

105TH CONGRESS
1ST SESSION

H. R. 2513

To amend the Internal Revenue Code of 1986 to restore and modify the provision of the Taxpayer Relief Act of 1997 relating to exempting active financing income from foreign personal holding company income and to provide for the nonrecognition of gain on the sale of stock in agricultural processors to certain farmers' cooperatives.

IN THE HOUSE OF REPRESENTATIVES

SEPTEMBER 23, 1997

Mr. ARCHER (for himself, Mr. HULSHOF, Mr. RANGEL, Mr. THOMAS, Mr. HOUGHTON, Mr. NUSSLE, Ms. DUNN, and Mr. LEVIN) introduced the following bill; which was referred to the Committee on Ways and Means, and in addition to the Committee on the Budget, for a period to be subsequently determined by the Speaker, in each case for consideration of such provisions as fall within the jurisdiction of the committee concerned

A BILL

To amend the Internal Revenue Code of 1986 to restore and modify the provision of the Taxpayer Relief Act of 1997 relating to exempting active financing income from foreign personal holding company income and to provide for the nonrecognition of gain on the sale of stock in agricultural processors to certain farmers' cooperatives.

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

1 **SECTION 1. EXEMPTION FOR ACTIVE FINANCING INCOME.**

2 (a) EXEMPTION FROM FOREIGN PERSONAL HOLD-
3 ING COMPANY INCOME.—Section 954 of the Internal Rev-
4 enue Code of 1986 (as amended by subsection (d)) is
5 amended by adding at the end the following new sub-
6 section:

7 “(h) SPECIAL RULE FOR INCOME DERIVED IN THE
8 ACTIVE CONDUCT OF INSURANCE BUSINESSES AND
9 BANKING, FINANCING, OR SIMILAR BUSINESSES.—

10 “(1) IN GENERAL.—For purposes of subsection
11 (c)(1), foreign personal holding company income
12 shall not include income which is—

13 “(A) derived in the active conduct by a
14 controlled foreign corporation of a banking, fi-
15 nancing, or similar business, but only if—

16 “(i) the corporation is predominantly
17 engaged in the active conduct of such busi-
18 ness, and

19 “(ii) such income is derived from
20 transactions with customers located within
21 the country under the laws of which the
22 corporation is created or organized,

23 “(B) received from a person other than a
24 related person (within the meaning of sub-
25 section (d)(3)) and derived from the invest-
26 ments made by a qualifying insurance company

1 of its reserves or of 80 percent of its unearned
2 premiums (as both are determined in the man-
3 ner prescribed under paragraph (4)), or

4 “(C) received from a person other than a
5 related person (within the meaning of sub-
6 section (d)(3)) and derived from investments
7 made by a qualifying insurance company of an
8 amount of its assets equal to—

9 “(i) in the case of contracts regulated
10 in the country in which sold as property,
11 casualty, or health insurance contracts,
12 one-third of its premiums earned on such
13 insurance contracts during the taxable year
14 (as defined in section 832(b)(4)), and

15 “(ii) in the case of contracts regulated
16 in the country in which sold as life insur-
17 ance or annuity contracts, 10 percent of
18 the reserves described in subparagraph (B)
19 for such contracts.

20 “(2) PREDOMINANTLY ENGAGED.—For pur-
21 poses of paragraph (1)(A), a controlled foreign cor-
22 poration shall be deemed predominantly engaged in
23 the active conduct of a banking, financing, or similar
24 business only if—

1 “(A) more than 70 percent of its gross in-
2 come is derived from such business from trans-
3 actions with customers which are located within
4 the country under the laws of which the cor-
5 poration is created or organized, or

6 “(B) the corporation is—

7 “(i) engaged in the active conduct of
8 a banking business and is an institution li-
9 censed to do business as a bank in the
10 United States (or is any other corporation
11 not so licensed which is specified by the
12 Secretary in regulations), or

13 “(ii) engaged in the active conduct of
14 a securities business and is registered as a
15 securities broker or dealer under section
16 15(a) of the Securities Exchange Act of
17 1934 or is registered as a Government se-
18 curities broker or dealer under section
19 15C(a) of such Act (or is any other cor-
20 poration not so registered which is speci-
21 fied by the Secretary in regulations).

22 “(3) PRINCIPLES FOR DETERMINING INSUR-
23 ANCE INCOME.—Except as provided by the Sec-
24 retary, for purposes of paragraphs (1) (B) and
25 (C)—

1 “(A) in the case of any contract which is
2 a separate account-type contract (including any
3 variable contract not meeting the requirements
4 of section 817), income credited under such
5 contract shall be allocable only to such contract,
6 and

7 “(B) income not allocable under subpara-
8 graph (A) shall be allocated ratably among con-
9 tracts not described in subparagraph (A).

10 “(4) METHODS FOR DETERMINING UNEARNED
11 PREMIUMS AND RESERVES.—For purposes of para-
12 graph (1)(B)—

13 “(A) PROPERTY AND CASUALTY CON-
14 TRACTS.—The unearned premiums and reserves
15 of a qualifying insurance company with respect
16 to property, casualty, or health insurance con-
17 tracts shall be determined using the same meth-
18 ods and interest rates which would be used if
19 such company were subject to tax under sub-
20 chapter L.

21 “(B) LIFE INSURANCE AND ANNUITY CON-
22 TRACTS.—The amount of the reserve of a quali-
23 fying insurance company for any life insurance
24 or annuity contract shall be equal to the greater
25 of—

1 “(i) the net surrender value of such
2 contract (as defined in section
3 807(e)(1)(A)), or

4 “(ii) the reserve determined under
5 paragraph (5).

6 “(C) LIMITATION ON RESERVES.—In no
7 event shall the reserve determined under this
8 paragraph for any contract as of any time ex-
9 ceed the amount which would be taken into ac-
10 count with respect to such contract as of such
11 time in determining foreign statement reserves
12 (less any catastrophe, deficiency, or similar re-
13 serves).

14 “(5) AMOUNT OF RESERVE.—The amount of
15 the reserve determined under this paragraph with
16 respect to any contract shall be determined in the
17 same manner as it would be determined if the quali-
18 fying insurance company were subject to tax under
19 subchapter L, except that in applying such sub-
20 chapter—

21 “(A) the interest rate determined for the
22 foreign country in which such company is cre-
23 ated or organized and which, except as provided
24 by the Secretary, is calculated in the same man-
25 ner as the Federal mid-term rate under section

1 1274(d) shall be substituted for the applicable
2 Federal interest rate,

3 “(B) the highest assumed interest rate
4 permitted to be used in determining foreign
5 statement reserves shall be substituted for the
6 prevailing State assumed interest rate, and

7 “(C) tables for mortality and morbidity
8 which reasonably reflect the current mortality
9 and morbidity risks in the foreign country shall
10 be substituted for the mortality and morbidity
11 tables otherwise used for such subchapter.

12 “(6) DEFINITIONS.—For purposes of this sub-
13 section—

14 “(A) QUALIFYING INSURANCE COMPANY.—
15 The term ‘qualifying insurance company’ means
16 any entity which—

17 “(i) is subject to regulation as an in-
18 surance company by the country under the
19 laws of which the entity is created or orga-
20 nized,

21 “(ii) derives at least 50 percent of its
22 net written premiums from the insurance
23 or reinsurance of risks located within such
24 country, and

1 “(iii) is engaged in the active conduct
2 of an insurance business and would be sub-
3 ject to tax under subchapter L if it were
4 a domestic corporation.

5 “(B) LIFE INSURANCE OR ANNUITY CON-
6 TRACT.—For purposes of this section and sec-
7 tion 953, the determination of whether a con-
8 tract issued by a controlled foreign corporation
9 is a life insurance contract or an annuity con-
10 tract shall be made without regard to sections
11 72(s), 101(f), 817(h), and 7702 if—

12 “(i) such contract is regulated as a
13 life insurance or annuity contract by the
14 country under the laws of which the cor-
15 poration is created or organized, and

16 “(ii) no policyholder, insured, annu-
17 itant, or beneficiary with respect to the
18 contract is a United States person.

19 “(C) LOCATED.—

20 “(i) IN GENERAL.—The determination
21 of where a customer is located shall be
22 made under rules prescribed by the Sec-
23 retary.

24 “(ii) SPECIAL RULE FOR QUALIFIED
25 BUSINESS UNITS.—Gross income derived

1 by a corporation's qualified business unit
2 (within the meaning of section 989(a))
3 from transactions with customers which
4 are located in the country in which the
5 qualified business unit both maintains its
6 principal office and conducts substantial
7 business activity shall be treated as derived
8 from transactions with customers which
9 are located within the country under the
10 laws of which the controlled foreign cor-
11 poration is created or organized.

12 “(D) CUSTOMER.—

13 “(i) IN GENERAL.—The term ‘cus-
14 tomer’ means, with respect to any con-
15 trolled foreign corporation, any person
16 which has a customer relationship with
17 such corporation.

18 “(ii) EXCEPTION FOR RELATED, ETC.
19 PERSONS.—A person who is a related per-
20 son (as defined in section 954(d)(3)), an
21 officer, a director, or an employee with re-
22 spect to any controlled foreign corporation
23 shall not be treated as a customer with re-
24 spect to any transaction if a principal pur-

1 pose of such transaction is to satisfy any
2 requirement of this subsection.

3 “(7) ANTI-ABUSE RULES.—For purposes of ap-
4 plying this subsection and subsection (c)(2)(C)(ii),
5 there shall be disregarded any item of income, gain,
6 loss, or deduction with respect to any transaction or
7 series of transactions one of the principal purposes
8 of which is qualifying income or gain for the exclu-
9 sion under this section, including—

10 “(A) any change in the method of comput-
11 ing reserves or any other transaction or series
12 of transactions a principal purpose of which is
13 the acceleration or deferral of any item in order
14 to claim the benefits of such exclusion through
15 the application of this subsection, and

16 “(B) organizing entities in order to satisfy
17 any same country requirement under this sub-
18 section.

19 “(8) COORDINATION WITH OTHER PROVI-
20 SIONS.—

21 “(A) SECTION 901(K).—This subsection,
22 subsection (c)(2)(C)(ii), and subsection
23 (e)(2)(C) shall not apply for any taxable year of
24 a foreign corporation unless such corporation
25 (and all members of each affiliated group of

1 which such corporation is a member) elect not
2 to have the provisions of section 901(k)(4)
3 apply to any taxes paid or accrued during such
4 taxable year by such foreign corporation or any
5 such member.

6 “(B) SECTION 953.—This subsection shall
7 not apply to investment income allocable to con-
8 tracts that insure related party risks or risks lo-
9 cated in a foreign country other than the coun-
10 try in which the qualifying insurance company
11 is created or organized.

12 “(9) APPLICATION.—This subsection, sub-
13 section (e)(2)(C)(ii), and subsection (e)(2)(C) shall
14 apply only to the first full taxable year of a foreign
15 corporation beginning after December 31, 1997, and
16 before January 1, 1999, and to taxable years of
17 United States shareholders with or within which
18 such taxable year of such foreign corporation ends.”.

19 (b) SPECIAL RULES FOR DEALERS.—Section
20 954(e)(2)(C) of such Code is amended to read as follows:

21 “(C) EXCEPTION FOR DEALERS.—Except
22 as provided by regulations, in the case of a reg-
23 ular dealer in property (within the meaning of
24 paragraph (1)(B)), forward contracts, option
25 contracts, or similar financial instruments (in-

1 including notional principal contracts and all in-
2 struments referenced to commodities), there
3 shall not be taken into account in computing
4 foreign personal holding income—

5 “(i) any item of income, gain, deduc-
6 tion, or loss (other than any item described
7 in subparagraph (A), (E), or (G) of para-
8 graph (1)) from any transaction (including
9 hedging transactions) entered into in the
10 ordinary course of such dealer’s trade or
11 business as such a dealer, and

12 “(ii) if such dealer is a dealer in secu-
13 rities (within the meaning of section 475),
14 any interest or dividend or equivalent
15 amount described in subparagraph (E) or
16 (G) of paragraph (1) from any transaction
17 (including any hedging transaction or
18 transaction described in section
19 956(c)(2)(J)) entered into in the ordinary
20 course of such dealer’s trade or business as
21 such a dealer in securities, but only if em-
22 ployees of the dealer which are located in
23 the country under the laws of which the
24 dealer is created or organized (or in the
25 case of a qualified business unit described

1 in section 989(a) which both maintains its
2 principal office and conducts substantial
3 business activity in a country, employees of
4 such unit which are located in such coun-
5 try) materially participate in such trans-
6 action.”.

7 (c) EXEMPTION FROM FOREIGN BASE COMPANY
8 SERVICES INCOME.—Paragraph (2) of section 954(e) of
9 such Code (as amended by subsection (d)) is amended by
10 striking “or” at the end of subparagraph (A), by striking
11 the period at the end of subparagraph (B) and inserting
12 “, or”, and by adding at the end the following:

13 “(C)(i) a transaction the income from
14 which is not foreign personal holding company
15 income by reason of subsection (h), or

16 “(ii) a transaction to which subsection
17 (e)(2)(C)(ii) applies.”.

18 (d) REPEAL OF CANCELED PROVISIONS.—Section
19 1175 of the Taxpayer Relief Act of 1997, and the amend-
20 ments made by such section, are hereby repealed, and the
21 Internal Revenue Code of 1986 shall be applied and ad-
22 ministered as if such section (and amendments) had never
23 been enacted.

24 (e) BUDGETARY TREATMENT.—For purposes of sec-
25 tion 10213 of the Balanced Budget Act of 1997, the provi-

1 sions of this section shall be considered to have been en-
2 acted as part of the Taxpayer Relief Act of 1997.

3 **SEC. 2. NONRECOGNITION OF GAIN ON SALE OF STOCK TO**
4 **CERTAIN FARMERS' COOPERATIVES.**

5 (a) IN GENERAL.—Part III of subchapter O of chap-
6 ter 1 of the Internal Revenue Code of 1986 (relating to
7 nontaxable exchanges) is amended by inserting after sec-
8 tion 1042 the following new section:

9 **“SEC. 1042A. SALES OF STOCK TO CERTAIN FARMERS' CO-**
10 **OPERATIVES.**

11 “(a) NONRECOGNITION OF GAIN.—If—

12 “(1) the taxpayer elects the application of this
13 section with respect to any sale of qualified agricul-
14 tural processor stock,

15 “(2) the taxpayer purchases qualified replace-
16 ment property within the replacement period, and

17 “(3) the requirements of subsection (c) are met
18 with respect to such sale,

19 then the gain (if any) on such sale which would be recog-
20 nized as long-term capital gain shall be recognized only
21 to the extent that the amount realized on such sale exceeds
22 the cost to the taxpayer of such qualified replacement
23 property.

24 “(b) LIMITATION.—

1 “(1) IN GENERAL.—If subsection (a) applies to
2 the sale of any stock by the taxpayer in a qualified
3 agricultural processor, the aggregate amount of gain
4 taken into account by the taxpayer under subsection
5 (a) with respect to stock in such processor shall not
6 exceed the amount of the limitation under paragraph
7 (2) which is allocated to such sale by the eligible
8 farmers’ cooperative.

9 “(2) ALLOCATION.—The amount allocated
10 under this paragraph by any cooperative with re-
11 spect to stock acquired by such cooperative during
12 any taxable year of such cooperative shall not exceed
13 \$75,000,000.

14 “(3) AGGREGATION RULES.—All eligible farm-
15 ers’ cooperatives which are under common control
16 (within the meaning of subsection (a) or (b) of sec-
17 tion 52) shall be treated as 1 cooperative for pur-
18 poses of paragraph (2), and the limitation under
19 such paragraph shall be allocated among such co-
20 operatives in such manner as the Secretary shall
21 prescribe.

22 “(c) REQUIREMENTS TO QUALIFY FOR NON-
23 RECOGNITION.—A sale of qualified agricultural processor
24 stock meets the requirements of this subsection if—

1 “(1) SALE TO ELIGIBLE FARMERS’ COOPERA-
2 TIVE.—Such stock is sold to an eligible farmers’ co-
3 operative.

4 “(2) COOPERATIVE MUST HOLD 100 PERCENT
5 OF STOCK AFTER SALE.—The eligible farmers’ coop-
6 erative owns, immediately after the sale, all of the
7 qualified agricultural processor stock of the corpora-
8 tion.

9 “(3) WRITTEN STATEMENT AND HOLDING PE-
10 RIOD.—Requirements similar to the requirements of
11 paragraphs (3) and (4) of section 1042(b) are met.

12 “(d) DEFINITIONS.—For purposes of this section—

13 “(1) QUALIFIED AGRICULTURAL PROCESSOR
14 STOCK.—The term ‘qualified agricultural processor
15 stock’ means stock (other than stock described in
16 section 1504(a)(4)) issued by a qualified agricultural
17 processor.

18 “(2) QUALIFIED AGRICULTURAL PROCESSOR.—
19 The term ‘qualified agricultural processor’ means a
20 domestic C corporation—

21 “(A) substantially all of the assets of
22 which are used in the active conduct of the
23 trade or business of refining or processing agri-
24 cultural or horticultural products in the United
25 States, and

1 “(B) which, during at least 3 of the 5 most
2 recent taxable years of such processor ending
3 on or before the date of the sale, purchased
4 more than one-half of such products to be re-
5 fined or processed from—

6 “(i) farmers who make up the eligible
7 farmers’ cooperative which is purchasing
8 stock in the corporation in a transaction to
9 which this subsection is to apply, or

10 “(ii) such cooperative.

11 “(3) ELIGIBLE FARMERS’ COOPERATIVE.—The
12 term ‘eligible farmers’ cooperative’ means an organi-
13 zation to which part I of subchapter T applies and
14 which is engaged in the marketing of agricultural or
15 horticultural products.

16 “(4) REPLACEMENT PERIOD.—The term ‘re-
17 placement period’ means the period which begins 3
18 months before the date on which the sale of qualified
19 agricultural processor stock occurs and which ends
20 12 months after the date of such sale.

21 “(5) QUALIFIED REPLACEMENT PROPERTY.—

22 “(A) IN GENERAL.—Except as provided in
23 subparagraph (B), the term ‘qualified replace-
24 ment property’ has the meaning given such
25 term by section 1042(c)(4).

1 “(B) EXCEPTION.—The term ‘qualified re-
2 placement property’ shall not include any secu-
3 rity issued by the taxpayer or by any corpora-
4 tion controlled by the taxpayer immediately
5 after the purchase. For purposes of the preced-
6 ing sentence, the term ‘control’ has the mean-
7 ing given such term by section 304(c) (deter-
8 mined by substituting ‘10 percent’ for ‘50 per-
9 cent’ each place it appears in paragraph (1)
10 thereof).

11 “(e) SPECIAL RULES.—

12 “(1) IN GENERAL.—Except as otherwise pro-
13 vided in this subsection, rules similar to the rules of
14 paragraphs (5) and (6) of section 1042(c), sub-
15 sections (d), (e), and (f) of section 1042, section
16 1016(a)(22), and section 1223(13) shall apply for
17 purposes of this section.

18 “(2) CERTAIN PROVISIONS NOT TO APPLY.—

19 “(A) RECOGNITION ON COMPLETE LIQ-
20 UIDATION.—Section 332 shall not apply to the
21 liquidation into the cooperative or any related
22 person of a qualified agricultural processor if
23 the cooperative or related person acquired the
24 stock in such processor in a sale to which sub-
25 section (a) applied.

1 “(1) TERMS USED IN SECTION 1042a.—Terms
2 used in this section which also are used in section
3 1042A shall have the respective meanings given such
4 terms by section 1042A.

5 “(2) DISPOSITION.—

6 “(A) IN GENERAL.—The term ‘disposition’
7 includes any distribution.

8 “(B) EXCHANGES AS PART OF REORGA-
9 NIZATION.—Such term shall not include an ex-
10 change of stock in any reorganization described
11 in section 368(a)(1) for stock of another cor-
12 poration except to the extent that such reorga-
13 nization results in the cooperative owning di-
14 rectly or indirectly less than all outstanding
15 stock of the processor (other than stock de-
16 scribed in section 1504(a)(4)).

17 “(C) ISSUANCES OF NEW STOCK.—Any is-
18 suance of new stock of the processor (other
19 than to the cooperative) shall be treated as a
20 disposition of such stock by the cooperative and
21 the cooperative shall be treated as realizing on
22 such disposition an amount equal to the fair
23 market value of such stock as of the date of is-
24 suance.

1 “(3) ORDERING RULE.—In any case in which
2 the eligible farmers’ cooperative holds stock in a
3 qualified agricultural processor which was acquired
4 in a sale to which section 1042A applied and holds
5 stock in such processor which was not so acquired,
6 any disposition of stock by the cooperative shall be
7 treated as the disposition of stock acquired in the
8 sale to which section 1042A applied to the extent
9 thereof.”

10 (c) CLERICAL AMENDMENTS.—

11 (1) The table of sections for part III of sub-
12 chapter O of chapter 1 of such Code is amended by
13 inserting after the item relating to section 1042 the
14 following new item:

 “Sec. 1042A. Sales of stock to certain farmers’ cooperatives.”

15 (2) The table of sections for chapter 43 of such
16 Code is amended by inserting after the item relating
17 to section 4978 the following new item:

 “Sec. 4978A. Tax on certain dispositions of stock to which section
 1042A applied.”

18 (d) EFFECTIVE DATE.—The amendments made by
19 this section shall apply to sales after December 31, 1997.

20 (e) BUDGETARY TREATMENT.—For purposes of sec-
21 tion 10213 of the Balanced Budget Act of 1997, the provi-

1 sions of this section shall be considered to have been en-
2 acted as part of the Taxpayer Relief Act of 1997.

○