108TH CONGRESS
2D SESSION

H. R. 4520

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.

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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.
Sec. 102. Reduced corporate income tax rate for domestic production activities income.
Sec. 103. Reduced corporate income tax rate for small corporations.

TITLE II—JOB CREATION TAX INCENTIVES FOR MANUFACTURERS, SMALL BUSINESSES, AND FARMERS

Subtitle A—Small Business Expensing

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Sec. 212. Modification of depreciation allowance for aircraft.
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Sec. 226. Use of passive activity loss and at-risk amounts by qualified subchapter S trust income beneficiaries.
Sec. 227. Exclusion of investment securities income from passive income test for bank S corporations.
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Subtitle E—Restructuring of Incentives for Alcohol Fuels, Etc.

Sec. 251. Reduced rates of tax on gasohol replaced with excise tax credit; repeal of other alcohol-based fuel incentives; etc.
Sec. 252. Alcohol fuel subsidies borne by general fund.

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Sec. 261. Exclusion of incentive stock options and employee stock purchase plan stock options from wages.

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Sec. 271. Incentives to reinvest foreign earnings in United States.

Subtitle H—Other Incentive Provisions

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Sec. 282. Payment of dividends on stock of cooperatives without reducing patronage dividends.
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Sec. 284. Distributions from publicly traded partnerships treated as qualifying income of regulated investment companies.
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Sec. 286. Treatment of certain dividends of regulated investment companies.
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Sec. 289. Simplification of excise tax imposed on bows and arrows.
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Sec. 291. Sonar devices suitable for finding fish.
Sec. 292. Income tax credit to distilled spirits wholesalers for cost of carrying Federal excise taxes on bottled distilled spirits.
Sec. 293. Suspension of occupational taxes relating to distilled spirits, wine, and beer.
Sec. 294. Modification of unrelated business income limitation on investment in certain small business investment companies.

Sec. 295. Election to determine taxable income from certain international shipping activities using per ton rate.
Sec. 296. Charitable contribution deduction for certain expenses incurred in support of Native Alaskan subsistence whaling.

TITLE III—TAX REFORM AND SIMPLIFICATION FOR UNITED STATES BUSINESSES

Sec. 301. Interest expense allocation rules.
Sec. 302. Recharacterization of overall domestic loss.
Sec. 303. Reduction to 2 foreign tax credit baskets.
Sec. 304. Look-thru rules to apply to dividends from noncontrolled section 902 corporations.
Sec. 305. Attribution of stock ownership through partnerships to apply in determining section 902 and 960 credits.
Sec. 306. Clarification of treatment of certain transfers of intangible property.
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Sec. 712. Termination of tobacco price support program and related provisions.
Sec. 713. Continuation of liability and no net loss assessments to prevent losses on price support loans.

Subtitle B—Transitional Payments to Tobacco Quota Holders and Active Producers of Tobacco

Sec. 721. Definitions of active tobacco producer and quota holder.
Sec. 722. Payments to tobacco quota holders.
Sec. 723. Transition payments for active producers of quota tobacco.
Sec. 724. Resolution of disputes.
Sec. 725. Source of funds for payments.

TITLE VIII—TRADE PROVISIONS

Sec. 801. Ceiling fans.
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TITLE I—END SANCTIONS AND REDUCE CORPORATE TAX RATES FOR DOMESTIC MANUFACTURING AND SMALL CORPORATIONS

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.—Except as provided in subsection (d), 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 includible 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 January 14, 2002, 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. REDUCED CORPORATE INCOME TAX RATE FOR DOMESTIC PRODUCTION ACTIVITIES INCOME.

(a) LIMITATION ON TAX ON QUALIFIED PRODUCTION ACTIVITIES INCOME.—Section 11 is amended by redesignating subsections (c) and (d) as subsections (d) and (e), respectively, and by inserting after subsection (b) the following new subsection:

"(c) LIMITATION ON TAX ON QUALIFIED PRODUCTION ACTIVITIES INCOME.—

"(1) IN GENERAL.—If a corporation has qualified production activities income for any taxable year, the tax imposed by this section shall not exceed the sum of—

"(A) a tax computed at the rates and in the manner as if this subsection had not been enacted on the taxable income reduced by the amount of qualified production activities income, plus

"(B) a tax equal to 32 percent (34 percent in the case of taxable years beginning before January 1, 2007) of the qualified production activities income (or, if less, taxable income).

"(2) QUALIFIED PRODUCTION ACTIVITIES INCOME.—

"(A) IN GENERAL.—The term 'qualified production activities income' for any taxable year means an amount equal to the excess (if any) of—

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

"(ii) 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.

"(B) 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) DOMESTIC PRODUCTION GROSS RECEIPTS.—For purposes of this subsection, the term 'domestic production gross receipts' means the gross receipts of the taxpayer which are derived from—

"(A) any lease, rental, license, sale, exchange, or other disposition of—

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

"(ii) any qualified film produced by the taxpayer, or

"(B) construction, engineering, or architectural services performed in the United States for construction projects in the United States.

"(4) QUALIFYING PRODUCTION PROPERTY.—For purposes of this subsection, the term 'qualifying production property' means—

"(A) tangible personal property,

"(B) any computer software, and

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

"(5) QUALIFIED FILM.—For purposes of this subsection—

"(A) IN GENERAL.—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.

"(B) EXCEPTION.—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.

"(6) RELATED PERSONS.—For purposes of this subsection—

"(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).".

(b) SPECIAL RULE RELATING TO ELECTION TO TREAT CUTTING OF TIMBER AS A SALE OR EXCHANGE.—In the case of a corporation, 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.

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

SEC. 103. REDUCED CORPORATE INCOME TAX RATE FOR SMALL CORPORATIONS.

(a) IN GENERAL.—Subsection (b) of section 11 (relating to tax imposed on corporations) is amended by redesignating paragraph (2) as paragraph (6) and by striking paragraph (1) and inserting the following new paragraphs:

"(1) FOR TAXABLE YEARS BEGINNING AFTER 2012.—In the case of taxable years beginning after 2012, the amount of the tax imposed by subsection (a) shall be determined in accordance with the following table:

"If taxable income is:	**The tax is:**
Not over $50,000	15% of taxable income.
Over $50,000 but not over $75,000.	$7,500, plus 25% of the excess over $50,000.
Over $75,000 but not over $20,000,000.	$13,750, plus 32% of the excess over $75,000.
Over $20,000,000	$6,389,750, plus 35% of the excess over $20,000,000.

"(2) FOR TAXABLE YEARS BEGINNING IN 2011 OR 2012.—In the case of taxable years beginning in 2011 or 2012, the amount of the tax imposed by subsection (a) shall be determined in accordance with the following table:

"If taxable income is:	**The tax is:**
Not over $50,000	15% of taxable income.

"If taxable income is:	The tax is:
Over $50,000 but not over $75,000.	$7,500, plus 25% of the excess over $50,000.
Over $75,000 but not over $5,000,000.	$13,750, plus 32% of the excess over $75,000.
Over $5,000,000 but not over $10,000,000.	$1,589,750, plus 34% of the excess over $5,000,000.
Over $10,000,000	$3,289,750, plus 35% of the excess over $10,000,000.

"(3) FOR TAXABLE YEARS BEGINNING IN 2008, 2009, OR 2010.—In the case of taxable years beginning in 2008, 2009, or 2010, the amount of the tax imposed by subsection (a) shall be determined in accordance with the following table:

"If taxable income is:	The tax is:
Not over $50,000	15% of taxable income.
Over $50,000 but not over $75,000.	$7,500, plus 25% of the excess over $50,000.
Over $75,000 but not over $1,000,000.	$13,750, plus 32% of the excess over $75,000.
Over $1,000,000 but not over $10,000,000.	$309,750, plus 34% of the excess over $1,000,000.
Over $10,000,000	$3,369,750, plus 35% of the excess over $10,000,000.

"(4) FOR TAXABLE YEARS BEGINNING IN 2005, 2006, OR 2007.—In the case of taxable years beginning in 2005, 2006, or 2007, the amount of the tax imposed by subsection (a) shall be determined in accordance with the following table:

"If taxable income is:	The tax is:
Not over $50,000	15% of taxable income.
Over $50,000 but not over $75,000.	$7,500, plus 25% of the excess over $50,000.
Over $75,000 but not over $1,000,000.	$13,750, plus 33% of the excess over $75,000.
Over $1,000,000 but not over $10,000,000.	$319,000, plus 34% of the excess over $1,000,000.
Over $10,000,000	$3,379,000, plus 35% of the excess over $10,000,000.

"(5) PHASEOUT OF LOWER RATES FOR CERTAIN TAXPAYERS.—

"(A) GENERAL RULE FOR YEARS BEFORE 2013.—

"(i) IN GENERAL.—In the case of taxable years beginning before 2013 with respect to a corporation which has taxable income in excess of the applicable amount for any taxable year, the amount of tax determined under paragraph (1), (2), (3) or (4) for such taxable year shall be increased by the lesser of (I) 5 percent of such excess, or (II) the maximum increase amount.

"(ii) MAXIMUM INCREASE AMOUNT.—For purposes of clause (i)—

"In the case of any taxable year beginning during:	The applicable amount is:	The maximum increase amount is:
2005, 2006, or 2007	$1,000,000	$21,000
2008, 2009, or 2010	$1,000,000	$30,250
2011 or 2012	$5,000,000	$110,250.

"(B) HIGHER INCOME CORPORATIONS.—In the case of a corporation which has taxable income in excess of $20,000,000 ($15,000,000 in the case of taxable years beginning before 2013), the amount of the tax determined under the foregoing provisions of this subsection shall

be increased by an additional amount equal to the lesser of (i) 3 percent of such excess, or (ii) $610,250 ($100,000 in the case of taxable years beginning before 2013).''.

(b) CONFORMING AMENDMENTS.—

(1) Section 904(b)(3)(D)(ii) is amended to read as follows:

''(ii) in the case of a corporation, section 1201(a) applies to such taxable year.''.

(2) Section 1201(a) is amended by striking ''the last 2 sentences of section 11(b)(1)'' and inserting ''section 11(b)(5)''.

(3) Section 1561(a) is amended—

(A) by striking ''the last 2 sentences of section 11(b)(1)'' and inserting ''section 11(b)(5)'', and

(B) by striking ''such last 2 sentences'' and inserting ''section 11(b)(5)''.

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

TITLE II—JOB CREATION TAX INCENTIVES FOR MANUFACTURERS, SMALL BUSINESSES, AND FARMERS

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.

SEC. 212. 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. 213. MODIFICATION OF PLACED IN SERVICE RULE FOR BONUS DEPRECIATION PROPERTY.

(a) IN GENERAL.—Section 168(k)(2)(D) (relating to special rules) is amended by adding at the end the following new clause:

''(iii) SYNDICATION.—For purposes of subparagraph (A)(ii), if—

"(I) property is originally placed in service after September 10, 2001, by the lessor of such property,

"(II) such property is sold by such lessor or any subsequent purchaser within 3 months after the date so placed in service (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), and

"(III) the user of such property after the last sale during such 3-month period remains the same as when such property was originally placed in service,

such property shall be treated as originally placed in service not earlier than the date of such last sale, so long as no previous owner of such property elects the applica-

tion of this subsection with respect to such property.''.

(b) 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; except that the parenthetical material in section 168(k)(2)(D)(iii)(II) of the Internal Revenue Code of 1986, as added by this section, shall apply to property sold after June 4, 2004.

Subtitle C—S Corporation Reform and Simplification

SEC. 221. 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 3 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 section 229, 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. 222. 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. 223. 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. 224. 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. 225. 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. 226. 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. 227. 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. 228. TREATMENT OF BANK DIRECTOR SHARES.

(a) IN GENERAL.—Section 1361 (defining S corporation) is amended by adding at the end the following new subsection:

"(f) RESTRICTED BANK DIRECTOR STOCK.—

"(1) IN GENERAL.—Restricted bank director stock shall not be taken into account as outstanding stock of the S corporation in applying this subchapter (other than section 1368(f)).

"(2) RESTRICTED BANK DIRECTOR STOCK.—For purposes of this subsection, the term 'restricted bank director stock' means stock in 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), registered with the Federal Reserve System, if such stock—

"(A) is required to be held by an individual under applicable Federal or State law in order to permit such individual to serve as a director, and

"(B) is subject to an agreement with such bank or company (or a corporation which controls (within the meaning of section 368(c)) such bank or company) pursuant to which the holder is required to sell back such stock (at the same price as the individual acquired such stock) upon ceasing to hold the office of director.

"(3) CROSS REFERENCE.—

"For treatment of certain distributions with respect to restricted bank director stock, see section 1368(f).".

(b) DISTRIBUTIONS.—Section 1368 (relating to distributions) is amended by adding at the end the following new subsection:

"(f) RESTRICTED BANK DIRECTOR STOCK.—If a director receives a distribution (not in part or full payment in exchange for stock) from an S corporation with respect to any restricted bank director stock (as defined in section 1361(f)), the amount of such distribution—

"(1) shall be includible in gross income of the director, and

"(2) shall be deductible by the corporation for the taxable year of such corporation in which or with which ends the taxable year in which such amount in included in the gross income of the director.".

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

SEC. 229. 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 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, 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 taxable years beginning after December 31, 2004.

SEC. 230. 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. 231. 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, 2004.

Subtitle D—Alternative Minimum Tax Relief

SEC. 241. 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. 242. EXPANSION OF EXEMPTION FROM ALTERNATIVE MINIMUM TAX FOR SMALL CORPORATIONS.

(a) IN GENERAL.—Subparagraphs (A) and (B) of section 55(e)(1) are each amended by striking ''$7,500,000'' each place it appears and inserting ''$20,000,000''.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 2005.

SEC. 243. INCOME AVERAGING FOR FARMERS NOT TO INCREASE ALTERNATIVE MINIMUM TAX.

(a) IN GENERAL.—Subsection (c) of section 55 (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.—Solely for purposes of this section, section 1301 (relating to averaging of farm income) shall not apply in computing the regular tax liability.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 2003.

Subtitle E—Restructuring of Incentives for Alcohol Fuels, Etc.

SEC. 251. REDUCED RATES OF TAX ON GASOHOL REPLACED WITH EXCISE TAX CREDIT; REPEAL OF OTHER ALCOHOL-BASED FUEL INCENTIVES; ETC.

(a) EXCISE TAX CREDIT FOR ALCOHOL FUEL MIXTURES.—

(1) IN GENERAL.—Subsection (f) of section 6427 is amended to read as follows:

"(f) ALCOHOL FUEL MIXTURES.—

"(1) IN GENERAL.—The amount of credit which would (but for section 40(c)) be determined under section 40(a)(1) for any period—

"(A) shall, with respect to taxable events occurring during such period, be treated—

"(i) as a payment of the taxpayer's liability for tax imposed by section 4081, and

"(ii) as received at the time of the taxable event, and

"(B) to the extent such amount of credit exceeds such liability for such period, shall (except as provided in subsection (k)) be paid subject to subsection (i)(3) by the Secretary without interest.

"(2) SPECIAL RULES.—

"(A) ONLY CERTAIN ALCOHOL TAKEN INTO ACCOUNT.—For purposes of paragraph (1), section 40 shall be applied—

"(i) by not taking into account alcohol with a proof of less than 190, and

"(ii) by treating as alcohol the alcohol gallon equivalent of ethyl tertiary butyl ether or other ethers produced from such alcohol.

"(B) TREATMENT OF REFINERS.—For purposes of paragraph (1), in the case of a mixture—

"(i) the alcohol in which is described in subparagraph (A)(ii), and

"(ii) which is produced by any person at a refinery prior to any taxable event,

section 40 shall be applied by treating such person as having sold such mixture at the time of its removal from the refinery (and only at such time) to another person for use as a fuel.

"(3) MIXTURES NOT USED AS FUEL.—Rules similar to the rules of subparagraphs (A) and (D) of section 40(d)(3) shall apply for purposes of this subsection.

"(4) TERMINATION.—This section shall apply only to periods to which section 40 applies, determined by substituting in section 40(e)—

"(A) 'December 31, 2010' for 'December 31, 2007', and

"(B) 'January 1, 2011' for 'January 1, 2008'."

(2) REVISION OF RULES FOR PAYMENT OF CREDIT.—Paragraph (3) of section 6427(i) is amended to read as follows:

"(3) SPECIAL RULE FOR ALCOHOL MIXTURE CREDIT.—

"(A) IN GENERAL.—A claim may be filed under subsection (f)(1)(B) by any person for any period—

"(i) for which $200 or more is payable under such subsection (f)(1)(B), and

"(ii) which is not less than 1 week.

In the case of an electronic claim, this subparagraph shall be applied without regard to clause (i).

"(B) PAYMENT OF CLAIM.—Notwithstanding subsection (f)(1)(B), if the Secretary has not paid pursuant to a claim filed under this section within 45 days of the date of the filing of such claim (20 days in the case of an electronic claim), the claim shall be paid with interest from such date determined by using the overpayment rate and method under section 6621.

"(C) TIME FOR FILING CLAIM.—No claim filed under this paragraph shall be allowed unless filed on or before the last day of the first quarter following the earliest quarter included in the claim."

(b) REPEAL OF OTHER INCENTIVES FOR FUEL MIXTURES.—

(1) Subsection (b) of section 4041 is amended to read as follows:

"(b) EXEMPTION FOR OFF-HIGHWAY BUSINESS USE.—

"(1) IN GENERAL.—No tax shall be imposed by subsection (a) or (d)(1) on liquids sold for use or used in an off-highway business use.

"(2) TAX WHERE OTHER USE.—If a liquid on which no tax was imposed by reason of paragraph (1) is used otherwise than in an off-highway business use, a tax shall be imposed by paragraph (1)(B), (2)(B), or (3)(A)(ii) of subsection (a) (whichever is appropriate) and by the corresponding provision of subsection (d)(1) (if any).

"(3) OFF-HIGHWAY BUSINESS USE DEFINED.—For purposes of this subsection, the term 'off-highway business use' has the meaning given to such term by section 6421(e)(2); except that such term shall not, for purposes of subsection (a)(1), include use in a diesel-powered train."

(2) Section 4041(k) is hereby repealed.

(3) Section 4081(c) is hereby repealed.

(4) Section 4091(c) is hereby repealed.

(c) TRANSFERS TO HIGHWAY TRUST FUND.—

(1) Paragraph (4) of section 9503(b) is amended by adding ''or'' at the end of subparagraph (C), by striking the comma at the end of subparagraph (D) and inserting a period, and by striking subparagraphs (E) and (F).

(2) Paragraph (4) of section 9503(b), as amended by paragraph (1), is further amended by adding ''or'' at the end of subparagraph (B), by striking the comma at the end of subparagraph (C) and inserting a period, and by striking subparagraph (D).

(d) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 40 is amended to read as follows:

''(c) COORDINATION WITH EXCISE TAX BENEFITS.—The amount of the credit determined under this section with respect to any alcohol shall, under regulations prescribed by the Secretary, be properly reduced to take into account the benefit provided with respect to such alcohol under section 6427(f).''

(2) Subparagraph (B) of section 40(d)(4) is amended by striking ''under section 4041(k) or 4081(c)'' and inserting ''under section 6427(f)''.

(e) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided by paragraph (2), the amendments made by this section shall apply to fuel sold or used after September 30, 2004.

(2) SUBSECTION (c).—

(A) The amendments made by subsection (c)(1) shall apply to taxes imposed after September 30, 2003.

(B) The amendments made by subsection (c)(2) shall apply to taxes imposed after September 30, 2006.

SEC. 252. ALCOHOL FUEL SUBSIDIES BORNE BY GENERAL FUND.

(a) TRANSFERS TO FUND.—Section 9503(b)(1) is amended by adding at the end the following new flush sentence:

''For purposes of this paragraph, the amount of taxes received under section 4081 shall include any amount treated as a payment under section 6427(f)(1)(A) and shall not be reduced by the amount paid under section 6427(f)(1)(B).''.

(b) TRANSFERS FROM FUND.—Subparagraph (A) of section 9503(c)(2) is amended by adding at the end the following new sentence: ''Clauses (i)(III) and (ii) shall not apply to claims under section 6427(f)(1)(B).''

(c) EFFECTIVE DATE.—

(1) SUBSECTION (a).—The amendment made by subsection (a) shall apply to taxes received after September 30, 2004.

(2) SUBSECTION (b).—The amendment made by subsection (b) shall apply to amounts paid after September 30, 2004, and (to the extent related to section 34 of the Internal Revenue Code of 1986) to fuel used after such date.

Subtitle F—Stock Options and Employee Stock Purchase Plan Stock Options

SEC. 261. 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.

Subtitle G—Incentives to Reinvest Foreign Earnings in United States

SEC. 271. 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 cor-

porations) 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, there shall be allowed as a deduction an amount equal to 85 percent of the dividends which are received by such shareholder from controlled foreign corporations during the election period.

"(2) DIVIDENDS PAID INDIRECTLY FROM CONTROLLED FOREIGN CORPORATIONS.—If, within the election period, a United States shareholder receives a 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 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 dividend paid during the election period 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 distributions described in section 959(b) which are made during the election period 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 of such earnings determined in such manner as the Secretary may prescribe.

Except as provided in subparagraph (C), if there is no statement or such statement fails to show a spe-

cific amount of such earnings or liability, such amount shall be treated as being zero for purposes of this paragraph.

"(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 such corporations,

"(ii) the amounts includible in such shareholder's gross income for each base period year under section 951(a)(1)(B) with respect to such corporations, and

"(iii) the amounts that would have been included for each base period year but for section 959(a) with respect to such corporations.

The amount taken into account under clause (iii) for any base period year shall not include

any amount which is not includible in gross income by reason of an amount described in clause (ii) with respect to a prior taxable year.

"(3) 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 plan describing the expenditures to be made with such amount—

"(A) which, before the dividend is received, is approved by the president or chief executive officer of such shareholder, and

"(B) which is approved by the Board of Directors (or management committee) of such shareholder no later than its first meeting on or after the date the dividend is received.

"(c) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) ELECTION PERIOD.—The term 'election period' means—

"(A) if this section applies to the taxpayer's last taxable year beginning before the date of the enactment of this section, any 6-month or shorter period during such year which

is after the date of the enactment of this section and which is selected by the taxpayer, and

"(B) if this section applies to the taxpayer's first taxable year beginning on or after such date, the 1st 6 months of such taxable year.

"(2) APPLICABLE FINANCIAL STATEMENT.—The term 'applicable financial statement' means the most recently audited financial statement (including notes and other documents which accompany such statement)—

"(A) which is certified on or before March 31, 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 March 31, 2003.

"(3) BASE PERIOD YEARS.—The base period years are the 3 taxable years—

"(A) which are among the 5 most recent taxable years ending on or before March 31, 2003, and

"(B) 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.

Rules similar to the rules of subparagraphs (A) and (B) of section 41(f)(3) shall apply for purposes of this paragraph.

"(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.

"(d) DENIAL OF FOREIGN TAX CREDIT.—

"(1) IN GENERAL.—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 any dividend or of any amount

described in subsection (a)(2). No deduction shall be allowed under this chapter for any tax for which credit is not allowable by reason of the preceding sentence.

"(2) DEDUCTIBLE PORTION.—For purposes of paragraph (1), unless the taxpayer otherwise specifies, the deductible portion of any dividend is the amount which bears the same ratio to the amount of such dividend 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) INCLUSIONS MAY NOT BE OFFSET BY NET OPERATING LOSSES.—

"(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.—This section shall apply for the taxpayer's first taxable year beginning on or after the date of the enactment of this section if the taxpayer elects its

application for such taxable year. The taxpayer may elect to apply this section to the taxpayer's last taxable year beginning before the date of the enactment of this section in lieu of such first taxable year.''

(b) ALTERNATIVE MINIMUM TAX.—Subparagraph (C) of section 56(g)(4) is amended by adding at the end the following new clause:

''(v) 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.

Subtitle H—Other Incentive Provisions

SEC. 281. SPECIAL RULES FOR LIVESTOCK SOLD ON ACCOUNT OF WEATHER-RELATED CONDITIONS.

(a) RULES FOR REPLACEMENT 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.''.

(b) INCOME INCLUSION RULES.—Subsection (e) of section 451 (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.".

(c) 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. 282. 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. 283. 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. 284. DISTRIBUTIONS 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) distributions or other 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 part-

nership 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. 285. 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 matu-

rity which does not exceed the greater of ¼ 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 trans-

actions) 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 accord-

ance 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. 286. 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, an interest-related dividend is 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.

"(D) QUALIFIED NET INTEREST INCOME.—For purposes of subparagraph (C), the term 'qualified net interest income' means the qualified interest income of the regulated in-

vestment 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 includible 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 includible 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, a short-term capital gain dividend is 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.

"(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 includible 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 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 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."

(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.—The term 'qualified investment entity' means any real estate investment trust and any regulated investment company.

"(B) DOMESTICALLY CONTROLLED.—The term 'domestically controlled qualified investment entity' means any qualified investment entity in which at all times during the testing period less than 50 percent in value of the stock was held directly or indirectly by foreign persons."

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

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

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall apply to dividends with respect to taxable years of regulated investment companies beginning after 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. 287. TAXATION OF CERTAIN SETTLEMENT FUNDS.

(a) IN GENERAL.—Subsection (g) of section 468B (relating to clarification of taxation of certain funds) is amended to read as follows:

''(g) CLARIFICATION OF TAXATION OF CERTAIN FUNDS.—

''(1) IN GENERAL.—Except as provided in paragraph (2), nothing in any provision of law shall be construed as providing that an escrow account, set-

tlement fund, or similar fund is not subject to current income tax. The Secretary shall prescribe regulations providing for the taxation of any such account or fund whether as a grantor trust or otherwise.

"(2) EXEMPTION FROM TAX FOR CERTAIN SETTLEMENT FUNDS.—An escrow account, settlement fund, or similar fund shall be treated as beneficially owned by the United States and shall be exempt from taxation under this subtitle if—

"(A) it is established pursuant to a consent decree entered by a judge of a United States District Court,

"(B) it is created for the receipt of settlement payments as directed by a government entity for the sole purpose of resolving or satisfying one or more claims asserting liability under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980,

"(C) the authority and control over the expenditure of funds therein (including the expenditure of contributions thereto and any net earnings thereon) is with such government entity, and

"(D) upon termination, any remaining funds will be disbursed to such government entity for use in accordance with applicable law. For purposes of this paragraph, the term 'government entity' means the United States, any State or political subdivision thereof, the District of Columbia, any possession of the United States, and any agency or instrumentality of any of the foregoing.".

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

SEC. 288. EXPANSION OF HUMAN CLINICAL TRIALS QUALIFYING FOR ORPHAN DRUG CREDIT.

(a) IN GENERAL.—Paragraph (2) of section 45C(b) (relating to qualified clinical testing expenses) is amended by adding at the end the following new subparagraph:

"(C) TREATMENT OF CERTAIN EXPENSES INCURRED BEFORE DESIGNATION.—For purposes of subparagraph (A)(ii)(I), if a drug is designated under section 526 of the Federal Food, Drug, and Cosmetic Act not later than the due date (including extensions) for filing the return of tax under this subtitle for the taxable year in which the application for such designation of such drug was filed, such drug shall

be treated as having been designated on the date that such application was filed.''.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to expenses incurred after the date of the enactment of this Act.

SEC. 289. 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 December 31, 2004.

SEC. 290. REPEAL OF EXCISE TAX ON FISHING TACKLE BOXES.

(a) REPEAL.—Paragraph (6) of section 4162(a) (defining sport fishing equipment) is amended by striking subparagraph (C) and by redesignating subparagraphs (D) through (J) as subparagraphs (C) through (I), respectively.

(b) EFFECTIVE DATE.—The amendments made this section shall apply to articles sold by the manufacturer, producer, or importer after December 31, 2004.

SEC. 291. 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. 292. INCOME TAX CREDIT TO DISTILLED SPIRITS WHOLESALERS FOR COST OF CARRYING FEDERAL EXCISE TAXES ON BOTTLED DISTILLED SPIRITS.

(a) IN GENERAL.—Subpart A of part I of subchapter A of chapter 51 (relating to gallonage and occupational taxes) is amended by adding at the end the following new section:

''SEC. 5011. INCOME TAX CREDIT FOR WHOLESALER'S AVERAGE COST OF CARRYING EXCISE TAX.

''(a) IN GENERAL.—For purposes of section 38, in the case of an eligible wholesaler, the amount of the dis-

tilled spirits wholesalers credit for any taxable year is the amount equal to the product of—

"(1) the number of cases of bottled distilled spirits—

"(A) which were bottled in the United States, and

"(B) which are purchased by such wholesaler during the taxable year directly from the bottler of such spirits, and

"(2) the average tax-financing cost per case for the most recent calendar year ending before the beginning of such taxable year.

"(b) ELIGIBLE WHOLESALER.—For purposes of this section, the term 'eligible wholesaler' means any person who holds a permit under the Federal Alcohol Administration Act as a wholesaler of distilled spirits.

"(c) AVERAGE TAX-FINANCING COST.—

"(1) IN GENERAL.—For purposes of this section, the average tax-financing cost per case for any calendar year is the amount of interest which would accrue at the deemed financing rate during a 60-day period on an amount equal to the deemed Federal excise per case.

"(2) DEEMED FINANCING RATE.—For purposes of paragraph (1), the deemed financing rate for any

calendar year is the average of the corporate overpayment rates under paragraph (1) of section 6621(a) (determined without regard to the last sentence of such paragraph) for calendar quarters of such year.

''(3) DEEMED FEDERAL EXCISE TAX BASED ON CASE.—For purposes of paragraph (1), the deemed Federal excise tax per case of 12 80-proof 750ml bottles is $22.83.

''(4) NUMBER OF CASES IN LOT.—For purposes of this section, the number of cases in any lot of distilled spirits shall be determined by dividing the number of liters in such lot by 9.''

(b) CONFORMING AMENDMENTS.—

(1) Subsection (b) of section 38 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) in the case of an eligible wholesaler (as defined in section 5011(b)), the distilled spirits wholesalers credit determined under section 5011(a).''

(2) Subsection (d) of section 39 (relating to carryback and carryforward of unused credits) is

amended by adding at the end the following new paragraph:

"(11) NO CARRYBACK OF SECTION 5011 CREDIT BEFORE JANUARY 1, 2005.—No portion of the unused business credit for any taxable year which is attributable to the credit determined under section 5011(a) may be carried back to a taxable year beginning before January 1, 2005.".

(3) The table of sections for subpart A of part I of subchapter A of chapter 51 is amended by adding at the end the following new item:

"Sec. 5011. Income tax credit for wholesaler's average cost of carrying excise tax.".

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

SEC. 293. 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, 2004, and ending on June 30, 2007.".

(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. 294. 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 under the Small Business Investment Act of 1958 and formed after the date of the enactment of the American Jobs Creation Act of 2004, 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 by small business investment companies formed after the date of the enactment of the American Jobs Creation Act of 2004.

SEC. 295. ELECTION TO DETERMINE TAXABLE INCOME FROM CERTAIN INTERNATIONAL SHIPPING ACTIVITIES USING PER TON RATE.

(a) IN GENERAL.—Chapter 1 of the Internal Revenue Code of 1986 is amended by inserting after subchapter Q the following new subchapter:

"Subchapter R—Election To Determine Taxable Income From Certain International Shipping Activities Using per Ton Rate

"Sec. 1352. Alternative tax on qualifying shipping activities.
"Sec. 1353. Taxable income from qualifying shipping activities.
"Sec. 1354. Qualifying shipping 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 shipping assets.

"SEC. 1352. ALTERNATIVE TAX ON QUALIFYING SHIPPING ACTIVITIES.

"(a) IN GENERAL.—The taxable income of an electing corporation from qualifying shipping activities shall be the amount determined under this subchapter, and the corporate percentages of the items of income, gain, loss, deduction, or credit of an electing corporation and of other members of the electing group of such corporation which would otherwise be taken into account by reason of its qualifying shipping activities shall be taken into account to the extent provided in section 1357.

"(b) ALTERNATIVE TAX.—The taxable income of an electing corporation from qualifying shipping activities, if otherwise taxable under section 11, 55, 882, 887, or 1201(a) shall be subject to tax only under this section at the maximum rate specified in section 11(b). The income of a foreign corporation shall not be subject to tax under this subchapter to the extent its income is excludible from gross income under section 883(a)(1).

"SEC. 1353. TAXABLE INCOME FROM QUALIFYING SHIPPING ACTIVITIES.

"(a) IN GENERAL.—For purposes of this subchapter, the taxable income of an electing corporation from qualifying shipping activities shall be its corporate income percentage of the sum of the amounts determined under subsection (b) for each qualifying vessel operated by such electing corporation or other electing entity.

"(b) AMOUNTS.—For purposes of subsection (a), the amount of taxable income of an electing entity for each qualifying vessel shall equal the product of—

"(1) the daily notional taxable income from the operation of the qualifying vessel in United States foreign trade, and

"(2) the number of days during the taxable year that the electing entity operated such vessel as a qualifying vessel in United States foreign trade.

"(c) DAILY NOTIONAL TAXABLE INCOME.—For purposes of subsection (b), the daily notional taxable income from the operation of a qualifying vessel is 40 cents for each 100 tons of the net tonnage of the vessel, up to 25,000 net tons, and 20 cents for each 100 tons of the net tonnage of the vessel, in excess of 25,000 net tons.

"(d) MULTIPLE OPERATORS OF VESSEL.—If 2 or more persons have a joint interest in a qualifying vessel and are treated as operators of that vessel, the taxable income from the operation of such vessel for that time (as determined under this section) shall be allocated among such persons on the basis of their ownership and charter interests in such vessel or on such other basis as the Secretary may prescribe by regulations.

"(e) NONCORPORATE PERCENTAGE.—Notwithstanding any contrary provision of this subchapter, the noncorporate percentage of any item of income, gain, loss, deduction, or credit of any member of an electing group shall be taken into account for all purposes of this subtitle as if this subchapter were not in effect.

"SEC. 1354. QUALIFYING SHIPPING TAX ELECTION; REVOCATION; TERMINATION.

"(a) IN GENERAL.—Except as provided in subsections (b) and (f), a qualifying shipping tax election may be made in respect of any qualifying entity.

"(b) CONDITION OF ELECTION.—An election may be made by a member of a controlled group under this subsection for any taxable year only if all qualifying entities that are members of the controlled group join in the election.

"(c) WHEN MADE.—An election under subsection (a) may be made by a qualifying entity in such form as prescribed by the Secretary. Such election shall be filed with the qualifying entity's return for the first taxable year to which the election shall apply, by the due date for such return (including any applicable extensions).

"(d) YEARS FOR WHICH EFFECTIVE.—An election under subsection (a) shall be effective for the taxable year of the qualifying entity for which it is made and for all succeeding taxable years of the entity, until such election is terminated under subsection (e).

"(e) 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 3rd 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 on and after the date so specified.

"(2) BY ENTITY CEASING TO BE QUALIFYING ENTITY.—

"(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 entity is an electing entity) such entity ceases to be a qualifying entity.

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

"(f) ELECTION AFTER TERMINATION.—If a qualifying entity has made an election under subsection (a) and

if such election has been terminated under subsection (e), such entity (and any successor entity) 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) The term 'controlled group' means any group of trusts and business entities whose members would be treated as a single employer under the rules of section 52(a) (without regard to paragraphs (1) and (2) thereof) and section 52(b)(1).

''(2) The term 'corporate income percentage' means the least aggregate share, expressed as a percentage, of any item of income or gain of an electing corporation or electing group of which such corporation is a member from qualifying shipping activities that would, but for an election in effect under this subchapter, be required to be reported on the Federal income tax return of an electing corporation during any taxable period. In the case of an electing group which includes two or more electing corporations, the corporate income percentage of each such

corporation shall be determined on the basis of such corporations' direct and indirect ownership and charter interests in qualifying vessels of the electing group or on such other basis as the Secretary may prescribe by regulations.

''(3) The term 'corporate loss percentage' means the greatest aggregate share, expressed as a percentage, of any item of loss, deduction or credit of an electing corporation or electing group of which such corporation is a member from qualifying shipping activities that would, but for an election in effect under this subchapter, be required to be reported on the Federal income tax return of an electing corporation during any taxable period.

''(4) The term 'corporate percentages' means the corporate income percentage and the corporate loss percentage.

''(5) The term 'electing corporation' means any C corporation that is an electing entity or that would, but for an election in effect under this subchapter, be required to report any item of income, gain, loss, deduction, or credit of an electing entity on its Federal income tax return.

"(6) The term 'electing entity' means any qualifying entity for which an election is in effect under this subchapter.

"(7) The term 'electing group' means a controlled group of which one or more members is an electing entity.

"(8) The term 'noncorporate percentage' means the difference between one hundred percent and the corporate income percentage or corporate loss percentage, as applicable.

"(9) The term 'qualifying entity' means a trust or business entity that—

"(A) operates one or more qualifying vessels, and

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

"(10) The term 'qualifying shipping assets' means any qualifying vessel and other assets which are used in core qualifying activities as described in section 1356(b).

"(11) 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 in the United States foreign trade.

"(12) The term 'United States domestic trade' means the transportation of goods or passengers between places in the United States.

"(13) The term 'United States flag vessel' means any vessel documented under the laws of the United States.

"(14) 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.

"(b) OPERATING A VESSEL.—For purposes of this subchapter:

"(1) Except as provided in paragraph (2), an entity is treated as operating any vessel owned by, or chartered (including a time charter) to, the entity.

"(2) An entity is treated as operating a vessel that it has chartered out on bareboat charter terms only if—

"(A) the vessel is temporarily surplus to the entity's requirements and the term of the charter does not exceed three years; or

"(B) the vessel is bareboat chartered to a member of a controlled group which includes such entity or to an unrelated third party that

sub-bareboats or time charters the vessel to a member of such controlled group (including the owner).

"(c) SHIPPING ACTIVITY REQUIREMENT.—For purposes of this section, the shipping activity requirement is met for a taxable year only by an entity described in paragraph (1), (2), or (3).

"(1) An entity in the first taxable year of its qualifying shipping tax election if, for the preceding taxable year, the test in paragraph (4) is met.

"(2) An entity in the second or any subsequent taxable year of its qualifying shipping tax election if, for each of the two preceding taxable years, the test in paragraph (4) is met.

"(3) An entity that would be described in paragraph (1) or (2) if the test in paragraph (4) were applied on an aggregate basis to the controlled group of which such entity is a member, and vessel charters between members of the controlled group were disregarded.

"(4) The test in this paragraph is met if on average at least 25 percent of the aggregate tonnage of qualifying vessels operated by the entity were owned by the entity or chartered to the entity on bareboat charter terms. For purposes of the pre-

ceding sentence, vessels chartered (including time chartered) to an entity by a member of a controlled group which includes the entity, or by a third party that bareboat charters the vessels from the entity or a member of the entity's controlled group, shall be treated as chartered to the entity on bareboat charter terms.

"(d) EFFECT OF TEMPORARILY CEASING TO OPERATE A QUALIFYING VESSEL.—

"(1) A temporary cessation by an electing entity in operation of a qualifying vessel shall be disregarded for purposes of subsections (b) and (c) if the electing entity 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 shall be deemed timely if given not later than the due date (including extensions) for the electing entity's tax return (as set forth in section 6072(b)) for the taxable year in which the temporary cessation begins.

"(3) The treatment provided by paragraph (1) shall continue until the earlier of—

"(A) the electing entity abandoning its intention to resume operation of the qualifying vessel, or

"(B) the electing entity resuming operation of the qualifying vessel.

"(e) EFFECT OF TEMPORARILY OPERATING A QUALIFYING VESSEL IN THE UNITED STATES DOMESTIC TRADE.—

"(1) The temporary operation in the United States domestic trade of any qualifying vessel which had been used in the United States foreign trade shall be disregarded for purposes of this subchapter if the electing entity 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 shall be deemed timely if given not later than the due date (including extensions) for the electing entity's tax return (as set forth in section 6072(b)) for the taxable year in which the temporary cessation begins.

"(3) The treatment provided by paragraph (1) shall continue until the earlier of—

"(A) the electing entity abandoning its intention to resume operations of the vessel in the United States foreign trade, or

"(B) the electing entity resuming operation of the vessel in the United States foreign trade.

"(f) EFFECT OF CHANGE IN USE.—

"(1) Except as provided in subsection (e), a vessel that is used other than for operations in the United States foreign trade on other than a temporary basis ceases to be a qualifying vessel when such use begins.

"(2) For purposes of this subsection, a change in use of a vessel, other than a commencement of operation in the United States domestic trade, is taken to be permanent unless there are circumstances indicating that it is temporary.

"(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 'qualifying shipping activities' of an electing entity consist of—

"(1) core qualifying activities,

"(2) qualifying secondary activities, and

"(3) qualifying incidental activities.

"(b) CORE QUALIFYING ACTIVITIES.—

"(1) The 'core qualifying activities' of an electing entity are—

"(A) its activities in operating qualifying vessels in United States foreign trade, and

"(B) other activities of the electing entity 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 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, the inland haulage of cargo shipped, or to be shipped, on qualifying vessels in United States foreign trade, and the provision of terminal, maintenance, repair, logistical, or other vessel, container, or cargo-related services that are an integral part of operating qualifying vessels in United States foreign trade.

"(2) 'Core qualifying activities' do not include the provision by an entity of facilities or services to any person, other than—

"(A) another member of such entity's electing group,

"(B) a consignor, consignee, or other customer of such entity's business of operating qualifying vessels in United States foreign trade, or

"(C) a member of an alliance, joint venture, pool, partnership or similar undertaking involving the operation of qualifying vessels in United States foreign trade of which such entity is a member.

"(c) QUALIFYING SECONDARY ACTIVITIES.—For purposes of this subsection—

"(1) the term 'secondary activities' means activities that are not core qualifying activities, and—

"(A) are the active management or operation of vessels in the United States foreign trade,

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

"(C) such other activities as may be prescribed by the Secretary pursuant to regulations, and

"(2) the 'qualified secondary activities' of an electing entity are its secondary activities and the secondary activities of other members of its electing group, but only to the extent that, without regard to this subchapter, the aggregate gross income derived by the electing entity and the other members of its electing group from such activities does not exceed 20 percent of the aggregate gross income derived by the electing entity and the other members of its electing group from their core qualifying activities.

"(d) QUALIFYING INCIDENTAL ACTIVITIES.—Shipping-related activities carried on by an electing entity or another member of its electing group are qualified incidental activities of the electing entity if—

"(1) incidental to its core qualifying activities,

"(2) not qualifying secondary activities, and

"(3) without regard to this subchapter, the aggregate gross income derived by the electing entity and other members of its electing group from such activities does not exceed 0.1 percent of such entities' aggregate gross income from their core qualifying activities.

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

"(a) EXCLUSION FROM GROSS INCOME.—Gross income of an electing entity shall not include the corporate income percentage of—

"(1) income from qualifying shipping activities in the United States foreign trade,

"(2) income from money, bank deposits and other temporary investments which are reasonably necessary to meet the working capital requirements of qualifying shipping activities, and

"(3) income from money or other intangible assets accumulated pursuant to a plan to purchase qualifying shipping assets.

"(b) ELECTING GROUP MEMBER.—Gross income of a member of an electing group that is not an electing entity shall not include the corporate income percentage of its income from qualifying shipping activities that are taken into account under this subchapter as qualifying shipping activities of an electing entity.

"(c) DENIAL OF LOSSES, DEDUCTIONS, AND CREDITS.—

"(1) GENERAL RULE.—Subject to paragraph (2), the corporate loss percentage of 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.—Notwithstanding paragraph (1), the deduction for depreciation of a qualifying shipping asset shall be allowed in determining the adjusted basis of such asset for purposes of determining gain from its disposition.

"(A) Except as provided in subparagraph (B), the straight line method of depreciation shall apply to the corporate income percentage of qualifying shipping assets the income from operation of which is excluded from gross income under this section.

"(B) Subparagraph (A) shall not apply to any qualifying shipping asset which is subject to a charter entered into prior to the effective date of this subchapter.

"(3) INTEREST.—The corporate loss percentage of an electing entity's interest expense shall be disallowed in the ratio that the fair market value of its qualifying vessel assets bears to the fair market value of its total assets.

"(d) SECTION INAPPLICABLE TO UNRELATED PERSONS.—This section shall not apply to a taxpayer that is not a member of an electing group.

"SEC. 1358. ALLOCATION OF CREDITS, INCOME, AND DEDUCTIONS.

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

"(b) EXCLUSION OF CREDITS OR DEDUCTIONS.—

"(1) No deduction shall be allowed against the taxable income of an electing corporation from qualifying shipping activities, and no credit shall be allowed against the tax imposed by section 1352(b).

"(2) No deduction shall be allowed for any net operating loss attributable to the qualifying shipping activities of a corporation to the extent that such loss is carried forward by the corporation from a taxable year preceding the first taxable year for which such corporation was an electing corporation.

"(c) TRANSACTIONS NOT AT ARM'S LENGTH.—Section 482 shall apply in accordance with this subsection to a transaction or series of transactions—

"(1) as between an electing entity and another person, or

"(2) as between an entity's qualifying shipping activities and other activities carried on by it.

"SEC. 1359. DISPOSITION OF QUALIFYING SHIPPING ASSETS.

"(a) IN GENERAL.—If an electing entity sells or disposes of qualifying shipping assets (as defined in subsection (c)) in an otherwise taxable transaction, at the election of the entity no gain shall be recognized if replacement qualifying shipping assets are 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 shipping assets.

"(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 shipping assets 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) TIME FOR ASSESSMENT OF DEFICIENCY ATTRIBUTABLE TO GAIN.—If an electing entity 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 the entity (in such manner as the Secretary may by regulations prescribe) of the replacement tonnage tax property 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.

"(d) BASIS OF REPLACEMENT QUALIFYING SHIPPING ASSETS.—In the case of replacement qualifying shipping assets purchased by an electing entity which resulted in the nonrecognition of any part of the gain realized as the result of a sale or other disposition of qualifying shipping assets, the basis shall be the cost of such property 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.

"(e) REPLACEMENT QUALIFYING SHIPPING ASSETS MUST BE ACQUIRED FROM UNRELATED PERSON IN CERTAIN CASES.—

"(1) IN GENERAL.—Subsection (a) shall not apply if the replacement qualifying shipping assets are acquired from a related person except to the extent that the related person acquired the replacement qualifying shipping assets from an unrelated person during the period applicable under subsection (b).

"(2) RELATED PERSON.—For purposes of this subsection, a person is related to another person if the person bears a relationship to the other person described in section 267(b) or 707(b)(1).".

(b) TECHNICAL AND CONFORMING AMENDMENT.—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".

(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. 296. 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.".

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to contributions made after December 31, 2004.

TITLE III—TAX REFORM AND SIMPLIFICATION FOR UNITED STATES BUSINESSES

SEC. 301. 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)(C)(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) ANTIABUSE 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. 302. 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. 303. 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 in-

serting 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) 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) 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, 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) 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.—Tax imposed under the law of a foreign country or possession of the United States on an amount which does not constitute income under United States tax principles shall

be treated as imposed on income described in paragraph (1)(B).''

(6) Paragraph (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 to such a taxable year for purposes of allocating such income among the separate categories in effect for such taxable year.''.

(7) Section 904(j)(3)(A)(i) is amended by striking ''subsection (d)(2)(A)'' and inserting ''subsection (d)(2)(B)''.

(f) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2006.

SEC. 304. 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 for-

eign 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 to such a taxable year for purposes of allocating such dividend among the separate categories in effect for such taxable year.".

(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. 305. 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. 306. 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. 307. 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. 308. ELECTION NOT TO USE AVERAGE EXCHANGE RATE FOR FOREIGN TAX PAID OTHER THAN IN FUNCTIONAL CURRENCY.

(a) IN GENERAL.—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) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2004.

SEC. 309. 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. 310. PROVIDE EQUAL TREATMENT FOR 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. 311. LOOK-THRU TREATMENT OF PAYMENTS BETWEEN RELATED CONTROLLED FOREIGN CORPORATIONS UNDER FOREIGN PERSONAL HOLDING COMPANY INCOME RULES.

(a) IN GENERAL.—Subsection (c) of section 954, as amended by this Act, is amended by adding after paragraph (4) the following new paragraph:

''(5) LOOK-THRU IN THE CASE OF RELATED CONTROLLED FOREIGN CORPORATIONS.—For purposes of this subsection, dividends, interest, rents, and royalties received or accrued from a controlled foreign corporation which is a related person (as defined in subsection (b)(9)) shall not be treated as foreign personal holding company income to the extent attributable or properly allocable (determined under rules similar to the rules of subparagraphs (C) and (D) of section 904(d)(3)) to income of the related person which is not subpart F income (as defined in section 952). For purposes of this paragraph, interest shall include factoring income which is treated as income equivalent to interest for purposes of paragraph (1)(E). The Secretary shall prescribe such regulations as may be appropriate to prevent the abuse of the purposes of this paragraph.''.

(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. 312. LOOK-THRU TREATMENT FOR SALES OF PARTNERSHIP INTERESTS.

(a) IN GENERAL.—Section 954(c) (defining foreign personal holding company income), as amended by this Act, is amended by adding after paragraph (5) the following new paragraph:

"(6) 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. 313. 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 des-

ignated (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) Section 163(e)(3)(B), as amended by section 642(a) of this Act, is amended by striking ''which is a foreign personal holding company (as defined in section 552), a controlled foreign corporation (as defined in section 957), or'' and inserting ''which is a controlled foreign corporation (as defined in section 957) or''.

(3) 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".

(4) Paragraph (2) of section 245(a) is amended by striking "foreign personal holding company or".

(5) Section 267(a)(3)(B), as amended by section 642(b) of this Act, is amended by striking "to a foreign personal holding company (as defined in section 552), a controlled foreign corporation (as defined in section 957), or" and inserting "to a controlled foreign corporation (as defined in section 957) or".

(6) Section 312 is amended by striking subsection (j).

(7) 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)".

(8) Subsection (e) of section 443 is amended by striking paragraph (3) and by redesignating paragraphs (4) and (5) as paragraphs (3) and (4), respectively.

(9) 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).

(10) 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).

(11) Paragraph (1) of section 562(b) is amended by striking ''or a foreign personal holding company described in section 552''.

(12) 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)''.

(13) 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)''.

(14) Paragraph (2) of section 864(d) is amended by striking subparagraph (A) and by redesig-

nating subparagraphs (B) and (C) as subparagraphs (A) and (B), respectively.

(15)(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.".

(16) 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 includible in gross income under section 1293 (relating to certain passive foreign investment companies).".

(17)(A) Subparagraph (A) of section 904(h)(1), as redesignated by section 302, 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".

(18) Section 951 is amended by striking subsections (c) and (d) and by redesignating subsections (e) and (f) as subsections (c) and (d), respectively.

(19) Paragraph (3) of section 989(b) is amended by striking ", 551(a),".

(20) Paragraph (5) of section 1014(b) is amended by inserting "and before January 1, 2005," after "August 26, 1937,".

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

(22)(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.

(23) Section 1223 is amended by striking paragraph (10) and by redesignating the following paragraphs accordingly.

(24) Subsection (d) of section 1248 is amended by striking paragraph (5) and by redesignating paragraphs (6) and (7) as paragraphs (5) and (6), respectively.

(25) Paragraph (2) of section 1260(c) is amended by striking subparagraphs (H) and (I) and by redesignating subparagraph (J) as subparagraph (H).

(26)(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''.

(27) 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.''.

(28) Section 6035 is hereby repealed.

(29) 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.

(30) 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.''.

(31) 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).

(32) Sections 170(f)(10)(A), 508(d), 4947, and 4948(c)(4) are each amended by striking ''556(b)(2),'' each place it appears.

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

(34) 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.

(35) 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)(29).—The amendments made by subsection (c)(29) shall apply to disclosures of return or return information with respect to taxable years beginning after December 31, 2004.

SEC. 314. 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 is amended by adding after paragraph (3) the following new paragraph:

"(4) 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. 315. 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. 316. 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.

TITLE IV—EXTENSION OF CERTAIN EXPIRING PROVISIONS

SEC. 401. ALLOWANCE OF NONREFUNDABLE PERSONAL CREDITS AGAINST REGULAR AND MINIMUM TAX LIABILITY.

(a) IN GENERAL.—Paragraph (2) of section 26(a) is amended—

(1) by striking ''RULE FOR 2000, 2001, 2002, AND 2003.—'' and inserting ''RULE FOR TAXABLE YEARS 2000 THROUGH 2005.—'', and

(2) by striking ''or 2003,'' and inserting ''2003, 2004, or 2005,''.

(b) CONFORMING PROVISIONS.—

(1) Section 904(h) is amended by striking ''or 2003'' and inserting ''2003, 2004, or 2005''.

(2) The amendments made by sections 201(b), 202(f), and 618(b) of the Economic Growth and Tax Relief Reconciliation Act of 2001 shall not apply to taxable years beginning during 2004 or 2005.

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

SEC. 402. EXTENSION OF RESEARCH CREDIT.

(a) EXTENSION.—

(1) IN GENERAL.—Section 41(h)(1)(B) (relating to termination) is amended by striking ''June 30, 2004'' and inserting ''December 31, 2005''.

(2) CONFORMING AMENDMENT.—Section 45C(b)(1)(D) is amended by striking ''June 30, 2004'' and inserting ''December 31, 2005''.

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to amounts paid or incurred after June 30, 2004.

SEC. 403. EXTENSION OF CREDIT FOR ELECTRICITY PRODUCED FROM CERTAIN RENEWABLE RESOURCES.

(a) IN GENERAL.—Subparagraphs (A) and (B) of section 45(c)(3) (defining qualified facility) are both amended by striking ''2004'' and inserting ''2006''.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to facilities placed in service after December 31, 2003.

SEC. 404. INDIAN EMPLOYMENT TAX CREDIT.

Section 45A(f) (relating to termination) is amended by striking ''December 31, 2004'' and inserting ''December 31, 2005''.

SEC. 405. WORK OPPORTUNITY CREDIT.

(a) IN GENERAL.—Subparagraph (B) of section 51(c)(4) is amended by striking ''December 31, 2003'' and inserting ''December 31, 2005''.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to individuals who begin work for the employer after December 31, 2003.

SEC. 406. WELFARE-TO-WORK CREDIT.

(a) IN GENERAL.—Subsection (f) of section 51A is amended by striking ''December 31, 2003'' and inserting ''December 31, 2005''.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to individuals who begin work for the employer after December 31, 2003.

SEC. 407. CERTAIN EXPENSES OF ELEMENTARY AND SECONDARY SCHOOL TEACHERS.

(a) IN GENERAL.—Subparagraph (D) of section 62(a)(2) (relating to certain trade and business deductions of employees) is amended by striking ''or 2003'' and inserting '', 2003, 2004, or 2005''.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 2003.

SEC. 408. EXTENSION OF ACCELERATED DEPRECIATION BENEFIT FOR PROPERTY ON INDIAN RESERVATIONS.

Paragraph (8) of section 168(j) (relating to termination) is amended by striking ''December 31, 2004'' and inserting ''December 31, 2005''.

SEC. 409. CHARITABLE CONTRIBUTIONS OF COMPUTER TECHNOLOGY AND EQUIPMENT USED FOR EDUCATIONAL PURPOSES.

(a) IN GENERAL.—Subparagraph (G) of section 170(e)(6) (relating to special rule for contributions of computer technology and equipment for educational purposes) is amended by striking ''December 31, 2003'' and inserting ''December 31, 2005''.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 2003.

SEC. 410. EXPENSING OF ENVIRONMENTAL REMEDIATION COSTS.

(a) IN GENERAL.—Subsection (h) of section 198 (relating to termination) is amended by striking ''December 31, 2003'' and inserting ''December 31, 2005''.

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to expenditures paid or incurred after December 31, 2003.

SEC. 411. AVAILABILITY OF MEDICAL SAVINGS ACCOUNTS.

(a) IN GENERAL.—Paragraphs (2) and (3)(B) of section 220(i) (defining cut-off year) are each amended by striking ''2003'' each place it appears in the text and headings and inserting ''2005''.

(b) CONFORMING AMENDMENTS.—

(1) Paragraph (2) of section 220(j) is amended—

(A) in the text by striking ''or 2002'' each place it appears and inserting ''2002, or 2004'', and

(B) in the heading by striking ''OR 2002'' and inserting ''2002, OR 2004''.

(2) Subparagraph (A) of section 220(j)(4) is amended by striking ''and 2002'' and inserting ''2002, and 2004''.

(3) Subparagraph (C) of section 220(j)(2) is amended to read as follows:

''(C) NO LIMITATION FOR 2000 OR 2003.—The numerical limitation shall not apply for 2000 or 2003.''.

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on January 1, 2004.

(d) TIME FOR FILING REPORTS, ETC.—

(1) The report required by section 220(j)(4) of the Internal Revenue Code of 1986 to be made on

August 1, 2004, shall be treated as timely if made before the close of the 90-day period beginning on the date of the enactment of this Act.

(2) The determination and publication required by section 220(j)(5) of such Code with respect to calendar year 2004 shall be treated as timely if made before the close of the 120-day period beginning on the date of the enactment of this Act. If the determination under the preceding sentence is that 2004 is a cut-off year under section 220(i) of such Code, the cut-off date under such section 220(i) shall be the last day of such 120-day period.

SEC. 412. TAXABLE INCOME LIMIT ON PERCENTAGE DEPLETION FOR OIL AND NATURAL GAS PRODUCED FROM MARGINAL PROPERTIES.

(a) IN GENERAL.—Subparagraph (H) of section 613A(c)(6) is amended by striking ''January 1, 2004'' and inserting ''January 1, 2006''.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 2003.

SEC. 413. QUALIFIED ZONE ACADEMY BONDS.

(a) IN GENERAL.—Paragraph (1) of section 1397E(e) is amended by striking ''and 2003'' and inserting ''2003, 2004, and 2005''.

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to obligations issued after the date of the enactment of this Act.

SEC. 414. DISTRICT OF COLUMBIA.

(a) DISTRICT OF COLUMBIA ENTERPRISE ZONE.—Subsection (f) of section 1400 is amended by striking ''December 31, 2003'' both places it appears and inserting ''December 31, 2005''.

(b) TAX-EXEMPT ECONOMIC DEVELOPMENT BONDS.—Subsection (b) of section 1400A is amended by striking ''December 31, 2003'' and inserting ''December 31, 2005''.

(c) ZERO PERCENT CAPITAL GAINS RATE.—

(1) Section 1400B is amended by striking ''January 1, 2004'' each place it appears and inserting ''January 1, 2006''.

(2) Subsections (e)(2) and (g)(2) of section 1400B are each amended by striking ''2008'' each place it appears in the headings and text and inserting ''2010''.

(3) Subsection (d) of section 1400F is amended by striking ''December 31, 2008'' and inserting ''December 31, 2010''.

(d) FIRST-TIME HOMEBUYER CREDIT.—Subsection (i) of section 1400C is amended by striking ''January 1, 2004'' and inserting ''January 1, 2006''.

(e) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall take effect on the date of the enactment of this Act.

(2) TAX-EXEMPT ECONOMIC DEVELOPMENT BONDS.—The amendment made by subsection (b) shall apply to obligations issued after December 31, 2003.

SEC. 415. EXTENSION OF CERTAIN NEW YORK LIBERTY ZONE BOND FINANCING.

Subparagraph (D) of section 1400L(d)(2) is amended by striking ''2005'' and inserting ''2010''.

SEC. 416. DISCLOSURES RELATING TO TERRORIST ACTIVITIES.

(a) IN GENERAL.—Clause (iv) of section 6103(i)(3)(C) and subparagraph (E) of section 6103(i)(7) are both amended by striking ''December 31, 2003'' and inserting ''December 31, 2005''.

(b) DISCLOSURE OF TAXPAYER IDENTITY TO LAW ENFORCEMENT AGENCIES INVESTIGATING TERRORISM.—

Subparagraph (A) of section 6103(i)(7) is amended by adding at the end the following new clause:

"(v) TAXPAYER IDENTITY.—For purposes of this subparagraph, a taxpayer's identity shall not be treated as taxpayer return information.".

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by subsection (a) shall apply to disclosures on or after the date of the enactment of this Act.

(2) SUBSECTION (b).—The amendment made by subsection (b) shall take effect as if included in section 201 of the Victims of Terrorism Tax Relief Act of 2001.

SEC. 417. DISCLOSURE OF RETURN INFORMATION RELATING TO STUDENT LOANS.

Section 6103(l)(13)(D) (relating to termination) is amended by striking "December 31, 2004" and inserting "December 31, 2005".

SEC. 418. COVER OVER OF TAX ON DISTILLED SPIRITS.

(a) IN GENERAL.—Paragraph (1) of section 7652(f) is amended by striking "January 1, 2004" and inserting "January 1, 2006".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to articles brought into the United States after December 31, 2003.

SEC. 419. JOINT REVIEW OF STRATEGIC PLANS AND BUDGET FOR THE INTERNAL REVENUE SERVICE.

(a) IN GENERAL.—Paragraph (2) of section 8021(f) (relating to joint reviews) is amended by striking ''2004'' and inserting ''2005''.

(b) REPORT.—Subparagraph (C) of section 8022(3) (regarding reports) is amended—

(1) by striking ''2004'' and inserting ''2005'', and

(2) by striking ''with respect to—'' and all that follows and inserting ''with respect to the matters addressed in the joint review referred to in section 8021(f)(2).''.

(c) TIME FOR JOINT REVIEW.—The joint review required by section 8021(f)(2) of the Internal Revenue Code of 1986 to be made before June 1, 2004, shall be treated as timely if made before June 1, 2005.

SEC. 420. PARITY IN THE APPLICATION OF CERTAIN LIMITS TO MENTAL HEALTH BENEFITS.

(a) IN GENERAL.—Subsection (f) of section 9812 is amended by striking ''and'' at the end of paragraph (1),

by striking paragraph (2), and by inserting after paragraph (1) the following new paragraphs:

"(2) on or after January 1, 2004, and before the date of the enactment of American Jobs Creation Act of 2004, and

"(3) after December 31, 2005.".

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to benefits for services furnished on or after December 31, 2003.

SEC. 421. COMBINED EMPLOYMENT TAX REPORTING PROJECT.

(a) IN GENERAL.—Paragraph (1) of section 976(b) of the Taxpayer Relief Act of 1997 (111 Stat. 898) is amended by striking "for a period ending with the date which is 5 years after the date of the enactment of this Act" and inserting "during the period ending on December 31, 2005".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to disclosures on or after the date of the enactment of this Act.

SEC. 422. CLEAN-FUEL VEHICLES.

(a) CREDIT FOR QUALIFIED ELECTRIC VEHICLES.—Paragraph (2) of section 30(b) (relating to phaseout) is amended to read as follows:

"(2) PHASEOUT.—In the case of any qualified electric vehicle placed in service after December 31, 2005, the credit otherwise allowable under subsection (a) (determined after the application of paragraph (1)) shall be reduced by 75 percent.".

(b) DEDUCTION FOR QUALIFIED CLEAN-FUEL VEHICLE PROPERTY.—Subparagraph (B) of section 179A(b)(1) (relating to phaseout) is amended to read as follows:

"(B) PHASEOUT.—In the case of any qualified clean-fuel vehicle property placed in service after December 31, 2005, the limit otherwise applicable under subparagraph (A) shall be reduced by 75 percent.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to property placed in service after December 31, 2003.

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 TO BE DETERMINED UNDER TABLES.—

"(i) IN GENERAL.—The amount of the deduction allowed under this paragraph shall be determined under tables prescribed by the Secretary.

"(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, 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—REVENUE PROVISIONS

Subtitle A—Provisions to Reduce Tax Avoidance Through Individual and Corporate Expatriation

SEC. 601. 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 prop-

erties 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.

''(b) 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 de-

termine 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.

"(c) 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.

"(d) 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 para-

graphs (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.

"(e) 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.

"(f) 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. 602. 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 15 percent of 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 be-

fore 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. 603. 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. 604. 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 18½, 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 dis-

regarded 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. 605. 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. 606. 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, par-

ticularly 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) IMPACT OF CORPORATE EXPATRIATION PROVISIONS.—The Secretary of the Treasury or the Secretary's delegate shall conduct a study of the impact 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 impact of such provisions in carrying out the purposes of this title. Not later than December 31, 2005, 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. 611. 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 re-

quired 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 or the head of the Office of Tax

Shelter Analysis 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) 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. 612. 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 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.

"(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) CONFORMING AMENDMENTS.—

(1) Sections 461(i)(3)(C), 1274(b)(3), and 7525(b) are each amended by striking "section 6662(d)(2)(C)(iii)" and inserting "section 6662(d)(2)(C)(ii)".

(2) The heading for section 6662 is amended to read as follows:

"SEC. 6662. IMPOSITION OF ACCURACY-RELATED PENALTY ON UNDERPAYMENTS."

(3) 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. 613. 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. 614. 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. 615. 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, 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. 616. 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. 617. 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. 618. 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. 619. 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) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after the date of the enactment of this Act.

SEC. 620. 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, subject to penalty under section 6700, 6701, 6707, or 6708.''.

(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. 621. 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 $5,000.

"(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) $25,000, or

"(II) the amount (not exceeding $100,000) 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. 622. 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. Any such penalty imposed on an individual may be in addition to, or in lieu of, any suspension, disbarment, or censure of such individual."

(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. 631. 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. 632. 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:

"(l) 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 30-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 sub-

section (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. 633. 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 sub-

stantial 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 at the end 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 re-

gard 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 and during the 24-month period beginning on 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) 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 ''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) 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. 634. 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. 635. 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 inter-

est 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. 636. LIMITATION ON TRANSFER OF BUILT-IN LOSSES ON REMIC RESIDUALS.

(a) IN GENERAL.—Section 362 (relating to basis to corporations) is amended by adding at the end the following new subsection:

"(e) LIMITATION ON TRANSFER OF BUILT-IN LOSSES ON REMIC RESIDUALS IN SECTION 351 TRANSACTIONS.—If—

"(1) a residual interest (as defined in section 860G(a)(2)) in a REMIC is transferred in any transaction which is described in subsection (a), and

"(2) the transferee's adjusted basis in such residual interest would (but for this paragraph) exceed its fair market value immediately after such transaction,

then, notwithstanding subsection (a), the transferee's adjusted basis in such residual interest shall not exceed its fair market value (whether or not greater than zero) immediately after such transaction.".

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

SEC. 637. 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 persons described in paragraph (4);".

(b) ELIGIBLE PERSONS.—Section 956(c) (relating to exceptions to definition of United States property) is amended by adding at the end the following new paragraph:

"(4) FINANCIAL SERVICES PROVIDERS.—

"(A) IN GENERAL.—For purposes of paragraph (2)(A), a person is described in this paragraph if at least 80 percent of the person's income is from the active conduct of a banking business which is derived from persons who are not related persons.

"(B) SPECIAL RULES.—For purposes of subparagraph (A) all related persons shall be treated as 1 person in applying the 80-percent test.

"(C) RELATED PERSON.—For purposes of this paragraph, a person is a related person to another person if—

"(i) the related person bears a relationship to such person specified in section 267(b) or 707(b)(1), or

"(ii) such persons are members of the same controlled group of corporations (as defined in section 1563(a), except that 'more than 50 percent' shall be substituted for 'at least 80 percent' each place it appears therein).".

(b) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act.

SEC. 638. ALTERNATIVE TAX FOR CERTAIN SMALL INSURANCE COMPANIES.

(a) IN GENERAL.—Clause (i) of section 831(b)(2)(A) is amended by striking "$1,200,000" and inserting "$1,890,000".

(b) INFLATION ADJUSTMENT.—Paragraph (2) of section 831(b) is amended by adding at the end the following new subparagraph:

"(C) INFLATION ADJUSTMENT.—In the case of any taxable year beginning in a calendar year after 2004, the $1,890,000 amount in subparagraph (A) shall be increased by an amount equal to—

"(i) $1,890,000, multiplied by

"(ii) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year by substituting 'calendar year 2003' for 'calendar year 1992' in subparagraph (B) thereof.

If the amount as adjusted under the preceding sentence is not a multiple of $1,000, such amount shall be rounded to the next lowest multiple of $1,000.".

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

SEC. 639. 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. 640. 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. 641. 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. 642. 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 foreign personal holding

company (as defined in section 552), 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 (reduced by properly allowable deductions and qualified deficits under section 952(c)(1)(B)) is includible 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 foreign personal holding company (as defined in section 552), 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 (reduced by properly allowable deductions and qualified deficits under section 952(c)(1)(B)) is includible 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 8½ 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. 643. EXCLUSION FROM GROSS INCOME FOR INTEREST ON OVERPAYMENTS OF INCOME TAX BY INDIVIDUALS.

(a) IN GENERAL.—Part III of subchapter B of chapter 1 (relating to items specifically excluded from gross income) is amended by inserting after section 139A the following new section:

"SEC. 139B. EXCLUSION FROM GROSS INCOME FOR INTEREST ON OVERPAYMENTS OF INCOME TAX BY INDIVIDUALS.

"(a) IN GENERAL.—In the case of an individual, gross income shall not include interest paid under section 6611 on any overpayment of tax imposed by this subtitle.

"(b) EXCEPTION.—Subsection (a) shall not apply in the case of a failure to claim items resulting in the overpayment on the original return if the Secretary determines that the principal purpose of such failure is to take advantage of subsection (a).

"(c) SPECIAL RULE FOR DETERMINING MODIFIED ADJUSTED GROSS INCOME.—For purposes of this title, interest not included in gross income under subsection (a) shall not be treated as interest which is exempt from tax for purposes of sections 32(i)(2)(B) and 6012(d) or any computation in which interest exempt from tax under this title is added to adjusted gross income.".

(b) CLERICAL AMENDMENT.—The table of sections for part III of subchapter B of chapter 1 is amended by inserting after the item relating to section 139A the following new item:

"Sec. 139B. Exclusion from gross income for interest on overpayments of income tax by individuals.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to interest received in calendar

years beginning after the date of the enactment of this Act.

SEC. 644. 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), 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 allowable 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. 645. 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. 646. 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 § 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.

Part III—Leasing

SEC. 647. 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 ''(not-

withstanding any other subparagraph of this paragraph)'' after ''shall''.

(b) LIMITATION ON DEPRECIATION PERIOD FOR SOFTWARE LEASED TO TAX-EXEMPT ENTITY.—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)).''.

(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.".

SEC. 648. 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) (without regard to paragraphs (1)(C) and (3) thereof and determined as if property described in section 167(f)(1)(B) 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 OTHER THAN AT FAIR MARKET VALUE.—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.

"(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 provisions 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. 649. 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, 2005, 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 this section, shall apply to property exchanged or converted after the date of the enactment of this Act.

Subtitle C—Reduction of Fuel Tax Evasion

SEC. 651. 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 par-

ticular 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.".

(2) NO TAX-FREE SALES.—Subsection (b) of section 4082, as amended by section 652, is amended by inserting before the period at the end "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. 652. 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.—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.—In the case of aviation-grade kerosene which is removed from any terminal directly into the fuel tank of an aircraft (determined without regard to any refueler truck, tanker, or tank wagon which meets the requirements of subparagraph (B)), a refueler truck, tanker, or tank wagon shall be treated as part of such terminal if—

"(i) such truck, tanker, or wagon meets the requirements of subparagraph (B) with respect to an airport, and

"(ii) 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 an airport if such truck, tanker, or wagon—

"(i) is loaded with aviation-grade kerosene at such terminal located within such airport and delivers such kerosene only into aircraft at such airport,

"(ii) has storage tanks, hose, and coupling equipment designed and used for the purposes of fueling aircraft,

"(iii) is not registered for highway use, and

"(iv) 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)(iv)(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.".

(4) LIABILITY FOR TAX ON AVIATION-GRADE KEROSENE USED IN COMMERCIAL AVIATION.—Sub-

section (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 allo-

cable 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 specified in 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) Sections 4101(a), 4103, 4221(a), and 6206 are each amended by striking ", 4081, or 4091" and inserting "or 4081".

(F) Section 6416(b)(2) is amended by striking "4091 or".

(G) Section 6416(b)(3) is amended by striking "or 4091" each place it appears.

(H) 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)".

(I) Section 6427(j)(1) is amended by striking ", 4081, and 4091" and inserting "and 4081".

(J)(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)".

(K) Subparagraph (B) of section 6724(d)(1) is amended by striking clause (xv) and by redesignating the succeeding clauses accordingly.

(L) Paragraph (2) of section 6724(d) is amended by striking subparagraph (W) and by redesignating the succeeding subparagraphs accordingly.

(M) 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''.

(N) 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).''.

(O) Subsection (b) of section 9508 is amended by striking paragraph (3) and by redesignating paragraphs (4) and (5) as paragraphs (3) and (4), respectively.

(P) Section 9508(c)(2)(A) is amended by striking ''sections 4081 and 4091'' and inserting ''section 4081''.

(Q) 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.".

(R) 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".

(S) 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 September 30, 2004.

(f) FLOOR STOCKS TAX.—

(1) IN GENERAL.—There is hereby imposed on aviation-grade kerosene held on October 1, 2004, 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 tax imposed before such date under section 4091 of the Internal Revenue Code of 1986, as in effect on the day before the date of the enactment of this Act.

(2) LIABILITY FOR TAX AND METHOD OF PAYMENT.—

(A) LIABILITY FOR TAX.—The person holding the kerosene on October 1, 2004, 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.

(3) 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) 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) to the extent of the remainder.

(4) HELD BY A PERSON.—For purposes of this section, 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).

(5) 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. 653. 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 Sec-

retary, 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. 654. AUTHORITY TO INSPECT ON-SITE RECORDS.

(a) IN GENERAL.—Section 4083(d)(1)(A) (relating to administrative authority), as previously 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. 655. 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 October 1, 2004.

(c) PUBLICATION OF REGISTERED PERSONS.—Beginning on July 1, 2004, the Secretary of the Treasury (or the Secretary's delegate) shall periodically publish a current list of persons registered under section 4101 of the Internal Revenue Code of 1986 who are required to register under such section.

SEC. 656. 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 electronic 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) is amended by inserting after section 6716 the following new section:

''SEC. 6717. 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 is amended by inserting after the item relating to section 6716 the following new item:

"Sec. 6717. Failure to display tax registration on vessels.".

(c) EFFECTIVE DATES.—

(1) SUBSECTION (a).—The amendments made by subsection (a) shall take effect on October 1, 2004.

(2) SUBSECTION (b).—The amendments made by subsection (b) shall apply to penalties imposed after September 30, 2004.

SEC. 657. 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) is amended by inserting after section 6717 the following new section:

''SEC. 6718. 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 is amended by inserting after the item relating to section 6717 the following new item:

"Sec. 6718. 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 September 30, 2004.

SEC. 658. COLLECTION FROM CUSTOMS BOND WHERE IMPORTER NOT REGISTERED.

(a) TAX AT POINT OF ENTRY WHERE IMPORTER NOT REGISTERED.—Subpart B of part III of subchapter A of chapter 32, as redesignated by section 652(d), is amended by adding after section 4103 the following new section:

"SEC. 4104. COLLECTION FROM CUSTOMS BOND WHERE IMPORTER NOT REGISTERED.

"(a) IN GENERAL.—The importer of record shall be jointly and severally liable for the tax imposed by section 4081(a)(1)(A)(iii) if, under regulations prescribed by the Secretary, any other person that is not a person who is registered under section 4101 is liable for such tax.

"(b) COLLECTION FROM CUSTOMS BOND.—If any tax for which any importer of record is liable under subsection (a), or for which any importer of record that is not a person registered under section 4101 is otherwise liable, is not paid on or before the last date prescribed for payment, the Secretary may collect such tax from the Customs bond posted with respect to the importation of the taxable fuel to which the tax relates. For purposes of determining the jurisdiction of any court of the United States or any agency of the United States, any action by the Secretary described in the preceding sentence shall be treated as an action to collect the tax from a bond described in section 4101(b)(1) and not as an action to collect from a bond relating to the importation of merchandise.".

(b) CONFORMING AMENDMENT.—The table of sections for subpart B of part III of subchapter A of chapter 32, as redesignated by section 652(d), is amended by add-

ing after the item related to section 4103 the following new item:

"Sec. 4104. Collection from Customs bond where importer not registered.".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to fuel entered after September 30, 2004.

SEC. 659. 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. 660. MODIFICATION OF ULTIMATE VENDOR REFUND CLAIMS WITH RESPECT TO FARMING.

(a) IN GENERAL.—

(1) REFUNDS.—Section 6427(l) is amended by adding at the end the following new paragraph:

''(6) REGISTERED VENDORS PERMITTED TO ADMINISTER CERTAIN CLAIMS FOR REFUND OF DIESEL FUEL AND KEROSENE SOLD TO FARMERS.—

''(A) IN GENERAL.—In the case of diesel fuel or kerosene used on a farm for farming purposes (within the meaning of section 6420(c)), paragraph (1) shall not apply to the

aggregate amount of such diesel fuel or kerosene if such amount does not exceed 250 gallons (as determined under subsection (i)(5)(A)(iii)).

"(B) PAYMENT TO ULTIMATE VENDOR.—The amount which would (but for subparagraph (A)) have been paid under paragraph (1) with respect to any fuel shall be paid to the ultimate vendor of such fuel, if such vendor—

"(i) is registered under section 4101, and

"(ii) meets the requirements of subparagraph (A), (B), or (D) of section 6416(a)(1).".

(2) FILING OF CLAIMS.—Section 6427(i) is amended by inserting at the end the following new paragraph:

"(5) SPECIAL RULE FOR VENDOR REFUNDS WITH RESPECT TO FARMERS.—

"(A) IN GENERAL.—A claim may be filed under subsection (l)(6) by any person with respect to fuel sold by such person for any period—

"(i) for which $200 or more ($100 or more in the case of kerosene) is payable under subsection (l)(6),

"(ii) which is not less than 1 week, and

"(iii) which is for not more than 250 gallons for each farmer for which there is a claim.

Notwithstanding subsection (l)(1), paragraph (3)(B) shall apply to claims filed under the preceding sentence.

"(B) TIME FOR FILING CLAIM.—No claim filed under this paragraph shall be allowed unless filed on or before the last day of the first quarter following the earliest quarter included in the claim.".

(3) CONFORMING AMENDMENTS.—

(A) Section 6427(l)(5)(A) is amended to read as follows:

"(A) IN GENERAL.—Paragraph (1) shall not apply to diesel fuel or kerosene used by a State or local government.".

(B) The heading for section 6427(l)(5) is amended by striking "FARMERS AND".

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to fuels sold for nontaxable use after the date of the enactment of this Act.

SEC. 661. 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, 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 after October 1, 2004.

SEC. 662. 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. For purposes of this subparagraph, if the sale of gasoline is made by means of a credit card, the person extending

the credit to the ultimate purchaser shall be deemed to be the ultimate vendor.

"(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 covered by such claim are certified and entitled to a refund under subparagraph (C) or (D) of subsection (b)(2).".

(b) CREDIT CARD PURCHASES OF DIESEL FUEL OR KEROSENE BY STATE AND LOCAL GOVERNMENTS.—Section 6427(l)(5)(C) (relating to nontaxable uses of diesel fuel, kerosene, and aviation fuel) is amended by adding at the end the following new flush sentence: "For purposes of this subparagraph, if the sale of diesel fuel or kerosene is made by means of a credit card, the person extending the credit to the ultimate purchaser shall be deemed to be the ultimate vendor.".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on October 1, 2004.

SEC. 663. TWO-PARTY EXCHANGES.

(a) IN GENERAL.—Subpart B of part III of subchapter A of chapter 32, as amended by this Act, is amended by adding 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 fuel 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 taxable fuel 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 B of part III of subchapter A of chapter 32, as amended by this Act, is amended by adding after the item relating to section 4104 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. 664. 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 9.4 cents (4.7 cents in the case of a biasply tire) for each 10 pounds so much of the maximum rated load capacity thereof as exceeds 3,500 pounds."

(b) TAXABLE TIRE.—Section 4072 is amended by redesignating subsections (a) and (b) as subsections (b) and (c), 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.

Subtitle D—Nonqualified Deferred Compensation Plans

SEC. 671. 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) IN GENERAL.—

"(A) GROSS INCOME INCLUSION.—In the case of a nonqualified deferred compensation plan, all compensation deferred under the plan for all taxable years (to the extent not subject to a substantial risk of forfeiture and not previously included in gross income) shall be includible in gross income for the taxable year unless at all times during the taxable year the plan meets the requirements of paragraphs (2), (3), and (4) and is operated in accordance with such requirements.

"(B) INTEREST ON TAX LIABILITY 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 such taxable year shall be increased by the amount of interest determined under clause (ii).

"(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 includible 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 specified employees, the requirement of subparagraph (A)(i) is met only if distributions may not be made earlier than

6 months after the date of separation from service. For purposes of the preceding sentence, a specified employee is a key employee (as defined in section 416(i)) of a corporation the 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 a sudden and unexpected 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 subpara-

graph (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.—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. 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.

"(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 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 are located outside of the United States, or

"(B) at the time transferred if such assets are subsequently transferred outside of the United States.

"(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.

"(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 amount of interest determined under subparagraph (B).

"(B) INTEREST.—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 includible 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.

"(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), and

"(B) any eligible deferred compensation plan (within the meaning of section 457(b)) of an employer described in section 457(e)(1)(A).

"(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.

"(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) W–2 FORMS.—

(1) 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 under a nonqualified deferred compensation plan (within the meaning of section 409A(d)).".

(2) 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 (by regulation) may establish a minimum amount of deferrals below which paragraph (13) does not apply and may provide that paragraph (13) does not apply with respect to amounts of deferrals which are not reasonably ascertainable.".

(c) CONFORMING AND CLERICAL AMENDMENTS.—

(1) Section 414(b) is amended by inserting "409A," after "408(p),".

(2) Section 414(c) is amended by inserting "409A," after "408(p),".

(3) 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 June 3, 2004.

(2) CERTAIN AMOUNTS DEFERRED IN 2004 UNDER CERTAIN IRREVOCABLE ELECTIONS AND BINDING ARRANGEMENTS.—The amendments made by this section shall not apply to amounts deferred after June 3, 2004, and before January 1, 2005, pursuant to an irrevocable election or binding arrangement made before June 4, 2004.

(3) EARNINGS ATTRIBUTABLE TO AMOUNT PREVIOUSLY DEFERRED.—The amendments made by this section shall apply to earnings on deferred compensation only to the extent that such amendments apply to such compensation.

(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 90 days after the date of the enactment of this Act, the Secretary of the Treasury shall issue guidance providing a limited period during which an individual participating in a nonqualified deferred compensation plan adopted before June 4, 2004, may, without violating the requirements of paragraphs (2), (3), and (4) of section 409A(a)(2) of the Internal Revenue Code of 1986 (as added by this section), terminate participation or cancel an outstanding deferral election with regard to amounts earned after June 3, 2004, if such amounts are includible in income as earned.

Subtitle E—Other Revenue Provisions

SEC. 681. 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 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. 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 ex-

tent 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(a)(4).".

(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) EFFECTIVE DATE.—The amendments made to this section shall take effect on the date of the enactment of this Act.

SEC. 682. 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:

"Taxable Year of Donor Ending on or After Date of Contribution:	Applicable Percentage:
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 re-

ceive 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 section 683, 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. 683. 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), and publicly traded securities (as defined in section 6050L(a)(2)(B)).

"(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. 684. DONATIONS OF MOTOR VEHICLES, BOATS, AND AIRCRAFT.

(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 (11) the following new paragraph:

"(12) CONTRIBUTIONS OF MOTOR VEHICLES, BOATS, AND AIRCRAFT.—

"(A) IN GENERAL.—Except as provided in regulations or other guidance, in the case of a contribution of a specified vehicle to which paragraph (8) applies, no deduction shall be allowed under subsection (a) for such contribution unless the taxpayer obtains a qualified appraisal of the specified vehicle on or before the date of such contribution.

"(B) EXCEPTION FOR INVENTORY PROPERTY.—Subparagraph (A) shall not apply to property which is described in section 1221(a)(1).

"(C) SPECIFIED VEHICLE.—For purposes of this paragraph, the term 'specified vehicle' means any—

"(i) motor vehicle manufactured primarily for use on public streets, roads, and highways,

"(ii) boat, or

"(iii) aircraft.

"(D) QUALIFIED APPRAISAL.—For purposes of this paragraph, the term 'qualified appraisal' means any appraisal which is treated for purposes of this paragraph as a qualified appraisal under regulations or other guidance prescribed by the Secretary.

"(E) 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.".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to contributions made after June 3, 2004.

SEC. 685. 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. 686. MODIFICATION OF CONTINUING LEVY ON PAYMENTS TO FEDERAL VENDERS.

(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. 687. 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 unrec-

ognized 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 prop-

erly 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.—The term 'personal property' includes—

"(i) any stock which is a part of a straddle at least 1 of the offsetting positions of which is a position with respect to

such stock or substantially similar or related property, or

"(ii) any stock 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 includible 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. 688. 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. 689. 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. 690. 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. 691. 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 avail-

able 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.

TITLE VII—MARKET REFORM FOR TOBACCO GROWERS

SEC. 701. SHORT TITLE.

This title may be cited as the ''Fair and Equitable Tobacco Reform Act of 2004''.

SEC. 702. EFFECTIVE DATE.

This title and the amendments made by this title shall apply beginning with the 2005 marketing year of each kind of tobacco.

Subtitle A—Termination of Federal Tobacco Quota and Price Support Programs

SEC. 711. 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) PROCESSING.—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,".

(c) DECLARATION OF POLICY.—Section 2 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1282) is amended by striking "tobacco,".

(d) 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).

(e) 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,''.

(f) ADMINISTRATIVE PROVISIONS.—Section 361 of the Agricultural Adjustment Act of 1938 (7 U.S.C. 1361) is amended by striking ''tobacco,''.

(g) 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''.

(h) 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).

(i) 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).

(j) 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).

(k) ACREAGE-POUNDAGE QUOTAS.—Section 4 of the Act of April 16, 1955 (Public Law 89–12; 7 U.S.C. 1314c note), is repealed.

(l) BURLEY TOBACCO ACREAGE ALLOTMENTS.—The Act of July 12, 1952 (7 U.S.C. 1315), is repealed.

(m) TRANSFER OF ALLOTMENTS.—Section 703 of the Food and Agriculture Act of 1965 (7 U.S.C. 1316) is repealed.

(n) 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''.

(o) TOBACCO FIELD MEASUREMENT.—Section 1112 of the Omnibus Budget Reconciliation Act of 1987 (Public Law 100–203) is amended by striking subsection (c).

SEC. 712. 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. 713. CONTINUATION OF LIABILITY AND NO NET LOSS ASSESSMENTS TO PREVENT LOSSES ON PRICE SUPPORT LOANS.

(a) LIABILITY.—The amendments made by this subtitle shall not affect the liability of any person under any provision of law so amended with respect to any crop of tobacco planted before the effective date applicable to that kind of tobacco under section 702.

(b) ASSESSMENT AUTHORITY.—

(1) ASSESSMENTS TO COVER OUTSTANDING LOAN COSTS.—The Commodity Credit Corporation shall impose and collect an assessment on the sale of 2005 and subsequent crops of each kind of tobacco and on the importation of tobacco in such amounts as may be necessary to obtain funds sufficient to cover any losses incurred by the Corporation with respect to price support loans that—

(A) were made for that kind of tobacco under section 106 of the Agricultural Act of 1949 (7 U.S.C. 1445), before the repeal of such section by section 712 of this Act; and

(B) remain outstanding on or after the date of the enactment of this Act.

(2) ADMINISTRATION.—Assessments under paragraph (1) shall be administered in the manner provided for in section 106B of the Agricultural Act of 1949 (7 U.S.C. 1445–2), as in effect the day before the date of the enactment of this Act. To cover the costs of administering such assessments, the Commodity Credit Corporation shall use funds remaining in the No Net Cost Tobacco Funds and No Net Cost Tobacco Accounts established pursuant to sections 106A and 106B of the Agricultural Act of 1949 (7 U.S.C. 1445–1, 1445–2).

Subtitle B—Transitional Payments to Tobacco Quota Holders and Active Producers of Tobacco

SEC. 721. DEFINITIONS OF ACTIVE TOBACCO PRODUCER AND QUOTA HOLDER.

In this subtitle:

(1) ACTIVE TOBACCO PRODUCER.—The term ''active tobacco producer'' means an owner, operator, landlord, tenant, or sharecropper who—

(A) shared in the risk of producing tobacco on a farm where tobacco was produced or considered planted pursuant to a tobacco farm marketing 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.) for the 2004 marketing year; and

(B) was actively engaged on that farm.

(2) 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.

(3) TOBACCO QUOTA HOLDER.—The term ''tobacco quota holder'' means a person that was an owner of a farm, as of July 1, 2004, for which a

basic tobacco farm marketing quota or farm acreage allotment for quota tobacco was established for the 2004 tobacco marketing year.

(4) SECRETARY.—The term ''Secretary'' means the Secretary of Agriculture.

SEC. 722. PAYMENTS TO TOBACCO QUOTA HOLDERS.

(a) PAYMENT REQUIRED.—The Secretary shall make payments to each eligible tobacco quota holder for the termination of tobacco marketing quotas and related price support under subtitle A, which shall constitute full and fair compensation for any losses relating to such termination.

(b) ELIGIBILITY.—To be eligible to receive a 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 satisfies the definition of tobacco quota holder. The application shall be submitted within such time, in such form, and in such manner as the Secretary may require.

(c) INDIVIDUAL BASE QUOTA LEVEL.—

(1) IN GENERAL.—The Secretary shall establish a base quota level applicable to each eligible 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 tobacco marketing quota under the Agriculture Adjustment Act of 1938 for the marketing year in effect on the date of the enactment of this Act for quota tobacco 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 amount equal to the product obtained by multiplying—

(A) the basic tobacco farm marketing quota or allotment for the marketing year in effect on the date of the enactment of this Act, as established by the Secretary for quota tobacco on the farm owned by the tobacco quota holder; by

(B) the average county production yield per acre for the county in which the farm is lo-

cated for the kind of tobacco for that marketing year.

(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 Act, and the parties to the sale are unable to agree to the disposition of eligibility for payments under this section, the Secretary, taking into account any transfer of quota that has been agreed to, shall provide for the equitable division of the payments among the parties by adjusting the determination of who is the tobacco quota holder with respect to particular pounds 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 Act, 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) TOTAL PAYMENT AMOUNTS BASED ON 2002 MARKETING YEAR.—

(1) CALCULATION OF ANNUAL PAYMENT AMOUNT.—During fiscal years 2005 through 2009, the Secretary shall make payments to all eligible tobacco quota holders identified under subsection (b) in an annual amount equal to the product obtained by multiplying, for each kind of tobacco—

(A) $1.40 per pound; by

(B) the total national basic marketing quota established under the Agriculture Adjustment Act of 1938 for the 2002 marketing year for that kind of tobacco.

(2) MARKETING QUOTAS OTHER THAN POUNDAGE QUOTAS.—For each kind of tobacco for which there is a marketing quota or allotment on an acreage basis, the Secretary shall convert the tobacco farm marketing quotas or allotments established under the Agriculture Adjustment Act of 1938 for the 2002 marketing year for that kind of tobacco as the Secretary considers appropriate.

(f) INDIVIDUAL PAYMENT AMOUNTS.—The annual payment amount for each eligible tobacco quota holder

with respect to a kind of tobacco under this section shall bear the same ratio to the amount determined by the Secretary under subsection (e) with respect to that kind of tobacco as the individual base quota level of that eligible tobacco quota holder under subsection (c) with respect to that kind of tobacco bears to the total base quota levels of all eligible tobacco quota holders with respect to that kind of tobacco.

(g) DEATH OF TOBACCO QUOTA HOLDER.—If a tobacco quota holder who is entitled to 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. 723. TRANSITION PAYMENTS FOR ACTIVE PRODUCERS OF QUOTA TOBACCO.

(a) TRANSITION PAYMENTS REQUIRED.—The Secretary shall make transition payments under this section to eligible active producers of quota tobacco.

(b) ELIGIBILITY.—To be eligible to receive a transition 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 satisfies the definition of active producer of quota tobacco. The application

shall be submitted within such time, in such form, and in such manner as the Secretary may require.

(c) CURRENT PRODUCTION BASE.—The Secretary shall establish a production base applicable to each eligible active producer of quota tobacco identified under subsection (b). A producer's production base shall be equal to the quantity, in pounds, of quota tobacco subject to the basic marketing quota marketed or considered planted by the producer under the Agriculture Adjustment Act of 1938 for the marketing year in effect on the date of the enactment of this Act.

(d) TOTAL PAYMENT AMOUNTS BASED ON 2002 MARKETING YEAR.—

(1) CALCULATION OF ANNUAL PAYMENT AMOUNT.—During fiscal years 2005 through 2009, the Secretary shall make payments to all eligible active producers of quota tobacco identified under subsection (b) in an annual amount equal to the product obtained by multiplying, for each kind of tobacco—

(A) $0.60 per pound; by

(B) the total national effective marketing quota established under the Agriculture Adjustment Act of 1938 for the 2002 marketing year for that kind of tobacco.

(2) MARKETING QUOTAS OTHER THAN POUNDAGE QUOTAS.—For each kind of tobacco for which there is a marketing quota or allotment on an acreage basis, the Secretary shall convert the tobacco farm marketing quotas or allotments established under the Agriculture Adjustment Act of 1938 for the 2002 marketing year for that kind of tobacco to a poundage basis before executing the mathematical equation specified in paragraph (1).

(e) INDIVIDUAL PAYMENT AMOUNTS.—The annual payment amount for each eligible active producer of quota tobacco identified under subsection (b) with respect to a kind of tobacco under this section shall bear the same ratio to the amount determined by the Secretary under subsection (d) with respect to that kind of tobacco as the individual production base of that eligible active producer under subsection (c) with respect to that kind of tobacco bears to the total production bases determined under that subsection for all eligible active producers of that kind of tobacco.

(f) DEATH OF TOBACCO PRODUCER.—If a tobacco producer who is entitled to 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 producer.

SEC. 724. RESOLUTION OF DISPUTES.

Any dispute regarding the eligibility of a person to receive a payment under this subtitle, or the amount of the payment, shall be resolved by 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.

SEC. 725. SOURCE OF FUNDS FOR PAYMENTS.

There is hereby appropriated to the Secretary, from amounts in the general fund of the Treasury, such amounts as the Secretary needs in order to make the payments required by sections 722 and 723, except that such amounts shall not exceed the lesser of—

(1) amounts received in the Treasury under chapter 52 of the Internal Revenue Code of 1986 (relating to tobacco products and cigarette papers and tubes) during the period beginning on October 1, 2004, and ending on September 30, 2009, or

(2) $9,600,000,000.

TITLE VIII—TRADE PROVISIONS

SEC. 801. 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:

"	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	".

(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. 802. CERTAIN STEAM GENERATORS, AND CERTAIN REACTOR VESSEL HEADS, 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.—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:

“	9902.84.03	Reactor vessel heads for nuclear reactors (provided for in subheading 8401.40.00)	Free	No change	No change	On or before 12/31/2008	”.

(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 by 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.

Passed the House of Representatives June 17, 2004.

Attest:

Clerk.