

105TH CONGRESS
1ST SESSION

H. R. 228

To amend the Internal Revenue Code of 1986 to allow penalty-free withdrawals from IRAs for certain purposes, to increase the amount of tax deductible IRA contributions, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

JANUARY 7, 1997

Mr. McCOLLUM introduced the following bill; which was referred to the
Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to allow penalty-free withdrawals from IRAs for certain purposes, to increase the amount of tax deductible IRA contributions, and for other purposes.

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

3 **SECTION 1. PENALTY-FREE DISTRIBUTIONS FROM IRAS**
4 **AND EXCLUSION FROM INCOME OF CERTAIN**
5 **IRA DISTRIBUTIONS WHICH ARE REPAID.**

6 (a) PENALTY-FREE DISTRIBUTIONS.—

7 (1) IN GENERAL.—Paragraph (2) of section
8 72(t) of the Internal Revenue Code of 1986 (relating

to exceptions to 10-percent additional tax on early distributions from qualified retirement plans) is amended by adding at the end the following new subparagraph:

“(E) DISTRIBUTIONS FROM CERTAIN PLANS FOR FIRST HOME PURCHASES, HIGHER EDUCATION EXPENSES, AND QUALIFIED LONG TERM CARE EXPENSES.—Distributions to an individual from an individual retirement plan—

“(i) which are qualified first-time homebuyer distributions,

“(ii) to the extent such distributions do not exceed the qualified higher education expenses of the taxpayer for the taxable year, or

“(iii) to the extent such distributions do not exceed the expenses paid by the taxpayer during the taxable year for qualified long-term care services (as defined in section 7702B(c)).”

(2) DEFINITIONS.—Section 72(t) of such Code is amended by adding at the end the following new paragraphs:

“(7) QUALIFIED FIRST-TIME HOMEBUYER DISTRIBUTIONS.—

1 “(A) IN GENERAL.—For purposes of para-
2 graph (2)(E)(i), the term ‘qualified first-time
3 homebuyer distribution’ means any payment or
4 distribution received by an individual to the ex-
5 tent such payment or distribution is used by the
6 individual before the close of the 60th day after
7 the day on which such payment or distribution
8 is received to pay qualified acquisition costs
9 with respect to a principal residence for such
10 individual as a first-time homebuyer.

11 “(B) QUALIFIED ACQUISITION COSTS.—
12 For purposes of this paragraph, the term
13 ‘qualified acquisition costs’ means the costs of
14 acquiring, constructing, or reconstructing a res-
15 idence. Such term includes any usual or reason-
16 able settlement, financing, or other closing
17 costs.

18 “(C) FIRST-TIME HOMEBUYER; OTHER
19 DEFINITIONS.—For purposes of this para-
20 graph—

21 “(i) FIRST-TIME HOMEBUYER.—The
22 term ‘first-time homebuyer’ means any in-
23 dividual if such individual (and, if married,
24 such individual’s spouse) had no present
25 ownership interest in a principal residence

1 during the 3-year period ending on the
2 date of acquisition of the principal resi-
3 dence to which this paragraph applies.

4 “(ii) PRINCIPAL RESIDENCE.—The
5 term ‘principal residence’ has the same
6 meaning as when used in section 1034.

7 “(iii) DATE OF ACQUISITION.—The
8 term ‘date of acquisition’ means the date—

9 “(I) on which a binding contract
10 to acquire the principal residence to
11 which subparagraph (A) applies is en-
12 tered into, or

13 “(II) on which a binding contract
14 to construct or reconstruct such a
15 principal residence is entered into.

16 “(D) SPECIAL RULE WHERE DELAY IN AC-
17 QUISITION.—If any payment or distribution
18 fails to meet the requirements of subparagraph
19 (A) solely by reason of a delay or cancellation
20 of the purchase, construction, or reconstruction
21 of the residence, the amount of the payment or
22 distribution may be contributed to an individual
23 retirement account as provided in subsection

1 (d)(3)(A)(i) of section 408 (determined by sub-
2 stituting ‘120th day’ for ‘60th day’ in such sub-
3 section), except that—

4 “(i) subsection (d)(3)(B) of such sec-
5 tion shall not be applied to such contribu-
6 tion, and

7 “(ii) such amount shall not be taken
8 into account in applying subsection
9 (d)(3)(B) to any other amount.

10 “(8) QUALIFIED HIGHER EDUCATION EX-
11 PENSES.—For purposes of paragraph (2)(E)(ii)—

12 “(A) IN GENERAL.—The term ‘qualified
13 higher education expenses’ means tuition, fees,
14 books, supplies, and equipment required for the
15 enrollment or attendance of—

16 “(i) the taxpayer,

17 “(ii) the taxpayer’s spouse, or

18 “(iii) the taxpayer’s dependent (as de-
19 fined in section 152),

20 at an eligible educational institution (as defined
21 in section 135(c)(3)).

22 “(B) COORDINATION WITH SAVINGS BOND
23 PROVISIONS.—The amount of qualified higher
24 education expenses for any taxable year shall be

1 reduced by any amount excludable from gross
 2 income under section 135.”

3 (3) EXPANDED PENALTY-FREE WITHDRAWALS
 4 FOR UNEMPLOYED.—

5 (A) IN GENERAL.—Clause (i) of section
 6 72(t)(2)(D) of such Code is amended by insert-
 7 ing “and” at the end of subclause (I), by strik-
 8 ing “, and” at the end of subclause (II) and in-
 9 serting a period, and by striking subclause
 10 (III).

11 (B) CONFORMING AMENDMENT.—The
 12 heading for subparagraph (D) of section
 13 72(t)(2) of such Code is amended by striking
 14 “FOR HEALTH INSURANCE PREMIUMS”.

15 (4) CONFORMING AMENDMENT.—Subparagraph
 16 (B) of section 72(t)(2) of such Code is amended by
 17 striking “or (D)” and inserting “, (D), or (E)”.

18 (b) IRA DISTRIBUTIONS TO PAY FINANCIALLY DEV-
 19 ASTATING MEDICAL EXPENSES OF CERTAIN LINEAL DE-
 20 SCENDANTS AND ANCESTORS.—Subparagraph (B) of sec-
 21 tion 72(t)(2) of such Code is amended by striking “medi-
 22 cal care” and all that follows and inserting “medical care
 23 determined—

1 “(i) without regard to whether the
2 employee itemizes deductions for such tax-
3 able year, and

4 “(ii) in the case of an individual re-
5 tirement plan, by treating such employee’s
6 dependents as including—

7 “(I) all children and grand-
8 children of the employee or such em-
9 ployee’s spouse, and

10 “(II) all ancestors of the em-
11 ployee or such employee’s spouse.”

12 (c) EXCLUSION FROM INCOME OF CERTAIN DIS-
13 TRIBUTIONS WHICH ARE REPAYED.—Section 408 of the In-
14 ternal Revenue Code of 1986 (relating to individual retire-
15 ment accounts) is amended by redesignating subsection
16 (q) as subsection (r) and by inserting after subsection (p)
17 the following new subsection:

18 “(q) REPAYABLE DISTRIBUTIONS FROM INDIVIDUAL
19 RETIREMENT ACCOUNTS FOR FIRST HOME PURCHASES,
20 HIGHER EDUCATION EXPENSES, QUALIFIED LONG TERM
21 CARE EXPENSES, QUALIFIED UNEMPLOYMENT DIS-
22 TRIBUTIONS, AND FINANCIALLY DEVASTATING MEDICAL
23 EXPENSES.—

1 “(1) IN GENERAL.—Notwithstanding any other
2 provision of this section, gross income shall not in-
3 clude any qualified distribution.

4 “(2) REPAYMENT REQUIREMENT.—

5 “(A) ADDITION TO TAX.—If the required
6 recontributions made by the taxpayer during
7 the repayment period are less than the qualified
8 distribution, the tax imposed by this chapter for
9 the last taxable year in the repayment period
10 shall be increased by the amount determined
11 under subparagraph (B).

12 “(B) DETERMINATION OF AMOUNT.—The
13 amount determined under this subparagraph
14 shall be an amount which bears the same ratio
15 to the tax benefit amount as—

16 “(i) the excess (if any) of the qualified
17 distribution over required recontributions
18 made during the repayment period, bears
19 to

20 “(ii) the qualified distribution.

21 “(C) REPAYMENT PERIOD.—For purposes
22 of this subsection, the term ‘repayment period’
23 means, with respect to any qualified distribu-
24 tion, the 5-taxable year period beginning after

1 the taxable year in which such distribution is
2 received.

3 “(D) TAX BENEFIT AMOUNT.—For pur-
4 poses of this subsection, the term ‘tax benefit
5 amount’ means, with respect to any qualified
6 distribution, the sum of—

7 “(i) the aggregate reduction in the tax
8 imposed by this chapter for the taxable
9 year in which such distribution is received
10 by reason of the exclusion under paragraph
11 (1), and

12 “(ii) interest on the amount of such
13 reduction for the repayment period com-
14 puted at the Federal mid-term rate (within
15 the meaning of section 1274(d)(1)) and
16 compounded annually.

17 “(3) QUALIFIED DISTRIBUTION.—For purposes
18 of this subsection, the term ‘qualified distribution’
19 means any distribution described in subparagraph
20 (B), (D) or (E) of section 72(d)(2) to an individual
21 from an individual retirement plan maintained for
22 the benefit of such individual.

23 “(4) RECONTRIBUTION OF QUALIFIED DIS-
24 TRIBUTIONS.—

1 “(A) IN GENERAL.—If an individual re-
2 ceived a qualified distribution, such individual
3 shall make required recontributions in the man-
4 ner provided in this paragraph to an individual
5 retirement plan maintained for the benefit of
6 such individual.

7 “(B) METHOD OF MAKING RECONTRIBU-
8 TION.—Any required recontribution—

9 “(i) shall be made during the repay-
10 ment period for the qualified distribution,

11 “(ii) shall not exceed the qualified dis-
12 tribution reduced by any prior recontribu-
13 tion under this paragraph with respect to
14 such distribution, and

15 “(iii) shall be made by making a pay-
16 ment in cash to an individual retirement
17 plan for the benefit of such individual.

18 An individual making a required recontribution
19 under this paragraph shall designate (in the
20 manner prescribed by the Secretary) such con-
21 tribution as a required recontribution under
22 this paragraph and shall specify the qualified
23 distribution with respect to which such recon-
24 tribution is being made.

1 “(C) TREATMENT AS ROLLOVER CON-
 2 TRIBUTION.—For purposes of this title, any re-
 3 quired recontribution under this paragraph
 4 shall be treated as a rollover contribution de-
 5 scribed in subsection (d)(3).

6 “(7) OTHER SPECIAL RULES.—

7 “(A) BASIS RULES NOT AFFECTED.—The
 8 tax treatment under this chapter of any dis-
 9 tribution (other than a qualified distribution)
 10 shall be determined as if this subsection had
 11 not been enacted.

12 “(B) AGGREGATION RULE.—For purposes
 13 of this subsection, all qualified distributions re-
 14 ceived by an individual during a taxable year
 15 shall be treated as a single distribution.”

16 (d) EFFECTIVE DATE.—The amendments made by
 17 this section shall apply to distributions received in taxable
 18 years beginning after December 31, 1997.

19 **SEC. 2. INCREASE IN AMOUNT OF DEDUCTIBLE IRA CON-**
 20 **TRIBUTIONS AND INDEXING FOR INFLATION.**

21 (a) INCREASE IN MAXIMUM AMOUNT OF DEDUC-
 22 TION.—Subparagraph (A) of section 219(b)(1) of the In-
 23 ternal Revenue Code of 1986 (relating to maximum
 24 amount of deduction) is amended by striking “\$2,000”
 25 and inserting “\$4,500”.

1 (b) INFLATION ADJUSTMENTS.—Subsection (f) of
 2 section 219 of such Code is amended by adding at the
 3 end the following new paragraph:

4 “(8) INFLATION ADJUSTMENTS.—In the case of
 5 a taxable year beginning in a calendar year after
 6 1998, each dollar amount set forth in subsections
 7 (b)(1)(A) and (g)(3)(B) shall be increased by an
 8 amount equal to—

9 “(A) such dollar amount, multiplied by

10 “(B) the cost-of-living adjustment deter-
 11 mined under section 1(f)(3) for such calendar
 12 year by substituting ‘calendar year 1997’ for
 13 ‘calendar year 1992’ in subparagraph (B)
 14 thereof.

15 If any increase determined under the preceding sen-
 16 tence is not a multiple of \$100, such increase shall
 17 be rounded to the nearest multiple of \$100.”

18 (c) CONFORMING AMENDMENTS.—

19 (1) Subsections (a)(1) and (b)(2)(B) of section
 20 408 of such Code are each amended by striking
 21 “\$2,000” and inserting “the dollar limitation in ef-
 22 fect under section 219(b)(1)(A)”.

1 (2) Subsection (j) of section 408 of such Code
 2 is amended by striking “the \$2,000 amounts con-
 3 tained” and inserting “the dollar limitations referred
 4 to”.

5 (d) EFFECTIVE DATE.—The amendments made by
 6 this section shall apply to taxable years beginning after
 7 December 31, 1997.

8 **SEC. 3. ELIMINATION OF PHASE-OUT FOR INDIVIDUALS**
 9 **NOT ACTIVE PARTICIPANTS IN DEFINED CON-**
 10 **TRIBUTION PLANS AND INCREASE OF IN-**
 11 **COME LIMITS FOR OTHERS.**

12 (a) ELIMINATION OF PHASE-OUT FOR INDIVIDUALS
 13 NOT ACTIVE PARTICIPANTS IN DEFINED CONTRIBUTION
 14 PLAN.—Paragraph (5) of section 219(g) of the Internal
 15 Revenue Code of 1986 (relating to active participant) is
 16 amended by striking the period at the end of subpara-
 17 graph (B) and inserting a comma, and by inserting after
 18 subparagraph (B) the following:

19 “if such plan, contract, pension, or trust is a defined
 20 contribution plan (as defined in section 414(i)).”

21 (b) INCREASE IN INCOME PHASEOUT LEVELS.—

22 (1) IN GENERAL.—Subparagraph (B) of section
 23 219(g)(3) of such Code (relating to applicable dollar
 24 amount) is amended—

1 (A) by striking “\$40,000” and inserting
 2 “\$120,000”, and

3 (B) by striking “\$25,000” and inserting
 4 “\$75,000”.

5 (2) CROSS REFERENCE TO INFLATION ADJUST-
 6 MENT.—Paragraph (3) of section 219(g) of such
 7 Code is amended by adding at the end the following
 8 new subparagraph:

9 “(C) CROSS REFERENCE.—

“For inflation adjustment of dollar amounts set
 forth in subparagraph (B), see subsection (f)(8).”

10 (c) EFFECTIVE DATE.—The amendments made by
 11 this section shall apply to taxable years beginning after
 12 December 31, 1997.

13 **SEC. 4. WITHHOLDING, CONTRIBUTION LIMITS, AND**
 14 **MATCHING CONTRIBUTION NONDISCRIMINA-**
 15 **TION REQUIREMENTS FOR 401(k) PLANS.**

16 (a) INAPPLICABILITY OF WITHHOLDING REQUIRE-
 17 MENT TO 401(k) DISTRIBUTIONS.—

18 (1) IN GENERAL.—Paragraph (3) of section
 19 3405(c) of the Internal Revenue Code of 1986 (re-
 20 lating to eligible rollover distribution) is amended by
 21 striking the period at the end and inserting the fol-
 22 lowing: “, except that such term shall not include a
 23 distribution from a qualified cash or deferred ar-
 24 rangement (as defined in section 401(k)).”

1 (2) EFFECTIVE DATE.—The amendment made
2 by this subsection shall apply to distributions made
3 after December 31, 1997.

4 (b) INCREASE IN CONTRIBUTION LIMITS FOR 401(k)
5 PLANS.—

6 (1) IN GENERAL.—Paragraph (1) of section
7 402(g) of such Code (relating to limitation on exclu-
8 sion for elective deferrals) is amended by striking
9 “\$7,000” and inserting “\$20,000”.

10 (2) CONFORMING AMENDMENT.—Paragraph (5)
11 of section 402(g) of such Code (relating to cost-of-
12 living adjustment) is amended by striking “\$7,000”
13 and inserting “\$20,000” and by inserting before the
14 period “and the base period taken into account shall
15 be the calendar quarter beginning October 1, 1997”.

16 (3) EFFECTIVE DATE.—The amendments made
17 by this subsection shall apply to taxable years begin-
18 ning after December 31, 1997.

19 (c) ALTERNATIVE METHODS FOR MEETING SECTION
20 401(k) NONDISCRIMINATION TEST AND NONDISCRIMINA-
21 TION TEST FOR MATCHING CONTRIBUTIONS.—

22 (1) SECTION 401(k) NONDISCRIMINATION
23 TEST.—Subsection (k) of section 401 of such Code
24 (relating to cash or deferred arrangements) is

1 amended by adding at the end the following new
2 paragraph:

3 “(13) ADDITIONAL ALTERNATIVE METHOD OF
4 MEETING NONDISCRIMINATION REQUIREMENTS.—

5 “(A) IN GENERAL.—A cash or deferred ar-
6 rangement shall be treated as meeting the re-
7 quirements of paragraph (3)(A)(ii) if—

8 “(i) under the arrangement, the em-
9 ployer makes matching contributions on
10 behalf of each employee in an amount
11 equal to a percentage of the contributions
12 and elective deferrals of such employee,

13 “(ii) the same such percentage applies
14 to all employees of the employer, and

15 “(iii) not less than biannually, each
16 employee eligible to participate under the
17 arrangement is given written notice of the
18 employee’s rights and obligations under the
19 arrangement which meets the requirements
20 of clauses (i) and (ii) of paragraph
21 (12)(D).

22 “(B) SPECIAL RULES REGARDING IN-
23 CREASE AND DECREASE IN MATCHING CON-
24 TRIBUTIONS.—

1 “(i) INCREASE IN RATE OF MATCHING
 2 CONTRIBUTIONS.—An arrangement shall
 3 not be treated as meeting the requirement
 4 of subparagraph (A)(ii) if the rate of the
 5 employer’s matching contributions in-
 6 creases as the rate of an employee’s con-
 7 tributions or elective deferrals increases.

8 “(ii) PERMISSIBLE DECREASE AS
 9 ELECTIVE DEFERRALS AND CONTRIBU-
 10 TIONS INCREASE.—An arrangement shall
 11 not fail to be treated as meeting the re-
 12 quirement of subparagraph (A)(ii) by rea-
 13 son of a decrease in the rate of the employ-
 14 er’s matching contributions as the rate of
 15 the employee’s contributions or elective de-
 16 ferrals increases, if the same such rate of
 17 decrease applies to all employees of the
 18 employer.”

19 (2) NONDISCRIMINATION TEST FOR MATCHING
 20 CONTRIBUTIONS.—Subsection (m) of section 401 of
 21 such Code is amended by redesignating paragraph
 22 (12) as paragraph (13) and by inserting after para-
 23 graph (11) the following new paragraph:

24 “(12) ADDITIONAL ALTERNATIVE METHOD FOR
 25 CASH OR DEFERRED ARRANGEMENTS.—A qualified

1 cash or deferred arrangement (as defined in sub-
 2 section (k)) shall be treated as meeting the require-
 3 ments of paragraph (2) with respect to matching
 4 contributions if the arrangement meets the require-
 5 ments of subsection (k)(13).”

6 (3) EFFECTIVE DATE.—The amendments made
 7 by this section shall apply to years beginning after
 8 December 31, 1997.

9 **SEC. 5. INHERITED IRAS AND INHERITED 401(k) AMOUNTS.**

10 (a) EXCLUSION OF INHERITED IRAS AND CERTAIN
 11 INHERITED 401(k) AMOUNTS FROM GROSS ESTATE.—

12 (1) IN GENERAL.—Section 2039 of the Internal
 13 Revenue Code of 1986 is amended by adding at the
 14 end the following new subsection:

15 “(c) EXCLUSION OF INDIVIDUAL RETIREMENT AC-
 16 COUNTS AND CERTAIN INHERITED 401(k) AMOUNTS.—
 17 Notwithstanding any other provision of this section or of
 18 any other provision of law, there shall be excluded from
 19 the value of the gross estate any amount receivable by any
 20 beneficiary (other than the executor) under—

21 “(1) an individual retirement plan of the dece-
 22 dent, or

23 “(2) a qualified cash or deferred arrangement
 24 (as defined in section 401(k)) of the decedent, if the

1 requirements of section 408(o)(2)(B)(iii) are met
2 with respect to such amount.”

3 (2) EFFECTIVE DATE.—The amendment made
4 by paragraph (1) shall apply to estates of decedents
5 dying after December 31, 1997.

6 (b) BENEFICIARY PERMITTED TO HOLD IRA RE-
7 CEIVED FROM DECEDENT.—

8 (1) IN GENERAL.—Subparagraph (B) of section
9 401(a)(9) of such Code (relating to required dis-
10 tributions) is amended by adding at the end the fol-
11 lowing new clause:

12 “(v) EXCEPTION FOR DESIGNATED
13 BENEFICIARY OF INDIVIDUAL RETIREMENT
14 PLAN.—Notwithstanding clauses (iii) and
15 (iv), if any portion of the interest in an in-
16 dividual retirement plan is payable to (or
17 for the benefit of) a designated beneficiary
18 by reason of the death of another individ-
19 ual, the date on which distributions from
20 such plan are required to begin under this
21 paragraph shall be determined by applying
22 this paragraph as if such beneficiary were
23 the employee.”

1 (2) CONFORMING AMENDMENT.—Paragraph (3)
 2 of section 408(d) of such Code is amended by strik-
 3 ing subparagraph (C) (relating to denial of rollover
 4 treatment for inherited accounts, etc.).

5 (3) EFFECTIVE DATE.—The amendments made
 6 by this subsection shall apply to amounts payable
 7 after, and acquisitions after, December 31, 1997.

8 (c) CONTRIBUTION OF INHERITED 401(k) AMOUNTS
 9 TO IRA; EXCLUSION FROM GROSS INCOME FOR SUCH
 10 AMOUNTS.—

11 (1) IN GENERAL.—Subparagraph (B) of section
 12 408(o)(2) of such Code (relating to nondeductible
 13 limit) is amended by adding at the end the following
 14 new clause:

15 “(iii) INHERITED 401(k) AMOUNTS.—
 16 If, by reason of the death of an employee,
 17 an individual receives an amount attrib-
 18 utable to an elective deferral described in
 19 section 402(g)(3)(A) of such employee—

20 “(I) such individual’s nondeduct-
 21 ible limit for the taxable year in which
 22 such amount is received shall be in-
 23 creased by the portion of such amount
 24 which is paid (not later than the 60th
 25 day after the date of such receipt)

1 into an individual retirement plan for
2 the benefit of such individual, and
3 “(II) such portion shall not be
4 includible in the gross income of such
5 individual.”

6 (2) CONFORMING AMENDMENT.—Paragraph (1)
7 of section 4973(b) of such Code (relating to excess
8 contributions) is amended by striking “408(d)(3))”
9 and inserting “408(d)(3)) and other than amounts
10 excluded from gross income under section
11 408(o)(2)(B)(iii)”.

12 (3) EFFECTIVE DATE.—The amendments made
13 by this subsection shall apply to amounts received
14 after December 31, 1997.

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