

105TH CONGRESS  
1ST SESSION

# S. 2

To amend the Internal Revenue Code of 1986 to provide tax relief for American families, and for other purposes.

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## IN THE SENATE OF THE UNITED STATES

JANUARY 21, 1997

Mr. ROTH (for himself, Mr. LOTT, Mr. ABRAHAM, Mr. ALLARD, Mr. ASHCROFT, Mr. BROWNBACK, Mr. CRAIG, Mr. D'AMATO, Mr. DEWINE, Mr. DOMENICI, Mr. ENZI, Mr. FAIRCLOTH, Mr. GORTON, Mr. GRAMS, Mr. HAGEL, Mr. HATCH, Mr. HELMS, Mrs. HUTCHISON, Mr. KYL, Mr. MURKOWSKI, Mr. NICKLES, Mr. ROBERTS, Mr. SANTORUM, Mr. SESSIONS, Mr. SMITH of New Hampshire, Mr. SMITH of Oregon, Mr. THOMAS, Mr. THURMOND, Mr. WARNER, Mr. COVERDELL, Mr. COATS, and Mr. KEMPTHORNE) introduced the following bill; which was read twice and referred to the Committee on Finance

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## A BILL

To amend the Internal Revenue Code of 1986 to provide tax relief for American families, 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. SHORT TITLE; AMENDMENT OF 1986 CODE;**

4 **TABLE OF CONTENTS.**

5 (a) SHORT TITLE.—This Act may be cited as the  
6 “American Family Tax Relief Act”.

1 (b) AMENDMENT OF 1986 CODE.—Except as other-  
 2 wise expressly provided, whenever in this Act an amend-  
 3 ment or repeal is expressed in terms of an amendment  
 4 to, or repeal of, a section or other provision, the reference  
 5 shall be considered to be made to a section or other provi-  
 6 sion of the Internal Revenue Code of 1986.

7 (c) TABLE OF CONTENTS.—The table of contents is  
 8 as follows:

Sec. 1. Short title; amendment of 1986 Code; table of contents.

#### TITLE I—CHILD TAX CREDIT

Sec. 101. Child tax credit.

#### TITLE II—CAPITAL GAINS REFORM

##### Subtitle A—Taxpayers Other Than Corporations

Sec. 201. Capital gains deduction.

Sec. 202. Indexing of certain assets acquired after December 31, 1996, for pur-  
 poses of determining gain.

Sec. 203. Modifications to exclusion of gain on certain small business stock.

##### Subtitle B—Corporate Capital Gains

Sec. 211. Reduction of alternative capital gain tax for corporations.

##### Subtitle C—Capital Loss Deduction Allowed With Respect to Sale or Exchange of Principal Residence

Sec. 221. Capital loss deduction allowed with respect to sale or exchange of  
 principal residence.

#### TITLE III—ESTATE AND GIFT PROVISIONS

Sec. 301. Increase in unified estate and gift tax credit.

Sec. 302. Family-owned business exclusion.

Sec. 303. 20-year installment payment where estate consists largely of interest  
 in closely held business.

Sec. 304. No interest on certain portion of estate tax extended under 6166.

#### TITLE IV—SAVINGS INCENTIVES

Sec. 401. Restoration of IRA deduction.

Sec. 402. IRA allowed for spouses who are not active plan participants.

Sec. 403. Establishment of nondeductible tax-free individual retirement ac-  
 counts.

Sec. 404. Tax-free withdrawals from individual retirement plans for business  
 startups.

Sec. 405. Tax-free withdrawals from individual retirement plans for long-term unemployed.

Sec. 406. Distributions from certain plans may be used without penalty to pay higher education expenses.

# 1       **TITLE I—CHILD TAX CREDIT**

## 2       **SEC. 101. CHILD TAX CREDIT.**

3       (a) IN GENERAL.—Subpart A of part IV of sub-  
4 chapter A of chapter 1 (relating to nonrefundable personal  
5 credits) is amended by inserting after section 23 the fol-  
6 lowing new section:

### 7       **“SEC. 24. CHILD TAX CREDIT.**

8       “(a) ALLOWANCE OF CREDIT.—There shall be al-  
9 lowed as a credit against the tax imposed by this chapter  
10 for the taxable year an amount equal to \$500 multiplied  
11 by the number of qualifying children of the taxpayer.

12       “(b) LIMITATION.—

13               “(1) IN GENERAL.—The amount of the credit  
14 which would (but for this subsection) be allowed by  
15 subsection (a) shall be reduced (but not below zero)  
16 by \$25 for each \$1,000 (or fraction thereof) by  
17 which the taxpayer’s adjusted gross income exceeds  
18 the threshold amount.

19               “(2) THRESHOLD AMOUNT.—For purposes of  
20 paragraph (1), the term ‘threshold amount’ means—

21                       “(A) \$110,000 in the case of a joint re-  
22                       turn,

1           “(B) \$75,000 in the case of an individual  
2           who is not married, and

3           “(C) \$55,000 in the case of a married in-  
4           dividual filing a separate return.

5           For purposes of this paragraph, marital status shall  
6           be determined under section 7703.

7           “(c) QUALIFYING CHILD.—For purposes of this sec-  
8           tion—

9           “(1) IN GENERAL.—The term ‘qualifying child’  
10          means any individual if—

11           “(A) the taxpayer is allowed a deduction  
12           under section 151 with respect to such individ-  
13           ual for such taxable year,

14           “(B) such individual has not attained the  
15           age of 18 as of the close of the calendar year  
16           in which the taxable year of the taxpayer be-  
17           gins, and

18           “(C) such individual bears a relationship to  
19           the taxpayer described in section 32(c)(3)(B)  
20           (determined without regard to clause (ii) there-  
21           of).

22           “(2) EXCEPTION FOR CERTAIN NONCITIZENS.—  
23           The term ‘qualifying child’ shall not include any in-  
24           dividual who would not be a dependent if the first  
25           sentence of section 152(b)(3) were applied without

1 regard to all that follows ‘resident of the United  
2 States’.

3 “(d) TAXABLE YEAR MUST BE FULL TAXABLE  
4 YEAR.—Except in the case of a taxable year closed by rea-  
5 son of the death of the taxpayer, no credit shall be allow-  
6 able under this section in the case of a taxable year cover-  
7 ing a period of less than 12 months.”

8 (b) CONFORMING AMENDMENT.—The table of sec-  
9 tions for subpart A of part IV of subchapter A of chapter  
10 1 is amended by inserting after the item relating to section  
11 23 the following new item:

“Sec. 24. Child tax credit.”

12 (c) EFFECTIVE DATE.—The amendments made by  
13 this section shall apply to taxable years beginning after  
14 December 31, 1996.

15 **TITLE II—CAPITAL GAINS**  
16 **REFORM**  
17 **Subtitle A—Taxpayers Other Than**  
18 **Corporations**

19 **SEC. 201. CAPITAL GAINS DEDUCTION.**

20 (a) IN GENERAL.—Part I of subchapter P of chapter  
21 1 (relating to treatment of capital gains) is amended by  
22 redesignating section 1202 as section 1203 and by insert-  
23 ing after section 1201 the following new section:

1 **“SEC. 1202. CAPITAL GAINS DEDUCTION.**

2       “(a) GENERAL RULE.—If for any taxable year a tax-  
3 payer other than a corporation has a net capital gain, 50  
4 percent of such gain shall be a deduction from gross in-  
5 come.

6       “(b) ESTATES AND TRUSTS.—In the case of an es-  
7 tate or trust, the deduction shall be computed by excluding  
8 the portion (if any) of the gains for the taxable year from  
9 sales or exchanges of capital assets which, under sections  
10 652 and 662 (relating to inclusions of amounts in gross  
11 income of beneficiaries of trusts), is includible by the in-  
12 come beneficiaries as gain derived from the sale or ex-  
13 change of capital assets.

14       “(c) COORDINATION WITH TREATMENT OF CAPITAL  
15 GAIN UNDER LIMITATION ON INVESTMENT INTEREST.—  
16 For purposes of this section, the net capital gain for any  
17 taxable year shall be reduced (but not below zero) by the  
18 amount which the taxpayer takes into account as invest-  
19 ment income under section 163(d)(4)(B)(iii).

20       “(d) ADJUSTMENTS TO NET CAPITAL GAIN.—For  
21 purposes of subsection (a)—

22               “(1) COLLECTIBLES.—

23                       “(A) IN GENERAL.—Net capital gain shall  
24 be computed without regard to collectibles gain.

25                       “(B) COLLECTIBLES GAIN.—

“(i) IN GENERAL.—The term ‘collectibles gain’ means gain from the sale or exchange of a collectible (as defined in section 408(m) without regard to paragraph (3) thereof) which is a capital asset held for more than 1 year but only to the extent such gain is taken into account in computing gross income.

“(ii) COORDINATION WITH SECTION 1022.—Gain from the disposition of a collectible which is an indexed asset to which section 1022(a) applies shall be disregarded for purposes of this section. A taxpayer may elect to treat any collectible specified in such election as not being an indexed asset for purposes of section 1022. Any such election (and specification) once made, shall be irrevocable.

“(iii) PARTNERSHIPS, ETC.—For purposes of clause (i), any gain from the sale of an interest in a partnership, S corporation, or trust which is attributable to unrealized appreciation in the value of collectibles shall be treated as gain from the sale or exchange of a collectible. Rules similar

1 to the rules of section 751 shall apply for  
 2 purposes of the preceding sentence.

3 “(2) GAIN FROM SMALL BUSINESS STOCK.—Net  
 4 capital gain shall be computed without regard to any  
 5 gain from the sale or exchange of any qualified small  
 6 business stock (within the meaning of section  
 7 1203(b)) held more than 5 years which is taken into  
 8 account in computing gross income.

9 “(3) PRE-1997 GAIN.—

10 “(A) IN GENERAL.—In the case of a tax-  
 11 able year which includes January 1, 1997, net  
 12 capital gain shall be computed without regard  
 13 to pre-1997 gain.

14 “(B) PRE-1997 GAIN.—The term ‘pre-1997  
 15 gain’ means the amount which would be net  
 16 capital gain under subsection (a) for a taxable  
 17 year if such net capital gain were determined by  
 18 taking into account only gain or loss properly  
 19 taken into account for the portion of the tax-  
 20 able year before January 1, 1997.

21 “(C) SPECIAL RULES FOR PASS-THRU EN-  
 22 TITIES.—

23 “(i) IN GENERAL.—In applying sub-  
 24 paragraph (A) with respect to any pass-  
 25 thru entity, the determination of when



1 gains and losses are properly taken into  
 2 account shall be made at the entity level.

3 “(ii) PASS-THRU ENTITY DEFINED.—

4 For purposes of clause (i), the term ‘pass-  
 5 thru entity’ means—

6 “(I) a regulated investment com-  
 7 pany,

8 “(II) a real estate investment  
 9 trust,

10 “(III) an S corporation,

11 “(IV) a partnership,

12 “(V) an estate or trust, and

13 “(VI) a common trust fund.

14 “(e) MAXIMUM RATE ON NONDEDUCTIBLE CAPITAL  
 15 GAIN.—

16 “(1) IN GENERAL.—If a taxpayer other than a  
 17 corporation has a nondeductible net capital gain for  
 18 any taxable year, then the tax imposed by section 1  
 19 for the taxable year shall not exceed the sum of—

20 “(A) a tax computed on the taxable income  
 21 reduced by the amount of the nondeductible net  
 22 capital gain, at the same rates and in the same  
 23 manner as if this subsection had not been en-  
 24 acted, plus

1                   “(B) a tax of 28 percent of the nondeduct-  
2                   ible net capital gain.

3                   “(2) NONDEDUCTIBLE NET CAPITAL GAIN.—  
4                   For purposes of paragraph (1), the term ‘nondeduct-  
5                   ible net capital gain’ means an amount equal to the  
6                   amount of the reduction in net capital gain under  
7                   subsection (a) by reason of subsection (d).”

8                   (b) DEDUCTION ALLOWABLE IN COMPUTING AD-  
9 JUSTED GROSS INCOME.—Subsection (a) of section 62 is  
10 amended by inserting after paragraph (16) the following  
11 new paragraph:

12                   “(17) LONG-TERM CAPITAL GAINS.—The de-  
13                   duction allowed by section 1202.”

14                   (c) TECHNICAL AND CONFORMING CHANGES.—

15                   (1)(A) Section 1 is amended by striking sub-  
16                   section (h).

17                   (B)(i) Section 641(d)(2)(A) is amended by  
18                   striking “Except as provided in section 1(h), the”  
19                   and inserting “The”.

20                   (ii) Section 641(d)(2)(C) is amended by insert-  
21                   ing after clause (iii) the following new clause:

22                   “(iv) The deduction under section  
23                   1202.”

1           (2) Paragraph (1) of section 170(e) is amended  
2       by striking “the amount of gain” in the material fol-  
3       lowing subparagraph (B)(ii) and inserting “50 per-  
4       cent (80 percent in the case of a corporation) of the  
5       amount of gain”.

6           (3) Subparagraph (B) of section 172(d)(2) is  
7       amended to read as follows:

8                 “(B) the deduction under section 1202  
9       shall not be allowed.”

10          (4) The last sentence of section 453A(c)(3) is  
11       amended by striking all that follows “long-term cap-  
12       ital gain,” and inserting “the maximum rate on net  
13       capital gain under section 1201 or the deduction  
14       under section 1202 (whichever is appropriate) shall  
15       be taken into account.”

16          (5) Paragraph (4) of section 642(c) is amended  
17       to read as follows:

18                 “(4) ADJUSTMENTS.—To the extent that the  
19       amount otherwise allowable as a deduction under  
20       this subsection consists of gain from the sale or ex-  
21       change of capital assets held for more than 1 year,  
22       proper adjustment shall be made for any deduction  
23       allowable to the estate or trust under section 1202  
24       (relating to capital gains deduction). In the case of  
25       a trust, the deduction allowed by this subsection

1 shall be subject to section 681 (relating to unrelated  
2 business income).”

3 (6) The last sentence of section 643(a)(3) is  
4 amended to read as follows: “The deduction under  
5 section 1202 (relating to capital gains deduction)  
6 shall not be taken into account.”

7 (7) Subparagraph (C) of section 643(a)(6) is  
8 amended by inserting “(i)” before “there shall” and  
9 by inserting before the period “, and (ii) the deduc-  
10 tion under section 1202 (relating to capital gains de-  
11 duction) shall not be taken into account”.

12 (8)(A) Paragraph (2) of section 904(b) is  
13 amended by striking subparagraph (A), by redesign-  
14 ating subparagraph (B) as subparagraph (A), and  
15 by inserting after subparagraph (A) (as so redesign-  
16 nated) the following new subparagraph:

17 “(B) OTHER TAXPAYERS.—In the case of  
18 a taxpayer other than a corporation, taxable in-  
19 come from sources outside the United States  
20 shall include gain from the sale or exchange of  
21 capital assets only to the extent of foreign  
22 source capital gain net income.”

23 (B) Subparagraph (A) of section 904(b)(2), as  
24 so redesignated, is amended—

1 (i) by striking all that precedes clause (i)  
 2 and inserting the following:

3 “(A) CORPORATIONS.—In the case of a  
 4 corporation—”, and

5 (ii) by striking in clause (i) “in lieu of ap-  
 6 plying subparagraph (A),”.

7 (C) Paragraph (3) of section 904(b) is amended  
 8 by striking subparagraphs (D) and (E) and inserting  
 9 the following new subparagraph:

10 “(D) RATE DIFFERENTIAL PORTION.—The  
 11 rate differential portion of foreign source net  
 12 capital gain, net capital gain, or the excess of  
 13 net capital gain from sources within the United  
 14 States over net capital gain, as the case may  
 15 be, is the same proportion of such amount as  
 16 the excess of the highest rate of tax specified in  
 17 section 11(b) over the alternative rate of tax  
 18 under section 1201(a) bears to the highest rate  
 19 of tax specified in section 11(b).”

20 (D) Clause (v) of section 593(b)(2)(D) is  
 21 amended—

22 (i) by striking “if there is a capital gain  
 23 rate differential (as defined in section  
 24 904(b)(3)(D)) for the taxable year,” and

1 (ii) by striking “section 904(b)(3)(E)” and  
2 inserting “section 904(b)(3)(D)”.

3 (9) The last sentence of section 1044(d) is  
4 amended by striking “1202” and inserting “1201(b)  
5 or 1203”.

6 (10)(A) Paragraph (2) of section 1211(b) is  
7 amended to read as follows:

8 “(2) the sum of—

9 “(A) the excess of the net short-term cap-  
10 ital loss over the net long-term capital gain, and

11 “(B) one-half of the excess of the net long-  
12 term capital loss over the net short-term capital  
13 gain.”

14 (B) So much of paragraph (2) of section  
15 1212(b) as precedes subparagraph (B) thereof is  
16 amended to read as follows:

17 “(2) SPECIAL RULES.—

18 “(A) ADJUSTMENTS.—

19 “(i) For purposes of determining the  
20 excess referred to in paragraph (1)(A),  
21 there shall be treated as short-term capital  
22 gain in the taxable year an amount equal  
23 to the lesser of—

1 “(I) the amount allowed for the  
 2 taxable year under paragraph (1) or  
 3 (2) of section 1211(b), or

4 “(II) the adjusted taxable income  
 5 for such taxable year.

6 “(ii) For purposes of determining the  
 7 excess referred to in paragraph (1)(B),  
 8 there shall be treated as short-term capital  
 9 gain in the taxable year an amount equal  
 10 to the sum of—

11 “(I) the amount allowed for the  
 12 taxable year under paragraph (1) or  
 13 (2) of section 1211(b) or the adjusted  
 14 taxable income for such taxable year,  
 15 whichever is the least, plus

16 “(II) the excess of the amount  
 17 described in subclause (I) over the net  
 18 short-term capital loss (determined  
 19 without regard to this subsection) for  
 20 such year.”

21 (C) Subsection (b) of section 1212 is amended  
 22 by adding at the end the following new paragraph:

23 “(3) TRANSITIONAL RULE.—

24 “(A) IN GENERAL.—The amount deter-  
 25 mined under subclause (II) of paragraph

1 (2)(A)(ii) for any taxable year shall be reduced  
 2 (but not below zero) by the excess of—

3 “(i) the amount of the unused pre-  
 4 1998 long-term capital loss for such year,  
 5 over

6 “(ii) the sum of the long-term capital  
 7 gain and the net short-term capital gain  
 8 for such taxable year.

9 Section 1211(b)(2)(B) shall be applied without  
 10 regard to ‘one-half of’ with respect to such ex-  
 11 cess for such taxable year.

12 “(B) UNUSED PRE-1998 LONG-TERM CAP-  
 13 ITAL LOSS.—For purposes of this paragraph,  
 14 the term ‘unused pre-1998 long-term capital  
 15 loss’ means, with respect to a taxable year, the  
 16 excess of—

17 “(i) the amount which under para-  
 18 graph (1)(B) (as in effect for taxable years  
 19 beginning before January 1, 1998) is  
 20 treated as a long-term capital loss for the  
 21 taxpayer’s first taxable year beginning  
 22 after December 31, 1997, over

23 “(ii) the sum of—

24 “(I) the aggregate amount deter-  
 25 mined under subparagraph (A)(ii) for



1 all prior taxable years beginning after  
 2 December 31, 1997, and  
 3 “(II) the aggregate reductions  
 4 under subparagraph (A) for all such  
 5 prior taxable years.”

6 (11) Paragraph (1) of section 1402(i) is amend-  
 7 ed by inserting “, and the deduction provided by sec-  
 8 tion 1202 shall not apply” before the period at the  
 9 end thereof.

10 (12) Subsection (e) of section 1445 is amend-  
 11 ed—

12 (A) in paragraph (1) by striking “35 per-  
 13 cent (or, to the extent provided in regulations,  
 14 28 percent)” and inserting “28 percent (or, to  
 15 the extent provided in regulations, 19.8 per-  
 16 cent)”, and

17 (B) in paragraph (2) by striking “35 per-  
 18 cent” and inserting “28 percent”.

19 (13)(A) The second sentence of section  
 20 7518(g)(6)(A) is amended—

21 (i) by striking “during a taxable year to  
 22 which section 1(h) or 1201(a) applies”, and

23 (ii) by striking “28 percent (34 percent”  
 24 and inserting “19.8 percent (28 percent”.

1 (B) The second sentence of section  
 2 607(h)(6)(A) of the Merchant Marine Act, 1936 is  
 3 amended—

4 (i) by striking “during a taxable year to  
 5 which section 1(h) or 1201(a) of such Code ap-  
 6 plies”, and

7 (ii) by striking “28 percent (34 percent”  
 8 and inserting “19.8 percent (28 percent”.

9 (d) CLERICAL AMENDMENT.—The table of sections  
 10 for part I of subchapter P of chapter 1 is amended by  
 11 striking the item relating to section 1202 and by inserting  
 12 after the item relating to section 1201 the following new  
 13 items:

“Sec. 1202. Capital gains deduction.

“Sec. 1203. 50-percent exclusion for gain from certain small  
 business stock.”

14 (e) EFFECTIVE DATE.—

15 (1) IN GENERAL.—Except as otherwise pro-  
 16 vided in this subsection, the amendments made by  
 17 this section shall apply to taxable years ending after  
 18 December 31, 1996.

19 (2) CONTRIBUTIONS.—The amendment made  
 20 by subsection (c)(2) shall apply to contributions  
 21 after December 31, 1996.

22 (3) USE OF LONG-TERM LOSSES.—The amend-  
 23 ments made by subsection (c)(10) shall apply to tax-  
 24 able years beginning after December 31, 1997.

1           (4) WITHHOLDING.—The amendments made by  
 2           subsection (c)(12) shall apply only to amounts paid  
 3           after the date of the enactment of this Act.

4   **SEC. 202. INDEXING OF CERTAIN ASSETS ACQUIRED AFTER**  
 5                   **DECEMBER 31, 1996, FOR PURPOSES OF DE-**  
 6                   **TERMINING GAIN.**

7           (a) IN GENERAL.—Part II of subchapter O of chap-  
 8   ter 1 (relating to basis rules of general application) is  
 9   amended by inserting after section 1021 the following new  
 10 section:

11   **“SEC. 1022. INDEXING OF CERTAIN ASSETS ACQUIRED**  
 12                   **AFTER DECEMBER 31, 1996, FOR PURPOSES**  
 13                   **OF DETERMINING GAIN.**

14           “(a) GENERAL RULE.—

15                   “(1) INDEXED BASIS SUBSTITUTED FOR AD-  
 16 JUSTED BASIS.—Solely for purposes of determining  
 17 gain on the sale or other disposition by a taxpayer  
 18 (other than a corporation) of an indexed asset which  
 19 has been held for more than 3 years, the indexed  
 20 basis of the asset shall be substituted for its ad-  
 21 justed basis.

22                   “(2) EXCEPTION FOR DEPRECIATION, ETC.—  
 23 The deductions for depreciation, depletion, and am-  
 24 ortization shall be determined without regard to the

1 application of paragraph (1) to the taxpayer or any  
 2 other person.

3 “(b) INDEXED ASSET.—

4 “(1) IN GENERAL.—For purposes of this sec-  
 5 tion, the term ‘indexed asset’ means—

6 “(A) common stock in a C corporation  
 7 (other than a foreign corporation), and

8 “(B) tangible property,  
 9 which is a capital asset or property used in the trade  
 10 or business (as defined in section 1231(b)).

11 “(2) STOCK IN CERTAIN FOREIGN CORPORA-  
 12 TIONS INCLUDED.—For purposes of this section—

13 “(A) IN GENERAL.—The term ‘indexed  
 14 asset’ includes common stock in a foreign cor-  
 15 poration which is regularly traded on an estab-  
 16 lished securities market.

17 “(B) EXCEPTION.—Subparagraph (A)  
 18 shall not apply to—

19 “(i) stock of a foreign investment  
 20 company (within the meaning of section  
 21 1246(b)),

22 “(ii) stock in a passive foreign invest-  
 23 ment company (as defined in section  
 24 1296),

1 “(iii) stock in a foreign corporation  
 2 held by a United States person who meets  
 3 the requirements of section 1248(a)(2),  
 4 and

5 “(iv) stock in a foreign personal hold-  
 6 ing company (as defined in section 552).

7 “(C) TREATMENT OF AMERICAN DEPOSI-  
 8 TORY RECEIPTS.—An American depository re-  
 9 ceipt for common stock in a foreign corporation  
 10 shall be treated as common stock in such cor-  
 11 poration.

12 “(c) INDEXED BASIS.—For purposes of this sec-  
 13 tion—

14 “(1) GENERAL RULE.—The indexed basis for  
 15 any asset is—

16 “(A) the adjusted basis of the asset, in-  
 17 creased by

18 “(B) the applicable inflation adjustment.

19 “(2) APPLICABLE INFLATION ADJUSTMENT.—  
 20 The applicable inflation adjustment for any asset is  
 21 an amount equal to—

22 “(A) the adjusted basis of the asset, multi-  
 23 plied by

24 “(B) the percentage (if any) by which—

1                   “(i) the gross domestic product  
2                   deflator for the last calendar quarter end-  
3                   ing before the asset is disposed of, exceeds

4                   “(ii) the gross domestic product  
5                   deflator for the last calendar quarter end-  
6                   ing before the asset was acquired by the  
7                   taxpayer.

8           The percentage under subparagraph (B) shall be  
9           rounded to the nearest  $\frac{1}{10}$  of 1 percentage point.

10           “(3) GROSS DOMESTIC PRODUCT DEFLATOR.—

11           The gross domestic product deflator for any cal-  
12           endar quarter is the implicit price deflator for the  
13           gross domestic product for such quarter (as shown  
14           in the last revision thereof released by the Secretary  
15           of Commerce before the close of the following cal-  
16           endar quarter).

17           “(d) SUSPENSION OF HOLDING PERIOD WHERE DI-  
18           MINISHED RISK OF LOSS; TREATMENT OF SHORT  
19           SALES.—

20           “(1) IN GENERAL.—If the taxpayer (or a relat-  
21           ed person) enters into any transaction which sub-  
22           stantially reduces the risk of loss from holding any  
23           asset, such asset shall not be treated as an indexed  
24           asset for the period of such reduced risk.

25           “(2) SHORT SALES.—

1           “(A) IN GENERAL.—In the case of a short  
 2           sale of an indexed asset with a short sale period  
 3           in excess of 3 years, for purposes of this title,  
 4           the amount realized shall be an amount equal  
 5           to the amount realized (determined without re-  
 6           gard to this paragraph) increased by the appli-  
 7           cable inflation adjustment. In applying sub-  
 8           section (c)(2) for purposes of the preceding sen-  
 9           tence, the date on which the property is sold  
 10          short shall be treated as the date of acquisition  
 11          and the closing date for the sale shall be treat-  
 12          ed as the date of disposition.

13           “(B) SHORT SALE PERIOD.—For purposes  
 14          of subparagraph (A), the short sale period be-  
 15          gins on the day that the property is sold and  
 16          ends on the closing date for the sale.

17          “(e) TREATMENT OF REGULATED INVESTMENT  
 18          COMPANIES AND REAL ESTATE INVESTMENT TRUSTS.—

19           “(1) ADJUSTMENTS AT ENTITY LEVEL.—

20           “(A) IN GENERAL.—Except as otherwise  
 21          provided in this paragraph, the adjustment  
 22          under subsection (a) shall be allowed to any  
 23          qualified investment entity (including for pur-  
 24          poses of determining the earnings and profits of  
 25          such entity).

1 “(B) EXCEPTION FOR CORPORATE SHARE-  
2 HOLDERS.—Under regulations—

3 “(i) in the case of a distribution by a  
4 qualified investment entity (directly or in-  
5 directly) to a corporation—

6 “(I) the determination of whether  
7 such distribution is a dividend shall be  
8 made without regard to this section,  
9 and

10 “(II) the amount treated as gain  
11 by reason of the receipt of any capital  
12 gain dividend shall be increased by the  
13 percentage by which the entity’s net  
14 capital gain for the taxable year (de-  
15 termined without regard to this sec-  
16 tion) exceeds the entity’s net capital  
17 gain for such year determined with re-  
18 gard to this section, and

19 “(ii) there shall be other appropriate  
20 adjustments (including deemed distribu-  
21 tions) so as to ensure that the benefits of  
22 this section are not allowed (directly or in-  
23 directly) to corporate shareholders of quali-  
24 fied investment entities.



1 For purposes of the preceding sentence, any  
2 amount includible in gross income under section  
3 852(b)(3)(D) shall be treated as a capital gain  
4 dividend and an S corporation shall not be  
5 treated as a corporation.

6 “(C) EXCEPTION FOR QUALIFICATION  
7 PURPOSES.—This section shall not apply for  
8 purposes of sections 851(b) and 856(e).

9 “(D) EXCEPTION FOR CERTAIN TAXES IM-  
10 POSED AT ENTITY LEVEL.—

11 “(i) TAX ON FAILURE TO DISTRIBUTE  
12 ENTIRE GAIN.—If any amount is subject to  
13 tax under section 852(b)(3)(A) for any  
14 taxable year, the amount on which tax is  
15 imposed under such section shall be in-  
16 creased by the percentage determined  
17 under subparagraph (B)(i)(II). A similar  
18 rule shall apply in the case of any amount  
19 subject to tax under paragraph (2) or (3)  
20 of section 857(b) to the extent attributable  
21 to the excess of the net capital gain over  
22 the deduction for dividends paid deter-  
23 mined with reference to capital gain divi-  
24 dends only. The first sentence of this  
25 clause shall not apply to so much of the

1 amount subject to tax under section  
 2 852(b)(3)(A) as is designated by the com-  
 3 pany under section 852(b)(3)(D).

4 “(ii) OTHER TAXES.—This section  
 5 shall not apply for purposes of determining  
 6 the amount of any tax imposed by para-  
 7 graph (4), (5), or (6) of section 857(b).

8 “(2) ADJUSTMENTS TO INTERESTS HELD IN  
 9 ENTITY.—

10 “(A) REGULATED INVESTMENT COMPA-  
 11 NIES.—Stock in a regulated investment com-  
 12 pany (within the meaning of section 851) shall  
 13 be an indexed asset for any calendar quarter in  
 14 the same ratio as—

15 “(i) the average of the fair market  
 16 values of the indexed assets held by such  
 17 company at the close of each month during  
 18 such quarter, bears to

19 “(ii) the average of the fair market  
 20 values of all assets held by such company  
 21 at the close of each such month.

22 “(B) REAL ESTATE INVESTMENT  
 23 TRUSTS.—Stock in a real estate investment  
 24 trust (within the meaning of section 856) shall

1 be an indexed asset for any calendar quarter in  
 2 the same ratio as—

3 “(i) the fair market value of the in-  
 4 dexed assets held by such trust at the close  
 5 of such quarter, bears to

6 “(ii) the fair market value of all as-  
 7 sets held by such trust at the close of such  
 8 quarter.

9 “(C) RATIO OF 80 PERCENT OR MORE.—If  
 10 the ratio for any calendar quarter determined  
 11 under subparagraph (A) or (B) would (but for  
 12 this subparagraph) be 80 percent or more, such  
 13 ratio for such quarter shall be 100 percent.

14 “(D) RATIO OF 20 PERCENT OR LESS.—If  
 15 the ratio for any calendar quarter determined  
 16 under subparagraph (A) or (B) would (but for  
 17 this subparagraph) be 20 percent or less, such  
 18 ratio for such quarter shall be zero.

19 “(E) LOOK-THRU OF PARTNERSHIPS.—For  
 20 purposes of this paragraph, a qualified invest-  
 21 ment entity which holds a partnership interest  
 22 shall be treated (in lieu of holding a partnership  
 23 interest) as holding its proportionate share of  
 24 the assets held by the partnership.

1           “(3) TREATMENT OF RETURN OF CAPITAL DIS-  
 2       TRIBUTIONS.—Except as otherwise provided by the  
 3       Secretary, a distribution with respect to stock in a  
 4       qualified investment entity which is not a dividend  
 5       and which results in a reduction in the adjusted  
 6       basis of such stock shall be treated as allocable to  
 7       stock acquired by the taxpayer in the order in which  
 8       such stock was acquired.

9           “(4) QUALIFIED INVESTMENT ENTITY.—For  
 10      purposes of this subsection, the term ‘qualified in-  
 11      vestment entity’ means—

12               “(A) a regulated investment company  
 13               (within the meaning of section 851), and

14               “(B) a real estate investment trust (within  
 15               the meaning of section 856).

16      “(f) OTHER PASS-THRU ENTITIES.—

17           “(1) PARTNERSHIPS.—

18               “(A) IN GENERAL.—In the case of a part-  
 19               nership, the adjustment made under subsection  
 20               (a) at the partnership level shall be passed  
 21               through to the partners.

22               “(B) SPECIAL RULE IN THE CASE OF SEC-  
 23               TION 754 ELECTIONS.—In the case of a transfer  
 24               of an interest in a partnership with respect to

1           which the election provided in section 754 is in  
2           effect—

3                   “(i) the adjustment under section  
4                   743(b)(1) shall, with respect to the trans-  
5                   feror partner, be treated as a sale of the  
6                   partnership assets for purposes of applying  
7                   this section, and

8                   “(ii) with respect to the transferee  
9                   partner, the partnership’s holding period  
10                  for purposes of this section in such assets  
11                  shall be treated as beginning on the date  
12                  of such adjustment.

13               “(2) S CORPORATIONS.—In the case of an S  
14               corporation, the adjustment made under subsection  
15               (a) at the corporate level shall be passed through to  
16               the shareholders. This section shall not apply for  
17               purposes of determining the amount of any tax im-  
18               posed by section 1374 or 1375.

19               “(3) COMMON TRUST FUNDS.—In the case of a  
20               common trust fund, the adjustment made under sub-  
21               section (a) at the trust level shall be passed through  
22               to the participants.

23               “(4) INDEXING ADJUSTMENT DISREGARDED IN  
24               DETERMINING LOSS ON SALE OF INTEREST IN EN-  
25               TITY.—Notwithstanding the preceding provisions of

1       this subsection, for purposes of determining the  
 2       amount of any loss on a sale or exchange of an in-  
 3       terest in a partnership, S corporation, or common  
 4       trust fund, the adjustment made under subsection  
 5       (a) shall not be taken into account in determining  
 6       the adjusted basis of such interest.

7       “(g) DISPOSITIONS BETWEEN RELATED PERSONS.—

8               “(1) IN GENERAL.—This section shall not apply  
 9       to any sale or other disposition of property between  
 10      related persons except to the extent that the basis  
 11      of such property in the hands of the transferee is a  
 12      substituted basis.

13              “(2) RELATED PERSONS DEFINED.—For pur-  
 14      poses of this section, the term ‘related persons’  
 15      means—

16                   “(A) persons bearing a relationship set  
 17                   forth in section 267(b), and

18                   “(B) persons treated as single employer  
 19                   under subsection (b) or (c) of section 414.

20       “(h) TRANSFERS TO INCREASE INDEXING ADJUST-  
 21      MENT.—If any person transfers cash, debt, or any other  
 22      property to another person and the principal purpose of  
 23      such transfer is to secure or increase an adjustment under  
 24      subsection (a), the Secretary may disallow part or all of  
 25      such adjustment or increase.

1 “(i) SPECIAL RULES.—For purposes of this section—

2 “(1) TREATMENT OF IMPROVEMENTS, ETC.—If  
3 there is an addition to the adjusted basis of any tan-  
4 gible property or of any stock in a corporation dur-  
5 ing the taxable year by reason of an improvement to  
6 such property or a contribution to capital of such  
7 corporation—

8 “(A) such addition shall never be taken  
9 into account under subsection (c)(1)(A) if the  
10 aggregate amount thereof during the taxable  
11 year with respect to such property or stock is  
12 less than \$1,000, and

13 “(B) such addition shall be treated as a  
14 separate asset acquired at the close of such tax-  
15 able year if the aggregate amount thereof dur-  
16 ing the taxable year with respect to such prop-  
17 erty or stock is \$1,000 or more.

18 A rule similar to the rule of the preceding sentence  
19 shall apply to any other portion of an asset to the  
20 extent that separate treatment of such portion is ap-  
21 propriate to carry out the purposes of this section.

22 “(2) ASSETS WHICH ARE NOT INDEXED ASSETS  
23 THROUGHOUT HOLDING PERIOD.—The applicable in-  
24 flation adjustment shall be appropriately reduced for

1 periods during which the asset was not an indexed  
2 asset.

3 “(3) TREATMENT OF CERTAIN DISTRIBUTIONS.—A distribution with respect to stock in a  
4 corporation which is not a dividend shall be treated  
5 as a disposition.  
6

7 “(4) ACQUISITION DATE WHERE THERE HAS  
8 BEEN PRIOR APPLICATION OF SUBSECTION (a)(1)  
9 WITH RESPECT TO THE TAXPAYER.—If there has  
10 been a prior application of subsection (a)(1) to an  
11 asset while such asset was held by the taxpayer, the  
12 date of acquisition of such asset by the taxpayer  
13 shall be treated as not earlier than the date of the  
14 most recent such prior application.

15 “(5) COLLAPSIBLE CORPORATIONS.—The appli-  
16 cation of section 341(a) (relating to collapsible cor-  
17 porations) shall be determined without regard to this  
18 section.

19 “(j) REGULATIONS.—The Secretary shall prescribe  
20 such regulations as may be necessary or appropriate to  
21 carry out the purposes of this section.”

22 (b) CLERICAL AMENDMENT.—The table of sections  
23 for part II of subchapter O of chapter 1 is amended by  
24 inserting after the item relating to section 1021 the follow-  
25 ing new item:



“Sec. 1022. Indexing of certain assets acquired after December 31, 1996, for purposes of determining gain.”

1 (c) EFFECTIVE DATE.—

2 (1) IN GENERAL.—The amendments made by  
3 this section shall apply to the disposition of any  
4 property the holding period of which begins after  
5 December 31, 1996.

6 (2) CERTAIN TRANSACTIONS BETWEEN RELAT-  
7 ED PERSONS.—The amendments made by this sec-  
8 tion shall not apply to the disposition of any prop-  
9 erty acquired after December 31, 1996, from a re-  
10 lated person (as defined in section 1022(g)(2) of the  
11 Internal Revenue Code of 1986, as added by this  
12 section) if—

13 (A) such property was so acquired for a  
14 price less than the property’s fair market value,  
15 and

16 (B) the amendments made by this section  
17 did not apply to such property in the hands of  
18 such related person.

19 (d) ELECTION TO RECOGNIZE GAIN ON ASSETS  
20 HELD ON JANUARY 1, 1997.—For purposes of the Inter-  
21 nal Revenue Code of 1986—

22 (1) IN GENERAL.—A taxpayer other than a cor-  
23 poration may elect to treat—

1 (A) any readily tradable stock (which is an  
2 indexed asset) held by such taxpayer on Janu-  
3 ary 1, 1997, and not sold before the next busi-  
4 ness day after such date, as having been sold  
5 on such next business day for an amount equal  
6 to its closing market price on such next busi-  
7 ness day (and as having been reacquired on  
8 such next business day for an amount equal to  
9 such closing market price), and

10 (B) any other indexed asset held by the  
11 taxpayer on January 1, 1997, as having been  
12 sold on such date for an amount equal to its  
13 fair market value on such date (and as having  
14 been reacquired on such date for an amount  
15 equal to such fair market value).

16 (2) TREATMENT OF GAIN OR LOSS.—

17 (A) Any gain resulting from an election  
18 under paragraph (1) shall be treated as received  
19 or accrued on the date the asset is treated as  
20 sold under paragraph (1) and shall be recog-  
21 nized notwithstanding any provision of the In-  
22 ternal Revenue Code of 1986.

23 (B) Any loss resulting from an election  
24 under paragraph (1) shall not be allowed for  
25 any taxable year.

1           (3) ELECTION.—An election under paragraph  
 2           (1) shall be made in such manner as the Secretary  
 3           of the Treasury or his delegate may prescribe and  
 4           shall specify the assets for which such election is  
 5           made. Such an election, once made with respect to  
 6           any asset, shall be irrevocable.

7           (4) READILY TRADABLE STOCK.—For purposes  
 8           of this subsection, the term “readily tradable stock”  
 9           means any stock which, as of January 1, 1997, is  
 10          readily tradable on an established securities market  
 11          or otherwise.

12          (e) TREATMENT OF PRINCIPAL RESIDENCES.—Prop-  
 13          erty held and used by the taxpayer on January 1, 1997,  
 14          as his principal residence (within the meaning of section  
 15          1034 of the Internal Revenue Code of 1986) shall be treat-  
 16          ed—

17               (1) for purposes of subsection (c)(1) of this sec-  
 18               tion and section 1022 of such Code, as having a  
 19               holding period which begins on January 1, 1997,  
 20               and

21               (2) for purposes of section 1022(c)(2)(B)(ii) of  
 22               such Code, as having been acquired on January 1,  
 23               1997.

24          Subsection (d) shall not apply to property to which this  
 25          subsection applies.

1 **SEC. 203. MODIFICATIONS TO EXCLUSION OF GAIN ON CER-**  
 2 **TAIN SMALL BUSINESS STOCK.**

3 (a) **REPEAL OF MINIMUM TAX PREFERENCE.**—

4 (1) Subsection (a) of section 57 is amended by  
 5 striking paragraph (7).

6 (2) Subclause (II) of section 53(d)(1)(B)(ii) is  
 7 amended by striking “, (5), and (7)” and inserting  
 8 “and (5)”.

9 (b) **STOCK OF LARGER BUSINESSES ELIGIBLE FOR**  
 10 **REDUCED RATES.**—Paragraph (1) of section 1203(d), as  
 11 redesignated by section 201, is amended by striking  
 12 “\$50,000,000” each place it appears and inserting  
 13 “\$100,000,000”.

14 (c) **REPEAL OF PER-ISSUER LIMITATION.**—Section  
 15 1203, as so redesignated, is amended by striking sub-  
 16 section (b).

17 (d) **OTHER MODIFICATIONS.**—

18 (1) **REPEAL OF WORKING CAPITAL LIMITA-**  
 19 **TION.**—Paragraph (6) of section 1203(e), as so re-  
 20 designated, is amended—

21 (A) by striking “2 years” in subparagraph

22 (B) and inserting “5 years”, and

23 (B) by striking the last sentence.

1           (2) EXCEPTION FROM REDEMPTION RULES  
 2       WHERE BUSINESS PURPOSE.—Paragraph (3) of sec-  
 3       tion 1203(c), as so redesignated, is amended by add-  
 4       ing at the end the following new subparagraph:

5           “(D) WAIVER WHERE BUSINESS PUR-  
 6       POSE.—A purchase of stock by the issuing cor-  
 7       poration shall be disregarded for purposes of  
 8       subparagraph (B) if the issuing corporation es-  
 9       tablishes that there was a business purpose for  
 10      such purchase and one of the principal purposes  
 11      of the purchase was not to avoid the limitations  
 12      of this section.”

13      (e) CONFORMING AMENDMENTS.—

14           (1) Subsection (c) of section 1203, as so redes-  
 15      ignated, is amended by striking “subsections (f) and  
 16      (h)” and inserting “subsections (e) and (g)”.

17           (2) Paragraph (2) of section 1203(c), as so re-  
 18      designated, is amended—

19           (A) by striking “subsection (e)” each place  
 20      it appears and inserting “subsection (d)”, and

21           (B) by striking “subsection (e)(4) in sub-  
 22      paragraph (B)(ii) and inserting “subsection  
 23      (d)(4)”.

1           (3) Paragraph (1) of section 1203(e), as so re-  
 2           designated, is amended by striking “subsection  
 3           (c)(2)” and inserting “subsection (b)(2)”.

4           (4) Paragraph (1) of section 1203(g), as so re-  
 5           designated, is amended to read as follows:

6           “(1) IN GENERAL.—If any amount included in  
 7           gross income by reason of holding an interest in a  
 8           pass-thru entity meets the requirements of para-  
 9           graph (2), such amount shall be treated as gain  
 10          from the sale or exchange of any qualified small  
 11          business stock held for more than 5 years.”

12          (5) Section 1203, as so redesignated, as amend-  
 13          ed by the preceding provisions of this section, is  
 14          amended by redesignating subsections (c) through  
 15          (k) as subsections (b) through (j), respectively.

16          (f) CLERICAL AMENDMENT.—Section 1203, as so re-  
 17          designated, is amended by adding at the end the following  
 18          new subsection:

19          “(k) CROSS REFERENCE.—

**“For reduced rates on gain of qualified small busi-  
 ness stock held more than 5 years, see sections  
 1201(b) and 1202(e).”**

20          (g) EFFECTIVE DATES.—

21               (1) IN GENERAL.—Except as provided in para-  
 22               graph (2), the amendments made by this section  
 23               shall apply to stock issued after August 10, 1993.

1           (2) INCREASE IN SIZE.—The amendment made  
 2           by subsection (b) shall apply to stock issued after  
 3           the date of the enactment of this Act.

4           **Subtitle B—Corporate Capital**  
 5           **Gains**

6   **SEC. 211. REDUCTION OF ALTERNATIVE CAPITAL GAIN TAX**  
 7           **FOR CORPORATIONS.**

8           (a) IN GENERAL.—Section 1201 is amended to read  
 9           as follows:

10   **“SEC. 1201. ALTERNATIVE TAX FOR CORPORATIONS.**

11           “(a) GENERAL RULE.—If for any taxable year a cor-  
 12           poration has a net capital gain, then, in lieu of the tax  
 13           imposed by sections 11, 511, and 831 (a) and (b) (which-  
 14           ever is applicable), there is hereby imposed a tax (if such  
 15           tax is less than the tax imposed by such sections) which  
 16           shall consist of the sum of—

17           “(1) a tax computed on the taxable income re-  
 18           duced by the amount of the net capital gain, at the  
 19           rates and in the manner as if this subsection had  
 20           not been enacted, plus

21           “(2) a tax of 28 percent of the net capital gain.

22           “(b) SPECIAL RULES FOR QUALIFIED SMALL BUSI-  
 23           NESS GAIN.—

24           “(1) IN GENERAL.—If for any taxable year a  
 25           corporation has gain from the sale or exchange of

1 any qualified small business stock held for more  
 2 than 5 years, the amount determined under sub-  
 3 section (a)(2) for such taxable year shall be equal to  
 4 the sum of—

5 “(A) 21 percent of the lesser of such gain  
 6 or the corporation’s net capital gain, plus

7 “(B) 28 percent of the net capital gain re-  
 8 duced by the gain taken into account under  
 9 subparagraph (A).

10 “(2) QUALIFIED SMALL BUSINESS STOCK.—For  
 11 purposes of paragraph (1), the term ‘qualified small  
 12 business stock’ has the meaning given such term by  
 13 section 1203(b), except that stock shall not be treat-  
 14 ed as qualified small business stock if such stock  
 15 was at any time held by a member of the parent-  
 16 subsidiary controlled group (as defined in section  
 17 1203(c)(3)) which includes the qualified small busi-  
 18 ness.

19 “(c) TRANSITIONAL RULE.—

20 “(1) IN GENERAL.—In applying this section,  
 21 net capital gain for any taxable year shall not exceed  
 22 the net capital gain determined by taking into ac-  
 23 count only gains and losses properly taken into ac-  
 24 count for the portion of the taxable year after De-  
 25 cember 31, 1996.



1           “(2) SPECIAL RULE FOR PASS-THRU ENTI-  
 2           TIES.—Section 1202(d)(3)(C) shall apply for pur-  
 3           poses of paragraph (1).

4           “(d) CROSS REFERENCES.—

**“For computation of the alternative tax—**

**“(1) in the case of life insurance companies, see**  
**section 801(a)(2),**

**“(2) in the case of regulated investment compa-**  
**nies and their shareholders, see section 852(b)(3) (A**  
**and (D), and**

**“(3) in the case of real estate investment trusts,**  
**see section 857(b)(3)(A).”**

5           (b) TECHNICAL AMENDMENT.—Clause (iii) of section  
 6           852(b)(3)(D) is amended by striking “65 percent” and in-  
 7           serting “72 percent”.

8           (c) EFFECTIVE DATE.—

9           (1) IN GENERAL.—The amendments made by  
 10          this section shall apply to taxable years ending after  
 11          December 31, 1996.

12          (2) QUALIFIED SMALL BUSINESS STOCK.—Sec-  
 13          tion 1201(b) of the Internal Revenue Code of 1986  
 14          (as added by subsection (a)) shall apply to gain from  
 15          qualified small business stock acquired on or after  
 16          the date of the enactment of this Act.

1 **Subtitle C—Capital Loss Deduction**  
 2 **Allowed With Respect to Sale or**  
 3 **Exchange of Principal Resi-**  
 4 **dence**

5 **SEC. 221. CAPITAL LOSS DEDUCTION ALLOWED WITH RE-**  
 6 **SPECT TO SALE OR EXCHANGE OF PRINCIPAL**  
 7 **RESIDENCE.**

8 (a) IN GENERAL.—Subsection (c) of section 165 (re-  
 9 lating to limitation on losses of individuals) is amended  
 10 by striking “and” at the end of paragraph (2), by striking  
 11 the period at the end of paragraph (3) and inserting “;  
 12 and”, and by adding at the end the following new para-  
 13 graph:

14 “(4) losses arising from the sale or exchange of  
 15 the principal residence (within the meaning of sec-  
 16 tion 1034) of the taxpayer.”

17 (b) EFFECTIVE DATE.—The amendment made by  
 18 subsection (a) shall apply to sales and exchanges after De-  
 19 cember 31, 1996, in taxable years ending after such date.

20 **TITLE III—ESTATE AND GIFT**  
 21 **PROVISIONS**

22 **SEC. 301. INCREASE IN UNIFIED ESTATE AND GIFT TAX**  
 23 **CREDIT.**

24 (a) ESTATE TAX CREDIT.—

1 (1) IN GENERAL.—Section 2010(a) (relating to  
 2 unified credit against estate tax) is amended by  
 3 striking “\$192,800” and inserting “the applicable  
 4 credit amount”.

5 (2) APPLICABLE CREDIT AMOUNT.—Section  
 6 2010 is amended by redesignating subsection (c) as  
 7 subsection (d) and by inserting after subsection (b)  
 8 the following new subsection:

9 “(c) APPLICABLE CREDIT AMOUNT.—For purposes  
 10 of this section, the applicable credit amount is the amount  
 11 of the tentative tax which would be determined under the  
 12 rate schedule set forth in section 2001(c) if the amount  
 13 with respect to which such tentative tax is to be computed  
 14 were the applicable exclusion amount determined in ac-  
 15 cordance with the following table:

<b>“In the case of estates of decedents dying, and gifts made, during:</b>	<b>The applicable exclusion amount is:</b>
1997 .....	\$650,000
1998 .....	\$700,000
1999 .....	\$750,000
2000 .....	\$800,000
2001 .....	\$850,000
2002 .....	\$900,000
2003 .....	\$950,000
2004 or thereafter .....	\$1,000,000.”

16 (3) CONFORMING AMENDMENTS.—

17 (A) Section 6018(a)(1) is amended by  
 18 striking “\$600,000” and inserting “the applica-  
 19 ble exclusion amount in effect under section

1           2010(c) for the calendar year which includes  
2           the date of death”.

3           (B) Section 2001(c)(2) is amended by  
4           striking “\$21,040,000” and inserting “the  
5           amount at which the average tax rate under  
6           this section is 55 percent”.

7           (C) Section 2102(c)(3)(A) is amended by  
8           striking “\$192,800” and inserting “the applica-  
9           ble credit amount in effect under section  
10          2010(c) for the calendar year which includes  
11          the date of death”.

12          (b) UNIFIED GIFT TAX CREDIT.—Section  
13   2505(a)(1) (relating to unified credit against gift tax) is  
14   amended by striking “\$192,800” and inserting “the appli-  
15   cable credit amount in effect under section 2010(c) for  
16   such calendar year”.

17          (c) EFFECTIVE DATE.—The amendments made by  
18   this section shall apply to the estates of decedents dying,  
19   and gifts made, after December 31, 1996.

20   **SEC. 302. FAMILY-OWNED BUSINESS EXCLUSION.**

21          (a) IN GENERAL.—Part III of subchapter A of chap-  
22   ter 11 (relating to gross estate) is amended by inserting  
23   after section 2033 the following new section:

1 **“SEC. 2033A. FAMILY-OWNED BUSINESS EXCLUSION.**

2 “(a) IN GENERAL.—In the case of an estate of a de-  
3 cedent to which this section applies, the value of the gross  
4 estate shall not include the lesser of—

5 “(1) the adjusted value of the qualified family-  
6 owned business interests of the decedent otherwise  
7 includible in the estate, or

8 “(2) the sum of—

9 “(A) \$1,500,000, plus

10 “(B) 50 percent of the excess (if any) of  
11 the adjusted value of such interests over  
12 \$1,500,000.

13 “(b) ESTATES TO WHICH SECTION APPLIES.—

14 “(1) IN GENERAL.—This section shall apply to  
15 an estate if—

16 “(A) the decedent was (at the date of the  
17 decedent’s death) a citizen or resident of the  
18 United States,

19 “(B) the sum of—

20 “(i) the adjusted value of the qualified  
21 family-owned business interests described  
22 in paragraph (2), plus

23 “(ii) the amount of the gifts of such  
24 interests determined under paragraph (3),  
25 exceeds 50 percent of the adjusted gross estate,  
26 and

1           “(C) during the 8-year period ending on  
 2           the date of the decedent’s death there have  
 3           been periods aggregating 5 years or more dur-  
 4           ing which—

5                   “(i) such interests were owned by the  
 6                   decedent or a member of the decedent’s  
 7                   family, and

8                   “(ii) there was material participation  
 9                   (within the meaning of section  
 10                  2032A(e)(6)) by the decedent or a member  
 11                  of the decedent’s family in the operation of  
 12                  the business to which such interests relate.

13           “(2) INCLUDIBLE QUALIFIED FAMILY-OWNED  
 14           BUSINESS INTERESTS.—The qualified family-owned  
 15           business interests described in this paragraph are  
 16           the interests which—

17                   “(A) are included in determining the value  
 18                   of the gross estate (without regard to this sec-  
 19                   tion), and

20                   “(B) are acquired by any qualified heir  
 21                   from, or passed to any qualified heir from, the  
 22                   decedent (within the meaning of section  
 23                   2032A(e)(9)).

1           “(3) INCLUDIBLE GIFTS OF INTERESTS.—The  
 2           amount of the gifts of qualified family-owned busi-  
 3           ness interests determined under this paragraph is  
 4           the excess of—

5                   “(A) the sum of—

6                           “(i) the amount of such gifts from the  
 7                           decedent to members of the decedent’s  
 8                           family taken into account under subsection  
 9                           2001(b)(1)(B), plus

10                           “(ii) the amount of such gifts other-  
 11                           wise excluded under section 2503(b),  
 12                           to the extent such interests are continuously  
 13                           held by members of such family (other than the  
 14                           decedent’s spouse) between the date of the gift  
 15                           and the date of the decedent’s death, over

16                           “(B) the amount of such gifts from the de-  
 17                           cedent to members of the decedent’s family oth-  
 18                           erwise included in the gross estate.

19           “(c) ADJUSTED GROSS ESTATE.—For purposes of  
 20           this section, the term ‘adjusted gross estate’ means the  
 21           value of the gross estate (determined without regard to  
 22           this section)—

23                   “(1) reduced by any amount deductible under  
 24                   paragraph (3) or (4) of section 2053(a), and

25                   “(2) increased by the excess of—

1 “(A) the sum of—

2 “(i) the amount of gifts determined  
3 under subsection (b)(3), plus

4 “(ii) the amount (if more than de  
5 minimis) of other transfers from the dece-  
6 dent to the decedent’s spouse (at the time  
7 of the transfer) within 10 years of the date  
8 of the decedent’s death, plus

9 “(iii) the amount of other gifts (not  
10 included under clause (i) or (ii)) from the  
11 decedent within 3 years of such date, other  
12 than gifts to members of the decedent’s  
13 family otherwise excluded under section  
14 2503(b), over

15 “(B) the sum of the amounts described in  
16 clauses (i), (ii), and (iii) of subparagraph (A)  
17 which are otherwise includible in the gross es-  
18 tate.

19 For purposes of the preceding sentence, the Secretary may  
20 provide that de minimis gifts to persons other than mem-  
21 bers of the decedent’s family shall not be taken into ac-  
22 count.

23 “(d) ADJUSTED VALUE OF THE QUALIFIED FAMILY-  
24 OWNED BUSINESS INTERESTS.—For purposes of this sec-  
25 tion, the adjusted value of any qualified family-owned



1 business interest is the value of such interest for purposes  
 2 of this chapter (determined without regard to this sec-  
 3 tion), reduced by the excess of—

4 “(1) any amount deductible under paragraph  
 5 (3) or (4) of section 2053(a), over

6 “(2) the sum of—

7 “(A) any indebtedness on any qualified  
 8 residence of the decedent the interest on which  
 9 is deductible under section 163(h)(3), plus

10 “(B) any indebtedness to the extent the  
 11 taxpayer establishes that the proceeds of such  
 12 indebtedness were used for the payment of edu-  
 13 cational and medical expenses of the decedent,  
 14 the decedent’s spouse, or the decedent’s depend-  
 15 ents (within the meaning of section 152), plus

16 “(C) any indebtedness not described in  
 17 clause (i) or (ii), to the extent such indebted-  
 18 ness does not exceed \$10,000.

19 “(e) QUALIFIED FAMILY-OWNED BUSINESS INTER-  
 20 EST.—

21 “(1) IN GENERAL.—For purposes of this sec-  
 22 tion, the term ‘qualified family-owned business inter-  
 23 est’ means—

24 “(A) an interest as a proprietor in a trade  
 25 or business carried on as a proprietorship, or

1           “(B) an interest in an entity carrying on  
2 a trade or business, if—

3           “(i) at least—

4           “(I) 50 percent of such entity is  
5 owned (directly or indirectly) by the  
6 decedent and members of the decedent’s family,

8           “(II) 70 percent of such entity is  
9 so owned by members of 2 families, or

10           “(III) 90 percent of such entity  
11 is so owned by members of 3 families,  
12 and

13           “(ii) for purposes of subclause (II) or  
14 (III) of clause (i), at least 30 percent of  
15 such entity is so owned by the decedent  
16 and members of the decedent’s family.

17           “(2) LIMITATION.—Such term shall not in-  
18 clude—

19           “(A) any interest in a trade or business  
20 the principal place of business of which is not  
21 located in the United States,

22           “(B) any interest in an entity, if the stock  
23 or debt of such entity or a controlled group (as  
24 defined in section 267(f)(1)) of which such en-  
25 tity was a member was readily tradable on an

1 established securities market or secondary mar-  
2 ket (as defined by the Secretary) at any time  
3 within 3 years of the date of the decedent's  
4 death,

5 “(C) any interest in a trade or business  
6 not described in section 542(c)(2), if more than  
7 35 percent of the adjusted ordinary gross in-  
8 come of such trade or business for the taxable  
9 year which includes the date of the decedent's  
10 death would qualify as personal holding com-  
11 pany income (as defined in section 543(a)),

12 “(D) that portion of an interest in a trade  
13 or business that is attributable to—

14 “(i) cash or marketable securities, or  
15 both, in excess of the reasonably expected  
16 day-to-day working capital needs of such  
17 trade or business, and

18 “(ii) any other assets of the trade or  
19 business (other than assets used in the ac-  
20 tive conduct of a trade or business de-  
21 scribed in section 542(c)(2)), the income of  
22 which is described in section 543(a) or in  
23 subparagraph (B), (C), (D), or (E) of sec-  
24 tion 954(c)(1) (determined by substituting

1                   ‘trade or business’ for ‘controlled foreign  
2                   corporation’).

3                   “(3) RULES REGARDING OWNERSHIP.—

4                   “(A) OWNERSHIP OF ENTITIES.—For pur-  
5                   poses of paragraph (1)(B)—

6                   “(i) CORPORATIONS.—Ownership of a  
7                   corporation shall be determined by the  
8                   holding of stock possessing the appropriate  
9                   percentage of the total combined voting  
10                  power of all classes of stock entitled to vote  
11                  and the appropriate percentage of the total  
12                  value of shares of all classes of stock.

13                  “(ii) PARTNERSHIPS.—Ownership of a  
14                  partnership shall be determined by the  
15                  owning of the appropriate percentage of  
16                  the capital interest in such partnership.

17                  “(B) OWNERSHIP OF TIERED ENTITIES.—  
18                  For purposes of this section, if by reason of  
19                  holding an interest in a trade or business, a de-  
20                  cedent, any member of the decedent’s family,  
21                  any qualified heir, or any member of any quali-  
22                  fied heir’s family is treated as holding an inter-  
23                  est in any other trade or business—

1           “(i) such ownership interest in the  
 2           other trade or business shall be dis-  
 3           regarded in determining if the ownership  
 4           interest in the first trade or business is a  
 5           qualified family-owned business interest,  
 6           and

7           “(ii) this section shall be applied sepa-  
 8           rately in determining if such interest in  
 9           any other trade or business is a qualified  
 10          family-owned business interest.

11          “(C) INDIVIDUAL OWNERSHIP RULES.—  
 12          For purposes of this section, an interest owned,  
 13          directly or indirectly, by or for an entity de-  
 14          scribed in paragraph (1)(B) shall be considered  
 15          as being owned proportionately by or for the en-  
 16          tity’s shareholders, partners, or beneficiaries. A  
 17          person shall be treated as a beneficiary of any  
 18          trust only if such person has a present interest  
 19          in such trust.

20          “(f) TAX TREATMENT OF FAILURE TO MATERIALLY  
 21          PARTICIPATE IN BUSINESS OR DISPOSITIONS OF INTER-  
 22          ESTS.—

23          “(1) IN GENERAL.—There is imposed an addi-  
 24          tional estate tax if, within 10 years after the date

1 of the decedent's death and before the date of the  
2 qualified heir's death—

3 “(A) the material participation require-  
4 ments described in section 2032A(c)(6)(B) are  
5 not met with respect to the qualified family-  
6 owned business interest which was acquired (or  
7 passed) from the decedent,

8 “(B) the qualified heir disposes of any por-  
9 tion of a qualified family-owned business inter-  
10 est (other than by a disposition to a member of  
11 the qualified heir's family or through a qualified  
12 conservation contribution under section  
13 170(h)),

14 “(C) the qualified heir loses United States  
15 citizenship (within the meaning of section 877)  
16 or with respect to whom an event described in  
17 subparagraph (A) or (B) of section 877(e)(1)  
18 occurs, and such heir does not comply with the  
19 requirements of subsection (g), or

20 “(D) the principal place of business of a  
21 trade or business of the qualified family-owned  
22 business interest ceases to be located in the  
23 United States.

24 “(2) ADDITIONAL ESTATE TAX.—

1           “(A) IN GENERAL.—The amount of the  
2 additional estate tax imposed by paragraph (1)  
3 shall be equal to—

4           “(i) the applicable percentage of the  
5 adjusted tax difference attributable to the  
6 qualified family-owned business interest  
7 (as determined under rules similar to the  
8 rules of section 2032A(c)(2)(B)), plus

9           “(ii) interest on the amount deter-  
10 mined under clause (i) at the underpay-  
11 ment rate established under section 6621  
12 for the period beginning on the date the  
13 estate tax liability was due under this  
14 chapter and ending on the date such addi-  
15 tional estate tax is due.

16           “(B) APPLICABLE PERCENTAGE.—For  
17 purposes of this paragraph, the applicable per-  
18 centage shall be determined under the following  
19 table:

<b>“If the event described in paragraph (1) occurs in the following year of material participation:</b>	<b>The applicable percentage is:</b>
1 through 6 .....	100
7 .....	80
8 .....	60
9 .....	40
10 .....	20.

20           “(g) SECURITY REQUIREMENTS FOR NONCITIZEN  
21 QUALIFIED HEIRS.—

1           “(1) IN GENERAL.—Except upon the applica-  
 2           tion of subparagraph (F) or (M) of subsection  
 3           (h)(3), if a qualified heir is not a citizen of the Unit-  
 4           ed States, any interest under this section passing to  
 5           or acquired by such heir (including any interest held  
 6           by such heir at a time described in subsection  
 7           (f)(1)(C)) shall be treated as a qualified family-  
 8           owned business interest only if the interest passes or  
 9           is acquired (or is held) in a qualified trust.

10           “(2) QUALIFIED TRUST.—The term ‘qualified  
 11           trust’ means a trust—

12                   “(A) which is organized under, and gov-  
 13                   erned by, the laws of the United States or a  
 14                   State, and

15                   “(B) except as otherwise provided in regu-  
 16                   lations, with respect to which the trust instru-  
 17                   ment requires that at least 1 trustee of the  
 18                   trust be an individual citizen of the United  
 19                   States or a domestic corporation.

20           “(h) OTHER DEFINITIONS AND APPLICABLE  
 21           RULES.—For purposes of this section—

22                   “(1) QUALIFIED HEIR.—The term ‘qualified  
 23                   heir’—

24                           “(A) has the meaning given to such term  
 25                           by section 2032A(e)(1), and



1           “(B) includes any active employee of the  
2           trade or business to which the qualified family-  
3           owned business interest relates if such employee  
4           has been employed by such trade or business  
5           for a period of at least 10 years before the date  
6           of the decedent’s death.

7           “(2) MEMBER OF THE FAMILY.—The term  
8           ‘member of the family’ has the meaning given to  
9           such term by section 2032A(e)(2).

10          “(3) APPLICABLE RULES.—Rules similar to the  
11          following rules shall apply:

12               “(A) Section 2032A(b)(4) (relating to de-  
13               cedents who are retired or disabled).

14               “(B) Section 2032A(b)(5) (relating to spe-  
15               cial rules for surviving spouses).

16               “(C) Section 2032A(c)(2)(D) (relating to  
17               partial dispositions).

18               “(D) Section 2032A(c)(3) (relating to only  
19               1 additional tax imposed with respect to any 1  
20               portion).

21               “(E) Section 2032A(c)(4) (relating to due  
22               date).

23               “(F) Section 2032A(c)(5) (relating to li-  
24               ability for tax; furnishing of bond).

1           “(G) Section 2032A(c)(7) (relating to no  
2           tax if use begins within 2 years; active manage-  
3           ment by eligible qualified heir treated as mate-  
4           rial participation).

5           “(H) Section 2032A(e)(10) (relating to  
6           community property).

7           “(I) Section 2032A(e)(14) (relating to  
8           treatment of replacement property acquired in  
9           section 1031 or 1033 transactions).

10          “(J) Section 2032A(f) (relating to statute  
11          of limitations).

12          “(K) Section 6166(b)(3) (relating to farm-  
13          houses and certain other structures taken into  
14          account).

15          “(L) Subparagraphs (B), (C), and (D) of  
16          section 6166(g)(1) (relating to acceleration of  
17          payment).

18          “(M) Section 6324B (relating to special  
19          lien for additional estate tax).

20          “(4) COORDINATION WITH OTHER ESTATE TAX  
21          BENEFITS.—If there is a reduction in the value of  
22          the gross estate under this section—

23                 “(A) the dollar limitation applicable under  
24                 section 2032A(a)(2), and

1                   “(B) the \$1,000,000 amount under section  
 2                   6601(j)(3) (as adjusted),  
 3           shall each be reduced (but not below zero) by the  
 4           amount of such reduction.”

5           (b) CLERICAL AMENDMENT.—The table of sections  
 6 for part III of subchapter A of chapter 11 is amended  
 7 by inserting after the item relating to section 2033 the  
 8 following new item:

                  “Sec. 2033A. Family-owned business exclusion.”

9           (c) EFFECTIVE DATE.—The amendments made by  
 10 this section shall apply to estates of decedents dying after  
 11 December 31, 1996.

12   **SEC. 303. 20-YEAR INSTALLMENT PAYMENT WHERE ESTATE**  
 13                   **CONSISTS LARGELY OF INTEREST IN CLOSE-**  
 14                   **LY HELD BUSINESS.**

15           (a) IN GENERAL.—Section 6166(a) (relating to ex-  
 16 tension of time for payment of estate tax where estate con-  
 17 sists largely of interest in closely held business) is amend-  
 18 ed by striking “10” in paragraph (1) and the heading  
 19 thereof and inserting “20”.

20           (b) EFFECTIVE DATE.—The amendments made by  
 21 this section shall apply to estates of decedents dying after  
 22 December 31, 1996.

1 **SEC. 304. NO INTEREST ON CERTAIN PORTION OF ESTATE**  
 2 **TAX EXTENDED UNDER 6166.**

3 (a) IN GENERAL.—Section 6601(j) (relating to 4-per-  
 4 cent rate on certain portion of estate tax extended under  
 5 section 6166) is amended—

6 (1) by striking the first sentence of paragraph  
 7 (1) and inserting the following new sentence: “If the  
 8 time for payment of an amount of tax imposed by  
 9 chapter 11 is extended as provided in section 6166,  
 10 no interest on the no-interest portion of such  
 11 amount shall (in lieu of the annual rate provided by  
 12 subsection (a)) be paid.”,

13 (2) by striking “4-percent” each place it ap-  
 14 pears in paragraphs (2) and (3) and inserting “no-  
 15 interest”,

16 (3) by striking “4-PERCENT” in the heading of  
 17 paragraph (2) and inserting “NO INTEREST”, and

18 (4) by striking “4-PERCENT RATE” in the  
 19 heading thereof and inserting “NO INTEREST”.

20 (b) CONFORMING AMENDMENTS.—

21 (1) Section 6166(b)(7)(A)(iii) is amended by  
 22 striking “4-percent rate of interest” and inserting  
 23 “no-interest portion”.

24 (2) Section 6166(b)(8)(A)(iii) is amended to  
 25 read as follows:

1 “(iii) NO-INTEREST PORTION NOT TO  
 2 APPLY.—Section 6601(j) (relating to no-in-  
 3 terest portion) shall not apply.”

4 (c) EFFECTIVE DATE.—The amendments made by  
 5 this section shall apply to estates of decedents dying after  
 6 December 31, 1996.

## 7 **TITLE IV—SAVINGS INCENTIVES**

### 8 **SEC. 401. RESTORATION OF IRA DEDUCTION.**

9 (a) MODIFICATIONS OF RESTRICTIONS ON ACTIVE  
 10 PARTICIPANTS.—Subparagraph (B) of section 219(g)(3)  
 11 (relating to applicable dollar amount) is amended to read  
 12 as follows:

13 “(B) APPLICABLE DOLLAR AMOUNT.—The  
 14 term ‘applicable dollar amount’ means the fol-  
 15 lowing:

16 “(i) In the case of a taxpayer filing a  
 17 joint return:

<b>“For taxable years beginning in:</b>	<b>The applicable dollar amount is:</b>
1997 .....	\$65,000
1998 .....	\$90,000
1999 .....	\$115,000
2000 .....	\$140,000.

18 “(ii) In the case of any other taxpayer  
 19 (other than a married individual filing a  
 20 separate return):

<b>“For taxable years beginning in:</b>	<b>The applicable dollar amount is:</b>
1997 .....	\$50,000
1998 .....	\$75,000

<b>“For taxable years beginning in:</b>	<b>The applicable dollar amount is:</b>
1999 .....	\$100,000
2000 .....	\$125,000.

1                               “(iii) In the case of a married individ-  
2                               ual filing a separate return, zero.”.

3               (b) REPEAL OF RESTRICTIONS ON ACTIVE PARTICI-  
4 PANTS.—

5               (1) IN GENERAL.—Section 219 (relating to de-  
6               duction for retirement savings), as amended by sec-  
7               tion 402, is amended by striking subsection (g) and  
8               by redesignating subsection (h) as subsection (g).

9               (2) TECHNICAL AND CONFORMING AMEND-  
10 MENTS.—

11               (A) Subsection (f) of section 219 is amend-  
12               ed by striking paragraph (7).

13               (B) Paragraph (5) of section 408(d) is  
14               amended by striking the last sentence.

15               (C) Section 408(o) is amended by adding  
16               at the end the following new paragraph:

17               “(5) TERMINATION.—This subsection shall not  
18               apply to any designated nondeductible contribution  
19               for any taxable year beginning after December 31,  
20               2000.”.

21               (D)       Sections       408A(c)(2)(A)       and  
22               4973(b)(2)(B)(ii), as added by section 403, are

1           each amended by striking “(computed without  
2           regard to subsection (g) of such section)”.

3           (c) COORDINATION OF IRA DEDUCTION LIMIT WITH  
4 ELECTIVE DEFERRAL LIMIT.—Section 219(b) (relating to  
5 maximum amount of deduction) is amended by adding at  
6 the end the following new paragraph:

7           “(5) COORDINATION WITH ELECTIVE DEFER-  
8 RAL LIMIT.—The amount determined under para-  
9 graph (1) with respect to any individual for any tax-  
10 able year shall not exceed the excess (if any) of—

11                   “(A) the limitation applicable for the tax-  
12 able year under section 402(g)(1), over

13                   “(B) the elective deferrals (as defined in  
14 section 402(g)(3)) of such individual for such  
15 taxable year.”.

16           (d) EFFECTIVE DATES.—

17           (1) IN GENERAL.—The amendments made by  
18 subsections (a) and (c) shall apply to taxable years  
19 beginning after December 31, 1996.

20           (2) TERMINATION.—The amendments made by  
21 subsection (b) shall apply to taxable years beginning  
22 after December 31, 2000.

1 **SEC. 402. IRA ALLOWED FOR SPOUSES WHO ARE NOT AC-**  
 2 **TIVE PLAN PARTICIPANTS.**

3 (a) IN GENERAL.—Section 219(g)(1) of the Internal  
 4 Revenue Code of 1986 is amended by striking “or the indi-  
 5 vidual’s spouse”.

6 (b) EFFECTIVE DATE.—The amendments made by  
 7 this section shall apply to taxable years beginning after  
 8 December 31, 1996.

9 **SEC. 403. ESTABLISHMENT OF NONDEDUCTIBLE TAX-FREE**  
 10 **INDIVIDUAL RETIREMENT ACCOUNTS.**

11 (a) IN GENERAL.—Subpart A of part I of subchapter  
 12 D of chapter 1 (relating to pension, profitsharing, stock  
 13 bonus plans, etc.) is amended by inserting after section  
 14 408 the following new section:

15 **“SEC. 408A. IRA PLUS ACCOUNTS.**

16 “(a) GENERAL RULE.—Except as provided in this  
 17 section, an IRA Plus account shall be treated for purposes  
 18 of this title in the same manner as an individual retire-  
 19 ment plan.

20 “(b) IRA PLUS ACCOUNT.—For purposes of this  
 21 title, the term ‘IRA Plus account’ means an individual re-  
 22 tirement plan (as defined in section 7701(a)(37)) which  
 23 is designated (in such manner as the Secretary may pre-  
 24 scribe) at the time of establishment of the plan as an IRA  
 25 Plus account.

26 “(c) TREATMENT OF CONTRIBUTIONS.—



1           “(1) NO DEDUCTION ALLOWED.—No deduction  
2           shall be allowed under section 219 for a contribution  
3           to an IRA Plus account.

4           “(2) CONTRIBUTION LIMIT.—The aggregate  
5           amount of contributions for any taxable year to all  
6           IRA Plus accounts maintained for the benefit of an  
7           individual shall not exceed the excess (if any) of—

8                   “(A) the maximum amount allowable as a  
9                   deduction under section 219 with respect to  
10                  such individual for such taxable year (computed  
11                  without regard to subsection (g) of such sec-  
12                  tion), over

13                   “(B) the amount so allowed.

14           “(3) CONTRIBUTIONS PERMITTED AFTER AGE  
15           70½.—Contributions to an IRA Plus account may be  
16           made even after the individual for whom the account  
17           is maintained has attained age 70½.

18           “(4) MANDATORY DISTRIBUTION RULES NOT  
19           TO APPLY, ETC.—

20                   “(A) IN GENERAL.—Except as provided in  
21                   subparagraph (B), subsections (a)(6) and (b)(3)  
22                   of section 408 (relating to required distribu-  
23                   tions) and section 4974 (relating to excise tax  
24                   on certain accumulations in qualified retirement  
25                   plans) shall not apply to any IRA Plus account.

1           “(B) POST-DEATH DISTRIBUTIONS.—Rules  
 2           similar to the rules of section 401(a)(9) (other  
 3           than subparagraph (A) thereof) shall apply for  
 4           purposes of this section.

5           “(5) ROLLOVER CONTRIBUTIONS.—

6           “(A) IN GENERAL.—No rollover contribu-  
 7           tion may be made to an IRA Plus account un-  
 8           less it is a qualified rollover contribution.

9           “(B) COORDINATION WITH LIMIT.—A  
 10          qualified rollover contribution shall not be taken  
 11          into account for purposes of paragraph (2).

12          “(6) TIME WHEN CONTRIBUTIONS MADE.—For  
 13          purposes of this section, the rule of section 219(f)(3)  
 14          shall apply.

15          “(d) DISTRIBUTION RULES.—For purposes of this  
 16          title—

17          “(1) GENERAL RULES.—

18               “(A) EXCLUSIONS FROM GROSS INCOME.—  
 19               Any qualified distribution from an IRA Plus ac-  
 20               count shall not be includible in gross income.

21               “(B) NONQUALIFIED DISTRIBUTIONS.—In  
 22               applying section 72 to any distribution from an  
 23               IRA Plus account which is not a qualified dis-  
 24               tribution, such distribution shall be treated as

made from contributions to the IRA Plus account to the extent that such distribution, when added to all previous distributions from the IRA Plus account, does not exceed the aggregate amount of contributions to the IRA Plus account. For purposes of the preceding sentence, all IRA Plus accounts maintained for the benefit of an individual shall be treated as 1 account.

“(C) EXCEPTION FROM PENALTY TAX.—Section 72(t) shall not apply to any qualified distribution from an IRA Plus account.

“(2) QUALIFIED DISTRIBUTION.—For purposes of this subsection—

“(A) IN GENERAL.—The term ‘qualified distribution’ means any payment or distribution—

“(i) made on or after the date on which the individual attains age 59½,

“(ii) made to a beneficiary (or to the estate of the individual) on or after the death of the individual,

“(iii) attributable to the individual’s being disabled (within the meaning of section 72(m)(7)), or

1 “(iv) which is a qualified special pur-  
2 pose distribution.

3 “(B) CERTAIN DISTRIBUTIONS WITHIN 5  
4 YEARS.—A payment or distribution shall not be  
5 treated as a qualified distribution under clause  
6 (i) of subparagraph (A) if—

7 “(i) it is made within the 5-taxable  
8 year period beginning with the 1st taxable  
9 year for which the individual made a con-  
10 tribution to an IRA Plus account (or such  
11 individual’s spouse made a contribution to  
12 an IRA Plus account) established for such  
13 individual, or

14 “(ii) in the case of a payment or dis-  
15 tribution properly allocable (as determined  
16 in the manner prescribed by the Secretary)  
17 to a qualified rollover contribution (or in-  
18 come allocable thereto), it is made within  
19 the 5-taxable year period beginning with  
20 the taxable year in which the rollover con-  
21 tribution was made.

22 Clause (ii) shall not apply to a qualified rollover  
23 contribution from an IRA plus account.

24 “(3) ROLLOVERS.—

1           “(A) IN GENERAL.—Paragraph (1) shall  
2           not apply to any distribution which is trans-  
3           ferred in a qualified rollover contribution to an  
4           IRA Plus account.

5           “(B) INCOME INCLUSION FOR ROLLOVERS  
6           FROM NON-PLUS IRAS.—In the case of any  
7           qualified rollover contribution from an individ-  
8           ual retirement plan (other than an IRA Plus  
9           account) to an IRA Plus account established for  
10          the benefit of the payee or distributee, as the  
11          case may be—

12               “(i) sections 72(t) and 408(d)(3) shall  
13               not apply, and

14               “(ii) in any case where such contribu-  
15               tion is made before January 1, 1999, any  
16               amount required to be included in gross in-  
17               come by reason of this paragraph shall be  
18               so included ratably over the 4-taxable year  
19               period beginning with the taxable year in  
20               which the payment or distribution is made.

21           “(C) ADDITIONAL REPORTING REQUIRE-  
22           MENTS.—The Secretary shall require that  
23           trustees of IRA Plus accounts, trustees of indi-  
24           vidual retirement plans, or both, whichever is

1 appropriate, shall include such additional infor-  
 2 mation in reports required under section 408(i)  
 3 as is necessary to ensure that amounts required  
 4 to be included in gross income under subpara-  
 5 graph (B) are so included.

6 “(4) QUALIFIED SPECIAL PURPOSE DISTRIBUTION.—For purposes of this section, the term ‘quali-  
 7 fied special purpose distribution’ means any distribu-  
 8 tion to which subparagraph (B), (D), (E), or (F) of  
 9 section 72(t)(2) applies.  
 10

11 “(e) QUALIFIED ROLLOVER CONTRIBUTION.—For  
 12 purposes of this section—

13 “(1) IN GENERAL.—The term ‘qualified rollover  
 14 contribution’ means a rollover contribution to an  
 15 IRA Plus account from another such account, or  
 16 from an individual retirement plan, but only if such  
 17 rollover contribution meets the requirements of sec-  
 18 tion 408(d)(3). For purposes of section  
 19 408(d)(3)(B), there shall be disregarded any quali-  
 20 fied rollover contribution from an individual retire-  
 21 ment plan to an IRA Plus account.

22 “(2) CONVERSIONS.—The conversion of an indi-  
 23 vidual retirement plan to an IRA Plus account shall  
 24 be treated as if it were a qualified rollover  
 25 contribution.”

1 (b) EXCESS DISTRIBUTIONS TAX NOT TO APPLY.—

2 (1) Subparagraph (A) of section 4980A(d)(3) is  
3 amended by inserting “(other than IRA Plus ac-  
4 counts described in section 408A(b))” after “retire-  
5 ment plans”.

6 (2) Section 4980A(e)(1) is amended by adding  
7 at the end the following flush sentence:

8 “Such term shall not include any amount distributed  
9 from an IRA Plus account or any qualified rollover  
10 contribution (as defined in section 408A(e)) from an  
11 individual retirement plan to an IRA Plus account.”

12 (c) EXCESS CONTRIBUTIONS.—Section 4973(b) is  
13 amended to read as follows:

14 “(b) EXCESS CONTRIBUTIONS.—For purposes of this  
15 section—

16 “(1) IN GENERAL.—In the case of individual re-  
17 tirement accounts or individual retirement annuities,  
18 the term ‘excess contributions’ means the sum of—

19 “(A) the amount determined under para-  
20 graph (2) for the taxable year, plus

21 “(B) the carryover amount determined  
22 under paragraph (3) for the taxable year.

23 “(2) CURRENT YEAR.—The amount determined  
24 under this paragraph for any taxable year is an  
25 amount equal to the sum of—

1 “(A) the excess (if any) of—

2 “(i) the amount contributed for the  
3 taxable year to the accounts or for the an-  
4 nuities or bonds (other than IRA Plus ac-  
5 counts), over

6 “(ii) the amount allowable as a deduc-  
7 tion under section 219 for the taxable  
8 year, plus

9 “(B) the excess (if any) of—

10 “(i) the amount described in clause (i)  
11 (taking into account contributions to IRA  
12 Plus accounts) contributed for the taxable  
13 year, over

14 “(ii) the amount allowable as a deduc-  
15 tion under section 219 for the taxable year  
16 (computed without regard to subsection (g)  
17 of such section).

18 “(3) CARRYOVER AMOUNT.—The carryover  
19 amount determined under this paragraph for any  
20 taxable year is the amount determined under para-  
21 graph (2) for the preceding taxable year, reduced by  
22 the sum of—

23 “(A) the distributions out of the account  
24 for the taxable year which were included in the



1 gross income of the payee under section  
2 408(d)(1),

3 “(B) the distributions out of the account  
4 for the taxable year to which section 408(d)(5)  
5 applies, and

6 “(C) the excess (if any) of the amount de-  
7 termined under paragraph (2)(B)(ii) over the  
8 amount determined under paragraph (2)(B)(i).

9 “(4) SPECIAL RULES.—For purposes of this  
10 subsection—

11 “(A) ROLLOVER CONTRIBUTIONS.—Roll-  
12 over distributions described in sections 402(c),  
13 403(a)(4), 403(b)(8), 408(d)(3), and 408A(e)  
14 shall not be taken into account.

15 “(B) CONTRIBUTIONS RETURNED BEFORE  
16 DUE DATE.—Any contribution which is distrib-  
17 uted from an individual retirement plan in a  
18 distribution to which section 408(d)(4) applies  
19 shall not be taken into account.

20 “(C) EXCESS CONTRIBUTIONS TREATED AS  
21 CONTRIBUTIONS.—In applying paragraph  
22 (3)(C), the determination as to amounts con-  
23 tributed for a taxable year shall be made with-  
24 out regard to section 219(f)(6).”

1 (d) SPOUSAL IRA.—Clause (ii) of section  
2 219(c)(1)(B) is amended to read as follows:

3 “(ii) the compensation includible in  
4 the gross income of such individual’s  
5 spouse for the taxable year reduced by—

6 “(I) the amount allowed as a de-  
7 duction under subsection (a) to such  
8 spouse for such taxable year, and

9 “(II) the amount of any contribu-  
10 tion on behalf of such spouse to an  
11 IRA Plus account under section 408A  
12 for such taxable year.”

13 (e) CONFORMING AMENDMENT.—The table of sec-  
14 tions for subpart A of part I of subchapter D of chapter  
15 1 is amended by inserting after the item relating to section  
16 408 the following new item:

“Sec. 408A. IRA Plus accounts.”

17 (f) EFFECTIVE DATE.—The amendments made by  
18 this section shall apply to taxable years beginning after  
19 December 31, 1996.

20 **SEC. 404. TAX-FREE WITHDRAWALS FROM INDIVIDUAL RE-**  
21 **TIREMENT PLANS FOR BUSINESS STARTUPS.**

22 (a) EXCLUSION.—Section 408(d) is amended by add-  
23 ing at the end the following new paragraph:

24 “(8) DISTRIBUTIONS USED FOR BUSINESS  
25 START-UP EXPENSES.—

“(A) IN GENERAL.—Paragraph (1) shall not apply to any payments or distributions from an individual retirement plan during any taxable year to the extent the aggregate amount of such payments and distributions does not exceed the business start-up costs of the taxpayer for the taxable year.

“(B) BUSINESS START-UP COSTS.—For purposes of this paragraph—

“(i) IN GENERAL.—The term ‘business start-up costs’ means any amount which is paid or incurred—

“(I) in connection with a trade or business with respect to which the taxpayer is a 50-percent owner, and

“(II) on or before the date which is one year after the date on which the active conduct of such trade or business began (as determined under section 195(c)).

“(ii) CERTAIN COSTS INCLUDED.—The term ‘business start-up costs’ shall include—

“(I) any start-up expenditures (as defined in section 195(c)), and

1                   “(II) any organizational expenses  
2                   (as defined in section 709(b)).

3                   “(C) DENIAL OF DOUBLE BENEFIT.—

4                   “(i) DEDUCTIONS.—No deduction  
5                   otherwise allowable under this chapter with  
6                   respect to any business start-up costs  
7                   taken into account under subparagraph  
8                   (A) shall be allowed to the extent of the  
9                   amount which would have been includible  
10                  in gross income but for the application of  
11                  this paragraph.

12                  “(ii) BASIS REDUCTIONS.—If any por-  
13                  tion of the business start-up costs taken  
14                  into account under subparagraph (A) are  
15                  properly chargeable to capital account, the  
16                  basis of the property to which such costs  
17                  are chargeable shall be reduced by the  
18                  amount which would have been includible  
19                  in gross income but for the application of  
20                  this paragraph.

21                  “(iii) ALLOCATION.—The Secretary  
22                  shall provide rules for the allocation of  
23                  amounts excluded from gross income by  
24                  reason of this paragraph to business start-

1 up costs for purposes for applying this  
 2 subparagraph.

3 “(D) 50-PERCENT OWNER.—For purposes  
 4 of clause (i), the term ‘50-percent owner’ means  
 5 any individual if the individual—

6 “(i) in the case of a corporation, own  
 7 more than 50 percent of the value of the  
 8 outstanding stock of the corporation or  
 9 stock possessing more than 50 percent of  
 10 the total combined voting power of all  
 11 stock of the corporation, or

12 “(ii) in the case of a trade or business  
 13 other than a corporation, own more than  
 14 50 percent of the capital or profits interest  
 15 in the trade or business.

16 For purposes of this subparagraph, an individ-  
 17 ual shall be treated as owning stock and capital  
 18 or profits interests owned by the individual’s  
 19 spouse.”

20 (b) EXEMPTION FROM ADDITIONAL TAX.—

21 (1) IN GENERAL.—Section 72(t)(2) is amended  
 22 by adding at the end the following new subpara-  
 23 graph:

24 “(E) DISTRIBUTIONS USED FOR BUSINESS  
 25 START-UP EXPENSES.—Distributions from an

1 individual retirement plan to the extent such  
 2 distributions do not exceed the business start-  
 3 up costs (as defined in section 408(d)(8)) of the  
 4 taxpayer for the taxable year.”

5 (2) CONFORMING AMENDMENT.—Section  
 6 72(t)(2)(B) is amended by striking “(C) or (D)”  
 7 and inserting “(C), (D), or (E)”.

8 (c) EXEMPTION FROM PROHIBITED TRANSACTION.—  
 9 Section 4975(d) is amended by striking “or” at the end  
 10 of paragraph (14), by striking the period at the end of  
 11 paragraph (15) and inserting “; or”, and by adding after  
 12 paragraph (15) the following new paragraph:

13 “(16) any distribution from an individual retire-  
 14 ment plan which is used for the payment of any  
 15 business start-up costs (as defined in section  
 16 408(d)(8)) of the distributee.”

17 (d) EFFECTIVE DATE.—The amendments made by  
 18 this section shall apply to distributions after December 31,  
 19 1996.

20 **SEC. 405. TAX-FREE WITHDRAWALS FROM INDIVIDUAL RE-**  
 21 **TIREMENT PLANS FOR LONG-TERM UNEM-**  
 22 **PLOYED.**

23 (a) EXCLUSION.—Section 408(d), as amended by sec-  
 24 tion 404, is amended by adding at the end the following  
 25 new paragraph:

1           “(9) DISTRIBUTIONS TO LONG-TERM UNEM-  
2       PLOYED.—

3           “(A) IN GENERAL.—Paragraph (1) shall  
4       not apply to any payments or distributions from  
5       an individual retirement plan during any tax-  
6       able year to an individual if—

7           “(i) such individual has received un-  
8       employment compensation for 12 consecu-  
9       tive weeks under any Federal or State un-  
10      employment compensation law by reason of  
11      such separation, and

12          “(ii) such payments and distributions  
13      are made during the taxable year in which  
14      such unemployment compensation was paid  
15      or the succeeding taxable year.

16          “(B) DISTRIBUTIONS AFTER REEMPLOY-  
17      MENT.—Subparagraph (A) shall not apply to  
18      any distribution or payment made after the in-  
19      dividual has been employed for at least 60 days  
20      after the separation from employment to which  
21      subparagraph (A) applies.

22          “(C) SELF-EMPLOYED INDIVIDUALS.—To  
23      the extent provided in regulations, a self-em-  
24      ployed individual shall be treated as meeting  
25      the requirements of subparagraph (A)(i) if,

1 under Federal or State law, the individual  
 2 would have received unemployment compensa-  
 3 tion but for the fact the individual was self-em-  
 4 ployed.”

5 (b) EXEMPTION FROM ADDITIONAL TAX.—Section  
 6 72(t)(2)(D) is amended to read as follows:

7 “(D) DISTRIBUTIONS TO UNEMPLOYED IN-  
 8 DIVIDUALS.—Distributions from an individual  
 9 retirement plan which are described in section  
 10 408(d)(9).”

11 (c) EFFECTIVE DATE.—The amendments made by  
 12 this section shall apply to distributions after December 31,  
 13 1996.

14 **SEC. 406. DISTRIBUTIONS FROM CERTAIN PLANS MAY BE**  
 15 **USED WITHOUT PENALTY TO PAY HIGHER**  
 16 **EDUCATION EXPENSES.**

17 (a) EXCLUSION.—Section 408(d), as amended by sec-  
 18 tions 404 and 405, is amended by adding at the end the  
 19 following new paragraph:

20 “(10) DISTRIBUTIONS USED FOR QUALIFIED  
 21 HIGHER EDUCATION EXPENSES.—

22 “(A) IN GENERAL.—Paragraph (1) shall  
 23 not apply to any payments or distributions from  
 24 an individual retirement plan during any tax-  
 25 able year to the extent the aggregate amount of



1 such payments and distributions does not ex-  
2 ceed the qualified higher education expenses of  
3 the taxpayer for the taxable year.

4 “(B) QUALIFIED HIGHER EDUCATION EX-  
5 PENSES.—For purposes of subparagraph (A)—

6 “(i) IN GENERAL.—The term ‘quali-  
7 fied higher education expenses’ means the  
8 cost of attendance (within the meaning of  
9 section 472 of the Higher Education Act  
10 of 1965 (20 U.S.C. 1087ll)) of—

11 “(I) the taxpayer,

12 “(II) the taxpayer’s spouse, or

13 “(III) any child (as defined in  
14 section 151(c)(3)), grandchild, or an-  
15 cestor of the taxpayer or the tax-  
16 payer’s spouse,  
17 at an eligible educational institution (as  
18 defined in section 135(c)(3)).

19 “(ii) COORDINATION WITH OTHER  
20 PROVISIONS.—The amount of qualified  
21 higher education expenses for any taxable  
22 year shall be reduced by—

23 “(I) any amount excludable from  
24 gross income under section 135, and

1 “(II) any amount described in  
 2 section 135(d)(1) (relating to certain  
 3 scholarships and veterans benefits).”

4 (b) EXEMPTION FROM ADDITIONAL TAX.—

5 (1) IN GENERAL.—Paragraph (2) of section  
 6 72(t) (relating to exceptions to 10-percent additional  
 7 tax on early distributions from qualified retirement  
 8 plans), as amended by section 402, is amended by  
 9 adding at the end the following new subparagraph:

10 “(F) DISTRIBUTIONS FROM INDIVIDUAL  
 11 RETIREMENT PLANS FOR EDUCATIONAL EX-  
 12 PENSES.—Distributions to an individual from  
 13 an individual retirement plan to the extent such  
 14 distributions do not exceed the qualified higher  
 15 education expenses (as defined in section  
 16 408(d)(10)(B)) of the taxpayer for the taxable  
 17 year.”

18 (2) CONFORMING AMENDMENT.—Section  
 19 72(t)(2)(B), as amended by section 402, is amended  
 20 by striking “or (E)” and inserting “, (E), or (F)”.

21 (c) EFFECTIVE DATE.—The amendments made by  
 22 this section shall apply to taxable years beginning after  
 23 December 31, 1996.

○