

108TH CONGRESS
1ST SESSION

H. R. 3655

To amend the Internal Revenue Code of 1986 to replace the earned income credit, the child tax credit, and the deduction for dependents with a simplified family tax credit.

IN THE HOUSE OF REPRESENTATIVES

DECEMBER 8, 2003

Mr. KUCINICH (for himself, Ms. LEE, and Mr. SANDERS) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to replace the earned income credit, the child tax credit, and the deduction for dependents with a simplified family tax credit.

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, ETC.**

4 (a) SHORT TITLE.—This Act may be cited as the
5 “Progressive Tax Act of 2003”.

6 (b) AMENDMENT OF 1986 CODE.—Except as other-
7 wise expressly provided, whenever in this Act an amend-
8 ment or repeal is expressed in terms of an amendment

1 to, or repeal of, a section or other provision, the reference
 2 shall be considered to be made to a section or other provi-
 3 sion of the Internal Revenue Code of 1986.

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1 **TITLE I—TAX RELIEF**

2 **SEC. 101. SIMPLIFIED FAMILY CREDIT.**

3 (a) IN GENERAL.—Section 32 of the Internal Rev-
 4 enue Code of 1986 (relating to earned income credit) is
 5 amended to read as follows:

6 **“SEC. 32. SIMPLIFIED FAMILY CREDIT.**

7 “(a) ALLOWANCE OF CREDIT.—In the case of an eli-
 8 gible individual, there shall be allowed as a credit against
 9 the tax imposed by this subtitle for the taxable year an
 10 amount equal to 50 percent of the taxpayer’s modified ad-
 11 justed gross income for the taxable year.

12 “(b) LIMITATIONS.—For purposes of subsection
 13 (a)—

14 “(1) LIMITATION BASED ON QUALIFYING CHIL-
 15 DREN.—The amount of the credit allowable to a tax-
 16 payer under paragraph (1) for any taxable year shall
 17 not exceed the lesser of—

1 “(A) \$2,000 multiplied by the number of
2 qualifying children of the taxpayer, and

3 “(B) 50 percent of earned income.

4 “(2) LIMITATION BASED ON ADJUSTED GROSS
5 INCOME.—

6 “(A) IN GENERAL.—The amount of the
7 credit allowable under subsection (a) shall be
8 reduced (but not below zero) by \$50 for each
9 \$1,000 (or fraction thereof) by which the tax-
10 payer’s modified adjusted gross income exceeds
11 the threshold amount.

12 “(B) THRESHOLD AMOUNT.—For purposes
13 of subparagraph (A), the term ‘threshold
14 amount’ means—

15 “(i) \$150,000 in the case of a joint
16 return,

17 “(ii) \$100,000 in the case of an indi-
18 vidual who is not married, and

19 “(iii) \$75,000 in the case of a married
20 individual filing a separate return.

21 For purposes of this paragraph, marital status
22 shall be determined under section 7703.

23 “(3) LIMITATION ON AMOUNT OF REFUNDABLE
24 CREDIT.—

1 “(A) IN GENERAL.—The amount of the
 2 credit allowed under subsection (a) for a tax-
 3 able year which is allowed under this subpart
 4 shall not exceed the earned income of the tax-
 5 payer for such year.

6 “(B) ALLOWANCE OF REMAINING AMOUNT
 7 OF CREDIT.—The excess of—

8 “(i) the amount of the credit allowed
 9 under subsection (a), over

10 “(ii) the amount of the credit allowed
 11 under this subpart by reason of subpara-
 12 graph (A),

13 shall be treated as a credit allowed under sub-
 14 part B for such taxable year and not under this
 15 subpart.

16 “(c) DEFINITIONS AND SPECIAL RULES.—For pur-
 17 poses of this section—

18 “(1) ELIGIBLE INDIVIDUAL.—

19 “(A) IN GENERAL.—The term ‘eligible in-
 20 dividual’ means any individual who has a quali-
 21 fying child for the taxable year.

22 “(B) INDIVIDUAL WHO IS QUALIFYING
 23 CHILD INELIGIBLE.—If an individual is the
 24 qualifying child of a taxpayer for any taxable
 25 year of such taxpayer beginning in a calendar

1 year, such individual shall not be treated as an
2 eligible individual for any taxable year of such
3 individual beginning in such calendar year.

4 “(C) EXCEPTION FOR INDIVIDUAL CLAIM-
5 ING BENEFITS UNDER SECTION 911.—The term
6 ‘eligible individual’ does not include any indi-
7 vidual who claims the benefits of section 911
8 (relating to citizens or residents living abroad)
9 for the taxable year.

10 “(D) LIMITATION ON ELIGIBILITY OF NON-
11 RESIDENT ALIENS.—The term ‘eligible indi-
12 vidual’ shall not include any individual who is
13 a nonresident alien individual for any portion of
14 the taxable year unless such individual is treat-
15 ed for such taxable year as a resident of the
16 United States for purposes of this chapter by
17 reason of an election under subsection (g) or
18 (h) of section 6013.

19 “(E) IDENTIFICATION NUMBER REQUIRE-
20 MENT.—No credit shall be allowed under this
21 section to an eligible individual who does not in-
22 clude on the return of tax for the taxable
23 year—

24 “(i) such individual’s taxpayer identi-
25 fication number, and

1 “(ii) if the individual is married (with-
2 in the meaning of section 7703), the tax-
3 payer identification number of such indi-
4 vidual’s spouse.

5 “(F) INDIVIDUALS WHO DO NOT INCLUDE
6 TIN, ETC., OF ANY QUALIFYING CHILD.—No
7 credit shall be allowed under this section to any
8 eligible individual who has one or more quali-
9 fying children if no qualifying child of such in-
10 dividual is taken into account under subsection
11 (b) by reason of paragraph (2)(F).

12 “(2) QUALIFYING CHILD.—

13 “(A) IN GENERAL.—The term ‘qualifying
14 child’ means, with respect to any taxpayer for
15 any taxable year, an individual—

16 “(i) who bears a relationship to the
17 taxpayer described in subparagraph (B),

18 “(ii) who has the same principal place
19 of abode as the taxpayer for more than
20 one-half of such taxable year (or, in the
21 case of a student, meets the requirements
22 of subparagraph (F)), and

23 “(iii) who meets the age requirements
24 of subparagraph (C).

25 “(B) RELATIONSHIP TEST.—

1 “(i) IN GENERAL.—An individual
2 bears a relationship to the taxpayer de-
3 scribed in this subparagraph if such indi-
4 vidual is—

5 “(I) a son, daughter, stepson, or
6 stepdaughter, or a descendant of any
7 such individual,

8 “(II) a brother, sister, step-
9 brother, or stepsister, or a descendant
10 of any such individual, who the tax-
11 payer cares for as the taxpayer’s own
12 child, or

13 “(III) an eligible foster child of
14 the taxpayer.

15 “(ii) MARRIED CHILDREN.—Clause (i)
16 shall not apply to any individual who has
17 made a joint return with his spouse under
18 section 6013 for the taxable year beginning
19 in the calendar year in which the taxable
20 year of the taxpayer begins.

21 “(iii) ELIGIBLE FOSTER CHILD.—For
22 purposes of clause (i), the term ‘eligible
23 foster child’ means an individual not de-
24 scribed in subclause (I) or (II) of clause (i)
25 who—

1 “(I) is placed with the taxpayer
2 by an authorized placement agency,
3 and

4 “(II) the taxpayer cares for as
5 the taxpayer’s own child.

6 “(iv) ADOPTION.—For purposes of
7 this subparagraph, a child who is legally
8 adopted, or who is placed with the tax-
9 payer by an authorized placement agency
10 for adoption by the taxpayer, shall be
11 treated as a child by blood.

12 “(C) AGE REQUIREMENTS.—An individual
13 meets the requirements of this subparagraph if
14 such individual—

15 “(i) has not attained the age of 19 as
16 of the close of the calendar year in which
17 the taxable year of the taxpayer begins,

18 “(ii) is a student who has not attained
19 the age of 24 as of the close of such cal-
20 endar year, or

21 “(iii) is permanently and totally dis-
22 abled (as defined in section 22(e)(3)) at
23 any time during the taxable year.

24 “(D) IDENTIFICATION REQUIREMENTS.—

1 “(i) IN GENERAL.—A qualifying child
 2 shall not be taken into account under sub-
 3 section (b) unless the taxpayer includes the
 4 name, age, and TIN of the qualifying child
 5 on the return of tax for the taxable year.

6 “(ii) OTHER METHODS.—The Sec-
 7 retary may prescribe other methods for
 8 providing the information described in
 9 clause (i).

10 “(E) ABODE MUST BE IN THE UNITED
 11 STATES.—The requirements of subparagraph
 12 (A)(ii) shall be met only if the principal place
 13 of abode is in the United States.

14 “(F) SPECIAL RULES RELATING TO STU-
 15 DENTS.—For purposes of this paragraph—

16 “(i) STUDENT DEFINED.—The term
 17 ‘student’ means an individual who during
 18 each of 5 calendar months during the cal-
 19 endar year in which the taxable year of the
 20 taxpayer begins—

21 “(I) is a full-time student at an
 22 educational organization described in
 23 section 170(b)(1)(A)(ii); or

24 “(II) is pursuing a full-time
 25 course of institutional on-farm train-

1 ing under the supervision of an ac-
2 credited agent of an educational orga-
3 nization described in section
4 170(b)(1)(A)(ii) or of a State or polit-
5 ical subdivision of a State.

6 “(ii) SUPPORT TEST.—In the case of
7 an individual who is a student, the indi-
8 vidual meets the requirements of this sub-
9 paragraph if such individual is a dependent
10 (within the meaning of section 152).

11 “(G) 2 OR MORE CLAIMING QUALIFYING
12 CHILD.—

13 “(i) IN GENERAL.—Except as pro-
14 vided in clause (ii), if (but for this sub-
15 paragraph) an individual may be claimed,
16 and is claimed, as a qualifying child by 2
17 or more taxpayers for a taxable year begin-
18 ning in the same calendar year, such indi-
19 vidual shall be treated as the qualifying
20 child of the taxpayer who is—

21 “(I) a parent of the individual, or

22 “(II) if subclause (I) does not
23 apply, the taxpayer with the highest
24 adjusted gross income for such tax-
25 able year.

1 “(ii) MORE THAN 1 CLAIMING CRED-
2 IT.—If the parents claiming the credit with
3 respect to any qualifying child do not file
4 a joint return together, such child shall be
5 treated as the qualifying child of—

6 “(I) the parent with whom the
7 child resided for the longest period of
8 time during the taxable year, or

9 “(II) if the child resides with
10 both parents for the same amount of
11 time during such taxable year, the
12 parent with the highest adjusted gross
13 income.

14 “(3) EARNED INCOME.—

15 “(A) IN GENERAL.—The term ‘earned in-
16 come’ means the sum of—

17 “(i) wages, salaries, tips, and other
18 employee compensation, but only if such
19 amounts are includible in gross income for
20 the taxable year,

21 “(ii) the amount of the taxpayer’s net
22 earnings from self-employment for the tax-
23 able year (within the meaning of section
24 1402(a)), but such net earnings shall be

1 determined with regard to the deduction
2 allowed to the taxpayer by section 164(f),

3 “(iii) alimony or separate maintenance
4 payments and child support received, plus

5 “(iv) amounts received under a Fed-
6 eral or State unemployment compensation
7 law which are in the nature of unemploy-
8 ment compensation.

9 “(B) MODIFICATIONS OF EARNED IN-
10 COME.—For purposes of subparagraph (A)—

11 “(i) the earned income of an indi-
12 vidual shall be computed without regard to
13 any community property laws,

14 “(ii) no amount received as a pension
15 or annuity shall be taken into account,

16 “(iii) no amount to which section
17 871(a) applies (relating to income of non-
18 resident alien individuals not connected
19 with United States business) shall be taken
20 into account, and

21 “(iv) no amount received for services
22 provided by an individual while the indi-
23 vidual is an inmate at a penal institution
24 shall be taken into account.

1 “(4) MODIFIED ADJUSTED GROSS INCOME.—

2 The term ‘modified adjusted gross income’ means
3 adjusted gross income increased by any amount ex-
4 cluded from gross income under section 911, 931, or
5 933.

6 “(5) TREATMENT OF MILITARY PERSONNEL

7 STATIONED OUTSIDE THE UNITED STATES.—For
8 purposes of subparagraphs (A)(ii) and (E) of para-
9 graph (3), the principal place of abode of a member
10 of the Armed Forces of the United States shall be
11 treated as in the United States during any period
12 during which such member is stationed outside the
13 United States while serving on extended active duty
14 with the Armed Forces of the United States. For
15 purposes of the preceding sentence, the term ‘ex-
16 tended active duty’ means any period of active duty
17 pursuant to a call or order to such duty for a period
18 in excess of 90 days or for an indefinite period.

19 “(d) MARRIED INDIVIDUALS.—In the case of an indi-
20 vidual who is married (within the meaning of section
21 7703), this section shall apply only if a joint return is filed
22 for the taxable year under section 6013.

23 “(e) TAXABLE YEAR MUST BE FULL TAXABLE
24 YEAR.—Except in the case of a taxable year closed by rea-
25 son of the death of the taxpayer, no credit shall be allow-

1 able under this section in the case of a taxable year cov-
 2 ering a period of less than 12 months.

3 “(f) INFLATION ADJUSTMENTS.—

4 “(1) IN GENERAL.—In the case of any taxable
 5 year beginning after 2004, each of the dollar
 6 amounts in subsections (b)(1)(A) and (b)(2)(B) shall
 7 be increased by an amount equal to—

8 “(A) such dollar amount, multiplied by

9 “(B) the cost-of-living adjustment deter-
 10 mined under section 1(f)(3) for the calendar
 11 year in which the taxable year begins, deter-
 12 mined by substituting ‘calendar year 2003’ for
 13 ‘calendar year 1992’ in subparagraph (B)
 14 thereof.

15 “(2) ROUNDING.—If any dollar amount in sub-
 16 section (b)(1)(A) after being increased under para-
 17 graph (1) is not a multiple of \$10, such dollar
 18 amount shall be rounded to the nearest multiple of
 19 \$10, and if any dollar amount in subsection
 20 (b)(2)(B) after being increased under paragraph (1)
 21 is not a multiple of \$1,000, such dollar amount shall
 22 be rounded to the nearest multiple of \$1,000.

23 “(i) COORDINATION WITH CERTAIN MEANS-TESTED
 24 PROGRAMS.—For purposes of—

25 “(1) the United States Housing Act of 1937,

1 “(2) title V of the Housing Act of 1949,

2 “(3) section 101 of the Housing and Urban De-
3 velopment Act of 1965,

4 “(4) sections 221(d)(3), 235, and 236 of the
5 National Housing Act, and

6 “(5) the Food Stamp Act of 1977—

7 any refund made to an individual (or the spouse of an
8 individual) by reason of this section, and any payment
9 made to such individual (or such spouse) by an employer
10 under section 3507, shall not be treated as income (and
11 shall not be taken into account in determining resources
12 for the month of its receipt and the following month).

13 “(j) IDENTIFICATION NUMBERS.—Solely for pur-
14 poses of subsections (c)(1)(F) and (c)(3)(D), a taxpayer
15 identification number means a social security number
16 issued to an individual by the Social Security Administra-
17 tion (other than a social security number issued pursuant
18 to clause (II) (or that portion of clause (III) that relates
19 to clause (II)) of section 205(c)(2)(B)(i) of the Social Se-
20 curity Act).”.

21 (b) REPEALS OF OTHER PROVISIONS.—

22 (1) CHILD CREDIT.—Section 24 is hereby re-
23 pealed.

24 (2) DEDUCTION FOR EXEMPTION FOR DEPEND-
25 ENTS DISALLOWED TO CREDIT RECIPIENTS.—Sub-

1 section (c) of section 151 is amended by adding at
2 the end the following new paragraph:

3 “(7) DEDUCTION FOR EXEMPTION FOR DE-
4 PENDENTS DISALLOWED TO CREDIT RECIPIENTS.—
5 No exemption shall be allowed under this section for
6 a dependent for a taxable year if a credit is allowed
7 under section 32 with respect to such dependent for
8 such taxable year.”.

9 (c) CONFORMING AMENDMENTS.—

10 (1) AMENDMENTS RELATING TO REPEAL OF
11 CHILD CREDIT.—

12 (A) Sections 25(e)(1)(C) and 1400C(d) (as
13 in effect for taxable years after December 31,
14 2003) are both amended by striking “24,”.

15 (B) Section 501(c)(26) is amended by in-
16 serting “(as in effect before the enactment of
17 the Progressive Tax Act of 2003)” after “sec-
18 tion 24(c)”.

19 (C) Section 6213(g)(2) is amended—

20 (i) by striking subparagraph (I), and

21 (ii) in subparagraph (L), by striking
22 “21, 24, or 32” and inserting “21 or 32”.

23 (2) AMENDMENTS RELATING TO REPEAL OF
24 DEDUCTION FOR EXEMPTION FOR DEPENDENTS.—

1 (A) Section 2(a) is amended by striking “a
2 deduction for the taxable year under section
3 151” and inserting “a credit for the taxable
4 year under section 32”.

5 (B) Section 2(b) is amended by striking “a
6 deduction for the taxable year for such person
7 under section 151” and inserting “a credit for
8 the taxable year for such person under section
9 32”.

10 (C) Section 21(b)(1)(A) is amended by
11 striking “a deduction under section 151(c)”
12 and inserting “a credit under section 32”.

13 (D) Section 21(e)(6)(A) is amended by
14 striking “deduction under section 151(c)” and
15 inserting “credit under section 32”.

16 (E) Sections 25A(f)(1)(A)(iii) and
17 25A(g)(3) are amended by striking “deduction
18 under section 151” both places it appears and
19 inserting “credit under section 32”.

20 (F) Section 25B(c)(2)(A) is amended by
21 striking “deduction under section 151” and in-
22 serting “credit under section 32”.

23 (G) Section 35(d)(1)(B) is amended by
24 striking “deduction under section 151(c)” and
25 inserting “credit under section 32”.

1 (H) Section 35(g)(4) is amended by strik-
2 ing “deduction under section 151” and insert-
3 ing “credit under section 32”.

4 (I) Section 63(c)(5) is amended by striking
5 “deduction under section 151” and inserting
6 “credit under section 32”.

7 (J) Section 129(c)(1) is amended by strik-
8 ing “deduction is allowable under section 151(c)
9 (relating to personal exemptions for depend-
10 ents) ” and inserting “credit is allowable under
11 section 32 (relating to simplified family cred-
12 it)”.

13 (K) Section 135(c)(2)(A)(iii) is amended
14 by striking “deduction under section 151” and
15 inserting “credit under section 32”.

16 (L) Section 220(b)(6) is amended by strik-
17 ing “deduction under section 151” and insert-
18 ing “credit under section 32”.

19 (M) Section 221(c) is amended by striking
20 “deduction under section 151” and inserting
21 “credit under section 32”.

22 (N) Section 222(c)(3) is amended by strik-
23 ing “deduction under section 151” and insert-
24 ing “credit under section 32”.

1 (O) Section 2032A(c)(7)(D) is amended by
2 striking “section 151(c)(4)” and inserting “sec-
3 tion 32(c)(3)(F)”.

4 (P) Section 6012(a)(1)(A) is amended by
5 striking “an exemption for such spouse under
6 section 151(c)” and inserting “a credit for such
7 spouse under section 32”.

8 (Q) Section 7703(b)(1) is amended by
9 striking “deduction for the taxable year under
10 section 151” and inserting “credit for the tax-
11 able year under section 32”.

12 (d) CLERICAL AMENDMENT.—The table of sections
13 for subpart C of part IV of subchapter A of chapter 1
14 is amended by striking the item relating to section 32 and
15 inserting the following:

“Sec. 32. Simplified family credit.”.

16 (e) EFFECTIVE DATE.—

17 (1) IN GENERAL.—The amendments made by
18 this section shall apply to taxable years beginning
19 after December 31, 2003.

20 (2) TRANSITIONAL RULE FOR NONCUSTODIAL
21 PARENTS.—

22 (A) IN GENERAL.—If, on the last day of
23 the taxable year, an eligible individual is the
24 noncustodial parent of a qualifying child, the
25 Internal Revenue Code of 1986 shall be applied

1 to such individual without regard to the amend-
 2 ments made by this section.

3 (B) DEFINITIONS.—For purposes of sub-
 4 paragraph (A), the terms ‘eligible individual’
 5 and ‘qualifying child’ shall have the meanings
 6 given such terms by section 32(c) of the Inter-
 7 nal Revenue Code of 1986 (as amended by this
 8 section).

9 **SEC. 102. CHILD SUPPORT INCLUDED IN GROSS INCOME OF**
 10 **RECIPIENT AND ALLOWED AS DEDUCTION TO**
 11 **PAYOR.**

12 (a) CHILD SUPPORT INCLUDED IN GROSS INCOME.—
 13 Subsection (c) of section 71 of the Internal Revenue Code
 14 of 1986 (relating to alimony and separate maintenance
 15 payments) is amended to read as follows:

16 “(c) PAYMENTS TO SUPPORT CHILDREN.—Notwith-
 17 standing any other provision of this section, the term ‘ali-
 18 mony or separate maintenance payment’ includes any pay-
 19 ment or part of a payment which the terms of the divorce
 20 or separation instrument fix (in terms of an amount of
 21 money or a part of the payment) as a sum which is pay-
 22 able for the support of children of the payor spouse.”.

23 (b) CLARIFICATION THAT CHILD SUPPORT AL-
 24 LOWED AS DEDUCTION.—Subsection (b) of section 215

1 (relating to alimony, etc., payments) is amended by strik-
 2 ing “section 71(b)” and inserting “section 71”.

3 (c) EFFECTIVE DATE.—The amendments made by
 4 this section shall apply to taxable years beginning after
 5 December 31, 2003.

6 **SEC. 103. REFUNDABLE CREDIT FOR PAYROLL TAXES.**

7 (a) IN GENERAL.—Subpart C of part IV of sub-
 8 chapter A of chapter 1 of the Internal Revenue Code of
 9 1986 (relating to refundable credits) is amended by redес-
 10 ignating section 36 as section 37 and by inserting after
 11 section 35 the following new section:

12 **“SEC. 36. CREDIT FOR PAYROLL TAXES.**

13 “(a) IN GENERAL.—In the case of an individual,
 14 there shall be allowed as a credit against the tax imposed
 15 by this subtitle for the taxable year an amount equal to
 16 the social security taxes paid with respect to the individual
 17 for the taxable year.

18 “(b) LIMITATION BASED ON ADJUSTED GROSS IN-
 19 COME.—The amount which (but for this subsection) would
 20 be allowable as a credit under this section shall be reduced
 21 (but not below zero) by the amount which bears the same
 22 ratio to the amount which would be so taken into account
 23 as—

24 “(1) the excess of—

1 “(A) the taxpayer’s modified adjusted
2 gross income for such taxable year, over

3 “(B) \$15,000 (\$30,000 in the case of a
4 joint return), bears to

5 “(2) \$15,000.

6 For purposes of the preceding sentence, the term ‘modi-
7 fied adjusted gross income’ means adjusted gross income
8 increased by any amount excluded from gross income
9 under section 911, 931, or 933.

10 “(c) SOCIAL SECURITY TAXES.—For purposes of this
11 section—

12 “(1) IN GENERAL.—The term ‘social security
13 taxes’ means, with respect to an individual for the
14 taxable year, the sum of—

15 “(A) the amount of the taxes imposed by
16 section 3101, 3111, 3201, 3211, and 3221 on
17 amounts received by the taxpayer during the
18 calendar year in which the taxable year begins,
19 and

20 “(B) the taxes imposed by section 1401 on
21 the self-employment income of the taxpayer for
22 the taxable year.

23 “(2) COORDINATION WITH SPECIAL REFUND OF
24 SOCIAL SECURITY TAXES.—The term ‘social security
25 taxes’ shall not include any taxes to the extent the

1 taxpayer is entitled to a special refund of such taxes
2 under section 6413(c).

3 “(3) SPECIAL RULE.—Any amounts paid pursu-
4 ant to an agreement under section 3121(l) (relating
5 to agreements entered into by American employers
6 with respect to foreign affiliates) which are equiva-
7 lent to the taxes referred to in paragraph (1)(A)
8 shall be treated as taxes referred to in such para-
9 graph.”.

10 (b) CONFORMING AMENDMENTS.—

11 (1) Paragraph (2) of section 1324(b) of title
12 31, United States Code, is amended by inserting “or
13 36” after “section 35”.

14 (2) The table of sections for subpart C of part
15 IV of subchapter A of chapter 1 of the Internal Rev-
16 enue Code of 1986 is amended by striking the last
17 item and inserting the following new items:

“Sec. 36. Credit for payroll taxes.

“Sec. 37. Overpayments of tax.”.

18 (c) EFFECTIVE DATE.—The amendments made by
19 this section shall apply to taxable years beginning after
20 December 31, 2003.

1 **TITLE II—PROVISIONS**
2 **RELATING TO CORPORATE TAX**
3 **Subtitle A—Provisions Designed To**
4 **Curtail Tax Shelters**

5 **SEC. 201. CLARIFICATION OF ECONOMIC SUBSTANCE DOC-**
6 **TRINE.**

7 (a) IN GENERAL.—Section 7701 is amended by re-
8 designating subsection (m) as subsection (n) and by in-
9 serting after subsection (l) the following new subsection:

10 “(m) CLARIFICATION OF ECONOMIC SUBSTANCE
11 DOCTRINE; ETC.—

12 “(1) GENERAL RULES.—

13 “(A) IN GENERAL.—In applying the eco-
14 nomic substance doctrine, the determination of
15 whether a transaction has economic substance
16 shall be made as provided in this paragraph.

17 “(B) DEFINITION OF ECONOMIC SUB-
18 STANCE.—For purposes of subparagraph (A)—

19 “(i) IN GENERAL.—A transaction has
20 economic substance only if—

21 “(I) the transaction changes in a
22 meaningful way (apart from Federal
23 tax effects and, if there are any Fed-
24 eral tax effects, also apart from any

foreign, State, or local tax effects) the taxpayer's economic position, and

“(II) the taxpayer has a substantial nontax purpose for entering into such transaction and the transaction is a reasonable means of accomplishing such purpose.

“(ii) SPECIAL RULE WHERE TAXPAYER RELIES ON PROFIT POTENTIAL.—A transaction shall not be treated as having economic substance by reason of having a potential for profit unless—

“(I) the present value of the reasonably expected pre-tax profit from the transaction is substantial in relation to the present value of the expected net tax benefits that would be allowed if the transaction were respected, and

“(II) the reasonably expected pre-tax profit from the transaction exceeds a risk-free rate of return.

“(C) TREATMENT OF FEES AND FOREIGN TAXES.—Fees and other transaction expenses and foreign taxes shall be taken into account as

1 expenses in determining pre-tax profit under
2 subparagraph (B)(ii).

3 “(2) SPECIAL RULES FOR TRANSACTIONS WITH
4 TAX-INDIFFERENT PARTIES.—

5 “(A) SPECIAL RULES FOR FINANCING
6 TRANSACTIONS.—The form of a transaction
7 which is in substance the borrowing of money
8 or the acquisition of financial capital directly or
9 indirectly from a tax-indifferent party shall not
10 be respected if the present value of the deduc-
11 tions to be claimed with respect to the trans-
12 action is substantially in excess of the present
13 value of the anticipated economic returns of the
14 person lending the money or providing the fi-
15 nancial capital. A public offering shall be treat-
16 ed as a borrowing, or an acquisition of financial
17 capital, from a tax-indifferent party if it is rea-
18 sonably expected that at least 50 percent of the
19 offering will be placed with tax-indifferent par-
20 ties.

21 “(B) ARTIFICIAL INCOME SHIFTING AND
22 BASIS ADJUSTMENTS.—The form of a trans-
23 action with a tax-indifferent party shall not be
24 respected if—

1 “(i) it results in an allocation of in-
 2 come or gain to the tax-indifferent party in
 3 excess of such party’s economic income or
 4 gain, or

5 “(ii) it results in a basis adjustment
 6 or shifting of basis on account of over-
 7 stating the income or gain of the tax-indif-
 8 ferent party.

9 “(3) DEFINITIONS AND SPECIAL RULES.—For
 10 purposes of this subsection—

11 “(A) ECONOMIC SUBSTANCE DOCTRINE.—
 12 The term ‘economic substance doctrine’ means
 13 the common law doctrine under which tax bene-
 14 fits under subtitle A with respect to a trans-
 15 action are not allowable if the transaction does
 16 not have economic substance or lacks a business
 17 purpose.

18 “(B) TAX-INDIFFERENT PARTY.—The
 19 term ‘tax-indifferent party’ means any person
 20 or entity not subject to tax imposed by subtitle
 21 A. A person shall be treated as a tax-indifferent
 22 party with respect to a transaction if the items
 23 taken into account with respect to the trans-
 24 action have no substantial impact on such per-
 25 son’s liability under subtitle A.

1 “(C) SUBSTANTIAL NONTAX PURPOSE.—In
2 applying subclause (II) of paragraph (1)(B)(i),
3 a purpose of achieving a financial accounting
4 benefit shall not be taken into account in deter-
5 mining whether a transaction has a substantial
6 nontax purpose if the origin of such financial
7 accounting benefit is a reduction of income tax.

8 “(D) EXCEPTION FOR PERSONAL TRANS-
9 ACTIONS OF INDIVIDUALS.—In the case of an
10 individual, this subsection shall apply only to
11 transactions entered into in connection with a
12 trade or business or an activity engaged in for
13 the production of income.

14 “(E) TREATMENT OF LESSORS.—In apply-
15 ing subclause (I) of paragraph (1)(B)(ii) to the
16 lessor of tangible property subject to a lease,
17 the expected net tax benefits shall not include
18 the benefits of depreciation, or any tax credit,
19 with respect to the leased property and sub-
20 clause (II) of paragraph (1)(B)(ii) shall be dis-
21 regarded in determining whether any of such
22 benefits are allowable.

23 “(4) OTHER COMMON LAW DOCTRINES NOT AF-
24 FECTED.—Except as specifically provided in this
25 subsection, the provisions of this subsection shall not

1 be construed as altering or supplanting any other
 2 rule of law, and the requirements of this subsection
 3 shall be construed as being in addition to any such
 4 other rule of law.

5 “(5) REGULATIONS.—The Secretary shall pre-
 6 scribe such regulations as may be necessary or ap-
 7 propriate to carry out the purposes of this sub-
 8 section. Such regulations may include exemptions
 9 from the application of this subsection.”

10 (b) EFFECTIVE DATE.—The amendments made by
 11 this section shall apply to transactions entered into after
 12 December 31, 2003.

13 **SEC. 202. PENALTY FOR FAILING TO DISCLOSE REPORT-**
 14 **ABLE TRANSACTION.**

15 (a) IN GENERAL.—Part I of subchapter B of chapter
 16 68 (relating to assessable penalties) is amended by insert-
 17 ing after section 6707 the following new section:

18 **“SEC. 6707A. PENALTY FOR FAILURE TO INCLUDE REPORT-**
 19 **ABLE TRANSACTION INFORMATION WITH RE-**
 20 **TURN OR STATEMENT.**

21 “(a) IMPOSITION OF PENALTY.—Any person who
 22 fails to include on any return or statement any informa-
 23 tion with respect to a reportable transaction which is re-
 24 quired under section 6011 to be included with such return

1 or statement shall pay a penalty in the amount determined
2 under subsection (b).

3 “(b) AMOUNT OF PENALTY.—

4 “(1) IN GENERAL.—Except as provided in para-
5 graphs (2) and (3), the amount of the penalty under
6 subsection (a) shall be \$50,000.

7 “(2) LISTED TRANSACTION.—The amount of
8 the penalty under subsection (a) with respect to a
9 listed transaction shall be \$100,000.

10 “(3) INCREASE IN PENALTY FOR LARGE ENTI-
11 TIES AND HIGH NET WORTH INDIVIDUALS.—

12 “(A) IN GENERAL.—In the case of a fail-
13 ure under subsection (a) by—

14 “(i) a large entity, or

15 “(ii) a high net worth individual,

16 the penalty under paragraph (1) or (2) shall be
17 twice the amount determined without regard to
18 this paragraph.

19 “(B) LARGE ENTITY.—For purposes of
20 subparagraph (A), the term ‘large entity’
21 means, with respect to any taxable year, a per-
22 son (other than a natural person) with gross re-
23 cepts in excess of \$10,000,000 for the taxable
24 year in which the reportable transaction occurs
25 or the preceding taxable year. Rules similar to

1 the rules of paragraph (2) and subparagraphs
2 (B), (C), and (D) of paragraph (3) of section
3 448(c) shall apply for purposes of this subpara-
4 graph.

5 “(C) HIGH NET WORTH INDIVIDUAL.—For
6 purposes of subparagraph (A), the term ‘high
7 net worth individual’ means, with respect to a
8 reportable transaction, a natural person whose
9 net worth exceeds \$2,000,000 immediately be-
10 fore the transaction.

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

12 “(1) REPORTABLE TRANSACTION.—The term
13 ‘reportable transaction’ means any transaction with
14 respect to which information is required to be in-
15 cluded with a return or statement because, as deter-
16 mined under regulations prescribed under section
17 6011, such transaction is of a type which the Sec-
18 retary determines as having a potential for tax
19 avoidance or evasion.

20 “(2) LISTED TRANSACTION.—Except as pro-
21 vided in regulations, the term ‘listed transaction’
22 means a reportable transaction which is the same as,
23 or substantially similar to, a transaction specifically
24 identified by the Secretary as a tax avoidance trans-
25 action for purposes of section 6011.

1 “(d) AUTHORITY TO RESCIND PENALTY.—

2 “(1) IN GENERAL.—The Commissioner of In-
3 ternal Revenue may rescind all or any portion of any
4 penalty imposed by this section with respect to any
5 violation if—

6 “(A) the violation is with respect to a re-
7 portable transaction other than a listed trans-
8 action,

9 “(B) the person on whom the penalty is
10 imposed has a history of complying with the re-
11 quirements of this title,

12 “(C) it is shown that the violation is due
13 to an unintentional mistake of fact;

14 “(D) imposing the penalty would be
15 against equity and good conscience, and

16 “(E) rescinding the penalty would promote
17 compliance with the requirements of this title
18 and effective tax administration.

19 “(2) DISCRETION.—The exercise of authority
20 under paragraph (1) shall be at the sole discretion
21 of the Commissioner and may be delegated only to
22 the head of the Office of Tax Shelter Analysis. The
23 Commissioner, in the Commissioner’s sole discretion,
24 may establish a procedure to determine if a penalty
25 should be referred to the Commissioner or the head

1 of such Office for a determination under paragraph
2 (1).

3 “(3) NO APPEAL.—Notwithstanding any other
4 provision of law, any determination under this sub-
5 section may not be reviewed in any administrative or
6 judicial proceeding.

7 “(4) RECORDS.—If a penalty is rescinded under
8 paragraph (1), the Commissioner shall place in the
9 file in the Office of the Commissioner the opinion of
10 the Commissioner or the head of the Office of Tax
11 Shelter Analysis with respect to the determination,
12 including—

13 “(A) the facts and circumstances of the
14 transaction,

15 “(B) the reasons for the rescission, and

16 “(C) the amount of the penalty rescinded.

17 “(5) REPORT.—The Commissioner shall each
18 year report to the Committee on Ways and Means
19 of the House of Representatives and the Committee
20 on Finance of the Senate—

21 “(A) a summary of the total number and
22 aggregate amount of penalties imposed, and re-
23 scinded, under this section, and

1 “(B) a description of each penalty re-
2 scinded under this subsection and the reasons
3 therefor.

4 “(e) PENALTY REPORTED TO SEC.—In the case of
5 a person—

6 “(1) which is required to file periodic reports
7 under section 13 or 15(d) of the Securities Ex-
8 change Act of 1934 or is required to be consolidated
9 with another person for purposes of such reports,
10 and

11 “(2) which—

12 “(A) is required to pay a penalty under
13 this section with respect to a listed transaction,

14 “(B) is required to pay a penalty under
15 section 6662A with respect to any reportable
16 transaction at a rate prescribed under section
17 6662A(c), or

18 “(C) is required to pay a penalty under
19 section 6662B with respect to any noneconomic
20 substance transaction,

21 the requirement to pay such penalty shall be disclosed in
22 such reports filed by such person for such periods as the
23 Secretary shall specify. Failure to make a disclosure in
24 accordance with the preceding sentence shall be treated

1 as a failure to which the penalty under subsection (b)(2)
 2 applies.

3 “(f) COORDINATION WITH OTHER PENALTIES.—The
 4 penalty imposed by this section is in addition to any pen-
 5 alty imposed under this title.”.

6 (b) CONFORMING AMENDMENT.—The table of sec-
 7 tions for part I of subchapter B of chapter 68 is amended
 8 by inserting after the item relating to section 6707 the
 9 following:

“Sec. 6707A. Penalty for failure to include reportable transaction
 information with return or statement.”.

10 (c) EFFECTIVE DATE.—The amendments made by
 11 this section shall apply to returns and statements the due
 12 date for which is after the date of the enactment of this
 13 Act.

14 **SEC. 203. ACCURACY-RELATED PENALTY FOR LISTED**
 15 **TRANSACTIONS AND OTHER REPORTABLE**
 16 **TRANSACTIONS HAVING A SIGNIFICANT TAX**
 17 **AVOIDANCE PURPOSE.**

18 (a) IN GENERAL.—Subchapter A of chapter 68 is
 19 amended by inserting after section 6662 the following new
 20 section:

1 **“SEC. 6662A. IMPOSITION OF ACCURACY-RELATED PEN-**
 2 **ALTY ON UNDERSTATEMENTS WITH RESPECT**
 3 **TO REPORTABLE TRANSACTIONS.**

4 “(a) IMPOSITION OF PENALTY.—If a taxpayer has a
 5 reportable transaction understatement for any taxable
 6 year, there shall be added to the tax an amount equal to
 7 20 percent of the amount of such understatement.

8 “(b) REPORTABLE TRANSACTION UNDERSTATE-
 9 MENT.—For purposes of this section—

10 “(1) IN GENERAL.—The term ‘reportable trans-
 11 action understatement’ means the sum of—

12 “(A) the product of—

13 “(i) the amount of the increase (if
 14 any) in taxable income which results from
 15 a difference between the proper tax treat-
 16 ment of an item to which this section ap-
 17 plies and the taxpayer’s treatment of such
 18 item (as shown on the taxpayer’s return of
 19 tax), and

20 “(ii) the highest rate of tax imposed
 21 by section 1 (section 11 in the case of a
 22 taxpayer which is a corporation), and

23 “(B) the amount of the decrease (if any)
 24 in the aggregate amount of credits determined
 25 under subtitle A which results from a difference
 26 between the taxpayer’s treatment of an item to

1 which this section applies (as shown on the tax-
 2 payer’s return of tax) and the proper tax treat-
 3 ment of such item.

4 For purposes of subparagraph (A), any reduction of
 5 the excess of deductions allowed for the taxable year
 6 over gross income for such year, and any reduction
 7 in the amount of capital losses which would (without
 8 regard to section 1211) be allowed for such year,
 9 shall be treated as an increase in taxable income.

10 “(2) ITEMS TO WHICH SECTION APPLIES.—This
 11 section shall apply to any item which is attributable
 12 to—

13 “(A) any listed transaction, and

14 “(B) any reportable transaction (other
 15 than a listed transaction) if a significant pur-
 16 pose of such transaction is the avoidance or
 17 evasion of Federal income tax.

18 “(c) HIGHER PENALTY FOR NONDISCLOSED LISTED
 19 AND OTHER AVOIDANCE TRANSACTIONS.—

20 “(1) IN GENERAL.—Subsection (a) shall be ap-
 21 plied by substituting ‘30 percent’ for ‘20 percent’
 22 with respect to the portion of any reportable trans-
 23 action understatement with respect to which the re-
 24 quirement of section 6664(d)(2)(A) is not met.

1 “(2) RULES APPLICABLE TO COMPROMISE OF
2 PENALTY.—

3 “(A) IN GENERAL.—If the 1st letter of
4 proposed deficiency which allows the taxpayer
5 an opportunity for administrative review in the
6 Internal Revenue Service Office of Appeals has
7 been sent with respect to a penalty to which
8 paragraph (1) applies, only the Commissioner
9 of Internal Revenue may compromise all or any
10 portion of such penalty.

11 “(B) APPLICABLE RULES.—The rules of
12 paragraphs (3), (4), and (5) of section
13 6707A(d) shall apply for purposes of subpara-
14 graph (A).

15 “(d) DEFINITIONS OF REPORTABLE AND LISTED
16 TRANSACTIONS.—For purposes of this section, the terms
17 ‘reportable transaction’ and ‘listed transaction’ have the
18 respective meanings given to such terms by section
19 6707A(c).

20 “(e) SPECIAL RULES.—

21 “(1) COORDINATION WITH PENALTIES, ETC.,
22 ON OTHER UNDERSTATEMENTS.—In the case of an
23 understatement (as defined in section 6662(d)(2))—

24 “(A) the amount of such understatement
25 (determined without regard to this paragraph)

shall be increased by the aggregate amount of reportable transaction understatements and noneconomic substance transaction understatements for purposes of determining whether such understatement is a substantial understatement under section 6662(d)(1), and

“(B) the addition to tax under section 6662(a) shall apply only to the excess of the amount of the substantial understatement (if any) after the application of subparagraph (A) over the aggregate amount of reportable transaction understatements and noneconomic substance transaction understatements.

“(2) COORDINATION WITH OTHER PENALTIES.—

“(A) APPLICATION OF FRAUD PENALTY.—References to an underpayment in section 6663 shall be treated as including references to a reportable transaction understatement and a noneconomic substance transaction understatement.

“(B) NO DOUBLE PENALTY.—This section shall not apply to any portion of an understatement on which a penalty is imposed under section 6662B or 6663.

1 “(3) SPECIAL RULE FOR AMENDED RE-
 2 TURNS.—Except as provided in regulations, in no
 3 event shall any tax treatment included with an
 4 amendment or supplement to a return of tax be
 5 taken into account in determining the amount of any
 6 reportable transaction understatement or non-
 7 economic substance transaction understatement if
 8 the amendment or supplement is filed after the ear-
 9 lier of the date the taxpayer is first contacted by the
 10 Secretary regarding the examination of the return or
 11 such other date as is specified by the Secretary.

12 “(4) NONECONOMIC SUBSTANCE TRANS-
 13 ACTION UNDERSTATEMENT.—For purposes of
 14 this subsection, the term ‘noneconomic sub-
 15 stance transaction understatement’ has the
 16 meaning given such term by section 6662B(c).

17 “(5) CROSS REFERENCE.—

**“For reporting of section 6662A(c) penalty to the
 Securities and Exchange Commission, see section
 6707A(e).”**

18 (b) DETERMINATION OF OTHER UNDERSTATE-
 19 MENTS.—Subparagraph (A) of section 6662(d)(2) is
 20 amended by adding at the end the following flush sen-
 21 tence:

22 “The excess under the preceding sentence shall
 23 be determined without regard to items to which
 24 section 6662A applies and without regard to

1 items with respect to which a penalty is im-
 2 posed by section 6662B.”

3 (c) REASONABLE CAUSE EXCEPTION.—

4 (1) IN GENERAL.—Section 6664 is amended by
 5 adding at the end the following new subsection:

6 “(d) REASONABLE CAUSE EXCEPTION FOR REPORT-
 7 ABLE TRANSACTION UNDERSTATEMENTS.—

8 “(1) IN GENERAL.—No penalty shall be im-
 9 posed under section 6662A with respect to any por-
 10 tion of a reportable transaction understatement if it
 11 is shown that there was a reasonable cause for such
 12 portion and that the taxpayer acted in good faith
 13 with respect to such portion.

14 “(2) SPECIAL RULES.—Paragraph (1) shall not
 15 apply to any reportable transaction understatement
 16 unless—

17 “(A) the relevant facts affecting the tax
 18 treatment of the item are adequately disclosed
 19 in accordance with the regulations prescribed
 20 under section 6011,

21 “(B) there is or was substantial authority
 22 for such treatment, and

23 “(C) the taxpayer reasonably believed that
 24 such treatment was more likely than not the
 25 proper treatment.

1 A taxpayer failing to adequately disclose in accord-
2 ance with section 6011 shall be treated as meeting
3 the requirements of subparagraph (A) if the penalty
4 for such failure was rescinded under section
5 6707A(d).

6 “(3) RULES RELATING TO REASONABLE BE-
7 LIEF.—For purposes of paragraph (2)(C)—

8 “(A) IN GENERAL.—A taxpayer shall be
9 treated as having a reasonable belief with re-
10 spect to the tax treatment of an item only if
11 such belief—

12 “(i) is based on the facts and law that
13 exist at the time the return of tax which
14 includes such tax treatment is filed, and

15 “(ii) relates solely to the taxpayer’s
16 chances of success on the merits of such
17 treatment and does not take into account
18 the possibility that a return will not be au-
19 dited, such treatment will not be raised on
20 audit, or such treatment will be resolved
21 through settlement if it is raised.

22 “(B) CERTAIN OPINIONS MAY NOT BE RE-
23 LIED UPON.—

24 “(i) IN GENERAL.—An opinion of a
25 tax advisor may not be relied upon to es-

1 tablish the reasonable belief of a taxpayer
2 if—

3 “(I) the tax advisor is described
4 in clause (ii), or

5 “(II) the opinion is described in
6 clause (iii).

7 “(ii) DISQUALIFIED TAX ADVISORS.—
8 A tax advisor is described in this clause if
9 the tax advisor—

10 “(I) is a material advisor (within
11 the meaning of section 6111(b)(1))
12 who participates in the organization,
13 management, promotion, or sale of
14 the transaction or who is related
15 (within the meaning of section 267(b)
16 or 707(b)(1)) to any person who so
17 participates,

18 “(II) is compensated directly or
19 indirectly by a material advisor with
20 respect to the transaction,

21 “(III) has a fee arrangement
22 with respect to the transaction which
23 is contingent on all or part of the in-
24 tended tax benefits from the trans-
25 action being sustained, or

1 “(IV) as determined under regu-
2 lations prescribed by the Secretary,
3 has a continuing financial interest
4 with respect to the transaction.

5 “(iii) DISQUALIFIED OPINIONS.—For
6 purposes of clause (i), an opinion is dis-
7 qualified if the opinion—

8 “(I) is based on unreasonable
9 factual or legal assumptions (includ-
10 ing assumptions as to future events),

11 “(II) unreasonably relies on rep-
12 resentations, statements, findings, or
13 agreements of the taxpayer or any
14 other person,

15 “(III) does not identify and con-
16 sider all relevant facts, or

17 “(IV) fails to meet any other re-
18 quirement as the Secretary may pre-
19 scribe.”

20 (2) CONFORMING AMENDMENT.—The heading
21 for subsection (c) of section 6664 is amended by in-
22 serting “FOR UNDERPAYMENTS” after “EXCEP-
23 TION”.

24 (d) CONFORMING AMENDMENTS.—

1 (1) Subparagraph (C) of section 461(i)(3) is
2 amended by striking “section 6662(d)(2)(C)(iii)”
3 and inserting “section 1274(b)(3)(C)”.

4 (2) Paragraph (3) of section 1274(b) is amend-
5 ed—

6 (A) by striking “(as defined in section
7 6662(d)(2)(C)(iii))” in subparagraph (B)(i),
8 and

9 (B) by adding at the end the following new
10 subparagraph:

11 “(C) TAX SHELTER.—For purposes of sub-
12 paragraph (B), the term ‘tax shelter’ means—

13 “(i) a partnership or other entity,

14 “(ii) any investment plan or arrange-
15 ment, or

16 “(iii) any other plan or arrange-
17 ment—

18 if a significant purpose of such partnership, en-
19 tity, plan, or arrangement is the avoidance or
20 evasion of Federal income tax.”

21 (3) Section 6662(d)(2) is amended by striking
22 subparagraphs (C) and (D).

23 (4) Section 6664(c)(1) is amended by striking
24 “this part” and inserting “section 6662 or 6663”.

4 (6)(A) The heading for section 6662 is amend-
5 ed to read as follows:

6 **“SEC. 6662. IMPOSITION OF ACCURACY-RELATED PENALTY**
7 **ON UNDERPAYMENTS.”**

8 (B) The table of sections for part II of sub-
9 chapter A of chapter 68 is amended by striking the
10 item relating to section 6662 and inserting the fol-
11 lowing new items:

“Sec. 6662. Imposition of accuracy-related penalty on underpayments.

“Sec. 6662A. Imposition of accuracy-related penalty on understatements with respect to reportable transactions.”

(e) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years ending after the date of the enactment of this Act.

15 SEC. 204. PENALTY FOR UNDERSTATEMENTS ATTRIB-
16 UTABLE TO TRANSACTIONS LACKING ECO-
17 NOMIC SUBSTANCE, ETC.

18 (a) IN GENERAL.—Subchapter A of chapter 68 is
19 amended by inserting after section 6662A the following
20 new section:

1 **“SEC. 6662B. PENALTY FOR UNDERSTATEMENTS ATTRIB-**
2 **UTABLE TO TRANSACTIONS LACKING ECO-**
3 **NOMIC SUBSTANCE, ETC.**

4 “(a) IMPOSITION OF PENALTY.—If a taxpayer has an
5 noneconomic substance transaction understatement for
6 any taxable year, there shall be added to the tax an
7 amount equal to 40 percent of the amount of such under-
8 statement.

9 “(b) REDUCTION OF PENALTY FOR DISCLOSED
10 TRANSACTIONS.—Subsection (a) shall be applied by sub-
11 stituting ‘20 percent’ for ‘40 percent’ with respect to the
12 portion of any noneconomic substance transaction under-
13 statement with respect to which the relevant facts affect-
14 ing the tax treatment of the item are adequately disclosed
15 in the return or a statement attached to the return.

16 “(c) NONECONOMIC SUBSTANCE TRANSACTION UN-
17 DERSTATEMENT.—For purposes of this section—

18 “(1) IN GENERAL.—The term ‘noneconomic
19 substance transaction understatement’ means any
20 amount which would be an understatement under
21 section 6662A(b)(1) if section 6662A were applied
22 by taking into account items attributable to non-
23 economic substance transactions rather than items
24 to which section 6662A would apply without regard
25 to this paragraph.

1 “(2) NONECONOMIC SUBSTANCE TRANS-
2 ACTION.—The term ‘noneconomic substance trans-
3 action’ means any transaction if—

4 “(A) there is a lack of economic substance
5 (within the meaning of section 7701(m)(1)) for
6 the transaction giving rise to the claimed tax
7 benefit or the transaction was not respected
8 under section 7701(m)(2), or

9 “(B) the transaction fails to meet the re-
10 quirements of any similar rule of law.

11 “(d) RULES APPLICABLE TO COMPROMISE OF PEN-
12 ALTY.—

13 “(1) IN GENERAL.—If the 1st letter of pro-
14 posed deficiency which allows the taxpayer an oppor-
15 tunity for administrative review in the Internal Rev-
16 enue Service Office of Appeals has been sent with
17 respect to a penalty to which this section applies,
18 only the Commissioner of Internal Revenue may
19 compromise all or any portion of such penalty.

20 “(2) APPLICABLE RULES.—The rules of para-
21 graphs (3), (4), and (5) of section 6707A(d) shall
22 apply for purposes of paragraph (1).

23 “(e) COORDINATION WITH OTHER PENALTIES.—Ex-
24 cept as otherwise provided in this part, the penalty im-

1 posed by this section shall be in addition to any other pen-
 2 alty imposed by this title.

3 “(f) CROSS REFERENCES.—

“**(1) For coordination of penalty with understate-
 ments under section 6662 and other special rules,
 see section 6662A(e).**

“**(2) For reporting of penalty imposed under this
 section to the Securities and Exchange Commission,
 see section 6707A(e).**”

4 (b) CLERICAL AMENDMENT.—The table of sections
 5 for part II of subchapter A of chapter 68 is amended by
 6 inserting after the item relating to section 6662A the fol-
 7 lowing new item:

“Sec. 6662B. Penalty for understatements attributable to trans-
 actions lacking economic substance, etc.”

8 (c) EFFECTIVE DATE.—The amendments made by
 9 this section shall apply to transactions entered into after
 10 December 31, 2003.

11 **SEC. 205. MODIFICATIONS OF SUBSTANTIAL UNDERSTATE-**
 12 **MENT PENALTY FOR NONREPORTABLE**
 13 **TRANSACTIONS.**

14 (a) SUBSTANTIAL UNDERSTATEMENT OF CORPORA-
 15 TIONS.—Section 6662(d)(1)(B) (relating to special rule
 16 for corporations) is amended to read as follows:

17 “(B) SPECIAL RULE FOR CORPORA-
 18 TIONS.—In the case of a corporation other than
 19 an S corporation or a personal holding company
 20 (as defined in section 542), there is a substan-
 21 tial understatement of income tax for any tax-

1 able year if the amount of the understatement
2 for the taxable year exceeds the lesser of—

3 “(i) 10 percent of the tax required to
4 be shown on the return for the taxable
5 year (or, if greater, \$10,000), or

6 “(ii) \$10,000,000.”

7 (b) REDUCTION FOR UNDERSTATEMENT OF TAX-
8 PAYER DUE TO POSITION OF TAXPAYER OR DISCLOSED
9 ITEM.—

10 (1) IN GENERAL.—Section 6662(d)(2)(B)(i)
11 (relating to substantial authority) is amended to
12 read as follows:

13 “(i) the tax treatment of any item by
14 the taxpayer if the taxpayer had reason-
15 able belief that the tax treatment was more
16 likely than not the proper treatment, or”.

17 (2) CONFORMING AMENDMENT.—Section
18 6662(d) is amended by adding at the end the fol-
19 lowing new paragraph:

20 “(3) SECRETARIAL LIST.—For purposes of this
21 subsection, section 6664(d)(2), and section
22 6694(a)(1), the Secretary may prescribe a list of po-
23 sitions for which the Secretary believes there is not
24 substantial authority or there is no reasonable belief
25 that the tax treatment is more likely than not the

1 proper tax treatment. Such list (and any revisions
2 thereof) shall be published in the Federal Register
3 or the Internal Revenue Bulletin.”

4 (c) EFFECTIVE DATE.—The amendments made by
5 this section shall apply to taxable years beginning after
6 the date of the enactment of this Act.

7 **SEC. 206. TAX SHELTER EXCEPTION TO CONFIDENTIALITY**
8 **PRIVILEGES RELATING TO TAXPAYER COM-**
9 **MUNICATIONS.**

10 (a) IN GENERAL.—Section 7525(b) (relating to sec-
11 tion not to apply to communications regarding corporate
12 tax shelters) is amended to read as follows:

13 “(b) SECTION NOT TO APPLY TO COMMUNICATIONS
14 REGARDING TAX SHELTERS.—The privilege under sub-
15 section (a) shall not apply to any written communication
16 which is—

17 “(1) between a federally authorized tax practi-
18 tioner and—

19 “(A) any person,

20 “(B) any director, officer, employee, agent,
21 or representative of the person, or

22 “(C) any other person holding a capital or
23 profits interest in the person, and

1 “(2) in connection with the promotion of the di-
 2 rect or indirect participation of the person in any
 3 tax shelter (as defined in section 1274(b)(3)(C)).”

4 (b) EFFECTIVE DATE.—The amendment made by
 5 this section shall apply to communications made on or
 6 after the date of the enactment of this Act.

7 **SEC. 207. DISCLOSURE OF REPORTABLE TRANSACTIONS.**

8 (a) IN GENERAL.—Section 6111 (relating to registra-
 9 tion of tax shelters) is amended to read as follows:

10 **“SEC. 6111. DISCLOSURE OF REPORTABLE TRANSACTIONS.**

11 “(a) IN GENERAL.—Each material advisor with re-
 12 spect to any reportable transaction shall make a return
 13 (in such form as the Secretary may prescribe) setting
 14 forth—

15 “(1) information identifying and describing the
 16 transaction,

17 “(2) information describing any potential tax
 18 benefits expected to result from the transaction, and

19 “(3) such other information as the Secretary
 20 may prescribe.

21 Such return shall be filed not later than the date specified
 22 by the Secretary.

23 “(b) DEFINITIONS.—For purposes of this section—

24 “(1) MATERIAL ADVISOR.—

1 “(A) IN GENERAL.—The term ‘material
2 advisor’ means any person—

3 “(i) who provides any material aid,
4 assistance, or advice with respect to orga-
5 nizing, promoting, selling, implementing,
6 or carrying out any reportable transaction,
7 and

8 “(ii) who directly or indirectly derives
9 gross income in excess of the threshold
10 amount for such aid, assistance, or advice.

11 “(B) THRESHOLD AMOUNT.—For purposes
12 of subparagraph (A), the threshold amount is—

13 “(i) \$50,000 in the case of a report-
14 able transaction substantially all of the tax
15 benefits from which are provided to nat-
16 ural persons, and

17 “(ii) \$250,000 in any other case.

18 “(2) REPORTABLE TRANSACTION.—The term
19 ‘reportable transaction’ has the meaning given to
20 such term by section 6707A(c).

21 “(c) REGULATIONS.—The Secretary may prescribe
22 regulations which provide—

23 “(1) that only 1 person shall be required to
24 meet the requirements of subsection (a) in cases in

1 which 2 or more persons would otherwise be re-
 2 quired to meet such requirements,

3 “(2) exemptions from the requirements of this
 4 section, and

5 “(3) such rules as may be necessary or appro-
 6 priate to carry out the purposes of this section.”

7 (b) CONFORMING AMENDMENTS.—

8 (1) The item relating to section 6111 in the
 9 table of sections for subchapter B of chapter 61 is
 10 amended to read as follows:

 “Sec. 6111. Disclosure of reportable transactions.”

11 (2)(A) So much of section 6112 as precedes
 12 subsection (c) thereof is amended to read as follows:

13 **“SEC. 6112. MATERIAL ADVISORS OF REPORTABLE TRANS-**
 14 **ACTIONS MUST KEEP LISTS OF ADVISEES.**

15 “(a) IN GENERAL.—Each material advisor (as de-
 16 fined in section 6111) with respect to any reportable
 17 transaction (as defined in section 6707A(c)) shall main-
 18 tain, in such manner as the Secretary may by regulations
 19 prescribe, a list—

20 “(1) identifying each person with respect to
 21 whom such advisor acted as such a material advisor
 22 with respect to such transaction, and

23 “(2) containing such other information as the
 24 Secretary may by regulations require.

1 This section shall apply without regard to whether a mate-
 2 rial advisor is required to file a return under section 6111
 3 with respect to such transaction.”

4 (B) Section 6112 is amended by redesignating
 5 subsection (c) as subsection (b).

6 (C) Section 6112(b), as redesignated by sub-
 7 paragraph (B), is amended—

8 (i) by inserting “written” before “request”
 9 in paragraph (1)(A), and

10 (ii) by striking “shall prescribe” in para-
 11 graph (2) and inserting “may prescribe”.

12 (D) The item relating to section 6112 in the
 13 table of sections for subchapter B of chapter 61 is
 14 amended to read as follows:

“Sec. 6112. Material advisors of reportable transactions must
 keep lists of advisees.”

15 (3)(A) The heading for section 6708 is amend-
 16 ed to read as follows:

17 **“SEC. 6708. FAILURE TO MAINTAIN LISTS OF ADVISEES**
 18 **WITH RESPECT TO REPORTABLE TRANS-**
 19 **ACTIONS.”**

20 (B) The item relating to section 6708 in the
 21 table of sections for part I of subchapter B of chap-
 22 ter 68 is amended to read as follows:

“Sec. 6708. Failure to maintain lists of advisees with respect to
 reportable transactions.”

1 (c) EFFECTIVE DATE.—The amendments made by
 2 this section shall apply to transactions with respect to
 3 which material aid, assistance, or advice referred to in sec-
 4 tion 6111(b)(1)(A)(i) of the Internal Revenue Code of
 5 1986 (as added by this section) is provided after the date
 6 of the enactment of this Act.

7 **SEC. 208. MODIFICATIONS TO PENALTY FOR FAILURE TO**
 8 **REGISTER TAX SHELTERS.**

9 (a) IN GENERAL.—Section 6707 (relating to failure
 10 to furnish information regarding tax shelters) is amended
 11 to read as follows:

12 **“SEC. 6707. FAILURE TO FURNISH INFORMATION REGARD-**
 13 **ING REPORTABLE TRANSACTIONS.**

14 “(a) IN GENERAL.—If a person who is required to
 15 file a return under section 6111(a) with respect to any
 16 reportable transaction—

17 “(1) fails to file such return on or before the
 18 date prescribed therefor, or

19 “(2) files false or incomplete information with
 20 the Secretary with respect to such transaction,

21 such person shall pay a penalty with respect to such return
 22 in the amount determined under subsection (b).

23 “(b) AMOUNT OF PENALTY.—

1 “(1) IN GENERAL.—Except as provided in para-
 2 graph (2), the penalty imposed under subsection (a)
 3 with respect to any failure shall be \$50,000.

4 “(2) LISTED TRANSACTIONS.—The penalty im-
 5 posed under subsection (a) with respect to any listed
 6 transaction shall be an amount equal to the greater
 7 of—

8 “(A) \$200,000, or

9 “(B) 50 percent of the gross income de-
 10 rived by such person with respect to aid, assist-
 11 ance, or advice which is provided with respect
 12 to the reportable transaction before the date the
 13 return including the transaction is filed under
 14 section 6111.

15 Subparagraph (B) shall be applied by substituting
 16 ‘75 percent’ for ‘50 percent’ in the case of an inten-
 17 tional failure or act described in subsection (a).

18 “(c) RESCISSION AUTHORITY.—The provisions of
 19 section 6707A(d) (relating to authority of Commissioner
 20 to rescind penalty) shall apply to any penalty imposed
 21 under this section.

22 “(d) REPORTABLE AND LISTED TRANSACTIONS.—
 23 The terms ‘reportable transaction’ and ‘listed transaction’
 24 have the respective meanings given to such terms by sec-
 25 tion 6707A(c).”.

1 (b) CLERICAL AMENDMENT.—The item relating to
 2 section 6707 in the table of sections for part I of sub-
 3 chapter B of chapter 68 is amended by striking “tax shel-
 4 ters” and inserting “reportable transactions”.

5 (c) EFFECTIVE DATE.—The amendments made by
 6 this section shall apply to returns the due date for which
 7 is after the date of the enactment of this Act.

8 **SEC. 209. MODIFICATION OF PENALTY FOR FAILURE TO**
 9 **MAINTAIN LISTS OF INVESTORS.**

10 (a) IN GENERAL.—Subsection (a) of section 6708 is
 11 amended to read as follows:

12 “(a) IMPOSITION OF PENALTY.—

13 “(1) IN GENERAL.—If any person who is re-
 14 quired to maintain a list under section 6112(a) fails
 15 to make such list available upon written request to
 16 the Secretary in accordance with section
 17 6112(b)(1)(A) within 20 business days after the
 18 date of the Secretary’s request, such person shall
 19 pay a penalty of \$10,000 for each day of such fail-
 20 ure after such 20th day.

21 “(2) REASONABLE CAUSE EXCEPTION.—No
 22 penalty shall be imposed by paragraph (1) with re-
 23 spect to the failure on any day if such failure is due
 24 to reasonable cause.”

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

4 **SEC. 210. MODIFICATION OF ACTIONS TO ENJOIN CERTAIN**
5 **CONDUCT RELATED TO TAX SHELTERS AND**
6 **REPORTABLE TRANSACTIONS.**

7 (a) IN GENERAL.—Section 7408 (relating to action
8 to enjoin promoters of abusive tax shelters, etc.) is amend-
9 ed by redesignating subsection (c) as subsection (d) and
10 by striking subsections (a) and (b) and inserting the fol-
11 lowing new subsections:

12 “(a) AUTHORITY TO SEEK INJUNCTION.—A civil ac-
13 tion in the name of the United States to enjoin any person
14 from further engaging in specified conduct may be com-
15 menced at the request of the Secretary. Any action under
16 this section shall be brought in the district court of the
17 United States for the district in which such person resides,
18 has his principal place of business, or has engaged in spec-
19 ified conduct. The court may exercise its jurisdiction over
20 such action (as provided in section 7402(a)) separate and
21 apart from any other action brought by the United States
22 against such person.

23 “(b) ADJUDICATION AND DECREE.—In any action
24 under subsection (a), if the court finds—

1 “(1) that the person has engaged in any speci-
2 fied conduct, and

3 “(2) that injunctive relief is appropriate to pre-
4 vent recurrence of such conduct—

5 the court may enjoin such person from engaging in such
6 conduct or in any other activity subject to penalty under
7 this title.

8 “(c) SPECIFIED CONDUCT.—For purposes of this
9 section, the term ‘specified conduct’ means any action, or
10 failure to take action, subject to penalty under section
11 6700, 6701, 6707, or 6708.”

12 (b) CONFORMING AMENDMENTS.—

13 (1) The heading for section 7408 is amended to
14 read as follows:

15 **“SEC. 7408. ACTIONS TO ENJOIN SPECIFIED CONDUCT RE-**
16 **LATED TO TAX SHELTERS AND REPORTABLE**
17 **TRANSACTIONS.”**

18 (2) The table of sections for subchapter A of
19 chapter 67 is amended by striking the item relating
20 to section 7408 and inserting the following new
21 item:

“Sec. 7408. Actions to enjoin specified conduct related to tax shelters and
reportable transactions.”

22 (c) EFFECTIVE DATE.—The amendment made by
23 this section shall take effect on the day after the date of
24 the enactment of this Act.

1 **SEC. 211. UNDERSTATEMENT OF TAXPAYER'S LIABILITY BY**
2 **INCOME TAX RETURN PREPARER.**

3 (a) STANDARDS CONFORMED TO TAXPAYER STAND-
4 ARDS.—Section 6694(a) (relating to understatements due
5 to unrealistic positions) is amended—

6 (1) by striking “realistic possibility of being
7 sustained on its merits” in paragraph (1) and in-
8 serting “reasonable belief that the tax treatment in
9 such position was more likely than not the proper
10 treatment”,

11 (2) by striking “or was frivolous” in paragraph
12 (3) and inserting “or there was no reasonable basis
13 for the tax treatment of such position”, and

14 (3) by striking “UNREALISTIC” in the heading
15 and inserting “IMPROPER”.

16 (b) AMOUNT OF PENALTY.—Section 6694 is amend-
17 ed—

18 (1) by striking “\$250” in subsection (a) and in-
19 serting “\$1,000”, and

20 (2) by striking “\$1,000” in subsection (b) and
21 inserting “\$5,000”.

22 (c) EFFECTIVE DATE.—The amendments made by
23 this section shall apply to documents prepared after the
24 date of the enactment of this Act.

1 **SEC. 212. PENALTY ON FAILURE TO REPORT INTERESTS IN**
2 **FOREIGN FINANCIAL ACCOUNTS.**

3 (a) IN GENERAL.—Section 5321(a)(5) of title 31,
4 United States Code, is amended to read as follows:

5 “(5) FOREIGN FINANCIAL AGENCY TRANS-
6 ACTION VIOLATION.—

7 “(A) PENALTY AUTHORIZED.—The Sec-
8 retary of the Treasury may impose a civil
9 money penalty on any person who violates, or
10 causes any violation of, any provision of section
11 5314.

12 “(B) AMOUNT OF PENALTY.—

13 “(i) IN GENERAL.—Except as pro-
14 vided in subparagraph (C), the amount of
15 any civil penalty imposed under subpara-
16 graph (A) shall not exceed \$5,000.

17 “(ii) REASONABLE CAUSE EXCEP-
18 TION.—No penalty shall be imposed under
19 subparagraph (A) with respect to any vio-
20 lation if—

21 “(I) such violation was due to
22 reasonable cause, and

23 “(II) the amount of the trans-
24 action or the balance in the account
25 at the time of the transaction was
26 properly reported.

1 “(C) WILLFUL VIOLATIONS.—In the case
2 of any person willfully violating, or willfully
3 causing any violation of, any provision of sec-
4 tion 5314—

5 “(i) the maximum penalty under sub-
6 paragraph (B)(i) shall be increased to the
7 greater of—

8 “(I) \$25,000, or

9 “(II) the amount (not exceeding
10 \$100,000) determined under subpara-
11 graph (D), and

12 “(ii) subparagraph (B)(ii) shall not
13 apply.

14 “(D) AMOUNT.—The amount determined
15 under this subparagraph is—

16 “(i) in the case of a violation involving
17 a transaction, the amount of the trans-
18 action, or

19 “(ii) in the case of a violation involv-
20 ing a failure to report the existence of an
21 account or any identifying information re-
22 quired to be provided with respect to an
23 account, the balance in the account at the
24 time of the violation.”

1 (b) EFFECTIVE DATE.—The amendment made by
2 this section shall apply to violations occurring after the
3 date of the enactment of this Act.

4 **SEC. 213. FRIVOLOUS TAX SUBMISSIONS.**

5 (a) CIVIL PENALTIES.—Section 6702 is amended to
6 read as follows:

7 **“SEC. 6702. FRIVOLOUS TAX SUBMISSIONS.**

8 “(a) CIVIL PENALTY FOR FRIVOLOUS TAX RE-
9 TURNS.—A person shall pay a penalty of \$5,000 if—

10 “(1) such person files what purports to be a re-
11 turn of a tax imposed by this title but which—

12 “(A) does not contain information on
13 which the substantial correctness of the self-as-
14 sessment may be judged, or

15 “(B) contains information that on its face
16 indicates that the self-assessment is substan-
17 tially incorrect; and

18 “(2) the conduct referred to in paragraph (1)—

19 “(A) is based on a position which the Sec-
20 retary has identified as frivolous under sub-
21 section (c), or

22 “(B) reflects a desire to delay or impede
23 the administration of Federal tax laws.

24 “(b) CIVIL PENALTY FOR SPECIFIED FRIVOLOUS
25 SUBMISSIONS.—

1 “(1) IMPOSITION OF PENALTY.—Except as pro-
2 vided in paragraph (3), any person who submits a
3 specified frivolous submission shall pay a penalty of
4 \$5,000.

5 “(2) SPECIFIED FRIVOLOUS SUBMISSION.—For
6 purposes of this section—

7 “(A) SPECIFIED FRIVOLOUS SUBMIS-
8 SION.—The term ‘specified frivolous submis-
9 sion’ means a specified submission if any por-
10 tion of such submission—

11 “(i) is based on a position which the
12 Secretary has identified as frivolous under
13 subsection (c), or

14 “(ii) reflects a desire to delay or im-
15 pede the administration of Federal tax
16 laws.

17 “(B) SPECIFIED SUBMISSION.—The term
18 ‘specified submission’ means—

19 “(i) a request for a hearing under—

20 “(I) section 6320 (relating to no-
21 tice and opportunity for hearing upon
22 filing of notice of lien), or

23 “(II) section 6330 (relating to
24 notice and opportunity for hearing be-
25 fore levy), and

1 “(ii) an application under—

2 “(I) section 6159 (relating to
3 agreements for payment of tax liabil-
4 ity in installments),

5 “(II) section 7122 (relating to
6 compromises), or

7 “(III) section 7811 (relating to
8 taxpayer assistance orders).

9 “(3) OPPORTUNITY TO WITHDRAW SUBMIS-
10 SION.—If the Secretary provides a person with no-
11 tice that a submission is a specified frivolous sub-
12 mission and such person withdraws such submission
13 within 30 days after such notice, the penalty im-
14 posed under paragraph (1) shall not apply with re-
15 spect to such submission.

16 “(c) LISTING OF FRIVOLOUS POSITIONS.—The Sec-
17 retary shall prescribe (and periodically revise) a list of po-
18 sitions which the Secretary has identified as being frivo-
19 lous for purposes of this subsection. The Secretary shall
20 not include in such list any position that the Secretary
21 determines meets the requirement of section
22 6662(d)(2)(B)(ii)(II).

23 “(d) REDUCTION OF PENALTY.—The Secretary may
24 reduce the amount of any penalty imposed under this sec-
25 tion if the Secretary determines that such reduction would

1 promote compliance with and administration of the Fed-
 2 eral tax laws.

3 “(e) PENALTIES IN ADDITION TO OTHER PEN-
 4 ALTIES.—The penalties imposed by this section shall be
 5 in addition to any other penalty provided by law.”

6 (b) TREATMENT OF FRIVOLOUS REQUESTS FOR
 7 HEARINGS BEFORE LEVY.—

8 (1) FRIVOLOUS REQUESTS DISREGARDED.—

9 Section 6330 (relating to notice and opportunity for
 10 hearing before levy) is amended by adding at the
 11 end the following new subsection:

12 “(g) FRIVOLOUS REQUESTS FOR HEARING, ETC.—
 13 Notwithstanding any other provision of this section, if the
 14 Secretary determines that any portion of a request for a
 15 hearing under this section or section 6320 meets the re-
 16 quirement of clause (i) or (ii) of section 6702(b)(2)(A),
 17 then the Secretary may treat such portion as if it were
 18 never submitted and such portion shall not be subject to
 19 any further administrative or judicial review.”

20 (2) PRECLUSION FROM RAISING FRIVOLOUS
 21 ISSUES AT HEARING.—Section 6330(c)(4) is amend-
 22 ed—

23 (A) by striking “(A)” and inserting
 24 “(A)(i)”;

25 (B) by striking “(B)” and inserting “(ii)”;

1 (C) by striking the period at the end of the
2 first sentence and inserting “; or”; and

3 (D) by inserting after subparagraph (A)(ii)
4 (as so redesignated) the following:

5 “(B) the issue meets the requirement of
6 clause (i) or (ii) of section 6702(b)(2)(A).”

7 (3) STATEMENT OF GROUNDS.—Section
8 6330(b)(1) is amended by striking “under sub-
9 section (a)(3)(B)” and inserting “in writing under
10 subsection (a)(3)(B) and states the grounds for the
11 requested hearing”.

12 (c) TREATMENT OF FRIVOLOUS REQUESTS FOR
13 HEARINGS UPON FILING OF NOTICE OF LIEN.—Section
14 6320 is amended—

15 (1) in subsection (b)(1), by striking “under sub-
16 section (a)(3)(B)” and inserting “in writing under
17 subsection (a)(3)(B) and states the grounds for the
18 requested hearing”, and

19 (2) in subsection (c), by striking “and (e)” and
20 inserting “(e), and (g)”.

21 (d) TREATMENT OF FRIVOLOUS APPLICATIONS FOR
22 OFFERS-IN-COMPROMISE AND INSTALLMENT AGREE-
23 MENTS.—Section 7122 is amended by adding at the end
24 the following new subsection:

1 “(e) FRIVOLOUS SUBMISSIONS, ETC.—Notwith-
 2 standing any other provision of this section, if the Sec-
 3 retary determines that any portion of an application for
 4 an offer-in-compromise or installment agreement sub-
 5 mitted under this section or section 6159 meets the re-
 6 quirement of clause (i) or (ii) of section 6702(b)(2)(A),
 7 then the Secretary may treat such portion as if it were
 8 never submitted and such portion shall not be subject to
 9 any further administrative or judicial review.”

10 (e) CLERICAL AMENDMENT.—The table of sections
 11 for part I of subchapter B of chapter 68 is amended by
 12 striking the item relating to section 6702 and inserting
 13 the following new item:

“Sec. 6702. Frivolous tax submissions.”

14 (f) EFFECTIVE DATE.—The amendments made by
 15 this section shall apply to submissions made and issues
 16 raised after the date on which the Secretary first pre-
 17 scribes a list under section 6702(c) of the Internal Rev-
 18 enue Code of 1986, as amended by subsection (a).

19 **SEC. 214. REGULATION OF INDIVIDUALS PRACTICING BE-**
 20 **FORE THE DEPARTMENT OF TREASURY.**

21 (a) CENSURE; IMPOSITION OF PENALTY.—

22 (1) IN GENERAL.—Section 330(b) of title 31,
 23 United States Code, is amended—

24 (A) by inserting “, or censure,” after “De-
 25 partment”, and

1 (B) by adding at the end the following new
2 flush sentence:

3 “The Secretary may impose a monetary penalty on any
4 representative described in the preceding sentence. If the
5 representative was acting on behalf of an employer or any
6 firm or other entity in connection with the conduct giving
7 rise to such penalty, the Secretary may impose a monetary
8 penalty on such employer, firm, or entity if it knew, or
9 reasonably should have known, of such conduct. Such pen-
10 alty shall not exceed the gross income derived (or to be
11 derived) from the conduct giving rise to the penalty and
12 may be in addition to, or in lieu of, any suspension, disbar-
13 ment, or censure.”

14 (2) EFFECTIVE DATE.—The amendments made
15 by this subsection shall apply to actions taken after
16 the date of the enactment of this Act.

17 (b) TAX SHELTER OPINIONS, ETC.—Section 330 of
18 such title 31 is amended by adding at the end the fol-
19 lowing new subsection:

20 “(d) Nothing in this section or in any other provision
21 of law shall be construed to limit the authority of the Sec-
22 retary of the Treasury to impose standards applicable to
23 the rendering of written advice with respect to any entity,
24 transaction plan or arrangement, or other plan or arrange-

1 ment, which is of a type which the Secretary determines
 2 as having a potential for tax avoidance or evasion.”

3 **SEC. 215. PENALTY ON PROMOTERS OF TAX SHELTERS.**

4 (a) PENALTY ON PROMOTING ABUSIVE TAX SHEL-
 5 TERS.—Section 6700(a) is amended by adding at the end
 6 the following new sentence: “Notwithstanding the first
 7 sentence, if an activity with respect to which a penalty
 8 imposed under this subsection involves a statement de-
 9 scribed in paragraph (2)(A), the amount of the penalty
 10 shall be equal to 50 percent of the gross income derived
 11 (or to be derived) from such activity by the person on
 12 which the penalty is imposed.”

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

16 **SEC. 216. STATUTE OF LIMITATIONS FOR TAXABLE YEARS**
 17 **FOR WHICH LISTED TRANSACTIONS NOT RE-**
 18 **PORTED.**

19 (a) IN GENERAL.—Section 6501(e)(1) (relating to
 20 substantial omission of items for income taxes) is amended
 21 by adding at the end the following new subparagraph:

22 “(C) LISTED TRANSACTIONS.—If a tax-
 23 payer fails to include on any return or state-
 24 ment for any taxable year any information with
 25 respect to a listed transaction (as defined in

1 section 6707A(c)(2)) which is required under
 2 section 6011 to be included with such return or
 3 statement, the tax for such taxable year may be
 4 assessed, or a proceeding in court for collection
 5 of such tax may be begun without assessment,
 6 at any time within 6 years after the time the
 7 return is filed. This subparagraph shall not
 8 apply to any taxable year if the time for assess-
 9 ment or beginning the proceeding in court has
 10 expired before the time a transaction is treated
 11 as a listed transaction under section 6011.”

12 (b) EFFECTIVE DATE.—The amendment made by
 13 this section shall apply to transactions after the date of
 14 the enactment of this Act in taxable years ending after
 15 such date.

16 **SEC. 217. DENIAL OF DEDUCTION FOR INTEREST ON UN-**
 17 **DERPAYMENTS ATTRIBUTABLE TO NONDIS-**
 18 **CLOSED REPORTABLE AND NONECONOMIC**
 19 **SUBSTANCE TRANSACTIONS.**

20 (a) IN GENERAL.—Section 163 (relating to deduction
 21 for interest) is amended by redesignating subsection (m)
 22 as subsection (n) and by inserting after subsection (l) the
 23 following new subsection:

24 “(m) INTEREST ON UNPAID TAXES ATTRIBUTABLE
 25 TO NONDISCLOSED REPORTABLE TRANSACTIONS AND

1 NONECONOMIC SUBSTANCE TRANSACTIONS.—No deduc-
 2 tion shall be allowed under this chapter for any interest
 3 paid or accrued under section 6601 on any underpayment
 4 of tax which is attributable to—

5 “(1) the portion of any reportable transaction
 6 understatement (as defined in section 6662A(b))
 7 with respect to which the requirement of section
 8 6664(d)(2)(A) is not met, or

9 “(2) any noneconomic substance transaction
 10 understatement (as defined in section 6662B(c)).”

11 (b) EFFECTIVE DATE.—The amendments made by
 12 this section shall apply to transactions after the date of
 13 the enactment of this Act in taxable years ending after
 14 such date.

15 **Subtitle B—Other Provisions**

16 **SEC. 221. LIMITATION ON TRANSFER OR IMPORTATION OF** 17 **BUILT-IN LOSSES.**

18 (a) IN GENERAL.—Section 362 (relating to basis to
 19 corporations) is amended by adding at the end the fol-
 20 lowing new subsection:

21 “(e) LIMITATIONS ON BUILT-IN LOSSES.—

22 “(1) LIMITATION ON IMPORTATION OF BUILT-
 23 IN LOSSES.—

24 “(A) IN GENERAL.—If in any transaction
 25 described in subsection (a) or (b) there would

(but for this subsection) be an importation of a net built-in loss, the basis of each property described in subparagraph (B) which is acquired in such transaction shall (notwithstanding subsections (a) and (b)) be its fair market value immediately after such transaction.

“(B) PROPERTY DESCRIBED.—For purposes of subparagraph (A), property is described in this paragraph if—

“(i) gain or loss with respect to such property is not subject to tax under this subtitle in the hands of the transferor immediately before the transfer, and

“(ii) gain or loss with respect to such property is subject to such tax in the hands of the transferee immediately after such transfer.

In any case in which the transferor is a partnership, the preceding sentence shall be applied by treating each partner in such partnership as holding such partner’s proportionate share of the property of such partnership.

“(C) IMPORTATION OF NET BUILT-IN LOSS.—For purposes of subparagraph (A), there is an importation of a net built-in loss in

a transaction if the transferee's aggregate adjusted bases of property described in subparagraph (B) which is transferred in such transaction would (but for this paragraph) exceed the fair market value of such property immediately after such transaction.

“(2) LIMITATION ON TRANSFER OF BUILT-IN LOSSES IN SECTION 351 TRANSACTIONS.—

“(A) IN GENERAL.—If—

“(i) property is transferred in any transaction which is described in subsection (a) and which is not described in paragraph (1) of this subsection, and

“(ii) the transferee's aggregate adjusted bases of the property so transferred would (but for this paragraph) exceed the fair market value of such property immediately after such transaction,

then, notwithstanding subsection (a), the transferee's aggregate adjusted bases of the property so transferred shall not exceed the fair market value of such property immediately after such transaction.

“(B) ALLOCATION OF BASIS REDUCTION.—The aggregate reduction in basis by

1 reason of subparagraph (A) shall be allocated
 2 among the property so transferred in proportion
 3 to their respective built-in losses immediately
 4 before the transaction.

5 “(C) EXCEPTION FOR TRANSFERS WITHIN
 6 AFFILIATED GROUP.—Subparagraph (A) shall
 7 not apply to any transaction if the transferor
 8 owns stock in the transferee meeting the re-
 9 quirements of section 1504(a)(2). In the case of
 10 property to which subparagraph (A) does not
 11 apply by reason of the preceding sentence, the
 12 transferor’s basis in the stock received for such
 13 property shall not exceed its fair market value
 14 immediately after the transfer.”

15 (b) COMPARABLE TREATMENT WHERE LIQUIDA-
 16 TION.—Paragraph (1) of section 334(b) (relating to liq-
 17 uidation of subsidiary) is amended to read as follows:

18 “(1) IN GENERAL.—If property is received by a
 19 corporate distributee in a distribution in a complete
 20 liquidation to which section 332 applies (or in a
 21 transfer described in section 337(b)(1)), the basis of
 22 such property in the hands of such distributee shall
 23 be the same as it would be in the hands of the trans-
 24 feror; except that the basis of such property in the
 25 hands of such distributee shall be the fair market

1 value of the property at the time of the distribu-
 2 tion—

3 “(A) in any case in which gain or loss is
 4 recognized by the liquidating corporation with
 5 respect to such property, or

6 “(B) in any case in which the liquidating
 7 corporation is a foreign corporation, the cor-
 8 porate distributee is a domestic corporation,
 9 and the corporate distributee’s aggregate ad-
 10 justed bases of property described in section
 11 362(e)(1)(B) which is distributed in such liq-
 12 uidation would (but for this subparagraph) ex-
 13 ceed the fair market value of such property im-
 14 mediately after such liquidation.”

15 (c) EFFECTIVE DATE.—The amendments made by
 16 this section shall apply to transactions after the date of
 17 the enactment of this Act.

18 **SEC. 222. DISALLOWANCE OF CERTAIN PARTNERSHIP LOSS**
 19 **TRANSFERS.**

20 (a) TREATMENT OF CONTRIBUTED PROPERTY WITH
 21 BUILT-IN LOSS.—Paragraph (1) of section 704(c) is
 22 amended by striking “and” at the end of subparagraph
 23 (A), by striking the period at the end of subparagraph
 24 (B) and inserting “, and”, and by adding at the end the
 25 following:

1 “(C) if any property so contributed has a
2 built-in loss—

3 “(i) such built-in loss shall be taken
4 into account only in determining the
5 amount of items allocated to the contrib-
6 uting partner, and

7 “(ii) except as provided in regulations,
8 in determining the amount of items allo-
9 cated to other partners, the basis of the
10 contributed property in the hands of the
11 partnership shall be treated as being equal
12 to its fair market value immediately after
13 the contribution.

14 For purposes of subparagraph (C), the term ‘built-
15 in loss’ means the excess of the adjusted basis of the
16 property (determined without regard to subpara-
17 graph (C)(ii)) over its fair market value immediately
18 after the contribution.”

19 (b) ADJUSTMENT TO BASIS OF PARTNERSHIP PROP-
20 erty ON TRANSFER OF PARTNERSHIP INTEREST IF
21 THERE IS SUBSTANTIAL BUILT-IN LOSS.—

22 (1) ADJUSTMENT REQUIRED.—Subsection (a)
23 of section 743 (relating to optional adjustment to
24 basis of partnership property) is amended by insert-
25 ing before the period “or unless the partnership has

1 a substantial built-in loss immediately after such
2 transfer”.

3 (2) ADJUSTMENT.—Subsection (b) of section
4 743 is amended by inserting “or with respect to
5 which there is a substantial built-in loss immediately
6 after such transfer” after “section 754 is in effect”.

7 (3) SUBSTANTIAL BUILT-IN LOSS.—Section 743
8 is amended by adding at the end the following new
9 subsection:

10 “(d) SUBSTANTIAL BUILT-IN LOSS.—

11 “(1) IN GENERAL.—For purposes of this sec-
12 tion, a partnership has a substantial built-in loss
13 with respect to a transfer of an interest in a part-
14 nership if the transferee partner’s proportionate
15 share of the adjusted basis of the partnership prop-
16 erty exceeds by more than \$250,000 the basis of
17 such partner’s interest in the partnership.

18 “(2) REGULATIONS.—The Secretary shall pre-
19 scribe such regulations as may be appropriate to
20 carry out the purposes of paragraph (1) and section
21 734(d), including regulations aggregating related
22 partnerships and disregarding property acquired by
23 the partnership in an attempt to avoid such pur-
24 poses.”

25 (4) CLERICAL AMENDMENTS.—

1 (A) The section heading for section 743 is
 2 amended to read as follows:

3 **“SEC. 743. ADJUSTMENT TO BASIS OF PARTNERSHIP PROP-**
 4 **ERTY WHERE SECTION 754 ELECTION OR**
 5 **SUBSTANTIAL BUILT-IN LOSS.”**

6 (B) The table of sections for subpart C of
 7 part II of subchapter K of chapter 1 is amend-
 8 ed by striking the item relating to section 743
 9 and inserting the following new item:

“Sec. 743. Adjustment to basis of partnership property where sec-
 tion 754 election or substantial built-in loss.”

10 (c) **ADJUSTMENT TO BASIS OF UNDISTRIBUTED**
 11 **PARTNERSHIP PROPERTY IF THERE IS SUBSTANTIAL**
 12 **BASIS REDUCTION.—**

13 (1) **ADJUSTMENT REQUIRED.—**Subsection (a)
 14 of section 734 (relating to optional adjustment to
 15 basis of undistributed partnership property) is
 16 amended by inserting before the period “or unless
 17 there is a substantial basis reduction”.

18 (2) **ADJUSTMENT.—**Subsection (b) of section
 19 734 is amended by inserting “or unless there is a
 20 substantial basis reduction” after “section 754 is in
 21 effect”.

22 (3) **SUBSTANTIAL BASIS REDUCTION.—**Section
 23 734 is amended by adding at the end the following
 24 new subsection:

1 “(d) SUBSTANTIAL BASIS REDUCTION.—

2 “(1) IN GENERAL.—For purposes of this sec-
 3 tion, there is a substantial basis reduction with re-
 4 spect to a distribution if the sum of the amounts de-
 5 scribed in subparagraphs (A) and (B) of subsection
 6 (b)(2) exceeds \$250,000.

7 “(2) REGULATIONS.—

“For regulations to carry out this subsection, see
 section 743(d)(2).”

8 (4) CLERICAL AMENDMENTS.—

9 (A) The section heading for section 734 is
 10 amended to read as follows:

11 **“SEC. 734. ADJUSTMENT TO BASIS OF UNDISTRIBUTED**
 12 **PARTNERSHIP PROPERTY WHERE SECTION**
 13 **754 ELECTION OR SUBSTANTIAL BASIS RE-**
 14 **DUCTION.”**

15 (B) The table of sections for subpart B of
 16 part II of subchapter K of chapter 1 is amend-
 17 ed by striking the item relating to section 734
 18 and inserting the following new item:

“Sec. 734. Adjustment to basis of undistributed partnership prop-
 erty where section 754 election or substantial basis
 reduction.”

19 (d) EFFECTIVE DATES.—

20 (1) SUBSECTION (a).—The amendment made
 21 by subsection (a) shall apply to contributions made
 22 after the date of the enactment of this Act.

1 (2) SUBSECTION (b).—The amendments made
2 by subsection (b) shall apply to transfers after the
3 date of the enactment of this Act.

4 (3) SUBSECTION (c).—The amendments made
5 by subsection (c) shall apply to distributions after
6 the date of the enactment of this Act.

7 **SEC. 223. NO REDUCTION OF BASIS UNDER SECTION 734 IN**
8 **STOCK HELD BY PARTNERSHIP IN COR-**
9 **PORATE PARTNER.**

10 (a) IN GENERAL.—Section 755 is amended by adding
11 at the end the following new subsection:

12 “(c) NO ALLOCATION OF BASIS DECREASE TO
13 STOCK OF CORPORATE PARTNER.—In making an alloca-
14 tion under subsection (a) of any decrease in the adjusted
15 basis of partnership property under section 734(b)—

16 “(1) no allocation may be made to stock in a
17 corporation which is a partner in the partnership,
18 and

19 “(2) any amount not allocable to stock by rea-
20 son of paragraph (1) shall be allocated under sub-
21 section (a) to other partnership property.

22 Gain shall be recognized to the partnership to the extent
23 that the amount required to be allocated under paragraph
24 (2) to other partnership property exceeds the aggregate

1 adjusted basis of such other property immediately before
2 the allocation required by paragraph (2).”

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

6 **SEC. 224. REPEAL OF SPECIAL RULES FOR FASITS.**

7 (a) IN GENERAL.—Part V of subchapter M of chap-
8 ter 1 (relating to financial asset securitization investment
9 trusts) is hereby repealed.

10 (b) CONFORMING AMENDMENTS.—

11 (1) Paragraph (6) of section 56(g) is amended
12 by striking “REMIC, or FASIT” and inserting “or
13 REMIC”.

14 (2) Clause (ii) of section 382(l)(4)(B) is amend-
15 ed by striking “a REMIC to which part IV of sub-
16 chapter M applies, or a FASIT to which part V of
17 subchapter M applies,” and inserting “or a REMIC
18 to which part IV of subchapter M applies,”.

19 (3) Paragraph (1) of section 582(c) is amended
20 by striking “, and any regular interest in a
21 FASIT,”.

22 (4) Subparagraph (E) of section 856(c)(5) is
23 amended by striking the last sentence.

24 (5) Paragraph (5) of section 860G(a) is amend-
25 ed by adding “and” at the end of subparagraph (B),

1 by striking “, and” at the end of subparagraph (C)
 2 and inserting a period, and by striking subparagraph
 3 (D).

4 (6) Subparagraph (C) of section 1202(e)(4) is
 5 amended by striking “REMIC, or FASIT” and in-
 6 serting “or REMIC”.

7 (7) Subparagraph (C) of section 7701(a)(19) is
 8 amended by adding “and” at the end of clause (ix),
 9 by striking “, and” at the end of clause (x) and in-
 10 serting a period, and by striking clause (xi).

11 (8) The table of parts for subchapter M of
 12 chapter 1 is amended by striking the item relating
 13 to part V.

14 (c) EFFECTIVE DATE.—

15 (1) IN GENERAL.—Except as provided in para-
 16 graph (2), the amendments made by this section
 17 shall apply to taxable years beginning after Decem-
 18 ber 31, 2003.

19 (2) EXCEPTION FOR EXISTING FASITS.—

20 (A) IN GENERAL.—Paragraph (1) shall not
 21 apply to any FASIT in existence on the date of
 22 the enactment of this Act.

23 (B) TRANSFER OF ADDITIONAL ASSETS
 24 NOT PERMITTED.—Except as provided in regu-
 25 lations prescribed by the Secretary of the

1 Treasury or the Secretary's delegate, subpara-
2 graph (A) shall cease to apply as of the earliest
3 date after the date of the enactment of this Act
4 that any property is transferred to the FASIT.

5 **SEC. 225. EXPANDED DISALLOWANCE OF DEDUCTION FOR**
6 **INTEREST ON CONVERTIBLE DEBT.**

7 (a) IN GENERAL.—Paragraph (2) of section 163(l)
8 is amended by striking “or a related party” and inserting
9 “or equity held by the issuer (or any related party) in any
10 other person”.

11 (b) CONFORMING AMENDMENT.—Paragraph (3) of
12 section 163(l) is amended by striking “or a related party”
13 in the material preceding subparagraph (A) and inserting
14 “or any other person”.

15 (c) EFFECTIVE DATE.—The amendments made by
16 this section shall apply to debt instruments issued after
17 the date of the enactment of this Act.

18 **SEC. 226. EXPANDED AUTHORITY TO DISALLOW TAX BENE-**
19 **FITS UNDER SECTION 269.**

20 (a) IN GENERAL.—Subsection (a) of section 269 (re-
21 lating to acquisitions made to evade or avoid income tax)
22 is amended to read as follows:

23 “(a) IN GENERAL.—If—

24 “(1)(A) any person acquires stock in a corpora-
25 tion, or

1 “(B) any corporation acquires, directly or indi-
 2 rectly, property of another corporation and the basis
 3 of such property, in the hands of the acquiring cor-
 4 poration, is determined by reference to the basis in
 5 the hands of the transferor corporation, and

6 “(2) the principal purpose for which such acqui-
 7 sition was made is evasion or avoidance of Federal
 8 income tax by securing the benefit of a deduction,
 9 credit, or other allowance,
 10 then the Secretary may disallow such deduction, credit,
 11 or other allowance.”

12 (b) EFFECTIVE DATE.—The amendment made by
 13 this section shall apply to stock and property acquired
 14 after December 31, 2003.

15 **SEC. 227. MODIFICATIONS OF CERTAIN RULES RELATING**
 16 **TO CONTROLLED FOREIGN CORPORATIONS.**

17 (a) LIMITATION ON EXCEPTION FROM PFIC RULES
 18 FOR UNITED STATES SHAREHOLDERS OF CONTROLLED
 19 FOREIGN CORPORATIONS.—Paragraph (2) of section
 20 1297(e) (relating to passive investment company) is
 21 amended by adding at the end the following flush sen-
 22 tence:

23 “Such term shall not include any period if there is
 24 only a remote likelihood of an inclusion in gross in-

1 come under section 951(a)(1)(A)(i) of subpart F in-
 2 come of such corporation for such period.”

3 (b) DETERMINATION OF PRO RATA SHARE OF SUB-
 4 PART F INCOME.—Subsection (a) of section 951 (relating
 5 to amounts included in gross income of United States
 6 shareholders) is amended by adding at the end the fol-
 7 lowing new paragraph:

8 “(4) SPECIAL RULES FOR DETERMINING PRO
 9 RATA SHARE OF SUBPART F INCOME.—The pro rata
 10 share under paragraph (2) shall be determined by
 11 disregarding—

12 “(A) any rights lacking substantial eco-
 13 nomic effect, and

14 “(B) stock owned by a shareholder who is
 15 a tax-indifferent party (as defined in section
 16 7701(m)(3)) if the amount which would (but
 17 for this paragraph) be allocated to such share-
 18 holder does not reflect such shareholder’s eco-
 19 nomic share of the earnings and profits of the
 20 corporation.”

21 (c) EFFECTIVE DATE.—The amendments made by
 22 this section shall apply to taxable years on controlled for-
 23 eign corporation beginning after December 31, 2003, and
 24 to taxable years of United States shareholder in which or

1 with which such taxable years of controlled foreign cor-
2 porations end.

3 **SEC. 228. BASIS FOR DETERMINING LOSS ALWAYS RE-**
4 **DUCED BY NONTAXED PORTION OF DIVI-**
5 **DENDS.**

6 (a) IN GENERAL.—Section 1059 (relating to cor-
7 porate shareholder’s basis in stock reduced by nontaxed
8 portion of extraordinary dividends) is amended by redesign-
9 nating subsection (g) as subsection (h) and by inserting
10 after subsection (f) the following new subsection:

11 “(g) BASIS FOR DETERMINING LOSS ALWAYS RE-
12 DUCED BY NONTAXED PORTION OF DIVIDENDS.—The
13 basis of stock in a corporation (for purposes of deter-
14 mining loss) shall be reduced by the nontaxed portion of
15 any dividend received with respect to such stock if this
16 section does not otherwise apply to such dividend.”

17 (b) EFFECTIVE DATE.—The amendment made by
18 this section shall apply to dividends received after the date
19 of the enactment of this Act.

20 **SEC. 229. AFFIRMATION OF CONSOLIDATED RETURN REGU-**
21 **LATION AUTHORITY.**

22 (a) IN GENERAL.—Section 1502 (relating to consoli-
23 dated return regulations) is amended by adding at the end
24 the following new sentence: “In prescribing such regula-
25 tions, the Secretary may prescribe rules applicable to cor-

1 porations filing consolidated returns under section 1501
 2 that are different from other provisions of this title that
 3 would apply if such corporations filed separate returns.”

4 (b) RESULT NOT OVERTURNED.—Notwithstanding
 5 subsection (a), the Internal Revenue Code of 1986 shall
 6 be construed by treating Treasury regulation § 1.1502–
 7 20(c)(1)(iii) (as in effect on January 1, 2001) as being
 8 inapplicable to the type of factual situation in 255 F.3d
 9 1357 (Fed. Cir. 2001).

10 (c) EFFECTIVE DATE.—The provisions of this section
 11 shall apply to taxable years beginning before, on, or after
 12 the date of the enactment of this Act.

13 **TITLE III—OTHER REVENUE** 14 **OFFSETS**

15 **SEC. 301. MODIFICATION OF INDIVIDUAL INCOME TAX** 16 **BRACKETS AND RATES.**

17 (a) IN GENERAL.—So much of section 1 as precedes
 18 subsection (f) is amended to read as follows:

19 **“SECTION 1. TAX IMPOSED.**

20 **“(a) MARRIED INDIVIDUALS FILING JOINT RETURNS**
 21 **AND SURVIVING SPOUSES.—**There is hereby imposed on
 22 the taxable income of—

23 **“(1)** every married individual (as defined in sec-
 24 **tion 7703)** who makes a single return jointly with
 25 **his spouse under section 6013, and**

1 “(2) every surviving spouse (as defined in sec-
 2 tion 2(a)), a tax determined in accordance with the
 3 following table:

If taxable income is:	The tax is:
Not over \$12,000	10% of taxable income
Over \$12,000 but not over \$47,450.	\$1,200, plus 15% of the excess over \$12,000
Over \$47,450 but not over \$114,650.	\$6,517.50, plus 25% of the excess over \$47,450
Over \$114,650 but not over \$122,080.	\$23,317.50, plus 28% of the excess over \$114,650
Over \$122,080 but not over \$311,950.	\$25,397.90, plus 36% of the excess over \$122,080
Over \$311,950	\$93,751.10, plus 39.6% of the excess over \$311,950

4 “(b) HEADS OF HOUSEHOLDS.—There is hereby im-
 5 posed on the taxable income of every head of a household
 6 (as defined in section 2(b)) a tax determined in accordance
 7 with the following table:

If taxable income is:	The tax is:
Not over \$10,00	10% of taxable income
Over \$10,000 but not over \$38,050.	\$1,000, plus 15% of the excess over \$10,000
Over \$38,050 but not over \$98,250.	\$5,207.50, plus 25% of the excess over \$38,050
Over \$98,250 but not over \$111,370.	\$20,257.50, plus 28% of the excess over \$98,250
Over \$111,370 but not over \$311,950.	\$23,931.10, plus 36% of the excess over \$111,370
Over \$311,950	\$96,139.90, plus 39.6% of the excess over \$311,950

8 “(c) UNMARRIED INDIVIDUALS FILING (OTHER
 9 THAN SURVIVING SPOUSES AND HEADS OF HOUSE-
 10 HOLDS).—There is hereby imposed on the taxable income
 11 of every individual (other than a surviving spouse as de-
 12 fined in section 2(a) or the head of a household as defined
 13 in section 2(b)) who is not a married individual (as defined

1 in section 7703) a tax determined in accordance with the
 2 following table:

If taxable income is:	The tax is:
Not over \$6,000	10% of taxable income
Over \$6,000 but not over \$28,400	\$600, plus 15% of the excess over \$6,000
Over \$28,400 but not over \$68,800.	\$3,960, plus 25% of the excess over \$28,400
Over \$68,800 but not over \$100,450.	\$14,060, plus 28% of the excess over \$68,800
Over \$100,450 but not over \$311,950.	\$22,922, plus 36% of the excess over \$100,450
Over \$311,950	\$99,062, plus 39.6% of the excess over \$311,950

3 “(d) MARRIED INDIVIDUALS FILING SEPARATE RE-
 4 TURNS.—There is hereby imposed on the taxable income
 5 of every married individual (as defined in section 7703)
 6 who does not make a single return jointly with his spouse
 7 under section 6013, a tax determined in accordance with
 8 the following table:

If taxable income is:	The tax is:
Not over \$6,000	10% of taxable income
Over \$6,000 but not over \$23,725	\$600, plus 15% of the excess over \$6,000
Over \$23,725 but not over \$57,325.	\$3,258.75, plus 25% of the excess over \$23,725
Over \$57,325 but not over \$61,040.	\$11,658.75, plus 28% of the excess over \$57,325
Over \$61,040 but not over \$155,975.	\$12,698.95, plus 36% of the excess over \$61,040
Over \$155,975	\$46,875.55, plus 39.6% of the excess over \$155,975

9 “(e) ESTATES AND TRUSTS.—There is hereby im-
 10 posed on the taxable income of—
 11 “(1) every estate, and
 12 “(2) every trust,
 13 taxable under this subsection a tax determined in accord-
 14 ance with the following table:

If taxable income is:

Not over \$1,900

Over \$1,900 but not over \$4,500 ..

Over \$4,500 but not over \$6,850 ..

Over \$6,850 but not over \$9,350 ..

Over \$9,350

The tax is:

15% of taxable income

\$285, plus 25% of the excess over \$4,500

\$935, plus 28% of the excess over \$6,850

\$1,593, plus 36% of the excess over \$6,850

\$2,493, plus 39.6% of the excess over \$9,350.”

1 (b) CONFORMING AMENDMENTS.—

2 (1) Section 1(f)(3)(B) is amended—

3 (A) by striking “For purposes” and insert-
 4 ing “In the case of calendar years beginning
 5 after 2003, for purposes”,

6 (B) in subparagraph (B) by striking
 7 “1992” and inserting “2002”, and

8 (C) by adding at the end the following
 9 flush sentence: “In the case of a reference to
 10 the preceding provisions of this paragraph by
 11 any other provision of law, subparagraph (B)
 12 shall be applied by substituting ‘1992’ for
 13 ‘2002’.”.

14 (2) Section 1(f) is amended by striking para-
 15 graph (7).

16 (3) Section 1(i)(1)(C)(iii) is amended by strik-
 17 ing “1992” and inserting “2002”.

18 (4) Section 1(i) is amended by striking para-
 19 graph (2).

1 (c) EFFECTIVE DATE.—The amendments made by
 2 this section shall apply to years beginning after December
 3 31, 2003.

4 **SEC. 302. REPEAL OF REMOVAL OF LIMITATIONS ON**
 5 **ITEMIZED DEDUCTIONS AND EXEMPTION**
 6 **AMOUNT.**

7 (a) ITEMIZED DEDUCTIONS.—Section 68 of the In-
 8 ternal Revenue Code of 1986 (relating to overall limitation
 9 on itemized deductions) is amended by striking sub-
 10 sections (f) and (g).

11 (b) EXEMPTION AMOUNT.—Paragraph (3) of section
 12 151(d) (relating to phaseout) is amended by striking sub-
 13 paragraphs (E) and (F).

14 **SEC. 303. INDIVIDUAL CAPITAL GAINS AND DIVIDENDS**
 15 **TREATED AS ORDINARY INCOME.**

16 (a) IN GENERAL.—Section 1 of the Internal Revenue
 17 Code of 1986 (relating to tax imposed) is amended by
 18 striking subsection (h).

19 (b) ALTERNATIVE MINIMUM TAX.—Section 55(b)
 20 (relating to tentative minimum tax) is amended by strik-
 21 ing paragraph (3).

22 (c) CONFORMING AMENDMENTS.—

23 (1) Section 57(a)(7) is amended by striking
 24 “(determined with the application of the last sen-
 25 tence of section 1(h)(2)(B))”.

1 (2) Section 453A(c)(3) is amended by striking
2 “section 1(h) or 1201 (whichever is appropriate)”
3 and inserting “section 1201”.

4 (3) Section 641(c)(2)(A) is amended by striking
5 “Except as provided in section 1(h), the” and insert-
6 ing “The”.

7 (4) Section 904(b)(2)(C) is amended by striking
8 “1(h) or”.

9 (5) Section 904(b)(3)(D) is amended by strik-
10 ing “if—” and all that follows and inserting “if, in
11 the case of a corporation, any rate of tax imposed
12 by section 11, 511, or 831(a) or (b) (whichever ap-
13 plies) exceeds the alternative rate of tax under sec-
14 tion 1201(a) (determined without regard to the last
15 sentence of section 11(b)(1)).”.

16 (6) Section 904(b)(3)(E)(iii) is amended by
17 striking “means—” and all that follows and insert-
18 ing “means, in the case of a corporation, the alter-
19 native rate of tax under section 1201(a).”.

20 (7) Section 1260(a) is amended by striking
21 “gain—” and all that follows and inserting “gain,
22 such gain shall be treated as ordinary income to the
23 extent that such gain exceeds the net underlying
24 long-term capital gain.”.

1 (8) Section 7518 is amended by striking “1(h)
2 or”.

3 (d) EFFECTIVE DATE.—The amendments made by
4 this section shall apply to taxable years beginning after
5 December 31, 2003.

6 **SEC. 304. RESTORATION AND MODIFICATIONS OF ESTATE**
7 **TAX; REPEAL OF CARRYOVER BASIS.**

8 (a) RESTORATION.—

9 (1) IN GENERAL.—Subtitles A and E of title V
10 of the Economic Growth and Tax Relief Reconcili-
11 ation Act of 2001, and the amendments made by
12 such subtitles, are hereby repealed; and the Internal
13 Revenue Code of 1986 shall be applied as if such
14 subtitles, and amendments, had never been enacted.

15 (2) SUNSET NOT TO APPLY.—

16 (A) Subsection (a) of section 901 of the
17 Economic Growth and Tax Relief Reconciliation
18 Act of 2001 is amended by striking “this Act”
19 and all that follows and inserting “this Act
20 (other than title V) shall not apply to taxable,
21 plan, or limitation years beginning after Decem-
22 ber 31, 2010.”.

23 (B) Subsection (b) of such section 901 is
24 amended by striking “, estates, gifts, and trans-
25 fers”.

1 (3) CONFORMING AMENDMENTS.—Subsections
 2 (d) and (e) of section 511 of the Economic Growth
 3 and Tax Relief Reconciliation Act of 2001, and the
 4 amendments made by such subsections, are hereby
 5 repealed; and the Internal Revenue Code of 1986
 6 shall be applied as if such subsections, and amend-
 7 ments, had never been enacted.

8 (b) MODIFICATIONS TO ESTATE TAX.—

9 (1) INCREASE IN EXCLUSION EQUIVALENT OF
 10 UNIFIED CREDIT TO \$2,000,000.—Subsection (c) of
 11 section 2010 of the Internal Revenue Code of 1986
 12 (relating to applicable credit amount) is amended by
 13 striking all that follows “the applicable exclusion
 14 amount” and inserting “. For purposes of the pre-
 15 ceding sentence, the applicable exclusion amount is
 16 \$2,000,000.”.

17 (2) RESTORATION OF RATE SCHEDULE.—The
 18 table in section 2001(c) is amended by striking the
 19 last item and inserting the following:

“Over \$2,500,000 but not over	\$1,025,800, plus 53% of the excess
\$3,000,000.	over \$2,500,000
Over \$3,000,000	\$1,290,800, plus 55% of the excess
	over \$3,000,000”.

20 (3) RESTORATION OF PHASEOUT OF GRAD-
 21 UATED RATES AND UNIFIED CREDIT.—Paragraph
 22 (2) of section 2001(c) is amended to read as follows:

1 “(2) PHASEOUT OF GRADUATED RATES AND
 2 UNIFIED CREDIT.—The tentative tax determined
 3 under paragraph (1) shall be increased by an
 4 amount equal to 5 percent of so much of the amount
 5 (with respect to which the tentative tax is to be com-
 6 puted) as exceeds \$10,000,000 but does not exceed
 7 the amount at which the average tax rate under this
 8 section is 55 percent.”.

9 (c) INCREASE IN DEDUCTION FOR FAMILY-OWNED
 10 BUSINESS INTERESTS.—

11 (1) IN GENERAL.—Paragraph (2) of section
 12 2057(a) is amended by striking “\$675,000” and in-
 13 serting “\$2,000,000”.

14 (2) REPEAL OF COORDINATION WITH UNIFIED
 15 CREDIT.—Section 2057(a) is amended by striking
 16 paragraph (3).

17 (3) REPEAL OF TERMINATION.—Section 2057
 18 is amended by striking subsection (j).

19 (d) EFFECTIVE DATE.—The amendments made by
 20 this section shall apply to estates of decedents dying, and
 21 gifts made, after December 31, 2003.

22 **SEC. 305. EXTENSION OF SUPERFUND, OIL SPILL LIABILITY,**
 23 **AND LEAKING UNDERGROUND STORAGE**
 24 **TANK TAXES.**

25 (a) EXCISE TAXES.—

1 (1) SUPERFUND TAXES.—Section 4611(e) of
 2 the Internal Revenue Code of 1986 is amended to
 3 read as follows:

4 “(e) APPLICATION OF HAZARDOUS SUBSTANCE
 5 SUPERFUND FINANCING RATE.—The Hazardous Sub-
 6 stance Superfund financing rate under this section shall
 7 apply after December 31, 1986, and before January 1,
 8 1996, and after the date of the enactment of this sentence
 9 and before October 1, 2013.”.

10 (2) OIL SPILL LIABILITY TAX.—Section 4611(f)
 11 is amended to read as follows:

12 “(f) APPLICATION OF OIL SPILL LIABILITY TRUST
 13 FUND FINANCING RATE.—The Oil Spill Liability Trust
 14 Fund financing rate under subsection (c) shall apply after
 15 December 31, 1989, and before January 1, 1995, and
 16 after the date of the enactment of this sentence and before
 17 October 1, 2013.”.

18 (3) LEAKING UNDERGROUND STORAGE TANK
 19 RATE.—Section 4081(d)(3) is amended by striking
 20 “April 1, 2005” and inserting “October 1, 2013”.

21 (b) CORPORATE ENVIRONMENTAL INCOME TAX.—
 22 Section 59A(e) is amended to read as follows:

23 “(e) APPLICATION OF TAX.—The tax imposed by this
 24 section shall apply to taxable years beginning after De-
 25 cember 31, 1986, and before January 1, 1996, and to tax-

1 able years beginning after the date of the enactment of
2 this sentence and before January 1, 2013.”.

3 (c) TECHNICAL AMENDMENTS.—

4 (1) Section 4611(b) is amended—

5 (A) by striking “or exported from” in
6 paragraph (1)(A),

7 (B) by striking “or exportation” in para-
8 graph (1)(B), and

9 (C) by striking “AND EXPORTATION” in
10 the heading.

11 (2) Section 4611(d)(3) is amended—

12 (A) by striking “or exporting the crude oil,
13 as the case may be” in the text and inserting
14 “the crude oil”, and

15 (B) by striking “OR EXPORTS” in the
16 heading.

17 (d) EFFECTIVE DATES.—

18 (1) EXCISE TAXES.—The amendments made by
19 subsections (a) and (c) shall take effect on the date
20 of the enactment of this Act.

21 (2) INCOME TAX.—The amendment made by
22 subsection (b) shall apply to taxable years beginning
23 after the date of the enactment of this Act.

1 **SEC. 306. LIMITATION ON CERTAIN BUSINESS PROVISIONS**

2 **ENACTED IN 2002 AND 2003.**

3 (a) SPECIAL DEPRECIATION.—Section 168(k) is
4 amended by striking “January 1, 2005” each place it oc-
5 curs in the headings and text and inserting “January 1,
6 2004”.

7 (b) CARRYBACK OF CERTAIN NET OPERATING
8 LOSSES.—Section 172(H) is amended by inserting at the
9 end the following: “The preceding sentence shall not apply
10 after December 31, 2003.”.

11 (c) EXPENSING.—Section 179 is amended by striking
12 “2006” each place it occurs and inserting “2004”.

13 **SEC. 307. REPEAL OF EXCLUSION FOR PARKING TRANS-**
14 **PORTATION FRINGE BENEFIT.**

15 (a) IN GENERAL.—Section 132(f) is amended—

16 (1) in paragraph (1) by striking subparagraph
17 (C), and

18 (2) in paragraph (5) by striking subparagraph
19 (C) and redesignating subparagraphs (D) and (E) as
20 subparagraphs (C) and (D), respectively.

21 (b) EFFECTIVE DATE.—The amendments made by
22 this section shall apply to taxable years beginning after
23 December 31, 2003.

24 **SEC. 308. REPEAL OF CERTAIN DEDUCTIONS RELATING TO**
25 **SECOND HOMES.**

26 (a) INTEREST.—

1 (1) IN GENERAL.—Subparagraph (A) of section
2 163(h)(4) is amended to read as follows:

3 “(A) QUALIFIED RESIDENCE.—The term
4 ‘qualified residence’ means the principal resi-
5 dence (within the meaning of section 121) of
6 the taxpayer.”.

7 (2) EFFECTIVE DATE.—The amendment made
8 by paragraph (1) shall apply to interest paid or ac-
9 crued after December 31, 2003.

10 (b) PROPERTY TAXES.—

11 (1) IN GENERAL.—Section 164 is amended by
12 redesignating subsection (g) as subsection (h) and
13 by inserting after subsection (f) the following new
14 subsection:

15 “(g) NO DEDUCTION FOR MULTIPLE RESIDENCES.—

16 “(1) IN GENERAL.—No deduction shall be al-
17 lowed under this section for real property taxes paid
18 or accrued in connection with any property of the
19 taxpayer used as a residence of the taxpayer at any
20 time during the taxable year other than as the prin-
21 cipal residence (within the meaning of section 121)
22 of the taxpayer during such year.

23 “(2) PROPERTY USED AS PRINCIPAL RESI-
24 DENCE FOR PORTION OF YEAR.—In the case that
25 more than one property is used by the taxpayer as

1 a principal residence (as so defined) during the tax-
2 able year, the real property taxes allowed as a de-
3 duction under this section with respect to a property
4 shall not exceed the amount which bears the same
5 ratio to the total amount of real property taxes paid
6 or accrued for the taxable year with respect to such
7 property as the number of days in the taxable year
8 during which the taxpayer used such property as a
9 principal residence bears to 365.

10 “(3) SPECIAL RULES FOR MARRIED INDIVID-
11 UALS.—For purposes of this subsection—

12 “(A) MARRIED COUPLES MUST FILE JOINT
13 RETURN.—If the taxpayer is married at the
14 close of the taxable year, the deduction under
15 this section for real property taxes with respect
16 to the principal residence of the taxpayer shall
17 only be allowed if the taxpayer and his spouse
18 file a joint return for the taxable year.

19 “(B) MARITAL STATUS.—An individual le-
20 gally separated from his spouse under a decree
21 of divorce or of separate maintenance shall not
22 be considered as married.

23 “(C) CERTAIN MARRIED INDIVIDUALS LIV-
24 ING APART.—If—

1 “(i) an individual who is married and
2 who files a separate return—

3 “(I) maintains as his home a
4 household which constitutes for more
5 than one-half of the taxable year the
6 principal place of abode of a quali-
7 fying individual, and

8 “(II) furnishes over half of the
9 cost of maintaining such household
10 during the taxable year, and

11 “(ii) during the last 6 months of such
12 taxable year such individual’s spouse is not
13 a member of such household,
14 such individual shall not be considered as mar-
15 ried.”.

16 (2) EFFECTIVE DATE.—The amendment made
17 by this subsection shall apply to taxes paid or ac-
18 crued for periods beginning after December 31,
19 2003, in taxable years beginning after such date.

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