

108TH CONGRESS
2D SESSION

H. R. 4138

To amend the Internal Revenue Code of 1986 to repeal the tax on personal holding companies.

IN THE HOUSE OF REPRESENTATIVES

APRIL 2, 2004

Mr. HOUGHTON 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 repeal the tax on personal holding companies.

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.**

4 This Act may be cited as the “Personal Holding Com-
5 pany Tax Repeal Act of 2004”.

6 **SEC. 2. REPEAL OF PERSONAL HOLDING COMPANY TAX.**

7 (a) IN GENERAL.—Part II of subchapter G of chap-
8 ter 1 of the Internal Revenue Code of 1986 (relating to
9 personal holding companies) is hereby repealed.

10 (b) CONFORMING AMENDMENTS.—

1 (1) Section 12(2) of such Code is amended to
2 read as follows:

3 “(2) For accumulated earnings tax, see part I
4 of subchapter G (sec. 531 and following).”.

5 (2) Section 26(b)(2) of such Code is amended
6 by striking subparagraph (G) and by redesignating
7 the succeeding subparagraphs accordingly.

8 (3) Section 30A(c) of such Code is amended by
9 striking paragraph (3), by inserting “or” at the end
10 of paragraph (2), and by redesignating paragraph
11 (4) as paragraph (3).

12 (4) Section 41(e)(7)(E) of such Code is amend-
13 ed by adding “and” at the end of clause (i), by
14 striking clause (ii), and by redesignating clause (iii)
15 as clause (ii).

16 (5) Section 56(b)(2) of such Code is amended
17 by striking subparagraph (C) and by redesignating
18 subparagraph (D) as subparagraph (C).

19 (6) Section 170(e)(4)(D) of such Code is
20 amended by adding “and” at the end of clause (i),
21 by striking clause (ii), and by redesignating clause
22 (iii) as clause (ii).

23 (7) Section 111(d) of such Code is amended to
24 read as follows:

1 “(d) SPECIAL RULES FOR ACCUMULATED EARNINGS
2 TAX.—In applying subsection (a) for the purpose of deter-
3 mining the accumulated earnings tax under section 531—

4 “(1) any excluded amount under subsection (a)
5 allowed for purposes of this subtitle (other than sec-
6 tion 531) shall be allowed whether or not such
7 amount resulted in a reduction of the tax under sec-
8 tion 531 for the prior taxable year, and

9 “(2) where any excluded amount under sub-
10 section (a) was not allowed as a deduction for the
11 prior taxable year for purposes of this subtitle other
12 than section 531 but was allowable for the same tax-
13 able year under section 531, then such excluded
14 amount shall be allowable if it did not result in a re-
15 duction of the tax under section 531.”.

16 (8)(A) Section 316(b) of such Code is amended
17 by striking paragraph (2) and by redesignating
18 paragraph (3) as paragraph (2).

19 (B) Section 331(b) of such Code is amended by
20 striking “(other than a distribution referred to in
21 paragraph (2)(B) of section 316(b))”.

22 (9) Section 341(d) of such Code is amended—

23 (A) by striking “section 544(a)” and in-
24 serting “section 465(f)”, and

1 (B) by inserting before the period at the
2 end of the next to the last sentence “and such
3 paragraph (2) shall be applied by inserting ‘by
4 or for his partner’ after ‘his family’”.

5 (10) Section 381(c) of such Code is amended by
6 striking paragraphs (14) and (17).

7 (11) Section 443(e) of such Code is amended by
8 striking paragraph (2) and by redesignating para-
9 graphs (3), (4), and (5) as paragraphs (2), (3), and
10 (4), respectively.

11 (12) Section 447(g)(4)(A) of such Code is
12 amended by striking “other than—” and all that fol-
13 lows and inserting “other than an S corporation.”

14 (13)(A) Section 465(a)(1)(B) of such Code is
15 amended to read as follows:

16 “(B) a C corporation which is closely
17 held,”.

18 (B) Section 465(a)(3) of such Code is amended
19 to read as follows:

20 “(3) CLOSELY HELD DETERMINATION.—For
21 purposes of paragraph (1), a corporation is closely
22 held if, at any time during the last half of the tax-
23 able year, more than 50 percent in value of its out-
24 standing stock is owned, directly or indirectly, by or
25 for not more than 5 individuals. For purposes of this

1 paragraph, an organization described in section
2 401(a), 501(c)(17), or 509(a) or a portion of a trust
3 permanently set aside or to be used exclusively for
4 the purposes described in section 642(c) shall be
5 considered an individual.”

6 (C) Section 465 of such Code is amended by
7 adding at the end the following new subsection:

8 “(f) CONSTRUCTIVE OWNERSHIP RULES.—For pur-
9 poses of subsection (a)(3)—

10 “(1) STOCK NOT OWNED BY INDIVIDUAL.—
11 Stock owned, directly or indirectly, by or for a cor-
12 poration, partnership, estate, or trust shall be con-
13 sidered as being owned proportionately by its share-
14 holders, partners, or beneficiaries.

15 “(2) FAMILY OWNERSHIP.—An individual shall
16 be considered as owning the stock owned, directly or
17 indirectly, by or for his family. For purposes of this
18 paragraph, the family of an individual includes only
19 his brothers and sisters (whether by the whole or
20 half blood), spouse, ancestors, and lineal descend-
21 ants.

22 “(3) OPTIONS.—If any person has an option to
23 acquire stock, such stock shall be considered as
24 owned by such person. For purposes of this para-
25 graph, an option to acquire such an option, and each

1 one of a series of such options, shall be considered
2 as an option to acquire such stock.

3 “(4) APPLICATION OF FAMILY AND OPTION
4 RULES.—Paragraphs (2) and (3) shall be applied if,
5 but only if, the effect is to make the corporation
6 closely held under subsection (a)(3).

7 “(5) CONSTRUCTIVE OWNERSHIP AS ACTUAL
8 OWNERSHIP.—Stock constructively owned by a per-
9 son by reason of the application of paragraph (1) or
10 (3), shall, for purposes of applying paragraph (1) or
11 (2), be treated as actually owned by such person;
12 but stock constructively owned by an individual by
13 reason of the application of paragraph (2) shall not
14 be treated as owned by him for purposes of again
15 applying such paragraph in order to make another
16 the constructive owner of such stock.

17 “(6) OPTION RULE IN LIEU OF FAMILY
18 RULE.—If stock may be considered as owned by an
19 individual under either paragraph (2) or (3) it shall
20 be considered as owned by him under paragraph (3).

21 “(7) CONVERTIBLE SECURITIES.—Outstanding
22 securities convertible into stock (whether or not con-
23 vertible during the taxable year) shall be considered
24 as outstanding stock if the effect of the inclusion of
25 all such securities is to make the corporation closely

1 held under subsection (a)(3). The requirement under
2 the preceding sentence that all convertible securities
3 must be included if any are to be included shall be
4 subject to the exception that, where some of the out-
5 standing securities are convertible only after a later
6 date than in the case of others, the class having the
7 earlier conversion date may be included although the
8 others are not included, but no convertible securities
9 shall be included unless all outstanding securities
10 having a prior conversion date are also included.”

11 (D) Section 465(c)(7)(B) of such Code is
12 amended by striking clause (i) and by redesignating
13 clauses (ii) and (iii) as clauses (i) and (ii), respec-
14 tively.

15 (E) Section 465(c)(7)(G) of such Code is
16 amended to read as follows:

17 “(G) LOSS OF 1 MEMBER OF AFFILIATED
18 GROUP MAY NOT OFFSET INCOME OF PERSONAL
19 SERVICE CORPORATION.—Nothing in this para-
20 graph shall permit any loss of a member of an
21 affiliated group to be used as an offset against
22 the income of any other member of such group
23 which is a personal service corporation (as de-
24 fined in section 269A(b) but determined by sub-

1 stituting ‘5 percent’ for ‘10 percent’ in section
2 269A(b)(2)).”

3 (14) Sections 508(d), 4947, and 4948(c)(4) of
4 such Code are each amended by striking
5 “545(b)(2),” each place it appears.

6 (15) Section 532(b) of such Code is amended
7 by striking paragraph (1) and by redesignating
8 paragraphs (2), (3), and (4) as paragraphs (1), (2),
9 and (3), respectively.

10 (16) Sections 535(b)(1) and 556(b)(1) of such
11 Code are each amended by striking “section 541”
12 and inserting “section 541 (as in effect before its re-
13 peal)”.

14 (17)(A) Section 553(a)(1) of such Code is
15 amended by striking “section 543(d)” and inserting
16 “subsection (e)”.

17 (B) Section 553 of such Code is amended by
18 adding at the end the following new subsection:

19 “(c) ACTIVE BUSINESS COMPUTER SOFTWARE ROY-
20 ALTIES.—

21 “(1) IN GENERAL.—For purposes of subsection
22 (a), the term ‘active business computer software roy-
23 alties’ means any royalties—

1 “(A) received by any corporation during
2 the taxable year in connection with the licensing
3 of computer software, and

4 “(B) with respect to which the require-
5 ments of paragraphs (2), (3), (4), and (5) are
6 met.

7 “(2) ROYALTIES MUST BE RECEIVED BY COR-
8 PORATION ACTIVELY ENGAGED IN COMPUTER SOFT-
9 WARE BUSINESS.—The requirements of this para-
10 graph are met if the royalties described in paragraph
11 (1)—

12 “(A) are received by a corporation engaged
13 in the active conduct of the trade or business
14 of developing, manufacturing, or producing
15 computer software, and

16 “(B) are attributable to computer software
17 which—

18 “(i) is developed, manufactured, or
19 produced by such corporation (or its prede-
20 cessor) in connection with the trade or
21 business described in subparagraph (A), or

22 “(ii) is directly related to such trade
23 or business.

24 “(3) ROYALTIES MUST CONSTITUTE AT LEAST
25 50 PERCENT OF INCOME.—The requirements of this

1 paragraph are met if the royalties described in para-
2 graph (1) constitute at least 50 percent of the ordi-
3 nary gross income of the corporation for the taxable
4 year.

5 “(4) DEDUCTIONS UNDER SECTIONS 162 AND
6 174 RELATING TO ROYALTIES MUST EQUAL OR EX-
7 CEED 25 PERCENT OF ORDINARY GROSS INCOME.—

8 “(A) IN GENERAL.—The requirements of
9 this paragraph are met if—

10 “(i) the sum of the deductions allow-
11 able to the corporation under sections 162,
12 174, and 195 for the taxable year which
13 are properly allocable to the trade or busi-
14 ness described in paragraph (2) equals or
15 exceeds 25 percent of the ordinary gross
16 income of such corporation for such tax-
17 able year, or

18 “(ii) the average of such deductions
19 for the 5-taxable year period ending with
20 such taxable year equals or exceeds 25 per-
21 cent of the average ordinary gross income
22 of such corporation for such period.

23 If a corporation has not been in existence dur-
24 ing the 5-taxable year period described in clause
25 (ii), then the period of existence of such cor-

1 poration shall be substituted for such 5-taxable
2 year period.

3 “(B) DEDUCTIONS ALLOWABLE UNDER
4 SECTION 162.—For purposes of subparagraph
5 (A), a deduction shall not be treated as allow-
6 able under section 162 if it is specifically allow-
7 able under another section.

8 “(C) LIMITATION ON ALLOWABLE DEDUC-
9 TIONS.—For purposes of subparagraph (A), no
10 deduction shall be taken into account with re-
11 spect to compensation for personal services ren-
12 dered by the 5 individual shareholders holding
13 the largest percentage (by value) of the out-
14 standing stock of the corporation. For purposes
15 of the preceding sentence individuals holding
16 less than 5 percent (by value) of the stock of
17 such corporation shall not be taken into ac-
18 count.”

19 (18) Section 561(a) of such Code is amended
20 by striking paragraph (3), by inserting “and” at the
21 end of paragraph (1), and by striking ”, and” at the
22 end of paragraph (2) and inserting a period.

23 (19) Section 562(b) of such Code is amended to
24 read as follows:

1 “(b) DISTRIBUTIONS IN LIQUIDATION.—Except in
2 the case of a foreign personal holding company described
3 in section 552—

4 “(1) in the case of amounts distributed in liq-
5 uidation, the part of such distribution which is prop-
6 erly chargeable to earnings and profits accumulated
7 after February 28, 1913, shall be treated as a divi-
8 dend for purposes of computing the dividends paid
9 deduction, and

10 “(2) in the case of a complete liquidation occur-
11 ring within 24 months after the adoption of a plan
12 of liquidation, any distribution within such period
13 pursuant to such plan shall, to the extent of the
14 earnings and profits (computed without regard to
15 capital losses) of the corporation for the taxable year
16 in which such distribution is made, be treated as a
17 dividend for purposes of computing the dividends
18 paid deduction.

19 For purposes of paragraph (1), a liquidation includes a
20 redemption of stock to which section 302 applies. Except
21 to the extent provided in regulations, the preceding sen-
22 tence shall not apply in the case of any mere holding or
23 investment company which is not a regulated investment
24 company.”

1 (20) Section 563 of such Code is amended by
2 striking subsection (b).

3 (21) Section 564 of such Code is hereby re-
4 pealed.

5 (22) Section 631(c) of such Code is amended by
6 striking “or section 545(b)(5)”.

7 (23) Section 852(b)(1) of such Code is amend-
8 ed by striking “which is a personal holding company
9 (as defined in section 542) or”.

10 (24)(A) Section 856(h)(1) of such Code is
11 amended to read as follows:

12 “(1) IN GENERAL.—For purposes of subsection
13 (a)(6), a corporation, trust, or association is closely
14 held if the stock ownership requirement of section
15 465(a)(3) is met.”

16 (B) Section 856(h)(3)(A)(i) of such Code is
17 amended by striking “section 542(a)(2)” and insert-
18 ing “section 465(a)(3)”.

19 (C) Paragraph (3) of section 856(h) of such
20 Code is amended by striking subparagraph (B) and
21 by redesignating subparagraphs (C) and (D) as sub-
22 subparagraphs (B) and (C), respectively.

23 (D) Subparagraph (C) of section 856(h)(3) of
24 such Code, as redesignating by the preceding sub-

1 paragraph, is amended by striking “subparagraph
2 (C)” and inserting “subparagraph (B)”.

3 (25) The last sentence of section 882(c)(2) of
4 such Code is amended to read as follows: “The pre-
5 ceding sentence shall not be construed to deny the
6 credit provided by section 33 for tax withheld at
7 source or the credit provided by section 34 for cer-
8 tain uses of gasoline.”.

9 (26) Section 936(a)(3) of such Code is amended
10 by striking subparagraph (C), by inserting “or” at
11 the end of subparagraph (B), and by redesignating
12 subparagraph (D) as subparagraph (C).

13 (27) Section 992(d) of such Code is amended
14 by striking paragraph (2) and by redesignating suc-
15 ceeding paragraphs accordingly.

16 (28) Section 992(e) of such Code is amended by
17 striking “and section 541 (relating to personal hold-
18 ing company tax)”.

19 (29) Section 1202(e)(8) of such Code is amend-
20 ed by striking “section 543(d)(1)” and inserting
21 “section 553(c)(1)”.

22 (30) Section 1362(d)(3)(C)(iii) of such Code is
23 amended by adding at the end the following new
24 sentence: “References to section 542 in the pre-
25 ceding sentence shall be treated as references to

1 such section as in effect on the day before its re-
2 peal.”

3 (31) Section 1504(e)(2)(B) of such Code is
4 amended by adding “and” at the end of clause (i),
5 by striking clause (ii), and by redesignating clause
6 (iii) as clause (ii).

7 (32) Section 2057(e)(2)(C) of such Code is
8 amended by adding at the end the following new
9 sentence: “References to sections 542 and 543 in
10 the preceding sentence shall be treated as references
11 to such sections as in effect on the day before their
12 repeal.”

13 (33) Sections 6422 of such Code is amended by
14 striking paragraph (3) and by redesignating para-
15 graphs (4) through (12) and paragraphs (3) through
16 (11), respectively.

17 (34) Section 6501 of such Code is amended by
18 striking subsection (f).

19 (35) Section 6503(k) of such Code is amended
20 by striking paragraph (1) and by redesignating
21 paragraphs (2) through (5) as paragraphs (1)
22 through (4), respectively.

23 (36) Section 6515 of such Code is amended by
24 striking paragraph (1) and by redesignating para-

1 graphs (2) through (6) as paragraphs (1) through
2 (5), respectively.

3 (37) Subsections (d)(1)(B) and (e)(2) of section
4 6662 of such Code are each amended by striking “or
5 a personal holding company (as defined in section
6 542)”.

7 (38) Section 6683 of such Code is hereby re-
8 pealed.

9 (c) CLERICAL AMENDMENTS.—

10 (1) The table of parts for subchapter G of
11 chapter 1 of such Code is amended by striking the
12 item relating to part II.

13 (2) The table of sections for part IV of such
14 subchapter G of such Code is amended by striking
15 the item relating to section 564.

16 (3) The table of sections for part I of sub-
17 chapter B of chapter 68 of such Code is amended
18 by striking the item relating to section 6683.

19 (d) EFFECTIVE DATE.—The amendments made by
20 this section shall apply to taxable years beginning after
21 December 31, 2004.

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