

104TH CONGRESS  
1ST SESSION

# S. 1299

To amend the Internal Revenue Code of 1986 to bring opportunity to small business and taxpayers.

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IN THE SENATE OF THE UNITED STATES

OCTOBER 10, 1995

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

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## A BILL

To amend the Internal Revenue Code of 1986 to bring opportunity to small business and taxpayers.

1 *Be it enacted by the Senate and House of Representa-*  
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE; AMENDMENT OF 1986 CODE;**

4 **TABLE OF CONTENTS.**

5 (a) SHORT TITLE.—This Act may be cited as the  
6 “Bringing Opportunity to Our Small Business and Tax-  
7 payers (BOOST) Act”.

8 (b) AMENDMENT OF 1986 CODE.—Except as other-  
9 wise expressly provided, whenever in this Act an amend-  
10 ment or repeal is expressed in terms of an amendment

1 to, or repeal of, a section or other provision, the reference  
 2 shall be considered to be made to a section or other provi-  
 3 sion of the Internal Revenue Code of 1986.

4 (c) TABLE OF CONTENTS.—The table of contents of  
 5 this Act is as follows:

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

#### TITLE I—TAXPAYER BILL OF RIGHTS 2

Sec. 1001. Short title.

##### Subtitle A—Taxpayer Advocate

Sec. 1011. Establishment of position of Taxpayer Advocate within Internal Revenue Service.

Sec. 1012. Expansion of authority to issue taxpayer assistance orders.

##### Subtitle B—Modifications to Installment Agreement Provisions

Sec. 1021. Taxpayer's right to installment agreement.

Sec. 1022. Running of failure to pay penalty suspended during period installment agreement in effect.

Sec. 1023. Notification of reasons for termination or denial of installment agreements.

Sec. 1024. Administrative review of denial of request for, or termination of, installment agreement.

##### Subtitle C—Interest

Sec. 1031. Expansion of authority to abate interest.

Sec. 1032. Extension of interest-free period for payment of tax after notice and demand.

##### Subtitle D—Joint Returns

Sec. 1041. Disclosure of collection activities.

Sec. 1042. Joint return may be made after separate returns without full payment of tax.

##### Subtitle E—Collection Activities

Sec. 1051. Modifications to lien and levy provisions.

Sec. 1052. Offers-in-compromise.

Sec. 1053. Notification of examination.

Sec. 1054. Increase in limit on recovery of civil damages for unauthorized collection actions.

Sec. 1055. Safeguards relating to designated summons.

##### Subtitle F—Information Returns

Sec. 1061. Phone number of person providing payee statements required to be shown on such statement.

Sec. 1062. Civil damages for fraudulent filing of information returns.

Sec. 1063. Requirement to conduct reasonable investigations of information returns.

Subtitle G—Modifications to Penalty for Failure To Collect and Pay Over Tax

Sec. 1071. Preliminary notice requirement.  
 Sec. 1072. Disclosure of certain information where more than 1 person subject to penalty.  
 Sec. 1073. Penalties under section 6672.

Subtitle H—Awarding of Costs and Certain Fees

Sec. 1081. Motion for disclosure of information.  
 Sec. 1082. Increased limit on attorney fees.  
 Sec. 1083. Failure to agree to extension not taken into account.  
 Sec. 1084. Authority for court to award reasonable administrative costs.  
 Sec. 1085. Effective date.

Subtitle I—Other Provisions

Sec. 1091. Required content of certain notices.  
 Sec. 1092. Treatment of substitute returns under section 6651.  
 Sec. 1093. Relief from retroactive application of Treasury Department regulations.  
 Sec. 1094. Required notice of certain payments.  
 Sec. 1095. Unauthorized enticement of information disclosure.

Subtitle J—Form Modifications; Studies

Sec. 1100. Definitions.

CHAPTER 1—FORM MODIFICATIONS

Sec. 1101. Explanation of certain provisions.  
 Sec. 1102. Improved procedures for notifying service of change of address or name.  
 Sec. 1103. Rights and responsibilities of divorced individuals.

CHAPTER 2—STUDIES

Sec. 1111. Pilot program for appeal of enforcement actions.  
 Sec. 1112. Study on taxpayers with special needs.  
 Sec. 1113. Reports on taxpayer-rights education program.  
 Sec. 1114. Biennial reports on misconduct by Internal Revenue Service employees.  
 Sec. 1115. Study of notices of deficiency.  
 Sec. 1116. Notice and form accuracy study.

TITLE II—INCREASE OF DEDUCTION FOR HEALTH INSURANCE COSTS OF SELF-EMPLOYED INDIVIDUALS

Sec. 2001. Increase of deduction for health insurance costs of self-employed individuals.

TITLE III—S CORPORATION REFORM ACT OF 1995

Sec. 3001. Short title.

Subtitle A—Eligible Shareholders of S Corporation

CHAPTER 1—NUMBER OF SHAREHOLDERS

- Sec. 3101. S corporations permitted to have 50 shareholders.
- Sec. 3102. Members of family treated as 1 shareholder.

CHAPTER 2—PERSONS ALLOWED AS SHAREHOLDERS

- Sec. 3111. Certain exempt organizations.
- Sec. 3112. Financial institutions.
- Sec. 3113. Nonresident aliens.
- Sec. 3114. Electing small business trusts.

CHAPTER 3—OTHER PROVISIONS

- Sec. 3121. Expansion of post-death qualification for certain trusts.

Subtitle B—Qualification and Eligibility Requirements for S Corporations

CHAPTER 1—ONE CLASS OF STOCK

- Sec. 3201. Issuance of preferred stock permitted.
- Sec. 3202. Financial institutions permitted to hold safe harbor debt.

CHAPTER 2—ELECTIONS AND TERMINATIONS

- Sec. 3211. Rules relating to inadvertent terminations and invalid elections.
- Sec. 3212. Agreement to terminate year.
- Sec. 3213. Expansion of post-termination transition period.
- Sec. 3214. Repeal of excessive passive investment income as a termination event.

CHAPTER 3—OTHER PROVISIONS

- Sec. 3221. S corporations permitted to hold subsidiaries.
- Sec. 3222. Treatment of distributions during loss years.
- Sec. 3223. Consent dividend for AAA bypass election.
- Sec. 3224. Treatment of S corporations under subchapter C.
- Sec. 3225. Elimination of pre-1983 earnings and profits.
- Sec. 3226. Allowance of charitable contributions of inventory and scientific property.
- Sec. 3227. C corporation rules to apply for fringe benefit purposes.

Subtitle C—Taxation of S Corporation Shareholders

- Sec. 3301. Uniform treatment of owner-employees under prohibited transaction rules.
- Sec. 3302. Treatment of losses to shareholders.

Subtitle D—Effective Date

- Sec. 3401. Effective date.

TITLE IV—PENSION SIMPLIFICATION

Subtitle A—Simplification of Nondiscrimination Provisions

- Sec. 4000. Short title.



1           “(1) IN GENERAL.—There is established in the  
2 Internal Revenue Service an office to be known as  
3 the ‘Office of the Taxpayer Advocate’. Such office,  
4 including all problem resolution officers, shall be  
5 under the supervision and direction of an official to  
6 be known as the ‘Taxpayer Advocate’ who shall re-  
7 port directly to the Commissioner of Internal Reve-  
8 nue. The Taxpayer Advocate shall be entitled to  
9 compensation at the same rate as the Chief Counsel  
10 for the Internal Revenue Service.

11           “(2) FUNCTIONS OF OFFICE.—

12           “(A) IN GENERAL.—It shall be the func-  
13 tion of the Office of Taxpayer Advocate to—

14           “(i) assist taxpayers in resolving prob-  
15 lems with the Internal Revenue Service,

16           “(ii) identify areas in which taxpayers  
17 have problems in dealings with the Internal  
18 Revenue Service,

19           “(iii) to the extent possible, propose  
20 changes in the administrative practices of  
21 the Internal Revenue Service to mitigate  
22 problems identified under clause (ii), and

23           “(iv) identify potential legislative  
24 changes which may be appropriate to miti-  
25 gate such problems.

1 “(B) ANNUAL REPORTS.—

2 “(i) OBJECTIVES.—Not later than  
3 June 30 of each calendar year after 1995,  
4 the Taxpayer Advocate shall report to the  
5 Committee on Ways and Means of the  
6 House of Representatives and the Commit-  
7 tee on Finance of the Senate on the objec-  
8 tives of the Taxpayer Advocate for the fis-  
9 cal year beginning in such calendar year.  
10 Any such report shall contain full and sub-  
11 stantive analysis, in addition to statistical  
12 information.

13 “(ii) ACTIVITIES.—Not later than De-  
14 cember 31 of each calendar year after  
15 1995, the Taxpayer Advocate shall report  
16 to the Committee on Ways and Means of  
17 the House of Representatives and the  
18 Committee on Finance of the Senate on  
19 the activities of the Taxpayer Advocate  
20 during the fiscal year ending during such  
21 calendar year. Any such report shall con-  
22 tain full and substantive analysis, in addi-  
23 tion to statistical information, and shall—

24 “(I) identify the initiatives the  
25 Taxpayer Advocate has taken on im-

1 proving taxpayer services and Internal  
2 Revenue Service responsiveness,

3 “(II) contain recommendations  
4 received from individuals with the au-  
5 thority to issue taxpayer assistance  
6 orders under section 7811,

7 “(III) contain a summary of at  
8 least 20 of the most serious problems  
9 encountered by taxpayers, including a  
10 description of the nature of such prob-  
11 lems,

12 “(IV) contain an inventory of the  
13 items described in subclauses (I), (II),  
14 and (III) for which action has been  
15 taken and the result of such action,

16 “(V) contain an inventory of the  
17 items described in subclauses (I), (II),  
18 and (III) for which action remains to  
19 be completed and the period during  
20 which each item has remained on such  
21 inventory,

22 “(VI) contain an inventory of the  
23 items described in subclauses (II) and  
24 (III) for which no action has been  
25 taken, the period during which each

1 item has remained on such inventory,  
2 the reasons for the inaction, and iden-  
3 tify any Internal Revenue Service offi-  
4 cial who is responsible for such inac-  
5 tion,

6 “(VII) identify any Taxpayer As-  
7 sistance Order which was not honored  
8 by the Internal Revenue Service in a  
9 timely manner, as specified under sec-  
10 tion 7811(b),

11 “(VIII) contain recommendations  
12 for such administrative and legislative  
13 action as may be appropriate to re-  
14 solve problems encountered by tax-  
15 payers, and

16 “(IX) include such other infor-  
17 mation as the Taxpayer Advocate may  
18 deem advisable.

19 “(iii) REPORT TO BE SUBMITTED DI-  
20 RECTLY.—Each report required under this  
21 subparagraph shall be provided directly to  
22 the Committees referred to in clauses (i)  
23 and (ii) without any prior review or com-  
24 ment from the Commissioner of the Inter-  
25 nal Revenue Service, the Secretary of the

1 Treasury, any other officer or employee of  
2 the Department of the Treasury, or the  
3 Office of Management and Budget.

4 “(3) RESPONSIBILITIES OF COMMISSIONER OF  
5 INTERNAL REVENUE SERVICE.—The Commissioner  
6 of Internal Revenue shall establish procedures re-  
7 quiring a formal response to all recommendations  
8 submitted to the Commissioner by the Taxpayer  
9 Advocate.”

10 (b) CONFORMING AMENDMENTS.—

11 (1) Section 7811 (relating to taxpayer assist-  
12 ance orders) is amended—

13 (A) by striking “the Office of Ombuds-  
14 man” in subsection (a) and inserting “the Of-  
15 fice of the Taxpayer Advocate”, and

16 (B) by striking “Ombudsman” each place  
17 it appears (including in the headings of sub-  
18 sections (e) and (f)) and inserting “Taxpayer  
19 Advocate”.

20 (2) The heading for section 7802 is amended to  
21 read as follows:

1 **“SEC. 7802. COMMISSIONER OF INTERNAL REVENUE; AS-**  
2 **SISTANT COMMISSIONERS; TAXPAYER ADVO-**  
3 **CATE.”**

4 (3) The table of sections for subchapter A of  
5 chapter 80 of subtitle F is amended by striking the  
6 item relating to section 7802 and inserting the  
7 following new item:

“Sec. 7802. Commissioner of Internal Revenue; Assistant Com-  
missioners; Taxpayer Advocate.”

8 (c) **EFFECTIVE DATE.**—The amendments made by  
9 this section shall take effect on the date of the enactment  
10 of this Act.

11 **SEC. 1012. EXPANSION OF AUTHORITY TO ISSUE TAXPAYER**  
12 **ASSISTANCE ORDERS.**

13 (a) **TAXPAYER’S HARDSHIP.**—Section 7811(a) (relat-  
14 ing to authority to issue) is amended by striking “signifi-  
15 cant”.

16 (b) **TERMS OF ORDERS.**—Subsection (b) of section  
17 7811 (relating to terms of taxpayer assistance orders) is  
18 amended—

19 (1) by inserting “within a specified time pe-  
20 riod” after “the Secretary”, and

21 (2) by inserting “take any action as permitted  
22 by law,” after “cease any action,”.

1 (c) LIMITATION ON AUTHORITY TO MODIFY OR RE-  
 2 SCIND.—Section 7811(c) (relating to authority to modify  
 3 or rescind) is amended to read as follows:

4 “(c) AUTHORITY TO MODIFY OR RESCIND.—Any  
 5 Taxpayer Assistance Order issued by the Taxpayer Advo-  
 6 cate under this section may be modified or rescinded only  
 7 by the Taxpayer Advocate, the Commissioner, or any supe-  
 8 rior of either.”

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

## 12 **Subtitle B—Modifications to** 13 **Installment Agreement Provisions**

### 14 **SEC. 1021. TAXPAYER’S RIGHT TO INSTALLMENT AGREE-** 15 **MENT.**

16 (a) IN GENERAL.—Subsection (a) of section 6159  
 17 (relating to agreements for payment of tax liability in in-  
 18 stallments) is amended to read as follows:

19 “(a) IN GENERAL.—

20 “(1) AUTHORIZATION OF AGREEMENTS.—The  
 21 Secretary is authorized to enter into written agree-  
 22 ments with any taxpayer under which such taxpayer  
 23 is allowed to satisfy liability for payment of any tax  
 24 in installment payments if the Secretary determines

1 that such agreement will facilitate collection of such  
2 liability.

3 “(2) AGREEMENT AS A MATTER OF RIGHT.—In  
4 the case of any taxpayer other than a corporation,  
5 the Secretary shall enter into such an agreement  
6 if—

7 “(A) the taxpayer requests such an agree-  
8 ment,

9 “(B) the tax liability is attributable to the  
10 tax imposed under chapter 1 and is less than  
11 \$10,000, and

12 “(C) the taxpayer has paid any tax liability  
13 for the 3 preceding taxable years at the time  
14 such liability was due.

15 “(3) NOTICE.—The Secretary shall include in  
16 the instructions for returns of the tax imposed under  
17 chapter 1 the rights of taxpayers under this sub-  
18 section and the steps necessary to exercise those  
19 rights.”

20 (b) EFFECTIVE DATE.—The amendment made by  
21 subsection (a) shall take effect on the date of the enact-  
22 ment of this Act.

1 **SEC. 1022. RUNNING OF FAILURE TO PAY PENALTY SUS-**  
2 **PENDED DURING PERIOD INSTALLMENT**  
3 **AGREEMENT IN EFFECT.**

4 (a) GENERAL RULE.—Section 6651 (relating to pen-  
5 alty for failure to file tax return or to pay tax) is amended  
6 by adding at the end the following new subsection:

7 “(g) TREATMENT OF INSTALLMENT AGREEMENTS  
8 UNDER SECTION 6159.—If—

9 “(1) an agreement is entered into under section  
10 6159 for the payment of any tax in installments,  
11 and

12 “(2) the taxpayer requested the Secretary to  
13 enter into the agreement on or before the due date  
14 (including extensions) for the return of the tax,  
15 the period during which such agreement is in effect shall  
16 be disregarded in determining the amount of any addition  
17 under paragraph (2) or (3) of subsection (a) with respect  
18 to such tax.”

19 (b) EFFECTIVE DATE.—The amendment made by  
20 subsection (a) shall apply to installment agreements en-  
21 tered into after the date of the enactment of this Act.

22 **SEC. 1023. NOTIFICATION OF REASONS FOR TERMINATION**  
23 **OR DENIAL OF INSTALLMENT AGREEMENTS.**

24 (a) TERMINATIONS.—Subsection (b) of section 6159  
25 (relating to extent to which agreements remain in effect)

1 is amended by adding at the end the following new para-  
2 graph:

3 “(5) NOTICE REQUIREMENTS.—The Secretary  
4 may not take any action under paragraph (2), (3),  
5 or (4) unless—

6 “(A) a notice of such action is provided to  
7 the taxpayer not later than the day 30 days be-  
8 fore the date of such action, and

9 “(B) such notice includes an explanation  
10 why the Secretary intends to take such action.

11 The preceding sentence shall not apply in any case  
12 in which the Secretary believes that collection of any  
13 tax to which an agreement under this section relates  
14 is in jeopardy.”

15 (b) DENIALS.—Section 6159 (relating to agreements  
16 for payment of tax liability in installments) is amended  
17 by adding at the end the following new subsection:

18 “(c) NOTICE REQUIREMENTS FOR DENIALS.—The  
19 Secretary may not deny any request for an installment  
20 agreement under this section unless—

21 “(1) a notice of the proposed denial is provided  
22 to the taxpayer not later than the day 30 days be-  
23 fore the date of such denial,

24 “(2) such notice includes an explanation why  
25 the Secretary intends to deny such request, and

1           “(3) such notice includes a statement of the  
2 taxpayer’s right to administrative review under sub-  
3 section (d).

4 The preceding sentence shall not apply in any case in  
5 which the Secretary believes that collection of any tax to  
6 which a request for an agreement under this section re-  
7 lates is in jeopardy.”

8           (c) CONFORMING AMENDMENT.—Paragraph (3) of  
9 section 6159(b) is amended to read as follows:

10           “(3) SUBSEQUENT CHANGE IN FINANCIAL CON-  
11 DITIONS.—If the Secretary makes a determination  
12 that the financial condition of a taxpayer with whom  
13 the Secretary has entered into an agreement under  
14 subsection (a) has significantly changed, the Sec-  
15 retary may alter, modify, or terminate such agree-  
16 ment.”

17           (d) EFFECTIVE DATE.—The amendments made by  
18 this section shall take effect on the date 6 months after  
19 the date of the enactment of this Act.

20 **SEC. 1024. ADMINISTRATIVE REVIEW OF DENIAL OF RE-**  
21 **QUEST FOR, OR TERMINATION OF, INSTALL-**  
22 **MENT AGREEMENT.**

23           (a) GENERAL RULE.—Section 6159 (relating to  
24 agreements for payment of tax liability in installments),

1 as amended by section 1023(b), is amended by adding at  
2 the end the following new subsection:

3 “(d) ADMINISTRATIVE REVIEW.—The Secretary shall  
4 establish procedures for an independent administrative re-  
5 view of denials of requests for, or terminations of, install-  
6 ment agreements under this section.”

7 (b) EFFECTIVE DATE.—The amendment made by  
8 subsection (a) shall take effect on January 1, 1996.

### 9 **Subtitle C—Interest**

#### 10 **SEC. 1031. EXPANSION OF AUTHORITY TO ABATE INTEREST.**

11 (a) GENERAL RULE.—Paragraph (1) of section  
12 6404(e) (relating to abatement of interest in certain cases)  
13 is amended—

14 (1) by inserting “unreasonable” before “error”  
15 each place it appears in subparagraphs (A) and (B),  
16 and

17 (2) by striking “in performing a ministerial  
18 act” each place it appears.

19 (b) MANDATORY ABATEMENT FOR SMALL TAX-  
20 PAYERS.—The first sentence of section 6404(e)(1) is  
21 amended by inserting “in the case of a taxpayer not de-  
22 scribed in section 7430(c)(4)(A)(iii) and shall abate the  
23 assessment of such interest until the date demand for pay-  
24 ment is made in the case of a taxpayer described in section  
25 7430(c)(4)(A)(iii)” before the period at the end.

1 (c) CLERICAL AMENDMENT.—The subsection head-  
 2 ing for subsection (e) of section 6404 is amended by strik-  
 3 ing “Assessments” and inserting “Abatement”.

4 (d) EFFECTIVE DATE.—The amendments made by  
 5 this section shall apply to interest accruing with respect  
 6 to deficiencies or payments for taxable years beginning  
 7 after the date of the enactment of this Act.

8 **SEC. 1032. EXTENSION OF INTEREST-FREE PERIOD FOR**  
 9 **PAYMENT OF TAX AFTER NOTICE AND DE-**  
 10 **MAND.**

11 (a) GENERAL RULE.—Paragraph (3) of section  
 12 6601(e) (relating to payments made within 10 days after  
 13 notice and demand) is amended to read as follows:

14 “(3) PAYMENTS MADE WITHIN SPECIFIED PE-  
 15 RIOD AFTER NOTICE AND DEMAND.—If notice and  
 16 demand is made for payment of any amount and if  
 17 such amount is paid within 21 days (10 days if the  
 18 amount for which such notice and demand is made  
 19 equals or exceeds \$100,000) after the date of such  
 20 notice and demand, interest under this section on  
 21 the amount so paid shall not be imposed for the pe-  
 22 riod after the date of such notice and demand.”

23 (b) CONFORMING AMENDMENT.—Paragraph (3) of  
 24 section 6651(a) (relating to addition to tax for failure to  
 25 file tax return or pay tax) is amended by striking “10

1 days” and inserting “21 days (10 days if the amount for  
 2 which such notice and demand is made equals or exceeds  
 3 \$100,000)”.

4 (c) EFFECTIVE DATE.—The amendments made by  
 5 this section shall apply in the case of any notice and de-  
 6 mand given after December 31, 1995.

## 7 **Subtitle D—Joint Returns**

### 8 **SEC. 1041. DISCLOSURE OF COLLECTION ACTIVITIES.**

9 (a) GENERAL RULE.—Subsection (e) of section 6103  
 10 (relating to disclosure to persons having material interest)  
 11 is amended by adding at the end the following new para-  
 12 graph:

13 “(8) DISCLOSURE OF COLLECTION ACTIVITIES  
 14 WITH RESPECT TO JOINT RETURN.—If any defi-  
 15 ciency of tax with respect to a joint return is as-  
 16 sessed and the individuals filing such return are no  
 17 longer married or no longer reside in the same  
 18 household, upon request in writing of either of such  
 19 individuals, the Secretary may disclose in writing to  
 20 the individual making the request whether the Sec-  
 21 retary has attempted to collect such deficiency from  
 22 such other individual, the general nature of such col-  
 23 lection activities, and the amount collected.”

1 (b) EFFECTIVE DATE.—The amendment made by  
 2 subsection (a) shall take effect on the date of the enact-  
 3 ment of this Act.

4 **SEC. 1042. JOINT RETURN MAY BE MADE AFTER SEPARATE**  
 5 **RETURNS WITHOUT FULL PAYMENT OF TAX.**

6 (a) GENERAL RULE.—Paragraph (2) of section  
 7 6013(b) (relating to limitations on filing of joint return  
 8 after filing separate returns) is amended by striking sub-  
 9 paragraph (A) and redesignating the following subpara-  
 10 graphs accordingly.

11 (b) EFFECTIVE DATE.—The amendment made by  
 12 subsection (a) shall apply to taxable years beginning after  
 13 the date of the enactment of this Act.

14 **Subtitle E—Collection Activities**

15 **SEC. 1051. MODIFICATIONS TO LIEN AND LEVY PROVI-**  
 16 **SIONS.**

17 (a) WITHDRAWAL OF CERTAIN NOTICES.—Section  
 18 6323 (relating to validity and priority against certain per-  
 19 sons) is amended by adding at the end the following new  
 20 subsection:

21 “(j) WITHDRAWAL OF NOTICE IN CERTAIN CIR-  
 22 CUMSTANCES.—

23 “(1) IN GENERAL.—The Secretary may with-  
 24 draw a notice of a lien filed under this section and  
 25 this chapter shall be applied as if the withdrawn no-

1        tice had not been filed, if the Secretary determines  
2        that—

3                “(A) the filing of such notice was pre-  
4                mature or otherwise not in accordance with ad-  
5                ministrative procedures of the Secretary,

6                “(B) the taxpayer has entered into an  
7                agreement under section 6159 to satisfy the tax  
8                liability for which the lien was imposed by  
9                means of installment payments, unless such  
10              agreement provides otherwise,

11              “(C) the withdrawal of such notice will fa-  
12              cilitate the collection of the tax liability, or

13              “(D) with the consent of the taxpayer or  
14              the Taxpayer Advocate, the withdrawal of such  
15              notice would be in the best interests of the tax-  
16              payer (as determined by the Taxpayer Advo-  
17              cate) and the United States.

18        Any such withdrawal shall be made by filing notice  
19        at the same office as the withdrawn notice. A copy  
20        of such notice of withdrawal shall be provided to the  
21        taxpayer.

22              “(2) NOTICE TO CREDIT AGENCIES, ETC.—  
23        Upon written request by the taxpayer with respect  
24        to whom a notice of a lien was withdrawn under  
25        paragraph (1), the Secretary shall promptly make

1 reasonable efforts to notify credit reporting agencies,  
2 and any financial institution or creditor whose name  
3 and address is specified in such request, of the with-  
4 drawal of such notice. Any such request shall be in  
5 such form as the Secretary may prescribe.”

6 (b) RETURN OF LEVIED PROPERTY IN CERTAIN  
7 CASES.—Section 6343 (relating to authority to release  
8 levy and return property) is amended by adding at the  
9 end the following new subsection:

10 “(d) RETURN OF PROPERTY IN CERTAIN CASES.—  
11 If—

12 “(1) any property has been levied upon, and

13 “(2) the Secretary determines that—

14 “(A) the levy on such property was pre-  
15 mature or otherwise not in accordance with ad-  
16 ministrative procedures of the Secretary,

17 “(B) the taxpayer has entered into an  
18 agreement under section 6159 to satisfy the tax  
19 liability for which the levy was imposed by  
20 means of installment payments, unless such  
21 agreement provides otherwise,

22 “(C) the return of such property will facili-  
23 tate the collection of the tax liability, or

24 “(D) with the consent of the taxpayer or  
25 the Taxpayer Advocate, the return of such

1 property would be in the best interests of the  
2 taxpayer (as determined by the Taxpayer Advo-  
3 cate) and the United States,  
4 the provisions of subsection (b) shall apply in the same  
5 manner as if such property had been wrongly levied upon,  
6 except that no interest shall be allowed under subsection  
7 (c).”

8 (c) MODIFICATIONS IN CERTAIN LEVY EXEMPTION  
9 AMOUNTS.—

10 (1) FUEL, ETC.—Paragraph (2) of section  
11 6334(a) (relating to fuel, provisions, furniture, and  
12 personal effects exempt from levy) is amended—

13 (A) by striking “If the taxpayer is the  
14 head of a family, so” and inserting “So”, and

15 (B) by striking “\$1,650 (\$1,550 in the  
16 case of levies issued during 1989)” and insert-  
17 ing “\$1,750”.

18 (2) BOOKS, ETC.—Paragraph (3) of section  
19 6334(a) (relating to books and tools of a trade, busi-  
20 ness, or profession exempt from levy) is amended by  
21 striking “\$1,100 (\$1,050 in the case of levies issued  
22 during 1989)” and inserting “\$1,250”.

23 (3) INDEXED FOR INFLATION.—Section 6334  
24 (relating to property exempt from levy) is amended  
25 by adding at the end the following new subsection:

1 “(f) INFLATION ADJUSTMENTS.—

2 “(1) IN GENERAL.—In the case of any calendar  
3 year beginning after 1996, each dollar amount re-  
4 ferred to in paragraphs (2) and (3) of subsection (a)  
5 shall be increased by an amount equal to—

6 “(A) such dollar amount, multiplied by

7 “(B) the cost-of-living adjustment deter-  
8 mined under section 1(f)(3) for such calendar  
9 year, by substituting ‘calendar year 1995’ for  
10 ‘calendar year 1992’ in subparagraph (B)  
11 thereof.

12 “(2) ROUNDING.—If any dollar amount after  
13 being increased under paragraph (1) is not a mul-  
14 tiple of \$10, such dollar amount shall be rounded to  
15 the nearest multiple of \$10 (or, if such dollar  
16 amount is a multiple of \$5, such dollar amount shall  
17 be increased to the next higher multiple of \$10).”

18 (d) EFFECTIVE DATES.—

19 (1) IN GENERAL.—Except as provided in para-  
20 graph (2), the amendments made by this section  
21 shall take effect on the date of the enactment of this  
22 Act.

23 (2) EXEMPT AMOUNTS.—The amendments  
24 made by subsection (c) shall take effect with respect  
25 to levies issued after December 31, 1995.

1 **SEC. 1052. OFFERS-IN-COMPROMISE.**

2 (a) GENERAL RULE.—Subsection (a) of section 7122  
3 (relating to compromises) is amended by adding at the end  
4 the following new sentence: “The Secretary may make  
5 such a compromise in any case where the Secretary deter-  
6 mines that such compromise would be in the best interests  
7 of the United States.”

8 (b) REVIEW REQUIREMENTS.—Subsection (b) of sec-  
9 tion 7122 (relating to records) is amended by striking  
10 “\$500.” and inserting “\$50,000. However, such com-  
11 promise shall be subject to continuing quality review by  
12 the Secretary.”

13 (c) EFFECTIVE DATE.—The amendments made by  
14 this section shall take effect on the date of the enactment  
15 of this Act.

16 **SEC. 1053. NOTIFICATION OF EXAMINATION.**

17 (a) IN GENERAL.—Section 7605 (relating to restric-  
18 tions on examination of taxpayer) is amended by redesignig-  
19 nating subsection (c) as subsection (d) and by inserting  
20 after subsection (b) the following new subsection:

21 “(c) NOTIFICATION REQUIREMENT.—No examina-  
22 tion described in subsection (a) shall be made unless the  
23 Secretary notifies the taxpayer in writing by mail to an  
24 address determined under section 6212(b) that the tax-  
25 payer is under examination and provides the taxpayer with  
26 an explanation of the process as described in section

1 7521(b)(1). The preceding sentence shall not apply in the  
2 case of any examination if the Secretary determines  
3 that—

4 “(1) such examination is in connection with a  
5 criminal investigation or is with respect to a tax the  
6 collection of which is in jeopardy, or

7 “(2) the application of the preceding sentence  
8 would be inconsistent with national security needs or  
9 would interfere with the effective conduct of a con-  
10 fidential law enforcement or foreign counterintel-  
11 ligence activity.”

12 (b) CONFORMING AMENDMENT.—Paragraph (1) of  
13 section 7521(b) (relating to safeguards) is amended by  
14 striking “or at”.

15 (c) EFFECTIVE DATE.—The amendments made by  
16 this section shall take effect on the date of the enactment  
17 of this Act.

18 **SEC. 1054. INCREASE IN LIMIT ON RECOVERY OF CIVIL**  
19 **DAMAGES FOR UNAUTHORIZED COLLECTION**  
20 **ACTIONS.**

21 (a) GENERAL RULE.—Subsection (b) of section 7433  
22 (relating to damages) is amended by striking “\$100,000”  
23 and inserting “\$1,000,000”.

24 (b) EFFECTIVE DATE.—The amendment made by  
25 subsection (a) shall apply to actions by officers or employ-

1 ees of the Internal Revenue Service after the date of the  
2 enactment of this Act.

3 **SEC. 1055. SAFEGUARDS RELATING TO DESIGNATED SUM-**  
4 **MONS.**

5 (a) STANDARD OF REVIEW.—Subparagraph (A) of  
6 section 6503(k)(2) (defining designated summons) is  
7 amended by redesignating clauses (i) and (ii) as clauses  
8 (ii) and (iii), respectively, and by inserting before clause  
9 (ii) (as so redesignated) the following new clause:

10 “(i) the issuance of such summons is  
11 preceded by a review of such issuance by  
12 the regional counsel of the Office of Chief  
13 Counsel for the region in which the exam-  
14 ination of the corporation is being con-  
15 ducted.”.

16 (b) NOTICE REQUIREMENTS FOR ISSUANCE.—Sec-  
17 tion 6503(k) is amended by adding at the end the follow-  
18 ing new paragraph:

19 “(4) NOTICE REQUIREMENTS.—With respect to  
20 any summons referred to in paragraph (1)(A) issued  
21 to any person other than the corporation, the Sec-  
22 retary shall promptly notify the corporation, in writ-  
23 ing, that such summons has been issued with respect  
24 to such corporation’s return of tax.”

1 (c) EFFECTIVE DATE.—The amendments made by  
 2 this section shall apply to summons issued after the date  
 3 of the enactment of this Act.

## 4 **Subtitle F—Information Returns**

### 5 **SEC. 1061. PHONE NUMBER OF PERSON PROVIDING PAYEE** 6 **STATEMENTS REQUIRED TO BE SHOWN ON** 7 **SUCH STATEMENT.**

8 (a) GENERAL RULE.—The following provisions are  
 9 each amended by striking “name and address” and insert-  
 10 ing “name, address, and phone number of the information  
 11 contact”:

- 12 (1) Section 6041(d)(1).
- 13 (2) Section 6041A(e)(1).
- 14 (3) Section 6042(c)(1).
- 15 (4) Section 6044(e)(1).
- 16 (5) Section 6045(b)(1).
- 17 (6) Section 6049(c)(1)(A).
- 18 (7) Section 6050B(b)(1).
- 19 (8) Section 6050H(d)(1).
- 20 (9) Section 6050I(e)(1).
- 21 (10) Section 6050J(e).
- 22 (11) Section 6050K(b)(1).
- 23 (12) Section 6050N(b)(1).

24 (b) EFFECTIVE DATE.—The amendments made by  
 25 subsection (a) shall apply to statements required to be fur-

1 nished after December 31, 1995 (determined without  
2 regard to any extension).

3 **SEC. 1062. CIVIL DAMAGES FOR FRAUDULENT FILING OF**  
4 **INFORMATION RETURNS.**

5 (a) GENERAL RULE.—Subchapter B of chapter 76  
6 (relating to proceedings by taxpayers and third parties)  
7 is amended by redesignating section 7434 as section 7435  
8 and by inserting after section 7433 the following new  
9 section:

10 **“SEC. 7434. CIVIL DAMAGES FOR FRAUDULENT FILING OF**  
11 **INFORMATION RETURNS.**

12 “(a) IN GENERAL.—If any person willfully files a  
13 false or fraudulent information return with respect to pay-  
14 ments purported to be made to any other person, such  
15 other person may bring a civil action for damages against  
16 the person so filing such return.

17 “(b) DAMAGES.—In any action brought under sub-  
18 section (a), upon a finding of liability on the part of the  
19 defendant, the defendant shall be liable to the plaintiff in  
20 an amount equal to the greater of \$5,000 or the sum of—

21 “(1) any actual damages sustained by the plain-  
22 tiff as a proximate result of the filing of the false  
23 or fraudulent information return (including any  
24 costs attributable to resolving deficiencies asserted  
25 as a result of such filing), and

1           “(2) the costs of the action.

2           “(c) PERIOD FOR BRINGING ACTION.—Notwith-  
3 standing any other provision of law, an action to enforce  
4 the liability created under this section may be brought  
5 without regard to the amount in controversy and may be  
6 brought only within the later of—

7           “(1) 6 years after the date of the filing of the  
8 false or fraudulent information return, or

9           “(2) 1 year after the date such false or fraudu-  
10 lent information return would have been discovered  
11 by exercise of reasonable care.

12          “(d) COPY OF COMPLAINT FILED WITH IRS.—Any  
13 person bringing an action under subsection (a) shall pro-  
14 vide a copy of the complaint to the Internal Revenue Serv-  
15 ice upon the filing of such complaint with the court.

16          “(e) FINDING OF COURT TO INCLUDE CORRECT  
17 AMOUNT OF PAYMENT.—The judgment of the court in an  
18 action brought under subsection (a) shall include a finding  
19 of the correct amount which should have been reported  
20 in the information return.

21          “(f) INFORMATION RETURN.—For purposes of this  
22 section, the term ‘information return’ means any state-  
23 ment described in section 6724(d)(1)(A).”

24          (b) CLERICAL AMENDMENT.—The table of sections  
25 for subchapter B of chapter 76 is amended by striking

1 the item relating to section 7434 and inserting the  
2 following:

“Sec. 7434. Civil damages for fraudulent filing of information re-  
turns.

“Sec. 7435. Cross references.”

3 (c) **EFFECTIVE DATE.**—The amendments made by  
4 this section shall apply to false or fraudulent information  
5 returns filed after the date of the enactment of this Act.

6 **SEC. 1063. REQUIREMENT TO CONDUCT REASONABLE IN-**  
7 **VESTIGATIONS OF INFORMATION RETURNS.**

8 (a) **GENERAL RULE.**—Section 6201 (relating to as-  
9 sessment authority) is amended by redesignating sub-  
10 section (d) as subsection (e) and by inserting after sub-  
11 section (c) the following new subsection:

12 “(d) **REQUIRED REASONABLE INVESTIGATION OF IN-**  
13 **FORMATION RETURNS.**—If a taxpayer asserts a reason-  
14 able dispute with respect to any item of income reported  
15 on an information return filed with the Secretary under  
16 chapter 61 by a third party, the Secretary, when making  
17 a determination of a deficiency based on such information  
18 return, shall have the burden of proof with respect to such  
19 determination unless the Secretary has conducted a rea-  
20 sonable investigation to corroborate the accuracy of such  
21 information return.”

22 (b) **EFFECTIVE DATE.**—The amendment made by  
23 subsection (a) shall take effect on the date of the enact-  
24 ment of this Act.

1 **Subtitle G—Modifications to Pen-**  
2 **alty for Failure To Collect and**  
3 **Pay Over Tax**

4 **SEC. 1071. PRELIMINARY NOTICE REQUIREMENT.**

5 (a) IN GENERAL.—Section 6672 (relating to failure  
6 to collect and pay over tax, or attempt to evade or defeat  
7 tax) is amended by redesignating subsection (b) as sub-  
8 section (c) and by inserting after subsection (a) the follow-  
9 ing new subsection:

10 “(b) PRELIMINARY NOTICE REQUIREMENT.—

11 “(1) IN GENERAL.—No penalty shall be im-  
12 posed under subsection (a) unless the Secretary noti-  
13 fies the taxpayer in writing by mail to an address as  
14 determined under section 6212(b) that the taxpayer  
15 shall be subject to an assessment of such penalty.

16 “(2) TIMING OF NOTICE.—The mailing of the  
17 notice described in paragraph (1) shall precede any  
18 notice and demand of any penalty under subsection  
19 (a) by at least 60 days.

20 “(3) STATUTE OF LIMITATIONS.—If a notice  
21 described in paragraph (1) with respect to any pen-  
22 alty is mailed before the expiration of the period  
23 provided by section 6501 for the assessment of such  
24 penalty (determined without regard to this para-  
25 graph), the period provided by such section for the

1 assessment of such penalty shall not expire before  
 2 the date 90 days after the date on which such notice  
 3 was mailed.

4 “(4) EXCEPTION FOR JEOPARDY.—This sub-  
 5 section shall not apply if the Secretary finds that the  
 6 collection of the penalty is in jeopardy.”

7 (b) EFFECTIVE DATE.—The amendment made by  
 8 subsection (a) shall apply to assessments made after De-  
 9 cember 31, 1995.

10 **SEC. 1072. DISCLOSURE OF CERTAIN INFORMATION**

11 **WHERE MORE THAN 1 PERSON SUBJECT TO**

12 **PENALTY.**

13 (a) IN GENERAL.—Subsection (e) of section 6103  
 14 (relating to disclosure to persons having material interest),  
 15 as amended by section 1041(a), is amended by adding at  
 16 the end the following new paragraph:

17 “(9) DISCLOSURE OF CERTAIN INFORMATION  
 18 WHERE MORE THAN 1 PERSON SUBJECT TO PEN-  
 19 ALTY UNDER SECTION 6672.—If the Secretary deter-  
 20 mines that a person is liable for a penalty under sec-  
 21 tion 6672(a) with respect to any failure, upon re-  
 22 quest in writing of such person, the Secretary shall  
 23 disclose in writing to such person—

1           “(A) the name of any other person whom  
2           the Secretary has determined to be liable for  
3           such penalty with respect to such failure, and

4           “(B) whether the Secretary has attempted  
5           to collect such penalty from such other person,  
6           the general nature of such collection activities,  
7           and the amount collected.”

8           (b) EFFECTIVE DATE.—The amendment made by  
9           subsection (a) shall take effect on the date of the enact-  
10          ment of this Act.

11       **SEC. 1073. PENALTIES UNDER SECTION 6672.**

12          (a) PUBLIC INFORMATION REQUIREMENTS.—The  
13          Secretary of the Treasury or the Secretary’s delegate  
14          (hereafter in this section referred to as the “Secretary”)  
15          shall take such actions as may be appropriate to ensure  
16          that employees are aware of their responsibilities under  
17          the Federal tax depository system, the circumstances  
18          under which employees may be liable for the penalty im-  
19          posed by section 6672 of the Internal Revenue Code of  
20          1986, and the responsibility to promptly report to the In-  
21          ternal Revenue Service any failure referred to in sub-  
22          section (a) of such section 6672. Such actions shall in-  
23          clude—

24                  (1) printing of a warning on deposit coupon  
25          booklets and the appropriate tax returns that certain

1 employees may be liable for the penalty imposed by  
2 such section 6672, and

3 (2) the development of a special information  
4 packet.

5 (b) BOARD MEMBERS OF TAX-EXEMPT ORGANIZA-  
6 TIONS.—

7 (1) VOLUNTARY BOARD MEMBERS.—

8 (A) IN GENERAL.—The penalty under sec-  
9 tion 6672 of the Internal Revenue Code of 1986  
10 shall not be imposed on unpaid, volunteer mem-  
11 bers of any board of trustees or directors of an  
12 organization referred to in section 501 of such  
13 Code to the extent such members are solely  
14 serving in an honorary capacity, do not partici-  
15 pate in the day-to-day or financial operations of  
16 the organization, and do not have actual knowl-  
17 edge of the failure on which such penalty is im-  
18 posed.

19 (B) APPLICATION OF PARAGRAPH.—This  
20 paragraph shall not apply if it results in no per-  
21 son being held liable for the penalty described  
22 in section 6672(a) of the Internal Revenue  
23 Code of 1986.

24 (2) DEVELOPMENT OF EXPLANATORY MATE-  
25 RIALS.—The Secretary shall develop materials ex-

1       plaining the circumstances under which board mem-  
2       bers of tax-exempt organizations (including vol-  
3       untary and honorary members) may be subject to  
4       penalty under section 6672 of such Code. Such ma-  
5       terials shall be made available to tax-exempt organi-  
6       zations.

7               (3) IRS INSTRUCTIONS.—The Secretary shall  
8       clarify the instructions to Internal Revenue Service  
9       employees on the application of the penalty under  
10      section 6672 of such Code with regard to voluntary  
11      members of boards of trustees or directors of tax-  
12      exempt organizations.

13      (c) PROMPT NOTIFICATION.—To the maximum ex-  
14      tent practicable, the Secretary shall notify all persons who  
15      have failed to make timely and complete deposit of any  
16      taxes described in section 6672 of the Internal Revenue  
17      Code of 1986 of such failure within 30 days after the re-  
18      turn was filed reflecting such failure or after the date on  
19      which the Secretary is first aware of such failure. If the  
20      person failing to make the deposit is not an individual,  
21      the Secretary shall notify the entity subject to such deposit  
22      requirement and that entity shall notify, within 15 days  
23      of the notification by the Secretary, all officers, general  
24      partners, trustees, or other managers of the failure.

1 **Subtitle H—Awarding of Costs and**  
2 **Certain Fees**

3 **SEC. 1081. MOTION FOR DISCLOSURE OF INFORMATION.**

4 Paragraph (4) of section 7430(c) (defining prevailing  
5 party) is amended by adding at the end the following new  
6 subparagraph:

7 “(C) MOTION FOR DISCLOSURE OF INFOR-  
8 MATION.—Once a taxpayer substantially pre-  
9 vails as described in subparagraph (A)(ii), the  
10 taxpayer may file a motion for an order requir-  
11 ing the disclosure (within a reasonable period of  
12 time specified by the court) of all information  
13 and copies of relevant records in the possession  
14 of the Internal Revenue Service with respect to  
15 such taxpayer’s case and the substantial jus-  
16 tification for the position taken by the Internal  
17 Revenue Service.”

18 **SEC. 1082. INCREASED LIMIT ON ATTORNEY FEES.**

19 Paragraph (1) of section 7430(c) (defining reason-  
20 able litigation costs) is amended—

21 (1) by striking “\$75” in clause (iii) of subpara-  
22 graph (B) and inserting “\$110”,

23 (2) by striking “an increase in the cost of living  
24 or” in clause (iii) of subparagraph (B), and

25 (3) by adding after clause (iii) the following:

1 “In the case of any calendar year beginning after  
2 1995, the dollar amount referred to in clause (iii)  
3 shall be increased by an amount equal to such dollar  
4 amount multiplied by the cost-of-living adjustment  
5 determined under section 1(f)(3) for such calendar  
6 year, by substituting ‘calendar year 1994’ for ‘cal-  
7 endar year 1992’ in subparagraph (B) thereof. If  
8 any dollar amount after being increased under the  
9 preceding sentence is not a multiple of \$10, such  
10 dollar amount shall be rounded to the nearest mul-  
11 tiple of \$10 (or, if such dollar amount is a multiple  
12 of \$5, such dollar amount shall be increased to the  
13 next higher multiple of \$10).”

14 **SEC. 1083. FAILURE TO AGREE TO EXTENSION NOT TAKEN**  
15 **INTO ACCOUNT.**

16 Paragraph (1) of section 7430(b) (relating to require-  
17 ment that administrative remedies be exhausted) is  
18 amended by adding at the end the following new sentence:  
19 “Any failure to agree to an extension of the time for the  
20 assessment of any tax shall not be taken into account for  
21 purposes of determining whether the prevailing party  
22 meets the requirements of the preceding sentence.”

23 **SEC. 1084. AUTHORITY FOR COURT TO AWARD REASON-**  
24 **ABLE ADMINISTRATIVE COSTS.**

25 Section 7430(c)(7)(B) is amended to read as follows:

1                   “(B) the position taken in an administra-  
2                   tive proceeding to which subsection (a) applies.”

3 **SEC. 1085. EFFECTIVE DATE.**

4           The amendments made by this subtitle shall apply in  
5 the case of proceedings commenced after the date of the  
6 enactment of this Act.

7                   **Subtitle I—Other Provisions**

8 **SEC. 1091. REQUIRED CONTENT OF CERTAIN NOTICES.**

9           (a) GENERAL RULE.—Subsection (a) of section 7522  
10 (relating to content of tax due, deficiency, and other no-  
11 tices) is amended by striking “shall describe the basis for,  
12 and identify” and inserting “shall set forth the adjust-  
13 ments which are the basis for, and shall identify”.

14           (b) EFFECTIVE DATE.—The amendment made by  
15 subsection (a) shall apply to notices sent after the date  
16 6 months after the date of the enactment of this Act.

17 **SEC. 1092. TREATMENT OF SUBSTITUTE RETURNS UNDER**  
18                   **SECTION 6651.**

19           (a) GENERAL RULE.—Section 6651 (relating to fail-  
20 ure to file tax return or to pay tax), as amended by section  
21 1022(a), is amended by adding at the end the following  
22 new subsection:

23           “(h) TREATMENT OF RETURNS PREPARED BY SEC-  
24 RETARY UNDER SECTION 6020(b).—In the case of any  
25 return made by the Secretary under section 6020(b)—



1           “(B) In the case of any final regulation,  
2           the date on which any proposed or temporary  
3           regulation to which such final regulation relates  
4           was filed with the Federal Register.

5           “(C) The date on which any notice sub-  
6           stantially describing the expected contents of  
7           any temporary, proposed, or final regulation is  
8           issued to the public.

9           “(2) PREVENTION OF ABUSE.—The Secretary  
10          may provide that any regulation may take effect or  
11          apply retroactively to prevent abuse of a statute to  
12          which the regulation relates.

13          “(3) CORRECTION OF PROCEDURAL DE-  
14          FECTS.—The Secretary may provide that any regu-  
15          lation may apply retroactively to correct a proce-  
16          dural defect in the issuance of any prior regulation.

17          “(4) INTERNAL REGULATIONS.—The limitation  
18          of paragraph (1) shall not apply to any regulation  
19          relating to internal Treasury Department policies,  
20          practices, or procedures.

21          “(5) CONGRESSIONAL AUTHORIZATION.—The  
22          limitation of paragraph (1) may be superseded by a  
23          legislative grant from Congress authorizing the Sec-  
24          retary to prescribe the effective date with respect to  
25          any regulation.

1           “(6) ELECTION TO APPLY RETROACTIVELY.—  
2           The Secretary may provide for any taxpayer to elect  
3           to apply any regulation before the dates specified in  
4           paragraph (1).

5           “(7) APPLICATION TO RULINGS.—The Sec-  
6           retary may prescribe the extent, if any, to which any  
7           ruling (including any judicial decision or any admin-  
8           istrative determination other than by regulation) re-  
9           lating to the internal revenue laws shall be applied  
10          without retroactive effect.”

11          (b) EFFECTIVE DATE.—

12           (1) IN GENERAL.—Except as provided in para-  
13          graph (2), the amendment made by subsection (a)  
14          shall apply with respect to—

15           (A) any temporary or proposed regulation  
16          filed on or after January 5, 1993, and

17           (B) any temporary or proposed regulation  
18          filed before January 5, 1993, and filed as a  
19          final regulation after such date.

20          (2) SPECIAL RULE.—Section 7805(b)(2) of the  
21          Internal Revenue Code of 1986 (as added by sub-  
22          section (a)) shall apply only to statutes enacted on  
23          or after the date of the enactment of this Act.

1 **SEC. 1094. REQUIRED NOTICE OF CERTAIN PAYMENTS.**

2 If any payment is received by the Secretary of the  
3 Treasury or the Secretary's delegate (hereafter in this sec-  
4 tion referred to as the "Secretary") from any taxpayer  
5 and the Secretary cannot associate such payment with any  
6 outstanding tax liability of such taxpayer, the Secretary  
7 shall make reasonable efforts to notify the taxpayer of  
8 such inability within 60 days after the receipt of such  
9 payment.

10 **SEC. 1095. UNAUTHORIZED ENTICEMENT OF INFORMATION**  
11 **DISCLOSURE.**

12 (a) IN GENERAL.—Subchapter B of chapter 76 (re-  
13 lating to proceedings by taxpayers and third parties), as  
14 amended by section 1062(a), is amended by redesignating  
15 section 7435 as section 7436 and by inserting after sec-  
16 tion 7434 the following new section:

17 **"SEC. 7435. CIVIL DAMAGES FOR UNAUTHORIZED ENTICE-**  
18 **MENT OF INFORMATION DISCLOSURE.**

19 "(a) IN GENERAL.—If any officer or employee of the  
20 United States intentionally compromises the determina-  
21 tion or collection of any tax due from an attorney, certified  
22 public accountant, or enrolled agent representing a tax-  
23 payer in exchange for information conveyed by the tax-  
24 payer to the attorney, certified public accountant, or en-  
25 rolled agent for purposes of obtaining advice concerning  
26 the taxpayer's tax liability, such taxpayer may bring a civil

1 action for damages against the United States in a district  
2 court of the United States. Such civil action shall be the  
3 exclusive remedy for recovering damages resulting from  
4 such actions.

5 “(b) DAMAGES.—In any action brought under sub-  
6 section (a), upon a finding of liability on the part of the  
7 defendant, the defendant shall be liable to the plaintiff in  
8 an amount equal to the lesser of \$500,000 or the sum  
9 of—

10 “(1) actual, direct economic damages sustained  
11 by the plaintiff as a proximate result of the informa-  
12 tion disclosure, and

13 “(2) the costs of the action.

14 Damages shall not include the taxpayer’s liability for any  
15 civil or criminal penalties, or other losses attributable to  
16 incarceration or the imposition of other criminal sanctions.

17 “(c) PAYMENT AUTHORITY.—Claims pursuant to  
18 this section shall be payable out of funds appropriated  
19 under section 1304 of title 31, United States Code.

20 “(d) PERIOD FOR BRINGING ACTION.—Notwith-  
21 standing any other provision of law, an action to enforce  
22 liability created under this section may be brought without  
23 regard to the amount in controversy and may be brought  
24 only within 2 years after the date the actions creating such

1 liability would have been discovered by exercise of reason-  
2 able care.

3       “(e) MANDATORY STAY.—Upon a certification by the  
4 Commissioner or the Commissioner’s delegate that there  
5 is an ongoing investigation or prosecution of the taxpayer,  
6 the district court before which an action under this section  
7 is pending, shall stay all proceedings with respect to such  
8 action pending the conclusion of the investigation or  
9 prosecution.

10       “(f) CRIME-FRAUD EXCEPTION.—Subsection (a)  
11 shall not apply to information conveyed to an attorney,  
12 certified public accountant, or enrolled agent for the pur-  
13 pose of perpetrating a fraud or crime.”

14       (b) CLERICAL AMENDMENT.—The table of sections  
15 for subchapter B of chapter 76, as amended by section  
16 1062(b), is amended by striking the item relating to sec-  
17 tion 7435 and by adding at the end the following new  
18 items:

“Sec. 7435. Civil damages for unauthorized enticement of infor-  
mation disclosure.

“Sec. 7436. Cross references.”

19       (c) EFFECTIVE DATE.—The amendments made by  
20 this section shall apply to actions after the date of the  
21 enactment of this Act.

1       **Subtitle J—Form Modifications;**  
2                               **Studies**

3       **SEC. 1100. DEFINITIONS.**

4       For purposes of this subtitle:

5               (1) **SECRETARY.**—The term “Secretary” means  
6       the Secretary of the Treasury or his delegate.

7               (2) **1986 CODE.**—The term “1986 Code”  
8       means the Internal Revenue Code of 1986.

9               (3) **TAX-WRITING COMMITTEES.**—The term  
10       “tax-writing Committees” means the Committee on  
11       Ways and Means of the House of Representatives  
12       and the Committee on Finance of the Senate.

13       **CHAPTER 1—FORM MODIFICATIONS**

14       **SEC. 1101. EXPLANATION OF CERTAIN PROVISIONS.**

15       (a) **GENERAL RULE.**—The Secretary shall take such  
16       actions as may be appropriate to ensure that taxpayers  
17       are aware of the provisions of the 1986 Code permitting  
18       payment of tax in installments, extensions of time for pay-  
19       ment of tax, and compromises of tax liability. Such actions  
20       shall include revising the instructions for filing income tax  
21       returns so that such instructions include an explanation  
22       of—

23               (1) the procedures for requesting the benefits of  
24       such provisions, and



1                                   **CHAPTER 2—STUDIES**

2   **SEC. 1111. PILOT PROGRAM FOR APPEAL OF ENFORCE-**  
3                                   **MENT ACTIONS.**

4           (a) **GENERAL RULE.**—The Secretary shall establish  
5 a 1-year pilot program for appeals of enforcement actions  
6 (including lien, levy, and seizure actions) to the Appeals  
7 Division of the Internal Revenue Service—

8                   (1) where the deficiency was assessed without  
9                   actual knowledge of the taxpayer,

10                   (2) where the deficiency was assessed without  
11                   an opportunity for administrative appeal, and

12                   (3) in other appropriate circumstances.

13           (b) **REPORT.**—Not later than June 30, 1997, the  
14 Secretary shall submit to the tax-writing Committees a re-  
15 port on the pilot program established under subsection (a),  
16 together with such recommendations as he may deem  
17 advisable.

18   **SEC. 1112. STUDY ON TAXPAYERS WITH SPECIAL NEEDS.**

19           (a) **GENERAL RULE.**—The Secretary shall conduct a  
20 study on ways to assist the elderly, physically impaired,  
21 foreign-language speaking, and other taxpayers with spe-  
22 cial needs to comply with the internal revenue laws.

23           (b) **REPORT.**—Not later than June 30, 1996, the  
24 Secretary shall submit to the tax-writing Committees a re-

1 port on the study conducted under subsection (a), together  
 2 with such recommendations as he may deem advisable.

3 **SEC. 1113. REPORTS ON TAXPAYER-RIGHTS EDUCATION**  
 4 **PROGRAM.**

5 Not later than April 1, 1996, the Secretary shall sub-  
 6 mit a report to the tax-writing Committees on the scope  
 7 and content of the Internal Revenue Service's taxpayer-  
 8 rights education program for its officers and employees.  
 9 Not later than June 30, 1996, the Secretary shall submit  
 10 a report to the tax-writing Committees on the effectiveness  
 11 of the program referred to in the preceding sentence.

12 **SEC. 1114. BIENNIAL REPORTS ON MISCONDUCT BY INTER-**  
 13 **NAL REVENUE SERVICE EMPLOYEES.**

14 Not later than June 30, 1996, and during June of  
 15 each second calendar year thereafter, the Secretary shall  
 16 report to the tax-writing Committees on all cases involving  
 17 complaints about misconduct of Internal Revenue Service  
 18 employees and the disposition of such complaints.

19 **SEC. 1115. STUDY OF NOTICES OF DEFICIENCY.**

20 (a) GENERAL RULE.—The Comptroller General shall  
 21 conduct a study on—

22 (1) the effectiveness of current Internal Reve-  
 23 nue Service efforts to notify taxpayers with regard  
 24 to tax deficiencies under section 6212 of the 1986  
 25 Code,

1           (2) the number of registered or certified letters  
2           and other notices returned to the Internal Revenue  
3           Service as undeliverable,

4           (3) any followup action taken by the Internal  
5           Revenue Service to locate taxpayers who did not re-  
6           ceive actual notice,

7           (4) the effect that failures to receive notice of  
8           such deficiencies have on taxpayers, and

9           (5) recommendations to improve Internal Reve-  
10          nue Service notification of taxpayers.

11         (b) REPORT.—Not later than June 30, 1996, the  
12         Comptroller General shall submit to the tax-writing Com-  
13         mittees a report on the study conducted under subsection  
14         (a), together with such recommendations as he may deem  
15         advisable.

16         **SEC. 1116. NOTICE AND FORM ACCURACY STUDY.**

17         (a) GENERAL RULE.—The Comptroller General shall  
18         conduct annual studies of the accuracy of 25 of the most  
19         commonly used Internal Revenue Service forms, notices,  
20         and publications. In conducting any such study, the Comp-  
21         troller General shall examine the suitability and usefulness  
22         of Internal Revenue Service telephone numbers on Inter-  
23         nal Revenue Service notices and shall solicit and consider  
24         the comments of organizations representing taxpayers,  
25         employers, and tax professionals.

1 (b) REPORTS.—The Comptroller General shall sub-  
2 mit to the tax-writing Committees a report on each study  
3 conducted under subsection (a), together with such rec-  
4 ommendations as he may deem advisable. The first such  
5 report shall be submitted not later than June 30, 1996.

6 **TITLE II—INCREASE OF DEDUC-**  
7 **TION FOR HEALTH INSUR-**  
8 **ANCE COSTS OF SELF-EM-**  
9 **PLOYED INDIVIDUALS**

10 **SEC. 2001. INCREASE OF DEDUCTION FOR HEALTH INSUR-**  
11 **ANCE COSTS OF SELF-EMPLOYED INDIVID-**  
12 **UALS.**

13 (a) INCREASE IN DEDUCTION.—Section 162(l) is  
14 amended—

15 (1) by striking “30 percent” in paragraph (1)  
16 and inserting “the applicable percentage”, and

17 (2) by adding at the end the following new  
18 paragraph:

19 “(6) APPLICABLE PERCENTAGE.—For purposes  
20 of paragraph (1), the applicable percentage shall be  
21 determined as follows:

<b>“For taxable years beginning in:</b>	<b>The applicable percentage is:</b>
1996 .....	75
1997 and thereafter .....	100.”

1 (b) EFFECTIVE DATE.—The amendments made by  
 2 this section shall apply to taxable years beginning after  
 3 December 31, 1995.

4 **TITLE III—S CORPORATION**  
 5 **REFORM ACT OF 1995**

6 **SEC. 3001. SHORT TITLE.**

7 This title may be cited as the “S Corporation Reform  
 8 Act of 1995”.

9 **Subtitle A—Eligible Shareholders**  
 10 **of S Corporation**

11 **CHAPTER 1—NUMBER OF SHAREHOLDERS**

12 **SEC. 3101. S CORPORATIONS PERMITTED TO HAVE 50**  
 13 **SHAREHOLDERS.**

14 Subparagraph (A) of section 1361(b)(1) (defining  
 15 small business corporation) is amended by striking “35  
 16 shareholders” and inserting “50 shareholders”.

17 **SEC. 3102. MEMBERS OF FAMILY TREATED AS 1 SHARE-**  
 18 **HOLDER.**

19 Paragraph (1) of section 1361(c) (relating to special  
 20 rules for applying subsection (b)) is amended to read as  
 21 follows:

22 “(1) MEMBERS OF FAMILY TREATED AS 1  
 23 SHAREHOLDER.—

24 “(A) IN GENERAL.—For purposes of sub-  
 25 section (b)(1)(A)—

1           “(i) except as provided in clause (ii),  
2           a husband and wife (and their estates)  
3           shall be treated as 1 shareholder, and

4           “(ii) in the case of a family with re-  
5           spect to which an election is in effect  
6           under subparagraph (E), all members of  
7           the family shall be treated as 1 share-  
8           holder.

9           “(B) MEMBERS OF THE FAMILY.—For  
10          purposes of subparagraph (A)(ii), the term  
11          ‘members of the family’ means the lineal de-  
12          scendants of the common ancestor and the  
13          spouses (or former spouses) of such lineal de-  
14          scendants or common ancestor.

15          “(C) COMMON ANCESTOR.—For purposes  
16          of this paragraph, an individual shall not be  
17          considered a common ancestor if, as of the later  
18          of the effective date of this paragraph or the  
19          time the election under section 1362(a) is  
20          made, the individual is more than 6 generations  
21          removed from the youngest generation of share-  
22          holders.

23          “(D) EFFECT OF ADOPTION, ETC.—In de-  
24          termining whether any relationship specified in

1           subparagraph (B) or (C) exists, the rules of  
2           section 152(b)(2) shall apply.

3           “(E) ELECTION.—An election under sub-  
4           paragraph (A)(ii)—

5                   “(i) must be made with the consent of  
6                   all shareholders,

7                   “(ii) shall remain in effect until termi-  
8                   nated, and

9                   “(iii) shall apply only with respect to  
10                  1 family in any corporation.”

11           **CHAPTER 2—PERSONS ALLOWED AS**  
12           **SHAREHOLDERS**

13   **SEC. 3111. CERTAIN EXEMPT ORGANIZATIONS.**

14           (a) CERTAIN EXEMPT ORGANIZATIONS ALLOWED TO  
15   BE SHAREHOLDERS.—

16                   (1) IN GENERAL.—Subparagraph (B) of section  
17           1361(b)(1) (defining small business corporation) is  
18           amended to read as follows:

19                           “(B) have as a shareholder a person (other  
20                           than an estate, a trust described in subsection  
21                           (c)(2), or an organization described in sub-  
22                           section (c)(7)) who is not an individual.”.

23                   (2) ELIGIBLE EXEMPT ORGANIZATIONS.—Sec-  
24           tion 1361(c) (relating to special rules for applying

1 subsection (b)) is amended by adding at the end the  
2 following new paragraph:

3 “(7) CERTAIN EXEMPT ORGANIZATIONS PER-  
4 MITTED AS SHAREHOLDERS.—For purposes of sub-  
5 section (b)(1)(B), an organization described in sec-  
6 tion 401(a) or 501(c)(3) may be a shareholder in an  
7 S corporation.”

8 (b) CONTRIBUTIONS OF S CORPORATION STOCK.—  
9 Section 170(e)(1) (relating to certain contributions of or-  
10 dinary income and capital gain property) is amended by  
11 adding at the end the following sentence: “For purposes  
12 of applying this paragraph in the case of a charitable con-  
13 tribution of stock in an S corporation, rules similar to the  
14 rules of section 751 shall apply in determining whether  
15 gain on such stock would have been long-term capital gain  
16 if such stock were sold by the taxpayer.”

17 (c) SPECIAL RULES APPLICABLE TO PARTNERSHIPS  
18 AND S CORPORATIONS.—

19 (1) IN GENERAL.—Subsection (c) of section  
20 512 (relating to unrelated business tax income) is  
21 amended—

22 (A) by inserting “or S corporation” after  
23 “partnership” each place it appears in para-  
24 graphs (1) and (3),

1 (B) by inserting “or shareholder” after  
2 “member” in paragraph (1), and

3 (C) by inserting “AND S CORPORATIONS”  
4 after “PARTNERSHIPS” in the heading.

5 (2) REPORTING REQUIREMENT.—Section 6037  
6 (relating to return of S corporation) is amended by  
7 adding at the end the following new subsection:

8 “(c) SEPARATE STATEMENT OF ITEMS OF UNRE-  
9 LATED BUSINESS TAXABLE INCOME.—In the case of any  
10 S corporation regularly carrying on a trade or business  
11 (within the meaning of section 512(c)(1)), the information  
12 required under subsection (b) to be furnished to any  
13 shareholder described in section 1361(c)(7) shall include  
14 such information as is necessary to enable the shareholder  
15 to compute its pro rata share of the corporation’s income  
16 or loss from the trade or business in accordance with sec-  
17 tion 512(a)(1), but without regard to the modifications de-  
18 scribed in paragraphs (8) through (15) of section 512(b).”

19 **SEC. 3112. FINANCIAL INSTITUTIONS.**

20 Subparagraph (B) of section 1361(b)(2) (defining in-  
21 eligible corporation) is amended to read as follows:

22 “(B) a financial institution which uses the  
23 reserve method of accounting for bad debts de-  
24 scribed in section 585 or 593,”.

1 **SEC. 3113. NONRESIDENT ALIENS.**

2 (a) NONRESIDENT ALIENS ALLOWED TO BE SHARE-  
3 HOLDERS.—

4 (1) IN GENERAL.—Paragraph (1) of section  
5 1361(b) (defining small business corporation) is  
6 amended—

7 (A) by adding “and” at the end of sub-  
8 paragraph (B),

9 (B) by striking subparagraph (C), and

10 (C) by redesignating subparagraph (D) as  
11 subparagraph (C).

12 (2) CONFORMING AMENDMENTS.—Paragraphs  
13 (4) and (5)(A) of section 1361(e) (relating to special  
14 rules for applying subsection (b)) are each amended  
15 by striking “subsection (b)(1)(D)” and inserting  
16 “subsection (b)(1)(C)”.

17 (b) NONRESIDENT ALIEN SHAREHOLDER TREATED  
18 AS ENGAGED IN TRADE OR BUSINESS WITHIN UNITED  
19 STATES.—

20 (1) IN GENERAL.—Section 875 is amended—

21 (A) by striking “and” at the end of para-  
22 graph (1),

23 (B) by striking the period at the end of  
24 paragraph (2) and inserting “, and”, and

25 (C) by adding at the end the following new  
26 paragraph:

1           “(3) a nonresident alien individual shall be con-  
2           sidered as being engaged in a trade or business  
3           within the United States if the S corporation of  
4           which such individual is a shareholder is so en-  
5           gaged.”

6           (2) APPLICATION OF WITHHOLDING TAX ON  
7           NONRESIDENT ALIEN SHAREHOLDERS.—Section  
8           1446 (relating to withholding tax on foreign part-  
9           ners’ share of effectively connected income) is  
10          amended by redesignating subsection (f) as sub-  
11          section (g) and by inserting after subsection (e) the  
12          following new subsection:

13          “(f) S CORPORATION TREATED AS PARTNERSHIP,  
14          ETC.—For purposes of this section—

15                 “(1) an S corporation shall be treated as a  
16                 partnership,

17                 “(2) the shareholders of such corporation shall  
18                 be treated as partners of such partnership, and

19                 “(3) any reference to section 704 shall be treat-  
20                 ed as a reference to section 1366.”

21          (3) CONFORMING AMENDMENTS.—

22                 (A) The heading of section 875 is amended  
23                 to read as follows:

1 **“SEC. 875. PARTNERSHIPS; BENEFICIARIES OF ESTATES**  
 2 **AND TRUSTS; S CORPORATIONS.”**

3 (B) The heading of section 1446 is amend-  
 4 ed to read as follows:

5 **“SEC. 1446. WITHHOLDING TAX ON FOREIGN PARTNERS’**  
 6 **AND S CORPORATE SHAREHOLDERS’ SHARE**  
 7 **OF EFFECTIVELY CONNECTED INCOME.”**

8 (4) CLERICAL AMENDMENTS.—

9 (A) The item relating to section 875 in the  
 10 table of sections for subpart A of part II of  
 11 subchapter N of chapter 1 is amended to read  
 12 as follows:

“Sec. 875. Partnerships; beneficiaries of estates and trusts; S corporations.”

13 (B) The item relating to section 1446 in  
 14 the table of sections for subchapter A of chap-  
 15 ter 3 is amended to read as follows:

“Sec. 1446. Withholding tax on foreign partners’ and S corporate shareholders’  
 share of effectively connected income.”

16 (c) PERMANENT ESTABLISHMENT OF PARTNERS  
 17 AND S CORPORATION SHAREHOLDERS.—Section 894 (re-  
 18 lating to income affected by treaty) is amended by adding  
 19 at the end the following new subsection:

20 “(c) PERMANENT ESTABLISHMENT OF PARTNERS  
 21 AND S CORPORATION SHAREHOLDERS.—If a partnership  
 22 or S corporation has a permanent establishment in the  
 23 United States (within the meaning of a treaty to which

1 the United States is a party) at any time during a taxable  
2 year of such entity, a nonresident alien individual or for-  
3 eign corporation which is a partner in such partnership,  
4 or a nonresident alien individual who is a shareholder in  
5 such S corporation, shall be treated as having a permanent  
6 establishment in the United States for purposes of such  
7 treaty.”

8 **SEC. 3114. ELECTING SMALL BUSINESS TRUSTS.**

9 (a) GENERAL RULE.—Subparagraph (A) of section  
10 1361(c)(2) (relating to certain trusts permitted as share-  
11 holders) is amended by inserting after clause (iv) the fol-  
12 lowing new clause:

13 “(v) An electing small business trust.”

14 (b) CURRENT BENEFICIARIES TREATED AS SHARE-  
15 HOLDERS.—Subparagraph (B) of section 1361(c)(2) is  
16 amended by adding at the end the following new clause:

17 “(v) In the case of a trust described  
18 in clause (v) of subparagraph (A), each po-  
19 tential current beneficiary of such trust  
20 shall be treated as a shareholder; except  
21 that, if for any period there is no potential  
22 current beneficiary of such trust, such  
23 trust shall be treated as the shareholder  
24 during such period.”

1           (c) ELECTING SMALL BUSINESS TRUST DEFINED.—  
2 Section 1361 (defining S corporation) is amended by add-  
3 ing at the end the following new subsection:

4           “(e) ELECTING SMALL BUSINESS TRUST DE-  
5 FINED.—

6                   “(1) ELECTING SMALL BUSINESS TRUST.—For  
7 purposes of this section—

8                           “(A) IN GENERAL.—Except as provided in  
9 subparagraph (B), the term ‘electing small  
10 business trust’ means any trust if—

11                                   “(i) such trust does not have as a  
12 beneficiary any person other than an indi-  
13 vidual, an estate, or an organization de-  
14 scribed in section 401(a) or 501(c)(3),

15                                   “(ii) no interest in such trust was ac-  
16 quired by purchase, and

17                                   “(iii) an election under this subsection  
18 applies to such trust.

19                           “(B) CERTAIN TRUSTS NOT ELIGIBLE.—  
20 The term ‘electing small business trust’ shall  
21 not include—

22                                   “(i) any qualified subchapter S trust  
23 (as defined in subsection (d)(3)) if an elec-  
24 tion under subsection (d)(2) applies to any

1 corporation the stock of which is held by  
2 such trust, and

3 “(ii) any trust exempt from tax under  
4 this subtitle.

5 “(C) PURCHASE.—For purposes of sub-  
6 paragraph (A), the term ‘purchase’ means any  
7 acquisition if the basis of the property acquired  
8 is determined under section 1012.

9 “(2) POTENTIAL CURRENT BENEFICIARY.—For  
10 purposes of this section, the term ‘potential current  
11 beneficiary’ means, with respect to any period, any  
12 person who at any time during such period is enti-  
13 tled to, or at the discretion of any person may re-  
14 ceive, a distribution from the principal or income of  
15 the trust. If a trust disposes of all of the stock which  
16 it holds in an S corporation, then, with respect to  
17 such corporation, the term ‘potential current bene-  
18 ficiary’ does not include any person who first met  
19 the requirements of the preceding sentence during  
20 the 60-day period ending on the date of such dis-  
21 position.

22 “(3) ELECTION.—An election under this sub-  
23 section shall be made by the trustee in such manner  
24 and form, and at such time, as the Secretary may  
25 prescribe. Any such election shall apply to the tax-

1       able year of the trust for which made and all subse-  
 2       quent taxable years of such trust unless revoked  
 3       with the consent of the Secretary.

4               “(4) CROSS REFERENCE.—

**“For special treatment of electing small business trusts, see section 641(d).”**

5       (d) TAXATION OF ELECTING SMALL BUSINESS  
 6 TRUSTS.—Section 641 (relating to imposition of tax on  
 7 trusts) is amended by adding at the end the following new  
 8 subsection:

9               “(d) SPECIAL RULES FOR TAXATION OF ELECTING  
 10 SMALL BUSINESS TRUSTS.—

11               “(1) IN GENERAL.—For purposes of this chap-  
 12 ter—

13                       “(A) the portion of any electing small busi-  
 14 ness trust which consists of stock in 1 or more  
 15 S corporations shall be treated as a separate  
 16 trust, and

17                       “(B) the amount of the tax imposed by  
 18 this chapter on such separate trust shall be de-  
 19 termined with the modifications of paragraph  
 20 (2).

21               “(2) MODIFICATIONS.—For purposes of para-  
 22 graph (1), the modifications of this paragraph are  
 23 the following:

1           “(A) Except as provided in section 1(h),  
2 the amount of the tax imposed by section 1(e)  
3 shall be determined by using the highest rate of  
4 tax set forth in section 1(e).

5           “(B) The exemption amount under section  
6 55(d) shall be zero.

7           “(C) The only items of income, loss, deduc-  
8 tion, or credit to be taken into account are the  
9 following:

10                   “(i) The items required to be taken  
11 into account under section 1366.

12                   “(ii) Any gain or loss from the dis-  
13 position of stock in an S corporation.

14                   “(iii) To the extent provided in regu-  
15 lations, State or local income taxes or ad-  
16 ministrative expenses to the extent alloca-  
17 ble to items described in clauses (i) and  
18 (ii).

19 No deduction or credit shall be allowed for any  
20 amount not described in this paragraph, and no  
21 item described in this paragraph shall be appor-  
22 tioned to any beneficiary.

23           “(D) No amount shall be allowed under  
24 paragraph (1) or (2) of section 1211(b).

1           “(3) TREATMENT OF REMAINDER OF TRUST  
2           AND DISTRIBUTIONS.—For purposes of determin-  
3           ing—

4                   “(A) the amount of the tax imposed by  
5                   this chapter on the portion of any electing small  
6                   business trust not treated as a separate trust  
7                   under paragraph (1), and

8                   “(B) the distributable net income of the  
9                   entire trust,

10           the items referred to in paragraph (2)(C) shall be  
11           excluded. Except as provided in the preceding sen-  
12           tence, this subsection shall not affect the taxation of  
13           any distribution from the trust.

14           “(4) TREATMENT OF UNUSED DEDUCTIONS  
15           WHERE TERMINATION OF SEPARATE TRUST.—If a  
16           portion of an electing small business trust ceases to  
17           be treated as a separate trust under paragraph (1),  
18           any carryover or excess deduction of the separate  
19           trust which is referred to in section 642(h) shall be  
20           taken into account by the entire trust.

21           “(5) ELECTING SMALL BUSINESS TRUST.—For  
22           purposes of this subsection, the term ‘electing small  
23           business trust’ has the meaning given such term by  
24           section 1361(e)(1).”

1           **CHAPTER 3—OTHER PROVISIONS**

2   **SEC. 3121. EXPANSION OF POST-DEATH QUALIFICATION**  
 3                           **FOR CERTAIN TRUSTS.**

4           Subparagraph (A) of section 1361(e)(2) (relating to  
 5 certain trusts permitted as shareholders) is amended—

6                   (1) by striking “60-day period” each place it  
 7           appears in clauses (ii) and (iii) and inserting “2-year  
 8           period”, and

9                   (2) by striking the last sentence in clause (ii).

10 **Subtitle B—Qualification and Eligibility**  
 11 **Requirements for S Cor-**  
 12 **porations**

13           **CHAPTER 1—ONE CLASS OF STOCK**

14 **SEC. 3201. ISSUANCE OF PREFERRED STOCK PERMITTED.**

15           (a) **IN GENERAL.**—Section 1361(c), as amended by  
 16 section 3111(a)(2), is amended by adding at the end the  
 17 following new paragraph:

18                   “(8) **TREATMENT OF QUALIFIED PREFERRED**  
 19           **STOCK.**—

20                           “(A) **IN GENERAL.**—Notwithstanding sub-  
 21           section (b)(1)(D), an S corporation may issue  
 22           qualified preferred stock.

23                           “(B) **QUALIFIED PREFERRED STOCK DE-**  
 24           **FINED.**—For purposes of this paragraph, the  
 25           term ‘qualified preferred stock’ means stock de-

1           scribed in section 1504(a)(4) which is issued to  
2           a person eligible to hold common stock of an S  
3           corporation.

4           “(C) DISTRIBUTIONS.—A distribution (not  
5           in part or full payment in exchange for stock)  
6           made by the corporation with respect to quali-  
7           fied preferred stock shall be includible as inter-  
8           est income of the holder and deductible to the  
9           corporation as interest expense in computing  
10          taxable income under section 1363(b) in the  
11          year such distribution is received.”

12          (b) CONFORMING AMENDMENTS.—

13           (1) Subparagraph (C) of section 1361(b)(1), as  
14           redesignated by section 3113(a)(1)(C), is amended  
15           by inserting “except as provided in paragraph (8),”  
16           before “have”.

17           (2) Subsection (a) of section 1366 is amended  
18           by adding at the end the following new paragraph:

19           “(3) ALLOCATION WITH RESPECT TO QUALI-  
20           FIED PREFERRED STOCK.—The holders of qualified  
21           preferred stock shall not, with respect to such stock,  
22           be allocated any of the items described in paragraph  
23           (1).”

1 **SEC. 3202. FINANCIAL INSTITUTIONS PERMITTED TO HOLD**  
2 **SAFE HARBOR DEBT.**

3 Subparagraph (B) of section 1361(e)(5) (defining  
4 straight debt) is amended by adding “and” at the end of  
5 clause (i) and by striking clauses (ii) and (iii) and insert-  
6 ing the following:

7 “(ii) in any case in which the terms of  
8 such promise include a provision under  
9 which the obligation to pay may be con-  
10 verted (directly or indirectly) into stock of  
11 the corporation, such terms, taken as a  
12 whole, are substantially the same as the  
13 terms which could have been obtained on  
14 the effective date of the promise from a  
15 person which is not a related person (with-  
16 in the meaning of section 465(b)(3)(C)) to  
17 the S corporation or its shareholders, and

18 “(iii) the creditor is—

19 “(I) an individual,

20 “(II) an estate,

21 “(III) a trust described in para-  
22 graph (2), or

23 “(IV) a person which is actively  
24 and regularly engaged in the business  
25 of lending money.”

1                   **CHAPTER 2—ELECTIONS AND**  
2                   **TERMINATIONS**

3 **SEC. 3211. RULES RELATING TO INADVERTENT TERMI-**  
4                   **NATIONS AND INVALID ELECTIONS.**

5           (a) GENERAL RULE.—Subsection (f) of section 1362  
6 (relating to inadvertent terminations) is amended to read  
7 as follows:

8           “(f) INADVERTENT INVALID ELECTIONS OR TERMI-  
9 NATIONS.—If—

10                   “(1) an election under subsection (a) by any  
11 corporation—

12                           “(A) was not effective for the taxable year  
13 for which made (determined without regard to  
14 subsection (b)(2)) by reason of a failure to meet  
15 the requirements of section 1361(b) or to ob-  
16 tain shareholder consents, or

17                           “(B) was terminated under paragraph (2)  
18 of subsection (d),

19                   “(2) the Secretary determines that the cir-  
20 cumstances resulting in such ineffectiveness or ter-  
21 mination were inadvertent,

22                   “(3) no later than a reasonable period of time  
23 after discovery of the circumstances resulting in  
24 such ineffectiveness or termination, steps were  
25 taken—

1           “(A) so that the corporation is a small  
2           business corporation, or

3           “(B) to acquire the required shareholder  
4           consents, and

5           “(4) the corporation, and each person who was  
6           a shareholder in the corporation at any time during  
7           the period specified pursuant to this subsection,  
8           agrees to make such adjustments (consistent with  
9           the treatment of the corporation as an S corpora-  
10          tion) as may be required by the Secretary with re-  
11          spect to such period,

12 then, notwithstanding the circumstances resulting in such  
13 ineffectiveness or termination, such corporation shall be  
14 treated as an S corporation during the period specified  
15 by the Secretary.”

16          (b) LATE ELECTIONS.—Subsection (b) of section  
17 1362 is amended by adding at the end the following new  
18 paragraph:

19           “(5) AUTHORITY TO TREAT LATE ELECTIONS  
20          AS TIMELY.—If—

21           “(A) an election under subsection (a) is  
22           made for any taxable year (determined without  
23           regard to paragraph (3)) after the date pre-  
24           scribed by this subsection for making such elec-  
25           tion for such taxable year, and

1           “(B) the Secretary determines that there  
2           was reasonable cause for the failure to timely  
3           make such election,  
4           the Secretary may treat such election as timely  
5           made for such taxable year (and paragraph (3) shall  
6           not apply).”

7           (c) **AUTOMATIC WAIVERS.**—The Secretary of the  
8           Treasury shall provide for an automatic waiver procedure  
9           under section 1362(f) of the Internal Revenue Code of  
10          1986 in cases in which the Secretary determines appro-  
11          prium.

12          (d) **EFFECTIVE DATE.**—The amendments made by  
13          subsection (a) and (b) shall apply with respect to elections  
14          for taxable years beginning after December 31, 1982.

15          **SEC. 3212. AGREEMENT TO TERMINATE YEAR.**

16          Paragraph (2) of section 1377(a) (relating to pro  
17          rata share) is amended to read as follows:

18                  “(2) **ELECTION TO TERMINATE YEAR.**—

19                          “(A) **IN GENERAL.**—Under regulations  
20                          prescribed by the Secretary, if any shareholder  
21                          terminates the shareholder’s interest in the cor-  
22                          poration during the taxable year and all af-  
23                          fected shareholders agree to the application of  
24                          this paragraph, paragraph (1) shall be applied  
25                          to the affected shareholders as if the taxable

1 year consisted of 2 taxable years the first of  
2 which ends on the date of the termination.

3 “(B) AFFECTED SHAREHOLDERS.—For  
4 purposes of subparagraph (A), the term ‘af-  
5 fected shareholders’ means the shareholder  
6 whose interest is terminated and all sharehold-  
7 ers to whom such shareholder has transferred  
8 shares during the taxable year. If such share-  
9 holder has transferred shares to the corpora-  
10 tion, the term ‘affected shareholders’ shall in-  
11 clude all persons who are shareholders during  
12 the taxable year.”

13 **SEC. 3213. EXPANSION OF POST-TERMINATION TRANSITION**  
14 **PERIOD.**

15 (a) IN GENERAL.—Paragraph (1) of section 1377(b)  
16 (relating to post-termination transition period) is amended  
17 by striking “and” at the end of subparagraph (A), by re-  
18 designating subparagraph (B) as subparagraph (C), and  
19 by inserting after subparagraph (A) the following new sub-  
20 paragraph:

21 “(B) the 120-day period beginning on the  
22 date of any determination pursuant to an audit  
23 of the taxpayer which follows the termination of  
24 the corporation’s election and which adjusts a  
25 subchapter S item of income, loss, or deduction

1           of the corporation arising during the S period  
2           (as defined in section 1368(e)(2)), and”.

3           (b) DETERMINATION DEFINED.—Paragraph (2) of  
4 section 1377(b) is amended by striking subparagraphs (A)  
5 and (B), by redesignating subparagraph (C) as subpara-  
6 graph (B), and by inserting before subparagraph (B) (as  
7 so redesignated) the following new subparagraph:

8                   “(A) a determination as defined in section  
9                   1313(a), or”.

10          (c) REPEAL OF SPECIAL AUDIT PROVISIONS FOR  
11 SUBCHAPTER S ITEMS.—

12           (1) GENERAL RULE.—Subchapter D of chapter  
13          63 (relating to tax treatment of subchapter S items)  
14          is hereby repealed.

15           (2) CONSISTENT TREATMENT REQUIRED.—Sec-  
16          tion 6037 (relating to return of S corporation), as  
17          amended by section 3111(c)(2), is amended by add-  
18          ing at the end the following new subsection:

19                   “(d) SHAREHOLDER’S RETURN MUST BE CONSIST-  
20 ENT WITH CORPORATE RETURN OR SECRETARY NOTI-  
21 FIED OF INCONSISTENCY.—

22                   “(1) IN GENERAL.—A shareholder of an S cor-  
23          poration shall, on such shareholder’s return, treat a  
24          subchapter S item in a manner which is consistent

1 with the treatment of such item on the corporate  
2 return.

3 “(2) NOTIFICATION OF INCONSISTENT TREAT-  
4 MENT.—

5 “(A) IN GENERAL.—In the case of any  
6 subchapter S item, if—

7 “(i)(I) the corporation has filed a re-  
8 turn but the shareholder’s treatment on  
9 his return is (or may be) inconsistent with  
10 the treatment of the item on the corporate  
11 return, or

12 “(II) the corporation has not filed a  
13 return, and

14 “(ii) the shareholder files with the  
15 Secretary a statement identifying the in-  
16 consistency,

17 paragraph (1) shall not apply to such item.

18 “(B) SHAREHOLDER RECEIVING INCOR-  
19 RECT INFORMATION.—A shareholder shall be  
20 treated as having complied with clause (ii) of  
21 subparagraph (A) with respect to a subchapter  
22 S item if the shareholder—

23 “(i) demonstrates to the satisfaction  
24 of the Secretary that the treatment of the  
25 subchapter S item on the shareholder’s re-

1                   turn is consistent with the treatment of the  
2                   item on the schedule furnished to the  
3                   shareholder by the corporation, and

4                   “(ii) elects to have this paragraph  
5                   apply with respect to that item.

6                   “(3) EFFECT OF FAILURE TO NOTIFY.—In any  
7                   case—

8                   “(A) described in subparagraph (A)(i)(I)  
9                   of paragraph (2), and

10                   “(B) in which the shareholder does not  
11                   comply with subparagraph (A)(ii) of paragraph  
12                   (2),

13                   any adjustment required to make the treatment of  
14                   the items by such shareholder consistent with the  
15                   treatment of the items on the corporate return shall  
16                   be treated as arising out of mathematical or clerical  
17                   errors and assessed according to section 6213(b)(1).  
18                   Paragraph (2) of section 6213(b) shall not apply to  
19                   any assessment referred to in the preceding sen-  
20                   tence.

21                   “(4) SUBCHAPTER S ITEM.—For purposes of  
22                   this subsection, the term ‘subchapter S item’ means  
23                   any item of an S corporation to the extent that reg-  
24                   ulations prescribed by the Secretary provide that, for  
25                   purposes of this subtitle, such item is more appro-

1 priately determined at the corporation level than at  
 2 the shareholder level.

3 “(5) ADDITION TO TAX FOR FAILURE TO COM-  
 4 PLY WITH SECTION.—

“For addition to tax in the case of a shareholder’s  
 negligence in connection with, or disregard of, the  
 requirements of this section, see part II of sub-  
 chapter A of chapter 68.”

5 (3) CONFORMING AMENDMENTS.—

6 (A) Section 1366 is amended by striking  
 7 subsection (g).

8 (B) Subsection (b) of section 6233 is  
 9 amended to read as follows:

10 “(b) SIMILAR RULES IN CERTAIN CASES.—If a part-  
 11 nership return is filed for any taxable year but it is deter-  
 12 mined that there is no entity for such taxable year, to the  
 13 extent provided in regulations, rules similar to the rules  
 14 of subsection (a) shall apply.”

15 (C) The table of subchapters for chapter  
 16 63 is amended by striking the item relating to  
 17 subchapter D.

18 **SEC. 3214. REPEAL OF EXCESSIVE PASSIVE INVESTMENT**  
 19 **INCOME AS A TERMINATION EVENT.**

20 (a) IN GENERAL.—Section 1362(d) (relating to ter-  
 21 mination) is amended by striking paragraph (3).

22 (b) MODIFICATION OF TAX IMPOSED ON EXCESSIVE  
 23 PASSIVE INVESTMENT INCOME.—

1           (1) INCREASE IN THRESHOLD.—Subsections  
 2           (a)(2) and (b)(1)(A)(i) of section 1375 (relating to  
 3           tax imposed when passive investment income of a  
 4           corporation having subchapter C earnings and prof-  
 5           its exceeds 25 percent of gross receipts) are each  
 6           amended by striking “25 percent” and inserting “50  
 7           percent”.

8           (2) TAX RATE INCREASE AFTER THIRD CON-  
 9           SECUTIVE YEAR.—Section 1375 is amended by re-  
 10          designating subsections (c) and (d) as subsections  
 11          (d) and (e), respectively, and by inserting after sub-  
 12          section (b) the following new subsection:

13          “(c) TAX RATE INCREASE AFTER THIRD CONSECU-  
 14          TIVE YEAR.—

15                 “(1) IN GENERAL.—If an S corporation is de-  
 16                 scribed in subsection (a) for more than 3 consecutive  
 17                 taxable years, then the rate of tax imposed under  
 18                 subsection (a) with respect to each succeeding con-  
 19                 secutive taxable year (if any) shall be determined  
 20                 under the following table:

<b>“In the case of the—</b>	<b>The rate of tax imposed under subsection (a) shall be equal to such rate of tax for the 3rd taxable year, plus the following percentage points:</b>
4th taxable year .....	10
5th taxable year .....	20
6th taxable year .....	30
7th taxable year .....	40
8th taxable year and thereafter .....	50.

1           “(2) YEARS TAKEN INTO ACCOUNT.—No tax  
2 shall be increased under paragraph (1) for any tax-  
3 able year beginning before January 1, 1996.”

4           (c) CONFORMING AMENDMENTS.—

5           (1) Section 1362(f)(1) is amended by striking  
6 “or (3)”.

7           (2) Subsection (b) of section 1375 is amended  
8 by striking paragraphs (3) and (4) and inserting the  
9 following new paragraphs:

10           “(3) SUBCHAPTER C EARNINGS AND PROF-  
11 ITS.—The term ‘subchapter C earnings and profits’  
12 means earnings and profits of any corporation for  
13 any taxable year with respect to which an election  
14 under section 1362(a) (or under section 1372 of  
15 prior law) was not in effect.

16           “(4) GROSS RECEIPTS FROM SALES OF CAPITAL  
17 ASSETS (OTHER THAN STOCK AND SECURITIES).—In  
18 the case of dispositions of capital assets (other than  
19 stock and securities), gross receipts from such dis-  
20 positions shall be taken into account only to the ex-  
21 tent of the capital gain net income therefrom.

22           “(5) PASSIVE INVESTMENT INCOME DE-  
23 FINED.—

24           “(A) IN GENERAL.—Except as otherwise  
25 provided in this paragraph, the term ‘passive

1 investment income’ means gross receipts de-  
2 rived from royalties, rents, dividends, interest,  
3 and annuities.

4 “(B) EXCEPTION FOR INTEREST ON  
5 NOTES FROM SALES OF INVENTORY.—The term  
6 ‘passive investment income’ shall not include in-  
7 terest on any obligation acquired in the ordi-  
8 nary course of the corporation’s trade or busi-  
9 ness from its sale of property described in sec-  
10 tion 1221(1).

11 “(C) TREATMENT OF CERTAIN LENDING  
12 OR FINANCE COMPANIES.—If the S corporation  
13 meets the requirements of section 542(c)(6) for  
14 the taxable year, the term ‘passive investment  
15 income’ shall not include gross receipts for the  
16 taxable year which are derived directly from the  
17 active and regular conduct of a lending or fi-  
18 nance business (as defined in section  
19 542(d)(1)).

20 “(D) SPECIAL RULE FOR OPTIONS AND  
21 COMMODITY DEALINGS.—

22 “(i) IN GENERAL.—In the case of any  
23 options dealer or commodities dealer, pas-  
24 sive investment income shall be determined  
25 by not taking into account any gain or loss

1 (in the normal course of the taxpayer's ac-  
2 tivity of dealing in or trading section 1256  
3 contracts) from any section 1256 contract  
4 or property related to such a contract.

5 “(ii) DEFINITIONS.—For purposes of  
6 this subparagraph—

7 “(I) OPTIONS DEALER.—The  
8 term ‘options dealer’ has the meaning  
9 given such term by section  
10 1256(g)(8).

11 “(II) COMMODITIES DEALER.—  
12 The term ‘commodities dealer’ means  
13 a person who is actively engaged in  
14 trading section 1256 contracts and is  
15 registered with a domestic board of  
16 trade which is designated as a con-  
17 tract market by the Commodities Fu-  
18 tures Trading Commission.

19 “(III) SECTION 1256 CON-  
20 TRACT.—The term ‘section 1256 con-  
21 tract’ has the meaning given to such  
22 term by section 1256(b).

23 “(E) COORDINATION WITH SECTION  
24 1374.—The amount of passive investment in-  
25 come shall be determined by not taking into ac-

1 count any recognized built-in gain or loss of the  
2 S corporation for any taxable year in the rec-  
3 ognition period. Terms used in the preceding  
4 sentence shall have the same respective mean-  
5 ing as when used in section 1374.”

6 (3) The heading for section 1375 is amended by  
7 striking “**25**” and inserting “**50**”.

8 (4) The table of sections for part III of sub-  
9 chapter S of chapter 1 is amended by striking “25”  
10 in the item relating to section 1375 and inserting  
11 “50”.

12 (5) Clause (i) of section 1042(e)(4)(A) is  
13 amended by striking “section 1362(d)(3)(D)” and  
14 inserting “section 1375(b)(5)”.

### 15 **CHAPTER 3—OTHER PROVISIONS**

#### 16 **SEC. 3221. S CORPORATIONS PERMITTED TO HOLD SUB-** 17 **SIDIARIES.**

18 (a) IN GENERAL.—Paragraph (2) of section 1361(b)  
19 (defining ineligible corporation), as amended by section  
20 3112, is amended by striking subparagraph (A) and by  
21 redesignating subparagraphs (B), (C), (D), and (E) as  
22 subparagraphs (A), (B), (C), and (D), respectively.

23 (b) TREATMENT OF CERTAIN WHOLLY OWNED S  
24 CORPORATION SUBSIDIARIES.—Section 1361(b) (defining

1 small business corporation) is amended by adding at the  
2 end the following new subsection:

3           “(3) TREATMENT OF CERTAIN WHOLLY OWNED  
4           SUBSIDIARIES.—

5                   “(A) IN GENERAL.—For purposes of this  
6           title—

7                           “(i) a corporation which is a qualified  
8                           subchapter S subsidiary shall not be treat-  
9                           ed as a separate corporation, and

10                           “(ii) all assets, liabilities, and items of  
11                           income, deduction, and credit of a qualified  
12                           subchapter S subsidiary shall be treated as  
13                           assets, liabilities, and such items (as the  
14                           case may be) of the S corporation.

15                   “(B) QUALIFIED SUBCHAPTER S SUBSIDI-  
16                   ARY.—For purposes of this subsection, the term  
17                   ‘qualified subchapter S subsidiary’ means any  
18                   corporation 100 percent of the stock of which  
19                   is held by an S corporation as of the later of  
20                   the effective date of the S election of the S cor-  
21                   poration or the acquisition of the subsidiary,  
22                   and at all times thereafter.

23                   “(C) TREATMENT OF TERMINATIONS OF  
24                   QUALIFIED SUBCHAPTER S SUBSIDIARY STA-  
25                   TUS.—For purposes of this subtitle, if any cor-

1           poration which was a qualified subchapter S  
 2           subsidiary ceases to meet the requirements of  
 3           subparagraph (B), such corporation shall be  
 4           treated as a new corporation acquiring all of its  
 5           assets (and assuming all of its liabilities) imme-  
 6           diately before such cessation from the S cor-  
 7           poration in exchange for its stock.”.

8           (c) CERTAIN DIVIDENDS NOT TREATED AS PASSIVE  
 9 INVESTMENT INCOME.—Section 1375(b)(5) (defining pas-  
 10 sive investment income), as added by section 3214(c)(2),  
 11 is amended by adding at the end the following new sub-  
 12 paragraph:

13                   “(F) TREATMENT OF CERTAIN DIVI-  
 14                   DENDS.—If an S corporation holds stock in a  
 15                   C corporation meeting the requirements of sec-  
 16                   tion 1504(a)(2), the term ‘passive investment  
 17                   income’ shall not include dividends from such C  
 18                   corporation to the extent such dividends are at-  
 19                   tributable to the earnings and profits of such C  
 20                   corporation derived from the active conduct of  
 21                   a trade or business.”

22           (d) CONFORMING AMENDMENTS.—

23                   (1) Subsection (c) of section 1361, as amended  
 24                   by sections 3111(a)(2) and 3201(a), is amended by

1 striking paragraph (6) and redesignating paragraphs  
2 (7) and (8) as paragraphs (6) and (7), respectively.

3 (2) Subsection (b) of section 1504 (defining in-  
4 cludible corporation) is amended by adding at the  
5 end the following new paragraph:

6 “(8) An S corporation.”

7 **SEC. 3222. TREATMENT OF DISTRIBUTIONS DURING LOSS**  
8 **YEARS.**

9 (a) **ADJUSTMENTS FOR DISTRIBUTIONS TAKEN INTO**  
10 **ACCOUNT BEFORE LOSSES.—**

11 (1) Subparagraph (A) of section 1366(d)(1)  
12 (relating to losses and deductions cannot exceed  
13 shareholder’s basis in stock and debt) is amended by  
14 striking “paragraph (1)” and inserting “paragraphs  
15 (1) and (2)(A)”.

16 (2) Subsection (d) of section 1368 (relating to  
17 certain adjustments taken into account) is amended  
18 by adding at the end the following new sentence:

19 “In the case of any distribution made during any taxable  
20 year, the adjusted basis of the stock shall be determined  
21 with regard to the adjustments provided in paragraph (1)  
22 of section 1367(a) for the taxable year.”

23 (b) **ACCUMULATED ADJUSTMENTS ACCOUNT.—Para-**  
24 **graph (1) of section 1368(e) (relating to accumulated ad-**

1 justments account) is amended by adding at the end the  
2 following new subparagraph:

3 “(C) NET LOSS FOR YEAR DISREGARDED.—

4 “(i) IN GENERAL.—In applying this section  
5 to distributions made during any taxable year,  
6 the amount in the accumulated adjustments ac-  
7 count as of the close of such taxable year shall  
8 be determined without regard to any net nega-  
9 tive adjustment for such taxable year.

10 “(ii) NET NEGATIVE ADJUSTMENT.—For  
11 purposes of clause (i), the term ‘net negative  
12 adjustment’ means, with respect to any taxable  
13 year, the excess (if any) of—

14 “(I) the reductions in the account for  
15 the taxable year (other than for distribu-  
16 tions), over

17 “(II) the increases in such account for  
18 such taxable year.”

19 (c) CONFORMING AMENDMENTS.—Subparagraph (A)  
20 of section 1368(e)(1) is amended—

21 (1) by striking “as provided in subparagraph  
22 (B)” and inserting “as otherwise provided in this  
23 paragraph”, and

24 (2) by striking “section 1367(b)(2)(A)” and in-  
25 serting “section 1367(a)(2)”.

1 **SEC. 3223. CONSENT DIVIDEND FOR AAA BYPASS ELEC-**  
2 **TION.**

3 Section 1368(e)(3) (relating to election to distribute  
4 earnings first) is amended by adding at the end the follow-  
5 ing new subparagraph:

6 “(C) CONSENT DIVIDEND.—Under regula-  
7 tions prescribed by the Secretary, an S corpora-  
8 tion may, subject to the election under this  
9 paragraph, consent to treat as a distribution  
10 the amount specified in such consent, to the ex-  
11 tent such amount does not exceed the accumu-  
12 lated earnings and profits of such corporation.

13 The amount so specified shall be considered—

14 “(i) as distributed in money by the  
15 corporation to its shareholders on the last  
16 day of the taxable year of the corporation  
17 and as contributed to the capital of the  
18 corporation by the shareholders on such  
19 day, and

20 “(ii) if any such shareholder is an or-  
21 ganization described in section 511(a)(2),  
22 as unrelated business taxable income (as  
23 defined in section 512) to such share-  
24 holder.”

1 **SEC. 3224. TREATMENT OF S CORPORATIONS UNDER SUB-**  
2 **CHAPTER C.**

3 Subsection (a) of section 1371 (relating to applica-  
4 tion of subchapter C rules) is amended to read as follows:

5 “(a) APPLICATION OF SUBCHAPTER C RULES.—Ex-  
6 cept as otherwise provided in this title, and except to the  
7 extent inconsistent with this subchapter, subchapter C  
8 shall apply to an S corporation and its shareholders.”

9 **SEC. 3225. ELIMINATION OF PRE-1983 EARNINGS AND**  
10 **PROFITS.**

11 (a) IN GENERAL.—If—

12 (1) a corporation was an electing small business  
13 corporation under subchapter S of chapter 1 of the  
14 Internal Revenue Code of 1986 for any taxable year  
15 beginning before January 1, 1983, and

16 (2) such corporation is an S corporation under  
17 subchapter S of chapter 1 of such Code for its first  
18 taxable year beginning after December 31, 1995,

19 the amount of such corporation’s accumulated earnings  
20 and profits (as of the beginning of such first taxable year)  
21 shall be reduced by an amount equal to the portion (if  
22 any) of such accumulated earnings and profits which were  
23 accumulated in any taxable year beginning before January  
24 1, 1983, for which such corporation was an electing small  
25 business corporation under such subchapter S.

26 (b) CONFORMING AMENDMENTS.—

1           (1)(A) Subsection (a) of section 1375 is amend-  
2           ed by striking “subchapter C” in paragraph (1) and  
3           inserting “accumulated”.

4           (B) Subsection (b) of section 1375, as amended  
5           by section 3214(c)(2), is amended by striking para-  
6           graph (3) and by redesignating paragraphs (4) and  
7           (5) as paragraphs (3) and (4), respectively.

8           (C) The section heading for section 1375 is  
9           amended by striking “**SUBCHAPTER C**” and insert-  
10          ing “**ACCUMULATED**”.

11          (D) The table of sections for part III of sub-  
12          chapter S of chapter 1 is amended by striking “sub-  
13          chapter C” in the item relating to section 1375 and  
14          inserting “accumulated”.

15          (2) Clause (i) of section 1042(c)(4)(A), as  
16          amended by section 3214(c)(5), is amended by strik-  
17          ing “section 1375(b)(5)” and inserting “section  
18          1375(b)(4)”.

19   **SEC. 3226. ALLOWANCE OF CHARITABLE CONTRIBUTIONS**  
20                   **OF INVENTORY AND SCIENTIFIC PROPERTY.**

21          (a) IN GENERAL.—Section 170(e) (relating to certain  
22          contributions of ordinary income and capital gain prop-  
23          erty) is amended—

1           (1) by striking “(other than a corporation  
2           which is an S corporation)” in paragraph (3)(A),  
3           and

4           (2) by striking clause (i) of paragraph (4)(D)  
5           and by redesignating clauses (ii) and (iii) of such  
6           paragraph as clauses (i) and (ii), respectively.

7           (b) STOCK BASIS ADJUSTMENT.—Paragraph (1) of  
8           section 1367(a) (relating to adjustments to basis of stock  
9           of shareholders, etc.) is amended by striking “and” at the  
10          end of subparagraph (B), by striking the period at the  
11          end of subparagraph (C) and inserting “, and”, and by  
12          adding at the end the following new subparagraph:

13                         “(D) the excess of the deductions for char-  
14                         itable contributions over the basis of the prop-  
15                         erty contributed.”

16         **SEC. 3227. C CORPORATION RULES TO APPLY FOR FRINGE**  
17                         **BENEFIT PURPOSES.**

18           (a) IN GENERAL.—Section 1372 (relating to partner-  
19           ship rules to apply for fringe benefit purposes) is repealed.

20           (b) PARTNERSHIP RULES TO APPLY FOR HEALTH  
21           INSURANCE COSTS OF CERTAIN S CORPORATION SHARE-  
22           HOLDERS.—Paragraph (5) of section 162(*l*) is amended  
23           to read as follows:

24                         “(5) TREATMENT OF CERTAIN S CORPORATION  
25                         SHAREHOLDERS.—

1           “(A) IN GENERAL.—This subsection shall  
2           apply in the case of any 2-percent shareholder  
3           of an S corporation, except that—

4                   “(i) for purposes of this subsection,  
5                   such shareholder’s wages (as defined in  
6                   section 3121) from the S corporation shall  
7                   be treated as such shareholder’s earned in-  
8                   come (within the meaning of section  
9                   401(c)(1)), and

10                   “(ii) there shall be such adjustments  
11                   in the application of this subsection as the  
12                   Secretary may by regulations prescribe.

13           “(B) 2-PERCENT SHAREHOLDER DE-  
14           FINED.—For purposes of this paragraph, the  
15           term ‘2-percent shareholder’ means any person  
16           who owns (or is considered as owning within  
17           the meaning of section 318) on any day during  
18           the taxable year of the S corporation more than  
19           2 percent of the outstanding stock of such cor-  
20           poration or stock possessing more than 2 per-  
21           cent of the total combined voting power of all  
22           stock of such corporation.”

23           (b) CONFORMING AMENDMENT.—The table of sec-  
24           tions for part III of subchapter S of chapter 1 is amended  
25           by striking the item relating to section 1372.

1                   **Subtitle C—Taxation of S**  
2                   **Corporation Shareholders**

3   **SEC. 3301. UNIFORM TREATMENT OF OWNER-EMPLOYEES**  
4                   **UNDER PROHIBITED TRANSACTION RULES.**

5           The last sentence of section 4975(d) (relating to ex-  
6   emptions from prohibited transactions) is amended by  
7   striking “a shareholder-employee (as defined in section  
8   1379, as in effect on the day before the date of the enact-  
9   ment of the Subchapter S Revision Act of 1982),”.

10   **SEC. 3302. TREATMENT OF LOSSES TO SHAREHOLDERS.**

11           (a) TREATMENT OF LOSSES IN LIQUIDATIONS.—Sec-  
12   tion 331 (relating to gain or loss to shareholders in cor-  
13   porate liquidations) is amended by redesignating sub-  
14   section (c) as subsection (d) and by inserting after sub-  
15   section (b) the following new subsection:

16           “(c) LOSSES ON LIQUIDATIONS OF S CORPORA-  
17   TION.—

18                   “(1) IN GENERAL.—The portion of any loss rec-  
19   ognized by a shareholder of an S corporation (as de-  
20   fined in section 1361(a)(1)) on amounts received by  
21   such shareholder in a distribution in complete liq-  
22   uidation of such S corporation which does not exceed  
23   the ordinary income basis of stock of such S cor-  
24   poration in the hands of such shareholder shall not

1 be treated as a loss from the sale or exchange of a  
2 capital asset but shall be treated as an ordinary loss.

3 “(2) ORDINARY INCOME BASIS.—For purposes  
4 of this subsection, the ordinary income basis of stock  
5 of an S corporation in the hands of a shareholder of  
6 such S corporation shall be an amount equal to the  
7 portion of such shareholder’s basis in such stock  
8 which is equal to the aggregate increases in such  
9 basis under section 1367(a)(1) resulting from such  
10 shareholder’s pro rata share of ordinary income of  
11 such S corporation attributable to the complete liq-  
12 uidation.”

13 (b) CARRYOVER OF DISALLOWED LOSSES AND DE-  
14 Ductions UNDER AT-RISK RULES ALLOWED.—Para-  
15 graph (3) of section 1366(d) (relating to carryover of dis-  
16 allowed losses and deductions to post-termination transi-  
17 tion period) is amended by adding at the end the following  
18 new subparagraph:

19 “(D) AT-RISK LIMITATIONS.—To the ex-  
20 tent that any increase in adjusted basis de-  
21 scribed in subparagraph (B) would have in-  
22 creased the shareholder’s amount at risk under  
23 section 465 if such increase had occurred on  
24 the day preceding the commencement of the  
25 post-termination transition period, rules similar

1 to the rules described in subparagraphs (A)  
2 through (C) shall apply to any losses disallowed  
3 by reason of section 465(a).”

## 4 **Subtitle D—Effective Date**

### 5 **SEC. 3401. EFFECTIVE DATE.**

6 (a) IN GENERAL.—Except as otherwise provided in  
7 this title, the amendments made by this title shall apply  
8 to taxable years beginning after December 31, 1995.

9 (b) TREATMENT OF CERTAIN ELECTIONS UNDER  
10 PRIOR LAW.—For purposes of section 1362(g) of the In-  
11 ternal Revenue Code of 1986 (relating to election after  
12 termination), any termination under section 1362(d) of  
13 such Code (as in effect on the day before the date of the  
14 enactment of this Act) shall not be taken into account.

## 15 **TITLE IV—PENSION**

### 16 **SIMPLIFICATION**

#### 17 **Subtitle A—Simplification of** 18 **Nondiscrimination Provisions**

### 19 **SEC. 4000. SHORT TITLE.**

20 This title may be cited as the “Pension Simplification  
21 Act of 1995”.

1 **SEC. 4001. DEFINITION OF HIGHLY COMPENSATED EM-**  
 2 **PLoyEES; REPEAL OF FAMILY AGGREGATION.**

3 (a) IN GENERAL.—Paragraph (1) of section 414(q)  
 4 (defining highly compensated employee) is amended to  
 5 read as follows:

6 “(1) IN GENERAL.—The term ‘highly com-  
 7 pensated employee’ means any employee who—

8 “(A) was a 5-percent owner at any time  
 9 during the year or the preceding year,

10 “(B) had compensation for the preceding  
 11 year from the employer in excess of \$80,000, or

12 “(C) was the most highly compensated of-  
 13 ficer of the employer for the preceding year.

14 The Secretary shall adjust the \$80,000 amount  
 15 under subparagraph (B) at the same time and in the  
 16 same manner as under section 415(d), except that  
 17 the base period shall be the calendar quarter begin-  
 18 ning October 1, 1995.”

19 (b) SPECIAL RULE WHERE NO EMPLOYEE HAS  
 20 COMPENSATION OVER SPECIFIED AMOUNT.—Paragraph  
 21 (2) of section 414(q) is amended to read as follows:

22 “(2) SPECIAL RULE IF NO EMPLOYEE HAS COM-  
 23 PENSATION OVER SPECIFIED AMOUNT.—

24 “(A) IN GENERAL.—Except as provided in  
 25 subparagraph (B), if a defined benefit plan or  
 26 a defined contribution plan meets the require-

1           ments of sections 401(a)(4) and 410(b) with re-  
2           spect to the availability of contributions, bene-  
3           fits, and other plan features, then for all other  
4           purposes, subparagraphs (A) and (C) of para-  
5           graph (1) shall not apply to such plan.

6           “(B)   EXCEPTION.—Subparagraph   (A)  
7           shall not apply to a plan to the extent provided  
8           in regulations that are prescribed by the Sec-  
9           retary to prevent the evasion of the purposes of  
10          this paragraph.”

11       (c) REPEAL OF FAMILY AGGREGATION RULES.—

12           (1) IN GENERAL.—Paragraph (6) of section  
13           414(q) is hereby repealed.

14           (2) COMPENSATION LIMIT.—Paragraph (17)(A)  
15           of section 401(a) is amended by striking the last  
16           sentence.

17           (3) DEDUCTION.—Subsection (1) of section 404  
18           is amended by striking the last sentence.

19       (d) CONFORMING AMENDMENTS.—

20           (1) Paragraphs (4), (5), (8), and (12) of section  
21           414(q) are hereby repealed.

22           (2)(A) Section 414(r) is amended by adding at  
23           the end the following new paragraph:

1           “(9) EXCLUDED EMPLOYEES.—For purposes of  
2 this subsection, the following employees shall be ex-  
3 cluded:

4           “(A) Employees who have not completed 6  
5 months of service.

6           “(B) Employees who normally work less  
7 than 17½ hours per week.

8           “(C) Employees who normally work not  
9 more than 6 months during any year.

10          “(D) Employees who have not attained the  
11 age of 21.

12          “(E) Except to the extent provided in reg-  
13 ulations, employees who are included in a unit  
14 of employees covered by an agreement which  
15 the Secretary of Labor finds to be a collective  
16 bargaining agreement between employee rep-  
17 resentatives and the employer.

18          Except as provided by the Secretary, the employer  
19 may elect to apply subparagraph (A), (B), (C), or  
20 (D) by substituting a shorter period of service,  
21 smaller number of hours or months, or lower age for  
22 the period of service, number of hours or months, or  
23 age (as the case may be) specified in such subpara-  
24 graph.”

1 (B) Subparagraph (A) of section 414(r)(2) is  
2 amended by striking “subsection (q)(8)” and insert-  
3 ing “paragraph (9)”.

4 (3) Section 1114(c)(4) of the Tax Reform Act  
5 of 1986 is amended by adding at the end the follow-  
6 ing new sentence: “Any reference in this paragraph  
7 to section 414(q) shall be treated as a reference to  
8 such section as in effect before the Pension Sim-  
9 plification Act of 1995.”

10 (e) EFFECTIVE DATE.—The amendments made by  
11 this section shall apply to years beginning after Decem-  
12 ber 31, 1995, except that in determining whether an em-  
13 ployee is a highly compensated employee for years begin-  
14 ning in 1996, such amendments shall be treated as having  
15 been in effect for years beginning in 1995.

16 **Subtitle B—Targeted Access to**  
17 **Pension Plans for Small Employers**

18 **SEC. 4011. CREDIT FOR PENSION PLAN START-UP COSTS OF**

19 **SMALL EMPLOYERS.**

20 (a) ALLOWANCE OF CREDIT.—Section 38(b) (defin-  
21 ing current year business credit) is amended by striking  
22 “plus” at the end of paragraph (10), by striking the period  
23 at the end of paragraph (11) and inserting “, plus”, and  
24 by adding at the end the following new paragraph:

1           “(12) the small employer pension plan start-up  
2           cost credit.”

3           (b) **SMALL EMPLOYER PENSION PLAN START-UP**  
4 **COST CREDIT.**—Subpart D of part IV of subchapter A  
5 of chapter 1 (relating to business related credits) is  
6 amended by adding at the end the following new section:

7 **“SEC. 45C. SMALL EMPLOYER PENSION PLAN START-UP**  
8 **COST CREDIT.**

9           “(a) **AMOUNT OF CREDIT.**—For purposes of section  
10 38—

11           “(1) **IN GENERAL.**—The small employer pen-  
12 sion plan start-up cost credit for any taxable year is  
13 an amount equal to the qualified start-up costs of an  
14 eligible employer in establishing a qualified pension  
15 plan.

16           “(2) **AGGREGATE LIMITATION.**—The amount of  
17 the credit under paragraph (1) for any taxable year  
18 shall not exceed \$1,000, reduced by the aggregate  
19 amount determined under this section for all preced-  
20 ing taxable years of the taxpayer.

21           “(b) **QUALIFIED START-UP COSTS; QUALIFIED PEN-**  
22 **SION PLAN.**—For purposes of this section—

23           “(1) **QUALIFIED START-UP COSTS.**—The term  
24 ‘qualified start-up costs’ means any ordinary and  
25 necessary expenses of an eligible employer which—

1           “(A) are paid or incurred in connection  
2           with the establishment of a qualified pension  
3           plan, and

4           “(B) are of a nonrecurring nature.

5           “(2) QUALIFIED PENSION PLAN.—The term  
6           ‘qualified pension plan’ means—

7           “(A) a plan described in section 401(a)  
8           which includes a trust exempt from tax under  
9           section 501(a), or

10           “(B) a simplified employee pension (as de-  
11           fined in section 408(k)).

12           “(c) ELIGIBLE EMPLOYER.—For purposes of this  
13           section—

14           “(1) IN GENERAL.—The term ‘eligible em-  
15           ployer’ means an employer which—

16           “(A) had an average daily number of em-  
17           ployees during the preceding taxable year not in  
18           excess of 50, and

19           “(B) did not make any contributions on  
20           behalf of any employee to a qualified pension  
21           plan during the 2 taxable years immediately  
22           preceding the taxable year.

23           “(2) PROFESSIONAL SERVICE EMPLOYERS EX-  
24           CLUDED.—Such term shall not include an employer  
25           substantially all of the activities of which involve the

1 performance of services in the fields of health, law,  
2 engineering, architecture, accounting, actuarial  
3 science, performing arts, or consulting.

4 “(d) SPECIAL RULES.—For purposes of this sec-  
5 tion—

6 “(1) AGGREGATION RULES.—All persons treat-  
7 ed as a single employer under subsection (a) or (b)  
8 of section 52 or subsection (n) or (o) of section 414  
9 shall be treated as one person.

10 “(2) DISALLOWANCE OF DEDUCTION.—No de-  
11 duction shall be allowable under this chapter for any  
12 qualified start-up costs for which a credit is allow-  
13 able under subsection (a).”

14 (c) CONFORMING AMENDMENTS.—

15 (1) Section 39(d) is amended by adding at the  
16 end the following new paragraph:

17 “(7) NO CARRYBACK OF PENSION CREDIT.—No  
18 portion of the unused business credit for any taxable  
19 year which is attributable to the small employer pen-  
20 sion plan start-up cost credit determined under sec-  
21 tion 45C may be carried back to a taxable year end-  
22 ing before the date of the enactment of section  
23 45C.”



1 (c) ALTERNATIVE TEST.—Clause (ii) of section  
 2 408(k)(6)(A), as redesignated by subsection (b)(1), is  
 3 amended by adding at the end the following new flush sen-  
 4 tence:

5 “The requirements of the preceding sen-  
 6 tence are met if the employer makes con-  
 7 tributions to the simplified employee pen-  
 8 sion meeting the requirements of sections  
 9 401(k)(11) (B) or (C), 401(k)(11)(D), and  
 10 401(m)(10)(B).”

11 (d) EFFECTIVE DATE.—The amendments made by  
 12 this section shall apply to years beginning after December  
 13 31, 1995.

14 **SEC. 4013. EXEMPTION FROM TOP-HEAVY PLAN REQUIRE-**  
 15 **MENTS.**

16 (a) EXEMPTION FROM TOP-HEAVY PLAN REQUIRE-  
 17 MENTS.—Section 416(g) (defining top-heavy plans) is  
 18 amended by adding at the end the following new para-  
 19 graph:

20 “(3) EXEMPTION FOR CERTAIN PLANS.—A plan  
 21 shall not be treated as a top-heavy plan if, for such  
 22 plan year, the employer has no highly compensated  
 23 employees (as defined in section 414(q)) by reason  
 24 of section 414(q)(2).”

1 (b) EFFECTIVE DATE.—The amendment made by  
2 this section shall apply to years beginning after December  
3 31, 1995.

4 **SEC. 4014. REGULATORY TREATMENT OF SMALL EMPLOY-**  
5 **ERS.**

6 (a) IN GENERAL.—Section 7805(f) (relating to re-  
7 view of impact of regulations on small business) is amend-  
8 ed by adding at the end the following new subparagraph:

9 “(4) SPECIAL RULE FOR PENSION REGULA-  
10 TIONS.—

11 “(A) IN GENERAL.—Any regulation pro-  
12 posed to be issued by the Secretary which re-  
13 lates to qualified pension plans shall not take  
14 effect unless the Secretary includes provisions  
15 to address any special needs of the small em-  
16 ployers.

17 “(B) QUALIFIED PENSION PLAN.—For  
18 purposes of this paragraph, the term ‘qualified  
19 pension plan’ means—

20 “(i) any plan which includes a trust  
21 described in section 401(a) which is ex-  
22 empt from tax under section 501(a), or

23 “(ii) any simplified employee pension  
24 (as defined in section 408(k)).”

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

4 **TITLE V—ESTATE TAX EXCLU-**  
 5 **SION FOR FAMILY-OWNED**  
 6 **BUSINESS**

7 **SEC. 5001. SHORT TITLE.**

8 This title may be cited as the “American Family-  
 9 Owned Business Act”.

10 **SEC. 5002. FAMILY-OWNED BUSINESS EXCLUSION.**

11 (a) IN GENERAL.—Part III of subchapter A of chap-  
 12 ter 11 (relating to gross estate) is amended by inserting  
 13 after section 2033 the following new section:

14 **“SEC. 2033A. FAMILY-OWNED BUSINESS EXCLUSION.**

15 “(a) IN GENERAL.—In the case of an estate of a de-  
 16 cedent to which this section applies, the value of the gross  
 17 estate shall not include the lesser of—

18 “(1) the adjusted value of the qualified family-  
 19 owned business interests of the decedent otherwise  
 20 includible in the estate, or

21 “(2) the sum of—

22 “(A) \$1,500,000, plus

23 “(B) 50 percent of the excess (if any) of  
 24 the adjusted value of such interests over  
 25 \$1,500,000.

1       “(b) ESTATES TO WHICH SECTION APPLIES.—This  
2 section shall apply to an estate if—

3               “(1) the decedent was (at the date of the dece-  
4 dent’s death) a citizen or resident of the United  
5 States,

6               “(2) the excess of—

7                       “(A) the sum of—

8                               “(i) the adjusted value of the qualified  
9 family-owned business interests which—

10                                       “(I) are included in determining  
11 the value of the gross estate (without  
12 regard to this section), and

13                                       “(II) are acquired by a qualified  
14 heir from, or passed to a qualified  
15 heir from, the decedent (within the  
16 meaning of section 2032A(e)(9)), plus

17                               “(ii) the amount of the adjusted tax-  
18 able gifts of such interests from the dece-  
19 dent to members of the decedent’s family  
20 taken into account under subsection  
21 2001(b)(1)(B), to the extent such interests  
22 are continuously held by such members be-  
23 tween the date of the gift and the date of  
24 the decedent’s death, over

1           “(B) the amount included in the gross es-  
2           tate under section 2035,

3           exceeds 50 percent of the adjusted gross estate, and

4           “(3) during the 8-year period ending on the  
5           date of the decedent’s death there have been periods  
6           aggregating 5 years or more during which—

7           “(A) such interests were owned by the de-  
8           cedent or a member of the decedent’s family,  
9           and

10           “(B) there was material participation  
11           (within the meaning of section 2032A(e)(6)) by  
12           the decedent or a member of the decedent’s  
13           family in the operation of the business to which  
14           such interests relate.

15           “(c) ADJUSTED GROSS ESTATE.—For purposes of  
16           this section, the term ‘adjusted gross estate’ means the  
17           value of the gross estate (determined without regard to  
18           this section)—

19           “(1) reduced by any amount deductible under  
20           section 2053(a)(4), and

21           “(2) increased by the excess of—

22           “(A) the sum of—

23           “(i) the amount taken into account  
24           under subsection (b)(2)(B)), plus

1           “(ii) the amount of other gifts from  
2           the decedent to the decedent’s spouse (at  
3           the time of the gift) within 10 years of the  
4           date of the decedent’s death, plus

5           “(iii) the amount of other gifts (not  
6           included under clause (i) or (ii)) from the  
7           decedent within 3 years of such date, over

8           “(B) the amount included in the gross es-  
9           tate under section 2035.

10          “(d) ADJUSTED VALUE OF THE QUALIFIED FAMILY-  
11 OWNED BUSINESS INTERESTS.—For purposes of this sec-  
12 tion, the adjusted value of any qualified family-owned  
13 business interest is the value of such interest for purposes  
14 of this chapter (determined without regard to this sec-  
15 tion), reduced by the excess of—

16           “(1) any amount deductible under section  
17           2053(a)(4), over

18           “(2) the sum of—

19           “(A) any indebtedness on any qualified  
20           residence of the decedent the interest on which  
21           is deductible under section 163(h)(3), plus

22           “(B) any indebtedness to the extent the  
23           taxpayer establishes that the proceeds of such  
24           indebtedness were used for the payment of edu-  
25           cational and medical expenses of the decedent,

1 the decedent's spouse, or the decedent's depend-  
2 ents (within the meaning of section 152), plus

3 “(C) any indebtedness not described in  
4 subparagraph (A) or (B), to the extent such in-  
5 debtedness does not exceed \$10,000.

6 “(e) QUALIFIED FAMILY-OWNED BUSINESS INTER-  
7 EST.—

8 “(1) IN GENERAL.—For purposes of this sec-  
9 tion, the term ‘qualified family-owned business inter-  
10 est’ means—

11 “(A) an interest as a proprietor in a trade  
12 or business carried on as a proprietorship, or

13 “(B) an interest as a partner in a partner-  
14 ship, or stock in a corporation, carrying on a  
15 trade or business, if—

16 “(i) at least—

17 “(I) 50 percent of such partner-  
18 ship or corporation is owned (directly  
19 or indirectly) by the decedent or mem-  
20 bers of the decedent's family,

21 “(II) 70 percent of such partner-  
22 ship or corporation is so owned by 2  
23 families (including the decedent's fam-  
24 ily), or

1                   “(III) 90 percent of such part-  
2                   nership or corporation is so owned by  
3                   3 families (including the decedent’s  
4                   family), and

5                   “(ii) at least 30 percent of such part-  
6                   nership or corporation is so owned by each  
7                   family described in subclause (II) or (III)  
8                   of clause (i).

9                   “(2) LIMITATION.—Such term shall not in-  
10                  clude—

11                  “(A) any interest in a trade or business  
12                  the principal place of business of which is not  
13                  located in the United States,

14                  “(B) any interest in—

15                          “(i) an entity which had, or

16                          “(ii) an entity which is a member of  
17                          a controlled group (as defined in section  
18                          267(f)(1)) which had,

19                          readily tradable stock or debt on an established  
20                          securities market or secondary market (as de-  
21                          fined by the Secretary) within 3 years of the  
22                          date of the decedent’s death,

23                  “(C) any interest in a trade or business  
24                  not described in section 542(c)(2), if more than  
25                  35 percent of the adjusted ordinary gross in-

1           come of such trade or business for the taxable  
2           year which includes the date of the decedent's  
3           death would qualify as personal holding com-  
4           pany income (as defined in section 543(a)), and

5           “(D) that portion of an interest in a trade  
6           or business that is attributable to cash or mar-  
7           ketable securities, or both, in excess of the rea-  
8           sonably expected day-to-day working capital  
9           needs of such trade or business.

10          “(3) OWNERSHIP RULES.—

11           “(A) INDIRECT OWNERSHIP.—For pur-  
12           poses of determining indirect ownership under  
13           paragraph (1), rules similar to the rules of  
14           paragraphs (2) and (3) of section 447(e) shall  
15           apply.

16           “(B) TIERED ENTITIES.—For purposes of  
17           this section, if—

18           “(i) a qualified family-owned business  
19           holds an interest in another trade or busi-  
20           ness, and

21           “(ii) such interest would be a qualified  
22           family-owned business interest if held di-  
23           rectly by the family (or families) holding  
24           interests in the qualified family-owned

1           business meeting the requirements of para-  
2           graph (1)(B),  
3           then the value of the qualified family-owned  
4           business shall include the portion attributable  
5           to the interest in the other trade or business.

6           “(f) TAX TREATMENT OF FAILURE TO MATERIALLY  
7 PARTICIPATE IN BUSINESS OR DISPOSITIONS OF INTER-  
8 ESTS.—

9           “(1) IN GENERAL.—There is imposed an addi-  
10          tional estate tax if, within 10 years after the date  
11          of the decedent’s death and before the date of the  
12          qualified heir’s death—

13                 “(A) the qualified heir ceases to use for  
14                 the qualified use (within the meaning of section  
15                 2032A(c)(6)(B)) the qualified family-owned  
16                 business interest which was acquired (or  
17                 passed) from the decedent, or

18                 “(B) the qualified heir disposes of any por-  
19                 tion of a qualified family-owned business inter-  
20                 est (other than by a disposition to a member of  
21                 the qualified heir’s family or through a qualified  
22                 conservation contribution under section  
23                 170(h)).

1           “(2) ADDITIONAL ESTATE TAX.—The amount  
2 of the additional estate tax imposed by paragraph  
3 (1) shall be equal to—

4                   “(A) the adjusted tax difference attrib-  
5 utable to the qualified family-owned business  
6 interest (as determined under rules similar to  
7 the rules of section 2032A(c)(2)(B)), plus

8                   “(B) interest on the amount determined  
9 under subparagraph (A) at the annual rate of  
10 4 percent for the period beginning on the date  
11 the estate tax liability was due under this chap-  
12 ter and ending on the date such additional es-  
13 tate tax is due.

14           “(g) OTHER DEFINITIONS AND APPLICABLE  
15 RULES.—For purposes of this section—

16                   “(1) QUALIFIED HEIR.—The term ‘qualified  
17 heir’—

18                   “(A) has the meaning given to such term  
19 by section 2032A(e)(1), and

20                   “(B) includes any active employee of the  
21 trade or business to which the qualified family-  
22 owned business interest relates if such employee  
23 has been employed by such trade or business  
24 for a period of at least 10 years before the date  
25 of the decedent’s death.

1           “(2) MEMBER OF THE FAMILY.—The term  
2           ‘member of the family’ has the meaning given to  
3           such term by section 2032A(e)(2).

4           “(3) APPLICABLE RULES.—Rules similar to the  
5           following rules shall apply:

6                   “(A) Section 2032A(b)(4) (relating to de-  
7                   cedents who are retired or disabled).

8                   “(B) Section 2032A(b)(5) (relating to spe-  
9                   cial rules for surviving spouses).

10                   “(C) Section 2032A(c)(2)(D) (relating to  
11                   partial dispositions).

12                   “(D) Section 2032A(c)(3) (relating to only  
13                   1 additional tax imposed with respect to any 1  
14                   portion).

15                   “(E) Section 2032A(c)(4) (relating to due  
16                   date).

17                   “(F) Section 2032A(c)(5) (relating to li-  
18                   ability for tax; furnishing of bond).

19                   “(G) Section 2032A(c)(7) (relating to no  
20                   tax if use begins within 2 years; active manage-  
21                   ment by eligible qualified heir treatment as ma-  
22                   terial participation).

23                   “(H) Section 2032A(e)(10) (relating to  
24                   community property).

1           “(I) Section 2032A(e)(14) (relating to  
2 treatment of replacement property acquired in  
3 section 1031 or 1033 transactions).

4           “(J) Section 2032A(f) (relating to statute  
5 of limitations).

6           “(K) Section 6166(b)(3) (relating to farm-  
7 houses and certain other structures taken into  
8 account).

9           “(L) Subparagraphs (B), (C), and (D) of  
10 section 6166(g)(1) (relating to acceleration of  
11 payment).”

12       (b) CLERICAL AMENDMENT.—The table of sections  
13 for part III of subchapter A of chapter 11 is amended  
14 by inserting after the item relating to section 2033 the  
15 following new item:

          “Sec. 2033A. Family-owned business exclusion.”

16       (c) EFFECTIVE DATE.—The amendments made by  
17 this section shall apply to estates of decedents dying after  
18 December 31, 1995.

19                           **TITLE VI—SPENDING**  
20                           **REDUCTIONS**

21       **SEC. 6001. SHORT TITLE.**

22       This title may be cited as the “Spending Reductions  
23 Act of 1995”.

1 **SEC. 6002. SERVICE CONTRACTS.**

2 Notwithstanding any other provision of law, of the  
3 funds available for fiscal year 1996, the total amount  
4 available for service contracts shall not exceed  
5 \$105,000,000,000.

6 **SEC. 6003. FEDERALLY FUNDED RESEARCH AND DEVELOP-**  
7 **MENT CENTERS.**

8 Notwithstanding any other provision of law, of the  
9 funds available for the Department of Defense for fiscal  
10 year 1996, the total amount available for procurement of  
11 work from federally funded research and development cen-  
12 ters shall not exceed \$1,000,000,000.

13 **SEC. 6004. FOREIGN MILITARY FINANCING.**

14 Notwithstanding any other provision of law, of the  
15 funds available for fiscal year 1996, the total amount  
16 available for the Foreign Military Financing Program  
17 under section 23 of the Arms Export Control Act shall  
18 not exceed \$3,500,000,000.

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S 1299 IS—2

S 1299 IS—3

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S 1299 IS—5

S 1299 IS—6

S 1299 IS—7

S 1299 IS—8

S 1299 IS—9