

108TH CONGRESS  
1ST SESSION

# S. 1475

To amend the Internal Revenue Code of 1986 to promote the competitiveness of American businesses, and for other purposes.

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## IN THE SENATE OF THE UNITED STATES

JULY 28 (legislative day, JULY 21), 2003

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

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## A BILL

To amend the Internal Revenue Code of 1986 to promote the competitiveness of American businesses, 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; REFERENCES; TABLE OF CON-**  
4       **TENTS.**

5       (a) SHORT TITLE.—This Act may be cited as the  
6       “Promote Growth and Jobs in the USA Act of 2003” (the  
7       PRO GROW USA Act of 2003).

8       (b) AMENDMENT OF 1986 CODE.—Except as other-  
9       wise expressly provided, whenever in this Act an amend-  
10      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.

4 (c) TABLE OF CONTENTS.—

Sec. 1. Short title; references; table of contents.

TITLE I—REPEAL OF EXCLUSION FOR EXTRATERRITORIAL  
INCOME

Sec. 101. Repeal of exclusion for extraterritorial income.

TITLE II—SIMPLIFICATION OF RULES RELATING TO TAXATION  
OF UNITED STATES BUSINESSES OPERATING ABROAD

Subtitle A—Treatment of Controlled Foreign Corporations

Sec. 201. Exceptions from foreign base company sales and services income rules.

Sec. 202. Look-thru treatment of payments between related controlled foreign corporations under foreign personal holding company income rules.

Sec. 203. Look-thru treatment for sales of partnership interests.

Sec. 204. Repeal of foreign personal holding company rules and foreign investment company rules.

Sec. 205. Clarification of treatment of pipeline transportation income.

Sec. 206. Permanent extension and modification of subpart F exemption for active financing.

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

Sec. 208. Modification of interaction between subpart F and passive foreign investment company rules.

Sec. 209. Determination of foreign personal holding company income with respect to transactions in commodities.

Sec. 210. Repeal of foreign base company shipping income rules.

Sec. 211. Reduced tax on repatriated earnings previously exempt from tax under subpart F.

Sec. 212. Effective date.

Subtitle B—Provisions Relating to Foreign Tax Credit

Sec. 221. Interest expense allocation rules.

Sec. 222. Extension of period to which excess foreign taxes may be carried.

Sec. 223. Ordering rules for foreign tax credit carryforwards.

Sec. 224. Repeal of limitation of foreign tax credit under alternative minimum tax.

Sec. 225. Look-thru rules to apply to dividends from noncontrolled section 902 corporations.

Sec. 226. Reduction to 2 foreign tax credit baskets.

Sec. 227. Recharacterization of overall domestic loss.

Sec. 228. Repeal of special rules for applying foreign tax credit in case of foreign oil and gas income.

Sec. 229. Increase in individual exemption from foreign tax credit limitation.

- Sec. 230. United States property not to include certain assets of controlled foreign corporation.
- Sec. 231. Attribution of stock ownership through partnerships to apply in determining section 902 and 960 credits.
- Sec. 232. Provide equal treatment for interest paid by foreign partnerships and foreign corporations.
- Sec. 233. Application of look-thru rules to interest, rents, and royalties.
- Sec. 234. Clarification of treatment of certain transfers of intangible property.

#### Subtitle C—Other Provisions

- Sec. 251. Application of uniform capitalization rules to foreign persons.
- Sec. 252. Treatment of certain dividends of regulated investment companies.
- Sec. 253. Repeal of withholding tax on dividends from certain foreign corporations.
- Sec. 254. Airline mileage awards to certain foreign persons.
- Sec. 255. Interest payments deductible where disqualified guarantee has no economic effect.
- Sec. 256. Modifications of reporting requirements for certain foreign-owned corporations.
- Sec. 257. Repeal of tax on certain United States source capital gains of non-resident aliens.
- Sec. 258. Election not to use average exchange rate for foreign tax paid other than in functional currency.
- Sec. 259. Study of impact of international tax laws on taxpayers other than large corporations.

#### TITLE III—CREDIT FOR INCREASING RESEARCH ACTIVITIES

- Sec. 301. Permanent extension of research credit.
- Sec. 302. Increase in rates of alternative incremental credit.
- Sec. 303. Alternative simplified credit for qualified research expenses.

#### TITLE IV—REFORM OF DEPRECIATION OF BUSINESS PROPERTY

- Sec. 401. 100-percent expensing for certain property through 2006.
- Sec. 402. Extension of expensing for small business.
- Sec. 403. Election to increase minimum tax credit limitation in lieu of bonus depreciation.

## 1 **TITLE I—REPEAL OF EXCLUSION** 2 **FOR EXTRATERRITORIAL IN-** 3 **COME**

### 4 **SEC. 101. REPEAL OF EXCLUSION FOR EXTRATERRITORIAL** 5 **INCOME.**

6 (a) REPEAL.—Section 114 (relating to  
7 extraterritorial income) is repealed.

8 (b) CONFORMING AMENDMENTS.—

1           (1)(A) Subpart E of part III of subchapter N  
2 of chapter 1 (relating to qualifying foreign trade in-  
3 come) is repealed.

4           (B) The table of subparts for such part III is  
5 amended by striking the item relating to subpart E.

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

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

12           (4) Section 275(a) is amended—

13               (A) by inserting “or” at the end of para-  
14 graph (4)(A), by striking “or” at the end of  
15 paragraph (4)(B) and inserting a period, and  
16 by striking subparagraph (C), and

17               (B) by striking the last sentence.

18           (5) Paragraph (3) of section 864(e) is amend-  
19 ed—

20               (A) by striking:

21               “(3) TAX-EXEMPT ASSETS NOT TAKEN INTO  
22 ACCOUNT.—

23               “(A) IN GENERAL.—For purposes of”; and  
24 inserting:

1           “(3) TAX-EXEMPT ASSETS NOT TAKEN INTO  
2       ACCOUNT.—For purposes of”, and

3                       (B) by striking subparagraph (B).

4           (6) Section 903 is amended by striking “114,  
5       164(a),” and inserting “164(a)”.

6           (7) Section 999(c)(1) is amended by striking  
7       “941(a)(5),”.

8       (c) EFFECTIVE DATE.—Except as provided in sub-  
9       sections (d) and (f), the amendments made by this section  
10      shall apply to transactions after December 31, 2003.

11      (d) TRANSITIONAL RULES FOR 2004, 2005, AND  
12      2006.—

13           (1) IN GENERAL.—In the case of transactions  
14      during 2004, 2005, and 2006, the amount includible  
15      in gross income by reason of the amendments made  
16      by this section shall not exceed the applicable per-  
17      centage of the amount which would have been so in-  
18      cluded but for this subsection.

19           (2) APPLICABLE PERCENTAGE.—For purposes  
20      of paragraph (1), the applicable percentage is—

21                       (A) 25 percent for 2004,

22                       (B) 50 percent for 2005, and

23                       (C) 75 percent for 2006.

24      (e) REVOCATION OF ELECTION TO BE TREATED AS  
25      DOMESTIC CORPORATION.—If, during the 1-year period

1 beginning on the date of the enactment of this Act, a cor-  
 2 poration for which an election is in effect under section  
 3 943(e) of the Internal Revenue Code of 1986 revokes such  
 4 election, no gain or loss shall be recognized with respect  
 5 to property treated as transferred under clause (ii) of sec-  
 6 tion 943(e)(4)(B) of such Code to the extent such prop-  
 7 erty—

8 (1) was treated as transferred under clause (i)  
 9 thereof, or

10 (2) was acquired during a taxable year to which  
 11 such election applies and before May 1, 2003, in the  
 12 ordinary course of its trade or business.

13 The Secretary of the Treasury (or such Secretary's dele-  
 14 gate) may prescribe such regulations as may be necessary  
 15 to prevent the abuse of the purposes of this subsection.

16 (f) CLARIFICATION OF TRANSITION RULE TO RE-  
 17 PEAL OF PROVISIONS RELATING TO FOREIGN SALES COR-  
 18 PORATIONS.—

19 (1) IN GENERAL.—The last sentence of section  
 20 5(c)(1) of the FSC Repeal and Extraterritorial In-  
 21 come Exclusion Act of 2000 (Public Law 106–519)  
 22 is amended by inserting “, once exercised by the  
 23 purchaser or lessee (and, if required by the contract,  
 24 accepted by the seller or lessor),” before “is enforce-  
 25 able”.

1           (2) EFFECTIVE DATE.—The amendment made  
 2           by this section shall take effect as if included in the  
 3           provisions of the FSC Repeal and Extraterritorial  
 4           Income Exclusion Act of 2000.

5 **TITLE II—SIMPLIFICATION OF**  
 6 **RULES RELATING TO TAX-**  
 7 **ATION OF UNITED STATES**  
 8 **BUSINESSES OPERATING**  
 9 **ABROAD**

10 **Subtitle A—Treatment of**  
 11 **Controlled Foreign Corporations**

12 **SEC. 201. EXCEPTIONS FROM FOREIGN BASE COMPANY**  
 13 **SALES AND SERVICES INCOME RULES.**

14           (a) IN GENERAL.—Section 954(b) (relating to exclu-  
 15           sions and special rules regarding foreign base company in-  
 16           come) is amended by adding at the end the following new  
 17           paragraph:

18                   “(9) EXCEPTIONS FROM FOREIGN SALES AND  
 19                   SERVICES INCOME.—For purposes of subsection (a),  
 20                   foreign base company income of a controlled foreign  
 21                   corporation for a taxable year shall not include for-  
 22                   eign base company sales income or foreign base com-  
 23                   pany services income for the taxable year—

24                           “(A) if the controlled foreign corporation is  
 25                           eligible for benefits of a comprehensive income

1 tax treaty with the United States (other than  
 2 the treaty with Barbados in force on July 28,  
 3 2003) which the Secretary determines is satis-  
 4 factory for purposes of this paragraph and  
 5 which includes an exchange of information pro-  
 6 gram, or

7 “(B) to the extent that the foreign base  
 8 company sales income or foreign base company  
 9 services income is derived in connection with an  
 10 exempt transaction (as defined in subsection  
 11 (j)).”

12 (b) EXEMPT TRANSACTIONS DEFINED.—Section 954  
 13 (defining foreign base company income) is amended by  
 14 adding at the end the following new subsection:

15 “(j) EXEMPT TRANSACTIONS.—For purposes of sub-  
 16 section (b)(9)—

17 “(1) IN GENERAL.—The term ‘exempt trans-  
 18 action’ means any transaction—

19 “(A) which is subject to an advance pricing  
 20 agreement under section 482 or is treated as  
 21 subject to such an agreement under paragraph  
 22 (2)(C),

23 “(B) with respect to which the cor-  
 24 responding related person transaction described  
 25 in subsection (d)(1) or (e)(1), whichever is ap-



plicable, is subject to an advance pricing agreement under section 482 or is treated as subject to such an agreement under paragraph (2)(C), or

“(C) with respect to which the related person described in subsection (d)(1) or (e)(1), whichever is applicable, with respect to the transaction is, at the time of the transaction—

“(i) a controlled foreign corporation,  
or

“(ii) to the extent provided in regulations, a foreign person or a foreign branch.

“(2) ADVANCE PRICING AGREEMENT APPROVAL  
PROCESS.—

“(A) IN GENERAL.—A United States shareholder of a controlled foreign corporation may file an application for an advance pricing agreement under section 482 which would be applicable to transactions of the controlled foreign corporation or any related person during any 3-taxable year period of the controlled foreign corporation specified in the application. Such application shall be filed at such time and manner, and shall contain such information, as the Secretary shall prescribe.

1 “(B) SECRETARIAL ACTION.—Within 180  
2 days of receipt of an application under subpara-  
3 graph (A) (or such longer period as the Sec-  
4 retary and the applicant may agree upon), the  
5 Secretary shall—

6 “(i) enter into an advance pricing  
7 agreement under section 482 for the tax-  
8 able years covered by the application (or  
9 such greater number of taxable years spec-  
10 ified in the agreement),

11 “(ii) notify the applicant that the Sec-  
12 retary has determined that the application  
13 was filed in good faith and substantially  
14 complies with the requirements for the ap-  
15 plication under subparagraph (A), or

16 “(iii) notify the applicant that the  
17 Secretary has determined that the applica-  
18 tion was not filed in good faith or does not  
19 substantially comply with such require-  
20 ments.

21 If the Secretary fails to act within the time pre-  
22 scribed under the preceding sentence, the appli-  
23 cant shall be treated for purposes of this para-  
24 graph as having received notice under clause  
25 (ii).

1           “(C) EFFECT OF APPROVAL NOTICE.—For  
2           purposes of paragraph (1)(B)(ii), an advance  
3           pricing agreement under section 482 shall be  
4           treated as in effect with respect to transactions  
5           of the controlled foreign corporation or related  
6           person which would otherwise be covered by the  
7           agreement during the period—

8                   “(i) beginning on the date notice  
9                   under subparagraph (B)(ii) is received or  
10                  treated as received (or, if later, the first  
11                  day of the first taxable year to which the  
12                  agreement was to apply), and

13                  “(ii) ending on the effective date of an  
14                  advance pricing agreement entered into  
15                  pursuant to the application or the date the  
16                  Secretary determines the parties will not  
17                  be able to enter into such an agreement.

18           “(3) MULTIPLE SHAREHOLDERS.—An applica-  
19           tion may be filed under paragraph (1) only with the  
20           consent of United States shareholders who own (or  
21           are treated as owning) under section 958 more than  
22           50 percent (by vote or value) of stock of the con-  
23           trolled foreign corporation.”

1       (c) CERTAIN SALES.—Paragraph (1) of section  
2 954(c) is amended by adding at the end the following new  
3 subparagraph:

4               “(H) CERTAIN SALES.—Income (whether  
5               in the form of profits, commissions, fees, or  
6               otherwise) derived in connection with the pur-  
7               chase of personal property from a related per-  
8               son and its sale to any person, the sale of per-  
9               sonal property to any person on behalf of a re-  
10              lated person, the purchase of personal property  
11              from any person and its sale to a related per-  
12              son, or the purchase of personal property from  
13              any person on behalf of a related person if—

14               “(i) the property which is purchased  
15               (or in the case of property sold on behalf  
16               of a related person, the property which is  
17               sold) is manufactured, produced, grown, or  
18               extracted in the United States, and

19               “(ii) the property is sold for use, con-  
20               sumption, or disposition in the United  
21               States, or, in the case of property pur-  
22               chased on behalf of a related person, is  
23               purchased for use, consumption, or disposi-  
24               tion in the United States.

1           This subparagraph shall not apply to income  
 2           otherwise treated as foreign base company in-  
 3           come for the taxable year.”

4           (d) EFFECTIVE DATE.—The amendments made by  
 5 this section shall apply to taxable years of foreign corpora-  
 6 tions beginning after December 31, 2005, and to taxable  
 7 years of United States shareholders with or within which  
 8 such taxable years of foreign corporations end.

9 **SEC. 202. LOOK-THRU TREATMENT OF PAYMENTS BE-**  
 10 **TWEEN RELATED CONTROLLED FOREIGN**  
 11 **CORPORATIONS UNDER FOREIGN PERSONAL**  
 12 **HOLDING COMPANY INCOME RULES.**

13           Subsection (c) of section 954 is amended by adding  
 14 at the end the following new paragraph:

15           “(4) LOOK-THRU IN THE CASE OF RELATED  
 16 CONTROLLED FOREIGN CORPORATIONS.—For pur-  
 17 poses of this subsection, dividends, interest, rents,  
 18 and royalties received or accrued from a controlled  
 19 foreign corporation which is a related person (as de-  
 20 fined in subsection (d)(3)) shall not be treated as  
 21 foreign personal holding company income to the ex-  
 22 tent properly allocable or attributable (determined  
 23 under rules similar to the rules of subparagraphs  
 24 (C) and (D) of section 904(d)(3)) to income of the  
 25 related person which is not subpart F income. The

1 Secretary shall prescribe such regulations as may be  
2 appropriate to prevent the abuse of the purposes of  
3 this paragraph.”

4 **SEC. 203. LOOK-THRU TREATMENT FOR SALES OF PART-**  
5 **NERSHIP INTERESTS.**

6 Section 954(c) (defining foreign personal holding  
7 company income), as amended by section 202, is amended  
8 by adding at the end the following new paragraph:

9 “(5) LOOK-THROUGH RULE FOR CERTAIN  
10 PARTNERSHIP SALES.—

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

19 “(B) 25-PERCENT OWNER.—For purposes  
20 of this paragraph, the term ‘25-percent owner’  
21 means a controlled foreign corporation which  
22 owns (within the meaning of section 958(a)) 25  
23 percent or more of the capital or profits interest  
24 in the partnership.”

1 **SEC. 204. REPEAL OF FOREIGN PERSONAL HOLDING COM-**  
 2 **PANY RULES AND FOREIGN INVESTMENT**  
 3 **COMPANY RULES.**

4 (a) GENERAL RULE.—The following provisions are  
 5 hereby repealed:

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

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

10 (3) Section 1247 (relating to election by foreign  
 11 investment companies to distribute income cur-  
 12 rently).

13 (b) EXEMPTION OF FOREIGN CORPORATIONS FROM  
 14 PERSONAL HOLDING COMPANY RULES.—

15 (1) IN GENERAL.—Subsection (c) of section  
 16 542 (relating to exceptions) is amended—

17 (A) by striking paragraph (5) and insert-  
 18 ing the following:

19 “(5) a foreign corporation,”

20 (B) by striking paragraphs (7) and (10)  
 21 and by redesignating paragraphs (8) and (9) as  
 22 paragraphs (7) and (8), respectively,

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

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

4 (2) TREATMENT OF INCOME FROM PERSONAL  
 5 SERVICE CONTRACTS.—Paragraph (1) of section  
 6 954(c), as amended by section 201(c), is amended  
 7 by adding at the end the following new subpara-  
 8 graph:

9 “(I) PERSONAL SERVICE CONTRACTS.—

10 “(i) Amounts received under a con-  
 11 tract under which the corporation is to fur-  
 12 nish personal services if—

13 “(I) some person other than the  
 14 corporation has the right to designate  
 15 (by name or by description) the indi-  
 16 vidual who is to perform the services,  
 17 or

18 “(II) the individual who is to per-  
 19 form the services is designated (by  
 20 name or by description) in the con-  
 21 tract, and

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

24 This subparagraph shall apply with respect to  
 25 amounts received for services under a particular



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

8 (c) CONFORMING AMENDMENTS.—

9 (1) Clause (iii) of section 1(h)(11)(C) is amend-  
 10 ed by striking “a foreign personal holding company  
 11 (as defined in section 552), a foreign investment  
 12 company (as defined in section 1246(b)), or”.

13 (2) Paragraph (2) of section 171(c) is amend-  
 14 ed—

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

18 (B) by striking “, or foreign personal hold-  
 19 ing company”.

20 (3) Paragraph (2) of section 245(a) is amended  
 21 by striking “foreign personal holding company or”.

22 (4) Section 312 is amended by striking sub-  
 23 section (j).

24 (5) Subsection (m) of section 312 is amended  
 25 by striking “, a foreign investment company (within

1 the meaning of section 1246(b)), or a foreign per-  
 2 sonal holding company (within the meaning of sec-  
 3 tion 552)’’.

4 (6) Subsection (e) of section 443 is amended by  
 5 striking paragraph (3) and by redesignating para-  
 6 graphs (4) and (5) as paragraphs (3) and (4), re-  
 7 spectively.

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

12 (8) Paragraph (1) of section 543(b) is amended  
 13 by inserting “and” at the end of subparagraph (A),  
 14 by striking “, and” at the end of subparagraph (B)  
 15 and inserting a period, and by striking subparagraph  
 16 (C).

17 (9) Paragraph (1) of section 562(b) is amended  
 18 by striking “or a foreign personal holding company  
 19 described in section 552’’.

20 (10) Section 563 is amended—

21 (A) by striking subsection (c),

22 (B) by redesignating subsection (d) as sub-  
 23 section (c), and

1 (C) by striking “subsection (a), (b), or (c)”  
 2 in subsection (c) (as so redesignated) and in-  
 3 serting “subsection (a) or (b)”.

4 (11) Subsection (d) of section 751 is amended  
 5 by adding “and” at the end of paragraph (2), by  
 6 striking paragraph (3), by redesignating paragraph  
 7 (4) as paragraph (3), and by striking “paragraph  
 8 (1), (2), or (3)” in paragraph (3) (as so redesign-  
 9 ated) and inserting “paragraph (1) or (2)”.

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

14 (13)(A) Subparagraph (A) of section 898(b)(1)  
 15 is amended to read as follows:

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

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

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

24 “(3) UNITED STATES SHAREHOLDER.—The  
 25 term ‘United States shareholder’ has the meaning

1 given to such term by section 951(b), except that,  
 2 in the case of a foreign corporation having related  
 3 person insurance income (as defined in section  
 4 953(c)(2)), the Secretary may treat any person as  
 5 a United States shareholder for purposes of this sec-  
 6 tion if such person is treated as a United States  
 7 shareholder under section 953(c)(1).”

8 (D) Subsection (c) of section 898 is amended to  
 9 read as follows:

10 “(c) DETERMINATION OF REQUIRED YEAR.—

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

12 “(A) the majority U.S. shareholder year,

13 or

14 “(B) if there is no majority U.S. share-

15 holder year, the taxable year prescribed under  
 16 regulations.

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

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

23 “(A) IN GENERAL.—For purposes of this  
 24 subsection, the term ‘majority U.S. shareholder  
 25 year’ means the taxable year (if any) which, on

each testing day, constituted the taxable year  
of—

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

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

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

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

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

(14) Clause (ii) of section 904(d)(2)(A) is  
amended to read as follows:

“(ii) CERTAIN AMOUNTS INCLUDED.—  
Except as provided in clause (iii), the term  
‘passive income’ includes, except as pro-  
vided in subparagraph (E)(iii) or para-  
graph (3)(I), any amount includible in  
gross income under section 1293 (relating

1 to certain passive foreign investment com-  
2 panies).”

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

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

10 (16) Section 951 is amended by striking sub-  
11 sections (c) and (d) and by redesignating subsections  
12 (e) and (f) as subsections (c) and (d), respectively.

13 (17) Paragraph (3) of section 989(b) is amend-  
14 ed by striking “, 551(a),”.

15 (18) Paragraph (5) of section 1014(b) is  
16 amended by inserting “and before January 1,  
17 2005,” after “August 26, 1937,”.

18 (19) Subsection (a) of section 1016 is amended  
19 by striking paragraph (13).

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

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

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

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

5 (B) The amendment made by subparagraph (A)  
6 shall apply to taxable years beginning after Decem-  
7 ber 31, 2007.

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

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

15 (23) Paragraph (2) of section 1260(c) is  
16 amended by striking subparagraphs (H) and (I) and  
17 by redesignating subparagraph (J) as subparagraph  
18 (H).

19 (24)(A) Subparagraph (F) of section  
20 1291(b)(3) is amended by striking “551(d), 959(a),”  
21 and inserting “959(a)”.

22 (B) Subsection (e) of section 1291 is amended  
23 by inserting “(as in effect on the day before the date  
24 of the enactment of the PRO GROW USA Act of  
25 2003)” after “section 1246”.

1           (25) Paragraph (2) of section 1294(a) is  
2           amended to read as follows:

3           “(2) ELECTION NOT PERMITTED WHERE  
4           AMOUNTS OTHERWISE INCLUDIBLE UNDER SECTION  
5           951.—The taxpayer may not make an election under  
6           paragraph (1) with respect to the undistributed  
7           PFIC earnings tax liability attributable to a quali-  
8           fied electing fund for the taxable year if any amount  
9           is includible in the gross income of the taxpayer  
10          under section 951 with respect to such fund for such  
11          taxable year.”

12          (26) Section 6035 is hereby repealed.

13          (27) Subparagraph (D) of section 6103(e)(1) is  
14          amended by striking clause (iv) and redesignating  
15          clauses (v) and (vi) as clauses (iv) and (v), respec-  
16          tively.

17          (28) Subparagraph (B) of section 6501(e)(1) is  
18          amended to read as follows:

19               “(B) CONSTRUCTIVE DIVIDENDS.—If the  
20               taxpayer omits from gross income an amount  
21               properly includible therein under section  
22               951(a), the tax may be assessed, or a pro-  
23               ceeding in court for the collection of such tax  
24               may be done without assessing, at any time  
25               within 6 years after the return was filed.”



1           (29) Subsection (a) of section 6679 is amend-  
2       ed—

3                   (A) by striking “6035, 6046, and 6046A”  
4           in paragraph (1) and inserting “6046 and  
5           6046A”, and

6                   (B) by striking paragraph (3).

7           (30) Sections 170(f)(10)(A), 508(d), 4947, and  
8       4948(c)(4) are each amended by striking  
9       “556(b)(2),” each place it appears.

10          (31) The table of parts for subchapter G of  
11       chapter 1 is amended by striking the item relating  
12       to part III.

13          (32) The table of sections for part IV of sub-  
14       chapter P of chapter 1 is amended by striking the  
15       items relating to sections 1246 and 1247.

16          (33) The table of sections for subpart A of part  
17       III of subchapter A of chapter 61 is amended by  
18       striking the item relating to section 6035.

19       **SEC. 205. CLARIFICATION OF TREATMENT OF PIPELINE**  
20                   **TRANSPORTATION INCOME.**

21       Section 954(g)(1) (defining foreign base company oil  
22       related income) is amended by striking “or” at the end  
23       of subparagraph (A), by striking the period at the end  
24       of subparagraph (B) and inserting “, or”, and by inserting  
25       after subparagraph (B) the following new subparagraph:

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

3 **SEC. 206. PERMANENT EXTENSION AND MODIFICATION OF**  
4 **SUBPART F EXEMPTION FOR ACTIVE FINANC-**  
5 **ING.**

6 (a) PERMANENT EXTENSION.—

7 (1) EXEMPT INSURANCE INCOME.—Section  
8 953(e)(10) is amended—

9 (A) by striking “, and before January 1,  
10 2007,” and

11 (B) by striking the second sentence.

12 (2) FOREIGN PERSONAL HOLDING COMPANY IN-  
13 COME.—Section 954(h)(9) is amended by striking “,  
14 and before January 1, 2007,”.

15 (b) DIRECT CONDUCT OF ACTIVITIES.—Section  
16 954(h)(3) is amended by adding at the end the following:

17 “(E) DIRECT CONDUCT OF ACTIVITIES.—

18 For purposes of subparagraph (A)(ii)(II), an  
19 activity shall be treated as conducted directly by  
20 an eligible controlled foreign corporation or  
21 qualified business unit in its home country if  
22 the activity is performed by employees of a re-  
23 lated person and—

24 “(i) the related person is an eligible  
25 controlled foreign corporation the home

country of which is the same as the home country of the corporation or unit to which subparagraph (A)(ii)(II) is being applied,

“(ii) the activity is performed in the home country of the related person, and

“(iii) the related person is compensated on an arm’s-length basis for the performance of the activity by its employees and such compensation is treated as earned by such person in its home country for purposes of the home country’s tax laws.”

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

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

(b) TECHNICAL AMENDMENTS.—

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

(2) Clause (i) of section 881(c)(5)(A) is amended by striking “\$1,000,000” and inserting “\$5,000,000”.

1 **SEC. 208. MODIFICATION OF INTERACTION BETWEEN SUB-**  
 2 **PART F AND PASSIVE FOREIGN INVESTMENT**  
 3 **COMPANY RULES.**

4 (a) LIMITATION ON EXCEPTION FROM PFIC RULES  
 5 FOR UNITED STATES SHAREHOLDERS OF CONTROLLED  
 6 FOREIGN CORPORATIONS.—Paragraph (2) of section  
 7 1297(e) (relating to passive investment company) is  
 8 amended by adding at the end the following flush sen-  
 9 tence:

10 “Such term shall not include any period if the  
 11 earning of subpart F income by such corpora-  
 12 tion during such period would only result in a  
 13 remote likelihood of an inclusion in gross in-  
 14 come under section 951(a)(1)(A)(i).”

15 (b) EFFECTIVE DATE.—The amendment made by  
 16 this section shall apply to taxable years of controlled for-  
 17 eign corporations beginning after December 31, 2003, and  
 18 to taxable years of United States shareholders in which  
 19 or with which such taxable years of controlled foreign cor-  
 20 porations end.

21 **SEC. 209. DETERMINATION OF FOREIGN PERSONAL HOLD-**  
 22 **ING COMPANY INCOME WITH RESPECT TO**  
 23 **TRANSACTIONS IN COMMODITIES.**

24 (a) IN GENERAL.—Clauses (i) and (ii) of section  
 25 954(c)(1)(C) (relating to commodity transactions) are  
 26 amended to read as follows:

1 “(i) arise out of commodity hedging  
 2 transactions (as defined in paragraph  
 3 (6)(A)),

4 “(ii) are active business gains or  
 5 losses from the sale of commodities, but  
 6 only if substantially all of the controlled  
 7 foreign corporation’s commodities are  
 8 property described in paragraph (1), (2),  
 9 or (8) of section 1221(a), or”.

10 (b) DEFINITION AND SPECIAL RULES.—Subsection  
 11 (c) of section 954, as amended by sections 202 and 203,  
 12 is amended by adding at the end the following new para-  
 13 graph:

14 “(6) DEFINITION AND SPECIAL RULES RELAT-  
 15 ING TO COMMODITY TRANSACTIONS.—

16 “(A) COMMODITY HEDGING TRANS-  
 17 ACTIONS.—For purposes of paragraph  
 18 (1)(C)(i), the term ‘commodity hedging trans-  
 19 action’ means any transaction with respect to a  
 20 commodity if such transaction—

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

23 “(I) without regard to subpara-  
 24 graph (A)(ii) thereof,

1 “(II) by applying subparagraph  
 2 (A)(i) thereof by substituting ‘ordi-  
 3 nary property or property described in  
 4 section 1231(b)’ for ‘ordinary prop-  
 5 erty’, and

6 “(III) by substituting ‘controlled  
 7 foreign corporation’ for ‘taxpayer’  
 8 each place it appears, and

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

11 “(B) REGULATIONS.—The Secretary shall  
 12 prescribe such regulations as are appropriate to  
 13 carry out the purposes of paragraph (1)(C) in  
 14 the case of transactions involving related per-  
 15 sons.”

16 (c) EFFECTIVE DATE.—The amendments made by  
 17 this section shall apply to transactions entered into after  
 18 December 31, 2004.

19 **SEC. 210. REPEAL OF FOREIGN BASE COMPANY SHIPPING**  
 20 **INCOME RULES.**

21 (a) ELIMINATION OF FOREIGN BASE COMPANY SHIP-  
 22 PING INCOME.—Section 954 (relating to foreign base com-  
 23 pany income) is amended—

1 (1) in subsection (a), by striking paragraph (4)  
 2 and by redesignating paragraph (5) as paragraph  
 3 (4), and

4 (2) by striking subsection (f) (relating to for-  
 5 eign base company shipping income).

6 (b) ACTIVE LEASING INCOME FROM AIRCRAFT AND  
 7 VESSELS.—

8 (1) IN GENERAL.—Section 954(c)(2) is amend-  
 9 ed by adding at the end the following new subpara-  
 10 graph:

11 “(D) CERTAIN RENTS, ETC.—

12 “(i) IN GENERAL.—Foreign personal  
 13 holding company income shall not include  
 14 qualified leasing income derived from or in  
 15 connection with the leasing or rental of  
 16 any aircraft or vessel.

17 “(ii) QUALIFIED LEASING INCOME.—  
 18 For purposes of this subparagraph, the  
 19 term ‘qualified leasing income’ means rents  
 20 and gains derived in the active conduct of  
 21 a trade or business of leasing with respect  
 22 to which the controlled foreign corporation  
 23 conducts substantial activity, but only if—

24 “(I) the leased property is used  
 25 by the lessee or other end-user in for-

1                   eign commerce and predominantly  
2                   outside the United States, and

3                   “(II) the lessee or other end-user  
4                   is not a related person (as defined in  
5                   subsection (d)(3)).

6                   Any amount not treated as foreign per-  
7                   sonal holding income under this subpara-  
8                   graph shall not be treated as foreign base  
9                   company income under any other provision  
10                  of this section.”

11               (2)     CONFORMING     AMENDMENT.—Section  
12               954(c)(1)(B) is amended by inserting “or (2)(D)”  
13               after “paragraph (2)(A)”.

14               (c) CONFORMING AMENDMENTS.—

15               (1)     Section 952(c)(1)(B)(iii) is amended by  
16               striking subclause (I) and redesignating subclauses  
17               (II) through (VI) as subclauses (I) through (V), re-  
18               spectively.

19               (2)     Subsection (b) of section 954 is amended—

20                   (A) by striking “the foreign base shipping  
21                   income,” in paragraph (5),

22                   (B) by striking paragraphs (6) and (7),  
23                   and

24                   (C) by redesignating paragraph (8) as  
25                   paragraph (6).



1 (d) EFFECTIVE DATE.—The amendments made by  
 2 this section shall apply to taxable years of foreign corpora-  
 3 tions beginning after December 31, 2005, and to taxable  
 4 years of United States shareholders with or within which  
 5 such taxable years of foreign corporations end.

6 **SEC. 211. REDUCED TAX ON REPATRIATED EARNINGS PRE-**  
 7 **VIOUSLY EXEMPT FROM TAX UNDER SUB-**  
 8 **PART F.**

9 (a) IN GENERAL.—Subpart F of part III of sub-  
 10 chapter N of chapter 1 is amended by adding at the end  
 11 the following new section:

12 **“SEC. 965. REDUCED TAX ON REPATRIATED EARNINGS PRE-**  
 13 **VIOUSLY EXEMPT FROM TAX.**

14 “(a) IN GENERAL.—If a corporation which is a  
 15 United States shareholder elects the application of this  
 16 section, a tax shall be imposed on the taxpayer in an  
 17 amount equal to the applicable percentage of—

18 “(1) the taxpayer’s qualified foreign distribu-  
 19 tion amount, and

20 “(2) the amount determined under section 78  
 21 which is attributable to the qualified foreign dis-  
 22 tribution amount.

23 Such tax shall be imposed in lieu of the tax imposed under  
 24 section 11 or 55 on the amounts described in paragraphs  
 25 (1) and (2) for such taxable year. For purposes of this

1 subsection, the applicable percentage for any taxable year  
 2 is the percentage equal to 15 percent of the highest rate  
 3 of tax in effect under section 11(b) for the taxable year.

4 “(b) QUALIFIED FOREIGN DISTRIBUTION  
 5 AMOUNT.—For purposes of this section—

6 “(1) IN GENERAL.—The term ‘qualified foreign  
 7 distribution amount’ means the lesser of—

8 “(A) the aggregate dividends received by  
 9 the taxpayer during the taxable year which are  
 10 from 1 or more corporations which are con-  
 11 trolled foreign corporations in which the tax-  
 12 payer is a United States shareholder on the  
 13 date such dividends are paid, or

14 “(B) the amount designated by the tax-  
 15 payer under subsection (c)(6).

16 “(2) LIMITATION BASED ON QUALIFIED INNO-  
 17 VATION SPENDING.—

18 “(A) IN GENERAL.—The qualified foreign  
 19 distribution amount for any taxable year shall  
 20 not exceed the excess (if any) of—

21 “(i) the qualified innovation expenses  
 22 of the taxpayer for the taxable year, over

23 “(ii) the base innovation expense  
 24 amount.

“(B) QUALIFIED INNOVATION EXPENSES.—For purposes of this paragraph, the term ‘qualified innovation expenses’ means the sum of the following amounts for the taxable year:

“(i) Qualified research expenses taken into account in determining the credit determined under section 41 for the taxable year.

“(ii) The aggregate adjusted bases of all property placed in service during the taxable year to which section 168(k) applies.

“(C) BASE INNOVATION EXPENSE AMOUNT.—For purposes of this paragraph, the base innovation expense amount is 85 percent of the average of the taxpayer’s qualified innovation expenses during the base period.

“(3) BASE PERIOD.—

“(A) IN GENERAL.—The term ‘base period’ means, with respect to any taxable year, the 3-taxable-year period ending with the taxable year preceding the taxable year.

“(B) SHORTER PERIOD.—If the taxpayer has fewer than 3 taxable years immediately pre-

1           ceding the taxable year, then in lieu of applying  
2           subparagraph (A), the base period shall include  
3           all preceding taxable years of the taxpayer.

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

6           “(1) DIVIDENDS.—The term ‘dividend’ has the  
7 meaning given such term by section 316, except that  
8 such term shall not include amounts described in  
9 sections 78 and 959.

10          “(2) FOREIGN TAX CREDITS AND DEDUC-  
11 TIONS.—The amount of any income, war, profits, or  
12 excess profit taxes paid (or deemed paid under sec-  
13 tions 902 and 960) or accrued by the taxpayer with  
14 respect to the qualified foreign distribution amount  
15 for which a credit would be allowable under section  
16 901 without regard to this section shall be reduced  
17 by 85 percent. No deduction shall be allowed under  
18 this chapter for the portion of any tax for which  
19 credit is not allowable by reason of the preceding  
20 sentence.

21          “(3) FOREIGN TAX CREDIT LIMITATION.—For  
22 purposes of section 904, there shall be disregarded  
23 85 percent of—

24               “(A) the qualified foreign distribution  
25 amount,

1           “(B) the amount determined under section  
2           78 which is attributable to such qualified for-  
3           eign distribution amount, and

4           “(C) the amounts (including assets, gross  
5           income, and other relevant bases of apportion-  
6           ment) which are attributable to the qualified  
7           foreign distribution amount which would, deter-  
8           mined without regard to this section, be used to  
9           apportion the expenses, losses, and deductions  
10          of the taxpayer under section 861 and 864 in  
11          determining its taxable income from sources  
12          without the United States.

13          For purposes of applying subparagraph (C), the  
14          principles of section 864(e)(3)(A) shall apply.

15          “(4) TREATMENT OF ACQUISITIONS AND DIS-  
16          POSITIONS.—Rules similar to the rules of section  
17          41(f)(3) shall apply in the case of acquisitions or  
18          dispositions of controlled foreign corporations occur-  
19          ring on or after the first day of the earliest taxable  
20          year taken into account in determining the base pe-  
21          riod.

22          “(5) TREATMENT OF CONSOLIDATED  
23          GROUPS.—Members of an affiliated group of cor-  
24          porations filing a consolidated return under section

1       1501 shall be treated as a single taxpayer for pur-  
2       poses of this section.

3               “(6) DESIGNATION OF DIVIDENDS.—For pur-  
4       poses of subsection (b)(1)(B), the taxpayer may des-  
5       ignate the particular dividends received during the  
6       taxable year from 1 or more corporations which are  
7       controlled foreign corporations in which the taxpayer  
8       is a United States shareholder on the date the divi-  
9       dends are paid which are to be treated as the tax-  
10      payer’s qualified foreign distribution amount.

11              “(7) TREATMENT OF EXPENSES, LOSSES, AND  
12      DEDUCTIONS AND CREDITS.—

13              “(A) EXPENSES, LOSSES, AND DEDUC-  
14      TIONS.—Any expenses, losses, or deductions of  
15      the taxpayer allowable under subchapter B—

16              “(i) shall not be applied to reduce any  
17              amount described in subsection (a) (1) or  
18              (2), and

19              “(ii) shall be applied to reduce other  
20              income of the taxpayer (determined with-  
21              out regard to any amount described in sub-  
22              section (a) (1) or (2)).

23              “(B) DENIAL OF CREDIT.—No credit shall  
24      be allowed under this chapter against the tax  
25      imposed by subsection (a).

1           “(8) TRANSITION RULE FOR 2004 FOR LOOK-  
 2           THRU ON DIVIDENDS.—For purposes of this section,  
 3           a United States shareholder shall be treated for pur-  
 4           poses of this section as having received a dividend  
 5           from a controlled foreign corporation to the extent  
 6           of any amount included in gross income by such  
 7           shareholder under section 951(a)(1)(A) as a result  
 8           of any dividend paid during any taxable year of such  
 9           corporation beginning in 2004 to—

10                   “(A) such corporation from another con-  
 11                   trolled foreign corporation which is in a chain  
 12                   of ownerships described in section 958(a), or

13                   “(B) any other controlled foreign corpora-  
 14                   tion in such chain of ownership, but only to the  
 15                   extent of distributions described in section  
 16                   959(b) which are made during such taxable  
 17                   year to the controlled foreign corporation from  
 18                   which such shareholder received such dividend.

19           “(d) ELECTION.—

20                   “(1) IN GENERAL.—An election under this sec-  
 21                   tion for any taxable year shall be made no later than  
 22                   the due date for the taxpayer’s income tax return for  
 23                   the taxable year (determined by taking extensions  
 24                   into account) and shall be included on such return.

1       Such election, once made, may be revoked only with  
2       the consent of the Secretary.

3               “(2) ALL CONTROLLED FOREIGN CORPORA-  
4       TIONS.—An election under paragraph (1) shall apply  
5       to all corporations which are controlled foreign cor-  
6       porations in which the taxpayer is a United States  
7       shareholder during the taxable year.

8               “(3) CONSOLIDATED GROUPS.—If a taxpayer is  
9       a member of an affiliated group of corporations fil-  
10      ing a consolidated return under section 1501 for the  
11      taxable year, an election under this section shall be  
12      made by the common parent of the affiliated group  
13      which includes the taxpayer and shall apply to all  
14      members of the affiliated group.

15              “(e) REGULATIONS.—The Secretary shall prescribe  
16      such regulations as may be necessary or appropriate to  
17      carry out the purposes of this section, including regula-  
18      tions relating to the application of section 55 and regula-  
19      tions addressing corporations which, during the base pe-  
20      riod or thereafter, join or leave an affiliated group of cor-  
21      porations filing a consolidated return.”

22              (b) CONFORMING AMENDMENT.—The table of sec-  
23      tions for subpart F of part III of subchapter N of chapter  
24      1 is amended by adding at the end the following new item:

“Sec. 965. Reduced tax on repatriated earnings previously exempt  
from tax.”



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

4 **SEC. 212. EFFECTIVE DATE.**

5 Except as otherwise provided in this subtitle, the  
 6 amendments made by this subtitle shall apply to taxable  
 7 years of foreign corporations beginning after December  
 8 31, 2004, and to taxable years of United States share-  
 9 holders with or within which such taxable years of foreign  
 10 corporations end.

11 **Subtitle B—Provisions Relating to**  
 12 **Foreign Tax Credit**

13 **SEC. 221. INTEREST EXPENSE ALLOCATION RULES.**

14 (a) ELECTION TO ALLOCATE ON WORLDWIDE  
 15 BASIS.—Section 864 is amended by redesignating sub-  
 16 section (f) as subsection (g) and by inserting after sub-  
 17 section (e) the following new subsection:

18 “(f) ELECTION TO ALLOCATE INTEREST, ETC. ON  
 19 WORLDWIDE BASIS.—For purposes of this subchapter, at  
 20 the election of the worldwide affiliated group—

21 “(1) ALLOCATION AND APPORTIONMENT OF IN-  
 22 TEREST EXPENSE.—

23 “(A) IN GENERAL.—The taxable income of  
 24 each domestic corporation which is a member of  
 25 a worldwide affiliated group shall be determined

1 by allocating and apportioning interest expense  
2 of each member as if all members of such group  
3 were a single corporation.

4 “(B) TREATMENT OF WORLDWIDE AFFILI-  
5 ATED GROUP.—The taxable income of the do-  
6 mestic members of a worldwide affiliated group  
7 from sources outside the United States shall be  
8 determined by allocating and apportioning the  
9 interest expense of such domestic members to  
10 such income in an amount equal to the excess  
11 (if any) of—

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

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

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

3 “(C) WORLDWIDE AFFILIATED GROUP.—  
4 For purposes of this paragraph, the term  
5 ‘worldwide affiliated group’ means a group con-  
6 sisting of—

7 “(i) the includible members of an af-  
8 filiated group (as defined in section  
9 1504(a), determined without regard to  
10 paragraphs (2) and (4) of section  
11 1504(b)), and

12 “(ii) all controlled foreign corpora-  
13 tions in which such members in the aggre-  
14 gate meet the ownership requirements of  
15 section 1504(a)(2) either directly or indi-  
16 rectly through applying paragraph (2) of  
17 section 958(a) or through applying rules  
18 similar to the rules of such paragraph to  
19 stock owned directly or indirectly by do-  
20 mestic partnerships, trusts, or estates.

21 “(2) ALLOCATION AND APPORTIONMENT OF  
22 OTHER EXPENSES.—Expenses other than interest  
23 which are not directly allocable or apportioned to  
24 any specific income producing activity shall be allo-  
25 cated and apportioned as if all members of the affili-

ated group were a single corporation. For purposes of the preceding sentence, the term ‘affiliated group’ has the meaning given such term by section 1504 (determined without regard to paragraph (4) of section 1504(b)).

“(3) TREATMENT OF TAX-EXEMPT ASSETS; BASIS OF STOCK IN NONAFFILIATED 10-PERCENT OWNED CORPORATIONS.—The rules of paragraphs (3) and (4) of subsection (e) shall apply for purposes of this subsection, except that paragraph (4) shall be applied on worldwide affiliated group basis.

“(4) TREATMENT OF CERTAIN FINANCIAL INSTITUTIONS.—

“(A) IN GENERAL.—For purposes of paragraph (1), any corporation described in subparagraph (B) shall be treated as an includible corporation for purposes of section 1504 only for purposes of applying this subsection separately to corporations so described.

“(B) DESCRIPTION.—A corporation is described in this subparagraph if—

“(i) such corporation is a financial institution described in section 581 or 591,

“(ii) the business of such financial institution is predominantly with persons

other than related persons (within the meaning of subsection (d)(4)) or their customers, and

“(iii) such financial institution is required by State or Federal law to be operated separately from any other entity which is not such an institution.

“(C) TREATMENT OF BANK HOLDING COMPANIES.—To the extent provided in regulations—

“(i) a bank holding company (within the meaning of section 2(a) of the Bank Holding Company Act of 1956), and

“(ii) any subsidiary of a financial institution described in section 581 or 591 or of any bank holding company if such subsidiary is predominantly engaged (directly or indirectly) in the active conduct of a banking, financing, or similar business, shall be treated as a corporation described in subparagraph (B).

“(5) ELECTION TO EXPAND FINANCIAL INSTITUTION GROUP OF WORLDWIDE GROUP.—

1           “(A) IN GENERAL.—If a worldwide affi-  
 2           lated group elects the application of this sub-  
 3           section, all financial corporations which—

4                   “(i) are members of such worldwide  
 5                   affiliated group, but

6                   “(ii) are not corporations described in  
 7                   paragraph (4)(B),  
 8           shall be treated as described in paragraph  
 9           (4)(B) for purposes of applying paragraph  
 10          (4)(A). This subsection (other than this para-  
 11          graph) shall apply to any such group in the  
 12          same manner as this subsection (other than this  
 13          paragraph) applies to the pre-election worldwide  
 14          affiliated group of which such group is a part.

15          “(B) FINANCIAL CORPORATION.—For pur-  
 16          poses of this paragraph, the term ‘financial cor-  
 17          poration’ means any corporation if at least 80  
 18          percent of its gross income is income described  
 19          in section 904(d)(2)(D)(ii) and the regulations  
 20          thereunder which is derived from transactions  
 21          with persons who are not related (within the  
 22          meaning of section 267(b) or 707(b)(1)) to the  
 23          corporation. For purposes of the preceding sen-  
 24          tence, there shall be disregarded any item of in-  
 25          come or gain from a transaction or series of

1 transactions a principal purpose of which is the  
 2 qualification of any corporation as a financial  
 3 corporation.

4 “(C) ANTIABUSE RULES.—In the case of a  
 5 corporation which is a member of an electing fi-  
 6 nancial institution group, to the extent that  
 7 such corporation—

8 “(i) distributes dividends or makes  
 9 other distributions with respect to its stock  
 10 after the date of the enactment of this  
 11 paragraph to any member of the pre-elec-  
 12 tion worldwide affiliated group (other than  
 13 to a member of the electing financial insti-  
 14 tution group) in excess of the greater of—

15 “(I) its average annual dividend  
 16 (expressed as a percentage of current  
 17 earnings and profits) during the 5-  
 18 taxable-year period ending with the  
 19 taxable year preceding the taxable  
 20 year, or

21 “(II) 25 percent of its average  
 22 annual earnings and profits for such  
 23 5-taxable-year period, or

24 “(ii) deals with any person in any  
 25 manner not clearly reflecting the income of

1           the corporation (as determined under prin-  
2           ciples similar to the principles of section  
3           482),

4           an amount of indebtedness of the electing fi-  
5           nancial institution group equal to the excess  
6           distribution or the understatement or overstate-  
7           ment of income, as the case may be, shall be re-  
8           characterized (for the taxable year and subse-  
9           quent taxable years) for purposes of this para-  
10          graph as indebtedness of the worldwide affili-  
11          ated group (excluding the electing financial in-  
12          stitution group). If a corporation has not been  
13          in existence for 5 taxable years, this subpara-  
14          graph shall be applied with respect to the pe-  
15          riod it was in existence.

16               “(D) ELECTION.—An election under this  
17          paragraph with respect to any financial institu-  
18          tion group may be made only by the common  
19          parent of the pre-election worldwide affiliated  
20          group and may be made only for the first tax-  
21          able year beginning after December 31, 2005,  
22          in which such affiliated group includes 1 or  
23          more financial corporations. Such an election,  
24          once made, shall apply to all financial corpora-  
25          tions which are members of the electing finan-



1           cial institution group for such taxable year and  
 2           all subsequent years unless revoked with the  
 3           consent of the Secretary.

4           “(E)     DEFINITIONS     RELATING     TO  
 5           GROUPS.—For purposes of this paragraph—

6                     “(i) PRE-ELECTION WORLDWIDE AF-  
 7                     FILIATED GROUP.—The term ‘pre-election  
 8                     worldwide affiliated group’ means, with re-  
 9                     spect to a corporation, the worldwide affili-  
 10                    ated group of which such corporation  
 11                    would (but for an election under this para-  
 12                    graph) be a member for purposes of apply-  
 13                    ing paragraph (1).

14                   “(ii) ELECTING FINANCIAL INSTITU-  
 15                    TION GROUP.—The term ‘electing financial  
 16                    institution group’ means the group of cor-  
 17                    porations to which this subsection applies  
 18                    separately by reason of the application of  
 19                    paragraph (4)(A) and which includes fi-  
 20                    nancial corporations by reason of an elec-  
 21                    tion under subparagraph (A).

22           “(F) REGULATIONS.—The Secretary shall  
 23           prescribe such regulations as may be appro-  
 24           priate to carry out this subsection, including  
 25           regulations—

1 “(i) providing for the direct allocation  
2 of interest expense in other circumstances  
3 where such allocation would be appropriate  
4 to carry out the purposes of this sub-  
5 section,

6 “(ii) preventing assets or interest ex-  
7 pense from being taken into account more  
8 than once, and

9 “(iii) dealing with changes in mem-  
10 bers of any group (through acquisitions or  
11 otherwise) treated under this paragraph as  
12 an affiliated group for purposes of this  
13 subsection.

14 “(6) ELECTION.—An election to have this sub-  
15 section apply with respect to any worldwide affiliated  
16 group may be made only by the common parent of  
17 the domestic affiliated group referred to in para-  
18 graph (1)(C) and may be made only for the first  
19 taxable year beginning after December 31, 2005, in  
20 which a worldwide affiliated group exists which in-  
21 cludes such affiliated group and at least one foreign  
22 corporation. Such an election, once made, shall apply  
23 to such common parent and all other corporations  
24 which are members of such worldwide affiliated

1 group for such taxable year and all subsequent years  
 2 unless revoked with the consent of the Secretary.”.

3 (b) EXPANSION OF REGULATORY AUTHORITY.—

4 Paragraph (7) of section 864(e) is amended—

5 (1) by inserting before the comma at the end of  
 6 subparagraph (B) “and in other circumstances  
 7 where such allocation would be appropriate to carry  
 8 out the purposes of this subsection”, and

9 (2) by striking “and” at the end of subpara-  
 10 graph (E), by redesignating subparagraph (F) as  
 11 subparagraph (G), and by inserting after subpara-  
 12 graph (E) the following new subparagraph:

13 “(F) preventing assets or interest expense  
 14 from being taken into account more than once,  
 15 and”.

16 (c) EFFECTIVE DATE.—The amendments made by  
 17 this section shall apply to taxable years beginning after  
 18 December 31, 2005.

19 **SEC. 222. EXTENSION OF PERIOD TO WHICH EXCESS FOR-**  
 20 **EIGN TAXES MAY BE CARRIED.**

21 (a) GENERAL RULE.—Section 904(c) (relating to  
 22 carryback and carryover of excess tax paid) is amended  
 23 by striking “in the first, second, third, fourth, or fifth”  
 24 and inserting “in any of the first 20”.

1 (b) EXCESS EXTRACTION TAXES.—Paragraph (1) of  
 2 section 907(f) is amended by striking “in the first, second,  
 3 third, fourth, or fifth” and inserting “in any of the first  
 4 20”.

5 (c) EFFECTIVE DATE.—The amendments made by  
 6 this section shall apply to excess foreign taxes arising in  
 7 taxable years beginning after December 31, 2003.

8 **SEC. 223. ORDERING RULES FOR FOREIGN TAX CREDIT**  
 9 **CARRYFORWARDS.**

10 (a) IN GENERAL.—Section 904(c) (relating to  
 11 carryback and carryover of excess tax paid), as amended  
 12 by section 222, is amended to read as follows:

13 “(c) CARRYBACK AND CARRYFORWARD OF EXCESS  
 14 TAX PAID.—

15 “(1) IN GENERAL.—If, for any taxable year for  
 16 which the taxpayer elects to have the benefits of this  
 17 subpart apply, the sum of—

18 “(A) the foreign tax credit carryforwards  
 19 under this subsection to a taxable year, plus

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

22 exceeds the limitation under subsection (a), such ex-  
 23 cess (to the extent attributable to the taxes de-  
 24 scribed in subparagraph (B)) shall be a foreign tax  
 25 credit carryback to each of the 2 preceding taxable

1 years and a foreign tax credit carryforward to each  
 2 of the 20 following taxable years.

3 “(2) AMOUNTS CARRIED TO EARLIEST  
 4 YEARS.—The excess described in paragraph (1) for  
 5 any taxable year shall be carried to the earliest of  
 6 the 22 taxable years to which (by reason of para-  
 7 graph (1)) such excess may be carried. The amount  
 8 of such excess shall be carried to each of the other  
 9 21 taxable years to the extent that such excess may  
 10 not be taken into account under subsection (a) for  
 11 a prior taxable year because of the limitations of  
 12 paragraph (4).

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

20 “(4) LIMITATIONS.—

21 “(A) CARRYBACKS USED LAST.—The ex-  
 22 cess described in paragraph (1) for any taxable  
 23 year (in this paragraph referred to as the ‘cur-  
 24 rent taxable year’) which is carried to any pre-  
 25 ceding taxable year shall not exceed the amount

1 by which the limitation under subsection (a) for  
2 such preceding taxable year exceeds the sum  
3 of—

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

6 “(ii) the amount of the foreign taxes  
7 paid or accrued for any taxable year earlier  
8 than the current taxable year which have  
9 been carried to such preceding taxable  
10 year.

11 “(B) CARRYFORWARDS USED FIRST.—The  
12 excess described in paragraph (1) for a taxable  
13 year which is carried to any succeeding taxable  
14 year shall not exceed the amount by which the  
15 limitation under subsection (a) for such suc-  
16 ceeding taxable year exceeds the sum of the  
17 amounts which, by reason of this subsection,  
18 are carried to such succeeding taxable year and  
19 are attributable to taxable years preceding the  
20 taxable year of such excess.

21 “(C) CREDIT ONLY.—The excess described  
22 in paragraph (1) may be carried to a taxable  
23 year under this subsection only if the taxpayer  
24 elects to have the benefits of this subpart apply  
25 to foreign taxes paid or accrued for such tax-

1           able year. Any amount so carried may be al-  
2           lowed only as a credit and not a deduction.

3           “(5) TREATMENT OF AMOUNTS CARRIED BACK  
4           OR FORWARD.—The amount of any foreign tax  
5           carryback or foreign tax carryforward to a taxable  
6           year under this subsection shall, for purposes of sec-  
7           tion 901, be treated as foreign taxes paid or accrued  
8           in such year.

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

13          (b) EFFECTIVE DATE.—The amendment made by  
14          this section shall apply to taxes paid or accrued for taxable  
15          years beginning after December 31, 2003, and to  
16          carryforwards of taxes from taxable years beginning after  
17          December 31, 1997.

18       **SEC. 224. REPEAL OF LIMITATION OF FOREIGN TAX CREDIT**

19                       **UNDER ALTERNATIVE MINIMUM TAX.**

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

1           (b)           CONFORMING           AMENDMENT.—Section  
 2 53(d)(1)(B)(i)(II) is amended by striking “and if section  
 3 59(a)(2) did not apply”.

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

7 **SEC. 225. LOOK-THRU RULES TO APPLY TO DIVIDENDS**  
 8 **FROM NONCONTROLLED SECTION 902 COR-**  
 9 **PORATIONS.**

10          (a) IN GENERAL.—Paragraph (4) of section 904(d)  
 11 (relating to separate application of section with respect to  
 12 certain categories of income) is amended to read as fol-  
 13 lows:

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

16                   “(A) IN GENERAL.—For purposes of this  
 17 subsection, any dividend from a noncontrolled  
 18 section 902 corporation with respect to the tax-  
 19 payer shall be treated as income in a separate  
 20 category in proportion to the ratio of—

21                           “(i) the portion of earnings and prof-  
 22 its attributable to income in such category,  
 23 to

24                           “(ii) the total amount of earnings and  
 25 profits.



1           “(B) EARNINGS AND PROFITS OF CON-  
 2           TROLLED FOREIGN CORPORATIONS.—In the  
 3           case of any distribution from a controlled for-  
 4           eign corporation to a United States share-  
 5           holder, rules similar to the rules of subpara-  
 6           graph (A) shall apply in determining the extent  
 7           to which earnings and profits of the controlled  
 8           foreign corporation which are attributable to a  
 9           noncontrolled section 902 corporation may be  
 10          treated as income in a separate category.

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

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

15                   “(ii) EARNINGS AND PROFITS.—

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

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

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

9 “(iv) LOOK-THRU WITH RESPECT TO  
 10 CARRYFORWARDS OF CREDIT.—Rules simi-  
 11 lar to the rules of subparagraph (A) shall  
 12 apply to any carryforward under sub-  
 13 section (c) from a taxable year beginning  
 14 before January 1, 2003, of tax allocable to  
 15 a dividend from a noncontrolled section  
 16 902 corporation with respect to the tax-  
 17 payer.”.

18 (b) CONFORMING AMENDMENTS.—

19 (1) Subparagraph (E) of section 904(d)(1) is  
 20 hereby repealed.

21 (2) Section 904(d)(2)(C)(iii) is amended by  
 22 striking subclause (II) and by redesignating sub-  
 23 clause (III) as subclause (II).

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

4           (4) Section 904(d)(2)(E) is amended—  
 5                   (A) by inserting “or (4)” after “paragraph  
 6           (3)” in clause (i), and

7                   (B) by striking clauses (ii) and (iv) and by  
 8           redesignating clause (iii) as clause (ii).

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

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

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

16   **SEC. 226. REDUCTION TO 2 FOREIGN TAX CREDIT BASKETS.**

17          (a) IN GENERAL.—Paragraph (1) of section 904(d)  
 18          (relating to separate application of section with respect to  
 19          certain categories of income), as amended by section 225,  
 20          is amended to read as follows:

21               “(1) IN GENERAL.—The provisions of sub-  
 22          sections (a), (b), and (c) and sections 902, 907, and  
 23          960 shall be applied separately with respect to—

24                   “(A) typically low-taxed income, and

25                   “(B) general category income.”

1 (b) CATEGORIES.—Paragraph (2) of section 904(d),  
 2 as amended by section 204(c)(14), is amended by striking  
 3 subparagraph (B), by redesignating subparagraph (A) as  
 4 subparagraph (B), and by inserting before subparagraph  
 5 (B) (as so redesignated) the following new subparagraph:

6 “(A) CATEGORIES.—

7 “(i) TYPICALLY LOW-TAXED IN-  
 8 COME.—The term ‘typically low-taxed in-  
 9 come’ means passive income and specified  
 10 typically low-taxed income.

11 “(ii) GENERAL CATEGORY INCOME.—  
 12 The term ‘general category income’ means  
 13 income other than typically low-taxed in-  
 14 come.”

15 (c) SPECIFIED TYPICALLY LOW-TAXED INCOME.—  
 16 Subparagraph (B) of section 904(d)(2), as redesignated  
 17 by subsection (b), is amended by adding at the end the  
 18 following new clause:

19 “(v) SPECIFIED TYPICALLY LOW-  
 20 TAXED INCOME.—The term ‘specified typi-  
 21 cally low-taxed income’ means—

22 “(I) dividends from a DISC or  
 23 former DISC (as defined in section  
 24 992(a)) to the extent such dividends

1 are treated as income from sources  
 2 without the United States,

3 “(II) taxable income attributable  
 4 to foreign trade income (within the  
 5 meaning of section 923(b)),

6 “(III) distributions from a FSC  
 7 (or a former FSC) out of earnings  
 8 and profits attributable to foreign  
 9 trade income (within the meaning of  
 10 section 923(b)) or interest or carrying  
 11 charges (as defined in section  
 12 927(d)(1)) derived from a transaction  
 13 which results in foreign trade income  
 14 (as defined in section 923(b)), and

15 “(IV) shipping income.”

16 (d) TREATMENT OF FINANCIAL SERVICES.—Para-  
 17 graph (2) of section 904(d) is amended by redesignating  
 18 subparagraphs (H) and (I) as subparagraphs (I) and (J)  
 19 and by inserting after subparagraph (G) the following new  
 20 subparagraph:

21 “(H) TREATMENT OF FINANCIAL SERVICES  
 22 INCOME AND COMPANIES.—

23 “(i) IN GENERAL.—Financial services  
 24 income shall be treated as general category  
 25 income in the case of—

1                   “(I) a member of a financial  
2 services group, and

3                   “(II) any other person if such  
4 person is predominantly engaged in  
5 the active conduct of a banking, insur-  
6 ance, financing, or similar business.

7                   “(ii) FINANCIAL SERVICES GROUP.—  
8 The term ‘financial services group’ means  
9 any affiliated group (as defined in section  
10 1504(a) without regard to paragraphs (2)  
11 and (3) of section 1504(b)) which is pre-  
12 dominantly engaged in the active conduct  
13 of a banking, insurance, financing, or simi-  
14 lar business. In determining whether such  
15 a group is so engaged, there shall be taken  
16 into account only the income of members  
17 of the group that are—

18                   “(I) United States corporations,  
19 or

20                   “(II) controlled foreign corpora-  
21 tions in which United States corpora-  
22 tions own, directly or indirectly, at  
23 least 80 percent of the total voting  
24 power and value of the stock.

1                   “(iii) PASS-THRU ENTITIES.—The  
 2                   Secretary shall by regulation specify for  
 3                   purposes of this subparagraph the treat-  
 4                   ment of financial services income received  
 5                   or accrued by partnerships and by other  
 6                   pass-thru entities which are not members  
 7                   of a financial services group.”

8                   (e) CONFORMING AMENDMENTS.—

9                   (1) Clause (iii) of section 904(d)(2)(B) (relating  
 10                  to exceptions from passive income), as redesignated  
 11                  by subsection (b), is amended by striking subclause  
 12                  (I) and by redesignating subclauses (II) and (III) as  
 13                  subclauses (I) and (II), respectively.

14                  (2) Clause (i) of section 904(d)(2)(C) (defining  
 15                  financial services income) is amended by adding  
 16                  “or” at the end of subclause (I) and by striking sub-  
 17                  clauses (II) and (III) and inserting the following  
 18                  new subclause:

19                                 “(II) passive income (determined  
 20                                 without regard to subparagraph  
 21                                 (B)(iii)(II)).”

22                  (3) Section 904(d)(2)(C) (defining financial  
 23                  services income), as amended by section 225(b)(2),  
 24                  is amended by striking clause (iii).

1           (4) Paragraph (3) of section 904(d), as amend-  
2       ed by section 225(b)(5), is amended to read as fol-  
3       lows:

4           “(3) LOOK-THRU IN CASE OF CONTROLLED  
5       FOREIGN CORPORATIONS.—

6           “(A) IN GENERAL.—Except as otherwise  
7       provided in this paragraph, dividends, interest,  
8       rents, and royalties received or accrued by the  
9       taxpayer from a controlled foreign corporation  
10      in which the taxpayer is a United States share-  
11      holder shall not be treated as typically low-  
12      taxed income.

13          “(B) SUBPART F INCLUSIONS.—Any  
14      amount included in gross income under section  
15      951(a)(1)(A) shall be treated as typically low-  
16      taxed income to the extent the amount so in-  
17      cluded is attributable to typically low-taxed in-  
18      come.

19          “(C) INTEREST, RENTS, AND ROYAL-  
20      TIES.—Any interest, rent, or royalty which is  
21      received or accrued from a controlled foreign  
22      corporation in which the taxpayer is a United  
23      States shareholder shall be treated as typically  
24      low-taxed income to the extent it is properly al-  
25      locable (under regulations prescribed by the



1 Secretary) to typically low-taxed income of the  
2 controlled foreign corporation.

3 “(D) DIVIDENDS.—Any dividend paid out  
4 of the earnings and profits of any controlled  
5 foreign corporation in which the taxpayer is a  
6 United States shareholder shall be treated as  
7 typically low-taxed income in proportion to the  
8 ratio of—

9 “(i) the portion of the earnings and  
10 profits attributable to typically low-taxed  
11 income, to

12 “(ii) the total amount of earnings and  
13 profits.

14 “(E) LOOK-THRU APPLIES ONLY WHERE  
15 SUBPART F APPLIES.—If a controlled foreign  
16 corporation meets the requirements of section  
17 954(b)(3)(A) (relating to de minimis rule) for  
18 any taxable year, for purposes of this para-  
19 graph, none of its foreign base company income  
20 (as defined in section 954(a) without regard to  
21 section 954(b)(5)) and none of its gross insur-  
22 ance income (as defined in section  
23 954(b)(3)(C)) for such taxable year shall be  
24 treated as typically low-taxed income, except  
25 that this sentence shall not apply to any income

1 which (without regard to this sentence) would  
 2 be treated as financial services income. Solely  
 3 for purposes of applying subparagraph (D),  
 4 passive income of a controlled foreign corpora-  
 5 tion shall not be treated as typically low-taxed  
 6 income if the requirements of section 954(b)(4)  
 7 are met with respect to such income.

8 “(F) COORDINATION WITH HIGH-TAXED  
 9 INCOME PROVISIONS.—

10 “(i) In determining whether any in-  
 11 come of a controlled foreign corporation is  
 12 typically low-taxed income, subclause (II)  
 13 of paragraph (2)(B)(iii) shall not apply.

14 “(ii) Any income of the taxpayer  
 15 which is treated as typically low-taxed in-  
 16 come under this paragraph shall be so  
 17 treated notwithstanding any provision of  
 18 paragraph (2); except that the determina-  
 19 tion of whether any amount is high-taxed  
 20 income shall be made after the application  
 21 of this paragraph.”

22 (5) TREATMENT OF INCOME TAX BASE DIF-  
 23 FERENCES.—Paragraph (2) of section 904(d), as  
 24 amended by subsection (d), is amended by redesign-  
 25 ating subparagraphs (I) and (J) as subparagraphs

(J) and (K), respectively, and by inserting after subparagraph (H) the following new subparagraph:

“(I) TREATMENT OF INCOME TAX BASE DIFFERENCES.—Tax imposed under the law of a foreign country or possession of the United States on an amount which does not constitute income under United States tax principles shall be treated as imposed on income described in paragraph (1)(B).”

(6) Paragraph (3) of section 904(d) is amended by striking subparagraph (H) and by redesignating subparagraph (I) as subparagraph (H).

(7) Paragraph (2) of section 904(d), as amended by this subsection, is amended by adding at the end the following new subparagraph:

“(L) TRANSITIONAL RULES FOR 2004 CHANGES.—For purposes of paragraph (1)—

“(i) taxes carried from any taxable year beginning before January 1, 2005, to any taxable year beginning on or after such date, with respect to any item of income, shall be treated as described in the subparagraph of paragraph (1) in which such income would be described were such

1 taxes paid or accrued in a taxable year be-  
 2 ginning on or after such date,

3 “(ii) the Secretary may by regulations  
 4 provide for the allocation of any carryback  
 5 of taxes with respect to income to such a  
 6 taxable year for purposes of allocating such  
 7 income among the separate categories in  
 8 effect for such taxable year, and

9 “(iii) the Secretary may by regula-  
 10 tions provide for the allocation under sub-  
 11 section (f) of any overall foreign loss for  
 12 such a taxable year to income among the  
 13 separate categories for taxable years begin-  
 14 ning on or after such date.”

15 (8) Section 904(j)(3)(A)(i) is amended by strik-  
 16 ing “subsection (d)(2)(A)” and inserting “subsection  
 17 (d)(2)(B)”.

18 (f) EFFECTIVE DATE.—The amendments made by  
 19 this section shall apply to taxable years beginning after  
 20 December 31, 2004.

21 **SEC. 227. RECHARACTERIZATION OF OVERALL DOMESTIC**  
 22 **LOSS.**

23 (a) GENERAL RULE.—Section 904, as amended by  
 24 section 204, is amended by redesignating subsections (g),  
 25 (h), (i), (j), and (k) as subsections (h), (i), (j), (k), and

1 (l) respectively, and by inserting after subsection (f) the  
 2 following new subsection:

3 “(g) RECHARACTERIZATION OF OVERALL DOMESTIC  
 4 LOSS.—

5 “(1) GENERAL RULE.—For purposes of this  
 6 subpart and section 936, in the case of any taxpayer  
 7 who sustains an overall domestic loss for any taxable  
 8 year beginning after December 31, 2004, that por-  
 9 tion of the taxpayer’s taxable income from sources  
 10 within the United States for each succeeding taxable  
 11 year which is equal to the lesser of—

12 “(A) the amount of such loss (to the extent  
 13 not used under this paragraph in prior taxable  
 14 years), or

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

21 “(2) OVERALL DOMESTIC LOSS DEFINED.—For  
 22 purposes of this subsection—

23 “(A) IN GENERAL.—The term ‘overall do-  
 24 mestic loss’ means any domestic loss to the ex-  
 25 tent such loss offsets taxable income from

1 sources without the United States for the tax-  
2 able year or for any preceding taxable year by  
3 reason of a carryback. For purposes of the pre-  
4 ceding sentence, the term ‘domestic loss’ means  
5 the amount by which the gross income for the  
6 taxable year from sources within the United  
7 States is exceeded by the sum of the deductions  
8 properly apportioned or allocated thereto (deter-  
9 mined without regard to any carryback from a  
10 subsequent taxable year).

11 “(B) TAXPAYER MUST HAVE ELECTED  
12 FOREIGN TAX CREDIT FOR YEAR OF LOSS.—  
13 The term ‘overall domestic loss’ shall not in-  
14 clude any loss for any taxable year unless the  
15 taxpayer elected the benefits of this subpart for  
16 such taxable year.

17 “(3) CHARACTERIZATION OF SUBSEQUENT IN-  
18 COME.—

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

1 United States previously allocated to those in-  
 2 come categories.

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

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

11 (b) CONFORMING AMENDMENTS.—

12 (1) Section 535(d)(2) is amended by striking  
 13 “section 904(g)(6)” and inserting “section  
 14 904(h)(6)”.

15 (2) Subparagraph (A) of section 936(a)(2) is  
 16 amended by striking “section 904(f)” and inserting  
 17 “subsections (f) and (g) of section 904”.

18 (c) EFFECTIVE DATE.—The amendments made by  
 19 this section shall apply to losses for taxable years begin-  
 20 ning after December 31, 2004.

21 **SEC. 228. REPEAL OF SPECIAL RULES FOR APPLYING FOR-**  
 22 **EIGN TAX CREDIT IN CASE OF FOREIGN OIL**  
 23 **AND GAS INCOME.**

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

1 (b) CONFORMING AMENDMENTS.—

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

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

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

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

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

8 (2) Section 904(f)(5)(E)(iii) is amended by in-  
9 serting “, as in effect before its repeal by the Pro-  
10 mote Growth and Jobs in the USA Act of 2003”  
11 after “section 907(c)(4)(B)”.

12 (3) Section 954(g)(1) is amended by inserting  
13 “, as in effect before its repeal by the Promote  
14 Growth and Jobs in the USA Act of 2003” after  
15 “907(c)”.

16 (4) Section 6501(i) is amended—

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

20 (B) by striking “or 907(f)”.

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



1 (c) EFFECTIVE DATE.—The amendments made by  
 2 this section shall apply to taxable years beginning after  
 3 December 31, 2005.

4 **SEC. 229. INCREASE IN INDIVIDUAL EXEMPTION FROM**  
 5 **FOREIGN TAX CREDIT LIMITATION.**

6 (a) IN GENERAL.—Paragraph (2)(B) of section  
 7 904(k) (relating to certain individuals exempt), as redesignig-  
 8 nated by section 227, is amended by striking “\$300 (\$600  
 9 in the case of a joint return)” and inserting “the exemp-  
 10 tion amount (twice the exemption amount in the case of  
 11 a joint return)”.

12 (b) EXEMPTION AMOUNT.—Section 904(k)(3), as so  
 13 redesignated, is amended by adding at the end the fol-  
 14 lowing new subparagraph:

15 “(E) EXEMPTION AMOUNT.—

16 “(i) IN GENERAL.—The exemption  
 17 amount is \$500.

18 “(ii) COST-OF-LIVING ADJUSTMENT.—

19 In the case of a taxable year beginning  
 20 after 2004, the exemption amount shall be  
 21 increased by an amount equal to the prod-  
 22 uct of \$500 and the cost-of-living adjust-  
 23 ment determined under section 1(f)(3) for  
 24 the calendar year in which the taxable year  
 25 begins, determined by substituting ‘2003’

1           for ‘1992’ in subparagraph (B) thereof. If  
 2           the exemption amount after an increase  
 3           under this clause is not a multiple of \$10,  
 4           such amount shall be rounded to the next  
 5           lowest multiple of \$10.”

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

9   **SEC. 230. UNITED STATES PROPERTY NOT TO INCLUDE**  
 10                   **CERTAIN ASSETS OF CONTROLLED FOREIGN**  
 11                   **CORPORATION.**

12           (a) IN GENERAL.—Section 956(c)(2) (relating to ex-  
 13 ceptions from property treated as United States property)  
 14 is amended by striking “and” at the end of subparagraph  
 15 (J), by striking the period at the end of subparagraph (K)  
 16 and inserting a semicolon, and by adding at the end the  
 17 following new subparagraphs:

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

1 period consistent with the holding of securities  
 2 for sale to customers in the ordinary course of  
 3 business; and

4 “(M) an obligation of a United States per-  
 5 son which—

6 “(i) is not a domestic corporation, and

7 “(ii) is not—

8 “(I) a United States shareholder  
 9 (as defined in section 951(b)) of the  
 10 controlled foreign corporation, or

11 “(II) a partnership, estate, or  
 12 trust in which the controlled foreign  
 13 corporation, or any related person (as  
 14 defined in section 954(d)(3)), is a  
 15 partner, beneficiary, or trustee imme-  
 16 diately after the acquisition of any ob-  
 17 ligation of such partnership, estate, or  
 18 trust by the controlled foreign cor-  
 19 poration.”

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

23 (c) EFFECTIVE DATE.—The amendments made by  
 24 this section shall apply to taxable years of foreign corpora-  
 25 tions beginning after December 31, 2004, and to taxable

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

3 **SEC. 231. ATTRIBUTION OF STOCK OWNERSHIP THROUGH**  
 4 **PARTNERSHIPS TO APPLY IN DETERMINING**  
 5 **SECTION 902 AND 960 CREDITS.**

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

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

23 (b) CLARIFICATION OF COMPARABLE ATTRIBUTION  
 24 UNDER SECTION 901(b)(5).—Paragraph (5) of section

1 901(b) is amended by striking “any individual” and in-  
 2 serting “any person”.

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

7 **SEC. 232. PROVIDE EQUAL TREATMENT FOR INTEREST**  
 8 **PAID BY FOREIGN PARTNERSHIPS AND FOR-**  
 9 **EIGN CORPORATIONS.**

10 (a) IN GENERAL.—Paragraph (1) of section 861(a)  
 11 is amended by striking “and” at the end of subparagraph  
 12 (A), by striking the period at the end of subparagraph  
 13 (B) and inserting “, and”, and by adding at the end the  
 14 following new subparagraph:

15 “(C) in the case of a foreign partnership,  
 16 any interest not paid by a trade or business en-  
 17 gaged in by the partnership in the United  
 18 States and not allocable to income which is ef-  
 19 fectively connected (or treated as effectively  
 20 connected) with the conduct of a trade or busi-  
 21 ness in the United States.”

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

1 **SEC. 233. APPLICATION OF LOOK-THRU RULES TO INTER-**  
 2 **EST, RENTS, AND ROYALTIES.**

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

4 (1) NONCONTROLLED SECTION 902 CORPORA-  
 5 TION.—Section 904(d)(4)(A), as amended by sec-  
 6 tions 204 and 225, is amended to read as follows:

7 “(A) IN GENERAL.—For purposes of this  
 8 subsection—

9 “(i) any applicable dividend shall be  
 10 treated as income in a separate category in  
 11 proportion to the ratio of—

12 “(I) the portion of the earnings  
 13 and profits attributable to income in  
 14 such category, to

15 “(II) the total amount of earn-  
 16 ings and profits, and

17 “(ii) any interest, rent, or royalty  
 18 which is received or accrued from a non-  
 19 controlled section 902 corporation with re-  
 20 spect to the taxpayer shall be treated as  
 21 income in a separate category to the extent  
 22 it is properly allocable (under regulations  
 23 prescribed by the Secretary) to income of  
 24 such corporation in such category.”

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

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

3 (B) by inserting “or noncontrolled section  
 4 902 corporations, whichever is applicable” after  
 5 “controlled foreign corporations”.

6 (3) CONFORMING AMENDMENT.—The heading  
 7 for section 904(d)(4), as amended by sections 204  
 8 and 225, is amended by inserting “, INTEREST,  
 9 RENTS, OR ROYALTIES” after “DIVIDENDS”.

10 (b) EFFECTIVE DATE.—The amendments made by  
 11 this section shall apply to taxable years beginning after  
 12 December 31, 2004.

13 **SEC. 234. CLARIFICATION OF TREATMENT OF CERTAIN**  
 14 **TRANSFERS OF INTANGIBLE PROPERTY.**

15 (a) IN GENERAL.—Subparagraph (C) of section  
 16 367(d)(2) is amended by adding at the end the following  
 17 new sentence: “For purposes of applying section 904(d),  
 18 any such amount shall be treated in the same manner as  
 19 if such amount were a royalty.”

20 (b) EFFECTIVE DATE.—The amendment made by  
 21 this section shall apply to amounts treated as received pur-  
 22 suant to section 367(d)(2) of the Internal Revenue Code  
 23 of 1986 on or after August 5, 1997.

1       **Subtitle C—Other Provisions**

2       **SEC. 251. APPLICATION OF UNIFORM CAPITALIZATION**

3               **RULES TO FOREIGN PERSONS.**

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

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

16          (b) EFFECTIVE DATE.—The amendment made by  
17 subsection (a) shall apply to taxable years beginning after  
18 December 31, 2004. Section 481 of the Internal Revenue  
19 Code of 1986 shall not apply to any change in a method  
20 of accounting by reason of such amendment.

21       **SEC. 252. TREATMENT OF CERTAIN DIVIDENDS OF REGU-**

22               **LATED INVESTMENT COMPANIES.**

23          (a) TREATMENT OF CERTAIN DIVIDENDS.—

24               (1) NONRESIDENT ALIEN INDIVIDUALS.—Sec-  
25 tion 871 (relating to tax on nonresident alien indi-



viduals) is amended by redesignating subsection (k) as subsection (l) and by inserting after subsection (j) the following new subsection:

“(k) EXEMPTION FOR CERTAIN DIVIDENDS OF REGULATED INVESTMENT COMPANIES.—

“(1) INTEREST-RELATED DIVIDENDS.—

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

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

“(i) to any interest-related dividend received from a regulated investment company by a person to the extent such dividend is attributable to interest (other than interest described in subparagraph (E) (i) or (iii)) received by such company on indebtedness issued by such person or by any corporation or partnership with respect to which such person is a 10-percent shareholder,

“(ii) to any interest-related dividend with respect to stock of a regulated invest-

1           ment company unless the person who  
 2           would otherwise be required to deduct and  
 3           withhold tax from such dividend under  
 4           chapter 3 receives a statement (which  
 5           meets requirements similar to the require-  
 6           ments of subsection (h)(5)) that the bene-  
 7           ficial owner of such stock is not a United  
 8           States person, and

9           “(iii) to any interest-related dividend  
 10          paid to any person within a foreign coun-  
 11          try (or any interest-related dividend pay-  
 12          ment addressed to, or for the account of,  
 13          persons within such foreign country) dur-  
 14          ing any period described in subsection  
 15          (h)(6) with respect to such country.

16          Clause (iii) shall not apply to any dividend with  
 17          respect to any stock which was acquired on or  
 18          before the date of the publication of the Sec-  
 19          retary’s determination under subsection (h)(6).

20          “(C) INTEREST-RELATED DIVIDEND.—For  
 21          purposes of this paragraph, an interest-related  
 22          dividend is any dividend (or part thereof) which  
 23          is designated by the regulated investment com-  
 24          pany as an interest-related dividend in a writ-  
 25          ten notice mailed to its shareholders not later

1           than 60 days after the close of its taxable year.  
2           If the aggregate amount so designated with re-  
3           spect to a taxable year of the company (includ-  
4           ing amounts so designated with respect to divi-  
5           dends paid after the close of the taxable year  
6           described in section 855) is greater than the  
7           qualified net interest income of the company for  
8           such taxable year, the portion of each distribu-  
9           tion which shall be an interest-related dividend  
10          shall be only that portion of the amounts so  
11          designated which such qualified net interest in-  
12          come bears to the aggregate amount so des-  
13          ignated.

14               “(D) QUALIFIED NET INTEREST IN-  
15          COME.—For purposes of subparagraph (C), the  
16          term ‘qualified net interest income’ means the  
17          qualified interest income of the regulated in-  
18          vestment company reduced by the deductions  
19          properly allocable to such income.

20               “(E) QUALIFIED INTEREST INCOME.—For  
21          purposes of subparagraph (D), the term ‘quali-  
22          fied interest income’ means the sum of the fol-  
23          lowing amounts derived by the regulated invest-  
24          ment company from sources within the United  
25          States:

1           “(i) Any amount includible in gross  
 2           income as original issue discount (within  
 3           the meaning of section 1273) on an obliga-  
 4           tion payable 183 days or less from the date  
 5           of original issue (without regard to the pe-  
 6           riod held by the company).

7           “(ii) Any interest includible in gross  
 8           income (including amounts recognized as  
 9           ordinary income in respect of original issue  
 10          discount or market discount or acquisition  
 11          discount under part V of subchapter P and  
 12          such other amounts as regulations may  
 13          provide) on an obligation which is in reg-  
 14          istered form; except that this clause shall  
 15          not apply to—

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

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

24           “(iii) Any interest referred to in sub-  
 25          section (i)(2)(A) (without regard to the

1 trade or business of the regulated invest-  
 2 ment company).

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

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

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

12 “(A) IN GENERAL.—Except as provided in  
 13 subparagraph (B), no tax shall be imposed  
 14 under paragraph (1)(A) of subsection (a) on  
 15 any short-term capital gain dividend received  
 16 from a regulated investment company.

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

22 “(C) SHORT-TERM CAPITAL GAIN DIVI-  
 23 DEND.—For purposes of this paragraph, a  
 24 short-term capital gain dividend is any dividend  
 25 (or part thereof) which is designated by the reg-

1           ulated investment company as a short-term cap-  
 2           ital gain dividend in a written notice mailed to  
 3           its shareholders not later than 60 days after the  
 4           close of its taxable year. If the aggregate  
 5           amount so designated with respect to a taxable  
 6           year of the company (including amounts so des-  
 7           ignated with respect to dividends paid after the  
 8           close of the taxable year described in section  
 9           855) is greater than the qualified short-term  
 10          gain of the company for such taxable year, the  
 11          portion of each distribution which shall be a  
 12          short-term capital gain dividend shall be only  
 13          that portion of the amounts so designated  
 14          which such qualified short-term gain bears to  
 15          the aggregate amount so designated.

16               “(D) QUALIFIED SHORT-TERM GAIN.—For  
 17          purposes of subparagraph (C), the term ‘quali-  
 18          fied short-term gain’ means the excess of the  
 19          net short-term capital gain of the regulated in-  
 20          vestment company for the taxable year over the  
 21          net long-term capital loss (if any) of such com-  
 22          pany for such taxable year. For purposes of this  
 23          subparagraph—

24                       “(i) the net short-term capital gain of  
 25                       the regulated investment company shall be

1           computed by treating any short-term cap-  
 2           ital gain dividend includible in gross in-  
 3           come with respect to stock of another regu-  
 4           lated investment company as a short-term  
 5           capital gain, and

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

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

21          (2) FOREIGN CORPORATIONS.—Section 881 (re-  
 22          lating to tax on income of foreign corporations not  
 23          connected with United States business) is amended  
 24          by redesignating subsection (e) as subsection (f) and

1 by inserting after subsection (d) the following new  
 2 subsection:

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

5 “(1) INTEREST-RELATED DIVIDENDS.—

6 “(A) IN GENERAL.—Except as provided in  
 7 subparagraph (B), no tax shall be imposed  
 8 under paragraph (1) of subsection (a) on any  
 9 interest-related dividend (as defined in section  
 10 871(k)(1)) received from a regulated investment  
 11 company.

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

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

16 “(ii) to any interest-related dividend  
 17 received by a controlled foreign corporation  
 18 (within the meaning of section 957(a)) to  
 19 the extent such dividend is attributable to  
 20 interest received by the regulated invest-  
 21 ment company from a person who is a re-  
 22 lated person (within the meaning of section  
 23 864(d)(4)) with respect to such controlled  
 24 foreign corporation.



1           “(C) TREATMENT OF DIVIDENDS RE-  
 2           CEIVED BY CONTROLLED FOREIGN CORPORA-  
 3           TIONS.—The rules of subsection (c)(5)(A) shall  
 4           apply to any interest-related dividend received  
 5           by a controlled foreign corporation (within the  
 6           meaning of section 957(a)) to the extent such  
 7           dividend is attributable to interest received by  
 8           the regulated investment company which is de-  
 9           scribed in clause (ii) of section 871(k)(1)(E)  
 10          (and not described in clause (i) or (iii) of such  
 11          section).

12          “(2) SHORT-TERM CAPITAL GAIN DIVIDENDS.—  
 13          No tax shall be imposed under paragraph (1) of sub-  
 14          section (a) on any short-term capital gain dividend  
 15          (as defined in section 871(k)(2)) received from a  
 16          regulated investment company.”

17          (3) WITHHOLDING TAXES.—

18                 (A) Section 1441(c) (relating to excep-  
 19                 tions) is amended by adding at the end the fol-  
 20                 lowing new paragraph:

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

23                 “(A) IN GENERAL.—No tax shall be re-  
 24                 quired to be deducted and withheld under sub-  
 25                 section (a) from any amount exempt from the

1 tax imposed by section 871(a)(1)(A) by reason  
 2 of section 871(k).

3 “(B) SPECIAL RULE.—For purposes of  
 4 subparagraph (A), clause (i) of section  
 5 871(k)(1)(B) shall not apply to any dividend  
 6 unless the regulated investment company knows  
 7 that such dividend is a dividend referred to in  
 8 such clause. A similar rule shall apply with re-  
 9 spect to the exception contained in section  
 10 871(k)(2)(B).”

11 (B) Section 1442(a) (relating to with-  
 12 holding of tax on foreign corporations) is  
 13 amended—

14 (i) by striking “and the reference in  
 15 section 1441(c)(10)” and inserting “the  
 16 reference in section 1441(c)(10)”, and

17 (ii) by inserting before the period at  
 18 the end the following: “, and the references  
 19 in section 1441(c)(12) to sections 871(a)  
 20 and 871(k) shall be treated as referring to  
 21 sections 881(a) and 881(e) (except that for  
 22 purposes of applying subparagraph (A) of  
 23 section 1441(c)(12), as so modified, clause  
 24 (ii) of section 881(e)(1)(B) shall not apply  
 25 to any dividend unless the regulated invest-

1                   ment company knows that such dividend is  
 2                   a dividend referred to in such clause)”.  
 3

4       (b) ESTATE TAX TREATMENT OF INTEREST IN CER-  
 5 TAIN REGULATED INVESTMENT COMPANIES.—Section  
 6 2105 (relating to property without the United States for  
 7 estate tax purposes) is amended by adding at the end the  
 8 following new subsection:

9       “(d) STOCK IN A RIC.—

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

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

1                   “(A) amounts, deposits, or debt obligations  
 2                   described in subsection (b) of this section,  
 3                   “(B) debt obligations described in the last  
 4                   sentence of section 2104(c), or  
 5                   “(C) other property not within the United  
 6                   States.”

7           (c) TREATMENT OF REGULATED INVESTMENT COM-  
 8 PANIES UNDER SECTION 897.—

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

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

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

19               “(3) DISTRIBUTIONS BY DOMESTICALLY CON-  
 20          TROLLED QUALIFIED INVESTMENT ENTITIES.—In  
 21          the case of a domestically controlled qualified invest-  
 22          ment entity, rules similar to the rules of subsection  
 23          (d) shall apply to the foreign ownership percentage  
 24          of any gain.”

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

“(A) QUALIFIED INVESTMENT ENTITY.—

The term ‘qualified investment entity’ means any real estate investment trust and any regulated investment company.

“(B) DOMESTICALLY CONTROLLED.—The

term ‘domestically controlled qualified investment entity’ means any qualified investment entity in which at all times during the testing period less than 50 percent in value of the stock was held directly or indirectly by foreign persons.”

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

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

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall apply to dividends with respect to taxable years of regulated investment companies beginning after the date of the enactment of this Act.

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

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

9   **SEC. 253. REPEAL OF WITHHOLDING TAX ON DIVIDENDS**  
 10                           **FROM CERTAIN FOREIGN CORPORATIONS.**

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

15                       “(D) Dividends paid by a foreign corpora-  
 16                       tion which are treated under section  
 17                       861(a)(2)(B) as income from sources within the  
 18                       United States.”.

19          (b) EFFECTIVE DATE.—The amendment made by  
 20          this section shall apply to payments made after December  
 21          31, 2004.

22   **SEC. 254. AIRLINE MILEAGE AWARDS TO CERTAIN FOREIGN**  
 23                           **PERSONS.**

24          (a) IN GENERAL.—The last sentence of section  
 25          4261(e)(3)(C) (relating to regulations) is amended by in-

1 setting “and mileage awards which are issued to individ-  
 2 uals whose mailing addresses on record with the person  
 3 providing the right to air transportation are outside the  
 4 United States” before the period at the end thereof.

5 (b) EFFECTIVE DATE.—The amendment made by  
 6 this section shall apply to amounts paid, and benefits pro-  
 7 vided, after December 31, 2003.

8 **SEC. 255. INTEREST PAYMENTS DEDUCTIBLE WHERE DIS-**  
 9 **QUALIFIED GUARANTEE HAS NO ECONOMIC**  
 10 **EFFECT.**

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

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

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

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

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

1           (4) by adding at the end the following new sen-  
 2           tence: “For purposes of subclause (III), to the ex-  
 3           tent provided in regulations, the Secretary may re-  
 4           ject a showing that a taxpayer could have borrowed  
 5           substantially the same principal amount if such bor-  
 6           rowing is on terms substantially dissimilar to those  
 7           of the actual loan.”

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

11   **SEC. 256. MODIFICATIONS OF REPORTING REQUIREMENTS**  
 12                           **FOR CERTAIN FOREIGN-OWNED CORPORA-**  
 13                           **TIONS.**

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

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

23          (b) **TIME FOR PROVIDING TRANSLATIONS OF SPE-**  
 24          **CIFIC DOCUMENTS.**—Notwithstanding Internal Revenue  
 25          Service Regulation § 1.6038A-3(f)(2), a taxpayer shall



1 have at least 60 days to provide translations of specific  
 2 documents it is requested to translate. Nothing in this  
 3 subsection shall limit the right of a taxpayer to file a writ-  
 4 ten request for an extension of time to comply with the  
 5 request.

6 (c) EFFECTIVE DATES.—

7 (1) EXCEPTION.—The amendment made by  
 8 subsection (a) shall apply to taxable years beginning  
 9 after December 31, 2003.

10 (2) TRANSLATIONS.—Subsection (b) shall apply  
 11 to requests made by the Internal Revenue Service  
 12 after December 31, 2003.

13 **SEC. 257. REPEAL OF TAX ON CERTAIN UNITED STATES**  
 14 **SOURCE CAPITAL GAINS OF NONRESIDENT**  
 15 **ALIENS.**

16 (a) IN GENERAL.—Subsection (a) of section 871 is  
 17 amended by striking paragraph (2) and by redesignating  
 18 paragraph (3) as paragraph (2).

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

1 **SEC. 258. ELECTION NOT TO USE AVERAGE EXCHANGE**  
 2 **RATE FOR FOREIGN TAX PAID OTHER THAN**  
 3 **IN FUNCTIONAL CURRENCY.**

4 (a) IN GENERAL.—Paragraph (1) of section 986(a)  
 5 (relating to determination of foreign taxes and foreign cor-  
 6 poration’s earnings and profits) is amended by redesign-  
 7 ating subparagraph (D) as subparagraph (E) and by in-  
 8 serting after subparagraph (C) the following new subpara-  
 9 graph:

10 “(D) ELECTIVE EXCEPTION FOR TAXES  
 11 PAID OTHER THAN IN FUNCTIONAL CUR-  
 12 RENCY.—

13 “(i) IN GENERAL.—At the election of  
 14 the taxpayer, subparagraph (A) shall not  
 15 apply to any foreign income taxes the li-  
 16 ability for which is denominated in any  
 17 currency other than in the taxpayer’s func-  
 18 tional currency.

19 “(ii) APPLICATION TO QUALIFIED  
 20 BUSINESS UNITS.—An election under this  
 21 subparagraph may apply to foreign income  
 22 taxes attributable to a qualified business  
 23 unit in accordance with regulations pre-  
 24 scribed by the Secretary.

25 “(iii) ELECTION.—Any such election  
 26 shall apply to the taxable year for which

1           made and all subsequent taxable years un-  
2           less revoked with the consent of the Sec-  
3           retary.”

4       (b) EFFECTIVE DATE.—The amendment made by  
5 this section shall apply to taxable years beginning after  
6 December 31, 2004.

7 **SEC. 259. STUDY OF IMPACT OF INTERNATIONAL TAX LAWS**  
8                   **ON TAXPAYERS OTHER THAN LARGE COR-**  
9                   **PORATIONS.**

10       (a) STUDY.—The Secretary of the Treasury or the  
11 Secretary’s delegate shall conduct a study of the impact  
12 of Federal international tax rules on taxpayers other than  
13 large corporations, including the burdens placed on such  
14 taxpayers in complying with such rules.

15       (b) REPORT.—Not later than 180 days after the date  
16 of the enactment of this Act, the Secretary shall report  
17 to the Committee on Finance of the Senate and the Com-  
18 mittee on Ways and Means of the House of Representa-  
19 tives the results of the study conducted under subsection  
20 (a), including any recommendations for legislative or ad-  
21 ministrative changes to reduce the compliance burden on  
22 taxpayers other than large corporations and for such other  
23 purposes as the Secretary determines appropriate.

1 **TITLE III—CREDIT FOR IN-**  
 2 **CREASING RESEARCH ACTIVI-**  
 3 **TIES**

4 **SEC. 301. PERMANENT EXTENSION OF RESEARCH CREDIT.**

5 (a) IN GENERAL.—Section 41 (relating to credit for  
 6 increasing research activities) is amended by striking sub-  
 7 section (h).

8 (b) CONFORMING AMENDMENT.—Paragraph (1) of  
 9 section 45C(b) is amended by striking subparagraph (D).

10 (c) EFFECTIVE DATE.—The amendments made by  
 11 this section shall apply to amounts paid or incurred after  
 12 the date of the enactment of this Act.

13 **SEC. 302. INCREASE IN RATES OF ALTERNATIVE INCRE-**  
 14 **MENTAL CREDIT.**

15 (a) IN GENERAL.—Subparagraph (A) of section  
 16 41(c)(4) (relating to election of alternative incremental  
 17 credit) is amended—

18 (1) by striking “2.65 percent” and inserting “3  
 19 percent”,

20 (2) by striking “3.2 percent” and inserting “4  
 21 percent”, and

22 (3) by striking “3.75 percent” and inserting “5  
 23 percent”.

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

4 **SEC. 303. ALTERNATIVE SIMPLIFIED CREDIT FOR QUALI-**  
 5 **FIED RESEARCH EXPENSES.**

6 (a) IN GENERAL.—Subsection (c) of section 41 (re-  
 7 lating to base amount) is amended by redesignating para-  
 8 graphs (5) and (6) as paragraphs (6) and (7), respectively,  
 9 and by inserting after paragraph (4) the following new  
 10 paragraph:

11 “(5) ELECTION OF ALTERNATIVE SIMPLIFIED  
 12 CREDIT.—

13 “(A) IN GENERAL.—At the election of the  
 14 taxpayer, the credit determined under sub-  
 15 section (a)(1) shall be equal to 12 percent of so  
 16 much of the qualified research expenses for the  
 17 taxable year as exceeds 50 percent of the aver-  
 18 age qualified research expenses for the 3 tax-  
 19 able years preceding the taxable year for which  
 20 the credit is being determined.

21 “(B) SPECIAL RULE IN CASE OF NO  
 22 QUALIFIED RESEARCH EXPENSES IN ANY OF 3  
 23 PRECEDING TAXABLE YEARS.—

24 “(i) TAXPAYERS TO WHICH SUBPARA-  
 25 GRAPH APPLIES.—The credit under this

paragraph shall be determined under this subparagraph if the taxpayer has no qualified research expenses in any 1 of the 3 taxable years preceding the taxable year for which the credit is being determined.

“(ii) CREDIT RATE.—The credit determined under this subparagraph shall be equal to 6 percent of the qualified research expenses for the taxable year.

“(C) ELECTION.—An election under this paragraph shall apply to the taxable year for which made and all succeeding taxable years unless revoked with the consent of the Secretary. An election under this paragraph may not be made for any taxable year to which an election under paragraph (4) applies.”

(b) COORDINATION WITH ELECTION OF ALTERNATIVE INCREMENTAL CREDIT.—

(1) IN GENERAL.—Section 41(c)(4)(B) (relating to election) is amended by adding at the end the following: “An election under this paragraph may not be made for any taxable year to which an election under paragraph (5) applies.”

(2) TRANSITION RULE.—In the case of an election under section 41(c)(4) of the Internal Revenue

1 Code of 1986 which applies to the taxable year  
 2 which includes the date of the enactment of this Act,  
 3 such election shall be treated as revoked with the  
 4 consent of the Secretary of the Treasury if the tax-  
 5 payer makes an election under section 41(c)(5) of  
 6 such Code (as added by subsection (a)) for such  
 7 year.

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

## 11 **TITLE IV—REFORM OF DEPRE-** 12 **CIATION OF BUSINESS PROP-** 13 **ERTY**

### 14 **SEC. 401. 100-PERCENT EXPENSING FOR CERTAIN PROP-** 15 **ERTY THROUGH 2006.**

16 (a) IN GENERAL.—

17 (1) INCREASE.—Paragraph (4) of section  
 18 168(k) is amended by striking “50-percent” each  
 19 place it appears and inserting “100-percent”.

20 (2) EXTENSION.—

21 (A) Section 168(k)(4) is amended by strik-  
 22 ing “January 1, 2005” each place it appears  
 23 and inserting “January 1, 2007”.

1 (B) Clause (iii) of section 168(k)(4)(B) is  
 2 amended by striking “January 1, 2006” and in-  
 3 serting “January 1, 2008”.

4 (b) EXTENSION OF CERTAIN DATES FOR 30-PER-  
 5 CENT BONUS DEPRECIATION PROPERTY.—Section  
 6 168(k)(2) is amended—

7 (1) by striking “January 1, 2005” each place  
 8 it appears in the text and inserting “January 1,  
 9 2007”,

10 (2) in subparagraph (A)(iv), by striking “Janu-  
 11 ary 1, 2006” and inserting “January 1, 2008”, and

12 (3) in subparagraph (B)(ii), by striking “PRE-  
 13 JANUARY 1, 2005” in the heading and inserting  
 14 “PRE-JANUARY 1, 2007”.

15 (c) CONFORMING AMENDMENTS.—

16 (1) Section 168(k)(4) is amended by striking  
 17 “50-PERCENT” in the heading and inserting “100-  
 18 PERCENT”.

19 (2) The subsection heading for section 168(k) is  
 20 amended by striking “JANUARY 1, 2005” and insert-  
 21 ing “JANUARY 1, 2007”.

22 (d) EFFECTIVE DATE.—The amendments made by  
 23 this section shall apply to taxable years ending after May  
 24 5, 2003.



1 **SEC. 402. EXTENSION OF EXPENSING FOR SMALL BUSI-**  
 2 **NESS.**

3 Section 179 is amended by striking “2006” each  
 4 place it appears in the text and inserting “2007”.

5 **SEC. 403. ELECTION TO INCREASE MINIMUM TAX CREDIT**  
 6 **LIMITATION IN LIEU OF BONUS DEPRECIATION.**  
 7 **TION.**

8 (a) IN GENERAL.—Section 53 (relating to credit for  
 9 prior year minimum tax liability) is amended by adding  
 10 at the end the following new subsection:

11 “(e) ADDITIONAL CREDIT IN LIEU OF BONUS DE-  
 12 PRECIATION.—

13 “(1) IN GENERAL.—In the case of a corpora-  
 14 tion making an election under this subsection for a  
 15 taxable year, the limitation under subsection (c)  
 16 shall be increased by an amount equal to the bonus  
 17 depreciation amount.

18 “(2) BONUS DEPRECIATION AMOUNT.—For  
 19 purposes of paragraph (1), the bonus depreciation  
 20 amount for any taxable year is an amount equal to  
 21 the product of—

22 “(A) 35 percent, and

23 “(B) the excess (if any) of—

24 “(i) the aggregate amount of depre-  
 25 ciation which would be determined under  
 26 section 168 for property placed in service

1           during such taxable year if no election  
2           under this subsection were made, over

3           “(ii) the aggregate allowance for de-  
4           preciation allowable with respect to such  
5           property placed in service for such taxable  
6           year.

7           “(3) ELECTION.—Sections 168(k) (other than  
8           paragraph (2)(F) thereof) shall not apply to any  
9           property placed in service during a taxable year by  
10          a corporation making an election under this sub-  
11          section for such taxable year. An election under this  
12          subsection may only be revoked with the consent of  
13          the Secretary.

14          “(4) CREDIT REFUNDABLE.—The aggregate in-  
15          crease in the credit allowed by this section for any  
16          taxable year by reason of this subsection shall for  
17          purposes of this title (other than subsection (b)(2)  
18          of this section) be treated as a credit allowed to the  
19          taxpayer under subpart C.”.

20          (b) CONFORMING AMENDMENTS.—Subsection (k) of  
21          section 168, as amended by section 401, is amended by  
22          adding at the end the following new paragraph:

23               “(5) CROSS REFERENCE.—For an election to  
24          claim certain minimum tax credits in lieu of the al-

1 lowance determined under this subsection, see sec-  
2 tion 53(e).”.

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

○