

104TH CONGRESS
2D SESSION

S. 2086

To amend the Internal Revenue Code of 1986 to simplify certain rules relating to the taxation of United States business operating abroad, and for other purposes.

IN THE SENATE OF THE UNITED STATES

SEPTEMBER 17, 1996

Mr. PRESSLER (for himself, Mr. LOTT, Mr. BAUCUS, Mr. HATCH, Mr. D'AMATO, Mr. NICKLES, Mr. GORTON, Mr. HATFIELD, Mr. BURNS, and Mrs. MURRAY) introduced the following bill; which was read twice and referred to the Committee on Finance

A BILL

To amend the Internal Revenue Code of 1986 to simplify certain rules relating to the taxation of United States business operating abroad, and for other purposes.

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

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

4 **TABLE OF CONTENTS.**

5 (a) SHORT TITLE.—This Act may be cited as the
6 “International Tax Simplification for American Competi-
7 tiveness Act”.

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

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

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

TITLE I—TREATMENT OF PASSIVE FOREIGN INVESTMENT COMPANIES

- Sec. 101. United States shareholders of controlled foreign corporations not sub-
 ject to PFIC inclusion.
 Sec. 102. Election of mark to market for marketable stock in passive foreign
 investment company.
 Sec. 103. Modification to definition of passive income.
 Sec. 104. Modifications to asset valuation test.
 Sec. 105. Effective date.

TITLE II—TREATMENT OF CONTROLLED FOREIGN CORPORATIONS

- Sec. 201. Gain on certain stock sales by controlled foreign corporations treated
 as dividends.
 Sec. 202. Miscellaneous modifications to subpart F.
 Sec. 203. Indirect foreign tax credit allowed for certain lower tier companies.
 Sec. 204. Exemption for active financing income.
 Sec. 205. Repeal of separate foreign tax credit limitation for noncontrolled sec-
 tion 902 corporations.
 Sec. 206. Countries in European Union treated as a single country under same
 country exceptions.
 Sec. 207. Expansion of de minimis rule under subpart F.
 Sec. 208. Subpart F earnings and profits determined under generally accepted
 accounting principles.
 Sec. 209. Affiliated foreign insurance companies may offset losses.

TITLE III—OTHER PROVISIONS

- Sec. 301. Exchange rate used in translating foreign taxes.
 Sec. 302. Election to use simplified section 904 limitation for alternative mini-
 mum tax.
 Sec. 303. Modification of section 1491.
 Sec. 304. Modification of section 367(b).
 Sec. 305. Increase in filing thresholds for returns as to organization of foreign
 corporations and acquisitions of stock in such corporations.

- Sec. 306. Application of uniform capitalization rules to foreign persons.
 Sec. 307. Extension of period to which excess foreign taxes may be carried.
 Sec. 308. Recharacterization of overall domestic loss.
 Sec. 309. Treatment of nonresident aliens engaged in international transportation services.
 Sec. 310. Export property of FSC to include computer software.
 Sec. 311. Special rules relating to financial services income.
 Sec. 312. United States property not to include certain assets acquired by dealers in ordinary course of trade or business.

1 **TITLE I—TREATMENT OF PAS-**
 2 **SIVE FOREIGN INVESTMENT**
 3 **COMPANIES**

4 **SEC. 101. UNITED STATES SHAREHOLDERS OF CON-**
 5 **TROLLED FOREIGN CORPORATIONS NOT**
 6 **SUBJECT TO PFIC INCLUSION.**

7 Section 1297, as redesignated by section 102, is
 8 amended by adding at the end the following new sub-
 9 section:

10 “(e) EXCEPTION FOR UNITED STATES SHAREHOLD-
 11 ERS OF CONTROLLED FOREIGN CORPORATIONS.—

12 “(1) IN GENERAL.—For purposes of this part,
 13 a corporation shall not be treated with respect to a
 14 shareholder as a passive foreign investment company
 15 during the qualified portion of such shareholder’s
 16 holding period with respect to stock in such corpora-
 17 tion.

18 “(2) QUALIFIED PORTION.—For purposes of
 19 this subsection, the term ‘qualified portion’ means
 20 the portion of the shareholder’s holding period—

1 “(A) which is after December 31, 1996,
2 and

3 “(B) during which the shareholder is a
4 United States shareholder (as defined in section
5 951(b)) of the corporation and the corporation
6 is a controlled foreign corporation.

7 “(3) NEW HOLDING PERIOD IF QUALIFIED POR-
8 TION ENDS.—

9 “(A) IN GENERAL.—Except as provided in
10 subparagraph (B), if the qualified portion of a
11 shareholder’s holding period with respect to any
12 stock ends after December 31, 1996, solely for
13 purposes of this part, the shareholder’s holding
14 period with respect to such stock shall be treat-
15 ed as beginning as of the first day following
16 such period.

17 “(B) EXCEPTION.—Subparagraph (A)
18 shall not apply if such stock was, with respect
19 to such shareholder, stock in a passive foreign
20 investment company at any time before the
21 qualified portion of the shareholder’s holding
22 period with respect to such stock and no elec-
23 tion under section 1298(b)(1) is made.”

1 **SEC. 102. ELECTION OF MARK TO MARKET FOR MARKET-**
2 **ABLE STOCK IN PASSIVE FOREIGN INVEST-**
3 **MENT COMPANY.**

4 (a) IN GENERAL.—Part VI of subchapter P of chap-
5 ter 1 is amended by redesignating subpart C as subpart
6 D, by redesignating sections 1296 and 1297 as sections
7 1297 and 1298, respectively, and by inserting after sub-
8 part B the following new subpart:

9 **“Subpart C—Election of Mark to Market for**
10 **Marketable Stock**

“Sec. 1296. Election of mark to market for marketable stock.

11 **“SEC. 1296. ELECTION OF MARK TO MARKET FOR MARKET-**
12 **ABLE STOCK.**

13 “(a) GENERAL RULE.—In the case of marketable
14 stock in a passive foreign investment company which is
15 owned (or treated under subsection (g) as owned) by a
16 United States person at the close of any taxable year of
17 such person, at the election of such person—

18 “(1) If the fair market value of such stock as
19 of the close of such taxable year exceeds its adjusted
20 basis, such United States person shall include in
21 gross income for such taxable year an amount equal
22 to the amount of such excess.

23 “(2) If the adjusted basis of such stock exceeds
24 the fair market value of such stock as of the close

1 of such taxable year, such United States person
2 shall be allowed a deduction for such taxable year
3 equal to the lesser of—

4 “(A) the amount of such excess, or

5 “(B) the unreversed inclusions with respect
6 to such stock.

7 “(b) BASIS ADJUSTMENTS.—

8 “(1) IN GENERAL.—The adjusted basis of stock
9 in a passive foreign investment company—

10 “(A) shall be increased by the amount in-
11 cluded in the gross income of the United States
12 person under subsection (a)(1) with respect to
13 such stock, and

14 “(B) shall be decreased by the amount al-
15 lowed as a deduction to the United States per-
16 son under subsection (a)(2) with respect to
17 such stock.

18 “(2) SPECIAL RULE FOR STOCK CONSTRUC-
19 TIVELY OWNED.—In the case of stock in a passive
20 foreign investment company which the United States
21 person is treated as owning under subsection (g)—

22 “(A) the adjustments under paragraph (1)
23 shall apply to such stock in the hands of the
24 person actually holding such stock but only for
25 purposes of determining the subsequent treat-

1 ment under this chapter of the United States
2 person with respect to such stock, and

3 “(B) similar adjustments shall be made to
4 the adjusted basis of the property by reason of
5 which the United States person is treated as
6 owning such stock.

7 “(c) CHARACTER AND SOURCE RULES.—

8 “(1) ORDINARY TREATMENT.—

9 “(A) GAIN.—Any amount included in gross
10 income under subsection (a)(1), and any gain
11 on the sale or other disposition of marketable
12 stock in a passive foreign investment company
13 (with respect to which an election under this
14 section is in effect), shall be treated as ordinary
15 income.

16 “(B) LOSS.—Any—

17 “(i) amount allowed as a deduction
18 under subsection (a)(2), and

19 “(ii) loss on the sale or other disposi-
20 tion of marketable stock in a passive for-
21 eign investment company (with respect to
22 which an election under this section is in
23 effect) to the extent that the amount of
24 such loss does not exceed the unreversed
25 inclusions with respect to such stock,

1 shall be treated as an ordinary loss. The
2 amount so treated shall be treated as a deduc-
3 tion allowable in computing adjusted gross in-
4 come.

5 “(2) SOURCE.—The source of any amount in-
6 cluded in gross income under subsection (a)(1) (or
7 allowed as a deduction under subsection (a)(2)) shall
8 be determined in the same manner as if such
9 amount were gain or loss (as the case may be) from
10 the sale of stock in the passive foreign investment
11 company.

12 “(d) UNREVERSED INCLUSIONS.—For purposes of
13 this section, the term ‘unreversed inclusions’ means, with
14 respect to any stock in a passive foreign investment com-
15 pany, the excess (if any) of—

16 “(1) the amount included in gross income of
17 the taxpayer under subsection (a)(1) with respect to
18 such stock for prior taxable years, over

19 “(2) the amount allowed as a deduction under
20 subsection (a)(2) with respect to such stock for prior
21 taxable years.

22 The amount referred to in paragraph (1) shall include any
23 amount which would have been included in gross income
24 under subsection (a)(1) with respect to such stock for any
25 prior taxable year but for section 1291.

1 “(e) MARKETABLE STOCK.—For purposes of this
2 section—

3 “(1) IN GENERAL.—The term ‘marketable
4 stock’ means—

5 “(A) any stock which is regularly traded
6 on—

7 “(i) a national securities exchange
8 which is registered with the Securities and
9 Exchange Commission or the national mar-
10 ket system established pursuant to section
11 11A of the Securities and Exchange Act of
12 1934, or

13 “(ii) any exchange or other market
14 which the Secretary determines has rules
15 adequate to carry out the purposes of this
16 part,

17 “(B) to the extent provided in regulations,
18 stock in any foreign corporation which is com-
19 parable to a regulated investment company and
20 which offers for sale or has outstanding any
21 stock of which it is the issuer and which is re-
22 deemable at its net asset value, and

23 “(C) to the extent provided in regulations,
24 any option on stock described in subparagraph
25 (A) or (B).

1 “(2) SPECIAL RULE FOR REGULATED INVEST-
2 MENT COMPANIES.—In the case of any regulated in-
3 vestment company which is offering for sale or has
4 outstanding any stock of which it is the issuer and
5 which is redeemable at its net asset value, all stock
6 in a passive foreign investment company which it
7 owns directly or indirectly shall be treated as mar-
8 ketable stock for purposes of this section. Except as
9 provided in regulations, similar treatment as mar-
10 ketable stock shall apply in the case of any other
11 regulated investment company which publishes net
12 asset valuations at least annually.

13 “(f) TREATMENT OF CONTROLLED FOREIGN COR-
14 PORATIONS WHICH ARE SHAREHOLDERS IN PASSIVE
15 FOREIGN INVESTMENT COMPANIES.—In the case of a for-
16 eign corporation which is a controlled foreign corporation
17 and which owns (or is treated under subsection (g) as own-
18 ing) stock in a passive foreign investment company—

19 “(1) this section (other than subsection (c)(2))
20 shall apply to such foreign corporation in the same
21 manner as if such corporation were a United States
22 person, and

23 “(2) for purposes of subpart F of part III of
24 subchapter N—

1 “(A) any amount included in gross income
2 under subsection (a)(1) shall be treated as for-
3 foreign personal holding company income de-
4 scribed in section 954(c)(1)(A), and

5 “(B) any amount allowed as a deduction
6 under subsection (a)(2) shall be treated as a de-
7 duction allocable to foreign personal holding
8 company income so described.

9 “(g) STOCK OWNED THROUGH CERTAIN FOREIGN
10 ENTITIES.—Except as provided in regulations—

11 “(1) IN GENERAL.—For purposes of this sec-
12 tion, stock owned, directly or indirectly, by or for a
13 foreign partnership or foreign trust or foreign estate
14 shall be considered as being owned proportionately
15 by its partners or beneficiaries. Stock considered to
16 be owned by a person by reason of the application
17 of the preceding sentence shall, for purposes of ap-
18 plying such sentence, be treated as actually owned
19 by such person.

20 “(2) TREATMENT OF CERTAIN DISPOSITIONS.—
21 In any case in which a United States person is
22 treated as owning stock in a passive foreign invest-
23 ment company by reason of paragraph (1)—

24 “(A) any disposition by the United States
25 person or by any other person which results in

1 the United States person being treated as no
2 longer owning such stock, and

3 “(B) any disposition by the person owning
4 such stock,

5 shall be treated as a disposition by the United
6 States person of the stock in the passive foreign in-
7 vestment company.

8 “(h) COORDINATION WITH SECTION 851(b).—For
9 purposes of paragraphs (2) and (3) of section 851(b), any
10 amount included in gross income under subsection (a)
11 shall be treated as a dividend.

12 “(i) STOCK ACQUIRED FROM A DECEDENT.—In the
13 case of stock of a passive foreign investment company
14 which is acquired by bequest, devise, or inheritance (or
15 by the decedent’s estate) and with respect to which an
16 election under this section was in effect as of the date of
17 the decedent’s death, notwithstanding section 1014, the
18 basis of such stock in the hands of the person so acquiring
19 it shall be the adjusted basis of such stock in the hands
20 of the decedent immediately before his death (or, if lesser,
21 the basis which would have been determined under section
22 1014 without regard to this subsection).

23 “(j) COORDINATION WITH SECTION 1291 FOR FIRST
24 YEAR OF ELECTION.—

1 “(1) TAXPAYERS OTHER THAN REGULATED IN-
2 VESTMENT COMPANIES.—

3 “(A) IN GENERAL.—If the taxpayer elects
4 the application of this section with respect to
5 any marketable stock in a corporation after the
6 beginning of the taxpayer’s holding period in
7 such stock, and if the requirements of subpara-
8 graph (B) are not satisfied, section 1291 shall
9 apply to—

10 “(i) any distributions with respect to,
11 or disposition of, such stock in the first
12 taxable year of the taxpayer for which such
13 election is made, and

14 “(ii) any amount which, but for sec-
15 tion 1291, would have been included in
16 gross income under subsection (a) with re-
17 spect to such stock for such taxable year in
18 the same manner as if such amount were
19 gain on the disposition of such stock.

20 “(B) REQUIREMENTS.—The requirements
21 of this subparagraph are met if, with respect to
22 each of such corporation’s taxable years for
23 which such corporation was a passive foreign
24 investment company and which begin after De-
25 cember 31, 1986, and included any portion of

1 the taxpayer's holding period in such stock,
2 such corporation was treated as a qualified
3 electing fund under this part with respect to the
4 taxpayer.

5 “(2) SPECIAL RULES FOR REGULATED INVEST-
6 MENT COMPANIES.—

7 “(A) IN GENERAL.—If a regulated invest-
8 ment company elects the application of this sec-
9 tion with respect to any marketable stock in a
10 corporation after the beginning of the tax-
11 payer's holding period in such stock, then, with
12 respect to such company's first taxable year for
13 which such company elects the application of
14 this section with respect to such stock—

15 “(i) section 1291 shall not apply to
16 such stock with respect to any distribution
17 or disposition during, or amount included
18 in gross income under this section for,
19 such first taxable year, but

20 “(ii) such regulated investment com-
21 pany's tax under this chapter for such first
22 taxable year shall be increased by the ag-
23 gregate amount of interest which would
24 have been determined under section

1 1291(c)(3) if section 1291 were applied
2 without regard to this subparagraph.

3 Clause (ii) shall not apply if for the preceding
4 taxable year the company elected to mark to
5 market the stock held by such company as of
6 the last day of such preceding taxable year.

7 “(B) DISALLOWANCE OF DEDUCTION.—No
8 deduction shall be allowed to any regulated in-
9 vestment company for the increase in tax under
10 subparagraph (A)(ii).

11 “(k) ELECTION.—This section shall apply to market-
12 able stock in a passive foreign investment company which
13 is held by a United States person only if such person elects
14 to apply this section with respect to such stock. Such an
15 election shall apply to the taxable year for which made
16 and all subsequent taxable years unless—

17 “(1) such stock ceases to be marketable stock,
18 or

19 “(2) the Secretary consents to the revocation of
20 such election.

21 “(l) TRANSITION RULE FOR INDIVIDUALS BECOMING
22 SUBJECT TO UNITED STATES TAX.—If any individual be-
23 comes a United States person in a taxable year beginning
24 after December 31, 1996, solely for purposes of this sec-
25 tion, the adjusted basis (before adjustments under sub-

1 section (b)) of any marketable stock in a passive foreign
2 investment company owned by such individual on the first
3 day of such taxable year shall be treated as being the
4 greater of its fair market value on such first day or its
5 adjusted basis on such first day.”

6 (b) COORDINATION WITH INTEREST CHARGE,
7 ETC.—

8 (1) Paragraph (1) of section 1291(d) is amend-
9 ed by adding at the end the following new flush sen-
10 tence:

11 “Except as provided in section 1296(j), this section
12 also shall not apply if an election under section
13 1296(k) is in effect for the taxpayer’s taxable year.”

14 (2) The subsection heading for subsection (d) of
15 section 1291 is amended by striking “SUBPART B”
16 and inserting “SUBPARTS B AND C”.

17 (3) Subparagraph (A) of section 1291(a)(3) is
18 amended to read as follows:

19 “(A) HOLDING PERIOD.—The taxpayer’s
20 holding period shall be determined under sec-
21 tion 1223; except that—

22 “(i) for purposes of applying this sec-
23 tion to an excess distribution, such holding
24 period shall be treated as ending on the
25 date of such distribution, and

1 “(ii) if section 1296 applied to such
2 stock with respect to the taxpayer for any
3 prior taxable year, such holding period
4 shall be treated as beginning on the first
5 day of the first taxable year beginning
6 after the last taxable year for which sec-
7 tion 1296 so applied.”

8 (c) TREATMENT OF MARK-TO-MARKET GAIN UNDER
9 SECTION 4982.—

10 (1) Subsection (e) of section 4982 is amended
11 by adding at the end the following new paragraph:

12 “(6) TREATMENT OF GAIN RECOGNIZED UNDER
13 SECTION 1296.—For purposes of determining a regu-
14 lated investment company’s ordinary income—

15 “(A) notwithstanding paragraph (1)(C),
16 section 1296 shall be applied as if such compa-
17 ny’s taxable year ended on October 31, and

18 “(B) any ordinary gain or loss from an ac-
19 tual disposition of stock in a passive foreign in-
20 vestment company during the portion of the
21 taxable year after October 31 shall be taken
22 into account in determining such company’s or-
23 dinary income for the following taxable year.

24 This paragraph shall not apply to a company mak-
25 ing an election under paragraph (4).”

1 (2) Subsection (b) of section 852 is amended by
2 adding at the end the following new paragraph:

3 “(10) SPECIAL RULE FOR CERTAIN LOSSES ON
4 STOCK IN PASSIVE FOREIGN INVESTMENT COMPA-
5 NIES.—To the extent provided in regulations, the
6 taxable income of a regulated investment company
7 (other than a company to which an election under
8 section 4982(e)(4) applies) shall be computed with-
9 out regard to any net reduction in the value of any
10 stock with respect to which an election under section
11 1296(k) is in effect occurring after October 31 of
12 the taxable year, and any such reduction shall be
13 treated as occurring on the first day of the following
14 taxable year.”

15 (3) Subsection (c)(2) of section 852 is amended
16 by inserting after: “, without regard to any net re-
17 duction in the value of any stock of a passive foreign
18 investment company with respect to which an elec-
19 tion under section 1296(k) is in effect occurring
20 after October 31 of such year,” after “October 31
21 of such year”.

22 (d) CONFORMING AMENDMENTS.—

23 (1) Sections 532(b)(4) and 542(c)(10) are each
24 amended by striking “section 1296” and inserting
25 “section 1297”.

1 (2) Subsection (f) of section 551 is amended by
2 striking “section 1297(b)(5)” and inserting “section
3 1298(b)(5)”

4 (3) Subsections (a)(1) and (d) of section 1293
5 are each amended by striking “section 1297(a)” and
6 inserting “section 1298(a)”.

7 (4) Paragraph (3) of section 1297(b), as redesi-
8 gnated by subsection (a), is hereby repealed.

9 (5) The table of sections for subpart D of part
10 VI of subchapter P of chapter 1, as redesignated by
11 subsection (a), is amended to read as follows:

“Sec. 1297. Passive foreign investment company.
“Sec. 1298. Special rules.”

12 (6) The table of subparts for part VI of sub-
13 chapter P of chapter 1 is amended by striking the
14 last item and inserting the following new items:

“Subpart C. Election of mark to market for marketable stock.
“Subpart D. General provisions.”

15 (e) CLARIFICATION OF GAIN RECOGNITION ELEC-
16 TION.—The last sentence of section 1298(b)(1), as so re-
17 designated, is amended by inserting “(determined without
18 regard to the preceding sentence)” after “investment com-
19 pany”.

20 **SEC. 103. MODIFICATION TO DEFINITION OF PASSIVE IN-**
21 **COME.**

22 Paragraph (1) of section 1297(b) (defining passive
23 income), as redesignated by section 102, is amended by

1 inserting before the period “without regard to paragraph
2 (3) thereof”.

3 **SEC. 104. MODIFICATIONS TO ASSET VALUATION TEST.**

4 (a) IN GENERAL.—Section 1297(a), as redesignated
5 by section 102, is amended—

6 (1) by striking “(by value)” in paragraph (2),

7 and

8 (2) by striking the last two sentences and in-
9 serting:

10 “The determination under paragraph (2) shall be made
11 as provided under section 1298(f).”

12 (b) METHODS FOR VALUING ASSETS.—Section 1298,
13 as so redesignated, is amended by redesignating sub-
14 section (f) as subsection (g) and by inserting after sub-
15 section (e) the following new subsection:

16 “(f) METHOD FOR VALUING ASSETS.—For purposes
17 of section 1297(a)(2)—

18 “(1) PUBLICLY TRADED CORPORATIONS.—In
19 the case of a foreign corporation the stock in which
20 is readily tradeable on an established securities mar-
21 ket, the value of its assets shall be treated as being
22 equal to the sum of—

23 “(A) the aggregate value of its outstanding
24 stock, plus

25 “(B) its liabilities.

1 “(2) OTHER CORPORATIONS.—In the case of a
 2 foreign corporation to which paragraph (1) does not
 3 apply, the determination under subsection (a)(2)
 4 shall be based on the adjusted bases (as determined
 5 for purposes of computing earnings and profits) of
 6 its assets.”

7 **SEC. 105. EFFECTIVE DATE.**

8 The amendments made by this title shall apply to—

9 (1) taxable years of United States persons be-
 10 ginning after December 31, 1996, and

11 (2) taxable years of foreign corporations ending
 12 with or within such taxable years of United States
 13 persons.

14 **TITLE II—TREATMENT OF CON-**
 15 **TROLLED FOREIGN COR-**
 16 **PORATIONS**

17 **SEC. 201. GAIN ON CERTAIN STOCK SALES BY CONTROLLED**

18 **FOREIGN CORPORATIONS TREATED AS DIVI-**

19 **DENDS.**

20 (a) GENERAL RULE.—Section 964 (relating to mis-
 21 cellaneous provisions) is amended by adding at the end
 22 the following new subsection:

23 “(e) GAIN ON CERTAIN STOCK SALES BY CON-
 24 TROLLED FOREIGN CORPORATIONS TREATED AS DIVI-
 25 DENDS.—

1 “(1) IN GENERAL.—If a controlled foreign cor-
2 poration sells or exchanges stock in any other for-
3 eign corporation, gain recognized on such sale or ex-
4 change shall be included in the gross income of such
5 controlled foreign corporation as a dividend to the
6 same extent that it would have been so included
7 under section 1248(a) if such controlled foreign cor-
8 poration were a United States person. For purposes
9 of determining the amount which would have been so
10 includible, the determination of whether such other
11 foreign corporation was a controlled foreign corpora-
12 tion shall be made without regard to the preceding
13 sentence.

14 “(2) SAME COUNTRY EXCEPTION NOT APPLICA-
15 BLE.—Clause (i) of section 954(c)(3)(A) shall not
16 apply to any amount treated as a dividend by reason
17 of paragraph (1).

18 “(3) CLARIFICATION OF DEEMED SALES.—For
19 purposes of this subsection, a controlled foreign cor-
20 poration shall be treated as having sold or ex-
21 changed any stock if, under any provision of this
22 subtitle, such controlled foreign corporation is treat-
23 ed as having gain from the sale or exchange of such
24 stock.”

1 (b) AMENDMENT OF SECTION 904(d).—Clause (i) of
2 section 904(d)(2)(E) is amended by striking “and except
3 as provided in regulations, the taxpayer was a United
4 States shareholder in such corporation”.

5 (c) EFFECTIVE DATES.—

6 (1) The amendment made by subsection (a)
7 shall apply to gain recognized on transactions occur-
8 ring after the date of the enactment of this Act.

9 (2) The amendment made by subsection (b)
10 shall apply to distributions after the date of the en-
11 actment of this Act.

12 **SEC. 202. MISCELLANEOUS MODIFICATIONS TO SUBPART F.**

13 (a) SECTION 1248 GAIN TAKEN INTO ACCOUNT IN
14 DETERMINING PRO RATA SHARE.—

15 (1) IN GENERAL.—Paragraph (2) of section
16 951(a) (defining pro rata share of subpart F in-
17 come) is amended by adding at the end the following
18 new sentence:

19 “For purposes of subparagraph (B), any gain in-
20 cluded in the gross income of any person as a divi-
21 dend under section 1248 shall be treated as a dis-
22 tribution received by such person with respect to the
23 stock involved.”

1 (2) EFFECTIVE DATE.—The amendment made
2 by paragraph (1) shall apply to dispositions after the
3 date of the enactment of this Act.

4 (b) BASIS ADJUSTMENTS IN STOCK HELD BY FOR-
5 EIGN CORPORATION.—

6 (1) IN GENERAL.—Section 961 (relating to ad-
7 justments to basis of stock in controlled foreign cor-
8 porations and of other property) is amended by add-
9 ing at the end the following new subsection:

10 “(c) BASIS ADJUSTMENTS IN STOCK HELD BY FOR-
11 EIGN CORPORATION.—Under regulations prescribed by
12 the Secretary, if a United States shareholder is treated
13 under section 958(a)(2) as owning any stock in a con-
14 trolled foreign corporation which is actually owned by an-
15 other controlled foreign corporation, adjustments similar
16 to the adjustments provided by subsections (a) and (b)
17 shall be made to the basis of such stock in the hands of
18 such other controlled foreign corporation, but only for the
19 purposes of determining the amount included under sec-
20 tion 951 in the gross income of such United States share-
21 holder (or any other United States shareholder who ac-
22 quires from any person any portion of the interest of such
23 United States shareholder by reason of which such share-
24 holder was treated as owning such stock, but only to the
25 extent of such portion, and subject to such proof of iden-

1 tity of such interest as the Secretary may prescribe by reg-
2 ulations).”

3 (2) EFFECTIVE DATE.—The amendment made
4 by paragraph (1) shall apply for purposes of deter-
5 mining inclusions for taxable years of United States
6 shareholders beginning after December 31, 1996.

7 (c) DETERMINATION OF PREVIOUSLY TAXED IN-
8 COME IN SECTION 304 DISTRIBUTIONS, ETC.—

9 (1) IN GENERAL.—Section 959 (relating to ex-
10 clusion from gross income of previously taxed earn-
11 ings and profits) is amended by adding at the end
12 the following new subsection:

13 “(g) ADJUSTMENTS FOR CERTAIN TRANSACTIONS.—
14 If, by reason of—

15 “(1) a transaction to which section 304 applies,

16 “(2) the structure of a United States sharehold-
17 er’s holdings in controlled foreign corporations, or

18 “(3) other circumstances,

19 there would be a multiple inclusion of any item in income
20 (or an inclusion or exclusion without an appropriate basis
21 adjustment) by reason of this subpart, the Secretary may
22 prescribe regulations providing such modifications in the
23 application of this subpart as may be necessary to elimi-
24 nate such multiple inclusion or provide such basis adjust-
25 ment, as the case may be.”

1 (2) EFFECTIVE DATE.—The amendment made
2 by paragraph (1) shall take effect on the date of the
3 enactment of this Act.

4 (d) CLARIFICATION OF TREATMENT OF BRANCH TAX
5 EXEMPTIONS OR REDUCTIONS.—

6 (1) IN GENERAL.—Subsection (b) of section
7 952 is amended by adding at the end the following
8 new sentence: “For purposes of this subsection, any
9 exemption (or reduction) with respect to the tax im-
10 posed by section 884 shall not be taken into ac-
11 count.”

12 (2) EFFECTIVE DATE.—The amendment made
13 by paragraph (1) shall apply to taxable years begin-
14 ning after December 31, 1986.

15 **SEC. 203. INDIRECT FOREIGN TAX CREDIT ALLOWED FOR**
16 **CERTAIN LOWER TIER COMPANIES.**

17 (a) SECTION 902 CREDIT.—

18 (1) IN GENERAL.—Subsection (b) of section
19 902 (relating to deemed taxes increased in case of
20 certain 2nd and 3rd tier foreign corporations) is
21 amended to read as follows:

22 “(b) DEEMED TAXES INCREASED IN CASE OF CER-
23 TAIN LOWER TIER CORPORATIONS.—

24 “(1) IN GENERAL.—If—

1 “(A) any foreign corporation is a member
2 of a qualified group, and

3 “(B) such foreign corporation owns 10 per-
4 cent or more of the voting stock of another
5 member of such group from which it receives
6 dividends in any taxable year,

7 such foreign corporation shall be deemed to have
8 paid the same proportion of such other member’s
9 post-1986 foreign income taxes as would be deter-
10 mined under subsection (a) if such foreign corpora-
11 tion were a domestic corporation.

12 “(2) QUALIFIED GROUP.—For purposes of
13 paragraph (1), the term ‘qualified group’ means—

14 “(A) the foreign corporation described in
15 subsection (a), and

16 “(B) any other foreign corporation if—

17 “(i) the domestic corporation owns at
18 least 5 percent of the voting stock of such
19 other foreign corporation indirectly
20 through a chain of foreign corporations
21 connected through stock ownership of at
22 least 10 percent of their voting stock,

23 “(ii) the foreign corporation described
24 in subsection (a) is the first tier corpora-
25 tion in such chain, and

1 “(iii) such other corporation is not
2 below the sixth tier in such chain.

3 The term ‘qualified group’ shall not include any for-
4 foreign corporation below the third tier in the chain re-
5 ferred to in clause (i) unless such foreign corpora-
6 tion is a controlled foreign corporation (as defined in
7 section 957) and the domestic corporation is a Unit-
8 ed States shareholder (as defined in section 951(b))
9 in such foreign corporation. Paragraph (1) shall
10 apply to those taxes paid by a member of the quali-
11 fied group below the third tier only with respect to
12 periods during which it was a controlled foreign cor-
13 poration.”

14 (2) CONFORMING AMENDMENTS.—

15 (A) Subparagraph (B) of section 902(c)(3)
16 is amended by adding “or” at the end of clause
17 (i) and by striking clauses (ii) and (iii) and in-
18 serting the following new clause:

19 “(ii) the requirements of subsection
20 (b)(2) are met with respect to such foreign
21 corporation.”

22 (B) Subparagraph (B) of section 902(c)(4)
23 is amended by striking “3rd foreign corpora-
24 tion” and inserting “sixth tier foreign corpora-
25 tion”.

1 (C) The heading for paragraph (3) of sec-
2 tion 902(c) is amended by striking “WHERE DO-
3 MESTIC CORPORATION ACQUIRES 10 PERCENT
4 OF FOREIGN CORPORATION” and inserting
5 “WHERE FOREIGN CORPORATION FIRST QUALI-
6 FIES”.

7 (D) Paragraph (3) of section 902(c) is
8 amended by striking “ownership” each place it
9 appears.

10 (b) SECTION 960 CREDIT.—Paragraph (1) of section
11 960(a) (relating to special rules for foreign tax credits)
12 is amended to read as follows:

13 “(1) DEEMED PAID CREDIT.—For purposes of
14 subpart A of this part, if there is included under
15 section 951(a) in the gross income of a domestic cor-
16 poration any amount attributable to earnings and
17 profits of a foreign corporation which is a member
18 of a qualified group (as defined in section 902(b))
19 with respect to the domestic corporation, then, ex-
20 cept to the extent provided in regulations, section
21 902 shall be applied as if the amount so included
22 were a dividend paid by such foreign corporation
23 (determined by applying section 902(c) in accord-
24 ance with section 904(d)(3)(B)).”

25 (c) EFFECTIVE DATE.—

1 (1) IN GENERAL.—The amendments made by
2 this section shall apply to taxes of foreign corpora-
3 tions for taxable years of such corporations begin-
4 ning after the date of enactment of this Act.

5 (2) SPECIAL RULE.—In the case of any chain
6 of foreign corporations described in clauses (i) and
7 (ii) of section 902(b)(2)(B) of the Internal Revenue
8 Code of 1986 (as amended by this section), no liq-
9 uidation, reorganization, or similar transaction in a
10 taxable year beginning after the date of the enact-
11 ment of this Act shall have the effect of permitting
12 taxes to be taken into account under section 902 of
13 the Internal Revenue Code of 1986 which could not
14 have been taken into account under such section but
15 for such transaction.

16 **SEC. 204. EXEMPTION FOR ACTIVE FINANCING INCOME.**

17 (a) EXEMPTION FROM FOREIGN PERSONAL HOLD-
18 ING COMPANY INCOME.—Subsection (c) of section 954 is
19 amended by adding at the end the following new para-
20 graph:

21 “(4) CERTAIN INCOME DERIVED IN ACTIVE
22 CONDUCT OF TRADE OR BUSINESS.—

23 “(A) IN GENERAL.—For purposes of para-
24 graph (1), foreign personal holding company in-
25 come shall not include income which is—

1 “(i) derived in or incident to the ac-
2 tive conduct by a controlled foreign cor-
3 poration of a banking, financing, or similar
4 business, but only if the corporation is pre-
5 dominantly engaged in the active conduct
6 of such business,

7 “(ii) received from a person other
8 than a related person (within the meaning
9 of subsection (d)(3)) and derived from the
10 investments made by a qualifying insur-
11 ance company of its unearned premiums or
12 reserves ordinary and necessary for the
13 proper conduct of its insurance business,
14 or

15 “(iii) received from a person other
16 than a related person (within the meaning
17 of subsection (d)(3)) and derived from in-
18 vestments made by a qualifying insurance
19 company of an amount of its assets equal
20 to—

21 “(I) in the case of contracts reg-
22 ulated in the country in which sold as
23 property, casualty, or health insurance
24 contracts, one-third of its premiums
25 earned on insurance contracts during

1 the taxable year (as defined in section
2 832(b)(4)), and

3 “(II) in the case of contracts reg-
4 ulated in the country in which sold as
5 life insurance or annuity contracts,
6 the greater of 10 percent of the re-
7 serves described in clause (ii) or
8 \$10,000,000,

9 which are not directly or indirectly attrib-
10 utable to the insurance or reinsurance of
11 risks of persons who are related persons
12 (within the meaning of subsection (d)(3)).

13 “(B) APPLICABLE PRINCIPLES.—

14 “(i) BANKING, ETC. INCOME.—The
15 Secretary shall prescribe regulations which
16 interpret subparagraph (A)(i) in accord-
17 ance with the applicable principles of sec-
18 tion 904(d)(2)(C).

19 “(ii) LOOK-THRU RULES.—The Sec-
20 retary shall prescribe regulations consist-
21 ent with the principles of section 904(d)(3)
22 which provide that dividends, interest, in-
23 come equivalent to interest, rents, or royal-
24 ties received or accrued from a related per-
25 son (within the meaning of subsection

1 (d)(3)) shall be subject to look-thru treat-
2 ment for purposes of this section.

3 “(iii) SPECIAL RULE FOR BANKING OR
4 SECURITIES BUSINESS.—In the case of a
5 corporation described in subparagraph
6 (C)(ii), the regulations under clauses (i)
7 and (ii) shall be consistent with the appli-
8 cable principles of section 1296(b) (as in
9 effect on the day before the enactment of
10 the International Tax Simplification for
11 American Competitiveness Act).

12 “(C) PREDOMINANTLY ENGAGED.—For
13 purposes of subparagraph (A)(i), a corporation
14 shall be deemed predominantly engaged in the
15 active conduct of a banking, financing or simi-
16 lar business only if—

17 “(i) more than 70 percent of its gross
18 income from such business is derived from
19 transactions with unrelated persons (as de-
20 fined in subsection (d)(3)), and more than
21 20 percent of its gross income from that
22 business is derived from transactions with
23 unrelated persons (as so defined) located
24 within the country under the laws of which

1 the controlled foreign corporation is cre-
2 ated or organized, or

3 “(ii) the corporation is—

4 “(I) predominantly engaged in
5 the active conduct of a banking or se-
6 curities business (within the meaning
7 of section 1296(b), as in effect before
8 the enactment of the International
9 Tax Simplification for Competitive-
10 ness Act), or

11 “(II) a qualified bank affiliate or
12 a qualified securities affiliate for pur-
13 poses of section 1296(b) (as so in ef-
14 fect).

15 “(D) QUALIFYING INSURANCE COMPANY.—

16 For purposes of clauses (ii) and (iii) of sub-
17 paragraph (A), the term ‘qualifying insurance
18 company’ means any entity which is subject to
19 regulation as an insurance company under the
20 laws of its country of incorporation and which
21 realizes at least 50 percent of its gross income
22 (other than gross income derived from invest-
23 ments) from premiums written on risks situated
24 within its country of incorporation.”

1 (b) EXEMPTION FROM FOREIGN BASE COMPANY
 2 SERVICES INCOME.—Paragraph (2) of section 954(e) is
 3 amended by striking “or” at the end of subparagraph (A),
 4 by striking the period at the end of subparagraph (B) and
 5 inserting “, or”, and by adding at the end the following:

6 “(C) the active conduct by a controlled for-
 7 eign corporation of a banking, financing, insur-
 8 ance, or similar business, but only if the cor-
 9 poration is predominantly engaged in the active
 10 conduct of that business (within the meaning of
 11 subsection (c)(4)(C)).”

12 (c) EFFECTIVE DATE.—The amendments made by
 13 this section shall apply to taxable years of foreign corpora-
 14 tions beginning after December 31, 1996, and to taxable
 15 years of United States shareholders with or within which
 16 such taxable years of foreign corporations end.

17 **SEC. 205. REPEAL OF SEPARATE FOREIGN TAX CREDIT LIM-**
 18 **ITATION FOR NONCONTROLLED SECTION 902**
 19 **CORPORATIONS.**

20 (a) REPEAL OF SEPARATE BASKET.—

21 (1) IN GENERAL.—Subparagraph (E) of section
 22 904(d)(1) is amended to read as follows:

23 “(E) in the case of a corporation, divi-
 24 dends from noncontrolled section 902 corpora-
 25 tions out of earnings and profits accumulated in

1 taxable years beginning before January 1,
2 1997.”.

3 (2) CONFORMING AMENDMENTS.—

4 (A) Subparagraph (E) of section 904(d)(2)
5 is repealed.

6 (B) Section 904(d)(2)(A)(ii) is amended by
7 striking “subparagraph (E)(iii) or”.

8 (C) Section 904(d)(2)(C)(iii)(II) is amend-
9 ed by inserting “out of earnings and profits ac-
10 cumulated in taxable years beginning before
11 January 1, 1997” after “corporation”.

12 (b) APPLICATION OF LOOK-THRU RULES TO NON-
13 CONTROLLED SECTION 902 CORPORATIONS.—

14 (1) IN GENERAL.—Section 904(d)(3) is amend-
15 ed by adding at the end the following new subpara-
16 graph:

17 “(J) LOOK-THRU APPLIES TO NONCON-
18 TROLLED SECTION 902 CORPORATIONS.—

19 “(i) IN GENERAL.—For purposes of
20 this paragraph (other than subparagraph
21 (E) thereof)—

22 “(I) any foreign corporation
23 which is a noncontrolled section 902
24 corporation with respect to the tax-
25 payer shall be treated as a controlled

1 foreign corporation with respect to the
2 taxpayer, and

3 “(II) the taxpayer shall be treat-
4 ed as a United States shareholder in
5 such corporation.

6 “(ii) NONCONTROLLED SECTION 902
7 CORPORATION.—For purposes of this sub-
8 section, the term ‘noncontrolled section
9 902 corporation’ means, with respect to
10 any taxpayer, any foreign corporation with
11 respect to which the taxpayer meets the
12 stock ownership requirements of subsection
13 (a) or (b) of section 902 and which is not
14 otherwise a controlled foreign corporation.”

15 (2) CONFORMING AMENDMENTS.—

16 (A) Section 904(d)(5)(C) is amended by
17 inserting “or noncontrolled section 902 corpora-
18 tions” after “controlled foreign corporations”.

19 (B) The heading for section 904(d)(3) is
20 amended by inserting “AND CERTAIN OTHER
21 CORPORATIONS” after “CORPORATIONS”.

22 (c) EFFECTIVE DATES.—

23 (1) IN GENERAL.—The amendments made by
24 this section shall apply to taxable years of foreign
25 corporations beginning after December 31, 1996,

1 and to taxable years of United States shareholders
2 with or within which such taxable years of foreign
3 corporations end.

4 (2) DIVIDENDS.—The amendments made by
5 this section shall apply to dividends paid out of
6 earnings and profits accumulated during taxable
7 years of foreign corporations beginning after Decem-
8 ber 31, 1996. For purposes of the preceding sen-
9 tence, the rules of section 316 of the Internal Reve-
10 nue Code of 1986 shall apply.

11 **SEC. 206. COUNTRIES IN EUROPEAN UNION TREATED AS A**
12 **SINGLE COUNTRY UNDER SAME COUNTRY**
13 **EXCEPTIONS.**

14 (a) IN GENERAL.—Subsection (d) of section 954 is
15 amended by adding at the end the following new para-
16 graph:

17 “(5) COUNTRIES IN EUROPEAN UNION TREAT-
18 ED AS 1 COUNTRY.—

19 “(A) IN GENERAL.—For purposes of this
20 subsection, subsections (c), (e), and (g), and
21 section 953(a)(1), in the case of a controlled
22 foreign corporation which is created or orga-
23 nized under the laws of a country included in
24 the European Union, all countries included in
25 such Union shall be considered 1 country.

1 “(B) EXCEPTION WHERE NO SUBSTANTIAL
2 EFFECTIVE RATE OF TAX.—Subparagraph (A)
3 shall not apply to a controlled foreign corpora-
4 tion unless such corporation is subject to a sub-
5 stantial effective rate of foreign tax on income
6 described in such subsection.”

7 (b) EFFECTIVE DATE.—The amendment made by
8 this section shall apply to taxable years of foreign corpora-
9 tions beginning after December 31, 1996, and to taxable
10 years of United States shareholders with or within which
11 such taxable years of foreign corporations end.

12 **SEC. 207. EXPANSION OF DE MINIMIS RULE UNDER SUB-**
13 **PART F.**

14 (a) IN GENERAL.—Subparagraph (A) of section
15 954(b)(3) (relating to de minimis, etc., rules) is amended
16 to read as follows:

17 “(A) DE MINIMIS RULE.—If the sum of
18 foreign base company income (determined with-
19 out regard to paragraph (5)) and the gross in-
20 surance income for the taxable year is less than
21 10 percent of gross income, no part of the gross
22 income for the taxable year shall be treated as
23 foreign base company income or insurance in-
24 come.”

25 (b) TECHNICAL AMENDMENTS.—

1 (1) Clause (ii) of section 864(d)(5)(A) is
2 amended by striking “5 percent or \$1,000,000” and
3 inserting “10 percent”.

4 (2) Clause (i) of section 881(c)(5)(A) is amend-
5 ed by striking “5 percent or \$1,000,000” and insert-
6 ing “10 percent”.

7 (c) EFFECTIVE DATE.—The amendments made by
8 this section shall apply to taxable years beginning after
9 December 31, 1996.

10 **SEC. 208. SUBPART F EARNINGS AND PROFITS DETER-**
11 **MINED UNDER GENERALLY ACCEPTED AC-**
12 **COUNTING PRINCIPLES.**

13 (a) IN GENERAL.—Subsection (a) of section 964 (re-
14 lating to miscellaneous provisions) is amended by striking
15 “rules substantially similar to those applicable to domestic
16 corporations, under regulations prescribed by the Sec-
17 retary” and inserting “generally accepted accounting prin-
18 ciples in the United States”.

19 (b) EFFECTIVE DATE.—The amendment made by
20 subsection (a) shall apply to distributions during, and the
21 determination of the inclusion under section 951 of the
22 Internal Revenue Code of 1986 with respect to, taxable
23 years of foreign corporations beginning after December
24 31, 1996.

1 **SEC. 209. AFFILIATED FOREIGN INSURANCE COMPANIES**
2 **MAY OFFSET LOSSES.**

3 (a) **IN GENERAL.**—Section 953(d)(3) is amended by
4 adding at the end the following new subparagraph:

5 “(B) **SPECIAL RULE WHERE 2 OR MORE**
6 **ELECTING COMPANIES ARE AFFILIATED.**—If 2
7 or more corporations treated as domestic cor-
8 porations under this subsection—

9 “(i) were created or organized under
10 the laws of the same foreign country,

11 “(ii) are treated as members of the
12 same affiliated group for purposes of chap-
13 ter 6, and

14 “(iii) elect the application of this sub-
15 paragraph,

16 such corporations shall be treated as 1 corpora-
17 tion for purposes of subparagraph (A).”

18 (b) **CONFORMING AMENDMENT.**—Section 953(d)(3)
19 is amended by striking “If” and inserting: “(A) **IN GEN-**
20 **ERAL.**—If”.

21 (c) **EFFECTIVE DATE.**—The amendments made by
22 this section shall apply to taxable years beginning after
23 December 31, 1996.

1 **TITLE III—OTHER PROVISIONS**

2 **SEC. 301. EXCHANGE RATE USED IN TRANSLATING FOR-**
3 **EIGN TAXES.**

4 (a) ACCRUED TAXES TRANSLATED BY USING AVER-
5 AGE RATE FOR YEAR TO WHICH TAXES RELATE.—

6 (1) IN GENERAL.—Subsection (a) of section
7 986 (relating to translation of foreign taxes) is
8 amended to read as follows:

9 “(a) FOREIGN INCOME TAXES.—

10 “(1) TRANSLATION OF ACCRUED TAXES.—

11 “(A) IN GENERAL.—For purposes of deter-
12 mining the amount of the foreign tax credit, in
13 the case of a taxpayer who takes foreign income
14 taxes into account when accrued, the amount of
15 any foreign income taxes (and any adjustment
16 thereto) shall be translated into dollars by using
17 the average exchange rate for the taxable year
18 to which such taxes relate.

19 “(B) EXCEPTION FOR TAXES NOT PAID
20 WITHIN FOLLOWING 2 YEARS.—

21 “(i) Subparagraph (A) shall not apply
22 to any foreign income taxes paid after the
23 date 2 years after the close of the taxable
24 year to which such taxes relate.

1 “(ii) Subparagraph (A) shall not
2 apply to taxes paid before the beginning of
3 the taxable year to which such taxes relate.

4 “(C) EXCEPTION FOR INFLATIONARY CUR-
5 RENCIES.—Subparagraph (A) shall not apply to
6 any foreign income taxes the liability for which
7 is denominated in any currency determined to
8 be an inflationary currency under regulations
9 prescribed by the Secretary.

10 “(D) CROSS REFERENCE.—

**“For adjustments where tax is not paid within 2
 years, see section 905(c).**

11 “(2) TRANSLATION OF TAXES TO WHICH PARA-
12 GRAPH (1) DOES NOT APPLY.—For purposes of de-
13 termining the amount of the foreign tax credit, in
14 the case of any foreign income taxes to which sub-
15 paragraph (A) of paragraph (1) does not apply—

16 “(A) such taxes shall be translated into
17 dollars using the exchange rates as of the time
18 such taxes were paid to the foreign country or
19 possession of the United States, and

20 “(B) any adjustment to the amount of
21 such taxes shall be translated into dollars
22 using—

23 “(i) except as provided in clause (ii),
24 the exchange rate as of the time when such

1 adjustment is paid to the foreign country
2 or possession, or

3 “(ii) in the case of any refund or cred-
4 it of foreign income taxes, using the ex-
5 change rate as of the time of the original
6 payment of such foreign income taxes.

7 “(3) FOREIGN INCOME TAXES.—For purposes
8 of this subsection, the term ‘foreign income taxes’
9 means any income, war profits, or excess profits
10 taxes paid or accrued to any foreign country or to
11 any possession of the United States.”

12 (2) ADJUSTMENT WHEN NOT PAID WITHIN 2
13 YEARS AFTER YEAR TO WHICH TAXES RELATE.—
14 Subsection (c) of section 905 is amended to read as
15 follows:

16 “(c) ADJUSTMENTS TO ACCRUED TAXES.—

17 “(1) IN GENERAL.—If—

18 “(A) accrued taxes when paid differ from
19 the amounts claimed as credits by the taxpayer,

20 “(B) accrued taxes are not paid before the
21 date 2 years after the close of the taxable year
22 to which such taxes relate, or

23 “(C) any tax paid is refunded in whole or
24 in part,

1 the taxpayer shall notify the Secretary, who shall re-
2 determine the amount of the tax for the year or
3 years affected.

4 “(2) SPECIAL RULE FOR TAXES NOT PAID
5 WITHIN 2 YEARS.—In making the redetermination
6 under paragraph (1), no credit shall be allowed for
7 accrued taxes not paid before the date referred to in
8 subparagraph (B) of paragraph (1). Any such taxes
9 subsequently paid shall be taken into account for the
10 taxable year to which they relate and a redetermina-
11 tion under this section shall be made on account of
12 such payment.

13 “(3) ADJUSTMENTS.—The amount of tax due
14 on any redetermination under paragraph (1) (if any)
15 shall be paid by the taxpayer on notice and demand
16 by the Secretary, and the amount of tax overpaid (if
17 any) shall be credited or refunded to the taxpayer in
18 accordance with subchapter B of chapter 66 (section
19 6511 et seq.).

20 “(4) BOND REQUIREMENTS.—In the case of
21 any tax accrued but not paid, the Secretary, as a
22 condition precedent to the allowance of the credit
23 provided in this subpart, may require the taxpayer
24 to give a bond, with sureties satisfactory to and ap-
25 proved by the Secretary, in such sum as the Sec-

1 retary may require, conditioned on the payment by
2 the taxpayer of any amount of tax found due on any
3 such redetermination. Any such bond shall contain
4 such further conditions as the Secretary may re-
5 quire.

6 “(5) OTHER SPECIAL RULES.—In any redeter-
7 mination under paragraph (1) by the Secretary of
8 the amount of tax due from the taxpayer for the
9 year or years affected by a refund, the amount of
10 the taxes refunded for which credit has been allowed
11 under this section shall be reduced by the amount of
12 any tax described in section 901 imposed by the for-
13 eign country or possession of the United States with
14 respect to such refund; but no credit under this sub-
15 part, or deduction under section 164, shall be al-
16 lowed for any taxable year with respect to any such
17 tax imposed on the refund. No interest shall be as-
18 sessed or collected on any amount of tax due on any
19 redetermination by the Secretary, resulting from a
20 refund to the taxpayer, for any period before the re-
21 ceipt of such refund, except to the extent interest
22 was paid by the foreign country or possession of the
23 United States on such refund for such period.”

24 (b) AUTHORITY TO USE AVERAGE RATES.—

1 (1) IN GENERAL.—Subsection (a) of section
2 986 (as amended by subsection (a)) is amended by
3 redesignating paragraph (3) as paragraph (4) and
4 inserting after paragraph (2) the following new
5 paragraph:

6 “(3) AUTHORITY TO PERMIT USE OF AVERAGE
7 RATES.—To the extent prescribed in regulations, the
8 average exchange rate for the period (specified in
9 such regulations) during which the taxes or adjust-
10 ment is paid may be used instead of the exchange
11 rate as of the time of such payment.”

12 (2) DETERMINATION OF AVERAGE RATES.—
13 Subsection (c) of section 989 is amended by striking
14 “and” at the end of paragraph (4), by striking the
15 period at the end of paragraph (5) and inserting “,
16 and”, and by adding at the end the following new
17 paragraph:

18 “(6) setting forth procedures for determining
19 the average exchange rate for any period.”

20 (3) CONFORMING AMENDMENTS.—Subsection
21 (b) of section 989 is amended by striking “weight-
22 ed” each place it appears.

23 (c) EFFECTIVE DATES.—

24 (1) IN GENERAL.—The amendments made by
25 subsections (a)(1) and (b) shall apply to taxes paid

1 or accrued in taxable years beginning after Decem-
 2 ber 31, 1996.

3 (2) SUBSECTION (a)(2).—The amendment made
 4 by subsection (a)(2) shall apply to taxes which relate
 5 to taxable years beginning after December 31, 1996.

6 **SEC. 302. ELECTION TO USE SIMPLIFIED SECTION 904 LIM-**
 7 **TATION FOR ALTERNATIVE MINIMUM TAX.**

8 (a) GENERAL RULE.—Subsection (a) of section 59
 9 (relating to alternative minimum tax foreign tax credit)
 10 is amended by adding at the end the following new para-
 11 graph:

12 “(4) ELECTION TO USE SIMPLIFIED SECTION
 13 904 LIMITATION.—

14 “(A) IN GENERAL.—In determining the al-
 15 ternative minimum tax foreign tax credit for
 16 any taxable year to which an election under this
 17 paragraph applies—

18 “(i) subparagraph (B) of paragraph
 19 (1) shall not apply, and

20 “(ii) the limitation of section 904
 21 shall be based on the proportion which—

22 “(I) the taxpayer’s taxable in-
 23 come (as determined for purposes of
 24 the regular tax) from sources without
 25 the United States (but not in excess

1 of the taxpayer's entire alternative
2 minimum taxable income), bears to

3 “(II) the taxpayer's entire alter-
4 native minimum taxable income for
5 the taxable year.

6 “(B) ELECTION.—

7 “(i) IN GENERAL.—An election under
8 this paragraph may be made only for the
9 taxpayer's first taxable year which begins
10 after December 31, 1996, and for which
11 the taxpayer claims an alternative mini-
12 mum tax foreign tax credit.

13 “(ii) ELECTION REVOCABLE ONLY
14 WITH CONSENT.—An election under this
15 paragraph, once made, shall apply to the
16 taxable year for which made and all subse-
17 quent taxable years unless revoked with
18 the consent of the Secretary.”

19 (b) EFFECTIVE DATE.—The amendments made by
20 this section shall apply to taxable years beginning after
21 December 31, 1996.

22 **SEC. 303. MODIFICATION OF SECTION 1491.**

23 (a) GENERAL RULE.—So much of chapter 5 (relating
24 to tax on transfers to avoid income tax) as precedes sec-
25 tion 1492 is amended to read as follows:

1 **“CHAPTER 5—TREATMENT OF TRANSFERS**
2 **TO AVOID INCOME TAX**

“Sec. 1491. Recognition of gain.

“Sec. 1492. Exceptions.

3 **“SEC. 1491. RECOGNITION OF GAIN.**

4 “In the case of any transfer of property by a United
5 States person to a foreign corporation as paid-in surplus
6 or as a contribution to capital, to a foreign estate or trust,
7 or to a foreign partnership, for purposes of this subtitle
8 (other than for purposes of section 679), such transfer
9 shall be treated as a sale or exchange for an amount equal
10 to the fair market value of the property transferred, and
11 the transferor shall recognize as gain the excess of—

12 “(1) the fair market value of the property so
13 transferred, over

14 “(2) the adjusted basis (for purposes of deter-
15 mining gain) of such property in the hands of the
16 transferor.

17 If a trust which is not a foreign trust becomes a foreign
18 trust, such trust shall be treated for purposes of this sec-
19 tion as having transferred, immediately before becoming
20 a foreign trust, all of its assets to a foreign trust.”

21 (b) CONFORMING AMENDMENTS.—

22 (1) Section 1057 is hereby repealed.

23 (2) Section 1492 is amended to read as follows:

1 **“SEC. 1492. EXCEPTIONS.**

2 “The provisions of section 1491 shall not apply—

3 “(1) if the transferee is an organization exempt
4 from income tax under part I of subchapter F of
5 chapter 1 (other than an organization described in
6 section 401(a)),

7 “(2) to a transfer described in section 367, or

8 “(3) to any other transfer, to the extent pro-
9 vided in regulations in accordance with principles
10 similar to the principles of section 367 or otherwise
11 consistent with the purpose of section 1491.”

12 (3) Section 1494 is hereby repealed.

13 (4) Paragraph (8) of section 6501(c) is amend-
14 ed by inserting “or on any transfer by reason of sec-
15 tion 1491” after “section 367”.

16 (5) Subsection (a) of section 6038B is amended
17 by striking “or” at the end of paragraph (1), by
18 adding “or” at the end of paragraph (2), and by in-
19 serting after paragraph (2) the following new para-
20 graph:

21 “(3) makes any transfer described in section
22 1491,”.

23 (6) The table of sections for part IV of sub-
24 chapter O of chapter 1 is amended by striking the
25 item relating to section 1057.

1 (7) The table of chapters for subtitle A is
2 amended by striking “Tax on” in the item relating
3 to chapter 5 and inserting “Treatment of”.

4 (c) EFFECTIVE DATE.—The amendments made by
5 this section shall apply to transfers after December 31,
6 1996.

7 **SEC. 304. MODIFICATION OF SECTION 367(b).**

8 (a) GENERAL RULE.—Paragraph (1) of section
9 367(b) is amended to read as follows:

10 “(1) IN GENERAL.—In the case of any trans-
11 action described in section 332, 351, 354, 355, 356,
12 or 361 in which the status of a foreign corporation
13 as a corporation is a general condition for non-
14 recognition by 1 or more of the parties to the trans-
15 action, income shall be required to be recognized to
16 the extent provided in regulations prescribed by the
17 Secretary which are necessary or appropriate to pre-
18 vent the avoidance of Federal income taxes. This
19 subsection shall not apply to a transaction in which
20 the foreign corporation is not treated as a corpora-
21 tion under subsection (a)(1).”

22 (b) EFFECTIVE DATE.—The amendment made by
23 subsection (a) shall apply to transfers after December 31,
24 1996.

1 **SEC. 305. INCREASE IN FILING THRESHOLDS FOR RETURNS**
2 **AS TO ORGANIZATION OF FOREIGN COR-**
3 **PORATIONS AND ACQUISITIONS OF STOCK IN**
4 **SUCH CORPORATIONS.**

5 (a) IN GENERAL.—Subsection (a) of section 6046
6 (relating to returns as to organization or reorganization
7 of foreign corporations and as to acquisitions of their
8 stock) is amended to read as follows:

9 “(a) REQUIREMENT OF RETURN.—

10 “(1) IN GENERAL.—A return complying with
11 the requirements of subsection (b) shall be made
12 by—

13 “(A) each United States citizen or resident
14 who becomes an officer or director of a foreign
15 corporation if a United States person (as de-
16 fined in section 7701(a)(30)) meets the stock
17 ownership requirements of paragraph (2) with
18 respect to such corporation,

19 “(B) each United States person—

20 “(i) who acquires stock which, when
21 added to any stock owned on the date of
22 such acquisition, meets the stock owner-
23 ship requirements of paragraph (2) with
24 respect to a foreign corporation, or

25 “(ii) who acquires stock which, with-
26 out regard to stock owned on the date of

1 such acquisition, meets the stock owner-
2 ship requirements of paragraph (2) with
3 respect to a foreign corporation,

4 “(C) each person (not described in sub-
5 paragraph (B)) who is treated as a United
6 States shareholder under section 953(c) with
7 respect to a foreign corporation, and

8 “(D) each person who becomes a United
9 States person while meeting the stock owner-
10 ship requirements of paragraph (2) with respect
11 to stock of a foreign corporation.

12 In the case of a foreign corporation with respect to
13 which any person is treated as a United States
14 shareholder under section 953(c), subparagraph (A)
15 shall be treated as including a reference to each
16 United States person who is an officer or director of
17 such corporation.

18 “(2) STOCK OWNERSHIP REQUIREMENTS.—A
19 person meets the stock ownership requirements of
20 this paragraph with respect to any corporation if
21 such person owns 10 percent or more of—

22 “(A) the total combined voting power of all
23 classes of stock of such corporation entitled to
24 vote, or

1 “(B) the total value of the stock of such
2 corporation.”

3 (b) **EFFECTIVE DATE.**—The amendment made by
4 this section shall take effect on January 1, 1997.

5 **SEC. 306. APPLICATION OF UNIFORM CAPITALIZATION**
6 **RULES TO FOREIGN PERSONS.**

7 (a) **IN GENERAL.**—Section 263A(c) (relating to ex-
8 ceptions) is amended by adding at the end the following
9 new paragraph:

10 “(7) **FOREIGN PERSONS.**—This section shall
11 apply to any taxpayer who is not a United States
12 person only for purposes of tax liability with respect
13 to income which is effectively connected with the
14 conduct of a trade or business in the United
15 States.”

16 (b) **EFFECTIVE DATE.**—The amendment made by
17 subsection (a) shall apply to taxable years beginning after
18 December 31, 1996. Section 481 of the Internal Revenue
19 Code of 1986 shall not apply to any change in a method
20 of accounting by reason of such amendment.

21 **SEC. 307. EXTENSION OF PERIOD TO WHICH EXCESS FOR-**
22 **EIGN TAXES MAY BE CARRIED.**

23 (a) **GENERAL RULE.**—Subsection (c) of section 904
24 (relating to carryback and carryover of excess tax paid)
25 is amended—

1 (1) by inserting “in the third preceding taxable
2 year,” before “in the second preceding taxable
3 year”, and

4 (2) by striking “in the first, second, third,
5 fourth, or fifth” and inserting “in any of the first
6 15”.

7 (b) **EXCESS EXTRACTION TAXES.**—Paragraph (1) of
8 section 907(f) is amended—

9 (1) by inserting “in the third preceding taxable
10 year,” before “in the second preceding taxable
11 year”, and

12 (2) by striking “in the first, second, third,
13 fourth, or fifth” and inserting “in any of the first
14 15”.

15 (c) **EFFECTIVE DATE.**—The amendments made by
16 this section shall apply to excess foreign taxes for taxable
17 years beginning after December 31, 1996.

18 **SEC. 308. RECHARACTERIZATION OF OVERALL DOMESTIC**

19 **LOSS.**

20 (a) **GENERAL RULE.**—Section 904 is amended by re-
21 designating subsections (g), (h), (i), and (j) as subsections
22 (h), (i), (j), and (k), respectively, and by inserting after
23 subsection (f) the following new subsection:

24 “(g) **RECHARACTERIZATION OF OVERALL DOMESTIC**
25 **LOSS.**—

1 “(1) GENERAL RULE.—For purposes of this
2 subpart, in the case of any taxpayer who sustains an
3 overall domestic loss for any taxable year beginning
4 after December 31, 1996, that portion of the tax-
5 payer’s taxable income from sources within the Unit-
6 ed States for each succeeding taxable year which is
7 equal to the lesser of—

8 “(A) the amount of such loss (to the extent
9 not used under this paragraph in prior taxable
10 years), or

11 “(B) 50 percent of the taxpayer’s taxable
12 income from sources within the United States
13 for such succeeding taxable year,
14 shall be treated as income from sources without the
15 United States (and not as income from sources with-
16 in the United States).

17 “(2) OVERALL DOMESTIC LOSS DEFINED.—For
18 purposes of this subsection—

19 “(A) IN GENERAL.—The term ‘overall do-
20 mestic loss’ means any domestic loss to the ex-
21 tent such loss offsets taxable income from
22 sources without the United States for the tax-
23 able year or for any preceding taxable year by
24 reason of a carryback. For purposes of the pre-
25 ceding sentence, the term ‘domestic loss’ means

1 the amount by which the gross income for the
2 taxable year from sources within the United
3 States is exceeded by the sum of the deductions
4 properly apportioned or allocated thereto (deter-
5 mined without regard to any carryback from a
6 subsequent taxable year).

7 “(B) TAXPAYER MUST HAVE ELECTED
8 FOREIGN TAX CREDIT FOR YEAR OF LOSS.—
9 The term ‘overall domestic loss’ shall not in-
10 clude any loss for any taxable year unless the
11 taxpayer chose the benefits of this subpart for
12 such taxable year.

13 “(3) CHARACTERIZATION OF SUBSEQUENT IN-
14 COME.—

15 “(A) IN GENERAL.—Any income from
16 sources within the United States that is treated
17 as income from sources without the United
18 States under paragraph (1) shall be allocated
19 among and increase the income categories in
20 proportion to the loss from sources within the
21 United States previously allocated to those in-
22 come categories.

23 “(B) INCOME CATEGORY.—For purposes of
24 this paragraph, the term ‘income category’ has

1 the meaning given to such term by subsection
2 (f)(5)(E)(i).

3 “(4) COORDINATION WITH SUBSECTION (f).—
4 The Secretary shall prescribe such regulations as
5 may be necessary to coordinate the provisions of this
6 subsection with the provisions of subsection (f).”

7 (b) CONFORMING AMENDMENT.—Subparagraph (A)
8 of section 936(a)(2) is amended by striking “section
9 904(f)” and inserting “subsections (f) and (g) of section
10 904”.

11 (c) EFFECTIVE DATE.—The amendments made by
12 this section shall apply to losses for taxable years begin-
13 ning after December 31, 1996.

14 **SEC. 309. TREATMENT OF NONRESIDENT ALIENS ENGAGED**
15 **IN INTERNATIONAL TRANSPORTATION SERV-**
16 **ICES.**

17 (a) SOURCING RULES.—

18 (1) IN GENERAL.—Section 861(a)(3) is amend-
19 ed by adding at the end the following new flush sen-
20 tence:

21 “In addition, compensation for labor or services per-
22 formed in the United States shall not be deemed to
23 be income from sources within the United States if
24 the labor or services are performed by a nonresident
25 alien individual in connection with the individual’s

1 temporary presence in the United States as a mem-
2 ber of the crew of a foreign aircraft or vessel en-
3 gaged in transportation between the United States
4 and a foreign country or a possession of the United
5 States.”

6 (2) TRANSPORTATION INCOME.—Subparagraph
7 (B) of section 863(c)(2) is amended by inserting
8 “the taxpayer is a citizen or resident alien and”
9 after “unless”.

10 (b) EXCLUSION FROM INCOME.—Section 872(b) is
11 amended by redesignating paragraphs (6) and (7) as para-
12 graphs (7) and (8), respectively, and by inserting after
13 paragraph (5) the following new paragraph:

14 “(6) PERSONAL SERVICES OF CREW MEM-
15 BERS.—Income derived by an individual resident of
16 a foreign country from personal services as an indi-
17 vidual crew member on board a vessel or aircraft to
18 which paragraph (1) or (2) applies.”

19 (c) PRESENCE IN UNITED STATES.—

20 (1) IN GENERAL.—Paragraph (7) of section
21 7701(b) is amended by adding at the end the follow-
22 ing new subparagraph:

23 “(D) CREW MEMBERS TEMPORARILY
24 PRESENT.—If an individual is temporarily
25 present in the United States as a member of

1 the crew of a foreign aircraft or vessel engaged
2 in transportation between the United States
3 and a foreign country or a possession of the
4 United States, such individual shall not be
5 treated as present in the United States on any
6 such day.”

7 (2) CONFORMING AMENDMENT.—Subparagraph
8 (A) of section 7701(b)(7) is amended by striking “or
9 (C)” and inserting “, (C), or (D)”.

10 (d) EFFECTIVE DATES.—

11 (1) IN GENERAL.—The amendments made by
12 this section shall apply to remuneration for services
13 performed after the date of the enactment of this
14 Act.

15 (2) PRESENCE.—The amendment made by sub-
16 section (c) shall apply to taxable years beginning
17 after December 31, 1996.

18 **SEC. 310. EXPORT PROPERTY OF FSC TO INCLUDE COM-**
19 **PUTER SOFTWARE.**

20 (a) IN GENERAL.—Section 927(a)(2) is amended by
21 adding at the end the following new sentence: “Computer
22 software (whether or not patented) shall not be treated
23 as described in subparagraph (B).”

1 (b) EFFECTIVE DATE.—The amendment made by
2 this section shall apply to sales, exchanges, or other dis-
3 positions after the date of the enactment of this Act.

4 **SEC. 311. SPECIAL RULES RELATING TO FINANCIAL SERV-**
5 **ICES INCOME.**

6 (a) EXCEPTION FOR INTEREST ON CERTAIN SECURI-
7 TIES.—Subparagraph (B) of section 904(d)(2) (relating to
8 high withholding tax interest) is amended by redesignating
9 clause (iii) as clause (iv) and by inserting after clause (ii)
10 the following new clause:

11 “(iii) EXCEPTION FOR INTEREST ON
12 DEALER PROPERTY.—The term ‘high with-
13 holding tax interest’ shall not include any
14 interest on a security (within the meaning
15 of section 475(c)(2)) which is received or
16 accrued by a person that holds the security
17 in connection with the holder’s activities as
18 a dealer in securities (within the meaning
19 of section 475(c)(1)).”

20 (b) DE MINIMIS RULE.—Subparagraph (C) of sec-
21 tion 904(d)(2) (relating to financial services income) is
22 amended by adding at the end the following new clause:

23 “(iv) DE MINIMIS RULE.—If the fi-
24 nancial services income (as defined by
25 clause (i)) of any person exceeds 80 per-

1 cent of gross income, the entire gross in-
2 come for the taxable year shall be treated
3 as financial services income.”

4 (c) EXCEPTION FOR INCOME ON DEALER PROP-
5 ERTY.—Subsection 904(g) is amended by redesignating
6 paragraph (11) as paragraph (12) and by adding after
7 paragraph (10) the following new paragraph:

8 “(11) EXCEPTION FOR INCOME ON DEALER
9 PROPERTY.—Paragraph (1) shall not apply to any
10 amount derived from a United States-owned foreign
11 corporation that is derived from income on a secu-
12 rity (within the meaning of section 475(c)(2)) which
13 is received or accrued by a person that holds the se-
14 curity in connection with the holder’s activities as a
15 dealer in securities (within the meaning of section
16 475(c)(1)).”

17 (d) EFFECTIVE DATES.—

18 (1) IN GENERAL.—The amendments made by
19 this section shall apply to taxable years beginning
20 after December 31, 1996.

21 (2) DEEMED PAID CREDITS.—In the case of
22 any credit under section 901 of the Internal Revenue
23 Code of 1986 by reason of section 902 or 960 of
24 such Code, the amendments made by this section
25 shall apply to taxable years of foreign corporations

1 beginning after December 31, 1996, and to taxable
2 years of United States shareholders in such corpora-
3 tions with or within which such taxable years of for-
4 eign corporations end.

5 **SEC. 312. UNITED STATES PROPERTY NOT TO INCLUDE**
6 **CERTAIN ASSETS ACQUIRED BY DEALERS IN**
7 **ORDINARY COURSE OF TRADE OR BUSINESS.**

8 (a) IN GENERAL.—Section 956(c)(2) is amended by
9 striking “and” at the end of subparagraph (H), by strik-
10 ing the period at the end of subparagraph (I) and insert-
11 ing a semicolon, and by adding at the end the following
12 new subparagraphs:

13 “(J) deposits of cash or securities made or
14 received on commercial terms in the ordinary
15 course of a United States or foreign person’s
16 business as a dealer in securities or in commod-
17 ities, but only to the extent such deposits are
18 made or received as collateral or margin for (i)
19 a securities loan, notional principal contract,
20 options contract, forward contract, or futures
21 contract, or (ii) any other financial transaction
22 in which the Secretary determines that it is cus-
23 tomary to post collateral or margin;

24 “(K) an obligation of a United States per-
25 son to the extent the principal amount of the

1 obligation does not exceed the fair market value
2 of readily marketable securities sold or pur-
3 chased pursuant to a sale and repurchase
4 agreement or otherwise posted or received as
5 collateral for the obligation in the ordinary
6 course of its business by a United States or for-
7 eign person which is a dealer in securities or
8 commodities; and

9 “(L) securities acquired and held by a con-
10 trolled foreign corporation in the ordinary
11 course of its business as a dealer in securities
12 if (i) the dealer accounts for the securities as
13 securities held primarily for sale to customers
14 in the ordinary course of business, and (ii) the
15 dealer disposes of the securities (or they mature
16 while held by the dealer) within a period con-
17 sistent with the holding of securities for sale to
18 customers in the ordinary course of business.

19 For purposes of subparagraphs (J), (K), and (L),
20 the term ‘dealer in securities’ has the meaning given
21 such term by section 475(c)(1), and the term ‘dealer
22 in commodities’ means a futures commission mer-
23 chant or any person which would be a dealer in se-
24 curities if securities under section 475(c)(2) included
25 commodities, evidences of an interest in commod-

1 ities, and derivative instruments in respect of com-
2 modities (other than any activity gain or loss from
3 which is described in section 1256(a)(3)).”

4 (b) EFFECTIVE DATE.—The amendments made by
5 this section shall apply to taxable years of foreign corpora-
6 tions beginning after December 31, 1996, and to taxable
7 years of United States shareholders or with or within
8 which such taxable years of foreign corporations end.

○