

108TH CONGRESS
1ST SESSION

S. 135

To amend the Internal Revenue Code of 1986 to expand the 10 percent tax bracket, to freeze the rate of the top tax brackets, to provide an immediate \$4,000,000 estate tax exemption and complete estate tax exclusion for family-owned businesses while eliminating the repeal of the estate tax, and for other purposes.

IN THE SENATE OF THE UNITED STATES

JANUARY 9, 2003

Mr. DAYTON introduced the following bill; which was read twice and referred to the Committee on Finance

A BILL

To amend the Internal Revenue Code of 1986 to expand the 10 percent tax bracket, to freeze the rate of the top tax brackets, to provide an immediate \$4,000,000 estate tax exemption and complete estate tax exclusion for family-owned businesses while eliminating the repeal of the estate tax, and for other purposes.

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

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Dayton Fair Tax Cut
5 Act”.

1 **SEC. 2. TABLE OF CONTENTS.**

2 (a) TABLE OF CONTENTS.—The table of contents of
 3 this Act is as follows:

Sec. 1. Short title.

Sec. 2. Table of contents.

TITLE I—10 PERCENT BRACKET

Sec. 101. Expansion of 10 percent bracket.

TITLE II—TAX RATES

Sec. 201. Repeal of income tax rate reductions for highest income taxpayers.

TITLE III—ESTATE TAX

Sec. 301. Estate tax with full tax deduction for family-owned business interests.

TITLE IV—TAX SHELTER TRANSACTIONS

Sec. 401. Findings and purpose.

Subtitle A—Clarification of Economic Substance Doctrine

Sec. 411. Clarification of economic substance doctrine.

Subtitle B—Penalties

Sec. 421. Increase in penalty on underpayments resulting from failure to satisfy certain common law rules.

Sec. 422. Penalty on promoters of tax avoidance strategies which have no economic substance, etc.

Sec. 423. Modifications of penalties for aiding and abetting understatement of tax liability involving tax shelters.

Sec. 424. Failure to maintain lists.

Sec. 425. Penalty for failing to disclose reportable transaction.

Sec. 426. Registration of certain tax shelters without corporate participants.

Sec. 427. Effective dates.

Subtitle C—Limitation on Importation or Transfer of Built-in Losses

Sec. 431. Limitation on importation of built-in losses.

Sec. 432. Disallowance of partnership loss transfers.

TITLE V—EXPATRIATE CORPORATIONS

Sec. 501. Foreign corporations created through inversion transactions taxed as domestic corporations.

TITLE VI—CHILD TAX CREDIT

Sec. 601. Acceleration of child tax credit.

TITLE VII—MARRIAGE PENALTY RELIEF

Sec. 701. Acceleration of marriage penalty relief provisions.

TITLE VIII—ALTERNATIVE MINIMUM TAX

Sec. 801. Alternative minimum tax relief.

1 **TITLE I—10 PERCENT BRACKET**

2 **SEC. 101. EXPANSION OF 10 PERCENT BRACKET.**

3 (a) IN GENERAL.—Subparagraph (B) of section
4 1(i)(1) of the Internal Revenue Code of 1986 (relating to
5 initial bracket amount) is amended by—

6 (1) striking “\$14,000 (\$12,000 in the case of
7 taxable years beginning before January 1, 2008)” in
8 clause (i) and inserting “\$24,000”, and

9 (2) striking “\$10,000” in clause (ii) and insert-
10 ing “\$15,000”.

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

14 **TITLE II—TAX RATES**

15 **SEC. 201. REPEAL OF INCOME TAX RATE REDUCTIONS FOR**
16 **HIGHEST INCOME TAXPAYERS.**

17 (a) IN GENERAL.—The table contained in section
18 1(i)(2) of the Internal Revenue Code of 1986 (relating to
19 reductions in rates after June 30, 2001) is amended—

20 (1) in the second column, by striking “29.0%”
21 and inserting “30.0%”,

22 (2) in the second column, by striking “28.9%”
23 and inserting “30.0%”,

1 (3) in the third column, by striking “34.0%”
 2 and inserting “35.0%”,

3 (4) in the third column, by striking “33.0%”
 4 and inserting “35.0%”,

5 (5) in the last column, by striking “37.6%” and
 6 inserting “38.6%”, and

7 (6) in the last column, by striking “35.0%” and
 8 inserting “38.6%”.

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

12 **TITLE III—ESTATE TAX**

13 **SEC. 301. ESTATE TAX WITH FULL TAX DEDUCTION FOR** 14 **FAMILY-OWNED BUSINESS INTERESTS.**

15 (a) ELIMINATION OF ESTATE TAX REPEAL.—

16 (1) IN GENERAL.—Subtitle A of title V, sec-
 17 tions 511(d), 511(e), and 521(b)(2), and subtitle E
 18 of title V of the Economic Growth and Tax Relief
 19 Reconciliation Act of 2001 are repealed.

20 (2) CONFORMING AMENDMENTS.—

21 (A) The table contained in section
 22 2001(c)(2)(B) of the Internal Revenue Code of
 23 1986 is amended by striking “2007, 2008, and
 24 2009” and inserting “2007 and thereafter”.

1 (B) Section 901 of the Economic Growth
2 and Tax Relief Reconciliation Act of 2001 is
3 amended—

4 (i) by striking “this Act” and all that
5 follows through “2010.” in subsection (a)
6 and inserting “this Act (other than title V)
7 shall not apply to taxable, plan, or limita-
8 tion years beginning after December 31,
9 2010.”, and

10 (ii) by striking “, estates, gifts, and
11 transfers” in subsection (b).

12 (b) INCREASE IN EXCLUSION AMOUNT.—Subsection
13 (c) of section 2010 of the Internal Revenue Code of 1986
14 is amended by striking “were the applicable exclusion
15 amount” and all that follows and inserting “\$4,000,000.”.

16 (c) FULL TAX DEDUCTION FOR FAMILY-OWNED
17 BUSINESS INTERESTS.—

18 (1) IN GENERAL.—Section 2057(a) of the In-
19 ternal Revenue Code of 1986 (relating to deduction
20 for family-owned business interests) is amended—

21 (A) by striking paragraphs (2) and (3),
22 and

23 (B) by striking “GENERAL RULE.—” and
24 all that follows through “For purposes” and in-

1 serting “ALLOWANCE OF DEDUCTION.—For
2 purposes”.

3 (2) PERMANENT DEDUCTION.—Section 2057 of
4 such Code is amended by striking subsection (j).

5 (d) EFFECTIVE DATE.—The amendments made by
6 this section shall apply to the estates of decedents dying,
7 and gifts made, after December 31, 2002.

8 **TITLE IV—TAX SHELTER**
9 **TRANSACTIONS**

10 **SEC. 401. FINDINGS AND PURPOSE.**

11 (a) FINDINGS.—The Congress hereby finds that:

12 (1) Many corporate tax shelter transactions are
13 complicated ways of accomplishing nothing aside
14 from claimed tax benefits, and the legal opinions
15 justifying those transactions take an inappropriately
16 narrow and restrictive view of well-developed court
17 doctrines under which—

18 (A) the taxation of a transaction is deter-
19 mined in accordance with its substance and not
20 merely its form,

21 (B) transactions which have no significant
22 effect on the taxpayer’s economic or beneficial
23 interests except for tax benefits are treated as
24 sham transactions and disregarded,

1 (C) transactions involving multiple steps
2 are collapsed when those steps have no substan-
3 tial economic meaning and are merely designed
4 to create tax benefits,

5 (D) transactions with no business purpose
6 are not given effect, and

7 (E) in the absence of a specific congres-
8 sional authorization, it is presumed that Con-
9 gress did not intend a transaction to result in
10 a negative tax where the taxpayer's economic
11 position or rate of return is better after tax
12 than before tax.

13 (2) Permitting aggressive and abusive tax shel-
14 ters not only results in large revenue losses but also
15 undermines voluntary compliance with the Internal
16 Revenue Code of 1986.

17 (b) PURPOSE.—The purpose of this title is to elimi-
18 nate abusive tax shelters by denying tax attributes claimed
19 to arise from transactions that do not meet a heightened
20 economic substance requirement and by repealing the pro-
21 vision that permits legal opinions to be used to avoid pen-
22 alties on tax underpayments resulting from transactions
23 without significant economic substance or business pur-
24 pose.

1 **Subtitle A—Clarification of**
 2 **Economic Substance Doctrine**

3 **SEC. 411. CLARIFICATION OF ECONOMIC SUBSTANCE DOC-**
 4 **TRINE.**

5 (a) IN GENERAL.—Section 7701 of the Internal Rev-
 6 enue Code of 1986 (relating to definitions) is amended by
 7 redesignating subsection (n) as subsection (o) and by in-
 8 serting after subsection (m) the following new subsection:

9 “(n) CLARIFICATION OF ECONOMIC SUBSTANCE
 10 DOCTRINE; ETC.—

11 “(1) GENERAL RULES.—

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

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

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

20 “(I) the transaction changes in a
 21 meaningful way (apart from Federal
 22 income tax effects) the taxpayer’s eco-
 23 nomic position, and

24 “(II) the taxpayer has a substan-
 25 tial nontax purpose for entering into

1 such transaction and the transaction
2 is a reasonable means of accom-
3 plishing such purpose.

4 “(ii) SPECIAL RULE WHERE TAX-
5 PAYER RELIES ON PROFIT POTENTIAL.—A
6 transaction shall not be treated as having
7 economic substance by reason of having a
8 potential for profit unless—

9 “(I) the present value of the rea-
10 sonably expected pre-tax profit from
11 the transaction is substantial in rela-
12 tion to the present value of the ex-
13 pected net tax benefits that would be
14 allowed if the transaction were re-
15 spected, and

16 “(II) the reasonably expected
17 pre-tax profit from the transaction ex-
18 ceeds a risk-free rate of return.

19 “(C) TREATMENT OF FEES AND FOREIGN
20 TAXES.—Fees and other transaction expenses
21 and foreign taxes shall be taken into account as
22 expenses in determining pre-tax profit under
23 subparagraph (B)(ii).

24 “(2) SPECIAL RULES FOR TRANSACTIONS WITH
25 TAX-INDIFFERENT PARTIES.—

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

17 “(B) ARTIFICIAL INCOME SHIFTING AND
18 BASIS ADJUSTMENTS.—The form of a trans-
19 action with a tax-indifferent party shall not be
20 respected if—

21 “(i) it results in an allocation of in-
22 come or gain to the tax-indifferent party in
23 excess of such party’s economic income or
24 gain, or

1 “(ii) it results in a basis adjustment
2 or shifting of basis on account of over-
3 stating the income or gain of the tax-indif-
4 ferent party.

5 “(3) DEFINITIONS AND SPECIAL RULES.—For
6 purposes of this subsection—

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

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

22 “(C) EXCEPTION FOR PERSONAL TRANS-
23 ACTIONS OF INDIVIDUALS.—In the case of an
24 individual, this subsection shall apply only to
25 transactions entered into in connection with a

1 trade or business or an activity engaged in for
2 the production of income.

3 “(D) TREATMENT OF LESSORS.—In apply-
4 ing subclause (I) of paragraph (1)(B)(ii) to the
5 lessor of tangible property subject to a lease,
6 the expected net tax benefits shall not include
7 the benefits of depreciation, or any tax credit,
8 with respect to the leased property and sub-
9 clause (II) of paragraph (1)(B)(ii) shall be dis-
10 regarded in determining whether any of such
11 benefits are allowable.

12 “(4) OTHER COMMON LAW DOCTRINES NOT AF-
13 FECTED.—Except as specifically provided in this
14 subsection, the provisions of this subsection shall not
15 be construed as altering or supplanting any other
16 rule of law referred to in section 6662(i)(2), and the
17 requirements of this subsection shall be construed as
18 being in addition to any such other rule of law.”.

19 (b) EFFECTIVE DATE.—The amendments made by
20 this section shall apply to transactions after the date of
21 the enactment of this Act.

1 the transaction was not respected under section
2 7701(n)(2),

3 “(B) a lack of business purpose for such
4 transaction or because the form of the trans-
5 action does not reflect its substance, or

6 “(C) a failure to meet the requirements of
7 any other similar rule of law.

8 “(3) INCREASE IN PENALTY NOT TO APPLY IF
9 COMPLIANCE WITH DISCLOSURE REQUIREMENTS.—
10 Paragraph (1)(A) shall not apply if the taxpayer dis-
11 closes to the Secretary (as such time and in such
12 manner as the Secretary shall prescribe) such infor-
13 mation as the Secretary shall prescribe with respect
14 to such transaction.”.

15 (b) MODIFICATIONS TO PENALTY ON SUBSTANTIAL
16 UNDERSTATEMENT OF INCOME TAX.—

17 (1) MODIFICATION OF THRESHOLD.—Subpara-
18 graph (A) of section 6662(d)(1) of the Internal Rev-
19 enue Code of 1986 is amended to read as follows:

20 “(A) IN GENERAL.—For purposes of this
21 section, there is a substantial understatement of
22 income tax for any taxable year if the amount
23 of the understatement for the taxable year ex-
24 ceeds the lesser of—

25 “(i) \$500,000, or

1 “(ii) the greater of 10 percent of the
2 tax required to be shown on the return for
3 the taxable year or \$5,000.”.

4 (2) MODIFICATION OF PENALTY ON TAX SHEL-
5 TERS, ETC.—Clauses (i) and (ii) of section
6 6662(d)(2)(C) of such Code are amended to read as
7 follows:

8 “(i) IN GENERAL.—Subparagraph (B)
9 shall not apply to any item attributable to
10 a tax shelter.

11 “(ii) DETERMINATION OF UNDER-
12 STATEMENTS WITH RESPECT TO TAX
13 SHELTERS, ETC.—In any case in which
14 there are one or more items attributable to
15 a tax shelter, the amount of the under-
16 statement under subparagraph (A) shall in
17 no event be less than the amount of under-
18 statement which would be determined for
19 the taxable year if all items shown on the
20 return which are not attributable to any
21 tax shelter were treated as being correct. A
22 similar rule shall apply in cases to which
23 subsection (i) applies, whether or not the
24 items are attributable to a tax shelter.”.

1 (c) TREATMENT OF AMENDED RETURNS.—Sub-
 2 section (a) of section 6664 of the Internal Revenue Code
 3 of 1986 is amended by adding at the end the following
 4 new sentence: “For purposes of this subsection, an amend-
 5 ed return shall be disregarded if such return is filed on
 6 or after the date the taxpayer is first contacted by the
 7 Secretary regarding the examination of the return.”.

8 **SEC. 422. PENALTY ON PROMOTERS OF TAX AVOIDANCE**
 9 **STRATEGIES WHICH HAVE NO ECONOMIC**
 10 **SUBSTANCE, ETC.**

11 (a) PENALTY.—

12 (1) IN GENERAL.—Section 6700 of the Internal
 13 Revenue Code of 1986 (relating to promoting abu-
 14 sive tax shelters, etc.) is amended by redesignating
 15 subsection (c) as subsection (d) and by inserting
 16 after subsection (b) the following new subsection:

17 “(c) PENALTY ON SUBSTANTIAL PROMOTERS FOR
 18 PROMOTING TAX AVOIDANCE STRATEGIES WHICH HAVE
 19 NO ECONOMIC SUBSTANCE, ETC.—

20 “(1) IMPOSITION OF PENALTY.—Any substan-
 21 tial promoter of a tax avoidance strategy shall pay
 22 a penalty in the amount determined under para-
 23 graph (2) with respect to such strategy if such strat-
 24 egy (or any similar strategy promoted by such pro-

1 promoter) fails to meet the requirements of any rule of
2 law referred to in section 6662(i)(2).

3 “(2) AMOUNT OF PENALTY.—The penalty
4 under paragraph (1) with respect to a promoter of
5 a tax avoidance strategy is an amount equal to 100
6 percent of the gross income derived (or to be de-
7 rived) by such promoter from such strategy.

8 “(3) TAX AVOIDANCE STRATEGY.—For pur-
9 poses of this subsection, the term ‘tax avoidance
10 strategy’ means any entity, plan, arrangement, or
11 transaction a significant purpose of the structure of
12 which is the avoidance or evasion of Federal income
13 tax.

14 “(4) SUBSTANTIAL PROMOTER.—For purposes
15 of this subsection—

16 “(A) IN GENERAL.—The term ‘substantial
17 promoter’ means, with respect to any tax avoid-
18 ance strategy, any promoter if—

19 “(i) such promoter offers such strat-
20 egy to more than 1 potential participant,
21 and

22 “(ii) such promoter may receive fees
23 in excess of \$500,000 in the aggregate
24 with respect to such strategy.

1 “(B) AGGREGATION RULES.—For purposes
2 of this paragraph—

3 “(i) RELATED PERSONS.—A promoter
4 and all persons related to such promoter
5 shall be treated as 1 person who is a pro-
6 moter.

7 “(ii) SIMILAR STRATEGIES.—All simi-
8 lar tax avoidance strategies of a promoter
9 shall be treated as 1 tax avoidance strat-
10 egy.

11 “(C) PROMOTER.—The term ‘promoter’
12 means any person who participates in the pro-
13 motion, offering, or sale of the tax avoidance
14 strategy.

15 “(D) RELATED PERSON.—Persons are re-
16 lated if they bear a relationship to each other
17 which is described in section 267(b) or 707(b).

18 “(4) COORDINATION WITH SUBSECTION (a).—
19 No penalty shall be imposed by this subsection on
20 any promoter with respect to a tax avoidance strat-
21 egy if a penalty is imposed under subsection (a) on
22 such promoter with respect to such strategy.”.

23 “(2) CONFORMING AMENDMENT.—Subsection (d)
24 of section 6700 of such Code is amended—

1 (A) by striking “PENALTY” and inserting
2 “PENALTIES”, and

3 (B) by striking “penalty” the first place it
4 appears in the text and inserting “penalties”.

5 (b) INCREASE IN PENALTY ON PROMOTING ABUSIVE
6 TAX SHELTERS.—The first sentence of section 6700(a)
7 of the Internal Revenue Code of 1986 is amended by strik-
8 ing “a penalty equal to” and all that follows and inserting
9 “a penalty equal to the greater of \$1,000 or 100 percent
10 of the gross income derived (or to be derived) by such per-
11 son from such activity.”.

12 **SEC. 423. MODIFICATIONS OF PENALTIES FOR AIDING AND**
13 **ABETTING UNDERSTATEMENT OF TAX LI-**
14 **ABILITY INVOLVING TAX SHELTERS.**

15 (a) IMPOSITION OF PENALTY.—Section 6701(a) of
16 the Internal Revenue Code of 1986 (relating to imposition
17 of penalty) is amended to read as follows:

18 “(a) IMPOSITION OF PENALTIES.—

19 “(1) IN GENERAL.—Any person—

20 “(A) who aids or assists in, procures, or
21 advises with respect to, the preparation or pres-
22 entation of any portion of a return, affidavit,
23 claim, or other document,

24 “(B) who knows (or has reason to believe)
25 that such portion will be used in connection

1 with any material matter arising under the in-
2 ternal revenue laws, and

3 “(C) who knows that such portion (if so
4 used) would result in an understatement of the
5 liability for tax of another person,

6 shall pay a penalty with respect to each such docu-
7 ment in the amount determined under subsection
8 (b).

9 “(2) CERTAIN TAX SHELTERS.—If—

10 “(A) any person—

11 “(i) aids or assists in, procures, or ad-
12 vises with respect to the creation, organiza-
13 tion, sale, implementation, management, or
14 reporting of a tax shelter (as defined in
15 section 6662(d)(2)(C)(iii)) or of any entity,
16 plan, arrangement, or transaction that
17 fails to meet the requirements of any rule
18 of law referred to in section 6662(i)(2),
19 and

20 “(ii) opines, advises, represents, or
21 otherwise indicates (directly or indirectly)
22 that the taxpayer’s tax treatment of items
23 attributable to such tax shelter or such en-
24 tity, plan, arrangement, or transaction and
25 giving rise to an understatement of tax li-

1 ability would more likely than not prevail
2 or not give rise to a penalty, and
3 “(B) such opinion, advice, representation,
4 or indication is unreasonable,
5 then such person shall pay a penalty in the amount
6 determined under subsection (b). If a standard high-
7 er than the more likely than not standard was used
8 in any such opinion, advice, representation, or indi-
9 cation, then subparagraph (A)(ii) shall be applied as
10 if such standard were substituted for the more likely
11 than not standard.”.

12 (b) AMOUNT OF PENALTY.—Section 6701(b) of the
13 Internal Revenue Code of 1986 (relating to amount of
14 penalty) is amended—

15 (1) by inserting “or (3)” after “paragraph (2)”
16 in paragraph (1),

17 (2) by striking “subsection (a)” each place it
18 appears and inserting “subsection (a)(1)”, and

19 (3) by redesignating paragraph (3) as para-
20 graph (4) and by adding after paragraph (2) the fol-
21 lowing:

22 “(3) TAX SHELTERS.—In the case of—

23 “(A) a penalty imposed by subsection
24 (a)(1) which involves a return, affidavit, claim,
25 or other document relating to a tax shelter or

1 an entity, plan, arrangement, or transaction
2 that fails to meet the requirements of any rule
3 of law referred to in section 6662(i)(2), and

4 “(B) any penalty imposed by subsection
5 (a)(2),

6 the amount of the penalty shall be equal to 100 per-
7 cent of the gross proceeds derived (or to be derived)
8 by the person in connection with the tax shelter or
9 entity, plan, arrangement, or transaction.”.

10 (c) REFERRAL AND PUBLICATION.—If a penalty is
11 imposed under section 6701(a)(2) of the Internal Revenue
12 Code of 1986 (as added by subsection (a)) on any person,
13 the Secretary of the Treasury shall—

14 (1) notify the Director of Practice of the Inter-
15 nal Revenue Service and any appropriate State li-
16 censing authority of the penalty and the cir-
17 cumstances under which it was imposed, and

18 (2) publish the identity of the person and the
19 fact the penalty was imposed on the person.

20 (d) CONFORMING AMENDMENTS.—

21 (1) Section 6701(d) of the Internal Revenue
22 Code of 1986 is amended by striking “Subsection
23 (a)” and inserting “Subsection (a)(1)”.

1 (2) Section 6701(e) of such Code is amended by
2 striking “subsection (a)(1)” and inserting “sub-
3 section (a)(1)(A)”.

4 (3) Section 6701(f) of such Code is amended by
5 inserting “, tax shelter, or entity, plan, arrangement,
6 or transaction” after “document” each place it ap-
7 pears.

8 **SEC. 424. FAILURE TO MAINTAIN LISTS.**

9 Section 6708(a) of the Internal Revenue Code of
10 1986 (relating to failure to maintain lists of investors in
11 potentially abusive tax shelters) is amended by adding at
12 the end the following: “In the case of a tax shelter (as
13 defined in section 6662(d)(2)(C)(iii)) or entity, plan, ar-
14 rangement, or transaction that fails to meet the require-
15 ments of any rule of law referred to in section 6662(i)(2),
16 the penalty shall be equal to 50 percent of the gross pro-
17 ceeds derived (or to be derived) from each person with re-
18 spect to which there was a failure and the limitation of
19 the preceding sentence shall not apply.”.

20 **SEC. 425. PENALTY FOR FAILING TO DISCLOSE REPORT-**
21 **ABLE TRANSACTION.**

22 (a) IN GENERAL.—Part I of subchapter B of chapter
23 68 of the Internal Revenue Code of 1986 (relating to as-
24 sessable penalties) is amended by inserting after section
25 6707 the following new section:

1 **“SEC. 6707A. PENALTY FOR FAILURE TO INCLUDE TAX**
2 **SHELTER INFORMATION WITH RETURN.**

3 “(a) IMPOSITION OF PENALTY.—Any person who
4 fails to include with its return of Federal income tax any
5 information required to be included under section 6011
6 with respect to a reportable transaction shall pay a penalty
7 in the amount determined under subsection (b). No pen-
8 alty shall be imposed on any such failure if it is shown
9 that such failure is due to reasonable cause.

10 “(b) AMOUNT OF PENALTY.—

11 “(1) IN GENERAL.—The amount of the penalty
12 under subsection (a) shall be equal to the greater
13 of—

14 “(A) 5 percent of any increase in Federal
15 tax which results from a difference between the
16 taxpayer’s treatment (as shown on its return)
17 of items attributable to the reportable trans-
18 action to which the failure relates and the prop-
19 er tax treatment of such items, or

20 “(B) \$100,000.

21 For purposes of subparagraph (A), the last sentence
22 of section 6664(a) shall apply.

23 “(2) LISTED TRANSACTION.—If the failure
24 under subsection (a) relates to a reportable trans-
25 action which is the same as, or substantially similar
26 to, a transaction specifically identified by the Sec-

1 retary as a tax avoidance transaction for purposes of
 2 section 6011, paragraph (1)(A) shall be applied by
 3 substituting ‘10 percent’ for ‘5 percent’.

4 “(c) REPORTABLE TRANSACTION.—For purposes of
 5 this section, the term ‘reportable transaction’ means any
 6 transaction with respect to which information is required
 7 under section 6011 to be included with a taxpayer’s return
 8 of tax because, as determined under regulations prescribed
 9 under section 6011, such transaction has characteristics
 10 which may be indicative of a tax avoidance transaction.

11 “(d) COORDINATION WITH OTHER PENALTIES.—
 12 The penalty imposed by this section is in addition to any
 13 penalty imposed under section 6662.”.

14 (b) CONFORMING AMENDMENT.—The table of sec-
 15 tions for part I of subchapter B of chapter 68 of the Inter-
 16 nal Revenue Code of 1986 is amended by inserting after
 17 the item relating to section 6707 the following:

“Sec. 6707A. Penalty for failure to include tax shelter information with re-
 turn.”.

18 **SEC. 426. REGISTRATION OF CERTAIN TAX SHELTERS**
 19 **WITHOUT CORPORATE PARTICIPANTS.**

20 Section 6111(d)(1)(A) of the Internal Revenue Code
 21 of 1986 (relating to certain confidential arrangements
 22 treated as tax shelters) is amended by striking “for a di-
 23 rect or indirect participant which is a corporation”.

1 **SEC. 427. EFFECTIVE DATES.**

2 (a) IN GENERAL.—Except as provided in subsections
3 (b) and (c), the amendments made by this subtitle shall
4 apply to transactions after the date of the enactment of
5 this Act.

6 (b) SECTION 421.—The amendments made by sub-
7 sections (b) and (c) of section 421 shall apply to taxable
8 years ending after the date of the enactment of this Act.

9 (c) SECTION 422.—The amendments made by sub-
10 section (a) of section 422 shall apply to any tax avoidance
11 strategy (as defined in section 6700(c) of the Internal
12 Revenue Code of 1986, as amended by this title) which
13 is offered to potential participants after the date of the
14 enactment of this Act.

15 (d) SECTION 426.—The amendment made by section
16 426 shall apply to any tax shelter interest which is offered
17 to potential participants after the date of the enactment
18 of this Act.

19 **Subtitle C—Limitation on Importa-**
20 **tion or Transfer of Built-in**
21 **Losses**

22 **SEC. 431. LIMITATION ON IMPORTATION OF BUILT-IN**
23 **LOSSES.**

24 (a) IN GENERAL.—Section 362 of the Internal Rev-
25 enue Code of 1986 (relating to basis corporations) is

1 amended by adding at the end the following new sub-
2 section:

3 “(e) LIMITATION ON IMPORTATION OF BUILT-IN
4 LOSSES.—

5 “(1) IN GENERAL.—If in any transaction de-
6 scribed in subsection (a) or (b) there would (but for
7 this subsection) be an importation of a net built-in
8 loss, the basis of each property described in para-
9 graph (2) which is acquired in such transaction shall
10 (notwithstanding subsections (a) and (b)) be its fair
11 market value immediately after such transaction.

12 “(2) PROPERTY DESCRIBED.—For purposes of
13 paragraph (1), property is described in this para-
14 graph if—

15 “(A) gain or loss with respect to such
16 property is not subject to tax under this subtitle
17 in the hands of the transferor immediately be-
18 fore the transfer, and

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

22 In any case in which the transferor is a partnership,
23 the preceding sentence shall be applied by treating
24 each partner in such partnership as holding such

1 partner's proportionate share of the property of such
2 partnership.

3 “(3) IMPORTATION OF NET BUILT-IN LOSS.—
4 For purposes of paragraph (1), there is an importa-
5 tion of a net built-in loss in a transaction if the
6 transferee's aggregate adjusted bases of property de-
7 scribed in paragraph (2) which is transferred in
8 such transaction would (but for this subsection) ex-
9 ceed the fair market value of such property imme-
10 diately after such transaction.”.

11 (b) COMPARABLE TREATMENT WHERE LIQUIDA-
12 TION.—Paragraph (1) of section 334(b) of the Internal
13 Revenue Code of 1986 (relating to liquidation of sub-
14 sidiary) is amended to read as follows:

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

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

4 “(B) in any case in which the liquidating
5 corporation is a foreign corporation, the cor-
6 porate distributee is a domestic corporation,
7 and the corporate distributee’s aggregate ad-
8 justed bases of property described in section
9 362(e)(2) which is distributed in such liquida-
10 tion would (but for this subparagraph) exceed
11 the fair market value of such property imme-
12 diately after such liquidation.”.

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

16 **SEC. 432. DISALLOWANCE OF PARTNERSHIP LOSS TRANS-**
17 **FERS.**

18 (a) TREATMENT OF CONTRIBUTED PROPERTY WITH
19 BUILT-IN LOSS.—Paragraph (1) of section 704(c) of the
20 Internal Revenue Code of 1986 is amended by striking
21 “and” at the end of subparagraph (A), by striking the
22 period at the end of subparagraph (B) and inserting “,
23 and”, and by adding at the end the following:

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

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

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

12 For purposes of subparagraph (C), the term ‘built-
13 in loss’ means the excess of the adjusted basis of the
14 property over its fair market value immediately after
15 the contribution.”.

16 (b) ADJUSTMENT TO BASIS OF PARTNERSHIP PROP-
17 ERTY ON TRANSFER OF PARTNERSHIP INTEREST IF
18 THERE IS SUBSTANTIAL BUILT-IN LOSS.—

19 (1) ADJUSTMENT REQUIRED.—Subsection (a)
20 of section 743 of the Internal Revenue Code of 1986
21 (relating to optional adjustment to basis of partner-
22 ship property) is amended by inserting before the
23 period “or unless the partnership has a substantial
24 built-in loss immediately after such transfer”.

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

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

9 “(d) SUBSTANTIAL BUILT-IN LOSS.—For purposes
 10 of this section, a partnership has a substantial built-in loss
 11 with respect to a transfer of an interest in a partnership
 12 if the transferee partner’s proportionate share of the ad-
 13 justed basis of the partnership property exceeds 110 per-
 14 cent of the basis of such partner’s interest in the partner-
 15 ship.”.

16 (4) CLERICAL AMENDMENTS.—

17 (A) The section heading for section 743 of
 18 such Code is amended to read as follows:

19 **“SEC. 743. ADJUSTMENT TO BASIS OF PARTNERSHIP PROP-**
 20 **ERTY WHERE SECTION 754 ELECTION OR**
 21 **SUBSTANTIAL BUILT-IN LOSS.”.**

22 (B) The table of sections for subpart C of
 23 part II of subchapter K of chapter 1 of such
 24 Code is amended by striking the item relating

1 to section 743 and inserting the following new
2 item:

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

3 (c) ADJUSTMENT TO BASIS OF UNDISTRIBUTED
4 PARTNERSHIP PROPERTY IF THERE IS SUBSTANTIAL
5 BASIS REDUCTION.—

6 (1) ADJUSTMENT REQUIRED.—Subsection (a)
7 of section 734 of the Internal Revenue Code of 1986
8 (relating to optional adjustment to basis of undistributed
9 partnership property) is amended by inserting
10 before the period “or unless there is a substantial
11 basis reduction”.

12 (2) ADJUSTMENT.—Subsection (b) of section
13 734 of such Code is amended by inserting “or unless
14 there is a substantial basis reduction” after “section
15 754 is in effect”.

16 (3) SUBSTANTIAL BASIS REDUCTION.—Section
17 734 of such Code is amended by adding at the end
18 the following new subsection:

19 “(d) SUBSTANTIAL BASIS REDUCTION.—For purposes
20 of this section, there is a substantial basis reduction
21 with respect to a distribution if the sum of the amounts
22 described in subparagraphs (A) and (B) of subsection
23 (b)(2) exceeds 10 percent of the aggregate adjusted basis

1 of partnership property immediately after the distribu-
2 tion.”.

3 (4) CLERICAL AMENDMENTS.—

4 (A) The section heading for section 734 of
5 such Code is amended to read as follows:

6 **“SEC. 734. ADJUSTMENT TO BASIS OF UNDISTRIBUTED**
7 **PARTNERSHIP PROPERTY WHERE SECTION**
8 **754 ELECTION OR SUBSTANTIAL BASIS RE-**
9 **DUCTION.”.**

10 (B) The table of sections for subpart B of
11 part II of subchapter K of chapter 1 of such
12 Code is amended by striking the item relating
13 to section 734 and inserting the following new
14 item:

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

15 (d) EFFECTIVE DATES.—

16 (1) SUBSECTION (a).—The amendment made
17 by subsection (a) shall apply to contributions made
18 after the date of the enactment of this Act.

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

22 (3) SUBSECTION (c).—The amendments made
23 by subsection (c) shall apply to distributions after
24 the date of the enactment of this Act.

1 **TITLE V—EXPATRIATE**
2 **CORPORATIONS**

3 **SEC. 501. FOREIGN CORPORATIONS CREATED THROUGH IN-**
4 **VERSION TRANSACTIONS TAXED AS DOMES-**
5 **TIC CORPORATIONS.**

6 (a) IN GENERAL.—Paragraph (4) of section 7701(a)
7 of the Internal Revenue Code of 1986 (defining domestic)
8 is amended to read as follows:

9 “(4) DOMESTIC.—

10 “(A) IN GENERAL.—Except as provided in
11 subparagraph (B), the term ‘domestic’ when ap-
12 plied to a corporation or partnership means cre-
13 ated or organized in the United States or under
14 the law of the United States or of any State
15 unless, in the case of a partnership, the Sec-
16 retary provides otherwise by regulations.

17 “(B) INVERSION TRANSACTIONS DIS-
18 REGARDED.—

19 “(i) IN GENERAL.—A corporation
20 which would (but for this subparagraph)
21 be treated as a foreign corporation shall be
22 treated as a domestic corporation if such
23 corporation is an inverted domestic cor-
24 poration.

1 “(ii) INVERTED DOMESTIC CORPORA-
2 TION.—For purposes of clause (i), a for-
3 eign corporation is an inverted domestic
4 corporation if, immediately after a trans-
5 action in which—

6 “(I) property is directly or indi-
7 rectly transferred by a domestic cor-
8 poration to such foreign corporation,
9 or

10 “(II) stock in a domestic cor-
11 poration is transferred directly or in-
12 directly by its shareholders to such
13 foreign corporation,

14 more than 50 percent of the stock (by vote
15 or value) of such foreign corporation is
16 held by former shareholders of the domes-
17 tic corporation by reason of holding stock
18 in such domestic corporation.

19 “(iii) REGULATIONS RELATING TO IN-
20 VERTED DOMESTIC CORPORATIONS.—The
21 Secretary may by regulations provide that
22 clause (i) shall not apply to a foreign cor-
23 poration which is an inverted domestic cor-
24 poration if, immediately before the trans-
25 action described in clause (ii), such foreign

1 corporation was engaged in the active con-
2 duct of 1 or more trades or businesses
3 which are substantial in relation to the
4 trades or businesses which the domestic
5 corporation described in clause (ii) was en-
6 gaged in the active conduct of at such
7 time.”.

8 (b) EFFECTIVE DATE.—The amendment made by
9 this section shall apply to taxable years of any inverted
10 domestic corporation beginning after December 31, 2002,
11 without regard to whether the corporation became an in-
12 verted domestic corporation before, on, or after such date.

13 **TITLE VI—CHILD TAX CREDIT**

14 **SEC. 601. ACCELERATION OF CHILD TAX CREDIT.**

15 (a) IN GENERAL.—Subsection (a) of section 24 of the
16 Internal Revenue Code of 1986 (relating to child tax cred-
17 it) is amended by striking “the per child amount” and
18 all that follows and inserting “\$1,000”.

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

1 **TITLE VII—MARRIAGE PENALTY**
2 **RELIEF**

3 **SEC. 701. ACCELERATION OF MARRIAGE PENALTY RELIEF**
4 **PROVISIONS.**

5 (a) **ELIMINATION OF MARRIAGE PENALTY IN STAND-**
6 **ARD DEDUCTION.—**

7 (1) **IN GENERAL.—**Paragraph (2) of section
8 63(c) of the Internal Revenue Code of 1986 (relat-
9 ing to standard deduction) is amended—

10 (A) by striking “\$5,000” in subparagraph
11 (A) and inserting “200 percent of the dollar
12 amount in effect under subparagraph (C) for
13 the taxable year”;

14 (B) by adding “or” at the end of subpara-
15 graph (B);

16 (C) by striking “in the case of” and all
17 that follows in subparagraph (C) and inserting
18 “in any other case.”; and

19 (D) by striking subparagraph (D).

20 (2) **TECHNICAL AMENDMENTS.—**

21 (A) Subparagraph (B) of section 1(f)(6) of
22 such Code is amended by striking “(other than
23 with” and all that follows through “shall be ap-
24 plied” and inserting “(other than with respect

1 to sections 63(c)(4) and 151(d)(4)(A)) shall be
 2 applied”.

3 (B) Paragraph (4) of section 63(c) of such
 4 Code is amended by adding at the end the fol-
 5 lowing flush sentence:

6 “The preceding sentence shall not apply to the
 7 amount referred to in paragraph (2)(A).”.

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

11 (b) ELIMINATION OF MARRIAGE PENALTY IN 15-
 12 PERCENT BRACKET.—

13 (1) IN GENERAL.—Section 1(f) of the Internal
 14 Revenue Code of 1986 (relating to adjustments in
 15 tax tables so that inflation will not result in tax in-
 16 creases) is amended by adding at the end the fol-
 17 lowing new paragraph:

18 “(8) ELIMINATION OF MARRIAGE PENALTY IN
 19 15-PERCENT BRACKET.—

20 “(A) IN GENERAL.—With respect to tax-
 21 able years beginning after December 31, 2002,
 22 in prescribing the tables under paragraph (1)—

23 “(i) the maximum taxable income in
 24 the 15-percent rate bracket in the table
 25 contained in subsection (a) (and the min-

1 imum taxable income in the next higher
2 taxable income bracket in such table) shall
3 be 200 percent of the maximum taxable in-
4 come in the 15-percent rate bracket in the
5 table contained in subsection (c) (after any
6 other adjustment under this subsection),
7 and

8 “(ii) the comparable taxable income
9 amounts in the table contained in sub-
10 section (d) shall be $\frac{1}{2}$ of the amounts de-
11 termined under clause (i).

12 “(B) ROUNDING.—If any amount deter-
13 mined under subparagraph (A)(i) is not a mul-
14 tiple of \$50, such amount shall be rounded to
15 the next lowest multiple of \$50.”.

16 (2) TECHNICAL AMENDMENTS.—

17 (A) Subparagraph (A) of section 1(f)(2) of
18 such Code is amended by inserting “except as
19 provided in paragraph (8),” before “by increas-
20 ing”.

21 (B) The heading for subsection (f) of sec-
22 tion 1 is amended by inserting “ELIMINATION
23 OF MARRIAGE PENALTY IN 15-PERCENT
24 BRACKET;” before “ADJUSTMENTS”.

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

4 (c) MARRIAGE PENALTY RELIEF FOR EARNED IN-
5 COME CREDIT.—

6 (1) INCREASED PHASEOUT AMOUNT.—

7 (A) IN GENERAL.—Section 32(b)(2)(B) of
8 the Internal Revenue Code of 1986 (relating to
9 amounts) is amended by striking “increased
10 by—” and all that follows and inserting “in-
11 creased by \$3,000.”.

12 (B) INFLATION ADJUSTMENT.—Paragraph
13 (1)(B)(ii) of section 32(j) of such Code (relat-
14 ing to inflation adjustments) is amended to
15 read as follows:

16 “(ii) in the case of the \$3,000 amount
17 in subsection (b)(2)(B), by substituting
18 ‘calendar year 2003’ for ‘calendar year
19 1992’ in subparagraph (B) of such section
20 1.”.

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

24 (2) EXPANSION OF MATHEMATICAL ERROR AU-
25 THORITY.—

1 (A) IN GENERAL.—Paragraph (2) of sec-
2 tion 6213(g) of such Code is amended by strik-
3 ing “and” at the end of subparagraph (K), by
4 striking the period at the end of subparagraph
5 (L) and inserting “, and”, and by inserting
6 after subparagraph (L) the following new sub-
7 paragraph:

8 “(M) the entry on the return claiming the
9 credit under section 32 with respect to a child
10 if, according to the Federal Case Registry of
11 Child Support Orders established under section
12 453(h) of the Social Security Act, the taxpayer
13 is a noncustodial parent of such child.”.

14 (B) EFFECTIVE DATE.—The amendment
15 made by this paragraph shall take effect on
16 January 1, 2003.

17 (d) CONFORMING AMENDMENTS.—

18 (1) REPEAL OF AMENDMENTS.—Sections 301,
19 302, and 303(g) of the Economic Growth and Tax
20 Relief Reconciliation Act of 2001 are repealed.

21 (2) REPEAL OF SUNSET.—Title IX of the Eco-
22 nomic Growth and Tax Relief Reconciliation Act of
23 2001 (relating to sunset of provisions of such Act)
24 shall not apply to section 303 (other than subsection

1 (g) of such section) of such Act (relating to mar-
2 riage penalty relief).

3 **TITLE VIII—ALTERNATIVE**
4 **MINIMUM TAX**

5 **SEC. 801. ALTERNATIVE MINIMUM TAX RELIEF.**

6 (a) IN GENERAL.—Paragraph (2) of section 26(a) of
7 the Internal Revenue Code of 1986 is amended—

8 (1) by striking “2000, 2001, 2002, or 2003”
9 and inserting “2003, 2004, or 2005”, and

10 (2) in the heading by striking “2000, 2001,
11 2002, AND 2003” in the heading and inserting
12 “2003, 2004, AND 2005”.

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

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