

105TH CONGRESS
1ST SESSION

H. R. 1517

To amend the Internal Revenue Code of 1986 to reduce the capital gains tax on individuals and to index the basis of assets of individuals for purposes of determining gains and losses.

IN THE HOUSE OF REPRESENTATIVES

MAY 1, 1997

Mr. COOKSEY introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to reduce the capital gains tax on individuals and to index the basis of assets of individuals for purposes of determining gains and losses.

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. REDUCTION IN INDIVIDUAL CAPITAL GAINS**

4 **RATE.**

5 (a) IN GENERAL.—Subsection (h) of section 1 of the
6 Internal Revenue Code of 1986 (relating to maximum cap-
7 ital gains rate) is amended to read as follows:

8 “(h) MAXIMUM CAPITAL GAINS RATE.—

1 “(1) IN GENERAL.—If a taxpayer has a net
2 capital gain for any taxable year, the tax imposed by
3 this section for such taxable year shall not exceed
4 the sum of—

5 “(A) a tax computed at the rates and in
6 the same manner as if this subsection had not
7 been enacted on taxable income reduced by the
8 net capital gain, plus

9 “(B) a tax equal to the applicable percent-
10 age of the net capital gain or, if less, taxable
11 income.

12 “(2) APPLICABLE PERCENTAGE.—For purposes
13 of paragraph (1), the term ‘applicable percentage’
14 means the percentage determined in accordance with
15 the following table:

“For taxable years beginning in:	The applicable percentage is:
1997	20
1998	19
1999	18
2000	17
2001	16
2002	15
2003	14
2004	13
2005	12
2006	11
2007	10
2008	9
2009	8
2010	7
2011	6
2012	5
2013	4
2014	3
2015	2
2016	1
2017 or thereafter	0.

1 “(3) NET CAPITAL GAIN TAKEN INTO ACCOUNT
2 AS INVESTMENT INCOME.—For purposes of this sub-
3 section and section 55(b)(1)(A)(ii), the net capital
4 gain for any taxable year shall be reduced (but not
5 below zero) by the amount which the taxpayer elects
6 to take into account as investment income under sec-
7 tion 163(d)(4)(B)(iii).”

8 (b) MINIMUM TAX.—

9 (1) IN GENERAL.—Subparagraph (A) of section
10 55(b)(1) of such Code is amended by redesignating
11 clauses (ii) and (iii) as clauses (iii) and (iv), respec-
12 tively, and by inserting after clause (i) the following
13 new clause:

14 “(ii) MAXIMUM RATE OF TAX ON NET
15 CAPITAL GAIN.—The amount determined
16 under the first sentence of clause (i) shall
17 not exceed the sum of—

18 “(I) the amount determined
19 under such first sentence computed at
20 the rates and in the same manner as
21 if this clause had not been enacted on
22 the taxable excess reduced by the net
23 capital gain, plus

24 “(II) a tax equal to the applica-
25 ble percentage (as defined in section

1 1(h)) of the lesser of the net capital
2 gain or the taxable excess.”

3 (2) CONFORMING AMENDMENT.—Clause (iii) of
4 section 55(a)(1)(A) of such Code (as redesignated by
5 paragraph (1)) is amended by striking “clause (i)”
6 and inserting “this subparagraph”.

7 (c) CONFORMING AMENDMENTS.—

8 (1) Section 1202 of such Code (relating to 50-
9 percent exclusion for gain from certain small busi-
10 ness stock) is hereby repealed.

11 (2)(A) Subsection (a) of section 57 of such
12 Code is amended by striking paragraph (7).

13 (B) Subclause (II) of section 53(d)(1)(B)(ii) of
14 such Code is amended by striking “, (5), and (7)”
15 and inserting “and (5)”.

16 (3) Paragraph (1) of section 170(e) of such
17 Code is amended—

18 (A) by inserting after “the amount of
19 gain” in the material following subparagraph
20 (B)(ii) the following: “(or in the case of a tax-
21 payer other than a corporation, the appropriate
22 percentage of the amount of gain)”, and

23 (B) by adding at the end the following new
24 sentence: “In the case of a taxpayer other than
25 a corporation, for purposes of subparagraph

1 (B), the term ‘appropriate percentage’ means
2 the percentage equal to the fraction the numer-
3 ator of which is the applicable percentage under
4 section 1(h) over 28 percent.”

5 (4) Paragraph (2) of section 172(d) of such
6 Code is amended to read as follows:

7 “(2) CAPITAL GAINS AND LOSSES OF TAX-
8 PAYERS OTHER THAN CORPORATIONS.—In the case
9 of a taxpayer other than a corporation, the amount
10 deductible on account of losses from sales or ex-
11 changes of capital assets shall not exceed the
12 amount includible on account of gains from sales or
13 exchanges of capital assets.”

14 (5) Paragraph (4) of section 642(c) of such
15 Code is amended by striking the first sentence.

16 (6) Paragraph (3) of section 643(a) of such
17 Code is amended by striking the last sentence.

18 (7) Paragraph (4) of section 691(c) of such
19 Code is amended by striking “1202,”.

20 (8) The second sentence of section 871(a)(2) of
21 such Code is amended by striking “such gains and
22 losses shall be determined without regard to section
23 1202 and”.

24 (9) Subsection (d) of section 1044 of such Code
25 is amended by striking the last sentence.

1 (10) Paragraph (1) of section 1445(e) of such
2 Code is amended by striking “28 percent” and in-
3 serting “the applicable percentage under section
4 1(h)”.

5 (11) Section 6652 of such Code is amended by
6 striking subsection (k) and by redesignating sub-
7 sections (l) and (m) as subsections (k) and (l), re-
8 spectively.

9 (12)(A) The second sentence of section
10 7518(g)(6)(A) of such Code is amended by striking
11 “28 percent” and inserting “the applicable percent-
12 age under section 1(h)”.

13 (B) The second sentence of section
14 607(h)(6)(A) of the Merchant Marine Act, 1936 is
15 amended by striking “28 percent” and inserting
16 “the applicable percentage under section 1(h)”.

17 (13) The table of sections for part I of sub-
18 chapter P of chapter 1 of such Code is amended by
19 striking the item relating to section 1202.

20 (d) EFFECTIVE DATES.—

21 (1) IN GENERAL.—Except as provided in para-
22 graph (2), the amendments made by this section
23 shall apply to taxable years beginning after Decem-
24 ber 31, 1996.

1 (2) WITHHOLDING.—The amendment made by
2 subsection (c)(10) shall apply to amounts paid after
3 the date of the enactment of this Act.

4 **SEC. 2. INDEXING OF CERTAIN ASSETS FOR PURPOSES OF**
5 **DETERMINING GAIN OR LOSS.**

6 (a) IN GENERAL.—Part II of subchapter O of chap-
7 ter 1 of the Internal Revenue Code of 1986 (relating to
8 basis rules of general application) is amended by inserting
9 after section 1021 the following new section:

10 **“SEC. 1022. INDEXING OF CERTAIN ASSETS FOR PURPOSES**
11 **OF DETERMINING GAIN OR LOSS.**

12 “(a) GENERAL RULE.—

13 “(1) INDEXED BASIS SUBSTITUTED FOR AD-
14 JUSTED BASIS.—Solely for purposes of determining
15 gain or loss on the sale or other disposition by a tax-
16 payer (other than a corporation) of an indexed asset
17 which has been held for more than 3 years, the in-
18 dexed basis of the asset shall be substituted for its
19 adjusted basis.

20 “(2) EXCEPTION FOR DEPRECIATION, ETC.—

21 The deductions for depreciation, depletion, and am-
22 ortization shall be determined without regard to the
23 application of paragraph (1) to the taxpayer or any
24 other person.

25 “(b) INDEXED ASSET.—

1 “(1) IN GENERAL.—For purposes of this sec-
2 tion, the term ‘indexed asset’ means—

3 “(A) common stock in a C corporation
4 (other than a foreign corporation), and

5 “(B) tangible property,
6 which is a capital asset or property used in the trade
7 or business (as defined in section 1231(b)).

8 “(2) STOCK IN CERTAIN FOREIGN CORPORA-
9 TIONS INCLUDED.—For purposes of this section—

10 “(A) IN GENERAL.—The term ‘indexed
11 asset’ includes common stock in a foreign cor-
12 poration which is regularly traded on an estab-
13 lished securities market.

14 “(B) EXCEPTION.—Subparagraph (A)
15 shall not apply to—

16 “(i) stock of a foreign investment
17 company (within the meaning of section
18 1246(b)),

19 “(ii) stock in a passive foreign invest-
20 ment company (as defined in section
21 1296),

22 “(iii) stock in a foreign corporation
23 held by a United States person who meets
24 the requirements of section 1248(a)(2),
25 and

1 “(iv) stock in a foreign personal hold-
2 ing company (as defined in section 552).

3 “(C) TREATMENT OF AMERICAN DEPOSI-
4 TORY RECEIPTS.—An American depository re-
5 ceipt for common stock in a foreign corporation
6 shall be treated as common stock in such cor-
7 poration.

8 “(c) INDEXED BASIS.—For purposes of this sec-
9 tion—

10 “(1) GENERAL RULE.—The indexed basis for
11 any asset is—

12 “(A) the adjusted basis of the asset, in-
13 creased by

14 “(B) the applicable inflation adjustment.

15 “(2) APPLICABLE INFLATION ADJUSTMENT.—
16 The applicable inflation adjustment for any asset is
17 an amount equal to—

18 “(A) the adjusted basis of the asset, multi-
19 plied by

20 “(B) the percentage (if any) by which—

21 “(i) the gross domestic product
22 deflator for the last calendar quarter end-
23 ing before the asset is disposed of, exceeds

24 “(ii) the gross domestic product
25 deflator for the last calendar quarter end-

1 ing before the asset was acquired by the
2 taxpayer (or, if later, the calendar quarter
3 ending on December 31, 1996).

4 The percentage under subparagraph (B) shall be
5 rounded to the nearest $\frac{1}{10}$ of 1 percentage point.

6 “(3) GROSS DOMESTIC PRODUCT DEFLATOR.—

7 The gross domestic product deflator for any cal-
8 endar quarter is the implicit price deflator for the
9 gross domestic product for such quarter (as shown
10 in the last revision thereof released by the Secretary
11 of Commerce before the close of the following cal-
12 endar quarter).

13 “(d) SUSPENSION OF HOLDING PERIOD WHERE DI-
14 MINISHED RISK OF LOSS; TREATMENT OF SHORT
15 SALES.—

16 “(1) IN GENERAL.—If the taxpayer (or a relat-
17 ed person) enters into any transaction which sub-
18 stantially reduces the risk of loss from holding any
19 asset, such asset shall not be treated as an indexed
20 asset for the period of such reduced risk.

21 “(2) SHORT SALES.—

22 “(A) IN GENERAL.—In the case of a short
23 sale of an indexed asset with a short sale period
24 in excess of 3 years, for purposes of this title,
25 the amount realized shall be an amount equal

1 to the amount realized (determined without re-
2 gard to this paragraph) increased by the appli-
3 cable inflation adjustment. In applying sub-
4 section (c)(2) for purposes of the preceding sen-
5 tence, the date on which the property is sold
6 short shall be treated as the date of acquisition
7 and the closing date for the sale shall be treat-
8 ed as the date of disposition.

9 “(B) SHORT SALE PERIOD.—For purposes
10 of subparagraph (A), the short sale period be-
11 gins on the day that the property is sold and
12 ends on the closing date for the sale.

13 “(e) TREATMENT OF REGULATED INVESTMENT
14 COMPANIES AND REAL ESTATE INVESTMENT TRUSTS.—

15 “(1) ADJUSTMENTS AT ENTITY LEVEL.—

16 “(A) IN GENERAL.—Except as otherwise
17 provided in this paragraph, the adjustment
18 under subsection (a) shall be allowed to any
19 qualified investment entity (including for pur-
20 poses of determining the earnings and profits of
21 such entity).

22 “(B) EXCEPTION FOR CORPORATE SHARE-
23 HOLDERS.—Under regulations—

1 “(i) in the case of a distribution by a
2 qualified investment entity (directly or in-
3 directly) to a corporation—

4 “(I) the determination of whether
5 such distribution is a dividend shall be
6 made without regard to this section,
7 and

8 “(II) the amount treated as gain
9 by reason of the receipt of any capital
10 gain dividend shall be increased by the
11 percentage by which the entity’s net
12 capital gain for the taxable year (de-
13 termined without regard to this sec-
14 tion) exceeds the entity’s net capital
15 gain for such year determined with re-
16 gard to this section, and

17 “(ii) there shall be other appropriate
18 adjustments (including deemed distribu-
19 tions) so as to ensure that the benefits of
20 this section are not allowed (directly or in-
21 directly) to corporate shareholders of quali-
22 fied investment entities.

23 For purposes of the preceding sentence, any
24 amount includible in gross income under section
25 852(b)(3)(D) shall be treated as a capital gain

1 dividend and an S corporation shall not be
2 treated as a corporation.

3 “(C) EXCEPTION FOR QUALIFICATION
4 PURPOSES.—This section shall not apply for
5 purposes of sections 851(b) and 856(e).

6 “(D) EXCEPTION FOR CERTAIN TAXES IM-
7 POSED AT ENTITY LEVEL.—

8 “(i) TAX ON FAILURE TO DISTRIBUTE
9 ENTIRE GAIN.—If any amount is subject to
10 tax under section 852(b)(3)(A) for any
11 taxable year, the amount on which tax is
12 imposed under such section shall be in-
13 creased by the percentage determined
14 under subparagraph (B)(i)(II). A similar
15 rule shall apply in the case of any amount
16 subject to tax under paragraph (2) or (3)
17 of section 857(b) to the extent attributable
18 to the excess of the net capital gain over
19 the deduction for dividends paid deter-
20 mined with reference to capital gain divi-
21 dends only. The first sentence of this
22 clause shall not apply to so much of the
23 amount subject to tax under section
24 852(b)(3)(A) as is designated by the com-
25 pany under section 852(b)(3)(D).

1 “(ii) OTHER TAXES.—This section
2 shall not apply for purposes of determining
3 the amount of any tax imposed by para-
4 graph (4), (5), or (6) of section 857(b).

5 “(2) ADJUSTMENTS TO INTERESTS HELD IN
6 ENTITY.—

7 “(A) REGULATED INVESTMENT COMPA-
8 NIES.—Stock in a regulated investment com-
9 pany (within the meaning of section 851) shall
10 be an indexed asset for any calendar quarter in
11 the same ratio as—

12 “(i) the average of the fair market
13 values of the indexed assets held by such
14 company at the close of each month during
15 such quarter, bears to

16 “(ii) the average of the fair market
17 values of all assets held by such company
18 at the close of each such month.

19 “(B) REAL ESTATE INVESTMENT
20 TRUSTS.—Stock in a real estate investment
21 trust (within the meaning of section 856) shall
22 be an indexed asset for any calendar quarter in
23 the same ratio as—

1 “(i) the fair market value of the in-
2 dexed assets held by such trust at the close
3 of such quarter, bears to

4 “(ii) the fair market value of all as-
5 sets held by such trust at the close of such
6 quarter.

7 “(C) RATIO OF 80 PERCENT OR MORE.—If
8 the ratio for any calendar quarter determined
9 under subparagraph (A) or (B) would (but for
10 this subparagraph) be 80 percent or more, such
11 ratio for such quarter shall be 100 percent.

12 “(D) RATIO OF 20 PERCENT OR LESS.—If
13 the ratio for any calendar quarter determined
14 under subparagraph (A) or (B) would (but for
15 this subparagraph) be 20 percent or less, such
16 ratio for such quarter shall be zero.

17 “(E) LOOK-THRU OF PARTNERSHIPS.—For
18 purposes of this paragraph, a qualified invest-
19 ment entity which holds a partnership interest
20 shall be treated (in lieu of holding a partnership
21 interest) as holding its proportionate share of
22 the assets held by the partnership.

23 “(3) TREATMENT OF RETURN OF CAPITAL DIS-
24 TRIBUTIONS.—Except as otherwise provided by the
25 Secretary, a distribution with respect to stock in a

1 qualified investment entity which is not a dividend
2 and which results in a reduction in the adjusted
3 basis of such stock shall be treated as allocable to
4 stock acquired by the taxpayer in the order in which
5 such stock was acquired.

6 “(4) QUALIFIED INVESTMENT ENTITY.—For
7 purposes of this subsection, the term ‘qualified in-
8 vestment entity’ means—

9 “(A) a regulated investment company
10 (within the meaning of section 851), and

11 “(B) a real estate investment trust (within
12 the meaning of section 856).

13 “(f) OTHER PASS-THRU ENTITIES.—

14 “(1) PARTNERSHIPS.—

15 “(A) IN GENERAL.—In the case of a part-
16 nership, the adjustment made under subsection
17 (a) at the partnership level shall be passed
18 through to the partners.

19 “(B) SPECIAL RULE IN THE CASE OF SEC-
20 TION 754 ELECTIONS.—In the case of a transfer
21 of an interest in a partnership with respect to
22 which the election provided in section 754 is in
23 effect—

24 “(i) the adjustment under section
25 743(b)(1) shall, with respect to the trans-

1 feror partner, be treated as a sale of the
2 partnership assets for purposes of applying
3 this section, and

4 “(ii) with respect to the transferee
5 partner, the partnership’s holding period
6 for purposes of this section in such assets
7 shall be treated as beginning on the date
8 of such adjustment.

9 “(2) S CORPORATIONS.—In the case of an S
10 corporation, the adjustment made under subsection
11 (a) at the corporate level shall be passed through to
12 the shareholders. This section shall not apply for
13 purposes of determining the amount of any tax im-
14 posed by section 1374 or 1375.

15 “(3) COMMON TRUST FUNDS.—In the case of a
16 common trust fund, the adjustment made under sub-
17 section (a) at the trust level shall be passed through
18 to the participants.

19 “(4) INDEXING ADJUSTMENT DISREGARDED IN
20 DETERMINING LOSS ON SALE OF INTEREST IN EN-
21 TITY.—Notwithstanding the preceding provisions of
22 this subsection, for purposes of determining the
23 amount of any loss on a sale or exchange of an in-
24 terest in a partnership, S corporation, or common
25 trust fund, the adjustment made under subsection

1 (a) shall not be taken into account in determining
2 the adjusted basis of such interest.

3 “(g) DISPOSITIONS BETWEEN RELATED PERSONS.—

4 “(1) IN GENERAL.—This section shall not apply
5 to any sale or other disposition of property between
6 related persons except to the extent that the basis
7 of such property in the hands of the transferee is a
8 substituted basis.

9 “(2) RELATED PERSONS DEFINED.—For pur-
10 poses of this section, the term ‘related persons’
11 means—

12 “(A) persons bearing a relationship set
13 forth in section 267(b), and

14 “(B) persons treated as single employer
15 under subsection (b) or (c) of section 414.

16 “(h) TRANSFERS TO INCREASE INDEXING ADJUST-
17 MENT.—If any person transfers cash, debt, or any other
18 property to another person and the principal purpose of
19 such transfer is to secure or increase an adjustment under
20 subsection (a), the Secretary may disallow part or all of
21 such adjustment or increase.

22 “(i) SPECIAL RULES.—For purposes of this section—

23 “(1) TREATMENT OF IMPROVEMENTS, ETC.—If
24 there is an addition to the adjusted basis of any tan-
25 gible property or of any stock in a corporation dur-

1 ing the taxable year by reason of an improvement to
2 such property or a contribution to capital of such
3 corporation—

4 “(A) such addition shall never be taken
5 into account under subsection (e)(1)(A) if the
6 aggregate amount thereof during the taxable
7 year with respect to such property or stock is
8 less than \$1,000, and

9 “(B) such addition shall be treated as a
10 separate asset acquired at the close of such tax-
11 able year if the aggregate amount thereof dur-
12 ing the taxable year with respect to such prop-
13 erty or stock is \$1,000 or more.

14 A rule similar to the rule of the preceding sentence
15 shall apply to any other portion of an asset to the
16 extent that separate treatment of such portion is ap-
17 propriate to carry out the purposes of this section.

18 “(2) ASSETS WHICH ARE NOT INDEXED ASSETS
19 THROUGHOUT HOLDING PERIOD.—The applicable in-
20 flation adjustment shall be appropriately reduced for
21 periods during which the asset was not an indexed
22 asset.

23 “(3) TREATMENT OF CERTAIN DISTRIBUTIONS.—A distribution with respect to stock in a
24

1 corporation which is not a dividend shall be treated
2 as a disposition.

3 “(4) SECTION CANNOT INCREASE ORDINARY
4 LOSS.—To the extent that (but for this paragraph)
5 this section would create or increase a net ordinary
6 loss to which section 1231(a)(2) applies or an ordi-
7 nary loss to which any other provision of this title
8 applies, such provision shall not apply. The taxpayer
9 shall be treated as having a long-term capital loss in
10 an amount equal to the amount of the ordinary loss
11 to which the preceding sentence applies.

12 “(5) ACQUISITION DATE WHERE THERE HAS
13 BEEN PRIOR APPLICATION OF SUBSECTION (a)(1)
14 WITH RESPECT TO THE TAXPAYER.—If there has
15 been a prior application of subsection (a)(1) to an
16 asset while such asset was held by the taxpayer, the
17 date of acquisition of such asset by the taxpayer
18 shall be treated as not earlier than the date of the
19 most recent such prior application.

20 “(6) COLLAPSIBLE CORPORATIONS.—The appli-
21 cation of section 341(a) (relating to collapsible cor-
22 porations) shall be determined without regard to this
23 section.

1 “(j) REGULATIONS.—The Secretary shall prescribe
2 such regulations as may be necessary or appropriate to
3 carry out the purposes of this section.”

4 (b) CLERICAL AMENDMENT.—The table of sections
5 for part II of subchapter O of chapter 1 of such Code
6 is amended by inserting after the item relating to section
7 1021 the following new item:

“Sec. 1022. Indexing of certain assets for purposes of determining
gain or loss.”

8 (c) EFFECTIVE DATE.—The amendments made by
9 this section shall apply to dispositions after December 31,
10 1996, in taxable years ending after such date.

○