

107TH CONGRESS  
2D SESSION

# H. R. 4151

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

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## IN THE HOUSE OF REPRESENTATIVES

APRIL 10, 2002

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

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## A BILL

To amend the Internal Revenue Code of 1986 to simplify certain rules relating to the taxation of United States businesses 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 “Fairness, Simplification and Competitiveness for Amer-  
7 ican Business Act of 2002”.

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 CONTROLLED FOREIGN CORPORATIONS

Sec. 101. Expansion of de minimis rule under subpart F.

Sec. 102. Clarification of treatment of pipeline transportation income.

Sec. 103. Look-through treatment for sales of partnership interests.

Sec. 104. Repeal of foreign personal holding company rules and foreign invest-  
 ment company rules.

Sec. 105. Determination of foreign personal holding company income with re-  
 spect to transactions in commodities.

Sec. 106. Study of proper treatment of European Union under same country  
 exceptions.

Sec. 107. Effective date.

#### TITLE II—PROVISIONS RELATING TO FOREIGN TAX CREDIT

Sec. 201. Recharacterization of overall domestic loss.

Sec. 202. Special rules relating to financial services income.

Sec. 203. Look-thru rules to apply to dividends from noncontrolled section 902  
 corporations.

Sec. 204. Application of look-thru rules to foreign tax credit.

Sec. 205. Ordering rules for foreign tax credit carryovers; 10-year  
 carryforward.

Sec. 206. Repeal of limitation of foreign tax credit under alternative minimum  
 tax.

Sec. 207. Attribution of stock ownership through partnerships to apply in de-  
 termining section 902 and 960 credits.

Sec. 208. Repeal of special rules for applying foreign tax credit in case of for-  
 eign oil and gas income.

#### TITLE III—OTHER PROVISIONS

Sec. 301. Deduction for dividends received from certain foreign corporations.

Sec. 302. Application of uniform capitalization rules to foreign persons.

Sec. 303. United States property not to include certain assets acquired by deal-  
 ers in ordinary course of trade or business.

Sec. 304. Treatment of certain dividends of regulated investment companies.

Sec. 305. Airline mileage awards to certain foreign persons.

Sec. 306. Interest payments deductible where disqualified guarantee has eco-  
 nomic effect.

Sec. 307. Modifications of reporting requirements for certain foreign-owned cor-  
 porations.

Sec. 308. Election not to use average exchange rate for foreign tax paid other than in functional currency.

Sec. 309. Repeal of special capital gains tax on aliens present in the United States for 183 days or more.

Sec. 310. Repeal of withholding tax on dividends from certain foreign corporations.

Sec. 311. Interest allocation rules.

Sec. 312. Permanent extension of Subpart F exemption for active financing.

Sec. 313. Repeal of treatment of extraterritorial income.

# 1 **TITLE I—TREATMENT OF CON-** 2 **TROLLED FOREIGN COR-** 3 **PORATIONS**

## 4 **SEC. 101. EXPANSION OF DE MINIMIS RULE UNDER SUB-** 5 **PART F.**

6 (a) IN GENERAL.—Clause (ii) of section  
7 954(b)(3)(A) (relating to de minimis, etc., rules) is  
8 amended by striking “\$1,000,000” and inserting  
9 “\$5,000,000”.

10 (b) TECHNICAL AMENDMENTS.—

11 (1) Clause (ii) of section 864(d)(5)(A) is  
12 amended by striking “\$1,000,000” and inserting  
13 “\$5,000,000”.

14 (2) Clause (i) of section 881(c)(5)(A) is amend-  
15 ed by striking “\$1,000,000” and inserting  
16 “\$5,000,000”.

## 17 **SEC. 102. CLARIFICATION OF TREATMENT OF PIPELINE** 18 **TRANSPORTATION INCOME.**

19 Section 954(g)(1) (defining foreign base company oil  
20 related income) is amended by striking “or” at the end  
21 of subparagraph (A), by striking the period at the end

1 of subparagraph (B) and inserting “, or”, and by inserting  
 2 after subparagraph (B) the following new subparagraph:

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

5 **SEC. 103. LOOK-THROUGH TREATMENT FOR SALES OF**  
 6 **PARTNERSHIP INTERESTS.**

7 (a) IN GENERAL.—Section 954(c) (defining foreign  
 8 personal holding company income) is amended by adding  
 9 at the end the following new paragraph:

10 “(4) LOOK-THROUGH RULE FOR CERTAIN  
 11 PARTNERSHIP SALES.—

12 “(A) IN GENERAL.—In the case of any  
 13 sale by a controlled foreign corporation of an  
 14 interest in a partnership with respect to which  
 15 such corporation is a 25-percent owner, such  
 16 corporation shall be treated for purposes of this  
 17 subsection as selling the proportionate share of  
 18 the assets of the partnership attributable to  
 19 such interest.

20 “(B) 25-PERCENT OWNER.—For purposes  
 21 of this paragraph, the term ‘25-percent owner’  
 22 means a controlled foreign corporation which  
 23 owns 25 percent or more of the capital or prof-  
 24 its interest in the partnership. The constructive

1 ownership rules of section 958(b) shall apply  
 2 for purposes of the preceding sentence.”

3 (b) CONFORMING AMENDMENT.—Section  
 4 954(c)(1)(B)(ii) is amended by inserting “except as pro-  
 5 vided in paragraph (4),” before “which”.

6 **SEC. 104. REPEAL OF FOREIGN PERSONAL HOLDING COM-**  
 7 **PANY RULES AND FOREIGN INVESTMENT**  
 8 **COMPANY RULES.**

9 (a) GENERAL RULE.—The following provisions are  
 10 hereby repealed:

11 (1) Part III of subchapter G of chapter 1 (re-  
 12 lating to foreign personal holding companies).

13 (2) Section 1246 (relating to gain on foreign in-  
 14 vestment company stock).

15 (3) Section 1247 (relating to election by foreign  
 16 investment companies to distribute income cur-  
 17 rently).

18 (b) EXEMPTION OF FOREIGN CORPORATIONS FROM  
 19 PERSONAL HOLDING COMPANY RULES.—

20 (1) IN GENERAL.—Subsection (c) of section  
 21 542 (relating to exceptions) is amended—

22 (A) by striking paragraph (5) and insert-  
 23 ing the following:

24 “(5) a foreign corporation,”

1 (B) by striking paragraphs (7) and (10)  
2 and by redesignating paragraphs (8) and (9) as  
3 paragraphs (7) and (8), respectively,

4 (C) by inserting “and” at the end of para-  
5 graph (7) (as so redesignated), and

6 (D) by striking “; and” at the end of para-  
7 graph (8) (as so redesignated) and inserting a  
8 period.

9 (2) TREATMENT OF INCOME FROM PERSONAL  
10 SERVICE CONTRACTS.—Paragraph (1) of section  
11 954(c) is amended by adding at the end the fol-  
12 lowing new subparagraph:

13 “(H) PERSONAL SERVICE CONTRACTS.—

14 “(i) Amounts received under a con-  
15 tract under which the corporation is to fur-  
16 nish personal services; if some person other  
17 than the corporation has the right to des-  
18 ignate (by name or by description) the in-  
19 dividual who is to perform the services, or  
20 if the individual who is to perform the  
21 services is designated (by name or by de-  
22 scription) in the contract; and

23 “(ii) amounts received from the sale  
24 or other disposition of such a contract.

1           This subparagraph shall apply with respect to  
2           amounts received for services under a particular  
3           contract only if at some time during the taxable  
4           year 25 percent or more in value of the out-  
5           standing stock of the corporation is owned, di-  
6           rectly or indirectly, by or for the individual who  
7           has performed, is to perform, or may be des-  
8           ignated (by name or by description) as the one  
9           to perform, such services.”

10       (c) CONFORMING AMENDMENTS.—

11           (1) Paragraph (2) of section 171(c) is  
12       amended—

13                (A) by striking “, or by a foreign personal  
14           holding company, as defined in section 552”,  
15           and

16                (B) by striking “, or a foreign personal  
17           holding company”.

18           (2) Paragraph (2) of section 245(a) is amended  
19       by striking “foreign personal holding company or”

20           (3) Section 312 is amended by striking sub-  
21       section (j).

22           (4) Subsection (m) of section 312 is amended  
23       by striking “, a foreign investment company (within  
24       the meaning of section 1246(b)), or a foreign per-

sonal holding company (within the meaning of section 552)’’.

(5) Subsection (e) of section 443 is amended by striking paragraph (3) and by redesignating paragraphs (4) and (5) as paragraphs (3) and (4), respectively.

(6) Subparagraph (B) of section 465(c)(7) is amended to by adding “or” at the end of clause (i), by striking clause (ii), and by redesignating clause (iii) as clause (ii).

(7) Paragraph (1) of section 543(b) is amended by inserting “and” at the end of subparagraph (A), by striking “, and” at the end of subparagraph (B) and inserting a period, and by striking subparagraph (C).

(8) Paragraph (1) of section 562(b) is amended by striking “or a foreign personal holding company described in section 552”.

(9) Section 563 is amended—

(A) by striking subsection (c),

(B) by redesignating subsection (d) as subsection (c), and

(C) by striking “subsection (a), (b), or (c)” in subsection (c) (as so redesignated) and inserting “subsection (a) or (b)”.



1           (10) Subsection (d) of section 751 is amended  
2           by adding “and” at the end of paragraph (2), by  
3           striking paragraph (3), by redesignating paragraph  
4           (4) as paragraph (3), and by striking “paragraph  
5           (1), (2), or (3)” in paragraph (3) (as so redesign-  
6           ated) and inserting paragraph (1) or (2)”.

7           (11) Paragraph (2) of section 864(d) is amend-  
8           ed by striking subparagraph (A) and by redesign-  
9           ating subparagraphs (B) and (C) as subparagraphs  
10          (A) and (B), respectively.

11          (12)(A) Subparagraph (A) of section 898(b)(1)  
12          is amended to read as follows:

13                 “(A) which is treated as a controlled for-  
14                 eign corporation for any purpose under subpart  
15                 F of part III of this subchapter, and”.

16          (B) Subparagraph (B) of section 898(b)(2) is  
17          amended by striking “and sections 551(f) and 554,  
18          whichever are applicable,”.

19          (C) Paragraph (3) of section 898(b) is amended  
20          to read as follows:

21                 “(3) UNITED STATES SHAREHOLDER.—The  
22                 term ‘United States shareholder’ has the meaning  
23                 given to such term by section 951(b), except that, in  
24                 the case of a foreign corporation having related per-  
25                 son insurance income (as defined in section

1       953(c)(2)), the Secretary may treat any person as a  
 2       United States shareholder for purposes of this sec-  
 3       tion if such person is treated as a United States  
 4       shareholder under section 953(c)(1).”

5               (D) Subsection (c) of section 898 is amended to  
 6       read as follows:

7       “(c) DETERMINATION OF REQUIRED YEAR.—

8               “(1) IN GENERAL.—The required year is—

9                       “(A) the majority U.S. shareholder year,  
 10                      or

11                     “(B) if there is no majority U.S. share-  
 12                     holder year, the taxable year prescribed under  
 13                     regulations.

14               “(2) 1-MONTH DEFERRAL ALLOWED.—A speci-  
 15       fied foreign corporation may elect, in lieu of the tax-  
 16       able year under paragraph (1)(A), a taxable year be-  
 17       ginning 1 month earlier than the majority U.S.  
 18       shareholder year.

19               “(3) MAJORITY U.S. SHAREHOLDER YEAR.—

20                     “(A) IN GENERAL.—For purposes of this  
 21       subsection, the term ‘majority U.S. shareholder  
 22       year’ means the taxable year (if any) which, on  
 23       each testing day, constituted the taxable year  
 24       of—

1 “(i) each United States shareholder  
2 described in subsection (b)(2)(A), and

3 “(ii) each United States shareholder  
4 not described in clause (i) whose stock was  
5 treated as owned under subsection  
6 (b)(2)(B) by any shareholder described in  
7 such clause.

8 “(B) TESTING DAY.—The testing days  
9 shall be—

10 “(i) the first day of the corporation’s  
11 taxable year (determined without regard to  
12 this section), or

13 “(ii) the days during such representa-  
14 tive period as the Secretary may pre-  
15 scribe.”

16 (13) Clause (ii) of section 904(d)(2) is amended  
17 to read as follows:

18 “(ii) CERTAIN AMOUNTS INCLUDED.—  
19 Except as provided in clause (iii), the term  
20 ‘passive income’ includes, except as pro-  
21 vided in subparagraph (E)(iii) or para-  
22 graph (3)(I), any amount includible in  
23 gross income under section 1293 (relating  
24 to certain passive foreign investment com-  
25 panies).”

1           (14)(A) Subparagraph (A) of section 904(g)(1)  
2           is amended by adding “or” at the end of clause (i),  
3           by striking clause (ii), and by redesignating clause  
4           (iii) as clause (ii).

5           (B) The paragraph heading of paragraph (2) of  
6           section 904(g) is amended by striking “FOREIGN  
7           PERSONAL HOLDING OR”.

8           (15) Section 951 is amended by striking sub-  
9           sections (c) and (d) and by redesignating subsections  
10          (e) and (f) as subsections (c) and (d), respectively.

11          (16) Paragraph (3) of section 989(b) is amend-  
12          ed by striking “, 551(a),”.

13          (17) Paragraph (5) of section 1014(b) is hereby  
14          repealed.

15          (18) Subsection (a) of section 1016 is amended  
16          by striking paragraph (13) and by redesignating the  
17          following paragraphs accordingly.

18          (19)(A) Paragraph (3) of section 1212(a) is  
19          amended to read as follows:

20               “(3) SPECIAL RULES ON CARRYBACKS.—A net  
21               capital loss of a corporation shall not be carried  
22               back under paragraph (1)(A) to a taxable year—

23                       “(A) for which it is a regulated investment  
24                       company (as defined in section 851), or

1           “(B) for which it is a real estate invest-  
2           ment trust (as defined in section 856).”

3           (B) The amendment made by subparagraph (A)  
4           shall apply to taxable years beginning after Decem-  
5           ber 31, 2004.

6           (20) Section 1223 is amended by striking para-  
7           graph (10) and by redesignating the following para-  
8           graphs accordingly.

9           (21) Subsection (d) of section 1248 is amended  
10          by striking paragraph (5) and by redesignating  
11          paragraphs (6) and (7) as paragraphs (5) and (6),  
12          respectively.

13          (22) Paragraph (2) of section 1260(c) is  
14          amended by striking subparagraphs (H) and (I) and  
15          by redesignating subparagraph (J) as subparagraph  
16          (H).

17          (23) Subparagraph (F) of section 1291(b)(3) is  
18          amended by striking “551(d), 959(a),” and inserting  
19          “959(a)”.

20          (24) Paragraph (2) of section 1294(a) is  
21          amended to read as follows:

22               “(2) ELECTION NOT PERMITTED WHERE  
23               AMOUNTS OTHERWISE INCLUDIBLE UNDER SECTION  
24               951.—The taxpayer may not make an election under  
25               paragraph (1) with respect to the undistributed

1 PFIC earnings tax liability attributable to a quali-  
2 fied electing fund for the taxable year if any amount  
3 is includible in the gross income of the taxpayer  
4 under section 951 with respect to such fund for such  
5 taxable year.”

6 (25) Section 6035 is hereby repealed.

7 (26) Subparagraph (D) of section 6103(e)(1) is  
8 amended by striking clause (iv) and redesignating  
9 clauses (v) and (vi) as clauses (iv) and (v), respec-  
10 tively.

11 (27) Subparagraph (B) of section 6501(e)(1) is  
12 amended to read as follows:

13 “(B) CONSTRUCTIVE DIVIDENDS.—If the  
14 taxpayer omits from gross income an amount  
15 properly includible therein under section  
16 951(a), the tax may be assessed, or a pro-  
17 ceeding in court for the collection of such tax  
18 may be done without assessing, at any time  
19 within 6 years after the return was filed.”

20 (28) Subsection (a) of section 6679 is  
21 amended—

22 (A) by striking “6035, 6046, and 6046A”  
23 in paragraph (1) and inserting “6046 and  
24 6046A”, and

25 (B) by striking paragraph (3).

1           (29) Sections 170(f)(10)(A), 508(d), 4947 and  
 2           section 4948(c)(4) are each amended by striking  
 3           “556(b)(2),” each place it appears.

4           (30) The table of parts for subchapter G of  
 5           chapter 1 is amended by striking the item relating  
 6           to part III.

7           (31) The table of sections for part IV of sub-  
 8           chapter P of chapter 1 is amended by striking the  
 9           items relating to sections 1246 and 1247.

10          (32) The table of sections for subpart A of part  
 11          III of subchapter A of chapter 61 of such Code is  
 12          amended by striking the item relating to section  
 13          6035.

14   **SEC. 105. DETERMINATION OF FOREIGN PERSONAL HOLD-**  
 15                           **ING COMPANY INCOME WITH RESPECT TO**  
 16                           **TRANSACTIONS IN COMMODITIES.**

17          (a) IN GENERAL.—Clauses (i) and (ii) of section  
 18          954(c)(1)(C) (relating to commodity transactions) are  
 19          amended to read as follows:

20                           “(i) arise out of commodity hedging  
 21                           transactions (as defined in paragraph  
 22                           (5)(A)),

23                           “(ii) are active business gains or  
 24                           losses from the sale of commodities, but  
 25                           only if substantially all of the controlled

1 foreign corporation's commodities are  
 2 property described in paragraph (1), (2) or  
 3 (8) of section 1221(a), or”.

4 (b) DEFINITION AND SPECIAL RULES.—Subsection  
 5 (c) of section 954 is amended by adding after paragraph  
 6 (4) the following new paragraph:

7 “(5) DEFINITION AND SPECIAL RULES RELAT-  
 8 ING TO COMMODITY TRANSACTIONS.—

9 “(A) COMMODITY HEDGING TRANS-  
 10 ACTIONS.—For purposes of paragraph  
 11 (1)(C)(i), the term ‘commodity hedging trans-  
 12 action’ means any transaction with respect to a  
 13 commodity if such transaction—

14 “(i) is a hedging transaction as de-  
 15 fined in section 1221(b)(2), determined—

16 “(I) without regard to subpara-  
 17 graph (A)(ii) thereof,

18 “(II) by applying subparagraph  
 19 (A)(i) thereof by substituting ‘ordi-  
 20 nary property or property described in  
 21 section 1231(b)’ for ‘ordinary prop-  
 22 erty’, and

23 “(III) by substituting ‘controlled  
 24 foreign corporation’ for ‘taxpayer’  
 25 each place it appears, and



1 “(ii) is clearly identified as such in ac-  
2 cordance with section 1221(a)(7).

3 “(B) REGULATIONS.—The Secretary shall  
4 prescribe such regulations as are appropriate to  
5 carry out the purposes of paragraph (1)(C) in  
6 the case of transactions involving related par-  
7 ties.”

8 (c) EFFECTIVE DATE.—The amendments made by  
9 this section shall apply to commodity hedging transactions  
10 entered into on or after the date of enactment of this Act.

11 **SEC. 106. STUDY OF PROPER TREATMENT OF EUROPEAN**  
12 **UNION UNDER SAME COUNTRY EXCEPTIONS.**

13 (a) STUDY.—The Secretary of the Treasury or the  
14 Secretary’s delegate shall conduct a study on the feasi-  
15 bility of treating all countries included in the European  
16 Union as 1 country for purposes of applying the same  
17 country exceptions under subpart F of part III of sub-  
18 chapter N of chapter 1 of the Internal Revenue Code of  
19 1986. Such study shall include consideration of methods  
20 of ensuring that taxpayers are subject to a substantial ef-  
21 fective rate of foreign tax in such countries if such treat-  
22 ment is adopted.

23 (b) REPORT.—Not later than 6 months after the date  
24 of the enactment of this Act, the Secretary of the Treasury  
25 shall report to the Committee on Ways and Means of the

1 House of Representatives and the Committee on Finance  
 2 of the Senate the results of the study conducted under  
 3 subsection (a), including recommendations (if any) for leg-  
 4 islation.

5 **SEC. 107. EFFECTIVE DATE.**

6 Except as otherwise provided in this title, the amend-  
 7 ments made by this title shall apply to taxable years of  
 8 foreign corporations beginning after December 31, 2002,  
 9 and taxable years of United States persons owning stock  
 10 in such corporations with or within which such corpora-  
 11 tions' taxable years end.

12 **TITLE II—PROVISIONS RELAT-**  
 13 **ING TO FOREIGN TAX CREDIT**

14 **SEC. 201. RECHARACTERIZATION OF OVERALL DOMESTIC**  
 15 **LOSS.**

16 (a) GENERAL RULE.—Section 904 is amended by re-  
 17 designating subsections (g), (h), (i), (j), and (k) as sub-  
 18 sections (h), (i), (j), (k), and (l) respectively, and by in-  
 19 serting after subsection (f) the following new subsection:

20 “(g) RECHARACTERIZATION OF OVERALL DOMESTIC  
 21 LOSS.—

22 “(1) GENERAL RULE.—For purposes of this  
 23 subpart, in the case of any taxpayer who sustains an  
 24 overall domestic loss for any taxable year beginning  
 25 after December 31, 2002, that portion of the tax-

1       payer’s taxable income from sources within the  
 2       United States for each succeeding taxable year  
 3       which is equal to the lesser of—

4               “(A) the amount of such loss (to the extent  
 5               not used under this paragraph in prior taxable  
 6               years), or

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

13               “(2) OVERALL DOMESTIC LOSS DEFINED.—For  
 14       purposes of this subsection and section 936—

15               “(A) IN GENERAL.—The term ‘overall do-  
 16               mestic loss’ means any domestic loss to the ex-  
 17               tent such loss offsets taxable income from  
 18               sources without the United States for the tax-  
 19               able year or for any preceding taxable year by  
 20               reason of a carryback. For purposes of the pre-  
 21               ceding sentence, the term ‘domestic loss’ means  
 22               the amount by which the gross income for the  
 23               taxable year from sources within the United  
 24               States is exceeded by the sum of the deductions  
 25               properly apportioned or allocated thereto (deter-

1           mined without regard to any carryback from a  
2           subsequent taxable year).

3           “(B) TAXPAYER MUST HAVE ELECTED  
4           FOREIGN TAX CREDIT FOR YEAR OF LOSS.—  
5           The term ‘overall domestic loss’ shall not in-  
6           clude any loss for any taxable year unless the  
7           taxpayer chose the benefits of this subpart for  
8           such taxable year.

9           “(3) CHARACTERIZATION OF SUBSEQUENT IN-  
10          COME.—

11           “(A) IN GENERAL.—Any income from  
12           sources within the United States that is treated  
13           as income from sources without the United  
14           States under paragraph (1) shall be allocated  
15           among and increase the income categories in  
16           proportion to the loss from sources within the  
17           United States previously allocated to those in-  
18           come categories.

19           “(B) INCOME CATEGORY.—For purposes of  
20           this paragraph, the term ‘income category’ has  
21           the meaning given such term by subsection  
22           (f)(5)(E)(i).

23           “(4) COORDINATION WITH SUBSECTION (f).—  
24          The Secretary shall prescribe such regulations as

1       may be necessary to coordinate the provisions of this  
2       subsection with the provisions of subsection (f).”

3       (b) CONFORMING AMENDMENTS.—

4           (1) Section 535(d)(2) is amended by striking  
5       “section 904(g)(6)” and inserting “section  
6       904(h)(6)”.

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

10       (c) EFFECTIVE DATE.—The amendments made by  
11       this section shall apply to losses for taxable years begin-  
12       ning after December 31, 2002.

13       **SEC. 202. SPECIAL RULES RELATING TO FINANCIAL SERV-**  
14       **ICES INCOME.**

15       (a) EXCEPTION FOR INTEREST ON CERTAIN SECURI-  
16       TIES.—Section 904(d)(2)(B) (relating to high withholding  
17       tax interest) is amended by redesignating clause (iii) as  
18       clause (iv) and by inserting after clause (ii) the following  
19       new clause:

20                       “(iii) EXCEPTION FOR INTEREST ON  
21                       DEALER PROPERTY.—The term ‘high with-  
22                       holding tax interest’ shall not include any  
23                       interest on a security (within the meaning  
24                       of section 475(c)(2)) which is received or  
25                       accrued by a person that holds the security

1 in connection with the holder’s activities as  
 2 a dealer in securities (within the meaning  
 3 of section 475(c)(1)).”

4 (b) FINANCIAL SERVICES INCOME IN EXCESS OF 80  
 5 PERCENT OF GROSS INCOME.—Section 904(d)(2)(C) (re-  
 6 lating to financial services income) is amended by adding  
 7 at the end the following new clause:

8 “(iv) INCOME EXCEEDING 80 PERCENT  
 9 OF GROSS INCOME.—If the financial serv-  
 10 ices income (as defined in clause (i)) of  
 11 any person exceeds 80 percent of gross in-  
 12 come, the entire gross income for the tax-  
 13 able year shall be treated as financial serv-  
 14 ices income.”

15 (c) EXCEPTION FOR INCOME ON DEALER PROP-  
 16 erty.—Subsection 904(g) (relating to source rules in case  
 17 of United States-owned foreign corporations) is amended  
 18 by redesignating paragraph (11) as paragraph (12) and  
 19 by adding after paragraph (10) the following new para-  
 20 graph:

21 “(11) EXCEPTION FOR INCOME ON DEALER  
 22 PROPERTY.—Paragraph (1) shall not apply to any  
 23 amount derived from a United States-owned foreign  
 24 corporation that is derived from income on a secu-  
 25 rity (within the meaning of section 475(c)(2)) which

1 is received or accrued by a person that holds the se-  
 2 curity in connection with the holder's activities as a  
 3 dealer in securities (within the meaning of section  
 4 475(c)(1)).”

5 (d) EFFECTIVE DATES.—

6 (1) IN GENERAL.—The amendments made by  
 7 this section shall apply to taxable years beginning  
 8 after December 31, 2002.

9 (2) DEEMED PAID CREDITS.—In the case of  
 10 any credit under section 901 of the Internal Revenue  
 11 Code of 1986 by reason of section 902 or 960 of  
 12 such Code, the amendments made by this section  
 13 shall apply to taxable years of foreign corporations  
 14 beginning after December 31, 2002, and to taxable  
 15 years of United States shareholders in such corpora-  
 16 tions with or within which such taxable years of for-  
 17 eign corporations end.

18 **SEC. 203. LOOK-THRU RULES TO APPLY TO DIVIDENDS**  
 19 **FROM NONCONTROLLED SECTION 902 COR-**  
 20 **PORATIONS.**

21 (a) IN GENERAL.—Section 904(d)(4) (relating to  
 22 look-thru rules apply to dividends from noncontrolled sec-  
 23 tion 902 corporations) is amended to read as follows:

24 “(4) LOOK-THRU APPLIES TO DIVIDENDS FROM  
 25 NONCONTROLLED SECTION 902 CORPORATIONS.—

1           “(A) IN GENERAL.—For purposes of this  
2 subsection, any dividend from a noncontrolled  
3 section 902 corporation with respect to the tax-  
4 payer shall be treated as income in a separate  
5 category in proportion to the ratio of—

6                   “(i) the portion of earnings and prof-  
7 its attributable to income in such category,  
8 to

9                   “(ii) the total amount of earnings and  
10 profits.

11           “(B) SPECIAL RULES.—For purposes of  
12 this paragraph—

13                   “(i) IN GENERAL.—Rules similar to  
14 the rules of paragraph (3)(F) shall apply.

15                   “(ii) EARNINGS AND PROFITS.—

16                           “(I) IN GENERAL.—The rules of  
17 section 316 shall apply.

18                           “(II) REGULATIONS.—The Sec-  
19 retary may prescribe regulations re-  
20 garding the treatment of distributions  
21 out of earnings and profits for periods  
22 before the taxpayer’s acquisition of  
23 the stock to which the distributions  
24 relate.



1 “(iii) DIVIDENDS NOT ALLOCABLE TO  
2 SEPARATE CATEGORY.—The portion of any  
3 dividend from a noncontrolled section 902  
4 corporation which is not treated as income  
5 in a separate category under subparagraph  
6 (A) shall be treated as a dividend to which  
7 subparagraph (A) does not apply.

8 “(iv) LOOK-THRU WITH RESPECT TO  
9 CARRYFORWARDS OF CREDIT.—Rules simi-  
10 lar to subparagraph (A) also shall apply to  
11 any carryforward under subsection (c)  
12 from a taxable year beginning before Janu-  
13 ary 1, 2002, of tax allocable to a dividend  
14 from a noncontrolled section 902 corpora-  
15 tion with respect to the taxpayer.”.

16 (b) CONFORMING AMENDMENTS.—

17 (1) Subparagraph (E) of section 904(d)(1), as  
18 in effect both before and after the amendments  
19 made by section 1105 of the Taxpayer Relief Act of  
20 1997, is hereby repealed.

21 (2) Section 904(d)(2)(C)(iii), as so in effect, is  
22 amended by striking subclause (II) and by redesign-  
23 ating subclause (III) as subclause (II).

1           (3) The last sentence of section 904(d)(2)(D),  
 2           as so in effect, is amended to read as follows: “Such  
 3           term does not include any financial services income.”

4           (4) Section 904(d)(2)(E) is amended by strik-  
 5           ing clauses (ii) and (iv) and by redesignating clause  
 6           (iii) as clause (ii).

7           (5) Section 904(d)(3)(F) is amended by strik-  
 8           ing “(D), or (E)” and inserting “or (D)”.

9           (6) Section 864(d)(5)(A)(i) is amended by  
 10          striking “(C)(iii)(III)” and inserting “(C)(iii)(II)”.

11          (c) EFFECTIVE DATE.—The amendments made by  
 12          this section shall apply to taxable years beginning after  
 13          December 31, 2001.

14      **SEC. 204. APPLICATION OF LOOK-THRU RULES TO FOREIGN**  
 15                              **TAX CREDIT.**

16          (a) INTEREST, RENTS, AND ROYALTIES.—

17               (1) NONCONTROLLED SECTION 902 CORPORA-  
 18          TION.—Section 904(d)(4)(A), as amended by section  
 19          203, is amended to read as follows:

20                       “(A) IN GENERAL.—For purposes of this  
 21          subsection—

22                               “(i) any applicable dividend shall be  
 23                               treated as income in a separate category in  
 24                               proportion to the ratio of—

1 “(I) the portion of the earnings  
2 and profits attributable to income in  
3 such category, to

4 “(II) the total amount of earn-  
5 ings and profits, and

6 “(ii) any interest, rent, or royalty  
7 which is received or accrued from a non-  
8 controlled section 902 corporation with re-  
9 spect to the taxpayer shall be treated as  
10 income in a separate category to the extent  
11 it is properly allocable (under regulations  
12 prescribed by the Secretary) to income of  
13 such corporation in such category.”

14 (2) PARTNERSHIPS.—Section 904(d)(6)(C) (re-  
15 lating to regulations) is amended—

16 (A) by inserting “or (4)(A)(ii)” after  
17 “paragraph (3)(C)”, and

18 (B) by inserting “or noncontrolled section  
19 902 corporations, whichever is applicable” after  
20 “controlled foreign corporations”.

21 (3) CONFORMING AMENDMENT.—The heading  
22 for section 904(d)(4), as amended by section 203, is  
23 amended by inserting “, INTEREST, RENTS, OR ROY-  
24 ALTIES” after “DIVIDENDS”.

1 (b) EFFECTIVE DATE.—The amendments made by  
 2 this section shall apply to taxable years beginning after  
 3 December 31, 2002.

4 **SEC. 205. ORDERING RULES FOR FOREIGN TAX**  
 5 **CARRYOVERS; 10-YEAR CARRYFORWARD.**

6 (a) IN GENERAL.—Section 904(c) (relating to  
 7 carryback and carryover of excess tax paid) is amended  
 8 to read as follows:

9 “(c) CARRYBACK AND CARRYFORWARD OF EXCESS  
 10 FOREIGN TAXES.—

11 “(1) CARRYFORWARDS USED FIRST.—If, for  
 12 any taxable year for which the taxpayer elects to  
 13 have the benefits of this subpart apply, the sum of—

14 “(A) the foreign tax carryforwards under  
 15 this subsection to such taxable year, and

16 “(B) the amount of foreign taxes paid or  
 17 accrued for the taxable year,

18 exceeds the limitation under subsection (a), such ex-  
 19 cess (to the extent attributable to the taxes de-  
 20 scribed in subparagraph (B)) shall be a foreign tax  
 21 carryback to each of the 2 preceding taxable years  
 22 and a foreign tax carryforward to each of the 10 fol-  
 23 lowing taxable years.

24 “(2) AMOUNTS CARRIED TO EARLIEST  
 25 YEARS.—The entire amount of the excess described

1 in paragraph (1) for any taxable year shall be car-  
2 ried to the earliest of the 12 taxable years to which  
3 (by reason of paragraph (1)) such excess may be  
4 carried. The amount of such excess shall be carried  
5 to each of the other 11 taxable years to the extent  
6 that such excess may not be taken into account  
7 under subsection (a) for a prior taxable year because  
8 of the limitations of paragraph (3).

9 “(3) ORDERING RULES.—For purposes of de-  
10 termining under this subsection whether foreign  
11 taxes are taken into account for a taxable year or  
12 as a carryback or carryforward, such taxes shall be  
13 treated as taken into account in the order of the tax-  
14 able years in which such taxes were actually paid or  
15 accrued, beginning with the earliest such year.

16 “(4) LIMITATIONS.—

17 “(A) CARRYBACKS USED LAST.—The ex-  
18 cess described in paragraph (1) for any taxable  
19 year (hereafter in this paragraph referred to as  
20 the ‘current taxable year’) which is carried to  
21 any preceding taxable year shall not exceed the  
22 amount by which the limitation under sub-  
23 section (a) for such preceding taxable year ex-  
24 ceeds the sum of—

1 “(i) the foreign taxes paid or accrued  
2 for such preceding taxable year, and

3 “(ii) the amount of the foreign taxes  
4 paid or accrued for any taxable year earlier  
5 than the current taxable year which have  
6 been carried to such preceding taxable year  
7 (whether or not the taxpayer chooses to  
8 have the benefits of this subpart with re-  
9 spect to such earlier taxable year).

10 “(B) CREDIT ONLY.—Taxes may be car-  
11 ried to a taxable year under this subsection only  
12 if the taxpayer chooses for such taxable year to  
13 have the benefits of this subpart apply to for-  
14 eign taxes paid or accrued for such year. Any  
15 amount so carried may be availed of only as a  
16 credit and not a deduction.

17 “(C) CARRYFORWARDS.—The excess de-  
18 scribed in paragraph (1) for a taxable year  
19 which is carried to any succeeding taxable year  
20 shall not exceed the amount by which the limi-  
21 tation under subsection (a) for such succeeding  
22 taxable year exceeds the sum of the amounts  
23 which, by reason of this subsection, are carried  
24 to such succeeding taxable year and are attrib-

1           utable to taxable years preceding the taxable  
2           year of such excess.

3           “(5) FOREIGN TAXES.—For purposes of this  
4           subsection, the term ‘foreign taxes’ means taxes paid  
5           or accrued to foreign countries or any possessions of  
6           the United States.”

7           (b) EFFECTIVE DATE.—The amendment made by  
8           this section shall apply to taxes paid or accrued for taxable  
9           years beginning after December 31, 2002, and to  
10          carryforwards of taxes from taxable years beginning after  
11          December 31, 1997.

12   **SEC. 206. REPEAL OF LIMITATION OF FOREIGN TAX CREDIT**  
13                           **UNDER ALTERNATIVE MINIMUM TAX.**

14          (a) IN GENERAL.—Section 59(a) (relating to alter-  
15          native minimum tax foreign tax credit) is amended by  
16          striking paragraph (2) and by redesignating paragraphs  
17          (3) and (4) as paragraphs (2) and (3), respectively.

18          (b)           CONFORMING           AMENDMENT.—Section  
19          53(d)(1)(B)(i)(II) is amended by striking “and if section  
20          59(a)(2) did not apply”.

21          (c) EFFECTIVE DATE.—The amendments made by  
22          this section shall apply to taxable years beginning after  
23          December 31, 2002.

1 **SEC. 207. ATTRIBUTION OF STOCK OWNERSHIP THROUGH**  
2 **PARTNERSHIPS TO APPLY IN DETERMINING**  
3 **SECTION 902 AND 960 CREDITS.**

4 (a) IN GENERAL.—Subsection (c) of section 902 is  
5 amended by redesignating paragraph (7) as paragraph (8)  
6 and by inserting after paragraph (6) the following new  
7 paragraph:

8 “(7) CONSTRUCTIVE OWNERSHIP THROUGH  
9 PARTNERSHIPS.—Stock owned, directly or indirectly,  
10 by or for a partnership shall be considered as being  
11 owned proportionately by its partners. Stock consid-  
12 ered to be owned by a person by reason of the pre-  
13 ceding sentence shall, for purposes of applying such  
14 sentence, be treated as actually owned by such per-  
15 son. The Secretary may prescribe such regulations  
16 as may be necessary to carry out the purposes of  
17 this paragraph, including rules to account for special  
18 partnership allocations of dividends, credits, and  
19 other incidents of ownership of stock in determining  
20 proportionate ownership.”

21 (b) EFFECTIVE DATE.—The amendment made by  
22 this section shall apply to taxes of foreign corporations  
23 for taxable years of such corporations beginning after De-  
24 cember 31, 2002.



1 **SEC. 208. REPEAL OF SPECIAL RULES FOR APPLYING FOR-**  
 2 **EIGN TAX CREDIT IN CASE OF FOREIGN OIL**  
 3 **AND GAS INCOME.**

4 (a) IN GENERAL.—Section 907 (relating to special  
 5 rules in case of foreign oil and gas income) is repealed.

6 (b) CONFORMING AMENDMENTS.—

7 (1) Each of the following provisions are amend-  
 8 ed by striking “907,”:

9 (A) Section 245(a)(10).

10 (B) Section 865(h)(1)(B).

11 (C) Section 904(d)(1).

12 (D) Section 904(g)(10)(A).

13 (2) Section 904(f)(5)(E)(iii) is amended by in-  
 14 serting “, as in effect before its repeal by the Fair-  
 15 ness, Simplification and Competitiveness for Amer-  
 16 ican Business Act of 2002” after “section  
 17 907(c)(4)(B)”.

18 (3) Section 954(g)(1) is amended by inserting  
 19 “, as in effect before its repeal by the Fairness, Sim-  
 20 plification and Competitiveness for American Busi-  
 21 ness Act of 2002” after “907(c)”.

22 (4) Section 6501(i) is amended—

23 (A) by striking “, or under section 907(f)  
 24 (relating to carryback and carryover of dis-  
 25 allowed oil and gas extraction taxes)”, and

26 (B) by striking “or 907(f)”.

1           (5) The table of sections for subpart A of part  
 2           III of subchapter N of chapter 1 is amended by  
 3           striking the item relating to section 907.

4           (c) EFFECTIVE DATE.—The amendments made by  
 5           this section shall apply to taxable years beginning after  
 6           December 31, 2002.

## 7       **TITLE III—OTHER PROVISIONS**

### 8       **SEC. 301. DEDUCTION FOR DIVIDENDS RECEIVED FROM** 9                               **CERTAIN FOREIGN CORPORATIONS.**

10          (a) CONSTRUCTIVE OWNERSHIP RULES TO APPLY IN  
 11       DETERMINING 80-PERCENT OWNERSHIP.—Section 245  
 12       (a)(5) (relating to post-1986 undistributed U.S. earnings)  
 13       is amended by adding at the end the following flush sen-  
 14       tence:

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

17          (b) DIVIDENDS TO INCLUDE SUBPART F DISTRIBU-  
 18       TIONS.—Section 245(a) (relating to dividends from 10-  
 19       percent owned foreign corporations) is amended by adding  
 20       at the end the following new paragraph:

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

1 (c) EFFECTIVE DATE.—The amendments made by  
2 this section shall apply to taxable years beginning after  
3 December 31, 2002.

4 **SEC. 302. APPLICATION OF UNIFORM CAPITALIZATION**  
5 **RULES TO FOREIGN PERSONS.**

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

9 “(7) FOREIGN PERSONS.—Except for purposes  
10 of applying sections 871(b)(1) and 882(a)(1), this  
11 section shall not apply to any taxpayer who is not  
12 a United States person if such taxpayer capitalizes  
13 costs of produced property or property acquired for  
14 resale by applying the method used to ascertain the  
15 income, profit, or loss for purposes of reports or  
16 statements to shareholders, partners, other propri-  
17 etors, or beneficiaries, or for credit purposes.”

18 (b) EFFECTIVE DATE.—The amendment made by  
19 subsection (a) shall apply to taxable years beginning after  
20 December 31, 2002. Section 481 of the Internal Revenue  
21 Code of 1986 shall not apply to any change in a method  
22 of accounting by reason of such amendment.

1 **SEC. 303. UNITED STATES PROPERTY NOT TO INCLUDE**  
2 **CERTAIN ASSETS ACQUIRED BY DEALERS IN**  
3 **ORDINARY COURSE OF TRADE OR BUSINESS.**

4 (a) IN GENERAL.—Section 956(c)(2) (relating to ex-  
5 ceptions from property treated as United States property)  
6 is amended by striking “and” at the end of subparagraph  
7 (J), by striking the period at the end of subparagraph (K)  
8 and inserting “; and”, and by adding at the end the fol-  
9 lowing new subparagraph:

10 “(L) securities acquired and held by a con-  
11 trolled foreign corporation in the ordinary  
12 course of its business as a dealer in securities  
13 if (i) the dealer accounts for the securities as  
14 securities held primarily for sale to customers  
15 in the ordinary course of business, and (ii) the  
16 dealer disposes of the securities (or such securi-  
17 ties mature while held by the dealer) within a  
18 period consistent with the holding of securities  
19 for sale to customers in the ordinary course of  
20 business.”

21 (b) CONFORMING AMENDMENT.—Section 956(c)(2)  
22 is amended by striking “and (K)” in the last sentence and  
23 inserting “, (K), and (L)”.

24 (c) EFFECTIVE DATE.—The amendments made by  
25 this section shall apply to taxable years of foreign corpora-  
26 tions beginning after December 31, 2002, and to taxable

1 years of United States shareholders with or within which  
 2 such taxable years of foreign corporations end.

3 **SEC. 304. TREATMENT OF CERTAIN DIVIDENDS OF REGU-**  
 4 **LATED INVESTMENT COMPANIES.**

5 (a) TREATMENT OF CERTAIN DIVIDENDS.—

6 (1) NONRESIDENT ALIEN INDIVIDUALS.—Sec-  
 7 tion 871 (relating to tax on nonresident alien indi-  
 8 viduals) is amended by redesignating subsection (k)  
 9 as subsection (l) and by inserting after subsection (j)  
 10 the following new subsection:

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

13 “(1) INTEREST-RELATED DIVIDENDS.—

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

19 “(B) EXCEPTIONS.—Subparagraph (A)  
 20 shall not apply—

21 “(i) to any interest-related dividend  
 22 received from a regulated investment com-  
 23 pany by a person to the extent such divi-  
 24 dend is attributable to interest (other than  
 25 interest described in subparagraph (E) (i)

1 or (iii)) received by such company on in-  
2 debtedness issued by such person or by any  
3 corporation or partnership with respect to  
4 which such person is a 10-percent share-  
5 holder,

6 “(ii) to any interest-related dividend  
7 with respect to stock of a regulated invest-  
8 ment company unless the person who  
9 would otherwise be required to deduct and  
10 withhold tax from such dividend under  
11 chapter 3 receives a statement (which  
12 meets requirements similar to the require-  
13 ments of subsection (h)(5)) that the bene-  
14 ficial owner of such stock is not a United  
15 States person, and

16 “(iii) to any interest-related dividend  
17 paid to any person within a foreign coun-  
18 try (or any interest-related dividend pay-  
19 ment addressed to, or for the account of,  
20 persons within such foreign country) dur-  
21 ing any period described in subsection  
22 (h)(6) with respect to such country.

23 Clause (iii) shall not apply to any dividend with  
24 respect to any stock which was acquired on or

1 before the date of the publication of the Sec-  
2 retary's determination under subsection (h)(6).

3 “(C) INTEREST-RELATED DIVIDEND.—For  
4 purposes of this paragraph, an interest-related  
5 dividend is any dividend (or part thereof) which  
6 is designated by the regulated investment com-  
7 pany as an interest-related dividend in a writ-  
8 ten notice mailed to its shareholders not later  
9 than 60 days after the close of its taxable year.  
10 If the aggregate amount so designated with re-  
11 spect to a taxable year of the company (includ-  
12 ing amounts so designated with respect to divi-  
13 dends paid after the close of the taxable year  
14 described in section 855) is greater than the  
15 qualified net interest income of the company for  
16 such taxable year, the portion of each distribu-  
17 tion which shall be an interest-related dividend  
18 shall be only that portion of the amounts so  
19 designated which such qualified net interest in-  
20 come bears to the aggregate amount so des-  
21 ignated.

22 “(D) QUALIFIED NET INTEREST IN-  
23 COME.—For purposes of subparagraph (C), the  
24 term ‘qualified net interest income’ means the  
25 qualified interest income of the regulated in-

1 vestment company reduced by the deductions  
2 properly allocable to such income.

3 “(E) QUALIFIED INTEREST INCOME.—For  
4 purposes of subparagraph (D), the term ‘quali-  
5 fied interest income’ means the sum of the fol-  
6 lowing amounts derived by the regulated invest-  
7 ment company from sources within the United  
8 States:

9 “(i) Any amount includible in gross  
10 income as original issue discount (within  
11 the meaning of section 1273) on an obliga-  
12 tion payable 183 days or less from the date  
13 of original issue (without regard to the pe-  
14 riod held by the company).

15 “(ii) Any interest includible in gross  
16 income (including amounts recognized as  
17 ordinary income in respect of original issue  
18 discount or market discount or acquisition  
19 discount under part V of subchapter P and  
20 such other amounts as regulations may  
21 provide) on an obligation which is in reg-  
22 istered form; except that this clause shall  
23 not apply to—

24 “(I) any interest on an obligation  
25 issued by a corporation or partnership



1 if the regulated investment company  
2 is a 10-percent shareholder in such  
3 corporation or partnership, and

4 “(II) any interest which is treat-  
5 ed as not being portfolio interest  
6 under the rules of subsection (h)(4).

7 “(iii) Any interest referred to in sub-  
8 section (i)(2)(A) (without regard to the  
9 trade or business of the regulated invest-  
10 ment company).

11 “(iv) Any interest-related dividend in-  
12 cludable in gross income with respect to  
13 stock of another regulated investment com-  
14 pany.

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

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

20 “(A) IN GENERAL.—Except as provided in  
21 subparagraph (B), no tax shall be imposed  
22 under paragraph (1)(A) of subsection (a) on  
23 any short-term capital gain dividend received  
24 from a regulated investment company.

1           “(B) EXCEPTION FOR ALIENS TAXABLE  
2 UNDER SUBSECTION (a)(2).—In the case of divi-  
3 dends received from a regulated investment  
4 company before January 1, 2003, subparagraph  
5 (A) shall not apply in the case of any non-  
6 resident alien individual subject to tax under  
7 subsection (a)(2).

8           “(C) SHORT-TERM CAPITAL GAIN DIVI-  
9 DEND.—For purposes of this paragraph, a  
10 short-term capital gain dividend is any dividend  
11 (or part thereof) which is designated by the reg-  
12 ulated investment company as a short-term cap-  
13 ital gain dividend in a written notice mailed to  
14 its shareholders not later than 60 days after the  
15 close of its taxable year. If the aggregate  
16 amount so designated with respect to a taxable  
17 year of the company (including amounts so des-  
18 ignated with respect to dividends paid after the  
19 close of the taxable year described in section  
20 855) is greater than the qualified short-term  
21 gain of the company for such taxable year, the  
22 portion of each distribution which shall be a  
23 short-term capital gain dividend shall be only  
24 that portion of the amounts so designated

1           which such qualified short-term gain bears to  
2           the aggregate amount so designated.

3           “(D) QUALIFIED SHORT-TERM GAIN.—For  
4           purposes of subparagraph (C), the term ‘quali-  
5           fied short-term gain’ means the excess of the  
6           net short-term capital gain of the regulated in-  
7           vestment company for the taxable year over the  
8           net long-term capital loss (if any) of such com-  
9           pany for such taxable year. For purposes of this  
10          subparagraph—

11               “(i) the net short-term capital gain of  
12               the regulated investment company shall be  
13               computed by treating any short-term cap-  
14               ital gain dividend includible in gross in-  
15               come with respect to stock of another regu-  
16               lated investment company as a short-term  
17               capital gain, and

18               “(ii) the excess of the net short-term  
19               capital gain for a taxable year over the net  
20               long-term capital loss for a taxable year (to  
21               which an election under section 4982(e)(4)  
22               does not apply) shall be determined with-  
23               out regard to any net capital loss or net  
24               short-term capital loss attributable to  
25               transactions after October 31 of such year,

1                   and any such net capital loss or net short-  
 2                   term capital loss shall be treated as arising  
 3                   on the 1st day of the next taxable year.

4                   To the extent provided in regulations, clause  
 5                   (ii) shall apply also for purposes of computing  
 6                   the taxable income of the regulated investment  
 7                   company.”

8                   (2) FOREIGN CORPORATIONS.—Section 881 (re-  
 9                   lating to tax on income of foreign corporations not  
 10                  connected with United States business) is amended  
 11                  by redesignating subsection (e) as subsection (f) and  
 12                  by inserting after subsection (d) the following new  
 13                  subsection:

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

16                   “(1) INTEREST-RELATED DIVIDENDS.—

17                           “(A) IN GENERAL.—Except as provided in  
 18                           subparagraph (B), no tax shall be imposed  
 19                           under paragraph (1) of subsection (a) on any  
 20                           interest-related dividend (as defined in section  
 21                           871(k)(1)) received from a regulated investment  
 22                           company.

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

1 “(i) to any dividend referred to in sec-  
 2 tion 871(k)(1)(B), and

3 “(ii) to any interest-related dividend  
 4 received by a controlled foreign corporation  
 5 (within the meaning of section 957(a)) to  
 6 the extent such dividend is attributable to  
 7 interest received by the regulated invest-  
 8 ment company from a person who is a re-  
 9 lated person (within the meaning of section  
 10 864(d)(4)) with respect to such controlled  
 11 foreign corporation.

12 “(C) TREATMENT OF DIVIDENDS RE-  
 13 CEIVED BY CONTROLLED FOREIGN CORPORA-  
 14 TIONS.—The rules of subsection (c)(5)(A) shall  
 15 apply to any interest-related dividend received  
 16 by a controlled foreign corporation (within the  
 17 meaning of section 957(a)) to the extent such  
 18 dividend is attributable to interest received by  
 19 the regulated investment company which is de-  
 20 scribed in clause (ii) of section 871(k)(1)(E)  
 21 (and not described in clause (i) or (iii) of such  
 22 section).

23 “(2) SHORT-TERM CAPITAL GAIN DIVIDENDS.—  
 24 No tax shall be imposed under paragraph (1) of sub-  
 25 section (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) Section 1441(c) (relating to exceptions) 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 that such dividend is a dividend referred to in such clause. A similar rule shall apply with respect to the exception contained in section 871(k)(2)(B).”

(B) Section 1442(a) (relating to withholding of tax on foreign corporations) is amended—

1 (i) by striking “and the reference in  
 2 section 1441(c)(10)” and inserting “the  
 3 reference in section 1441(c)(10)”, and

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

15 (b) ESTATE TAX TREATMENT OF INTEREST IN CER-  
 16 TAIN REGULATED INVESTMENT COMPANIES.—Section  
 17 2105 (relating to property without the United States for  
 18 estate tax purposes) is amended by adding at the end the  
 19 following new subsection:

20 “(d) STOCK IN A RIC.—

21 “(1) IN GENERAL.—For purposes of this sub-  
 22 chapter, stock in a regulated investment company  
 23 (as defined in section 851) owned by a nonresident  
 24 not a citizen of the United States shall not be  
 25 deemed property within the United States in the

1 proportion that, at the end of the quarter of such in-  
 2 vestment company's taxable year immediately pre-  
 3 ceding a decedent's date of death (or at such other  
 4 time as the Secretary may designate in regulations),  
 5 the assets of the investment company that were  
 6 qualifying assets with respect to the decedent bore  
 7 to the total assets of the investment company.

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

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

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

16 “(C) other property not within the United  
 17 States.”

18 (c) TREATMENT OF REGULATED INVESTMENT COM-  
 19 PANIES UNDER SECTION 897.—

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

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



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

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

12          (3) Subparagraphs (A) and (B) of section  
13          897(h)(4) are amended to read as follows:

14               “(A) QUALIFIED INVESTMENT ENTITY.—  
15               The term ‘qualified investment entity’ means  
16               any real estate investment trust and any regu-  
17               lated investment company.

18               “(B) DOMESTICALLY CONTROLLED.—The  
19               term ‘domestically controlled qualified invest-  
20               ment entity’ means any qualified investment en-  
21               tity in which at all times during the testing pe-  
22               riod less than 50 percent in value of the stock  
23               was held directly or indirectly by foreign per-  
24               sons.”

1           (4) Subparagraphs (C) and (D) of section  
 2           897(h)(4) are each amended by striking “REIT”  
 3           and inserting “qualified investment entity”.

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

7           (d) EFFECTIVE DATE.—

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

13          (2) ESTATE TAX TREATMENT.—The amend-  
 14          ment made by subsection (b) shall apply to estates  
 15          of decedents dying after the date of the enactment  
 16          of this Act.

17          (3) CERTAIN OTHER PROVISIONS.—The amend-  
 18          ments made by subsection (c) (other than paragraph  
 19          (1) thereof) shall take effect on the date of the en-  
 20          actment of this Act.

21   **SEC. 305. AIRLINE MILEAGE AWARDS TO CERTAIN FOREIGN**  
 22                   **PERSONS.**

23          (a) IN GENERAL.—The last sentence of section  
 24          4261(e)(3)(C) (relating to regulations) is amended by in-  
 25          serting “and mileage awards which are issued to individ-

1 uals whose mailing addresses on record with the person  
 2 providing the right to air transportation are outside the  
 3 United States” before the period at the end thereof.

4 (b) EFFECTIVE DATE.—The amendment made by  
 5 this section shall apply to amounts paid, and benefits pro-  
 6 vided, after December 31, 2002.

7 **SEC. 306. INTEREST PAYMENTS DEDUCTIBLE WHERE DIS-**  
 8 **QUALIFIED GUARANTEE HAS ECONOMIC EF-**  
 9 **FECT.**

10 (a) IN GENERAL.—Section 163(j)(6)(D)(ii) (relating  
 11 to exceptions to disqualified guarantee) is amended—

12 (1) by striking “or” at the end of subclause (I),

13 (2) by striking the period at the end of sub-  
 14 clause (II) and inserting “, or”,

15 (3) by inserting after subclause (II) the fol-  
 16 lowing new subclause:

17 “(III) if, in the case of a guar-  
 18 antee by a foreign person, the tax-  
 19 payer establishes to the satisfaction of  
 20 the Secretary that the taxpayer could  
 21 have borrowed substantially the same  
 22 principal amount from an unrelated  
 23 person without the guarantee.”, and

24 (4) by adding at the end the following new sen-  
 25 tence: “For purposes of subclause (III), to the ex-

1       tent provided in regulations, the Secretary may re-  
2       ject a showing that a taxpayer could have borrowed  
3       substantially the same principal amount if such bor-  
4       rowing is on terms substantially dissimilar to those  
5       of the actual loan.”

6       (b) EFFECTIVE DATE.—The amendments made by  
7       this section shall apply to guarantees issued on and after  
8       the date of the enactment of this Act.

9       **SEC. 307. MODIFICATIONS OF REPORTING REQUIREMENTS**  
10                   **FOR CERTAIN FOREIGN-OWNED CORPORA-**  
11                   **TIONS.**

12       (a) DE MINIMIS EXCEPTION.—Section 6038A(b) (re-  
13       lating to required information) is amended by adding at  
14       the end the following new flush sentence:

15       “The Secretary shall not require the reporting corporation  
16       to report any information with respect to any foreign per-  
17       son which is a related person if the aggregate value of  
18       the transactions between the corporation and the related  
19       person (and any person related to such person) during the  
20       taxable year does not exceed \$5,000,000.”

21       (b) TIME FOR PROVIDING TRANSLATIONS OF SPE-  
22       CIFIC DOCUMENTS.—Notwithstanding Internal Revenue  
23       Service Regulation § 1.6038A–3(f)(2), a taxpayer shall  
24       have at least 60 days to provide translations of specific  
25       documents it is requested to translate. Nothing in this

1 subsection shall limit the right of a taxpayer to file a writ-  
 2 ten request for an extension of time to comply with the  
 3 request.

4 (c) EFFECTIVE DATES.—

5 (1) EXCEPTION.—The amendment made by  
 6 subsection (a) shall apply to taxable years beginning  
 7 after December 31, 2002.

8 (2) TRANSLATIONS.—Subsection (b) shall apply  
 9 to requests made by the Internal Revenue Service  
 10 after December 31, 2002.

11 **SEC. 308. ELECTION NOT TO USE AVERAGE EXCHANGE**  
 12 **RATE FOR FOREIGN TAX PAID OTHER THAN**  
 13 **IN FUNCTIONAL CURRENCY.**

14 (a) IN GENERAL.—Paragraph (1) of section 986(a)  
 15 (relating to determination of foreign taxes and foreign cor-  
 16 poration's earnings and profits) is amended by redesign-  
 17 ating subparagraph (D) as subparagraph (E) and by in-  
 18 serting after subparagraph (C) the following new subpara-  
 19 graph:

20 “(D) ELECTIVE EXCEPTION FOR TAXES  
 21 PAID OTHER THAN IN FUNCTIONAL CUR-  
 22 RENCY.—

23 “(i) IN GENERAL.—At the election of  
 24 the taxpayer, subparagraph (A) shall not  
 25 apply to any foreign income taxes the li-

1 ability for which is denominated in any  
 2 currency other than in the taxpayer's func-  
 3 tional currency.

4 “(ii) APPLICATION TO QUALIFIED  
 5 BUSINESS UNITS.—An election under this  
 6 subparagraph may apply to foreign income  
 7 taxes attributable to a qualified business  
 8 unit in accordance with regulations pre-  
 9 scribed by the Secretary.

10 “(iii) ELECTION.—Any such election  
 11 shall apply to the taxable year for which  
 12 made and all subsequent taxable years un-  
 13 less revoked with the consent of the Sec-  
 14 retary.”

15 (b) EFFECTIVE DATE.—The amendment made by  
 16 this section shall apply to taxable years beginning after  
 17 December 31, 2002.

18 **SEC. 309. REPEAL OF SPECIAL CAPITAL GAINS TAX ON**  
 19 **ALIENS PRESENT IN THE UNITED STATES**  
 20 **FOR 183 DAYS OR MORE.**

21 (a) IN GENERAL.—Subsection (a) of section 871 is  
 22 amended by striking paragraph (2) and by redesignating  
 23 paragraph (3) as paragraph (2).

1 (b) EFFECTIVE DATE.—The amendment made by  
 2 this section shall apply to taxable years beginning after  
 3 December 31, 2002.

4 **SEC. 310. REPEAL OF WITHHOLDING TAX ON DIVIDENDS**  
 5 **FROM CERTAIN FOREIGN CORPORATIONS.**

6 (a) IN GENERAL.—Paragraph (2) of section 871(i)  
 7 (relating to tax not to apply to certain interest and divi-  
 8 dends) is amended by adding at the end the following new  
 9 subparagraph:

10 “(D) Dividends paid by a foreign corpora-  
 11 tion.”.

12 (b) EFFECTIVE DATE.—The amendment made by  
 13 this section shall apply to payments made after December  
 14 31, 2002.

15 **SEC. 311. INTEREST ALLOCATION RULES.**

16 (a) ELECTION TO ALLOCATE INTEREST ON A  
 17 WORLDWIDE BASIS.—Subsection (e) of section 864 (relat-  
 18 ing to rules for allocating interest, etc.) is amended by  
 19 redesignating paragraphs (6) and (7) as paragraphs (7)  
 20 and (8), respectively, and by inserting after paragraph (5)  
 21 the following new paragraph:

22 “(6) ELECTION TO ALLOCATE INTEREST ON A  
 23 WORLDWIDE BASIS.—

24 “(A) IN GENERAL.—Except as provided in  
 25 this paragraph, this subsection shall be applied

1 by treating a worldwide affiliated group for  
2 which an election under this paragraph is in ef-  
3 fect as an affiliated group solely for purposes of  
4 allocating and apportioning interest expense of  
5 each domestic corporation which is a member of  
6 such group.

7 “(B) WORLDWIDE AFFILIATED GROUP.—  
8 For purposes of this paragraph, the term  
9 ‘worldwide affiliated group’ means the group of  
10 corporations which consists of—

11 “(i) all corporations in an affiliated  
12 group (as defined in section 1504 without  
13 regard to paragraphs (2) and (4) of section  
14 1504(b)), and

15 “(ii) all foreign corporations (other  
16 than a FSC, as defined in section 922(a)  
17 as in effect on the day before the date of  
18 the enactment of the FSC Repeal and  
19 Extraterritorial Income Exclusion Act of  
20 2000) with respect to which corporations  
21 described in clause (i) own stock meeting  
22 the ownership requirements of section  
23 957(a).

24 For purposes of clause (ii), ownership shall be  
25 determined under section 958; except that para-



1           graphs (3) and (4) of section 318(a) shall not  
2           apply for purposes of section 958(b).

3           “(C) TREATMENT OF WORLDWIDE AFFILI-  
4           ATED GROUP.—For purposes of applying para-  
5           graph (1), the taxable income of the domestic  
6           members of a worldwide affiliated group from  
7           sources outside the United States shall be de-  
8           termined by allocating and apportioning the in-  
9           terest expense of such domestic members to  
10          such income in an amount equal to the excess  
11          (if any) of—

12                 “(i) the total interest expense of the  
13                 worldwide affiliated group multiplied by  
14                 the ratio which the foreign assets of the  
15                 worldwide affiliated group bears to all the  
16                 assets of the worldwide affiliated group,  
17                 over

18                 “(ii) the interest expense of all foreign  
19                 corporations which are members of the  
20                 worldwide affiliated group to the extent  
21                 such interest expense of such foreign cor-  
22                 porations would have been allocated and  
23                 apportioned to foreign source income if  
24                 this subsection were applied to a group

1 consisting of all the foreign corporations in  
2 such worldwide affiliated group.

3 “(D) ASSETS AND INTEREST EXPENSE OF  
4 FOREIGN CORPORATIONS.—

5 “(i) IN GENERAL.—For purposes of  
6 subparagraph (C), only the applicable per-  
7 centage of the interest expense and assets  
8 of a foreign corporation described in sub-  
9 paragraph (B)(ii) shall be taken into ac-  
10 count.

11 “(ii) APPLICABLE PERCENTAGE.—For  
12 purposes of this paragraph, the term ‘ap-  
13 plicable percentage’ means, with respect to  
14 any foreign corporation, the percentage  
15 equal to the ratio which the value of the  
16 stock in such corporation taken into ac-  
17 count under subparagraph (B)(ii) (without  
18 regard to stock considered as owned under  
19 section 958(b)) bears to the aggregate  
20 value of all stock in such corporation.

21 “(E) ELECTION.—An election under this  
22 paragraph with respect to any worldwide affili-  
23 ated group may be made only by the common  
24 parent of the affiliated group referred to in sub-  
25 paragraph (B)(i) and may be made only for the

1 first taxable year beginning after December 31,  
 2 2001, in which a worldwide affiliated group ex-  
 3 ists which includes such affiliated group and at  
 4 least one corporation described in subparagraph  
 5 (B)(ii). Such an election, once made, shall apply  
 6 to such common parent and all other corpora-  
 7 tions which are members of such worldwide af-  
 8 filiated group for such taxable year and all sub-  
 9 sequent years unless revoked with the consent  
 10 of the Secretary.”.

11 (b) ELECTION TO ALLOCATE INTEREST WITHIN FI-  
 12 NANCIAL INSTITUTION GROUPS AND SUBSIDIARY  
 13 GROUPS.—Section 864 is amended by redesignating sub-  
 14 section (f) as subsection (g) and by inserting after sub-  
 15 section (e) the following new subsection:

16 “(f) ELECTION TO APPLY SUBSECTION (e) ON BASIS  
 17 OF FINANCIAL INSTITUTION GROUP AND SUBSIDIARY  
 18 GROUPS.—

19 “(1) IN GENERAL.—In the case of a worldwide  
 20 affiliated group for which an election under sub-  
 21 section (e)(6) is in effect, subsection (e) shall be  
 22 applied—

23 “(A) by treating an electing financial insti-  
 24 tution group as if it were a separate worldwide  
 25 affiliated group, and

1           “(B) by treating each electing subsidiary  
 2           group as if it were a separate worldwide affili-  
 3           ated group for purposes of allocating interest  
 4           expense with respect to qualified indebtedness  
 5           of members of an electing subsidiary group.

6           Subsection (e) shall apply to any such electing group  
 7           in the same manner as subsection (e) applies to the  
 8           pre-election worldwide affiliated group of which such  
 9           electing group is a part.

10           “(2) ELECTING FINANCIAL INSTITUTION  
 11           GROUP.—For purposes of this subsection—

12           “(A) IN GENERAL.—The term ‘electing fi-  
 13           nancial institution group’ means any group of  
 14           corporations if—

15           “(i) such group consists only of all of  
 16           the financial corporations in the pre-elec-  
 17           tion worldwide affiliated group, and

18           “(ii) an election under this paragraph  
 19           is in effect for such group of corporations.

20           “(B) FINANCIAL CORPORATION.—

21           “(i) IN GENERAL.—The term ‘finan-  
 22           cial corporation’ means any corporation if  
 23           at least 80 percent of its gross income is  
 24           income described in section  
 25           904(d)(2)(C)(ii) and the regulations there-

1 under which is derived from transactions  
2 with unrelated persons.

3 “(ii) INCOME FROM RELATED FINAN-  
4 CIAL CORPORATIONS.—Dividend income,  
5 and income described in section  
6 904(d)(2)(C)(ii) and the regulations there-  
7 under, which is derived directly or indi-  
8 rectly from a financial corporation (as de-  
9 fined in clause (i) without regard to this  
10 clause) which is not an unrelated person  
11 shall be treated as income described in  
12 clause (i).

13 “(iii) BANK HOLDING COMPANIES.—  
14 To the extent provided in regulations pre-  
15 scribed by the Secretary, a bank holding  
16 company (within the meaning of section  
17 2(a) of the Bank Holding Company Act of  
18 1956) shall be treated as a corporation  
19 meeting the requirements of clause (i).

20 “(iv) ANTIABUSE RULE.—For pur-  
21 poses of this subparagraph, there shall be  
22 disregarded any item of income or gain  
23 from a transaction or series of transactions  
24 a principal purpose of which is the quali-

1           fication of any corporation as a financial  
2           corporation.

3           “(C) EFFECT OF CERTAIN TRANS-  
4           ACTIONS.—Rules similar to the rules of para-  
5           graph (3)(D) shall apply to transactions be-  
6           tween any member of the electing financial in-  
7           stitution group and any member of the pre-elec-  
8           tion worldwide affiliated group (other than a  
9           member of the electing financial institution  
10          group).

11          “(D) ELECTION.—An election under this  
12          paragraph with respect to any financial institu-  
13          tion group may be made only by the common  
14          parent of the pre-election worldwide affiliated  
15          group and may be made only for the first tax-  
16          able year beginning after December 31, 2001,  
17          in which such affiliated group includes one or  
18          more financial corporations described in sub-  
19          paragraph (B). Such an election, once made,  
20          shall apply to such taxable year and all subse-  
21          quent years unless revoked with the consent of  
22          the Secretary.

23          “(3) ELECTING SUBSIDIARY GROUPS.—

1           “(A) IN GENERAL.—The term ‘electing  
2 subsidiary group’ means any group of corpora-  
3 tions if—

4           “(i) such group consists only of cor-  
5 porations in the pre-election worldwide af-  
6 filiated group,

7           “(ii) such group includes—

8           “(I) a domestic corporation  
9 (which is not the common parent of  
10 the pre-election worldwide affiliated  
11 group or a member of an electing fi-  
12 nancial institution group) which in-  
13 curs interest expense with respect to  
14 qualified indebtedness, and

15           “(II) every other corporation  
16 (other than a member of an electing  
17 financial institution group) which is in  
18 the pre-election worldwide affiliated  
19 group and which would be a member  
20 of an affiliated group having such do-  
21 mestic corporation as the common  
22 parent, and

23           “(iii) an election under this paragraph  
24 is in effect for such group.

1           “(B) EQUALIZATION RULE.—All interest  
2           expense of a domestic corporation which is a  
3           member of a pre-election worldwide affiliated  
4           group (other than subsidiary group interest ex-  
5           pense) shall be treated as allocated to foreign  
6           source income to the extent such expense does  
7           not exceed the excess (if any) of—

8                   “(i) the interest expense of the pre-  
9                   election worldwide affiliated group (includ-  
10                  ing subsidiary group interest expense)  
11                  which would (but for any election under  
12                  this paragraph) be allocated to foreign  
13                  source income, over

14                  “(ii) the subsidiary group interest ex-  
15                  pense allocated to foreign source income.

16           For purposes of the preceding sentence, the  
17           subsidiary group interest expense is the interest  
18           expense to which subsection (e) applies sepa-  
19           rately by reason of paragraph (1)(B).

20           “(C) QUALIFIED INDEBTEDNESS.—For  
21           purposes of this subsection, the term ‘qualified  
22           indebtedness’ means any indebtedness of a do-  
23           mestic corporation—

24                   “(i) which is held by an unrelated per-  
25                   son, and



1 “(ii) which is not guaranteed (or oth-  
2 erwise supported) by any corporation  
3 which is a member of the pre-election  
4 worldwide affiliated group other than a  
5 corporation which is a member of the elect-  
6 ing subsidiary group.

7 “(D) EFFECT OF CERTAIN TRANSACTIONS  
8 ON QUALIFIED INDEBTEDNESS.—In the case of  
9 a corporation which is a member of an electing  
10 subsidiary group, to the extent that such  
11 corporation—

12 “(i) distributes dividends or makes  
13 other distributions with respect to its stock  
14 after the date of the enactment of this  
15 paragraph to any member of the pre-elec-  
16 tion worldwide affiliated group (other than  
17 to a member of the electing subsidiary  
18 group) in excess of the greater of—

19 “(I) its average annual dividend  
20 (expressed as a percentage of current  
21 earnings and profits) during the 5-  
22 taxable-year period ending with the  
23 taxable year preceding the taxable  
24 year, or

1 “(II) 25 percent of its average  
2 annual earnings and profits for such 5  
3 taxable year period, or

4 “(ii) deals with any person in any  
5 manner not clearly reflecting the income of  
6 the corporation (as determined under prin-  
7 ciples similar to the principles of section  
8 482),

9 except as provided by the Secretary, an amount  
10 of qualified indebtedness equal to the excess  
11 distribution or the understatement or overstate-  
12 ment of income, as the case may be, shall be re-  
13 characterized (for the taxable year and subse-  
14 quent taxable years) for purposes of this sub-  
15 section as indebtedness which is not qualified  
16 indebtedness. If a corporation has not been in  
17 existence for 5 taxable years, this subparagraph  
18 shall be applied with respect to the period it  
19 was in existence.

20 “(E) ELECTION.—An election under this  
21 paragraph with respect to any electing sub-  
22 sidiary group may be made only by the common  
23 parent of the pre-election worldwide affiliated  
24 group. Such an election, once made, shall apply  
25 to the taxable year for which made and the 4

1           succeeding taxable years unless revoked with  
2           the consent of the Secretary. No election may  
3           be made under this paragraph if the effect of  
4           the election would be to have the same member  
5           of the pre-election worldwide affiliated group in-  
6           cluded in more than one electing subsidiary  
7           group.

8           “(4) PRE-ELECTION WORLDWIDE AFFILIATED  
9           GROUP.—For purposes of this subsection, the term  
10          ‘pre-election worldwide affiliated group’ means, with  
11          respect to a corporation, the worldwide affiliated  
12          group of which such corporation would (but for an  
13          election under this subsection) be a member for pur-  
14          poses of applying subsection (e).

15          “(5) UNRELATED PERSON.—For purposes of  
16          this subsection, the term ‘unrelated person’ means  
17          any person not bearing a relationship specified in  
18          section 267(b) or 707(b)(1) to the corporation.

19          “(6) REGULATIONS.—The Secretary shall pre-  
20          scribe such regulations as may be appropriate to  
21          carry out this subsection and subsection (e), includ-  
22          ing regulations—

23                 “(A) providing for the direct allocation of  
24                 interest expense in other circumstances where

1           such allocation would be appropriate to carry  
2           out the purposes of this subsection,

3           “(B) preventing assets or interest expense  
4           from being taken into account more than once,  
5           and

6           “(C) dealing with changes in members of  
7           any group (through acquisitions or otherwise)  
8           treated under this subsection as an affiliated  
9           group for purposes of subsection (e).”.

10       (c) EFFECTIVE DATE.—The amendments made by  
11 this section shall apply to taxable years beginning after  
12 December 31, 2002.

13 **SEC. 312. PERMANENT EXTENSION OF SUBPART F EXEMP-**  
14 **TION FOR ACTIVE FINANCING.**

15       (a) IN GENERAL.—

16           (1) Section 953(e)(10) is amended—

17               (A) by striking “, and before January 1,  
18               2007,”, and

19               (B) by striking the second sentence.

20           (2) Section 954(h)(9) is amended by striking “,  
21           and before January 1, 2007,”.

22       (b) EFFECTIVE DATE.—The amendments made by  
23 subsection (a) shall apply to taxable years beginning after  
24 December 31, 2002.

1 **SEC. 313. REPEAL OF TREATMENT OF EXTRATERRITORIAL**  
2 **INCOME.**

3 (a) IN GENERAL.—Part III of subchapter B of chap-  
4 ter 1 (relating to items specifically excluded from gross  
5 income) is amended by striking section 114 (relating to  
6 treatment of extraterritorial income).

7 (b) TECHNICAL AMENDMENTS.—

8 (1) Part III of subchapter N of chapter 1 is  
9 amended by striking subpart E.

10 (2) The second sentence of section  
11 56(g)(4)(B)(i) is amended by striking “or under sec-  
12 tion 114”.

13 (3) Section 275(a) is amended by adding “or”  
14 at the end of paragraph (4)(A), by striking “, or”  
15 at the end of paragraph (4)(B) and inserting a pe-  
16 riod, by striking subparagraph (4)(C), and by strik-  
17 ing the last sentence.

18 (4) Paragraph (3) of section 864(e) is amended  
19 by striking “(A) IN GENERAL.—For purposes of”  
20 and inserting “For purposes of” and by striking  
21 subparagraph (B).

22 (5) Section 903 is amended by striking “114,”.

23 (6) Section 999(c)(1) is amended by striking  
24 “941(a)(5),”.

1           (7) The table of sections for part III of sub-  
2       chapter B of chapter 1 is amended by striking the  
3       item relating to section 114.

4           (8) The table of subparts for part III of sub-  
5       chapter N of chapter 1 is amended by striking the  
6       item relating to subpart E.

7       (c) EFFECTIVE DATE.—The amendments made by  
8       this Act shall apply to transactions after December 31,  
9       2002.

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