3) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1166(a)(3)) is amended by striking "at the time of a qualifying event described in section 603(2)" and inserting "at any time during the first 60 days of continuation coverage under this part".

(3) BIRTH OR ADOPTION OF A CHILD.—Section 607(3)(A) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1167(3)) is amended by adding at the end thereof the following new flush sentence:

"Such term shall also include a child who is born to or placed for adoption with the covered employee during the period of continuation coverage under this part.".

(c) INTERNAL REVENUE CODE OF 1986.—

(1) PERIOD OF COVERAGE.—Section 4980B(f)(2)(B) of the Internal Revenue Code of 1986 is amended—

(A) in the last sentence of clause (i)—

(i) by striking "at the time of a qualifying event described in paragraph (3)(B)" and inserting "at any time during the first 60 days of continuation coverage under this section";

(ii) by striking "with respect to such event"; and

(iii) by inserting "(with respect to all qualified beneficiaries)" after "29 months";

(B) in clause (iv)(I), by inserting before ", or" the following: "(other than such an exclusion or limitation which does not apply to (or is satisfied by) such beneficiary by reason of chapter 100 of this title, part 7 of subtitle B of title I of the Employee Retirement Income Security Act of 1974, or title XXVII of the Public Health Service Act)"; and

(C) in clause (v), by striking "at the time of a qualifying event described in paragraph (3)(B)" and inserting "at any time during the first 60 days of continuation coverage under this section".

(2) NOTICES.—Section 4980B(f)(6)(C) of the Internal Revenue Code of 1986 is amended by striking "at the time of a qualifying event described in paragraph (3)(B)" and inserting "at any time during the first 60 days of continuation coverage under this section".

(3) BIRTH OR ADOPTION OF A CHILD.—Section 4980B(g)(1)(A) of the Internal Revenue Code of 1986 is amended by adding at the end thereof the following new flush sentence:

"Such term shall also include a child who is born to or placed for adoption with the covered employee during the period of continuation coverage under this section.".

(d) EFFECTIVE DATE.—The amendments made by this section shall become effective on January 1, 1997, regardless of whether the qualifying event occurred before, on, or after such date. 26 USC 4980B note.

(e) NOTIFICATION OF CHANGES.—Not later than November 1, 1996, each group health plan (covered under title XXII of the Public Health Service Act, part 6 of subtitle B of title I of the Employee Retirement Income Security Act of 1974, and section 4980B(f) of the Internal Revenue Code of 1986) shall notify each qualified beneficiary who has elected continuation coverage under such title, part or section of the amendments made by this section. 26 USC 4980B note.

TITLE V—REVENUE OFFSETS

SEC. 500. AMENDMENT OF 1986 CODE.

Except as otherwise expressly provided, whenever in this title an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

Subtitle A—Company-Owned Life Insurance

SEC. 501. DENIAL OF DEDUCTION FOR INTEREST ON LOANS WITH RESPECT TO COMPANY-OWNED LIFE INSURANCE.

(a) IN GENERAL.—Paragraph (4) of section 264(a) is amended—

(1) by inserting ", or any endowment or annuity contracts owned by the taxpayer covering any individual," after "the life of any individual", and

(2) by striking all that follows "carried on by the taxpayer" and inserting a period.

(b) EXCEPTION FOR CONTRACTS RELATING TO KEY PERSONS; PERMISSIBLE INTEREST RATES.—Section 264 is amended—

(1) by striking "Any" in subsection (a)(4) and inserting "Except as provided in subsection (d), any", and

(2) by adding at the end the following new subsection:

"(d) SPECIAL RULES FOR APPLICATION OF SUBSECTION (a)(4).—

"(1) EXCEPTION FOR KEY PERSONS.—Subsection (a)(4) shall not apply to any interest paid or accrued on any indebtedness with respect to policies or contracts covering an individual who is a key person to the extent that the aggregate amount of such indebtedness with respect to policies and contracts covering such individual does not exceed $50,000.

"(2) INTEREST RATE CAP ON KEY PERSONS AND PRE-1986 CONTRACTS.—

"(A) IN GENERAL.—No deduction shall be allowed by reason of paragraph (1) or the last sentence of subsection (a) with respect to interest paid or accrued for any month beginning after December 31, 1995, to the extent the amount of such interest exceeds the amount which would have been determined if the applicable rate of interest were used for such month.

"(B) APPLICABLE RATE OF INTEREST.—For purposes of subparagraph (A)—

"(i) IN GENERAL.—The applicable rate of interest for any month is the rate of interest described as Moody's Corporate Bond Yield Average-Monthly Average Corporates as published by Moody's Investors Service, Inc., or any successor thereto, for such month.

"(ii) PRE-1986 CONTRACTS.—In the case of indebtedness on a contract purchased on or before June 20, 1986—

"(I) which is a contract providing a fixed rate of interest, the applicable rate of interest for any month shall be the Moody's rate described in clause (i) for the month in which the contract was purchased, or

"(II) which is a contract providing a variable rate of interest, the applicable rate of interest for any month in an applicable period shall be such Moody's rate for the third month preceding the first month in such period.

For purposes of subclause (II), the taxpayer shall elect an applicable period for such contract on its return of tax imposed by this chapter for its first taxable year ending on or after October 13, 1995. Such

applicable period shall be for any number of months (not greater than 12) specified in the election and may not be changed by the taxpayer without the consent of the Secretary.

"(3) KEY PERSON.—For purposes of paragraph (1), the term 'key person' means an officer or 20-percent owner, except that the number of individuals who may be treated as key persons with respect to any taxpayer shall not exceed the greater of—

"(A) 5 individuals, or

"(B) the lesser of 5 percent of the total officers and employees of the taxpayer or 20 individuals.

"(4) 20-PERCENT OWNER.—For purposes of this subsection, the term '20-percent owner' means—

"(A) if the taxpayer is a corporation, any person who owns directly 20 percent or more of the outstanding stock of the corporation or stock possessing 20 percent or more of the total combined voting power of all stock of the corporation, or

"(B) if the taxpayer is not a corporation, any person who owns 20 percent or more of the capital or profits interest in the employer.

"(5) AGGREGATION RULES.—

"(A) IN GENERAL.—For purposes of paragraph (4)(A) and applying the $50,000 limitation in paragraph (1)—

"(i) all members of a controlled group shall be treated as one taxpayer, and

"(ii) such limitation shall be allocated among the members of such group in such manner as the Secretary may prescribe.

"(B) CONTROLLED GROUP.—For purposes of this paragraph, all persons treated as a single employer under subsection (a) or (b) of section 52 or subsection (m) or (o) of section 414 shall be treated as members of a controlled group.".

(c) EFFECTIVE DATES.— 26 USC 264 note.

(1) IN GENERAL.—The amendments made by this section shall apply to interest paid or accrued after October 13, 1995.

(2) TRANSITION RULE FOR EXISTING INDEBTEDNESS.—

(A) IN GENERAL.—In the case of—

(i) indebtedness incurred before January 1, 1996, or

(ii) indebtedness incurred before January 1, 1997 with respect to any contract or policy entered into in 1994 or 1995,

the amendments made by this section shall not apply to qualified interest paid or accrued on such indebtedness after October 13, 1995, and before January 1, 1999.

(B) QUALIFIED INTEREST.—For purposes of subparagraph (A), the qualified interest with respect to any indebtedness for any month is the amount of interest (otherwise deductible) which would be paid or accrued for such month on such indebtedness if—

(i) in the case of any interest paid or accrued after December 31, 1995, indebtedness with respect to no more than 20,000 insured individuals were taken into account, and

(ii) the lesser of the following rates of interest were used for such month:

(I) The rate of interest specified under the terms of the indebtedness as in effect on October 13, 1995 (and without regard to modification of such terms after such date).

(II) The applicable percentage of the rate of interest described as Moody's Corporate Bond Yield Average-Monthly Average Corporates as published by Moody's Investors Service, Inc., or any successor thereto, for such month.

For purposes of clause (i), all persons treated as a single employer under subsection (a) or (b) of section 52 of the Internal Revenue Code of 1986 or subsection (m) or (o) of section 414 of such Code shall be treated as 1 person. Subclause (II) of clause (ii) shall not apply to any month before January 1, 1996.

(C) APPLICABLE PERCENTAGE.—For purposes of subparagraph (B), the applicable percentage is as follows:

For calendar year:	The percentage is:
1996	100 percent
1997	90 percent
1998	80 percent.

(3) SPECIAL RULE FOR GRANDFATHERED CONTRACTS.—This section shall not apply to any contract purchased on or before June 20, 1986, except that section 264(d)(2) of the Internal Revenue Code of 1986 shall apply to interest paid or accrued after October 13, 1995.

26 USC 264 note.

(d) SPREAD OF INCOME INCLUSION ON SURRENDER, ETC. OF CONTRACTS.—

(1) IN GENERAL.—If any amount is received under any life insurance policy or endowment or annuity contract described in paragraph (4) of section 264(a) of the Internal Revenue Code of 1986—

(A) on the complete surrender, redemption, or maturity of such policy or contract during calendar year 1996, 1997, or 1998, or

(B) in full discharge during any such calendar year of the obligation under the policy or contract which is in the nature of a refund of the consideration paid for the policy or contract,

then (in lieu of any other inclusion in gross income) such amount shall be includible in gross income ratably over the 4-taxable year period beginning with the taxable year such amount would (but for this paragraph) be includible. The preceding sentence shall only apply to the extent the amount is includible in gross income for the taxable year in which the event described in subparagraph (A) or (B) occurs.

(2) SPECIAL RULES FOR APPLYING SECTION 264.—A contract shall not be treated as—

(A) failing to meet the requirement of section 264(c)(1) of the Internal Revenue Code of 1986, or

(B) a single premium contract under section 264(b)(1) of such Code,

solely by reason of an occurrence described in subparagraph (A) or (B) of paragraph (1) of this subsection or solely by

reason of no additional premiums being received under the contract by reason of a lapse occurring after October 13, 1995.

(3) SPECIAL RULE FOR DEFERRED ACQUISITION COSTS.—In the case of the occurrence of any event described in subparagraph (A) or (B) of paragraph (1) of this subsection with respect to any policy or contract—

(A) section 848 of the Internal Revenue Code of 1986 shall not apply to the unamortized balance (if any) of the specified policy acquisition expenses attributable to such policy or contract immediately before the insurance company's taxable year in which such event occurs, and

(B) there shall be allowed as a deduction to such company for such taxable year under chapter 1 of such Code an amount equal to such unamortized balance.

Subtitle B—Treatment of Individuals Who Lose United States Citizenship

SEC. 511. REVISION OF INCOME, ESTATE, AND GIFT TAXES ON INDIVIDUALS WHO LOSE UNITED STATES CITIZENSHIP.

(a) IN GENERAL.—Subsection (a) of section 877 is amended to read as follows:

"(a) TREATMENT OF EXPATRIATES.—

"(1) IN GENERAL.—Every nonresident alien individual who, within the 10-year period immediately preceding the close of the taxable year, lost United States citizenship, unless such loss did not have for one of its principal purposes the avoidance of taxes under this subtitle or subtitle B, shall be taxable for such taxable year in the manner provided in subsection (b) if the tax imposed pursuant to such subsection exceeds the tax which, without regard to this section, is imposed pursuant to section 871.

"(2) CERTAIN INDIVIDUALS TREATED AS HAVING TAX AVOIDANCE PURPOSE.—For purposes of paragraph (1), an individual shall be treated as having a principal purpose to avoid such taxes if—

"(A) the average annual net income tax (as defined in section 38(c)(1)) of such individual for the period of 5 taxable years ending before the date of the loss of United States citizenship is greater than $100,000, or

"(B) the net worth of the individual as of such date is $500,000 or more.

In the case of the loss of United States citizenship in any calendar year after 1996, such $100,000 and $500,000 amounts shall be increased by an amount equal to such dollar amount multiplied by the cost-of-living adjustment determined under section 1(f)(3) for such calendar year by substituting '1994' for '1992' in subparagraph (B) thereof. Any increase under the preceding sentence shall be rounded to the nearest multiple of $1,000.".

(b) EXCEPTIONS.—

(1) IN GENERAL.—Section 877 is amended by striking subsection (d), by redesignating subsection (c) as subsection (d), and by inserting after subsection (b) the following new subsection:

"(c) TAX AVOIDANCE NOT PRESUMED IN CERTAIN CASES.—

"(1) IN GENERAL.—Subsection (a)(2) shall not apply to an individual if—

"(A) such individual is described in a subparagraph of paragraph (2) of this subsection, and

"(B) within the 1-year period beginning on the date of the loss of United States citizenship, such individual submits a ruling request for the Secretary's determination as to whether such loss has for one of its principal purposes the avoidance of taxes under this subtitle or subtitle B.

"(2) INDIVIDUALS DESCRIBED.—

"(A) DUAL CITIZENSHIP, ETC.—An individual is described in this subparagraph if—

"(i) the individual became at birth a citizen of the United States and a citizen of another country and continues to be a citizen of such other country, or

"(ii) the individual becomes (not later than the close of a reasonable period after loss of United States citizenship) a citizen of the country in which—

"(I) such individual was born,

"(II) if such individual is married, such individual's spouse was born, or

"(III) either of such individual's parents were born.

"(B) LONG-TERM FOREIGN RESIDENTS.—An individual is described in this subparagraph if, for each year in the 10-year period ending on the date of loss of United States citizenship, the individual was present in the United States for 30 days or less. The rule of section 7701(b)(3)(D)(ii) shall apply for purposes of this subparagraph.

"(C) RENUNCIATION UPON REACHING AGE OF MAJORITY.—An individual is described in this subparagraph if the individual's loss of United States citizenship occurs before such individual attains age 18½.

"(D) INDIVIDUALS SPECIFIED IN REGULATIONS.—An individual is described in this subparagraph if the individual is described in a category of individuals prescribed by regulation by the Secretary.".

(2) TECHNICAL AMENDMENT.—Paragraph (1) of section 877(b) of such Code is amended by striking "subsection (c)" and inserting "subsection (d)".

(c) TREATMENT OF PROPERTY DISPOSED OF IN NONRECOGNITION TRANSACTIONS; TREATMENT OF DISTRIBUTIONS FROM CERTAIN CONTROLLED FOREIGN CORPORATIONS.—Subsection (d) of section 877, as redesignated by subsection (b), is amended to read as follows:

"(d) SPECIAL RULES FOR SOURCE, ETC.—For purposes of subsection (b)—

"(1) SOURCE RULES.—The following items of gross income shall be treated as income from sources within the United States:

"(A) SALE OF PROPERTY.—Gains on the sale or exchange of property (other than stock or debt obligations) located in the United States.

"(B) STOCK OR DEBT OBLIGATIONS.—Gains on the sale or exchange of stock issued by a domestic corporation or debt obligations of United States persons or of the United

States, a State or political subdivision thereof, or the District of Columbia.

"(C) INCOME OR GAIN DERIVED FROM CONTROLLED FOREIGN CORPORATION.—Any income or gain derived from stock in a foreign corporation but only—

"(i) if the individual losing United States citizenship owned (within the meaning of section 958(a)), or is considered as owning (by applying the ownership rules of section 958(b)), at any time during the 2-year period ending on the date of the loss of United States citizenship, more than 50 percent of—

"(I) the total combined voting power of all classes of stock entitled to vote of such corporation, or

"(II) the total value of the stock of such corporation, and

"(ii) to the extent such income or gain does not exceed the earnings and profits attributable to such stock which were earned or accumulated before the loss of citizenship and during periods that the ownership requirements of clause (i) are met.

"(2) GAIN RECOGNITION ON CERTAIN EXCHANGES.—

"(A) IN GENERAL.—In the case of any exchange of property to which this paragraph applies, notwithstanding any other provision of this title, such property shall be treated as sold for its fair market value on the date of such exchange, and any gain shall be recognized for the taxable year which includes such date.

"(B) EXCHANGES TO WHICH PARAGRAPH APPLIES.—This paragraph shall apply to any exchange during the 10-year period described in subsection (a) if—

"(i) gain would not (but for this paragraph) be recognized on such exchange in whole or in part for purposes of this subtitle,

"(ii) income derived from such property was from sources within the United States (or, if no income was so derived, would have been from such sources), and

"(iii) income derived from the property acquired in the exchange would be from sources outside the United States.

"(C) EXCEPTION.—Subparagraph (A) shall not apply if the individual enters into an agreement with the Secretary which specifies that any income or gain derived from the property acquired in the exchange (or any other property which has a basis determined in whole or part by reference to such property) during such 10-year period shall be treated as from sources within the United States. If the property transferred in the exchange is disposed of by the person acquiring such property, such agreement shall terminate and any gain which was not recognized by reason of such agreement shall be recognized as of the date of such disposition.

"(D) SECRETARY MAY EXTEND PERIOD.—To the extent provided in regulations prescribed by the Secretary, subparagraph (B) shall be applied by substituting the 15-

year period beginning 5 years before the loss of United States citizenship for the 10-year period referred to therein.

"(E) SECRETARY MAY REQUIRE RECOGNITION OF GAIN IN CERTAIN CASES.—To the extent provided in regulations prescribed by the Secretary—

"(i) the removal of appreciated tangible personal property from the United States, and

"(ii) any other occurrence which (without recognition of gain) results in a change in the source of the income or gain from property from sources within the United States to sources outside the United States,

shall be treated as an exchange to which this paragraph applies.

"(3) SUBSTANTIAL DIMINISHING OF RISKS OF OWNERSHIP.—For purposes of determining whether this section applies to any gain on the sale or exchange of any property, the running of the 10-year period described in subsection (a) shall be suspended for any period during which the individual's risk of loss with respect to the property is substantially diminished by—

"(A) the holding of a put with respect to such property (or similar property),

"(B) the holding by another person of a right to acquire the property, or

"(C) a short sale or any other transaction.

"(4) TREATMENT OF PROPERTY CONTRIBUTED TO CONTROLLED FOREIGN CORPORATIONS.—

"(A) IN GENERAL.—If—

"(i) an individual losing United States citizenship contributes property to any corporation which, at the time of the contribution, is described in subparagraph (B), and

"(ii) income derived from such property was from sources within the United States (or, if no income was so derived, would have been from such sources),

during the 10-year period referred to in subsection (a), any income or gain on such property (or any other property which has a basis determined in whole or part by reference to such property) received or accrued by the corporation shall be treated as received or accrued directly by such individual and not by such corporation. The preceding sentence shall not apply to the extent the property has been treated under subparagraph (C) as having been sold by such corporation.

"(B) CORPORATION DESCRIBED.—A corporation is described in this subparagraph with respect to an individual if, were such individual a United States citizen—

"(i) such corporation would be a controlled foreign corporation (as defined in 957), and

"(ii) such individual would be a United States shareholder (as defined in section 951(b)) with respect to such corporation.

"(C) DISPOSITION OF STOCK IN CORPORATION.—If stock in the corporation referred to in subparagraph (A) (or any other stock which has a basis determined in whole or part by reference to such stock) is disposed of during the 10-year period referred to in subsection (a) and while the

property referred to in subparagraph (A) is held by such corporation, a pro rata share of such property (determined on the basis of the value of such stock) shall be treated as sold by the corporation immediately before such disposition.

"(D) ANTI-ABUSE RULES.—The Secretary shall prescribe such regulations as may be necessary to prevent the avoidance of the purposes of this paragraph, including where—

"(i) the property is sold to the corporation, and

"(ii) the property taken into account under subparagraph (A) is sold by the corporation.

"(E) INFORMATION REPORTING.—The Secretary shall require such information reporting as is necessary to carry out the purposes of this paragraph.".

(d) CREDIT FOR FOREIGN TAXES IMPOSED ON UNITED STATES SOURCE INCOME.—

(1) Subsection (b) of section 877 is amended by adding at the end the following new sentence: "The tax imposed solely by reason of this section shall be reduced (but not below zero) by the amount of any income, war profits, and excess profits taxes (within the meaning of section 903) paid to any foreign country or possession of the United States on any income of the taxpayer on which tax is imposed solely by reason of this section."

(2) Subsection (a) of section 877, as amended by subsection (a), is amended by inserting "(after any reduction in such tax under the last sentence of such subsection)" after "such subsection".

(e) COMPARABLE ESTATE AND GIFT TAX TREATMENT.—

(1) ESTATE TAX.—

(A) IN GENERAL.—Subsection (a) of section 2107 is amended to read as follows:

"(a) TREATMENT OF EXPATRIATES.—

"(1) RATE OF TAX.—A tax computed in accordance with the table contained in section 2001 is hereby imposed on the transfer of the taxable estate, determined as provided in section 2106, of every decedent nonresident not a citizen of the United States if, within the 10-year period ending with the date of death, such decedent lost United States citizenship, unless such loss did not have for one of its principal purposes the avoidance of taxes under this subtitle or subtitle A.

"(2) CERTAIN INDIVIDUALS TREATED AS HAVING TAX AVOIDANCE PURPOSE.—

"(A) IN GENERAL.—For purposes of paragraph (1), an individual shall be treated as having a principal purpose to avoid such taxes if such individual is so treated under section 877(a)(2).

"(B) EXCEPTION.—Subparagraph (A) shall not apply to a decedent meeting the requirements of section 877(c)(1).".

(B) CREDIT FOR FOREIGN DEATH TAXES.—Subsection (c) of section 2107 is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following new paragraph:

"(2) CREDIT FOR FOREIGN DEATH TAXES.—

"(A) IN GENERAL.—The tax imposed by subsection (a) shall be credited with the amount of any estate, inherit-

ance, legacy, or succession taxes actually paid to any foreign country in respect of any property which is included in the gross estate solely by reason of subsection (b).

"(B) LIMITATION ON CREDIT.—The credit allowed by subparagraph (A) for such taxes paid to a foreign country shall not exceed the lesser of—

"(i) the amount which bears the same ratio to the amount of such taxes actually paid to such foreign country in respect of property included in the gross estate as the value of the property included in the gross estate solely by reason of subsection (b) bears to the value of all property subjected to such taxes by such foreign country, or

"(ii) such property's proportionate share of the excess of—

"(I) the tax imposed by subsection (a), over

"(II) the tax which would be imposed by section 2101 but for this section.

"(C) PROPORTIONATE SHARE.—For purposes of subparagraph (B), a property's proportionate share is the percentage of the value of the property which is included in the gross estate solely by reason of subsection (b) bears to the total value of the gross estate.".

(C) EXPANSION OF INCLUSION IN GROSS ESTATE OF STOCK OF FOREIGN CORPORATIONS.—Paragraph (2) of section 2107(b) is amended by striking "more than 50 percent of" and all that follows and inserting "more than 50 percent of—

"(A) the total combined voting power of all classes of stock entitled to vote of such corporation, or

"(B) the total value of the stock of such corporation,"

(2) GIFT TAX.—

(A) IN GENERAL.—Paragraph (3) of section 2501(a) is amended to read as follows:

"(3) EXCEPTION.—

"(A) CERTAIN INDIVIDUALS.—Paragraph (2) shall not apply in the case of a donor who, within the 10-year period ending with the date of transfer, lost United States citizenship, unless such loss did not have for one of its principal purposes the avoidance of taxes under this subtitle or subtitle A.

"(B) CERTAIN INDIVIDUALS TREATED AS HAVING TAX AVOIDANCE PURPOSE.—For purposes of subparagraph (A), an individual shall be treated as having a principal purpose to avoid such taxes if such individual is so treated under section 877(a)(2).

"(C) EXCEPTION FOR CERTAIN INDIVIDUALS.—Subparagraph (B) shall not apply to a decedent meeting the requirements of section 877(c)(1).

"(D) CREDIT FOR FOREIGN GIFT TAXES.—The tax imposed by this section solely by reason of this paragraph shall be credited with the amount of any gift tax actually paid to any foreign country in respect of any gift which is taxable under this section solely by reason of this paragraph.".

(f) COMPARABLE TREATMENT OF LAWFUL PERMANENT RESIDENTS WHO CEASE TO BE TAXED AS RESIDENTS.—

(1) IN GENERAL.—Section 877 is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) COMPARABLE TREATMENT OF LAWFUL PERMANENT RESIDENTS WHO CEASE TO BE TAXED AS RESIDENTS.—

"(1) IN GENERAL.—Any long-term resident of the United States who—

"(A) ceases to be a lawful permanent resident of the United States (within the meaning of section 7701(b)(6)), or

"(B) commences to be treated as a resident of a foreign country under the provisions of a tax treaty between the United States and the foreign country and who does not waive the benefits of such treaty applicable to residents of the foreign country,

shall be treated for purposes of this section and sections 2107, 2501, and 6039F in the same manner as if such resident were a citizen of the United States who lost United States citizenship on the date of such cessation or commencement.

"(2) LONG-TERM RESIDENT.—For purposes of this subsection, the term 'long-term resident' means any individual (other than a citizen of the United States) who is a lawful permanent resident of the United States in at least 8 taxable years during the period of 15 taxable years ending with the taxable year during which the event described in subparagraph (A) or (B) of paragraph (1) occurs. For purposes of the preceding sentence, an individual shall not be treated as a lawful permanent resident for any taxable year if such individual is treated as a resident of a foreign country for the taxable year under the provisions of a tax treaty between the United States and the foreign country and does not waive the benefits of such treaty applicable to residents of the foreign country.

"(3) SPECIAL RULES.—

"(A) EXCEPTIONS NOT TO APPLY.—Subsection (c) shall not apply to an individual who is treated as provided in paragraph (1).

"(B) STEP-UP IN BASIS.—Solely for purposes of determining any tax imposed by reason of this subsection, property which was held by the long-term resident on the date the individual first became a resident of the United States shall be treated as having a basis on such date of not less than the fair market value of such property on such date. The preceding sentence shall not apply if the individual elects not to have such sentence apply. Such an election, once made, shall be irrevocable.

"(4) AUTHORITY TO EXEMPT INDIVIDUALS.—This subsection shall not apply to an individual who is described in a category of individuals prescribed by regulation by the Secretary.

"(5) REGULATIONS.—The Secretary shall prescribe such regulations as may be appropriate to carry out this subsection, including regulations providing for the application of this subsection in cases where an alien individual becomes a resident of the United States during the 10-year period after being treated as provided in paragraph (1).".

(2) CONFORMING AMENDMENTS.—

(A) Section 2107 is amended by striking subsection (d), by redesignating subsection (e) as subsection (d), and

by inserting after subsection (d) (as so redesignated) the following new subsection:

"(e) CROSS REFERENCE.—

"For comparable treatment of long-term lawful permanent residents who ceased to be taxed as residents, see section 877(e).".

(B) Paragraph (3) of section 2501(a) (as amended by subsection (e)) is amended by adding at the end the following new subparagraph:

"(E) CROSS REFERENCE.—

"For comparable treatment of long-term lawful permanent residents who ceased to be taxed as residents, see section 877(e).".

26 USC 877 note.

(g) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to—

(A) individuals losing United States citizenship (within the meaning of section 877 of the Internal Revenue Code of 1986) on or after February 6, 1995, and

(B) long-term residents of the United States with respect to whom an event described in subparagraph (A) or (B) of section 877(e)(1) of such Code occurs on or after February 6, 1995.

(2) RULING REQUESTS.—In no event shall the 1-year period referred to in section 877(c)(1)(B) of such Code, as amended by this section, expire before the date which is 90 days after the date of the enactment of this Act.

(3) SPECIAL RULE.—

(A) IN GENERAL.—In the case of an individual who performed an act of expatriation specified in paragraph (1), (2), (3), or (4) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(1)–(4)) before February 6, 1995, but who did not, on or before such date, furnish to the United States Department of State a signed statement of voluntary relinquishment of United States nationality confirming the performance of such act, the amendments made by this section and section 512 shall apply to such individual except that the 10-year period described in section 877(a) of such Code shall not expire before the end of the 10-year period beginning on the date such statement is so furnished.

(B) EXCEPTION.—Subparagraph (A) shall not apply if the individual establishes to the satisfaction of the Secretary of the Treasury that such loss of United States citizenship occurred before February 6, 1994.

SEC. 512. INFORMATION ON INDIVIDUALS LOSING UNITED STATES CITIZENSHIP.

(a) IN GENERAL.—Subpart A of part III of subchapter A of chapter 61 is amended by inserting after section 6039E the following new section:

"SEC. 6039F. INFORMATION ON INDIVIDUALS LOSING UNITED STATES CITIZENSHIP.

"(a) IN GENERAL.—Notwithstanding any other provision of law, any individual who loses United States citizenship (within the meaning of section 877(a)) shall provide a statement which

includes the information described in subsection (b). Such statement shall be—

"(1) provided not later than the earliest date of any act referred to in subsection (c), and

"(2) provided to the person or court referred to in subsection (c) with respect to such act.

"(b) INFORMATION TO BE PROVIDED.—Information required under subsection (a) shall include—

"(1) the taxpayer's TIN,

"(2) the mailing address of such individual's principal foreign residence,

"(3) the foreign country in which such individual is residing,

"(4) the foreign country of which such individual is a citizen,

"(5) in the case of an individual having a net worth of at least the dollar amount applicable under section 877(a)(2)(B), information detailing the assets and liabilities of such individual, and

"(6) such other information as the Secretary may prescribe.

"(c) ACTS DESCRIBED.—For purposes of this section, the acts referred to in this subsection are—

"(1) the individual's renunciation of his United States nationality before a diplomatic or consular officer of the United States pursuant to paragraph (5) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(5)),

"(2) the individual's furnishing to the United States Department of State a signed statement of voluntary relinquishment of United States nationality confirming the performance of an act of expatriation specified in paragraph (1), (2), (3), or (4) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(1)–(4)),

"(3) the issuance by the United States Department of State of a certificate of loss of nationality to the individual, or

"(4) the cancellation by a court of the United States of a naturalized citizen's certificate of naturalization.

"(d) PENALTY.—Any individual failing to provide a statement required under subsection (a) shall be subject to a penalty for each year (of the 10-year period beginning on the date of loss of United States citizenship) during any portion of which such failure continues in an amount equal to the greater of—

"(1) 5 percent of the tax required to be paid under section 877 for the taxable year ending during such year, or

"(2) $1,000,

unless it is shown that such failure is due to reasonable cause and not to willful neglect.

"(e) INFORMATION TO BE PROVIDED TO SECRETARY.—Notwithstanding any other provision of law—

"(1) any Federal agency or court which collects (or is required to collect) the statement under subsection (a) shall provide to the Secretary—

"(A) a copy of any such statement, and

"(B) the name (and any other identifying information) of any individual refusing to comply with the provisions of subsection (a),

"(2) the Secretary of State shall provide to the Secretary a copy of each certificate as to the loss of American nationality under section 358 of the Immigration and Nationality Act which is approved by the Secretary of State, and

"(3) the Federal agency primarily responsible for administering the immigration laws shall provide to the Secretary the name of each lawful permanent resident of the United States (within the meaning of section 7701(b)(6)) whose status as such has been revoked or has been administratively or judicially determined to have been abandoned.

Notwithstanding any other provision of law, not later than 30 days after the close of each calendar quarter, the Secretary shall publish in the Federal Register the name of each individual losing United States citizenship (within the meaning of section 877(a)) with respect to whom the Secretary receives information under the preceding sentence during such quarter.

"(f) REPORTING BY LONG-TERM LAWFUL PERMANENT RESIDENTS WHO CEASE TO BE TAXED AS RESIDENTS.—In lieu of applying the last sentence of subsection (a), any individual who is required to provide a statement under this section by reason of section 877(e)(1) shall provide such statement with the return of tax imposed by chapter 1 for the taxable year during which the event described in such section occurs.

"(g) EXEMPTION.—The Secretary may by regulations exempt any class of individuals from the requirements of this section if he determines that applying this section to such individuals is not necessary to carry out the purposes of this section.".

(b) CLERICAL AMENDMENT.—The table of sections for such subpart A is amended by inserting after the item relating to section 6039E the following new item:

"Sec. 6039F. Information on individuals losing United States citizenship.".

26 USC 6039F note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to—

(1) individuals losing United States citizenship (within the meaning of section 877 of the Internal Revenue Code of 1986) on or after February 6, 1995, and

(2) long-term residents of the United States with respect to whom an event described in subparagraph (A) or (B) of section 877(e)(1) of such Code occurs on or after such date.

In no event shall any statement required by such amendments be due before the 90th day after the date of the enactment of this Act.

SEC. 513. REPORT ON TAX COMPLIANCE BY UNITED STATES CITIZENS AND RESIDENTS LIVING ABROAD.

Not later than 90 days after the date of the enactment of this Act, the Secretary of the Treasury shall prepare and submit to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate a report—

(1) describing the compliance with subtitle A of the Internal Revenue Code of 1986 by citizens and lawful permanent residents of the United States (within the meaning of section 7701(b)(6) of such Code) residing outside the United States, and

(2) recommending measures to improve such compliance (including improved coordination between executive branch agencies).

Subtitle C—Repeal of Financial Institution Transition Rule to Interest Allocation Rules

SEC. 521. REPEAL OF FINANCIAL INSTITUTION TRANSITION RULE TO INTEREST ALLOCATION RULES.

(a) IN GENERAL.—Paragraph (5) of section 1215(c) of the Tax Reform Act of 1986 (Public Law 99–514, 100 Stat. 2548) is hereby repealed. 26 USC 864 note.

(b) EFFECTIVE DATE.— 26 USC 864 note.

(1) IN GENERAL.—The amendment made by this section shall apply to taxable years beginning after December 31, 1995.

(2) SPECIAL RULE.—In the case of the first taxable year beginning after December 31, 1995, the pre-effective date portion of the interest expense of the corporation referred to in such paragraph (5) of such section 1215(c) for such taxable year shall be allocated and apportioned without regard to such amendment. For purposes of the preceding sentence, the pre-effective date portion is the amount which bears the same ratio to the interest expense for such taxable year as the number of days during such taxable year before the date of the enactment of this Act bears to 366.

Approved August 21, 1996.

Public Law 104–193
104th Congress, H.R. 3734[1]
August 22, 1996

An Act to provide for reconciliation pursuant to section 201(a)(1) of the concurrent resolution on the budget for fiscal year 1997.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Personal Responsibility and Work Opportunity Reconciliation Act of 1996".

* * * * *

TITLE I—BLOCK GRANTS FOR TEMPORARY ASSISTANCE FOR NEEDY FAMILIES

* * * * *

SEC. 110. CONFORMING AMENDMENTS TO OTHER LAWS.

* * * * *

(l) The Internal Revenue Code of 1986 (26 U.S.C. 1 et seq.) is amended—

(1) in section 51(d)(9) (26 U.S.C. 51(d)(9)), by striking all that follows "agency as" and inserting "being eligible for financial assistance under part A of title IV of the Social Security Act and as having continually received such financial assistance during the 90-day period which immediately precedes the date on which such individual is hired by the employer.";

(2) in section 3304(a)(16) (26 U.S.C. 3304(a)(16)), by striking "eligibility for aid or services," and all that follows through "children approved" and inserting "eligibility for assistance, or the amount of such assistance, under a State program funded";

(3) in section 6103(l)(7)(D)(i) (26 U.S.C. 6103(l)(7)(D)(i)), by striking "aid to families with dependent children provided under a State plan approved" and inserting "a State program funded";

(4) in section 6103(l)(10) (26 U.S.C. 6103(l)(10))—

(A) by striking "(c) or (d)" each place it appears and inserting "(c), (d), or (e)"; and

(B) by adding at the end of subparagraph (B) the following new sentence: "Any return information disclosed with respect to section 6402(e) shall only be disclosed to officers and employees of the State agency requesting such information.";

(5) in section 6103(p)(4) (26 U.S.C. 6103(p)(4)), in the matter preceding subparagraph (A)—

(A) by striking "(5), (10)" and inserting "(5)"; and

(B) by striking "(9), or (12)" and inserting "(9), (10), or (12)";

(6) in section 6334(a)(11)(A) (26 U.S.C. 6334(a)(11)(A)), by striking "(relating to aid to families with dependent children)";

(7) in section 6402 (26 U.S.C. 6402)—

(A) in subsection (a), by striking "(c) and (d)" and inserting "(c), (d), and (e)";

(B) by redesignating subsections (e) through (i) as subsections (f) through (j), respectively; and

(C) by inserting after subsection (d) the following:

"(e) COLLECTION OF OVERPAYMENTS UNDER TITLE IV–A OF THE SOCIAL SECURITY ACT.—The amount of any overpayment to be refunded to the person making the overpayment shall be reduced (after reductions pursuant to subsections (c) and (d), but before a credit against future liability for an internal revenue tax) in accordance with section 405(e) of the Social Security Act (concering recovery of overpayments to individuals under State plans approved under part A of title IV of such Act).";

and

(8) in section 7523(b)(3)(C) (26 U.S.C. 7523(b)(3)(C)), by striking "aid to families with dependent children" and inserting "assistance under a State program funded under part A of title IV of the Social Security Act".

(m) Section 3(b) of the Wagner-Peyser Act (29 U.S.C. 49b(b)) is amended by striking "State plan approved under part A of title IV" and inserting "State program funded under part A of title IV".

* * * * *

TITLE III—CHILD SUPPORT

* * * * *

Subtitle B—Locate and Case Tracking

* * * * *

SEC. 316. EXPANSION OF THE FEDERAL PARENT LOCATOR SERVICE.

* * * * *

(g) CONFORMING AMENDMENTS.—

* * * * *

(2) TO FEDERAL UNEMPLOYMENT TAX ACT.—Section 3304(a)(16) of the Internal Revenue Code of 1986 is amended—

(A) by striking "Secretary of Health, Education, and Welfare" each place such term appears and inserting "Secretary of Health and Human Services";

(B) in subparagraph (B), by striking "such information" and all that follows and inserting "information furnished under subparagraph (A) or (B) is used only for the purposes authorized under such subparagraph;";

(C) by striking "and" at the end of subparagraph (A);

(D) by redesignating subparagraph (B) as subparagraph (C); and

E) by inserting after subparagraph (A) the following new subparagraph:

"(B) wage and unemployment compensation information contained in the records of such agency shall be furnished to the Secretary of Health and Human Services (in accordance with regulations promulgated by such Secretary) as necessary for the purposes of the National Directory of New Hires established under section 453(i) of the Social Security Act, and".

* * * * *

(4) DISCLOSURE OF CERTAIN INFORMATION TO AGENTS OF CHILD SUPPORT ENFORCEMENT AGENCIES.—

(A) IN GENERAL.—Paragraph (6) of section 6103(l) of the Internal Revenue Code of 1986 (relating to disclosure of return information to Federal, State, and local child support enforcement agencies) is amended by redesignating subparagraph (B) as subparagraph (C) and by inserting

[1]This publication of the law is restricted to excerpts involving tax matters.

after subparagraph (A) the following new subparagraph:

"(B) DISCLOSURE TO CERTAIN AGENTS.—The following information disclosed to any child support enforcement agency under subparagraph (A) with respect to any individual with respect to whom child support obligations are sought to be established or enforced may be disclosed by such agency to any agent of such agency which is under contract with such agency to carry out the purposes described in subparagraph (C):

"(i) The address and social security account number (or numbers) of such individual.

"(ii) The amount of any reduction under section 6402(c) (relating to offset of past-due support against overpayments) in any overpayment otherwise payable to such individual.".

(B) CONFORMING AMENDMENTS.—

(i) Paragraph (3) of section 6103(a) of such Code is amended by striking "(l)(12)" and inserting "paragraph (6) or (12) of subsection (l)".

(ii) Subparagraph (C) of section 6103(l)(6) of such Code, as redesignated by subsection (a), is amended to read as follows:

"(C) RESTRICTION ON DISCLOSURE.—Information may be disclosed under this paragraph only for purposes of, and to the extent necessary in, establishing and collecting child support obligations from, and locating, individuals owing such obligations.".

(iii) The material following subparagraph (F) of section 6103(p)(4) of such Code is amended by striking "subsection (l)(12)(B)" and inserting "paragraph (6)(A or (12)(B) of subsection (l)".

* * * * *

Subtitle G—Enforcement of Support Orders

SEC. 361. INTERNAL REVENUE SERVICE COLLECTION OF ARREARAGES.

(a) COLLECTION OF FEES.—Section 6305(a) of the Internal Revenue Code of 1986 (relating to collection of certain liability) is amended—

(1) by striking "and" at the end of paragraph (3);

(2) by striking the period at the end of paragraph (4) and inserting ", and";

(3) by adding at the end the following new paragraph:

"(5) no additional fee may be assessed for adjustments to an amount previously certified pursuant to such section 452(b) with respect to the same obligor."; and

(4) by striking "Secretary of Health, Education, and Welfare" each place it appears and inserting "Secretary of Health and Human Services".

(b) EFFECTIVE DATE.—The amendments made by this section shall become effective October 1, 1997.

* * * * *

TITLE IV—RESTRICTING WELFARE AND PUBLIC BENEFITS FOR ALIENS

* * * * *

Subtitle F—Earned Income Credit Denied to Unauthorized Employees

SEC. 451. EARNED INCOME CREDIT DENIED TO INDIVIDUALS NOT AUTHORIZED TO BE EMPLOYED IN THE UNITED STATES.

IN GENERAL.—Section 32(c)(1) of the Internal Revenue Code of 1986 (relating to individuals eligible to claim the earned income credit) is amended by adding at the end the following new subparagraph:

"(F) IDENTIFICATION NUMBER REQUIREMENT.—The term 'eligible individual' does not include any individual who does not include on the return of tax for the taxable year—

"(i) such individual's taxpayer identification number, and

"(ii) if the individual is married (within the meaning of section 7703), the taxpayer identification number of such individual's spouse.".

(b) SPECIAL IDENTIFICATION NUMBER.—Section 32 of such Code is amended by adding at the end the following new subsection:

"(l) IDENTIFICATION NUMBERS.—Solely for purposes of subsections (c)(1)(F) and (c)(3)(D), a taxpayer identification number means a social security number issued to an individual by the Social Security Administration (other than a social security number issued pursant to clause (II) (or that portion of clause (III) that relates to clause (II)) of section 205(c)(2)(B)(i) of the Social Security Act).".

(c) EXTENSION OF PROCEDURES APPLICABLE TO MATHEMATICAL OR CLERICAL ERRORS.—Section 6213(g)(2) of such Code (relating to the definition of mathematical or clerical errors) is amended by striking "and" at the end of subparagraph (D), by striking the period at the end of subparagraph (E) and inserting a comma, and by inserting after subparagraph (E) the following new subparagraphs:

"(F) an omission of a correct taxpayer identification number required under section 32 (relating to the earned income credit) to be included on a return, and

"(G) an entry on a return claiming the credit under section 32 with respect to net earnings from self-employment described in section 32(c)(2)(A) to the extent the tax imposed by section 1401 (relating to self-employment tax) on such net earnings has not been paid.".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to returns the due date for which (without regard to extensions) is more than 30 days after the date of the enactment of this Act.

* * * * *

TITLE IX—MISCELLANEOUS

* * * * *

SEC. 909. RULES RELATING TO DENIAL OF EARNED INCOME CREDIT ON BASIS OF DISQUALIFIED INCOME.

(a) REDUCTION IN DISQUALIFIED INCOME THRESHOLD.—

(1) IN GENERAL.—Paragraph (1) of section 32(i) of the Internal Revenue Code of 1986 (relating to denial of credit for individuals having excessive investment income) is amended by striking "$2,350" and inserting "$2,200".

(2) ADJUSTMENT FOR INFLATION.—Subsection (j) of section 32 of such Code is amended to read as follows:

"(j) INFLATION ADJUSTMENTS.—

"(1) IN GENERAL.—In the case of any taxable year beginning after 1996, each of the dolar amounts in subsections (b)(2) and (i)(1) shall be increased by an amount equal to—

"(A) such dollar amount, multiplied by

"(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting 'calendar year 1995' for 'calendar year 1992' in subparagraph (B) thereof.

"(2) ROUNDING.—

"(A) IN GENERAL.—If any dollar amount in subsection (b)(2), after being increased under paragraph (1), is not a multiple of $10, such dollar amount shall be rounded to the nearest multiple of $10.

"(B) DISQUALIFIED INCOME THRESHOLD AMOUNT.—If the dollar amount in subsection (i)(1), after being increased under paragraph (1), is not a multiple of $50, such amount shall be rounded to the next lowest multiple of $50.".

(3) CONFORMING AMENDMENT.—Paragraph (2) of section 32(b) of such Code is amended to read as follows:

"(2) AMOUNTS.—The earned income amount and the phase-out amount shall be determined as follows:

In the case of an eligible individual with:	The earned income amount is:	The phaseout amount is:
1 qualifying child	$6,330	$11,610
2 or more qualifying children	$8,890	$11,610
No qualifying children	$4,220	$ 5,280".

(b) DEFINITION OF DISQUALIFIED INCOME.—Paragraph (2) of section 32(i) of such Code (defining disqualified income) is amended by striking "and" at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting a comma, and by adding at the end the following new subparagraphs:

"(D) the capital gain net income (as defined in section 1222) of the taxpayer for such taxable year, and

"(E) the excess (if any) of—

"(i) the aggregate income from all passive activities for the taxable year (determined without regard to any amount included in earned income under subsection (c)(2) or described in a preceding subparagraph), over

"(ii) the aggregate losses from all passive activities for the taxable year (as so determined).

For purposes of subparagraph (E), the term 'passive activity' has the meaning given such term by section 469.".

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1995.

(2) ADVANCE PAYMENT INDIVIDUALS.—In the case of any individual who on or before June 26, 1996, has in effect an earned income eligibility certificate for the individual's taxable year beginning in 1996, the amendments made by this section shall apply to taxable years beginning after December 31, 1996.

SEC. 910. MODIFICATION OF ADJUSTED GROSS INCOME DEFINITION FOR EARNED INCOME CREDIT.

(a) IN GENERAL.—Subsections (a)(2)(B), (c)(1)(C), and (f)(2)(B) of section 32 of the Internal Revenue Code of 1986 are each amended by striking "adjusted gross income" each place it appears and isnerting "modified adjusted gross income".

(b) MODIFIED ADJUSTED GROSS INCOME DEFINED.—Section 32(c) of such Code (relating to definitions and special rules) is amended by adding at the end the following new paragraph:

"(5) MODIFIED ADJUSTED GROSS INCOME.—

"(A) IN GENERAL.—The term 'modified adjusted gross income' means adjusted gross income determined without regard to the amounts described in subparagraph (B).

"(B) CERTAIN AMOUNTS DISREGARDED.—An amount is described in this subparagraph if it is—

"(i) the amount of losses from sales or exchanges of capital assets in excess of gains from such sales or exchanges to the extent such amount does not exceed the amount under section 1211(b)(1),

"(ii) the net loss from estates and trusts,

"(iii) the excess (if any) of amounts described in subsection (i)(2)(C)(ii) over the amounts described in subsection (i)(2)(C)(i) (relating to nonbusiness rents and royalties), and

"(iv) 50 percent of the net loss from the carrying on of trades or businesses, computed separately with respect to—

"(I) trades or businesses (other than farming) conducted as sole proprietorships,

"(II) trades or businesses of farming conducted as sole proprietorships, and

"(III) other trades or businesses.

For purposes of clause (iv), there shall not be taken into account items which are attributable to a trade or business which consists of the performance of services by the taxpayer as an employee.".

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1995.

(2) ADVANCE PAYMENT INDIVIDUALS.—In the case of any individual who on or before June 26, 1996, has in effect an earned income eligibility certificate for the individual's taxable year beginning in 1996, the amendments made by this section shall apply to taxable years beginning after December 31, 1996.

* * * * *

Approved August 22, 1996.

Conference Report No. 104-725[1]
2nd Session
[Bracketed numerals indicate official report page numbers]

PERSONAL RESPONSIBILITY AND WORK OPPORTUNITY RECONCILIATION ACT OF 1996

August 1, 1996

Mr. KASICH, from the committee of conference, submitted the following conference report to accompany H.R. 3734

* * * * *

TITLE I—BLOCK GRANTS FOR TEMPORARY ASSISTANCE FOR NEEDY FAMILIES

* * * * *

[319] 99. CONFORMING AMENDMENTS TO OTHER LAWS

Present Law

No provision.

House bill

This section makes a series of amendments that conform provisions of the proposal to the Unemployment Compensation Amendments of 1976, the Omnibus Budget Reconciliation Act of 1987, the Housing and Urban-Rural Recovery Act of 1983, the Tax Equity and Fiscal Responsibility Act of 1982, the Social Security Amendments of 1967, the Stewart B. McKinney Homeless Assistance Amendments Act of 1988, the Higher Education Act of 1965, the Carl D. Perkins Vocational and Applied Technology Education Act, the Elementary and Secondary Education Act of 1965, Public Law 99-88, the Internal Revenue Code of 1986, the Wagner-Peyser Act, the Job Training Partnership Act, the Low-Income Home Energy Assistance Act of 1981, the Family Support Act of 1988, the Balanced Budget and Emergency Deficit Control Act of 1985, the Immigration and Nationality Act, the Head Start Act, and the School-to-Work Opportunities Act of 1994.

Senate anendment

Same.

Conference agreement

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

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TITLE III—CHILD SUPPORT ENFORCEMENT

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[1]This publication of the Conference Report is restricted to excerpts involving tax matters. Public Law 104-193, page 4, this Bulletin.

[347] 11. EXPANSION OF THE FEDERAL PARENT LOCATOR SERVICE

Present law

The law requires that the Federal Parent Locator Service (FPLS) be used to obtain and transmit information about the location of any absent parent when that information is to be used for the purpose of enforcing child support. Federal law also requires departments or agencies of the United States to be reimbursed for costs incurred in providing requested information to the FPLS.

Information Comparisons and Other Disclosures. Upon request, the Secretary must provide to an "authorized person" (i.e., an employee or attorney of a child support agency, a court with jurisdiction over the parties involved, the custodial parent, the legal guardian, or the child's attorney) the most recent address and place of employment of any nonresident parent if the information is contained in the records of the Department of Health and Human Services or can be obtained from any other department or agency of the United States or of any State. The FPLS also can be used in connection with the enforcement or determination of child custody, visitation, and parental kidnapping. Federal law requires the Secretary of Labor and the Secretary of Health and Human Services to enter into an agreement to give the FPLS prompt access to wage and unemployment compensation claims information useful in locating a noncustodial parent or his employer.

Fees. "Authorized persons" who request information from FPLS must be charged a fee.

Restriction on Disclosure and Use. Federal law stipulates that no information shall be disclosed if the disclosure would contravene the national policy or security interests of the United States or the confidentiality of Census data.

Quarterly Wage Reporting. The Secretary of Labor must provide prompt access by the Secretary of HHS to wage and unemployment compensation claims information and data maintained by the Labor Department or State employment security agencies.

House bill

The purposes of the Federal Parent Locator Service are expanded. For the purposes of establishing parentage, establishing support orders or modifying them, or enforcing support orders, the Federal Parent Locator Service will provide information to locate individuals who owe child support or against whom an obligation is sought or to whom such an obligation is owed. Information in the FPLS includes Social Security number, address, name and address of employer, wages and employee benefits (including information about health care coverage), and information about assets and debts. The provision also clarifies the statute so that parents with orders providing child custody or visitation rights are given access to information from the FPLS unless the State has notified the Secretary that there is reasonable evidence of domestic violence or child abuse or that the information could be harmful to the custodial parent or child.

The Secretary is authorized to set reasonable rates for reimbursing Federal and State agencies for the costs of providing information to the FPLS and to set reimbursement rates that State and Federal agencies that use information from the FPLS must pay to the Secretary.

Federal Case Registry of Child Support Orders. Establishes within the FPLS an automated registry known as the Federal Case Registry of Child Support Orders. The Federal Case Registry contains abstracts of child support orders and other information specified by the Secretary (such as names, Social Security numbers or other uniform identification numbers, and State case identification numbers) to identify individuals who owe or are owed support, or for or against whom support is sought to be established, and the State which has the case. States must begin reporting this information in accord with regulations issued by the Secretary by October 1, 1998.

National Directory of New Hires. This provision establishes within the FPLS a National Directory of New Hires containing information supplied by State Directories of New Hires. When fully implemented, the Federal Directory of New Hires will contain identifying information on virtually every person who is hired in the United States. In addition, the FPLS will contain quarterly data supplied by the State Directory of New Hires on wages and Unemployment Compensation paid. The Secretary of the Treasury must have access to information in the Federal Directory of New Hires for the purpose of administering section 32 of the Internal Revenue Code and the Earned Income Credit. The information for the National Directory of New Hires must be entered within 2 days of receipt, and requires the Secretary to maintain within the National Directory of New Hires a

list of multistate employers that choose to send their report to one State and the name of the State so elected. The Secretary must establish a National Directory of New Hires by October 1, 1997.

Information Comparisons and Other Disclosures. The Secretary must verify the accuracy of the name, Social Security number, birth date, and employer identification number of individuals in the Federal Parent Locator Service with the Social Security Administration. The Secretary is required to match data in the National Directory of New Hires against the child support order abstracts in the Federal Case Registry at least every 2 working days and to report information obtained from matches to the State child support agency responsible for the case within 2 days. The information is to be used for purposes of locating individuals to establish paternity, and to establish, modify, or enforce child support orders. The Secretary may also compare information across all components of the FPLS to the extent and with the frequency that the Secretary determines will be effective. The Secretary will share information from the FPLS with several potential users including State agencies administering the Temporary Assistance for Needy Families program, the Commissioner of Social Security (to determine the accuracy of Social Security and Supplemental Security Income), and researchers under some circumstances.

Fees. The Secretary must reimburse the Commissioner of Social Security for costs incurred in performing verification of Social Security information and States for submitting information on New Hires. States or Federal agencies that use information from FPLS must pay fees established by the Secretary.

Restriction on Disclosure and Use. Information from the FPLS cannot be used for purposes other than those provided in this section, subject to section 6103 of the Internal Revenue Code (confidentiality and disclosure of returns and return information).

Information Integrity and Security. The Secretary must establish and use safeguards to ensure the accuracy and completeness of information from the FPLS and restrict access to confidential information in the FPLS to authorized persons and purposes.

Federal Government Reporting. Each department of the U.S. must submit the name, Social Security number, and wages paid the employee on a quarterly basis to the FPLS. Quarterly wage reporting must not be filed for a Federal or State employee performing intelligence or counter-intelligence functions if it is determined that filing such a report could endanger the employee or compromise an ongoing investigation.

Conforming Amendments. This section makes several conforming amendments to Titles III and IV of the Social Security Act, to the Federal Unemployment Tax Act, and to the Internal Revenue Code. Among the more important are that: State employment security agencies are required to report quarterly wage information to the Secretary of HHS or suffer financial penalties and that private agencies working under contract to State child support agencies can have access to certain specified information from IRS records under some circumstances.

Requirement for Cooperation. The Secretaries of HHS and Labor must work together to develop cost-effective and efficient methods of accessing information in the various directories required by this title; they must also consider the need to ensure the proper and authorized use of wage record information.

Senate amendment

Same, except under "Information Comparisons and Other Disclosures" the Senate amendment drops the requirement that the Social Security Administration must determine the accuracy of payments under the Social Security and SSI programs.

Conference agreement

The conference agreement follows the House bill and the Senate amendment with the modification that the agreement follows the Senate provision dropping the requirement that the Social Security Administration determine the accuracy of Social Security and SSI payments.

* * * * *

[366] Subtitle G—Enforcement of Support Orders

31. INTERNAL REVENUE SERVICE COLLECTION OF ARREARAGES

Present law

If the amount of overdue child support is at least $750, the Internal Revenue Service (IRS) can enforce the child support obligation through its regular collection process, which may include seizure of property, freezing accounts, or use of other procedures if child support agencies request assistance according to prescribed rules (e.g., certifying that the delinquency is at least $750, etc.)

House bill

The Internal Revenue Code is amended so that no additional fees can be assessed for adjustment to previously certified amounts for the same obligor.

Senate amendment

Same.

Conference agreement

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

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TITLE IV—RESTRICTING WELFARE AND PUBLIC BENEFITS FOR ALIENS

[392] Subtitle F—Earned Income Credit Denied to Unauthorized Employees

17. EARNED INCOME CREDIT DENIED TO INDIVIDUALS NOT AUTHORIZED TO BE EMPLOYED IN THE UNITED STATES

[NOTE.—For further description of this and additional earned income credit provisions, see Title IX: Miscellaneous, page 9.]

Present law

Certain eligible low-income workers are entitled to claim a refundable credit of up to $3,556 in 1996 on their income tax return. The amount of the credit an eligible individual may claim depends upon whether the individual has one, more than one, or no qualifying children and is determined by multiplying the credit rate by the taxpayer's earned income up to an earned income amount. The maximum amount of the credit is the product of the credit rate and the earned income amount. For taxpayers with earned income (or adjusted gross income (AGI), if greater) in excess of the beginning of the phaseout range, the maximum credit amount is reduced by the phaseout rate multiplied by the amount of earned income (or AGI, if greater) in excess of the beginning of the phaseout range. For taxpayers with earned income (or AGI, if greater) in excess of the end of the phaseout range, no credit is allowed.

In order to claim the credit, an individual must either have a qualifying child or meet other requirements. A qualifying child must meet a relationship test, an age test, an identification test, and a residence test. In order to claim the credit without a qualifying

child, an individual must not be a dependent and must be over age 24 and under age 65.

To satisfy the identification test, individuals must include on their tax return the name and age of each qualifying child. For returns filed with respect to tax year 1996, individuals must provide a taxpayer identification number (TIN) for all qualifying children born on or before November 30, 1996. For returns filed with respect to tax year 1997 and all subsequent years, individuals must provide TINs for all qualifying children, regardless of their age. An individual's TIN is generally that individual's social security number.

The Internal Revenue Service may summarily assess additional tax due as a result of a mathematical or clerical error without sending the taxpayer a notice of deficiency and giving the taxpayer an opportunity to petition the Tax Court. Where the IRS uses the summary assessment procedure for mathematical or clerical errors, the taxpayer must be given an explanation of the asserted error and a period of 60 days to request that the IRS abate its assessment. The IRS may not proceed to collect the amount of the assessment until the taxpayer has agreed to it or has allowed the 60-day period for objecting to expire. If the taxpayer files a request for abatement of the assessment specified in the notice, the IRS must abate the assessment. Any reassessment of the abated amount is subject to the ordinary deficiency procedures. The request for abatement of the assessment is the only procedure a taxpayer may use prior to paying the assessed amount in order to contest an assessment arising out of a mathematical or clerical error. Once the assessment is satisfied, however, the taxpayer may file a claim for refund if he or she believes the assessment was made in error.

House bill

Individuals are not eligible for the credit if they do not include their taxpayer identification number (and, if married, their spouse's taxpayer identification number) on their tax return. Solely for these purposes and for purposes of the present-law identification test for a qualifying child, a taxpayer identification number is defined as a social security number issued to an individual by the Social Security Administration other than a number issued under section 205(c)(2)(B)(i)(II) (or that portion of sec. 205(c)(2)(B)(i)(III) relating to it) of the Social Security Act (regarding the issuance of a number to an individual applying for or receiving Federally funded benefits).

If an individual fails to provide a correct taxpayer identification number, such omission will be treated as a mathematical or clerical error. If an individual who claims the credit with respect to net earnings from self-employment fails to pay the proper amount of self-employment tax on such net earnings, the failure will be treated as a mathematical or clerical error for purposes of the amount of credit allowed.

Senate amendment

Similar to House bill.

Conference agreement

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

* * * * *

TITLE IX—MISCELLANEOUS

[494] 10. EARNED INCOME CREDIT PROVISIONS

A. Deny earned income credit to individuals not authorized to be employed in the United States

[NOTE.—For additional discussion of this provision, refer to Title IV: Restricting Welfare and Public Benefits for Aliens, page 8.]

Present law

In general. Certain eligible low-income workers are entitled to claim a refundable credit on their income tax return. The amount of the credit an eligible individual may claim depends upon whether the individual has one, more than one, or no qualifying children and is determined by multiplying the credit rate by the individual's[1] earned income up to an earned income amount. The maximum amount of the credit is the product of the credit rate and the earned income amount. For individuals with earned income (or adjusted gross income (AGI), if greater) in excess of the beginning of the phaseout range, the maximum credit amount is reduced by the phaseout rate multiplied by the amount of earned income (or AGI, if greater) in excess of the beginning of the phaseout range. For individuals with earned income (or AGI, if greater) in excess of the end of the phaseout range, no credit is allowed.

The parameters for the credit depend upon the number of qualifying children the individual claims. For 1996, the parameters are given in the following table:

[1]In the case of a married individual who files a joint return with his or her spouse, the income for purposes of these tests is the combined income of the couple.

	Two or more children	One qualifying child	No qualifying children
Credit rate (percent)	40.00	34.00	7.65
Earned income amount	$8,890	$6,330	$4,220
Maximum credit	$3,556	$2,152	$323
Phaseout begins	$11,610	$11,610	$5,280
Phaseout rate (percent)	21.06	15.98	7.65
Phaseout ends	$28,495	$25,078	$9,500

For years after 1996, the credit rates and the phaseout rates will be the same as in the preceding table. The earned income amount and the beginning of the phaseout range are indexed for inflation; because the end of the phaseout range depends on those amounts as well as the phaseout rate and the credit rate, the end of the phaseout range will also increase if there is inflation.

In order to claim the credit, an individual must either have a qualifying child or meet other requirements. A qualifying child must meet a relationship test, an age test, an identification

test, and a residence test. In order to claim the credit without a qualifying child, an individual must be over age 24 and under age 65.

To satisfy the identification test, individuals must include on their tax return the name and age of each qualifying child. For returns filed with respect to tax year 1996, individuals must provide a taxpayer identification number (TIN) for all qualifying children born on or before November 30, 1996. For returns filed with respect to tax year 1997 and all subsequent years, individuals must provide TINs for all qualifying children, regardless of their age. An individuals TIN is generally that individual's social security number.

An individual with qualifying children may elect to receive a portion of the credit on an advance basis by furnishing an advance payment certificate to his or her employer. For such an individual, the employer makes an advance payment of the credit at the time wages are paid. The amount of advance payment allowable in a taxable year is limited to 60 percent of the maximum credit available to an individual with one qualifying child.

Mathematical or clerical errors. The Internal Revenue Service may summarily assess additional tax due as a result of a mathematical or clerical error without sending the taxpayer a notice of deficiency and giving the taxpayer an opportunity to petition the Tax Court. Where the IRS uses the summary assessment procedure for mathematical or clerical errors, the taxpayer must be given an explanation of the asserted error and a period of 60 days to request that the IRS abate its assessment. The IRS may not proceed to collect the amount of the assessment until the taxpayer has agreed to it or has allowed the 60-day period for objecting to expire. If the taxpayer files a request for abatement of the assessment specified in the notice, the IRS must abate the assessment. Any reassessment of the abated amount is subject to the ordinary deficiency procedures. The request for abatement of the assessment is the only procedure a taxpayer may use prior to paying the assessed amount in order to contest an assessment arising out of a mathematical or clerical error. Once the assessment is satisfied, however, the taxpayer may file a claim for refund if he or she believes the assessment was made in error.

House bill

Individuals are not eligible for the credit if they do not include their taxpayer identification number (and, if married, their spouse's taxpayer identification number) on their tax return. Solely for these purposes and for purposes of the present-law identification test for a qualifying child, a taxpayer identification number is defined as a social security number issued to an individual by the Social Security Administration other than a number issued under section 205(c)(2)(B)(i)(II) (or that portion of sec. 205(c)(2)(B)(i)(III) relating to it) of the Social Security Act (regarding the issuance of a number to an individual applying for or receiving Federally funded benefits).

If an individual fails to provide a correct taxpayer identification number, such omission will be treated as a mathematical or clerical error. If an individual who claims the credit with respect to net earnings from self-employment fails to pay the proper amount of self-employment tax on such net earnings, the failure will be treated as a mathematical or clerical error for purposes of the amount of credit allowed.

Effective date. The provision is effective for taxable years beginning after December 31, 1995.

Senate amendment

The provision in the Senate amendment is identical to that in the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment with a modification to the effective date. The conference agreement is effective with respect to returns the due date for which (without regard to extensions) is more than 30 days after the date of enactment of this Act.

B. Change disqualified income test for earned income credit

Present law

For taxable years beginning after December 31, 1995, an individual is not eligible for the earned income credit if the aggregate amount of "disqualified income" of the taxpayer for the taxable year exceeds $2,350. This threshold is not indexed. Disqualified income is the sum of:

(1) interest (taxable and tax-exempt),

(2) dividends, and

(3) net rent and royalty income (if greater than zero).

House bill

No provision.

Senate amendment

For purposes of the disqualified income test for the earned income credit, the following items are added to the definition of disqualified income: capital gain net income and net passive income (if greater than zero) that is not self-employment income.

The threshold above which an individual is not eligible for the credit is reduced from $2,350 to $2,200, and the threshold is indexed for inflation after 1996.

Effective date. The provision generally is effective for taxable years beginning after December 31, 1995. For individuals who, as of June 26, 1996, had made an election to receive the current-year credit on an advance basis, the provision is effective for taxable years beginning after December 31, 1996.

Conference agreement

The conference agreement follows the Senate amendment.

C. Modify definition of adjusted gross income used for phasing out the earned income credit

Present law

For taxpayers with earned income (or AGI, if greater) in excess of the beginning of the phaseout range, the maximum earned income credit amount is reduced by the phaseout rate multiplied by the amount of earned income (or AGI, if greater) in excess of the beginning of the phaseout range. For taxpayers with earned income (or AGI, if greater) in excess of the end of the phaseout range, no credit is allowed.

House bill

No provision.

Senate amendment

The provision modifies the definition of AGI used for phasing out the earned income credit by including certain nontaxable income and by disregarding certain losses. The nontaxable items included are:

(1) tax-exempt interest, and

(2) nontaxable distributions from pensions, annuities, and individual retirement arrangements (but only if not rolled over into similar vehicles during the applicable rollover period).

The losses disregarded are:

(1) net capital losses (if greater than zero),

(2) net losses from trusts and estates,

(3) net losses from nonbusiness rents and royalties, and

(4) net losses from businesses, computed separately with respect to sole proprietorships (other than in farming), sole proprietorships in farming, and other businesses.

For purposes of item (4), above, amounts attributable to a business that consists of the performance of services by the taxpayer as an employee are not taken into account.

Effective date. The provision generally is effective for taxable years beginning after December 31, 1995. For individuals who, as of June 26, 1996, had made an election to receive the current-year credit on an advance basis, the provision is effective for taxable years beginning after December 31, 1996.

Conference agreement

The conference agreement modifies the definition of AGI used for phasing out the earned income credit by disregarding certain losses. The losses disregarded are:

(1) net capital losses (if greater than zero),

(2) net losses from trusts and estates,

(3) net losses from nonbusiness rents and royalties, and

(4) 50 percent of the net losses from businesses, computed separately with respect to sole proprietorships (other than in farming), sole proprietorships in farming, and other businesses.

For purposes of item (4), above, amounts attributable to a business that consists of the performance of services by the taxpayer as an employee are not taken into account.

Effective date. Same as the Senate amendment provision.

D. Suspend inflation adjustments for earned income credit for individuals with no qualifying children

Present law

To claim the earned income credit, an individual must either have a qualifying child or meet other requirements. In order to claim a credit without a qualifying child, an individual must not be a dependent and must be over age 24 and under age 65.

The earned income amount and the beginning of the phaseout range are indexed for inflation; because the end of the phaseout range depends on these amounts as well as the phaseout rate and the credit rate, the end of the phaseout range will also increase if there is inflation.

House bill

No provision.

Senate amendment

In the case of individuals with no qualifying children there will be no adjustment for inflation after 1996 to the earned income amount or the beginning of the phaseout range.

Effective date. The provision is effective for taxable years beginning after December 31, 1996.

Conference agreement

The conference agreement follows the House bill (no provision).