

108TH CONGRESS
1ST SESSION

S. 907

To amend the Internal Revenue Code of 1986 to impose a flat tax only on individual taxable earned income and business taxable income, and for other purposes.

IN THE SENATE OF THE UNITED STATES

APRIL 11, 2003

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

A BILL

To amend the Internal Revenue Code of 1986 to impose a flat tax only on individual taxable earned income and business taxable income, 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; TABLE OF CONTENTS; AMEND-
4 MENT OF 1986 CODE.**

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

7 (b) TABLE OF CONTENTS.—The table of contents for
8 this Act is as follows:

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

Sec. 2. Flat tax on individual taxable earned income and business taxable income.

Sec. 3. Repeal of estate and gift taxes.

Sec. 4. Additional repeals.

Sec. 5. Effective dates.

1 (c) AMENDMENT OF 1986 CODE.—Except as other-
2 wise expressly provided, whenever in this Act an amend-
3 ment or repeal is expressed in terms of an amendment
4 to, or repeal of, a section or other provision, the reference
5 shall be considered to be made to a section or other provi-
6 sion of the Internal Revenue Code of 1986.

**7 SEC. 2. FLAT TAX ON INDIVIDUAL TAXABLE EARNED IN-
8 COME AND BUSINESS TAXABLE INCOME.**

9 (a) IN GENERAL.—Subchapter A of chapter 1 of sub-
10 title A is amended to read as follows:

“Part I. Tax on individuals.

“Part II. Tax on business activities.

13 **“PART I—TAX ON INDIVIDUALS**

“Sec. 1. Tax imposed.

“Sec. 2. Standard deduction.

“Sec. 3. Deduction for cash charitable contributions.

“Sec. 4. Deduction for home acquisition indebtedness.

“Sec. 5. Definitions and special rules.

14 "SECTION 1. TAX IMPOSED.

15 "(a) IMPOSITION OF TAX.—There is hereby imposed
16 on every individual a tax equal to 20 percent of the taxable
17 earned income of such individual.

1 “(b) TAXABLE EARNED INCOME.—For purposes of
2 this section, the term ‘taxable earned income’ means the
3 excess (if any) of—

4 “(1) the earned income received or accrued dur-
5 ing the taxable year, over

6 “(2) the sum of—

7 “(A) the standard deduction,

8 “(B) the deduction for cash charitable con-
9 tributions, and

10 “(C) the deduction for home acquisition in-
11 debtedness,

12 for such taxable year.

13 “(c) EARNED INCOME.—For purposes of this sec-
14 tion—

15 “(1) IN GENERAL.—The term ‘earned income’
16 means wages, salaries, or professional fees, and
17 other amounts received from sources within the
18 United States as compensation for personal services
19 actually rendered, but does not include that part of
20 compensation derived by the taxpayer for personal
21 services rendered by the taxpayer to a corporation
22 which represents a distribution of earnings or profits
23 rather than a reasonable allowance as compensation
24 for the personal services actually rendered.

1 “(2) TAXPAYER ENGAGED IN TRADE OR BUSI-
2 NESS.—In the case of a taxpayer engaged in a trade
3 or business in which both personal services and cap-
4 ital are material income-producing factors, under
5 regulations prescribed by the Secretary, a reasonable
6 allowance as compensation for the personal services
7 rendered by the taxpayer, not in excess of 30 per-
8 cent of the taxpayer’s share of the net profits of
9 such trade or business, shall be considered as earned
10 income.

11 **“SEC. 2. STANDARD DEDUCTION.**

12 “(a) IN GENERAL.—For purposes of this subtitle, the
13 term ‘standard deduction’ means the sum of—
14 “(1) the basic standard deduction, plus
15 “(2) the additional standard deduction.

16 “(b) BASIC STANDARD DEDUCTION.—For purposes
17 of subsection (a), the basic standard deduction is—

18 “(1) \$17,500 in the case of—
19 “(A) a joint return, and
20 “(B) a surviving spouse (as defined in sec-
21 tion 5(a)),
22 “(2) \$15,000 in the case of a head of household
23 (as defined in section 5(b)), and
24 “(3) \$10,000 in the case of an individual—

1 “(A) who is not married and who is not a
2 surviving spouse or head of household, or

3 “(B) who is a married individual filing a
4 separate return.

5 “(c) ADDITIONAL STANDARD DEDUCTION.—For pur-
6 poses of subsection (a), the additional standard deduction
7 is \$5,000 for each dependent (as defined in section
8 5(d))—

9 “(1) whose earned income for the calendar year
10 in which the taxable year of the taxpayer begins is
11 less than the basic standard deduction specified in
12 subsection (b)(3), or

13 “(2) who is a child of the taxpayer and who—
14 “(A) has not attained the age of 19 at the
15 close of the calendar year in which the taxable
16 year of the taxpayer begins, or

17 “(B) is a student who has not attained the
18 age of 24 at the close of such calendar year.

19 “(d) INFLATION ADJUSTMENT.—

20 “(1) IN GENERAL.—In the case of any taxable
21 year beginning in a calendar year after 2004, each
22 dollar amount contained in subsections (b) and (c)
23 shall be increased by an amount equal to—

24 “(A) such dollar amount, multiplied by

1 “(B) the cost-of-living adjustment for the
2 calendar year in which the taxable year begins.

3 “(2) COST-OF-LIVING ADJUSTMENT.—For pur-
4 poses of paragraph (1), the cost-of-living adjustment
5 for any calendar year is the percentage (if any) by
6 which—

7 “(A) the CPI for the preceding calendar
8 year, exceeds

9 “(B) the CPI for calendar year 2003.

10 “(3) CPI FOR ANY CALENDAR YEAR.—For pur-
11 poses of paragraph (2), the CPI for any calendar
12 year is the average of the Consumer Price Index as
13 of the close of the 12-month period ending on Au-
14 gust 31 of such calendar year.

15 “(4) CONSUMER PRICE INDEX.—For purposes
16 of paragraph (3), the term ‘Consumer Price Index’
17 means the last Consumer Price Index for all-urban
18 consumers published by the Department of Labor.
19 For purposes of the preceding sentence, the revision
20 of the Consumer Price Index which is most con-
21 sistent with the Consumer Price Index for calendar
22 year 1986 shall be used.

23 “(5) ROUNDING.—If any increase determined
24 under paragraph (1) is not a multiple of \$50, such

1 amount shall be rounded to the next lowest multiple
2 of \$50.

3 **“SEC. 3. DEDUCTION FOR CASH CHARITABLE CONTRIBU-**
4 **TIONS.**

5 “(a) GENERAL RULE.—For purposes of this part,
6 there shall be allowed as a deduction any charitable con-
7 tribution (as defined in subsection (b)) not to exceed
8 \$2,500 (\$1,250, in the case of a married individual filing
9 a separate return), payment of which is made within the
10 taxable year.

11 “(b) CHARITABLE CONTRIBUTION DEFINED.—For
12 purposes of this section, the term ‘charitable contribution’
13 means a contribution or gift of cash or its equivalent to
14 or for the use of the following:

15 “(1) A State, a possession of the United States,
16 or any political subdivision of any of the foregoing,
17 or the United States or the District of Columbia,
18 but only if the contribution or gift is made for exclu-
19 sively public purposes.

20 “(2) A corporation, trust, or community chest,
21 fund, or foundation—

22 “(A) created or organized in the United
23 States or in any possession thereof, or under
24 the law of the United States, any State, the

3 “(B) organized and operated exclusively
4 for religious, charitable, scientific, literary, or
5 educational purposes, or to foster national or
6 international amateur sports competition (but
7 only if no part of its activities involve the provi-
8 sion of athletic facilities or equipment), or for
9 the prevention of cruelty to children or animals,

10 “(C) no part of the net earnings of which
11 inures to the benefit of any private shareholder
12 or individual, and

13 “(D) which is not disqualified for tax ex-
14 emption under section 501(c)(3) by reason of
15 attempting to influence legislation, and which
16 does not participate in, or intervene in (includ-
17 ing the publishing or distributing of state-
18 ments), any political campaign on behalf of (or
19 in opposition to) any candidate for public office.

20 A contribution or gift by a corporation to a trust,
21 chest, fund, or foundation shall be deductible by rea-
22 son of this paragraph only if it is to be used within
23 the United States or any of its possessions exclu-
24 sively for purposes specified in subparagraph (B).

1 Rules similar to the rules of section 501(j) shall
2 apply for purposes of this paragraph.

3 “(3) A post or organization of war veterans, or
4 an auxiliary unit or society of, or trust or foundation
5 for, any such post or organization—

6 “(A) organized in the United States or any
7 of its possessions, and

8 “(B) no part of the net earnings of which
9 inures to the benefit of any private shareholder
10 or individual.

11 “(4) In the case of a contribution or gift by an
12 individual, a domestic fraternal society, order, or as-
13 sociation, operating under the lodge system, but only
14 if such contribution or gift is to be used exclusively
15 for religious, charitable, scientific, literary, or edu-
16 cational purposes, or for the prevention of cruelty to
17 children or animals.

18 “(5) A cemetery company owned and operated
19 exclusively for the benefit of its members, or any
20 corporation chartered solely for burial purposes as a
21 cemetery corporation and not permitted by its char-
22 ter to engage in any business not necessarily inci-
23 dent to that purpose, if such company or corporation
24 is not operated for profit and no part of the net

1 earnings of such company or corporation inures to
2 the benefit of any private shareholder or individual.

3 For purposes of this section, the term ‘charitable contribu-
4 tion’ also means an amount treated under subsection (d)
5 as paid for the use of an organization described in para-
6 graph (2), (3), or (4).

7 “(c) DISALLOWANCE OF DEDUCTION IN CERTAIN
8 CASES AND SPECIAL RULES.—

9 “(1) SUBSTANTIATION REQUIREMENT FOR CER-
10 TAIN CONTRIBUTIONS.—

11 “(A) GENERAL RULE.—No deduction shall
12 be allowed under subsection (a) for any con-
13 tribution of \$250 or more unless the taxpayer
14 substantiates the contribution by a contempora-
15 neous written acknowledgment of the contribu-
16 tion by the donee organization that meets the
17 requirements of subparagraph (B).

18 “(B) CONTENT OF ACKNOWLEDGMENT.—
19 An acknowledgment meets the requirements of
20 this subparagraph if it includes the following
21 information:

22 “(i) The amount of cash contributed.
23 “(ii) Whether the donee organization
24 provided any goods or services in consider-

8 For purposes of this subparagraph, the term
9 ‘intangible religious benefit’ means any intan-
10 gible religious benefit which is provided by an
11 organization organized exclusively for religious
12 purposes and which generally is not sold in a
13 commercial transaction outside the donative
14 context.

15 “(C) CONTEMPORANEOUS.—For purposes
16 of subparagraph (A), an acknowledgment shall
17 be considered to be contemporaneous if the tax-
18 payer obtains the acknowledgment on or before
19 the earlier of—

1 “(D) SUBSTANTIATION NOT REQUIRED
2 FOR CONTRIBUTIONS REPORTED BY THE
3 DONEE ORGANIZATION.—Subparagraph (A)
4 shall not apply to a contribution if the donee
5 organization files a return, on such form and in
6 accordance with such regulations as the Sec-
7 retary may prescribe, which includes the infor-
8 mation described in subparagraph (B) with re-
9 spect to the contribution.

10 “(E) REGULATIONS.—The Secretary shall
11 prescribe such regulations as may be necessary
12 or appropriate to carry out the purposes of this
13 paragraph, including regulations that may pro-
14 vide that some or all of the requirements of this
15 paragraph do not apply in appropriate cases.

16 “(2) DENIAL OF DEDUCTION WHERE CON-
17 TRIBUTION FOR LOBBYING ACTIVITIES.—No deduc-
18 tion shall be allowed under this section for a con-
19 tribution to an organization which conducts activities
20 to which section 11(d)(2)(C)(i) applies on matters of
21 direct financial interest to the donor’s trade or busi-
22 ness, if a principal purpose of the contribution was
23 to avoid Federal income tax by securing a deduction
24 for such activities under this section which would be
25 disallowed by reason of section 11(d)(2)(C) if the

1 donor had conducted such activities directly. No de-
2 duction shall be allowed under section 11(d) for any
3 amount for which a deduction is disallowed under
4 the preceding sentence.

5 “(d) AMOUNTS PAID TO MAINTAIN CERTAIN STU-
6 DENTS AS MEMBERS OF TAXPAYER’S HOUSEHOLD.—

7 “(1) IN GENERAL.—Subject to the limitations
8 provided by paragraph (2), amounts paid by the tax-
9 payer to maintain an individual (other than a de-
10 pendent, as defined in section 5(d), or a relative of
11 the taxpayer) as a member of such taxpayer’s house-
12 hold during the period that such individual is—

13 “(A) a member of the taxpayer’s household
14 under a written agreement between the tax-
15 payer and an organization described in para-
16 graph (2), (3), or (4) of subsection (b) to imple-
17 ment a program of the organization to provide
18 educational opportunities for pupils or students
19 in private homes, and

20 “(B) a full-time pupil or student in the
21 twelfth or any lower grade at an educational or-
22 ganization located in the United States which
23 normally maintains a regular faculty and cur-
24 riculum and normally has a regularly enrolled
25 body of pupils or students in attendance at the

1 place where its educational activities are regu-
2 larly carried on,
3 shall be treated as amounts paid for the use of the
4 organization.

5 “(2) LIMITATIONS.—

6 “(A) AMOUNT.—Paragraph (1) shall apply
7 to amounts paid within the taxable year only to
8 the extent that such amounts do not exceed \$50
9 multiplied by the number of full calendar
10 months during the taxable year which fall with-
11 in the period described in paragraph (1). For
12 purposes of the preceding sentence, if 15 or
13 more days of a calendar month fall within such
14 period such month shall be considered as a full
15 calendar month.

16 “(B) COMPENSATION OR REIMBURSE-
17 MENT.—Paragraph (1) shall not apply to any
18 amount paid by the taxpayer within the taxable
19 year if the taxpayer receives any money or
20 other property as compensation or reimburse-
21 ment for maintaining the individual in the tax-
22 payer’s household during the period described
23 in paragraph (1).

24 “(3) RELATIVE DEFINED.—For purposes of
25 paragraph (1), the term ‘relative of the taxpayer’

1 means an individual who, with respect to the tax-
2 payer, bears any of the relationships described in
3 subparagraphs (A) through (H) of section 5(d)(1).

4 “(4) NO OTHER AMOUNT ALLOWED AS DEDUC-
5 TION.—No deduction shall be allowed under sub-
6 section (a) for any amount paid by a taxpayer to
7 maintain an individual as a member of the tax-
8 payer’s household under a program described in
9 paragraph (1)(A) except as provided in this sub-
10 section.

11 “(e) DENIAL OF DEDUCTION FOR CERTAIN TRAVEL
12 EXPENSES.—No deduction shall be allowed under this sec-
13 tion for traveling expenses (including amounts expended
14 for meals and lodging) while away from home, whether
15 paid directly or by reimbursement, unless there is no sig-
16 nificant element of personal pleasure, recreation, or vaca-
17 tion in such travel.

18 “(f) DISALLOWANCE OF DEDUCTIONS IN CERTAIN
19 CASES.—For disallowance of deductions for contributions
20 to or for the use of Communist controlled organizations,
21 see section 11(a) of the Internal Security Act of 1950 (50
22 U.S.C. 790).

23 “(g) TREATMENT OF CERTAIN AMOUNTS PAID TO OR
24 FOR THE BENEFIT OF INSTITUTIONS OF HIGHER EDU-
25 CATION.—

1 “(1) IN GENERAL.—For purposes of this sec-
2 tion, 80 percent of any amount described in para-
3 graph (2) shall be treated as a charitable contribu-
4 tion.

5 “(2) AMOUNT DESCRIBED.—For purposes of
6 paragraph (1), an amount is described in this para-
7 graph if—

8 “(A) the amount is paid by the taxpayer to
9 or for the benefit of an educational organiza-
10 tion—

11 “(i) which is described in subsection
12 (d)(1)(B), and

13 “(ii) which is an institution of higher
14 education (as defined in section 3304(f)),
15 and

16 “(B) such amount would be allowable as a
17 deduction under this section but for the fact
18 that the taxpayer receives (directly or indi-
19 rectly) as a result of paying such amount the
20 right to purchase tickets for seating at an ath-
21 letic event in an athletic stadium of such insti-
22 tution.

23 If any portion of a payment is for the purchase of
24 such tickets, such portion and the remaining portion

1 (if any) of such payment shall be treated as separate
2 amounts for purposes of this subsection.

3 “(h) OTHER CROSS REFERENCES.—

4 “(1) For treatment of certain organizations
5 providing child care, see section 501(k).

6 “(2) For charitable contributions of partners,
7 see section 702.

8 “(3) For treatment of gifts for benefit of or use
9 in connection with the Naval Academy as gifts to or
10 for the use of the United States, see section 6973
11 of title 10, United States Code.

12 “(4) For treatment of gifts accepted by the
13 Secretary of State, the Director of the International
14 Communication Agency, or the Director of the
15 United States International Development Cooper-
16 ation Agency, as gifts to or for the use of the United
17 States, see section 25 of the State Department Basic
18 Authorities Act of 1956.

19 “(5) For treatment of gifts of money accepted
20 by the Attorney General for credit to the ‘Com-
21 missary Funds, Federal Prisons’ as gifts to or for
22 the use of the United States, see section 4043 of
23 title 18, United States Code.

1 “(6) For charitable contributions to or for the
2 use of Indian tribal governments (or subdivisions of
3 such governments), see section 7871.

4 **“SEC. 4. DEDUCTION FOR HOME ACQUISITION INDEBTED-**
5 **NESS.**

6 “(a) GENERAL RULE.—For purposes of this part,
7 there shall be allowed as a deduction all qualified residence
8 interest paid or accrued within the taxable year.

9 “(b) QUALIFIED RESIDENCE INTEREST DEFINED.—
10 The term ‘qualified residence interest’ means any interest
11 which is paid or accrued during the taxable year on acqui-
12 sition indebtedness with respect to any qualified residence
13 of the taxpayer. For purposes of the preceding sentence,
14 the determination of whether any property is a qualified
15 residence of the taxpayer shall be made as of the time
16 the interest is accrued.

17 “(c) ACQUISITION INDEBTEDNESS.—

18 “(1) IN GENERAL.—The term ‘acquisition in-
19 debt edness’ means any indebtedness which—

20 “(A) is incurred in acquiring, constructing,
21 or substantially improving any qualified resi-
22 dence of the taxpayer, and

23 “(B) is secured by such residence.

24 Such term also includes any indebtedness secured by
25 such residence resulting from the refinancing of in-

1 debtiness meeting the requirements of the pre-
2 ceding sentence (or this sentence); but only to the
3 extent the amount of the indebtedness resulting
4 from such refinancing does not exceed the amount of
5 the refinanced indebtedness.

6 “(2) \$100,000 LIMITATION.—The aggregate
7 amount treated as acquisition indebtedness for any
8 period shall not exceed \$100,000 (\$50,000 in the
9 case of a married individual filing a separate re-
10 turn).

11 “(d) TREATMENT OF INDEBTEDNESS INCURRED ON
12 OR BEFORE OCTOBER 13, 1987.—

13 “(1) IN GENERAL.—In the case of any pre-Oc-
14 tober 13, 1987, indebtedness—

15 “(A) such indebtedness shall be treated as
16 acquisition indebtedness, and

17 “(B) the limitation of subsection (c)(2)
18 shall not apply.

19 “(2) REDUCTION IN \$100,000 LIMITATION.—The
20 limitation of subsection (c)(2) shall be reduced (but
21 not below zero) by the aggregate amount of out-
22 standing pre-October 13, 1987, indebtedness.

23 “(3) PRE-OCTOBER 13, 1987, INDEBTEDNESS.—
24 The term ‘pre-October 13, 1987, indebtedness’
25 means—

1 “(A) any indebtedness which was incurred
2 on or before October 13, 1987, and which was
3 secured by a qualified residence on October 13,
4 1987, and at all times thereafter before the in-
5 terest is paid or accrued, or

6 “(B) any indebtedness which is secured by
7 the qualified residence and was incurred after
8 October 13, 1987, to refinance indebtedness de-
9 scribed in subparagraph (A) (or refinanced in-
10 debt edness meeting the requirements of this
11 subparagraph) to the extent (immediately after
12 the refinancing) the principal amount of the in-
13 debt edness resulting from the refinancing does
14 not exceed the principal amount of the refi-
15 nanced indebtedness (immediately before the re-
16 financing).

17 “(4) LIMITATION ON PERIOD OF REFI-
18 NANCING.—Subparagraph (B) of paragraph (3)
19 shall not apply to any indebtedness after—

20 “(A) the expiration of the term of the in-
21 debt edness described in paragraph (3)(A), or

22 “(B) if the principal of the indebtedness
23 described in paragraph (3)(A) is not amortized
24 over its term, the expiration of the term of the
25 first refinancing of such indebtedness (or if ear-

1 lier, the date which is 30 years after the date
2 of such first refinancing).

3 “(e) OTHER DEFINITIONS AND SPECIAL RULES.—

4 For purposes of this section—

5 “(1) QUALIFIED RESIDENCE.—For purposes of
6 this subsection—

7 “(A) IN GENERAL.—Except as provided in
8 subparagraph (C), the term ‘qualified residence’
9 means the principal residence of the taxpayer.

10 “(B) MARRIED INDIVIDUALS FILING SEPA-
11 RATE RETURNS.—If a married couple does not
12 file a joint return for the taxable year—

13 “(i) such couple shall be treated as 1
14 taxpayer for purposes of subparagraph
15 (A), and

16 “(ii) each individual shall be entitled
17 to take into account $\frac{1}{2}$ of the principal
18 residence unless both individuals consent
19 in writing to 1 individual taking into ac-
20 count the principal residence.

21 “(C) PRE-OCTOBER 13, 1987, INDEBTED-
22 NESS.—In the case of any pre-October 13,
23 1987, indebtedness, the term ‘qualified resi-
24 dence’ has the meaning given that term in sec-

“(2) SPECIAL RULE FOR COOPERATIVE HOUSING CORPORATIONS.—Any indebtedness secured by stock held by the taxpayer as a tenant-stockholder in a cooperative housing corporation shall be treated as secured by the house or apartment which the taxpayer is entitled to occupy as such a tenant-stockholder. If stock described in the preceding sentence may not be used to secure indebtedness, indebtedness shall be treated as so secured if the taxpayer establishes to the satisfaction of the Secretary that such indebtedness was incurred to acquire such stock.

15 “(3) UNENFORCEABLE SECURITY INTERESTS.—
16 Indebtedness shall not fail to be treated as secured
17 by any property solely because, under any applicable
18 State or local homestead or other debtor protection
19 law in effect on August 16, 1986, the security inter-
20 est is ineffective or the enforceability of the security
21 interest is restricted.

22 “(4) SPECIAL RULES FOR ESTATES AND
23 TRUSTS.—For purposes of determining whether any
24 interest paid or accrued by an estate or trust is
25 qualified residence interest, any residence held by

1 such estate or trust shall be treated as a qualified
2 residence of such estate or trust if such estate or
3 trust establishes that such residence is a qualified
4 residence of a beneficiary who has a present interest
5 in such estate or trust or an interest in the resid-
6 uary of such estate or trust.

7 **“SEC. 5. DEFINITIONS AND SPECIAL RULES.**

8 “(a) DEFINITION OF SURVIVING SPOUSE.—

9 “(1) IN GENERAL.—For purposes of this part,
10 the term ‘surviving spouse’ means a taxpayer—

11 “(A) whose spouse died during either of
12 the taxpayer’s 2 taxable years immediately pre-
13 ceding the taxable year, and

14 “(B) who maintains as the taxpayer’s
15 home a household which constitutes for the tax-
16 able year the principal place of abode (as a
17 member of such household) of a dependent—

18 “(i) who (within the meaning of sub-
19 section (d)) is a son, stepson, daughter, or
20 stepdaughter of the taxpayer, and

21 “(ii) with respect to whom the tax-
22 payer is entitled to a deduction for the tax-
23 able year under section 2.

24 For purposes of this paragraph, an individual shall
25 be considered as maintaining a household only if

1 over one-half of the cost of maintaining the house-
2 hold during the taxable year is furnished by such in-
3 dividual.

4 “(2) LIMITATIONS.—Notwithstanding para-
5 graph (1), for purposes of this part a taxpayer shall
6 not be considered to be a surviving spouse—

7 “(A) if the taxpayer has remarried at any
8 time before the close of the taxable year, or

9 “(B) unless, for the taxpayer’s taxable
10 year during which the taxpayer’s spouse died, a
11 joint return could have been made under the
12 provisions of section 6013 (without regard to
13 subsection (a)(3) thereof).

14 “(3) SPECIAL RULE WHERE DECEASED SPOUSE
15 WAS IN MISSING STATUS.—If an individual was in a
16 missing status (within the meaning of section
17 6013(f)(3)) as a result of service in a combat zone
18 and if such individual remains in such status until
19 the date referred to in subparagraph (A) or (B),
20 then, for purposes of paragraph (1)(A), the date on
21 which such individual dies shall be treated as the
22 earlier of the date determined under subparagraph
23 (A) or the date determined under subparagraph (B):

24 “(A) The date on which the determination
25 is made under section 556 of title 37 of the

1 United States Code or under section 5566 of
2 title 5 of such Code (whichever is applicable)
3 that such individual died while in such missing
4 status.

5 “(B) Except in the case of the combat
6 zone designated for purposes of the Vietnam
7 conflict, the date which is 2 years after the date
8 designated as the date of termination of com-
9 batant activities in that zone.

10 “(b) DEFINITION OF HEAD OF HOUSEHOLD.—

11 “(1) IN GENERAL.—For purposes of this part,
12 an individual shall be considered a head of a house-
13 hold if, and only if, such individual is not married
14 at the close of such individual’s taxable year, is not
15 a surviving spouse (as defined in subsection (a)),
16 and either—

17 “(A) maintains as such individual’s home a
18 household which constitutes for more than one-
19 half of such taxable year the principal place of
20 abode, as a member of such household, of—

21 “(i) a son, stepson, daughter, or step-
22 daughter of the taxpayer, or a descendant
23 of a son or daughter of the taxpayer, but
24 if such son, stepson, daughter, step-
25 daughter, or descendant is married at the

1 close of the taxpayer's taxable year, only if
2 the taxpayer is entitled to a deduction for
3 the taxable year for such person under sec-
4 tion 2 (or would be so entitled but for sub-
5 paragraph (B) or (D) of subsection
6 (d)(5)), or

7 “(ii) any other person who is a de-
8 pendent of the taxpayer, if the taxpayer is
9 entitled to a deduction for the taxable year
10 for such person under section 2, or

11 “(B) maintains a household which con-
12 stitutes for such taxable year the principal place
13 of abode of the father or mother of the tax-
14 payer, if the taxpayer is entitled to a deduction
15 for the taxable year for such father or mother
16 under section 2.

17 For purposes of this paragraph, an individual shall
18 be considered as maintaining a household only if
19 over one-half of the cost of maintaining the house-
20 hold during the taxable year is furnished by such in-
21 dividual.

22 “(2) DETERMINATION OF STATUS.—For pur-
23 poses of this subsection—

1 “(A) a legally adopted child of a person
2 shall be considered a child of such person by
3 blood,

4 “(B) an individual who is legally separated
5 from such individual’s spouse under a decree of
6 divorce or of separate maintenance shall not be
7 considered as married,

8 “(C) a taxpayer shall be considered as not
9 married at the close of such taxpayer’s taxable
10 year if at any time during the taxable year such
11 taxpayer’s spouse is a nonresident alien, and

12 “(D) a taxpayer shall be considered as
13 married at the close of such taxpayer’s taxable
14 year if such taxpayer’s spouse (other than a
15 spouse described in subparagraph (C)) died
16 during the taxable year.

17 “(3) LIMITATIONS.—Notwithstanding para-
18 graph (1), for purposes of this part, a taxpayer shall
19 not be considered to be a head of a household—

20 “(A) if at any time during the taxable year
21 the taxpayer is a nonresident alien, or

22 “(B) by reason of an individual who would
23 not be a dependent for the taxable year but
24 for—

1 “(i) subparagraph (I) of subsection
2 (d)(1), or

3 “(ii) paragraph (3) of subsection (d).

4 “(c) CERTAIN MARRIED INDIVIDUALS LIVING
5 APART.—For purposes of this part, an individual shall be
6 treated as not married at the close of the taxable year
7 if such individual is so treated under the provisions of sec-
8 tion 7703(b).

9 “(d) DEPENDENT DEFINED.—

10 “(1) GENERAL DEFINITION.—For purposes of
11 this part, the term ‘dependent’ means any of the fol-
12 lowing individuals over one-half of whose support,
13 for the calendar year in which the taxable year of
14 the taxpayer begins, was received from the taxpayer
15 (or is treated under paragraph (3) or (5) as received
16 from the taxpayer):

17 “(A) A son or daughter of the taxpayer, or
18 a descendant of either.

19 “(B) A stepson or stepdaughter of the tax-
20 payer.

21 “(C) A brother, sister, stepbrother, or
22 stepsister of the taxpayer.

23 “(D) The father or mother of the taxpayer,
24 or an ancestor of either.

1 “(E) A stepfather or stepmother of the
2 taxpayer.

3 “(F) A son or daughter of a brother or sis-
4 ter of the taxpayer.

5 “(G) A brother or sister of the father or
6 mother of the taxpayer.

7 “(H) A son-in-law, daughter-in-law, father-
8 in-law, mother-in-law, brother-in-law, or sister-
9 in-law of the taxpayer.

10 “(I) An individual (other than an indi-
11 vidual who at any time during the taxable year
12 was the spouse, determined without regard to
13 section 7703, of the taxpayer) who, for the tax-
14 able year of the taxpayer, has as such individ-
15 ual’s principal place of abode the home of the
16 taxpayer and is a member of the taxpayer’s
17 household.

18 “(2) RULES RELATING TO GENERAL DEFINI-
19 TION.—For purposes of this section—

20 “(A) BROTHER; SISTER.—The terms
21 ‘brother’ and ‘sister’ include a brother or sister
22 by the halfblood.

23 “(B) CHILD.—In determining whether any
24 of the relationships specified in paragraph (1)
25 or subparagraph (A) of this paragraph exists, a

1 legally adopted child of an individual (and a
2 child who is a member of an individual's house-
3 hold, if placed with such individual by an au-
4 thorized placement agency for legal adoption by
5 such individual), or a foster child of an indi-
6 vidual (if such child satisfies the requirements
7 of paragraph (1)(I) with respect to such indi-
8 vidual), shall be treated as a child of such indi-
9 vidual by blood.

10 “(C) CITIZENSHIP.—The term ‘dependent’
11 does not include any individual who is not a cit-
12 izen or national of the United States unless
13 such individual is a resident of the United
14 States or of a country contiguous to the United
15 States. The preceding sentence shall not ex-
16 clude from the definition of ‘dependent’ any
17 child of the taxpayer legally adopted by such
18 taxpayer, if, for the taxable year of the tax-
19 payer, the child has as such child's principal
20 place of abode the home of the taxpayer and is
21 a member of the taxpayer's household, and
22 if the taxpayer is a citizen or national of the
23 United States.

24 “(D) ALIMONY, ETC.—A payment to a wife
25 which is alimony or separate maintenance shall

1 not be treated as a payment by the wife's hus-
2 band for the support of any dependent.

3 “(E) UNLAWFUL ARRANGEMENTS.—An in-
4 dividual is not a member of the taxpayer's
5 household if at any time during the taxable
6 year of the taxpayer the relationship between
7 such individual and the taxpayer is in violation
8 of local law.

9 “(3) MULTIPLE SUPPORT AGREEMENTS.—For
10 purposes of paragraph (1), over one-half of the sup-
11 port of an individual for a calendar year shall be
12 treated as received from the taxpayer if—

13 “(A) no one person contributed over one-
14 half of such support,

15 “(B) over one-half of such support was re-
16 ceived from persons each of whom, but for the
17 fact that such person did not contribute over
18 one-half of such support, would have been enti-
19 tled to claim such individual as a dependent for
20 a taxable year beginning in such calendar year,

21 “(C) the taxpayer contributed over 10 per-
22 cent of such support, and

23 “(D) each person described in subpara-
24 graph (B) (other than the taxpayer) who con-
25 tributed over 10 percent of such support files a

1 written declaration (in such manner and form
2 as the Secretary may by regulations prescribe)
3 that such person will not claim such individual
4 as a dependent for any taxable year beginning
5 in such calendar year.

6 “(4) SPECIAL SUPPORT TEST IN CASE OF STU-
7 DENTS.—For purposes of paragraph (1), in the case
8 of any individual who is—

9 “(A) a son, stepson, daughter, or step-
10 daughter of the taxpayer (within the meaning
11 of this subsection), and

12 “(B) a student,
13 amounts received as scholarships for study at an
14 educational organization described in section
15 3(d)(1)(B) shall not be taken into account in deter-
16 mining whether such individual received more than
17 one-half of such individual’s support from the tax-
18 payer.

19 “(5) SUPPORT TEST IN CASE OF CHILD OF DI-
20 VORCED PARENTS, ETC.—

21 “(A) CUSTODIAL PARENT GETS EXEMP-
22 TION.—Except as otherwise provided in this
23 paragraph, if—

1 “(i) a child receives over one-half of
2 such child’s support during the calendar
3 year from such child’s parents—

4 “(I) who are divorced or legally
5 separated under a decree of divorce or
6 separate maintenance,

7 “(II) who are separated under a
8 written separation agreement, or

9 “(III) who live apart at all times
10 during the last 6 months of the cal-
11 endar year, and

12 “(ii) such child is in the custody of 1
13 or both of such child’s parents for more
14 than one-half of the calendar year,

15 such child shall be treated, for purposes of
16 paragraph (1), as receiving over one-half of
17 such child’s support during the calendar year
18 from the parent having custody for a greater
19 portion of the calendar year (hereafter in this
20 paragraph referred to as the ‘custodial parent’).

21 “(B) EXCEPTION WHERE CUSTODIAL PAR-
22 ENT RELEASES CLAIM TO EXEMPTION FOR THE
23 YEAR.—A child of parents described in sub-
24 paragraph (A) shall be treated as having re-
25 ceived over one-half of such child’s support dur-

14 For purposes of this paragraph, the term ‘non-
15 custodial parent’ means the parent who is not
16 the custodial parent.

17 “(C) EXCEPTION FOR MULTIPLE-SUPPORT
18 AGREEMENT.—This paragraph shall not apply
19 in any case where over one-half of the support
20 of the child is treated as having been received
21 from a taxpayer under the provisions of para-
22 graph (3).

23 “(D) EXCEPTION FOR CERTAIN PRE-1985
24 INSTRUMENTS.—

1 “(i) IN GENERAL.—A child of parents
2 described in subparagraph (A) shall be
3 treated as having received over one-half
4 such child’s support during a calendar year
5 from the noncustodial parent if—

6 “(I) a qualified pre-1985 instru-
7 ment between the parents applicable
8 to the taxable year beginning in such
9 calendar year provides that the non-
10 custodial parent shall be entitled to
11 any deduction allowable under section
12 2 for such child, and

13 “(II) the noncustodial parent
14 provides at least \$600 for the support
15 of such child during such calendar
16 year.

17 For purposes of this clause, amounts ex-
18 pended for the support of a child or chil-
19 dren shall be treated as received from the
20 noncustodial parent to the extent that such
21 parent provided amounts for such support.

22 “(ii) QUALIFIED PRE-1985 INSTRU-
23 MENT.—For purposes of this subpara-
24 graph, the term ‘qualified pre-1985 instru-

19 **“PART II—TAX ON BUSINESS ACTIVITIES**

“Sec. 11. Tax imposed on business activities.

20 "SEC. 11. TAX IMPOSED ON BUSINESS ACTIVITIES.

21 “(a) TAX IMPOSED.—There is hereby imposed on
22 every person engaged in a business activity located in the
23 United States a tax equal to 20 percent of the business
24 taxable income of such person.

1 “(b) LIABILITY FOR TAX.—The tax imposed by this
2 section shall be paid by the person engaged in the business
3 activity, whether such person is an individual, partnership,
4 corporation, or otherwise.

5 “(c) BUSINESS TAXABLE INCOME.—

6 “(1) IN GENERAL.—For purposes of this sec-
7 tion, the term ‘business taxable income’ means gross
8 active income reduced by the deductions specified in
9 subsection (d).

10 “(2) GROSS ACTIVE INCOME.—For purposes of
11 paragraph (1), the term ‘gross active income’ means
12 gross income other than investment income.

13 “(d) DEDUCTIONS.—

14 “(1) IN GENERAL.—The deductions specified in
15 this subsection are—

16 “(A) the cost of business inputs for the
17 business activity,

18 “(B) the compensation (including contribu-
19 tions to qualified retirement plans but not in-
20 cluding other fringe benefits) paid for employ-
21 ees performing services in such activity, and

22 “(C) the cost of personal and real property
23 used in such activity.

24 “(2) BUSINESS INPUTS.—

1 “(A) IN GENERAL.—For purposes of para-
2 graph (1)(A), the term ‘cost of business inputs’
3 means—

4 “(i) the actual cost of goods, services,
5 and materials, whether or not resold dur-
6 ing the taxable year, and

7 “(ii) the actual cost, if reasonable, of
8 travel and entertainment expenses for busi-
9 ness purposes.

10 “(B) PURCHASES OF GOODS AND SERV-
11 ICES EXCLUDED.—Such term shall not include
12 purchases of goods and services provided to em-
13 ployees or owners.

14 “(C) CERTAIN LOBBYING AND POLITICAL
15 EXPENDITURES EXCLUDED.—

16 “(i) IN GENERAL.—Such term shall
17 not include any amount paid or incurred in
18 connection with—

19 “(I) influencing legislation,

20 “(II) participation in, or inter-
21 vention in, any political campaign on
22 behalf of (or in opposition to) any
23 candidate for public office,

24 “(III) any attempt to influence
25 the general public, or segments there-

1 of, with respect to elections, legislative
2 matters, or referendums, or

3 “(IV) any direct communication
4 with a covered executive branch offi-
5 cial in an attempt to influence the of-
6 ficial actions or positions of such offi-
7 cial.

8 “(ii) EXCEPTION FOR LOCAL LEGISLA-
9 TION.—In the case of any legislation of
10 any local council or similar governing
11 body—

12 “(I) clause (i)(I) shall not apply,
13 and

14 “(II) such term shall include all
15 ordinary and necessary expenses (in-
16 cluding, but not limited to, traveling
17 expenses described in subparagraph
18 (A)(iii) and the cost of preparing tes-
19 timony) paid or incurred during the
20 taxable year in carrying on any trade
21 or business—

22 “(aa) in direct connection
23 with appearances before, submis-
24 sion of statements to, or sending
25 communications to the commit-

tees, or individual members, of such council or body with respect to legislation or proposed legislation of direct interest to the taxpayer, or

“(bb) in direct connection with communication of information between the taxpayer and an organization of which the taxpayer is a member with respect to any such legislation or proposed legislation which is of direct interest to the taxpayer and to such organization, and that portion of the dues so paid or incurred with respect to any organization of which the taxpayer is a member which is attributable to the expenses of the activities carried on by such organization.

“(iii) APPLICATION TO DUES OF TAX-

EXEMPT ORGANIZATIONS.—Such term shall include the portion of dues or other similar amounts paid by the taxpayer to an organization which is exempt from tax

1 under this subtitle which the organization
2 notifies the taxpayer under section
3 6033(e)(1)(A)(ii) is allocable to expendi-
4 tures to which clause (i) applies.

6 For purposes of this subparagraph—

1 behalf of another person (but shall
2 apply to payments by such other per-
3 son to the taxpayer for conducting
4 such activities).

5 “(II) DE MINIMIS EXCEPTION.—

6 “(aa) IN GENERAL.—Clause
7 (i) shall not apply to any in-
8 house expenditures for any tax-
9 able year if such expenditures do
10 not exceed \$2,000. In deter-
11 mining whether a taxpayer ex-
12 ceeds the \$2,000 limit, there
13 shall not be taken into account
14 overhead costs otherwise allocable
15 to activities described in sub-
16 clauses (I) and (IV) of clause (i).

17 “(bb) IN-HOUSE EXPENDI-
18 TURES.—For purposes of provi-
19 sion (aa), the term ‘in-house ex-
20 penditures’ means expenditures
21 described in subclauses (I) and
22 (IV) of clause (i) other than pay-
23 ments by the taxpayer to a per-
24 son engaged in the trade or busi-
25 ness of conducting activities de-

1 scribed in clause (i) for the con-
2 duct of such activities on behalf
3 of the taxpayer, or dues or other
4 similar amounts paid or incurred
5 by the taxpayer which are allo-
6 cable to activities described in
7 clause (i).

21 “(II) the Vice President,

“For reporting requirements and alternative taxes related to this subsection, see section 6033(e).”

18 "(e) CARRYOVER OF EXCESS DEDUCTIONS.—

19 “(1) IN GENERAL.—If the aggregate deductions
20 for any taxable year exceed the gross active income
21 for such taxable year, the amount of the deductions
22 specified in subsection (d) for the succeeding taxable
23 year (determined without regard to this subsection)
24 shall be increased by the sum of—

1 “(A) such excess, plus
2 “(B) the product of such excess and the 3-
3 month Treasury rate for the last month of such
4 taxable year.

5 “(2) 3-MONTH TREASURY RATE.—For purposes
6 of paragraph (1), the 3-month Treasury rate is the
7 rate determined by the Secretary based on the aver-
8 age market yield (during any 1-month period se-
9 lected by the Secretary and ending in the calendar
10 month in which the determination is made) on out-
11 standing marketable obligations of the United States
12 with remaining periods to maturity of 3 months or
13 less.”

14 (b) CONFORMING REPEALS AND REDESIGNATIONS.—

15 (1) REPEALS.—The following subchapters of
16 chapter 1 of subtitle A and the items relating to
17 such subchapters in the table of subchapters for
18 such chapter 1 are repealed:

19 (A) Subchapter B (relating to computation
20 of taxable income).

21 (B) Subchapter C (relating to corporate
22 distributions and adjustments).

23 (C) Subchapter D (relating to deferred
24 compensation, etc.).

1 (D) Subchapter G (relating to corporations
2 used to avoid income tax on shareholders).

3 (E) Subchapter H (relating to banking in-
4 stitutions).

5 (F) Subchapter I (relating to natural re-
6 sources).

7 (G) Subchapter J (relating to estates,
8 trusts, beneficiaries, and decedents).

11 (I) Subchapter M (relating to regulated in-
12 vestment companies and real estate investment
13 trusts).

14 (J) Subchapter N (relating to tax based on
15 income from sources within or without the
16 United States).

17 (K) Subchapter O (relating to gain or loss
18 on disposition of property)

19 (L) Subchapter P (relating to capital gains
20 and losses).

21 (M) Subchapter Q (relating to readjust-
22 ment of tax between years and special limita-
23 tions)

24 (N) Subchapter S (relating to tax treat-
25 ment of S corporations and their shareholders)

1 (O) Subchapter T (relating to cooperatives
2 and their patrons).

(P) Subchapter U (relating to designation and treatment of empowerment zones, enterprise communities, and rural development investment areas).

7 (Q) Subchapter V (relating to title 11
8 cases).

9 (R) Subchapter W (relating to District of
10 Columbia Enterprise Zone).

15 (A) Subchapter E (relating to accounting
16 periods and methods of accounting) as sub-
17 chapter B.

18 (B) Subchapter F (relating to exempt or-
19 ganizations) as subchapter C.

20 (C) Subchapter K (relating to partners
21 and partnerships) as subchapter D.

22 SEC. 3. REPEAL OF ESTATE AND GIFT TAXES.

23 Subtitle B (relating to estate, gift, and generation-
24 skipping taxes) and the item relating to such subtitle in
25 the table of subtitles is repealed.

1 **SEC. 4. ADDITIONAL REPEALS.**

2 Subtitles H (relating to financing of presidential elec-
3 tion campaigns) and J (relating to coal industry health
4 benefits) and the items relating to such subtitles in the
5 table of subtitles are repealed.

6 **SEC. 5. EFFECTIVE DATES.**

7 (a) IN GENERAL.—Except as provided in subsection
8 (b), the amendments made by this Act apply to taxable
9 years beginning after December 31, 2003.

10 (b) REPEAL OF ESTATE AND GIFT TAXES.—The re-
11 peal made by section 3 applies to estates of decedents
12 dying, and transfers made, after December 31, 2003.

13 (c) TECHNICAL AND CONFORMING CHANGES.—The
14 Secretary of the Treasury or the Secretary's delegate
15 shall, as soon as practicable but in any event not later
16 than 90 days after the date of enactment of this Act, sub-
17 mit to the Committee on Ways and Means of the House
18 of Representatives and the Committee on Finance of the
19 Senate a draft of any technical and conforming changes
20 in the Internal Revenue Code of 1986 which are necessary
21 to reflect throughout such Code the changes in the sub-
22 stantive provisions of law made by this Act.

○