

--H.R.4520--

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*One Hundred Eighth Congress
of the
United States of America
AT THE SECOND SESSION*

Begun and held at the City of Washington on Tuesday,

the twentieth day of January, two thousand and four

An Act

To amend the Internal Revenue Code of 1986 to remove impediments in such Code and make our manufacturing, service, and high-technology businesses and workers more competitive and productive both at home and abroad.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE; ETC.

- (a) SHORT TITLE- This Act may be cited as the `American Jobs Creation Act of 2004'.
- (b) AMENDMENT OF 1986 CODE- Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.
- (c) TABLE OF CONTENTS- The table of contents of this Act is as follows:
Sec. 1. Short title; etc.

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- Sec. 101. Repeal of exclusion for extraterritorial income.
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TITLE I--PROVISIONS RELATING TO REPEAL OF EXCLUSION FOR EXTRATERRITORIAL INCOME

SEC. 101. REPEAL OF EXCLUSION FOR EXTRATERRITORIAL INCOME.

(a) IN GENERAL- Section 114 is hereby repealed.

(b) CONFORMING AMENDMENTS-

- (1) Subpart E of part III of subchapter N of chapter 1 (relating to qualifying foreign trade income) is hereby repealed.
- (2) The table of subparts for such part III is amended by striking the item relating to subpart E.
- (3) The table of sections for part III of subchapter B of chapter 1 is amended by striking the item relating to section 114.
- (4) The second sentence of section 56(g)(4)(B)(i) is amended by striking '114 or'.
- (5) Section 275(a) is amended--
 - (A) by inserting 'or' at the end of paragraph (4)(A), by striking 'or' at the end of paragraph (4)(B) and inserting a period, and by striking subparagraph (C), and
 - (B) by striking the last sentence.
- (6) Paragraph (3) of section 864(e) is amended--
 - (A) by striking:
 - '(3) TAX-EXEMPT ASSETS NOT TAKEN INTO ACCOUNT-
 - '(A) IN GENERAL- For purposes of'; and inserting:
 - '(3) TAX-EXEMPT ASSETS NOT TAKEN INTO ACCOUNT- For purposes of', and
 - (B) by striking subparagraph (B).
- (7) Section 903 is amended by striking '114, 164(a)', and inserting '164(a)'.
- (8) Section 999(c)(1) is amended by striking '941(a)(5)'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to transactions after December 31, 2004.

(d) TRANSITIONAL RULE FOR 2005 AND 2006-

- (1) IN GENERAL- In the case of transactions during 2005 or 2006, the amount includable in gross income by reason of the amendments made by this section shall not exceed the applicable percentage of the amount which would have been so included but for this subsection.
- (2) APPLICABLE PERCENTAGE- For purposes of paragraph (1), the applicable percentage shall be as follows:
 - (A) For 2005, the applicable percentage shall be 20 percent.
 - (B) For 2006, the applicable percentage shall be 40 percent.

(e) REVOCATION OF ELECTION TO BE TREATED AS DOMESTIC CORPORATION- If, during the 1-year period beginning on the date of the enactment of this Act, a corporation for which an election is in effect under section 943(e) of the Internal Revenue Code of 1986 revokes such election, no gain or loss shall be recognized with respect to property treated as transferred under clause (ii) of section 943(e)(4)(B) of such Code to the extent such property

- (1) was treated as transferred under clause (i) thereof, or
- (2) was acquired during a taxable year to which such election applies and before May 1, 2003, in the ordinary course of its trade or business.

The Secretary of the Treasury (or such Secretary's delegate) may prescribe such regulations as may be necessary to prevent the abuse of the purposes of this subsection.

(f) BINDING CONTRACTS- The amendments made by this section shall not apply to any transaction in the ordinary course of a trade or business which occurs pursuant to a binding contract--

- (1) which is between the taxpayer and a person who is not a related person (as defined in section 943(b)(3) of such Code, as in effect on the day before the date of the enactment of this Act), and
- (2) which is in effect on September 17, 2003, and at all times thereafter.

For purposes of this subsection, a binding contract shall include a purchase option, renewal option, or replacement option which is included in such contract and which is enforceable against the seller or lessor.

SEC. 102. DEDUCTION RELATING TO INCOME ATTRIBUTABLE TO DOMESTIC PRODUCTION ACTIVITIES.

(a) IN GENERAL- Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by adding at the end the following new section:

SEC. 199. INCOME ATTRIBUTABLE TO DOMESTIC PRODUCTION ACTIVITIES.

^(a) ALLOWANCE OF DEDUCTION-

^(1) IN GENERAL- There shall be allowed as a deduction an amount equal to 9 percent of the lesser of-

- ^(A) the qualified production activities income of the taxpayer for the taxable year, or
- ^(B) taxable income (determined without regard to this section) for the taxable year.

^(2) PHASEIN- In the case of any taxable year beginning after 2004 and before 2010, paragraph (1) and subsections (d)(1) and (d)(6) shall be applied by substituting for the percentage contained therein the transition percentage determined under the following table:

For taxable years

The transition

beginning in:

percentage is:

2005 or 2006

^(b) DEDUCTION LIMITED TO WAGES PAID-

^(1) IN GENERAL- The amount of the deduction allowable under subsection (a) for any taxable year shall not exceed 50 percent of the W-2 wages of the employer for the taxable year.

^(2) W-2 wages- For purposes of paragraph (1), the term 'W-2 wages' means the sum of the aggregate amounts the taxpayer is required to include on statements under paragraphs (3) and (8) of section 6051(a) with respect to employment of employees of the taxpayer during the calendar year ending during the taxpayer's taxable year.

^(3) ACQUISITIONS AND DISPOSITIONS- The Secretary shall provide for the application of this subsection in cases where the taxpayer acquires, or disposes of, the major portion of a trade or business or the major portion of a separate unit of a trade or business during the taxable year.

^(c) QUALIFIED PRODUCTION ACTIVITIES INCOME- For purposes of this section-

^(1) IN GENERAL- The term 'qualified production activities income' for any taxable year means an amount equal to the excess (if any) of-

^(A) the taxpayer's domestic production gross receipts for such taxable year, over

^(B) the sum of-

^(i) the cost of goods sold that are allocable to such receipts,

^(ii) other deductions, expenses, or losses directly allocable to such receipts, and

^(iii) a ratable portion of other deductions, expenses, and losses that are not directly allocable to such receipts or another class of income.

^(2) ALLOCATION METHOD- The Secretary shall prescribe rules for the proper allocation of items of income, deduction, expense, and loss for purposes of determining income attributable to domestic production activities.

^(3) SPECIAL RULES FOR DETERMINING COSTS-

^(A) IN GENERAL- For purposes of determining costs under clause (i) of paragraph (1)(B), any item or service brought into the United States shall be treated as acquired by purchase, and its cost shall be treated as not less than its value immediately after it entered the United States. A similar rule shall apply in determining the adjusted basis of leased or rented property where the lease or rental gives rise to domestic production gross receipts.

^(B) EXPORTS FOR FURTHER MANUFACTURE- In the case of any property described in subparagraph (A) that had been exported by the taxpayer for further manufacture, the increase in cost or adjusted basis under subparagraph (A) shall not exceed the difference between the value of the property when exported and the value of the property when brought back into the United States after the further manufacture.

^(4) DOMESTIC PRODUCTION GROSS RECEIPTS-

^(A) IN GENERAL- The term 'domestic production gross receipts' means the gross receipts of the taxpayer which are derived from-

^(i) any lease, rental, license, sale, exchange, or other disposition of-

^(I) qualifying production property which was manufactured, produced, grown, or extracted by the taxpayer in whole or in significant part within the United States,

^(II) any qualified film produced by the taxpayer, or

^(III) electricity, natural gas, or potable water produced by the taxpayer in the United States,

^(ii) construction performed in the United States, or

^(iii) engineering or architectural services performed in the United States for construction projects in the United States.

^(B) EXCEPTIONS- Such term shall not include gross receipts of the taxpayer which are derived from-

^(i) the sale of food and beverages prepared by the taxpayer at a retail establishment, and

^(ii) the transmission or distribution of electricity, natural gas, or potable water.

^(5) QUALIFYING PRODUCTION PROPERTY- The term 'qualifying production property' means--

^(A) tangible personal property,

^(B) any computer software, and

^(C) any property described in section 168(f)(4).

^(6) QUALIFIED FILM- The term 'qualified film' means any property described in section 168(f)(3) if not less than 50 percent of the total compensation relating to the production of such property is compensation for services performed in the United States by actors, production personnel, directors, and producers. Such term does not include property with respect to which records are required to be maintained under section 2257 of title 18, United States Code.

^(7) RELATED PERSONS-

^(A) IN GENERAL- The term 'domestic production gross receipts' shall not include any gross receipts of the taxpayer derived from property leased, licensed, or rented by the taxpayer for use by any related person.

^(B) RELATED PERSON- For purposes of subparagraph (A), a person shall be treated as related to another person if such persons are treated as a single employer under subsection (a) or (b) of section 52 or subsection (m) or (o) of section 414, except that determinations under subsections (a) and (b) of section 52 shall be made without regard to section 1563(b).

^(d) DEFINITIONS AND SPECIAL RULES-

^(1) APPLICATION OF SECTION TO PASS-THRU ENTITIES-

``(A) IN GENERAL- In the case of an S corporation, partnership, estate or trust, or other pass-thru entity--

``(i) subject to the provisions of paragraphs (2) and (3), this section shall be applied at the shareholder, partner, or similar level, and

``(ii) the Secretary shall prescribe rules for the application of this section, including rules relating to--

``(I) restrictions on the allocation of the deduction to taxpayers at the partner or similar level, and

``(II) additional reporting requirements.

``(B) APPLICATION OF WAGE LIMITATION- Notwithstanding subparagraph (A)(i), for purposes of applying subsection (b), a shareholder, partner, or similar person which is allocated qualified production activities income from an S corporation, partnership, estate, trust, or other pass-thru entity shall also be treated as having been allocated W-2 wages from such entity in an amount equal to the lesser of--

``(i) such person's allocable share of such wages (without regard to this subparagraph), as determined under regulations prescribed by the Secretary, or

``(ii) 2 times 9 percent of the qualified production activities income allocated to such person for the taxable year.

``(2) APPLICATION TO INDIVIDUALS- In the case of an individual, subsection (a)(1)(B) shall be applied by substituting 'adjusted gross income' for 'taxable income'. For purposes of the preceding sentence, adjusted gross income shall be determined--

``(A) after application of sections 86, 135, 137, 219, 221, 222, and 469, and

``(B) without regard to this section.

``(3) PATRONS OF AGRICULTURAL AND HORTICULTURAL COOPERATIVES-

``(A) IN GENERAL- If any amount described in paragraph (1) or (3) of section 1385(a)--

``(i) is received by a person from an organization to which part I of subchapter T applies which is engaged--

``(I) in the manufacturing, production, growth, or extraction in whole or significant part of any agricultural or horticultural product, or

``(II) in the marketing of agricultural or horticultural products, and

``(ii) is allocable to the portion of the qualified production activities income of the organization which, but for this paragraph, would be deductible under subsection (a) by the organization and is designated as such by the organization in a written notice mailed to its patrons during the payment period described in section 1382(d),

then such person shall be allowed a deduction under subsection (a) with respect to such amount. The taxable income of the organization shall not be reduced under section 1382 by reason of any amount to which the preceding sentence applies.

^(B) SPECIAL RULES- For purposes of applying subparagraph (A), in determining the qualified production activities income which would be deductible by the organization under subsection (a)--

^(i) there shall not be taken into account in computing the organization's taxable income any deduction allowable under subsection (b) or (c) of section 1382 (relating to patronage dividends, per-unit retain allocations, and nonpatronage distributions), and

^(ii) in the case of an organization described in subparagraph (A)(i)(II), the organization shall be treated as having manufactured, produced, grown, or extracted in whole or significant part any qualifying production property marketed by the organization which its patrons have so manufactured, produced, grown, or extracted.

^(4) SPECIAL RULE FOR AFFILIATED GROUPS-

^(A) IN GENERAL- All members of an expanded affiliated group shall be treated as a single corporation for purposes of this section.

^(B) EXPANDED AFFILIATED GROUP- For purposes of this section, the term 'expanded affiliated group' means an affiliated group as defined in section 1504(a), determined--

^(i) by substituting '50 percent' for '80 percent' each place it appears, and

^(ii) without regard to paragraphs (2) and (4) of section 1504(b).

^(C) ALLOCATION OF DEDUCTION- Except as provided in regulations, the deduction under subsection (a) shall be allocated among the members of the expanded affiliated group in proportion to each member's respective amount (if any) of qualified production activities income.

^(5) TRADE OR BUSINESS REQUIREMENT- This section shall be applied by only taking into account items which are attributable to the actual conduct of a trade or business.

^(6) COORDINATION WITH MINIMUM TAX- The deduction under this section shall be allowed for purposes of the tax imposed by section 55; except that for purposes of section 55, the deduction under subsection (a) shall be 9 percent of the lesser of--

^(A) qualified production activities income (determined without regard to part IV of subchapter A), or

^(B) alternative minimum taxable income (determined without regard to this section) for the taxable year.

In the case of an individual, subparagraph (B) shall be applied by substituting 'adjusted gross income' for 'alternative minimum taxable income'. For purposes of the preceding sentence, adjusted gross income shall be determined in the same manner as provided in paragraph (2).

'(7) REGULATIONS- The Secretary shall prescribe such regulations as are necessary to carry out the purposes of this section.'

(b) MINIMUM TAX- Section 56(g)(4)(C) (relating to disallowance of items not deductible in computing earnings and profits) is amended by adding at the end the following new clause:

'(v) DEDUCTION FOR DOMESTIC PRODUCTION-

Clause (i) shall not apply to any amount allowable as a deduction under section 199.'

(c) SPECIAL RULE RELATING TO ELECTION TO TREAT CUTTING OF TIMBER AS A SALE OR EXCHANGE- Any election under section 631(a) of the Internal Revenue Code of 1986 made for a taxable year ending on or before the date of the enactment of this Act may be revoked by the taxpayer for any taxable year ending after such date. For purposes of determining whether such taxpayer may make a further election under such section, such election (and any revocation under this section) shall not be taken into account.

(d) TECHNICAL AMENDMENTS-

(1) Sections 86(b)(2)(A), 135(c)(4)(A), 137(b)(3)(A), and 219(g)(3)(A)(ii) are each amended by inserting '199,' before '221'.

(2) Clause (i) of section 221(b)(2)(C) is amended by inserting by inserting '199,' before '222'.

(3) Clause (i) of section 222(b)(2)(C) is amended by inserting '199,' before '911'.

(4) Paragraph (1) of section 246(b) is amended by inserting '199,' after '172,'.

(5) Clause (iii) of section 469(i)(3)(F) is amended by inserting '199,' before '219,'.

(6) Subsection (a) of section 613 is amended by inserting 'and without the deduction under section 199' after 'without allowances for depletion'.

(7) Subsection (a) of section 1402 is amended by striking 'and' at the end of paragraph (14), by striking the period at the end of paragraph (15) and inserting ' , and', and by inserting after paragraph (15) the following new paragraph:

'(16) the deduction provided by section 199 shall not be allowed.'

(8) The table of sections for part VI of subchapter B of chapter 1 is amended by adding at the end the following new item:

'Sec. 199. Income attributable to domestic production activities.'

(e) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years beginning after December 31, 2004.

TITLE II--BUSINESS TAX INCENTIVES

Subtitle A--Small Business Expensing

SEC. 201. 2-YEAR EXTENSION OF INCREASED EXPENSING FOR SMALL BUSINESS.

Subsections (b), (c), and (d) of section 179 are each amended by striking `2006' each place it appears and inserting `2008'.

Subtitle B--Depreciation

SEC. 211. RECOVERY PERIOD FOR DEPRECIATION OF CERTAIN LEASEHOLD IMPROVEMENTS AND RESTAURANT PROPERTY.

(a) 15-YEAR RECOVERY PERIOD- Subparagraph (E) of section 168(e)(3) (relating to classification of certain property) is amended by striking `and' at the end of clause (ii), by striking the period at the end of clause (iii) and inserting a comma, and by adding at the end the following new clauses:

- ` (iv) any qualified leasehold improvement property placed in service before January 1, 2006, and
- ` (v) any qualified restaurant property placed in service before January 1, 2006.'

(b) QUALIFIED LEASEHOLD IMPROVEMENT PROPERTY- Subsection (e) of section 168 is amended by adding at the end the following new paragraph:

`(6) QUALIFIED LEASEHOLD IMPROVEMENT PROPERTY- The term `qualified leasehold improvement property' has the meaning given such term in section 168(k)(3) except that the following special rules shall apply:

`(A) IMPROVEMENTS MADE BY LESSOR- In the case of an improvement made by the person who was the lessor of such improvement when such improvement was placed in service, such improvement shall be qualified leasehold improvement property (if at all) only so long as such improvement is held by such person.

`(B) EXCEPTION FOR CHANGES IN FORM OF BUSINESS- Property shall not cease to be qualified leasehold improvement property under subparagraph (A) by reason of-

- ` (i) death,
- ` (ii) a transaction to which section 381(a) applies,
- ` (iii) a mere change in the form of conducting the trade or business so long as the property is retained in such trade or business as qualified leasehold improvement property and the taxpayer retains a substantial interest in such trade or business,
- ` (iv) the acquisition of such property in an exchange described in section 1031, 1033, or 1038 to the extent that the basis of such property includes an amount representing

the adjusted basis of other property owned by the taxpayer or a related person, or

``(v) the acquisition of such property by the taxpayer in a transaction described in section 332, 351, 361, 721, or 731 (or the acquisition of such property by the taxpayer from the transferee or acquiring corporation in a transaction described in such section), to the extent that the basis of the property in the hands of the taxpayer is determined by reference to its basis in the hands of the transferor or distributor.'.

(c) **QUALIFIED RESTAURANT PROPERTY**- Subsection (e) of section 168 (as amended by subsection (b)) is further amended by adding at the end the following new paragraph:

``(7) **QUALIFIED RESTAURANT PROPERTY**- The term `qualified restaurant property' means any section 1250 property which is an improvement to a building if--

``(A) such improvement is placed in service more than 3 years after the date such building was first placed in service, and

``(B) more than 50 percent of the building's square footage is devoted to preparation of, and seating for on-premises consumption of, prepared meals.'.

(d) **REQUIREMENT TO USE STRAIGHT LINE METHOD**-

(1) Paragraph (3) of section 168(b) is amended by adding at the end the following new subparagraphs:

``(G) Qualified leasehold improvement property described in subsection (e)(6).

``(H) Qualified restaurant property described in subsection (e)(7).'

(2) Subparagraph (A) of section 168(b)(2) is amended by inserting before the comma `not referred to in paragraph (3)'.

(e) **ALTERNATIVE SYSTEM**- The table contained in section 168(g)(3)(B) is amended by adding at the end the following new items:

``(E)(iv)

--39

``(E)(v)

--39'.

(f) **EFFECTIVE DATE**- The amendments made by this section shall apply to property placed in service after the date of the enactment of this Act.

Subtitle C--Community Revitalization

SEC. 221. MODIFICATION OF TARGETED AREAS AND LOW-INCOME COMMUNITIES FOR NEW MARKETS TAX CREDIT.

(a) TARGETED AREAS- Paragraph (2) of section 45D(e) (relating to targeted areas) is amended to read as follows:

`(2) TARGETED POPULATIONS- The Secretary shall prescribe regulations under which 1 or more targeted populations (within the meaning of section 103(20) of the Riegle Community Development and Regulatory Improvement Act of 1994 (12 U.S.C. 4702(20))) may be treated as low-income communities. Such regulations shall include procedures for determining which entities are qualified active low-income community businesses with respect to such populations.'.

(b) TRACTS WITH LOW POPULATION- Subsection (e) of section 45D (defining low-income community) is amended by adding at the end the following:

`(4) TRACTS WITH LOW POPULATION- A population census tract with a population of less than 2,000 shall be treated as a low-income community for purposes of this section if such tract--

`(A) is within an empowerment zone the designation of which is in effect under section 1391, and
 `(B) is contiguous to 1 or more low-income communities (determined without regard to this paragraph).'.

(c) EFFECTIVE DATES-

(1) TARGETED AREAS- The amendment made by subsection (a) shall apply to designations made by the Secretary of the Treasury after the date of the enactment of this Act.

(2) TRACTS WITH LOW POPULATION- The amendment made by subsection (b) shall apply to investments made after the date of the enactment of this Act.

SEC. 222. EXPANSION OF DESIGNATED RENEWAL COMMUNITY AREA BASED ON 2000 CENSUS DATA.

(a) IN GENERAL- Section 1400E (relating to designation of renewal communities) is amended by adding at the end the following new subsection:

`(g) EXPANSION OF DESIGNATED AREA BASED ON 2000 CENSUS-

`(1) IN GENERAL- At the request of all governments which nominated an area as a renewal community, the Secretary of Housing and Urban Development may expand the area of such community to include any census tract if-

`(A)(i) at the time such community was nominated, such community would have met the requirements of this section using 1990 census data even if such tract had been included in such community, and

`(ii) such tract has a poverty rate using 2000 census data which exceeds the poverty rate for such tract using 1990 census data, or

``(B)(i) such community would be described in subparagraph (A)(i) but for the failure to meet one or more of the requirements of paragraphs (2)(C)(i), (3)(C), and (3)(D) of subsection (c) using 1990 census data,

``(ii) such community, including such tract, has a population of not more than 200,000 using either 1990 census data or 2000 census data,

``(iii) such tract meets the requirement of subsection (c)(3)(C) using 2000 census data, and

``(iv) such tract meets the requirement of subparagraph (A)(ii).

``(2) EXCEPTION FOR CERTAIN CENSUS TRACTS WITH LOW POPULATION IN 1990- In the case of any census tract which did not have a poverty rate determined by the Bureau of the Census using 1990 census data, paragraph (1)(B) shall be applied without regard to clause (iv) thereof.

``(3) SPECIAL RULE FOR CERTAIN CENSUS TRACTS WITH LOW POPULATION IN 2000- At the request of all governments which nominated an area as a renewal community, the Secretary of Housing and Urban Development may expand the area of such community to include any census tract if-

``(A) either--

``(i) such tract has no population using 2000 census data, or

``(ii) no poverty rate for such tract is determined by the Bureau of the Census using 2000 census data,

``(B) such tract is one of general distress, and

``(C) such community, including such tract, meets the requirements of subparagraphs (A) and (B) of subsection (c)(2).

``(4) PERIOD IN EFFECT- Any expansion under this subsection shall take effect as provided in subsection (b).'

(b) EFFECTIVE DATE- The amendment made by subsection (a) shall take effect as if included in the amendments made by section 101 of the Community Renewal Tax Relief Act of 2000.

SEC. 223. MODIFICATION OF INCOME REQUIREMENT FOR CENSUS TRACTS WITHIN HIGH MIGRATION RURAL COUNTIES.

(a) IN GENERAL- Section 45D(e) (relating to low-income community), as amended by this Act, is amended by inserting after paragraph (4) the following new paragraph:

``(5) MODIFICATION OF INCOME REQUIREMENT FOR CENSUS TRACTS WITHIN HIGH MIGRATION RURAL COUNTIES-

``(A) IN GENERAL- In the case of a population census tract located within a high migration rural county, paragraph (1)(B)(i) shall be applied by substituting `85 percent' for `80 percent'.

``(B) HIGH MIGRATION RURAL COUNTY- For purposes of this paragraph, the term `high migration rural county' means any

county which, during the 20-year period ending with the year in which the most recent census was conducted, has a net out-migration of inhabitants from the county of at least 10 percent of the population of the county at the beginning of such period.'.

(b) EFFECTIVE DATE- The amendment made by this section shall take effect as if included in the amendment made by section 121(a) of the Community Renewal Tax Relief Act of 2000.

Subtitle D--S Corporation Reform and Simplification

SEC. 231. MEMBERS OF FAMILY TREATED AS 1 SHAREHOLDER.

(a) IN GENERAL- Paragraph (1) of section 1361(c) (relating to special rules for applying subsection (b)) is amended to read as follows:

- ^(1) MEMBERS OF FAMILY TREATED AS 1 SHAREHOLDER
 - ^(A) IN GENERAL- For purpose of subsection (b)(1)(A)--
 - ^(i) except as provided in clause (ii), a husband and wife (and their estates) shall be treated as 1 shareholder, and
 - ^(ii) in the case of a family with respect to which an election is in effect under subparagraph (D), all members of the family shall be treated as 1 shareholder.
 - ^(B) MEMBERS OF THE FAMILY- For purpose of subparagraph (A)(ii)--
 - ^(i) IN GENERAL- The term 'members of the family' means the common ancestor, lineal descendants of the common ancestor, and the spouses (or former spouses) of such lineal descendants or common ancestor.
 - ^(ii) COMMON ANCESTOR--For purposes of this paragraph, an individual shall not be considered a common ancestor if, as of the later of the effective date of this paragraph or the time the election under section 1362(a) is made, the individual is more than 6 generations removed from the youngest generation of shareholders who would (but for this clause) be members of the family. For purposes of the preceding sentence, a spouse (or former spouse) shall be treated as being of the same generation as the individual to which such spouse is (or was) married.
 - ^(C) EFFECT OF ADOPTION, ETC- In determining whether any relationship specified in subparagraph (B) exists, the rules of section 152(b)(2) shall apply.
 - ^(D) ELECTION- An election under subparagraph (A)(ii)--
 - ^(i) may, except as otherwise provided in regulations prescribed by the Secretary, be made by any member of the family, and
 - ^(ii) shall remain in effect until terminated as provided in regulations prescribed by the Secretary.'

(b) RELIEF FROM INADVERTENT INVALID ELECTION OR TERMINATION- Section 1362(f) (relating to inadvertent invalid elections or terminations), as amended by this Act, is amended--

- (1) by inserting `or section 1361(c)(1)(A)(ii)' after `section 1361(b)(3)(B)(ii)', in paragraph (1), and
- (2) by inserting `or section 1361(c)(1)(D)(iii)' after `section 1361(b)(3)(C)', in paragraph (1)(B).

(c) EFFECTIVE DATES-

- (1) SUBSECTION (a)- The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 2004.
- (2) SUBSECTION (b)- The amendments made by subsection (b) shall apply to elections and terminations made after December 31, 2004.

SEC. 232. INCREASE IN NUMBER OF ELIGIBLE SHAREHOLDERS TO 100.

(a) IN GENERAL- Section 1361(b)(1)(A) (defining small business corporation) is amended by striking `75' and inserting `100'.

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

SEC. 233. EXPANSION OF BANK S CORPORATION ELIGIBLE SHAREHOLDERS TO INCLUDE IRAS.

(a) IN GENERAL- Section 1361(c)(2)(A) (relating to certain trusts permitted as shareholders) is amended by inserting after clause (v) the following new clause:

`^(vi) In the case of a corporation which is a bank (as defined in section 581), a trust which constitutes an individual retirement account under section 408(a), including one designated as a Roth IRA under section 408A, but only to the extent of the stock held by such trust in such bank as of the date of the enactment of this clause.'

(b) TREATMENT AS SHAREHOLDER- Section 1361(c)(2)(B) (relating to treatment as shareholders) is amended by adding at the end the following new clause:

`^(vi) In the case of a trust described in clause (vi) of subparagraph (A), the individual for whose benefit the trust was created shall be treated as a shareholder.'

(c) SALE OF BANK STOCK IN IRA RELATING TO S CORPORATION ELECTION EXEMPT FROM PROHIBITED TRANSACTION RULES- Section 4975(d) (relating to exemptions) is amended by striking `or' at the end of paragraph (14), by striking the period at the end of paragraph (15) and inserting `; or', and by adding at the end the following new paragraph:

`⁽¹⁶⁾ a sale of stock held by a trust which constitutes an individual retirement account under section 408(a) to the individual for whose benefit such account is established if-

- `(A) such stock is in a bank (as defined in section 581),
- `(B) such stock is held by such trust as of the date of the enactment of this paragraph,
- `(C) such sale is pursuant to an election under section 1362(a) by such bank,
- `(D) such sale is for fair market value at the time of sale (as established by an independent appraiser) and the terms of the sale are otherwise at least as favorable to such trust as the terms that would apply on a sale to an unrelated party,
- `(E) such trust does not pay any commissions, costs, or other expenses in connection with the sale, and
- `(F) the stock is sold in a single transaction for cash not later than 120 days after the S corporation election is made.'

(d) CONFORMING AMENDMENT- Section 512(e)(1) is amended by inserting `1361(c)(2)(A)(vi) or' before `1361(c)(6)'.

(e) EFFECTIVE DATE- The amendments made by this section shall take effect on the date of the enactment of this Act.

SEC. 234. DISREGARD OF UNEXERCISED POWERS OF APPOINTMENT IN DETERMINING POTENTIAL CURRENT BENEFICIARIES OF ESBT.

(a) IN GENERAL- Section 1361(e)(2) (defining potential current beneficiary) is amended--

- (1) by inserting `(determined without regard to any power of appointment to the extent such power remains unexercised at the end of such period)' after `of the trust' in the first sentence, and
- (2) by striking `60-day' in the second sentence and inserting `1-year'.

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

SEC. 235. TRANSFER OF SUSPENDED LOSSES INCIDENT TO DIVORCE, ETC.

(a) IN GENERAL- Section 1366(d)(2) (relating to indefinite carryover of disallowed losses and deductions) is amended to read as follows:

`(2) INDEFINITE CARRYOVER OF DISALLOWED LOSSES AND DEDUCTIONS-

- `(A) IN GENERAL- Except as provided in subparagraph (B), any loss or deduction which is disallowed for any taxable year by reason of paragraph (1) shall be treated as incurred by the corporation in the succeeding taxable year with respect to that shareholder.
- `(B) TRANSFERS OF STOCK BETWEEN SPOUSES OR INCIDENT TO DIVORCE- In the case of any transfer described in section 1041(a) of stock of an S corporation, any loss or

deduction described in subparagraph (A) with respect such stock shall be treated as incurred by the corporation in the succeeding taxable year with respect to the transferee.'

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

SEC. 236. USE OF PASSIVE ACTIVITY LOSS AND AT-RISK AMOUNTS BY QUALIFIED SUBCHAPTER S TRUST INCOME BENEFICIARIES.

(a) IN GENERAL- Section 1361(d)(1) (relating to special rule for qualified subchapter S trust) is amended--

- (1) by striking `and' at the end of subparagraph (A),
- (2) by striking the period at the end of subparagraph (B) and inserting `, and', and
- (3) by adding at the end the following new subparagraph:

`(C) for purposes of applying sections 465 and 469 to the beneficiary of the trust, the disposition of the S corporation stock by the trust shall be treated as a disposition by such beneficiary.'

(b) EFFECTIVE DATE- The amendments made by this section shall apply to transfers made after December 31, 2004.

SEC. 237. EXCLUSION OF INVESTMENT SECURITIES INCOME FROM PASSIVE INCOME TEST FOR BANK S CORPORATIONS.

(a) IN GENERAL- Section 1362(d)(3) (relating to where passive investment income exceeds 25 percent of gross receipts for 3 consecutive taxable years and corporation has accumulated earnings and profits) is amended by adding at the end the following new subparagraph:

`(F) EXCEPTION FOR BANKS; ETC- In the case of a bank (as defined in section 581), a bank holding company (within the meaning of section 2(a) of the Bank Holding Company Act of 1956 (12 U.S.C. 1841(a))), or a financial holding company (within the meaning of section 2(p) of such Act), the term `passive investment income' shall not include--

`

- (i) interest income earned by such bank or company, or
- (ii) dividends on assets required to be held by such bank or company, including stock in the Federal Reserve Bank, the Federal Home Loan Bank, or the Federal Agricultural Mortgage Bank or participation certificates issued by a Federal Intermediate Credit Bank.'

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

SEC. 238. RELIEF FROM INADVERTENTLY INVALID QUALIFIED SUBCHAPTER S SUBSIDIARY ELECTIONS AND TERMINATIONS.

(a) IN GENERAL- Section 1362(f) (relating to inadvertent invalid elections or terminations) is amended--

- (1) by inserting `, section 1361(b)(3)(B)(ii),' after `subsection (a)' in paragraph (1),
- (2) by inserting `, section 1361(b)(3)(C),' after `subsection (d)' in paragraph (1)(B),
- (3) by amending paragraph (3)(A) to read as follows:

` (A) so that the corporation for which the election was made or the termination occurred is a small business corporation or a qualified subchapter S subsidiary, as the case may be, or',
- (4) by amending paragraph (4) to read as follows:

` (4) the corporation for which the election was made or the termination occurred, and each person who was a shareholder in such corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of such corporation as an S corporation or a qualified subchapter S subsidiary, as the case may be) as may be required by the Secretary with respect to such period,' and

(5) by inserting `or a qualified subchapter S subsidiary, as the case may be' after `S corporation' in the matter following paragraph (4).

(b) EFFECTIVE DATE- The amendments made by this section shall apply to elections made and terminations made after December 31, 2004.

SEC. 239. INFORMATION RETURNS FOR QUALIFIED SUBCHAPTER S SUBSIDIARIES.

(a) IN GENERAL- Section 1361(b)(3)(A) (relating to treatment of certain wholly owned subsidiaries) is amended by inserting `and in the case of information returns required under part III of subchapter A of chapter 61' after `Secretary'.

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

SEC. 240. REPAYMENT OF LOANS FOR QUALIFYING EMPLOYER SECURITIES.

(a) IN GENERAL- Subsection (f) of section 4975 (relating to other definitions and special rules) is amended by adding at the end the following new paragraph:

` (7) S CORPORATION REPAYMENT OF LOANS FOR QUALIFYING EMPLOYER SECURITIES- A plan shall not be treated as violating the requirements of section 401 or 409 or subsection (e)(7), or as engaging in a prohibited transaction for purposes of subsection (d)(3), merely by reason of any distribution (as described in section 1368(a)) with respect to S corporation stock that constitutes qualifying employer securities, which in accordance with the plan provisions is used to make payments on a loan described in subsection (d)(3) the proceeds of which were used to acquire such qualifying employer securities (whether or not allocated to participants). The preceding sentence shall not apply in the case of a

distribution which is paid with respect to any employer security which is allocated to a participant unless the plan provides that employer securities with a fair market value of not less than the amount of such distribution are allocated to such participant for the year which (but for the preceding sentence) such distribution would have been allocated to such participant.'.

(b) EFFECTIVE DATE- The amendment made by this section shall apply to distributions with respect to S corporation stock made after December 31, 1997.

Subtitle E--Other Business Incentives

SEC. 241. PHASEOUT OF 4.3-CENT MOTOR FUEL EXCISE TAXES ON RAILROADS AND INLAND WATERWAY TRANSPORTATION WHICH REMAIN IN GENERAL FUND.

(a) TAXES ON TRAINS-

(1) IN GENERAL- Clause (ii) of section 4041(a)(1)(C) is amended by striking subclauses (I), (II), and (III) and inserting the following new subclauses:

``(I) 3.3 cents per gallon after December 31, 2004, and before July 1, 2005,
``(II) 2.3 cents per gallon after June 30, 2005, and before January 1, 2007, and
``(III) 0 after December 31, 2006.'.

(2) CONFORMING AMENDMENTS-

(A) Subsection (d) of section 4041 is amended by redesignating paragraph (3) as paragraph (4) and by inserting after paragraph (2) the following new paragraph:

``(3) DIESEL FUEL USED IN TRAINS- In the case of any sale for use or use after December 31, 2006, there is hereby imposed a tax of 0.1 cent per gallon on any liquid other than gasoline (as defined in section 4083)--

``(A) sold by any person to an owner, lessee, or other operator of a diesel-powered train for use as a fuel in such train, or

``(B) used by any person as a fuel in a diesel-powered train unless there was a taxable sale of such fuel under subparagraph (A).

No tax shall be imposed by this paragraph on the sale or use of any liquid if tax was imposed on such liquid under section 4081.'.

(B) Subsection (f) of section 4082 is amended by striking `section 4041(a)(1)' and inserting `subsections (a)(1) and (d)(3) of section 4041'.

(C) Subparagraph (B) of section 6421(f)(3) is amended to read as follows:

``(B) so much of the rate specified in section 4081(a)(2)(A) as does not exceed the rate applicable under section 4041(a)(1)(C)(ii).'

(D) Subparagraph (B) of section 6427(l)(3) is amended to read as follows:

``(B) so much of the rate specified in section 4081(a)(2)(A) as does not exceed the rate applicable under section 4041(a)(1)(C)(ii).'.

(b) FUEL USED ON INLAND WATERWAYS- Subparagraph (C) of section 4042(b)(2) is amended to read as follows:

``(C) The deficit reduction rate is--

``(i) 3.3 cents per gallon after December 31, 2004, and before July 1, 2005,

``(ii) 2.3 cents per gallon after June 30, 2005, and before January 1, 2007, and

``(iii) 0 after December 31, 2006.'.'

(c) EFFECTIVE DATE- The amendments made by this section shall take effect on January 1, 2005.

SEC. 242. MODIFICATION OF APPLICATION OF INCOME FORECAST METHOD OF DEPRECIATION.

(a) IN GENERAL- Section 167(g) (relating to depreciation under income forecast method) is amended by adding at the end the following new paragraph:

``(7) TREATMENT OF PARTICIPATIONS AND RESIDUALS-

``(A) IN GENERAL- For purposes of determining the depreciation deduction allowable with respect to a property under this subsection, the taxpayer may include participations and residuals with respect to such property in the adjusted basis of such property for the taxable year in which the property is placed in service, but only to the extent that such participations and residuals relate to income estimated (for purposes of this subsection) to be earned in connection with the property before the close of the 10th taxable year referred to in paragraph (1)(A).

``(B) PARTICIPATIONS AND RESIDUALS- For purposes of this paragraph, the term `participations and residuals' means, with respect to any property, costs the amount of which by contract varies with the amount of income earned in connection with such property.

``(C) SPECIAL RULES RELATING TO RECOMPUTATION YEARS- If the adjusted basis of any property is determined under this paragraph, paragraph (4) shall be applied by substituting `for each taxable year in such period' for `for such period'.

``(D) OTHER SPECIAL RULES-

``(i) PARTICIPATIONS AND RESIDUALS-

Notwithstanding subparagraph (A), the taxpayer may exclude participations and residuals from the adjusted basis of such property and deduct such participations and residuals in the taxable year that such participations and residuals are paid.

``(ii) COORDINATION WITH OTHER RULES-

Deductions computed in accordance with this paragraph

shall be allowable notwithstanding paragraph (1)(B), section 263, 263A, 404, 419, or 461(h).

``(E) AUTHORITY TO MAKE ADJUSTMENTS- The Secretary shall prescribe appropriate adjustments to the basis of property and to the look-back method for the additional amounts allowable as a deduction solely by reason of this paragraph.'

(b) DETERMINATION OF INCOME- Section 167(g)(5) (relating to special rules) is amended by redesignating subparagraphs (E) and (F) as subparagraphs (F) and (G), respectively, and inserting after subparagraph (D) the following new subparagraph:

``(E) TREATMENT OF DISTRIBUTION COSTS- For purposes of this subsection, the income with respect to any property shall be the taxpayer's gross income from such property.'

(c) EFFECTIVE DATE- The amendments made by this section shall apply to property placed in service after the date of the enactment of this Act.

SEC. 243. IMPROVEMENTS RELATED TO REAL ESTATE INVESTMENT TRUSTS.

(a) EXPANSION OF STRAIGHT DEBT SAFE HARBOR- Section 856 (defining real estate investment trust) is amended--

(1) in subsection (c) by striking paragraph (7), and

(2) by adding at the end the following new subsection:

``(m) SAFE HARBOR IN APPLYING SUBSECTION (c)(4)-

``(1) IN GENERAL- In applying subclause (III) of subsection (c)(4)(B)(iii), except as otherwise determined by the Secretary in regulations, the following shall not be considered securities held by the trust:

``(A) Straight debt securities of an issuer which meet the requirements of paragraph (2).

``(B) Any loan to an individual or an estate.

``(C) Any section 467 rental agreement (as defined in section 467(d)), other than with a person described in subsection (d)(2)(B).

``(D) Any obligation to pay rents from real property (as defined in subsection (d)(1)).

``(E) Any security issued by a State or any political subdivision thereof, the District of Columbia, a foreign government or any political subdivision thereof, or the Commonwealth of Puerto Rico, but only if the determination of any payment received or accrued under such security does not depend in whole or in part on the profits of any entity not described in this subparagraph or payments on any obligation issued by such an entity,

``(F) Any security issued by a real estate investment trust.

``(G) Any other arrangement as determined by the Secretary.

``(2) SPECIAL RULES RELATING TO STRAIGHT DEBT SECURITIES-

``(A) IN GENERAL- For purposes of paragraph (1)(A), securities meet the requirements of this paragraph if such securities are straight debt, as defined in section 1361(c)(5) (without regard to subparagraph (B)(iii) thereof).

``(B) SPECIAL RULES RELATING TO CERTAIN CONTINGENCIES- For purposes of subparagraph (A), any interest or principal shall not be treated as failing to satisfy section 1361(c)(5)(B)(i) solely by reason of the fact that--

````(i) the time of payment of such interest or principal is subject to a contingency, but only if--

``````(I) any such contingency does not have the effect of changing the effective yield to maturity, as determined under section 1272, other than a change in the annual yield to maturity which does not exceed the greater of 1/4 of 1 percent or 5 percent of the annual yield to maturity, or

``````(II) neither the aggregate issue price nor the aggregate face amount of the issuer's debt instruments held by the trust exceeds \$1,000,000 and not more than 12 months of unaccrued interest can be required to be prepaid thereunder, or

````(ii) the time or amount of payment is subject to a contingency upon a default or the exercise of a prepayment right by the issuer of the debt, but only if such contingency is consistent with customary commercial practice.

``(C) SPECIAL RULES RELATING TO CORPORATE OR PARTNERSHIP ISSUERS- In the case of an issuer which is a corporation or a partnership, securities that otherwise would be described in paragraph (1)(A) shall be considered not to be so described if the trust holding such securities and any of its controlled taxable REIT subsidiaries (as defined in subsection (d)(8)(A)(iv)) hold any securities of the issuer which-

````(i) are not described in paragraph (1) (prior to the application of this subparagraph), and

````(ii) have an aggregate value greater than 1 percent of the issuer's outstanding securities determined without regard to paragraph (3)(A)(i).

``(3) LOOK-THROUGH RULE FOR PARTNERSHIP SECURITIES-

````(A) IN GENERAL- For purposes of applying subclause (III) of subsection (c)(4)(B)(iii)--

``````(i) a trust's interest as a partner in a partnership (as defined in section 7701(a)(2)) shall not be considered a security, and

``````(ii) the trust shall be deemed to own its proportionate share of each of the assets of the partnership.

^(B) DETERMINATION OF TRUST'S INTEREST IN PARTNERSHIP ASSETS- For purposes of subparagraph (A), with respect to any taxable year beginning after the date of the enactment of this subparagraph--

- ^(i) the trust's interest in the partnership assets shall be the trust's proportionate interest in any securities issued by the partnership (determined without regard to subparagraph (A)(i) and paragraph (4), but not including securities described in paragraph (1)), and
- ^(ii) the value of any debt instrument shall be the adjusted issue price thereof, as defined in section 1272(a)(4).

^(4) CERTAIN PARTNERSHIP DEBT INSTRUMENTS NOT TREATED AS A SECURITY- For purposes of applying subclause (III) of subsection (c)(4)(B)(iii)--

- ^(A) any debt instrument issued by a partnership and not described in paragraph (1) shall not be considered a security to the extent of the trust's interest as a partner in the partnership, and
- ^(B) any debt instrument issued by a partnership and not described in paragraph (1) shall not be considered a security if at least 75 percent of the partnership's gross income (excluding gross income from prohibited transactions) is derived from sources referred to in subsection (c)(3).

^(5) SECRETARIAL GUIDANCE- The Secretary is authorized to provide guidance (including through the issuance of a written determination, as defined in section 6110(b)) that an arrangement shall not be considered a security held by the trust for purposes of applying subclause (III) of subsection (c)(4)(B)(iii) notwithstanding that such arrangement otherwise could be considered a security under subparagraph (F) of subsection (c)(5).!

(b) CLARIFICATION OF APPLICATION OF LIMITED RENTAL EXCEPTION- Subparagraph (A) of section 856(d)(8) (relating to special rules for taxable REIT subsidiaries) is amended to read as follows:

^(A) LIMITED RENTAL EXCEPTION-

^(i) IN GENERAL- The requirements of this subparagraph are met with respect to any property if at least 90 percent of the leased space of the property is rented to persons other than taxable REIT subsidiaries of such trust and other than persons described in paragraph (2)(B).

^(ii) RENTS MUST BE SUBSTANTIALLY COMPARABLE- Clause (i) shall apply only to the extent that the amounts paid to the trust as rents from real property (as defined in paragraph (1) without regard to paragraph (2)(B)) from such property are substantially comparable to such rents paid by the other tenants of the trust's property for comparable space.

^(iii) TIMES FOR TESTING RENT COMPARABILITY-  
The substantial comparability requirement of clause (ii) shall be treated as met with respect to a lease to a taxable REIT subsidiary of the trust if such requirement is met under the terms of the lease--

- ^(I) at the time such lease is entered into,
- ^(II) at the time of each extension of the lease, including a failure to exercise a right to terminate, and
- ^(III) at the time of any modification of the lease between the trust and the taxable REIT subsidiary if the rent under such lease is effectively increased pursuant to such modification.

With respect to subclause (III), if the taxable REIT subsidiary of the trust is a controlled taxable REIT subsidiary of the trust, the term `rents from real property' shall not in any event include rent under such lease to the extent of the increase in such rent on account of such modification.

^(iv) CONTROLLED TAXABLE REIT SUBSIDIARY-  
For purposes of clause (iii), the term `controlled taxable REIT subsidiary' means, with respect to any real estate investment trust, any taxable REIT subsidiary of such trust if such trust owns directly or indirectly--

- ^(I) stock possessing more than 50 percent of the total voting power of the outstanding stock of such subsidiary, or
- ^(II) stock having a value of more than 50 percent of the total value of the outstanding stock of such subsidiary.

^(v) CONTINUING QUALIFICATION BASED ON THIRD PARTY ACTIONS- If the requirements of clause (i) are met at a time referred to in clause (iii), such requirements shall continue to be treated as met so long as there is no increase in the space leased to any taxable REIT subsidiary of such trust or to any person described in paragraph (2)(B).

^(vi) CORRECTION PERIOD- If there is an increase referred to in clause (v) during any calendar quarter with respect to any property, the requirements of clause (iii) shall be treated as met during the quarter and the succeeding quarter if such requirements are met at the close of such succeeding quarter.'

(c) DELETION OF CUSTOMARY SERVICES EXCEPTION- Subparagraph (B) of section 857(b)(7) (relating to redetermined rents) is amended by striking clause

(ii) and by redesignating clauses (iii), (iv), (v), (vi), and (vii) as clauses (ii), (iii), (iv), (v), and (vi), respectively.

(d) CONFORMITY WITH GENERAL HEDGING DEFINITION- Subparagraph (G) of section 856(c)(5) (relating to treatment of certain hedging instruments) is amended to read as follows:

‘(G) TREATMENT OF CERTAIN HEDGING INSTRUMENTS- Except to the extent provided by regulations, any income of a real estate investment trust from a hedging transaction (as defined in clause (ii) or (iii) of section 1221(b)(2)(A)) which is clearly identified pursuant to section 1221(a)(7), including gain from the sale or disposition of such a transaction, shall not constitute gross income under paragraph (2) to the extent that the transaction hedges any indebtedness incurred or to be incurred by the trust to acquire or carry real estate assets.’.

(e) CONFORMITY WITH REGULATED INVESTMENT COMPANY RULES- Clause (i) of section 857(b)(5)(A) (relating to imposition of tax in case of failure to meet certain requirements) is amended by striking ‘90 percent’ and inserting ‘95 percent’.

(f) SAVINGS PROVISIONS-

(1) RULES OF APPLICATION FOR FAILURE TO SATISFY SECTION 856(c)(4)- Section 856(c) (relating to definition of real estate investment trust) is amended by inserting after paragraph (6) the following new paragraph:

‘(7) RULES OF APPLICATION FOR FAILURE TO SATISFY PARAGRAPH (4)-

‘(A) DE MINIMIS FAILURE- A corporation, trust, or association that fails to meet the requirements of paragraph (4)(B)(iii) for a particular quarter shall nevertheless be considered to have satisfied the requirements of such paragraph for such quarter if-

‘(i) such failure is due to the ownership of assets the total value of which does not exceed the lesser of-

‘(I) 1 percent of the total value of the trust's assets at the end of the quarter for which such measurement is done, and

‘(II) \$10,000,000, and

‘(ii)(I) the corporation, trust, or association, following the identification of such failure, disposes of assets in order to meet the requirements of such paragraph within 6 months after the last day of the quarter in which the corporation, trust or association's identification of the failure to satisfy the requirements of such paragraph occurred or such other time period prescribed by the Secretary and in the manner prescribed by the Secretary, or

‘(II) the requirements of such paragraph are otherwise met within the time period specified in subclause (I).

^(B) FAILURES EXCEEDING DE MINIMIS AMOUNT- A corporation, trust, or association that fails to meet the requirements of paragraph (4) for a particular quarter shall nevertheless be considered to have satisfied the requirements of such paragraph for such quarter if--

- ^(i) such failure involves the ownership of assets the total value of which exceeds the de minimis standard described in subparagraph (A)(i) at the end of the quarter for which such measurement is done,
- ^(ii) following the corporation, trust, or association's identification of the failure to satisfy the requirements of such paragraph for a particular quarter, a description of each asset that causes the corporation, trust, or association to fail to satisfy the requirements of such paragraph at the close of such quarter of any taxable year is set forth in a schedule for such quarter filed in accordance with regulations prescribed by the Secretary,
- ^(iii) the failure to meet the requirements of such paragraph for a particular quarter is due to reasonable cause and not due to willful neglect,
- ^(iv) the corporation, trust, or association pays a tax computed under subparagraph (C), and
- ^(v)(I) the corporation, trust, or association disposes of the assets set forth on the schedule specified in clause (ii) within 6 months after the last day of the quarter in which the corporation, trust or association's identification of the failure to satisfy the requirements of such paragraph occurred or such other time period prescribed by the Secretary and in the manner prescribed by the Secretary, or
- ^(II) the requirements of such paragraph are otherwise met within the time period specified in subclause (I).

^(C) TAX- For purposes of subparagraph (B)(iv)--

- ^(i) TAX IMPOSED- If a corporation, trust, or association elects the application of this subparagraph, there is hereby imposed a tax on the failure described in subparagraph (B) of such corporation, trust, or association. Such tax shall be paid by the corporation, trust, or association.
- ^(ii) TAX COMPUTED- The amount of the tax imposed by clause (i) shall be the greater of-
  - ^(I) \$50,000, or
  - ^(II) the amount determined (pursuant to regulations promulgated by the Secretary) by multiplying the net income generated by the assets described in the schedule specified in subparagraph (B)(ii) for the period specified in clause (iii) by the highest rate of tax specified in section 11.

``(iii) PERIOD- For purposes of clause (ii)(II), the period described in this clause is the period beginning on the first date that the failure to satisfy the requirements of such paragraph (4) occurs as a result of the ownership of such assets and ending on the earlier of the date on which the trust disposes of such assets or the end of the first quarter when there is no longer a failure to satisfy such paragraph (4).

``(iv) ADMINISTRATIVE PROVISIONS- For purposes of subtitle F, the taxes imposed by this subparagraph shall be treated as excise taxes with respect to which the deficiency procedures of such subtitle apply.'

(2) MODIFICATION OF RULES OF APPLICATION FOR FAILURE TO SATISFY SECTIONS 856(c)(2) OR 856(c)(3)- Paragraph (6) of section 856(c) (relating to definition of real estate investment trust) is amended by striking subparagraphs (A) and (B), by redesignating subparagraph (C) as subparagraph (B), and by inserting before subparagraph (B) (as so redesignated) the following new subparagraph:

``(A) following the corporation, trust, or association's identification of the failure to meet the requirements of paragraph (2) or (3), or of both such paragraphs, for any taxable year, a description of each item of its gross income described in such paragraphs is set forth in a schedule for such taxable year filed in accordance with regulations prescribed by the Secretary, and'.

(3) REASONABLE CAUSE EXCEPTION TO LOSS OF REIT STATUS IF FAILURE TO SATISFY REQUIREMENTS- Subsection (g) of section 856 (relating to termination of election) is amended--

(A) in paragraph (1) by inserting before the period at the end of the first sentence the following: `unless paragraph (5) applies', and

(B) by adding at the end the following new paragraph:

``(5) ENTITIES TO WHICH PARAGRAPH APPLIES- This paragraph applies to a corporation, trust, or association-

``(A) which is not a real estate investment trust to which the provisions of this part apply for the taxable year due to one or more failures to comply with one or more of the provisions of this part (other than subsection (c)(6) or (c)(7) of section 856),

``(B) such failures are due to reasonable cause and not due to willful neglect, and

``(C) if such corporation, trust, or association pays (as prescribed by the Secretary in regulations and in the same manner as tax) a penalty of \$50,000 for each failure to satisfy a provision of this part due to reasonable cause and not willful neglect.'

(4) DEDUCTION OF TAX PAID FROM AMOUNT REQUIRED TO BE DISTRIBUTED- Subparagraph (E) of section 857(b)(2) is amended by striking `(7)' and inserting `(7) of this subsection, section 856(c)(7)(B)(iii), and section 856(g)(1).'

(5) EXPANSION OF DEFICIENCY DIVIDEND PROCEDURE- Subsection (e) of section 860 is amended by striking 'or' at the end of paragraph (2), by striking the period at the end of paragraph (3) and inserting ';' or', and by adding at the end the following new paragraph: '(4) a statement by the taxpayer attached to its amendment or supplement to a return of tax for the relevant tax year.'

(g) EFFECTIVE DATES-

- (1) IN GENERAL- Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 2000.
- (2) SUBSECTIONS (c) THROUGH (f)- The amendments made by subsections (c), (d), (e), and (f) shall apply to taxable years beginning after the date of the enactment of this Act.

## **SEC. 244. SPECIAL RULES FOR CERTAIN FILM AND TELEVISION PRODUCTIONS.**

(a) IN GENERAL- Part VI of subchapter B of chapter 1 is amended by inserting after section 180 the following new section:

### **SEC. 181. TREATMENT OF CERTAIN QUALIFIED FILM AND TELEVISION PRODUCTIONS.**

(a) ELECTION TO TREAT COSTS AS EXPENSES-

(1) IN GENERAL- A taxpayer may elect to treat the cost of any qualified film or television production as an expense which is not chargeable to capital account. Any cost so treated shall be allowed as a deduction.

(2) DOLLAR LIMITATION-

(A) IN GENERAL- Paragraph (1) shall not apply to any qualified film or television production the aggregate cost of which exceeds \$15,000,000.

(B) HIGHER DOLLAR LIMITATION FOR PRODUCTIONS IN CERTAIN AREAS- In the case of any qualified film or television production the aggregate cost of which is significantly incurred in an area eligible for designation as-

- (i) a low-income community under section 45D, or
- (ii) a distressed county or isolated area of distress by the Delta Regional Authority established under section 2009aa-1 of title 7, United States Code,

subparagraph (A) shall be applied by substituting '\$20,000,000' for '\$15,000,000'.

(b) NO OTHER DEDUCTION OR AMORTIZATION DEDUCTION ALLOWABLE- With respect to the basis of any qualified film or television production to which an election is made under subsection (a), no other depreciation or amortization deduction shall be allowable.

(c) ELECTION-

`(1) IN GENERAL- An election under this section with respect to any qualified film or television production shall be made in such manner as prescribed by the Secretary and by the due date (including extensions) for filing the taxpayer's return of tax under this chapter for the taxable year in which costs of the production are first incurred.

`(2) REVOCATION OF ELECTION- Any election made under this section may not be revoked without the consent of the Secretary.

`(d) QUALIFIED FILM OR TELEVISION PRODUCTION- For purposes of this section-`

`(1) IN GENERAL- The term 'qualified film or television production' means any production described in paragraph (2) if 75 percent of the total compensation of the production is qualified compensation.

`(2) PRODUCTION-

`(A) IN GENERAL- A production is described in this paragraph if such production is property described in section 168(f)(3). For purposes of a television series, only the first 44 episodes of such series may be taken into account.

`(B) EXCEPTION- A production is not described in this paragraph if records are required under section 2257 of title 18, United States Code, to be maintained with respect to any performer in such production.

`(3) QUALIFIED COMPENSATION- For purposes of paragraph (1)--

`(A) IN GENERAL- The term 'qualified compensation' means compensation for services performed in the United States by actors, directors, producers, and other relevant production personnel.

`(B) PARTICIPATIONS AND RESIDUALS EXCLUDED- The term 'compensation' does not include participations and residuals (as defined in section 167(g)(7)(B)).

`(e) APPLICATION OF CERTAIN OTHER RULES- For purposes of this section, rules similar to the rules of subsections (b)(2) and (c)(4) of section 194 shall apply.

`(f) TERMINATION- This section shall not apply to qualified film and television productions commencing after December 31, 2008.'

(b) CONFORMING AMENDMENT- The table of sections for part VI of subchapter B of chapter 1 is amended by inserting after the item relating to section 180 the following new item:

`Sec. 181. Treatment of certain qualified film and television productions.'

(c) EFFECTIVE DATE- The amendments made by this section shall apply to qualified film and television productions (as defined in section 181(d)(1) of the Internal Revenue Code of 1986, as added by this section) commencing after the date of the enactment of this Act.

## **SEC. 245. CREDIT FOR MAINTENANCE OF RAILROAD TRACK.**

(a) IN GENERAL- Subpart D of part IV of subchapter A of chapter 1 (relating to business-related credits) is amended by adding at the end the following new section:

## **SEC. 45G. RAILROAD TRACK MAINTENANCE CREDIT.**

`(a) GENERAL RULE- For purposes of section 38, the railroad track maintenance credit determined under this section for the taxable year is an amount equal to 50 percent of the qualified railroad track maintenance expenditures paid or incurred by an eligible taxpayer during the taxable year.

`(b) LIMITATION- The credit allowed under subsection (a) for any taxable year shall not exceed the product of-

    `(1) \$3,500, and

    `(2) the number of miles of railroad track owned or leased by the eligible taxpayer as of the close of the taxable year.

A mile of railroad track may be taken into account by a person other than the owner only if such mile is assigned to such person by the owner for purposes of this subsection. Any mile which is so assigned may not be taken into account by the owner for purposes of this subsection.

`(c) ELIGIBLE TAXPAYER- For purposes of this section, the term `eligible taxpayer' means--

    `(1) any Class II or Class III railroad, and

    `(2) any person who transports property using the rail facilities of a person described in paragraph (1) or who furnishes railroad-related property or services to such a person.

`(d) QUALIFIED RAILROAD TRACK MAINTENANCE EXPENDITURES- For purposes of this section, the term `qualified railroad track maintenance expenditures' means expenditures (whether or not otherwise chargeable to capital account) for maintaining railroad track (including roadbed, bridges, and related track structures) owned or leased as of January 1, 2005, by a Class II or Class III railroad.

`(e) OTHER DEFINITIONS AND SPECIAL RULES-

    `(1) CLASS II OR CLASS III RAILROAD- For purposes of this section, the terms `Class II railroad' and `Class III railroad' have the respective meanings given such terms by the Surface Transportation Board.

    `(2) CONTROLLED GROUPS- Rules similar to the rules of paragraph (1) of section 41(f) shall apply for purposes of this section.

    `(3) BASIS ADJUSTMENT- For purposes of this subtitle, if a credit is allowed under this section with respect to any railroad track, the basis of such track shall be reduced by the amount of the credit so allowed.

`(f) APPLICATION OF SECTION- This section shall apply to qualified railroad track maintenance expenditures paid or incurred during taxable years beginning after December 31, 2004, and before January 1, 2008.'

(b) LIMITATION ON CARRYBACK-

    `1) IN GENERAL- Subsection (d) of section 39 is amended to read as follows:

``(d) TRANSITIONAL RULE- No portion of the unused business credit for any taxable year which is attributable to a credit specified in section 38(b) or any portion thereof may be carried back to any taxable year before the first taxable year for which such specified credit or such portion is allowable (without regard to subsection (a)).'.

(2) EFFECTIVE DATE- The amendment made by paragraph (1) shall apply with respect to taxable years ending after December 31, 2003.

(c) CONFORMING AMENDMENTS-

(1) Section 38(b) (relating to general business credit) is amended by striking `plus' at the end of paragraph (14), by striking the period at the end of paragraph (15) and inserting `, plus', and by adding at the end the following new paragraph:

``(16) the railroad track maintenance credit determined under section 45G(a).'.

(2) Subsection (a) of section 1016 is amended by striking `and' at the end of paragraph (27), by striking the period at the end of paragraph (28) and inserting `, and', and by inserting after paragraph (28) the following new paragraph:

``(29) in the case of railroad track with respect to which a credit was allowed under section 45G, to the extent provided in section 45G(e)(3).'.

(d) CLERICAL AMENDMENT- The table of sections for subpart D of part IV of subchapter A of chapter 1 is amended by inserting after the item relating to section 45F the following new item:

``Sec. 45G. Railroad track maintenance credit.'

(e) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years beginning after December 31, 2004.

## **SEC. 246. SUSPENSION OF OCCUPATIONAL TAXES RELATING TO DISTILLED SPIRITS, WINE, AND BEER.**

(a) IN GENERAL- Subpart G of part II of subchapter A of chapter 51 is amended by redesignating section 5148 as section 5149 and by inserting after section 5147 the following new section:

## **SEC. 5148. SUSPENSION OF OCCUPATIONAL TAX.**

``(a) IN GENERAL- Notwithstanding sections 5081, 5091, 5111, 5121, and 5131, the rate of tax imposed under such sections for the suspension period shall be zero. During such period, persons engaged in or carrying on a trade or business covered by such sections shall register under section 5141 and shall comply with the recordkeeping requirements under this part.

``(b) SUSPENSION PERIOD- For purposes of subsection (a), the suspension period is the period beginning on July 1, 2005, and ending on June 30, 2008.'

(b) CONFORMING AMENDMENT- Section 5117 is amended by adding at the end the following new subsection:

``(d) SPECIAL RULE DURING SUSPENSION PERIOD- Except as provided in subsection (b) or by the Secretary, during the suspension period (as defined in section 5148) it shall be unlawful for any dealer to purchase distilled spirits for resale from any person other than a wholesale dealer in liquors who is required to keep records under section 5114.'.

(c) CLERICAL AMENDMENT- The table of sections for subpart G of part II of subchapter A of chapter 51 is amended by striking the last item and inserting the following new items:

``Sec. 5148. Suspension of occupational tax.

``Sec. 5149. Cross references.'

(d) EFFECTIVE DATE- The amendments made by this section shall take effect on the date of the enactment of this Act.

## **SEC. 247. MODIFICATION OF UNRELATED BUSINESS INCOME LIMITATION ON INVESTMENT IN CERTAIN SMALL BUSINESS INVESTMENT COMPANIES.**

(a) IN GENERAL- Paragraph (6) of section 514(c) (relating to acquisition indebtedness) is amended to read as follows:

``(6) CERTAIN FEDERAL FINANCING-

``(A) IN GENERAL- For purposes of this section, the term 'acquisition indebtedness' does not include--

``(i) an obligation, to the extent that it is insured by the Federal Housing Administration, to finance the purchase, rehabilitation, or construction of housing for low and moderate income persons, or

``(ii) indebtedness incurred by a small business investment company licensed after the date of the enactment of the American Jobs Creation Act of 2004 under the Small Business Investment Act of 1958 if such indebtedness is evidenced by a debenture--

``(I) issued by such company under section 303(a) of such Act, and

``(II) held or guaranteed by the Small Business Administration.

``(B) LIMITATION- Subparagraph (A)(ii) shall not apply with respect to any small business investment company during any period that--

``(i) any organization which is exempt from tax under this title (other than a governmental unit) owns more than 25 percent of the capital or profits interest in such company, or

``(ii) organizations which are exempt from tax under this title (including governmental units other than any agency or instrumentality of the United States) own, in the aggregate, 50 percent or more of the capital or profits interest in such company.'.

(b) EFFECTIVE DATE- The amendment made by this section shall apply to indebtedness incurred after the date of the enactment of this Act by a small business investment company licensed after the date of the enactment of this Act.

## **SEC. 248. ELECTION TO DETERMINE CORPORATE TAX ON CERTAIN INTERNATIONAL SHIPPING ACTIVITIES USING PER TON RATE.**

(a) IN GENERAL- Chapter 1 is amended by inserting after subchapter Q the following new subchapter:

### **``Subchapter R--Election To Determine Corporate Tax on Certain International Shipping Activities Using Per Ton Rate**

``Sec. 1352. Alternative tax on qualifying shipping activities.

``Sec. 1353. Notional shipping income.

``Sec. 1354. Alternative tax election; revocation; termination.

``Sec. 1355. Definitions and special rules.

``Sec. 1356. Qualifying shipping activities.

``Sec. 1357. Items not subject to regular tax; depreciation; interest.

``Sec. 1358. Allocation of credits, income, and deductions.

``Sec. 1359. Disposition of qualifying vessels.

### **``SEC. 1352. ALTERNATIVE TAX ON QUALIFYING SHIPPING ACTIVITIES.**

``In the case of an electing corporation, the tax imposed by section 11 shall be the amount equal to the sum of--

``(1) the tax imposed by section 11 determined after the application of this subchapter, and

``(2) a tax equal to--

``(A) the highest rate of tax specified in section 11, multiplied by

``(B) the notional shipping income for the taxable year.

## **SEC. 1353. NOTIONAL SHIPPING INCOME.**

^(a) IN GENERAL- For purposes of this subchapter, the notional shipping income of an electing corporation shall be the sum of the amounts determined under subsection (b) for each qualifying vessel operated by such electing corporation.

^(b) AMOUNTS-

^(1) IN GENERAL- For purposes of subsection (a), the amount of notional shipping income of an electing corporation for each qualifying vessel for the taxable year shall equal the product of-

^(A) the daily notional shipping income, and

^(B) the number of days during the taxable year that the electing corporation operated such vessel as a qualifying vessel in United States foreign trade.

^(2) TREATMENT OF VESSELS THE INCOME FROM WHICH IS NOT OTHERWISE SUBJECT TO TAX- In the case of a qualifying vessel any of the income from which is not included in gross income by reason of section 883 or otherwise, the amount of notional shipping income from such vessel for the taxable year shall be the amount which bears the same ratio to such shipping income (determined without regard to this paragraph) as the gross income from the operation of such vessel in the United States foreign trade bears to the sum of such gross income and the income so excluded.

^(c) DAILY NOTIONAL SHIPPING INCOME- For purposes of subsection (b), the daily notional shipping income from the operation of a qualifying vessel is--

^(1) 40 cents for each 100 tons of so much of the net tonnage of the vessel as does not exceed 25,000 net tons, and

^(2) 20 cents for each 100 tons of so much of the net tonnage of the vessel as exceeds 25,000 net tons.

^(d) MULTIPLE OPERATORS OF VESSEL- If for any period 2 or more persons are operators of a qualifying vessel, the notional shipping income from the operation of such vessel for such period shall be allocated among such persons on the basis of their respective ownership and charter interests in such vessel or on such other basis as the Secretary may prescribe by regulations.

## **SEC. 1354. ALTERNATIVE TAX ELECTION; REVOCATION; TERMINATION.**

^(a) IN GENERAL- A qualifying vessel operator may elect the application of this subchapter.

^(b) TIME AND MANNER; YEARS FOR WHICH EFFECTIVE- An election under this subchapter--

^(1) shall be made in such form as prescribed by the Secretary, and

^(2) shall be effective for the taxable year for which made and all succeeding taxable years until terminated under subsection (d).

Such election may be effective for any taxable year only if made before the due date (including extensions) for filing the corporation's return for such taxable year.

``(c) CONSISTENT ELECTIONS BY MEMBERS OF CONTROLLED GROUPS- An election under subsection (a) by a member of a controlled group shall apply to all qualifying vessel operators that are members of such group.

``(d) TERMINATION-

``(1) BY REVOCATION-

``(A) IN GENERAL- An election under subsection (a) may be terminated by revocation.

``(B) WHEN EFFECTIVE- Except as provided in subparagraph (C)--

``(i) a revocation made during the taxable year and on or before the 15th day of the 3d month thereof shall be effective on the 1st day of such taxable year, and

``(ii) a revocation made during the taxable year but after such 15th day shall be effective on the 1st day of the following taxable year.

``(C) REVOCATION MAY SPECIFY PROSPECTIVE DATE- If the revocation specifies a date for revocation which is on or after the day on which the revocation is made, the revocation shall be effective for taxable years beginning on and after the date so specified.

``(2) BY PERSON CEASING TO BE QUALIFYING VESSEL OPERATOR-

``(A) IN GENERAL- An election under subsection (a) shall be terminated whenever (at any time on or after the 1st day of the 1st taxable year for which the corporation is an electing corporation) such corporation ceases to be a qualifying vessel operator.

``(B) WHEN EFFECTIVE- Any termination under this paragraph shall be effective on and after the date of cessation.

``(C) ANNUALIZATION- The Secretary shall prescribe such annualization and other rules as are appropriate in the case of a termination under this paragraph.

``(e) ELECTION AFTER TERMINATION- If a qualifying vessel operator has made an election under subsection (a) and if such election has been terminated under subsection (d), such operator (and any successor operator) shall not be eligible to make an election under subsection (a) for any taxable year before its 5th taxable year which begins after the 1st taxable year for which such termination is effective, unless the Secretary consents to such election.

## **``SEC. 1355. DEFINITIONS AND SPECIAL RULES.**

``(a) DEFINITIONS- For purposes of this subchapter--

``(1) ELECTING CORPORATION- The term `electing corporation' means any corporation for which an election is in effect under this subchapter.

``(2) ELECTING GROUP; CONTROLLED GROUP-

``(A) ELECTING GROUP- The term `electing group' means a controlled group of which one or more members is an electing corporation.

``(B) CONTROLLED GROUP- The term `controlled group' means any group which would be treated as a single employer under subsection (a) or (b) of section 52 if paragraphs (1) and (2) of section 52(a) did not apply.

``(3) QUALIFYING VESSEL OPERATOR- The term `qualifying vessel operator' means any corporation--

``(A) who operates one or more qualifying vessels, and

``(B) who meets the shipping activity requirement in subsection (c).

``(4) QUALIFYING VESSEL- The term `qualifying vessel' means a self-propelled (or a combination self-propelled and non-self-propelled) United States flag vessel of not less than 10,000 deadweight tons used exclusively in the United States foreign trade during the period that the election under this subchapter is in effect.

``(5) UNITED STATES FLAG VESSEL- The term `United States flag vessel' means any vessel documented under the laws of the United States.

``(6) UNITED STATES DOMESTIC TRADE- The term `United States domestic trade' means the transportation of goods or passengers between places in the United States.

``(7) UNITED STATES FOREIGN TRADE- The term `United States foreign trade' means the transportation of goods or passengers between a place in the United States and a foreign place or between foreign places.

``(8) CHARTER- The term `charter' includes an operating agreement.

``(b) OPERATING A VESSEL- For purposes of this subchapter--

``(1) IN GENERAL- Except as provided in paragraph (2), a person is treated as operating any vessel during any period if such vessel is--

``(A) owned by, or chartered (including a time charter) to, the person, and

``(B) is in use as a qualifying vessel during such period.

``(2) BAREBOAT CHARTERS- A person is treated as operating and using a vessel that it has chartered out on bareboat charter terms only if--

``(A)(i) the vessel is temporarily surplus to the person's requirements and the term of the charter does not exceed 3 years, or

``(ii) the vessel is bareboat chartered to a member of a controlled group which includes such person or to an unrelated person who sub-bareboats or time charters the vessel to such a member (including the owner of the vessel), and

``(B) the vessel is used as a qualifying vessel by the person to whom ultimately chartered.

``(c) SHIPPING ACTIVITY REQUIREMENT- For purposes of this section--

``(1) IN GENERAL- Except as otherwise provided in this subsection, a corporation meets the shipping activity requirement of this subsection for

any taxable year only if the requirement of paragraph (4) is met for each of the 2 preceding taxable years.

`(2) SPECIAL RULE FOR 1ST YEAR OF ELECTION- A corporation meets the shipping activity requirement of this subsection for the first taxable year for which the election under section 1354(a) is in effect only if the requirement of paragraph (4) is met for the preceding taxable year.

`(3) CONTROLLED GROUPS- A corporation who is a member of a controlled group meets the shipping activity requirement of this subsection only if such requirement is met determined--

    `**(A)** by treating all members of such group as 1 person, and

    `**(B)** by disregarding vessel charters between members of such group.

`(4) REQUIREMENT- The requirement of this paragraph is met for any taxable year if, on average during such year, at least 25 percent of the aggregate tonnage of qualifying vessels used by the corporation were owned by such corporation or chartered to such corporation on bareboat charter terms.

`(d) ACTIVITIES CARRIED ON PARTNERSHIPS, ETC- In applying this subchapter to a partner in a partnership--

    `**(1)** each partner shall be treated as operating vessels operated by the partnership,

    `**(2)** each partner shall be treated as conducting the activities conducted by the partnership, and

    `**(3)** the extent of a partner's ownership or charter interest in any vessel owned by or chartered to the partnership shall be determined on the basis of the partner's interest in the partnership.

A similar rule shall apply with respect to other pass-thru entities.

`(e) EFFECT OF TEMPORARILY CEASING TO OPERATE A QUALIFYING VESSEL-

    `**(1) IN GENERAL-** For purposes of subsections (b) and (c), an electing corporation shall be treated as continuing to use a qualifying vessel during any period of temporary cessation if the electing corporation gives timely notice to the Secretary stating--

        `**(A)** that it has temporarily ceased to operate the qualifying vessel, and

        `**(B)** its intention to resume operating the qualifying vessel.

    `**(2) NOTICE-** Notice shall be deemed timely if given not later than the due date (including extensions) for the corporation's tax return for the taxable year in which the temporary cessation begins.

    `**(3) PERIOD DISREGARD IN EFFECT-** The period of temporary cessation under paragraph (1) shall continue until the earlier of the date on which--

        `**(A)** the electing corporation abandons its intention to resume operation of the qualifying vessel, or

        `**(B)** the electing corporation resumes operation of the qualifying vessel.

``(f) EFFECT OF TEMPORARILY OPERATING A QUALIFYING VESSEL IN THE UNITED STATES DOMESTIC TRADE-

``(1) IN GENERAL- For purposes of this subchapter, an electing corporation shall be treated as continuing to use a qualifying vessel in the United States foreign trade during any period of temporary use in the United States domestic trade if the electing corporation gives timely notice to the Secretary stating--

``(A) that it temporarily operates or has operated in the United States domestic trade a qualifying vessel which had been used in the United States foreign trade, and

``(B) its intention to resume operation of the vessel in the United States foreign trade.

``(2) NOTICE- Notice shall be deemed timely if given not later than the due date (including extensions) for the corporation's tax return for the taxable year in which the temporary cessation begins.

``(3) PERIOD DISREGARD IN EFFECT- The period of temporary use under paragraph (1) continues until the earlier of the date of which--

``(A) the electing corporation abandons its intention to resume operations of the vessel in the United States foreign trade, or  
``(B) the electing corporation resumes operation of the vessel in the United States foreign trade.

``(4) NO DISREGARD IF DOMESTIC TRADE USE EXCEEDS 30 DAYS- Paragraph (1) shall not apply to any qualifying vessel which is operated in the United States domestic trade for more than 30 days during the taxable year.

``(g) REGULATIONS- The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.

**``SEC. 1356. QUALIFYING SHIPPING ACTIVITIES.**

``(a) QUALIFYING SHIPPING ACTIVITIES- For purposes of this subchapter, the term `qualifying shipping activities' means--

``(1) core qualifying activities,  
``(2) qualifying secondary activities, and  
``(3) qualifying incidental activities.

``(b) CORE QUALIFYING ACTIVITIES- For purposes of this subchapter, the term `core qualifying activities' means activities in operating qualifying vessels in United States foreign trade.

``(c) QUALIFYING SECONDARY ACTIVITIES- For purposes of this section--

``(1) IN GENERAL- The term `qualifying secondary activities' means secondary activities but only to the extent that, without regard to this subchapter, the gross income derived by such corporation from such activities does not exceed 20 percent of the gross income derived by the corporation from its core qualifying activities.

``(2) SECONDARY ACTIVITIES- The term `secondary activities' means--

``(A) the active management or operation of vessels other than qualifying vessels in the United States foreign trade,

``(B) the provision of vessel, barge, container, or cargo-related facilities or services to any person,

``(C) other activities of the electing corporation and other members of its electing group that are an integral part of its business of operating qualifying vessels in United States foreign trade, including--

``(i) ownership or operation of barges, containers, chassis, and other equipment that are the complement of, or used in connection with, a qualifying vessel in United States foreign trade,

``(ii) the inland haulage of cargo shipped, or to be shipped, on qualifying vessels in United States foreign trade, and

``(iii) the provision of terminal, maintenance, repair, logistical, or other vessel, barge, container, or cargo-related services that are an integral part of operating qualifying vessels in United States foreign trade, and

``(D) such other activities as may be prescribed by the Secretary pursuant to regulations.

``(3) COORDINATION WITH CORE ACTIVITIES-

``(A) IN GENERAL- Such term shall not include any core qualifying activities.

``(B) NONELECTING CORPORATIONS- In the case of a corporation (other than an electing corporation) which is a member of an electing group, any core qualifying activities of the corporation shall be treated as qualifying secondary activities (and not as core qualifying activities).

``(d) QUALIFYING INCIDENTAL ACTIVITIES- For purposes of this section, the term 'qualified incidental activities' means shipping-related activities if--

``(1) they are incidental to the corporation's core qualifying activities,

``(2) they are not qualifying secondary activities, and

``(3) without regard to this subchapter, the gross income derived by such corporation from such activities does not exceed 0.1 percent of the corporation's gross income from its core qualifying activities.

``(e) APPLICATION OF GROSS INCOME TESTS IN CASE OF ELECTING GROUP- In the case of an electing group, subsections (c)(1) and (d)(3) shall be applied as if such group were 1 entity, and the limitations under such subsections shall be allocated among the corporations in such group.

**``SEC. 1357. ITEMS NOT SUBJECT TO REGULAR TAX; DEPRECIATION; INTEREST.**

``(a) EXCLUSION FROM GROSS INCOME- Gross income of an electing corporation shall not include its income from qualifying shipping activities.

^(b) ELECTING GROUP MEMBER- Gross income of a corporation (other than an electing corporation) which is a member of an electing group shall not include its income from qualifying shipping activities conducted by such member.

^(c) DENIAL OF LOSSES, DEDUCTIONS, AND CREDITS-

^(1) GENERAL RULE- Subject to paragraph (2), each item of loss, deduction (other than for interest expense), or credit of any taxpayer with respect to any activity the income from which is excluded from gross income under this section shall be disallowed.

^(2) DEPRECIATION-

^(A) IN GENERAL- Notwithstanding paragraph (1), the adjusted basis (for purposes of determining gain) of any qualifying vessel shall be determined as if the deduction for depreciation had been allowed.

^(B) METHOD-

^(i) IN GENERAL- Except as provided in clause (ii), the straight-line method of depreciation shall apply to qualifying vessels the income from operation of which is excluded from gross income under this section.

^(ii) EXCEPTION- Clause (i) shall not apply to any qualifying vessel which is subject to a charter entered into before the date of the enactment of this subchapter.

^(3) INTEREST-

^(A) IN GENERAL- Except as provided in subparagraph (B), the interest expense of an electing corporation shall be disallowed in the ratio that the fair market value of such corporation's qualifying vessels bears to the fair market value of such corporation's total assets.

^(B) ELECTING GROUP- In the case of a corporation which is a member of an electing group, the interest expense of such corporation shall be disallowed in the ratio that the fair market value of such corporation's qualifying vessels bears to the fair market value of the electing groups total assets.

## **^SEC. 1358. ALLOCATION OF CREDITS, INCOME, AND DEDUCTIONS.**

^(a) QUALIFYING SHIPPING ACTIVITIES- For purposes of this chapter, the qualifying shipping activities of an electing corporation shall be treated as a separate trade or business activity distinct from all other activities conducted by such corporation.

^(b) EXCLUSION OF CREDITS OR DEDUCTIONS-

^(1) No deduction shall be allowed against the notional shipping income of an electing corporation, and no credit shall be allowed against the tax imposed by section 1352(a)(2).

^(2) No deduction shall be allowed for any net operating loss attributable to the qualifying shipping activities of any person to the extent that such

loss is carried forward by such person from a taxable year preceding the first taxable year for which such person was an electing corporation.

^(c) TRANSACTIONS NOT AT ARM'S LENGTH- Section 482 applies in accordance with this subsection to a transaction or series of transactions--

^(1) as between an electing corporation and another person, or

^(2) as between a person's qualifying shipping activities and other activities carried on by it.

## **SEC. 1359. DISPOSITION OF QUALIFYING VESSELS.**

^(a) IN GENERAL- If any qualifying vessel operator sells or disposes of any qualifying vessel in an otherwise taxable transaction, at the election of such operator, no gain shall be recognized if any replacement qualifying vessel is acquired during the period specified in subsection (b), except to the extent that the amount realized upon such sale or disposition exceeds the cost of the replacement qualifying vessel.

^(b) PERIOD WITHIN WHICH PROPERTY MUST BE REPLACED- The period referred to in subsection (a) shall be the period beginning one year prior to the disposition of the qualifying vessel and ending--

^(1) 3 years after the close of the first taxable year in which the gain is realized, or

^(2) subject to such terms and conditions as may be specified by the Secretary, on such later date as the Secretary may designate on application by the taxpayer.

Such application shall be made at such time and in such manner as the Secretary may by regulations prescribe.

^(c) APPLICATION OF SECTION TO NONCORPORATE OPERATORS- For purposes of this section, the term 'qualifying vessel operator' includes any person who would be a qualifying vessel operator were such person a corporation.

^(d) TIME FOR ASSESSMENT OF DEFICIENCY ATTRIBUTABLE TO GAIN- If a qualifying vessel operator has made the election provided in subsection (a), then--

^(1) the statutory period for the assessment of any deficiency, for any taxable year in which any part of the gain is realized, attributable to such gain shall not expire prior to the expiration of 3 years from the date the Secretary is notified by such operator (in such manner as the Secretary may by regulations prescribe) of the replacement qualifying vessel or of an intention not to replace, and

^(2) such deficiency may be assessed before the expiration of such 3-year period notwithstanding the provisions of section 6212(c) or the provisions of any other law or rule of law which would otherwise prevent such assessment.

^(e) BASIS OF REPLACEMENT QUALIFYING VESSEL- In the case of any replacement qualifying vessel purchased by the qualifying vessel operator which resulted in the nonrecognition of any part of the gain realized as the result of a sale or other disposition of a qualifying vessel, the basis shall be the cost of the

replacement qualifying vessel decreased in the amount of the gain not so recognized; and if the property purchased consists of more than one piece of property, the basis determined under this sentence shall be allocated to the purchased properties in proportion to their respective costs.'.

(b) TECHNICAL AMENDMENTS-

(1) The second sentence of section 56(g)(4)(B)(i), as amended by this Act, is further amended by inserting 'or 1357' after 'section 139A'.

(2) The table of subchapters for chapter 1 is amended by inserting after the item relating to subchapter S the following new item:

'Subchapter R. Election to determine corporate tax on certain international shipping activities using per ton rate.'

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

**Subtitle F--Stock Options and Employee Stock Purchase Plan Stock Options**

**SEC. 251. EXCLUSION OF INCENTIVE STOCK OPTIONS AND EMPLOYEE STOCK PURCHASE PLAN STOCK OPTIONS FROM WAGES.**

(a) EXCLUSION FROM EMPLOYMENT TAXES-

(1) SOCIAL SECURITY TAXES-

(A) Section 3121(a) (relating to definition of wages) is amended by striking 'or' at the end of paragraph (20), by striking the period at the end of paragraph (21) and inserting ';' or', and by inserting after paragraph (21) the following new paragraph:

'(22) remuneration on account of-

'(A) a transfer of a share of stock to any individual pursuant to an exercise of an incentive stock option (as defined in section 422(b)) or under an employee stock purchase plan (as defined in section 423(b)), or

'(B) any disposition by the individual of such stock.'

(B) Section 209(a) of the Social Security Act is amended by striking 'or' at the end of paragraph (17), by striking the period at the end of paragraph (18) and inserting ';' or', and by inserting after paragraph (18) the following new paragraph:

'(19) Remuneration on account of-

'(A) a transfer of a share of stock to any individual pursuant to an exercise of an incentive stock option (as defined in section 422(b)) of the Internal Revenue Code of 1986 or under an employee stock purchase plan (as defined in section 423(b) of such Code), or

'(B) any disposition by the individual of such stock.'

(2) RAILROAD RETIREMENT TAXES- Subsection (e) of section 3231 is amended by adding at the end the following new paragraph:

`(12) QUALIFIED STOCK OPTIONS- The term `compensation' shall not include any remuneration on account of-`

`(A) a transfer of a share of stock to any individual pursuant to an exercise of an incentive stock option (as defined in section 422(b)) or under an employee stock purchase plan (as defined in section 423(b)), or

`(B) any disposition by the individual of such stock.'.

(3) UNEMPLOYMENT TAXES- Section 3306(b) (relating to definition of wages) is amended by striking `or' at the end of paragraph (17), by striking the period at the end of paragraph (18) and inserting `; or', and by inserting after paragraph (18) the following new paragraph:

`(19) remuneration on account of-`

`(A) a transfer of a share of stock to any individual pursuant to an exercise of an incentive stock option (as defined in section 422(b)) or under an employee stock purchase plan (as defined in section 423(b)), or

`(B) any disposition by the individual of such stock.'.

(b) WAGE WITHHOLDING NOT REQUIRED ON DISQUALIFYING DISPOSITIONS- Section 421(b) (relating to effect of disqualifying dispositions) is amended by adding at the end the following new sentence: `No amount shall be required to be deducted and withheld under chapter 24 with respect to any increase in income attributable to a disposition described in the preceding sentence.'

(c) WAGE WITHHOLDING NOT REQUIRED ON COMPENSATION WHERE OPTION PRICE IS BETWEEN 85 PERCENT AND 100 PERCENT OF VALUE OF STOCK- Section 423(c) (relating to special rule where option price is between 85 percent and 100 percent of value of stock) is amended by adding at the end the following new sentence: `No amount shall be required to be deducted and withheld under chapter 24 with respect to any amount treated as compensation under this subsection.'

(d) EFFECTIVE DATE- The amendments made by this section shall apply to stock acquired pursuant to options exercised after the date of the enactment of this Act.

### **TITLE III--TAX RELIEF FOR AGRICULTURE AND SMALL MANUFACTURERS**

#### **Subtitle A--Volumetric Ethanol Excise Tax Credit**

### **SEC. 301. ALCOHOL AND BIODIESEL EXCISE TAX CREDIT AND EXTENSION OF ALCOHOL FUELS INCOME TAX CREDIT.**

(a) IN GENERAL- Subchapter B of chapter 65 (relating to rules of special application) is amended by inserting after section 6425 the following new section:

## **SEC. 6426. CREDIT FOR ALCOHOL FUEL AND BIODIESEL MIXTURES.**

^(a) ALLOWANCE OF CREDITS- There shall be allowed as a credit against the tax imposed by section 4081 an amount equal to the sum of-

- ^(1) the alcohol fuel mixture credit, plus
- ^(2) the biodiesel mixture credit.

^(b) ALCOHOL FUEL MIXTURE CREDIT-

^(1) IN GENERAL- For purposes of this section, the alcohol fuel mixture credit is the product of the applicable amount and the number of gallons of alcohol used by the taxpayer in producing any alcohol fuel mixture for sale or use in a trade or business of the taxpayer.

^(2) APPLICABLE AMOUNT- For purposes of this subsection-

^(A) IN GENERAL- Except as provided in subparagraph (B), the applicable amount is 51 cents.

^(B) MIXTURES NOT CONTAINING ETHANOL- In the case of an alcohol fuel mixture in which none of the alcohol consists of ethanol, the applicable amount is 60 cents.

^(3) ALCOHOL FUEL MIXTURE- For purposes of this subsection, the term `alcohol fuel mixture' means a mixture of alcohol and a taxable fuel which-

^(A) is sold by the taxpayer producing such mixture to any person for use as a fuel, or

^(B) is used as a fuel by the taxpayer producing such mixture.

For purposes of subparagraph (A), a mixture produced by any person at a refinery prior to a taxable event which includes ethyl tertiary butyl ether or other ethers produced from alcohol shall be treated as sold at the time of its removal from the refinery (and only at such time) to another person for use as a fuel.

^(4) OTHER DEFINITIONS- For purposes of this subsection-

^(A) ALCOHOL- The term `alcohol' includes methanol and ethanol but does not include--

^(i) alcohol produced from petroleum, natural gas, or coal (including peat), or

^(ii) alcohol with a proof of less than 190 (determined without regard to any added denaturants).

Such term also includes an alcohol gallon equivalent of ethyl tertiary butyl ether or other ethers produced from such alcohol.

^(B) TAXABLE FUEL- The term `taxable fuel' has the meaning given such term by section 4083(a)(1).

^(5) TERMINATION- This subsection shall not apply to any sale, use, or removal for any period after December 31, 2010.

^(c) BIODIESEL MIXTURE CREDIT-

^(1) IN GENERAL- For purposes of this section, the biodiesel mixture credit is the product of the applicable amount and the number of gallons of

biodiesel used by the taxpayer in producing any biodiesel mixture for sale or use in a trade or business of the taxpayer.

`(2) APPLICABLE AMOUNT- For purposes of this subsection--

` (A) IN GENERAL- Except as provided in subparagraph (B), the applicable amount is 50 cents.

` (B) AMOUNT FOR AGRI-BIODIESEL- In the case of any biodiesel which is agri-biodiesel, the applicable amount is \$1.00.

`(3) BIODIESEL MIXTURE- For purposes of this section, the term 'biodiesel mixture' means a mixture of biodiesel and diesel fuel (as defined in section 4083(a)(3)), determined without regard to any use of kerosene, which--

` (A) is sold by the taxpayer producing such mixture to any person for use as a fuel, or

` (B) is used as a fuel by the taxpayer producing such mixture.

`(4) CERTIFICATION FOR BIODIESEL- No credit shall be allowed under this subsection unless the taxpayer obtains a certification (in such form and manner as prescribed by the Secretary) from the producer of the biodiesel which identifies the product produced and the percentage of biodiesel and agri-biodiesel in the product.

`(5) OTHER DEFINITIONS- Any term used in this subsection which is also used in section 40A shall have the meaning given such term by section 40A.

`(6) TERMINATION- This subsection shall not apply to any sale, use, or removal for any period after December 31, 2006.

`(d) MIXTURE NOT USED AS A FUEL, ETC-

`(1) IMPOSITION OF TAX- If--

` (A) any credit was determined under this section with respect to alcohol or biodiesel used in the production of any alcohol fuel mixture or biodiesel mixture, respectively, and

` (B) any person--

` ` (i) separates the alcohol or biodiesel from the mixture, or

` ` (ii) without separation, uses the mixture other than as a fuel,

then there is hereby imposed on such person a tax equal to the product of the applicable amount and the number of gallons of such alcohol or biodiesel.

`(2) APPLICABLE LAWS- All provisions of law, including penalties, shall, insofar as applicable and not inconsistent with this section, apply in respect of any tax imposed under paragraph (1) as if such tax were imposed by section 4081 and not by this section.

`(e) COORDINATION WITH EXEMPTION FROM EXCISE TAX- Rules similar to the rules under section 40(c) shall apply for purposes of this section.'

(b) REGISTRATION REQUIREMENT- Section 4101(a)(1) (relating to registration), as amended by section 861, is amended by inserting 'and every person producing or importing biodiesel (as defined in section 40A(d)(1)) or

alcohol (as defined in section 6426(b)(4)(A))' before `shall register with the Secretary'.

(c) ADDITIONAL AMENDMENTS-

(1) Section 40(c) is amended by striking `subsection (b)(2), (k), or (m) of section 4041, section 4081(c), or section 4091(c)' and inserting `section 4041(b)(2), section 6426, or section 6427(e)'.

(2) Paragraph (4) of section 40(d) is amended to read as follows:

`(4) VOLUME OF ALCOHOL- For purposes of determining under subsection (a) the number of gallons of alcohol with respect to which a credit is allowable under subsection (a), the volume of alcohol shall include the volume of any denaturant (including gasoline) which is added under any formulas approved by the Secretary to the extent that such denaturants do not exceed 5 percent of the volume of such alcohol (including denaturants).`

(3) Section 40(e)(1) is amended--

(A) by striking `2007' in subparagraph (A) and inserting `2010', and

(B) by striking `2008' in subparagraph (B) and inserting `2011'.

(4) Section 40(h) is amended--

(A) by striking `2007' in paragraph (1) and inserting `2010', and

(B) by striking `2006, or 2007' in the table contained in paragraph (2) and inserting `through 2010'.

(5) Section 4041(b)(2)(B) is amended by striking `a substance other than petroleum or natural gas' and inserting `coal (including peat)'.

(6) Section 4041 is amended by striking subsection (k).

(7) Section 4081 is amended by striking subsection (c).

(8) Paragraph (2) of section 4083(a) is amended to read as follows:

`(2) GASOLINE- The term `gasoline'--

`(A) includes any gasoline blend, other than qualified methanol or ethanol fuel (as defined in section 4041(b)(2)(B)), partially exempt methanol or ethanol fuel (as defined in section 4041(m)(2)), or a denatured alcohol, and

`(B) includes, to the extent prescribed in regulations--

`(i) any gasoline blend stock, and

`(ii) any product commonly used as an additive in gasoline (other than alcohol).

For purposes of subparagraph (B)(i), the term `gasoline blend stock' means any petroleum product component of gasoline.'

(9) Section 6427 is amended by inserting after subsection (d) the following new subsection:

(e) ALCOHOL OR BIODIESEL USED TO PRODUCE ALCOHOL FUEL AND BIODIESEL MIXTURES- Except as provided in subsection (k)--

`(1) USED TO PRODUCE A MIXTURE- If any person produces a mixture described in section 6426 in such person's trade or business, the Secretary shall pay (without interest) to such person an amount equal to

the alcohol fuel mixture credit or the biodiesel mixture credit with respect to such mixture.

‘(2) COORDINATION WITH OTHER REPAYMENT PROVISIONS-  
No amount shall be payable under paragraph (1) with respect to any mixture with respect to which an amount is allowed as a credit under section 6426.

‘(3) TERMINATION- This subsection shall not apply with respect to--

- ‘(A) any alcohol fuel mixture (as defined in section 6426(b)(3)) sold or used after December 31, 2010, and
- ‘(B) any biodiesel mixture (as defined in section 6426(c)(3)) sold or used after December 31, 2006.’.

(10) Section 6427(i)(3) is amended--

- (A) by striking ‘subsection (f) both places it appears in subparagraph (A) and inserting ‘subsection (e)(1)’,
- (B) by striking ‘gasoline, diesel fuel, or kerosene used to produce a qualified alcohol mixture (as defined in section 4081(c)(3))’ in subparagraph (A) and inserting ‘a mixture described in section 6426’,
- (C) by adding at the end of subparagraph (A) the following new flush sentence:  
‘In the case of an electronic claim, this subparagraph shall be applied without regard to clause (i).’,
- (D) by striking ‘subsection (f)(1)’ in subparagraph (B) and inserting ‘subsection (e)(1)’,
- (E) by striking ‘20 days of the date of the filing of such claim’ in subparagraph (B) and inserting ‘45 days of the date of the filing of such claim (20 days in the case of an electronic claim)’, and
- (F) by striking ‘ALCOHOL MIXTURE’ in the heading and inserting ‘ALCOHOL FUEL AND BIODIESEL MIXTURE’.

(11) Section 9503(b)(1) is amended by adding at the end the following new flush sentence:

‘For purposes of this paragraph, taxes received under sections 4041 and 4081 shall be determined without reduction for credits under section 6426.’.

(12) Section 9503(b)(4) is amended--

- (A) by adding ‘or’ at the end of subparagraph (C),
- (B) by striking the comma at the end of subparagraph (D)(iii) and inserting a period, and
- (C) by striking subparagraphs (E) and (F).

(13) Section 9503(c)(2)(A) is amended by adding at the end the following:  
‘Clauses (i)(III) and (ii) shall not apply to claims under section 6427(e).’.

(14) The table of sections for subchapter B of chapter 65 is amended by inserting after the item relating to section 6425 the following new item:  
**‘Sec. 6426. Credit for alcohol fuel and biodiesel mixtures.’.**

(d) EFFECTIVE DATES-

- (1) IN GENERAL- Except as otherwise provided in this subsection, the amendments made by this section shall apply to fuel sold or used after December 31, 2004.
- (2) REGISTRATION REQUIREMENT- The amendment made by subsection (b) shall take effect on April 1, 2005.
- (3) EXTENSION OF ALCOHOL FUELS CREDIT- The amendments made by paragraphs (3), (4), and (14) of subsection (c) shall take effect on the date of the enactment of this Act.
- (4) REPEAL OF GENERAL FUND RETENTION OF CERTAIN ALCOHOL FUELS TAXES- The amendments made by subsection (c)(12) shall apply to fuel sold or used after September 30, 2004.
- (e) FORMAT FOR FILING- The Secretary of the Treasury shall describe the electronic format for filing claims described in section 6427(i)(3)(B) of the Internal Revenue Code of 1986 (as amended by subsection (c)(10)(C)) not later than December 31, 2004.

## **SEC. 302. BIODIESEL INCOME TAX CREDIT.**

- (a) IN GENERAL- Subpart D of part IV of subchapter A of chapter 1 (relating to business related credits) is amended by inserting after section 40 the following new section:

### **SEC. 40A. BIODIESEL USED AS FUEL.**

- ^(a) GENERAL RULE- For purposes of section 38, the biodiesel fuels credit determined under this section for the taxable year is an amount equal to the sum of--
  - ^(1) the biodiesel mixture credit, plus
  - ^(2) the biodiesel credit.
- ^(b) DEFINITION OF BIODIESEL MIXTURE CREDIT AND BIODIESEL CREDIT- For purposes of this section--
  - ^(1) BIODIESEL MIXTURE CREDIT-
    - ^(A) IN GENERAL- The biodiesel mixture credit of any taxpayer for any taxable year is 50 cents for each gallon of biodiesel used by the taxpayer in the production of a qualified biodiesel mixture.
    - ^(B) QUALIFIED BIODIESEL MIXTURE- The term 'qualified biodiesel mixture' means a mixture of biodiesel and diesel fuel (as defined in section 4083(a)(3)), determined without regard to any use of kerosene, which--
      - ^(i) is sold by the taxpayer producing such mixture to any person for use as a fuel, or
      - ^(ii) is used as a fuel by the taxpayer producing such mixture.
    - ^(C) SALE OR USE MUST BE IN TRADE OR BUSINESS, ETC- Biodiesel used in the production of a qualified biodiesel mixture shall be taken into account--

``(i) only if the sale or use described in subparagraph (B) is in a trade or business of the taxpayer, and

``(ii) for the taxable year in which such sale or use occurs.

``(D) CASUAL OFF-FARM PRODUCTION NOT ELIGIBLE- No credit shall be allowed under this section with respect to any casual off-farm production of a qualified biodiesel mixture.

``(2) BIODIESEL CREDIT-

``(A) IN GENERAL- The biodiesel credit of any taxpayer for any taxable year is 50 cents for each gallon of biodiesel which is not in a mixture with diesel fuel and which during the taxable year--

``(i) is used by the taxpayer as a fuel in a trade or business, or

``(ii) is sold by the taxpayer at retail to a person and placed in the fuel tank of such person's vehicle.

``(B) USER CREDIT NOT TO APPLY TO BIODIESEL SOLD AT RETAIL- No credit shall be allowed under subparagraph (A)(i) with respect to any biodiesel which was sold in a retail sale described in subparagraph (A)(ii).

``(3) CREDIT FOR AGRI-BIODIESEL- In the case of any biodiesel which is agri-biodiesel, paragraphs (1)(A) and (2)(A) shall be applied by substituting ``\$1.00' for `50 cents'.

``(4) CERTIFICATION FOR BIODIESEL- No credit shall be allowed under this section unless the taxpayer obtains a certification (in such form and manner as prescribed by the Secretary) from the producer or importer of the biodiesel which identifies the product produced and the percentage of biodiesel and agri-biodiesel in the product.

``(c) COORDINATION WITH CREDIT AGAINST EXCISE TAX- The amount of the credit determined under this section with respect to any biodiesel shall be properly reduced to take into account any benefit provided with respect to such biodiesel solely by reason of the application of section 6426 or 6427(e).

``(d) DEFINITIONS AND SPECIAL RULES- For purposes of this section--

``(1) BIODIESEL- The term `biodiesel' means the monoalkyl esters of long chain fatty acids derived from plant or animal matter which meet--

``(A) the registration requirements for fuels and fuel additives established by the Environmental Protection Agency under section 211 of the Clean Air Act (42 U.S.C. 7545), and

``(B) the requirements of the American Society of Testing and Materials D6751.

``(2) AGRI-BIODIESEL- The term `agri-biodiesel' means biodiesel derived solely from virgin oils, including esters derived from virgin vegetable oils from corn, soybeans, sunflower seeds, cottonseeds, canola, crambe, rapeseeds, safflowers, flaxseeds, rice bran, and mustard seeds, and from animal fats.

``(3) MIXTURE OR BIODIESEL NOT USED AS A FUEL, ETC-

``(A) MIXTURES- If--

``(i) any credit was determined under this section with respect to biodiesel used in the production of any qualified biodiesel mixture, and

``(ii) any person--

``(I) separates the biodiesel from the mixture, or

``(II) without separation, uses the mixture other than as a fuel,

then there is hereby imposed on such person a tax equal to the product of the rate applicable under subsection (b)(1)(A) and the number of gallons of such biodiesel in such mixture.

``(B) BIODIESEL- If--

``(i) any credit was determined under this section with respect to the retail sale of any biodiesel, and

``(ii) any person mixes such biodiesel or uses such biodiesel other than as a fuel,

then there is hereby imposed on such person a tax equal to the product of the rate applicable under subsection (b)(2)(A) and the number of gallons of such biodiesel.

``(C) APPLICABLE LAWS- All provisions of law, including penalties, shall, insofar as applicable and not inconsistent with this section, apply in respect of any tax imposed under subparagraph (A) or (B) as if such tax were imposed by section 4081 and not by this chapter.

``(4) PASS-THRU IN THE CASE OF ESTATES AND TRUSTS- Under regulations prescribed by the Secretary, rules similar to the rules of subsection (d) of section 52 shall apply.

``(e) TERMINATION- This section shall not apply to any sale or use after December 31, 2006.'

(b) CREDIT TREATED AS PART OF GENERAL BUSINESS CREDIT-

Section 38(b) (relating to current year business credit), as amended by this Act, is amended by striking `plus' at the end of paragraph (15), by striking the period at the end of paragraph (16) and inserting `, plus', and by inserting after paragraph (16) the following new paragraph:

``(17) the biodiesel fuels credit determined under section 40A(a).'

(c) CONFORMING AMENDMENTS-

(1)(A) Section 87 is amended to read as follows:

## **``SEC. 87. ALCOHOL AND BIODIESEL FUELS CREDITS.**

``Gross income includes--

``(1) the amount of the alcohol fuel credit determined with respect to the taxpayer for the taxable year under section 40(a), and

``(2) the biodiesel fuels credit determined with respect to the taxpayer for the taxable year under section 40A(a).'

(B) The item relating to section 87 in the table of sections for part II of subchapter B of chapter 1 is amended by striking 'fuel credit' and inserting 'and biodiesel fuels credits'.

(2) Section 196(c) is amended by striking 'and' at the end of paragraph (9), by striking the period at the end of paragraph (10) and inserting ', and', and by adding at the end the following new paragraph:

'(11) the biodiesel fuels credit determined under section 40A(a).'

(3) The table of sections for subpart D of part IV of subchapter A of chapter 1 is amended by adding after the item relating to section 40 the following new item:

'Sec. 40A. Biodiesel used as fuel.'

(d) EFFECTIVE DATE- The amendments made by this section shall apply to fuel produced, and sold or used, after December 31, 2004, in taxable years ending after such date.

### **SEC. 303. INFORMATION REPORTING FOR PERSONS CLAIMING CERTAIN TAX BENEFITS.**

(a) IN GENERAL- Subpart C of part III of subchapter A of chapter 32 is amended by adding at the end the following new section:

### **SEC. 4104. INFORMATION REPORTING FOR PERSONS CLAIMING CERTAIN TAX BENEFITS.**

(a) IN GENERAL- The Secretary shall require any person claiming tax benefits--

'(1) under the provisions of section 34, 40, and 40A, to file a return at the time such person claims such benefits (in such manner as the Secretary may prescribe), and

'(2) under the provisions of section 4041(b)(2), 6426, or 6427(e) to file a quarterly return (in such manner as the Secretary may prescribe).

(b) CONTENTS OF RETURN- Any return filed under this section shall provide such information relating to such benefits and the coordination of such benefits as the Secretary may require to ensure the proper administration and use of such benefits.

(c) ENFORCEMENT- With respect to any person described in subsection (a) and subject to registration requirements under this title, rules similar to rules of section 4222(c) shall apply with respect to any requirement under this section.'

(b) CONFORMING AMENDMENT- The table of sections for subpart C of part III of subchapter A of chapter 32 is amended by adding at the end the following new item:

**'Sec. 4104. Information reporting for persons claiming certain tax benefits.'**

(c) EFFECTIVE DATE- The amendments made by this section shall take effect on January 1, 2005.

## **Subtitle B--Agricultural Incentives**

### **SEC. 311. SPECIAL RULES FOR LIVESTOCK SOLD ON ACCOUNT OF WEATHER-RELATED CONDITIONS.**

**(a) REPLACEMENT OF LIVESTOCK WITH OTHER FARM PROPERTY-** Subsection (f) of section 1033 (relating to involuntary conversions) is amended--

- (1) by inserting `drought, flood, or other weather-related conditions, or' after `because of',
- (2) by inserting `in the case of soil contamination or other environmental contamination' after `including real property', and
- (3) by striking `WHERE THERE HAS BEEN ENVIRONMENTAL CONTAMINATION' in the heading and inserting `IN CERTAIN CASES'.

**(b) EXTENSION OF REPLACEMENT PERIOD OF INVOLUNTARILY CONVERTED LIVESTOCK-** Subsection (e) of section 1033 (relating to involuntary conversions) is amended--

- (1) by striking `CONDITIONS- For purposes' and inserting `CONDITIONS-  
(1) IN GENERAL- For purposes', and
- (2) by adding at the end the following new paragraph:  
(2) EXTENSION OF REPLACEMENT PERIOD-  
(A) IN GENERAL- In the case of drought, flood, or other weather-related conditions described in paragraph (1) which result in the area being designated as eligible for assistance by the Federal Government, subsection (a)(2)(B) shall be applied with respect to any converted property by substituting `4 years' for `2 years'.  
(B) FURTHER EXTENSION BY SECRETARY- The Secretary may extend on a regional basis the period for replacement under this section (after the application of subparagraph (A)) for such additional time as the Secretary determines appropriate if the weather-related conditions which resulted in such application continue for more than 3 years.'

**(c) INCOME INCLUSION RULES-** Section 451(e) (relating to special rule for proceeds from livestock sold on account of drought, flood, or other weather-related conditions) is amended by adding at the end the following new paragraph:

(3) SPECIAL ELECTION RULES- If section 1033(e)(2) applies to a sale or exchange of livestock described in paragraph (1), the election under paragraph (1) shall be deemed valid if made during the replacement period described in such section.'

**(d) EFFECTIVE DATE-** The amendments made by this section shall apply to any taxable year with respect to which the due date (without regard to extensions) for the return is after December 31, 2002.

## **SEC. 312. PAYMENT OF DIVIDENDS ON STOCK OF COOPERATIVES WITHOUT REDUCING PATRONAGE DIVIDENDS.**

(a) IN GENERAL- Subsection (a) of section 1388 (relating to patronage dividend defined) is amended by adding at the end the following: `For purposes of paragraph (3), net earnings shall not be reduced by amounts paid during the year as dividends on capital stock or other proprietary capital interests of the organization to the extent that the articles of incorporation or bylaws of such organization or other contract with patrons provide that such dividends are in addition to amounts otherwise payable to patrons which are derived from business done with or for patrons during the taxable year.'.

(b) EFFECTIVE DATE- The amendment made by this section shall apply to distributions in taxable years beginning after the date of the enactment of this Act.

## **SEC. 313. APPORTIONMENT OF SMALL ETHANOL PRODUCER CREDIT.**

(a) ALLOCATION OF ALCOHOL FUELS CREDIT TO PATRONS OF A COOPERATIVE- Section 40(g) (relating to definitions and special rules for eligible small ethanol producer credit) is amended by adding at the end the following new paragraph:

`(6) ALLOCATION OF SMALL ETHANOL PRODUCER CREDIT TO PATRONS OF COOPERATIVE-

`(A) ELECTION TO ALLOCATE-

`(i) IN GENERAL- In the case of a cooperative organization described in section 1381(a), any portion of the credit determined under subsection (a)(3) for the taxable year may, at the election of the organization, be apportioned pro rata among patrons of the organization on the basis of the quantity or value of business done with or for such patrons for the taxable year.

`(ii) FORM AND EFFECT OF ELECTION- An election under clause (i) for any taxable year shall be made on a timely filed return for such year. Such election, once made, shall be irrevocable for such taxable year.

`(B) TREATMENT OF ORGANIZATIONS AND PATRONS-

`(i) ORGANIZATIONS- The amount of the credit not apportioned to patrons pursuant to subparagraph (A) shall be included in the amount determined under subsection (a)(3) for the taxable year of the organization.

`(ii) PATRONS- The amount of the credit apportioned to patrons pursuant to subparagraph (A) shall be included in the amount determined under such subsection for the first taxable year of each patron ending on or after the last day of the payment period (as defined in section 1382(d)) for the taxable year of the organization or, if earlier, for the

taxable year of each patron ending on or after the date on which the patron receives notice from the cooperative of the apportionment.

``(iii) SPECIAL RULES FOR DECREASE IN CREDITS FOR TAXABLE YEAR- If the amount of the credit of the organization determined under such subsection for a taxable year is less than the amount of such credit shown on the return of the organization for such year, an amount equal to the excess of-'

``(I) such reduction, over

``(II) the amount not apportioned to such patrons under subparagraph (A) for the taxable year,

shall be treated as an increase in tax imposed by this chapter on the organization. Such increase shall not be treated as tax imposed by this chapter for purposes of determining the amount of any credit under this chapter or for purposes of section 55.'

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

## **SEC. 314. COORDINATE FARMERS AND FISHERMEN INCOME AVERAGING AND THE ALTERNATIVE MINIMUM TAX.**

(a) IN GENERAL- Section 55(c) (defining regular tax) is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following new paragraph:

``(2) COORDINATION WITH INCOME AVERAGING FOR FARMERS AND FISHERMEN- Solely for purposes of this section, section 1301 (relating to averaging of farm and fishing income) shall not apply in computing the regular tax.'

(b) ALLOWING INCOME AVERAGING FOR FISHERMEN-

(1) IN GENERAL- Section 1301(a) is amended by striking `farming business' and inserting `farming business or fishing business'.

(2) DEFINITION OF ELECTED FARM INCOME-

(A) IN GENERAL- Clause (i) of section 1301(b)(1)(A) is amended by inserting `or fishing business' before the semicolon.

(B) CONFORMING AMENDMENT- Subparagraph (B) of section 1301(b)(1) is amended by inserting `or fishing business' after `farming business' both places it occurs.

(3) DEFINITION OF FISHING BUSINESS- Section 1301(b) is amended by adding at the end the following new paragraph:

``(4) FISHING BUSINESS- The term `fishing business' means the conduct of commercial fishing as defined in section 3 of the Magnuson-Stevens Fishery Conservation and Management Act (16 U.S.C. 1802).'

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

## **SEC. 315. CAPITAL GAIN TREATMENT UNDER SECTION 631(b) TO APPLY TO OUTRIGHT SALES BY LANDOWNERS.**

- (a) IN GENERAL- The first sentence of section 631(b) (relating to disposal of timber with a retained economic interest) is amended by striking `retains an economic interest in such timber' and inserting `either retains an economic interest in such timber or makes an outright sale of such timber'.
- (b) CONFORMING AMENDMENTS-
  - (1) The third sentence of section 631(b) is amended by striking `The date of disposal' and inserting `In the case of disposal of timber with a retained economic interest, the date of disposal'.
  - (2) The heading for section 631(b) is amended by striking `WITH A RETAINED ECONOMIC INTEREST'.
- (c) EFFECTIVE DATE- The amendments made by this section shall apply to sales after December 31, 2004.

## **SEC. 316. MODIFICATION TO COOPERATIVE MARKETING RULES TO INCLUDE VALUE ADDED PROCESSING INVOLVING ANIMALS.**

- (a) IN GENERAL- Section 1388 (relating to definitions and special rules) is amended by adding at the end the following new subsection:
  - `(k) COOPERATIVE MARKETING INCLUDES VALUE-ADDED PROCESSING INVOLVING ANIMALS- For purposes of section 521 and this subchapter, the marketing of the products of members or other producers shall include the feeding of such products to cattle, hogs, fish, chickens, or other animals and the sale of the resulting animals or animal products.'
- (b) CONFORMING AMENDMENT- Section 521(b) is amended by adding at the end the following new paragraph:
  - `(7) Cross Reference-
    - 'For treatment of value-added processing involving animals, see section 1388(k).'.
- (c) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years beginning after the date of the enactment of this Act.

## **SEC. 317. EXTENSION OF DECLARATORY JUDGMENT PROCEDURES TO FARMERS' COOPERATIVE ORGANIZATIONS.**

- (a) IN GENERAL- Section 7428(a)(1) (relating to declaratory judgments of tax exempt organizations) is amended by striking `or' at the end of subparagraph (B) and by adding at the end the following new subparagraph:
  - `(D) with respect to the initial classification or continuing classification of a cooperative as an organization described in section 521(b) which is exempt from tax under section 521(a), or'.
- (b) EFFECTIVE DATE- The amendments made by this section shall apply with respect to pleadings filed after the date of the enactment of this Act.

## **SEC. 318. CERTAIN EXPENSES OF RURAL LETTER CARRIERS.**

(a) IN GENERAL- Section 162(o) (relating to treatment of certain reimbursed expenses of rural mail carriers) is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following:

**`(2) SPECIAL RULE WHERE EXPENSES EXCEED**

**REIMBURSEMENTS**- Notwithstanding paragraph (1)(A), if the expenses incurred by an employee for the use of a vehicle in performing services described in paragraph (1) exceed the qualified reimbursements for such expenses, such excess shall be taken into account in computing the miscellaneous itemized deductions of the employee under section 67.'.

(b) CONFORMING AMENDMENT- The heading for section 162(o) is amended by striking 'REIMBURSED'.

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

## **SEC. 319. TREATMENT OF CERTAIN INCOME OF COOPERATIVES.**

(a) INCOME FROM OPEN ACCESS AND NUCLEAR DECOMMISSIONING TRANSACTIONS-

(1) IN GENERAL- Subparagraph (C) of section 501(c)(12) is amended by striking clause (ii) and adding at the end the following:

**`(ii) from any provision or sale of electric energy transmission services or ancillary services if such services are provided on a nondiscriminatory open access basis under an open access transmission tariff approved or accepted by FERC or under an independent transmission provider agreement approved or accepted by FERC (other than income received or accrued directly or indirectly from a member),**

**`(iii) from the provision or sale of electric energy distribution services or ancillary services if such services are provided on a nondiscriminatory open access basis to distribute electric energy not owned by the mutual or electric cooperative company--**

**`(I) to end-users who are served by distribution facilities not owned by such company or any of its members (other than income received or accrued directly or indirectly from a member), or**

**`(II) generated by a generation facility not owned or leased by such company or any of its members and which is directly connected to distribution facilities owned by such company or any of its members (other than income received or accrued directly or indirectly from a member),**

``(iv) from any nuclear decommissioning transaction, or  
``(v) from any asset exchange or conversion transaction.

Clauses (ii) through (v) shall not apply to taxable years beginning after December 31, 2006.'

(2) DEFINITIONS AND SPECIAL RULES- Paragraph (12) of section 501(c) is amended by adding at the end the following new subparagraphs:

``(E) For purposes of subparagraph (C)(ii), the term `FERC' means the Federal Energy Regulatory Commission and references to such term shall be treated as including the Public Utility Commission of Texas with respect to any ERCOT utility (as defined in section 212(k)(2)(B) of the Federal Power Act (16 U.S.C. 824k(k)(2)(B))).

``(F) For purposes of subparagraph (C)(iii), the term `nuclear decommissioning transaction' means--

``(i) any transfer into a trust, fund, or instrument established to pay any nuclear decommissioning costs if the transfer is in connection with the transfer of the mutual or cooperative electric company's interest in a nuclear power plant or nuclear power plant unit,

``(ii) any distribution from any trust, fund, or instrument established to pay any nuclear decommissioning costs, or

``(iii) any earnings from any trust, fund, or instrument established to pay any nuclear decommissioning costs.

``(G) For purposes of subparagraph (C)(iv), the term `asset exchange or conversion transaction' means any voluntary exchange or involuntary conversion of any property related to generating, transmitting, distributing, or selling electric energy by a mutual or cooperative electric company, the gain from which qualifies for deferred recognition under section 1031 or 1033, but only if the replacement property acquired by such company pursuant to such section constitutes property which is used, or to be used, for--

``(i) generating, transmitting, distributing, or selling electric energy, or

``(ii) producing, transmitting, distributing, or selling natural gas.'

(b) TREATMENT OF INCOME FROM LOAD LOSS TRANSACTIONS, ETC- Paragraph (12) of section 501(c), as amended by subsection (a)(2), is amended by adding after subparagraph (G) the following new subparagraph:

``(H)(i) In the case of a mutual or cooperative electric company described in this paragraph or an organization described in section 1381(a)(2)(C), income received or accrued from a load loss transaction shall be treated as an amount collected from members for the sole purpose of meeting losses and expenses.

``(ii) For purposes of clause (i), the term `load loss transaction' means any wholesale or retail sale of electric energy (other than to members) to the extent that the aggregate sales during the recovery

period do not exceed the load loss mitigation sales limit for such period.

``(iii) For purposes of clause (ii), the load loss mitigation sales limit for the recovery period is the sum of the annual load losses for each year of such period.

``(iv) For purposes of clause (iii), a mutual or cooperative electric company's annual load loss for each year of the recovery period is the amount (if any) by which--

``(I) the megawatt hours of electric energy sold during such year to members of such electric company are less than

``(II) the megawatt hours of electric energy sold during the base year to such members.

``(v) For purposes of clause (iv)(II), the term 'base year' means--

``(I) the calendar year preceding the start-up year, or

``(II) at the election of the mutual or cooperative electric company, the second or third calendar years preceding the start-up year.

``(vi) For purposes of this subparagraph, the recovery period is the 7-year period beginning with the start-up year.

``(vii) For purposes of this subparagraph, the start-up year is the first year that the mutual or cooperative electric company offers nondiscriminatory open access or the calendar year which includes the date of the enactment of this subparagraph, if later, at the election of such company.

``(viii) A company shall not fail to be treated as a mutual or cooperative electric company for purposes of this paragraph or as a corporation operating on a cooperative basis for purposes of section 1381(a)(2)(C) by reason of the treatment under clause (i).

``(ix) For purposes of subparagraph (A), in the case of a mutual or cooperative electric company, income received, or accrued, indirectly from a member shall be treated as an amount collected from members for the sole purpose of meeting losses and expenses.

``(x) This subparagraph shall not apply to taxable years beginning after December 31, 2006.'

(c) EXCEPTION FROM UNRELATED BUSINESS TAXABLE INCOME-

Subsection (b) of section 512 (relating to modifications) is amended by adding at the end the following new paragraph:

``(18) TREATMENT OF MUTUAL OR COOPERATIVE ELECTRIC COMPANIES- In the case of a mutual or cooperative electric company described in section 501(c)(12), there shall be excluded income which is treated as member income under subparagraph (H) thereof.'

(d) CROSS REFERENCE- Section 1381 is amended by adding at the end the following new subsection:

``(c) Cross Reference-

`For treatment of income from load loss transactions of organizations described in subsection (a)(2)(C), see section 501(c)(12)(H).`.

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

## **SEC. 320. EXCLUSION FOR PAYMENTS TO INDIVIDUALS UNDER NATIONAL HEALTH SERVICE CORPS LOAN REPAYMENT PROGRAM AND CERTAIN STATE LOAN REPAYMENT PROGRAMS.**

(a) IN GENERAL- Section 108(f) (relating to student loans) is amended by adding at the end the following new paragraph:

`(4) PAYMENTS UNDER NATIONAL HEALTH SERVICE CORPS LOAN REPAYMENT PROGRAM AND CERTAIN STATE LOAN REPAYMENT PROGRAMS- In the case of an individual, gross income shall not include any amount received under section 338B(g) of the Public Health Service Act or under a State program described in section 338I of such Act.'.

(b) TREATMENT FOR PURPOSES OF EMPLOYMENT TAXES- Each of the following provisions is amended by inserting `108(f)(4),' after `74(c),':

- (1) Section 3121(a)(20).
- (2) Section 3231(e)(5).
- (3) Section 3306(b)(16).
- (4) Section 3401(a)(19).
- (5) Section 209(a)(17) of the Social Security Act.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to amounts received by an individual in taxable years beginning after December 31, 2003.

## **SEC. 321. MODIFICATION OF SAFE HARBOR RULES FOR TIMBER REITs.**

(a) EXPANSION OF PROHIBITED TRANSACTION SAFE HARBOR- Section 857(b)(6) (relating to income from prohibited transactions) is amended by redesignating subparagraphs (D) and (E) as subparagraphs (E) and (F), respectively, and by inserting after subparagraph (C) the following new subparagraph:

`(D) CERTAIN SALES NOT TO CONSTITUTE PROHIBITED TRANSACTIONS- For purposes of this part, the term `prohibited transaction' does not include a sale of property which is a real estate asset (as defined in section 856(c)(5)(B)) if-

- `(i) the trust held the property for not less than 4 years in connection with the trade or business of producing timber,
- `(ii) the aggregate expenditures made by the trust, or a partner of the trust, during the 4-year period preceding the date of sale which--

``(I) are includable in the basis of the property (other than timberland acquisition expenditures), and  
``(II) are directly related to operation of the property for the production of timber or for the preservation of the property for use as timberland,  
do not exceed 30 percent of the net selling price of the property,  
``(iii) the aggregate expenditures made by the trust, or a partner of the trust, during the 4-year period preceding the date of sale which-  
``(I) are includable in the basis of the property (other than timberland acquisition expenditures), and  
``(II) are not directly related to operation of the property for the production of timber, or for the preservation of the property for use as timberland,  
do not exceed 5 percent of the net selling price of the property,  
``(iv)(I) during the taxable year the trust does not make more than 7 sales of property (other than sales of foreclosure property or sales to which section 1033 applies), or  
``(II) the aggregate adjusted bases (as determined for purposes of computing earnings and profits) of property (other than sales of foreclosure property or sales to which section 1033 applies) sold during the taxable year does not exceed 10 percent of the aggregate bases (as so determined) of all of the assets of the trust as of the beginning of the taxable year,  
``(v) in the case that the requirement of clause (iv)(I) is not satisfied, substantially all of the marketing expenditures with respect to the property were made through an independent contractor (as defined in section 856(d)(3)) from whom the trust itself does not derive or receive any income, and  
``(vi) the sales price of the property sold by the trust is not based in whole or in part on income or profits, including income or profits derived from the sale or operation of such property.'

(b) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years beginning after the date of the enactment of this Act.

## **SEC. 322. EXPENSING OF CERTAIN REFORESTATION EXPENDITURES.**

(a) IN GENERAL- So much of subsection (b) of section 194 (relating to amortization of reforestation expenditures) as precedes paragraph (2) is amended to read as follows:

~(b) TREATMENT AS EXPENSES-

~(1) ELECTION TO TREAT CERTAIN REFORESTATION EXPENDITURES AS EXPENSES-

~(A) IN GENERAL- In the case of any qualified timber property with respect to which the taxpayer has made (in accordance with regulations prescribed by the Secretary) an election under this subsection, the taxpayer shall treat reforestation expenditures which are paid or incurred during the taxable year with respect to such property as an expense which is not chargeable to capital account. The reforestation expenditures so treated shall be allowed as a deduction.

~(B) DOLLAR LIMITATION- The aggregate amount of reforestation expenditures which may be taken into account under subparagraph (A) with respect to each qualified timber property for any taxable year shall not exceed \$10,000 (\$5,000 in the case of a separate return by a married individual (as defined in section 7703)).'

(b) NET AMORTIZABLE BASIS- Section 194(c)(2) (defining amortizable basis) is amended by inserting 'which have not been taken into account under subsection (b)' after 'expenditures'.

(c) CONFORMING AMENDMENTS-

(1) Section 194(b) is amended by striking paragraphs (3) and (4).

(2) Section 194(b)(2) is amended by striking 'paragraph (1)' both places it appears and inserting 'paragraph (1)(B)'.

(3) Section 194(c) is amended by striking paragraph (4) and inserting the following new paragraphs:

~(4) TREATMENT OF TRUSTS AND ESTATES-

~(A) IN GENERAL- Except as provided in subparagraph (B), this section shall not apply to trusts and estates.

~(B) AMORTIZATION DEDUCTION ALLOWED TO ESTATES- The benefit of the deduction for amortization provided by subsection (a) shall be allowed to estates in the same manner as in the case of an individual. The allowable deduction shall be apportioned between the income beneficiary and the fiduciary under regulations prescribed by the Secretary. Any amount so apportioned to a beneficiary shall be taken into account for purposes of determining the amount allowable as a deduction under subsection (a) to such beneficiary.

~(5) APPLICATION WITH OTHER DEDUCTIONS- No deduction shall be allowed under any other provision of this chapter with respect to any expenditure with respect to which a deduction is allowed or allowable under this section to the taxpayer.'

(4) The heading for section 194 is amended by striking `amortization' and inserting `treatment'.

(5) The item relating to section 194 in the table of sections for part VI of subchapter B of chapter 1 is amended by striking `Amortization' and inserting `Treatment'.

(d) REPEAL OF REFORESTATION CREDIT-

(1) IN GENERAL- Section 46 (relating to amount of credit) is amended--

- (A) by adding `and' at the end of paragraph (1),
- (B) by striking `, and' at the end of paragraph (2) and inserting a period, and
- (C) by striking paragraph (3).

(2) CONFORMING AMENDMENTS-

(A) Section 48 is amended--

- (i) by striking subsection (b),
- (ii) by striking `this subsection' in paragraph (5) of subsection (a) and inserting `subsection (a)', and
- (iii) by redesignating such paragraph (5) as subsection (b).

(B) The heading for section 48 is amended by striking `; reforestation credit'.

(C) The item relating to section 48 in the table of sections for subpart E of part IV of subchapter A of chapter 1 is amended by striking `, reforestation credit'.

(D) Section 50(c)(3) is amended by striking `or reforestation credit'.

(e) EFFECTIVE DATE- The amendments made by this section shall apply with respect to expenditures paid or incurred after the date of the enactment of this Act.

### **Subtitle C--Incentives for Small Manufacturers**

## **SEC. 331. NET INCOME FROM PUBLICLY TRADED PARTNERSHIPS TREATED AS QUALIFYING INCOME OF REGULATED INVESTMENT COMPANIES.**

(a) IN GENERAL- Paragraph (2) of section 851(b) (defining regulated investment company) is amended to read as follows:

`(2) at least 90 percent of its gross income is derived from--

- `(A) dividends, interest, payments with respect to securities loans (as defined in section 512(a)(5)), and gains from the sale or other disposition of stock or securities (as defined in section 2(a)(36) of the Investment Company Act of 1940, as amended) or foreign currencies, or other income (including but not limited to gains from options, futures or forward contracts) derived with respect to its business of investing in such stock, securities, or currencies, and
- `(B) net income derived from an interest in a qualified publicly traded partnership (as defined in subsection (h)); and'.

(b) SOURCE FLOW-THROUGH RULE NOT TO APPLY- The last sentence of section 851(b) is amended by inserting `(other than a qualified publicly traded partnership as defined in subsection (h))' after `derived from a partnership'.

(c) LIMITATION ON OWNERSHIP- Subsection (c) of section 851 is amended by redesignating paragraph (5) as paragraph (6) and inserting after paragraph (4) the following new paragraph:

`(5) The term `outstanding voting securities of such issuer' shall include the equity securities of a qualified publicly traded partnership (as defined in subsection (h)).'.

(d) DEFINITION OF QUALIFIED PUBLICLY TRADED PARTNERSHIP-

Section 851 is amended by adding at the end the following new subsection:

`(h) QUALIFIED PUBLICLY TRADED PARTNERSHIP- For purposes of this section, the term `qualified publicly traded partnership' means a publicly traded partnership described in section 7704(b) other than a partnership which would satisfy the gross income requirements of section 7704(c)(2) if qualifying income included only income described in subsection (b)(2)(A).'.

(e) DEFINITION OF QUALIFYING INCOME- Section 7704(d)(4) is amended by striking `section 851(b)(2)' and inserting `section 851(b)(2)(A)'.

(f) LIMITATION ON COMPOSITION OF ASSETS- Subparagraph (B) of section 851(b)(3) is amended to read as follows:

`(B) not more than 25 percent of the value of its total assets is invested in-

`(i) the securities (other than Government securities or the securities of other regulated investment companies) of any one issuer,

`(ii) the securities (other than the securities of other regulated investment companies) of two or more issuers which the taxpayer controls and which are determined, under regulations prescribed by the Secretary, to be engaged in the same or similar trades or businesses or related trades or businesses, or

`(iii) the securities of one or more qualified publicly traded partnerships (as defined in subsection (h)).'.

(g) APPLICATION OF SPECIAL PASSIVE ACTIVITY RULE TO REGULATED INVESTMENT COMPANIES- Subsection (k) of section 469 (relating to separate application of section in case of publicly traded partnerships) is amended by adding at the end the following new paragraph:

`(4) APPLICATION TO REGULATED INVESTMENT COMPANIES- For purposes of this section, a regulated investment company (as defined in section 851) holding an interest in a qualified publicly traded partnership (as defined in section 851(h)) shall be treated as a taxpayer described in subsection (a)(2) with respect to items attributable to such interest.'.

(h) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years beginning after the date of the enactment of this Act.

## **SEC. 332. SIMPLIFICATION OF EXCISE TAX IMPOSED ON BOWS AND ARROWS.**

(a) BOWS- Paragraph (1) of section 4161(b) (relating to bows) is amended to read as follows:

  `**(1) BOWS-**

    `**(A) IN GENERAL-** There is hereby imposed on the sale by the manufacturer, producer, or importer of any bow which has a peak draw weight of 30 pounds or more, a tax equal to 11 percent of the price for which so sold.

    `**(B) ARCHERY EQUIPMENT-** There is hereby imposed on the sale by the manufacturer, producer, or importer--

      `**(i)** of any part or accessory suitable for inclusion in or attachment to a bow described in subparagraph (A), and  
      `**(ii)** of any quiver or broadhead suitable for use with an arrow described in paragraph (2),

      a tax equal to 11 percent of the price for which so sold.'

(b) ARROWS- Subsection (b) of section 4161 (relating to bows and arrows, etc.) is amended by redesignating paragraph (3) as paragraph (4) and inserting after paragraph (2) the following:

  `**(3) ARROWS-**

    `**(A) IN GENERAL-** There is hereby imposed on the sale by the manufacturer, producer, or importer of any arrow, a tax equal to 12 percent of the price for which so sold.

    `**(B) EXCEPTION-** In the case of any arrow of which the shaft or any other component has been previously taxed under paragraph (1) or (2)--

      `**(i)** section 6416(b)(3) shall not apply, and  
      `**(ii)** the tax imposed by subparagraph (A) shall be an amount equal to the excess (if any) of-

        `**(I)** the amount of tax imposed by this paragraph (determined without regard to this subparagraph), over

        `**(II)** the amount of tax paid with respect to the tax imposed under paragraph (1) or (2) on such shaft or component.

    `**(C) ARROW-** For purposes of this paragraph, the term 'arrow' means any shaft described in paragraph (2) to which additional components are attached.'

(c) CONFORMING AMENDMENTS- Section 4161(b)(2) is amended--

  (1) by inserting `(other than broadheads)' after 'point', and

  (2) by striking 'ARROWS-' in the heading and inserting 'ARROW COMPONENTS-'.

(d) EFFECTIVE DATE- The amendments made by this section shall apply to articles sold by the manufacturer, producer, or importer after the date which is 30 days after the date of the enactment of this Act.

## **SEC. 333. REDUCTION OF EXCISE TAX ON FISHING TACKLE BOXES.**

(a) IN GENERAL- Subsection (a) of section 4161 (relating to sport fishing equipment) is amended by redesignating paragraph (3) as paragraph (4) and by inserting after paragraph (2) the following new paragraph:

(3) 3 PERCENT RATE OF TAX FOR TACKLE BOXES- In the case of fishing tackle boxes, paragraph (1) shall be applied by substituting '3 percent' for '10 percent'.

(b) EFFECTIVE DATE- The amendments made this section shall apply to articles sold by the manufacturer, producer, or importer after December 31, 2004.

## **SEC. 334. SONAR DEVICES SUITABLE FOR FINDING FISH.**

(a) NOT TREATED AS SPORT FISHING EQUIPMENT- Subsection (a) of section 4162 (relating to sport fishing equipment defined) is amended by inserting 'and' at the end of paragraph (8), by striking ' ', and' at the end of paragraph (9) and inserting a period, and by striking paragraph (10).

(b) CONFORMING AMENDMENT- Section 4162 is amended by striking subsection (b) and by redesignating subsection (c) as subsection (b).

(c) EFFECTIVE DATE- The amendments made this section shall apply to articles sold by the manufacturer, producer, or importer after December 31, 2004.

## **SEC. 335. CHARITABLE CONTRIBUTION DEDUCTION FOR CERTAIN EXPENSES INCURRED IN SUPPORT OF NATIVE ALASKAN SUBSISTENCE WHALING.**

(a) IN GENERAL- Section 170 (relating to charitable, etc., contributions and gifts), as amended by this Act, is amended by redesignating subsection (n) as subsection (o) and by inserting after subsection (m) the following new subsection:

(n) EXPENSES PAID BY CERTAIN WHALING CAPTAINS IN SUPPORT OF NATIVE ALASKAN SUBSISTENCE WHALING-

(1) IN GENERAL- In the case of an individual who is recognized by the Alaska Eskimo Whaling Commission as a whaling captain charged with the responsibility of maintaining and carrying out sanctioned whaling activities and who engages in such activities during the taxable year, the amount described in paragraph (2) (to the extent such amount does not exceed \$10,000 for the taxable year) shall be treated for purposes of this section as a charitable contribution.

(2) AMOUNT DESCRIBED-

(A) IN GENERAL- The amount described in this paragraph is the aggregate of the reasonable and necessary whaling expenses paid by the taxpayer during the taxable year in carrying out sanctioned whaling activities.

(B) WHALING EXPENSES- For purposes of subparagraph (A), the term 'whaling expenses' includes expenses for--

- `(i) the acquisition and maintenance of whaling boats, weapons, and gear used in sanctioned whaling activities,
- `(ii) the supplying of food for the crew and other provisions for carrying out such activities, and
- `(iii) storage and distribution of the catch from such activities.

`(3) SANCTIONED WHALING ACTIVITIES- For purposes of this subsection, the term `sanctioned whaling activities' means subsistence bowhead whale hunting activities conducted pursuant to the management plan of the Alaska Eskimo Whaling Commission.

`(4) SUBSTANTIATION OF EXPENSES- The Secretary shall issue guidance requiring that the taxpayer substantiate the whaling expenses for which a deduction is claimed under this subsection, including by maintaining appropriate written records with respect to the time, place, date, amount, and nature of the expense, as well as the taxpayer's eligibility for such deduction, and that (to the extent provided by the Secretary) such substantiation be provided as part of the taxpayer's return of tax.'

(b) EFFECTIVE DATE- The amendments made by subsection (a) shall apply to contributions made after December 31, 2004.

## **SEC. 336. MODIFICATION OF DEPRECIATION ALLOWANCE FOR AIRCRAFT.**

(a) AIRCRAFT TREATED AS QUALIFIED PROPERTY-

(1) IN GENERAL- Paragraph (2) of section 168(k) is amended by redesignating subparagraphs (C) through (F) as subparagraphs (D) through (G), respectively, and by inserting after subparagraph (B) the following new subparagraph:

`(C) CERTAIN AIRCRAFT- The term `qualified property' includes property--

- `(i) which meets the requirements of clauses (ii) and (iii) of subparagraph (A),
- `(ii) which is an aircraft which is not a transportation property (as defined in subparagraph (B)(iii)) other than for agricultural or firefighting purposes,
- `(iii) which is purchased and on which such purchaser, at the time of the contract for purchase, has made a nonrefundable deposit of the lesser of-

  - `(I) 10 percent of the cost, or
  - `(II) \$100,000, and

- `(iv) which has--

- `(I) an estimated production period exceeding 4 months, and
- `(II) a cost exceeding \$200,000.'

(2) PLACED IN SERVICE DATE- Clause (iv) of section 168(k)(2)(A) is amended by striking `subparagraph (B)' and inserting `subparagraphs (B) and (C)'.

(b) CONFORMING AMENDMENTS-

(1) Section 168(k)(2)(B) is amended by adding at the end the following new clause:

` (iv) APPLICATION OF SUBPARAGRAPH- This subparagraph shall not apply to any property which is described in subparagraph (C).'

(2) Section 168(k)(4)(A)(ii) is amended by striking `paragraph (2)(C)' and inserting `paragraph (2)(D)'.

(3) Section 168(k)(4)(B)(iii) is amended by inserting `and paragraph (2)(C)' after `of this paragraph)'.

(4) Section 168(k)(4)(C) is amended by striking `subparagraphs (B) and (D)' and inserting `subparagraphs (B), (C), and (E)'.

(5) Section 168(k)(4)(D) is amended by striking `Paragraph (2)(E)' and inserting `Paragraph (2)(F)'.

(c) EFFECTIVE DATE- The amendments made by this section shall take effect as if included in the amendments made by section 101 of the Job Creation and Worker Assistance Act of 2002.

### **SEC. 337. MODIFICATION OF PLACED IN SERVICE RULE FOR BONUS DEPRECIATION PROPERTY.**

(a) IN GENERAL- Subclause (II) of section 168(k)(2)(E)(iii) (relating to syndication), as amended by the Working Families Tax Relief Act of 2004 and as redesignated by this Act, is amended by inserting before the comma at the end the following: `(or, in the case of multiple units of property subject to the same lease, within 3 months after the date the final unit is placed in service, so long as the period between the time the first unit is placed in service and the time the last unit is placed in service does not exceed 12 months)'.

(b) EFFECTIVE DATE- The amendment made by this section shall apply to property sold after June 4, 2004.

### **SEC. 338. EXPENSING OF CAPITAL COSTS INCURRED IN COMPLYING WITH ENVIRONMENTAL PROTECTION AGENCY SULFUR REGULATIONS.**

(a) IN GENERAL- Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by inserting after section 179A the following new section:

### **SEC. 179B. DEDUCTION FOR CAPITAL COSTS INCURRED IN COMPLYING WITH ENVIRONMENTAL PROTECTION AGENCY SULFUR REGULATIONS.**

^(a) ALLOWANCE OF DEDUCTION- In the case of a small business refiner (as defined in section 45H(c)(1)) which elects the application of this section, there shall be allowed as a deduction an amount equal to 75 percent of qualified capital costs (as defined in section 45H(c)(2)) which are paid or incurred by the taxpayer during the taxable year.

^(b) REDUCED PERCENTAGE- In the case of a small business refiner with average daily domestic refinery runs for the 1-year period ending on December 31, 2002, in excess of 155,000 barrels, the number of percentage points described in subsection (a) shall be reduced (not below zero) by the product of such number (before the application of this subsection) and the ratio of such excess to 50,000 barrels.

^(c) BASIS REDUCTION-

^(1) IN GENERAL- For purposes of this title, the basis of any property shall be reduced by the portion of the cost of such property taken into account under subsection (a).

^(2) ORDINARY INCOME RECAPTURE- For purposes of section 1245, the amount of the deduction allowable under subsection (a) with respect to any property which is of a character subject to the allowance for depreciation shall be treated as a deduction allowed for depreciation under section 167.'

^(d) COORDINATION WITH OTHER PROVISIONS- Section 280B shall not apply to amounts which are treated as expenses under this section.'

(b) CONFORMING AMENDMENTS-

(1) Section 263(a)(1), as amended by this Act, is amended by striking 'or' at the end of subparagraph (G), by striking the period at the end of subparagraph (H) and inserting ', or', and by adding at the end the following new subparagraph:

^(I) expenditures for which a deduction is allowed under section 179B.'

(2) Section 263A(c)(3) is amended by inserting '179B,' after 'section'.

(3) Section 312(k)(3)(B) is amended by striking 'or 179A' each place it appears in the heading and text and inserting '179A, or 179B'.

(4) Section 1016(a) is amended by striking 'and' at the end of paragraph (28), by striking the period at the end of paragraph (29) and inserting ', and', and by inserting after paragraph (29) the following new paragraph: '(30) to the extent provided in section 179B(c).'

(5) Paragraphs (2)(C) and (3)(C) of section 1245(a) are each amended by inserting '179B,' after '179A.'

(6) The table of sections for part VI of subchapter B of chapter 1, as amended by this Act, is amended by inserting after the item relating to section 179A the following new item:

^Sec. 179B. Deduction for capital costs incurred in complying with Environmental Protection Agency sulfur regulations.'

(c) EFFECTIVE DATE- The amendment made by this section shall apply to expenses paid or incurred after December 31, 2002, in taxable years ending after such date.

## **SEC. 339. CREDIT FOR PRODUCTION OF LOW SULFUR DIESEL FUEL.**

(a) IN GENERAL- Subpart D of part IV of subchapter A of chapter 1 (relating to business-related credits), as amended by this Act, is amended by inserting after section 45G the following new section:

## **SEC. 45H. CREDIT FOR PRODUCTION OF LOW SULFUR DIESEL FUEL.**

(a) IN GENERAL- For purposes of section 38, the amount of the low sulfur diesel fuel production credit determined under this section with respect to any facility of a small business refiner is an amount equal to 5 cents for each gallon of low sulfur diesel fuel produced during the taxable year by such small business refiner at such facility.

(b) MAXIMUM CREDIT-

(1) IN GENERAL- The aggregate credit determined under subsection (a) for any taxable year with respect to any facility shall not exceed--

(A) 25 percent of the qualified capital costs incurred by the small business refiner with respect to such facility, reduced by

(B) the aggregate credits determined under this section for all prior taxable years with respect to such facility.

(2) REDUCED PERCENTAGE- In the case of a small business refiner with average daily domestic refinery runs for the 1-year period ending on December 31, 2002, in excess of 155,000 barrels, the number of percentage points described in paragraph (1) shall be reduced (not below zero) by the product of such number (before the application of this paragraph) and the ratio of such excess to 50,000 barrels.

(c) DEFINITIONS AND SPECIAL RULE- For purposes of this section-

(1) SMALL BUSINESS REFINER- The term 'small business refiner' means, with respect to any taxable year, a refiner of crude oil--

(A) with respect to which not more than 1,500 individuals are engaged in the refinery operations of the business on any day during such taxable year, and

(B) the average daily domestic refinery run or average retained production of which for all facilities of the taxpayer for the 1-year period ending on December 31, 2002, did not exceed 205,000 barrels.

(2) QUALIFIED CAPITAL COSTS- The term 'qualified capital costs' means, with respect to any facility, those costs paid or incurred during the applicable period for compliance with the applicable EPA regulations with respect to such facility, including expenditures for the construction of new

process operation units or the dismantling and reconstruction of existing process units to be used in the production of low sulfur diesel fuel, associated adjacent or offsite equipment (including tankage, catalyst, and power supply), engineering, construction period interest, and sitework.

^(3) APPLICABLE EPA REGULATIONS- The term `applicable EPA regulations' means the Highway Diesel Fuel Sulfur Control Requirements of the Environmental Protection Agency.

^(4) APPLICABLE PERIOD- The term `applicable period' means, with respect to any facility, the period beginning on January 1, 2003, and ending on the earlier of the date which is 1 year after the date on which the taxpayer must comply with the applicable EPA regulations with respect to such facility or December 31, 2009.

^(5) LOW SULFUR DIESEL FUEL- The term `low sulfur diesel fuel' means diesel fuel with a sulfur content of 15 parts per million or less.

^(d) REDUCTION IN BASIS- For purposes of this subtitle, if a credit is determined under this section for any expenditure with respect to any property, the increase in basis of such property which would (but for this subsection) result from such expenditure shall be reduced by the amount of the credit so determined.

^(e) SPECIAL RULE FOR DETERMINATION OF REFINERY RUNS- For purposes this section and section 179B(b), in the calculation of average daily domestic refinery run or retained production, only refineries which on April 1, 2003, were refineries of the refiner or a related person (within the meaning of section 613A(d)(3)), shall be taken into account.

^(f) Certification-

^(1) REQUIRED- No credit shall be allowed unless, not later than the date which is 30 months after the first day of the first taxable year in which the low sulfur diesel fuel production credit is determined with respect to a facility, the small business refiner obtains certification from the Secretary, after consultation with the Administrator of the Environmental Protection Agency, that the taxpayer's qualified capital costs with respect to such facility will result in compliance with the applicable EPA regulations.

^(2) CONTENTS OF APPLICATION- An application for certification shall include relevant information regarding unit capacities and operating characteristics sufficient for the Secretary, after consultation with the Administrator of the Environmental Protection Agency, to determine that such qualified capital costs are necessary for compliance with the applicable EPA regulations.

^(3) REVIEW PERIOD- Any application shall be reviewed and notice of certification, if applicable, shall be made within 60 days of receipt of such application. In the event the Secretary does not notify the taxpayer of the results of such certification within such period, the taxpayer may presume the certification to be issued until so notified.

^(4) STATUTE OF LIMITATIONS- With respect to the credit allowed under this section--

^(A) the statutory period for the assessment of any deficiency attributable to such credit shall not expire before the end of the 3-

year period ending on the date that the review period described in paragraph (3) ends with respect to the taxpayer, and

``(B) such deficiency may be assessed before the expiration of such 3-year period notwithstanding the provisions of any other law or rule of law which would otherwise prevent such assessment.

``(g) COOPERATIVE ORGANIZATIONS-

``(1) APPORTIONMENT OF CREDIT-

``(A) IN GENERAL- In the case of a cooperative organization described in section 1381(a), any portion of the credit determined under subsection (a) for the taxable year may, at the election of the organization, be apportioned among patrons eligible to share in patronage dividends on the basis of the quantity or value of business done with or for such patrons for the taxable year.

``(B) FORM AND EFFECT OF ELECTION- An election under subparagraph (A) for any taxable year shall be made on a timely filed return for such year. Such election, once made, shall be irrevocable for such taxable year.

``(2) TREATMENT OF ORGANIZATIONS AND PATRONS-

``(A) ORGANIZATIONS- The amount of the credit not apportioned to patrons pursuant to paragraph (1) shall be included in the amount determined under subsection (a) for the taxable year of the organization.

``(B) PATRONS- The amount of the credit apportioned to patrons pursuant to paragraph (1) shall be included in the amount determined under subsection (a) for the first taxable year of each patron ending on or after the last day of the payment period (as defined in section 1382(d)) for the taxable year of the organization or, if earlier, for the taxable year of each patron ending on or after the date on which the patron receives notice from the cooperative of the apportionment.

``(3) SPECIAL RULE- If the amount of a credit which has been apportioned to any patron under this subsection is decreased for any reason--

``(A) such amount shall not increase the tax imposed on such patron, and

``(B) the tax imposed by this chapter on such organization shall be increased by such amount.

The increase under subparagraph (B) shall not be treated as tax imposed by this chapter for purposes of determining the amount of any credit under this chapter or for purposes of section 55.'

(b) CREDIT MADE PART OF GENERAL BUSINESS CREDIT- Subsection (b) of section 38 (relating to general business credit), as amended by this Act, is amended by striking ``plus' at the end of paragraph (16), by striking the period at the end of paragraph (17) and inserting ``, plus', and by inserting after paragraph (17) the following new paragraph:

`(18) the low sulfur diesel fuel production credit determined under section 45H(a).`.

(c) DENIAL OF DOUBLE BENEFIT- Section 280C (relating to certain expenses for which credits are allowable) is amended by adding at the end the following new subsection:

`(d) LOW SULFUR DIESEL FUEL PRODUCTION CREDIT- No deduction shall be allowed for that portion of the expenses otherwise allowable as a deduction for the taxable year which is equal to the amount of the credit determined for the taxable year under section 45H(a).`.

(d) BASIS ADJUSTMENT- Section 1016(a) (relating to adjustments to basis), as amended by this Act, is amended by striking `and` at the end of paragraph (29), by striking the period at the end of paragraph (30) and inserting ` , and`, and by inserting after paragraph (30) the following new paragraph:

`(31) in the case of a facility with respect to which a credit was allowed under section 45H, to the extent provided in section 45H(d).`.

(e) DEDUCTION FOR CERTAIN UNUSED BUSINESS CREDITS- Section 196(c) (defining qualified business credits), as amended by this Act, is amended by striking `and` at the end of paragraph (10), by striking the period at the end of paragraph (11) and inserting ` , and`, and by adding after paragraph (11) the following new paragraph:

`(12) the low sulfur diesel fuel production credit determined under section 45H(a).`.

(e) CLERICAL AMENDMENT- The table of sections for subpart D of part IV of subchapter A of chapter 1, as amended by this Act, is amended by inserting after the item relating to section 45G the following new item:

`Sec. 45H. Credit for production of low sulfur diesel fuel.`.

(f) EFFECTIVE DATE- The amendments made by this section shall apply to expenses paid or incurred after December 31, 2002, in taxable years ending after such date.

## **SEC. 340. EXPANSION OF QUALIFIED SMALL-ISSUE BOND PROGRAM.**

(a) IN GENERAL- Section 144(a)(4) (relating to \$10,000,000 limit in certain cases) is amended by adding at the end the following new subparagraph:

`(G) ADDITIONAL CAPITAL EXPENDITURES NOT TAKEN INTO ACCOUNT- With respect to bonds issued after September 30, 2009, in addition to any capital expenditure described in subparagraph (C), capital expenditures of not to exceed \$10,000,000 shall not be taken into account for purposes of applying subparagraph (A)(ii).`.

(b) CONFORMING AMENDMENT- Subparagraph (F) of section 144(a)(4) is amended by adding at the end the following new sentence: `This subparagraph shall not apply to bonds issued after September 30, 2009.`.

## **SEC. 341. OIL AND GAS FROM MARGINAL WELLS.**

(a) IN GENERAL- Subpart D of part IV of subchapter A of chapter 1 (relating to business credits), as amended by this Act, is amended by inserting after section 45H the following:

## **SEC. 45I. CREDIT FOR PRODUCING OIL AND GAS FROM MARGINAL WELLS.**

(a) GENERAL RULE- For purposes of section 38, the marginal well production credit for any taxable year is an amount equal to the product of-

- ` (1) the credit amount, and
- ` (2) the qualified credit oil production and the qualified natural gas production which is attributable to the taxpayer.

(b) CREDIT AMOUNT- For purposes of this section--

` (1) IN GENERAL- The credit amount is--

- ` (A) \$3 per barrel of qualified crude oil production, and
- ` (B) 50 cents per 1,000 cubic feet of qualified natural gas production.

` (2) REDUCTION AS OIL AND GAS PRICES INCREASE-

` (A) IN GENERAL- The \$3 and 50 cents amounts under paragraph (1) shall each be reduced (but not below zero) by an amount which bears the same ratio to such amount (determined without regard to this paragraph) as--

- ` (i) the excess (if any) of the applicable reference price over \$15 (\$1.67 for qualified natural gas production), bears to
- ` (ii) \$3 (\$0.33 for qualified natural gas production).

The applicable reference price for a taxable year is the reference price of the calendar year preceding the calendar year in which the taxable year begins.

` (B) INFLATION ADJUSTMENT- In the case of any taxable year beginning in a calendar year after 2005, each of the dollar amounts contained in subparagraph (A) shall be increased to an amount equal to such dollar amount multiplied by the inflation adjustment factor for such calendar year (determined under section 43(b)(3)(B) by substituting `2004' for `1990').

` (C) REFERENCE PRICE- For purposes of this paragraph, the term `reference price' means, with respect to any calendar year--

- ` (i) in the case of qualified crude oil production, the reference price determined under section 29(d)(2)(C), and
- ` (ii) in the case of qualified natural gas production, the Secretary's estimate of the annual average wellhead price per 1,000 cubic feet for all domestic natural gas.

(c) QUALIFIED CRUDE OIL AND NATURAL GAS PRODUCTION- For purposes of this section--

``(1) IN GENERAL- The terms `qualified crude oil production' and `qualified natural gas production' mean domestic crude oil or natural gas which is produced from a qualified marginal well.

``(2) Limitation on amount of production which may qualify-

``(A) IN GENERAL- Crude oil or natural gas produced during any taxable year from any well shall not be treated as qualified crude oil production or qualified natural gas production to the extent production from the well during the taxable year exceeds 1,095 barrels or barrel-of-oil equivalents (as defined in section 29(d)(5)).

``(B) Proportionate reductions-

``(i) SHORT TAXABLE YEARS- In the case of a short taxable year, the limitations under this paragraph shall be proportionately reduced to reflect the ratio which the number of days in such taxable year bears to 365.

``(ii) WELLS NOT IN PRODUCTION ENTIRE YEAR- In the case of a well which is not capable of production during each day of a taxable year, the limitations under this paragraph applicable to the well shall be proportionately reduced to reflect the ratio which the number of days of production bears to the total number of days in the taxable year.

``(3) Definitions-

``(A) QUALIFIED MARGINAL WELL- The term `qualified marginal well' means a domestic well--

``(i) the production from which during the taxable year is treated as marginal production under section 613A(c)(6), or

``(ii) which, during the taxable year--

``(I) has average daily production of not more than 25 barrel-of-oil equivalents (as so defined), and

``(II) produces water at a rate not less than 95 percent of total well effluent.

``(B) CRUDE OIL, ETC- The terms `crude oil', `natural gas', `domestic', and `barrel' have the meanings given such terms by section 613A(e).

``(d) Other Rules-

``(1) PRODUCTION ATTRIBUTABLE TO THE TAXPAYER- In the case of a qualified marginal well in which there is more than one owner of operating interests in the well and the crude oil or natural gas production exceeds the limitation under subsection (c)(2), qualifying crude oil production or qualifying natural gas production attributable to the taxpayer shall be determined on the basis of the ratio which taxpayer's revenue interest in the production bears to the aggregate of the revenue interests of all operating interest owners in the production.

``(2) OPERATING INTEREST REQUIRED- Any credit under this section may be claimed only on production which is attributable to the holder of an operating interest.

`(3) PRODUCTION FROM NONCONVENTIONAL SOURCES

EXCLUDED- In the case of production from a qualified marginal well which is eligible for the credit allowed under section 29 for the taxable year, no credit shall be allowable under this section unless the taxpayer elects not to claim the credit under section 29 with respect to the well.'.

(b) CREDIT TREATED AS BUSINESS CREDIT- Section 38(b), as amended by this Act, is amended by striking `plus' at the end of paragraph (17), by striking the period at the end of paragraph (18) and inserting `, plus', and by inserting after paragraph (18) the following:

`(19) the marginal oil and gas well production credit determined under section 45I(a).'.

(c) CARRYBACK- Subsection (a) of section 39 (relating to carryback and carryforward of unused credits generally) is amended by adding at the end the following:

`(3) 5- YEAR CARRYBACK FOR MARGINAL OIL AND GAS WELL PRODUCTION CREDIT- Notwithstanding subsection (d), in the case of the marginal oil and gas well production credit--

`(A) this section shall be applied separately from the business credit (other than the marginal oil and gas well production credit),

`(B) paragraph (1) shall be applied by substituting `5 taxable years' for `1 taxable years' in subparagraph (A) thereof, and

`(C) paragraph (2) shall be applied--

`(i) by substituting `25 taxable years' for `21 taxable years' in subparagraph (A) thereof, and

`(ii) by substituting `24 taxable years' for `20 taxable years' in subparagraph (B) thereof.'

(d) CLERICAL AMENDMENT- The table of sections for subpart D of part IV of subchapter A of chapter 1, as amended by this Act, is amended by inserting after section 45H the following:

`Sec. 45I. Credit for producing oil and gas from marginal wells.'

(e) EFFECTIVE DATE- The amendments made by this section shall apply to production in taxable years beginning after December 31, 2004.

**TITLE IV--TAX REFORM AND SIMPLIFICATION FOR UNITED STATES BUSINESSES**

**SEC. 401. INTEREST EXPENSE ALLOCATION RULES.**

(a) ELECTION TO ALLOCATE ON WORLDWIDE BASIS- Section 864 is amended by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) the following new subsection:

`(f) ELECTION TO ALLOCATE INTEREST, ETC. ON WORLDWIDE BASIS- For purposes of this subchapter, at the election of the worldwide affiliated group--

**^(1) ALLOCATION AND APPORTIONMENT OF INTEREST EXPENSE-**

^(A) IN GENERAL- The taxable income of each domestic corporation which is a member of a worldwide affiliated group shall be determined by allocating and apportioning interest expense of each member as if all members of such group were a single corporation.

^(B) TREATMENT OF WORLDWIDE AFFILIATED GROUP-

The taxable income of the domestic members of a worldwide affiliated group from sources outside the United States shall be determined by allocating and apportioning the interest expense of such domestic members to such income in an amount equal to the excess (if any) of-

^(i) the total interest expense of the worldwide affiliated group multiplied by the ratio which the foreign assets of the worldwide affiliated group bears to all the assets of the worldwide affiliated group, over

^(ii) the interest expense of all foreign corporations which are members of the worldwide affiliated group to the extent such interest expense of such foreign corporations would have been allocated and apportioned to foreign source income if this subsection were applied to a group consisting of all the foreign corporations in such worldwide affiliated group.

^(C) WORLDWIDE AFFILIATED GROUP- For purposes of this paragraph, the term 'worldwide affiliated group' means a group consisting of-

^(i) the includible members of an affiliated group (as defined in section 1504(a), determined without regard to paragraphs (2) and (4) of section 1504(b)), and

^(ii) all controlled foreign corporations in which such members in the aggregate meet the ownership requirements of section 1504(a)(2) either directly or indirectly through applying paragraph (2) of section 958(a) or through applying rules similar to the rules of such paragraph to stock owned directly or indirectly by domestic partnerships, trusts, or estates.

**^(2) ALLOCATION AND APPORTIONMENT OF OTHER EXPENSES-** Expenses other than interest which are not directly allocable or

apportioned to any specific income producing activity shall be allocated and apportioned as if all members of the affiliated 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 a 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 AND FINANCIAL 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 (12 U.S.C. 1841(a)),

^(ii) a financial holding company (within the meaning of section 2(p) of the Bank Holding Company Act of 1956 (12 U.S.C. 1841(p))), and

^(iii) any subsidiary of a financial institution described in section 581 or 591, or of any such bank or financial 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-**

^(A) IN GENERAL- If a worldwide affiliated group elects the application of this subsection, all financial corporations which-

^(i) are members of such worldwide affiliated group, but

^(ii) are not corporations described in paragraph (4)(B), shall be treated as described in paragraph (4)(B) for purposes of applying paragraph (4)(A). This subsection (other than this paragraph) shall apply to any such group in the same manner as this subsection (other than this paragraph) applies to the pre-election worldwide affiliated group of which such group is a part.

``(B) FINANCIAL CORPORATION- For purposes of this paragraph, the term `financial corporation' means any corporation if at least 80 percent of its gross income is income described in section 904(d)(2)(D)(ii) and the regulations thereunder which is derived from transactions with persons who are not related (within the meaning of section 267(b) or 707(b)(1)) to the corporation. For purposes of the preceding sentence, there shall be disregarded any item of income or gain from a transaction or series of transactions a principal purpose of which is the qualification of any corporation as a financial corporation.

``(C) ANTI-ABUSE RULES- In the case of a corporation which is a member of an electing financial institution group, to the extent that such corporation--

``(i) distributes dividends or makes other distributions with respect to its stock after the date of the enactment of this paragraph to any member of the pre-election worldwide affiliated group (other than to a member of the electing financial institution group) in excess of the greater of--

``(I) its average annual dividend (expressed as a percentage of current earnings and profits) during the 5-taxable-year period ending with the taxable year preceding the taxable year, or

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

``(ii) deals with any person in any manner not clearly reflecting the income of the corporation (as determined under principles similar to the principles of section 482),

an amount of indebtedness of the electing financial institution group equal to the excess distribution or the understatement or overstatement of income, as the case may be, shall be recharacterized (for the taxable year and subsequent taxable years) for purposes of this paragraph as indebtedness of the worldwide affiliated group (excluding the electing financial institution group). If a corporation has not been in existence for 5 taxable years, this subparagraph shall be applied with respect to the period it was in existence.

``(D) ELECTION- An election under this paragraph with respect to any financial institution group may be made only by the common parent of the pre-election worldwide affiliated group and may be made only for the first taxable year beginning after December 31, 2008, in which such affiliated group includes 1 or more financial corporations. Such an election, once made, shall apply to all financial corporations which are members of the electing financial institution group for such taxable year and all subsequent years unless revoked with the consent of the Secretary.

^(E) DEFINITIONS RELATING TO GROUPS- For purposes of this paragraph--

^(i) PRE-ELECTION WORLDWIDE AFFILIATED GROUP- The term `pre-election worldwide affiliated group' means, with respect to a corporation, the worldwide affiliated group of which such corporation would (but for an election under this paragraph) be a member for purposes of applying paragraph (1).

^(ii) ELECTING FINANCIAL INSTITUTION GROUP- The term `electing financial institution group' means the group of corporations to which this subsection applies separately by reason of the application of paragraph (4)(A) and which includes financial corporations by reason of an election under subparagraph (A).

^(F) REGULATIONS- The Secretary shall prescribe such regulations as may be appropriate to carry out this subsection, including regulations--

^(i) providing for the direct allocation of interest expense in other circumstances where such allocation would be appropriate to carry out the purposes of this subsection,

^(ii) preventing assets or interest expense from being taken into account more than once, and

^(iii) dealing with changes in members of any group (through acquisitions or otherwise) treated under this paragraph as an affiliated group for purposes of this subsection.

^(6) ELECTION- An election to have this subsection apply with respect to any worldwide affiliated group may be made only by the common parent of the domestic affiliated group referred to in paragraph (1)(C) and may be made only for the first taxable year beginning after December 31, 2008, in which a worldwide affiliated group exists which includes such affiliated group and at least 1 foreign corporation. Such an election, once made, shall apply to such common parent and all other corporations which are members of such worldwide affiliated group for such taxable year and all subsequent years unless revoked with the consent of the Secretary.'

(b) EXPANSION OF REGULATORY AUTHORITY- Paragraph (7) of section 864(e) is amended--

(1) by inserting before the comma at the end of subparagraph (B) `and in other circumstances where such allocation would be appropriate to carry out the purposes of this subsection', and

(2) by striking `and' at the end of subparagraph (E), by redesignating subparagraph (F) as subparagraph (G), and by inserting after subparagraph (E) the following new subparagraph:

^(F) preventing assets or interest expense from being taken into account more than once, and'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years beginning after December 31, 2008.

## **SEC. 402. RECHARACTERIZATION OF OVERALL DOMESTIC LOSS.**

(a) GENERAL RULE- Section 904 is amended by redesignating subsections (g), (h), (i), (j), and (k) as subsections (h), (i), (j), (k), and (l) respectively, and by inserting after subsection (f) the following new subsection:

**^(g) RECHARACTERIZATION OF OVERALL DOMESTIC LOSS-**

^(1) GENERAL RULE- For purposes of this subpart and section 936, in the case of any taxpayer who sustains an overall domestic loss for any taxable year beginning after December 31, 2006, that portion of the taxpayer's taxable income from sources within the United States for each succeeding taxable year which is equal to the lesser of-

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

^(B) 50 percent of the taxpayer's taxable income from sources within the United States for such succeeding taxable year,

shall be treated as income from sources without the United States (and not as income from sources within the United States).

^(2) OVERALL DOMESTIC LOSS DEFINED- For purposes of this subsection-

^(A) IN GENERAL- The term 'overall domestic loss' means any domestic loss to the extent such loss offsets taxable income from sources without the United States for the taxable year or for any preceding taxable year by reason of a carryback. For purposes of the preceding sentence, the term 'domestic loss' means the amount by which the gross income for the taxable year from sources within the United States is exceeded by the sum of the deductions properly apportioned or allocated thereto (determined without regard to any carryback from a subsequent taxable year).

^(B) TAXPAYER MUST HAVE ELECTED FOREIGN TAX CREDIT FOR YEAR OF LOSS- The term 'overall domestic loss' shall not include any loss for any taxable year unless the taxpayer chose the benefits of this subpart for such taxable year.

^(3) CHARACTERIZATION OF SUBSEQUENT INCOME-

^(A) IN GENERAL- Any income from sources within the United States that is treated as income from sources without the United States under paragraph (1) shall be allocated among and increase the income categories in proportion to the loss from sources within the United States previously allocated to those income categories.

^(B) INCOME CATEGORY- For purposes of this paragraph, the term 'income category' has the meaning given such term by subsection (f)(5)(E)(i).

``(4) COORDINATION WITH SUBSECTION (f)- The Secretary shall prescribe such regulations as may be necessary to coordinate the provisions of this subsection with the provisions of subsection (f).''.

(b) CONFORMING AMENDMENTS-

- (1) Section 535(d)(2) is amended by striking `section 904(g)(6)' and inserting `section 904(h)(6)'.
- (2) Subparagraph (A) of section 936(a)(2) is amended by striking `section 904(f)' and inserting `subsections (f) and (g) of section 904'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to losses for taxable years beginning after December 31, 2006.

## **SEC. 403. LOOK-THRU RULES TO APPLY TO DIVIDENDS FROM NONCONTROLLED SECTION 902 CORPORATIONS.**

(a) IN GENERAL- Section 904(d)(4) (relating to look-thru rules apply to dividends from noncontrolled section 902 corporations) is amended to read as follows:

``(4) LOOK-THRU APPLIES TO DIVIDENDS FROM NONCONTROLLED SECTION 902 CORPORATIONS-

``(A) IN GENERAL- For purposes of this subsection, any dividend from a noncontrolled section 902 corporation with respect to the taxpayer shall be treated as income described in a subparagraph of paragraph (1) in proportion to the ratio of-

- (i) the portion of earnings and profits attributable to income described in such subparagraph, to
- (ii) the total amount of earnings and profits.

``(B) EARNINGS AND PROFITS OF CONTROLLED FOREIGN CORPORATIONS- In the case of any distribution from a controlled foreign corporation to a United States shareholder, rules similar to the rules of subparagraph (A) shall apply in determining the extent to which earnings and profits of the controlled foreign corporation which are attributable to dividends received from a noncontrolled section 902 corporation may be treated as income in a separate category.

``(C) SPECIAL RULES- For purposes of this paragraph-

``(i) EARNINGS AND PROFITS-

``(I) IN GENERAL- The rules of section 316 shall apply.

``(II) REGULATIONS- The Secretary may prescribe regulations regarding the treatment of distributions out of earnings and profits for periods before the taxpayer's acquisition of the stock to which the distributions relate.

``(ii) INADEQUATE SUBSTANTIATION- If the Secretary determines that the proper subparagraph of paragraph (1) in which a dividend is described has not been substantiated,

such dividend shall be treated as income described in paragraph (1)(A).

``(iii) COORDINATION WITH HIGH-TAXED INCOME PROVISIONS- Rules similar to the rules of paragraph (3)(F) shall apply for purposes of this paragraph.

``(iv) LOOK-THRU WITH RESPECT TO CARRYOVER OF CREDIT- Rules similar to subparagraph (A) also shall apply to any carryforward under subsection (c) from a taxable year beginning before January 1, 2003, of tax allocable to a dividend from a noncontrolled section 902 corporation with respect to the taxpayer. The Secretary may by regulations provide for the allocation of any carryback of tax allocable to a dividend from a noncontrolled section 902 corporation from a taxable year beginning on or after January 1, 2003, to a taxable year beginning before such date for purposes of allocating such dividend among the separate categories in effect for the taxable year to which carried.'.

(b) CONFORMING AMENDMENTS-

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

(2) Section 904(d)(2)(C)(iii) is amended by adding `and' at the end of subclause (I), by striking subclause (II), and by redesignating subclause (III) as subclause (II).

(3) The last sentence of section 904(d)(2)(D) is amended to read as follows: `Such term does not include any financial services income.'

(4) Section 904(d)(2)(E) is amended--

(A) by inserting `or (4)' after `paragraph (3)' in clause (i), and

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

(5) Section 904(d)(3)(F) is amended by striking `(D), or (E)' and inserting `or (D)'.

(6) Section 864(d)(5)(A)(i) is amended by striking `(C)(iii)(III)' and inserting `(C)(iii)(II)'.

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

## **SEC. 404. REDUCTION TO 2 FOREIGN TAX CREDIT BASKETS.**

(a) IN GENERAL- Paragraph (1) of section 904(d) (relating to separate application of section with respect to certain categories of income) is amended to read as follows:

``(1) IN GENERAL- The provisions of subsections (a), (b), and (c) and sections 902, 907, and 960 shall be applied separately with respect to--

``(A) passive category income, and

``(B) general category income.'

(b) CATEGORIES- Paragraph (2) of section 904(d) is amended by striking subparagraph (B), by redesignating subparagraph (A) as subparagraph (B), and by inserting before subparagraph (B) (as so redesignated) the following new subparagraph:

^(A) CATEGORIES-

^(i) PASSIVE CATEGORY INCOME- The term `passive category income' means passive income and specified passive category income.

^(ii) GENERAL CATEGORY INCOME- The term `general category income' means income other than passive category income.'

(c) SPECIFIED PASSIVE CATEGORY INCOME- Subparagraph (B) of section 904(d)(2), as so redesignated, is amended by adding at the end the following new clause:

^(v) SPECIFIED PASSIVE CATEGORY INCOME- The term `specified passive category income' means--

^(I) dividends from a DISC or former DISC (as defined in section 992(a)) to the extent such dividends are treated as income from sources without the United States,

^(II) taxable income attributable to foreign trade income (within the meaning of section 923(b)), and

^(III) distributions from a FSC (or a former FSC) out of earnings and profits attributable to foreign trade income (within the meaning of section 923(b)) or interest or carrying charges (as defined in section 927(d)(1)) derived from a transaction which results in foreign trade income (as defined in section 923(b)).'

(d) TREATMENT OF FINANCIAL SERVICES- Paragraph (2) of section 904(d), as amended by section 403(b)(3), is amended by striking subparagraph (D), by redesignating subparagraph (C) as subparagraph (D), and by inserting before subparagraph (D) (as so redesignated) the following new subparagraph:

^(C) TREATMENT OF FINANCIAL SERVICES INCOME AND COMPANIES-

^(i) IN GENERAL- Financial services income shall be treated as general category income in the case of-

^(I) a member of a financial services group, and

^(II) any other person if such person is predominantly engaged in the active conduct of a banking, insurance, financing, or similar business.

^(ii) FINANCIAL SERVICES GROUP- The term

`financial services group' means any affiliated group (as defined in section 1504(a) without regard to paragraphs (2) and (3) of section 1504(b)) which is predominantly engaged in the active conduct of a banking, insurance,

financing, or similar business. In determining whether such a group is so engaged, there shall be taken into account only the income of members of the group that are--

``(I) United States corporations, or  
``(II) controlled foreign corporations in which such United States corporations own, directly or indirectly, at least 80 percent of the total voting power and value of the stock.

``(iii) PASS-THRU ENTITIES- The Secretary shall by regulation specify for purposes of this subparagraph the treatment of financial services income received or accrued by partnerships and by other pass-thru entities which are not members of a financial services group.'

(e) TREATMENT OF INCOME TAX BASE DIFFERENCES- Paragraph (2) of section 904(d) is amended by redesignating subparagraphs (H) and (I) as subparagraphs (I) and (J), respectively, and by inserting after subparagraph (G) the following new subparagraph:

``(H) TREATMENT OF INCOME TAX BASE DIFFERENCES-

``(i) IN GENERAL- In the case of taxable years beginning after December 31, 2006, 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).

``(ii) SPECIAL RULE FOR YEARS BEFORE 2007-

``(I) IN GENERAL- In the case of taxes paid or accrued in taxable years beginning after December 31, 2004, and before January 1, 2007, a taxpayer may elect to treat 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 as tax imposed on income described in subparagraph (C) or (I) of paragraph (1).

``(II) ELECTION IRREVOCABLE- Any such election shall apply to the taxable year for which made and all subsequent taxable years described in subclause (I) unless revoked with the consent of the Secretary.'

(f) CONFORMING AMENDMENTS-

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

(2) Clause (i) of section 904(d)(2)(D) (defining financial services income), as so redesignated, is amended by adding `or' at the end of subclause (I)

and by striking subclauses (II) and (III) and inserting the following new subclause:

``(II) passive income (determined without regard to subparagraph (B)(iii)(II)).'.

(3) Section 904(d)(2)(D) (defining financial services income), as so redesignated and amended by section 404(b)(3), is amended by striking clause (iii).

(4) Paragraph (3) of section 904(d) is amended to read as follows:

**``(3) LOOK-THRU IN CASE OF CONTROLLED FOREIGN CORPORATIONS-**

``(A) IN GENERAL- Except as otherwise provided in this paragraph, dividends, interest, rents, and royalties received or accrued by the taxpayer from a controlled foreign corporation in which the taxpayer is a United States shareholder shall not be treated as passive category income.

``(B) SUBPART F INCLUSIONS- Any amount included in gross income under section 951(a)(1)(A) shall be treated as passive category income to the extent the amount so included is attributable to passive category income.

``(C) INTEREST, RENTS, AND ROYALTIES- Any interest, rent, or royalty which is received or accrued from a controlled foreign corporation in which the taxpayer is a United States shareholder shall be treated as passive category income to the extent it is properly allocable (under regulations prescribed by the Secretary) to passive category income of the controlled foreign corporation.

``(D) DIVIDENDS- Any dividend paid out of the earnings and profits of any controlled foreign corporation in which the taxpayer is a United States shareholder shall be treated as passive category income in proportion to the ratio of-

``(i) the portion of the earnings and profits attributable to passive category income, to

``(ii) the total amount of earnings and profits.

``(E) LOOK-THRU APPLIES ONLY WHERE SUBPART F APPLIES- If a controlled foreign corporation meets the requirements of section 954(b)(3)(A) (relating to de minimis rule) for any taxable year, for purposes of this paragraph, none of its foreign base company income (as defined in section 954(a) without regard to section 954(b)(5)) and none of its gross insurance income (as defined in section 954(b)(3)(C)) for such taxable year shall be treated as passive category income, except that this sentence shall not apply to any income which (without regard to this sentence) would be treated as financial services income. Solely for purposes of applying subparagraph (D), passive income of a controlled foreign corporation shall not be treated as passive category income if the requirements of section 954(b)(4) are met with respect to such income.

**^(F) COORDINATION WITH HIGH-TAXED INCOME PROVISIONS-**

- ^(i) In determining whether any income of a controlled foreign corporation is passive category income, subclause (II) of paragraph (2)(B)(iii) shall not apply.
- ^(ii) Any income of the taxpayer which is treated as passive category income under this paragraph shall be so treated notwithstanding any provision of paragraph (2); except that the determination of whether any amount is high-taxed income shall be made after the application of this paragraph.

**^(G) DIVIDEND-** For purposes of this paragraph, the term 'dividend' includes any amount included in gross income in section 951(a)(1)(B). Any amount included in gross income under section 78 to the extent attributable to amounts included in gross income in section 951(a)(1)(A) shall not be treated as a dividend but shall be treated as included in gross income under section 951(a)(1)(A).

**^(H) LOOK-THRU APPLIES TO PASSIVE FOREIGN INVESTMENT COMPANY INCLUSION- If-**

- ^(i) a passive foreign investment company is a controlled foreign corporation, and
- ^(ii) the taxpayer is a United States shareholder in such controlled foreign corporation,

any amount included in gross income under section 1293 shall be treated as income in a separate category to the extent such amount is attributable to income in such category.'

(5) Paragraph (2) of section 904(d) is amended by adding at the end the following new subparagraph:

**^(K) TRANSITIONAL RULES FOR 2007 CHANGES-** For purposes of paragraph (1)--

- ^(i) taxes carried from any taxable year beginning before January 1, 2007, 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 taxes paid or accrued in a taxable year beginning on or after such date, and
- ^(ii) the Secretary may by regulations provide for the allocation of any carryback of taxes with respect to income from a taxable year beginning on or after January 1, 2007, to a taxable year beginning before such date for purposes of allocating such income among the separate categories in effect for the taxable year to which carried.'

(6) Section 904(j)(3)(A)(i) is amended by striking 'subsection (d)(2)(A)' and inserting 'subsection (d)(2)(B)'.

**(g) EFFECTIVE DATES-**

(1) IN GENERAL- The amendments made by this section shall apply to taxable years beginning after December 31, 2006.

(2) TRANSITIONAL RULE RELATING TO INCOME TAX BASE DIFFERENCE- Section 904(d)(2)(H)(ii) of the Internal Revenue Code of 1986, as added by subsection (e), shall apply to taxable years beginning after December 31, 2004.

#### **SEC. 405. ATTRIBUTION OF STOCK OWNERSHIP THROUGH PARTNERSHIPS TO APPLY IN DETERMINING SECTION 902 AND 960 CREDITS.**

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

‘(7) CONSTRUCTIVE OWNERSHIP THROUGH PARTNERSHIPS- Stock owned, directly or indirectly, by or for a partnership shall be considered as being owned proportionately by its partners. Stock considered to be owned by a person by reason of the preceding sentence shall, for purposes of applying such sentence, be treated as actually owned by such person. The Secretary may prescribe such regulations as may be necessary to carry out the purposes of this paragraph, including rules to account for special partnership allocations of dividends, credits, and other incidents of ownership of stock in determining proportionate ownership.’.

(b) CLARIFICATION OF COMPARABLE ATTRIBUTION UNDER SECTION 901(b)(5)- Paragraph (5) of section 901(b) is amended by striking ‘any individual’ and inserting ‘any person’.

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

#### **SEC. 406. CLARIFICATION OF TREATMENT OF CERTAIN TRANSFERS OF INTANGIBLE PROPERTY.**

(a) IN GENERAL- Subparagraph (C) of section 367(d)(2) is amended by adding at the end the following new sentence: ‘For purposes of applying section 904(d), any such amount shall be treated in the same manner as if such amount were a royalty.’.

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

#### **SEC. 407. UNITED STATES PROPERTY NOT TO INCLUDE CERTAIN ASSETS OF CONTROLLED FOREIGN CORPORATION.**

(a) IN GENERAL- Section 956(c)(2) (relating to exceptions from property treated as United States property) is amended by striking `and' at the end of subparagraph (J), by striking the period at the end of subparagraph (K) and inserting a semicolon, and by adding at the end the following new subparagraphs:

`(L) securities acquired and held by a controlled foreign corporation in the ordinary course of its business as a dealer in securities if--

`(i) the dealer accounts for the securities as securities held primarily for sale to customers in the ordinary course of business, and

`(ii) the dealer disposes of the securities (or such securities mature while held by the dealer) within a period consistent with the holding of securities for sale to customers in the ordinary course of business; and

`(M) an obligation of a United States person which--

`(i) is not a domestic corporation, and

`(ii) is not--

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

`(II) a partnership, estate, or trust in which the controlled foreign corporation, or any related person (as defined in section 954(d)(3)), is a partner, beneficiary, or trustee immediately after the acquisition of any obligation of such partnership, estate, or trust by the controlled foreign corporation.'

(b) CONFORMING AMENDMENT- Section 956(c)(2) is amended by striking `and (K)' in the last sentence and inserting `, (K), and (L)'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years of foreign corporations beginning after December 31, 2004, and to taxable years of United States shareholders with or within which such taxable years of foreign corporations end.

## **SEC. 408. TRANSLATION OF FOREIGN TAXES.**

(a) ELECTIVE EXCEPTION FOR TAXES PAID OTHER THAN IN FUNCTIONAL CURRENCY- Paragraph (1) of section 986(a) (relating to determination of foreign taxes and foreign corporation's earnings and profits) is amended by redesignating subparagraph (D) as subparagraph (E) and by inserting after subparagraph (C) the following new subparagraph:

`(D) ELECTIVE EXCEPTION FOR TAXES PAID OTHER THAN IN FUNCTIONAL CURRENCY-

`(i) IN GENERAL- At the election of the taxpayer, subparagraph (A) shall not apply to any foreign income

taxes the liability for which is denominated in any currency other than in the taxpayer's functional currency.

``(ii) APPLICATION TO QUALIFIED BUSINESS

UNITS- An election under this subparagraph may apply to foreign income taxes attributable to a qualified business unit in accordance with regulations prescribed by the Secretary.

``(iii) ELECTION- Any such election shall apply to the taxable year for which made and all subsequent taxable years unless revoked with the consent of the Secretary.'

(b) SPECIAL RULE FOR REGULATED INVESTMENT COMPANIES-

(1) IN GENERAL- Section 986(a)(1), as amended by subsection (a), is amended by redesignating subparagraph (E) as subparagraph (F) and by inserting after subparagraph (D) the following:

``(E) SPECIAL RULE FOR REGULATED INVESTMENT COMPANIES- In the case of a regulated investment company which takes into account income on an accrual basis, subparagraphs (A) through (D) shall not apply and foreign income taxes paid or accrued with respect to such income shall be translated into dollars using the exchange rate as of the date the income accrues.'

(2) CONFORMING AMENDMENT- Section 986(a)(2) is amended by inserting `or (E)' after `subparagraph (A)'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years beginning after December 31, 2004.

## **SEC. 409. REPEAL OF WITHHOLDING TAX ON DIVIDENDS FROM CERTAIN FOREIGN CORPORATIONS.**

(a) IN GENERAL- Paragraph (2) of section 871(i) (relating to tax not to apply to certain interest and dividends) is amended by adding at the end the following new subparagraph:

``(D) Dividends paid by a foreign corporation which are treated under section 861(a)(2)(B) as income from sources within the United States.'

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

## **SEC. 410. EQUAL TREATMENT OF INTEREST PAID BY FOREIGN PARTNERSHIPS AND FOREIGN CORPORATIONS.**

(a) IN GENERAL- Paragraph (1) of section 861(a) is amended by striking `and' at the end of subparagraph (A), by striking the period at the end of subparagraph (B) and inserting `, and', and by adding at the end the following new subparagraph:

``(C) in the case of a foreign partnership, which is predominantly engaged in the active conduct of a trade or business outside the

United States, any interest not paid by a trade or business engaged in by the partnership in the United States and not allocable to income which is effectively connected (or treated as effectively connected) with the conduct of a trade or business in the United States.'

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

## **SEC. 411. TREATMENT OF CERTAIN DIVIDENDS OF REGULATED INVESTMENT COMPANIES.**

### **(a) TREATMENT OF CERTAIN DIVIDENDS-**

(1) NONRESIDENT ALIEN INDIVIDUALS- Section 871 (relating to tax on nonresident alien individuals) 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 investment company unless the person who would otherwise be required to deduct and withhold tax from such dividend under chapter 3 receives a statement (which meets requirements similar to the requirements of subsection (h)(5)) that the beneficial owner of such stock is not a United States person, and

`(iii) to any interest-related dividend paid to any person within a foreign country (or any interest-related dividend payment addressed to, or for the account of, persons within such foreign country) during any period described in subsection (h)(6) with respect to such country.

Clause (iii) shall not apply to any dividend with respect to any stock which was acquired on or before the date of the publication of the Secretary's determination under subsection (h)(6).

``(C) INTEREST-RELATED DIVIDEND- For purposes of this paragraph, the term `interest-related dividend' means any dividend (or part thereof) which is designated by the regulated investment company as an interest-related dividend in a written notice mailed to its shareholders not later than 60 days after the close of its taxable year. If the aggregate amount so designated with respect to a taxable year of the company (including amounts so designated with respect to dividends paid after the close of the taxable year described in section 855) is greater than the qualified net interest income of the company for such taxable year, the portion of each distribution which shall be an interest-related dividend shall be only that portion of the amounts so designated which such qualified net interest income bears to the aggregate amount so designated. Such term shall not include any dividend with respect to any taxable year of the company beginning after December 31, 2007.

``(D) QUALIFIED NET INTEREST INCOME- For purposes of subparagraph (C), the term `qualified net interest income' means the qualified interest income of the regulated investment company reduced by the deductions properly allocable to such income.

``(E) QUALIFIED INTEREST INCOME- For purposes of subparagraph (D), the term `qualified interest income' means the sum of the following amounts derived by the regulated investment company from sources within the United States:

``(i) Any amount includable in gross income as original issue discount (within the meaning of section 1273) on an obligation payable 183 days or less from the date of original issue (without regard to the period held by the company).

``(ii) Any interest includable in gross income (including amounts recognized as ordinary income in respect of original issue discount or market discount or acquisition discount under part V of subchapter P and such other amounts as regulations may provide) on an obligation which is in registered form; except that this clause shall not apply to--

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

``(II) any interest which is treated as not being portfolio interest under the rules of subsection (h)(4).

``(iii) Any interest referred to in subsection (i)(2)(A) (without regard to the trade or business of the regulated investment company).

^(iv) Any interest-related dividend includable in gross income with respect to stock of another regulated investment company.

^(F) 10-PERCENT SHAREHOLDER- For purposes of this paragraph, the term `10-percent shareholder' has the meaning given such term by subsection (h)(3)(B).

^(2) SHORT-TERM CAPITAL GAIN DIVIDENDS-

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

^(B) EXCEPTION FOR ALIENS TAXABLE UNDER SUBSECTION (a)(2)- Subparagraph (A) shall not apply in the case of any nonresident alien individual subject to tax under subsection (a)(2).

^(C) SHORT-TERM CAPITAL GAIN DIVIDEND- For purposes of this paragraph, the term `short-term capital gain dividend' means any dividend (or part thereof) which is designated by the regulated investment company as a short-term capital gain dividend in a written notice mailed to its shareholders not later than 60 days after the close of its taxable year. If the aggregate amount so designated with respect to a taxable year of the company (including amounts so designated with respect to dividends paid after the close of the taxable year described in section 855) is greater than the qualified short-term gain of the company for such taxable year, the portion of each distribution which shall be a short-term capital gain dividend shall be only that portion of the amounts so designated which such qualified short-term gain bears to the aggregate amount so designated. Such term shall not include any dividend with respect to any taxable year of the company beginning after December 31, 2007.

^(D) QUALIFIED SHORT-TERM GAIN- For purposes of subparagraph (C), the term `qualified short-term gain' means the excess of the net short-term capital gain of the regulated investment company for the taxable year over the net long-term capital loss (if any) of such company for such taxable year. For purposes of this subparagraph-

^(i) the net short-term capital gain of the regulated investment company shall be computed by treating any short-term capital gain dividend includable in gross income with respect to stock of another regulated investment company as a short-term capital gain, and

^(ii) the excess of the net short-term capital gain for a taxable year over the net long-term capital loss for a taxable year (to which an election under section 4982(e)(4) does not apply) shall be determined without regard to any net

capital loss or net short-term capital loss attributable to transactions after October 31 of such year, and any such net capital loss or net short-term capital loss shall be treated as arising on the 1st day of the next taxable year.

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

(2) FOREIGN CORPORATIONS- Section 881 (relating to tax on income of foreign corporations not connected with United States business) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

^(e) TAX NOT TO APPLY TO 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) of subsection (a) on any interest-related dividend (as defined in section 871(k)(1)) received from a regulated investment company.

^(B) EXCEPTION- Subparagraph (A) shall not apply--

^(i) to any dividend referred to in section 871(k)(1)(B), and  
^(ii) to any interest-related dividend received by a controlled foreign corporation (within the meaning of section 957(a)) to the extent such dividend is attributable to interest received by the regulated investment company from a person who is a related person (within the meaning of section 864(d)(4)) with respect to such controlled foreign corporation.

^(C) TREATMENT OF DIVIDENDS RECEIVED BY CONTROLLED FOREIGN CORPORATIONS- The rules of subsection (c)(5)(A) shall apply to any (within the meaning of section 957(a)) to the extent such dividend is attributable to interest received by the regulated investment company which is described in clause (ii) of section 871(k)(1)(E) (and not described in clause (i) or (iii) of such section).

^(2) SHORT-TERM CAPITAL GAIN DIVIDENDS- No tax shall be imposed under paragraph (1) of subsection (a) on any short-term capital gain dividend (as defined in section 871(k)(2)) received from a regulated investment company.'

(3) WITHHOLDING TAXES-

(A) Section 1441(c) (relating to exceptions) is amended by adding at the end the following new paragraph:

^(12) CERTAIN DIVIDENDS RECEIVED FROM REGULATED INVESTMENT COMPANIES-

^(A) IN GENERAL- No tax shall be required to be deducted and withheld under subsection (a) from any amount exempt from the tax imposed by section 871(a)(1)(A) by reason of section 871(k).

^(B) SPECIAL RULE- For purposes of subparagraph (A), clause (i) of section 871(k)(1)(B) shall not apply to any dividend unless the regulated investment company knows that such dividend is a dividend referred to in such clause. A similar rule shall apply with respect to the exception contained in section 871(k)(2)(B).'.

(B) Section 1442(a) (relating to withholding of tax on foreign corporations) is amended--

- (i) by striking `and the reference in section 1441(c)(10)' and inserting `the reference in section 1441(c)(10)', and
- (ii) by inserting before the period at the end the following: `, and the references in section 1441(c)(12) to sections 871(a) and 871(k) shall be treated as referring to sections 881(a) and 881(e) (except that for purposes of applying subparagraph (A) of section 1441(c)(12), as so modified, clause (ii) of section 881(e)(1)(B) shall not apply to any dividend unless the regulated investment company knows that such dividend is a dividend referred to in such clause)'.

(b) ESTATE TAX TREATMENT OF INTEREST IN CERTAIN REGULATED INVESTMENT COMPANIES- Section 2105 (relating to property without the United States for estate tax purposes) is amended by adding at the end the following new subsection:

^(d) STOCK IN A RIC-

^(1) IN GENERAL- For purposes of this subchapter, stock in a regulated investment company (as defined in section 851) owned by a nonresident not a citizen of the United States shall not be deemed property within the United States in the proportion that, at the end of the quarter of such investment company's taxable year immediately preceding a decedent's date of death (or at such other time as the Secretary may designate in regulations), the assets of the investment company that were qualifying assets with respect to the decedent bore to the total assets of the investment company.

^(2) QUALIFYING ASSETS- For purposes of this subsection, qualifying assets with respect to a decedent are assets that, if owned directly by the decedent, would have been-

- ^(A) amounts, deposits, or debt obligations described in subsection (b) of this section,
- ^(B) debt obligations described in the last sentence of section 2104(c), or
- ^(C) other property not within the United States.

^(3) TERMINATION- This subsection shall not apply to estates of decedents dying after December 31, 2007.'

(c) TREATMENT OF REGULATED INVESTMENT COMPANIES UNDER SECTION 897-

(1) Paragraph (1) of section 897(h) is amended by striking `REIT' each place it appears and inserting `qualified investment entity'.

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

‘(2) SALE OF STOCK IN DOMESTICALLY CONTROLLED ENTITY NOT TAXED- The term ‘United States real property interest’ does not include any interest in a domestically controlled qualified investment entity.

‘(3) DISTRIBUTIONS BY DOMESTICALLY CONTROLLED QUALIFIED INVESTMENT ENTITIES- In the case of a domestically controlled qualified investment entity, rules similar to the rules of subsection (d) shall apply to the foreign ownership percentage of any gain.’.

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

‘(A) QUALIFIED INVESTMENT ENTITY-

‘(i) IN GENERAL- The term ‘qualified investment entity’ means--

‘(I) any real estate investment trust, and

‘(II) any regulated investment company.

‘(ii) TERMINATION- Clause (i)(II) shall not apply after December 31, 2007.

‘(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 December 31, 2004.

(2) ESTATE TAX TREATMENT- The amendment made by subsection (b) shall apply to estates of decedents dying after December 31, 2004.

(3) CERTAIN OTHER PROVISIONS- The amendments made by subsection (c) (other than paragraph (1) thereof) shall take effect after December 31, 2004.

## **SEC. 412. LOOK-THRU TREATMENT FOR SALES OF PARTNERSHIP INTERESTS.**

(a) IN GENERAL- Section 954(c) (defining foreign personal holding company income) is amended by adding after paragraph (3) the following new paragraph:

‘(4) LOOK-THRU RULE FOR CERTAIN PARTNERSHIP SALES-

`(A) IN GENERAL- In the case of any sale by a controlled foreign corporation of an interest in a partnership with respect to which such corporation is a 25-percent owner, such corporation shall be treated for purposes of this subsection as selling the proportionate share of the assets of the partnership attributable to such interest. The Secretary shall prescribe such regulations as may be appropriate to prevent abuse of the purposes of this paragraph, including regulations providing for coordination of this paragraph with the provisions of subchapter K.

`(B) 25-PERCENT OWNER- For purposes of this paragraph, the term `25-percent owner' means a controlled foreign corporation which owns directly 25 percent or more of the capital or profits interest in a partnership. For purposes of the preceding sentence, if a controlled foreign corporation is a shareholder or partner of a corporation or partnership, the controlled foreign corporation shall be treated as owning directly its proportionate share of any such capital or profits interest held directly or indirectly by such corporation or partnership.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply to taxable years of foreign corporations beginning after December 31, 2004, and to taxable years of United States shareholders with or within which such taxable years of foreign corporations end.

## **SEC. 413. REPEAL OF FOREIGN PERSONAL HOLDING COMPANY RULES AND FOREIGN INVESTMENT COMPANY RULES.**

(a) GENERAL RULE- The following provisions are hereby repealed:

- (1) Part III of subchapter G of chapter 1 (relating to foreign personal holding companies).
- (2) Section 1246 (relating to gain on foreign investment company stock).
- (3) Section 1247 (relating to election by foreign investment companies to distribute income currently).

(b) EXEMPTION OF FOREIGN CORPORATIONS FROM PERSONAL HOLDING COMPANY RULES-

(1) IN GENERAL- Subsection (c) of section 542 (relating to exceptions) is amended--

(A) by striking paragraph (5) and inserting the following:

` (5) a foreign corporation,'

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

(C) by inserting `and' at the end of paragraph (7) (as so redesignated), and

(D) by striking `; and' at the end of paragraph (8) (as so redesignated) and inserting a period.

(2) TREATMENT OF INCOME FROM PERSONAL SERVICE CONTRACTS- Paragraph (1) of section 954(c) is amended by adding at the end the following new subparagraph:

  `(I) PERSONAL SERVICE CONTRACTS-

    ` (i) Amounts received under a contract under which the corporation is to furnish personal services if--

      ` (I) some person other than the corporation has the right to designate (by name or by description) the individual who is to perform the services, or

      ` (II) the individual who is to perform the services is designated (by name or by description) in the contract, and

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

This subparagraph shall apply with respect to amounts received for services under a particular contract only if at some time during the taxable year 25 percent or more in value of the outstanding stock of the corporation is owned, directly or indirectly, by or for the individual who has performed, is to perform, or may be designated (by name or by description) as the one to perform, such services.'

(c) CONFORMING AMENDMENTS-

(1) Section 1(h) is amended--

  (A) in paragraph (10), by inserting `and' at the end of subparagraph (F), by striking subparagraph (G), and by redesignating subparagraph (H) as subparagraph (G), and

  (B) by striking `a foreign personal holding company (as defined in section 552), a foreign investment company (as defined in section 1246(b)), or' in paragraph (11)(C)(iii).

(2) Paragraph (2) of section 171(c) is amended--

  (A) by striking `, or by a foreign personal holding company, as defined in section 552', and

  (B) by striking `, or foreign personal holding company'.

(3) Paragraph (2) of section 245(a) is amended by striking `foreign personal holding company or'.

(4) Section 312 is amended by striking subsection (j).

(5) Subsection (m) of section 312 is amended by striking `, a foreign investment company (within the meaning of section 1246(b)), or a foreign personal holding company (within the meaning of section 552)'.

(6) Subsection (e) of section 443 is amended by striking paragraph (3) and by redesignating paragraphs (4) and (5) as paragraphs (3) and (4), respectively.

(7) Subparagraph (B) of section 465(c)(7) is amended by adding `or' at the end of clause (i), by striking clause (ii), and by redesignating clause (iii) as clause (ii).

(8) Paragraph (1) of section 543(b) is amended by inserting `and' at the end of subparagraph (A), by striking `, and' at the end of subparagraph (B) and inserting a period, and by striking subparagraph (C).

(9) Paragraph (1) of section 562(b) is amended by striking `or a foreign personal holding company described in section 552'.

(10) Section 563 is amended--

- (A) by striking subsection (c),
- (B) by redesignating subsection (d) as subsection (c), and
- (C) by striking `subsection (a), (b), or (c)' in subsection (c) (as so redesignated) and inserting `subsection (a) or (b)'.

(11) Subsection (d) of section 751 is amended by adding `and' at the end of paragraph (2), by striking paragraph (3), by redesignating paragraph (4) as paragraph (3), and by striking `paragraph (1), (2), or (3)' in paragraph (3) (as so redesignated) and inserting `paragraph (1) or (2)'.

(12) Paragraph (2) of section 864(d) is amended by striking subparagraph (A) and by redesignating subparagraphs (B) and (C) as subparagraphs (A) and (B), respectively.

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

`(A) which is treated as a controlled foreign corporation for any purpose under subpart F of part III of this subchapter, and'.

(B) Subparagraph (B) of section 898(b)(2) is amended by striking `and sections 551(f) and 554, whichever are applicable,'.

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

`(3) UNITED STATES SHAREHOLDER- The term `United States shareholder' has the meaning given to such term by section 951(b), except that, in the case of a foreign corporation having related person insurance income (as defined in section 953(c)(2)), the Secretary may treat any person as a United States shareholder for purposes of this section if such person is treated as a United States shareholder under section 953(c)(1).'.

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

^(c) DETERMINATION OF REQUIRED YEAR-

^(1) IN GENERAL- The required year is--

^(A) the majority U.S. shareholder year, or

^(B) if there is no majority U.S. shareholder year, the taxable year prescribed under regulations.

^(2) 1-MONTH DEFERRAL ALLOWED- A specified foreign corporation may elect, in lieu of the taxable year under paragraph (1)(A), a taxable year beginning 1 month earlier than the majority U.S. shareholder year.

^(3) MAJORITY U.S. SHAREHOLDER YEAR-

^(A) IN GENERAL- For purposes of this subsection, the term `majority U.S. shareholder 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 representative period as the Secretary may prescribe.'

(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 provided in subparagraph (E)(iii) or paragraph (3)(I), any amount includable in gross income under section 1293 (relating to certain passive foreign investment companies).'

(15)(A) Subparagraph (A) of section 904(h)(1), as redesignated by this Act, is amended by adding `or' at the end of clause (i), by striking clause (ii), and by redesignating clause (iii) as clause (ii).

(B) The paragraph heading of paragraph (2) of section 904(h), as so redesignated, is amended by striking `FOREIGN PERSONAL HOLDING OR'.

(16) Section 951 is amended by striking subsections (c) and (d) and by redesignating subsections (e) and (f) as subsections (c) and (d), respectively.

(17) Paragraph (3) of section 989(b) is amended by striking `, 551(a).'.

(18) Paragraph (5) of section 1014(b) is amended by inserting `and before January 1, 2005,' after `August 26, 1937,'.

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

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

``(3) SPECIAL RULES ON CARRYBACKS- A net capital loss of a corporation shall not be carried back under paragraph (1)(A) to a taxable year--

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

``(B) for which it is a real estate investment trust (as defined in section 856).'

(B) The amendment made by subparagraph (A) shall apply to taxable years beginning after December 31, 2004.

(21) Section 1223 is amended by striking paragraph (10) and by redesignating the following paragraphs accordingly.

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

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

(24)(A) Subparagraph (F) of section 1291(b)(3) is amended by striking '551(d), 959(a),' and inserting '959(a)'.

(B) Subsection (e) of section 1291 is amended by inserting `(as in effect on the day before the date of the enactment of the American Jobs Creation Act of 2004)' after `section 1246'.

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

`(2) ELECTION NOT PERMITTED WHERE AMOUNTS OTHERWISE INCLUDIBLE UNDER SECTION 951- The taxpayer may not make an election under paragraph (1) with respect to the undistributed PFIC earnings tax liability attributable to a qualified electing fund for the taxable year if any amount is includible in the gross income of the taxpayer under section 951 with respect to such fund for such taxable year.'

(26) Section 6035 is hereby repealed.

(27) Subparagraph (D) of section 6103(e)(1) is amended by striking clause (iv) and redesignating clauses (v) and (vi) as clauses (iv) and (v), respectively.

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

`(B) CONSTRUCTIVE DIVIDENDS- If the taxpayer omits from gross income an amount properly includible therein under section 951(a), the tax may be assessed, or a proceeding in court for the collection of such tax may be done without assessing, at any time within 6 years after the return was filed.'

(29) Subsection (a) of section 6679 is amended--

(A) by striking `6035, 6046, and 6046A' in paragraph (1) and inserting `6046 and 6046A', and

(B) by striking paragraph (3).

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

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

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

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

(d) EFFECTIVE DATES-

(1) IN GENERAL- Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years of foreign corporations beginning after December 31, 2004, and to taxable years of United States shareholders with or within which such taxable years of foreign corporations end.

(2) SUBSECTION (c)(27)- The amendments made by subsection (c)(27) shall apply to disclosures of return or return information with respect to taxable years beginning after December 31, 2004.

## **SEC. 414. DETERMINATION OF FOREIGN PERSONAL HOLDING COMPANY INCOME WITH RESPECT TO TRANSACTIONS IN COMMODITIES.**

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

- ` (i) arise out of commodity hedging transactions (as defined in paragraph (4)(A)),
- ` (ii) are active business gains or losses from the sale of commodities, but only if substantially all of the controlled foreign corporation's commodities are property described in paragraph (1), (2), or (8) of section 1221(a), or'.

(b) DEFINITION AND SPECIAL RULES- Subsection (c) of section 954, as amended by this Act, is amended by adding after paragraph (4) the following new paragraph:

### **` (5) DEFINITION AND SPECIAL RULES RELATING TO COMMODITY TRANSACTIONS-**

**` (A) COMMODITY HEDGING TRANSACTIONS-** For purposes of paragraph (1)(C)(i), the term `commodity hedging transaction' means any transaction with respect to a commodity if such transaction--

- ` (i) is a hedging transaction as defined in section 1221(b)(2), determined--
  - ` (I) without regard to subparagraph (A)(ii) thereof,
  - ` (II) by applying subparagraph (A)(i) thereof by substituting `ordinary property or property described in section 1231(b)' for `ordinary property', and
  - ` (III) by substituting `controlled foreign corporation' for `taxpayer' each place it appears, and
- ` (ii) is clearly identified as such in accordance with section 1221(a)(7).

**` (B) TREATMENT OF DEALER ACTIVITIES UNDER PARAGRAPH (1)(C)-** Commodities with respect to which gains and losses are not taken into account under paragraph (2)(C) in computing a controlled foreign corporation's foreign personal holding company income shall not be taken into account in applying the substantially all test under paragraph (1)(C)(ii) to such corporation.

**` (C) REGULATIONS-** The Secretary shall prescribe such regulations as are appropriate to carry out the purposes of paragraph (1)(C) in the case of transactions involving related parties.'

(c) MODIFICATION OF EXCEPTION FOR DEALERS- Clause (i) of section 954(c)(2)(C) is amended by inserting `and transactions involving physical settlement' after `(including hedging transactions'.

(d) EFFECTIVE DATE- The amendments made by this section shall apply to transactions entered into after December 31, 2004.

## **SEC. 415. MODIFICATIONS TO TREATMENT OF AIRCRAFT LEASING AND SHIPPING INCOME.**

(a) ELIMINATION OF FOREIGN BASE COMPANY SHIPPING INCOME- Section 954 (relating to foreign base company income) is amended--

- (1) by striking paragraph (4) of subsection (a) (relating to foreign base company shipping income), and
- (2) by striking subsection (f) (relating to foreign base company shipping income).

(b) SAFE HARBOR FOR CERTAIN LEASING ACTIVITIES- Subparagraph (A) of section 954(c)(2) is amended by adding at the end the following new sentence: `For purposes of the preceding sentence, rents derived from leasing an aircraft or vessel in foreign commerce shall not fail to be treated as derived in the active conduct of a trade or business if, as determined under regulations prescribed by the Secretary, the active leasing expenses are not less than 10 percent of the profit on the lease.'.

(c) CONFORMING AMENDMENTS-

- (1) Section 952(c)(1)(B)(iii) is amended by striking subclause (I) and redesignating subclauses (II) through (VI) as subclauses (I) through (V), respectively.
- (2) Subsection (b) of section 954 is amended--
  - (A) by striking `the foreign base company shipping income,' in paragraph (5),
  - (B) by striking paragraphs (6) and (7), and
  - (C) by redesignating paragraph (8) as paragraph (6).

(d) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years of foreign corporations beginning after December 31, 2004, and to taxable years of United States shareholders with or within which such taxable years of foreign corporations end.

## **SEC. 416. MODIFICATION OF EXCEPTIONS UNDER SUBPART F FOR ACTIVE FINANCING.**

(a) IN GENERAL- Section 954(h)(3) is amended by adding at the end the following:

`(E) DIRECT CONDUCT OF ACTIVITIES- For purposes of subparagraph (A)(ii)(II), an activity shall be treated as conducted directly by an eligible controlled foreign corporation or qualified business unit in its home country if the activity is performed by employees of a related person and--

- `(i) the related person is an eligible 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.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply to taxable years of such foreign corporations beginning after December 31, 2004, and to taxable years of United States shareholders with or within which such taxable years of such foreign corporations end.

## **SEC. 417. 10-YEAR FOREIGN TAX CREDIT CARRYOVER; 1-YEAR FOREIGN TAX CREDIT CARRYBACK.**

(a) GENERAL RULE- Section 904(c) (relating to carryback and carryover of excess tax paid) is amended--

- (1) by striking `in the second preceding taxable year,' and
- (2) by striking `, and in the first, second, third, fourth, or fifth' and inserting `and in any of the first 10'.

(b) EXCESS EXTRACTION TAXES- Paragraph (1) of section 907(f) is amended--

- (1) by striking `in the second preceding taxable year,'
- (2) by striking `, and in the first, second, third, fourth, or fifth' and inserting `and in any of the first 10', and
- (3) by striking the last sentence.

(c) EFFECTIVE DATE-

(1) CARRYBACK- The amendments made by subsections (a)(1) and (b)(1) shall apply to excess foreign taxes arising in taxable years beginning after the date of the enactment of this Act.

(2) CARRYOVER- The amendments made by subsections (a)(2) and (b)(2) shall apply to excess foreign taxes which (without regard to the amendments made by this section) may be carried to any taxable year ending after the date of the enactment of this Act.

## **SEC. 418. MODIFICATION OF THE TREATMENT OF CERTAIN REIT DISTRIBUTIONS ATTRIBUTABLE TO GAIN FROM SALES OR EXCHANGES OF UNITED STATES REAL PROPERTY INTERESTS.**

(a) IN GENERAL- Paragraph (1) of section 897(h) (relating to look-through of distributions) is amended by adding at the end the following new sentence:

`Notwithstanding the preceding sentence, any distribution by a REIT with respect to any class of stock which is regularly traded on an established securities market located in the United States shall not be treated as gain recognized from the sale

or exchange of a United States real property interest if the shareholder did not own more than 5 percent of such class of stock at any time during the taxable year.'

(b) CONFORMING AMENDMENT- Paragraph (3) of section 857(b) (relating to capital gains) is amended by adding at the end the following new subparagraph:

`(F) CERTAIN DISTRIBUTIONS- In the case of a shareholder of a real estate investment trust to whom section 897 does not apply by reason of the second sentence of section 897(h)(1), the amount which would be included in computing long-term capital gains for such shareholder under subparagraph (B) or (D) (without regard to this subparagraph)--

`(i) shall not be included in computing such shareholder's long-term capital gains, and

`(ii) shall be included in such shareholder's gross income as a dividend from the real estate investment trust.'

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

## **SEC. 419. EXCLUSION OF INCOME DERIVED FROM CERTAIN WAGERS ON HORSE RACES AND DOG RACES FROM GROSS INCOME OF NONRESIDENT ALIEN INDIVIDUALS.**

(a) IN GENERAL- Subsection (b) of section 872 (relating to exclusions) is amended by redesignating paragraphs (5), (6), and (7) as paragraphs (6), (7), and (8), respectively, and inserting after paragraph (4) the following new paragraph:

`(5) INCOME DERIVED FROM WAGERING TRANSACTIONS IN CERTAIN PARIMUTUEL POOLS- Gross income derived by a nonresident alien individual from a legal wagering transaction initiated outside the United States in a parimutuel pool with respect to a live horse race or dog race in the United States.'

(b) CONFORMING AMENDMENT- Section 883(a)(4) is amended by striking `(5), (6), and (7)' and inserting `(6), (7), and (8)'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to wagers made after the date of the enactment of this Act.

## **SEC. 420. LIMITATION OF WITHHOLDING TAX FOR PUERTO RICO CORPORATIONS.**

(a) IN GENERAL- Subsection (b) of section 881 is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following new paragraph:

`(2) COMMONWEALTH OF PUERTO RICO-

`(A) IN GENERAL- If dividends are received during a taxable year by a corporation--

`(i) created or organized in, or under the law of, the Commonwealth of Puerto Rico, and

``(ii) with respect to which the requirements of subparagraphs (A), (B), and (C) of paragraph (1) are met for the taxable year,

subsection (a) shall be applied for such taxable year by substituting `10 percent' for `30 percent'.

``(B) APPLICABILITY- If, on or after the date of the enactment of this paragraph, an increase in the rate of the Commonwealth of Puerto Rico's withholding tax which is generally applicable to dividends paid to United States corporations not engaged in a trade or business in the Commonwealth to a rate greater than 10 percent takes effect, this paragraph shall not apply to dividends received on or after the effective date of the increase.'

(b) WITHHOLDING- Subsection (c) of section 1442 (relating to withholding of tax on foreign corporations) is amended--

(1) by striking `For purposes' and inserting the following:

``(1) GUAM, AMERICAN SAMOA, THE NORTHERN MARIANA ISLANDS, AND THE VIRGIN ISLANDS- For purposes', and

(2) by adding at the end the following new paragraph:

``(2) COMMONWEALTH OF PUERTO RICO-

``(A) IN GENERAL- If dividends are received during a taxable year by a corporation--

``(i) created or organized in, or under the law of, the Commonwealth of Puerto Rico, and

``(ii) with respect to which the requirements of subparagraphs (A), (B), and (C) of section 881(b)(1) are met for the taxable year,

subsection (a) shall be applied for such taxable year by substituting `10 percent' for `30 percent'.

``(B) APPLICABILITY- If, on or after the date of the enactment of this paragraph, an increase in the rate of the Commonwealth of Puerto Rico's withholding tax which is generally applicable to dividends paid to United States corporations not engaged in a trade or business in the Commonwealth to a rate greater than 10 percent takes effect, this paragraph shall not apply to dividends received on or after the effective date of the increase.'

(c) CONFORMING AMENDMENTS-

(1) Subsection (b) of section 881 is amended by striking `GUAM AND VIRGIN ISLANDS CORPORATIONS' in the heading and inserting `POSSESSIONS'.

(2) Paragraph (1) of section 881(b) is amended by striking `IN GENERAL' in the heading and inserting `GUAM, AMERICAN SAMOA, THE NORTHERN MARIANA ISLANDS, AND THE VIRGIN ISLANDS'.

(d) EFFECTIVE DATE- The amendments made by this section shall apply to dividends paid after the date of the enactment of this Act.

## **SEC. 421. FOREIGN TAX CREDIT UNDER ALTERNATIVE MINIMUM TAX.**

### **(a) IN GENERAL-**

- (1) Subsection (a) of section 59 is amended by striking paragraph (2) and by redesignating paragraphs (3) and (4) as paragraphs (2) and (3), respectively.
- (2) Section 53(d)(1)(B)(i)(II) is amended by striking 'and if section 59(a)(2) did not apply'.

**(b) EFFECTIVE DATE-** The amendments made by this section shall apply to taxable years beginning after December 31, 2004.

## **SEC. 422. INCENTIVES TO REINVEST FOREIGN EARNINGS IN UNITED STATES.**

**(a) IN GENERAL-** Subpart F of part III of subchapter N of chapter 1 (relating to controlled foreign corporations) is amended by adding at the end the following new section:

## **SEC. 965. TEMPORARY DIVIDENDS RECEIVED DEDUCTION.**

### **^(a) DEDUCTION-**

**^(1) IN GENERAL-** In the case of a corporation which is a United States shareholder and for which the election under this section is in effect for the taxable year, there shall be allowed as a deduction an amount equal to 85 percent of the cash dividends which are received during such taxable year by such shareholder from controlled foreign corporations.

**^(2) DIVIDENDS PAID INDIRECTLY FROM CONTROLLED FOREIGN CORPORATIONS-** If, within the taxable year for which the election under this section is in effect, a United States shareholder receives a cash distribution from a controlled foreign corporation which is excluded from gross income under section 959(a), such distribution shall be treated for purposes of this section as a cash dividend to the extent of any amount included in income by such United States shareholder under section 951(a)(1)(A) as a result of any cash dividend during such taxable year to--

**^(A)** such controlled foreign corporation from another controlled foreign corporation that is in a chain of ownership described in section 958(a), or

**^(B)** any other controlled foreign corporation in such chain of ownership, but only to the extent of cash distributions described in section 959(b) which are made during such taxable year to the controlled foreign corporation from which such United States shareholder received such distribution.

### **^(b) LIMITATIONS-**

**^(1) IN GENERAL-** The amount of dividends taken into account under subsection (a) shall not exceed the greater of--

- ^(A) \$500,000,000,
- ^(B) the amount shown on the applicable financial statement as earnings permanently reinvested outside the United States, or
- ^(C) in the case of an applicable financial statement which fails to show a specific amount of earnings permanently reinvested outside the United States and which shows a specific amount of tax liability attributable to such earnings, the amount equal to the amount of such liability divided by 0.35.

The amounts described in subparagraphs (B) and (C) shall be treated as being zero if there is no such statement or such statement fails to show a specific amount of such earnings or liability, as the case may be.

^(2) DIVIDENDS MUST BE EXTRAORDINARY- The amount of dividends taken into account under subsection (a) shall not exceed the excess (if any) of-

- ^(A) the dividends received during the taxable year by such shareholder from controlled foreign corporations, over
- ^(B) the annual average for the base period years of-
  - ^(i) the dividends received during each base period year by such shareholder from controlled foreign corporations,
  - ^(ii) the amounts includable in such shareholder's gross income for each base period year under section 951(a)(1)(B) with respect to controlled foreign corporations, and
  - ^(iii) the amounts that would have been included for each base period year but for section 959(a) with respect to controlled foreign corporations.

The amount taken into account under clause (iii) for any base period year shall not include any amount which is not includable in gross income by reason of an amount described in clause (ii) with respect to a prior taxable year. Amounts described in subparagraph (B) for any base period year shall be such amounts as shown on the most recent return filed for such year; except that amended returns filed after June 30, 2003, shall not be taken into account.

^(3) REDUCTION OF BENEFIT IF INCREASE IN RELATED PARTY INDEBTEDNESS- The amount of dividends which would (but for this paragraph) be taken into account under subsection (a) shall be reduced by the excess (if any) of-

- ^(A) the amount of indebtedness of the controlled foreign corporation to any related person (as defined in section 954(d)(3)) as of the close of the taxable year for which the election under this section is in effect, over
- ^(B) the amount of indebtedness of the controlled foreign corporation to any related person (as so defined) as of the close of October 3, 2004.

All controlled foreign corporations with respect to which the taxpayer is a United States shareholder shall be treated as 1 controlled foreign corporation for purposes of this paragraph.

^(4) REQUIREMENT TO INVEST IN UNITED STATES- Subsection (a) shall not apply to any dividend received by a United States shareholder unless the amount of the dividend is invested in the United States pursuant to a domestic reinvestment plan which--

^(A) is approved by the taxpayer's president, chief executive officer, or comparable official before the payment of such dividend and subsequently approved by the taxpayer's board of directors, management committee, executive committee, or similar body, and  
^(B) provides for the reinvestment of such dividend in the United States (other than as payment for executive compensation), including as a source for the funding of worker hiring and training, infrastructure, research and development, capital investments, or the financial stabilization of the corporation for the purposes of job retention or creation.

^(c) DEFINITIONS AND SPECIAL RULES- For purposes of this section--

^(1) APPLICABLE FINANCIAL STATEMENT- The term 'applicable financial statement' means, with respect to a United States shareholder, the most recently audited financial statement (including notes and other documents which accompany such statement) which includes such shareholder--

^(A) which is certified on or before June 30, 2003, as being prepared in accordance with generally accepted accounting principles, and

^(B) which is used for the purposes of a statement or report--

^(i) to creditors,

^(ii) to shareholders, or

^(iii) for any other substantial nontax purpose.

In the case of a corporation required to file a financial statement with the Securities and Exchange Commission, such term means the most recent such statement filed on or before June 30, 2003.

^(2) BASE PERIOD YEARS-

^(A) IN GENERAL- The base period years are the 3 taxable years--

^(i) which are among the 5 most recent taxable years ending on or before June 30, 2003, and

^(ii) which are determined by disregarding--

^(I) 1 taxable year for which the sum of the amounts described in clauses (i), (ii), and (iii) of subsection (b)(2)(B) is the largest, and

^(II) 1 taxable year for which such sum is the smallest.

^(B) SHORTER PERIOD- If the taxpayer has fewer than 5 taxable years ending on or before June 30, 2003, then in lieu of applying

subparagraph (A), the base period years shall include all the taxable years of the taxpayer ending on or before June 30, 2003.

^(C) MERGERS, ACQUISITIONS, ETC-

^(i) IN GENERAL- Rules similar to the rules of subparagraphs (A) and (B) of section 41(f)(3) shall apply for purposes of this paragraph.

^(ii) SPIN-OFFS, ETC- If there is a distribution to which section 355 (or so much of section 356 as relates to section 355) applies during the 5-year period referred to in subparagraph (A)(i) and the controlled corporation (within the meaning of section 355) is a United States shareholder--

^(I) the controlled corporation shall be treated as being in existence during the period that the distributing corporation (within the meaning of section 355) is in existence, and

^(II) for purposes of applying subsection (b)(2) to the controlled corporation and the distributing corporation, amounts described in subsection (b)(2)(B) which are received or includible by the distributing corporation or controlled corporation (as the case may be) before the distribution referred to in subclause (I) from a controlled foreign corporation shall be allocated between such corporations in proportion to their respective interests as United States shareholders of such controlled foreign corporation immediately after such distribution.

Subclause (II) shall not apply if neither the controlled corporation nor the distributing corporation is a United States shareholder of such controlled foreign corporation immediately after such distribution.

^(3) DIVIDEND- The term 'dividend' shall not include amounts includible in gross income as a dividend under section 78, 367, or 1248. In the case of a liquidation under section 332 to which section 367(b) applies, the preceding sentence shall not apply to the extent the United States shareholder actually receives cash as part of the liquidation.

^(4) COORDINATION WITH DIVIDENDS RECEIVED DEDUCTION- No deduction shall be allowed under section 243 or 245 for any dividend for which a deduction is allowed under this section.

^(5) CONTROLLED GROUPS-

^(A) IN GENERAL- All United States shareholders which are members of an affiliated group filing a consolidated return under section 1501 shall be treated as one United States shareholder.

^(B) APPLICATION OF \$500,000,000 LIMIT- All corporations which are treated as a single employer under section 52(a) shall be limited to one \$500,000,000 amount in subsection (b)(1)(A), and

such amount shall be divided among such corporations under regulations prescribed by the Secretary.

^(C) PERMANENTLY REINVESTED EARNINGS- If a financial statement is an applicable financial statement for more than 1 United States shareholder, the amount applicable under subparagraph (B) or (C) of subsection (b)(1) shall be divided among such shareholders under regulations prescribed by the Secretary.

^(d) DENIAL OF FOREIGN TAX CREDIT; DENIAL OF CERTAIN EXPENSES-

^(1) FOREIGN TAX CREDIT- No credit shall be allowed under section 901 for any taxes paid or accrued (or treated as paid or accrued) with respect to the deductible portion of-

^(A) any dividend, or

^(B) any amount described in subsection (a)(2) which is included in income under section 951(a)(1)(A).

No deduction shall be allowed under this chapter for any tax for which credit is not allowable by reason of the preceding sentence.

^(2) EXPENSES- No deduction shall be allowed for expenses properly allocated and apportioned to the deductible portion described in paragraph (1).

^(3) DEDUCTIBLE PORTION- For purposes of paragraph (1), unless the taxpayer otherwise specifies, the deductible portion of any dividend or other amount is the amount which bears the same ratio to the amount of such dividend or other amount as the amount allowed as a deduction under subsection (a) for the taxable year bears to the amount described in subsection (b)(2)(A) for such year.

^(e) INCREASE IN TAX ON INCLUDED AMOUNTS NOT REDUCED BY CREDITS, ETC-

^(1) IN GENERAL- Any tax under this chapter by reason of nondeductible CFC dividends shall not be treated as tax imposed by this chapter for purposes of determining-

^(A) the amount of any credit allowable under this chapter, or

^(B) the amount of the tax imposed by section 55.

Subparagraph (A) shall not apply to the credit under section 53 or to the credit under section 27(a) with respect to taxes attributable to such dividends.

^(2) LIMITATION ON REDUCTION IN TAXABLE INCOME, ETC-

^(A) IN GENERAL- The taxable income of any United States shareholder for any taxable year shall in no event be less than the amount of nondeductible CFC dividends received during such year.

^(B) COORDINATION WITH SECTION 172- The nondeductible CFC dividends for any taxable year shall not be taken into account--

- `(i) in determining under section 172 the amount of any net operating loss for such taxable year, and
- `(ii) in determining taxable income for such taxable year for purposes of the 2nd sentence of section 172(b)(2).
- `(3) NONDEDUCTIBLE CFC DIVIDENDS- For purposes of this subsection, the term `nondeductible CFC dividends' means the excess of the amount of dividends taken into account under subsection (a) over the deduction allowed under subsection (a) for such dividends.
- `(f) ELECTION- The taxpayer may elect to apply this section to--
  - `(1) the taxpayer's last taxable year which begins before the date of the enactment of this section, or
  - `(2) the taxpayer's first taxable year which begins during the 1-year period beginning on such date.
 Such election may be made for a taxable year only if made before the due date (including extensions) for filing the return of tax for such taxable year.'
- (b) ALTERNATIVE MINIMUM TAX- Subparagraph (C) of section 56(g)(4) is amended by inserting after clause (v) the following new clause:

`**(vi) SPECIAL RULE FOR CERTAIN DISTRIBUTIONS FROM CONTROLLED FOREIGN CORPORATIONS-**  
 Clause (i) shall not apply to any deduction allowable under section 965.'

- (c) CLERICAL AMENDMENT- The table of sections for subpart F of part III of subchapter N of chapter 1 is amended by adding at the end the following new item:

`Sec. 965. Temporary dividends received deduction.'

- (d) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years ending on or after the date of the enactment of this Act.

**SEC. 423. DELAY IN EFFECTIVE DATE OF FINAL REGULATIONS GOVERNING EXCLUSION OF INCOME FROM INTERNATIONAL OPERATION OF SHIPS OR AIRCRAFT.**

Notwithstanding the provisions of Treasury regulation Sec. 1.883-5, the final regulations issued by the Secretary of the Treasury relating to income derived by foreign corporations from the international operation of ships or aircraft (Treasury regulations 1.883-1 through 1.883-5) shall apply to taxable years of a foreign corporation seeking qualified foreign corporation status beginning after September 24, 2004.

**SEC. 424. STUDY OF EARNINGS STRIPPING PROVISIONS.**

- (a) IN GENERAL- The Secretary of the Treasury or the Secretary's delegate shall conduct a study of the effectiveness of the provisions of the Internal Revenue Code of 1986 applicable to earnings stripping, including a study of-

- (1) the effectiveness of section 163(j) of such Code in preventing the shifting of income outside the United States,
- (2) whether any deficiencies of such provisions place United States-based businesses at a competitive disadvantage relative to foreign-based businesses,
- (3) the impact of earnings stripping activities on the United States tax base,
- (4) whether laws of foreign countries facilitate stripping of earnings out of the United States, and
- (5) whether changes to the earning stripping rules would affect jobs in the United States.

(b) REPORT- Not later than June 30, 2005, the Secretary shall submit to the Congress a report of the study conducted under this section, including specific recommendations as to how to improve the provisions of such Code applicable to earnings stripping.

## **TITLE V--DEDUCTION OF STATE AND LOCAL GENERAL SALES TAXES**

### **SEC. 501. DEDUCTION OF STATE AND LOCAL GENERAL SALES TAXES IN LIEU OF STATE AND LOCAL INCOME TAXES.**

- (a) IN GENERAL- Subsection (b) of section 164 (relating to definitions and special rules) is amended by adding at the end the following:
  - (5) GENERAL SALES TAXES- For purposes of subsection (a)--
    - (A) ELECTION TO DEDUCT STATE AND LOCAL SALES TAXES IN LIEU OF STATE AND LOCAL INCOME TAXES-
      - (i) IN GENERAL- At the election of the taxpayer for the taxable year, subsection (a) shall be applied--
        - (I) without regard to the reference to State and local income taxes, and
        - (II) as if State and local general sales taxes were referred to in a paragraph thereof.
    - (B) DEFINITION OF GENERAL SALES TAX- The term 'general sales tax' means a tax imposed at one rate with respect to the sale at retail of a broad range of classes of items.
    - (C) SPECIAL RULES FOR FOOD, ETC- In the case of items of food, clothing, medical supplies, and motor vehicles--
      - (i) the fact that the tax does not apply with respect to some or all of such items shall not be taken into account in determining whether the tax applies with respect to a broad range of classes of items, and
      - (ii) the fact that the rate of tax applicable with respect to some or all of such items is lower than the general rate of tax shall not be taken into account in determining whether the tax is imposed at one rate.

``(D) ITEMS TAXED AT DIFFERENT RATES- Except in the case of a lower rate of tax applicable with respect to an item described in subparagraph (C), no deduction shall be allowed under this paragraph for any general sales tax imposed with respect to an item at a rate other than the general rate of tax.

``(E) COMPENSATING USE TAXES- A compensating use tax with respect to an item shall be treated as a general sales tax. For purposes of the preceding sentence, the term `compensating use tax' means, with respect to any item, a tax which--

    ``(i) is imposed on the use, storage, or consumption of such item, and

    ``(ii) is complementary to a general sales tax, but only if a deduction is allowable under this paragraph with respect to items sold at retail in the taxing jurisdiction which are similar to such item.

``(F) SPECIAL RULE FOR MOTOR VEHICLES- In the case of motor vehicles, if the rate of tax exceeds the general rate, such excess shall be disregarded and the general rate shall be treated as the rate of tax.

``(G) SEPARATELY STATED GENERAL SALES TAXES- If the amount of any general sales tax is separately stated, then, to the extent that the amount so stated is paid by the consumer (other than in connection with the consumer's trade or business) to the seller, such amount shall be treated as a tax imposed on, and paid by, such consumer.

``(H) AMOUNT OF DEDUCTION MAY BE DETERMINED UNDER TABLES-

    ``(i) IN GENERAL- At the election of the taxpayer for the taxable year, the amount of the deduction allowed under this paragraph for such year shall be--

        ``(I) the amount determined under this paragraph (without regard to this subparagraph) with respect to motor vehicles, boats, and other items specified by the Secretary, and

        ``(II) the amount determined under tables prescribed by the Secretary with respect to items to which subclause (I) does not apply.

    ``(ii) REQUIREMENTS FOR TABLES- The tables prescribed under clause (i)--

        ``(I) shall reflect the provisions of this paragraph,  
        ``(II) shall be based on the average consumption by taxpayers on a State-by-State basis (as determined by the Secretary) of items to which clause (i)(I) does not apply, taking into account filing status, number of dependents, adjusted gross income, and rates of State and local general sales taxation, and

``(III) need only be determined with respect to adjusted gross incomes up to the applicable amount (as determined under section 68(b)).

``(I) APPLICATION OF PARAGRAPH- This paragraph shall apply to taxable years beginning after December 31, 2003, and before January 1, 2006.'

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

## **TITLE VI--FAIR AND EQUITABLE TOBACCO REFORM**

### **SEC. 601. SHORT TITLE.**

This title may be cited as the `Fair and Equitable Tobacco Reform Act of 2004'.

#### **Subtitle A--Termination of Federal Tobacco Quota and Price Support Programs**

### **SEC. 611. TERMINATION OF TOBACCO QUOTA PROGRAM AND RELATED PROVISIONS.**

(a) Marketing Quotas- Part I of subtitle B of title III of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1311 et seq.) is repealed.

(b) TOBACCO INSPECTIONS- Section 213 of the Tobacco Adjustment Act of 1983 (7 U.S.C. 511r) is repealed.

(c) TOBACCO CONTROL- The Act of April 25, 1936 (commonly known as the Tobacco Control Act; 7 U.S.C. 515 et seq.), is repealed.

(d) Processing Tax- Section 9(b) of the Agricultural Adjustment Act (7 U.S.C. 609(b)), reenacted with amendments by the Agricultural Marketing Agreement Act of 1937, is amended--

- (1) in paragraph (2), by striking `tobacco,'; and
- (2) in paragraph (6)(B)(i), by striking `, or, in the case of tobacco, is less than the fair exchange value by not more than 10 per centum,'.

(e) Declaration of Policy- Section 2 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1282) is amended by striking `tobacco,'.

(f) Definitions- Section 301(b) of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1301(b)) is amended--

- (1) in paragraph (3)--

- (A) by striking subparagraph (C); and
  - (B) by redesignating subparagraph (D) as subparagraph (C);

- (2) in paragraph (6)(A), by striking `tobacco,';

- (3) in paragraph (10)--

- (A) by striking subparagraph (B); and
  - (B) by redesignating subparagraph (C) as subparagraph (B);

- (4) in paragraph (11)(B), by striking `and tobacco';

- (5) in paragraph (12), by striking `tobacco,';

- (6) in paragraph (14)--

- (A) in subparagraph (A), by striking `(A)'; and
- (B) by striking subparagraphs (B), (C), and (D);
- (7) by striking paragraph (15);
- (8) in paragraph (16)--
  - (A) by striking subparagraph (B); and
  - (B) by redesignating subparagraph (C) as subparagraph (B);
- (9) by striking paragraph (17); and
- (10) by redesignating paragraph (16) as paragraph (15).

(g) Parity Payments- Section 303 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1303) is amended in the first sentence by striking `rice, or tobacco,' and inserting `or rice,'.

(h) Administrative Provisions- Section 361 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1361) is amended by striking `tobacco,'.

(i) Adjustment of Quotas- Section 371 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1371) is amended--

- (1) in the first sentence of subsection (a), by striking `rice, or tobacco' and inserting `or rice'; and
- (2) in the first sentence of subsection (b), by striking `rice, or tobacco' and inserting `or rice'.

(j) REPORTS AND RECORDS- Section 373 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1373) is amended--

- (1) by striking `rice, or tobacco' each place it appears in subsections (a) and (b) and inserting `or rice'; and
- (2) in subsection (a)--
  - (A) in the first sentence, by striking `all persons engaged in the business of redrying, prizing, or stemming tobacco for producers,'; and
  - (B) in the last sentence, by striking `'\$500,' and all that follows through the period at the end of the sentence and inserting `'\$500.'.

(k) Regulations- Section 375 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1375) is amended--

- (1) in subsection (a), by striking `peanuts, or tobacco' and inserting `or peanuts'; and
- (2) by striking subsection (c).

(l) Eminent Domain- Section 378 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1378) is amended--

- (1) in the first sentence of subsection (c), by striking `cotton, and tobacco' and inserting `and cotton'; and
- (2) by striking subsections (d), (e), and (f).

(m) Burley Tobacco Farm Reconstitution- Section 379 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1379) is amended--

- (1) in subsection (a)--
  - (A) by striking `(a)'; and
  - (B) in paragraph (6), by striking `, but this clause (6) shall not be applicable in the case of burley tobacco'; and
- (2) by striking subsections (b) and (c).

- (n) Acreage-Poundage Quotas- Section 4 of the Act of April 16, 1955 (Public Law 89-12; 7 U.S.C. 1314c note), is repealed.
- (o) Burley Tobacco Acreage Allotments- The Act of July 12, 1952 (7 U.S.C. 1315), is repealed.
- (p) Transfer of Allotments- Section 703 of the Food and Agriculture Act of 1965 (7 U.S.C. 1316) is repealed.
- (q) Advance Recourse Loans- Section 13(a)(2)(B) of the Food Security Improvements Act of 1986 (7 U.S.C. 1433c-1(a)(2)(B)) is amended by striking 'tobacco and'.
- (r) Tobacco Field Measurement- Section 1112 of the Omnibus Budget Reconciliation Act of 1987 (Public Law 100-203; 101 Stat. 1330-8) is amended by striking subsection (c).
- (s) BURLEY TOBACCO IMPORT REVIEW- Section 3 of Public Law 98-59 (7 U.S.C. 625) is repealed.

## **SEC. 612. TERMINATION OF TOBACCO PRICE SUPPORT PROGRAM AND RELATED PROVISIONS.**

- (a) Termination of Tobacco Price Support and No Net Cost Provisions- Sections 106, 106A, and 106B of the Agricultural Act of 1949 (7 U.S.C. 1445, 1445-1, 1445-2) are repealed.
- (b) Parity Price Support- Section 101 of the Agricultural Act of 1949 (7 U.S.C. 1441) is amended--
  - (1) in the first sentence of subsection (a), by striking 'tobacco (except as otherwise provided herein), corn,' and inserting 'corn';
  - (2) by striking subsections (c), (g), (h), and (i);
  - (3) in subsection (d)(3)--
    - (A) by striking ' , except tobacco,'; and
    - (B) by striking 'and no price support shall be made available for any crop of tobacco for which marketing quotas have been disapproved by producers,'; and
  - (4) by redesignating subsections (d) and (e) as subsections (c) and (d), respectively.
- (c) Definition of Basic Agricultural Commodity- Section 408(c) of the Agricultural Act of 1949 (7 U.S.C. 1428(c)) is amended by striking 'tobacco,'.
- (d) Powers of Commodity Credit Corporation- Section 5 of the Commodity Credit Corporation Charter Act (15 U.S.C. 714c) is amended by inserting '(other than tobacco)' after 'agricultural commodities' each place it appears.

## **SEC. 613. CONFORMING AMENDMENTS.**

Section 320B(c)(1) of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1314h(c)(1)) is amended--

- (1) by inserting '(A)' after '(1)';
- (2) by striking 'by' at the end and inserting 'or'; and
- (3) by adding at the end the following:

`(B) in the case of the 2004 marketing year, the price support rate for the kind of tobacco involved in effect under section 106 of the Agricultural Act of 1949 (7 U.S.C. 1445) at the time of the violation; by'.

## **SEC. 614. CONTINUATION OF LIABILITY FOR 2004 AND EARLIER CROP YEARS.**

The amendments made by this subtitle shall not affect the liability of any person under any provision of law so amended with respect to the 2004 or an earlier crop of each kind of tobacco.

### **Subtitle B--Transitional Payments to Tobacco Quota Holders and Producers of Tobacco**

## **SEC. 621. DEFINITIONS.**

In this subtitle and subtitle C:

- (1) AGRICULTURAL ACT OF 1949- The term `Agricultural Act of 1949' means the Agricultural Act of 1949 (7 U.S.C. 1421 et seq.), as in effect on the day before the date of the enactment of this title.
- (2) AGRICULTURAL ADJUSTMENT ACT OF 1938- The term `Agricultural Adjustment Act of 1938' means the Agricultural Adjustment Act of 1938 (7 U.S.C. 1281 et seq.), as in effect on the day before the date of the enactment of this title.
- (3) Considered planted- The term `considered planted' means tobacco that was planted, but failed to be produced as a result of a natural disaster, as determined by the Secretary.
- (4) CONTRACT- The term `contract' means a contract entered into under section 622 or 623.
- (5) CONTRACT PAYMENT- The term `contract payment' means a payment made under section 622 or 623 pursuant to a contract.
- (6) Producer of quota tobacco- The term `producer of quota tobacco' means an owner, operator, landlord, tenant, or sharecropper that shared in the risk of producing tobacco on a farm where tobacco was produced or considered planted pursuant to a tobacco farm poundage quota or farm acreage allotment established under part I of subtitle B of title III of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1311 et seq.).
- (7) QUOTA TOBACCO- The term `quota tobacco' means a kind of tobacco that is subject to a farm marketing quota or farm acreage allotment for the 2004 tobacco marketing year under a marketing quota or allotment program established under part I of subtitle B of title III of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1311 et seq.).
- (8) TOBACCO- The term `tobacco' means each of the following kinds of tobacco:
  - (A) Flue-cured tobacco, comprising types 11, 12, 13, and 14.
  - (B) Fire-cured tobacco, comprising types 22 and 23.

- (C) Dark air-cured tobacco, comprising types 35 and 36.
- (D) Virginia sun-cured tobacco, comprising type 37.
- (E) Virginia fire-cured tobacco, comprising type 21.
- (F) Burley tobacco, comprising type 31.
- (G) Cigar-filler and cigar-binder tobacco, comprising types 42, 43, 44, 53, 54, and 55.
- (9) TOBACCO QUOTA HOLDER- The term 'tobacco quota holder' means a person that was an owner of a farm, as of the date of enactment of this title, for which a basic tobacco farm marketing quota or farm acreage allotment for quota tobacco was established for the 2004 tobacco marketing year.
- (10) TOBACCO TRUST FUND- The term 'Tobacco Trust Fund' means the Tobacco Trust Fund established under section 626.
- (11) Secretary- The term 'Secretary' means the Secretary of Agriculture.

## **SEC. 622. CONTRACT PAYMENTS TO TOBACCO QUOTA HOLDERS.**

- (a) Contract Offered- The Secretary shall offer to enter into a contract with each tobacco quota holder under which the tobacco quota holder shall be entitled to receive payments under this section in exchange for the termination of tobacco marketing quotas and related price support under the amendments made by sections 611 and 612. The contract payments shall constitute full and fair consideration for the termination of such tobacco marketing quotas and related price support.
- (b) Eligibility- To be eligible to enter into a contract to receive a contract payment under this section, a person shall submit to the Secretary an application containing such information as the Secretary may require to demonstrate to the satisfaction of the Secretary that the person is a tobacco quota holder. The application shall be submitted within such time, in such form, and in such manner as the Secretary may require.
- (c) Base Quota Level-
  - (1) Establishment- The Secretary shall establish a base quota level applicable to each tobacco quota holder identified under subsection (b).
  - (2) Poundage quotas- Subject to adjustment under subsection (d), for each kind of tobacco for which the marketing quota is expressed in pounds, the base quota level for each tobacco quota holder shall be equal to the basic quota for quota tobacco established for the 2002 tobacco marketing year under a marketing quota program established under part I of subtitle B of title III of the Agriculture Adjustment Act of 1938 on the farm owned by the tobacco quota holder.
  - (3) Marketing quotas other than poundage quotas- Subject to adjustment under subsection (d), for each kind of tobacco for which there is marketing quota or allotment on an acreage basis, the base quota level for each tobacco quota holder shall be the quantity equal to the product obtained by multiplying--

(A) the basic tobacco farm marketing quota or allotment for the 2002 marketing year established by the Secretary for quota tobacco owned by the tobacco quota holder; by

(B) the average production yield, per acre, for the period covering the 2001, 2002, and 2003 crop years for that kind of tobacco in the county in which the quota tobacco is located.

(d) Treatment of Certain Contracts and Agreements-

(1) Effect of purchase contract- If there was an agreement for the purchase of all or part of a farm described in subsection (c) as of the date of the enactment of this title, and the parties to the sale are unable to agree to the disposition of eligibility for contract payments, the Secretary, taking into account any transfer of quota that has been agreed to, shall provide for the equitable division of the contract payments among the parties by adjusting the determination of who is the tobacco quota holder with respect to particular pounds or allotment of the quota.

(2) Effect of agreement for permanent quota transfer- If the Secretary determines that there was in existence, as of the day before the date of the enactment of this title, an agreement for the permanent transfer of quota, but that the transfer was not completed by that date, the Secretary shall consider the tobacco quota holder to be the party to the agreement that, as of that date, was the owner of the farm to which the quota was to be transferred.

(e) CONTRACT PAYMENTS-

(1) CALCULATION OF TOTAL PAYMENT AMOUNT- The total amount of contract payments to which an eligible tobacco quota holder is entitled under this section, with respect to a kind of tobacco, shall be equal to the product obtained by multiplying--

(A) \$7.00 per pound; by

(B) the base quota level of the tobacco quota holder determined under subsection (c) with respect to that kind of tobacco.

(2) ANNUAL PAYMENT- During each of fiscal years 2005 through 2014, the Secretary shall make a contract payment under this section to each eligible tobacco quota holder, with respect to a kind of tobacco, in an amount equal to 1/10 of the amount determined under paragraph (1) for the tobacco quota holder for that kind of tobacco.

(f) Death of Tobacco Quota Holder- If a tobacco quota holder who is entitled to contract payments under this section dies and is survived by a spouse or one or more dependents, the right to receive the payments shall transfer to the surviving spouse or, if there is no surviving spouse, to the estate of the tobacco quota holder.

## **SEC. 623. CONTRACT PAYMENTS FOR PRODUCERS OF QUOTA TOBACCO.**

(a) Contract Offered- The Secretary shall offer to enter into a contract with each producer of quota tobacco under which the producer of quota tobacco shall be

entitled to receive payments under this section in exchange for the termination of tobacco marketing quotas and related price support under the amendments made by sections 611 and 612. The contract payments shall constitute full and fair consideration for the termination of such tobacco marketing quotas and related price support.

(b) Eligibility-

(1) APPLICATION AND DETERMINATION- To be eligible to enter into a contract to receive a contract payment under this section, a person shall submit to the Secretary an application containing such information as the Secretary may require to demonstrate to the satisfaction of the Secretary that the person is a producer of quota tobacco. The application shall be submitted within such time, in such form, and in such manner as the Secretary may require.

(2) EFFECT OF MULTIPLE PRODUCERS FOR SAME QUOTA TOBACCO- If, on the basis of the applications submitted under paragraph (1) or other information, the Secretary determines that two or more persons are a producer of the same quota tobacco, the Secretary shall provide for an equitable distribution among the persons of the contract payments made under this section with respect to that quota tobacco, based on relative share of such persons in the risk of producing the quota tobacco and such other factors as the Secretary considers appropriate.

(c) BASE QUOTA LEVEL-

(1) ESTABLISHMENT- The Secretary shall establish a base quota level applicable to each producer of quota tobacco, as determined under this subsection.

(2) FLUE-CURED AND BURLEY TOBACCO- In the case of Flue-cured tobacco (types 11, 12, 13, and 14) and Burley tobacco (type 31), the base quota level for each producer of quota tobacco shall be equal to the effective tobacco marketing quota (irrespective of disaster lease and transfers) under part I of subtitle B of title III of the Agriculture Adjustment Act of 1938 for the 2002 marketing year for quota tobacco produced on the farm.

(3) OTHER KINDS OF TOBACCO- In the case of each kind of tobacco (other than tobacco covered by paragraph (2)), for the purpose of calculating a contract payment to a producer of quota tobacco, the base quota level for the producer of quota tobacco shall be the quantity obtained by multiplying--

(A) the basic tobacco farm acreage allotment for the 2002 marketing year established by the Secretary for quota tobacco produced on the farm; by

(B) the average annual yield, per acre, of quota tobacco produced on the farm for the period covering the 2001, 2002, and 2003 crop years.

(d) CONTRACT PAYMENTS-

(1) CALCULATION OF TOTAL PAYMENT AMOUNT- Subject to subsection (b)(2), the total amount of contract payments to which an

eligible producer of quota tobacco is entitled under this section, with respect to a kind of tobacco, shall be equal to the product obtained by multiplying--

- (A) subject to paragraph (2), \$3.00 per pound; by
- (B) the base quota level of the producer of quota tobacco determined under subsection (c) with respect to that kind of tobacco.

(2) ANNUAL PAYMENT- During each of fiscal years 2005 through 2014, the Secretary shall make a contract payment under this section to each eligible producer of tobacco, with respect to a kind of tobacco, in an amount equal to 1/10 of the amount determined under paragraph (1) for the producer for that kind of tobacco.

(3) VARIABLE PAYMENT RATES- The rate for payments to a producer of quota tobacco under paragraph (1)(A) shall be equal to--

- (A) in the case of a producer of quota tobacco that produced quota tobacco marketed, or considered planted, under a marketing quota in all three of the 2002, 2003, or 2004 tobacco marketing years, the rate prescribed under paragraph (1)(A);
- (B) in the case of a producer of quota tobacco that produced quota tobacco marketed, or considered planted, under a marketing quota in only two of those tobacco marketing years, 2/3 of the rate prescribed under paragraph (1)(A);
- (C) in the case of a producer of quota tobacco that produced quota tobacco marketed, or considered planted, under a marketing quota in only one of those tobacco marketing years, 1/3 of the rate prescribed under paragraph (1)(A).

(e) Death of Tobacco Producer- If a producer of quota tobacco who is entitled to contract payments under this section dies and is survived by a spouse or one or more dependents, the right to receive the contract payments shall transfer to the surviving spouse or, if there is no surviving spouse, to the estate of the producer.

## **SEC. 624. ADMINISTRATION.**

(a) TIME FOR PAYMENT OF CONTRACT PAYMENTS- Contract payments required to be made for a fiscal year shall be made by the Secretary as soon as practicable.

(b) USE OF COUNTY COMMITTEES TO RESOLVE DISPUTES- Any dispute regarding the eligibility of a person to enter into a contract or to receive contract payments, and any dispute regarding the amount of a contract payment, may be appealed to the county committee established under section 8 of the Soil Conservation and Domestic Allotment Act (16 U.S.C. 590h) for the county or other area in which the farming operation of the person is located.

(c) ROLE OF NATIONAL APPEALS DIVISION- Any adverse determination of a county committee under subsection (b) may be appealed to the National Appeals Division established under subtitle H of the Department of Agriculture Reorganization Act of 1994 (7 U.S.C. 6991 et seq.).

(d) USE OF FINANCIAL INSTITUTIONS- The Secretary may use a financial institution to manage assets, make contract payments, and otherwise carry out this title.

(e) PAYMENT TO FINANCIAL INSTITUTIONS- The Secretary shall permit a tobacco quota holder or producer of quota tobacco entitled to contract payments to assign to a financial institution the right to receive the contract payments. Upon receiving notification of the assignment, the Secretary shall make subsequent contract payments for the tobacco quota holder or producer of quota tobacco directly to the financial institution designated by the tobacco quota holder or producer of quota tobacco. The Secretary shall make information available to tobacco quota holders and producers of quota tobacco regarding their ability to elect to have the Secretary make payments directly to a financial institution under this subsection so that they may obtain a lump sum or other payment.

## **SEC. 625. USE OF ASSESSMENTS AS SOURCE OF FUNDS FOR PAYMENTS.**

(a) **DEFINITIONS**- In this section:

(1) **BASE PERIOD**- The term 'base period' means the one-year period ending the June 30 before the beginning of a fiscal year.

(2) **GROSS DOMESTIC VOLUME**- The term 'gross domestic volume' means the volume of tobacco products--

(A) removed (as defined by section 5702 of the Internal Revenue Code of 1986); and

(B) not exempt from tax under chapter 52 of the Internal Revenue Code of 1986 at the time of their removal under that chapter or the Harmonized Tariff Schedule of the United States (19 U.S.C. 1202).

(3) **MARKET SHARE**- The term 'market share' means the share of each manufacturer or importer of a class of tobacco product (expressed as a decimal to the fourth place) of the total volume of domestic sales of the class of tobacco product during the base period for a fiscal year for an assessment under this section.

(b) **QUARTERLY ASSESSMENTS**-

(1) **IMPOSITION OF ASSESSMENT**- The Secretary, acting through the Commodity Credit Corporation, shall impose quarterly assessments during each of fiscal years 2005 through 2014, calculated in accordance with this section, on each tobacco product manufacturer and tobacco product importer that sells tobacco products in domestic commerce in the United States during that fiscal year.

(2) **AMOUNTS**- Beginning with the calendar quarter ending on December 31 of each of fiscal years 2005 through 2014, the assessment payments over each four-calendar quarter period shall be sufficient to cover--

(A) the contract payments made under sections 622 and 623 during that period; and

(B) other expenditures from the Tobacco Trust Fund made during the base quarter periods corresponding to the four calendar quarters of that period.

(3) DEPOSIT- Assessments collected under this section shall be deposited in the Tobacco Trust Fund.

(c) ASSESSMENTS FOR CLASSES OF TOBACCO PRODUCTS-

(1) INITIAL ALLOCATION- The percentage of the total amount required by subsection (b) to be assessed against, and paid by, the manufacturers and importers of each class of tobacco product in fiscal year 2005 shall be as follows:

(A) For cigarette manufacturers and importers, 96.331 percent.

(B) For cigar manufacturers and importers, 2.783 percent.

(C) For snuff manufacturers and importers, 0.539 percent.

(D) For roll-your-own tobacco manufacturers and importers, 0.171 percent.

(E) For chewing tobacco manufacturers and importers, 0.111 percent.

(F) For pipe tobacco manufacturers and importers, 0.066 percent.

(2) SUBSEQUENT ALLOCATIONS- For subsequent fiscal years, the Secretary shall periodically adjust the percentage of the total amount required under subsection (b) to be assessed against, and paid by, the manufacturers and importers of each class of tobacco product specified in paragraph (1) to reflect changes in the share of gross domestic volume held by that class of tobacco product.

(3) EFFECT OF INSUFFICIENT AMOUNTS- If the Secretary determines that the assessment imposed under subsection (b) will result in insufficient amounts to carry out this subtitle during a fiscal year, the Secretary shall assess such additional amounts as the Secretary determines to be necessary to carry out this subtitle during that fiscal year. The additional amount shall be allocated to manufacturers and importers of each class of tobacco product specified in paragraph (1) in the same manner and based on the same percentages applicable under paragraph (1) or (2) for that fiscal year.

(d) NOTIFICATION AND TIMING OF ASSESSMENTS-

(1) NOTIFICATION OF ASSESSMENTS- The Secretary shall provide each manufacturer or importer subject to an assessment under subsection (b) with written notice setting forth the amount to be assessed against the manufacturer or importer for each quarterly payment period. The notice for a quarterly period shall be provided not later than 30 days before the date payment is due under paragraph (3).

(2) CONTENT- The notice shall include the following information with respect to the quarterly period used by the Secretary in calculating the amount:

(A) The total combined assessment for all manufacturers and importers of tobacco products.

- (B) The total assessment with respect to the class of tobacco products manufactured or imported by the manufacturer or importer.
- (C) Any adjustments to the percentage allocations among the classes of tobacco products made pursuant to paragraph (2) or (3) of subsection (c).
- (D) The volume of gross sales of the applicable class of tobacco product treated as made by the manufacturer or importer for purposes of calculating the manufacturer's or importer's market share under subsection (f).
- (E) The total volume of gross sales of the applicable class of tobacco product that the Secretary treated as made by all manufacturers and importers for purposes of calculating the manufacturer's or importer's market share under subsection (f).
- (F) The manufacturer's or importer's market share of the applicable class of tobacco product, as determined by the Secretary under subsection (f).
- (G) The market share, as determined by the Secretary under subsection (f), of each other manufacturer and importer, for each applicable class of tobacco product.

**(3) TIMING OF ASSESSMENT PAYMENTS-**

- (A) **COLLECTION DATE-** Assessments shall be collected at the end of each calendar year quarter, except that the Secretary shall ensure that the final assessment due under this section is collected not later than September 30, 2014.
- (B) **BASE PERIOD QUARTER-** The assessment for a calendar year quarter shall correspond to the base period quarter that ended at the end of the preceding calendar year quarter.

**(e) ALLOCATION OF ASSESSMENT WITHIN EACH CLASS OF TOBACCO PRODUCT-**

- (1) **PRO RATA BASIS-** The assessment for each class of tobacco product specified in subsection (c)(1) shall be allocated on a pro rata basis among manufacturers and importers based on each manufacturer's or importer's share of gross domestic volume.
- (2) **LIMITATION-** No manufacturer or importer shall be required to pay an assessment that is based on a share that is in excess of the manufacturer's or importer's share of domestic volume.

**(f) ALLOCATION OF TOTAL ASSESSMENTS BY MARKET SHARE-** The amount of the assessment for each class of tobacco product specified in subsection (c)(1) to be paid by each manufacturer or importer of that class of tobacco product shall be determined for each quarterly payment period by multiplying--

- (1) the market share of the manufacturer or importer, as calculated with respect to that payment period, of the class of tobacco product; by
- (2) the total amount of the assessment for that quarterly payment period under subsection (c), for the class of tobacco product.

**(g) DETERMINATION OF VOLUME OF DOMESTIC SALES-**

(1) **IN GENERAL-** The calculation of the volume of domestic sales of a class of tobacco product by a manufacturer or importer, and by all manufacturers and importers as a group, shall be made by the Secretary based on information provided by the manufacturers and importers pursuant to subsection (h), as well as any other relevant information provided to or obtained by the Secretary.

(2) **GROSS DOMESTIC VOLUME-** The volume of domestic sales shall be calculated based on gross domestic volume.

(3) **MEASUREMENT-** For purposes of the calculations under this subsection and the certifications under subsection (h) by the Secretary, the volumes of domestic sales shall be measured by--

(A) in the case of cigarettes and cigars, the number of cigarettes and cigars; and

(B) in the case of the other classes of tobacco products specified in subsection (c)(1), in terms of number of pounds, or fraction thereof, of those products.

**(h) MEASUREMENT OF VOLUME OF DOMESTIC SALES-**

(1) **SUBMISSION OF INFORMATION-** Each manufacturer and importer of tobacco products shall submit to the Secretary a certified copy of each of the returns or forms described by paragraph (2) that are required to be filed with a Federal agency on the same date that those returns or forms are filed, or required to be filed, with the agency.

(2) **RETURNS AND FORMS-** The returns and forms described by this paragraph are those returns and forms that relate to--

(A) the removal of tobacco products into domestic commerce (as defined by section 5702 of the Internal Revenue Code of 1986); and

(B) the payment of the taxes imposed under chapter 52 of the Internal Revenue Code of 1986, including AFT Form 5000.24 and United States Customs Form 7501 under currently applicable regulations.

**(3) EFFECT OF FAILURE TO PROVIDE REQUIRED**

**INFORMATION-** Any person that knowingly fails to provide information required under this subsection or that provides false information under this subsection shall be subject to the penalties described in section 1003 of title 18, United States Code. The Secretary may also assess against the person a civil penalty in an amount not to exceed two percent of the value of the kind of tobacco products manufactured or imported by the person during the fiscal year in which the violation occurred, as determined by the Secretary.

**(i) CHALLENGE TO ASSESSMENT-**

(1) **APPEAL TO SECRETARY-** A manufacturer or importer subject to this section may contest an assessment imposed on the manufacturer or importer under this section by notifying the Secretary, not later than 30 business days after receiving the assessment notification required by

subsection (d), that the manufacturer or importer intends to contest the assessment.

(2) INFORMATION- Not later than 180 days after the date of the enactment of this title, the Secretary shall establish by regulation a procedure under which a manufacturer or importer contesting an assessment under this subsection may present information to the Secretary to demonstrate that the assessment applicable to the manufacturer or importer is incorrect. In challenging the assessment, the manufacturer or importer may use any information that is available, including third party data on industry or individual company sales volumes.

(3) REVISION- If a manufacturer or importer establishes that the initial determination of the amount of an assessment is incorrect, the Secretary shall revise the amount of the assessment so that the manufacturer or importer is required to pay only the amount correctly determined.

(4) TIME FOR REVIEW- Not later than 30 days after receiving notice from a manufacturer or importer under paragraph (1), the Secretary shall--

(A) decide whether the information provided to the Secretary under paragraph (2), and any other information that the Secretary determines is appropriate, is sufficient to establish that the original assessment was incorrect; and

(B) make any revisions necessary to ensure that each manufacturer and importer pays only its correct pro rata share of total gross domestic volume from all sources.

(5) IMMEDIATE PAYMENT OF UNDISPUTED AMOUNTS- The regulations promulgated by the Secretary under paragraph (2) shall provide for the immediate payment by a manufacturer or importer challenging an assessment of that portion of the assessment that is not in dispute. The manufacturer and importer may place into escrow, in accordance with such regulations, only the portion of the assessment being challenged in good faith pending final determination of the claim.

(j) JUDICIAL REVIEW-

(1) IN GENERAL- Any manufacturer or importer aggrieved by a determination of the Secretary with respect to the amount of any assessment may seek review of the determination in the United States District Court for the District of Columbia or for the district in which the manufacturer or importer resides or has its principal place of business at any time following exhaustion of the administrative remedies available under subsection (i).

(2) TIME LIMITS- Administrative remedies shall be deemed exhausted if no decision by the Secretary is made within the time limits established under subsection (i)(4).

(3) EXCESSIVE ASSESSMENTS- The court shall restrain collection of the excessive portion of any assessment or order a refund of excessive assessments already paid, along with interest calculated at the rate prescribed in section 3717 of title 31, United States Code, if it finds that

the Secretary's determination is not supported by a preponderance of the information available to the Secretary.

(k) TERMINATION DATE- The authority provided by this section to impose assessments terminates on September 30, 2014.

## **SEC. 626. TOBACCO TRUST FUND.**

(a) ESTABLISHMENT- There is established in the Commodity Credit Corporation a revolving trust fund, to be known as the 'Tobacco Trust Fund', which shall be used in carrying out this subtitle. The Tobacco Trust Fund shall consist of the following:

- (1) Assessments collected under section 625.
- (2) Such amounts as are necessary from the Commodity Credit Corporation.
- (3) Any interest earned on investment of amounts in the Tobacco Trust Fund under subsection (c).

(b) EXPENDITURES-

- (1) AUTHORIZED EXPENDITURES- Subject to paragraph (2), and notwithstanding any other provision of law, the Secretary shall use amounts in the Tobacco Trust Fund, in such amounts as the Secretary determines are necessary--
  - (A) to make payments under sections 622 and 623;
  - (B) to provide reimbursement under section 641(c);
  - (C) to reimburse the Commodity Credit Corporation for costs incurred by the Commodity Credit Corporation under paragraph (2); and
  - (D) to make payments to financial institutions to satisfy contractual obligations under section 622 or 623.
- (2) EXPENDITURES BY COMMODITY CREDIT CORPORATION- Notwithstanding any other provision of law, the Secretary shall use the funds, facilities, and authorities of the Commodity Credit Corporation to make payments described in paragraph (1). Not later than January 1, 2015, the Secretary shall use amounts in the Tobacco Trust Fund to fully reimburse, with interest, the Commodity Credit Corporation for all funds of the Commodity Credit Corporation expended under the authority of this paragraph. Administrative costs incurred by the Secretary or the Commodity Credit Corporation to carry out this title may not be paid using amounts in the Tobacco Trust Fund.

(c) INVESTMENT OF AMOUNTS-

- (1) IN GENERAL- The Commodity Credit Corporation shall invest such portion of the amounts in the Tobacco Trust Fund as are not, in the judgment of the Commodity Credit Corporation, required to meet current expenditures.
- (2) INTEREST-BEARING OBLIGATIONS- Investments may be made only in interest-bearing obligations of the United States.

(3) ACQUISITION OF OBLIGATIONS- For the purpose of investments under paragraph (1), obligations may be acquired--

(A) on original issue at the issue price; or

(B) by purchase of outstanding obligations at the market price.

(4) SALE OF OBLIGATIONS- Any obligation acquired by the Tobacco Trust Fund may be sold by the Commodity Credit Corporation at the market price.

(5) CREDITS TO FUND- The interest on, and the proceeds from the sale or redemption of, any obligations held in the Tobacco Trust Fund shall be credited to and form a part of the Fund.

## **SEC. 627. LIMITATION ON TOTAL EXPENDITURES.**

The total amount expended by the Secretary from the Tobacco Trust Fund to make payments under sections 622 and 623 and for the other authorized purposes of the Fund shall not exceed \$10,140,000,000.

### **Subtitle C-Implementation and Transition**

## **SEC. 641. TREATMENT OF TOBACCO LOAN POOL STOCKS AND OUTSTANDING LOAN COSTS.**

(a) DISPOSAL OF STOCKS- To provide for the orderly disposition of quota tobacco held by an association that has entered into a loan agreement with the Commodity Credit Corporation under section 106A or 106B of the Agricultural Act of 1949 (7 U.S.C. 1445-1, 1445-2) (referred to in this section as an 'association'), loan pool stocks for each kind of tobacco held by the association shall be disposed of in accordance with this section.

(b) DISPOSAL BY ASSOCIATIONS- For each kind of tobacco held by an association, the association shall be responsible for the disposal of a specific quantity of the loan pool stocks for that kind of tobacco held by the association. The quantity transferred to the association for disposal shall be equal to the quantity determined by dividing--

(1) the amount of funds held by the association in the No Net Cost Tobacco Fund and the No Net Cost Tobacco Account established under sections 106A and 106B of the Agricultural Act of 1949 (7 U.S.C. 1445-1, 1445-2) for the kind of tobacco; by

(2) the average list price per pound for the kind of tobacco, as determined by the Secretary.

(c) DISPOSAL OF REMAINDER BY COMMODITY CREDIT CORPORATION-

(1) DISPOSAL- Any loan pool stocks of a kind of tobacco of an association that are not transferred to the association under subsection (b) for disposal shall be disposed of by Commodity Credit Corporation in a manner determined by the Secretary.

(2) REIMBURSEMENT- As required by section 626(b)(1)(B), the Secretary shall transfer from the Tobacco Trust Fund to the No Net Cost Tobacco Fund or the No Net Cost Tobacco Account of an association established under section 106A or 106B of the Agricultural Act of 1949 (7 U.S.C. 1445-1, 1445-2) such amounts as the Secretary determines will be adequate to reimburse the Commodity Credit Corporation for any net losses that the Corporation may sustain under its loan agreements with the association.

(d) TRANSFER OF REMAINING NO NET COST FUNDS- Any funds in the No Net Cost Tobacco Fund or the No Net Cost Tobacco Account of an association established under sections 106A and 106B of the Agricultural Act of 1949 (7 U.S.C. 1445-1, 1445-2) that remain after the application of subsections (b) and (c) shall be transferred to the association for distribution to producers of quota tobacco in accordance with a plan approved by the Secretary.

## **SEC. 642. REGULATIONS.**

(a) IN GENERAL- The Secretary may promulgate such regulations as are necessary to implement this title and the amendments made by this title.

(b) PROCEDURE- The promulgation of the regulations and administration of this title and the amendments made by this title shall be made without regard to--

(1) the notice and comment provisions of section 553 of title 5, United States Code;

(2) the Statement of Policy of the Secretary of Agriculture effective July 24, 1971 (36 Fed. Reg. 13804), relating to notices of proposed rulemaking and public participation in rulemaking; and

(3) chapter 35 of title 44, United States Code (commonly known as the 'Paperwork Reduction Act').

(c) CONGRESSIONAL REVIEW OF AGENCY RULEMAKING- In carrying out this section, the Secretary shall use the authority provided under section 808 of title 5, United States Code.

## **SEC. 643. EFFECTIVE DATE.**

This title and the amendments made by this title shall apply to the 2005 and subsequent crops of each kind of tobacco.

## **TITLE VII--MISCELLANEOUS PROVISIONS**

### **SEC. 701. BROWNFIELDS DEMONSTRATION PROGRAM FOR QUALIFIED GREEN BUILDING AND SUSTAINABLE DESIGN PROJECTS.**

(a) TREATMENT AS EXEMPT FACILITY BOND- Subsection (a) of section 142 (relating to the definition of exempt facility bond) is amended by striking 'or' at the end of paragraph (12), by striking the period at the end of paragraph (13) and inserting ', or', and by inserting at the end the following new paragraph:

``(14) qualified green building and sustainable design projects.'.

(b) **QUALIFIED GREEN BUILDING AND SUSTAINABLE DESIGN PROJECTS-** Section 142 (relating to exempt facility bonds) is amended by adding at the end thereof the following new subsection:

``(1) **QUALIFIED GREEN BUILDING AND SUSTAINABLE DESIGN PROJECTS-**

``(1) **IN GENERAL-** For purposes of subsection (a)(14), the term `qualified green building and sustainable design project' means any project which is designated by the Secretary, after consultation with the Administrator of the Environmental Protection Agency, as a qualified green building and sustainable design project and which meets the requirements of clauses (i), (ii), (iii), and (iv) of paragraph (4)(A).

``(2) **DESIGNATIONS-**

``(A) **IN GENERAL-** Within 60 days after the end of the application period described in paragraph (3)(A), the Secretary, after consultation with the Administrator of the Environmental Protection Agency, shall designate qualified green building and sustainable design projects. At least one of the projects designated shall be located in, or within a 10-mile radius of, an empowerment zone as designated pursuant to section 1391, and at least one of the projects designated shall be located in a rural State. No more than one project shall be designated in a State. A project shall not be designated if such project includes a stadium or arena for professional sports exhibitions or games.

``(B) **MINIMUM CONSERVATION AND TECHNOLOGY INNOVATION**

**OBJECTIVES-** The Secretary, after consultation with the Administrator of the Environmental Protection Agency, shall ensure that, in the aggregate, the projects designated shall--

``(i) reduce electric consumption by more than 150 megawatts annually as compared to conventional generation,

``(ii) reduce daily sulfur dioxide emissions by at least 10 tons compared to coal generation power,

``(iii) expand by 75 percent the domestic solar photovoltaic market in the United States (measured in megawatts) as compared to the expansion of that market from 2001 to 2002, and

``(iv) use at least 25 megawatts of fuel cell energy generation.

``(3) **LIMITED DESIGNATIONS-** A project may not be designated under this subsection unless--

``(A) the project is nominated by a State or local government within 180 days of the enactment of this subsection, and

``(B) such State or local government provides written assurances that the project will satisfy the eligibility criteria described in paragraph (4).

``(4) **APPLICATION-**

``(A) **IN GENERAL-** A project may not be designated under this subsection unless the application for such designation includes a project proposal which describes the energy efficiency, renewable energy, and sustainable design features of the project and demonstrates that the project satisfies the following eligibility criteria:

``(i) **GREEN BUILDING AND SUSTAINABLE DESIGN-** At least 75 percent of the square footage of commercial buildings which are part of the project is registered for United States Green Building Council's LEED certification and is reasonably expected (at the time of the designation) to receive such certification. For purposes of determining

LEED certification as required under this clause, points shall be credited by using the following:

- ` (I) For wood products, certification under the Sustainable Forestry Initiative Program and the American Tree Farm System.
- ` (II) For renewable wood products, as credited for recycled content otherwise provided under LEED certification.
- ` (III) For composite wood products, certification under standards established by the American National Standards Institute, or such other voluntary standards as published in the Federal Register by the Administrator of the Environmental Protection Agency.
- ` (ii) BROWNFIELD REDEVELOPMENT- The project includes a brownfield site as defined by section 101(39) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (42 U.S.C. 9601), including a site described in subparagraph (D)(ii)(II)(aa) thereof.
- ` (iii) STATE AND LOCAL SUPPORT- The project receives specific State or local government resources which will support the project in an amount equal to at least \$5,000,000. For purposes of the preceding sentence, the term `resources' includes tax abatement benefits and contributions in kind.
- ` (iv) SIZE- The project includes at least one of the following:
  - ` (I) At least 1,000,000 square feet of building.
  - ` (II) At least 20 acres.
- ` (v) USE OF TAX BENEFIT- The project proposal includes a description of the net benefit of the tax-exempt financing provided under this subsection which will be allocated for financing of one or more of the following:
  - ` (I) The purchase, construction, integration, or other use of energy efficiency, renewable energy, and sustainable design features of the project.
  - ` (II) Compliance with certification standards cited under clause (i).
  - ` (III) The purchase, remediation, and foundation construction and preparation of the brownfields site.
- ` (vi) PROHIBITED FACILITIES- An issue shall not be treated as an issue described in subsection (a)(14) if any proceeds of such issue are used to provide any facility the principal business of which is the sale of food or alcoholic beverages for consumption on the premises.
- ` (vii) EMPLOYMENT- The project is projected to provide permanent employment of at least 1,500 full time equivalents (150 full time equivalents in rural States) when completed and construction employment of at least 1,000 full time equivalents (100 full time equivalents in rural States).  
The application shall include an independent analysis which describes the project's economic impact, including the amount of projected employment.

` (B) PROJECT DESCRIPTION- Each application described in subparagraph (A) shall contain for each project a description of-

- ` (i) the amount of electric consumption reduced as compared to conventional construction,
- ` (ii) the amount of sulfur dioxide daily emissions reduced compared to coal generation,
- ` (iii) the amount of the gross installed capacity of the project's solar photovoltaic capacity measured in megawatts, and
- ` (iv) the amount, in megawatts, of the project's fuel cell energy generation.

``(5) CERTIFICATION OF USE OF TAX BENEFIT- No later than 30 days after the completion of the project, each project must certify to the Secretary that the net benefit of the tax-exempt financing was used for the purposes described in paragraph (4).

``(6) DEFINITIONS- For purposes of this subsection--

``(A) RURAL STATE- The term `rural State' means any State which has--

``(i) a population of less than 4,500,000 according to the 2000 census,

``(ii) a population density of less than 150 people per square mile according to the 2000 census, and

``(iii) increased in population by less than half the rate of the national increase between the 1990 and 2000 censuses.

``(B) LOCAL GOVERNMENT- The term `local government' has the meaning given such term by section 1393(a)(5).

``(C) NET BENEFIT OF TAX-EXEMPT FINANCING- The term `net benefit of tax-exempt financing' means the present value of the interest savings (determined by a calculation established by the Secretary) which result from the tax-exempt status of the bonds.

``(7) AGGREGATE FACE AMOUNT OF TAX-EXEMPT FINANCING-

``(A) IN GENERAL- An issue shall not be treated as an issue described in subsection (a)(14) if the aggregate face amount of bonds issued by the State or local government pursuant thereto for a project (when added to the aggregate face amount of bonds previously so issued for such project) exceeds an amount designated by the Secretary as part of the designation.

``(B) LIMITATION ON AMOUNT OF BONDS- The Secretary may not allocate authority to issue qualified green building and sustainable design project bonds in an aggregate face amount exceeding \$2,000,000,000.

``(8) TERMINATION- Subsection (a)(14) shall not apply with respect to any bond issued after September 30, 2009.

``(9) TREATMENT OF CURRENT REFUNDING BONDS- Paragraphs (7)(B) and (8) shall not apply to any bond (or series of bonds) issued to refund a bond issued under subsection (a)(14) before October 1, 2009, if--

``(A) the average maturity date of the issue of which the refunding bond is a part is not later than the average maturity date of the bonds to be refunded by such issue,

``(B) the amount of the refunding bond does not exceed the outstanding amount of the refunded bond, and

``(C) the net proceeds of the refunding bond are used to redeem the refunded bond not later than 90 days after the date of the issuance of the refunding bond.

For purposes of subparagraph (A), average maturity shall be determined in accordance with section 147(b)(2)(A).'.

(c) EXEMPTION FROM GENERAL STATE VOLUME CAPS- Paragraph (3) of section 146(g) (relating to exception for certain bonds) is amended--

(1) by striking `or (13)' and inserting `(13), or (14)', and

(2) by striking `and qualified public educational facilities' and inserting `qualified public educational facilities, and qualified green building and sustainable design projects'.

(d) ACCOUNTABILITY- Each issuer shall maintain, on behalf of each project, an interest bearing reserve account equal to 1 percent of the net proceeds of any bond issued under this section for such project. Not later than 5 years after the date of issuance, the

Secretary of the Treasury, after consultation with the Administrator of the Environmental Protection Agency, shall determine whether the project financed with such bonds has substantially complied with the terms and conditions described in section 142(l)(4) of the Internal Revenue Code of 1986 (as added by this section). If the Secretary, after such consultation, certifies that the project has substantially complied with such terms and conditions and meets the commitments set forth in the application for such project described in section 142(l)(4) of such Code, amounts in the reserve account, including all interest, shall be released to the project. If the Secretary determines that the project has not substantially complied with such terms and conditions, amounts in the reserve account, including all interest, shall be paid to the United States Treasury.

(e) **EFFECTIVE DATE-** The amendments made by this section shall apply to bonds issued after December 31, 2004.

## **SEC. 702. EXCLUSION OF GAIN OR LOSS ON SALE OR EXCHANGE OF CERTAIN BROWNFIELD SITES FROM UNRELATED BUSINESS TAXABLE INCOME.**

(a) **IN GENERAL-** Subsection (b) of section 512 (relating to unrelated business taxable income) is amended by adding at the end the following new paragraph:

``(18) **TREATMENT OF GAIN OR LOSS ON SALE OR EXCHANGE OF CERTAIN BROWNFIELD SITES-**

``(A) **IN GENERAL-** Notwithstanding paragraph (5)(B), there shall be excluded any gain or loss from the qualified sale, exchange, or other disposition of any qualifying brownfield property by an eligible taxpayer.

``(B) **ELIGIBLE TAXPAYER-** For purposes of this paragraph--

``(i) **IN GENERAL-** The term `eligible taxpayer' means, with respect to a property, any organization exempt from tax under section 501(a) which--

``(I) acquires from an unrelated person a qualifying brownfield property, and

``(II) pays or incurs eligible remediation expenditures with respect to such property in an amount which exceeds the greater of \$550,000 or 12 percent of the fair market value of the property at the time such property was acquired by the eligible taxpayer, determined as if there was not a presence of a hazardous substance, pollutant, or contaminant on the property which is complicating the expansion, redevelopment, or reuse of the property.

``(ii) **EXCEPTION-** Such term shall not include any organization which is--

``(I) potentially liable under section 107 of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 with respect to the qualifying brownfield property,

``(II) affiliated with any other person which is so potentially liable through any direct or indirect familial relationship or any contractual, corporate, or financial relationship (other than a contractual, corporate, or financial relationship which is created by the instruments by which title to any qualifying brownfield property is conveyed or financed or by a contract of sale of goods or services), or

``(III) the result of a reorganization of a business entity which was so potentially liable.

``(C) **QUALIFYING BROWNFIELD PROPERTY-** For purposes of this paragraph--

``(i) **IN GENERAL-** The term `qualifying brownfield property' means any real property which is certified, before the taxpayer incurs any eligible remediation expenditures (other

than to obtain a Phase I environmental site assessment), by an appropriate State agency (within the meaning of section 198(c)(4)) in the State in which such property is located as a brownfield site within the meaning of section 101(39) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (as in effect on the date of the enactment of this paragraph).

``(ii) REQUEST FOR CERTIFICATION- Any request by an eligible taxpayer for a certification described in clause (i) shall include a sworn statement by the eligible taxpayer and supporting documentation of the presence of a hazardous substance, pollutant, or contaminant on the property which is complicating the expansion, redevelopment, or reuse of the property given the property's reasonably anticipated future land uses or capacity for uses of the property (including a Phase I environmental site assessment and, if applicable, evidence of the property's presence on a local, State, or Federal list of brownfields or contaminated property) and other environmental assessments prepared or obtained by the taxpayer.

``(D) QUALIFIED SALE, EXCHANGE, OR OTHER DISPOSITION- For purposes of this paragraph-

``(i) IN GENERAL- A sale, exchange, or other disposition of property shall be considered as qualified if--

``(I) such property is transferred by the eligible taxpayer to an unrelated person, and  
``(II) within 1 year of such transfer the eligible taxpayer has received a certification from the Environmental Protection Agency or an appropriate State agency (within the meaning of section 198(c)(4)) in the State in which such property is located that, as a result of the eligible taxpayer's remediation actions, such property would not be treated as a qualifying brownfield property in the hands of the transferee.

For purposes of subclause (II), before issuing such certification, the Environmental Protection Agency or appropriate State agency shall respond to comments received pursuant to clause (ii)(V) in the same form and manner as required under section 117(b) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (as in effect on the date of the enactment of this paragraph).

``(ii) REQUEST FOR CERTIFICATION- Any request by an eligible taxpayer for a certification described in clause (i) shall be made not later than the date of the transfer and shall include a sworn statement by the eligible taxpayer certifying the following:

``(I) Remedial actions which comply with all applicable or relevant and appropriate requirements (consistent with section 121(d) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980) have been substantially completed, such that there are no hazardous substances, pollutants, or contaminants which complicate the expansion, redevelopment, or reuse of the property given the property's reasonably anticipated future land uses or capacity for uses of the property.

``(II) The reasonably anticipated future land uses or capacity for uses of the property are more economically productive or environmentally beneficial than the uses of the property in existence on the date of the certification described in subparagraph (C)(i). For purposes of the preceding sentence, use of property as a landfill or other hazardous waste facility shall not be considered more economically productive or environmentally beneficial.

``(III) A remediation plan has been implemented to bring the property into compliance with all applicable local, State, and Federal environmental laws, regulations, and standards and to ensure that the remediation protects human health and the environment.

- ` (IV) The remediation plan described in subclause (III), including any physical improvements required to remediate the property, is either complete or substantially complete, and, if substantially complete, sufficient monitoring, funding, institutional controls, and financial assurances have been put in place to ensure the complete remediation of the property in accordance with the remediation plan as soon as is reasonably practicable after the sale, exchange, or other disposition of such property.
- ` (V) Public notice and the opportunity for comment on the request for certification was completed before the date of such request. Such notice and opportunity for comment shall be in the same form and manner as required for public participation required under section 117(a) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (as in effect on the date of the enactment of this paragraph). For purposes of this subclause, public notice shall include, at a minimum, publication in a major local newspaper of general circulation.
- ` (iii) ATTACHMENT TO TAX RETURNS- A copy of each of the requests for certification described in clause (ii) of subparagraph (C) and this subparagraph shall be included in the tax return of the eligible taxpayer (and, where applicable, of the qualifying partnership) for the taxable year during which the transfer occurs.
- ` (iv) SUBSTANTIAL COMPLETION- For purposes of this subparagraph, a remedial action is substantially complete when any necessary physical construction is complete, all immediate threats have been eliminated, and all long-term threats are under control.
- ` (E) ELIGIBLE REMEDIATION EXPENDITURES- For purposes of this paragraph--
  - ` (i) IN GENERAL- The term 'eligible remediation expenditures' means, with respect to any qualifying brownfield property, any amount paid or incurred by the eligible taxpayer to an unrelated third person to obtain a Phase I environmental site assessment of the property, and any amount so paid or incurred after the date of the certification described in subparagraph (C)(i) for goods and services necessary to obtain a certification described in subparagraph (D)(i) with respect to such property, including expenditures--
    - ` (I) to manage, remove, control, contain, abate, or otherwise remediate a hazardous substance, pollutant, or contaminant on the property,
    - ` (II) to obtain a Phase II environmental site assessment of the property, including any expenditure to monitor, sample, study, assess, or otherwise evaluate the release, threat of release, or presence of a hazardous substance, pollutant, or contaminant on the property,
    - ` (III) to obtain environmental regulatory certifications and approvals required to manage the remediation and monitoring of the hazardous substance, pollutant, or contaminant on the property, and
    - ` (IV) regardless of whether it is necessary to obtain a certification described in subparagraph (D)(i)(II), to obtain remediation cost-cap or stop-loss coverage, re-opener or regulatory action coverage, or similar coverage under environmental insurance policies, or financial guarantees required to manage such remediation and monitoring.
  - ` (ii) EXCEPTIONS- Such term shall not include--
    - ` (I) any portion of the purchase price paid or incurred by the eligible taxpayer to acquire the qualifying brownfield property,
    - ` (II) environmental insurance costs paid or incurred to obtain legal defense coverage, owner/operator liability coverage, lender liability coverage, professional liability coverage, or similar types of coverage,

- `(III) any amount paid or incurred to the extent such amount is reimbursed, funded, or otherwise subsidized by grants provided by the United States, a State, or a political subdivision of a State for use in connection with the property, proceeds of an issue of State or local government obligations used to provide financing for the property the interest of which is exempt from tax under section 103, or subsidized financing provided (directly or indirectly) under a Federal, State, or local program provided in connection with the property, or
- `(IV) any expenditure paid or incurred before the date of the enactment of this paragraph. For purposes of subclause (III), the Secretary may issue guidance regarding the treatment of government-provided funds for purposes of determining eligible remediation expenditures.
- `(F) DETERMINATION OF GAIN OR LOSS- For purposes of this paragraph, the determination of gain or loss shall not include an amount treated as gain which is ordinary income with respect to section 1245 or section 1250 property, including amounts deducted as section 198 expenses which are subject to the recapture rules of section 198(e), if the taxpayer had deducted such amounts in the computation of its unrelated business taxable income.
- `(G) SPECIAL RULES FOR PARTNERSHIPS-
  - `(i) IN GENERAL- In the case of an eligible taxpayer which is a partner of a qualifying partnership which acquires, remediates, and sells, exchanges, or otherwise disposes of a qualifying brownfield property, this paragraph shall apply to the eligible taxpayer's distributive share of the qualifying partnership's gain or loss from the sale, exchange, or other disposition of such property.
  - `(ii) QUALIFYING PARTNERSHIP- The term 'qualifying partnership' means a partnership which-
    - `(I) has a partnership agreement which satisfies the requirements of section 514(c)(9)(B)(vi) at all times beginning on the date of the first certification received by the partnership under subparagraph (C)(i),
    - `(II) satisfies the requirements of subparagraphs (B)(i), (C), (D), and (E), if 'qualified partnership' is substituted for 'eligible taxpayer' each place it appears therein (except subparagraph (D)(iii)), and
    - `(III) is not an organization which would be prevented from constituting an eligible taxpayer by reason of subparagraph (B)(ii).
  - `(iii) REQUIREMENT THAT TAX-EXEMPT PARTNER BE A PARTNER SINCE FIRST CERTIFICATION- This paragraph shall apply with respect to any eligible taxpayer which is a partner of a partnership which acquires, remediates, and sells, exchanges, or otherwise disposes of a qualifying brownfield property only if such eligible taxpayer was a partner of the qualifying partnership at all times beginning on the date of the first certification received by the partnership under subparagraph (C)(i) and ending on the date of the sale, exchange, or other disposition of the property by the partnership.
  - `(iv) REGULATIONS- The Secretary shall prescribe such regulations as are necessary to prevent abuse of the requirements of this subparagraph, including abuse through-
    - `(I) the use of special allocations of gains or losses, or
    - `(II) changes in ownership of partnership interests held by eligible taxpayers.
- `(H) SPECIAL RULES FOR MULTIPLE PROPERTIES-

- `**(i) IN GENERAL-** An eligible taxpayer or a qualifying partnership of which the eligible taxpayer is a partner may make a 1-time election to apply this paragraph to more than 1 qualifying brownfield property by averaging the eligible remediation expenditures for all such properties acquired during the election period. If the eligible taxpayer or qualifying partnership makes such an election, the election shall apply to all qualified sales, exchanges, or other dispositions of qualifying brownfield properties the acquisition and transfer of which occur during the period for which the election remains in effect.
- `**(ii) ELECTION-** An election under clause (i) shall be made with the eligible taxpayer's or qualifying partnership's timely filed tax return (including extensions) for the first taxable year for which the taxpayer or qualifying partnership intends to have the election apply. An election under clause (i) is effective for the period--
  - `**(I)** beginning on the date which is the first day of the taxable year of the return in which the election is included or a later day in such taxable year selected by the eligible taxpayer or qualifying partnership, and
  - `**(II)** ending on the date which is the earliest of a date of revocation selected by the eligible taxpayer or qualifying partnership, the date which is 8 years after the date described in subclause (I), or, in the case of an election by a qualifying partnership of which the eligible taxpayer is a partner, the date of the termination of the qualifying partnership.
- `**(iii) REVOCATION-** An eligible taxpayer or qualifying partnership may revoke an election under clause (i)(II) by filing a statement of revocation with a timely filed tax return (including extensions). A revocation is effective as of the first day of the taxable year of the return in which the revocation is included or a later day in such taxable year selected by the eligible taxpayer or qualifying partnership. Once an eligible taxpayer or qualifying partnership revokes the election, the eligible taxpayer or qualifying partnership is ineligible to make another election under clause (i) with respect to any qualifying brownfield property subject to the revoked election.
- `**(I) RECAPTURE-** If an eligible taxpayer excludes gain or loss from a sale, exchange, or other disposition of property to which an election under subparagraph (H) applies, and such property fails to satisfy the requirements of this paragraph, the unrelated business taxable income of the eligible taxpayer for the taxable year in which such failure occurs shall be determined by including any previously excluded gain or loss from such sale, exchange, or other disposition allocable to such taxpayer, and interest shall be determined at the overpayment rate established under section 6621 on any resulting tax for the period beginning with the due date of the return for the taxable year during which such sale, exchange, or other disposition occurred, and ending on the date of payment of the tax.
- `**(J) RELATED PERSONS-** For purposes of this paragraph, a person shall be treated as related to another person if--
  - `**(i)** such person bears a relationship to such other person described in section 267(b) (determined without regard to paragraph (9) thereof), or section 707(b)(1), determined by substituting '25 percent' for '50 percent' each place it appears therein, and
  - `**(ii)** in the case such other person is a nonprofit organization, if such person controls directly or indirectly more than 25 percent of the governing body of such organization.
- `**(K) TERMINATION-** Except for purposes of determining the average eligible remediation expenditures for properties acquired during the election period under

subparagraph (H), this paragraph shall not apply to any property acquired by the eligible taxpayer or qualifying partnership after December 31, 2009.'.

(b) EXCLUSION FROM DEFINITION OF DEBT-FINANCED PROPERTY- Section 514(b)(1) (defining debt-financed property) is amended by striking 'or' at the end of subparagraph (C), by striking the period at the end of subparagraph (D) and inserting `; or', and by inserting after subparagraph (D) the following new subparagraph:

`(E) any property the gain or loss from the sale, exchange, or other disposition of which would be excluded by reason of the provisions of section 512(b)(18) in computing the gross income of any unrelated trade or business.'

(c) SAVINGS CLAUSE- Nothing in the amendments made by this section shall affect any duty, liability, or other requirement imposed under any other Federal or State law. Notwithstanding section 128(b) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, a certification provided by the Environmental Protection Agency or an appropriate State agency (within the meaning of section 198(c)(4) of the Internal Revenue Code of 1986) shall not affect the liability of any person under section 107(a) of such Act.

(d) EFFECTIVE DATE- The amendments made by this section shall apply to any gain or loss on the sale, exchange, or other disposition of any property acquired by the taxpayer after December 31, 2004.

## **SEC. 703. CIVIL RIGHTS TAX RELIEF.**

(a) DEDUCTION ALLOWED WHETHER OR NOT TAXPAYER ITEMIZES OTHER DEDUCTIONS- Subsection (a) of section 62 (defining adjusted gross income) is amended by inserting after paragraph (18) the following new item:

`(19) COSTS INVOLVING DISCRIMINATION SUITS, ETC- Any deduction allowable under this chapter for attorney fees and court costs paid by, or on behalf of, the taxpayer in connection with any action involving a claim of unlawful discrimination (as defined in subsection (e)) or a claim of a violation of subchapter III of chapter 37 of title 31, United States Code or a claim made under section 1862(b)(3)(A) of the Social Security Act (42 U.S.C. 1395y(b)(3)(A)). The preceding sentence shall not apply to any deduction in excess of the amount includable in the taxpayer's gross income for the taxable year on account of a judgment or settlement (whether by suit or agreement and whether as lump sum or periodic payments) resulting from such claim.'

(b) UNLAWFUL DISCRIMINATION DEFINED- Section 62 is amended by adding at the end the following new subsection:

`(e) UNLAWFUL DISCRIMINATION DEFINED- For purposes of subsection (a)(19), the term 'unlawful discrimination' means an act that is unlawful under any of the following:

`(1) Section 302 of the Civil Rights Act of 1991 (2 U.S.C. 1202).

`(2) Section 201, 202, 203, 204, 205, 206, or 207 of the Congressional Accountability Act of 1995 (2 U.S.C. 1311, 1312, 1313, 1314, 1315, 1316, or 1317).

`(3) The National Labor Relations Act (29 U.S.C. 151 et seq.).

`(4) The Fair Labor Standards Act of 1938 (29 U.S.C. 201 et seq.).

`(5) Section 4 or 15 of the Age Discrimination in Employment Act of 1967 (29 U.S.C. 623 or 633a).

- ` (6) Section 501 or 504 of the Rehabilitation Act of 1973 (29 U.S.C. 791 or 794).
- ` (7) Section 510 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1140).
- ` (8) Title IX of the Education Amendments of 1972 (20 U.S.C. 1681 et seq.).
- ` (9) The Employee Polygraph Protection Act of 1988 (29 U.S.C. 2001 et seq.).
- ` (10) The Worker Adjustment and Retraining Notification Act (29 U.S.C. 2102 et seq.).
- ` (11) Section 105 of the Family and Medical Leave Act of 1993 (29 U.S.C. 2615).
- ` (12) Chapter 43 of title 38, United States Code (relating to employment and reemployment rights of members of the uniformed services).
- ` (13) Section 1977, 1979, or 1980 of the Revised Statutes (42 U.S.C. 1981, 1983, or 1985).
- ` (14) Section 703, 704, or 717 of the Civil Rights Act of 1964 (42 U.S.C. 2000e-2, 2000e-3, or 2000e-16).
- ` (15) Section 804, 805, 806, 808, or 818 of the Fair Housing Act (42 U.S.C. 3604, 3605, 3606, 3608, or 3617).
- ` (16) Section 102, 202, 302, or 503 of the Americans with Disabilities Act of 1990 (42 U.S.C. 12112, 12132, 12182, or 12203).
- ` (17) Any provision of Federal law (popularly known as whistleblower protection provisions) prohibiting the discharge of an employee, the discrimination against an employee, or any other form of retaliation or reprisal against an employee for asserting rights or taking other actions permitted under Federal law.
- ` (18) Any provision of Federal, State, or local law, or common law claims permitted under Federal, State, or local law--
  - ` (i) providing for the enforcement of civil rights, or
  - ` (ii) regulating any aspect of the employment relationship, including claims for wages, compensation, or benefits, or prohibiting the discharge of an employee, the discrimination against an employee, or any other form of retaliation or reprisal against an employee for asserting rights or taking other actions permitted by law.'

(c) EFFECTIVE DATE- The amendments made by this section shall apply to fees and costs paid after the date of the enactment of this Act with respect to any judgment or settlement occurring after such date.

## **SEC. 704. MODIFICATION OF CLASS LIFE FOR CERTAIN TRACK FACILITIES.**

- (a) 7-YEAR PROPERTY- Subparagraph (C) of section 168(e)(3) (relating to classification of certain property) is amended by redesignating clause (ii) as clause (iii) and by inserting after clause (i) the following new clause:
  - ` (ii) any motorsports entertainment complex, and'.
- (b) DEFINITION- Section 168(i) (relating to definitions and special rules) is amended by adding at the end the following new paragraph:
  - ` (15) MOTORSPORTS ENTERTAINMENT COMPLEX-
- ` (A) IN GENERAL- The term `motorsports entertainment complex' means a racing track facility which--
  - ` (i) is permanently situated on land, and

`(ii) during the 36-month period following the first day of the month in which the asset is placed in service, hosts 1 or more racing events for automobiles (of any type), trucks, or motorcycles which are open to the public for the price of admission.

`(B) ANCILLARY AND SUPPORT FACILITIES- Such term shall include, if owned by the taxpayer who owns the complex and provided for the benefit of patrons of the complex--

`(i) ancillary facilities and land improvements in support of the complex's activities (including parking lots, sidewalks, waterways, bridges, fences, and landscaping),

`(ii) support facilities (including food and beverage retailing, souvenir vending, and other nonlodging accommodations), and

`(iii) appurtenances associated with such facilities and related attractions and amusements (including ticket booths, race track surfaces, suites and hospitality facilities, grandstands and viewing structures, props, walls, facilities that support the delivery of entertainment services, other special purpose structures, facades, shop interiors, and buildings).

`(C) EXCEPTION- Such term shall not include any transportation equipment, administrative services assets, warehouses, administrative buildings, hotels, or motels.

`(D) TERMINATION- This paragraph shall not apply to any property placed in service after December 31, 2007.'

(c) EFFECTIVE DATE-

(1) IN GENERAL- The amendments made by this section shall apply to any property placed in service after the date of the enactment of this Act.

(2) SPECIAL RULE FOR ASSET CLASS 80.0- In the case of race track facilities placed in service after the date of the enactment of this Act, such facilities shall not be treated as theme and amusement facilities classified under asset class 80.0.

(3) NO INFERENCE- Nothing in this section or the amendments made by this section shall be construed to affect the treatment of property placed in service on or before the date of the enactment of this Act.

## **SEC. 705. SUSPENSION OF POLICYHOLDERS SURPLUS ACCOUNT PROVISIONS.**

(a) Distributions To Shareholders From Pre-1984 Policyholders Surplus Account- Section 815 (relating to distributions to shareholders from pre-1984 policyholders surplus account) is amended by adding at the end the following:

`(g) Special Rules Applicable During 2005 and 2006- In the case of any taxable year of a stock life insurance company beginning after December 31, 2004, and before January 1, 2007--

`(1) the amount under subsection (a)(2) for such taxable year shall be treated as zero, and

`(2) notwithstanding subsection (b), in determining any subtractions from an account under subsections (c)(3) and (d)(3), any distribution to shareholders during such taxable year shall be treated as made first out of the policyholders surplus account, then out of the shareholders surplus account, and finally out of other accounts.'

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

## **SEC. 706. CERTAIN ALASKA NATURAL GAS PIPELINE PROPERTY TREATED AS 7-YEAR PROPERTY.**

(a) IN GENERAL- Section 168(e)(3)(C) (defining 7-year property), as amended by this Act, is amended by striking `and' at the end of clause (ii), by redesignating clause (iii) as clause (iv), and by inserting after clause (ii) the following new clause:

`(iii) any Alaska natural gas pipeline, and'.

(b) ALASKA NATURAL GAS PIPELINE- Section 168(i) (relating to definitions and special rules), as amended by this Act, is amended by inserting after paragraph (15) the following new paragraph:

`(16) ALASKA NATURAL GAS PIPELINE- The term `Alaska natural gas pipeline' means the natural gas pipeline system located in the State of Alaska which--

`(A) has a capacity of more than 500,000,000,000 Btu of natural gas per day, and

`(B) is--

`(i) placed in service after December 31, 2013, or

`(ii) treated as placed in service on January 1, 2014, if the taxpayer who places such system in service before January 1, 2014, elects such treatment.

Such term includes the pipe, trunk lines, related equipment, and appurtenances used to carry natural gas, but does not include any gas processing plant.'

(c) ALTERNATIVE SYSTEM- The table contained in section 168(g)(3)(B) (relating to special rule for certain property assigned to classes) is amended by inserting after the item relating to subparagraph (C)(ii) the following new item:

`(C)(iii)

--22'.

(d) EFFECTIVE DATE- The amendments made by this section shall apply to property placed in service after December 31, 2004.

## **SEC. 707. EXTENSION OF ENHANCED OIL RECOVERY CREDIT TO CERTAIN ALASKA FACILITIES.**

(a) IN GENERAL- Section 43(c)(1) (defining qualified enhanced oil recovery costs) is amended by adding at the end the following new subparagraph:

`(D) Any amount which is paid or incurred during the taxable year to construct a gas treatment plant which--

`(i) is located in the area of the United States (within the meaning of section 638(1)) lying north of 64 degrees North latitude,

`(ii) prepares Alaska natural gas for transportation through a pipeline with a capacity of at least 2,000,000,000,000 Btu of natural gas per day, and

`(iii) produces carbon dioxide which is injected into hydrocarbon-bearing geological formations.'

(b) ALASKA NATURAL GAS- Section 43(c) is amended by adding at the end the following new paragraph:

`(5) ALASKA NATURAL GAS- For purposes of paragraph (1)(D)--

``(1) IN GENERAL- The term `Alaska natural gas' means natural gas entering the Alaska natural gas pipeline (as defined in section 168(i)(16) (determined without regard to subparagraph (B) thereof) which is produced from a well--  
``(A) located in the area of the State of Alaska lying north of 64 degrees North latitude, determined by excluding the area of the Alaska National Wildlife Refuge (including the continental shelf thereof within the meaning of section 638(1)), and  
``(B) pursuant to the applicable State and Federal pollution prevention, control, and permit requirements from such area (including the continental shelf thereof within the meaning of section 638(1)).  
``(2) NATURAL GAS- The term `natural gas' has the meaning given such term by section 613A(e)(2).'.  
(c) EFFECTIVE DATE- The amendment made by this section shall apply to costs paid or incurred in taxable years beginning after December 31, 2004.

## **SEC. 708. METHOD OF ACCOUNTING FOR NAVAL SHIPBUILDERS.**

(a) IN GENERAL- In the case of a qualified naval ship contract, the taxable income of such contract during the 5-taxable year period beginning with the taxable year in which the contract commencement date occurs shall be determined under a method identical to the method used in the case of a qualified ship contract (as defined in section 10203(b)(2)(B) of the Revenue Act of 1987).  
(b) RECAPTURE OF TAX BENEFIT- In the case of a qualified naval ship contract to which subsection (a) applies, the taxpayer's tax imposed by chapter 1 of the Internal Revenue Code of 1986 for the first taxable year following the 5-taxable year period described in subsection (a) shall be increased by the excess (if any) of-  
(1) the amount of tax which would have been imposed during such period if this section had not been enacted, over  
(2) the amount of tax so imposed during such period.  
(c) QUALIFIED NAVAL SHIP CONTRACT- For purposes of this section:  
(1) IN GENERAL- The term `qualified naval ship contract' means any contract or portion thereof that is for the construction in the United States of 1 ship or submarine for the Federal Government if the taxpayer reasonably expects the acceptance date will occur no later than 9 years after the construction commencement date.  
(2) ACCEPTANCE DATE- The term `acceptance date' means the date 1 year after the date on which the Federal Government issues a letter of acceptance or other similar document for the ship or submarine.  
(3) CONSTRUCTION COMMENCEMENT DATE- The term `construction commencement date' means the date on which the physical fabrication of any section or component of the ship or submarine begins in the taxpayer's shipyard.  
(d) EFFECTIVE DATE- This section shall apply to contracts for ships or submarines with respect to which the construction commencement date occurs after the date of the enactment of this Act.

## **SEC. 709. MODIFICATION OF MINIMUM COST REQUIREMENT FOR TRANSFER OF EXCESS PENSION ASSETS.**

(a) AMENDMENTS OF ERISA-

- (1) Section 101(e)(3) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1021(e)(3)) is amended by striking 'Pension Funding Equity Act of 2004' and inserting 'American Jobs Creation Act of 2004'.
- (2) Section 403(c)(1) of such Act (29 U.S.C. 1103(c)(1)) is amended by striking 'Pension Funding Equity Act of 2004' and inserting 'American Jobs Creation Act of 2004'.
- (3) Paragraph (13) of section 408(b) of such Act (29 U.S.C. 1108(b)(3)) is amended by striking 'Pension Funding Equity Act of 2004' and inserting 'American Jobs Creation Act of 2004'.

(b) MINIMUM COST REQUIREMENTS -

- (1) IN GENERAL- Section 420(c)(3)(E) is amended by adding at the end the following new clause:

  `(ii) INSIGNIFICANT COST REDUCTIONS PERMITTED-

    `(I) IN GENERAL- An eligible employer shall not be treated as failing to meet the requirements of this paragraph for any taxable year if, in lieu of any reduction of retiree health coverage permitted under the regulations prescribed under clause (i), the employer reduces applicable employer cost by an amount not in excess of the reduction in costs which would have occurred if the employer had made the maximum permissible reduction in retiree health coverage under such regulations. In applying such regulations to any subsequent taxable year, any reduction in applicable employer cost under this clause shall be treated as if it were an equivalent reduction in retiree health coverage.

    `(II) ELIGIBLE EMPLOYER- For purposes of subclause (I), an employer shall be treated as an eligible employer for any taxable year if, for the preceding taxable year, the qualified current retiree health liabilities of the employer were at least 5 percent of the gross receipts of the employer. For purposes of this subclause, the rules of paragraphs (2), (3)(B), and (3)(C) of section 448(c) shall apply in determining the amount of an employer's gross receipts.'

- (2) CONFORMING AMENDMENT- Section 420(c)(3)(E) is amended by striking 'The Secretary' and inserting:

  `(i) IN GENERAL- The Secretary'.

  (3) EFFECTIVE DATE- The amendments made by this subsection shall apply to taxable years ending after the date of the enactment of this Act.

## **SEC. 710. EXPANSION OF CREDIT FOR ELECTRICITY PRODUCED FROM CERTAIN RENEWABLE RESOURCES.**

(a) EXPANSION OF QUALIFIED ENERGY RESOURCES- Subsection (c) of section 45 (relating to electricity produced from certain renewable resources) is amended to read as follows:

  `(c) QUALIFIED ENERGY RESOURCES AND REFINED COAL- For purposes of this section:

- `(1) IN GENERAL- The term 'qualified energy resources' means--
  - `(A) wind,
  - `(B) closed-loop biomass,
  - `(C) open-loop biomass,
  - `(D) geothermal energy,

``(E) solar energy,

``(F) small irrigation power, and

``(G) municipal solid waste.

``(2) CLOSED-LOOP BIOMASS- The term `closed-loop biomass' means any organic material from a plant which is planted exclusively for purposes of being used at a qualified facility to produce electricity.

``(3) OPEN-LOOP BIOMASS-

``(A) IN GENERAL- The term `open-loop biomass' means--

``(i) any agricultural livestock waste nutrients, or

``(ii) any solid, nonhazardous, cellulosic waste material which is segregated from other waste materials and which is derived from--

``(I) any of the following forest-related resources: mill and harvesting residues, precommercial thinnings, slash, and brush,

``(II) solid wood waste materials, including waste pallets, crates, dunnage, manufacturing and construction wood wastes (other than pressure-treated, chemically-treated, or painted wood wastes), and landscape or right-of-way tree trimmings, but not including municipal solid waste, gas derived from the biodegradation of solid waste, or paper which is commonly recycled, or

``(III) agriculture sources, including orchard tree crops, vineyard, grain, legumes, sugar, and other crop by-products or residues.

Such term shall not include closed-loop biomass or biomass burned in conjunction with fossil fuel (cofiring) beyond such fossil fuel required for startup and flame stabilization.

``(B) AGRICULTURAL LIVESTOCK WASTE NUTRIENTS-

``(i) IN GENERAL- The term `agricultural livestock waste nutrients' means agricultural livestock manure and litter, including wood shavings, straw, rice hulls, and other bedding material for the disposition of manure.

``(ii) AGRICULTURAL LIVESTOCK- The term `agricultural livestock' includes bovine, swine, poultry, and sheep.

``(4) GEOTHERMAL ENERGY- The term `geothermal energy' means energy derived from a geothermal deposit (within the meaning of section 613(e)(2)).

``(5) SMALL IRRIGATION POWER- The term `small irrigation power' means power--

``(A) generated without any dam or impoundment of water through an irrigation system canal or ditch, and

``(B) the nameplate capacity rating of which is not less than 150 kilowatts but is less than 5 megawatts.

``(6) MUNICIPAL SOLID WASTE- The term `municipal solid waste' has the meaning given the term `solid waste' under section 2(27) of the Solid Waste Disposal Act (42 U.S.C. 6903).

``(7) REFINED COAL-

``(A) IN GENERAL- The term `refined coal' means a fuel which--

``(i) is a liquid, gaseous, or solid synthetic fuel produced from coal (including lignite) or high carbon fly ash, including such fuel used as a feedstock,

``(ii) is sold by the taxpayer with the reasonable expectation that it will be used for purpose of producing steam,

``(iii) is certified by the taxpayer as resulting (when used in the production of steam) in a qualified emission reduction, and

``(iv) is produced in such a manner as to result in an increase of at least 50 percent in the market value of the refined coal (excluding any increase caused by materials combined or added during the production process), as compared to the value of the feedstock coal.

``(B) QUALIFIED EMISSION REDUCTION- The term `qualified emission reduction' means a reduction of at least 20 percent of the emissions of nitrogen oxide and either sulfur dioxide or mercury released when burning the refined coal (excluding any dilution caused by materials combined or added during the production process), as compared to the emissions released when burning the feedstock coal or comparable coal predominantly available in the marketplace as of January 1, 2003.'

(b) EXPANSION OF QUALIFIED FACILITIES-

(1) IN GENERAL- Section 45 is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

``(d) QUALIFIED FACILITIES- For purposes of this section:

``(1) WIND FACILITY- In the case of a facility using wind to produce electricity, the term `qualified facility' means any facility owned by the taxpayer which is originally placed in service after December 31, 1993, and before January 1, 2006.

``(2) CLOSED-LOOP BIOMASS FACILITY-

``(A) IN GENERAL- In the case of a facility using closed-loop biomass to produce electricity, the term `qualified facility' means any facility--

``(i) owned by the taxpayer which is originally placed in service after December 31, 1992, and before January 1, 2006, or

``(ii) owned by the taxpayer which before January 1, 2006, is originally placed in service and modified to use closed-loop biomass to co-fire with coal, with other biomass, or with both, but only if the modification is approved under the Biomass Power for Rural Development Programs or is part of a pilot project of the Commodity Credit Corporation as described in 65 Fed. Reg. 63052.

``(B) SPECIAL RULES- In the case of a qualified facility described in subparagraph (A)(ii)--

``(i) the 10-year period referred to in subsection (a) shall be treated as beginning no earlier than the date of the enactment of this clause,

``(ii) the amount of the credit determined under subsection (a) with respect to the facility shall be an amount equal to the amount determined without regard to this clause multiplied by the ratio of the thermal content of the closed-loop biomass used in such facility to the thermal content of all fuels used in such facility, and

``(iii) if the owner of such facility is not the producer of the electricity, the person eligible for the credit allowable under subsection (a) shall be the lessee or the operator of such facility.

``(3) OPEN-LOOP BIOMASS FACILITIES-

``(A) IN GENERAL- In the case of a facility using open-loop biomass to produce electricity, the term `qualified facility' means any facility owned by the taxpayer which--

``(i) in the case of a facility using agricultural livestock waste nutrients--

``(I) is originally placed in service after the date of the enactment of this subclause and before January 1, 2006, and

``(II) the nameplate capacity rating of which is not less than 150 kilowatts, and

``(ii) in the case of any other facility, is originally placed in service before January 1, 2006.

``(B) CREDIT ELIGIBILITY- In the case of any facility described in subparagraph (A), if the owner of such facility is not the producer of the electricity, the person eligible for the credit allowable under subsection (a) shall be the lessee or the operator of such facility.

``(4) GEOTHERMAL OR SOLAR ENERGY FACILITY- In the case of a facility using geothermal or solar energy to produce electricity, the term `qualified facility' means any facility owned by the taxpayer which is originally placed in service after the date of the enactment of this paragraph and before January 1, 2006. Such term shall not include any property described in section 48(a)(3) the basis of which is taken into account by the taxpayer for purposes of determining the energy credit under section 48.

``(5) SMALL IRRIGATION POWER FACILITY- In the case of a facility using small irrigation power to produce electricity, the term `qualified facility' means any facility owned by the taxpayer which is originally placed in service after the date of the enactment of this paragraph and before January 1, 2006.

``(6) LANDFILL GAS FACILITIES- In the case of a facility producing electricity from gas derived from the biodegradation of municipal solid waste, the term `qualified facility' means any facility owned by the taxpayer which is originally placed in service after the date of the enactment of this paragraph and before January 1, 2006.

``(7) TRASH COMBUSTION FACILITIES- In the case of a facility which burns municipal solid waste to produce electricity, the term `qualified facility' means any facility owned by the taxpayer which is originally placed in service after the date of the enactment of this paragraph and before January 1, 2006.

``(8) REFINED COAL PRODUCTION FACILITY- The term `refined coal production facility' means a facility which is placed in service after the date of the enactment of this paragraph and before January 1, 2009.'

(2) RULES FOR REFINED COAL PRODUCTION FACILITIES- Subsection (e) of section 45, as so redesignated, is amended by adding at the end the following new paragraph:

``(8) REFINED COAL PRODUCTION FACILITIES-

``(A) DETERMINATION OF CREDIT AMOUNT- In the case of a producer of refined coal, the credit determined under this section (without regard to this paragraph) for any taxable year shall be increased by an amount equal to \$4.375 per ton of qualified refined coal-

``(i) produced by the taxpayer at a refined coal production facility during the 10-year period beginning on the date the facility was originally placed in service, and

``(ii) sold by the taxpayer-

``(I) to an unrelated person, and

``(II) during such 10-year period and such taxable year.

``(B) PHASEOUT OF CREDIT- The amount of the increase determined under subparagraph (A) shall be reduced by an amount which bears the same ratio to the amount of the increase (determined without regard to this subparagraph) as--

``(i) the amount by which the reference price of fuel used as a feedstock (within the meaning of subsection (c)(7)(A)) for the calendar year in which the sale occurs exceeds an amount equal to 1.7 multiplied by the reference price for such fuel in 2002, bears to

``(ii) \$8.75.

``(C) APPLICATION OF RULES- Rules similar to the rules of the subsection (b)(3) and paragraphs (1) through (5) and (9) of this subsection shall apply for purposes of determining the amount of any increase under this paragraph.'.

(3) CONFORMING AMENDMENTS-

(A) Section 45(e), as so redesignated, is amended by striking `subsection (c)(3)(A)' in paragraph (7)(A)(i) and inserting `subsection (d)(1)'.

(B) The heading of section 45 and the item relating to such section in the table of sections for subpart D of part IV of subchapter A of chapter 1 are each amended by inserting before the period at the end `, etc'.

(C) Paragraph (2) of section 45(b) is amended by striking `The 1.5 cent amount' and all that follows through `paragraph (1)' and inserting `The 1.5 cent amount in subsection (a), the 8 cent amount in paragraph (1), the \$4.375 amount in subsection (e)(8)(A), and in subsection (e)(8)(B)(i) the reference price of fuel used as a feedstock (within the meaning of subsection (c)(7)(A)) in 2002'.

(c) SPECIAL CREDIT RATE AND PERIOD FOR ELECTRICITY PRODUCED AND SOLD AFTER ENACTMENT DATE- Section 45(b) is amended by adding at the end the following new paragraph:

``(4) CREDIT RATE AND PERIOD FOR ELECTRICITY PRODUCED AND SOLD FROM CERTAIN FACILITIES-

``(A) CREDIT RATE- In the case of electricity produced and sold in any calendar year after 2003 at any qualified facility described in paragraph (3), (5), (6), or (7) of subsection (d), the amount in effect under subsection (a)(1) for such calendar year (determined before the application of the last sentence of paragraph (2) of this subsection) shall be reduced by one-half.

``(B) CREDIT PERIOD-

``(i) IN GENERAL- Except as provided in clause (ii), in the case of any facility described in paragraph (3), (4), (5), (6), or (7) of subsection (d), the 5-year period beginning on the date the facility was originally placed in service shall be substituted for the 10-year period in subsection (a)(2)(A)(ii).

``(ii) CERTAIN OPEN-LOOP BIOMASS FACILITIES- In the case of any facility described in subsection (d)(3)(A)(ii) placed in service before the date of the enactment of this paragraph, the 5-year period beginning on the date of the enactment of this Act shall be substituted for the 10-year period in subsection (a)(2)(A)(ii).'

(d) COORDINATION WITH OTHER CREDITS- Section 45(e), as redesignated and amended by this section, is amended by inserting after paragraph (8) the following new paragraph:

``(9) COORDINATION WITH CREDIT FOR PRODUCING FUEL FROM A NONCONVENTIONAL SOURCE- The term `qualified facility' shall not include any facility the production from which is allowed as a credit under section 29 for the taxable year or any prior taxable year.'

(e) COORDINATION WITH SECTION 48- Section 48(a)(3) (defining energy property) is amended by adding at the end the following new sentence: `Such term shall not include any property which is part of a facility the production from which is allowed as a credit under section 45 for the taxable year or any prior taxable year.'

(f) ELIMINATION OF CERTAIN CREDIT REDUCTIONS- Section 45(b)(3) (relating to credit reduced for grants, tax-exempt bonds, subsidized energy financing, and other credits) is amended--

- (1) by inserting 'the lesser of 1/2 or' before 'a fraction' in the matter preceding subparagraph (A), and
- (2) by adding at the end the following new sentence: 'This paragraph shall not apply with respect to any facility described in subsection (d)(2)(A)(ii).'

(g) EFFECTIVE DATES-

- (1) IN GENERAL- Except as otherwise provided in this subsection, the amendments made by this section shall apply to electricity produced and sold after the date of the enactment of this Act, in taxable years ending after such date.
- (2) CERTAIN BIOMASS FACILITIES- With respect to any facility described in section 45(d)(3)(A)(ii) of the Internal Revenue Code of 1986, as added by subsection (b)(1), which is placed in service before the date of the enactment of this Act, the amendments made by this section shall apply to electricity produced and sold after December 31, 2004, in taxable years ending after such date.
- (3) CREDIT RATE AND PERIOD FOR NEW FACILITIES- The amendments made by subsection (c) shall apply to electricity produced and sold after December 31, 2004, in taxable years ending after such date.
- (4) NONAPPLICATION OF AMENDMENTS TO PREEFFECTIVE DATE POULTRY WASTE FACILITIES- The amendments made by this section shall not apply with respect to any poultry waste facility (within the meaning of section 45(c)(3)(C), as in effect on the day before the date of the enactment of this Act) placed in service before January 1, 2004.
- (5) REFINED COAL PRODUCTION FACILITIES- Section 45(e)(8) of the Internal Revenue Code of 1986, as added by this section, shall apply to refined coal produced and sold after the date of the enactment of this Act.

## **SEC. 711. CERTAIN BUSINESS RELATED CREDITS ALLOWED AGAINST REGULAR AND MINIMUM TAX.**

(a) IN GENERAL- Subsection (c) of section 38 (relating to limitation based on amount of tax) is amended by redesignating paragraph (4) as paragraph (5) and by inserting after paragraph (3) the following new paragraph:

``(4) SPECIAL RULES FOR SPECIFIED CREDITS-

``(A) IN GENERAL- In the case of specified credits--

- ``(i) this section and section 39 shall be applied separately with respect to such credits, and
- ``(ii) in applying paragraph (1) to such credits--

``(I) the tentative minimum tax shall be treated as being zero, and

``(II) the limitation under paragraph (1) (as modified by subclause (I)) shall be reduced by the credit allowed under subsection (a) for the taxable year (other than the specified credits).

``(B) SPECIFIED CREDITS- For purposes of this subsection, the term 'specified credits' includes--

- ``(i) for taxable years beginning after December 31, 2004, the credit determined under section 40,

- ``(ii) the credit determined under section 45 to the extent that such credit is attributable to electricity or refined coal produced--
- ``(I) at a facility which is originally placed in service after the date of the enactment of this paragraph, and
- ``(II) during the 4-year period beginning on the date that such facility was originally placed in service'.
- (b) CONFORMING AMENDMENTS- Paragraph (2)(A)(ii)(II) and (3)(A)(ii)(II) of section 38(c) are each amended by inserting `or the specified credits' after `employee credit'.
- (c) EFFECTIVE DATE- Except as otherwise provided, the amendments made by this section shall apply to taxable years ending after the date of the enactment of this Act.

## **SEC. 712. INCLUSION OF PRIMARY AND SECONDARY MEDICAL STRATEGIES FOR CHILDREN AND ADULTS WITH SICKLE CELL DISEASE AS MEDICAL ASSISTANCE UNDER THE MEDICAID PROGRAM.**

- (a) OPTIONAL MEDICAL ASSISTANCE-
- (1) IN GENERAL- Section 1905 of the Social Security Act (42 U.S.C. 1396d) is amended--
  - (A) in subsection (a)--
    - (i) by striking `and' at the end of paragraph (26);
    - (ii) by redesignating paragraph (27) as paragraph (28); and
    - (iii) by inserting after paragraph (26), the following:
      - ``(27) subject to subsection (x), primary and secondary medical strategies and treatment and services for individuals who have Sickle Cell Disease; and'; and
  - (B) by adding at the end the following:
    - ``(x) For purposes of subsection (a)(27), the strategies, treatment, and services described in that subsection include the following:
      - ``(1) Chronic blood transfusion (with deferoxamine chelation) to prevent stroke in individuals with Sickle Cell Disease who have been identified as being at high risk for stroke.
      - ``(2) Genetic counseling and testing for individuals with Sickle Cell Disease or the sickle cell trait to allow health care professionals to treat such individuals and to prevent symptoms of Sickle Cell Disease.
      - ``(3) Other treatment and services to prevent individuals who have Sickle Cell Disease and who have had a stroke from having another stroke.'
- (2) RULE OF CONSTRUCTION- Nothing in subsections (a)(27) or (x) of section 1905 of the Social Security Act (42 U.S.C. 1396d), as added by paragraph (1), shall be construed as implying that a State medicaid program under title XIX of such Act could not have treated, prior to the date of enactment of this Act, any of the primary and secondary medical strategies and treatment and services described in such subsections as medical assistance under such program, including as early and periodic screening, diagnostic, and treatment services under section 1905(r) of such Act.
- (b) FEDERAL REIMBURSEMENT FOR EDUCATION AND OTHER SERVICES RELATED TO THE PREVENTION AND TREATMENT OF SICKLE CELL

DISEASE- Section 1903(a)(3) of the Social Security Act (42 U.S.C. 1396b(a)(3)) is amended--

- (1) in subparagraph (D), by striking 'plus' at the end and inserting 'and'; and
- (2) by adding at the end the following:

``(E) 50 percent of the sums expended with respect to costs incurred during such quarter as are attributable to providing--

``(i) services to identify and educate individuals who are likely to be eligible for medical assistance under this title and who have Sickle Cell Disease or who are carriers of the sickle cell gene, including education regarding how to identify such individuals; or

``(ii) education regarding the risks of stroke and other complications, as well as the prevention of stroke and other complications, in individuals who are likely to be eligible for medical assistance under this title and who have Sickle Cell Disease; plus'.

**(c) DEMONSTRATION PROGRAM FOR THE DEVELOPMENT AND ESTABLISHMENT OF SYSTEMIC MECHANISMS FOR THE PREVENTION AND TREATMENT OF SICKLE CELL DISEASE-**

**(1) AUTHORITY TO CONDUCT DEMONSTRATION PROGRAM-**

**(A) IN GENERAL-** The Administrator, through the Bureau of Primary Health Care and the Maternal and Child Health Bureau, shall conduct a demonstration program by making grants to up to 40 eligible entities for each fiscal year in which the program is conducted under this section for the purpose of developing and establishing systemic mechanisms to improve the prevention and treatment of Sickle Cell Disease, including through--

- (i) the coordination of service delivery for individuals with Sickle Cell Disease;
- (ii) genetic counseling and testing;
- (iii) bundling of technical services related to the prevention and treatment of Sickle Cell Disease;
- (iv) training of health professionals; and
- (v) identifying and establishing other efforts related to the expansion and coordination of education, treatment, and continuity of care programs for individuals with Sickle Cell Disease.

**(B) GRANT AWARD REQUIREMENTS-**

(i) **GEOGRAPHIC DIVERSITY-** The Administrator shall, to the extent practicable, award grants under this section to eligible entities located in different regions of the United States.

(ii) **PRIORITY-** In awarding grants under this subsection, the Administrator shall give priority to awarding grants to eligible entities that are--

(I) Federally-qualified health centers that have a partnership or other arrangement with a comprehensive Sickle Cell Disease treatment center that does not receive funds from the National Institutes of Health; or

(II) Federally-qualified health centers that intend to develop a partnership or other arrangement with a comprehensive Sickle Cell Disease treatment center that does not receive funds from the National Institutes of Health.

(2) **ADDITIONAL REQUIREMENTS-** An eligible entity awarded a grant under this subsection shall use funds made available under the grant to carry out, in addition to the activities described in paragraph (1)(A), the following activities:

(A) To facilitate and coordinate the delivery of education, treatment, and continuity of care for individuals with Sickle Cell Disease under--

- (i) the entity's collaborative agreement with a community-based Sickle Cell Disease organization or a nonprofit entity that works with individuals who have Sickle Cell Disease;
- (ii) the Sickle Cell Disease newborn screening program for the State in which the entity is located; and
- (iii) the maternal and child health program under title V of the Social Security Act (42 U.S.C. 701 et seq.) for the State in which the entity is located.

(B) To train nursing and other health staff who provide care for individuals with Sickle Cell Disease.

(C) To enter into a partnership with adult or pediatric hematologists in the region and other regional experts in Sickle Cell Disease at tertiary and academic health centers and State and county health offices.

(D) To identify and secure resources for ensuring reimbursement under the medicaid program, State children's health insurance program, and other health programs for the prevention and treatment of Sickle Cell Disease.

(3) NATIONAL COORDINATING CENTER-

(A) ESTABLISHMENT- The Administrator shall enter into a contract with an entity to serve as the National Coordinating Center for the demonstration program conducted under this subsection.

(B) ACTIVITIES DESCRIBED- The National Coordinating Center shall--

- (i) collect, coordinate, monitor, and distribute data, best practices, and findings regarding the activities funded under grants made to eligible entities under the demonstration program;
- (ii) develop a model protocol for eligible entities with respect to the prevention and treatment of Sickle Cell Disease;
- (iii) develop educational materials regarding the prevention and treatment of Sickle Cell Disease; and
- (iv) prepare and submit to Congress a final report that includes recommendations regarding the effectiveness of the demonstration program conducted under this subsection and such direct outcome measures as--

- (I) the number and type of health care resources utilized (such as emergency room visits, hospital visits, length of stay, and physician visits for individuals with Sickle Cell Disease); and
- (II) the number of individuals that were tested and subsequently received genetic counseling for the sickle cell trait.

(4) APPLICATION- An eligible entity desiring a grant under this subsection shall submit an application to the Administrator at such time, in such manner, and containing such information as the Administrator may require.

(5) DEFINITIONS- In this subsection:

(A) ADMINISTRATOR- The term 'Administrator' means the Administrator of the Health Resources and Services Administration.

(B) ELIGIBLE ENTITY- The term 'eligible entity' means a Federally-qualified health center, a nonprofit hospital or clinic, or a university health center that provides primary health care, that--

- (i) has a collaborative agreement with a community-based Sickle Cell Disease organization or a nonprofit entity with experience in working with individuals who have Sickle Cell Disease; and
- (ii) demonstrates to the Administrator that either the Federally-qualified health center, the nonprofit hospital or clinic, the university health center, the organization or entity described in clause (i), or the experts described in paragraph (2)(C), has at least 5 years of experience in working with individuals who have Sickle Cell Disease.

(C) FEDERALLY-QUALIFIED HEALTH CENTER- The term 'Federally-qualified health center' has the meaning given that term in section 1905(l)(2)(B) of the Social Security Act (42 U.S.C. 1396d(l)(2)(B)).

(6) AUTHORIZATION OF APPROPRIATIONS- There is authorized to be appropriated to carry out this subsection, \$10,000,000 for each of fiscal years 2005 through 2009.

(d) EFFECTIVE DATE- The amendments made by subsections (a) and (b) take effect on the date of enactment of this Act and apply to medical assistance and services provided under title XIX of the Social Security Act (42 U.S.C. 1396 et seq.) on or after that date.

## **SEC. 713. CEILING FANS.**

(a) IN GENERAL- Subchapter II of chapter 99 of the Harmonized Tariff Schedule of the United States is amended by inserting in numerical sequence the following new heading:

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` 9902.84.14 Ceiling fans for permanent installation (provided for in subheading 8414.51.00) Free No change No change On or before 12/31/2006  
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(b) EFFECTIVE DATE- The amendment made by this section applies to goods entered, or withdrawn from warehouse, for consumption on or after the 15th day after the date of enactment of this Act.

## **SEC. 714. CERTAIN STEAM GENERATORS, AND CERTAIN REACTOR VESSEL HEADS AND PRESSURIZERS, USED IN NUCLEAR FACILITIES.**

(a) CERTAIN STEAM GENERATORS- Heading 9902.84.02 of the Harmonized Tariff Schedule of the United States is amended by striking '12/31/2006' and inserting '12/31/2008'.

(b) CERTAIN REACTOR VESSEL HEADS AND PRESSURIZERS- Subchapter II of chapter 99 of the Harmonized Tariff Schedule of the United States is amended by inserting in numerical sequence the following new heading:

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` 9902.84.03 Reactor vessel heads and pressurizers for nuclear reactors (provided for in subheading 8401.40.00) Free No change No change On or before 12/31/2008 ' .  
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(c) **EFFECTIVE DATE-**

(1) **SUBSECTION (a)-** The amendment made by subsection (a) shall take effect on the date of the enactment of this Act.

(2) **SUBSECTION (b)-** The amendment made subsection (b) shall apply to goods entered, or withdrawn from warehouse, for consumption on or after the 15th day after the date of the enactment of this Act.

## **TITLE VIII--REVENUE PROVISIONS**

### **Subtitle A--Provisions to Reduce Tax Avoidance Through Individual and Corporate Expatriation**

#### **SEC. 801. TAX TREATMENT OF EXPATRIATED ENTITIES AND THEIR FOREIGN PARENTS.**

(a) **IN GENERAL-** Subchapter C of chapter 80 (relating to provisions affecting more than one subtitle) is amended by adding at the end the following new section:

#### **SEC. 7874. RULES RELATING TO EXPATRIATED ENTITIES AND THEIR FOREIGN PARENTS.**

**^(a) TAX ON INVERSION GAIN OF EXPATRIATED ENTITIES-**

**^(1) IN GENERAL-** The taxable income of an expatriated entity for any taxable year which includes any portion of the applicable period shall in no event be less than the inversion gain of the entity for the taxable year.

**^(2) EXPATRIATED ENTITY-** For purposes of this subsection-

**^(A) IN GENERAL-** The term 'expatriated entity' means--

**^(i)** the domestic corporation or partnership referred to in subparagraph (B)(i) with respect to which a foreign corporation is a surrogate foreign corporation, and

**^(ii)** any United States person who is related (within the meaning of section 267(b) or 707(b)(1)) to a domestic corporation or partnership described in clause (i).

**^(B) SURROGATE FOREIGN CORPORATION-** A foreign corporation shall be treated as a surrogate foreign corporation if, pursuant to a plan (or a series of related transactions)--

**^(i)** the entity completes after March 4, 2003, the direct or indirect acquisition of substantially all of the properties held directly or indirectly by a domestic corporation or substantially all of the properties constituting a trade or business of a domestic partnership,

- ``(ii) after the acquisition at least 60 percent of the stock (by vote or value) of the entity is held--
  - `(I) in the case of an acquisition with respect to a domestic corporation, by former shareholders of the domestic corporation by reason of holding stock in the domestic corporation, or
  - `(II) in the case of an acquisition with respect to a domestic partnership, by former partners of the domestic partnership by reason of holding a capital or profits interest in the domestic partnership, and
  - `(iii) after the acquisition the expanded affiliated group which includes the entity does not have substantial business activities in the foreign country in which, or under the law of which, the entity is created or organized, when compared to the total business activities of such expanded affiliated group.
- An entity otherwise described in clause (i) with respect to any domestic corporation or partnership trade or business shall be treated as not so described if, on or before March 4, 2003, such entity acquired directly or indirectly more than half of the properties held directly or indirectly by such corporation or more than half of the properties constituting such partnership trade or business, as the case may be.
- `(3) COORDINATION WITH SUBSECTION (b)- Paragraph (1) shall not apply to any entity which is treated as a domestic corporation under subsection (b).
- `(b) INVERTED CORPORATIONS TREATED AS DOMESTIC CORPORATIONS- Notwithstanding section 7701(a)(4), a foreign corporation shall be treated for purposes of this title as a domestic corporation if such corporation would be a surrogate foreign corporation if subsection (a)(2) were applied by substituting '80 percent' for '60 percent'.
- `(c) DEFINITIONS AND SPECIAL RULES-
  - `(1) EXPANDED AFFILIATED GROUP- The term 'expanded affiliated group' means an affiliated group as defined in section 1504(a) but without regard to section 1504(b)(3), except that section 1504(a) shall be applied by substituting 'more than 50 percent' for 'at least 80 percent' each place it appears.
  - `(2) CERTAIN STOCK DISREGARDED- There shall not be taken into account in determining ownership under subsection (a)(2)(B)(ii)--
    - `(A) stock held by members of the expanded affiliated group which includes the foreign corporation, or
    - `(B) stock of such foreign corporation which is sold in a public offering related to the acquisition described in subsection (a)(2)(B)(i).
  - `(3) PLAN DEEMED IN CERTAIN CASES- If a foreign corporation acquires directly or indirectly substantially all of the properties of a domestic corporation or partnership during the 4-year period beginning on the date which is 2 years before the ownership requirements of subsection (a)(2)(B)(ii) are met, such actions shall be treated as pursuant to a plan.
  - `(4) CERTAIN TRANSFERS DISREGARDED- The transfer of properties or liabilities (including by contribution or distribution) shall be disregarded if such transfers are part of a plan a principal purpose of which is to avoid the purposes of this section.
  - `(5) SPECIAL RULE FOR RELATED PARTNERSHIPS- For purposes of applying subsection (a)(2)(B)(ii) to the acquisition of a trade or business of a domestic partnership, except as provided in regulations, all partnerships which are under common control (within the meaning of section 482) shall be treated as 1 partnership.

- ``(6) REGULATIONS- The Secretary shall prescribe such regulations as may be appropriate to determine whether a corporation is a surrogate foreign corporation, including regulations--
  - ``(A) to treat warrants, options, contracts to acquire stock, convertible debt interests, and other similar interests as stock, and
  - ``(B) to treat stock as not stock.
- ``(d) OTHER DEFINITIONS- For purposes of this section--
  - ``(1) APPLICABLE PERIOD- The term `applicable period' means the period--
    - ``(A) beginning on the first date properties are acquired as part of the acquisition described in subsection (a)(2)(B)(i), and
    - ``(B) ending on the date which is 10 years after the last date properties are acquired as part of such acquisition.
  - ``(2) INVERSION GAIN- The term `inversion gain' means the income or gain recognized by reason of the transfer during the applicable period of stock or other properties by an expatriated entity, and any income received or accrued during the applicable period by reason of a license of any property by an expatriated entity--
    - ``(A) as part of the acquisition described in subsection (a)(2)(B)(i), or
    - ``(B) after such acquisition if the transfer or license is to a foreign related person.
  - Subparagraph (B) shall not apply to property described in section 1221(a)(1) in the hands of the expatriated entity.
  - ``(3) FOREIGN RELATED PERSON- The term `foreign related person' means, with respect to any expatriated entity, a foreign person which--
    - ``(A) is related (within the meaning of section 267(b) or 707(b)(1)) to such entity, or
    - ``(B) is under the same common control (within the meaning of section 482) as such entity.
- ``(e) SPECIAL RULES-
  - ``(1) CREDITS NOT ALLOWED AGAINST TAX ON INVERSION GAIN- Credits (other than the credit allowed by section 901) shall be allowed against the tax imposed by this chapter on an expatriated entity for any taxable year described in subsection (a) only to the extent such tax exceeds the product of--
    - ``(A) the amount of the inversion gain for the taxable year, and
    - ``(B) the highest rate of tax specified in section 11(b)(1).
  - For purposes of determining the credit allowed by section 901, inversion gain shall be treated as from sources within the United States.
  - ``(2) SPECIAL RULES FOR PARTNERSHIPS- In the case of an expatriated entity which is a partnership--
    - ``(A) subsection (a)(1) shall apply at the partner rather than the partnership level,
    - ``(B) the inversion gain of any partner for any taxable year shall be equal to the sum of--
      - ``(i) the partner's distributive share of inversion gain of the partnership for such taxable year, plus
      - ``(ii) gain recognized for the taxable year by the partner by reason of the transfer during the applicable period of any partnership interest of the partner in such partnership to the surrogate foreign corporation, and
    - ``(C) the highest rate of tax specified in the rate schedule applicable to the partner under this chapter shall be substituted for the rate of tax referred to in paragraph (1).

^(3) COORDINATION WITH SECTION 172 AND MINIMUM TAX- Rules similar to the rules of paragraphs (3) and (4) of section 860E(a) shall apply for purposes of subsection (a).

^(4) STATUTE OF LIMITATIONS-

^(A) IN GENERAL- The statutory period for the assessment of any deficiency attributable to the inversion gain of any taxpayer for any pre-inversion year shall not expire before the expiration of 3 years from the date the Secretary is notified by the taxpayer (in such manner as the Secretary may prescribe) of the acquisition described in subsection (a)(2)(B)(i) to which such gain relates and such deficiency may be assessed before the expiration of such 3-year period notwithstanding the provisions of any other law or rule of law which would otherwise prevent such assessment.

^(B) PRE-INVERSION YEAR- For purposes of subparagraph (A), the term 'pre-inversion year' means any taxable year if--

- ^(i) any portion of the applicable period is included in such taxable year, and
- ^(ii) such year ends before the taxable year in which the acquisition described in subsection (a)(2)(B)(i) is completed.

^(f) SPECIAL RULE FOR TREATIES- Nothing in section 894 or 7852(d) or in any other provision of law shall be construed as permitting an exemption, by reason of any treaty obligation of the United States heretofore or hereafter entered into, from the provisions of this section.

^(g) REGULATIONS- The Secretary shall provide such regulations as are necessary to carry out this section, including regulations providing for such adjustments to the application of this section as are necessary to prevent the avoidance of the purposes of this section, including the avoidance of such purposes through--

^(1) the use of related persons, pass-through or other noncorporate entities, or other intermediaries, or

^(2) transactions designed to have persons cease to be (or not become) members of expanded affiliated groups or related persons.'

(b) CONFORMING AMENDMENT- The table of sections for subchapter C of chapter 80 is amended by adding at the end the following new item:

^`Sec. 7874. Rules relating to expatriated entities and their foreign parents.'

(c) EFFECTIVE DATE- The amendments made by this section shall apply to taxable years ending after March 4, 2003.

## **SEC. 802. EXCISE TAX ON STOCK COMPENSATION OF INSIDERS IN EXPATRIATED CORPORATIONS.**

(a) IN GENERAL- Subtitle D is amended by inserting after chapter 44 end the following new chapter:

### **^`CHAPTER 45--PROVISIONS RELATING TO EXPATRIATED ENTITIES**

^`Sec. 4985. Stock compensation of insiders in expatriated corporations.

## **SEC. 4985. STOCK COMPENSATION OF INSIDERS IN EXPATRIATED CORPORATIONS.**

- ^(a) **IMPOSITION OF TAX**- In the case of an individual who is a disqualified individual with respect to any expatriated corporation, there is hereby imposed on such person a tax equal to--
  - ^(1) the rate of tax specified in section 1(h)(1)(C), multiplied by
  - ^(2) the value (determined under subsection (b)) of the specified stock compensation held (directly or indirectly) by or for the benefit of such individual or a member of such individual's family (as defined in section 267) at any time during the 12-month period beginning on the date which is 6 months before the expatriation date.
- ^(b) **VALUE**- For purposes of subsection (a)--
  - ^(1) **IN GENERAL**- The value of specified stock compensation shall be--
    - ^(A) in the case of a stock option (or other similar right) or a stock appreciation right, the fair value of such option or right, and
    - ^(B) in any other case, the fair market value of such compensation.
  - ^(2) **DATE FOR DETERMINING VALUE**- The determination of value shall be made--
    - ^(A) in the case of specified stock compensation held on the expatriation date, on such date,
    - ^(B) in the case of such compensation which is canceled during the 6 months before the expatriation date, on the day before such cancellation, and
    - ^(C) in the case of such compensation which is granted after the expatriation date, on the date such compensation is granted.
- ^(c) **TAX TO APPLY ONLY IF SHAREHOLDER GAIN RECOGNIZED**- Subsection (a) shall apply to any disqualified individual with respect to an expatriated corporation only if gain (if any) on any stock in such corporation is recognized in whole or part by any shareholder by reason of the acquisition referred to in section 7874(a)(2)(B)(i) with respect to such corporation.
- ^(d) **EXCEPTION WHERE GAIN RECOGNIZED ON COMPENSATION**- Subsection (a) shall not apply to--
  - ^(1) any stock option which is exercised on the expatriation date or during the 6-month period before such date and to the stock acquired in such exercise, if income is recognized under section 83 on or before the expatriation date with respect to the stock acquired pursuant to such exercise, and
  - ^(2) any other specified stock compensation which is exercised, sold, exchanged, distributed, cashed-out, or otherwise paid during such period in a transaction in which income, gain, or loss is recognized in full.
- ^(e) **DEFINITIONS**- For purposes of this section--
  - ^(1) **DISQUALIFIED INDIVIDUAL**- The term 'disqualified individual' means, with respect to a corporation, any individual who, at any time during the 12-month period beginning on the date which is 6 months before the expatriation date--
    - ^(A) is subject to the requirements of section 16(a) of the Securities Exchange Act of 1934 with respect to such corporation or any member of the expanded affiliated group which includes such corporation, or
    - ^(B) would be subject to such requirements if such corporation or member were an issuer of equity securities referred to in such section.

``(2) EXPATRIATED CORPORATION; EXPATRIATION DATE-

``(A) EXPATRIATED CORPORATION- The term `expatriated corporation' means any corporation which is an expatriated entity (as defined in section 7874(a)(2)). Such term includes any predecessor or successor of such a corporation.

``(B) EXPATRIATION DATE- The term `expatriation date' means, with respect to a corporation, the date on which the corporation first becomes an expatriated corporation.

``(3) SPECIFIED STOCK COMPENSATION-

``(A) IN GENERAL- The term `specified stock compensation' means payment (or right to payment) granted by the expatriated corporation (or by any member of the expanded affiliated group which includes such corporation) to any person in connection with the performance of services by a disqualified individual for such corporation or member if the value of such payment or right is based on (or determined by reference to) the value (or change in value) of stock in such corporation (or any such member).

``(B) EXCEPTIONS- Such term shall not include--

``(i) any option to which part II of subchapter D of chapter 1 applies, or

``(ii) any payment or right to payment from a plan referred to in section 280G(b)(6).

``(4) EXPANDED AFFILIATED GROUP- The term `expanded affiliated group' means an affiliated group (as defined in section 1504(a) without regard to section 1504(b)(3)); except that section 1504(a) shall be applied by substituting `more than 50 percent' for `at least 80 percent' each place it appears.

``(f) SPECIAL RULES- For purposes of this section-

``(1) CANCELLATION OF RESTRICTION- The cancellation of a restriction which by its terms will never lapse shall be treated as a grant.

``(2) PAYMENT OR REIMBURSEMENT OF TAX BY CORPORATION TREATED AS SPECIFIED STOCK COMPENSATION- Any payment of the tax imposed by this section directly or indirectly by the expatriated corporation or by any member of the expanded affiliated group which includes such corporation-

``(A) shall be treated as specified stock compensation, and

``(B) shall not be allowed as a deduction under any provision of chapter 1.

``(3) CERTAIN RESTRICTIONS IGNORED- Whether there is specified stock compensation, and the value thereof, shall be determined without regard to any restriction other than a restriction which by its terms will never lapse.

``(4) PROPERTY TRANSFERS- Any transfer of property shall be treated as a payment and any right to a transfer of property shall be treated as a right to a payment.

``(5) OTHER ADMINISTRATIVE PROVISIONS- For purposes of subtitle F, any tax imposed by this section shall be treated as a tax imposed by subtitle A.

``(g) REGULATIONS- The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.'

(b) DENIAL OF DEDUCTION-

(1) IN GENERAL- Paragraph (6) of section 275(a) is amended by inserting `45,' before `46.'

(2) \$1,000,000 limit on deductible compensation reduced by payment of excise tax on specified stock compensation- Paragraph (4) of section 162(m) is amended by adding at the end the following new subparagraph:

``(G) COORDINATION WITH EXCISE TAX ON SPECIFIED STOCK COMPENSATION- The dollar limitation contained in paragraph (1) with respect to any

covered employee shall be reduced (but not below zero) by the amount of any payment (with respect to such employee) of the tax imposed by section 4985 directly or indirectly by the expatriated corporation (as defined in such section) or by any member of the expanded affiliated group (as defined in such section) which includes such corporation.'

(c) CONFORMING AMENDMENTS-

(1) The last sentence of section 3121(v)(2)(A) is amended by inserting before the period `or to any specified stock compensation (as defined in section 4985) on which tax is imposed by section 4985'.

(2) The table of chapters for subtitle D is amended by inserting after the item relating to chapter 44 the following new item:

`Chapter 45. Provisions relating to expatriated entities.'

(d) EFFECTIVE DATE- The amendments made by this section shall take effect on March 4, 2003; except that periods before such date shall not be taken into account in applying the periods in subsections (a) and (e)(1) of section 4985 of the Internal Revenue Code of 1986, as added by this section.

## **SEC. 803. REINSURANCE OF UNITED STATES RISKS IN FOREIGN JURISDICTIONS.**

(a) IN GENERAL- Section 845(a) (relating to allocation in case of reinsurance agreement involving tax avoidance or evasion) is amended by striking `source and character' and inserting `amount, source, or character'.

(b) EFFECTIVE DATE- The amendments made by this section shall apply to any risk reinsured after the date of the enactment of this Act.

## **SEC. 804. REVISION OF TAX RULES ON EXPATRIATION OF INDIVIDUALS.**

(a) EXPATRIATION TO AVOID TAX-

(1) IN GENERAL- Subsection (a) of section 877 (relating to treatment of expatriates) is amended to read as follows:

`(a) TREATMENT OF EXPATRIATES-

`(1) IN GENERAL- Every nonresident alien individual to whom this section applies and who, within the 10-year period immediately preceding the close of the taxable year, lost United States citizenship shall be taxable for such taxable year in the manner provided in subsection (b) if the tax imposed pursuant to such subsection (after any reduction in such tax under the last sentence of such subsection) exceeds the tax which, without regard to this section, is imposed pursuant to section 871.

`(2) INDIVIDUALS SUBJECT TO THIS SECTION- This section shall apply to any individual if-

`(A) the average annual net income tax (as defined in section 38(c)(1)) of such individual for the period of 5 taxable years ending before the date of the loss of United States citizenship is greater than \$124,000,

`(B) the net worth of the individual as of such date is \$2,000,000 or more, or

``(C) such individual fails to certify under penalty of perjury that he has met the requirements of this title for the 5 preceding taxable years or fails to submit such evidence of such compliance as the Secretary may require.

In the case of the loss of United States citizenship in any calendar year after 2004, such \$124,000 amount shall be increased by an amount equal to such dollar amount multiplied by the cost-of-living adjustment determined under section 1(f)(3) for such calendar year by substituting `2003' for `1992' in subparagraph (B) thereof. Any increase under the preceding sentence shall be rounded to the nearest multiple of \$1,000.'

(2) REVISION OF EXCEPTIONS FROM ALTERNATIVE TAX- Subsection (c) of section 877 (relating to tax avoidance not presumed in certain cases) is amended to read as follows:

``(c) EXCEPTIONS-

``(1) IN GENERAL- Subparagraphs (A) and (B) of subsection (a)(2) shall not apply to an individual described in paragraph (2) or (3).

``(2) DUAL CITIZENS-

``(A) IN GENERAL- An individual is described in this paragraph if--

``(i) the individual became at birth a citizen of the United States and a citizen of another country and continues to be a citizen of such other country, and

``(ii) the individual has had no substantial contacts with the United States.

``(B) SUBSTANTIAL CONTACTS- An individual shall be treated as having no substantial contacts with the United States only if the individual-

``(i) was never a resident of the United States (as defined in section 7701(b)),

``(ii) has never held a United States passport, and

``(iii) was not present in the United States for more than 30 days during any calendar year which is 1 of the 10 calendar years preceding the individual's loss of United States citizenship.

``(3) CERTAIN MINORS- An individual is described in this paragraph if--

``(A) the individual became at birth a citizen of the United States,

``(B) neither parent of such individual was a citizen of the United States at the time of such birth,

``(C) the individual's loss of United States citizenship occurs before such individual attains age 18 1/2 , and

``(D) the individual was not present in the United States for more than 30 days during any calendar year which is 1 of the 10 calendar years preceding the individual's loss of United States citizenship.'

(3) CONFORMING AMENDMENT- Section 2107(a) is amended to read as follows:

``(a) TREATMENT OF EXPATRIATES- A tax computed in accordance with the table contained in section 2001 is hereby imposed on the transfer of the taxable estate, determined as provided in section 2106, of every decedent nonresident not a citizen of the United States if the date of death occurs during a taxable year with respect to which the decedent is subject to tax under section 877(b).'

(b) SPECIAL RULES FOR DETERMINING WHEN AN INDIVIDUAL IS NO LONGER A UNITED STATES CITIZEN OR LONG-TERM RESIDENT- Section 7701 (relating to definitions) is amended by redesignating subsection (n) as subsection (o) and by inserting after subsection (m) the following new subsection:

^(n) SPECIAL RULES FOR DETERMINING WHEN AN INDIVIDUAL IS NO LONGER A UNITED STATES CITIZEN OR LONG-TERM RESIDENT- An individual who would (but for this subsection) cease to be treated as a citizen or resident of the United States shall continue to be treated as a citizen or resident of the United States, as the case may be, until such individual-

^(1) gives notice of an expatriating act or termination of residency (with the requisite intent to relinquish citizenship or terminate residency) to the Secretary of State or the Secretary of Homeland Security, and

^(2) provides a statement in accordance with section 6039G.'

(c) PHYSICAL PRESENCE IN THE UNITED STATES FOR MORE THAN 30 DAYS- Section 877 (relating to expatriation to avoid tax) is amended by adding at the end the following new subsection:

^(g) PHYSICAL PRESENCE-

^(1) IN GENERAL- This section shall not apply to any individual to whom this section would otherwise apply for any taxable year during the 10-year period referred to in subsection (a) in which such individual is physically present in the United States at any time on more than 30 days in the calendar year ending in such taxable year, and such individual shall be treated for purposes of this title as a citizen or resident of the United States, as the case may be, for such taxable year.

^(2) EXCEPTION-

^(A) IN GENERAL- In the case of an individual described in any of the following subparagraphs of this paragraph, a day of physical presence in the United States shall be disregarded if the individual is performing services in the United States on such day for an employer. The preceding sentence shall not apply if--

^(i) such employer is related (within the meaning of section 267 and 707) to such individual, or

^(ii) such employer fails to meet such requirements as the Secretary may prescribe by regulations to prevent the avoidance of the purposes of this paragraph.

Not more than 30 days during any calendar year may be disregarded under this subparagraph.

^(B) INDIVIDUALS WITH TIES TO OTHER COUNTRIES- An individual is described in this subparagraph if-

^(i) the individual becomes (not later than the close of a reasonable period after loss of United States citizenship or termination of residency) a citizen or resident of the country in which-

^(I) such individual was born,

^(II) if such individual is married, such individual's spouse was born, or

^(III) either of such individual's parents were born, and

^(ii) the individual becomes fully liable for income tax in such country.

^(C) MINIMAL PRIOR PHYSICAL PRESENCE IN THE UNITED STATES- An individual is described in this subparagraph if, for each year in the 10-year period ending on the date of loss of United States citizenship or termination of residency, the individual was physically present in the United States for 30 days or less. The rule of section 7701(b)(3)(D)(ii) shall apply for purposes of this subparagraph.'

(d) TRANSFERS SUBJECT TO GIFT TAX-

(1) IN GENERAL- Subsection (a) of section 2501 (relating to taxable transfers) is amended by striking paragraph (4), by redesignating paragraph (5) as paragraph (4), and by striking paragraph (3) and inserting the following new paragraph:

``(3) EXCEPTION-

``(A) CERTAIN INDIVIDUALS- Paragraph (2) shall not apply in the case of a donor to whom section 877(b) applies for the taxable year which includes the date of the transfer.

``(B) CREDIT FOR FOREIGN GIFT TAXES- The tax imposed by this section solely by reason of this paragraph shall be credited with the amount of any gift tax actually paid to any foreign country in respect of any gift which is taxable under this section solely by reason of this paragraph.'

(2) TRANSFERS OF CERTAIN STOCK- Subsection (a) of section 2501 is amended by adding at the end the following new paragraph:

``(5) TRANSFERS OF CERTAIN STOCK-

``(A) IN GENERAL- In the case of a transfer of stock in a foreign corporation described in subparagraph (B) by a donor to whom section 877(b) applies for the taxable year which includes the date of the transfer--

``(i) section 2511(a) shall be applied without regard to whether such stock is situated within the United States, and

``(ii) the value of such stock for purposes of this chapter shall be its U.S.-asset value determined under subparagraph (C).

``(B) FOREIGN CORPORATION DESCRIBED- A foreign corporation is described in this subparagraph with respect to a donor if--

``(i) the donor owned (within the meaning of section 958(a)) at the time of such transfer 10 percent or more of the total combined voting power of all classes of stock entitled to vote of the foreign corporation, and

``(ii) such donor owned (within the meaning of section 958(a)), or is considered to have owned (by applying the ownership rules of section 958(b)), at the time of such transfer, more than 50 percent of--

``(I) the total combined voting power of all classes of stock entitled to vote of such corporation, or

``(II) the total value of the stock of such corporation.

``(C) U.S.-ASSET VALUE- For purposes of subparagraph (A), the U.S.-asset value of stock shall be the amount which bears the same ratio to the fair market value of such stock at the time of transfer as--

``(i) the fair market value (at such time) of the assets owned by such foreign corporation and situated in the United States, bears to

``(ii) the total fair market value (at such time) of all assets owned by such foreign corporation.'

(e) ENHANCED INFORMATION REPORTING FROM INDIVIDUALS LOSING UNITED STATES CITIZENSHIP-

(1) IN GENERAL- Subsection (a) of section 6039G is amended to read as follows:

``(a) IN GENERAL- Notwithstanding any other provision of law, any individual to whom section 877(b) applies for any taxable year shall provide a statement for such taxable year which includes the information described in subsection (b).'

(2) INFORMATION TO BE PROVIDED- Subsection (b) of section 6039G is amended to read as follows:

- ^(b) INFORMATION TO BE PROVIDED- Information required under subsection (a) shall include--
  - ^(1) the taxpayer's TIN,
  - ^(2) the mailing address of such individual's principal foreign residence,
  - ^(3) the foreign country in which such individual is residing,
  - ^(4) the foreign country of which such individual is a citizen,
  - ^(5) information detailing the income, assets, and liabilities of such individual,
  - ^(6) the number of days during any portion of which that the individual was physically present in the United States during the taxable year, and
  - ^(7) such other information as the Secretary may prescribe.'
- (3) INCREASE IN PENALTY- Subsection (d) of section 6039G is amended to read as follows:
  - ^(d) PENALTY- If--
    - ^(1) an individual is required to file a statement under subsection (a) for any taxable year, and
    - ^(2) fails to file such a statement with the Secretary on or before the date such statement is required to be filed or fails to include all the information required to be shown on the statement or includes incorrect information,
  - such individual shall pay a penalty of \$10,000 unless it is shown that such failure is due to reasonable cause and not to willful neglect.'
- (4) CONFORMING AMENDMENT- Section 6039G is amended by striking subsections (c), (f), and (g) and by redesignating subsections (d) and (e) as subsection (c) and (d), respectively.
- (f) EFFECTIVE DATE- The amendments made by this section shall apply to individuals who expatriate after June 3, 2004.

## **SEC. 805. REPORTING OF TAXABLE MERGERS AND ACQUISITIONS.**

- (a) IN GENERAL- Subpart B of part III of subchapter A of chapter 61 is amended by inserting after section 6043 the following new section:

### **SEC. 6043A. RETURNS RELATING TO TAXABLE MERGERS AND ACQUISITIONS.**

- ^(a) IN GENERAL- According to the forms or regulations prescribed by the Secretary, the acquiring corporation in any taxable acquisition shall make a return setting forth--
  - ^(1) a description of the acquisition,
  - ^(2) the name and address of each shareholder of the acquired corporation who is required to recognize gain (if any) as a result of the acquisition,
  - ^(3) the amount of money and the fair market value of other property transferred to each such shareholder as part of such acquisition, and
  - ^(4) such other information as the Secretary may prescribe.
- To the extent provided by the Secretary, the requirements of this section applicable to the acquiring corporation shall be applicable to the acquired corporation and not to the acquiring corporation.

``(b) NOMINEES- According to the forms or regulations prescribed by the Secretary:

``(1) REPORTING- Any person who holds stock as a nominee for another person shall furnish in the manner prescribed by the Secretary to such other person the information provided by the corporation under subsection (d).

``(2) REPORTING TO NOMINEES- In the case of stock held by any person as a nominee, references in this section (other than in subsection (c)) to a shareholder shall be treated as a reference to the nominee.

``(c) TAXABLE ACQUISITION- For purposes of this section, the term `taxable acquisition' means any acquisition by a corporation of stock in or property of another corporation if any shareholder of the acquired corporation is required to recognize gain (if any) as a result of such acquisition.

``(d) STATEMENTS TO BE FURNISHED TO SHAREHOLDERS- According to the forms or regulations prescribed by the Secretary, every person required to make a return under subsection (a) shall furnish to each shareholder whose name is required to be set forth in such return a written statement showing--

``(1) the name, address, and phone number of the information contact of the person required to make such return,

``(2) the information required to be shown on such return with respect to such shareholder, and

``(3) such other information as the Secretary may prescribe.

The written statement required under the preceding sentence shall be furnished to the shareholder on or before January 31 of the year following the calendar year during which the taxable acquisition occurred.'

(b) ASSESSABLE PENALTIES-

(1) Subparagraph (B) of section 6724(d)(1) (relating to definitions) is amended by redesignating clauses (ii) through (xviii) as clauses (iii) through (xix), respectively, and by inserting after clause (i) the following new clause:

``(ii) section 6043A(a) (relating to returns relating to taxable mergers and acquisitions),.'

(2) Paragraph (2) of section 6724(d) is amended by redesignating subparagraphs (F) through (BB) as subparagraphs (G) through (CC), respectively, and by inserting after subparagraph (E) the following new subparagraph:

``(F) subsections (b) and (d) of section 6043A (relating to returns relating to taxable mergers and acquisitions).'

(c) CLERICAL AMENDMENT- The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by inserting after the item relating to section 6043 the following new item:

``Sec. 6043A. Returns relating to taxable mergers and acquisitions.'

(d) EFFECTIVE DATE- The amendments made by this section shall apply to acquisitions after the date of the enactment of this Act.

## **SEC. 806. STUDIES.**

(a) TRANSFER PRICING RULES- The Secretary of the Treasury or the Secretary's delegate shall conduct a study regarding the effectiveness of current transfer pricing rules

and compliance efforts in ensuring that cross-border transfers and other related-party transactions, particularly transactions involving intangible assets, service contracts, or leases cannot be used improperly to shift income out of the United States. The study shall include a review of the contemporaneous documentation and penalty rules under section 6662 of the Internal Revenue Code of 1986, a review of the regulatory and administrative guidance implementing the principles of section 482 of such Code to transactions involving intangible property and services and to cost-sharing arrangements, and an examination of whether increased disclosure of cross-border transactions should be required. The study shall set forth specific recommendations to address all abuses identified in the study. Not later than June 30, 2005, such Secretary or delegate shall submit to the Congress a report of such study.

(b) INCOME TAX TREATIES- The Secretary of the Treasury or the Secretary's delegate shall conduct a study of United States income tax treaties to identify any inappropriate reductions in United States withholding tax that provide opportunities for shifting income out of the United States, and to evaluate whether existing anti-abuse mechanisms are operating properly. The study shall include specific recommendations to address all inappropriate uses of tax treaties. Not later than June 30, 2005, such Secretary or delegate shall submit to the Congress a report of such study.

(c) EFFECTIVENESS OF CORPORATE EXPATRIATION PROVISIONS- The Secretary of the Treasury or the Secretary's delegate shall conduct a study of the effectiveness of the provisions of this title on corporate expatriation. The study shall include such recommendations as such Secretary or delegate may have to improve the effectiveness of such provisions in carrying out the purposes of this title. Not later than December 31, 2006, such Secretary or delegate shall submit to the Congress a report of such study.

## **Subtitle B--Provisions Relating to Tax Shelters**

### ***Part I--Taxpayer-Related Provisions***

#### **SEC. 811. PENALTY FOR FAILING TO DISCLOSE REPORTABLE TRANSACTIONS.**

(a) IN GENERAL- Part I of subchapter B of chapter 68 (relating to assessable penalties) is amended by inserting after section 6707 the following new section:

#### **SEC. 6707A. PENALTY FOR FAILURE TO INCLUDE REPORTABLE TRANSACTION INFORMATION WITH RETURN.**

^(a) IMPOSITION OF PENALTY- Any person who fails to include on any return or statement any information with respect to a reportable transaction which is required under section 6011 to be included with such return or statement shall pay a penalty in the amount determined under subsection (b).

^(b) AMOUNT OF PENALTY-

- ``(1) IN GENERAL- Except as provided in paragraph (2), the amount of the penalty under subsection (a) shall be--
  - ``(A) \$10,000 in the case of a natural person, and
  - ``(B) \$50,000 in any other case.
- ``(2) LISTED TRANSACTION- The amount of the penalty under subsection (a) with respect to a listed transaction shall be--
  - ``(A) \$100,000 in the case of a natural person, and
  - ``(B) \$200,000 in any other case.
- ``(c) DEFINITIONS- For purposes of this section:
  - ``(1) REPORTABLE TRANSACTION- The term 'reportable transaction' means any transaction with respect to which information is required to be included with a return or statement because, as determined under regulations prescribed under section 6011, such transaction is of a type which the Secretary determines as having a potential for tax avoidance or evasion.
  - ``(2) LISTED TRANSACTION- The term 'listed transaction' means a reportable transaction which is the same as, or substantially similar to, a transaction specifically identified by the Secretary as a tax avoidance transaction for purposes of section 6011.
- ``(d) AUTHORITY TO RESCIND PENALTY-
  - ``(1) IN GENERAL- The Commissioner of Internal Revenue may rescind all or any portion of any penalty imposed by this section with respect to any violation if--
    - ``(A) the violation is with respect to a reportable transaction other than a listed transaction, and
    - ``(B) rescinding the penalty would promote compliance with the requirements of this title and effective tax administration.
  - ``(2) NO JUDICIAL APPEAL- Notwithstanding any other provision of law, any determination under this subsection may not be reviewed in any judicial proceeding.
  - ``(3) RECORDS- If a penalty is rescinded under paragraph (1), the Commissioner shall place in the file in the Office of the Commissioner the opinion of the Commissioner with respect to the determination, including--
    - ``(A) a statement of the facts and circumstances relating to the violation,
    - ``(B) the reasons for the rescission, and
    - ``(C) the amount of the penalty rescinded.
  - ``(e) PENALTY REPORTED TO SEC- In the case of a person--
    - ``(1) which is required to file periodic reports under section 13 or 15(d) of the Securities Exchange Act of 1934 or is required to be consolidated with another person for purposes of such reports, and
    - ``(2) which--
      - ``(A) is required to pay a penalty under this section with respect to a listed transaction,
      - ``(B) is required to pay a penalty under section 6662A with respect to any reportable transaction at a rate prescribed under section 6662A(c), or
      - ``(C) is required to pay a penalty under section 6662(h) with respect to any reportable transaction and would (but for section 6662A(e)(2)(C)) have been subject to penalty under section 6662A at a rate prescribed under section 6662A(c),

accordance with the preceding sentence shall be treated as a failure to which the penalty under subsection (b)(2) applies.

^(f) COORDINATION WITH OTHER PENALTIES- The penalty imposed by this section shall be in addition to any other penalty imposed by this title.'

(b) CONFORMING AMENDMENT- The table of sections for part I of subchapter B of chapter 68 is amended by inserting after the item relating to section 6707 the following:

^`Sec. 6707A. Penalty for failure to include reportable transaction information with return.'

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

(d) REPORT- The Commissioner of Internal Revenue shall annually report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate--

(1) a summary of the total number and aggregate amount of penalties imposed, and rescinded, under section 6707A of the Internal Revenue Code of 1986, and

(2) a description of each penalty rescinded under section 6707(c) of such Code and the reasons therefor.

## **SEC. 812. ACCURACY-RELATED PENALTY FOR LISTED TRANSACTIONS, OTHER REPORTABLE TRANSACTIONS HAVING A SIGNIFICANT TAX AVOIDANCE PURPOSE, ETC.**

(a) IN GENERAL- Subchapter A of chapter 68 is amended by inserting after section 6662 the following new section:

### **^`SEC. 6662A. IMPOSITION OF ACCURACY-RELATED PENALTY ON UNDERSTATEMENTS WITH RESPECT TO REPORTABLE TRANSACTIONS.**

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

^(b) REPORTABLE TRANSACTION UNDERSTATEMENT- For purposes of this section--

^(1) IN GENERAL- The term `reportable transaction understatement' means the sum of--

^(A) the product of--

^(i) the amount of the increase (if any) in taxable income which results from a difference between the proper tax treatment of an item to which this section applies and the taxpayer's treatment of such item (as shown on the taxpayer's return of tax), and

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

^(B) the amount of the decrease (if any) in the aggregate amount of credits determined under subtitle A which results from a difference between the taxpayer's treatment of an

item to which this section applies (as shown on the taxpayer's return of tax) and the proper tax treatment of such item.

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

``(2) ITEMS TO WHICH SECTION APPLIES- This section shall apply to any item which is attributable to--

``(A) any listed transaction, and

``(B) any reportable transaction (other than a listed transaction) if a significant purpose of such transaction is the avoidance or evasion of Federal income tax.

``(c) HIGHER PENALTY FOR NONDISCLOSED LISTED AND OTHER

AVOIDANCE TRANSACTIONS- Subsection (a) shall be applied by substituting `30 percent' for `20 percent' with respect to the portion of any reportable transaction understatement with respect to which the requirement of section 6664(d)(2)(A) is not met.

``(d) DEFINITIONS OF REPORTABLE AND LISTED TRANSACTIONS- For purposes of this section, the terms `reportable transaction' and `listed transaction' have the respective meanings given to such terms by section 6707A(c).

``(e) SPECIAL RULES-

``(1) COORDINATION WITH PENALTIES, ETC., ON OTHER UNDERSTATEMENTS- In the case of an understatement (as defined in section 6662(d)(2))--

``(A) the amount of such understatement (determined without regard to this paragraph) shall be increased by the aggregate amount of reportable transaction understatements for purposes of determining whether such understatement is a substantial understatement under section 6662(d)(1), and

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

``(2) COORDINATION WITH OTHER PENALTIES-

``(A) APPLICATION OF FRAUD PENALTY- References to an underpayment in section 6663 shall be treated as including references to a reportable transaction understatement.

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

``(C) COORDINATION WITH VALUATION PENALTIES-

``(i) SECTION 6662(e)- Section 6662(e) shall not apply to any portion of an understatement on which a penalty is imposed under this section.

``(ii) SECTION 6662(h)- This section shall not apply to any portion of an understatement on which a penalty is imposed under section 6662(h).

``(3) SPECIAL RULE FOR AMENDED RETURNS- Except as provided in regulations, in no event shall any tax treatment included with an amendment or supplement to a return of tax be taken into account in determining the amount of any reportable transaction understatement if the amendment or supplement is filed after the earlier of the date the taxpayer is first contacted by the Secretary regarding the examination of the return or such other date as is specified by the Secretary.'

(b) DETERMINATION OF OTHER UNDERSTATEMENTS- Subparagraph (A) of section 6662(d)(2) is amended by adding at the end the following flush sentence:  
`The excess under the preceding sentence shall be determined without regard to items to which section 6662A applies.'

(c) REASONABLE CAUSE EXCEPTION-

(1) IN GENERAL- Section 6664 is amended by adding at the end the following new subsection:

^(d) REASONABLE CAUSE EXCEPTION FOR REPORTABLE TRANSACTION UNDERSTATEMENTS-

^(1) IN GENERAL- No penalty shall be imposed under section 6662A with respect to any portion of a reportable transaction understatement if it is shown that there was a reasonable cause for such portion and that the taxpayer acted in good faith with respect to such portion.

^(2) SPECIAL RULES- Paragraph (1) shall not apply to any reportable transaction understatement unless--

^(A) the relevant facts affecting the tax treatment of the item are adequately disclosed in accordance with the regulations prescribed under section 6011,

^(B) there is or was substantial authority for such treatment, and

^(C) the taxpayer reasonably believed that such treatment was more likely than not the proper treatment.

A taxpayer failing to adequately disclose in accordance with section 6011 shall be treated as meeting the requirements of subparagraph (A) if the penalty for such failure was rescinded under section 6707A(d).

^(3) RULES RELATING TO REASONABLE BELIEF- For purposes of paragraph (2)(C)--

^(A) IN GENERAL- A taxpayer shall be treated as having a reasonable belief with respect to the tax treatment of an item only if such belief-

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

^(ii) relates solely to the taxpayer's chances of success on the merits of such treatment and does not take into account the possibility that a return will not be audited, such treatment will not be raised on audit, or such treatment will be resolved through settlement if it is raised.

^(B) CERTAIN OPINIONS MAY NOT BE RELIED UPON-

^(i) IN GENERAL- An opinion of a tax advisor may not be relied upon to establish the reasonable belief of a taxpayer if--

^(I) the tax advisor is described in clause (ii), or

^(II) the opinion is described in clause (iii).

^(ii) DISQUALIFIED TAX ADVISORS- A tax advisor is described in this clause if the tax advisor--

^(I) is a material advisor (within the meaning of section 6111(b)(1)) and participates in the organization, management, promotion, or sale of the transaction or is related (within the meaning of section 267(b) or 707(b)(1)) to any person who so participates,

^(II) is compensated directly or indirectly by a material advisor with respect to the transaction,

``(III) has a fee arrangement with respect to the transaction which is contingent on all or part of the intended tax benefits from the transaction being sustained, or  
``(IV) as determined under regulations prescribed by the Secretary, has a disqualifying financial interest with respect to the transaction.  
``(iii) **DISQUALIFIED OPINIONS**- For purposes of clause (i), an opinion is disqualified if the opinion-  
``(I) is based on unreasonable factual or legal assumptions (including assumptions as to future events),  
``(II) unreasonably relies on representations, statements, findings, or agreements of the taxpayer or any other person,  
``(III) does not identify and consider all relevant facts, or  
``(IV) fails to meet any other requirement as the Secretary may prescribe.'.

(2) **CONFORMING AMENDMENTS**-

(A) Paragraph (1) of section 6664(c) is amended by striking `this part' and inserting `section 6662 or 6663'.  
(B) The heading for subsection (c) of section 6664 is amended by inserting `FOR UNDERPAYMENTS' after `EXCEPTION'.  
(d) **REDUCTION IN PENALTY FOR SUBSTANTIAL UNDERSTATEMENT OF INCOME TAX NOT TO APPLY TO TAX SHELTERS**- Subparagraph (C) of section 6662(d)(2) (relating to substantial understatement of income tax) is amended to read as follows:  
``(C) **REDUCTION NOT TO APPLY TO TAX SHELTERS**-  
``(i) **IN GENERAL**- Subparagraph (B) shall not apply to any item attributable to a tax shelter.  
``(ii) **TAX SHELTER**- For purposes of clause (i), the term `tax shelter' means--  
``(I) a partnership or other entity,  
``(II) any investment plan or arrangement, or  
``(III) any other plan or arrangement,  
if a significant purpose of such partnership, entity, plan, or arrangement is the avoidance or evasion of Federal income tax.'.  
(e) **CLERICAL AMENDMENTS**-  
(1) The heading for section 6662 is amended to read as follows:

**``SEC. 6662. IMPOSITION OF ACCURACY-RELATED PENALTY ON UNDERPAYMENTS.'**

(2) The table of sections for part II of subchapter A of chapter 68 is amended by striking the item relating to section 6662 and inserting the following new items:

``Sec. 6662. Imposition of accuracy-related penalty on underpayments.  
``Sec. 6662A. Imposition of accuracy-related penalty on understatements with respect to reportable transactions.'.  
(f) **EFFECTIVE DATE**- The amendments made by this section shall apply to taxable years ending after the date of the enactment of this Act.

## **SEC. 813. TAX SHELTER EXCEPTION TO CONFIDENTIALITY PRIVILEGES RELATING TO TAXPAYER COMMUNICATIONS.**

(a) IN GENERAL- Section 7525(b) (relating to section not to apply to communications regarding corporate tax shelters) is amended to read as follows:

``(b) SECTION NOT TO APPLY TO COMMUNICATIONS REGARDING TAX SHELTERS- The privilege under subsection (a) shall not apply to any written communication which is--

``(1) between a federally authorized tax practitioner and--

``(A) any person,

``(B) any director, officer, employee, agent, or representative of the person, or

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

``(2) in connection with the promotion of the direct or indirect participation of the person in any tax shelter (as defined in section 6662(d)(2)(C)(ii)).'.

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

## **SEC. 814. STATUTE OF LIMITATIONS FOR TAXABLE YEARS FOR WHICH REQUIRED LISTED TRANSACTIONS NOT REPORTED.**

(a) IN GENERAL- Section 6501(c) (relating to exceptions) is amended by adding at the end the following new paragraph:

``(10) LISTED TRANSACTIONS- If a taxpayer fails to include on any return or statement for any taxable year any information with respect to a listed transaction (as defined in section 6707A(c)(2)) which is required under section 6011 to be included with such return or statement, the time for assessment of any tax imposed by this title with respect to such transaction shall not expire before the date which is 1 year after the earlier of--

``(A) the date on which the Secretary is furnished the information so required, or

``(B) the date that a material advisor (as defined in section 6111) meets the requirements of section 6112 with respect to a request by the Secretary under section 6112(b) relating to such transaction with respect to such taxpayer.'.

(b) EFFECTIVE DATE- The amendment made by this section shall apply to taxable years with respect to which the period for assessing a deficiency did not expire before the date of the enactment of this Act.

## **SEC. 815. DISCLOSURE OF REPORTABLE TRANSACTIONS.**

(a) IN GENERAL- Section 6111 (relating to registration of tax shelters) is amended to read as follows:

### **``SEC. 6111. DISCLOSURE OF REPORTABLE TRANSACTIONS.**

``(a) IN GENERAL- Each material advisor with respect to any reportable transaction shall make a return (in such form as the Secretary may prescribe) setting forth-

``(1) information identifying and describing the transaction,

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

``(3) such other information as the Secretary may prescribe.

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

``(b) DEFINITIONS- For purposes of this section:

``(1) MATERIAL ADVISOR-

``(A) IN GENERAL- The term `material advisor' means any person--

``(i) who provides any material aid, assistance, or advice with respect to organizing, managing, promoting, selling, implementing, insuring, or carrying out any reportable transaction, and

``(ii) who directly or indirectly derives gross income in excess of the threshold amount (or such other amount as may be prescribed by the Secretary) for such advice or assistance.

``(B) THRESHOLD AMOUNT- For purposes of subparagraph (A), the threshold amount is--

``(i) \$50,000 in the case of a reportable transaction substantially all of the tax benefits from which are provided to natural persons, and

``(ii) \$250,000 in any other case.

``(2) REPORTABLE TRANSACTION- The term `reportable transaction' has the meaning given to such term by section 6707A(c).

``(c) REGULATIONS- The Secretary may prescribe regulations which provide--

``(1) that only 1 person shall be required to meet the requirements of subsection (a) in cases in which 2 or more persons would otherwise be required to meet such requirements,

``(2) exemptions from the requirements of this section, and

``(3) such rules as may be necessary or appropriate to carry out the purposes of this section.'

(b) CONFORMING AMENDMENTS- (1) The item relating to section 6111 in the table of sections for subchapter B of chapter 61 is amended to read as follows:

``Sec. 6111. Disclosure of reportable transactions.'

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

## **``SEC. 6112. MATERIAL ADVISORS OF REPORTABLE TRANSACTIONS MUST KEEP LISTS OF ADVISEES, ETC.**

``(a) IN GENERAL- Each material advisor (as defined in section 6111) with respect to any reportable transaction (as defined in section 6707A(c)) shall (whether or not required to file a return under section 6111 with respect to such transaction) maintain (in such manner as the Secretary may by regulations prescribe) a list--

``(1) identifying each person with respect to whom such advisor acted as a material advisor with respect to such transaction, and

``(2) containing such other information as the Secretary may by regulations require.'

(3) Section 6112 is amended--

(A) by redesignating subsection (c) as subsection (b),

(B) by inserting `written' before `request' in subsection (b)(1) (as so redesignated), and

(C) by striking 'shall prescribe' in subsection (b)(2) (as so redesignated) and inserting 'may prescribe'.

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

'Sec. 6112. Material advisors of reportable transactions must keep lists of advisees, etc.'.

(5)(A) The heading for section 6708 is amended to read as follows:

**'SEC. 6708. FAILURE TO MAINTAIN LISTS OF ADVISEES WITH RESPECT TO REPORTABLE TRANSACTIONS.'**

(B) The item relating to section 6708 in the table of sections for part I of subchapter B of chapter 68 is amended to read as follows:

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

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

**SEC. 816. FAILURE TO FURNISH INFORMATION REGARDING REPORTABLE TRANSACTIONS.**

(a) **IN GENERAL**- Section 6707 (relating to failure to furnish information regarding tax shelters) is amended to read as follows:

**'SEC. 6707. FAILURE TO FURNISH INFORMATION REGARDING REPORTABLE TRANSACTIONS.'**

'(a) **IN GENERAL**- If a person who is required to file a return under section 6111(a) with respect to any reportable transaction--

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

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

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

'(b) **AMOUNT OF PENALTY**-

'(1) **IN GENERAL**- Except as provided in paragraph (2), the penalty imposed under subsection (a) with respect to any failure shall be \$50,000.

'(2) **LISTED TRANSACTIONS**- The penalty imposed under subsection (a) with respect to any listed transaction shall be an amount equal to the greater of-

'(A) \$200,000, or

``(B) 50 percent of the gross income derived by such person with respect to aid, assistance, or advice which is provided with respect to the listed transaction before the date the return is filed under section 6111.

Subparagraph (B) shall be applied by substituting `75 percent' for `50 percent' in the case of an intentional failure or act described in subsection (a).

``(c) RESCISSION AUTHORITY- The provisions of section 6707A(d) (relating to authority of Commissioner to rescind penalty) shall apply to any penalty imposed under this section.

``(d) REPORTABLE AND LISTED TRANSACTIONS- For purposes of this section, the terms `reportable transaction' and `listed transaction' have the respective meanings given to such terms by section 6707A(c).'

(b) CLERICAL AMENDMENT- The item relating to section 6707 in the table of sections for part I of subchapter B of chapter 68 is amended by striking `tax shelters' and inserting `reportable transactions'.

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

## **SEC. 817. MODIFICATION OF PENALTY FOR FAILURE TO MAINTAIN LISTS OF INVESTORS.**

(a) IN GENERAL- Subsection (a) of section 6708 is amended to read as follows:

``(a) IMPOSITION OF PENALTY-

``(1) IN GENERAL- If any person who is required to maintain a list under section 6112(a) fails to make such list available upon written request to the Secretary in accordance with section 6112(b) within 20 business days after the date of such request, such person shall pay a penalty of \$10,000 for each day of such failure after such 20th day.

``(2) REASONABLE CAUSE EXCEPTION- No penalty shall be imposed by paragraph (1) with respect to the failure on any day if such failure is due to reasonable cause.'

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

## **SEC. 818. PENALTY ON PROMOTERS OF TAX SHELTERS.**

(a) PENALTY ON PROMOTING ABUSIVE TAX SHELTERS- Section 6700(a) is amended by adding at the end the following new sentence: `Notwithstanding the first sentence, if an activity with respect to which a penalty imposed under this subsection involves a statement described in paragraph (2)(A), the amount of the penalty shall be equal to 50 percent of the gross income derived (or to be derived) from such activity by the person on which the penalty is imposed.'

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

## **SEC. 819. MODIFICATIONS OF SUBSTANTIAL UNDERSTATEMENT PENALTY FOR NONREPORTABLE TRANSACTIONS.**

(a) SUBSTANTIAL UNDERSTATEMENT OF CORPORATIONS- Section 6662(d)(1)(B) (relating to special rule for corporations) is amended to read as follows:

`(B) SPECIAL RULE FOR CORPORATIONS- In the case of a corporation other than an S corporation or a personal holding company (as defined in section 542), there is a substantial understatement of income tax for any taxable year if the amount of the understatement for the taxable year exceeds the lesser of-

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

`(ii) \$10,000,000.'

(b) SECRETARIAL LIST-

(1) IN GENERAL- Section 6662(d) is amended by adding at the end the following new paragraph:

`(3) SECRETARIAL LIST- The Secretary may prescribe a list of positions which the Secretary believes do not meet the 1 or more of the standards specified in paragraph (2)(B)(i), section 6664(d)(2), and section 6694(a)(1). Such list (and any revisions thereof) shall be published in the Federal Register or the Internal Revenue Bulletin.'

(2) CONFORMING AMENDMENT- Paragraph (2) of section 6662(d) is amended by striking subparagraph (D).

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

## **SEC. 820. MODIFICATION OF ACTIONS TO ENJOIN CERTAIN CONDUCT RELATED TO TAX SHELTERS AND REPORTABLE TRANSACTIONS.**

(a) IN GENERAL- Section 7408 (relating to action to enjoin promoters of abusive tax shelters, etc.) is amended by redesignating subsection (c) as subsection (d) and by striking subsections (a) and (b) and inserting the following new subsections:

`(a) AUTHORITY TO SEEK INJUNCTION- A civil action in the name of the United States to enjoin any person from further engaging in specified conduct may be commenced at the request of the Secretary. Any action under this section shall be brought in the district court of the United States for the district in which such person resides, has his principal place of business, or has engaged in specified conduct. The court may exercise its jurisdiction over such action (as provided in section 7402(a)) separate and apart from any other action brought by the United States against such person.

`(b) ADJUDICATION AND DECREE- In any action under subsection (a), if the court finds--

`(1) that the person has engaged in any specified conduct, and

`(2) that injunctive relief is appropriate to prevent recurrence of such conduct, the court may enjoin such person from engaging in such conduct or in any other activity subject to penalty under this title.

`(c) SPECIFIED CONDUCT- For purposes of this section, the term 'specified conduct' means any action, or failure to take action, which is--

`(1) subject to penalty under section 6700, 6701, 6707, or 6708, or

`(2) in violation of any requirement under regulations issued under section 330 of title 31, United States Code.'

(b) CONFORMING AMENDMENTS- (1) The heading for section 7408 is amended to read as follows:

**`SEC. 7408. ACTIONS TO ENJOIN SPECIFIED CONDUCT RELATED TO TAX SHELTERS AND REPORTABLE TRANSACTIONS.'.**

(2) The table of sections for subchapter A of chapter 76 is amended by striking the item relating to section 7408 and inserting the following new item:

**`Sec. 7408. Actions to enjoin specified conduct related to tax shelters and reportable transactions.'.**

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

**SEC. 821. PENALTY ON FAILURE TO REPORT INTERESTS IN FOREIGN FINANCIAL ACCOUNTS.**

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

**`(5) FOREIGN FINANCIAL AGENCY TRANSACTION VIOLATION-**

**`(A) PENALTY AUTHORIZED-** The Secretary of the Treasury may impose a civil money penalty on any person who violates, or causes any violation of, any provision of section 5314.

**`(B) AMOUNT OF PENALTY-**

**`(i) IN GENERAL-** Except as provided in subparagraph (C), the amount of any civil penalty imposed under subparagraph (A) shall not exceed \$10,000.

**`(ii) REASONABLE CAUSE EXCEPTION-** No penalty shall be imposed under subparagraph (A) with respect to any violation if--

**`(I) such violation was due to reasonable cause, and**

**`(II) the amount of the transaction or the balance in the account at the time of the transaction was properly reported.**

**`(C) WILLFUL VIOLATIONS-** In the case of any person willfully violating, or willfully causing any violation of, any provision of section 5314--

**`(i) the maximum penalty under subparagraph (B)(i) shall be increased to the greater of--**

**`(I) \$100,000, or**

**`(II) 50 percent of the amount determined under subparagraph (D), and**

**`(ii) subparagraph (B)(ii) shall not apply.**

**`(D) AMOUNT-** The amount determined under this subparagraph is--

**`(i) in the case of a violation involving a transaction, the amount of the transaction, or**

**`(ii) in the case of a violation involving a failure to report the existence of an account or any identifying information required to be provided with respect to an account, the balance in the account at the time of the violation.'**

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

**SEC. 822. REGULATION OF INDIVIDUALS PRACTICING BEFORE THE DEPARTMENT OF THE TREASURY.**

(a) CENSURE; IMPOSITION OF PENALTY-

(1) IN GENERAL- Section 330(b) of title 31, United States Code, is amended--

(A) by inserting `, or censure,' after `Department', and

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

`The Secretary may impose a monetary penalty on any representative described in the preceding sentence. If the representative was acting on behalf of an employer or any firm or other entity in connection with the conduct giving rise to such penalty, the Secretary may impose a monetary penalty on such employer, firm, or entity if it knew, or reasonably should have known, of such conduct. Such penalty shall not exceed the gross income derived (or to be derived) from the conduct giving rise to the penalty and may be in addition to, or in lieu of, any suspension, disbarment, or censure of the representative.'

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

(b) TAX SHELTER OPINIONS, ETC- Section 330 of such title 31 is amended by adding at the end the following new subsection:

`(d) Nothing in this section or in any other provision of law shall be construed to limit the authority of the Secretary of the Treasury to impose standards applicable to the rendering of written advice with respect to any entity, transaction plan or arrangement, or other plan or arrangement, which is of a type which the Secretary determines as having a potential for tax avoidance or evasion.'

## ***Part II--Other Provisions***

### **SEC. 831. TREATMENT OF STRIPPED INTERESTS IN BOND AND PREFERRED STOCK FUNDS, ETC.**

(a) IN GENERAL- Section 1286 (relating to tax treatment of stripped bonds) is amended by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) the following new subsection:

`(f) TREATMENT OF STRIPPED INTERESTS IN BOND AND PREFERRED STOCK FUNDS, ETC- In the case of an account or entity substantially all of the assets of which consist of bonds, preferred stock, or a combination thereof, the Secretary may by regulations provide that rules similar to the rules of this section and 305(e), as appropriate, shall apply to interests in such account or entity to which (but for this subsection) this section or section 305(e), as the case may be, would not apply.'

(b) CROSS REFERENCE- Subsection (e) of section 305 is amended by adding at the end the following new paragraph:

`(7) CROSS REFERENCE-

`For treatment of stripped interests in certain accounts or entities holding preferred stock, see section 1286(f).'

(c) EFFECTIVE DATE- The amendments made by this section shall apply to purchases and dispositions after the date of the enactment of this Act.

## **SEC. 832. MINIMUM HOLDING PERIOD FOR FOREIGN TAX CREDIT ON WITHHOLDING TAXES ON INCOME OTHER THAN DIVIDENDS.**

(a) IN GENERAL- Section 901 is amended by redesignating subsection (l) as subsection (m) and by inserting after subsection (k) the following new subsection:

### **^(I) MINIMUM HOLDING PERIOD FOR WITHHOLDING TAXES ON GAIN AND INCOME OTHER THAN DIVIDENDS ETC-**

^(1) IN GENERAL- In no event shall a credit be allowed under subsection (a) for any withholding tax (as defined in subsection (k)) on any item of income or gain with respect to any property if--

^(A) such property is held by the recipient of the item for 15 days or less during the 31-day period beginning on the date which is 15 days before the date on which the right to receive payment of such item arises, or

^(B) to the extent that the recipient of the item is under an obligation (whether pursuant to a short sale or otherwise) to make related payments with respect to positions in substantially similar or related property.

This paragraph shall not apply to any dividend to which subsection (k) applies.

### **^(2) EXCEPTION FOR TAXES PAID BY DEALERS-**

^(A) IN GENERAL- Paragraph (1) shall not apply to any qualified tax with respect to any property held in the active conduct in a foreign country of a business as a dealer in such property.

^(B) QUALIFIED TAX- For purposes of subparagraph (A), the term 'qualified tax' means a tax paid to a foreign country (other than the foreign country referred to in subparagraph (A)) if--

^(i) the item to which such tax is attributable is subject to taxation on a net basis by the country referred to in subparagraph (A), and

^(ii) such country allows a credit against its net basis tax for the full amount of the tax paid to such other foreign country.

^(C) DEALER- For purposes of subparagraph (A), the term 'dealer' means--

^(i) with respect to a security, any person to whom paragraphs (1) and (2) of subsection (k) would not apply by reason of paragraph (4) thereof if such security were stock, and

^(ii) with respect to any other property, any person with respect to whom such property is described in section 1221(a)(1).

^(D) REGULATIONS- The Secretary may prescribe such regulations as may be appropriate to carry out this paragraph, including regulations to prevent the abuse of the exception provided by this paragraph and to treat other taxes as qualified taxes.

^(3) EXCEPTIONS- The Secretary may by regulation provide that paragraph (1) shall not apply to property where the Secretary determines that the application of paragraph (1) to such property is not necessary to carry out the purposes of this subsection.

^(4) CERTAIN RULES TO APPLY- Rules similar to the rules of paragraphs (5), (6), and (7) of subsection (k) shall apply for purposes of this subsection.

^(5) DETERMINATION OF HOLDING PERIOD- Holding periods shall be determined for purposes of this subsection without regard to section 1235 or any similar rule.'

(b) CONFORMING AMENDMENT- The heading of subsection (k) of section 901 is amended by inserting 'ON DIVIDENDS' after 'TAXES'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to amounts paid or accrued more than 30 days after the date of the enactment of this Act.

## **SEC. 833. DISALLOWANCE OF CERTAIN PARTNERSHIP LOSS TRANSFERS.**

### **(a) TREATMENT OF CONTRIBUTED PROPERTY WITH BUILT-IN LOSS-**

Paragraph (1) of section 704(c) is amended by striking `and' at the end of subparagraph (A), by striking the period at the end of subparagraph (B) and inserting `, and', and by adding at the end the following:

`(C) if any property so contributed has a built-in loss--

`(i) such built-in loss shall be taken into account only in determining the amount of items allocated to the contributing partner, and

`(ii) except as provided in regulations, in determining the amount of items allocated to other partners, the basis of the contributed property in the hands of the partnership shall be treated as being equal to its fair market value at the time of contribution.

For purposes of subparagraph (C), the term `built-in loss' means the excess of the adjusted basis of the property (determined without regard to subparagraph (C)(ii)) over its fair market value at the time of contribution.'

### **(b) SPECIAL RULES FOR TRANSFERS OF PARTNERSHIP INTEREST IF THERE IS SUBSTANTIAL BUILT-IN LOSS-**

(1) ADJUSTMENT OF PARTNERSHIP BASIS REQUIRED- Subsection (a) of section 743 (relating to optional adjustment to basis of partnership property) is amended by inserting before the period `or unless the partnership has a substantial built-in loss immediately after such transfer'.

(2) ADJUSTMENT- Subsection (b) of section 743 is amended by inserting `or which has a substantial built-in loss immediately after such transfer' after `section 754 is in effect'.

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

#### **`(d) SUBSTANTIAL BUILT-IN LOSS-**

`(1) IN GENERAL- For purposes of this section, a partnership has a substantial built-in loss with respect to a transfer of an interest in a partnership if the partnership's adjusted basis in the partnership property exceeds by more than \$250,000 the fair market value of such property.

`(2) REGULATIONS- The Secretary shall prescribe such regulations as may be appropriate to carry out the purposes of paragraph (1) and section 734(d), including regulations aggregating related partnerships and disregarding property acquired by the partnership in an attempt to avoid such purposes.'

### **(4) ALTERNATIVE RULES FOR ELECTING INVESTMENT PARTNERSHIPS-**

(A) IN GENERAL- Section 743 is amended by adding after subsection (d) the following new subsection:

#### **`(e) ALTERNATIVE RULES FOR ELECTING INVESTMENT PARTNERSHIPS-**

`(1) NO ADJUSTMENT OF PARTNERSHIP BASIS- For purposes of this section, an electing investment partnership shall not be treated as having a substantial built-in loss with respect to any transfer occurring while the election under paragraph (6)(A) is in effect.

- `(2) LOSS DEFERRAL FOR TRANSFEREE PARTNER- In the case of a transfer of an interest in an electing investment partnership, the transferee partner's distributive share of losses (without regard to gains) from the sale or exchange of partnership property shall not be allowed except to the extent that it is established that such losses exceed the loss (if any) recognized by the transferor (or any prior transferor to the extent not fully offset by a prior disallowance under this paragraph) on the transfer of the partnership interest.
- `(3) NO REDUCTION IN PARTNERSHIP BASIS- Losses disallowed under paragraph (2) shall not decrease the transferee partner's basis in the partnership interest.
- `(4) EFFECT OF TERMINATION OF PARTNERSHIP- This subsection shall be applied without regard to any termination of a partnership under section 708(b)(1)(B).
- `(5) CERTAIN BASIS REDUCTIONS TREATED AS LOSSES- In the case of a transferee partner whose basis in property distributed by the partnership is reduced under section 732(a)(2), the amount of the loss recognized by the transferor on the transfer of the partnership interest which is taken into account under paragraph (2) shall be reduced by the amount of such basis reduction.
- `(6) ELECTING INVESTMENT PARTNERSHIP- For purposes of this subsection, the term 'electing investment partnership' means any partnership if-
  - `(A) the partnership makes an election to have this subsection apply,
  - `(B) the partnership would be an investment company under section 3(a)(1)(A) of the Investment Company Act of 1940 but for an exemption under paragraph (1) or (7) of section 3(c) of such Act,
  - `(C) such partnership has never been engaged in a trade or business,
  - `(D) substantially all of the assets of such partnership are held for investment,
  - `(E) at least 95 percent of the assets contributed to such partnership consist of money,
  - `(F) no assets contributed to such partnership had an adjusted basis in excess of fair market value at the time of contribution,
  - `(G) all partnership interests of such partnership are issued by such partnership pursuant to a private offering before the date which is 24 months after the date of the first capital contribution to such partnership,
  - `(H) the partnership agreement of such partnership has substantive restrictions on each partner's ability to cause a redemption of the partner's interest, and
  - `(I) the partnership agreement of such partnership provides for a term that is not in excess of 15 years.
- The election described in subparagraph (A), once made, shall be irrevocable except with the consent of the Secretary.
- `(7) REGULATIONS- The Secretary shall prescribe such regulations as may be appropriate to carry out the purposes of this subsection, including regulations for applying this subsection to tiered partnerships.'
- (B) INFORMATION REPORTING- Section 6031 is amended by adding at the end the following new subsection:
  - `(f) ELECTING INVESTMENT PARTNERSHIPS- In the case of any electing investment partnership (as defined in section 743(e)(6)), the information required under subsection (b) to be furnished to any partner to whom section 743(e)(2) applies shall include such information as is necessary to enable the partner to compute the amount of losses disallowed under section 743(e).'

(5) SPECIAL RULE FOR SECURITIZATION PARTNERSHIPS- Section 743 is amended by adding after subsection (e) the following new subsection:

`(f) EXCEPTION FOR SECURITIZATION PARTNERSHIPS-

`(1) NO ADJUSTMENT OF PARTNERSHIP BASIS- For purposes of this section, a securitization partnership shall not be treated as having a substantial built-in loss with respect to any transfer.

`(2) SECURITIZATION PARTNERSHIP- For purposes of paragraph (1), the term `securitization partnership' means any partnership the sole business activity of which is to issue securities which provide for a fixed principal (or similar) amount and which are primarily serviced by the cash flows of a discrete pool (either fixed or revolving) of receivables or other financial assets that by their terms convert into cash in a finite period, but only if the sponsor of the pool reasonably believes that the receivables and other financial assets comprising the pool are not acquired so as to be disposed of.'

(6) CLERICAL AMENDMENTS- (A) The section heading for section 743 is amended to read as follows:

**`SEC. 743. SPECIAL RULES WHERE SECTION 754 ELECTION OR SUBSTANTIAL BUILT-IN LOSS.'**

(B) The table of sections for subpart C of part II of subchapter K of chapter 1 is amended by striking the item relating to section 743 and inserting the following new item:

`Sec. 743. Special rules where section 754 election or substantial built-in loss.'

(c) ADJUSTMENT TO BASIS OF UNDISTRIBUTED PARTNERSHIP PROPERTY IF THERE IS SUBSTANTIAL BASIS REDUCTION-

(1) ADJUSTMENT REQUIRED- Subsection (a) of section 734 (relating to optional adjustment to basis of undistributed partnership property) is amended by inserting before the period the following: `or unless there is a substantial basis reduction'.

(2) ADJUSTMENT- Subsection (b) of section 734 is amended by inserting `or unless there is a substantial basis reduction' after `section 754 is in effect'.

(3) SUBSTANTIAL BASIS REDUCTION- Section 734 is amended by adding at the end the following new subsection:

`(d) SUBSTANTIAL BASIS REDUCTION-

`(1) IN GENERAL- For purposes of this section, there is a substantial basis reduction with respect to a distribution if the sum of the amounts described in subparagraphs (A) and (B) of subsection (b)(2) exceeds \$250,000.

`(2) REGULATIONS-

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

(4) EXCEPTION FOR SECURITIZATION PARTNERSHIPS- Section 734 is amended by inserting after subsection (d) the following new subsection:

`(e) EXCEPTION FOR SECURITIZATION PARTNERSHIPS- For purposes of this section, a securitization partnership (as defined in section 743(f)) shall not be treated as having a substantial basis reduction with respect to any distribution of property to a partner.'

(5) CLERICAL AMENDMENTS- (A) The section heading for section 734 is amended to read as follows:

**SEC. 734. ADJUSTMENT TO BASIS OF UNDISTRIBUTED PARTNERSHIP PROPERTY WHERE SECTION 754 ELECTION OR SUBSTANTIAL BASIS REDUCTION.‘.**

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

‘Sec. 734. Adjustment to basis of undistributed partnership property where section 754 election or substantial basis reduction.‘.

(d) EFFECTIVE DATES-

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

(2) SUBSECTION (b)-

(A) IN GENERAL- Except as provided in subparagraph (B), the amendments made by subsection (b) shall apply to transfers after the date of the enactment of this Act.

(B) TRANSITION RULE- In the case of an electing investment partnership which is in existence on June 4, 2004, section 743(e)(6)(H) of the Internal Revenue Code of 1986, as added by this section, shall not apply to such partnership and section 743(e)(6)(I) of such Code, as so added, shall be applied by substituting ‘20 years’ for ‘15 years’.

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

**SEC. 834. NO REDUCTION OF BASIS UNDER SECTION 734 IN STOCK HELD BY PARTNERSHIP IN CORPORATE PARTNER.**

(a) IN GENERAL- Section 755 is amended by adding at the end the following new subsection:

‘(c) NO ALLOCATION OF BASIS DECREASE TO STOCK OF CORPORATE PARTNER- In making an allocation under subsection (a) of any decrease in the adjusted basis of partnership property under section 734(b)--

‘(1) no allocation may be made to stock in a corporation (or any person related (within the meaning of sections 267(b) and 707(b)(1)) to such corporation) which is a partner in the partnership, and

‘(2) any amount not allocable to stock by reason of paragraph (1) shall be allocated under subsection (a) to other partnership property.

Gain shall be recognized to the partnership to the extent that the amount required to be allocated under paragraph (2) to other partnership property exceeds the aggregate adjusted basis of such other property immediately before the allocation required by paragraph (2).‘.

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

## SEC. 835. REPEAL OF SPECIAL RULES FOR FASITS.

(a) IN GENERAL- Part V of subchapter M of chapter 1 (relating to financial asset securitization investment trusts) is hereby repealed.

(b) CONFORMING AMENDMENTS-

(1) Paragraph (6) of section 56(g) is amended by striking 'REMIC, or FASIT' and inserting 'or REMIC'.

(2) Clause (ii) of section 382(l)(4)(B) is amended by striking 'a REMIC to which part IV of subchapter M applies, or a FASIT to which part V of subchapter M applies,' and inserting 'or a REMIC to which part IV of subchapter M applies,'.

(3) Paragraph (1) of section 582(c) is amended by striking ' , and any regular interest in a FASIT,'.

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

(5)(A) Section 860G(a)(1) is amended by adding at the end the following new sentence: 'An interest shall not fail to qualify as a regular interest solely because the specified principal amount of the regular interest (or the amount of interest accrued on the regular interest) can be reduced as a result of the nonoccurrence of 1 or more contingent payments with respect to any reverse mortgage loan held by the REMIC if, on the startup day for the REMIC, the sponsor reasonably believes that all principal and interest due under the regular interest will be paid at or prior to the liquidation of the REMIC.'

(B) The last sentence of section 860G(a)(3) is amended by inserting ' , and any reverse mortgage loan (and each balance increase on such loan meeting the requirements of subparagraph (A)(iii)) shall be treated as an obligation secured by an interest in real property' before the period at the end.

(6) Paragraph (3) of section 860G(a) is amended by adding 'and' at the end of subparagraph (B), by striking ' , and' at the end of subparagraph (C) and inserting a period, and by striking subparagraph (D).

(7) Section 860G(a)(3), as amended by paragraph (6), is amended by adding at the end the following new sentence: 'For purposes of subparagraph (A), if more than 50 percent of the obligations transferred to, or purchased by, the REMIC are originated by the United States or any State (or any political subdivision, agency, or instrumentality of the United States or any State) and are principally secured by an interest in real property, then each obligation transferred to, or purchased by, the REMIC shall be treated as secured by an interest in real property.'

(8)(A) Section 860G(a)(3)(A) is amended by striking 'or' at the end of clause (i), by inserting 'or' at the end of clause (ii), and by inserting after clause (ii) the following new clause:

`(iii) represents an increase in the principal amount under the original terms of an obligation described in clause (i) or (ii) if such increase--

`(I) is attributable to an advance made to the obligor pursuant to the original terms of the obligation,

`(II) occurs after the startup day, and

`(III) is purchased by the REMIC pursuant to a fixed price contract in effect on the startup day.'

(B) Section 860G(a)(7)(B) is amended to read as follows:

``(B) QUALIFIED RESERVE FUND- For purposes of subparagraph (A), the term `qualified reserve fund' means any reasonably required reserve to--

``(i) provide for full payment of expenses of the REMIC or amounts due on regular interests in the event of defaults on qualified mortgages or lower than expected returns on cash flow investments, or

``(ii) provide a source of funds for the purchase of obligations described in clause (ii) or (iii) of paragraph (3)(A).

The aggregate fair market value of the assets held in any such reserve shall not exceed 50 percent of the aggregate fair market value of all of the assets of the REMIC on the startup day, and the amount of any such reserve shall be promptly and appropriately reduced to the extent the amount held in such reserve is no longer reasonably required for purposes specified in clause (i) or (ii) of this subparagraph.'

(9) Subparagraph (C) of section 1202(e)(4) is amended by striking `REMIC, or FASIT' and inserting `or REMIC'.

(10) Clause (xi) of section 7701(a)(19)(C) is amended--

(A) by striking `and any regular interest in a FASIT', and

(B) by striking `or FASIT' each place it appears.

(11) Subparagraph (A) of section 7701(i)(2) is amended by striking `or a FASIT'.

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

(c) EFFECTIVE DATE-

(1) IN GENERAL- Except as provided in paragraph (2), the amendments made by this section shall take effect on January 1, 2005.

(2) EXCEPTION FOR EXISTING FASITS- Paragraph (1) shall not apply to any FASIT in existence on the date of the enactment of this Act to the extent that regular interests issued by the FASIT before such date continue to remain outstanding in accordance with the original terms of issuance.

## **SEC. 836. LIMITATION ON TRANSFER OR IMPORTATION OF BUILT-IN LOSSES.**

(a) IN GENERAL- Section 362 (relating to basis to corporations) is amended by adding at the end the following new subsection:

``(e) LIMITATIONS ON BUILT-IN LOSSES-

``(1) LIMITATION ON IMPORTATION OF BUILT-IN LOSSES-

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

``(B) PROPERTY DESCRIBED- For purposes of subparagraph (A), property is described in this subparagraph if--

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

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

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

^(C) IMPORTATION OF NET BUILT-IN LOSS- For purposes of subparagraph (A), there is an importation of a net built-in loss in a transaction if the transferee's aggregate adjusted bases of property described in subparagraph (B) which is transferred in such transaction would (but for this paragraph) exceed the fair market value of such property immediately after such transaction.

^(2) LIMITATION ON TRANSFER OF BUILT-IN LOSSES IN SECTION 351 TRANSACTIONS-

^(A) IN GENERAL- If--

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

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

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

^(B) ALLOCATION OF BASIS REDUCTION- The aggregate reduction in basis by reason of subparagraph (A) shall be allocated among the property so transferred in proportion to their respective built-in losses immediately before the transaction.

^(C) ELECTION TO APPLY LIMITATION TO TRANSFEROR'S STOCK BASIS-

^(i) IN GENERAL- If the transferor and transferee of a transaction described in subparagraph (A) both elect the application of this subparagraph--

^(I) subparagraph (A) shall not apply, and

^(II) the transferor's basis in the stock received for property to which subparagraph (A) does not apply by reason of the election shall not exceed its fair market value immediately after the transfer.

^(ii) ELECTION- An election under clause (i) shall be included with the return of tax for the taxable year in which the transaction occurred, shall be in such form and manner as the Secretary may prescribe, and, once made, shall be irrevocable.'

(b) COMPARABLE TREATMENT WHERE LIQUIDATION- Paragraph (1) of section 334(b) (relating to liquidation of subsidiary) is amended to read as follows:

^(1) IN GENERAL- If property is received by a corporate distributee in a distribution in a complete liquidation to which section 332 applies (or in a transfer described in section 337(b)(1)), the basis of such property in the hands of such distributee shall be the same as it would be in the hands of the transferor; except that the basis of such property in the hands of such distributee shall be the fair market value of the property at the time of the distribution--

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

^(B) in any case in which the liquidating corporation is a foreign corporation, the corporate distributee is a domestic corporation, and the corporate distributee's aggregate adjusted bases of property described in section 362(e)(1)(B) which is distributed in such

liquidation would (but for this subparagraph) exceed the fair market value of such property immediately after such liquidation.'.

(c) EFFECTIVE DATES-

(1) IN GENERAL- The amendment made by subsection (a) shall apply to transactions after the date of the enactment of this Act.

(2) LIQUIDATIONS- The amendment made by subsection (b) shall apply to liquidations after the date of the enactment of this Act.

**SEC. 837. CLARIFICATION OF BANKING BUSINESS FOR PURPOSES OF DETERMINING INVESTMENT OF EARNINGS IN UNITED STATES PROPERTY.**

(a) IN GENERAL- Subparagraph (A) of section 956(c)(2) is amended to read as follows:

`(A) obligations of the United States, money, or deposits with-

`(i) any bank (as defined by section 2(c) of the Bank Holding Company Act of 1956 (12 U.S.C. 1841(c)), without regard to subparagraphs (C) and (G) of paragraph (2) of such section), or

`(ii) any corporation not described in clause (i) with respect to which a bank holding company (as defined by section 2(a) of such Act) or financial holding company (as defined by section 2(p) of such Act) owns directly or indirectly more than 80 percent by vote or value of the stock of such corporation;'.

(b) EFFECTIVE DATE- The amendment made by this section shall take effect on the date of the enactment of this Act.

**SEC. 838. DENIAL OF DEDUCTION FOR INTEREST ON UNDERPAYMENTS ATTRIBUTABLE TO NONDISCLOSED REPORTABLE TRANSACTIONS.**

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

`(m) INTEREST ON UNPAID TAXES ATTRIBUTABLE TO NONDISCLOSED REPORTABLE TRANSACTIONS- No deduction shall be allowed under this chapter for any interest paid or accrued under section 6601 on any underpayment of tax which is attributable to the portion of any reportable transaction understatement (as defined in section 6662A(b)) with respect to which the requirement of section 6664(d)(2)(A) is not met.'.

(b) EFFECTIVE DATE- The amendments made by this section shall apply to transactions in taxable years beginning after the date of the enactment of this Act.

**SEC. 839. CLARIFICATION OF RULES FOR PAYMENT OF ESTIMATED TAX FOR CERTAIN DEEMED ASSET SALES.**

(a) IN GENERAL- Paragraph (13) of section 338(h) (relating to tax on deemed sale not taken into account for estimated tax purposes) is amended by adding at the end the

following: `The preceding sentence shall not apply with respect to a qualified stock purchase for which an election is made under paragraph (10).`.

(b) EFFECTIVE DATE- The amendment made by subsection (a) shall apply to transactions occurring after the date of the enactment of this Act.

## **SEC. 840. RECOGNITION OF GAIN FROM THE SALE OF A PRINCIPAL RESIDENCE ACQUIRED IN A LIKE-KIND EXCHANGE WITHIN 5 YEARS OF SALE.**

(a) IN GENERAL- Section 121(d) (relating to special rules for exclusion of gain from sale of principal residence) is amended by adding at the end the following new paragraph: `(10) PROPERTY ACQUIRED IN LIKE-KIND EXCHANGE- If a taxpayer acquired property in an exchange to which section 1031 applied, subsection (a) shall not apply to the sale or exchange of such property if it occurs during the 5-year period beginning with the date of the acquisition of such property.`.

(b) EFFECTIVE DATE- The amendment made by this section shall apply to sales or exchanges after the date of the enactment of this Act.

## **SEC. 841. PREVENTION OF MISMATCHING OF INTEREST AND ORIGINAL ISSUE DISCOUNT DEDUCTIONS AND INCOME INCLUSIONS IN TRANSACTIONS WITH RELATED FOREIGN PERSONS.**

(a) ORIGINAL ISSUE DISCOUNT- Section 163(e)(3) (relating to special rule for original issue discount on obligation held by related foreign person) is amended by redesignating subparagraph (B) as subparagraph (C) and by inserting after subparagraph (A) the following new subparagraph:

`(B) SPECIAL RULE FOR CERTAIN FOREIGN ENTITIES-

`(i) IN GENERAL- In the case of any debt instrument having original issue discount which is held by a related foreign person which is a controlled foreign corporation (as defined in section 957) or a passive foreign investment company (as defined in section 1297), a deduction shall be allowable to the issuer with respect to such original issue discount for any taxable year before the taxable year in which paid only to the extent such original issue discount is includible (determined without regard to properly allocable deductions and qualified deficits under section 952(c)(1)(B)) during such prior taxable year in the gross income of a United States person who owns (within the meaning of section 958(a)) stock in such corporation.

`(ii) SECRETARIAL AUTHORITY- The Secretary may by regulation exempt transactions from the application of clause (i), including any transaction which is entered into by a payor in the ordinary course of a trade or business in which the payor is predominantly engaged.`.

(b) INTEREST AND OTHER DEDUCTIBLE AMOUNTS- Section 267(a)(3) is amended--

(1) by striking `The Secretary` and inserting:

`(A) IN GENERAL- The Secretary`, and

(2) by adding at the end the following new subparagraph:

**^(B) SPECIAL RULE FOR CERTAIN FOREIGN ENTITIES-**

^(i) IN GENERAL- Notwithstanding subparagraph (A), in the case of any item payable to a controlled foreign corporation (as defined in section 957) or a passive foreign investment company (as defined in section 1297), a deduction shall be allowable to the payor with respect to such amount for any taxable year before the taxable year in which paid only to the extent that an amount attributable to such item is includible (determined without regard to properly allocable deductions and qualified deficits under section 952(c)(1)(B)) during such prior taxable year in the gross income of a United States person who owns (within the meaning of section 958(a)) stock in such corporation.

^(ii) SECRETARIAL AUTHORITY- The Secretary may by regulation exempt transactions from the application of clause (i), including any transaction which is entered into by a payor in the ordinary course of a trade or business in which the payor is predominantly engaged and in which the payment of the accrued amounts occurs within 8 1/2 months after accrual or within such other period as the Secretary may prescribe.'

(c) EFFECTIVE DATE- The amendments made by this section shall apply to payments accrued on or after the date of the enactment of this Act.

**SEC. 842. DEPOSITS MADE TO SUSPEND RUNNING OF INTEREST ON POTENTIAL UNDERPAYMENTS.**

(a) IN GENERAL- Subchapter A of chapter 67 (relating to interest on underpayments) is amended by adding at the end the following new section:

**^SEC. 6603. DEPOSITS MADE TO SUSPEND RUNNING OF INTEREST ON POTENTIAL UNDERPAYMENTS, ETC.**

^(a) AUTHORITY TO MAKE DEPOSITS OTHER THAN AS PAYMENT OF TAX- A taxpayer may make a cash deposit with the Secretary which may be used by the Secretary to pay any tax imposed under subtitle A or B or chapter 41, 42, 43, or 44 which has not been assessed at the time of the deposit. Such a deposit shall be made in such manner as the Secretary shall prescribe.

^(b) NO INTEREST IMPOSED- To the extent that such deposit is used by the Secretary to pay tax, for purposes of section 6601 (relating to interest on underpayments), the tax shall be treated as paid when the deposit is made.

^(c) RETURN OF DEPOSIT- Except in a case where the Secretary determines that collection of tax is in jeopardy, the Secretary shall return to the taxpayer any amount of the deposit (to the extent not used for a payment of tax) which the taxpayer requests in writing.

**^(d) PAYMENT OF INTEREST-**

^(1) IN GENERAL- For purposes of section 6611 (relating to interest on overpayments), except as provided in paragraph (4), a deposit which is returned to a taxpayer shall be treated as a payment of tax for any period to the extent (and only to the extent) attributable to a disputable tax for such period. Under regulations prescribed by the Secretary, rules similar to the rules of section 6611(b)(2) shall apply.

**^(2) DISPUTABLE TAX-**

``(A) IN GENERAL- For purposes of this section, the term `disputable tax' means the amount of tax specified at the time of the deposit as the taxpayer's reasonable estimate of the maximum amount of any tax attributable to disputable items.

``(B) SAFE HARBOR BASED ON 30-DAY LETTER- In the case of a taxpayer who has been issued a 30-day letter, the maximum amount of tax under subparagraph (A) shall not be less than the amount of the proposed deficiency specified in such letter.

``(3) OTHER DEFINITIONS- For purposes of paragraph (2)--

``(A) DISPUTABLE ITEM- The term `disputable item' means any item of income, gain, loss, deduction, or credit if the taxpayer--

``(i) has a reasonable basis for its treatment of such item, and

``(ii) reasonably believes that the Secretary also has a reasonable basis for disallowing the taxpayer's treatment of such item.

``(B) 30-DAY LETTER- The term `30-day letter' means the first letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the Internal Revenue Service Office of Appeals.

``(4) RATE OF INTEREST- The rate of interest under this subsection shall be the Federal short-term rate determined under section 6621(b), compounded daily.

``(e) USE OF DEPOSITS-

``(1) PAYMENT OF TAX- Except as otherwise provided by the taxpayer, deposits shall be treated as used for the payment of tax in the order deposited.

``(2) RETURNS OF DEPOSITS- Deposits shall be treated as returned to the taxpayer on a last-in, first-out basis.'

(b) CLERICAL AMENDMENT- The table of sections for subchapter A of chapter 67 is amended by adding at the end the following new item:

``Sec. 6603. Deposits made to suspend running of interest on potential underpayments, etc.'

(c) EFFECTIVE DATE-

(1) IN GENERAL- The amendments made by this section shall apply to deposits made after the date of the enactment of this Act.

(2) COORDINATION WITH DEPOSITS MADE UNDER REVENUE PROCEDURE 84-58- In the case of an amount held by the Secretary of the Treasury or his delegate on the date of the enactment of this Act as a deposit in the nature of a cash bond deposit pursuant to Revenue Procedure 84-58, the date that the taxpayer identifies such amount as a deposit made pursuant to section 6603 of the Internal Revenue Code (as added by this Act) shall be treated as the date such amount is deposited for purposes of such section 6603.

## **SEC. 843. PARTIAL PAYMENT OF TAX LIABILITY IN INSTALLMENT AGREEMENTS.**

(a) IN GENERAL-

(1) Section 6159(a) (relating to authorization of agreements) is amended--

(A) by striking `satisfy liability for payment of' and inserting `make payment on', and

(B) by inserting `full or partial' after `facilitate'.

(2) Section 6159(c) (relating to Secretary required to enter into installment agreements in certain cases) is amended in the matter preceding paragraph (1) by inserting 'full' before 'payment'.

(b) REQUIREMENT TO REVIEW PARTIAL PAYMENT AGREEMENTS EVERY TWO YEARS- Section 6159 is amended by redesignating subsections (d) and (e) as subsections (e) and (f), respectively, and inserting after subsection (c) the following new subsection:

`(d) SECRETARY REQUIRED TO REVIEW INSTALLMENT AGREEMENTS FOR PARTIAL COLLECTION EVERY TWO YEARS- In the case of an agreement entered into by the Secretary under subsection (a) for partial collection of a tax liability, the Secretary shall review the agreement at least once every 2 years.'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to agreements entered into on or after the date of the enactment of this Act.

#### **SEC. 844. AFFIRMATION OF CONSOLIDATED RETURN REGULATION AUTHORITY.**

(a) IN GENERAL- Section 1502 is amended by adding at the end the following new sentence: 'In carrying out the preceding sentence, the Secretary may prescribe rules that are different from the provisions of chapter 1 that would apply if such corporations filed separate returns.'

(b) RESULT NOT OVERTURNED- Notwithstanding the amendment made by subsection (a), the Internal Revenue Code of 1986 shall be construed by treating Treasury Regulation Sec. 1.1502-20(c)(1)(iii) (as in effect on January 1, 2001) as being inapplicable to the factual situation in *Rite Aid Corporation and Subsidiary Corporations v. United States*, 255 F.3d 1357 (Fed. Cir. 2001).

(c) EFFECTIVE DATE- This section, and the amendment made by this section, shall apply to taxable years beginning before, on, or after the date of the enactment of this Act.

#### **SEC. 845. EXPANDED DISALLOWANCE OF DEDUCTION FOR INTEREST ON CONVERTIBLE DEBT.**

(a) IN GENERAL- Paragraph (2) of section 163(l) is amended by inserting 'or equity held by the issuer (or any related party) in any other person' after 'or a related party'.

(b) CAPITALIZATION ALLOWED WITH RESPECT TO EQUITY OF PERSONS OTHER THAN ISSUER AND RELATED PARTIES- Section 163(l) is amended by redesignating paragraphs (4) and (5) as paragraphs (5) and (6) and by inserting after paragraph (3) the following new paragraph:

`(4) CAPITALIZATION ALLOWED WITH RESPECT TO EQUITY OF PERSONS OTHER THAN ISSUER AND RELATED PARTIES- If the disqualified debt instrument of a corporation is payable in equity held by the issuer (or any related party) in any other person (other than a related party), the basis of such equity shall be increased by the amount not allowed as a deduction by reason of paragraph (1) with respect to the instrument.'

(c) EXCEPTION FOR CERTAIN INSTRUMENTS ISSUED BY DEALERS IN SECURITIES- Section 163(l), as amended by subsection (b), is amended by

redesignating paragraphs (5) and (6) as paragraphs (6) and (7) and by inserting after paragraph (4) the following new paragraph:

‘(5) EXCEPTION FOR CERTAIN INSTRUMENTS ISSUED BY DEALERS IN SECURITIES- For purposes of this subsection, the term `disqualified debt instrument' does not include indebtedness issued by a dealer in securities (or a related party) which is payable in, or by reference to, equity (other than equity of the issuer or a related party) held by such dealer in its capacity as a dealer in securities. For purposes of this paragraph, the term `dealer in securities' has the meaning given such term by section 475.’.

(d) CONFORMING AMENDMENT- Paragraph (3) of section 163(l) is amended by striking `or a related party' in the material preceding subparagraph (A) and inserting `or any other person'.

(e) EFFECTIVE DATE- The amendments made by this section shall apply to debt instruments issued after October 3, 2004.

### ***Part III--Leasing***

#### **SEC. 847. REFORM OF TAX TREATMENT OF CERTAIN LEASING ARRANGEMENTS.**

(a) CLARIFICATION OF RECOVERY PERIOD FOR TAX-EXEMPT USE PROPERTY SUBJECT TO LEASE- Subparagraph (A) of section 168(g)(3) (relating to special rules for determining class life) is amended by inserting `(notwithstanding any other subparagraph of this paragraph)' after `shall'.

(b) LIMITATION ON DEPRECIATION AND AMORTIZATION PERIODS FOR INTANGIBLES LEASED TO TAX-EXEMPT ENTITY-

(1) COMPUTER SOFTWARE- Paragraph (1) of section 167(f) is amended by adding at the end the following new subparagraph:

‘(C) TAX-EXEMPT USE PROPERTY SUBJECT TO LEASE- In the case of computer software which would be tax-exempt use property as defined in subsection (h) of section 168 if such section applied to computer software, the useful life under subparagraph (A) shall not be less than 125 percent of the lease term (within the meaning of section 168(i)(3)).’.

(2) CERTAIN INTERESTS OR RIGHTS ACQUIRED SEPARATELY- Paragraph (2) of section 167(f) is amended by adding at the end the following new sentence: `If such property would be tax-exempt use property as defined in subsection (h) of section 168 if such section applied to such property, the useful life under such regulations shall not be less than 125 percent of the lease term (within the meaning of section 168(i)(3)).’.

(3) SECTION 197 INTANGIBLES- Section 197(f) (relating to special rules) is amended by adding at the end the following new paragraph:

‘(10) TAX-EXEMPT USE PROPERTY SUBJECT TO LEASE- In the case of any section 197 intangible which would be tax-exempt use property as defined in subsection (h) of section 168 if such section applied to such intangible, the amortization period under this section shall not be less than 125 percent of the lease term (within the meaning of section 168(i)(3)).’.

(c) LEASE TERM TO INCLUDE RELATED SERVICE CONTRACTS- Subparagraph (A) of section 168(i)(3) (relating to lease term) is amended by striking `and' at the end of clause (i), by redesignating clause (ii) as clause (iii), and by inserting after clause (i) the following new clause:

- `(ii) the term of a lease shall include the term of any service contract or similar arrangement (whether or not treated as a lease under section 7701(e))--
- `(I) which is part of the same transaction (or series of related transactions) which includes the lease, and
- `(II) which is with respect to the property subject to the lease or substantially similar property, and'.

(d) EXPANSION OF SHORT-TERM LEASE EXEMPTION FOR QUALIFIED TECHNOLOGICAL EQUIPMENT- Subparagraph (A) of section 168(h)(3) is amended by adding at the end the following new sentence: `Notwithstanding subsection (i)(3)(A)(i), in determining a lease term for purposes of the preceding sentence, there shall not be taken into account any option of the lessee to renew at the fair market value rent determined at the time of renewal; except that the aggregate period not taken into account by reason of this sentence shall not exceed 24 months.'

(e) TREATMENT OF CERTAIN INDIAN TRIBAL GOVERNMENTS AS TAX-EXEMPT ENTITIES- Section 168(h)(2)(A) is amended by striking `and' at the end of clause (ii), by striking the period at the end of clause (iii) and inserting `, and', and by inserting at the end the following:

- `(iv) any Indian tribal government described in section 7701(a)(40).

For purposes of applying this subsection, any Indian tribal government referred to in clause (iv) shall be treated in the same manner as a State.'

## **SEC. 848. LIMITATION ON DEDUCTIONS ALLOCABLE TO PROPERTY USED BY GOVERNMENTS OR OTHER TAX-EXEMPT ENTITIES.**

(a) IN GENERAL- Subpart C of part II of subchapter E of chapter 1 (relating to taxable year for which deductions taken) is amended by adding at the end the following new section:

## **SEC. 470. LIMITATION ON DEDUCTIONS ALLOCABLE TO PROPERTY USED BY GOVERNMENTS OR OTHER TAX-EXEMPT ENTITIES.**

`(a) LIMITATION ON LOSSES- Except as otherwise provided in this section, a tax-exempt use loss for any taxable year shall not be allowed.

`(b) DISALLOWED LOSS CARRIED TO NEXT YEAR- Any tax-exempt use loss with respect to any tax-exempt use property which is disallowed under subsection (a) for any taxable year shall be treated as a deduction with respect to such property in the next taxable year.

`(c) DEFINITIONS- For purposes of this section--

`(1) TAX-EXEMPT USE LOSS- The term `tax-exempt use loss' means, with respect to any taxable year, the amount (if any) by which--

``(A) the sum of--

``(i) the aggregate deductions (other than interest) directly allocable to a tax-exempt use property, plus

``(ii) the aggregate deductions for interest properly allocable to such property, exceed

``(B) the aggregate income from such property.

``(2) TAX-EXEMPT USE PROPERTY- The term 'tax-exempt use property' has the meaning given to such term by section 168(h), except that such section shall be applied--

``(A) without regard to paragraphs (1)(C) and (3) thereof, and

``(B) as if property described in--

``(i) section 167(f)(1)(B),

``(ii) section 167(f)(2), and

``(iii) section 197 intangible,

were tangible property.

Such term shall not include property which would (but for this sentence) be tax-exempt use property solely by reason of section 168(h)(6) if any credit is allowable under section 42 or 47 with respect to such property.

``(d) EXCEPTION FOR CERTAIN LEASES- This section shall not apply to any lease of property which meets the requirements of all of the following paragraphs:

``(1) AVAILABILITY OF FUNDS-

``(A) IN GENERAL- A lease of property meets the requirements of this paragraph if (at any time during the lease term) not more than an allowable amount of funds are--

``(i) subject to any arrangement referred to in subparagraph (B), or

``(ii) set aside or expected to be set aside,

to or for the benefit of the lessor or any lender, or to or for the benefit of the lessee to satisfy the lessee's obligations or options under the lease. For purposes of clause (ii), funds shall be treated as set aside or expected to be set aside only if a reasonable person would conclude, based on the facts and circumstances, that such funds are set aside or expected to be set aside.

``(B) ARRANGEMENTS- The arrangements referred to in this subparagraph include a defeasance arrangement, a loan by the lessee to the lessor or any lender, a deposit arrangement, a letter of credit collateralized with cash or cash equivalents, a payment undertaking agreement, prepaid rent (within the meaning of the regulations under section 467), a sinking fund arrangement, a guaranteed investment contract, financial guaranty insurance, and any similar arrangement (whether or not such arrangement provides credit support).

``(C) ALLOWABLE AMOUNT-

``(i) IN GENERAL- Except as otherwise provided in this subparagraph, the term

``allowable amount' means an amount equal to 20 percent of the lessor's adjusted basis in the property at the time the lease is entered into.

``(ii) HIGHER AMOUNT PERMITTED IN CERTAIN CASES- To the extent provided in regulations, a higher percentage shall be permitted under clause (i) where necessary because of the credit-worthiness of the lessee. In no event may such regulations permit a percentage of more than 50 percent.

``(iii) OPTION TO PURCHASE- If under the lease the lessee has the option to purchase the property for a fixed price or for other than the fair market value of the property

(determined at the time of exercise), the allowable amount at the time such option may be exercised may not exceed 50 percent of the price at which such option may be exercised.

``(iv) NO ALLOWABLE AMOUNT FOR CERTAIN ARRANGEMENTS- The allowable amount shall be zero with respect to any arrangement which involves--

``(I) a loan from the lessee to the lessor or a lender,

``(II) any deposit received, letter of credit issued, or payment undertaking agreement entered into by a lender otherwise involved in the transaction, or

``(III) in the case of a transaction which involves a lender, any credit support made available to the lessor in which any such lender does not have a claim that is senior to the lessor.

For purposes of subclause (I), the term `loan' shall not include any amount treated as a loan under section 467 with respect to a section 467 rental agreement.

``(2) LESSOR MUST MAKE SUBSTANTIAL EQUITY INVESTMENT-

``(A) IN GENERAL- A lease of property meets the requirements of this paragraph if--

``(i) the lessor--

``(I) has at the time the lease is entered into an unconditional at-risk equity investment (as determined by the Secretary) in the property of at least 20 percent of the lessor's adjusted basis in the property as of that time, and

``(II) maintains such investment throughout the term of the lease, and

``(ii) the fair market value of the property at the end of the lease term is reasonably expected to be equal to at least 20 percent of such basis.

``(B) RISK OF LOSS- For purposes of clause (ii), the fair market value at the end of the lease term shall be reduced to the extent that a person other than the lessor bears a risk of loss in the value of the property.

``(C) PARAGRAPH NOT TO APPLY TO SHORT-TERM LEASES- This paragraph shall not apply to any lease with a lease term of 5 years or less.

``(3) LESSEE MAY NOT BEAR MORE THAN MINIMAL RISK OF LOSS-

``(A) IN GENERAL- A lease of property meets the requirements of this paragraph if there is no arrangement under which the lessee bears--

``(i) any portion of the loss that would occur if the fair market value of the leased property were 25 percent less than its reasonably expected fair market value at the time the lease is terminated, or

``(ii) more than 50 percent of the loss that would occur if the fair market value of the leased property at the time the lease is terminated were zero.

``(B) EXCEPTION- The Secretary may by regulations provide that the requirements of this paragraph are not met where the lessee bears more than a minimal risk of loss.

``(C) PARAGRAPH NOT TO APPLY TO SHORT-TERM LEASES- This paragraph shall not apply to any lease with a lease term of 5 years or less.

``(4) PROPERTY WITH MORE THAN 7-YEAR CLASS LIFE- In the case of a lease--

``(A) of property with a class life (as defined in section 168(i)(1)) of more than 7 years, other than fixed-wing aircraft and vessels, and

``(B) under which the lessee has the option to purchase the property,

the lease meets the requirements of this paragraph only if the purchase price under the option equals the fair market value of the property (determined at the time of exercise).

``(e) SPECIAL RULES-

``(1) TREATMENT OF FORMER TAX-EXEMPT USE PROPERTY-

- ``(A) IN GENERAL- In the case of any former tax-exempt use property--
  - ``(i) any deduction allowable under subsection (b) with respect to such property for any taxable year shall be allowed only to the extent of any net income (without regard to such deduction) from such property for such taxable year, and
  - ``(ii) any portion of such unused deduction remaining after application of clause (i) shall be treated as a deduction allowable under subsection (b) with respect to such property in the next taxable year.
- ``(B) FORMER TAX-EXEMPT USE PROPERTY- For purposes of this subsection, the term `former tax-exempt use property' means any property which--
  - ``(i) is not tax-exempt use property for the taxable year, but
  - ``(ii) was tax-exempt use property for any prior taxable year.
- ``(2) DISPOSITION OF ENTIRE INTEREST IN PROPERTY- If during the taxable year a taxpayer disposes of the taxpayer's entire interest in tax-exempt use property (or former tax-exempt use property), rules similar to the rules of section 469(g) shall apply for purposes of this section.
- ``(3) COORDINATION WITH SECTION 469- This section shall be applied before the application of section 469.
- ``(4) COORDINATION WITH SECTIONS 1031 AND 1033-
  - ``(A) IN GENERAL- Sections 1031(a) and 1033(a) shall not apply if--
    - ``(i) the exchanged or converted property is tax-exempt use property subject to a lease which was entered into before March 13, 2004, and which would not have met the requirements of subsection (d) had such requirements been in effect when the lease was entered into, or
    - ``(ii) the replacement property is tax-exempt use property subject to a lease which does not meet the requirements of subsection (d).
  - ``(B) ADJUSTED BASIS- In the case of property acquired by the lessor in a transaction to which section 1031 or 1033 applies, the adjusted basis of such property for purposes of this section shall be equal to the lesser of--
    - ``(i) the fair market value of the property as of the beginning of the lease term, or
    - ``(ii) the amount which would be the lessor's adjusted basis if such sections did not apply to such transaction.
  - ``(f) OTHER DEFINITIONS- For purposes of this section--
    - ``(1) RELATED PARTIES- The terms `lessor', `lessee', and `lender' each include any related party (within the meaning of section 197(f)(9)(C)(i)).
    - ``(2) LEASE TERM- The term `lease term' has the meaning given to such term by section 168(i)(3).
    - ``(3) LENDER- The term `lender' means, with respect to any lease, a person that makes a loan to the lessor which is secured (or economically similar to being secured) by the lease or the leased property.
    - ``(4) LOAN- The term `loan' includes any similar arrangement.
    - ``(g) REGULATIONS- The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations which--
      - ``(1) allow in appropriate cases the aggregation of property subject to the same lease, and
      - ``(2) provide for the determination of the allocation of interest expense for purposes of this section.'

(b) CONFORMING AMENDMENT- The table of sections for subpart C of part II of subchapter E of chapter 1 is amended by adding at the end the following new item:

Sec. 470. Limitation on deductions allocable to property used by governments or other tax-exempt entities.'

## **SEC. 849. EFFECTIVE DATE.**

(a) IN GENERAL- Except as provided in this section, the amendments made by this part shall apply to leases entered into after March 12, 2004.

(b) EXCEPTION-

(1) IN GENERAL- The amendments made by this part shall not apply to qualified transportation property.

(2) QUALIFIED TRANSPORTATION PROPERTY- For purposes of paragraph (1), the term 'qualified transportation property' means domestic property subject to a lease with respect to which a formal application-

(A) was submitted for approval to the Federal Transit Administration (an agency of the Department of Transportation) after June 30, 2003, and before March 13, 2004,

(B) is approved by the Federal Transit Administration before January 1, 2006, and

(C) includes a description of such property and the value of such property.

(3) EXCHANGES AND CONVERSION OF TAX-EXEMPT USE PROPERTY- Section 470(e)(4) of the Internal Revenue Code of 1986, as added by section 848, shall apply to property exchanged or converted after the date of the enactment of this Act.

(4) INTANGIBLES AND INDIAN TRIBAL GOVERNMENTS- The amendments made subsections (b)(2), (b)(3), and (e) of section 847, and the treatment of property described in clauses (ii) and (iii) of section 470(c)(2)(B) of the Internal Revenue Code of 1986 (as added by section 848) as tangible property, shall apply to leases entered into after October 3, 2004.

## **Subtitle C-Reduction of Fuel Tax Evasion**

## **SEC. 851. EXEMPTION FROM CERTAIN EXCISE TAXES FOR MOBILE MACHINERY.**

(a) EXEMPTION FROM TAX ON HEAVY TRUCKS AND TRAILERS SOLD AT RETAIL-

(1) IN GENERAL- Section 4053 (relating to exemptions) is amended by adding at the end the following new paragraph:

“(8) MOBILE MACHINERY- Any vehicle which consists of a chassis--

“(A) to which there has been permanently mounted (by welding, bolting, riveting, or other means) machinery or equipment to perform a construction, manufacturing, processing, farming, mining, drilling, timbering, or similar operation if the operation of the machinery or equipment is unrelated to transportation on or off the public highways,

“(B) which has been specially designed to serve only as a mobile carriage and mount (and a power source, where applicable) for the particular machinery or equipment involved, whether or not such machinery or equipment is in operation, and

``(C) which, by reason of such special design, could not, without substantial structural modification, be used as a component of a vehicle designed to perform a function of transporting any load other than that particular machinery or equipment or similar machinery or equipment requiring such a specially designed chassis.'.

(2) EFFECTIVE DATE- The amendment made by this subsection shall take effect on the day after the date of the enactment of this Act.

(b) EXEMPTION FROM TAX ON USE OF CERTAIN VEHICLES-

(1) IN GENERAL- Section 4483 (relating to exemptions) is amended by redesignating subsection (g) as subsection (h) and by inserting after subsection (f) the following new subsection:

``(g) EXEMPTION FOR MOBILE MACHINERY- No tax shall be imposed by section 4481 on the use of any vehicle described in section 4053(8).''.

(2) EFFECTIVE DATE- The amendments made by this subsection shall take effect on the day after the date of the enactment of this Act.

(c) EXEMPTION FROM TAX ON TIRES-

(1) IN GENERAL- Section 4072(b)(2) is amended by adding at the end the following flush sentence: `Such term shall not include tires of a type used exclusively on vehicles described in section 4053(8).''.

(2) EFFECTIVE DATE- The amendment made by this subsection shall take effect on the day after the date of the enactment of this Act.

(d) REFUND OF FUEL TAXES-

(1) IN GENERAL- Section 6421(e)(2) (defining off-highway business use) is amended by adding at the end the following new subparagraph:

``(C) USES IN MOBILE MACHINERY-

``(i) IN GENERAL- The term `off-highway business use' shall include any use in a vehicle which meets the requirements described in clause (ii).

``(ii) REQUIREMENTS FOR MOBILE MACHINERY- The requirements described in this clause are--

``(I) the design-based test, and

``(II) the use-based test.

``(iii) DESIGN-BASED TEST- For purposes of clause (ii)(I), the design-based test is met if the vehicle consists of a chassis--

``(I) to which there has been permanently mounted (by welding, bolting, riveting, or other means) machinery or equipment to perform a construction, manufacturing, processing, farming, mining, drilling, timbering, or similar operation if the operation of the machinery or equipment is unrelated to transportation on or off the public highways,

``(II) which has been specially designed to serve only as a mobile carriage and mount (and a power source, where applicable) for the particular machinery or equipment involved, whether or not such machinery or equipment is in operation, and

``(III) which, by reason of such special design, could not, without substantial structural modification, be used as a component of a vehicle designed to perform a function of transporting any load other than that particular machinery or equipment or similar machinery or equipment requiring such a specially designed chassis.

``(iv) USE-BASED TEST- For purposes of clause (ii)(II), the use-based test is met if the use of the vehicle on public highways was less than 7,500 miles during the taxpayer's taxable year. This clause shall be applied without regard to use of the vehicle by any

organization which is described in section 501(c) and exempt from tax under section 501(a).'.

(2) NO TAX-FREE SALES- Subsection (b) of section 4082 is amended by inserting before the period at the end the following: `and such term shall not include any use described in section 6421(e)(2)(C)'.

(3) ANNUAL REFUND OF TAX PAID- Section 6427(i)(2) (relating to exceptions) is amended by adding at the end the following new subparagraph:

`(C) NONAPPLICATION OF PARAGRAPH- This paragraph shall not apply to any fuel used solely in any off-highway business use described in section 6421(e)(2)(C).'.

(4) EFFECTIVE DATE- The amendments made by this subsection shall apply to taxable years beginning after the date of the enactment of this Act.

## **SEC. 852. MODIFICATION OF DEFINITION OF OFF-HIGHWAY VEHICLE.**

(a) IN GENERAL- Section 7701(a) (relating to definitions) is amended by adding at the end the following new paragraph:

`(48) OFF-HIGHWAY VEHICLES-

`(A) OFF-HIGHWAY TRANSPORTATION VEHICLES-

`(i) IN GENERAL- A vehicle shall not be treated as a highway vehicle if such vehicle is specially designed for the primary function of transporting a particular type of load other than over the public highway and because of this special design such vehicle's capability to transport a load over the public highway is substantially limited or impaired.

`(ii) DETERMINATION OF VEHICLE'S DESIGN- For purposes of clause (i), a vehicle's design is determined solely on the basis of its physical characteristics.

`(iii) DETERMINATION OF SUBSTANTIAL LIMITATION OR IMPAIRMENT- For purposes of clause (i), in determining whether substantial limitation or impairment exists, account may be taken of factors such as the size of the vehicle, whether such vehicle is subject to the licensing, safety, and other requirements applicable to highway vehicles, and whether such vehicle can transport a load at a sustained speed of at least 25 miles per hour. It is immaterial that a vehicle can transport a greater load off the public highway than such vehicle is permitted to transport over the public highway.

`(B) NONTRANSPORTATION TRAILERS AND SEMITRAILERS- A trailer or semitrailer shall not be treated as a highway vehicle if it is specially designed to function only as an enclosed stationary shelter for the carrying on of an off-highway function at an off-highway site.'

(c) EFFECTIVE DATES-

(1) IN GENERAL- Except as provided in paragraph (2), the amendment made by this section shall take effect on the date of the enactment of this Act.

(2) FUEL TAXES- With respect to taxes imposed under subchapter B of chapter 31 and part III of subchapter A of chapter 32, the amendment made by this section shall apply to taxable periods beginning after the date of the enactment of this Act.

## **SEC. 853. TAXATION OF AVIATION-GRADE KEROSENE.**

(a) RATE OF TAX-

(1) IN GENERAL- Subparagraph (A) of section 4081(a)(2) is amended by striking `and' at the end of clause (ii), by striking the period at the end of clause (iii) and inserting `, and', and by adding at the end the following new clause:  
` (iv) in the case of aviation-grade kerosene, 21.8 cents per gallon.'.

(2) COMMERCIAL AVIATION- Paragraph (2) of section 4081(a) is amended by adding at the end the following new subparagraph:  
` (C) TAXES IMPOSED ON FUEL USED IN COMMERCIAL AVIATION- In the case of aviation-grade kerosene which is removed from any refinery or terminal directly into the fuel tank of an aircraft for use in commercial aviation, the rate of tax under subparagraph (A)(iv) shall be 4.3 cents per gallon.'

(3) CERTAIN REFUELER TRUCKS, TANKERS, AND TANK WAGONS TREATED AS TERMINAL-

(A) IN GENERAL- Subsection (a) of section 4081 is amended by adding at the end the following new paragraph:  
` (3) CERTAIN REFUELER TRUCKS, TANKERS, AND TANK WAGONS TREATED AS TERMINAL-

` (A) IN GENERAL- For purposes of paragraph (2)(C), a refueler truck, tanker, or tank wagon shall be treated as part of a terminal if-  
` (i) such terminal is located within a secured area of an airport,  
` (ii) any aviation-grade kerosene which is loaded in such truck, tanker, or wagon at such terminal is for delivery only into aircraft at the airport in which such terminal is located,  
` (iii) such truck, tanker, or wagon meets the requirements of subparagraph (B) with respect to such terminal, and  
` (iv) except in the case of exigent circumstances identified by the Secretary in regulations, no vehicle registered for highway use is loaded with aviation-grade kerosene at such terminal.

` (B) REQUIREMENTS- A refueler truck, tanker, or tank wagon meets the requirements of this subparagraph with respect to a terminal if such truck, tanker, or wagon-  
` (i) has storage tanks, hose, and coupling equipment designed and used for the purposes of fueling aircraft,  
` (ii) is not registered for highway use, and  
` (iii) is operated by-  
` (I) the terminal operator of such terminal, or  
` (II) a person that makes a daily accounting to such terminal operator of each delivery of fuel from such truck, tanker, or wagon.

` (C) REPORTING- The Secretary shall require under section 4101(d) reporting by such terminal operator of-  
` (i) any information obtained under subparagraph (B)(iii)(II), and  
` (ii) any similar information maintained by such terminal operator with respect to deliveries of fuel made by trucks, tankers, or wagons operated by such terminal operator.'

(B) LIST OF AIRPORTS WITH SECURED TERMINALS- Not later than December 15, 2004, the Secretary of the Treasury shall publish and maintain a list of airports which include a secured area in which a terminal is located (within the meaning of section 4081(a)(3)(A)(i) of the Internal Revenue Code of 1986, as added by this paragraph).

(4) LIABILITY FOR TAX ON AVIATION-GRADE KEROSENE USED IN COMMERCIAL AVIATION- Subsection (a) of section 4081 is amended by adding at the end the following new paragraph:

``(4) LIABILITY FOR TAX ON AVIATION-GRADE KEROSENE USED IN COMMERCIAL AVIATION- For purposes of paragraph (2)(C), the person who uses the fuel for commercial aviation shall pay the tax imposed under such paragraph. For purposes of the preceding sentence, fuel shall be treated as used when such fuel is removed into the fuel tank.'.

(5) NONTAXABLE USES-

(A) IN GENERAL- Section 4082 is amended by redesignating subsections (e) and (f) as subsections (f) and (g), respectively, and by inserting after subsection (d) the following new subsection:

``(e) AVIATION-GRADE KEROSENE- In the case of aviation-grade kerosene which is exempt from the tax imposed by section 4041(c) (other than by reason of a prior imposition of tax) and which is removed from any refinery or terminal directly into the fuel tank of an aircraft, the rate of tax under section 4081(a)(2)(A)(iv) shall be zero.'.

(B) CONFORMING AMENDMENTS- (i) Subsection (b) of section 4082 is amended by adding at the end the following new flush sentence:

``The term `nontaxable use' does not include the use of aviation-grade kerosene in an aircraft.'.

(ii) Section 4082(d) is amended by striking paragraph (1) and by redesignating paragraphs (2) and (3) as paragraphs (1) and (2), respectively.

(6) NONAIRCRAFT USE OF AVIATION-GRADE KEROSENE-

(A) IN GENERAL- Subparagraph (B) of section 4041(a)(1) is amended by adding at the end the following new sentence: ``This subparagraph shall not apply to aviation-grade kerosene.'.

(B) CONFORMING AMENDMENT- The heading for paragraph (1) of section 4041(a) is amended by inserting ``AND KEROSENE'' after ``DIESEL FUEL''.

(b) COMMERCIAL AVIATION- Section 4083 is amended by redesignating subsections (b) and (c) as subsections (c) and (d), respectively, and by inserting after subsection (a) the following new subsection:

``(b) COMMERCIAL AVIATION- For purposes of this subpart, the term `commercial aviation' means any use of an aircraft in a business of transporting persons or property for compensation or hire by air, unless properly allocable to any transportation exempt from the taxes imposed by sections 4261 and 4271 by reason of section 4281 or 4282 or by reason of section 4261(h)'.

(c) REFUNDS-

(1) IN GENERAL- Paragraph (4) of section 6427(l) is amended to read as follows:

``(4) REFUNDS FOR AVIATION-GRADE KEROSENE-

``(A) NO REFUND OF CERTAIN TAXES ON FUEL USED IN COMMERCIAL AVIATION- In the case of aviation-grade kerosene used in commercial aviation (as defined in section 4083(b)) (other than supplies for vessels or aircraft within the meaning of section 4221(d)(3)), paragraph (1) shall not apply to so much of the tax imposed by section 4081 as is attributable to--

``(i) the Leaking Underground Storage Tank Trust Fund financing rate imposed by such section, and

- ` (ii) so much of the rate of tax specified in section 4081(a)(2)(A)(iv) as does not exceed 4.3 cents per gallon.
- ` (B) PAYMENT TO ULTIMATE, REGISTERED VENDOR- With respect to aviation-grade kerosene, if the ultimate purchaser of such kerosene waives (at such time and in such form and manner as the Secretary shall prescribe) the right to payment under paragraph (1) and assigns such right to the ultimate vendor, then the Secretary shall pay the amount which would be paid under paragraph (1) to such ultimate vendor, but only if such ultimate vendor--
  - ` (i) is registered under section 4101, and
  - ` (ii) meets the requirements of subparagraph (A), (B), or (D) of section 6416(a)(1).'
- (2) TIME FOR FILING CLAIMS- Subparagraph (A) of section 6427(i)(4) is amended--
  - (A) by striking `subsection (l)(5)' both places it appears and inserting `paragraph (4)(B) or (5) of subsection (l)', and
  - (B) by striking `the preceding sentence' and inserting `subsection (l)(5)'.
- (3) CONFORMING AMENDMENT- Subparagraph (B) of section 6427(l)(2) is amended to read as follows:
  - ` (B) in the case of aviation-grade kerosene--
    - ` (i) any use which is exempt from the tax imposed by section 4041(c) other than by reason of a prior imposition of tax, or
    - ` (ii) any use in commercial aviation (within the meaning of section 4083(b)).'
- (d) REPEAL OF PRIOR TAXATION OF AVIATION FUEL-
- (1) IN GENERAL- Part III of subchapter A of chapter 32 is amended by striking subpart B and by redesignating subpart C as subpart B.
- (2) CONFORMING AMENDMENTS-
  - (A) Section 4041(c) is amended to read as follows:
    - ` (c) AVIATION-GRADE KEROSENE-
      - ` (1) IN GENERAL- There is hereby imposed a tax upon aviation-grade kerosene--
        - ` (A) sold by any person to an owner, lessee, or other operator of an aircraft for use in such aircraft, or
        - ` (B) used by any person in an aircraft unless there was a taxable sale of such fuel under subparagraph (A).
      - ` (2) EXEMPTION FOR PREVIOUSLY TAXED FUEL- No tax shall be imposed by this subsection on the sale or use of any aviation-grade kerosene if tax was imposed on such liquid under section 4081 and the tax thereon was not credited or refunded.
      - ` (3) RATE OF TAX- The rate of tax imposed by this subsection shall be the rate of tax applicable under section 4081(a)(2)(A)(iv) which is in effect at the time of such sale or use.'
    - (B) Section 4041(d)(2) is amended by striking `section 4091' and inserting `section 4081'.
    - (C) Section 4041 is amended by striking subsection (e).
    - (D) Section 4041 is amended by striking subsection (i).
    - (E) Section 4041(m)(1) is amended to read as follows:
      - ` (1) IN GENERAL- In the case of the sale or use of any partially exempt methanol or ethanol fuel the rate of the tax imposed by subsection (a)(2) shall be--
        - ` (A) after September 30, 1997, and before October 1, 2005--
          - ` (i) in the case of fuel none of the alcohol in which consists of ethanol, 9.15 cents per gallon, and

- ``(ii) in any other case, 11.3 cents per gallon, and
- ``(B) after September 30, 2005--
- ``(i) in the case of fuel none of the alcohol in which consists of ethanol, 2.15 cents per gallon, and
- ``(ii) in any other case, 4.3 cents per gallon.'.
- (F) Sections 4101(a), 4103, 4221(a), and 6206 are each amended by striking `, 4081, or 4091' and inserting `or 4081'.
- (G) Section 6416(b)(2) is amended by striking `4091 or'.
- (H) Section 6416(b)(3) is amended by striking `or 4091' each place it appears.
- (I) Section 6416(d) is amended by striking `or to the tax imposed by section 4091 in the case of refunds described in section 4091(d)'.
- (J) Section 6427(j)(1) is amended by striking `, 4081, and 4091' and inserting `and 4081'.
- (K)(i) Section 6427(l)(1) is amended to read as follows:
  - ``(1) IN GENERAL- Except as otherwise provided in this subsection and in subsection (k), if any diesel fuel or kerosene on which tax has been imposed by section 4041 or 4081 is used by any person in a nontaxable use, the Secretary shall pay (without interest) to the ultimate purchaser of such fuel an amount equal to the aggregate amount of tax imposed on such fuel under section 4041 or 4081, as the case may be, reduced by any payment made to the ultimate vendor under paragraph (4)(B).'
  - (ii) Paragraph (5)(B) of section 6427(l) is amended by striking `Paragraph (1)(A) shall not apply to kerosene' and inserting `Paragraph (1) shall not apply to kerosene (other than aviation-grade kerosene)'.
- (L) Subparagraph (B) of section 6724(d)(1), as amended by section 805, is amended by striking clause (xvi) and by redesignating the succeeding clauses accordingly.
- (M) Paragraph (2) of section 6724(d), as amended by section 805, is amended by striking subparagraph (X) and by redesignating the succeeding subparagraphs accordingly.
- (N) Paragraph (1) of section 9502(b) is amended by adding `and' at the end of subparagraph (B) and by striking subparagraphs (C) and (D) and inserting the following new subparagraph:
  - ``(C) section 4081 with respect to aviation gasoline and aviation-grade kerosene, and'.
- (O) The last sentence of section 9502(b) is amended to read as follows:
  - ``There shall not be taken into account under paragraph (1) so much of the taxes imposed by section 4081 as are determined at the rate specified in section 4081(a)(2)(B).'
- (P) Subsection (b) of section 9508 is amended by striking paragraph (3) and by redesignating paragraphs (4) and (5) as paragraphs (3) and (4), respectively.
- (Q) Section 9508(c)(2)(A) is amended by striking `sections 4081 and 4091' and inserting `section 4081'.
- (R) The table of subparts for part III of subchapter A of chapter 32 is amended to read as follows:
  - ``Subpart A. Motor and aviation fuels.
  - ``Subpart B. Special provisions applicable to fuels tax.'
- (S) The heading for subpart A of part III of subchapter A of chapter 32 is amended to read as follows:

## ***'Subpart A--Motor and Aviation Fuels'.***

(T) The heading for subpart B of part III of subchapter A of chapter 32, as redesignated by paragraph (1), is amended to read as follows:

## ***'Subpart B--Special Provisions Applicable to Fuels Tax'.***

(e) **EFFECTIVE DATE**- The amendments made by this section shall apply to aviation-grade kerosene removed, entered, or sold after December 31, 2004.

(f) **FLOOR STOCKS TAX**-

(1) **IN GENERAL**- There is hereby imposed on aviation-grade kerosene held on January 1, 2005, by any person a tax equal to--

(A) the tax which would have been imposed before such date on such kerosene had the amendments made by this section been in effect at all times before such date, reduced by

(B) the sum of--

(i) the tax imposed before such date on such kerosene under section 4091 of the Internal Revenue Code of 1986, as in effect on such date, and

(ii) in the case of kerosene held exclusively for such person's own use, the amount which such person would (but for this clause) reasonably expect (as of such date) to be paid as a refund under section 6427(l) of such Code with respect to such kerosene.

(2) **EXCEPTION FOR FUEL HELD IN AIRCRAFT FUEL TANK**- Paragraph (1) shall not apply to kerosene held in the fuel tank of an aircraft on January 1, 2005.

(3) **LIABILITY FOR TAX AND METHOD OF PAYMENT**-

(A) **LIABILITY FOR TAX**- The person holding the kerosene on January 1, 2005, to which the tax imposed by paragraph (1) applies shall be liable for such tax.

(B) **METHOD AND TIME FOR PAYMENT**- The tax imposed by paragraph (1) shall be paid at such time and in such manner as the Secretary of the Treasury (or the Secretary's delegate) shall prescribe, including the nonapplication of such tax on de minimis amounts of kerosene.

(4) **TRANSFER OF FLOOR STOCK TAX REVENUES TO TRUST FUNDS**- For purposes of determining the amount transferred to any trust fund, the tax imposed by this subsection shall be treated as imposed by section 4081 of the Internal Revenue Code of 1986--

(A) in any case in which tax was not imposed by section 4091 of such Code, at the Leaking Underground Storage Tank Trust Fund financing rate under such section to the extent of 0.1 cents per gallon, and

(B) at the rate under section 4081(a)(2)(A)(iv) of such Code to the extent of the remainder.

(5) **HELD BY A PERSON**- For purposes of this subsection, kerosene shall be considered as held by a person if title thereto has passed to such person (whether or not delivery to the person has been made).

(6) **OTHER LAWS APPLICABLE**- All provisions of law, including penalties, applicable with respect to the tax imposed by section 4081 of such Code shall, insofar as applicable and not inconsistent with the provisions of this subsection, apply with respect to the floor

stock tax imposed by paragraph (1) to the same extent as if such tax were imposed by such section.

## **SEC. 854. DYE INJECTION EQUIPMENT.**

- (a) IN GENERAL- Section 4082(a)(2) (relating to exemptions for diesel fuel and kerosene) is amended by inserting 'by mechanical injection' after 'indelibly dyed'.
- (b) DYE INJECTOR SECURITY- Not later than 180 days after the date of the enactment of this Act, the Secretary of the Treasury shall issue regulations regarding mechanical dye injection systems described in the amendment made by subsection (a), and such regulations shall include standards for making such systems tamper resistant.
- (c) PENALTY FOR TAMPERING WITH OR FAILING TO MAINTAIN SECURITY REQUIREMENTS FOR MECHANICAL DYE INJECTION SYSTEMS-
  - (1) IN GENERAL- Part I of subchapter B of chapter 68 (relating to assessable penalties) is amended by adding after section 6715 the following new section:

### **SEC. 6715A. TAMPERING WITH OR FAILING TO MAINTAIN SECURITY REQUIREMENTS FOR MECHANICAL DYE INJECTION SYSTEMS.**

- ^(a) IMPOSITION OF PENALTY-
  - ^(1) TAMPERING- If any person tampers with a mechanical dye injection system used to indelibly dye fuel for purposes of section 4082, such person shall pay a penalty in addition to the tax (if any).
  - ^(2) FAILURE TO MAINTAIN SECURITY REQUIREMENTS- If any operator of a mechanical dye injection system used to indelibly dye fuel for purposes of section 4082 fails to maintain the security standards for such system as established by the Secretary, then such operator shall pay a penalty in addition to the tax (if any).
- ^(b) AMOUNT OF PENALTY- The amount of the penalty under subsection (a) shall be--
  - ^(1) for each violation described in paragraph (1), the greater of--
    - ^(A) \$25,000, or
    - ^(B) \$10 for each gallon of fuel involved, and
    - ^(2) for each--
      - ^(A) failure to maintain security standards described in paragraph (2), \$1,000, and
      - ^(B) failure to correct a violation described in paragraph (2), \$1,000 per day for each day after which such violation was discovered or such person should have reasonably known of such violation.
  - ^(c) JOINT AND SEVERAL LIABILITY-
    - ^(1) IN GENERAL- If a penalty is imposed under this section on any business entity, each officer, employee, or agent of such entity or other contracting party who willfully participated in any act giving rise to such penalty shall be jointly and severally liable with such entity for such penalty.
    - ^(2) AFFILIATED GROUPS- If a business entity described in paragraph (1) is part of an affiliated group (as defined in section 1504(a)), the parent corporation of such entity shall be jointly and severally liable with such entity for the penalty imposed under this section.'

(2) CLERICAL AMENDMENT- The table of sections for part I of subchapter B of chapter 68 is amended by adding after the item related to section 6715 the following new item:

`Sec. 6715A. Tampering with or failing to maintain security requirements for mechanical dye injection systems.'

(d) EFFECTIVE DATE- The amendments made by subsections (a) and (c) shall take effect on the 180th day after the date on which the Secretary issues the regulations described in subsection (b).

### **SEC. 855. ELIMINATION OF ADMINISTRATIVE REVIEW FOR TAXABLE USE OF DYED FUEL.**

(a) IN GENERAL- Section 6715 is amended by inserting at the end the following new subsection:

`(e) NO ADMINISTRATIVE APPEAL FOR THIRD AND SUBSEQUENT VIOLATIONS- In the case of any person who is found to be subject to the penalty under this section after a chemical analysis of such fuel and who has been penalized under this section at least twice after the date of the enactment of this subsection, no administrative appeal or review shall be allowed with respect to such finding except in the case of a claim regarding--

`(1) fraud or mistake in the chemical analysis, or  
(2) mathematical calculation of the amount of the penalty.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply to penalties assessed after the date of the enactment of this Act.

### **SEC. 856. PENALTY ON UNTAXED CHEMICALLY ALTERED DYED FUEL MIXTURES.**

(a) IN GENERAL- Section 6715(a) (relating to dyed fuel sold for use or used in taxable use, etc.) is amended by striking `or' in paragraph (2), by inserting `or' at the end of paragraph (3), and by inserting after paragraph (3) the following new paragraph:

`(4) any person who has knowledge that a dyed fuel which has been altered as described in paragraph (3) sells or holds for sale such fuel for any use which the person knows or has reason to know is not a nontaxable use of such fuel.'

(b) CONFORMING AMENDMENT- Section 6715(a)(3) is amended by striking `alters, or attempts to alter,' and inserting `alters, chemically or otherwise, or attempts to so alter.'

(c) EFFECTIVE DATE- The amendments made by this section shall take effect on the date of the enactment of this Act.

### **SEC. 857. TERMINATION OF DYED DIESEL USE BY INTERCITY BUSES.**

- (a) IN GENERAL- Paragraph (3) of section 4082(b) (relating to nontaxable use) is amended to read as follows:
  - `(3) any use described in section 4041(a)(1)(C)(iii)(II).'.
- (b) ULTIMATE VENDOR REFUND- Subsection (b) of section 6427 is amended by adding at the end the following new paragraph:
  - `(4) REFUNDS FOR USE OF DIESEL FUEL IN CERTAIN INTERCITY BUSES- With respect to any fuel to which paragraph (2)(A) applies, if the ultimate purchaser of such fuel waives (at such time and in such form and manner as the Secretary shall prescribe) the right to payment under paragraph (1) and assigns such right to the ultimate vendor, then the Secretary shall pay the amount which would be paid under paragraph (1) to such ultimate vendor, but only if such ultimate vendor--
    - `(A) is registered under section 4101, and
    - `(B) meets the requirements of subparagraph (A), (B), or (D) of section 6416(a)(1).'.
- (c) PAYMENT OF REFUNDS- Subparagraph (A) of section 6427(i)(4), as amended by this Act, is amended by inserting `subsections (b)(4) and' after `filed under'.
- (d) EFFECTIVE DATE- The amendments made by this section shall apply to fuel sold after December 31, 2004.

## **SEC. 858. AUTHORITY TO INSPECT ON-SITE RECORDS.**

- (a) IN GENERAL- Section 4083(d)(1)(A) (relating to administrative authority), as amended by this Act, is amended by striking `and' at the end of clause (i) and by inserting after clause (ii) the following new clause:
  - `(iii) inspecting any books and records and any shipping papers pertaining to such fuel, and'.
- (b) EFFECTIVE DATE- The amendments made by this section shall take effect on the date of the enactment of this Act.

## **SEC. 859. ASSESSABLE PENALTY FOR REFUSAL OF ENTRY.**

- (a) IN GENERAL- Part I of subchapter B of chapter 68 (relating to assessable penalties), as amended by this Act, is amended by inserting after section 6716 the following new section:

### **`SEC. 6717. REFUSAL OF ENTRY.**

- `(a) IN GENERAL- In addition to any other penalty provided by law, any person who refuses to admit entry or refuses to permit any other action by the Secretary authorized by section 4083(d)(1) shall pay a penalty of \$1,000 for such refusal.
- `(b) JOINT AND SEVERAL LIABILITY-
  - `(1) IN GENERAL- If a penalty is imposed under this section on any business entity, each officer, employee, or agent of such entity or other contracting party who willfully participated in any act giving rise to such penalty shall be jointly and severally liable with such entity for such penalty.

``(2) AFFILIATED GROUPS- If a business entity described in paragraph (1) is part of an affiliated group (as defined in section 1504(a)), the parent corporation of such entity shall be jointly and severally liable with such entity for the penalty imposed under this section.

``(c) REASONABLE CAUSE EXCEPTION- No penalty shall be imposed under this section with respect to any failure if it is shown that such failure is due to reasonable cause.'

(b) CONFORMING AMENDMENTS- (1) Section 4083(d)(3), as amended by this Act, is amended--

(A) by striking `ENTRY- The penalty' and inserting: `ENTRY-

``(A) FORFEITURE- The penalty', and

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

``(B) ASSESSABLE PENALTY- For additional assessable penalty for the refusal to admit entry or other refusal to permit an action by the Secretary authorized by paragraph (1), see section 6717.'

(2) The table of sections for part I of subchapter B of chapter 68, as amended by this Act, is amended by inserting after the item relating to section 6716 the following new item:

``Sec. 6717. Refusal of entry.'

(c) EFFECTIVE DATE- The amendments made by this section shall take effect on January 1, 2005.

## **SEC. 860. REGISTRATION OF PIPELINE OR VESSEL OPERATORS REQUIRED FOR EXEMPTION OF BULK TRANSFERS TO REGISTERED TERMINALS OR REFINERIES.**

(a) IN GENERAL- Section 4081(a)(1)(B) (relating to exemption for bulk transfers to registered terminals or refineries) is amended--

(1) by inserting `by pipeline or vessel' after `transferred in bulk', and

(2) by inserting `, the operator of such pipeline or vessel,' after `the taxable fuel'.

(b) EFFECTIVE DATE- The amendments made by this section shall take effect on March 1, 2005.

(c) PUBLICATION OF REGISTERED PERSONS- Beginning on January 1, 2005, the Secretary of the Treasury (or the Secretary's delegate) shall periodically publish under section 6103(k)(7) of the Internal Revenue Code of 1986 a current list of persons registered under section 4101 of such Code who are required to register under such section.

## **SEC. 861. DISPLAY OF REGISTRATION.**

(a) IN GENERAL- Subsection (a) of section 4101 (relating to registration) is amended--

(1) by striking `Every' and inserting the following:

``(1) IN GENERAL- Every', and

(2) by adding at the end the following new paragraph:

``(2) DISPLAY OF REGISTRATION- Every operator of a vessel required by the Secretary to register under this section shall display proof of registration through an

identification device prescribed by the Secretary on each vessel used by such operator to transport any taxable fuel.'.

(b) CIVIL PENALTY FOR FAILURE TO DISPLAY REGISTRATION-

(1) IN GENERAL- Part I of subchapter B of chapter 68 (relating to assessable penalties), as amended by this Act, is amended by inserting after section 6717 the following new section:

**SEC. 6718. FAILURE TO DISPLAY TAX REGISTRATION ON VESSELS.**

^(a) FAILURE TO DISPLAY REGISTRATION- Every operator of a vessel who fails to display proof of registration pursuant to section 4101(a)(2) shall pay a penalty of \$500 for each such failure. With respect to any vessel, only one penalty shall be imposed by this section during any calendar month.

^(b) MULTIPLE VIOLATIONS- In determining the penalty under subsection (a) on any person, subsection (a) shall be applied by increasing the amount in subsection (a) by the product of such amount and the aggregate number of penalties (if any) imposed with respect to prior months by this section on such person (or a related person or any predecessor of such person or related person).

^(c) REASONABLE CAUSE EXCEPTION- No penalty shall be imposed under this section with respect to any failure if it is shown that such failure is due to reasonable cause.'

(2) CLERICAL AMENDMENT- The table of sections for part I of subchapter B of chapter 68, as amended by this Act, is amended by inserting after the item relating to section 6717 the following new item:

^`Sec. 6718. Failure to display tax registration on vessels.'

(c) EFFECTIVE DATES-

(1) SUBSECTION (a)- The amendments made by subsection (a) shall take effect on January 1, 2005.

(2) SUBSECTION (b)- The amendments made by subsection (b) shall apply to penalties imposed after December 31, 2004.

**SEC. 862. REGISTRATION OF PERSONS WITHIN FOREIGN TRADE ZONES, ETC.**

(a) IN GENERAL- Section 4101(a), as amended by this Act, is amended by redesignating paragraph (2) as paragraph (3), and by inserting after paragraph (1) the following new paragraph:

^(2) REGISTRATION OF PERSONS WITHIN FOREIGN TRADE ZONES, ETC- The Secretary shall require registration by any person which-

^(A) operates a terminal or refinery within a foreign trade zone or within a customs bonded storage facility, or

^(B) holds an inventory position with respect to a taxable fuel in such a terminal.'

- (b) TECHNICAL AMENDMENT- Section 6718(a), as added by this Act, is amended by striking `section 4101(a)(2)' and inserting `section 4101(a)(3)'.
- (c) EFFECTIVE DATE- The amendments made by this section shall take effect on January 1, 2005.

## **SEC. 863. PENALTIES FOR FAILURE TO REGISTER AND FAILURE TO REPORT.**

- (a) INCREASED PENALTY- Subsection (a) of section 7272 (relating to penalty for failure to register) is amended by inserting `(\$10,000 in the case of a failure to register under section 4101)' after `\$50'.
- (b) INCREASED CRIMINAL PENALTY- Section 7232 (relating to failure to register under section 4101, false representations of registration status, etc.) is amended by striking `\$5,000' and inserting `\$10,000'.
- (c) ASSESSABLE PENALTY FOR FAILURE TO REGISTER-
  - (1) IN GENERAL- Part I of subchapter B of chapter 68 (relating to assessable penalties), as amended by this Act, is amended by inserting after section 6718 at the end the following new section:

### **SEC. 6719. FAILURE TO REGISTER.**

- ^(a) FAILURE TO REGISTER- Every person who is required to register under section 4101 and fails to do so shall pay a penalty in addition to the tax (if any).
- ^(b) AMOUNT OF PENALTY- The amount of the penalty under subsection (a) shall be--
  - (1) \$10,000 for each initial failure to register, and
  - (2) \$1,000 for each day thereafter such person fails to register.
- ^(c) REASONABLE CAUSE EXCEPTION- No penalty shall be imposed under this section with respect to any failure if it is shown that such failure is due to reasonable cause.'
- (2) CLERICAL AMENDMENT- The table of sections for part I of subchapter B of chapter 68, as amended by this Act, is amended by inserting after the item relating to section 6718 the following new item:

^`Sec. 6719. Failure to register.'

- (d) ASSESSABLE PENALTY FOR FAILURE TO REPORT-
  - (1) IN GENERAL- Part II of subchapter B of chapter 68 (relating to assessable penalties) is amended by adding at the end the following new section:

### **SEC. 6725. FAILURE TO REPORT INFORMATION UNDER SECTION 4101.**

- ^(a) IN GENERAL- In the case of each failure described in subsection (b) by any person with respect to a vessel or facility, such person shall pay a penalty of \$10,000 in addition to the tax (if any).

`(b) FAILURES SUBJECT TO PENALTY- For purposes of subsection (a), the failures described in this subsection are--

`(1) any failure to make a report under section 4101(d) on or before the date prescribed therefor, and

`(2) any failure to include all of the information required to be shown on such report or the inclusion of incorrect information.

`(c) REASONABLE CAUSE EXCEPTION- No penalty shall be imposed under this section with respect to any failure if it is shown that such failure is due to reasonable cause.'

(2) CLERICAL AMENDMENT- The table of sections for part II of subchapter B of chapter 68 is amended by adding at the end the following new item:

`Sec. 6725. Failure to report information under section 4101.'

(e) EFFECTIVE DATE- The amendments made by this section shall apply to penalties imposed after December 31, 2004.

## **SEC. 864. ELECTRONIC FILING OF REQUIRED INFORMATION REPORTS.**

(a) IN GENERAL- Section 4101(d) is amended by adding at the end the following new flush sentence:

`Any person who is required to report under this subsection and who has 25 or more reportable transactions in a month shall file such report in electronic format.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply on January 1, 2006.

## **SEC. 865. TAXABLE FUEL REFUNDS FOR CERTAIN ULTIMATE VENDORS.**

(a) IN GENERAL- Paragraph (4) of section 6416(a) (relating to abatements, credits, and refunds) is amended to read as follows:

`(4) REGISTERED ULTIMATE VENDOR TO ADMINISTER CREDITS AND REFUNDS OF GASOLINE TAX-

`(A) IN GENERAL- For purposes of this subsection, if an ultimate vendor purchases any gasoline on which tax imposed by section 4081 has been paid and sells such gasoline to an ultimate purchaser described in subparagraph (C) or (D) of subsection (b)(2) (and such gasoline is for a use described in such subparagraph), such ultimate vendor shall be treated as the person (and the only person) who paid such tax, but only if such ultimate vendor is registered under section 4101.

`(B) TIMING OF CLAIMS- The procedure and timing of any claim under subparagraph (A) shall be the same as for claims under section 6427(i)(4), except that the rules of section 6427(i)(3)(B) regarding electronic claims shall not apply unless the ultimate vendor has certified to the Secretary for the most recent quarter of the taxable year that all ultimate purchasers of the vendor are certified and entitled to a refund under subparagraph (C) or (D) of subsection (b)(2).'

(b) EFFECTIVE DATE- The amendments made by this section shall take effect on January 1, 2005.

## **SEC. 866. TWO-PARTY EXCHANGES.**

(a) IN GENERAL- Subpart C of part III of subchapter A of chapter 32, as amended by this Act, is amended by inserting after section 4104 the following new section:

### **SEC. 4105. TWO-PARTY EXCHANGES.**

^(a) IN GENERAL- In a two-party exchange, the delivering person shall not be liable for the tax imposed under section 4081(a)(1)(A)(ii).

^(b) TWO-PARTY EXCHANGE- The term 'two-party exchange' means a transaction, other than a sale, in which taxable fuel is transferred from a delivering person registered under section 4101 as a taxable fuel registrant to a receiving person who is so registered where all of the following occur:

^(1) The transaction includes a transfer from the delivering person, who holds the inventory position for taxable fuel in the terminal as reflected in the records of the terminal operator.

^(2) The exchange transaction occurs before or contemporaneous with completion of removal across the rack from the terminal by the receiving person.

^(3) The terminal operator in its books and records treats the receiving person as the person that removes the product across the terminal rack for purposes of reporting the transaction to the Secretary.

^(4) The transaction is the subject of a written contract.'

(b) CONFORMING AMENDMENT- The table of sections for subpart C of part III of subchapter A of chapter 32, as amended by this Act, is amended by adding after the last item the following new item:

^`Sec. 4105. Two-party exchanges.'

(c) EFFECTIVE DATE- The amendment made by this section shall take effect on the date of the enactment of this Act.

## **SEC. 867. MODIFICATIONS OF TAX ON USE OF CERTAIN VEHICLES.**

(a) PRORATION OF TAX WHERE VEHICLE SOLD-

(1) IN GENERAL- Subparagraph (A) of section 4481(c)(2) (relating to where vehicle destroyed or stolen) is amended by striking 'destroyed or stolen' both places it appears and inserting 'sold, destroyed, or stolen'.

(2) CONFORMING AMENDMENT- The heading for section 4481(c)(2) is amended by striking 'DESTROYED OR STOLEN' and inserting 'SOLD, DESTROYED, OR STOLEN'.

(b) REPEAL OF INSTALLMENT PAYMENT- (1) Section 6156 (relating to installment payment of tax on use of highway motor vehicles) is repealed.

- (2) The table of sections for subchapter A of chapter 62 is amended by striking the item relating to section 6156.
- (c) ELECTRONIC FILING- Section 4481 is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:
  - `(e) ELECTRONIC FILING- Any taxpayer who files a return under this section with respect to 25 or more vehicles for any taxable period shall file such return electronically.'.
- (d) REPEAL OF REDUCTION IN TAX FOR CERTAIN TRUCKS- Section 4483 is amended by striking subsection (f).
- (e) EFFECTIVE DATE- The amendments made by this section shall apply to taxable periods beginning after the date of the enactment of this Act.

## **SEC. 868. DEDICATION OF REVENUES FROM CERTAIN PENALTIES TO THE HIGHWAY TRUST FUND.**

- (a) IN GENERAL- Subsection (b) of section 9503 (relating to transfer to Highway Trust Fund of amounts equivalent to certain taxes) is amended by redesignating paragraph (5) as paragraph (6) and inserting after paragraph (4) the following new paragraph:
  - `(5) CERTAIN PENALTIES- There are hereby appropriated to the Highway Trust Fund amounts equivalent to the penalties paid under sections 6715, 6715A, 6717, 6718, 6719, 6725, 7232, and 7272 (but only with regard to penalties under such section related to failure to register under section 4101).'
- (b) CONFORMING AMENDMENTS- (1) The heading of subsection (b) of section 9503 is amended by inserting `AND PENALTIES' after `TAXES'.
- (2) The heading of paragraph (1) of section 9503(b) is amended by striking `IN GENERAL' and inserting `CERTAIN TAXES'.
- (c) EFFECTIVE DATE- The amendments made by this section shall apply to penalties assessed on or after the date of the enactment of this Act.

## **SEC. 869. SIMPLIFICATION OF TAX ON TIRES.**

- (a) IN GENERAL- Subsection (a) of section 4071 is amended to read as follows:
  - `(a) IMPOSITION AND RATE OF TAX- There is hereby imposed on taxable tires sold by the manufacturer, producer, or importer thereof a tax at the rate of 9.45 cents (4.725 cents in the case of a biasply tire or super single tire) for each 10 pounds so much of the maximum rated load capacity thereof as exceeds 3,500 pounds.'
- (b) BIASPLY AND SUPER SINGLE TIRES- Section 4072 is amended by adding at the end the following new subsections:
  - `(c) BIASPLY- For purposes of this part, the term `biasply tire' means a pneumatic tire on which the ply cords that extend to the beads are laid at alternate angles substantially less than 90 degrees to the centerline of the tread.'
  - `(d) SUPER SINGLE TIRE- For purposes of this part, the term `super single tire' means a single tire greater than 13 inches in cross section width designed to replace 2 tires in a dual fitment.'
- (b) TAXABLE TIRE- Section 4072, as amended by subsection (a), is amended by redesignating subsections (a), (b), (c), and (d) as subsections (b), (c), (d), and (e)

respectively, and by inserting before subsection (b) (as so redesignated) the following new subsection:

``(a) TAXABLE TIRE- For purposes of this chapter, the term `taxable tire' means any tire of the type used on highway vehicles if wholly or in part made of rubber and if marked pursuant to Federal regulations for highway use.'.

(c) EXEMPTION FOR TIRES SOLD TO DEPARTMENT OF DEFENSE- Section 4073 is amended to read as follows:

### **``SEC. 4073. EXEMPTIONS.**

``The tax imposed by section 4071 shall not apply to tires sold for the exclusive use of the Department of Defense or the Coast Guard.'.

(d) CONFORMING AMENDMENTS- (1) Section 4071 is amended by striking subsection (c) and by moving subsection (e) after subsection (b) and redesignating subsection (e) as subsection (c).

(2) The item relating to section 4073 in the table of sections for part II of subchapter A of chapter 32 is amended to read as follows:

``Sec. 4073. Exemptions.'.

(e) EFFECTIVE DATE- The amendments made by this section shall apply to sales in calendar years beginning more than 30 days after the date of the enactment of this Act.

### **SEC. 870. TRANSMIX AND DIESEL FUEL BLEND STOCKS TREATED AS TAXABLE FUEL.**

(a) IN GENERAL- Paragraph (3) of section 4083(a) is amended to read as follows:

``(3) DIESEL FUEL-

``(A) IN GENERAL- The term `diesel fuel' means--

``(i) any liquid (other than gasoline) which is suitable for use as a fuel in a diesel-powered highway vehicle, or a diesel-powered train,

``(ii) transmix, and

``(iii) diesel fuel blend stocks identified by the Secretary.

``(B) TRANSMIX- For purposes of subparagraph (A), the term `transmix' means a byproduct of refined products pipeline operations created by the mixing of different specification products during pipeline transportation.'

(b) CONFORMING AMENDMENT- Subsection (h) of section 6427 is amended to read as follows:

``(h) BLEND STOCKS NOT USED FOR PRODUCING TAXABLE FUEL-

``(1) GASOLINE BLEND STOCKS OR ADDITIVES NOT USED FOR PRODUCING GASOLINE- Except as provided in subsection (k), if any gasoline blend stock or additive (within the meaning of section 4083(a)(2)) is not used by any person to produce gasoline and such person establishes that the ultimate use of such gasoline blend stock or additive is not to produce gasoline, the Secretary shall pay (without interest) to such person an amount equal to the aggregate amount of the tax imposed on such person with respect to such gasoline blend stock or additive.

``(2) DIESEL FUEL BLEND STOCKS OR ADDITIVES NOT USED FOR PRODUCING DIESEL- Except as provided in subsection (k), if any diesel fuel blend stock is not used by any person to produce diesel fuel and such person establishes that the ultimate use of such diesel fuel blend stock is not to produce diesel fuel, the Secretary shall pay (without interest) to such person an amount equal to the aggregate amount of the tax imposed on such person with respect to such diesel fuel blend stock.'.

(c) EFFECTIVE DATE- The amendment made by this section shall apply to fuel removed, sold, or used after December 31, 2004.

## **SEC. 871. STUDY REGARDING FUEL TAX COMPLIANCE.**

(a) IN GENERAL- Not later than January 31, 2005, the Secretary of the Treasury shall submit to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives a report regarding compliance with the tax imposed under subchapter B of chapter 31 and part III of subchapter A of chapter 32 of the Internal Revenue Code of 1986. Such report shall include the information, analysis, and recommendations specified in subsections (b), (c), and (d).

(b) TAXABLE FUEL BLENDSTOCKS- The Secretary shall identify chemical products to be added to the list of blendstocks from lab analysis of fuel samples collected by the Internal Revenue Service which have been blended with taxable fuel but are not treated as blendstocks. The Secretary shall include statistics regarding the frequency in which a chemical product has been collected, and whether the sample contained an above normal concentration of the chemical product.

(c) WASTE PRODUCTS ADDED TO TAXABLE FUELS- The report shall include a discussion of Internal Revenue Service findings regarding the addition of waste products to taxable fuel and any recommendations to address the taxation of such products.

(d) ERRONEOUS CLAIMS OF FUEL TAX EXEMPTIONS- The report shall include a discussion of Internal Revenue Service findings regarding sales of taxable fuel to entities claiming exempt status as a State or local government and the frequency of erroneous certifications of tax exempt status. The Secretary, in consultation with representatives of State and local governments, shall provide recommendations to address such erroneous claims, including recommendations on the feasibility of a State maintained list of exempt governmental entities within the State.

### **Subtitle D--Other Revenue Provisions**

## **SEC. 881. QUALIFIED TAX COLLECTION CONTRACTS.**

(a) CONTRACT REQUIREMENTS-

(1) IN GENERAL- Subchapter A of chapter 64 (relating to collection) is amended by adding at the end the following new section:

## **``SEC. 6306. QUALIFIED TAX COLLECTION CONTRACTS.**

``(a) IN GENERAL- Nothing in any provision of law shall be construed to prevent the Secretary from entering into a qualified tax collection contract.

- ``(b) QUALIFIED TAX COLLECTION CONTRACT- For purposes of this section, the term `qualified tax collection contract' means any contract which-
  - ``(1) is for the services of any person (other than an officer or employee of the Treasury Department)--
    - ``(A) to locate and contact any taxpayer specified by the Secretary,
    - ``(B) to request full payment from such taxpayer of an amount of Federal tax specified by the Secretary and, if such request cannot be met by the taxpayer, to offer the taxpayer an installment agreement providing for full payment of such amount during a period not to exceed 5 years, and
    - ``(C) to obtain financial information specified by the Secretary with respect to such taxpayer,
  - ``(2) prohibits each person providing such services under such contract from committing any act or omission which employees of the Internal Revenue Service are prohibited from committing in the performance of similar services,
  - ``(3) prohibits subcontractors from--
    - ``(A) having contacts with taxpayers,
    - ``(B) providing quality assurance services, and
    - ``(C) composing debt collection notices, and
  - ``(4) permits subcontractors to perform other services only with the approval of the Secretary.
- ``(c) FEES- The Secretary may retain and use--
  - ``(1) an amount not in excess of 25 percent of the amount collected under any qualified tax collection contract for the costs of services performed under such contract, and
  - ``(2) an amount not in excess of 25 percent of such amount collected for collection enforcement activities of the Internal Revenue Service.

The Secretary shall keep adequate records regarding amounts so retained and used. The amount credited as paid by any taxpayer shall be determined without regard to this subsection.
- ``(d) NO FEDERAL LIABILITY- The United States shall not be liable for any act or omission of any person performing services under a qualified tax collection contract.
- ``(e) APPLICATION OF FAIR DEBT COLLECTION PRACTICES ACT- The provisions of the Fair Debt Collection Practices Act (15 U.S.C. 1692 et seq.) shall apply to any qualified tax collection contract, except to the extent superseded by section 6304, section 7602(c), or by any other provision of this title.
- ``(f) CROSS REFERENCES-
  - ``(1) For damages for certain unauthorized collection actions by persons performing services under a qualified tax collection contract, see section 7433A.
  - ``(2) For application of Taxpayer Assistance Orders to persons performing services under a qualified tax collection contract, see section 7811(g).'
- (2) CONFORMING AMENDMENTS- (A) Section 7809(a) is amended by inserting `6306,' before `7651'.
  - (B) The table of sections for subchapter A of chapter 64 is amended by adding at the end the following new item:
    - ``Sec. 6306. Qualified tax collection contracts.'

(b) CIVIL DAMAGES FOR CERTAIN UNAUTHORIZED COLLECTION ACTIONS BY PERSONS PERFORMING SERVICES UNDER QUALIFIED TAX COLLECTION CONTRACTS-

(1) IN GENERAL- Subchapter B of chapter 76 (relating to proceedings by taxpayers and third parties) is amended by inserting after section 7433 the following new section:

**SEC. 7433A. CIVIL DAMAGES FOR CERTAIN UNAUTHORIZED COLLECTION ACTIONS BY PERSONS PERFORMING SERVICES UNDER QUALIFIED TAX COLLECTION CONTRACTS.**

^(a) IN GENERAL- Subject to the modifications provided by subsection (b), section 7433 shall apply to the acts and omissions of any person performing services under a qualified tax collection contract (as defined in section 6306(b)) to the same extent and in the same manner as if such person were an employee of the Internal Revenue Service.

^(b) MODIFICATIONS- For purposes of subsection (a):

^(1) Any civil action brought under section 7433 by reason of this section shall be brought against the person who entered into the qualified tax collection contract with the Secretary and shall not be brought against the United States.

^(2) Such person and not the United States shall be liable for any damages and costs determined in such civil action.

^(3) Such civil action shall not be an exclusive remedy with respect to such person.

^(4) Subsections (c), (d)(1), and (e) of section 7433 shall not apply.'

(2) CLERICAL AMENDMENT- The table of sections for subchapter B of chapter 76 is amended by inserting after the item relating to section 7433 the following new item:

^Sec. 7433A. Civil damages for certain unauthorized collection actions by persons performing services under qualified tax collection contracts.'

(c) APPLICATION OF TAXPAYER ASSISTANCE ORDERS TO PERSONS PERFORMING SERVICES UNDER A QUALIFIED TAX COLLECTION CONTRACT- Section 7811 (relating to taxpayer assistance orders) is amended by adding at the end the following new subsection:

^(g) APPLICATION TO PERSONS PERFORMING SERVICES UNDER A QUALIFIED TAX COLLECTION CONTRACT- Any order issued or action taken by the National Taxpayer Advocate pursuant to this section shall apply to persons performing services under a qualified tax collection contract (as defined in section 6306(b)) to the same extent and in the same manner as such order or action applies to the Secretary.'

(d) INELIGIBILITY OF INDIVIDUALS WHO COMMIT MISCONDUCT TO PERFORM UNDER CONTRACT- Section 1203 of the Internal Revenue Service Restructuring Act of 1998 (relating to termination of employment for misconduct) is amended by adding at the end the following new subsection:

^(e) INDIVIDUALS PERFORMING SERVICES UNDER A QUALIFIED TAX COLLECTION CONTRACT- An individual shall cease to be permitted to perform any services under any qualified tax collection contract (as defined in section 6306(b) of the Internal Revenue Code of 1986) if there is a final determination by the Secretary of the

Treasury under such contract that such individual committed any act or omission described under subsection (b) in connection with the performance of such services.'

(e) BIENNIAL REPORT- The Secretary of the Treasury shall biennially submit (beginning in 2005) to the Committee on Finance of the Senate and the Committee on Ways and Means of the House of Representatives a report with respect to qualified tax collection contracts under section 6306 of the Internal Revenue Code of 1986 (as added by this section) which includes--

- (1) a complete cost benefit analysis,
- (2) the impact of such contracts on collection enforcement staff levels in the Internal Revenue Service,
- (3) the impact of such contracts on the total number and amount of unpaid assessments, and on the number and amount of assessments collected by Internal Revenue Service personnel after initial contact by a contractor,
- (4) the amounts collected and the collection costs incurred (directly and indirectly) by the Internal Revenue Service,
- (5) an evaluation of contractor performance,
- (6) a disclosure safeguard report in a form similar to that required under section 6103(p)(5) of such Code, and
- (7) a measurement plan which includes a comparison of the best practices used by the private collectors with the Internal Revenue Service's own collection techniques and mechanisms to identify and capture information on successful collection techniques used by the contractors which could be adopted by the Internal Revenue Service.

(f) EFFECTIVE DATE- The amendments made to this section shall take effect on the date of the enactment of this Act.

## **SEC. 882. TREATMENT OF CHARITABLE CONTRIBUTIONS OF PATENTS AND SIMILAR PROPERTY.**

(a) In General- Subparagraph (B) of section 170(e)(1) is amended by striking 'or' at the end of clause (i), by adding 'or' at the end of clause (ii), and by inserting after clause (ii) the following new clause:

``(iii) of any patent, copyright (other than a copyright described in section 1221(a)(3) or 1231(b)(1)(C)), trademark, trade name, trade secret, know-how, software (other than software described in section 197(e)(3)(A)(i)), or similar property, or applications or registrations of such property.'

(b) Certain Donee Income From Intellectual Property Treated as an Additional Charitable Contribution- Section 170 is amended by redesignating subsection (m) as subsection (n) and by inserting after subsection (l) the following new subsection:

``(m) Certain Donee Income From Intellectual Property Treated as an Additional Charitable Contribution-

``(1) Treatment as additional contribution- In the case of a taxpayer who makes a qualified intellectual property contribution, the deduction allowed under subsection (a) for each taxable year of the taxpayer ending on or after the date of such contribution shall be increased (subject to the limitations under subsection (b)) by the applicable percentage of qualified donee income with respect to such contribution which is properly allocable to such year under this subsection.

``(2) REDUCTION IN ADDITIONAL DEDUCTIONS TO EXTENT OF INITIAL DEDUCTION- With respect to any qualified intellectual property contribution, the deduction allowed under subsection (a) shall be increased under paragraph (1) only to the extent that the aggregate amount of such increases with respect to such contribution exceed the amount allowed as a deduction under subsection (a) with respect to such contribution determined without regard to this subsection.

``(3) Qualified donee income- For purposes of this subsection, the term `qualified donee income' means any net income received by or accrued to the donee which is properly allocable to the qualified intellectual property.

``(4) ALLOCATION OF QUALIFIED DONEE INCOME TO TAXABLE YEARS OF DONOR- For purposes of this subsection, qualified donee income shall be treated as properly allocable to a taxable year of the donor if such income is received by or accrued to the donee for the taxable year of the donee which ends within or with such taxable year of the donor.

``(5) 10-YEAR LIMITATION- Income shall not be treated as properly allocable to qualified intellectual property for purposes of this subsection if such income is received by or accrued to the donee after the 10-year period beginning on the date of the contribution of such property.

``(6) Benefit limited to life of intellectual property- Income shall not be treated as properly allocable to qualified intellectual property for purposes of this subsection if such income is received by or accrued to the donee after the expiration of the legal life of such property.

``(7) Applicable percentage- For purposes of this subsection, the term `applicable percentage' means the percentage determined under the following table which corresponds to a taxable year of the donor ending on or after the date of the qualified intellectual property contribution:

| <b>Taxable Year of Donor<br/>Ending on or After</b> | <b>Applicable<br/>Date of Contribution:<br/>Percentage:</b> |
|-----------------------------------------------------|-------------------------------------------------------------|
|-----------------------------------------------------|-------------------------------------------------------------|

1st

--100

2nd

--100

3rd

--90

4th

--80

5th

--70

6th

--60

7th

--50

8th

--40

9th

--30

10th

--20

11th

--10

12th

--10.

^(8) Qualified intellectual property contribution- For purposes of this subsection, the term 'qualified intellectual property contribution' means any charitable contribution of qualified intellectual property-

^(A) the amount of which taken into account under this section is reduced by reason of subsection (e)(1), and

^(B) with respect to which the donor informs the donee at the time of such contribution that the donor intends to treat such contribution as a qualified intellectual property contribution for purposes of this subsection and section 6050L.

^(9) Qualified intellectual property- For purposes of this subsection, the term 'qualified intellectual property' means property described in subsection (e)(1)(B)(iii) (other than property contributed to or for the use of an organization described in subsection (e)(1)(B)(ii)).

``(10) Other special rules-

``(A) Application of limitations on charitable contributions- Any increase under this subsection of the deduction provided under subsection (a) shall be treated for purposes of subsection (b) as a deduction which is attributable to a charitable contribution to the donee to which such increase relates.

``(B) Net income determined by donee- The net income taken into account under paragraph (3) shall not exceed the amount of such income reported under section 6050L(b)(1).

``(C) DEDUCTION LIMITED TO 12 TAXABLE YEARS- Except as may be provided under subparagraph (D)(i), this subsection shall not apply with respect to any qualified intellectual property contribution for any taxable year of the donor after the 12th taxable year of the donor which ends on or after the date of such contribution.

``(D) Regulations- The Secretary may issue regulations or other guidance to carry out the purposes of this subsection, including regulations or guidance--

``(i) modifying the application of this subsection in the case of a donor or donee with a short taxable year, and

``(ii) providing for the determination of an amount to be treated as net income of the donee which is properly allocable to qualified intellectual property in the case of a donee who uses such property to further a purpose or function constituting the basis of the donee's exemption under section 501 (or, in the case of a governmental unit, any purpose described in section 170(c)) and does not possess a right to receive any payment from a third party with respect to such property.'

(c) Reporting Requirements-

(1) In general- Section 6050L (relating to returns relating to certain dispositions of donated property) is amended to read as follows:

## **``SEC. 6050L. RETURNS RELATING TO CERTAIN DONATED PROPERTY.**

``(a) Dispositions of Donated Property-

``(1) In general- If the donee of any charitable deduction property sells, exchanges, or otherwise disposes of such property within 2 years after its receipt, the donee shall make a return (in accordance with forms and regulations prescribed by the Secretary) showing--

``(A) the name, address, and TIN of the donor,

``(B) a description of the property,

``(C) the date of the contribution,

``(D) the amount received on the disposition, and

``(E) the date of such disposition.

``(2) Definitions- For purposes of this subsection:

``(A) Charitable deduction property- The term 'charitable deduction property' means any property (other than publicly traded securities) contributed in a contribution for which a deduction was claimed under section 170 if the claimed value of such property (plus the claimed value of all similar items of property donated by the donor to 1 or more donees) exceeds \$5,000.

``(B) Publicly traded securities- The term `publicly traded securities' means securities for which (as of the date of the contribution) market quotations are readily available on an established securities market.

``(b) Qualified Intellectual Property Contributions-

``(1) In general- Each donee with respect to a qualified intellectual property contribution shall make a return (at such time and in such form and manner as the Secretary may by regulations prescribe) with respect to each specified taxable year of the donee showing--

``(A) the name, address, and TIN of the donor,

``(B) a description of the qualified intellectual property contributed,

``(C) the date of the contribution, and

``(D) the amount of net income of the donee for the taxable year which is properly allocable to the qualified intellectual property (determined without regard to paragraph (10)(B) of section 170(m) and with the modifications described in paragraphs (5) and (6) of such section).

``(2) Definitions- For purposes of this subsection:

``(A) In general- Terms used in this subsection which are also used in section 170(m) have the respective meanings given such terms in such section.

``(B) Specified taxable year- The term `specified taxable year' means, with respect to any qualified intellectual property contribution, any taxable year of the donee any portion of which is part of the 10-year period beginning on the date of such contribution.

``(c) Statement To Be Furnished to Donors- Every person making a return under subsection (a) or (b) shall furnish a copy of such return to the donor at such time and in such manner as the Secretary may by regulations prescribe.'

(2) CLERICAL AMENDMENT- The table of sections for subpart A of part II of subchapter A of chapter 61 is amended by striking the item relating to section 6050L and inserting the following new item:

``Sec. 6050L. Returns relating to certain donated property.'

(d) Coordination With Appraisal Requirements- Subclause (I) of section 170(f)(11)(A)(ii), as added by this Act, is amended by inserting `subsection (e)(1)(B)(iii) or' before `section 1221(a)(1)'.

(e) Anti-Abuse Rules- The Secretary of the Treasury may prescribe such regulations or other guidance as may be necessary or appropriate to prevent the avoidance of the purposes of section 170(e)(1)(B)(iii) of the Internal Revenue Code of 1986 (as added by subsection (a)), including preventing--

(1) the circumvention of the reduction of the charitable deduction by embedding or bundling the patent or similar property as part of a charitable contribution of property that includes the patent or similar property,

(2) the manipulation of the basis of the property to increase the amount of the charitable deduction through the use of related persons, pass-thru entities, or other intermediaries, or through the use of any provision of law or regulation (including the consolidated return regulations), and

(3) a donor from changing the form of the patent or similar property to property of a form for which different deduction rules would apply.

(f) EFFECTIVE DATE- The amendments made by this section shall apply to contributions made after June 3, 2004.

## **SEC. 883. INCREASED REPORTING FOR NONCASH CHARITABLE CONTRIBUTIONS.**

(a) IN GENERAL- Subsection (f) of section 170 (relating to disallowance of deduction in certain cases and special rules) is amended by adding after paragraph (10) the following new paragraph:

`(11) QUALIFIED APPRAISAL AND OTHER DOCUMENTATION FOR CERTAIN CONTRIBUTIONS-

`(A) IN GENERAL-

`(i) DENIAL OF DEDUCTION- In the case of an individual, partnership, or corporation, no deduction shall be allowed under subsection (a) for any contribution of property for which a deduction of more than \$500 is claimed unless such person meets the requirements of subparagraphs (B), (C), and (D), as the case may be, with respect to such contribution.

`(ii) EXCEPTIONS-

`(I) READILY VALUED PROPERTY- Subparagraphs (C) and (D) shall not apply to cash, property described in section 1221(a)(1), publicly traded securities (as defined in section 6050L(a)(2)(B)), and any qualified vehicle described in paragraph (12)(A)(ii) for which an acknowledgement under paragraph (12)(B)(iii) is provided.

`(II) REASONABLE CAUSE- Clause (i) shall not apply if it is shown that the failure to meet such requirements is due to reasonable cause and not to willful neglect.

`(B) PROPERTY DESCRIPTION FOR CONTRIBUTIONS OF MORE THAN \$500- In the case of contributions of property for which a deduction of more than \$500 is claimed, the requirements of this subparagraph are met if the individual, partnership or corporation includes with the return for the taxable year in which the contribution is made a description of such property and such other information as the Secretary may require. The requirements of this subparagraph shall not apply to a C corporation which is not a personal service corporation or a closely held C corporation.

`(C) QUALIFIED APPRAISAL FOR CONTRIBUTIONS OF MORE THAN \$5,000- In the case of contributions of property for which a deduction of more than \$5,000 is claimed, the requirements of this subparagraph are met if the individual, partnership, or corporation obtains a qualified appraisal of such property and attaches to the return for the taxable year in which such contribution is made such information regarding such property and such appraisal as the Secretary may require.

`(D) SUBSTANTIATION FOR CONTRIBUTIONS OF MORE THAN \$500,000- In the case of contributions of property for which a deduction of more than \$500,000 is claimed, the requirements of this subparagraph are met if the individual, partnership, or corporation attaches to the return for the taxable year a qualified appraisal of such property.

`(E) QUALIFIED APPRAISAL- For purposes of this paragraph, the term 'qualified appraisal' means, with respect to any property, an appraisal of such property which is treated for purposes of this paragraph as a qualified appraisal under regulations or other guidance prescribed by the Secretary.

- ` (F) AGGREGATION OF SIMILAR ITEMS OF PROPERTY- For purposes of determining thresholds under this paragraph, property and all similar items of property donated to 1 or more donees shall be treated as 1 property.
- ` (G) SPECIAL RULE FOR PASS-THRU ENTITIES- In the case of a partnership or S corporation, this paragraph shall be applied at the entity level, except that the deduction shall be denied at the partner or shareholder level.
- ` (H) REGULATIONS- The Secretary may prescribe such regulations as may be necessary or appropriate to carry out the purposes of this paragraph, including regulations that may provide that some or all of the requirements of this paragraph do not apply in appropriate cases.'
- (b) EFFECTIVE DATE- The amendment made by this section shall apply to contributions made after June 3, 2004.

## **SEC. 884. DONATIONS OF MOTOR VEHICLES, BOATS, AND AIRPLANES.**

(a) IN GENERAL- Subsection (f) of section 170 (relating to disallowance of deduction in certain cases and special rules), as amended by this Act, is amended by inserting after paragraph (11) the following new paragraph:

### **` (12) CONTRIBUTIONS OF USED MOTOR VEHICLES, BOATS, AND AIRPLANES-**

` (A) IN GENERAL- In the case of a contribution of a qualified vehicle the claimed value of which exceeds \$500--

` (i) paragraph (8) shall not apply and no deduction shall be allowed under subsection (a) for such contribution unless the taxpayer substantiates the contribution by a contemporaneous written acknowledgement of the contribution by the donee organization that meets the requirements of subparagraph (B) and includes the acknowledgement with the taxpayer's return of tax which includes the deduction, and

` (ii) if the organization sells the vehicle without any significant intervening use or material improvement of such vehicle by the organization, the amount of the deduction allowed under subsection (a) shall not exceed the gross proceeds received from such sale.

` (B) CONTENT OF ACKNOWLEDGEMENT- An acknowledgement meets the requirements of this subparagraph if it includes the following information:

` (i) The name and taxpayer identification number of the donor.

` (ii) The vehicle identification number or similar number.

` (iii) In the case of a qualified vehicle to which subparagraph (A)(ii) applies--

` (I) a certification that the vehicle was sold in an arm's length transaction between unrelated parties,

` (II) the gross proceeds from the sale, and

` (III) a statement that the deductible amount may not exceed the amount of such gross proceeds.

` (iv) In the case of a qualified vehicle to which subparagraph (A)(ii) does not apply--

` (I) a certification of the intended use or material improvement of the vehicle and the intended duration of such use, and

` (II) a certification that the vehicle would not be transferred in exchange for money, other property, or services before completion of such use or improvement.

``(C) CONTEMPORANEOUS- For purposes of subparagraph (A), an acknowledgement shall be considered to be contemporaneous if the donee organization provides it within 30 days of--

``(i) the sale of the qualified vehicle, or

``(ii) in the case of an acknowledgement including a certification described in subparagraph (B)(iv), the contribution of the qualified vehicle.

``(D) INFORMATION TO SECRETARY- A donee organization required to provide an acknowledgement under this paragraph shall provide to the Secretary the information contained in the acknowledgement. Such information shall be provided at such time and in such manner as the Secretary may prescribe.

``(E) QUALIFIED VEHICLE- For purposes of this paragraph, the term `qualified vehicle' means any--

``(i) motor vehicle manufactured primarily for use on public streets, roads, and highways,

``(ii) boat, or

``(iii) airplane.

Such term shall not include any property which is described in section 1221(a)(1).

``(F) REGULATIONS OR OTHER GUIDANCE- The Secretary shall prescribe such regulations or other guidance as may be necessary to carry out the purposes of this paragraph. The Secretary may prescribe regulations or other guidance which exempts sales by the donee organization which are in direct furtherance of such organization's charitable purpose from the requirements of subparagraphs (A)(ii) and (B)(iv)(II).'

(b) PENALTY FOR FRAUDULENT ACKNOWLEDGMENTS-

(1) IN GENERAL- Part I of subchapter B of chapter 68 (relating to assessable penalties), as amended by this Act, is amended by inserting after section 6719 the following new section:

#### **``SEC. 6720. FRAUDULENT ACKNOWLEDGMENTS WITH RESPECT TO DONATIONS OF MOTOR VEHICLES, BOATS, AND AIRPLANES.**

``Any donee organization required under section 170(f)(12)(A) to furnish a contemporaneous written acknowledgment to a donor which knowingly furnishes a false or fraudulent acknowledgment, or which knowingly fails to furnish such acknowledgment in the manner, at the time, and showing the information required under section 170(f)(12), or regulations prescribed thereunder, shall for each such act, or for each such failure, be subject to a penalty equal to--

``(1) in the case of an acknowledgment with respect to a qualified vehicle to which section 170(f)(12)(A)(ii) applies, the greater of--

``(A) the product of the highest rate of tax specified in section 1 and the sales price stated on the acknowledgment, or

``(B) the gross proceeds from the sale of such vehicle, and

``(2) in the case of an acknowledgment with respect to any other qualified vehicle to which section 170(f)(12) applies, the greater of--

``(A) the product of the highest rate of tax specified in section 1 and the claimed value of the vehicle, or

``(B) \$5,000.'

(2) CONFORMING AMENDMENT- The table of sections for part I of subchapter B of chapter 68, as amended by this Act, is amended by inserting after the item relating to section 6719 the following new item:

``Sec. 6720. Fraudulent acknowledgments with respect to donations of motor vehicles, boats, and airplanes.''

(c) EFFECTIVE DATE- The amendments made by this section shall apply to contributions made after December 31, 2004.

## **SEC. 885. TREATMENT OF NONQUALIFIED DEFERRED COMPENSATION PLANS.**

(a) IN GENERAL- Subpart A of part I of subchapter D of chapter 1 is amended by adding at the end the following new section:

### **SEC. 409A. INCLUSION IN GROSS INCOME OF DEFERRED COMPENSATION UNDER NONQUALIFIED DEFERRED COMPENSATION PLANS.**

``(a) RULES RELATING TO CONSTRUCTIVE RECEIPT-

``(1) PLAN FAILURES-

``(A) GROSS INCOME INCLUSION-

``(i) IN GENERAL- If at any time during a taxable year a nonqualified deferred compensation plan-

``(I) fails to meet the requirements of paragraphs (2), (3), and (4), or

``(II) is not operated in accordance with such requirements,

all compensation deferred under the plan for the taxable year and all preceding taxable years shall be includable in gross income for the taxable year to the extent not subject to a substantial risk of forfeiture and not previously included in gross income.

``(ii) APPLICATION ONLY TO AFFECTED PARTICIPANTS- Clause (i) shall only apply with respect to all compensation deferred under the plan for participants with respect to whom the failure relates.

``(B) INTEREST AND ADDITIONAL TAX PAYABLE WITH RESPECT TO PREVIOUSLY DEFERRED COMPENSATION-

``(i) IN GENERAL- If compensation is required to be included in gross income under subparagraph (A) for a taxable year, the tax imposed by this chapter for the taxable year shall be increased by the sum of-

``(I) the amount of interest determined under clause (ii), and

``(II) an amount equal to 20 percent of the compensation which is required to be included in gross income.

``(ii) INTEREST- For purposes of clause (i), the interest determined under this clause for any taxable year is the amount of interest at the underpayment rate plus 1 percentage point on the underpayments that would have occurred had the deferred compensation been includable in gross income for the taxable year in which first deferred or, if later, the

first taxable year in which such deferred compensation is not subject to a substantial risk of forfeiture.

^(2) DISTRIBUTIONS-

^(A) IN GENERAL- The requirements of this paragraph are met if the plan provides that compensation deferred under the plan may not be distributed earlier than--

- ^(i) separation from service as determined by the Secretary (except as provided in subparagraph (B)(i)),
- ^(ii) the date the participant becomes disabled (within the meaning of subparagraph (C)),
- ^(iii) death,
- ^(iv) a specified time (or pursuant to a fixed schedule) specified under the plan at the date of the deferral of such compensation,
- ^(v) to the extent provided by the Secretary, a change in the ownership or effective control of the corporation, or in the ownership of a substantial portion of the assets of the corporation, or
- ^(vi) the occurrence of an unforeseeable emergency.

^(B) SPECIAL RULES-

^(i) SPECIFIED EMPLOYEES- In the case of any specified employee, the requirement of subparagraph (A)(i) is met only if distributions may not be made before the date which is 6 months after the date of separation from service (or, if earlier, the date of death of the employee). For purposes of the preceding sentence, a specified employee is a key employee (as defined in section 416(i) without regard to paragraph (5) thereof) of a corporation any stock in which is publicly traded on an established securities market or otherwise.

^(ii) UNFORESEEABLE EMERGENCY- For purposes of subparagraph (A)(vi)--

^(I) IN GENERAL- The term 'unforeseeable emergency' means a severe financial hardship to the participant resulting from an illness or accident of the participant, the participant's spouse, or a dependent (as defined in section 152(a)) of the participant, loss of the participant's property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the participant.

^(II) LIMITATION ON DISTRIBUTIONS- The requirement of subparagraph (A)(vi) is met only if, as determined under regulations of the Secretary, the amounts distributed with respect to an emergency do not exceed the amounts necessary to satisfy such emergency plus amounts necessary to pay taxes reasonably anticipated as a result of the distribution, after taking into account the extent to which such hardship is or may be relieved through reimbursement or compensation by insurance or otherwise or by liquidation of the participant's assets (to the extent the liquidation of such assets would not itself cause severe financial hardship).

^(C) DISABLED- For purposes of subparagraph (A)(ii), a participant shall be considered disabled if the participant--

- ^(i) is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, or
- ^(ii) is, by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, receiving income replacement benefits for a period of not less than 3

months under an accident and health plan covering employees of the participant's employer.

^(3) ACCELERATION OF BENEFITS- The requirements of this paragraph are met if the plan does not permit the acceleration of the time or schedule of any payment under the plan, except as provided in regulations by the Secretary.

^(4) ELECTIONS-

^(A) IN GENERAL- The requirements of this paragraph are met if the requirements of subparagraphs (B) and (C) are met.

^(B) INITIAL DEFERRAL DECISION-

^(i) IN GENERAL- The requirements of this subparagraph are met if the plan provides that compensation for services performed during a taxable year may be deferred at the participant's election only if the election to defer such compensation is made not later than the close of the preceding taxable year or at such other time as provided in regulations.

^(ii) FIRST YEAR OF ELIGIBILITY- In the case of the first year in which a participant becomes eligible to participate in the plan, such election may be made with respect to services to be performed subsequent to the election within 30 days after the date the participant becomes eligible to participate in such plan.

^(iii) PERFORMANCE-BASED COMPENSATION- In the case of any performance-based compensation based on services performed over a period of at least 12 months, such election may be made no later than 6 months before the end of the period.

^(C) CHANGES IN TIME AND FORM OF DISTRIBUTION- The requirements of this subparagraph are met if, in the case of a plan which permits under a subsequent election a delay in a payment or a change in the form of payment--

^(i) the plan requires that such election may not take effect until at least 12 months after the date on which the election is made,

^(ii) in the case of an election related to a payment not described in clause (ii), (iii), or (vi) of paragraph (2)(A), the plan requires that the first payment with respect to which such election is made be deferred for a period of not less than 5 years from the date such payment would otherwise have been made, and

^(iii) the plan requires that any election related to a payment described in paragraph (2)(A)(iv) may not be made less than 12 months prior to the date of the first scheduled payment under such paragraph.

^(b) RULES RELATING TO FUNDING-

^(1) OFFSHORE PROPERTY IN A TRUST- In the case of assets set aside (directly or indirectly) in a trust (or other arrangement determined by the Secretary) for purposes of paying deferred compensation under a nonqualified deferred compensation plan, for purposes of section 83 such assets shall be treated as property transferred in connection with the performance of services whether or not such assets are available to satisfy claims of general creditors--

^(A) at the time set aside if such assets (or such trust or other arrangement) are located outside of the United States, or

^(B) at the time transferred if such assets (or such trust or other arrangement) are subsequently transferred outside of the United States.

This paragraph shall not apply to assets located in a foreign jurisdiction if substantially all of the services to which the nonqualified deferred compensation relates are performed in such jurisdiction.

``(2) EMPLOYER'S FINANCIAL HEALTH- In the case of compensation deferred under a nonqualified deferred compensation plan, there is a transfer of property within the meaning of section 83 with respect to such compensation as of the earlier of--

``(A) the date on which the plan first provides that assets will become restricted to the provision of benefits under the plan in connection with a change in the employer's financial health, or

``(B) the date on which assets are so restricted, whether or not such assets are available to satisfy claims of general creditors.

``(3) INCOME INCLUSION FOR OFFSHORE TRUSTS AND EMPLOYER'S FINANCIAL HEALTH- For each taxable year that assets treated as transferred under this subsection remain set aside in a trust or other arrangement subject to paragraph (1) or (2), any increase in value in, or earnings with respect to, such assets shall be treated as an additional transfer of property under this subsection (to the extent not previously included in income).

``(4) INTEREST ON TAX LIABILITY PAYABLE WITH RESPECT TO TRANSFERRED PROPERTY-

``(A) IN GENERAL- If amounts are required to be included in gross income by reason of paragraph (1) or (2) for a taxable year, the tax imposed by this chapter for such taxable year shall be increased by the sum of--

``(i) the amount of interest determined under subparagraph (B), and

``(ii) an amount equal to 20 percent of the amounts required to be included in gross income.

``(B) INTEREST- For purposes of subparagraph (A), the interest determined under this subparagraph for any taxable year is the amount of interest at the underpayment rate plus 1 percentage point on the underpayments that would have occurred had the amounts so required to be included in gross income by paragraph (1) or (2) been includable in gross income for the taxable year in which first deferred or, if later, the first taxable year in which such amounts are not subject to a substantial risk of forfeiture.

``(c) NO INFERENCE ON EARLIER INCOME INCLUSION OR REQUIREMENT OF LATER INCLUSION- Nothing in this section shall be construed to prevent the inclusion of amounts in gross income under any other provision of this chapter or any other rule of law earlier than the time provided in this section. Any amount included in gross income under this section shall not be required to be included in gross income under any other provision of this chapter or any other rule of law later than the time provided in this section.

``(d) OTHER DEFINITIONS AND SPECIAL RULES- For purposes of this section:

``(1) NONQUALIFIED DEFERRED COMPENSATION PLAN- The term `nonqualified deferred compensation plan' means any plan that provides for the deferral of compensation, other than--

``(A) a qualified employer plan, and

``(B) any bona fide vacation leave, sick leave, compensatory time, disability pay, or death benefit plan.

``(2) QUALIFIED EMPLOYER PLAN- The term `qualified employer plan' means--

- ` (A) any plan, contract, pension, account, or trust described in subparagraph (A) or (B) of section 219(g)(5) (without regard to subparagraph (A)(iii)),
- ` (B) any eligible deferred compensation plan (within the meaning of section 457(b)), and
- ` (C) any plan described in section 415(m).

` (3) PLAN INCLUDES ARRANGEMENTS, ETC- The term `plan' includes any agreement or arrangement, including an agreement or arrangement that includes one person.

` (4) SUBSTANTIAL RISK OF FORFEITURE- The rights of a person to compensation are subject to a substantial risk of forfeiture if such person's rights to such compensation are conditioned upon the future performance of substantial services by any individual.

` (5) TREATMENT OF EARNINGS- References to deferred compensation shall be treated as including references to income (whether actual or notional) attributable to such compensation or such income.

` (6) AGGREGATION RULES- Except as provided by the Secretary, rules similar to the rules of subsections (b) and (c) of section 414 shall apply.

` (e) REGULATIONS- The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations--

- ` (1) providing for the determination of amounts of deferral in the case of a nonqualified deferred compensation plan which is a defined benefit plan,
- ` (2) relating to changes in the ownership and control of a corporation or assets of a corporation for purposes of subsection (a)(2)(A)(v),
- ` (3) exempting arrangements from the application of subsection (b) if such arrangements will not result in an improper deferral of United States tax and will not result in assets being effectively beyond the reach of creditors,
- ` (4) defining financial health for purposes of subsection (b)(2), and
- ` (5) disregarding a substantial risk of forfeiture in cases where necessary to carry out the purposes of this section.'

(b) TREATMENT OF DEFERRED AMOUNTS-

(1) W-2 FORMS-

(A) IN GENERAL- Subsection (a) of section 6051 (relating to receipts for employees) is amended by striking `and' at the end of paragraph (11), by striking the period at the end of paragraph (12) and inserting `, and', and by inserting after paragraph (12) the following new paragraph:

` (13) the total amount of deferrals for the year under a nonqualified deferred compensation plan (within the meaning of section 409A(d)).'

(B) THRESHOLD- Subsection (a) of section 6051 is amended by adding at the end the following: `In the case of the amounts required to be shown by paragraph (13), the Secretary may (by regulation) establish a minimum amount of deferrals below which paragraph (13) does not apply.'

(2) WAGE WITHHOLDING- Section 3401(a) (defining wages) is amended by adding at the end the following flush sentence: `The term `wages' includes any amount includible in gross income of an employee under section 409A and payment of such amount shall be treated as having been made in the taxable year in which the amount is so includible.'

(3) OTHER REPORTING- Section 6041 (relating to information at source) is amended by adding at the end the following new subsection:

` (g) NONQUALIFIED DEFERRED COMPENSATION- Subsection (a) shall apply to--

``(1) any deferrals for the year under a nonqualified deferred compensation plan (within the meaning of section 409A(d)), whether or not paid, except that this paragraph shall not apply to deferrals which are required to be reported under section 6051(a)(13) (without regard to any de minimis exception), and

``(2) any amount includable under section 409A and which is not treated as wages under section 3401(a).'

(c) CLERICAL AMENDMENT- The table of sections for such subpart A of part I of subchapter D of chapter 1 is amended by adding at the end the following new item:

``Sec. 409A. Inclusion in gross income of deferred compensation under nonqualified deferred compensation plans.'

(d) EFFECTIVE DATE-

(1) IN GENERAL- The amendments made by this section shall apply to amounts deferred after December 31, 2004.

(2) SPECIAL RULES-

(A) EARNINGS- The amendments made by this section shall apply to earnings on deferred compensation only to the extent that such amendments apply to such compensation.

(B) MATERIAL MODIFICATIONS- For purposes of this subsection, amounts deferred in taxable years beginning before January 1, 2005, shall be treated as amounts deferred in a taxable year beginning on or after such date if the plan under which the deferral is made is materially modified after October 3, 2004, unless such modification is pursuant to the guidance issued under subsection (f).

(3) EXCEPTION FOR NONELECTIVE DEFERRED COMPENSATION- The amendments made by this section shall not apply to any nonelective deferred compensation to which section 457 of the Internal Revenue Code of 1986 does not apply by reason of section 457(e)(12) of such Code, but only if such compensation is provided under a nonqualified deferred compensation plan-

(A) which was in existence on May 1, 2004,

(B) which was providing nonelective deferred compensation described in such section 457(e)(12) on such date, and

(C) which is established or maintained by an organization incorporated on July 2, 1974.

If, after May 1, 2004, a plan described in the preceding sentence adopts a plan amendment which provides a material change in the classes of individuals eligible to participate in the plan, this paragraph shall not apply to any nonelective deferred compensation provided under the plan on or after the date of the adoption of the amendment.

(e) GUIDANCE RELATING TO CHANGE OF OWNERSHIP OR CONTROL- Not later than 90 days after the date of the enactment of this Act, the Secretary of the Treasury shall issue guidance on what constitutes a change in ownership or effective control for purposes of section 409A of the Internal Revenue Code of 1986, as added by this section.

(f) GUIDANCE RELATING TO TERMINATION OF CERTAIN EXISTING ARRANGEMENTS- Not later than 60 days after the date of the enactment of this Act, the Secretary of the Treasury shall issue guidance providing a limited period during

which a nonqualified deferred compensation plan adopted before December 31, 2004, may, without violating the requirements of paragraphs (2), (3), and (4) of section 409A(a) of the Internal Revenue Code of 1986 (as added by this section), be amended--

- (1) to provide that a participant may terminate participation in the plan, or cancel an outstanding deferral election with regard to amounts deferred after December 31, 2004, but only if amounts subject to the termination or cancellation are includable in income of the participant as earned (or, if later, when no longer subject to substantial risk of forfeiture), and
- (2) to conform to the requirements of such section 409A with regard to amounts deferred after December 31, 2004.

## **SEC. 886. EXTENSION OF AMORTIZATION OF INTANGIBLES TO SPORTS FRANCHISES.**

(a) IN GENERAL- Section 197(e) (relating to exceptions to definition of section 197 intangible) is amended by striking paragraph (6) and by redesignating paragraphs (7) and (8) as paragraphs (6) and (7), respectively.

(b) CONFORMING AMENDMENTS-

- (1)(A) Section 1056 (relating to basis limitation for player contracts transferred in connection with the sale of a franchise) is repealed.
- (B) The table of sections for part IV of subchapter O of chapter 1 is amended by striking the item relating to section 1056.
- (2) Section 1245(a) (relating to gain from disposition of certain depreciable property) is amended by striking paragraph (4).
- (3) Section 1253 (relating to transfers of franchises, trademarks, and trade names) is amended by striking subsection (e).

(c) EFFECTIVE DATES-

- (1) IN GENERAL- Except as provided in paragraph (2), the amendments made by this section shall apply to property acquired after the date of the enactment of this Act.
- (2) SECTION 1245- The amendment made by subsection (b)(2) shall apply to franchises acquired after the date of the enactment of this Act.

## **SEC. 887. MODIFICATION OF CONTINUING LEVY ON PAYMENTS TO FEDERAL VENDORS.**

(a) IN GENERAL- Section 6331(h) (relating to continuing levy on certain payments) is amended by adding at the end the following new paragraph:

``(3) INCREASE IN LEVY FOR CERTAIN PAYMENTS- Paragraph (1) shall be applied by substituting ``100 percent'' for ``15 percent'' in the case of any specified payment due to a vendor of goods or services sold or leased to the Federal Government.''

(b) EFFECTIVE DATE- The amendment made by this section shall take effect on the date of the enactment of this Act.

## **SEC. 888. MODIFICATION OF STRADDLE RULES.**

(a) RULES RELATING TO IDENTIFIED STRADDLES-

(1) IN GENERAL- Subparagraph (A) of section 1092(a)(2) (relating to special rule for identified straddles) is amended to read as follows:

`(A) IN GENERAL- In the case of any straddle which is an identified straddle--

`(i) paragraph (1) shall not apply with respect to identified positions comprising the identified straddle,

`(ii) if there is any loss with respect to any identified position of the identified straddle, the basis of each of the identified offsetting positions in the identified straddle shall be increased by an amount which bears the same ratio to the loss as the unrecognized gain with respect to such offsetting position bears to the aggregate unrecognized gain with respect to all such offsetting positions, and

`(iii) any loss described in clause (ii) shall not otherwise be taken into account for purposes of this title.'

(2) IDENTIFIED STRADDLE- Section 1092(a)(2)(B) (defining identified straddle) is amended--

(A) by striking clause (ii) and inserting the following:

`(ii) to the extent provided by regulations, the value of each position of which (in the hands of the taxpayer immediately before the creation of the straddle) is not less than the basis of such position in the hands of the taxpayer at the time the straddle is created, and', and

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

`The Secretary shall prescribe regulations which specify the proper methods for clearly identifying a straddle as an identified straddle (and the positions comprising such straddle), which specify the rules for the application of this section for a taxpayer which fails to properly identify the positions of an identified straddle, and which specify the ordering rules in cases where a taxpayer disposes of less than an entire position which is part of an identified straddle.'

(3) UNRECOGNIZED GAIN- Section 1092(a)(3) (defining unrecognized gain) is amended by redesignating subparagraph (B) as subparagraph (C) and by inserting after subparagraph (A) the following new subparagraph:

`(B) SPECIAL RULE FOR IDENTIFIED STRADDLES- For purposes of paragraph (2)(A)(ii), the unrecognized gain with respect to any identified offsetting position shall be the excess of the fair market value of the position at the time of the determination over the fair market value of the position at the time the taxpayer identified the position as a position in an identified straddle.'

(4) CONFORMING AMENDMENT- Section 1092(c)(2) is amended by striking subparagraph (B) and by redesignating subparagraph (C) as subparagraph (B).

(b) PHYSICALLY SETTLED POSITIONS- Section 1092(d) (relating to definitions and special rules) is amended by adding at the end the following new paragraph:

`(8) SPECIAL RULES FOR PHYSICALLY SETTLED POSITIONS- For purposes of subsection (a), if a taxpayer settles a position which is part of a straddle by delivering property to which the position relates (and such position, if terminated, would result in a realization of a loss), then such taxpayer shall be treated as if such taxpayer--

`(A) terminated the position for its fair market value immediately before the settlement, and

`(B) sold the property so delivered by the taxpayer at its fair market value.'

(c) REPEAL OF STOCK EXCEPTION-

(1) IN GENERAL- Paragraph (3) of section 1092(d) (relating to definitions and special rules) is amended to read as follows:

  `(3) SPECIAL RULES FOR STOCK- For purposes of paragraph (1)--

    `**(A) IN GENERAL-** In the case of stock, the term 'personal property' includes stock only if--

      `**(i)** such stock is of a type which is actively traded and at least 1 of the positions offsetting such stock is a position with respect to such stock or substantially similar or related property, or

      `**(ii)** such stock is of a corporation formed or availed of to take positions in personal property which offset positions taken by any shareholder.

    `**(B) RULE FOR APPLICATION-** For purposes of determining whether subsection (e) applies to any transaction with respect to stock described in subparagraph (A)(ii), all includable corporations of an affiliated group (within the meaning of section 1504(a)) shall be treated as 1 taxpayer.'

(2) CONFORMING AMENDMENT- Section 1258(d)(1) is amended by striking `; except that the term 'personal property' shall include stock'.

(d) HOLDING PERIOD FOR DIVIDEND EXCLUSION- The last sentence of section 246(c) is amended by inserting: `, other than a qualified covered call option to which section 1092(f) applies' before the period at the end.

(e) EFFECTIVE DATE- The amendments made by this section shall apply to positions established on or after the date of the enactment of this Act.

## **SEC. 889. ADDITION OF VACCINES AGAINST HEPATITIS A TO LIST OF TAXABLE VACCINES.**

(a) IN GENERAL- Paragraph (1) of section 4132(a) (defining taxable vaccine) is amended by redesignating subparagraphs (I), (J), (K), and (L) as subparagraphs (J), (K), (L), and (M), respectively, and by inserting after subparagraph (H) the following new subparagraph:

  `**(I)** Any vaccine against hepatitis A.'

(b) EFFECTIVE DATE-

(1) SALES, ETC- The amendments made by subsection (a) shall apply to sales and uses on or after the first day of the first month which begins more than 4 weeks after the date of the enactment of this Act.

(2) DELIVERIES- For purposes of paragraph (1) and section 4131 of the Internal Revenue Code of 1986, in the case of sales on or before the effective date described in such paragraph for which delivery is made after such date, the delivery date shall be considered the sale date.

## **SEC. 890. ADDITION OF VACCINES AGAINST INFLUENZA TO LIST OF TAXABLE VACCINES.**

(a) IN GENERAL- Section 4132(a)(1) (defining taxable vaccine), as amended by this Act, is amended by adding at the end the following new subparagraph:

  `**(N)** Any trivalent vaccine against influenza.'

(b) EFFECTIVE DATE-

(1) SALES, ETC- The amendment made by this section shall apply to sales and uses on or after the later of-

(A) the first day of the first month which begins more than 4 weeks after the date of the enactment of this Act, or

(B) the date on which the Secretary of Health and Human Services lists any vaccine against influenza for purposes of compensation for any vaccine-related injury or death through the Vaccine Injury Compensation Trust Fund.

(2) DELIVERIES- For purposes of paragraph (1) and section 4131 of the Internal Revenue Code of 1986, in the case of sales on or before the effective date described in such paragraph for which delivery is made after such date, the delivery date shall be considered the sale date.

## **SEC. 891. EXTENSION OF IRS USER FEES.**

(a) IN GENERAL- Section 7528(c) (relating to termination) is amended by striking 'December 31, 2004' and inserting 'September 30, 2014'.

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

## **SEC. 892. COBRA FEES.**

(a) USE OF MERCHANDISE PROCESSING FEE- Section 13031(f) of the Consolidated Omnibus Budget Reconciliation Act of 1985 (19 U.S.C. 58c(f)) is amended--

(1) in paragraph (1), by aligning subparagraph (B) with subparagraph (A); and

(2) in paragraph (2), by striking 'commercial operations' and all that follows through 'processing.' and inserting 'customs revenue functions as defined in section 415 of the Homeland Security Act of 2002 (other than functions performed by the Office of International Affairs referred to in section 415(8) of that Act), and for automation (including the Automation Commercial Environment computer system), and for no other purpose. To the extent that funds in the Customs User Fee Account are insufficient to pay the costs of such customs revenue functions, customs duties in an amount equal to the amount of such insufficiency shall be available, to the extent provided for in appropriations Acts, to pay the costs of such customs revenue functions in the amount of such insufficiency, and shall be available for no other purpose. The provisions of the first and second sentences of this paragraph specifying the purposes for which amounts in the Customs User Fee Account may be made available shall not be superseded except by a provision of law which specifically modifies or supersedes such provisions.'

(b) REIMBURSEMENT OF APPROPRIATIONS FROM COBRA FEES- Section 13031(f)(3) of the Consolidated Omnibus Budget Reconciliation Act of 1985 (19 U.S.C. 58c(f)(3)) is amended by adding at the end the following:

'(E) Nothing in this paragraph shall be construed to preclude the use of appropriated funds, from sources other than the fees collected under subsection (a), to pay the costs set forth in clauses (i), (ii), and (iii) of subparagraph (A).'

(c) SENSE OF CONGRESS; EFFECTIVE PERIOD FOR COLLECTING FEES; STANDARD FOR SETTING FEES-

(1) SENSE OF CONGRESS- The Congress finds that--

(A) the fees set forth in paragraphs (1) through (8) of subsection (a) of section 13031 of the Consolidated Omnibus Budget Reconciliation Act of 1985 have been reasonably related to the costs of providing customs services in connection with the activities or items for which the fees have been charged under such paragraphs; and

(B) the fees collected under such paragraphs have not exceeded, in the aggregate, the amounts paid for the costs described in subsection (f)(3)(A) incurred in providing customs services in connection with the activities or items for which the fees were charged under such paragraphs.

(2) EFFECTIVE PERIOD; STANDARD FOR SETTING FEES- Section 13031(j)(3) of the Consolidated Omnibus Budget Reconciliation Act of 1985 is amended to read as follows:

`(3)(A) Fees may not be charged under paragraphs (9) and (10) of subsection (a) after September 30, 2014.

`(B)(i) Subject to clause (ii), Fees may not be charged under paragraphs (1) through (8) of subsection (a) after September 30, 2014.

`(ii) In fiscal year 2006 and in each succeeding fiscal year for which fees under paragraphs (1) through (8) of subsection (a) are authorized--

` (I) the Secretary of the Treasury shall charge fees under each such paragraph in amounts that are reasonably related to the costs of providing customs services in connection with the activity or item for which the fee is charged under such paragraph, except that in no case may the fee charged under any such paragraph exceed by more than 10 percent the amount otherwise prescribed by such paragraph;

` (II) the amount of fees collected under such paragraphs may not exceed, in the aggregate, the amounts paid in that fiscal year for the costs described in subsection (f)(3)(A) incurred in providing customs services in connection with the activity or item for which the fees are charged under such paragraphs;

` (III) a fee may not be collected under any such paragraph except to the extent such fee will be expended to pay the costs described in subsection (f)(3)(A) incurred in providing customs services in connection with the activity or item for which the fee is charged under such paragraph; and

` (IV) any fee collected under any such paragraph shall be available for expenditure only to pay the costs described in subsection (f)(3)(A) incurred in providing customs services in connection with the activity or item for which the fee is charged under such paragraph.'

(d) CLERICAL AMENDMENTS- Section 13031 of the Consolidated Omnibus Budget Reconciliation Act of 1985 is amended--

(1) in subsection (a)(5)(B), by striking '\$1.75' and inserting '\$1.75.';

(2) in subsection (b)--

(A) in paragraph (1)(A), by aligning clause (iii) with clause (ii);

(B) in paragraph (7), by striking 'paragraphs' and inserting 'paragraph'; and

(C) in paragraph (9), by aligning subparagraph (B) with subparagraph (A); and

(3) in subsection (e)(2), by aligning subparagraph (B) with subparagraph (A).

(e) STUDY OF ALL FEES COLLECTED BY DEPARTMENT OF HOMELAND SECURITY- The Secretary of the Treasury shall conduct a study of all the fees collected

by the Department of Homeland Security, and shall submit to the Congress, not later than September 30, 2005, a report containing the recommendations of the Secretary on--

- (1) what fees should be eliminated;
- (2) what the rate of fees retained should be; and
- (3) any other recommendations with respect to the fees that the Secretary considers appropriate.

## **SEC. 893. PROHIBITION ON NONRECOGNITION OF GAIN THROUGH COMPLETE LIQUIDATION OF HOLDING COMPANY.**

(a) IN GENERAL- Section 332 is amended by adding at the end the following new subsection:

``(d) RECOGNITION OF GAIN ON LIQUIDATION OF CERTAIN HOLDING COMPANIES-

``(1) IN GENERAL- In the case of any distribution to a foreign corporation in complete liquidation of an applicable holding company--

``(A) subsection (a) and section 331 shall not apply to such distribution, and

``(B) such distribution shall be treated as a distribution to which section 301 applies.

``(2) APPLICABLE HOLDING COMPANY- For purposes of this subsection:

``(A) IN GENERAL- The term `applicable holding company' means any domestic corporation--

``(i) which is a common parent of an affiliated group,

``(ii) stock of which is directly owned by the distributee foreign corporation,

``(iii) substantially all of the assets of which consist of stock in other members of such affiliated group, and

``(iv) which has not been in existence at all times during the 5 years immediately preceding the date of the liquidation.

``(B) AFFILIATED GROUP- For purposes of this subsection, the term `affiliated group' has the meaning given such term by section 1504(a) (without regard to paragraphs (2) and (4) of section 1504(b)).

``(3) COORDINATION WITH SUBPART F- If the distributee of a distribution described in paragraph (1) is a controlled foreign corporation (as defined in section 957), then notwithstanding paragraph (1) or subsection (a), such distribution shall be treated as a distribution to which section 331 applies.

``(4) REGULATIONS- The Secretary shall provide such regulations as appropriate to prevent the abuse of this subsection, including regulations which provide, for the purposes of clause (iv) of paragraph (2)(A), that a corporation is not in existence for any period unless it is engaged in the active conduct of a trade or business or owns a significant ownership interest in another corporation so engaged.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply to distributions in complete liquidation occurring on or after the date of the enactment of this Act.

## **SEC. 894. EFFECTIVELY CONNECTED INCOME TO INCLUDE CERTAIN FOREIGN SOURCE INCOME.**

(a) IN GENERAL- Section 864(c)(4)(B) (relating to treatment of income from sources without the United States as effectively connected income) is amended by adding at the end the following new flush sentence:

`Any income or gain which is equivalent to any item of income or gain described in clause (i), (ii), or (iii) shall be treated in the same manner as such item for purposes of this subparagraph.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply to taxable years beginning after the date of the enactment of this Act.

## **SEC. 895. RECAPTURE OF OVERALL FOREIGN LOSSES ON SALE OF CONTROLLED FOREIGN CORPORATION.**

(a) IN GENERAL- Section 904(f)(3) (relating to dispositions) is amending by adding at the end the following new subparagraph:

`(D) APPLICATION TO CERTAIN DISPOSITIONS OF STOCK IN CONTROLLED FOREIGN CORPORATION-

`(i) IN GENERAL- This paragraph shall apply to an applicable disposition in the same manner as if it were a disposition of property described in subparagraph (A), except that the exception contained in subparagraph (C)(i) shall not apply.

`(ii) APPLICABLE DISPOSITION- For purposes of clause (i), the term `applicable disposition' means any disposition of any share of stock in a controlled foreign corporation in a transaction or series of transactions if, immediately before such transaction or series of transactions, the taxpayer owned more than 50 percent (by vote or value) of the stock of the controlled foreign corporation. Such term shall not include a disposition described in clause (iii) or (iv), except that clause (i) shall apply to any gain recognized on any such disposition.

`(iii) EXCEPTION FOR CERTAIN EXCHANGES WHERE OWNERSHIP

PERCENTAGE RETAINED- A disposition shall not be treated as an applicable disposition under clause (ii) if it is part of a transaction or series of transactions--

`(I) to which section 351 or 721 applies, or under which the transferor receives stock in a foreign corporation in exchange for the stock in the controlled foreign corporation and the stock received is exchanged basis property (as defined in section 7701(a)(44)), and

`(II) immediately after which, the transferor owns (by vote or value) at least the same percentage of stock in the controlled foreign corporation (or, if the controlled foreign corporation is not in existence after such transaction or series of transactions, in another foreign corporation stock in which was received by the transferor in exchange for stock in the controlled foreign corporation) as the percentage of stock in the controlled foreign corporation which the taxpayer owned immediately before such transaction or series of transactions.

`(iv) EXCEPTION FOR CERTAIN ASSET ACQUISITIONS- A disposition shall not be treated as an applicable disposition under clause (ii) if it is part of a transaction or series of transactions in which the taxpayer (or any member of a controlled group of corporations filing a consolidated return under section 1501 which includes the taxpayer) acquires the assets of a controlled foreign corporation in exchange for the shares of the controlled foreign corporation in a liquidation described in section 332 or a reorganization described in section 368(a)(1).

``(v) CONTROLLED FOREIGN CORPORATION- For purposes of this subparagraph, the term `controlled foreign corporation' has the meaning given such term by section 957.  
``(vi) STOCK OWNERSHIP- For purposes of this subparagraph, ownership of stock shall be determined under the rules of subsections (a) and (b) of section 958.'.  
(b) EFFECTIVE DATE- The amendment made by this section shall apply to dispositions after the date of the enactment of this Act.

### **SEC. 896. RECOGNITION OF CANCELLATION OF INDEBTEDNESS INCOME REALIZED ON SATISFACTION OF DEBT WITH PARTNERSHIP INTEREST.**

(a) IN GENERAL- Paragraph (8) of section 108(e) (relating to general rules for discharge of indebtedness (including discharges not in title 11 cases or insolvency)) is amended to read as follows:

``(8) INDEBTEDNESS SATISFIED BY CORPORATE STOCK OR PARTNERSHIP  
INTEREST- For purposes of determining income of a debtor from discharge of  
indebtedness, if-

``(A) a debtor corporation transfers stock, or

``(B) a debtor partnership transfers a capital or profits interest in such partnership, to a creditor in satisfaction of its recourse or nonrecourse indebtedness, such corporation or partnership shall be treated as having satisfied the indebtedness with an amount of money equal to the fair market value of the stock or interest. In the case of any partnership, any discharge of indebtedness income recognized under this paragraph shall be included in the distributive shares of taxpayers which were the partners in the partnership immediately before such discharge.'.

(b) EFFECTIVE DATE- The amendment made by this section shall apply with respect to cancellations of indebtedness occurring on or after the date of the enactment of this Act.

### **SEC. 897. DENIAL OF INSTALLMENT SALE TREATMENT FOR ALL READILY TRADEABLE DEBT.**

(a) IN GENERAL- Section 453(f)(4)(B) (relating to purchaser evidences of indebtedness payable on demand or readily tradable) is amended by striking `is issued by a corporation or a government or political subdivision thereof and'.

(b) EFFECTIVE DATE- The amendment made by this section shall apply to sales occurring on or after the date of the enactment of this Act.

### **SEC. 898. MODIFICATION OF TREATMENT OF TRANSFERS TO CREDITORS IN DIVISIVE REORGANIZATIONS.**

(a) IN GENERAL- Section 361(b)(3) (relating to treatment of transfers to creditors) is amended by adding at the end the following new sentence: `In the case of a reorganization described in section 368(a)(1)(D) with respect to which stock or securities of the corporation to which the assets are transferred are distributed in a transaction which qualifies under section 355, this paragraph shall apply only to the extent that the

sum of the money and the fair market value of other property transferred to such creditors does not exceed the adjusted bases of such assets transferred.'.

(b) LIABILITIES IN EXCESS OF BASIS- Section 357(c)(1)(B) is amended by inserting 'with respect to which stock or securities of the corporation to which the assets are transferred are distributed in a transaction which qualifies under section 355' after 'section 368(a)(1)(D)'.

(c) EFFECTIVE DATE- The amendments made by this section shall apply to transfers of money or other property, or liabilities assumed, in connection with a reorganization occurring on or after the date of the enactment of this Act.

## **SEC. 899. CLARIFICATION OF DEFINITION OF NONQUALIFIED PREFERRED STOCK.**

(a) IN GENERAL- Section 351(g)(3)(A) is amended by adding at the end the following: 'Stock shall not be treated as participating in corporate growth to any significant extent unless there is a real and meaningful likelihood of the shareholder actually participating in the earnings and growth of the corporation.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply to transactions after May 14, 2003.

## **SEC. 900. MODIFICATION OF DEFINITION OF CONTROLLED GROUP OF CORPORATIONS.**

(a) IN GENERAL- Section 1563(a)(2) (relating to brother-sister controlled group) is amended by striking 'possessing--' and all that follows through '(B)' and inserting 'possessing'.

(b) APPLICATION OF EXISTING RULES TO OTHER CODE PROVISIONS- Section 1563(f) (relating to other definitions and rules) is amended by adding at the end the following new paragraph:

  `(5) BROTHER-SISTER CONTROLLED GROUP DEFINITION FOR PROVISIONS OTHER THAN THIS PART-

    `(A) IN GENERAL- Except as specifically provided in an applicable provision, subsection (a)(2) shall be applied to an applicable provision as if it read as follows:

    `  (2) BROTHER-SISTER CONTROLLED GROUP- Two or more corporations if 5 or fewer persons who are individuals, estates, or trusts own (within the meaning of subsection (d)(2) stock possessing--

    `  (A) at least 80 percent of the total combined voting power of all classes of stock entitled to vote, or at least 80 percent of the total value of shares of all classes of stock, of each corporation, and

    `  (B) more than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of shares of all classes of stock of each corporation, taking into account the stock ownership of each such person only to the extent such stock ownership is identical with respect to each such corporation.'

    `  (B) APPLICABLE PROVISION- For purposes of this paragraph, an applicable provision is any provision of law (other than this part) which incorporates the definition of controlled group of corporations under subsection (a).'

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

## **SEC. 901. CLASS LIVES FOR UTILITY GRADING COSTS.**

(a) GAS UTILITY PROPERTY- Section 168(e)(3)(E) (defining 15-year property), as amended by this Act, is amended by striking `and' at the end of clause (iv), by striking the period at the end of clause (v) and inserting `, and', and by adding at the end the following new clause:

`(vi) initial clearing and grading land improvements with respect to gas utility property.'.

(b) ELECTRIC UTILITY PROPERTY- Section 168(e)(3) is amended by adding at the end the following new subparagraph:

`(F) 20-YEAR PROPERTY- The term `20-year property' means initial clearing and grading land improvements with respect to any electric utility transmission and distribution plant.'.

(c) CONFORMING AMENDMENT- The table contained in section 168(g)(3)(B), as amended by this Act, is amended by inserting after the item relating to subparagraph (E)(v) the following new items:

`(E)(vi)

20'.

`(F)

25'.

(d) EFFECTIVE DATE- The amendments made by this section shall apply to property placed in service after the date of the enactment of this Act.

## **SEC. 902. CONSISTENT AMORTIZATION OF PERIODS FOR INTANGIBLES.**

(a) START-UP EXPENDITURES-

(1) ALLOWANCE OF DEDUCTION- Paragraph (1) of section 195(b) (relating to start-up expenditures) is amended to read as follows:

`(1) ALLOWANCE OF DEDUCTION- If a taxpayer elects the application of this subsection with respect to any start-up expenditures--

`(A) the taxpayer shall be allowed a deduction for the taxable year in which the active trade or business begins in an amount equal to the lesser of-

`(i) the amount of start-up expenditures with respect to the active trade or business, or

`(ii) \$5,000, reduced (but not below zero) by the amount by which such start-up expenditures exceed \$50,000, and

`(B) the remainder of such start-up expenditures shall be allowed as a deduction ratably over the 180-month period beginning with the month in which the active trade or business begins.'.

(2) CONFORMING AMENDMENT- Subsection (b) of section 195 is amended by striking `AMORTIZE' and inserting `DEDUCT' in the heading.

(b) ORGANIZATIONAL EXPENDITURES- Subsection (a) of section 248 (relating to organizational expenditures) is amended to read as follows:

`(a) ELECTION TO DEDUCT- If a corporation elects the application of this subsection (in accordance with regulations prescribed by the Secretary) with respect to any organizational expenditures--

`(1) the corporation shall be allowed a deduction for the taxable year in which the corporation begins business in an amount equal to the lesser of--

`(A) the amount of organizational expenditures with respect to the taxpayer, or

`(B) \$5,000, reduced (but not below zero) by the amount by which such organizational expenditures exceed \$50,000, and

`(2) the remainder of such organizational expenditures shall be allowed as a deduction ratably over the 180-month period beginning with the month in which the corporation begins business.'

(c) TREATMENT OF ORGANIZATIONAL AND SYNDICATION FEES OR PARTNERSHIPS-

(1) IN GENERAL- Section 709(b) (relating to amortization of organization fees) is amended by redesignating paragraph (2) as paragraph (3) and by amending paragraph (1) to read as follows:

`(1) ALLOWANCE OF DEDUCTION- If a taxpayer elects the application of this subsection (in accordance with regulations prescribed by the Secretary) with respect to any organizational expenses--

`(A) the taxpayer shall be allowed a deduction for the taxable year in which the partnership begins business in an amount equal to the lesser of--

`(i) the amount of organizational expenses with respect to the partnership, or

`(ii) \$5,000, reduced (but not below zero) by the amount by which such organizational expenses exceed \$50,000, and

`(B) the remainder of such organizational expenses shall be allowed as a deduction ratably over the 180-month period beginning with the month in which the partnership begins business.

`(2) DISPOSITIONS BEFORE CLOSE OF AMORTIZATION PERIOD- In any case in which a partnership is liquidated before the end of the period to which paragraph (1)(B) applies, any deferred expenses attributable to the partnership which were not allowed as a deduction by reason of this section may be deducted to the extent allowable under section 165.'

(2) CONFORMING AMENDMENT- Subsection (b) of section 709 is amended by striking `AMORTIZATION' and inserting `DEDUCTION' in the heading.

(d) EFFECTIVE DATE- The amendments made by this section shall apply to amounts paid or incurred after the date of the enactment of this Act.

## **SEC. 903. FREEZE OF PROVISIONS REGARDING SUSPENSION OF INTEREST WHERE SECRETARY FAILS TO CONTACT TAXPAYER.**

(a) IN GENERAL- Section 6404(g) (relating to suspension of interest and certain penalties where Secretary fails to contact taxpayer) is amended by striking `1-year period

(18-month period in the case of taxable years beginning before January 1, 2004)' both places it appears and inserting `18-month period'.

(b) EXCEPTION FOR GROSS MISSTATEMENT- Section 6404(g)(2) (relating to exceptions) is amended by striking `or' at the end of subparagraph (C), by redesignating subparagraph (D) as subparagraph (E), and by inserting after subparagraph (C) the following new subparagraph:

`(D) any interest, penalty, addition to tax, or additional amount with respect to any gross misstatement; or'.

(c) EXCEPTION FOR LISTED AND REPORTABLE TRANSACTIONS- Section 6404(g)(2) (relating to exceptions), as amended by subsection (b), is amended by striking `or' at the end of subparagraph (D), by redesignating subparagraph (E) as subparagraph (F), and by inserting after subparagraph (D) the following new subparagraph:

`(E) any interest, penalty, addition to tax, or additional amount with respect to any reportable transaction with respect to which the requirement of section 6664(d)(2)(A) is not met and any listed transaction (as defined in 6707A(c)); or'.

(d) EFFECTIVE DATES-

(1) IN GENERAL- Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 2003.

(2) EXCEPTION FOR REPORTABLE OR LISTED TRANSACTIONS- The amendments made by subsection (c) shall apply with respect to interest accruing after October 3, 2004.

## **SEC. 904. INCREASE IN WITHHOLDING FROM SUPPLEMENTAL WAGE PAYMENTS IN EXCESS OF \$1,000,000.**

(a) IN GENERAL- If an employer elects under Treasury Regulation 31.3402(g)-1 to determine the amount to be deducted and withheld from any supplemental wage payment by using a flat percentage rate, the rate to be used in determining the amount to be so deducted and withheld shall not be less than 28 percent (or the corresponding rate in effect under section 1(i)(2) of the Internal Revenue Code of 1986 for taxable years beginning in the calendar year in which the payment is made).

(b) SPECIAL RULE FOR LARGE PAYMENTS-

(1) IN GENERAL- Notwithstanding subsection (a), if the supplemental wage payment, when added to all such payments previously made by the employer to the employee during the calendar year, exceeds \$1,000,000, the rate used with respect to such excess shall be equal to the maximum rate of tax in effect under section 1 of such Code for taxable years beginning in such calendar year.

(2) AGGREGATION- All persons treated as a single employer under subsection (a) or (b) of section 52 of the Internal Revenue Code of 1986 shall be treated as a single employer for purposes of this subsection.

(c) CONFORMING AMENDMENT- Section 13273 of the Revenue Reconciliation Act of 1993 (Public Law 103-66) is repealed.

(d) EFFECTIVE DATE- The provisions of, and the amendment made by, this section shall apply to payments made after December 31, 2004.

## **SEC. 905. TREATMENT OF SALE OF STOCK ACQUIRED PURSUANT TO EXERCISE OF STOCK OPTIONS TO COMPLY WITH CONFLICT-OF-INTEREST REQUIREMENTS.**

(a) IN GENERAL- Section 421 (relating to general rules for certain stock options) is amended by adding at the end the following new subsection:

``(d) CERTAIN SALES TO COMPLY WITH CONFLICT-OF-INTEREST REQUIREMENTS- If-``

``(1) a share of stock is transferred to an eligible person (as defined in section 1043(b)(1)) pursuant to such person's exercise of an option to which this part applies, and

``(2) such share is disposed of by such person pursuant to a certificate of divestiture (as defined in section 1043(b)(2)),

such disposition shall be treated as meeting the requirements of section 422(a)(1) or 423(a)(1), whichever is applicable.'.

(b) EFFECTIVE DATE- The amendment made by this section shall apply to sales after the date of the enactment of this Act.

## **SEC. 906. APPLICATION OF BASIS RULES TO NONRESIDENT ALIENS.**

(a) IN GENERAL- Section 72 (relating to annuities and certain proceeds of endowment and life insurance contracts) is amended by redesignating subsection (w) as subsection (x) and by inserting after subsection (v) the following new subsection:

``(w) APPLICATION OF BASIS RULES TO NONRESIDENT ALIENS-

``(1) IN GENERAL- Notwithstanding any other provision of this section, for purposes of determining the portion of any distribution which is includable in gross income of a distributee who is a citizen or resident of the United States, the investment in the contract shall not include any applicable nontaxable contributions or applicable nontaxable earnings.

``(2) APPLICABLE NONTAXABLE CONTRIBUTION- For purposes of this subsection, the term `applicable nontaxable contribution' means any employer or employee contribution-``

``(A) which was made with respect to compensation-``

``(i) for labor or personal services performed by an employee who, at the time the labor or services were performed, was a nonresident alien for purposes of the laws of the United States in effect at such time, and

``(ii) which is treated as from sources without the United States, and

``(B) which was not subject to income tax (and would have been subject to income tax if paid as cash compensation when the services were rendered) under the laws of the United States or any foreign country.

``(3) APPLICABLE NONTAXABLE EARNINGS- For purposes of this subsection, the term `applicable nontaxable earnings' means earnings-``

``(A) which are paid or accrued with respect to any employer or employee contribution which was made with respect to compensation for labor or personal services performed by an employee,

``(B) with respect to which the employee was at the time the earnings were paid or accrued a nonresident alien for purposes of the laws of the United States, and  
``(C) which were not subject to income tax under the laws of the United States or any foreign country.

``(4) REGULATIONS- The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this subsection, including regulations treating contributions and earnings as not subject to tax under the laws of any foreign country where appropriate to carry out the purposes of this subsection.'

(b) BASIS- Section 83 (relating to property transferred in connection with the performance of services is amended by adding after paragraph (3) of subsection (c) the following new paragraph:

``(4) For purposes of determining an individual's basis in property transferred in connection with the performance of services, rules similar to the rules of section 72(w) shall apply.'

(c) EFFECTIVE DATE- The amendments made by this section shall apply to distributions on or after the date of the enactment of this Act.

## **SEC. 907. LIMITATION OF EMPLOYER DEDUCTION FOR CERTAIN ENTERTAINMENT EXPENSES.**

(a) IN GENERAL- Paragraph (2) of section 274(e) (relating to expenses treated as compensation) is amended to read as follows:

``(2) EXPENSES TREATED AS COMPENSATION-

``(A) IN GENERAL- Except as provided in subparagraph (B), expenses for goods, services, and facilities, to the extent that the expenses are treated by the taxpayer, with respect to the recipient of the entertainment, amusement, or recreation, as compensation to an employee on the taxpayer's return of tax under this chapter and as wages to such employee for purposes of chapter 24 (relating to withholding of income tax at source on wages).

``(B) SPECIFIED INDIVIDUALS-

``(i) IN GENERAL- In the case of a recipient who is a specified individual, subparagraph (A) and paragraph (9) shall each be applied by substituting `to the extent that the expenses do not exceed the amount of the expenses which' for `to the extent that the expenses'.

``(ii) SPECIFIED INDIVIDUAL- For purposes of clause (i), the term `specified individual' means any individual who--

``(I) is subject to the requirements of section 16(a) of the Securities Exchange Act of 1934 with respect to the taxpayer, or

``(II) would be subject to such requirements if the taxpayer were an issuer of equity securities referred to in such section.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply to expenses incurred after the date of the enactment of this Act.

## **SEC. 908. RESIDENCE AND SOURCE RULES RELATING TO UNITED STATES POSSESSIONS.**

(a) RESIDENCE AND SOURCE RULES- Subpart D of part III of subchapter N of chapter 1 (relating to possessions of the United States) is amended by adding at the end the following new section:

**SEC. 937. RESIDENCE AND SOURCE RULES INVOLVING POSSESSIONS.**

^(a) BONA FIDE RESIDENT- For purposes of this subpart, section 865(g)(3), section 876, section 881(b), paragraphs (2) and (3) of section 901(b), section 957(c), section 3401(a)(8)(C), and section 7654(a), except as provided in regulations, the term `bona fide resident' means a person--

^(1) who is present for at least 183 days during the taxable year in Guam, American Samoa, the Northern Mariana Islands, Puerto Rico, or the Virgin Islands, as the case may be, and

^(2) who does not have a tax home (determined under the principles of section 911(d)(3) without regard to the second sentence thereof) outside such specified possession during the taxable year and does not have a closer connection (determined under the principles of section 7701(b)(3)(B)(ii)) to the United States or a foreign country than to such specified possession.

For purposes of paragraph (1), the determination as to whether a person is present for any day shall be made under the principles of section 7701(b).

^(b) SOURCE RULES- Except as provided in regulations, for purposes of this title--

^(1) except as provided in paragraph (2), rules similar to the rules for determining whether income is income from sources within the United States or is effectively connected with the conduct of a trade or business within the United States shall apply for purposes of determining whether income is from sources within a possession specified in subsection (a)(1) or effectively connected with the conduct of a trade or business within any such possession, and

^(2) any income treated as income from sources within the United States or as effectively connected with the conduct of a trade or business within the United States shall not be treated as income from sources within any such possession or as effectively connected with the conduct of a trade or business within any such possession.

^(c) REPORTING REQUIREMENT-

^(1) IN GENERAL- If, for any taxable year, an individual takes the position for United States income tax reporting purposes that the individual became, or ceases to be, a bona fide resident of a possession specified in subsection (a)(1), such individual shall file with the Secretary, at such time and in such manner as the Secretary may prescribe, notice of such position.

^(2) TRANSITION RULE- If, for any of an individual's 3 taxable years ending before the individual's first taxable year ending after the date of the enactment of this subsection, the individual took a position described in paragraph (1), the individual shall file with the Secretary, at such time and in such manner as the Secretary may prescribe, notice of such position.'

(b) PENALTY- Section 6688 is amended--

(1) by inserting `under section 937(c) or' before `by regulations', and

(2) by striking `'\$100' and inserting `'\$1,000'.

(c) CONFORMING AND CLERICAL AMENDMENTS-

(1) Section 931(d) is amended to read as follows:

`(d) EMPLOYEES OF THE UNITED STATES- Amounts paid for services performed as an employee of the United States (or any agency thereof) shall be treated as not described in paragraph (1) or (2) of subsection (a).`.

(2) Section 932 is amended by striking `at the close of the taxable year' and inserting `during the entire taxable year' each place it appears.

(3) Section 934(b)(4) is amended by striking `the Virgin Islands or' each place it appears.

(4) Section 935, as in effect before the effective date of its repeal, is amended--

(A) by striking `for the taxable year who' in subsection (a) and inserting `who, during the entire taxable year',

(B) by inserting `bona fide' before `resident' in subsection (a)(1),

(C) in subsection (b)(1)--

(i) by inserting `(other a bona fide resident of Guam during the entire taxable year)' after `United States' in subparagraph (A), and

(ii) by inserting `bona fide' before `resident' in subparagraph (B), and

(D) in subsection (b)(2) by striking `residence and'.

(5) Section 957(c) is amended--

(A) in paragraph (2)(B) by striking `conduct of an active' and inserting `active conduct of a', and

(B) in the last sentence by striking `derived from sources within a possession, was effectively connected with the conduct of a trade or business within a possession, or'.

(6) The table of sections of subpart D of part III of subchapter N of chapter 1 is amended by adding at the end the following new item:

`Sec. 937. Residence and source rules involving possessions.'

(d) EFFECTIVE DATE-

(1) IN GENERAL- Except as otherwise provided in this subsection, the amendments made by this section shall apply to taxable years ending after the date of the enactment of this Act.

(2) 183-DAY RULE- Section 937(a)(1) of the Internal Revenue Code of 1986 (as added by this section) shall apply to taxable years beginning after the date of the enactment of this Act.

(3) SOURCING- Section 937(b)(2) of such Code (as so added) shall apply to income earned after the date of the enactment of this Act.

**SEC. 909. SALES OR DISPOSITIONS TO IMPLEMENT FEDERAL ENERGY REGULATORY COMMISSION OR STATE ELECTRIC RESTRUCTURING POLICY.**

(a) IN GENERAL- Section 451 (relating to general rule for taxable year of inclusion) is amended by adding at the end the following new subsection:

`(i) SPECIAL RULE FOR SALES OR DISPOSITIONS TO IMPLEMENT FEDERAL ENERGY REGULATORY COMMISSION OR STATE ELECTRIC RESTRUCTURING POLICY-

- ``(1) IN GENERAL- In the case of any qualifying electric transmission transaction for which the taxpayer elects the application of this section, qualified gain from such transaction shall be recognized--
  - ``(A) in the taxable year which includes the date of such transaction to the extent the amount realized from such transaction exceeds--
    - ``(i) the cost of exempt utility property which is purchased by the taxpayer during the 4-year period beginning on such date, reduced (but not below zero) by
    - ``(ii) any portion of such cost previously taken into account under this subsection, and
  - ``(B) ratably over the 8-taxable year period beginning with the taxable year which includes the date of such transaction, in the case of any such gain not recognized under subparagraph (A).
- ``(2) QUALIFIED GAIN- For purposes of this subsection, the term `qualified gain' means, with respect to any qualifying electric transmission transaction in any taxable year--
  - ``(A) any ordinary income derived from such transaction which would be required to be recognized under section 1245 or 1250 for such taxable year (determined without regard to this subsection), and
  - ``(B) any income derived from such transaction in excess of the amount described in subparagraph (A) which is required to be included in gross income for such taxable year (determined without regard to this subsection).
- ``(3) QUALIFYING ELECTRIC TRANSMISSION TRANSACTION- For purposes of this subsection, the term `qualifying electric transmission transaction' means any sale or other disposition before January 1, 2007, of--
  - ``(A) property used in the trade or business of providing electric transmission services, or
  - ``(B) any stock or partnership interest in a corporation or partnership, as the case may be, whose principal trade or business consists of providing electric transmission services, but only if such sale or disposition is to an independent transmission company.
- ``(4) INDEPENDENT TRANSMISSION COMPANY- For purposes of this subsection, the term `independent transmission company' means--
  - ``(A) an independent transmission provider approved by the Federal Energy Regulatory Commission,
  - ``(B) a person--
    - ``(i) who the Federal Energy Regulatory Commission determines in its authorization of the transaction under section 203 of the Federal Power Act (16 U.S.C. 824b) or by declaratory order is not a market participant within the meaning of such Commission's rules applicable to independent transmission providers, and
    - ``(ii) whose transmission facilities to which the election under this subsection applies are under the operational control of a Federal Energy Regulatory Commission-approved independent transmission provider before the close of the period specified in such authorization, but not later than the close of the period applicable under subsection (a)(2)(B) as extended under paragraph (2), or
  - ``(C) in the case of facilities subject to the jurisdiction of the Public Utility Commission of Texas--
    - ``(i) a person which is approved by that Commission as consistent with Texas State law regarding an independent transmission provider, or

- ``(ii) a political subdivision or affiliate thereof whose transmission facilities are under the operational control of a person described in clause (i).
- ``(5) EXEMPT UTILITY PROPERTY- For purposes of this subsection:
  - ``(A) IN GENERAL- The term `exempt utility property' means property used in the trade or business of-
    - ``(i) generating, transmitting, distributing, or selling electricity, or
    - ``(ii) producing, transmitting, distributing, or selling natural gas.
  - ``(B) NONRECOGNITION OF GAIN BY REASON OF ACQUISITION OF STOCK- Acquisition of control of a corporation shall be taken into account under this subsection with respect to a qualifying electric transmission transaction only if the principal trade or business of such corporation is a trade or business referred to in subparagraph (A).
- ``(6) SPECIAL RULE FOR CONSOLIDATED GROUPS- In the case of a corporation which is a member of an affiliated group filing a consolidated return, any exempt utility property purchased by another member of such group shall be treated as purchased by such corporation for purposes of applying paragraph (1)(A).
- ``(7) TIME FOR ASSESSMENT OF DEFICIENCIES- If the taxpayer has made the election under paragraph (1) and any gain is recognized by such taxpayer as provided in paragraph (1)(B), then-
  - ``(A) the statutory period for the assessment of any deficiency, for any taxable year in which any part of the gain on the transaction is realized, attributable to such gain shall not expire prior to the expiration of 3 years from the date the Secretary is notified by the taxpayer (in such manner as the Secretary may by regulations prescribe) of the purchase of exempt utility property or of an intention not to purchase such property, and
  - ``(B) such deficiency may be assessed before the expiration of such 3-year period notwithstanding any law or rule of law which would otherwise prevent such assessment.
- ``(8) PURCHASE- For purposes of this subsection, the taxpayer shall be considered to have purchased any property if the unadjusted basis of such property is its cost within the meaning of section 1012.
- ``(9) ELECTION- An election under paragraph (1) shall be made at such time and in such manner as the Secretary may require and, once made, shall be irrevocable.
- ``(10) NONAPPLICATION OF INSTALLMENT SALES TREATMENT- Section 453 shall not apply to any qualifying electric transmission transaction with respect to which an election to apply this subsection is made.'
- (b) EFFECTIVE DATE- The amendments made by this section shall apply to transactions occurring after the date of the enactment of this Act, in taxable years ending after such date.

## **SEC. 910. EXPANSION OF LIMITATION ON DEPRECIATION OF CERTAIN PASSENGER AUTOMOBILES.**

- (a) IN GENERAL- Section 179(b) (relating to limitations) is amended by adding at the end the following new paragraph:
  - ``(6) LIMITATION ON COST TAKEN INTO ACCOUNT FOR CERTAIN PASSENGER VEHICLES-
    - ``(A) IN GENERAL- The cost of any sport utility vehicle for any taxable year which may be taken into account under this section shall not exceed \$25,000.

``(B) SPORT UTILITY VEHICLE- For purposes of subparagraph (A)--

``(i) IN GENERAL- The term `sport utility vehicle' means any 4-wheeled vehicle--

``(I) which is primarily designed or which can be used to carry passengers over public streets, roads, or highways (except any vehicle operated exclusively on a rail or rails),

``(II) which is not subject to section 280F, and

``(III) which is rated at not more than 14,000 pounds gross vehicle weight.

``(ii) CERTAIN VEHICLES EXCLUDED- Such term does not include any vehicle which--

``(I) is designed to have a seating capacity of more than 9 persons behind the driver's seat,

``(II) is equipped with a cargo area of at least 6 feet in interior length which is an open area or is designed for use as an open area but is enclosed by a cap and is not readily accessible directly from the passenger compartment, or

``(III) has an integral enclosure, fully enclosing the driver compartment and load carrying device, does not have seating rearward of the driver's seat, and has no body section protruding more than 30 inches ahead of the leading edge of the windshield.'

(b) EFFECTIVE DATE- The amendment made by this section shall apply to property placed in service after the date of the enactment of this Act.

Speaker of the House of Representatives.

Vice President of the United States and

President of the Senate.

*END*