

105TH CONGRESS
2D SESSION

H. R. 3170

To amend the Internal Revenue Code of 1986 to prevent the conversion of ordinary income or short-term capital gain into income eligible for the long-term capital gain rates, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 5, 1998

Mrs. KENNELLY of Connecticut 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 prevent the conversion of ordinary income or short-term capital gain into income eligible for the long-term capital gain rates, 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. CAPITAL GAIN TREATMENT OF GAIN FROM**
4 **CONSTRUCTIVE OWNERSHIP TRANSACTIONS.**

5 (a) IN GENERAL.—Part IV of subchapter P of chap-
6 ter 1 of the Internal Revenue Code of 1986 (relating to
7 special rules for determining capital gains and losses) is

1 amended by inserting after section 1259 the following new
2 section:

3 **“SEC. 1260. GAINS FROM CONSTRUCTIVE OWNERSHIP**
4 **TRANSACTIONS.**

5 “(a) IN GENERAL.—If the taxpayer has gain from
6 a constructive ownership transaction with respect to any
7 financial position and such gain would (without regard to
8 this section) be treated as a long-term capital gain—

9 “(1) such gain shall be treated as short-term
10 capital gain to the extent that such gain exceeds the
11 net underlying long-term capital gain, and

12 “(2) to the extent such gain is treated as a
13 long-term capital gain after the application of para-
14 graph (1), the determination of the capital gain rate
15 (or rates) applicable to such gain under section 1(h)
16 shall be determined on the basis of the respective
17 rate (or rates) that would have been applicable to
18 the net underlying long-term capital gain.

19 “(b) INTEREST CHARGE ON DEFERRAL OF GAIN
20 RECOGNITION.—

21 “(1) IN GENERAL.—If any gain is treated as
22 short-term capital gain for any taxable year by rea-
23 son of subsection (a)(1), the taxpayer’s tax imposed
24 by this chapter for such taxable year shall be in-

1 creased by the amount of interest which would have
2 been imposed under section 6601—

3 “(A) for periods ending on the due date
4 (without extensions) for the return of tax im-
5 posed by this chapter for such taxable year, and

6 “(B) on underpayments of tax for prior
7 taxable years which would have resulted had
8 such gain been included in gross income ratably
9 during the period the constructive ownership
10 transaction was open.

11 Any amount payable under this paragraph shall be
12 taken into account in computing the amount of any
13 deduction allowable to the taxpayer for interest paid
14 or accrued during such taxable year.

15 “(2) NO CREDITS AGAINST INCREASE IN TAX.—
16 Any increase in tax under paragraph (1) shall not
17 be treated as tax imposed by this chapter for pur-
18 poses of determining—

19 “(A) the amount of any credit allowable
20 under subpart A, B, D, or G of part IV of sub-
21 chapter A of chapter 1, or

22 “(B) the amount of the tax imposed by
23 section 55.

24 “(c) FINANCIAL POSITION.—For purposes of this
25 section—

1 “(1) IN GENERAL.—The term ‘financial posi-
2 tion’ means any position with respect to any stock,
3 debt instrument, partnership interest, or investment
4 trust interest.

5 “(2) POSITION.—The term ‘position’ means an
6 interest, including a futures or forward contract,
7 short sale, or option.

8 “(d) CONSTRUCTIVE OWNERSHIP TRANSACTION.—

9 “(1) IN GENERAL.—The taxpayer shall be
10 treated as having entered into a constructive owner-
11 ship transaction with respect to any financial posi-
12 tion if the taxpayer (or a related person)—

13 “(A) holds a long position under a notional
14 principal contract with respect to the same or
15 substantially identical property,

16 “(B) enters into a forward or futures con-
17 tract to acquire the same or substantially iden-
18 tical property,

19 “(C) is the grantor of a put, and is the
20 holder of a call, with respect to the same or
21 substantially identical property and such op-
22 tions have substantially equal strike prices, or

23 “(D) enters into 1 or more other trans-
24 actions (or acquires 1 or more positions) that
25 have substantially the same effect as a trans-

1 action described in any of the preceding sub-
2 paragraphs.

3 “(2) EXCEPTION FOR POSITIONS WHICH ARE
4 MARKED TO MARKET.—This section shall not apply
5 to any constructive ownership transaction if all of
6 the positions which are part of such transaction are
7 marked to market under any provision of this title
8 or the regulations thereunder.

9 “(3) LONG POSITION.—A person shall be treat-
10 ed as holding a long position under a notional prin-
11 cipal contract with respect to any property if such
12 person—

13 “(A) has the right to be paid (or receive
14 credit for) all or substantially all of the invest-
15 ment yield (including appreciation) on such
16 property for a specified period, and

17 “(B) is obligated to reimburse (or provide
18 credit) for all or substantially all of any decline
19 in the value of such property.

20 “(4) FORWARD CONTRACT.—The term ‘forward
21 contract’ has the meaning given to such term by sec-
22 tion 1259(d)(1).

23 “(5) RELATED PERSON.—The term ‘related
24 person’ has the meaning given to such term by sec-
25 tion 1259(c)(4).

1 “(e) NET UNDERLYING LONG-TERM CAPITAL
2 GAIN.—For purposes of this section, in the case of any
3 constructive ownership transaction with respect to any fi-
4 nancial position, the term ‘net underlying long-term cap-
5 ital gain’ means the aggregate net capital gain that the
6 taxpayer would have had if—

7 “(1) such position had been acquired on the
8 date such transaction was opened and sold on the
9 date such transaction was closed, and

10 “(2) only gains and losses that would have re-
11 sulted from the deemed ownership under paragraph
12 (1) were taken into account.

13 The amount of the net underlying long-term capital gain
14 with respect to any financial position shall be treated as
15 zero unless the amount thereof is established by clear and
16 convincing evidence.

17 “(f) EXCEPTION IF MARK TO MARKET ELECTED.—

18 “(1) IN GENERAL.—In the case of a taxpayer
19 who elects to have this subsection apply—

20 “(A) subsections (a) and (b) shall not
21 apply,

22 “(B) such taxpayer shall recognize gain or
23 loss on any constructive ownership transaction
24 which is open as of the close of any taxable year
25 as if the financial position to which such trans-

1 action relates were sold for its fair market value
2 on the last business day of such taxable year,
3 and

4 “(C) any gain or loss shall be taken into
5 account for such taxable year.

6 Proper adjustment shall be made in the amount of
7 any gain or loss subsequently realized for gain or
8 loss taken into account under the preceding sen-
9 tence.

10 “(2) CHARACTER OF GAIN OR LOSS.—

11 “(A) IN GENERAL.—Any gain or loss with
12 respect to a constructive ownership transaction
13 under paragraph (1) shall be treated as ordi-
14 nary income or loss.

15 “(B) SPECIAL RULE FOR DISPOSITIONS.—

16 If—

17 “(i) gain or loss is recognized with re-
18 spect to a constructive ownership trans-
19 action before the close of the taxable year,
20 and

21 “(ii) paragraph (1) would have ap-
22 plied if the transaction were open as of the
23 close of the taxable year,

24 such gain or loss shall be treated as ordinary
25 income or loss.

1 “(3) ELECTION.—An election under paragraph
2 (1) may be made without the consent of the Sec-
3 retary. Such an election, once made, shall apply to
4 the taxable year for which made and all subsequent
5 taxable years unless revoked with the consent of the
6 Secretary.

7 “(g) REGULATIONS.—The Secretary shall prescribe
8 such regulations as may be necessary or appropriate to
9 carry out the purposes of this section.”.

10 (b) CLERICAL AMENDMENT.—The table of sections
11 for part IV of subchapter P of chapter 1 of such Code
12 is amended by adding at the end the following new item:

 “Sec. 1260. Gains from constructive ownership transactions.”.

13 (c) EFFECTIVE DATE.—The amendments made by
14 this section shall apply to gain recognized after the date
15 of the enactment of this Act.

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