

105TH CONGRESS
1ST SESSION

S. 843

To amend the Internal Revenue Code of 1986 to simplify certain rules relating to the taxation of United States business operating abroad, and for other purposes.

IN THE SENATE OF THE UNITED STATES

JUNE 5, 1997

Mr. HATCH (for himself, Mr. BAUCUS, and Mr. MACK) introduced the following bill; which was read twice and referred to the Committee on Finance

A BILL

To amend the Internal Revenue Code of 1986 to simplify certain rules relating to the taxation of United States business operating abroad, 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 “International Tax Simplification for American Competi-
7 tiveness Act”.

8 (b) AMENDMENT OF 1986 CODE.—Except as other-
9 wise expressly provided, whenever in this Act an amend-

1 ment or repeal is expressed in terms of an amendment
 2 to, or repeal of, a section or other provision, the reference
 3 shall be considered to be made to a section or other provi-
 4 sion of the Internal Revenue Code of 1986.

5 (c) TABLE OF CONTENTS.—The table of contents for
 6 this Act is as follows:

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

TITLE I—TREATMENT OF PASSIVE FOREIGN INVESTMENT COMPANIES

Sec. 101. United States shareholders of controlled foreign corporations not sub-
 ject to PFIC inclusion.

Sec. 102. Election of mark to market for marketable stock in passive foreign
 investment company.

Sec. 103. Modification to definition of passive income.

Sec. 104. Effective date.

TITLE II—TREATMENT OF CONTROLLED FOREIGN CORPORATIONS

Sec. 201. Gain on certain stock sales by controlled foreign corporations treated
 as dividends.

Sec. 202. Miscellaneous modifications to subpart F.

Sec. 203. Indirect foreign tax credit allowed for certain lower tier companies.

Sec. 204. Exemption for active financing income.

Sec. 205. Application of separate foreign tax credit limitation for noncontrolled
 section 902 corporations.

Sec. 206. Study of proper treatment of European Union under same country
 exceptions.

Sec. 207. Expansion of de minimis rule under subpart F.

Sec. 208. Subpart F earnings and profits determined under generally accepted
 accounting principles.

Sec. 209. Clarification of treatment of pipeline transportation income.

Sec. 210. Deduction for dividends received from certain foreign corporations.

TITLE III—OTHER PROVISIONS

Sec. 301. Exchange rate used in translating foreign taxes.

Sec. 302. Election to use simplified section 904 limitation for alternative mini-
 mum tax.

Sec. 303. Modification of section 1491.

Sec. 304. Modification of section 367(b).

Sec. 305. Increase in filing thresholds for returns as to organization of foreign
 corporations and acquisitions of stock in such corporations.

Sec. 306. Application of uniform capitalization rules to foreign persons.

Sec. 307. Extension of period to which excess foreign taxes may be carried.

Sec. 308. Recharacterization of overall domestic loss.

Sec. 309. Treatment of foreign sales corporations.

Sec. 310. Special rules relating to financial services income.

Sec. 311. United States property not to include certain assets acquired by dealers in ordinary course of trade or business.

Sec. 312. Treatment of certain dividends of regulated investment companies.

Sec. 313. Intangible property not to include certain preliminary agreements.

Sec. 314. Study of interest allocation.

1 TITLE I—TREATMENT OF PAS- **2 SIVE FOREIGN INVESTMENT** **3 COMPANIES**

4 SEC. 101. UNITED STATES SHAREHOLDERS OF CON- **5 TROLLED FOREIGN CORPORATIONS NOT** **6 SUBJECT TO PFIC INCLUSION.**

7 Section 1297, as redesignated by section 102, is
8 amended by adding at the end the following new
9 subsection:

10 “(e) EXCEPTION FOR UNITED STATES SHAREHOLD-
11 ERS OF CONTROLLED FOREIGN CORPORATIONS.—

12 “(1) IN GENERAL.—For purposes of this part,
13 a corporation shall not be treated with respect to a
14 shareholder as a passive foreign investment company
15 during the qualified portion of such shareholder’s
16 holding period with respect to stock in such
17 corporation.

18 “(2) QUALIFIED PORTION.—For purposes of
19 this subsection, the term ‘qualified portion’ means
20 the portion of the shareholder’s holding period—

21 “(A) which is after December 31, 1997,
22 and

1 “(B) during which the shareholder is a
2 United States shareholder (as defined in section
3 951(b)) of the corporation and the corporation
4 is a controlled foreign corporation.

5 “(3) NEW HOLDING PERIOD IF QUALIFIED
6 PORTION ENDS.—

7 “(A) IN GENERAL.—Except as provided in
8 subparagraph (B), if the qualified portion of a
9 shareholder’s holding period with respect to any
10 stock ends after December 31, 1997, solely for
11 purposes of this part, the shareholder’s holding
12 period with respect to such stock shall be treat-
13 ed as beginning as of the first day following
14 such period.

15 “(B) EXCEPTION.—Subparagraph (A)
16 shall not apply if such stock was, with respect
17 to such shareholder, stock in a passive foreign
18 investment company at any time before the
19 qualified portion of the shareholder’s holding
20 period with respect to such stock and no elec-
21 tion under section 1298(b)(1) is made.”

1 **SEC. 102. ELECTION OF MARK TO MARKET FOR MARKET-**
 2 **ABLE STOCK IN PASSIVE FOREIGN INVEST-**
 3 **MENT COMPANY.**

4 (a) IN GENERAL.—Part VI of subchapter P of chap-
 5 ter 1 is amended by redesignating subpart C as subpart
 6 D, by redesignating sections 1296 and 1297 as sections
 7 1297 and 1298, respectively, and by inserting after sub-
 8 part B the following new subpart:

9 **“Subpart C—Election of Mark to Market for**
 10 **Marketable Stock**

“Sec. 1296. Election of mark to market for marketable stock.

11 **“SEC. 1296. ELECTION OF MARK TO MARKET FOR**
 12 **MARKETABLE STOCK.**

13 “(a) GENERAL RULE.—In the case of marketable
 14 stock in a passive foreign investment company which is
 15 owned (or treated under subsection (g) as owned) by a
 16 United States person at the close of any taxable year of
 17 such person, at the election of such person—

18 “(1) If the fair market value of such stock as
 19 of the close of such taxable year exceeds its adjusted
 20 basis, such United States person shall include in
 21 gross income for such taxable year an amount equal
 22 to the amount of such excess.

23 “(2) If the adjusted basis of such stock exceeds
 24 the fair market value of such stock as of the close

1 of such taxable year, such United States person
 2 shall be allowed a deduction for such taxable year
 3 equal to the lesser of—

4 “(A) the amount of such excess, or

5 “(B) the unreversed inclusions with respect
 6 to such stock.

7 “(b) BASIS ADJUSTMENTS.—

8 “(1) IN GENERAL.—The adjusted basis of stock
 9 in a passive foreign investment company—

10 “(A) shall be increased by the amount in-
 11 cluded in the gross income of the United States
 12 person under subsection (a)(1) with respect to
 13 such stock, and

14 “(B) shall be decreased by the amount al-
 15 lowed as a deduction to the United States per-
 16 son under subsection (a)(2) with respect to
 17 such stock.

18 “(2) SPECIAL RULE FOR STOCK CONSTRUC-
 19 TIVELY OWNED.—In the case of stock in a passive
 20 foreign investment company which the United States
 21 person is treated as owning under subsection (g)—

22 “(A) the adjustments under paragraph (1)
 23 shall apply to such stock in the hands of the
 24 person actually holding such stock but only for
 25 purposes of determining the subsequent treat-

ment under this chapter of the United States person with respect to such stock, and

“(B) similar adjustments shall be made to the adjusted basis of the property by reason of which the United States person is treated as owning such stock.

“(c) CHARACTER AND SOURCE RULES.—

“(1) ORDINARY TREATMENT.—

“(A) GAIN.—Any amount included in gross income under subsection (a)(1), and any gain on the sale or other disposition of marketable stock in a passive foreign investment company (with respect to which an election under this section is in effect), shall be treated as ordinary income.

“(B) LOSS.—Any—

“(i) amount allowed as a deduction under subsection (a)(2), and

“(ii) loss on the sale or other disposition of marketable stock in a passive foreign investment company (with respect to which an election under this section is in effect) to the extent that the amount of such loss does not exceed the unreversed inclusions with respect to such stock,

1 shall be treated as an ordinary loss. The
2 amount so treated shall be treated as a deduc-
3 tion allowable in computing adjusted gross
4 income.

5 “(2) SOURCE.—The source of any amount in-
6 cluded in gross income under subsection (a)(1) (or
7 allowed as a deduction under subsection (a)(2)) shall
8 be determined in the same manner as if such
9 amount were gain or loss (as the case may be) from
10 the sale of stock in the passive foreign investment
11 company.

12 “(d) UNREVERSED INCLUSIONS.—For purposes of
13 this section, the term ‘unreversed inclusions’ means, with
14 respect to any stock in a passive foreign investment com-
15 pany, the excess (if any) of—

16 “(1) the amount included in gross income of
17 the taxpayer under subsection (a)(1) with respect to
18 such stock for prior taxable years, over

19 “(2) the amount allowed as a deduction under
20 subsection (a)(2) with respect to such stock for prior
21 taxable years.

22 The amount referred to in paragraph (1) shall include any
23 amount which would have been included in gross income
24 under subsection (a)(1) with respect to such stock for any
25 prior taxable year but for section 1291.

1 “(e) MARKETABLE STOCK.—For purposes of this
2 section—

3 “(1) IN GENERAL.—The term ‘marketable
4 stock’ means—

5 “(A) any stock which is regularly traded
6 on—

7 “(i) a national securities exchange
8 which is registered with the Securities and
9 Exchange Commission or the national mar-
10 ket system established pursuant to section
11 11A of the Securities and Exchange Act of
12 1934, or

13 “(ii) any exchange or other market
14 which the Secretary determines has rules
15 adequate to carry out the purposes of this
16 part,

17 “(B) to the extent provided in regulations,
18 stock in any foreign corporation which is com-
19 parable to a regulated investment company and
20 which offers for sale or has outstanding any
21 stock of which it is the issuer and which is re-
22 deemable at its net asset value, and

23 “(C) to the extent provided in regulations,
24 any option on stock described in subparagraph
25 (A) or (B).

1 “(2) SPECIAL RULE FOR REGULATED INVEST-
 2 MENT COMPANIES.—In the case of any regulated in-
 3 vestment company which is offering for sale or has
 4 outstanding any stock of which it is the issuer and
 5 which is redeemable at its net asset value, all stock
 6 in a passive foreign investment company which it
 7 owns directly or indirectly shall be treated as mar-
 8 ketable stock for purposes of this section. Except as
 9 provided in regulations, similar treatment as mar-
 10 ketable stock shall apply in the case of any other
 11 regulated investment company which publishes net
 12 asset valuations at least annually.

13 “(f) TREATMENT OF CONTROLLED FOREIGN COR-
 14 PORATIONS WHICH ARE SHAREHOLDERS IN PASSIVE
 15 FOREIGN INVESTMENT COMPANIES.—In the case of a for-
 16 eign corporation which is a controlled foreign corporation
 17 and which owns (or is treated under subsection (g) as own-
 18 ing) stock in a passive foreign investment company—

19 “(1) this section (other than subsection (c)(2))
 20 shall apply to such foreign corporation in the same
 21 manner as if such corporation were a United States
 22 person, and

23 “(2) for purposes of subpart F of part III of
 24 subchapter N—

1 “(A) any amount included in gross income
 2 under subsection (a)(1) shall be treated as for-
 3 eign personal holding company income de-
 4 scribed in section 954(c)(1)(A), and

5 “(B) any amount allowed as a deduction
 6 under subsection (a)(2) shall be treated as a de-
 7 duction allocable to foreign personal holding
 8 company income so described.

9 “(g) STOCK OWNED THROUGH CERTAIN FOREIGN
 10 ENTITIES.—Except as provided in regulations—

11 “(1) IN GENERAL.—For purposes of this sec-
 12 tion, stock owned, directly or indirectly, by or for a
 13 foreign partnership or foreign trust or foreign estate
 14 shall be considered as being owned proportionately
 15 by its partners or beneficiaries. Stock considered to
 16 be owned by a person by reason of the application
 17 of the preceding sentence shall, for purposes of ap-
 18 plying such sentence, be treated as actually owned
 19 by such person.

20 “(2) TREATMENT OF CERTAIN DISPOSITIONS.—
 21 In any case in which a United States person is
 22 treated as owning stock in a passive foreign invest-
 23 ment company by reason of paragraph (1)—

24 “(A) any disposition by the United States
 25 person or by any other person which results in

1 the United States person being treated as no
2 longer owning such stock, and

3 “(B) any disposition by the person owning
4 such stock,

5 shall be treated as a disposition by the United
6 States person of the stock in the passive foreign in-
7 vestment company.

8 “(h) COORDINATION WITH SECTION 851(b).—For
9 purposes of paragraphs (2) and (3) of section 851(b), any
10 amount included in gross income under subsection (a)
11 shall be treated as a dividend.

12 “(i) STOCK ACQUIRED FROM A DECEDENT.—In the
13 case of stock of a passive foreign investment company
14 which is acquired by bequest, devise, or inheritance (or
15 by the decedent’s estate) and with respect to which an
16 election under this section was in effect as of the date of
17 the decedent’s death, notwithstanding section 1014, the
18 basis of such stock in the hands of the person so acquiring
19 it shall be the adjusted basis of such stock in the hands
20 of the decedent immediately before his death (or, if lesser,
21 the basis which would have been determined under section
22 1014 without regard to this subsection).

23 “(j) COORDINATION WITH SECTION 1291 FOR FIRST
24 YEAR OF ELECTION.—

1 “(1) TAXPAYERS OTHER THAN REGULATED
2 INVESTMENT COMPANIES.—

3 “(A) IN GENERAL.—If the taxpayer elects
4 the application of this section with respect to
5 any marketable stock in a corporation after the
6 beginning of the taxpayer’s holding period in
7 such stock, and if the requirements of subpara-
8 graph (B) are not satisfied, section 1291 shall
9 apply to—

10 “(i) any distributions with respect to,
11 or disposition of, such stock in the first
12 taxable year of the taxpayer for which such
13 election is made, and

14 “(ii) any amount which, but for sec-
15 tion 1291, would have been included in
16 gross income under subsection (a) with re-
17 spect to such stock for such taxable year in
18 the same manner as if such amount were
19 gain on the disposition of such stock.

20 “(B) REQUIREMENTS.—The requirements
21 of this subparagraph are met if, with respect to
22 each of such corporation’s taxable years for
23 which such corporation was a passive foreign
24 investment company and which begin after De-
25 cember 31, 1986, and included any portion of

1 the taxpayer's holding period in such stock,
 2 such corporation was treated as a qualified
 3 electing fund under this part with respect to the
 4 taxpayer.

5 “(2) SPECIAL RULES FOR REGULATED INVEST-
 6 MENT COMPANIES.—

7 “(A) IN GENERAL.—If a regulated invest-
 8 ment company elects the application of this sec-
 9 tion with respect to any marketable stock in a
 10 corporation after the beginning of the tax-
 11 payer's holding period in such stock, then, with
 12 respect to such company's first taxable year for
 13 which such company elects the application of
 14 this section with respect to such stock—

15 “(i) section 1291 shall not apply to
 16 such stock with respect to any distribution
 17 or disposition during, or amount included
 18 in gross income under this section for,
 19 such first taxable year, but

20 “(ii) such regulated investment com-
 21 pany's tax under this chapter for such first
 22 taxable year shall be increased by the ag-
 23 gregate amount of interest which would
 24 have been determined under section

1 1291(c)(3) if section 1291 were applied
2 without regard to this subparagraph.

3 Clause (ii) shall not apply if for the preceding
4 taxable year the company elected to mark to
5 market the stock held by such company as of
6 the last day of such preceding taxable year.

7 “(B) DISALLOWANCE OF DEDUCTION.—No
8 deduction shall be allowed to any regulated in-
9 vestment company for the increase in tax under
10 subparagraph (A)(ii).

11 “(k) ELECTION.—This section shall apply to market-
12 able stock in a passive foreign investment company which
13 is held by a United States person only if such person elects
14 to apply this section with respect to such stock. Such an
15 election shall apply to the taxable year for which made
16 and all subsequent taxable years unless—

17 “(1) such stock ceases to be marketable stock,
18 or

19 “(2) the Secretary consents to the revocation of
20 such election.

21 “(l) TRANSITION RULE FOR INDIVIDUALS BECOMING
22 SUBJECT TO UNITED STATES TAX.—If any individual be-
23 comes a United States person in a taxable year beginning
24 after December 31, 1997, solely for purposes of this sec-
25 tion, the adjusted basis (before adjustments under sub-

1 section (b)) of any marketable stock in a passive foreign
 2 investment company owned by such individual on the first
 3 day of such taxable year shall be treated as being the
 4 greater of its fair market value on such first day or its
 5 adjusted basis on such first day.”

6 (b) COORDINATION WITH INTEREST CHARGE,
 7 ETC.—

8 (1) Paragraph (1) of section 1291(d) is amend-
 9 ed by adding at the end the following new flush
 10 sentence:

11 “Except as provided in section 1296(j), this section
 12 also shall not apply if an election under section
 13 1296(k) is in effect for the taxpayer’s taxable year.”

14 (2) The subsection heading for subsection (d) of
 15 section 1291 is amended by striking “SUBPART B”
 16 and inserting “SUBPARTS B AND C”.

17 (3) Subparagraph (A) of section 1291(a)(3) is
 18 amended to read as follows:

19 “(A) HOLDING PERIOD.—The taxpayer’s
 20 holding period shall be determined under sec-
 21 tion 1223; except that—

22 “(i) for purposes of applying this sec-
 23 tion to an excess distribution, such holding
 24 period shall be treated as ending on the
 25 date of such distribution, and

1 “(ii) if section 1296 applied to such
 2 stock with respect to the taxpayer for any
 3 prior taxable year, such holding period
 4 shall be treated as beginning on the first
 5 day of the first taxable year beginning
 6 after the last taxable year for which sec-
 7 tion 1296 so applied.”

8 (c) TREATMENT OF MARK-TO-MARKET GAIN UNDER
 9 SECTION 4982.—

10 (1) Subsection (e) of section 4982 is amended
 11 by adding at the end the following new paragraph:

12 “(6) TREATMENT OF GAIN RECOGNIZED UNDER
 13 SECTION 1296.—For purposes of determining a regu-
 14 lated investment company’s ordinary income—

15 “(A) notwithstanding paragraph (1)(C),
 16 section 1296 shall be applied as if such compa-
 17 ny’s taxable year ended on October 31, and

18 “(B) any ordinary gain or loss from an ac-
 19 tual disposition of stock in a passive foreign in-
 20 vestment company during the portion of the
 21 taxable year after October 31 shall be taken
 22 into account in determining such company’s or-
 23 dinary income for the following taxable year.

24 This paragraph shall not apply to a company mak-
 25 ing an election under paragraph (4).”

1 (2) Subsection (b) of section 852 is amended by
2 adding at the end the following new paragraph:

3 “(10) SPECIAL RULE FOR CERTAIN LOSSES ON
4 STOCK IN PASSIVE FOREIGN INVESTMENT COMPA-
5 NIES.—To the extent provided in regulations, the
6 taxable income of a regulated investment company
7 (other than a company to which an election under
8 section 4982(e)(4) applies) shall be computed with-
9 out regard to any net reduction in the value of any
10 stock with respect to which an election under section
11 1296(k) is in effect occurring after October 31 of
12 the taxable year, and any such reduction shall be
13 treated as occurring on the first day of the following
14 taxable year.”

15 (3) Subsection (c)(2) of section 852 is amended
16 by inserting “, without regard to any net reduction
17 in the value of any stock of a passive foreign invest-
18 ment company with respect to which an election
19 under section 1296(k) is in effect occurring after
20 October 31 of such year,” after “October 31 of such
21 year”.

22 (d) CONFORMING AMENDMENTS.—

23 (1) Sections 532(b)(4) and 542(c)(10) are each
24 amended by striking “section 1296” and inserting
25 “section 1297”.

1 (2) Subsection (f) of section 551 is amended by
2 striking “section 1297(b)(5)” and inserting “section
3 1298(b)(5)”

4 (3) Subsections (a)(1) and (d) of section 1293
5 are each amended by striking “section 1297(a)” and
6 inserting “section 1298(a)”.

7 (4) Paragraph (3) of section 1297(b), as redes-
8 ignated by subsection (a), is hereby repealed.

9 (5) The table of sections for subpart D of part
10 VI of subchapter P of chapter 1, as redesignated by
11 subsection (a), is amended to read as follows:

 “Sec. 1297. Passive foreign investment company.
 “Sec. 1298. Special rules.”

12 (6) The table of subparts for part VI of sub-
13 chapter P of chapter 1 is amended by striking the
14 last item and inserting the following new items:

 “Subpart C. Election of mark to market for marketable stock.
 “Subpart D. General provisions.”

15 (e) CLARIFICATION OF GAIN RECOGNITION ELEC-
16 TION.—The last sentence of section 1298(b)(1), as so re-
17 designated, is amended by inserting “(determined without
18 regard to the preceding sentence)” after “investment
19 company”.

20 **SEC. 103. MODIFICATION TO DEFINITION OF PASSIVE**
21 **INCOME.**

22 Paragraph (1) of section 1297(b) (defining passive
23 income), as redesignated by section 102, is amended by

1 inserting before the period “without regard to paragraph
2 (3) thereof”.

3 **SEC. 104. EFFECTIVE DATE.**

4 The amendments made by this title shall apply to—

5 (1) taxable years of United States persons be-
6 ginning after December 31, 1997, and

7 (2) taxable years of foreign corporations ending
8 with or within such taxable years of United States
9 persons.

10 **TITLE II—TREATMENT OF CON-**
11 **TROLLED FOREIGN COR-**
12 **PORATIONS**

13 **SEC. 201. GAIN ON CERTAIN STOCK SALES BY CONTROLLED**
14 **FOREIGN CORPORATIONS TREATED AS**
15 **DIVIDENDS.**

16 (a) GENERAL RULE.—Section 964 (relating to mis-
17 cellaneous provisions) is amended by adding at the end
18 the following new subsection:

19 “(e) GAIN ON CERTAIN STOCK SALES BY CON-
20 TROLLED FOREIGN CORPORATIONS TREATED AS
21 DIVIDENDS.—

22 “(1) IN GENERAL.—If a controlled foreign cor-
23 poration sells or exchanges stock in any other for-
24 eign corporation, gain recognized on such sale or ex-
25 change shall be included in the gross income of such

1 controlled foreign corporation as a dividend to the
 2 same extent that it would have been so included
 3 under section 1248(a) if such controlled foreign cor-
 4 poration were a United States person. For purposes
 5 of determining the amount which would have been so
 6 includible, the determination of whether such other
 7 foreign corporation was a controlled foreign corpora-
 8 tion shall be made without regard to the preceding
 9 sentence.

10 “(2) SAME COUNTRY EXCEPTION NOT APPLICA-
 11 BLE.—Clause (i) of section 954(c)(3)(A) shall not
 12 apply to any amount treated as a dividend by reason
 13 of paragraph (1).

14 “(3) CLARIFICATION OF DEEMED SALES.—For
 15 purposes of this subsection, a controlled foreign cor-
 16 poration shall be treated as having sold or ex-
 17 changed any stock if, under any provision of this
 18 subtitle, such controlled foreign corporation is treat-
 19 ed as having gain from the sale or exchange of such
 20 stock.”

21 (b) AMENDMENT OF SECTION 904(d).—Clause (i) of
 22 section 904(d)(2)(E) is amended by striking “and except
 23 as provided in regulations, the taxpayer was a United
 24 States shareholder in such corporation”.

25 (c) EFFECTIVE DATES.—

1 (1) TREATMENT AS DIVIDENDS.—The amend-
 2 ment made by subsection (a) shall apply to gain rec-
 3 ognized on transactions occurring after the date of
 4 the enactment of this Act.

5 (2) SECTION 904.—The amendment made by
 6 subsection (b) shall apply to distributions after the
 7 date of the enactment of this Act.

8 **SEC. 202. MISCELLANEOUS MODIFICATIONS TO SUBPART F.**

9 (a) SECTION 1248 GAIN TAKEN INTO ACCOUNT IN
 10 DETERMINING PRO RATA SHARE.—

11 (1) IN GENERAL.—Paragraph (2) of section
 12 951(a) (defining pro rata share of subpart F in-
 13 come) is amended by adding at the end the following
 14 new sentence:

15 “For purposes of subparagraph (B), any gain in-
 16 cluded in the gross income of any person as a divi-
 17 dend under section 1248 shall be treated as a dis-
 18 tribution received by such person with respect to the
 19 stock involved.”

20 (2) EFFECTIVE DATE.—The amendment made
 21 by paragraph (1) shall apply to dispositions after the
 22 date of the enactment of this Act.

23 (b) BASIS ADJUSTMENTS IN STOCK HELD BY FOR-
 24 EIGN CORPORATION.—

1 (1) IN GENERAL.—Section 961 (relating to ad-
 2 justments to basis of stock in controlled foreign cor-
 3 porations and of other property) is amended by add-
 4 ing at the end the following new subsection:

5 “(c) BASIS ADJUSTMENTS IN STOCK HELD BY FOR-
 6 EIGN CORPORATION.—Under regulations prescribed by
 7 the Secretary, if a United States shareholder is treated
 8 under section 958(a)(2) as owning any stock in a con-
 9 trolled foreign corporation which is actually owned by an-
 10 other controlled foreign corporation, adjustments similar
 11 to the adjustments provided by subsections (a) and (b)
 12 shall be made to the basis of such stock in the hands of
 13 such other controlled foreign corporation, but only for the
 14 purposes of determining the amount included under sec-
 15 tion 951 in the gross income of such United States share-
 16 holder (or any other United States shareholder who ac-
 17 quires from any person any portion of the interest of such
 18 United States shareholder by reason of which such share-
 19 holder was treated as owning such stock, but only to the
 20 extent of such portion, and subject to such proof of iden-
 21 tity of such interest as the Secretary may prescribe by reg-
 22 ulations).”

23 (2) EFFECTIVE DATE.—The amendment made
 24 by paragraph (1) shall apply for purposes of deter-

1 mining inclusions for taxable years of United States
 2 shareholders beginning after December 31, 1997.

3 (c) DETERMINATION OF PREVIOUSLY TAXED IN-
 4 COME IN SECTION 304 DISTRIBUTIONS, ETC.—

5 (1) IN GENERAL.—Section 959 (relating to ex-
 6 clusion from gross income of previously taxed earn-
 7 ings and profits) is amended by adding at the end
 8 the following new subsection:

9 “(g) ADJUSTMENTS FOR CERTAIN TRANSACTIONS.—
 10 If, by reason of—

11 “(1) a transaction to which section 304 applies,

12 “(2) the structure of a United States sharehold-
 13 er’s holdings in controlled foreign corporations, or

14 “(3) other circumstances,

15 there would be a multiple inclusion of any item in income
 16 (or an inclusion or exclusion without an appropriate basis
 17 adjustment) by reason of this subpart, the Secretary may
 18 prescribe regulations providing such modifications in the
 19 application of this subpart as may be necessary to elimi-
 20 nate such multiple inclusion or provide such basis adjust-
 21 ment, as the case may be.”

22 (2) EFFECTIVE DATE.—The amendment made
 23 by paragraph (1) shall take effect on the date of the
 24 enactment of this Act.

1 (d) CLARIFICATION OF TREATMENT OF BRANCH TAX
 2 EXEMPTIONS OR REDUCTIONS.—

3 (1) IN GENERAL.—Subsection (b) of section
 4 952 is amended by adding at the end the following
 5 new sentence: “For purposes of this subsection, any
 6 exemption (or reduction) with respect to the tax im-
 7 posed by section 884 shall not be taken into ac-
 8 count.”

9 (2) EFFECTIVE DATE.—The amendment made
 10 by paragraph (1) shall apply to taxable years begin-
 11 ning after December 31, 1986.

12 **SEC. 203. INDIRECT FOREIGN TAX CREDIT ALLOWED FOR**
 13 **CERTAIN LOWER TIER COMPANIES.**

14 (a) SECTION 902 CREDIT.—

15 (1) IN GENERAL.—Subsection (b) of section
 16 902 (relating to deemed taxes increased in case of
 17 certain 2nd and 3rd tier foreign corporations) is
 18 amended to read as follows:

19 “(b) DEEMED TAXES INCREASED IN CASE OF CER-
 20 TAIN LOWER TIER CORPORATIONS.—

21 “(1) IN GENERAL.—If—

22 “(A) any foreign corporation is a member
 23 of a qualified group, and

24 “(B) such foreign corporation owns 10 per-
 25 cent or more of the voting stock of another

1 member of such group from which it receives
 2 dividends in any taxable year,
 3 such foreign corporation shall be deemed to have
 4 paid the same proportion of such other member's
 5 post-1986 foreign income taxes as would be deter-
 6 mined under subsection (a) if such foreign corpora-
 7 tion were a domestic corporation.

8 “(2) QUALIFIED GROUP.—For purposes of
 9 paragraph (1), the term ‘qualified group’ means—

10 “(A) the foreign corporation described in
 11 subsection (a), and

12 “(B) any other foreign corporation if—

13 “(i) the domestic corporation owns at
 14 least 5 percent of the voting stock of such
 15 other foreign corporation indirectly
 16 through a chain of foreign corporations
 17 connected through stock ownership of at
 18 least 10 percent of their voting stock,

19 “(ii) the foreign corporation described
 20 in subsection (a) is the first tier corpora-
 21 tion in such chain, and

22 “(iii) such other corporation is not
 23 below the sixth tier in such chain.

24 The term ‘qualified group’ shall not include any for-
 25 eign corporation below the third tier in the chain re-

ferred to in clause (i) unless such foreign corporation is a controlled foreign corporation (as defined in section 957) and the domestic corporation is a United States shareholder (as defined in section 951(b)) in such foreign corporation. Paragraph (1) shall apply to those taxes paid by a member of the qualified group below the third tier only with respect to periods during which it was a controlled foreign corporation.”

(2) CONFORMING AMENDMENTS.—

(A) Subparagraph (B) of section 902(c)(3) is amended by adding “or” at the end of clause (i) and by striking clauses (ii) and (iii) and inserting the following new clause:

“(ii) the requirements of subsection (b)(2) are met with respect to such foreign corporation.”

(B) Subparagraph (B) of section 902(c)(4) is amended by striking “3rd foreign corporation” and inserting “sixth tier foreign corporation”.

(C) The heading for paragraph (3) of section 902(c) is amended by striking “WHERE DOMESTIC CORPORATION ACQUIRES 10 PERCENT OF FOREIGN CORPORATION” and inserting

1 “WHERE FOREIGN CORPORATION FIRST
2 QUALIFIES”.

3 (D) Paragraph (3) of section 902(c) is
4 amended by striking “ownership” each place it
5 appears.

6 (b) SECTION 960 CREDIT.—Paragraph (1) of section
7 960(a) (relating to special rules for foreign tax credits)
8 is amended to read as follows:

9 “(1) DEEMED PAID CREDIT.—For purposes of
10 subpart A of this part, if there is included under
11 section 951(a) in the gross income of a domestic cor-
12 poration any amount attributable to earnings and
13 profits of a foreign corporation which is a member
14 of a qualified group (as defined in section 902(b))
15 with respect to the domestic corporation, then, ex-
16 cept to the extent provided in regulations, section
17 902 shall be applied as if the amount so included
18 were a dividend paid by such foreign corporation
19 (determined by applying section 902(c) in accord-
20 ance with section 904(d)(3)(B)).”

21 (c) EFFECTIVE DATE.—

22 (1) IN GENERAL.—The amendments made by
23 this section shall apply to taxes of any foreign cor-
24 poration for taxable years of such corporation begin-
25 ning after December 31, 1997.

1 (2) SPECIAL RULE.—In the case of any chain
 2 of foreign corporations described in clauses (i) and
 3 (ii) of section 902(b)(2)(B) of the Internal Revenue
 4 Code of 1986 (as amended by this section), no liq-
 5 uidation, reorganization, or similar transaction in a
 6 taxable year beginning after December 31, 1997,
 7 shall have the effect of permitting taxes to be taken
 8 into account under section 902 of the Internal Reve-
 9 nue Code of 1986 which could not have been taken
 10 into account under such section but for such trans-
 11 action.

12 **SEC. 204. EXEMPTION FOR ACTIVE FINANCING INCOME.**

13 (a) EXEMPTION FROM FOREIGN PERSONAL HOLD-
 14 ING COMPANY INCOME.—Subsection (c) of section 954 is
 15 amended by adding at the end the following new para-
 16 graph:

17 “(4) CERTAIN INCOME DERIVED IN ACTIVE
 18 CONDUCT OF TRADE OR BUSINESS.—

19 “(A) IN GENERAL.—For purposes of para-
 20 graph (1), foreign personal holding company in-
 21 come shall not include income which is—

22 “(i) derived in or incident to the ac-
 23 tive conduct by a controlled foreign cor-
 24 poration of a banking, financing, or similar
 25 business, but only if the corporation is pre-

1 dominantly engaged in the active conduct
2 of such business,

3 “(ii) received from a person other
4 than a related person (within the meaning
5 of subsection (d)(3)) and derived from the
6 investments made by a qualifying insur-
7 ance company of its unearned premiums or
8 reserves ordinary and necessary for the
9 proper conduct of its insurance business,
10 or

11 “(iii) received from a person other
12 than a related person (within the meaning
13 of subsection (d)(3)) and derived from in-
14 vestments made by a qualifying insurance
15 company of an amount of its assets equal
16 to—

17 “(I) in the case of contracts reg-
18 ulated in the country in which sold as
19 property, casualty, or health insurance
20 contracts, one-third of its premiums
21 earned on insurance contracts during
22 the taxable year (as defined in section
23 832(b)(4)), and

24 “(II) in the case of contracts reg-
25 ulated in the country in which sold as

1 life insurance or annuity contracts,
 2 the greater of 10 percent of the re-
 3 serves described in clause (ii) or
 4 \$10,000,000,

5 which are not directly or indirectly attrib-
 6 utable to the insurance or reinsurance of
 7 risks of persons who are related persons
 8 (within the meaning of subsection (d)(3)).

9 “(B) APPLICABLE PRINCIPLES.—

10 “(i) BANKING, ETC. INCOME.—The
 11 Secretary shall prescribe regulations which
 12 interpret subparagraph (A)(i) in accord-
 13 ance with the applicable principles of sec-
 14 tion 904(d)(2)(C), except that in prescrib-
 15 ing such regulations, the Secretary shall
 16 include income from all leases in income
 17 from a banking, financing, or similar busi-
 18 ness.

19 “(ii) LOOK-THRU RULES.—The Sec-
 20 retary shall prescribe regulations consist-
 21 ent with the principles of section 904(d)(3)
 22 which provide that dividends, interest, in-
 23 come equivalent to interest, rents, or royal-
 24 ties received or accrued from a related per-
 25 son (within the meaning of subsection

(d)(3)) shall be subject to look-thru treatment for purposes of this section.

“(iii) SPECIAL RULE FOR BANKING OR SECURITIES BUSINESS.—In the case of a corporation described in subparagraph (C)(ii), the regulations under clauses (i) and (ii) shall be consistent with the applicable principles of section 1296(b) (as in effect on the day before the enactment of the International Tax Simplification for American Competitiveness Act).

“(C) PREDOMINANTLY ENGAGED.—For purposes of subparagraph (A)(i), a corporation shall be deemed predominantly engaged in the active conduct of a banking, financing, or similar business only if—

“(i) more than 70 percent of its gross income from such business is derived from transactions with unrelated persons (as defined in subsection (d)(3)), and more than 20 percent of its gross income from that business is derived from transactions with unrelated persons (as so defined) located within the country under the laws of which

1 the controlled foreign corporation is cre-
2 ated or organized, or

3 “(ii) the corporation is—

4 “(I) predominantly engaged in
5 the active conduct of a banking or se-
6 curities business (within the meaning
7 of section 1296(b), as in effect before
8 the enactment of the International
9 Tax Simplification for American Com-
10 petitiveness Act), or

11 “(II) a qualified bank affiliate or
12 a qualified securities affiliate for pur-
13 poses of section 1296(b) (as so in ef-
14 fect).

15 “(D) QUALIFYING INSURANCE COMPANY.—

16 For purposes of clauses (ii) and (iii) of sub-
17 paragraph (A), the term ‘qualifying insurance
18 company’ means any entity which is subject to
19 regulation as an insurance company under the
20 laws of its country of incorporation and which
21 realizes at least 50 percent of its gross income
22 (other than gross income derived from invest-
23 ments) from premiums written on risks situated
24 within its country of incorporation.”

1 (b) EXEMPTION FROM FOREIGN BASE COMPANY
 2 SERVICES INCOME.—Paragraph (2) of section 954(e) is
 3 amended by striking “or” at the end of subparagraph (A),
 4 by striking the period at the end of subparagraph (B) and
 5 inserting “, or”, and by adding at the end the following:

6 “(C) the active conduct by a controlled for-
 7 eign corporation of a banking, financing, insur-
 8 ance, or similar business, but only if the cor-
 9 poration is predominantly engaged in the active
 10 conduct of that business (within the meaning of
 11 subsection (c)(4)(C)).”

12 (c) EFFECTIVE DATE.—The amendments made by
 13 this section shall apply to taxable years of foreign corpora-
 14 tions beginning after December 31, 1997, and to taxable
 15 years of United States shareholders with or within which
 16 such taxable years of foreign corporations end.

17 **SEC. 205. APPLICATION OF SEPARATE FOREIGN TAX CRED-**
 18 **IT LIMITATION FOR NONCONTROLLED SEC-**
 19 **TION 902 CORPORATIONS.**

20 (a) LOOK-THRU IN CASE OF NONCONTROLLED SEC-
 21 TION 902 CORPORATIONS IF INFORMATION AVAILABLE.—
 22 Section 904(d) (relating to separate application of section
 23 with respect to certain categories of income) is amended
 24 by redesignating paragraphs (4) and (5) as paragraphs

1 (5) and (6), respectively, and by inserting after paragraph
 2 (3) the following new paragraph:

3 “(4) LOOK-THRU IN THE CASE OF CERTAIN
 4 NONCONTROLLED SECTION 902 CORPORATIONS.—

5 “(A) IN GENERAL.—Dividends received or
 6 accrued by a corporation from a noncontrolled
 7 section 902 corporation shall be treated as not
 8 described in paragraph (1)(E) if information
 9 necessary to make the determinations under
 10 subparagraph (B) is readily available to the
 11 taxpayer.

12 “(B) ALLOCATION OF DIVIDENDS AMONG
 13 CATEGORIES.—Dividends treated as provided in
 14 subparagraph (A) which are paid out of the
 15 earnings or profits of such corporation shall be
 16 treated as income in a separate category in pro-
 17 portion to the ratio of—

18 “(i) the portion of the earnings and
 19 profits attributable to income in such sepa-
 20 rate category, to

21 “(ii) the total amount of earnings and
 22 profits.

23 “(C) COORDINATION WITH OTHER PROVI-
 24 SIONS.—Dividends treated as provided in sub-
 25 paragraph (A) shall not be treated as dividends

1 from a noncontrolled section 902 corporation
 2 for purposes of subparagraphs (C)(iii) and (D)
 3 of paragraph (2).”

4 (b) DIVIDENDS FROM OTHER NONCONTROLLED
 5 SECTION 902 CORPORATIONS ALL IN SAME SEPARATE
 6 BASKET.—Subparagraph (E) of section 904(d)(1) is
 7 amended to read as follows:

8 “(E) in the case of a corporation, except as
 9 provided in paragraph (4), dividends from all
 10 noncontrolled section 902 corporations,”.

11 (c) EFFECTIVE DATES.—

12 (1) IN GENERAL.—The amendments made by
 13 this section shall apply to taxable years of foreign
 14 corporations beginning after December 31, 1997,
 15 and to taxable years of United States shareholders
 16 in which or with which such taxable years of foreign
 17 corporations end.

18 (2) DIVIDENDS.—The amendments made by
 19 this section shall apply to dividends paid out of
 20 earnings and profits accumulated during taxable
 21 years of foreign corporations beginning after Decem-
 22 ber 31, 1997. For purposes of the preceding sen-
 23 tence, the rules of section 316 of the Internal Reve-
 24 nue Code of 1986 shall apply.

1 **SEC. 206. STUDY OF PROPER TREATMENT OF EUROPEAN**
 2 **UNION UNDER SAME COUNTRY EXCEPTIONS.**

3 (a) STUDY.—The Secretary of the Treasury or the
 4 Secretary’s delegate shall conduct a study on the feasibil-
 5 ity of treating all countries included in the European
 6 Union as 1 country for purposes of applying the same
 7 country exceptions under subpart F of part III of sub-
 8 chapter N of chapter 1 of the Internal Revenue Code of
 9 1986. Such study shall include consideration of methods
 10 of ensuring that taxpayers are subject to a substantial ef-
 11 fective rate of foreign tax in such countries if such treat-
 12 ment is adopted.

13 (b) REPORT.—Not later than 6 months after the date
 14 of enactment of this Act, the Secretary of the Treasury
 15 shall report to the Committee on Ways and Means of the
 16 House of Representatives and the Committee on Finance
 17 of the Senate the results of the study conducted under
 18 subsection (a), including recommendations (if any) for
 19 legislation.

20 **SEC. 207. EXPANSION OF DE MINIMIS RULE UNDER SUB-**
 21 **PART F.**

22 (a) IN GENERAL.—Subparagraph (A) of section
 23 954(b)(3) (relating to de minimis, etc., rules) is
 24 amended—

25 (1) by striking “5 percent” in clause (i) and in-
 26 serting “10 percent”, and

1 (2) by striking “\$1,000,000” in clause (ii) and
2 inserting “\$2,000,000”.

3 (b) TECHNICAL AMENDMENTS.—

4 (1) Clause (ii) of section 864(d)(5)(A) is
5 amended by striking “5 percent or \$1,000,000” and
6 inserting “10 percent or \$2,000,000”.

7 (2) Clause (i) of section 881(c)(5)(A) is amend-
8 ed by striking “5 percent or \$1,000,000” and insert-
9 ing “10 percent or \$2,000,000”.

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

13 **SEC. 208. SUBPART F EARNINGS AND PROFITS DETER-**
14 **MINED UNDER GENERALLY ACCEPTED**
15 **ACCOUNTING PRINCIPLES.**

16 (a) IN GENERAL.—Subsection (a) of section 964 (re-
17 lating to miscellaneous provisions) is amended by striking
18 “rules substantially similar to those applicable to domestic
19 corporations, under regulations prescribed by the Sec-
20 retary” and inserting “generally accepted accounting prin-
21 ciples in the United States”.

22 (b) EFFECTIVE DATE.—The amendment made by
23 subsection (a) shall apply to distributions during, and the
24 determination of the inclusion under section 951 of the
25 Internal Revenue Code of 1986 with respect to, taxable

1 years of foreign corporations beginning after December
2 31, 1997.

3 **SEC. 209. CLARIFICATION OF TREATMENT OF PIPELINE**
4 **TRANSPORTATION INCOME.**

5 (a) IN GENERAL.—Section 954(g)(1) (defining for-
6 eign base company oil related income) is amended by strik-
7 ing “or” at the end of subparagraph (A), by striking the
8 period at the end of subparagraph (B) and inserting “,
9 or”, and by inserting after subparagraph (B) the following
10 new subparagraph:

11 “(C) the pipeline transportation of oil or
12 gas within such foreign country.”

13 (b) EFFECTIVE DATE.—The amendments made by
14 this section shall apply to taxable years beginning after
15 December 31, 1997.

16 **SEC. 210. DEDUCTION FOR DIVIDENDS RECEIVED FROM**
17 **CERTAIN FOREIGN CORPORATIONS.**

18 (a) CONSTRUCTIVE OWNERSHIP RULES TO APPLY IN
19 DETERMINING 80-PERCENT OWNERSHIP.—Section 245
20 (a)(5) (relating to post-1986 undistributed U.S. earnings)
21 is amended by adding at the end the following flush sen-
22 tence:

23 “Section 318(a) shall apply for purposes of subpara-
24 graph (B).”

1 (b) DIVIDENDS TO INCLUDE SUBPART F DISTRIBUTIONS.—Section 245(a) is amended by adding at the end
 2 TIONS.—Section 245(a) is amended by adding at the end
 3 the following new paragraph:

4 “(12) SUBPART F INCLUSIONS TREATED AS
 5 DIVIDENDS.—For purposes of this subsection, the
 6 term ‘dividend’ shall include any amount the tax-
 7 payer is required to include in gross income for the
 8 taxable year under section 951(a).”

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

12 **TITLE III—OTHER PROVISIONS**

13 **SEC. 301. EXCHANGE RATE USED IN TRANSLATING** 14 **FOREIGN TAXES.**

15 (a) ACCRUED TAXES TRANSLATED BY USING AVERAGE RATE FOR YEAR TO WHICH TAXES RELATE.—
 16 AGE RATE FOR YEAR TO WHICH TAXES RELATE.—

17 (1) IN GENERAL.—Subsection (a) of section
 18 986 (relating to translation of foreign taxes) is
 19 amended to read as follows:

20 “(a) FOREIGN INCOME TAXES.—

21 “(1) TRANSLATION OF ACCRUED TAXES.—

22 “(A) IN GENERAL.—For purposes of deter-
 23 mining the amount of the foreign tax credit, in
 24 the case of a taxpayer which takes foreign in-
 25 come taxes into account when accrued, the

1 amount of any foreign income taxes (and any
 2 adjustment thereto) shall be translated into dol-
 3 lars by using the average exchange rate for the
 4 taxable year to which such taxes relate.

5 “(B) EXCEPTION FOR CERTAIN TAXES.—
 6 Subparagraph (A) shall not apply to any for-
 7 eign income taxes paid—

8 “(i) after the date 2 years after the
 9 close of the taxable year to which such
 10 taxes relate, or

11 “(ii) before the beginning of the tax-
 12 able year to which such taxes relate.

13 “(C) EXCEPTION FOR INFLATIONARY CUR-
 14 RENCIES.—Subparagraph (A) shall not apply to
 15 any foreign income taxes the liability for which
 16 is denominated in any currency determined to
 17 be an inflationary currency under regulations
 18 prescribed by the Secretary.

19 “(D) CROSS REFERENCE.—

“**For adjustments where tax is not paid within 2
 years, see section 905(c).**

20 “(2) TRANSLATION OF TAXES TO WHICH PARA-
 21 GRAPH (1) DOES NOT APPLY.—For purposes of de-
 22 termining the amount of the foreign tax credit, in
 23 the case of any foreign income taxes to which sub-
 24 paragraph (A) of paragraph (1) does not apply—

1 “(A) such taxes shall be translated into
 2 dollars using the exchange rates as of the time
 3 such taxes were paid to the foreign country or
 4 possession of the United States, and

5 “(B) any adjustment to the amount of
 6 such taxes shall be translated into dollars
 7 using—

8 “(i) except as provided in clause (ii),
 9 the exchange rate as of the time when such
 10 adjustment is paid to the foreign country
 11 or possession, or

12 “(ii) in the case of any refund or cred-
 13 it of foreign income taxes, using the ex-
 14 change rate as of the time of the original
 15 payment of such foreign income taxes.

16 “(3) FOREIGN INCOME TAXES.—For purposes
 17 of this subsection, the term ‘foreign income taxes’
 18 means any income, war profits, or excess profits
 19 taxes paid or accrued to any foreign country or to
 20 any possession of the United States.”

21 (2) ADJUSTMENT WHEN NOT PAID WITHIN 2
 22 YEARS AFTER YEAR TO WHICH TAXES RELATE.—
 23 Subsection (c) of section 905 is amended to read as
 24 follows:

25 “(c) ADJUSTMENTS TO ACCRUED TAXES.—

1 “(1) IN GENERAL.—If—

2 “(A) accrued taxes when paid differ from
3 the amounts claimed as credits by the taxpayer,

4 “(B) accrued taxes are not paid before the
5 date 2 years after the close of the taxable year
6 to which such taxes relate, or

7 “(C) any tax paid is refunded in whole or
8 in part,

9 the taxpayer shall notify the Secretary, who shall re-
10 determine the amount of the tax for the year or
11 years affected.

12 “(2) SPECIAL RULE FOR TAXES NOT PAID
13 WITHIN 2 YEARS.—In making the redetermination
14 under paragraph (1), no credit shall be allowed for
15 accrued taxes not paid before the date referred to in
16 subparagraph (B) of paragraph (1). Any such taxes
17 subsequently paid shall be taken into account for the
18 taxable year to which they relate and a redetermina-
19 tion under this section shall be made on account of
20 such payment.

21 “(3) ADJUSTMENTS.—The amount of tax due
22 on any redetermination under paragraph (1) (if any)
23 shall be paid by the taxpayer on notice and demand
24 by the Secretary, and the amount of tax overpaid (if
25 any) shall be credited or refunded to the taxpayer in

1 accordance with subchapter B of chapter 66 (section
2 6511 et seq.).

3 “(4) BOND REQUIREMENTS.—In the case of
4 any tax accrued but not paid, the Secretary, as a
5 condition precedent to the allowance of the credit
6 provided in this subpart, may require the taxpayer
7 to give a bond, with sureties satisfactory to and ap-
8 proved by the Secretary, in such sum as the Sec-
9 retary may require, conditioned on the payment by
10 the taxpayer of any amount of tax found due on any
11 such redetermination. Any such bond shall contain
12 such further conditions as the Secretary may
13 require.

14 “(5) OTHER SPECIAL RULES.—In any redeter-
15 mination under paragraph (1) by the Secretary of
16 the amount of tax due from the taxpayer for the
17 year or years affected by a refund, the amount of
18 the taxes refunded for which credit has been allowed
19 under this section shall be reduced by the amount of
20 any tax described in section 901 imposed by the for-
21 eign country or possession of the United States with
22 respect to such refund; but no credit under this sub-
23 part, or deduction under section 164, shall be al-
24 lowed for any taxable year with respect to any such
25 tax imposed on the refund. No interest shall be as-

1 sessed or collected on any amount of tax due on any
 2 redetermination by the Secretary, resulting from a
 3 refund to the taxpayer, for any period before the re-
 4 ceipt of such refund, except to the extent interest
 5 was paid by the foreign country or possession of the
 6 United States on such refund for such period.”

7 (b) AUTHORITY TO USE AVERAGE RATES.—

8 (1) IN GENERAL.—Subsection (a) of section
 9 986 (as amended by subsection (a)) is amended by
 10 redesignating paragraph (3) as paragraph (4) and
 11 inserting after paragraph (2) the following new
 12 paragraph:

13 “(3) AUTHORITY TO PERMIT USE OF AVERAGE
 14 RATES.—To the extent prescribed in regulations, the
 15 average exchange rate for the period (specified in
 16 such regulations) during which the taxes or adjust-
 17 ment is paid may be used instead of the exchange
 18 rate as of the time of such payment.”

19 (2) DETERMINATION OF AVERAGE RATES.—
 20 Subsection (c) of section 989 is amended by striking
 21 “and” at the end of paragraph (4), by striking the
 22 period at the end of paragraph (5) and inserting “,
 23 and”, and by adding at the end the following new
 24 paragraph:

1 “(6) setting forth procedures for determining
2 the average exchange rate for any period.”

3 (3) CONFORMING AMENDMENTS.—Subsection
4 (b) of section 989 is amended by striking “weight-
5 ed” each place it appears.

6 (c) EFFECTIVE DATES.—

7 (1) IN GENERAL.—The amendments made by
8 subsections (a)(1) and (b) shall apply to taxes paid
9 or accrued in taxable years beginning after Decem-
10 ber 31, 1997.

11 (2) SUBSECTION (a)(2).—The amendment made
12 by subsection (a)(2) shall apply to taxes which relate
13 to taxable years beginning after December 31, 1997.

14 **SEC. 302. ELECTION TO USE SIMPLIFIED SECTION 904**
15 **LIMITATION FOR ALTERNATIVE MINIMUM**
16 **TAX.**

17 (a) GENERAL RULE.—Subsection (a) of section 59
18 (relating to alternative minimum tax foreign tax credit)
19 is amended by adding at the end the following new
20 paragraph:

21 “(4) ELECTION TO USE SIMPLIFIED SECTION
22 904 LIMITATION.—

23 “(A) IN GENERAL.—In determining the al-
24 ternative minimum tax foreign tax credit for

any taxable year to which an election under this paragraph applies—

“(i) subparagraph (B) of paragraph (1) shall not apply, and

“(ii) the limitation of section 904 shall be based on the proportion which—

“(I) the taxpayer’s taxable income (as determined for purposes of the regular tax) from sources without the United States (but not in excess of the taxpayer’s entire alternative minimum taxable income), bears to

“(II) the taxpayer’s entire alternative minimum taxable income for the taxable year.

“(B) ELECTION.—

“(i) IN GENERAL.—An election under this paragraph may be made only for the taxpayer’s first taxable year which begins after December 31, 1997, and for which the taxpayer claims an alternative minimum tax foreign tax credit.

“(ii) ELECTION REVOCABLE ONLY WITH CONSENT.—An election under this paragraph, once made, shall apply to the

1 taxable year for which made and all subse-
 2 quent taxable years unless revoked with
 3 the consent of the Secretary.”

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

7 **SEC. 303. MODIFICATION OF SECTION 1491.**

8 (a) GENERAL RULE.—So much of chapter 5 (relating
 9 to tax on transfers to avoid income tax) as precedes sec-
 10 tion 1492 is amended to read as follows:

11 **“CHAPTER 5—TREATMENT OF TRANSFERS**
 12 **TO AVOID INCOME TAX**

“Sec. 1491. Recognition of gain.

“Sec. 1492. Exceptions.

13 **“SEC. 1491. RECOGNITION OF GAIN.**

14 “In the case of any transfer of property by a United
 15 States person to a foreign corporation as paid-in surplus
 16 or as a contribution to capital, to a foreign estate or trust,
 17 or to a foreign partnership, for purposes of this subtitle
 18 (other than for purposes of section 679), such transfer
 19 shall be treated as a sale or exchange for an amount equal
 20 to the fair market value of the property transferred, and
 21 the transferor shall recognize as gain the excess of—

22 “(1) the fair market value of the property so
 23 transferred, over

1 “(2) the adjusted basis (for purposes of deter-
 2 mining gain) of such property in the hands of the
 3 transferor.

4 If a trust which is not a foreign trust becomes a foreign
 5 trust, such trust shall be treated for purposes of this sec-
 6 tion as having transferred, immediately before becoming
 7 a foreign trust, all of its assets to a foreign trust.”

8 (b) CONFORMING AMENDMENTS.—

9 (1) Section 1057 is hereby repealed.

10 (2) Section 1492 is amended to read as follows:

11 **“SEC. 1492. EXCEPTIONS.**

12 “The provisions of section 1491 shall not apply—

13 “(1) if the transferee is an organization exempt
 14 from income tax under part I of subchapter F of
 15 chapter 1 (other than an organization described in
 16 section 401(a)),

17 “(2) to a transfer described in section 367, or

18 “(3) to any other transfer, to the extent pro-
 19 vided in regulations in accordance with principles
 20 similar to the principles of section 367 or otherwise
 21 consistent with the purpose of section 1491.”

22 (3) Section 1494 is hereby repealed.

23 (4) Paragraph (8) of section 6501(c) is amend-
 24 ed by inserting “or on any transfer by reason of sec-
 25 tion 1491” after “section 367”.

1 (5) Subsection (a) of section 6038B is amended
 2 by striking “or” at the end of paragraph (1), by
 3 adding “or” at the end of paragraph (2), and by in-
 4 serting after paragraph (2) the following new para-
 5 graph:

6 “(3) makes any transfer described in section
 7 1491.”.

8 (6) The table of sections for part IV of sub-
 9 chapter O of chapter 1 is amended by striking the
 10 item relating to section 1057.

11 (7) The table of chapters for subtitle A is
 12 amended by striking “Tax on” in the item relating
 13 to chapter 5 and inserting “Treatment of”.

14 (c) EFFECTIVE DATE.—The amendments made by
 15 this section shall apply to transfers after December 31,
 16 1997.

17 **SEC. 304. MODIFICATION OF SECTION 367(b).**

18 (a) GENERAL RULE.—Paragraph (1) of section
 19 367(b) is amended to read as follows:

20 “(1) IN GENERAL.—In the case of any trans-
 21 action described in section 332, 351, 354, 355, 356,
 22 or 361 in which the status of a foreign corporation
 23 as a corporation is a general condition for non-
 24 recognition by 1 or more of the parties to the trans-
 25 action, income shall be required to be recognized to

1 the extent provided in regulations prescribed by the
 2 Secretary which are necessary or appropriate to pre-
 3 vent the avoidance of Federal income taxes. This
 4 subsection shall not apply to a transaction in which
 5 the foreign corporation is not treated as a corpora-
 6 tion under subsection (a)(1).”

7 (b) EFFECTIVE DATE.—The amendment made by
 8 subsection (a) shall apply to transfers after December 31,
 9 1997.

10 **SEC. 305. INCREASE IN FILING THRESHOLDS FOR RETURNS**
 11 **AS TO ORGANIZATION OF FOREIGN**
 12 **CORPORATIONS AND ACQUISITIONS OF**
 13 **STOCK IN SUCH CORPORATIONS.**

14 (a) IN GENERAL.—Subsection (a) of section 6046
 15 (relating to returns as to organization or reorganization
 16 of foreign corporations and as to acquisitions of their
 17 stock) is amended to read as follows:

18 “(a) REQUIREMENT OF RETURN.—

19 “(1) IN GENERAL.—A return complying with
 20 the requirements of subsection (b) shall be made
 21 by—

22 “(A) each United States citizen or resident
 23 who becomes an officer or director of a foreign
 24 corporation if a United States person (as de-
 25 fined in section 7701(a)(30)) meets the stock

1 ownership requirements of paragraph (2) with
 2 respect to such corporation,

3 “(B) each United States person—

4 “(i) who acquires stock which, when
 5 added to any stock owned on the date of
 6 such acquisition, meets the stock owner-
 7 ship requirements of paragraph (2) with
 8 respect to a foreign corporation, or

9 “(ii) who acquires stock which, with-
 10 out regard to stock owned on the date of
 11 such acquisition, meets the stock owner-
 12 ship requirements of paragraph (2) with
 13 respect to a foreign corporation,

14 “(C) each person (not described in sub-
 15 paragraph (B)) who is treated as a United
 16 States shareholder under section 953(c) with
 17 respect to a foreign corporation, and

18 “(D) each person who becomes a United
 19 States person while meeting the stock owner-
 20 ship requirements of paragraph (2) with respect
 21 to stock of a foreign corporation.

22 In the case of a foreign corporation with respect to
 23 which any person is treated as a United States
 24 shareholder under section 953(c), subparagraph (A)
 25 shall be treated as including a reference to each

1 United States person who is an officer or director of
 2 such corporation.

3 “(2) STOCK OWNERSHIP REQUIREMENTS.—A
 4 person meets the stock ownership requirements of
 5 this paragraph with respect to any corporation if
 6 such person owns 10 percent or more of—

7 “(A) the total combined voting power of all
 8 classes of stock of such corporation entitled to
 9 vote, or

10 “(B) the total value of the stock of such
 11 corporation.”

12 (b) EFFECTIVE DATE.—The amendment made by
 13 this section shall take effect on January 1, 1998.

14 **SEC. 306. APPLICATION OF UNIFORM CAPITALIZATION**
 15 **RULES TO FOREIGN PERSONS.**

16 (a) IN GENERAL.—Section 263A(c) (relating to ex-
 17 ceptions) is amended by adding at the end the following
 18 new paragraph:

19 “(7) FOREIGN PERSONS.—This section shall
 20 apply to any taxpayer who is not a United States
 21 person only for purposes of applying sections
 22 871(b)(1) and 882(a)(1) and subpart F of part III
 23 of subchapter N.”

24 (b) EFFECTIVE DATE.—The amendment made by
 25 subsection (a) shall apply to taxable years beginning after

1 December 31, 1996. Section 481 of the Internal Revenue
 2 Code of 1986 shall not apply to any change in a method
 3 of accounting by reason of such amendment.

4 **SEC. 307. EXTENSION OF PERIOD TO WHICH EXCESS**
 5 **FOREIGN TAXES MAY BE CARRIED.**

6 (a) GENERAL RULE.—Subsection (c) of section 904
 7 (relating to carryback and carryover of excess tax paid)
 8 is amended by striking “in the first, second, third, fourth,
 9 or fifth” and inserting “in any of the first 10”.

10 (b) EXCESS EXTRACTION TAXES.—Paragraph (1) of
 11 section 907(f) is amended by striking “in the first, second,
 12 third, fourth, or fifth” and inserting “in any of the first
 13 10”.

14 (c) EFFECTIVE DATE.—The amendments made by
 15 this section shall apply to excess foreign taxes for taxable
 16 years beginning after December 31, 1997.

17 **SEC. 308. RECHARACTERIZATION OF OVERALL DOMESTIC**
 18 **LOSS.**

19 (a) GENERAL RULE.—Section 904 is amended by re-
 20 designating subsections (g), (h), (i), and (j) as subsections
 21 (h), (i), (j), and (k), respectively, and by inserting after
 22 subsection (f) the following new subsection:

23 “(g) RECHARACTERIZATION OF OVERALL DOMESTIC
 24 LOSS.—

1 “(1) GENERAL RULE.—For purposes of this
 2 subpart, in the case of any taxpayer who sustains an
 3 overall domestic loss for any taxable year beginning
 4 after December 31, 1997, that portion of the tax-
 5 payer’s taxable income from sources within the Unit-
 6 ed States for each succeeding taxable year which is
 7 equal to the lesser of—

8 “(A) the amount of such loss (to the extent
 9 not used under this paragraph in prior taxable
 10 years), or

11 “(B) 50 percent of the taxpayer’s taxable
 12 income from sources within the United States
 13 for such succeeding taxable year,
 14 shall be treated as income from sources without the
 15 United States (and not as income from sources with-
 16 in the United States).

17 “(2) OVERALL DOMESTIC LOSS DEFINED.—For
 18 purposes of this subsection—

19 “(A) IN GENERAL.—The term ‘overall do-
 20 mestic loss’ means any domestic loss to the ex-
 21 tent such loss offsets taxable income from
 22 sources without the United States for the tax-
 23 able year or for any preceding taxable year by
 24 reason of a carryback. For purposes of the pre-
 25 ceding sentence, the term ‘domestic loss’ means

the amount by which the gross income for the taxable year from sources within the United States is exceeded by the sum of the deductions properly apportioned or allocated thereto (determined without regard to any carryback from a subsequent taxable year).

“(B) TAXPAYER MUST HAVE ELECTED FOREIGN TAX CREDIT FOR YEAR OF LOSS.—The term ‘overall domestic loss’ shall not include any loss for any taxable year unless the taxpayer chose the benefits of this subpart for such taxable year.

“(3) CHARACTERIZATION OF SUBSEQUENT INCOME.—

“(A) IN GENERAL.—Any income from sources within the United States that is treated as income from sources without the United States under paragraph (1) shall be allocated among and increase the income categories in proportion to the loss from sources within the United States previously allocated to those income categories.

“(B) INCOME CATEGORY.—For purposes of this paragraph, the term ‘income category’ has

1 the meaning given to such term by subsection
 2 (f)(5)(E)(i).

3 “(4) COORDINATION WITH SUBSECTION (f).—
 4 The Secretary shall prescribe such regulations as
 5 may be necessary to coordinate the provisions of this
 6 subsection with the provisions of subsection (f).”

7 (b) CONFORMING AMENDMENT.—Subparagraph (A)
 8 of section 936(a)(2) is amended by striking “section
 9 904(f)” and inserting “subsections (f) and (g) of section
 10 904”.

11 (c) EFFECTIVE DATE.—The amendments made by
 12 this section shall apply to losses for taxable years begin-
 13 ning after December 31, 1997.

14 **SEC. 309. TREATMENT OF FOREIGN SALES CORPORATIONS.**

15 (a) EXPORT PROPERTY TO INCLUDE COMPUTER
 16 SOFTWARE.—

17 (1) IN GENERAL.—Section 927(a)(2) is amend-
 18 ed by adding at the end the following new sentence:
 19 “Computer software (whether or not patented) shall
 20 not be treated as described in subparagraph (B).”

21 (2) EFFECTIVE DATE.—The amendment made
 22 by this subsection shall apply to sales, exchanges, or
 23 other dispositions after the date of the enactment of
 24 this Act.

25 (b) MILITARY PROPERTY.—

1 (1) IN GENERAL.—Section 923(a) (defining ex-
 2 empt foreign trade income) is amended by striking
 3 paragraph (5) and by redesignating paragraph (6)
 4 as paragraph (5).

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

8 **SEC. 310. SPECIAL RULES RELATING TO FINANCIAL**
 9 **SERVICES INCOME.**

10 (a) EXCEPTION FOR INTEREST ON CERTAIN SECURI-
 11 TIES.—Subparagraph (B) of section 904(d)(2) (relating to
 12 high withholding tax interest) is amended by redesignating
 13 clause (iii) as clause (iv) and by inserting after clause (ii)
 14 the following new clause:

15 “(iii) EXCEPTION FOR INTEREST ON
 16 DEALER PROPERTY.—The term ‘high with-
 17 holding tax interest’ shall not include any
 18 interest on a security (within the meaning
 19 of section 475(c)(2)) which is received or
 20 accrued by a person that holds the security
 21 in connection with the holder’s activities as
 22 a dealer in securities (within the meaning
 23 of section 475(c)(1)).”

1 (b) DE MINIMIS RULE.—Subparagraph (C) of sec-
 2 tion 904(d)(2) (relating to financial services income) is
 3 amended by adding at the end the following new clause:

4 “(iv) DE MINIMIS RULE.—If the fi-
 5 nancial services income (as defined by
 6 clause (i)) of any person exceeds 80 per-
 7 cent of gross income, the entire gross in-
 8 come for the taxable year shall be treated
 9 as financial services income.”

10 (c) EXCEPTION FOR INCOME ON DEALER PROP-
 11 erty.—Subsection 904(g) is amended by redesignating
 12 paragraph (11) as paragraph (12) and by adding after
 13 paragraph (10) the following new paragraph:

14 “(11) EXCEPTION FOR INCOME ON DEALER
 15 PROPERTY.—Paragraph (1) shall not apply to any
 16 amount derived from a United States-owned foreign
 17 corporation that is derived from income on a secu-
 18 rity (within the meaning of section 475(c)(2)) which
 19 is received or accrued by a person that holds the se-
 20 curity in connection with the holder’s activities as a
 21 dealer in securities (within the meaning of section
 22 475(c)(1)).”

23 (d) EFFECTIVE DATES.—

1 (1) IN GENERAL.—The amendments made by
 2 this section shall apply to taxable years beginning
 3 after December 31, 1997.

4 (2) DEEMED PAID CREDITS.—In the case of
 5 any credit under section 901 of the Internal Revenue
 6 Code of 1986 by reason of section 902 or 960 of
 7 such Code, the amendments made by this section
 8 shall apply to taxable years of foreign corporations
 9 beginning after December 31, 1997, and to taxable
 10 years of United States shareholders in such corpora-
 11 tions with or within which such taxable years of for-
 12 eign corporations end.

13 **SEC. 311. UNITED STATES PROPERTY NOT TO INCLUDE**
 14 **CERTAIN ASSETS ACQUIRED BY DEALERS IN**
 15 **ORDINARY COURSE OF TRADE OR BUSINESS.**

16 (a) IN GENERAL.—Section 956(c)(2) is amended by
 17 striking “and” at the end of subparagraph (H), by strik-
 18 ing the period at the end of subparagraph (I) and insert-
 19 ing a semicolon, and by adding at the end the following
 20 new subparagraphs:

21 “(J) deposits of cash or securities made or
 22 received on commercial terms in the ordinary
 23 course of a United States or foreign person’s
 24 business as a dealer in securities or in commod-
 25 ities, but only to the extent such deposits are

1 made or received as collateral or margin for (i)
2 a securities loan, notional principal contract,
3 options contract, forward contract, or futures
4 contract, or (ii) any other financial transaction
5 in which the Secretary determines that it is cus-
6 tomary to post collateral or margin;

7 “(K) an obligation of a United States per-
8 son to the extent the principal amount of the
9 obligation does not exceed the fair market value
10 of readily marketable securities sold or pur-
11 chased pursuant to a sale and repurchase
12 agreement or otherwise posted or received as
13 collateral for the obligation in the ordinary
14 course of its business by a United States or for-
15 eign person which is a dealer in securities or
16 commodities; and

17 “(L) securities acquired and held by a con-
18 trolled foreign corporation in the ordinary
19 course of its business as a dealer in securities
20 if (i) the dealer accounts for the securities as
21 securities held primarily for sale to customers
22 in the ordinary course of business, and (ii) the
23 dealer disposes of the securities (or they mature
24 while held by the dealer) within a period con-

(b) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years of foreign corporations beginning after December 31, 1997, and to taxable years of United States shareholders or with or within which such taxable years of foreign corporations end.

20 (a) TREATMENT OF CERTAIN DIVIDENDS.—

•S 843 IS

1 “(k) EXEMPTION FOR CERTAIN DIVIDENDS OF REG-
2 ULATED INVESTMENT COMPANIES.—

3 “(1) INTEREST-RELATED DIVIDENDS.—

4 “(A) IN GENERAL.—Except as provided in
5 subparagraph (B), no tax shall be imposed
6 under paragraph (1)(A) of subsection (a) on
7 any interest-related dividend received from a
8 regulated investment company.

9 “(B) EXCEPTIONS.—Subparagraph (A)
10 shall not apply—

11 “(i) to any interest-related dividend
12 received from a regulated investment com-
13 pany by a person to the extent such divi-
14 dend is attributable to interest (other than
15 interest described in subparagraph (E) (i)
16 or (iii)) received by such company on in-
17 debtedness issued by such person or by any
18 corporation or partnership with respect to
19 which such person is a 10-percent share-
20 holder,

21 “(ii) to any interest-related dividend
22 with respect to stock of a regulated invest-
23 ment company unless the person who
24 would otherwise be required to deduct and
25 withhold tax from such dividend under

chapter 3 receives a statement (which meets requirements similar to the requirements of subsection (h)(5)) that the beneficial owner of such stock is not a United States person, and

“(iii) to any interest-related dividend paid to any person within a foreign country (or any interest-related dividend payment addressed to, or for the account of, persons within such foreign country) during any period described in subsection (h)(6) with respect to such country.

Clause (iii) shall not apply to any dividend with respect to any stock which was acquired on or before the date of the publication of the Secretary’s determination under subsection (h)(6).

“(C) INTEREST-RELATED DIVIDEND.—For purposes of this paragraph, an interest-related dividend is any dividend (or part thereof) which is designated by the regulated investment company as an interest-related dividend in a written notice mailed to its shareholders not later than 60 days after the close of its taxable year. If the aggregate amount so designated with respect to a taxable year of the company (includ-

ing amounts so designated with respect to dividends paid after the close of the taxable year described in section 855) is greater than the qualified net interest income of the company for such taxable year, the portion of each distribution which shall be an interest-related dividend shall be only that portion of the amounts so designated which such qualified net interest income bears to the aggregate amount so designated.

“(D) QUALIFIED NET INTEREST INCOME.—For purposes of subparagraph (C), the term ‘qualified net interest income’ means the qualified interest income of the regulated investment company reduced by the deductions properly allocable to such income.

“(E) QUALIFIED INTEREST INCOME.—For purposes of subparagraph (D), the term ‘qualified interest income’ means the sum of the following amounts derived by the regulated investment company from sources within the United States:

“(i) Any amount includible in gross income as original issue discount (within the meaning of section 1273) on an obliga-

tion payable 183 days or less from the date of original issue (without regard to the period held by the company).

“(ii) Any interest includible in gross income (including amounts recognized as ordinary income in respect of original issue discount or market discount or acquisition discount under part V of subchapter P and such other amounts as regulations may provide) on an obligation which is in registered form; except that this clause shall not apply to—

“(I) any interest on an obligation issued by a corporation or partnership if the regulated investment company is a 10-percent shareholder in such corporation or partnership, and

“(II) any interest which is treated as not being portfolio interest under the rules of subsection (h)(4).

“(iii) Any interest referred to in subsection (i)(2)(A) (without regard to the trade or business of the regulated investment company).

1 “(iv) Any interest-related dividend in-
 2 cludable in gross income with respect to
 3 stock of another regulated investment com-
 4 pany.

5 “(F) 10-PERCENT SHAREHOLDER.—For
 6 purposes of this paragraph, the term ‘10-per-
 7 cent shareholder’ has the meaning given such
 8 term by subsection (h)(3)(B).

9 “(2) SHORT-TERM CAPITAL GAIN DIVIDENDS.—
 10 “(A) IN GENERAL.—Except as provided in
 11 subparagraph (B), no tax shall be imposed
 12 under paragraph (1)(A) of subsection (a) on
 13 any short-term capital gain dividend received
 14 from a regulated investment company.

15 “(B) EXCEPTION FOR ALIENS TAXABLE
 16 UNDER SUBSECTION (a)(2).—Subparagraph (A)
 17 shall not apply in the case of any nonresident
 18 alien individual subject to tax under subsection
 19 (a)(2).

20 “(C) SHORT-TERM CAPITAL GAIN DIVI-
 21 DEND.—For purposes of this paragraph, a
 22 short-term capital gain dividend is any dividend
 23 (or part thereof) which is designated by the reg-
 24 ulated investment company as a short-term cap-
 25 ital gain dividend in a written notice mailed to

its shareholders not later than 60 days after the close of its taxable year. If the aggregate amount so designated with respect to a taxable year of the company (including amounts so designated with respect to dividends paid after the close of the taxable year described in section 855) is greater than the qualified short-term gain of the company for such taxable year, the portion of each distribution which shall be a short-term capital gain dividend shall be only that portion of the amounts so designated which such qualified short-term gain bears to the aggregate amount so designated.

“(D) QUALIFIED SHORT-TERM GAIN.—For purposes of subparagraph (C), the term ‘qualified short-term gain’ means the excess of the net short-term capital gain of the regulated investment company for the taxable year over the net long-term capital loss (if any) of such company for such taxable year. For purposes of this subparagraph—

“(i) the net short-term capital gain of the regulated investment company shall be computed by treating any short-term capital gain dividend includible in gross in-

1 come with respect to stock of another regu-
 2 lated investment company as a short-term
 3 capital gain, and

4 “(ii) the excess of the net short-term
 5 capital gain for a taxable year over the net
 6 long-term capital loss for a taxable year (to
 7 which an election under section 4982(e)(4)
 8 does not apply) shall be determined with-
 9 out regard to any net capital loss or net
 10 short-term capital loss attributable to
 11 transactions after October 31 of such year,
 12 and any such net capital loss or net short-
 13 term capital loss shall be treated as arising
 14 on the 1st day of the next taxable year.

15 To the extent provided in regulations, clause
 16 (ii) shall apply also for purposes of computing
 17 the taxable income of the regulated investment
 18 company.”

19 (2) FOREIGN CORPORATIONS.—Section 881 is
 20 amended by redesignating subsection (e) as sub-
 21 section (f) and by inserting after subsection (d) the
 22 following new subsection:

23 “(e) TAX NOT TO APPLY TO CERTAIN DIVIDENDS
 24 OF REGULATED INVESTMENT COMPANIES.—

25 “(1) INTEREST-RELATED DIVIDENDS.—

“(A) IN GENERAL.—Except as provided in subparagraph (B), no tax shall be imposed under paragraph (1) of subsection (a) on any interest-related dividend (as defined in section 871(k)(1)) received from a regulated investment company.

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

“(i) to any dividend referred to in section 871(k)(1)(B), and

“(ii) to any interest-related dividend received by a controlled foreign corporation (within the meaning of section 957(a)) to the extent such dividend is attributable to interest received by the regulated investment company from a person who is a related person (within the meaning of section 864(d)(4)) with respect to such controlled foreign corporation.

“(C) TREATMENT OF DIVIDENDS RECEIVED BY CONTROLLED FOREIGN CORPORATIONS.—The rules of subsection (c)(5)(A) shall apply to any interest-related dividend received by a controlled foreign corporation (within the meaning of section 957(a)) to the extent such

dividend is attributable to interest received by the regulated investment company which is described in clause (ii) of section 871(k)(1)(E) (and not described in clause (i) or (iii) of such section).

“(2) SHORT-TERM CAPITAL GAIN DIVIDENDS.—

No tax shall be imposed under paragraph (1) of subsection (a) on any short-term capital gain dividend (as defined in section 871(k)(2)) received from a regulated investment company.”

(3) WITHHOLDING TAXES.—

(A) Subsection (c) of section 1441 is amended by adding at the end the following new paragraph:

“(12) CERTAIN DIVIDENDS RECEIVED FROM REGULATED INVESTMENT COMPANIES.—

“(A) IN GENERAL.—No tax shall be required to be deducted and withheld under subsection (a) from any amount exempt from the tax imposed by section 871(a)(1)(A) by reason of section 871(k).

“(B) SPECIAL RULE.—For purposes of subparagraph (A), clause (i) of section 871(k)(1)(B) shall not apply to any dividend unless the regulated investment company knows

1 that such dividend is a dividend referred to in
 2 such clause. A similar rule shall apply with re-
 3 spect to the exception contained in section
 4 871(k)(2)(B).”

5 (B) Subsection (a) of section 1442 is
 6 amended—

7 (i) by striking “and the reference in
 8 section 1441(c)(10)” and inserting “the
 9 reference in section 1441(c)(10)”, and

10 (ii) by inserting before the period at
 11 the end the following: “, and the references
 12 in section 1441(c)(12) to sections 871(a)
 13 and 871(k) shall be treated as referring to
 14 sections 881(a) and 881(e) (except that for
 15 purposes of applying subparagraph (A) of
 16 section 1441(c)(12), as so modified, clause
 17 (ii) of section 881(e)(1)(B) shall not apply
 18 to any dividend unless the regulated invest-
 19 ment company knows that such dividend is
 20 a dividend referred to in such clause)”.

21 (b) ESTATE TAX TREATMENT OF INTEREST IN CER-
 22 TAIN REGULATED INVESTMENT COMPANIES.—Section
 23 2105 (relating to property without the United States for
 24 estate tax purposes) is amended by adding at the end the
 25 following new subsection:

1 “(d) STOCK IN A RIC.—

2 “(1) IN GENERAL.—For purposes of this sub-
 3 chapter, stock in a regulated investment company
 4 (as defined in section 851) owned by a nonresident
 5 not a citizen of the United States shall not be
 6 deemed property within the United States in the
 7 proportion that, at the end of the quarter of such in-
 8 vestment company’s taxable year immediately pre-
 9 ceding a decedent’s date of death (or at such other
 10 time as the Secretary may designate in regulations),
 11 the assets of the investment company that were
 12 qualifying assets with respect to the decedent bore
 13 to the total assets of the investment company.

14 “(2) QUALIFYING ASSETS.—For purposes of
 15 this subsection, qualifying assets with respect to a
 16 decedent are assets that, if owned directly by the de-
 17 cedent, would have been—

18 “(A) amounts, deposits, or debt obligations
 19 described in subsection (b) of this section,

20 “(B) debt obligations described in the last
 21 sentence of section 2104(c), or

22 “(C) other property not within the United
 23 States.”

24 (c) TREATMENT OF REGULATED INVESTMENT COM-
 25 PANIES UNDER SECTION 897.—

1 (1) Paragraph (1) of section 897(h) is amended
 2 by striking “REIT” each place it appears and in-
 3 serting “qualified investment entity”.

4 (2) Paragraphs (2) and (3) of section 897(h)
 5 are amended to read as follows:

6 “(2) SALE OF STOCK IN DOMESTICALLY-CON-
 7 TROLLED ENTITY NOT TAXED.—The term ‘United
 8 States real property interest’ does not include any
 9 interest in a domestically-controlled qualified invest-
 10 ment entity.

11 “(3) DISTRIBUTIONS BY DOMESTICALLY-CON-
 12 TROLLED QUALIFIED INVESTMENT ENTITIES.—In
 13 the case of a domestically-controlled qualified invest-
 14 ment entity, rules similar to the rules of subsection
 15 (d) shall apply to the foreign ownership percentage
 16 of any gain.”

17 (3) Subparagraphs (A) and (B) of section
 18 897(h)(4) are amended to read as follows:

19 “(A) QUALIFIED INVESTMENT ENTITY.—
 20 The term ‘qualified investment entity’ means
 21 any real estate investment trust and any regu-
 22 lated investment company.

23 “(B) DOMESTICALLY-CONTROLLED.—The
 24 term ‘domestically-controlled qualified invest-
 25 ment entity’ means any qualified investment en-

1 tity in which at all times during the testing pe-
2 riod less than 50 percent in value of the stock
3 was held directly or indirectly by foreign
4 persons.”

5 (4) Subparagraphs (C) and (D) of section
6 897(h)(4) are each amended by striking “REIT”
7 and inserting “qualified investment entity”.

8 (5) The subsection heading for subsection (h) of
9 section 897 is amended by striking “REITS” and
10 inserting “CERTAIN INVESTMENT ENTITIES”.

11 (d) EFFECTIVE DATE.—

12 (1) IN GENERAL.—Except as otherwise pro-
13 vided in this subsection, the amendments made by
14 this section shall apply to dividends with respect to
15 taxable years of regulated investment companies be-
16 ginning after the date of the enactment of this Act.

17 (2) ESTATE TAX TREATMENT.—The amend-
18 ment made by subsection (b) shall apply to estates
19 of decedents dying after the date of the enactment
20 of this Act.

21 (3) CERTAIN OTHER PROVISIONS.—The amend-
22 ments made by subsection (c) (other than paragraph
23 (1) thereof) shall take effect on the date of enact-
24 ment of this Act.

1 **SEC. 313. INTANGIBLE PROPERTY NOT TO INCLUDE CER-**
2 **TAIN PRELIMINARY AGREEMENTS.**

3 (a) IN GENERAL.—Section 936(h)(3)(B) (defining
4 intangible property is amended by adding at the end the
5 following new sentence: “Such term shall not include any
6 preliminary agreement which is not legally enforceable.”

7 (b) EFFECTIVE DATE.—The amendment made by
8 this section shall apply to agreements entered into after
9 the date of enactment of this Act.

10 **SEC. 314. STUDY OF INTEREST ALLOCATION.**

11 (a) STUDY.—The Secretary of the Treasury or the
12 Secretary’s delegate shall conduct a study of the rules
13 under section 864(e) of the Internal Revenue Code of
14 1986 for allocating interest expense of members of an af-
15 filiated group. Such study shall include an analysis of the
16 effect of such rules, including the effects such rules have
17 on different industries.

18 (b) REPORT.—Not later than 6 months after the date
19 of enactment of this Act, the Secretary of the Treasury
20 shall report to the Committee on Ways and Means of the
21 House of Representatives and the Committee on Finance
22 of the Senate the results of the study conducted under
23 subsection (a), including recommendations (if any) for leg-
24 islation.

○