

112TH CONGRESS
2D SESSION

S. 3595

To amend the Internal Revenue Code of 1986 to provide an exception from the passive loss rules for investments in high technology research small business pass-thru entities.

IN THE SENATE OF THE UNITED STATES

SEPTEMBER 20, 2012

Mr. MENENDEZ (for himself and Ms. SNOWE) 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 provide an exception from the passive loss rules for investments in high technology research small business pass-thru entities.

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. EXCEPTION FROM PASSIVE LOSS RULES FOR**
4 **INVESTMENTS IN HIGH TECHNOLOGY RE-**
5 **SEARCH SMALL BUSINESS PASS-THRU ENTI-**
6 **TIES.**

7 (a) IN GENERAL.—Subsection (c) of section 469 of
8 the Internal Revenue Code of 1986 is amended by redesignig-

1 nating paragraphs (4) through (7) as paragraphs (5)
 2 through (8), respectively, and by inserting after paragraph
 3 (3) the following new paragraph:

4 “(4) HIGH TECHNOLOGY RESEARCH ACTIVITIES.—
 5 TIES.—

6 “(A) IN GENERAL.—The term ‘passive ac-
 7 tivity’ shall not include any activity of the tax-
 8 payer carried on by a high technology research
 9 small business pass-thru entity.

10 “(B) HIGH TECHNOLOGY RESEARCH
 11 SMALL BUSINESS PASS-THRU ENTITY.—For
 12 purposes of this paragraph, the term ‘high tech-
 13 nology research small business pass-thru entity’
 14 means any domestic pass-thru entity for any
 15 taxable year if—

16 “(i) either—

17 “(I) more than 75 percent of the
 18 entity’s expenditures (including sala-
 19 ries, rent and overhead) for such tax-
 20 able year are paid or incurred in con-
 21 nection with qualified research (within
 22 the meaning of section 41(d)(1)(B)
 23 taking into account section 41(d)(4)
 24 and constituting elements of a process
 25 of experimentation for a purpose de-

scribed in paragraph (3) of section
41(d)), or

“(II) more than 50 percent of
the entity’s expenditures for such tax-
able year constitute qualified research
expenses (as defined in section 41(b),
but determined without regard to the
phrase ‘65 percent of’ in paragraph
(3)(A) thereof),

“(ii) such entity is a small business
(within the meaning of section
41(b)(3)(D)(iii) applied by substituting
‘250’ for ‘500’ in subclause (I) thereof),
and

“(iii) at no time during the taxable
year does the entity have aggregate gross
assets in excess of \$150,000,000.

“(C) PROVISIONS RELATED TO AGGREGATE
GROSS ASSETS LIMITATION.—For purposes of
this paragraph—

“(i) IN GENERAL.—Except as other-
wise provided in this subparagraph, the
term ‘aggregate gross assets’ has the
meaning given such term in section
1202(d)(2).

1 “(ii) EXCEPTION FOR CERTAIN IN-
2 TANGIBLES.—Any section 197 intangible
3 (as defined in section 197(d) and deter-
4 mined without regard to section 197(e))
5 which is used directly in connection with
6 the research referred to in subparagraph
7 (B)(i) shall not be taken into account in
8 determining aggregate gross assets.

9 “(iii) EXCEPTION FOR CERTAIN FOL-
10 LOW-ON INVESTMENTS.—Cash from a sale
11 of equity interests shall not be taken into
12 account in determining aggregate gross as-
13 sets if—

14 “(I) the aggregate gross assets of
15 such entity (determined immediately
16 after such sale and without regard to
17 this clause) do not exceed the sum of
18 \$150,000,000, plus 25 percent of the
19 aggregate gross assets of such entity
20 (determined immediately before such
21 sale and without regard to this
22 clause), and

23 “(II) the aggregate gross assets
24 of such entity (determined imme-
25 diately before such sale and without

1 regard to this clause) do not exceed
2 \$150,000,000.

3 Sales of equity interests which are part of
4 the same plan or arrangement, or which
5 are carried out with the principal purpose
6 of increasing the amount of cash to which
7 this clause applies (determined without re-
8 gard to this sentence), shall be treated as
9 a single sale for purposes of this clause.

10 “(iv) INFLATION ADJUSTMENT.—In
11 the case of any taxable year beginning
12 after 2013, the \$150,000,000 amount in
13 subparagraph (B)(iii) and subclauses (I)
14 and (II) of clause (iii) shall each be in-
15 creased by an amount equal to—

16 “(I) such dollar amount, multi-
17 plied by

18 “(II) the cost of living adjust-
19 ment determined under section 1(f)(3)
20 for the calendar year in which the tax-
21 able year begins determined by sub-
22 stituting ‘calendar year 2012’ for ‘cal-
23 endar year 1992’ in subparagraph (B)
24 thereof.

1 Any increase determined under the pre-
2 ceding sentence shall be rounded to the
3 nearest \$100,000.

4 “(D) CAPITAL EXPENDITURES TAKEN
5 INTO ACCOUNT FOR EXPENDITURES TEST.—An
6 expenditure shall not fail to be taken into ac-
7 count under subparagraph (B)(i) merely be-
8 cause such expenditure is chargeable to capital
9 account.

10 “(E) PASS-THRU ENTITY.—For purposes
11 of this paragraph, the term ‘pass-thru entity’
12 means any partnership, S corporation, or other
13 entity identified by the Secretary as a pass-thru
14 entity for purposes of this paragraph.

15 “(F) AGGREGATION RULES.—All persons
16 treated as a single employer under subsection
17 (a) or (b) of section 52, or subsection (m) or
18 (o) of section 414, shall be treated as a single
19 entity for purposes of subparagraphs (B) and
20 (C)(iii).

21 “(G) ACTIVITIES NOT ENGAGED IN FOR
22 PROFIT AND ECONOMIC SUBSTANCE RULES.—
23 Section 183 and the economic substance rules
24 of section 7701(o) shall not apply to disallow
25 the losses, deductions, and credits of a high

1 technology research small business pass-thru
 2 entity solely as a result of losses incurred by
 3 such entity.”.

4 (b) MATERIAL PARTICIPATION NOT REQUIRED.—
 5 Paragraph (5) of section 469(c) of such Code, as redesign-
 6 nated by subsection (a), is amended by striking “and (3)”
 7 in the heading and text and inserting “, (3), and (4)”.

8 (c) CERTAIN RESEARCH-RELATED DEDUCTIONS AND
 9 CREDITS OF HIGH TECHNOLOGY RESEARCH SMALL
 10 BUSINESS PASS-THRU ENTITIES ALLOWED FOR PUR-
 11 POSES OF DETERMINING ALTERNATIVE MINIMUM TAX.—

12 (1) DEDUCTION FOR RESEARCH AND EXPERI-
 13 MENTAL EXPENDITURES.—Paragraph (2) of section
 14 56(b) of such Code is amended by adding at the end
 15 the following new subparagraph:

16 “(E) EXCEPTION FOR HIGH TECHNOLOGY
 17 RESEARCH SMALL BUSINESS PASS-THRU ENTI-
 18 TIES.—In the case of a high technology re-
 19 search small business pass-thru entity (as de-
 20 fined in section 469(c)(4)), this paragraph shall
 21 not apply to any amount allowable as a deduc-
 22 tion under section 174(a).”.

23 (2) ALLOWANCE OF CERTAIN RESEARCH-RE-
 24 LATED CREDITS.—Subparagraph (B) of section
 25 38(c)(4) of such Code is amended by redesignating

1 clauses (ii) through (ix) as clauses (iii) through (x),
 2 respectively, and by inserting after clause (i) the fol-
 3 lowing new clause:

4 “(ii) the credits determined under sec-
 5 tions 41 and 48D to the extent attrib-
 6 utable to a high technology research small
 7 business pass-thru entity (as defined in
 8 section 469(c)(4)),”.

9 (d) EXCEPTION TO LIMITATION ON PASS-THRU OF
 10 RESEARCH CREDIT.—Subsection (g) of section 41 of such
 11 Code is amended by adding at the end the following:
 12 “Paragraphs (2) and (4) shall not apply with respect to
 13 any high technology research small business pass-thru en-
 14 tity (as defined in section 469(c)(4)).”

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

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