

**PL, P.L. 101-239, Omnibus Budget Reconciliation Act of 1989, (December 19, 1988), Part 01 of 03
Omnibus Budget Reconciliation Act of 1989**

December 19, 1988

101th Congress

[Click here for Conference Committee Report, [HRRepNo 101-386](#), Senate Finance Committee Report, [SRepNo 101-56](#), and House Ways and Means Committee Report, [HRRepNo 101-247](#). — CCH]

Date Decided: Dec. 19, 1989

101st Congress H.R. 3299./

An Act to provide for reconciliation pursuant to section 5 of the concurrent resolution on the budget for the fiscal year 1990.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress

SECTION 1. SHORT TITLE.

This Act may be cited as the “Omnibus Budget Reconciliation Act of 1989”.

SEC. 2. TABLE OF CONTENTS.

Title I —Agriculture and related programs.

Title II —Student loan and pension fiduciary amendments.

Title III —Regulatory agency fees.

Title IV —Civil service and postal service programs.

Title V —Veterans programs.

Title VI —Medicare, Medicaid, maternal and child health, and other health provisions.

Title VII —Revenue provisions.

Title VIII —Human resource and income security provisions.

Title IX —Offshore oil pollution compensation fund.

Title X —Miscellaneous and technical Social Security Act amendments.

Title XI —Miscellaneous.

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SEC. 6202. MEDICARE AS SECONDARY PAYER.

(a) IDENTIFICATION OF MEDICARE SECONDARY PAYER SITUATIONS. —

(1) DISCLOSURE OF CERTAIN TAXPAYER IDENTITY INFORMATION FOR VERIFICATION OF EMPLOYMENT STATUS OF MEDICARE BENEFICIARY AND SPOUSE OF MEDICARE BENEFICIARY. —

(A) IN GENERAL. — Subsection (1) of section 6103 of the Internal Revenue Code of 1986 (relating to disclosure of returns and return information for purposes other than tax administration) is amended by adding at the end thereof the following new paragraph:

“(12) DISCLOSURE OF CERTAIN TAXPAYER IDENTITY INFORMATION FOR VERIFICATION OF EMPLOYMENT STATUS OF MEDICARE BENEFICIARY AND SPOUSE OF MEDICARE BENEFICIARY. —

“(A) RETURN INFORMATION FROM INTERNAL REVENUE SERVICE. — The Secretary shall, upon written request from the Commissioner of Social Security, disclose to the Commissioner available filing status and taxpayer identity information from the individual master files of the Internal Revenue Service relating to whether any Medicare beneficiary identified by the Commissioner was a married individual (as defined in section 7703) for any specified year after 1986, and, if so, the name of the spouse of such individual and such spouse's TIN.

“(B) RETURN INFORMATION FROM SOCIAL SECURITY ADMINISTRATION. — The Commissioner of Social Security shall, upon written request from the Administrator of the Health Care Financing Administration, disclose to the Administrator the following information:

“(i) The name and TIN of each Medicare beneficiary who is identified as having received wages (as defined in section 3401(a)) from a qualified employer in a previous year.

“(ii) For each Medicare beneficiary who was identified as married under subparagraph (A) and whose spouse is identified as having received wages from a qualified employer in a previous year —

“(I) the name and TIN of the Medicare beneficiary, and

“(II) the name and TIN of the spouse.

“(iii) With respect to each such qualified employer, the name, address, and TIN of the employer and the number of individuals with respect to whom written statements were furnished under section 6051 by the employer with respect to such previous year.

“(C) DISCLOSURE BY HEALTH CARE FINANCING ADMINISTRATION. — With respect to the information disclosed under subparagraph (B), the Administrator of Health Care Financing Administration may disclose —

“(i) to the qualified employer referred to in such subparagraph the name and TIN of each individual identified under such subparagraph as having received wages from the employer (hereinafter in this

subparagraph referred to as the `employee') for purposes of determining during what period such employee or the employee's spouse may be (or have been) covered under a group health plan of the employer and what benefits are or were covered under the plan (including the name, address, and identifying number of the plan),

“(ii) to any group health plan which provides or provided coverage to such an employee or spouse, the name of such employee and the employee's spouse (if the spouse is a Medicare beneficiary) and the name and address of the employer, and, for the purpose of presenting a claim to the plan —

“(I) the TIN of such employee if benefits were paid under title XVIII of the Social Security Act with respect to the employee during a period in which the plan was a primary plan (as defined in section 1862(b)(2)(A) of the Social Security Act), and

“(II) the TIN of such spouse if benefits were paid under such title with respect to the spouse during such period, and

“(iii) to any agent of such Administrator the information referred to in subparagraph (B) for purposes of carrying out clauses (i) and (ii) on behalf of such Administrator.

“(D) SPECIAL RULES. —

“(i) RESTRICTIONS ON DISCLOSURE. —Information may be disclosed under this paragraph only for purposes of, and to the extent necessary in, determining the extent to which any Medicare beneficiary is covered under any group health plan.

“(ii) TIMELY RESPONSE TO REQUESTS. —Any request made under subparagraph (A) or (B) shall be complied with as soon as possible but in no event later than 120 days after the date the request was made.

“(E) DEFINITIONS. —For purposes of this paragraph —

“(i) MEDICARE BENEFICIARY. —The term `Medicare beneficiary' means an individual entitled to benefits under part A, or enrolled under part B, of title XVIII of the Social Security Act, but does not include such an individual enrolled in part A under section 1818.

“(ii) GROUP HEALTH PLAN. —The term `group health plan' means —

“(I) any group health plan (as defined in section 5000(b)(1)), and

“(II) any large group health plan (as defined in section 5000(b)(2)).

“(iii) QUALIFIED EMPLOYER. —The term `qualified employer' means, for a calendar year, an employer which has furnished written statements under section 6051 with respect to at least 20 individuals for wages paid in the year.

“(F) TERMINATION. —Subparagraphs (A) and (B) shall not apply to —

“(i) any request made after September 30, 1991, and

“(ii) any request made before such date for information relating to —

“(I) 1990 or thereafter in the case of subparagraph (A), or

“(II) 1991 or thereafter in the case of subparagraph (B).”

(B) SAFEGUARDS. —

(i) Paragraph (3) of section 6103(a) of such Code is amended by inserting “(1)(12),” after “(e)(1)(D)(iii).”

(ii) Subparagraph (A) of section 6103(p)(3) of such Code is amended by striking “or (11)” and inserting “(11), or (12)”.

(iii) Paragraph (4) of section 6103(p) of such Code is amended in the material preceding subparagraph (A) by striking “or (9) shall” and inserting “(9), or (12) shall”.

(iv) Clause (ii) of section 6103(p)(4)(F) of such Code is amended by striking “or (11)” and inserting “(11), or (12)”.

(v) The next to the last sentence of paragraph (4) of section 6103(p) of such Code is amended by inserting “or which receives any information under subsection (1)(12)(B) and which discloses any such information to any agent” before “, this paragraph”.

(C) PENALTY. —Paragraph (2) of section 7213(a) of such Code is amended by striking “or (10)” and inserting “(10), or (12)”.

(D) EFFECTIVE DATE. —The amendments made by this paragraph shall take effect on the date of the enactment of this Act.

(2) RESPONSIBILITIES OF HCFA. —

(A) In general. —Section 1862(b) of the Social Security Act (42 U.S.C. 1395y(b)), as amended by subsection (b)(1) of this section, is amended by inserting after paragraph (4) the following new paragraph:

“(5) IDENTIFICATION OF SECONDARY PAYER SITUATIONS. —

“(A) REQUESTING MATCHING INFORMATION. —

“(i) COMMISSIONER OF SOCIAL SECURITY. —The Commissioner of Social Security shall, not less often than annually, transmit to the Secretary of the Treasury a list of the names and TINs of Medicare beneficiaries (as defined in section 6103(1)(12) of the Internal Revenue Code of 1986) and request that the Secretary disclose to the Commissioner the information described in subparagraph (A) of such section.

“(ii) ADMINISTRATOR. —The Administrator of the Health Care Financing Administration shall request, not less often than annually, the Commissioner of the Social Security Administration to disclose to the Administrator the information described in subparagraph (B) of section 6103(1)(12) of the Internal Revenue Code of 1986.

“(B) DISCLOSURE TO FISCAL INTERMEDIARIES AND CARRIERS. —In addition to any other information provided under this title to fiscal intermediaries and carriers, the Administrator shall disclose to such intermediaries and carriers (or to such a single intermediary or carrier as the Secretary may designate) the information received under subparagraph (A) for the purposes of carrying out this subsection.

“(C) CONTACTING EMPLOYERS. —

“(i) IN GENERAL. —With respect to each individual (in this subparagraph referred to as an ‘employee’)

who was furnished a written statement under section 6051 of the Internal Revenue Code of 1986 by a qualified employer (as defined in section 6103(1)(12)(D)(iii) of such Code), as disclosed under subparagraph (B), the appropriate fiscal intermediary or carrier shall contact the employer in order to determine during what period the employee or employee's spouse may be (or have been) covered under a group health plan of the employer and the nature of the coverage that is or was provided under the plan (including the name, address, and identifying number of the plan).

“(ii) EMPLOYER RESPONSE. —Within 30 days of the date of receipt of the inquiry, the employer shall notify the intermediary or carrier making the inquiry as to the determinations described in clause (i). An employer (other than a Federal or other governmental entity) who willfully or repeatedly fails to provide timely and accurate notice in accordance with the previous sentence shall be subject to a civil money penalty of not to exceed \$1,000 for each individual with respect to which such an inquiry is made. The provisions of section 1128A (other than subsections (a) and (b)) shall apply to a civil money penalty under the previous sentence in the same manner as such provisions apply to a penalty or proceeding under section 1128A(a).

“(iii) SUNSET ON REQUIREMENT. —Clause (ii) shall not apply to inquiries made after September 30, 1991.”.

(B) DEADLINE FOR FIRST REQUEST. —The Commissioner of Social Security shall first —

(i) transmit to the Secretary of the Treasury information under paragraph (5)(A)(i) of section 1862(b) of the Social Security Act (as inserted by subparagraph (A)), and

(ii) request from the Secretary disclosure of information described in section 6013(1)(12)(A) of the Internal Revenue Code of 1986,

by not later than 14 days after the date of the enactment of this Act.

(b) UNIFORM ENFORCEMENT AND COORDINATION OF BENEFITS. —

(1) IN GENERAL. —Section 1862 of the Social Security Act (42 U.S.C. 1395y) is amended —

(A) in the heading, by adding at the end of the following: “and Medicare as secondary payer”; and

(B) by amending subsection (b) to read as follows:

“(b) Medicare as Secondary Payer. —

“(1) REQUIREMENTS OF GROUP HEALTH PLANS. —

“(A) WORKING AGED UNDER GROUP HEALTH PLANS. —

“(i) IN GENERAL. —A group health plan —

“(I) may not take into account, for any item or service furnished to an individual 65 years of age or older at this time the individual is covered under the plan by reason of the current employment of the individual (or the individual's spouse), that the individual is entitled to benefits under this title under section 226(a), and

“(II) shall provide that any employee age 65 or older, and any employee's spouse age 65 or older, shall be entitled to the same benefits under the plan under the same conditions as any employee, and the spouse of such employee, under age 65.

“(ii) EXCLUSION OF GROUP HEALTH PLAN OF A SMALL EMPLOYER. —Clause (i) shall not apply to a group health plan unless the plan is sponsored by or contributed to by an employer that has 20 or more employees for each working day in each of 20 or more calendar weeks in the current calendar year or the preceding calendar year.

“(iii) EXCEPTION FOR SMALL EMPLOYERS IN MULTIEMPLOYER, OR MULTIPLE EMPLOYER GROUP HEALTH PLANS. —Clause (i) also shall not apply with respect to individuals enrolled in a multiemployer or multiple employer group health plan if the coverage of the individuals under the plan is by virtue of employment with an employer that does not have 20 or more employees for each working day in each of 20 or more calendar weeks in the current calendar year or the preceding calendar year; except that the exception provided in this clause shall only apply if the plan elects treatment under this clause.

“(iv) EXCEPTION FOR INDIVIDUALS WITH END STAGE RENAL DISEASE. —Clause (i) shall not apply to an item or service furnished in a month to an individual if for the month the individual is, or would upon application be, entitled to benefits under section 226A.

“(v) GROUP HEALTH PLAN DEFINED. —In this subparagraph, and subparagraph (C), the term ‘group health plan’ has the meaning given such term in section 5000(b)(1) of the Internal Revenue Code of 1986.

“(B) DISABLED ACTIVE INDIVIDUALS IN LARGE GROUP HEALTH PLANS. —

“(i) IN GENERAL. —A large group health plan (as defined in clause (iv)(II)) may not take into account that an active individual (as defined in clause (iv)(I)) is entitled to benefits under this title under section 226(b).

“(ii) EXCEPTION FOR INDIVIDUALS WITH END STAGE RENAL DISEASE. —Clause (i) shall not apply to an item or service furnished in a month to an individual if for the month the individual is, or would upon application be, entitled to benefits under section 226A.

“(iii) SUNSET. —Clause (i) shall only apply to items and services furnished on or after January 1, 1987, and before January 1, 1992.

“(iv) DEFINITIONS. —In this subparagraph:

“(I) ACTIVE INDIVIDUAL. —The term ‘active individual’ means an employee (as may be defined in regulations), the employer, self-employed individual (such as the employer), an individual associated with the employer in a business relationship, or a member of the family of any of such persons.

“(II) LARGE GROUP HEALTH PLAN. —The term ‘large group health plan’ has the meaning given such term in section 5000(b)(2) of the Internal Revenue Code of 1986.

“(C) INDIVIDUALS WITH END STAGE RENAL DISEASE. —A group health plan (as defined in subparagraph (A)(v)) —

“(i) may not take into account that an individual is entitled to benefits under this title solely by reason of section 226A during the 12-month period which begins with the earlier of —

“(I) the month in which a regular course of renal dialysis is initiated, or

“(II) in the case of an individual who receives a kidney transplant, the first month in which he would be eligible for benefits under part A (if he has filed an application for such benefits) under the provisions of section 226A(b)(1)(B); and

“(ii) may not differentiate in the benefits it provides between individuals having end stage renal disease and other individuals covered by such plan on the basis of the existence of end stage renal disease, the need for renal dialysis, or in any other manner;

except that clause (ii) shall not prohibit a plan from taking into account that an individual is entitled to benefits under this title solely by reason of section 226A after the end of the 12-month period described in clause (i).

“(2) MEDICARE SECONDARY PAYER. —

“(A) IN GENERAL. —Payment under this title may not be made, except as provided in subparagraph (B), with respect to any item or service to the extent that —

“(i) payment has been made, or can reasonably be expected to be made, with respect to the item or service as required under paragraph (1), or

“(ii) payment has been made or can reasonably be expected to be made promptly (as determined in accordance with regulations) under a workman's compensation law or plan of the United States or a State or under an automobile or liability insurance policy or plan (including a self-insured plan) or under no fault insurance.

In this subsection, the term `primary plan' means a group health plan or large group health plan, to the extent that clause (i) applies, and a workmen's compensation law or plan, an automobile or liability insurance policy or plan (including a self-insured plan) or no fault insurance, to the extent that clause (ii) applies.

“(B) CONDITIONAL PAYMENT. —

“(i) PRIMARY PLANS. —Any payment under this title with respect to any item or service to which subparagraph (A) applies shall be conditioned on reimbursement to the appropriate Trust Fund established by this title when notice or other information is received that payment for such item or service has been or could be made under such subparagraph.

“(ii) ACTION BY UNITED STATES. —In order to recover payment under this title for such an item or service, the United States may bring an action against any entity which is required or responsible under this subsection to pay with respect to such item or service (or any portion thereof) under a primary plan (and may, in accordance with paragraph (3)(A) collect double damages against that entity), or against any other entity (including any physician or provider) that has received payment from that entity with respect to the item or service, and may join or intervene in any action related to the events that gave rise to the need for the item or service.

“(iii) SUBROGATION RIGHTS. —The United States shall be subrogated (to the extent of payment made under this title for such an item or service) to any right under this subsection of an individual or any other entity to payment with respect to such item or service under a primary plan.

“(iv) WAIVER OF RIGHTS. —The Secretary may waive (in whole or in part) the provisions of this subparagraph in the case of an individual claim if the Secretary determines that the waiver is in the best interests of the program established under this title.

“(3) ENFORCEMENT. —

“(A) PRIVATE CAUSE OF ACTION. —There is established a private cause of action for damages (which

shall be in an amount double the amount otherwise provided) in the case of a primary plan which fails to provide for primary payment (or appropriate reimbursement) in accordance with such paragraphs (1) and (2)(A).

“(B) REFERENCE TO EXCISE TAX WITH RESPECT TO NONCONFORMING GROUP HEALTH PLANS. —For provisions imposing an excise tax with respect to nonconforming group health plans, see section 5000 of the Internal Revenue Code of 1986.

“(4) COORDINATION OF BENEFITS. —Where payment for an item or service by a primary plan is less than the amount of the charge for such item or service and is not payment in full, payment may be made under this title (without regard to deductibles and coinsurance under this title) for the remainder of such charge, but —

“(A) payment under this title may not exceed an amount which would be payable under this title for such item or service if paragraph (2)(A) did not apply; and

“(B) payment under this title, when combined with the amount payable under the primary plan, may not exceed —

“(i) in the case of an item or service payment for which is determined under this title on the basis of reasonable cost (or other cost-related basis) or under section 1886, the amount which would be payable under this title on such basis, and

“(ii) in the case of an item or service for which payment is authorized under this title on another basis —

“(I) the amount which would be payable under the primary plan (without regard to deductibles and coinsurance under such plan), or

“(II) the reasonable charge or other amount which would be payable under this title (without regard to deductibles and coinsurance under this title),

whichever is greater.”

(2) ENFORCEMENT THROUGH EXCISE TAX. —Section 5000 of the Internal Revenue Code of 1986 is amended —

(A) by striking “LARGE” in the heading;

(B) in subsection (a), by striking “large” each place it appears; and

(C) by amending subsections (b) and (c) to read as follows:

“(b) GROUP HEALTH PLAN AND LARGE GROUP HEALTH PLAN. —For purposes of this section —

“(1) GROUP HEALTH PLAN. —The term ‘group health plan’ means any plan of, or contributed to by, an employer (including a self-insured plan) to provide health care (directly or otherwise) to the employer’s employees, former employees, or the families of such employees or former employees.

“(2) LARGE GROUP HEALTH PLAN. —The term ‘large group health plan’ means a plan of, or contributed to by, an employer or employee organization (including a self-insured plan) to provide health care (directly or otherwise) to the employees, former employees, the employer, others associated or formerly associated with the employer in a business relationship, or their families, that covers employees of at least one employer that normally employed at least 100 employees on a typical business day during the

previous calendar year.

“(c) NONCONFORMING GROUP HEALTH PLAN. —For purposes of this section, the term ‘nonconforming group health plan’ means a group health plan or large group health plan that at any time during a calendar year does not comply with the requirements of subparagraphs (A) and (C) or subparagraph (B), respectively, of section 1862(b)(1) of the Social Security Act.”.

(3) REPEAL OF CERTAIN ALTERNATIVE ENFORCEMENT PROVISIONS. —

(A) DENIAL OF DEDUCTION FOR GROUP HEALTH PLANS. —Subsection (i) of section 162 of such Code (relating to group health plans) is repealed.

(B) CONFORMING AMENDMENT. —Section 4980(B)(g)(2) of such Code is amended by striking “162(i)” and inserting “5000(b)(1)”.

(C) AGE DISCRIMINATION IN EMPLOYMENT ACT. —The Age Discrimination in Employment Act of 1967 is amended —

(i) by striking subsection (g) of section 4, and

(ii) in section 12(a), by striking “(except the provisions of section 4(g))”.

(4) CLERICAL AND CONFORMING AMENDMENTS. —

(A) Chapter 47 of the Internal Revenue Code of 1986 is amended —

(i) in the heading, by striking “LARGE”, and

(ii) in the table of sections, by striking “large”.

(B) The item in the table of chapters of subtitle D of such Code relating to chapter 47 is amended by striking “large”.

(C) Sections 1837(i) and 1839(b) of the Social Security Act (42 U.S.C. 1395p(i), 1395r(b)) are each amended by striking “1862(b)(3)(A)(iv)” and “1862(b)(4)(B)” each place each appears and inserting “1862(b)(1)(A)(v)” and “1862(b)(1)(B)(iv)”, respectively:

(5) EFFECTIVE DATE. —The amendments made by this subsection shall apply to items and services furnished after the date of the enactment of this Act.

(c) SPECIAL ENROLLMENT PERIOD FOR DISABLED EMPLOYEES. —

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TITLE VII —REVENUE MEASURES

SEC. 7001. SHORT TITLE; ETC.

(a) SHORT TITLE. —This title may be cited as the “Revenue Reconciliation Act of 1989”.

(b) AMENDMENT OF 1986 CODE. —Except as otherwise expressly provided, whenever in this title an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

(c) TABLE OF CONTENTS. —

TITLE VII —REVENUE MEASURES

Sec. 7001. Short title; etc.

Subtitle A —Extension of Expiring Tax Provisions

Sec. 7101. Employer-provided educational assistance.

Sec. 7102. Employer-provided group legal services.

Sec. 7103. Extension and modification of targeted jobs credit.

Sec. 7104. Extension of qualified mortgage bonds.

Sec. 7105. Extension of qualified small issue bonds.

Sec. 7106. Extension of energy investment credit for solar, geothermal, and ocean thermal property.

Sec. 7107. Extension of special rules for health insurance costs of self-employed individuals.

Sec. 7108. Extension and modification of low-income housing credit.

Sec. 7109. Low-income housing credit exempt from income phase out of \$25,000 exemption from passive loss rules.

Sec. 7110. Extension and modification of research credit.

Sec. 7111. Allocation of research and experimental expenditures.

Subtitle B —Corporate Provisions

Sec. 7201. Limitation on use of group losses to offset income of subsidiary paying preferred dividends.

Sec. 7202. Treatment of certain high yield original issue discount obligations.

Sec. 7203. Securities treated as boot under section 351.

Sec. 7204. Provisions related to regulated investment companies.

Sec. 7205. Limitation on threshold requirement under section 382 built-in gain and loss provisions.

Sec. 7206. Distributions on certain preferred stock treated as extraordinary dividends.

Sec. 7207. Repeal of election to reduce excess loss account recapture by reducing basis of indebtedness.

Sec. 7208. Other provisions relating to treatment of stock and debt; etc.

Sec. 7209. Estimated tax payments required for S corporations.

Sec. 7210. Limitation on deduction for certain interest paid to related person.

Sec. 7211. Limitations on refunds due to net operating loss carrybacks or excess interest allocable to corporate equity reduction transactions.

Subtitle C —Employee Benefit Provisions

PART I —EMPLOYEE STOCK OWNERSHIP PLAN PROVISIONS

Sec. 7301. Limitations on partial exclusion of interest on loans used to acquire employer securities.

Sec. 7302. Limitations on deductions for dividends paid on employer securities.

Sec. 7303. 3-year holding period required before section 1042 sale.

Sec. 7304. Repeal of certain provisions relating to employee stock ownership plans.

PART II —SECTION 401(h) ACCOUNTS

Sec. 7311. Limitation on contributions to section 401(h) accounts.

Subtitle D —Foreign Provisions

Sec. 7401. Taxable year of certain foreign corporations.

Sec. 7402. Limitation on use of deconsolidation to avoid foreign tax credit limitations.

Sec. 7403. Information with respect to certain foreign-owned corporations.

Sec. 7404. Repeal of special treatment of interest on certain foreign loans.

Subtitle E —Excise Tax Provisions

Sec. 7501. 1-year suspension of automatic reduction in aviation-related taxes.

Sec. 7502. Acceleration of deposit requirements for airline ticket tax.

Sec. 7503. Increase in international air passenger departure tax.

Sec. 7504. Ship passengers international departure tax.

Sec. 7505. Oil Spill Liability Trust Fund tax to take effect on January 1, 1990.

Sec. 7506. Excise tax on sale of chemicals which deplete the ozone layer and of products containing such chemicals.

Sec. 7507. Acceleration of deposit requirements for gasoline excise tax.

Sec. 7508. Taxation of bulk cigar imports.

Subtitle F —Miscellaneous Provisions

PART I —LIMITATION ON NONRECOGNITION FOR CERTAIN EXCHANGES

Sec. 7601. Like kind exchanges between related persons.

PART II —MINIMUM TAX PROVISIONS

Sec. 7611. Simplification of adjusted current earnings preference.

Sec. 7612. Other modifications to minimum tax.

PART III —ACCOUNTING PROVISIONS

Sec. 7621. Repeal of completed contract method of accounting for long-term contracts.

Sec. 7622. Changes in treatment of transfers of franchises, trademarks, and trade names.

PART IV —EMPLOYMENT TAX PROVISIONS

Sec. 7631. Treatment of agricultural workers under wage withholding.

Sec. 7632. Acceleration of deposit requirements.

PART V —OTHER PROVISIONS

Sec. 7641. Limitation on section 104 exclusion.

Sec. 7642. Treatment of distributions by partnerships of contributed property.

Sec. 7643. Depreciation treatment of cellular telephones.

Sec. 7644. Elimination of retroactive certification of employees for work incentive job credit.

Sec. 7645. Disallowance of depreciation for certain term interests.

Sec. 7646. Reporting of points on mortgage loans.

Sec. 7647. Treatment of certain investment-oriented life insurance contracts.

PART VI —TAX EXEMPT BOND PROVISIONS

Sec. 7651. Treatment of hedge bonds.

Sec. 7652. Exceptions from arbitrage rebate requirement.

Subtitle G —Revision of Civil Penalties

Sec. 7701. Short title.

PART I —DOCUMENT AND INFORMATION RETURN PENALTIES

Sec. 7711. Uniform penalties for failures to comply with certain information reporting requirements.

Sec. 7712. Information required with respect to certain foreign corporations.

Sec. 7713. Uniform requirements for returns on magnetic media.

Sec. 7714. Study of procedures to prevent mismatching.

Sec. 7715. Study of service bureaus.

PART II —REVISION OF ACCURACY-RELATED PENALTIES

Sec. 7721. Revision of accuracy-related penalties.

PART III —PREPARER, PROMOTER, AND PROTESTER PENALTIES

Sec. 7731. Penalty for instituting proceedings before tax court primarily for delay, etc.

Sec. 7732. Modifications to penalties on return preparers for certain under statements.

Sec. 7733. Modifications to other assessable penalties with respect to return preparers.

Sec. 7734. Modifications to penalty for promoting abusive tax shelters, etc.

Sec. 7735. Modifications to penalties for aiding and abetting understatement of tax liability.

Sec. 7736. Modification to penalty for frivolous income tax return.

Sec. 7737. Authority to counterclaim for balance of penalty in partial refund suits.

Sec. 7738. Repeal of bonding requirement under section 7407.

Sec. 7739. Certain disclosures of information by preparers permitted.

PART IV —FAILURES TO FILE OR PAY

Sec. 7741. Increase in penalty for fraudulent failure to file.

Sec. 7742. Failure to make deposit of taxes.

Sec. 7743. Effect of payment of tax by recipient on certain penalties.

Subtitle H —Technical Corrections

Sec. 7801. Definitions; coordination with other subtitles.

PART I —AMENDMENTS RELATED TO TECHNICAL AND MISCELLANEOUS REVENUE ACT OF 1988

Sec. 7811. Amendments related to title I of the 1988 Act.

Sec. 7812. Amendments related to title II of the 1988 Act.

Sec. 7813. Amendments related to title III of the 1988 Act.

Sec. 7814. Amendments related to title IV of the 1988 Act.

Sec. 7815. Amendments related to title V of the 1988 Act.

Sec. 7816. Amendments related to title VI of the 1988 Act.

Sec. 7817. Effective date.

PART II —AMENDMENTS RELATED TO REVENUE ACT OF 1987

Sec. 7821. Amendments related to subtitle B.

Sec. 7822. Amendments related to subtitle C and following subtitles.

Sec. 7823. Effective date.

PART III —AMENDMENTS RELATED TO TAX REFORM ACT OF 1986

Sec. 7831. Amendment related to Tax Reform Act of 1986.

PART IV —MISCELLANEOUS CHANGES

Sec. 7841. Miscellaneous changes.

PART V —AMENDMENTS RELATED TO PENSION PROVISIONS

Sec. 7851. Definitions.

SUBPART A —AMENDMENTS RELATED TO TAX REFORM ACT OF 1986

Sec. 7861. Amendments related to title XI of the Reform Act.

Sec. 7862. Amendments related to title XVIII of the Reform Act.

Sec. 7863. Effective date.

SUBPART B —AMENDMENTS RELATED TO OMNIBUS BUDGET RECONCILIATION ACT OF 1986

Sec. 7871. Amendments related to Omnibus Budget Reconciliation Act of 1986.

SUBPART C —AMENDMENTS RELATED TO PENSION PROTECTION ACT

Sec. 7881. Amendments related to Pension Protection Act.

Sec. 7882. Effective date.

SUBPART D —ADDITIONAL PENSION PROVISIONS

Sec. 7891. Amendments relating to the Tax Reform Act of 1986.

Sec. 7892. Amendments relating to the Pension Protection Act.

Sec. 7983. Amendments relating to the Single-Employer Pension Plan Amendments Act of 1986.

Sec. 7894. Other amendments to ERISA.

Subtitle A —Extension of Expiring Tax Provisions

SEC. 7101. EMPLOYER-PROVIDED EDUCATIONAL ASSISTANCE.

(a) EXTENSION. —

(1) IN GENERAL. —Subsection (d) of section 127 (relating to educational assistance programs) is amended by striking “December 31, 1988” and inserting “September 30, 1990”.

(2) SPECIAL RULE. —In the case of any taxable year beginning in 1990, only amounts paid before October 1, 1990, by the employer for educational assistance for the employee shall be taken into account in determining the amount excluded under section 127 of the Internal Revenue Code of 1986 with respect to such employee for such taxable year.

(b) CERTAIN OTHERWISE TAXABLE EMPLOYER-PROVIDED EDUCATIONAL ASSISTANCE MAY BE EXCLUDIBLE AS WORKING CONDITION FRINGE —Subsection (h) of section 132 is amended by adding at the end thereof the following new paragraph:

“(9) APPLICATION OF SECTION TO OTHERWISE TAXABLE EMPLOYER-PROVIDED EDUCATIONAL ASSISTANCE. —Amounts which would be excludible from gross income under section 127 but for subsection (a)(2) thereof or the last sentence of subsection (c)(1) thereof shall be excluded from gross income under this section if (and only if) such amounts are a working condition fringe.”

(c) EFFECTIVE DATE. —The amendments made by this section shall apply to taxable years beginning after December 31, 1988.

SEC. 7102. EMPLOYER-PROVIDED GROUP LEGAL SERVICES.

(a) EXTENSION. —

(1) IN GENERAL. —Subsection (e) of section 120 (relating to group legal service plans) is amended by striking “ending after December 31, 1988” and inserting “beginning after September 30, 1990”.

(2) SPECIAL RULE. —In the case of any taxable year beginning in 1990, only amounts paid before October 1, 1990, by the employer for coverage for the employee, his spouse, or his dependents under a qualified group legal services plan for periods before October 1, 1990, shall be taken into account in determining the amount excluded under section 120 of the Internal Revenue Code of 1986 with respect to such employee for such taxable year.

(b) EFFECTIVE DATE. —The amendment made by subsection (a) shall apply to taxable years ending after Subparagraph December 31, 1988.

SEC. 7103. EXTENSION AND MODIFICATION OF TARGETED JOBS CREDIT.

(a) EXTENSION. —Paragraph (4) of section 51(c) (relating to termination) is amended by striking “December 31, 1989” and inserting “September 30, 1990”.

(b) EXTENSION OF AUTHORIZATION. —Paragraph (2) of section 261(f) of the Economic Recovery Tax Act of 1981 is amended by striking “and 1989” and inserting “1989, and 1990”.

(c) MODIFICATION OF REQUEST FOR CERTIFICATION. —

(1) IN GENERAL. —Paragraph (16) of section 51(d) is amended by adding at the end thereof the following new subparagraph:

“(C) EMPLOYER REQUEST MUST SPECIFY POTENTIAL BASIS FOR ELIGIBILITY. —In any request for a certification of an individual as a member of a targeted group, the employer shall —

“(i) specify each subparagraph (but not more than 2) of paragraph (1) by reason of which the employer believes that such individual is such a member, and

“(ii) certify that a good faith effort was made to determine that such individual is such a member.”

(2) EFFECTIVE DATE. —The amendment made by paragraph (1) shall apply to individuals who begin work for the employer after December 31, 1989.

SEC. 7104. EXTENSION OF QUALIFIED MORTGAGE BONDS.

(a) IN GENERAL. —Subparagraph (B) of section 143(a)(1) (defining qualified mortgage bond) is amended by striking “December 31, 1989” each place it appears and inserting “September 30, 1990”.

(b) MORTGAGE CREDIT CERTIFICATES. —Subsection (h) of section 25 is amended by striking “for any calendar year after 1989” and inserting “for any period after September 30, 1990”.

SEC. 7105. EXTENSION OF QUALIFIED SMALL ISSUE BONDS.

Subparagraph (B) of section 144(a)(12) is amended by striking “substituting `1989' for `1986' ” and inserting “substituting `September 30, 1990' for `December 31, 1986' ”

SEC. 7106. EXTENSION OF ENERGY INVESTMENT CREDIT FOR SOLAR, GEOTHERMAL, AND OCEAN THERMAL PROPERTY.

The table contained in section 46(b)(2)(A) (relating to energy percentage) is amended by striking “Dec. 31, 1989” in clauses (viii), (ix), and (x) and inserting “Sept. 30, 1990”.

SEC. 7107. EXTENSION OF SPECIAL RULES FOR HEALTH INSURANCE COSTS OF SELF-EMPLOYED INDIVIDUALS.

(a) EXTENSION. —

(1) GENERAL RULE. —Paragraph (5) of section 162(l) (relating to special rules for health insurance costs of self-employed individuals) is amended by striking “December 31, 1989” and inserting “September 30, 1990”.

(2) SPECIAL RULE. —In the case of any taxable year beginning in 1990 —

(A) only amounts paid before October 1, 1990, by the individual for insurance coverage for periods before October 1, 1990, shall be taken into account in determining the amount deductible under section 162(l) of the Internal Revenue Code of 1986 with respect to such individual for such taxable year, and

(B) for purposes of section 162(l)(2)(A) of such Code, the amount of the earned income described in such paragraph taken into account for such taxable year shall be the amount which bears the same ratio to the total amount of such earned income as the number of months in such taxable year ending before October 1, 1990, bears to the number of months in such taxable year.

(b) SPECIAL RULE FOR CERTAIN CORPORATION SHAREHOLDERS. —Subsection (1) of section 162 (as amended by subsection (a)) is amended by redesignating paragraph (5) as paragraph (6) and by inserting after paragraph (4) the following new paragraph:

“(5) TREATMENT OF CERTAIN S CORPORATION SHAREHOLDERS. —This subsection shall apply in the case of any individual treated as a partner under section 1372(a), except that —

“(A) for purposes of this subsection, such individual's wages (as defined in section 3121) from the S corporation shall be treated as such individual's earned income (within the meaning of section 401(c)(1)), and

“(B) there shall be such adjustments in the application of this subsection as the Secretary may by regulations prescribe.”

EFFECTIVE DATE. —The amendments made by this section shall apply to taxable years beginning after

December 31, 1989.

SEC. 7108. EXTENSION AND MODIFICATION OF LOW-INCOME HOUSING CREDIT.

(a) EXTENSION. —

(1) IN GENERAL. — Subsection (n) of section 42 (relating to low-income housing credit) is amended to read as follows —

“(n) TERMINATION. —

“(1) IN GENERAL. — Except as provided in paragraph (2), for any calendar year after 1990 —

“(A) clause (i) of subsection (h)(3)(C) shall not apply, and

“(B) subsection (h)(4) shall not apply to any building placed in service after 1990.

“(2) EXCEPTION FOR BOND-FINANCED BUILDINGS IN PROGRESS. — For purposes of paragraph (1)(B), a building shall be treated as placed in service before 1990 if —

“(A) the bonds with respect to such building are issued before 1990,

“(B) such building is constructed, reconstructed, or rehabilitated by the taxpayer,

“(C) more than 10 percent of the reasonably anticipated cost of such construction, reconstruction, or rehabilitation has been incurred as of January 1, 1990, and some of such cost is incurred on or after such date, and

“(D) such building is placed in service before January 1, 1992.

(2) SPECIAL RULE. — In the case of calendar year 1990, section 42(h)(3)(C)(i) of the Internal Revenue Code of 1986 (as amended by subsection (b)(1)) shall be applied by substituting “\$.9375” for “\$1.25”.

(b) 1-YEAR CARRYOVER OF UNUSED CREDIT AUTHORITY, ETC. —

(1) IN GENERAL. — Section 42(h)(3) (relating to housing credit dollar amount for agencies) is amended by redesignating subparagraphs (D), (E), and (F) as subparagraph (C) and inserting the following new subparagraphs:

“(C) STATE HOUSING CREDIT CEILING. — The State housing credit ceiling applicable to any State for any calendar year shall be an amount equal to the sum of —

“(i) \$1.25 multiplied by the State population,

“(ii) the unused State housing credit ceiling (if any) of such State for the preceding calendar year,

“(iii) the amount of State housing credit ceiling returned in the calendar year, plus

“(iv) the amount (if any) allocated under subparagraph (D) to such State by the Secretary.

For purposes of clause (ii), the unused State housing credit ceiling for any calendar year is the excess (if any) of the amount described in clause (i) over the aggregate housing credit dollar amount allocated for such year. For purposes of clause (iii), the amount of State housing credit ceiling returned in the calendar year equals the housing credit dollar amount previously allocated within the State to any project which does not become a qualified low-income housing project within the period required by this section or the terms of the allocation or to any project with respect to which an allocation is canceled by mutual consent of the housing credit agency and the allocation recipient.

“(D) UNUSED HOUSING CREDIT CARRYOVERS ALLOCATED AMONG CERTAIN STATES. —

“(i) IN GENERAL. —The unused housing credit carryover of a State for any calendar year shall be assigned to the Secretary for allocation among qualified States for the succeeding calendar year.

“(ii) UNUSED HOUSING CREDIT CARRYOVER. —For purposes of this subparagraph, the unused housing credit carryover of a State for any calendar year is the excess (if any) of the unused State housing credit ceiling for such year (as defined in subparagraph (C)(ii)) over the excess (if any) of —

“(I) the aggregate housing credit dollar amount allocated for such year, over

“(II) the amount described in clause (i) of subparagraph (C).

“(iii) FORMULA FOR ALLOCATION OF UNUSED HOUSING CREDIT CARRYOVERS AMONG QUALIFIED STATES. —The amount allocated under this subparagraph to a qualified State for any calendar year shall be the amount determined by the Secretary to bear the same ratio to the aggregate unused housing credit carryovers of all States for the preceding calendar year as such State's population for the calendar year bears to the population of all qualified States for the calendar year. For purposes of the preceding sentence, population shall be determined in accordance with section 146(j).

“(iv) QUALIFIED STATE. —For purposes of this subparagraph, the term “qualified State means, with respect to a calendar year, any State —

“(I) which allocated its entire State housing credit ceiling for the preceding calendar year, and

“(II) for which a request is made (not later than May 1 of the calendar year) to receive an allocation under clause (iii).”

(2) CONFORMING AMENDMENTS. —

(A) Subparagraph (E) of section 42(h)(5) is amended by striking “subparagraph (E)” and inserting “subparagraph (F)”.

(B) Paragraph (6) of section 42(h) is amended by striking subparagraph (B) and by redesignating subparagraphs (C), (D), and (E) as subparagraphs (B), (C), and (D), respectively.

(c) BUILDINGS ELIGIBLE FOR CREDIT ONLY IF MINIMUM LONG-TERM COMMITMENT TO LOW-INCOME HOUSING. —

(1) IN GENERAL. —Section 42(h) (relating to limitation on aggregate credit allowable with respect to projects located in a State) is amended by redesignating paragraphs (6) and (7) as paragraphs (7) and (8), respectively, and by inserting after paragraph (5) the following new paragraph:

“(6) BUILDINGS ELIGIBLE FOR CREDIT ONLY IF MINIMUM LONG-TERM COMMITMENT TO

LOW-INCOME HOUSING. —

“(A) IN GENERAL. —No credit shall be allowed by reason of this section with respect to any building for the taxable year unless an extended low-income housing commitment is in effect as of the end of such taxable year.

“(B) EXTENDED LOW-INCOME HOUSING COMMITMENT. —For purposes of this paragraph, the term `extended low-income housing commitment' means any agreement between the taxpayer and the housing credit agency —

“(i) which requires that the applicable fraction (as defined in subsection (c)(1)) for the building for each taxable year in the extended use period will not be less than the applicable fraction specified in such agreement.

“(ii) which allows individuals who meet the income limitation applicable to the building under subsection (g) (whether prospective, present, or former occupants of the building) the right to enforce in any State court the requirement of clause (i),

“(iii) which is binding on all successors of the taxpayer, and

“(iv) which, with respect to the property, is recorded pursuant to State law as a restrictive covenant.

“(C) ALLOCATION OF CREDIT MAY NOT EXCEED AMOUNT NECESSARY TO SUPPORT COMMITMENT. —

“(i) IN GENERAL. —The housing credit dollar amount allocated to any building may not exceed the amount necessary to support the applicable fraction specified in the extended low-income housing commitment for such building, including any increase in such fraction pursuant to the application of subsection (f)(3) if such increase is reflected in an amended low-income housing commitment.

“(ii) BUILDINGS FINANCED BY TAX-EXEMPT BONDS. —If paragraph (4) applies to any building the amount of credit allowed in any taxable year may not exceed the amount necessary to support the applicable fraction specified in the extended low-income housing commitment for such building. Such commitment may be amended to increase such fraction.

“(D) EXTENDED USE PERIOD. —For purposes of this paragraph, the term `extended use period' means the period —

“(i) beginning on the 1st day in the compliance period on which such building is part of a qualified low-income housing project, and

“(ii) ending on the later of —

“(I) the date specified by such agency in such agreement, or

“(II) the date which is 15 years after the close of the compliance period.

“(E) EXCEPTIONS IF FORECLOSURE OR IF NO BUYER WILLING TO MAINTAIN LOW-INCOME STATUS. —

“(i) IN GENERAL. —The extended use period for any building shall terminate —

“(I) on the date the building is acquired by foreclosure (or instrument in lieu of foreclosure), or

“(II) on the last day of the period specified in subparagraph (I) if the housing credit agency is unable to present during such period a qualified contract for the acquisition of the low-income portion of the building by any person who will continue to operate such portion as a qualified low-income building.

Subclause (II) shall not apply to the extent more stringent requirements are provided in the agreement or in State law.

“(ii) EVICTION, ETC. OF EXISTING LOW-INCOME TENANTS NOT PERMITTED. —The termination of an extended use period under clause (i) shall not be construed to permit before the close of the 3-year period following such termination —

“(I) the eviction or the termination of tenancy (other than for good cause) of an existing tenant of any low-income unit, or

“(II) any increase in the gross rent with respect to such unit.

“(F) QUALIFIED CONTRACT. —For purposes of subparagraph (E), the term ‘qualified contract’ means a bona fide contract to acquire (within a reasonable period after the contract is entered into) the low-income portion of the building for an amount not less than the applicable fraction (specified in the extended low-income housing commitment) of —

“(i) the sum of —

“(I) the outstanding indebtedness secured by, or with respect to, the building,

“(II) the adjusted investor equity in the building, plus

“(III) other capital contributions not reflected in the amounts described in subclause (I) or (II), reduced by

“(ii) cash distributions from (or available for distribution from) the project.

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out this paragraph, including regulations to prevent the manipulation of the amount determined under the preceding sentence.

“(G) ADJUSTED INVESTOR EQUITY. —

“(i) IN GENERAL. —For purposes of subparagraph (E), the term ‘adjusted investor equity’ means, with respect to any calendar year, the aggregate amount of cash taxpayers invested with respect to the project increased by the amount equal to —

“(I) such amount, multiplied by

“(II) the cost-of-living adjustment for such calendar year, determined under section 1(f)(3) by substituting the base calendar year for ‘calendar year 1987’.

An amount shall be taken into account as an investment in the project only to the extent there was an obligation to invest such amount as of the beginning of the credit period and to the extent such amount is reflected in the adjusted basis of the project.

“(ii) COST-OF-LIVING INCREASES IN EXCESS OF 5 PERCENT NOT TAKEN INTO ACCOUNT. — Under regulations prescribed by the Secretary, if the CPI for any calendar year (as defined in section 1(f)(4)) exceeds the CPI for the preceding calendar year by more than 5 percent, the CPI for the base calendar year shall be increased such that such excess shall never be taken into account under clause (i).

“(III) BASE CALENDAR YEAR. —For purposes of this subparagraph, the term ‘base calendar year’ means the calendar year with or within which the 1st taxable year of the credit period ends.

“(H) LOW-INCOME PORTION. —For purposes of this paragraph, the low-income portion of a building is the portion of such building equal to the applicable fraction specified in the extended low-income housing commitment for the building.

“(I) PERIOD FOR FINDING BUYER. —The period referred to in this subparagraph is the 1-year period beginning on the date (after the 14th year of the compliance period) the taxpayer submits a written request to the housing credit agency to find a period to acquire the taxpayer's interest in the low-income portion of the building.

“(J) SALES OF LESS THAN LOW-INCOME PORTION OF BUILDING. —In the case of a sale or exchange of only a portion of the low-income portion of the building, only the same portion (as the portion sold or exchanged) of the amount determined under subparagraph (F) shall be taken into account thereunder.

“(K) EFFECT OF NONCOMPLIANCE. —If during a taxable year, there is a determination that an extended low-income housing agreement was not in effect as of the beginning of such year, such determination shall not apply to any period before such year and subparagraph (A) shall be applied without regard to such determination if the failure is corrected within 1 year from the date of the determination.

“(L) PROJECTS WHICH CONSIST OF MORE THAN 1 BUILDING. —The application of this paragraph to projects which consist of more than 1 building shall be made under regulations prescribed by the Secretary.”

(2) CONFORMING AMENDMENT. —Subparagraph (C) of section 42(b)(3) is amended by striking “subsection (h)(6)” and inserting “subsection (h)(7)”.

(d) CREDIT FOR ACQUISITION OF EXISTING BUILDING TO APPLY ONLY IF BUILDING TO BE REHABILITATED; INCREASE IN REQUIRED REHABILITATION EXPENDITURES. —

(1) IN GENERAL. —Subparagraph (B) of section 42(d)(2) is amended by striking “and” at the end of clause (ii), by striking the period at the end of clause (iii) and inserting “, and”, and by adding at the end thereof the following new clause:

“(iv) except as provided in subsection (f)(5), a credit is allowable under subsection (a) by reason of subsection (e) with respect to the building.”

(2) CREDIT PERIOD FOR EXISTING BUILDINGS NOT TO BEGIN BEFORE REHABILITATION CREDIT ALLOWED. —Subsection (f) of section 42 (relating to definition and special rules relating to credit period), as amended by subtitle H, is amended by adding at the end thereof the following new paragraph:

“(5) CREDIT PERIOD FOR EXISTING BUILDINGS NOT TO BEGIN BEFORE REHABILITATION CREDIT ALLOWED. —

“(A) IN GENERAL. —The credit period for an existing building shall not begin before the 1st taxable year

of the credit period for rehabilitation expenditures with respect to the building.

“(B) ACQUISITION CREDIT ALLOWED FOR CERTAIN BUILDINGS NOT ALLOWED A REHABILITATION CREDIT. —

“(i) IN GENERAL. —In the case of a building described in clause (ii) —

“(I) subsection (d)(2)(B) (iv) shall not apply, and

“(II) the credit period for such building shall not begin before the taxable year which would be the 1st taxable year of the credit period for rehabilitation expenditures with respect to the building under the modifications described in clause (ii)(II).

“(ii) BUILDING DESCRIBED. —A building is described in this clause if —

“(I) a waiver is granted under subsection (d)(6)(C) with respect to the acquisition of the building, and

“(II) a credit would be allowed for rehabilitation expenditures with respect to such building if subsection (e)(3)(A)(ii)(I) did not apply and if subsection (e)(3)(A)(ii)(II) were applied by substituting ‘\$2,000’ for ‘\$3,000.’”

(3) INCREASE IN REQUIRED REHABILITATION EXPENDITURES. —Paragraph (3) of section 42(e) is amended by redesignating subparagraph (B) as subparagraph (C) and by striking so much of such paragraph as precedes such subparagraph and inserting the following:

“(3) MINIMUM EXPENDITURES TO QUALIFY. —

“(A) IN GENERAL. —Paragraph (1) shall apply to rehabilitation expenditures with respect to any building only if —

“(i) the expenditures are allocable to 1 or more low-income units or substantially benefit such units, and

“(ii) the amount of such expenditures during any 24-month period meets the requirements of whichever of the following subclauses requires the greater amount of such expenditures:

“(I) The requirement of this subclause is met if such amount is not less than 10 percent of the adjusted basis of the building (determined as of the 1st day of such period and without regard to paragraphs (2) and (3) of section 1016(a)).

“(II) The requirement of this subclause is met if the qualified basis attributable to such amount, when divided by the number of low-income units in the building, is \$3,000 or more.

“(B) EXCEPTION FROM 10 PERCENT REHABILITATION. —In the case of a building acquired by the taxpayer from a governmental unit, at the election of the taxpayer, subparagraph (A)(ii)(I) shall not apply and the credit under this section for such rehabilitation expenditures shall be determined using the percentage applicable under subsection (b)(2)(B)(ii).”

(e) CHANGES IN RULES RELATING TO RENT RESTRICTIONS. —

(1) RENT RESTRICTION DETERMINED ON BASIS OF NUMBER OF BEDROOMS. —

(A) Section 42(g)(2) is amended by redesignating subparagraph (C) as subparagraph (E) and by inserting

after subparagraph (B) the following new subparagraphs:

“(C) IMPUTED INCOME LIMITATION APPLICABLE TO UNIT. —For purposes of this paragraph, the imputed income limitation applicable to a unit is the income limitation which would apply under paragraph (1) to individuals occupying the unit of the number of individuals occupying the unit were as follows:

“(i) In the case of a unit which does not have a separate bedroom, 1 individual.

“(ii) In the case of a unit which has 1 or more separate bedrooms, 1.5 individuals for each separate bedroom.

In the case of a project with respect to which a credit is allowable by reason of this section and for which financing is provided by a bond described in section 142(a)(7), the imputed income limitation shall apply in lieu of the otherwise applicable income limitation for purposes of applying section 142(d)(4)(B)(ii).

“(D) TREATMENT OF UNITS OCCUPIED BY INDIVIDUALS WHOSE INCOMES RISE ABOVE LIMIT. —

“(i) IN GENERAL. —Except as provided in clause (ii), notwithstanding an increase in the income of the occupants of a low-income unit above the income limitation applicable under paragraph (1), such unit shall continue to be treated as a low-income unit if the income of such occupants initially met such income limitation.

“(ii) NEXT AVAILABLE UNIT MUST BE RENTED TO LOW-INCOME TENANT IF INCOME RISES ABOVE 140 PERCENT OF INCOME LIMIT. —If the income of the occupants of the unit increases above 140 percent of the income limitation applicable under paragraph (1), clause (i) shall cease to apply to such unit if any residential rental unit in the building (of a size comparable to, or smaller than, such unit) is occupied by a new resident whose income exceeds such income limitation.”

(B) Subparagraph (A) of section 42(g)(2) is amended by striking “the income limitation under paragraph (1) applicable to individuals occupying such unit” and inserting “the imputed income limitation applicable to such unit.”

(2) **REDUCTION IN AREA MEDIAN GROSS INCOME NOT TO REQUIRE REDUCTION OF RENT.** —Subparagraph (A) of section 42(g)(2) (relating to rent-restricted units) is amended by adding at the end thereof the following new sentence: “For purposes of the preceding sentence, the amount of the income limitation under paragraph (1) applicable for any period shall not be less than such limitation applicable for the earliest period the building (which contains the unit) was included in the determination of whether the project is a qualified low-income housing project.”

(3) **EXCLUSION WITH RESPECT TO CONTINUING CARE FACILITIES NOT TO APPLY IN DETERMINING INCOME.** —Subparagraph (B) of section 142(d)(2) is amended by adding at the end thereof the following:

“Section 7872(g) shall not apply in determining the income of individuals under this subparagraph.”

(f) **ADDITIONAL BUILDING ELIGIBLE FOR WAIVER OF 10-YEAR PERIOD APPLICABLE TO ACQUISITIONS OF EXISTING BUILDINGS.** —Paragraph (6) of section 42(d) is amended by redesignating subparagraph (6) of section 42(d) is amended by redesignating subparagraph (C) as subparagraph (E) and by inserting after subparagraph (B) the following new subparagraphs:

“(C) LOW-INCOME BUILDINGS WHERE MORTGAGE MAY BE PREPAID. —A waiver may be granted under subparagraph (A) (without regard to any clause thereof) with respect to a federally-assisted

building described in clause (ii) or (iii) of subparagraph (B) if —

“(i) the mortgage on such building is eligible for prepayment under subtitle B of the Emergency Low Income Housing Preservation Act of 1987 or under section 502(c) of the Housing Act of 1949 at any time within 1 year after the date of the application for such a waiver.

“(ii) the appropriate Federal official certifies to the Secretary that it is reasonable to expect that, if the waiver is not granted, such building will cease complying with its low-income occupancy requirements, and

“(iii) the eligibility to prepay such mortgage without the approval of the appropriate Federal official is waived by all persons who are so eligible and such waiver is binding on all successors of such persons.

“(D) BUILDINGS ACQUIRED FROM INSURED DEPOSITORY INSTITUTIONS IN DEFAULT. —A waiver may be granted under subparagraph (A) (without regard to any clause thereof) with respect to any building acquired from an insured depository institution in default (as defined in section 3 of the Federal Deposit Insurance Act) or from a receiver or conservator of such an institution.”

(g) INCREASE IN CREDIT FOR BUILDINGS IN HIGH COST AREAS. —Paragraph (5) of section 42(d) (relating to eligible basis) is amended by adding at the end thereof the following new subparagraph:

“(D) INCREASE IN CREDIT FOR BUILDINGS IN HIGH COST AREAS. —

“(i) IN GENERAL. —In the case of any building located in a qualified census tract or difficult development area which is designated for purposes of this subparagraph —

“(I) in the case of a new building, the eligible basis of such building shall be 130 percent of such basis determined without regard to this subparagraph, and

“(II) in the case of an existing building, the rehabilitation expenditures taken into account under subsection (e) shall be 130 percent of such expenditures determined without regard to this subparagraph.

“(ii) QUALIFIED CENSUS TRACT. —

“(I) IN GENERAL. —The term ‘qualified census tract’ means any census tract in which 50 percent or more of the households have an income which is less than 60 percent of the area median gross income.

“(II) LIMIT ON MSA'S DESIGNATED. —The portion of a metropolitan statistical area which may be designated for purposes of this subparagraph shall not exceed an area having 20 percent of the population of such metropolitan statistical area.

“(III) DETERMINATION OF AREAS. —For purposes of this clause, each metropolitan statistical area shall be treated as a separate area and all nonmetropolitan areas in a State shall be treated as 1 area.

“(iii) DIFFICULT DEVELOPMENT AREAS. —

“(I) IN GENERAL. —The term ‘difficult development areas’ means any area designated by the Secretary of Housing and Urban Development as an area which has high construction, land, and utility costs relative to area median gross income.

“(II) LIMIT ON AREAS DESIGNATED. —The portions of metropolitan statistical areas which may be designated for purposes of this subparagraph shall not exceed an aggregate area having 20 percent of the population of such metropolitan statistical areas. A comparable rule shall apply to nonmetropolitan areas.

“(iv) SPECIAL RULES AND DEFINITIONS. —For purposes of this subparagraph —

“(I) population shall be determined on the basis of the most recent decennial census for which data are available,

“(II) area median gross income shall be determined in accordance with subsection (g)(4),

“(III) the term ‘metropolitan statistical area’ has the same meaning as when used in section 143(k)(2)(B), and

“(IV) the term ‘nonmetropolitan area’ means any county (or portion thereof) which is not within a metropolitan statistical area.”

(h) CHANGES IN RULES RELATING TO BUILDING FOR WHICH CREDIT MAY BE ALLOWED.

—

(1) SINGLE-ROOM OCCUPANCY UNITS RENTED ON A MONTHLY BASIS. —Subparagraph (B) of section 42(i)(3) (relating to low income unit) is amended by adding at the end thereof the following new sentence: “For purposes of the preceding sentence, a single-room occupancy unit shall not be treated as used on a transient basis merely because it is rented on a month-by-month basis.”

(2) SPECIAL NEEDS HOUSING. —Subparagraph (B) of section 42(g)(2) (relating to gross rent) is amended —

(A) in clause (i), by striking “and” at the end,

(B) in clause (ii), by striking the period at the end and inserting “, and”, and

(C) by adding at the end the following:

“(iii) does not include any fee for a supportive service which is paid to the owner of the unit (on the basis of the low-income status of the tenant of the unit) by any governmental program of assistance (or by an organization described in section 501(c)(3) and exempt from tax under section 501(a) if such program (or organization) provides assistance for rent and the amount of assistance provided for rent is not separable from the amount of assistance provided for supportive services.

For purposes of clause (iii), the term ‘supportive service’ means any service provided under a planned program of services designed to enable residents of a residential rental property to remain independent and avoid placement in a hospital nursing home, or intermediate care facility for the mentally or physically handicapped. In the case of a single-room occupancy unit or a building described in subsection (i)(3)(B)(iii), such term includes any service provided to assist tenants in locating and retaining permanent housing.”

(3) SCATTERED SITE PROJECTS. —Section 42(g) (relating to qualified low-income housing project) is amended by adding at the end thereof the following new paragraph:

“(7) SCATTERED SITE PROJECTS. —Buildings which would (but for their lack of proximity) be treated as a project for purposes of this section shall be so treated if all of the dwelling units in each of the buildings are rent-restricted (within the meaning of paragraph (2)) residential rental units.”

(4) OWNER-OCCUPIED BUILDINGS HAVING 4 OR FEWER UNITS ELIGIBLE FOR CREDIT WHERE DEVELOPMENT PLAN. —Section 42(i)(3) (defining low-income unit), as amended by subtitle

H, is amended by adding at the end thereof the following new subparagraph:

“(E) OWNER-OCCUPIED BUILDINGS HAVING 4 OR FEWER UNITS ELIGIBLE FOR CREDIT WHERE DEVELOPMENT PLAN. —

“(i) IN GENERAL. —Subparagraph (C) shall not apply to the acquisition or rehabilitation of a building pursuant to a development plan of action sponsored by a State or local government or a qualified nonprofit organization (as defined in subsection (h)(5)(C)).

“(ii) LIMITATION ON CREDIT. —In the case of a building to which clause (i) applies, the applicable fraction shall not exceed 80 percent of the unit fraction.

“(iii) CERTAIN UNRENTED UNITS TREATED AS OWNER-OCCUPIED. —In the case of a building to which clause (i) applies, any unit which is not rented for 90 days or more shall be treated as occupied by the owner of the building as of the 1st day it is not rented.”

(5) BUILDINGS RECEIVING SECTION 8 MODERATE REHABILITATION ASSISTANCE OR SIMILAR ASSISTANCE NOT ELIGIBLE FOR CREDIT. —Section 42(b)(1) (relating to applicable percentage for buildings placed in service during 1987) is amended by adding at the end thereof the following new flush sentence:

“A building shall not be treated as described in subparagraph (B) if, at any time during the credit period, moderate rehabilitation assistance is provided with respect to such building under section 8(e)(2) of the United States Housing Act of 1937.”

(i) APPLICATION OF CREDIT TO TRANSITIONAL HOUSING FOR THE HOMELESS; DENIAL OF CREDIT FOR SUBSTANDARD HOUSING. —

(1) IN GENERAL. —Subparagraph (B) of section 42(i)(3) (defining low-income unit) is amended to read as follows:

“(B) EXCEPTIONS. —

“(i) IN GENERAL. —A unit shall not be treated as a low-income unit unless the unit is suitable for occupancy and used other than on a transient basis.

“(ii) SUITABILITY FOR OCCUPANCY. —For purposes of clause (i), the suitability of a unit for occupancy shall be determined under regulations prescribed by the Secretary taking into account local health, safety, and building codes.

“(iii) TRANSITIONAL HOUSING FOR HOMELESS. —For purposes of clause (i), a unit shall be considered to be used other than on a transient basis if the unit contains sleeping accommodations and kitchen and bathroom facilities and is located in a building —

“(I) which is used exclusively to facilitate the transition of homeless individuals (within the meaning of section 103 of the Stewart B. McKinney Homeless Assistance Act (42 U.S.C. 11302), as in effect on the date of the enactment of this clause) to independent living within 24 months, and

“(II) in which a governmental entity or qualified nonprofit organization (as defined in subsection (b)(5)) provides such individuals with temporary housing and supportive services designed to assist such individuals in locating and retaining permanent housing.

“(iv) SINGLE-ROOM OCCUPANCY UNITS. —For purposes of clause (i), a single-room occupancy unit

shall not be treated as used on a transient basis merely because it is rented on a month-by-month basis.”

(2) QUALIFIED BASIS TO INCLUDE PORTION OF BUILDING USED TO PROVIDE SUPPORTIVE SERVICES. —Paragraph (1) of section 42(c) is amended by adding at the end thereof the following new subparagraph:

“(E) QUALIFIED BASIS TO INCLUDE PORTION OF BUILDING USED TO PROVIDE SUPPORTIVE SERVICES FOR HOMELESS. —In the case of a qualified low-income building described in subsection (i)(3)(B)(iii), the qualified basis of such building for any taxable year shall be increased by the lesser of —

“(i) so much of the eligible basis of such building as is used throughout the year to provide supportive services designed to assist tenants in locating and retaining permanent housing, or

“(ii) 20 percent of the qualified basis of such building (determined without regard to this subparagraph).”

(j) VOLUME CAP NOT TO APPLY WHERE 50 PERCENT OR MORE OF BUILDING IS FINANCED WITH TAX-EXEMPT BONDS. —Subparagraph (B) of section 42(h)(4) is amended by striking “70 percent” each place it appears and inserting “50 percent”.

(k) BUILDING NOT TREATED AS FEDERALLY SUBSIDIZED BY REASON OF COMMUNITY DEVELOPMENT BLOCK GRANT. —Subparagraph (D) of section 42(i)(2) (defining below market Federal loan) is amended by adding at the end thereof the following new sentence: “Such term shall not include any loan which would be a below market Federal loan solely by reason of assistance provided under section 106, 107, or 108 of the Housing and Community Development Act of 1974 (as in effect on the date of the enactment of this sentence).”

(l) ELIGIBLE BASIS FOR NEW BUILDINGS TO INCLUDE EXPENDITURES BEFORE CLOSE OF 1ST YEAR OF CREDIT PERIOD. —

(1) NEW BUILDINGS. —Paragraph (1) of section 42(d) (relating to eligible basis for new buildings) is amended by inserting before the period “as of the close of the 1st taxable year of the credit period”.

(2) EXISTING BUILDINGS. —Subparagraph (A) of section 42(d)(2) (relating to eligible basis for existing buildings) is amended by striking “subparagraph (B)” and all that follows through the end of clause (i) and inserting “subparagraph (B), its adjusted basis as of the close of the 1st taxable year of the credit period, and”.

(3) CONFORMING AMENDMENTS. —

(A) Subparagraph (C) of section 42(d)(2) is amended by striking “ACQUISITION COST” in the heading and inserting “ADJUSTED BASIS” and by striking “cost” in the text and inserting “adjusted basis”.

(B) Paragraph (5) of section 42(d), as amended by subsection (g), is further amended by striking subparagraph (A), by redesignating subparagraphs (B), (C), and (D) as subparagraphs (A), (B), and (C), respectively, and by striking the paragraph heading and inserting the following:

“(5) SPECIAL RULES FOR DETERMINING ELIGIBLE BASIS. —

(C) Paragraph (5) of section 42(e) is amended by striking “subsection (d)(2)(A)(i)(II)” and inserting “subsection (d)(2)(A)(i)”.

(m) HOUSING CREDIT MAY BE ALLOCATED ON PROJECT BASIS. —

(1) IN GENERAL. —Section 42(h)(1) (relating to credit may not exceed credit amount allocated to building) is amended by adding at the end thereof the following new subparagraph:

“(F) ALLOCATION OF CREDIT ON A PROJECT BASIS. —

“(i) IN GENERAL. —In the case of a project which includes (or will include) more than 1 building, an allocation meets the requirements of this subparagraph if —

“(I) the allocation is made to the project for a calendar year during the project period.

“(II) the allocation only applies to buildings placed in service during or after the calendar year for which the allocation is made, and

“(III) the portion of such allocation which is allocated to any building in such project is specified not later than the close of the calendar year in which the building is placed in service.

“(ii) PROJECT PERIOD. —For purposes of clause (i), the term ‘project period’ means the period —

“(I) beginning with the 1st calendar year for which an allocation may be made for the 1st building placed in service as part of such project, and

“(II) ending with the calendar year the last building is placed in service as part of such project.”

(2) CONFORMING AMENDMENT. —Subparagraph (B) of section 42(h)(1) is amended by striking “or (E)” and inserting “(E), or (F)”.

(3) PROJECTS WITH MORE THAN 1 BUILDING MUST BE IDENTIFIED. —Section 42(g)(3) (relating to date for meeting requirements) is amended by adding at the end thereof the following new subparagraph:

“(D) PROJECTS WITH MORE THAN 1 BUILDING MUST BE IDENTIFIED. —For purposes of this section, a project shall be treated as consisting of only 1 building unless, before the close of the 1st calendar year in the project period (as defined in subsection (h)(1)(F)(ii), each building which is (or will be) part of such project is identified in such form and manner as the Secretary may provide.”

(n) CHANGES IN RULES RELATED TO DEEP RENT SKEWED PROJECTS. —

(1) Clause (iii) of section 142(d)(4)(B) (relating to deep rent skewed project) is amended by striking “1/3” and inserting “1/2”.

(2) Section 42(g)(4) (relating to certain rules made applicable) is amended by striking “(other than section 142(d)(4)(B)(iii))”.

(o) INCREASED RESPONSIBILITIES FOR HOUSING CREDIT AGENCIES. —Section 42 is amended by redesignating subsections (m) and (n) as subsections (n) and (o), respectively, and by inserting after subsection (l) the following new subsection:

“(m) RESPONSIBILITIES OF HOUSING CREDIT AGENCIES. —

“(1) PLANS FOR ALLOCATION OF CREDIT AMONG PROJECTS. —

“(A) IN GENERAL. —Notwithstanding any other provision of this section, the housing credit dollar amount with respect to any building shall be zero unless —

“(i) such amount was allocated pursuant to a qualified allocation plan of the housing credit agency which is approved by the governmental unit (in accordance with rules similar to the rules of section 147(f)(2) (other than subparagraph (B)(ii) thereof)) of which such agency is a part, and

“(ii) such agency notifies the chief executive officer (or the equivalent) of the local jurisdiction within which the building is located of such project and provides such individual a reasonable opportunity to comment on the project.

“(B) QUALIFIED ALLOCATION PLAN. —For purposes of this paragraph, the term ‘qualified allocation plan’ means any plan —

“(i) which sets forth selection criteria to be used to determine housing priorities of the housing credit agency which are appropriate to local conditions.

“(ii) which gives the highest priority to those projects as to which the highest percentage of the housing credit dollar amount is to be used for project costs other than the cost of intermediaries unless granting such priority would impede the development of projects in hard to develop areas,

“(iii) which also gives preference in allocating housing credit dollar amounts among selected projects to —

“(I) projects serving the lowest income tenants, and

“(II) projects obligated to serve qualified tenants for the longest periods, and

“(iv) which provides a procedure that the agency will follow in notifying the Internal Revenue Service of noncompliance with the provisions of this section which such agency becomes aware of.

“(C) CERTAIN SELECTION CRITERIA MUST BE USED. —The selection criteria set forth in a qualified allocation plan must include —

“(i) project location,

“(ii) housing needs characteristics,

“(iii) project characteristics,

“(iv) sponsor characteristics,

“(v) participation of local tax-exempt organizations,

“(vi) tenant populations with special housing needs, and

“(vii) public housing waiting lists.

“(D) APPLICATION TO BOND FINANCED PROJECTS. —Subsection (h)(4) shall not apply to any project unless the project satisfies the requirements for allocation of a housing credit dollar amount under the qualified allocation plan applicable to the area in which the project is located.

“(2) CREDIT ALLOCATED TO BUILDING NOT TO EXCEED AMOUNT NECESSARY TO ASSURE PROJECT FEASIBILITY. —

“(A) IN GENERAL. —The housing credit dollar amount allocated to a project shall not exceed the amount the housing credit agency determines is necessary for the financial feasibility of the project and its viability as a qualified low-income housing project throughout the credit period.

“(B) AGENCY EVALUATION. —In making the determination under subparagraph (A), the housing credit agency shall consider —

“(i) the sources and uses of funds and the total financing planned for the project, and

“(ii) any proceeds or receipts expected to be generated by reason of tax benefits.

Such a determination shall not be construed to be a representation or warranty as to the feasibility or viability of the project.

“(C) DETERMINATION MADE WHEN CREDIT AMOUNT APPLIED FOR AND WHEN BUILDING PLACED IN SERVICE. —

“(i) IN GENERAL. —A determination under subparagraph (A) shall be made as of each of the following times:

“(I) The application for the housing credit dollar amount.

“(II) The allocation of the housing credit dollar amount.

“(III) The date the building is placed in service.

“(ii) CERTIFICATION AS TO AMOUNT OF OTHER SUBSIDIES. —Prior to each determination under clause (i), the taxpayer shall certify to the housing credit agency the full extent of all Federal, State, and local subsidies which apply (or which the taxpayer expects to apply) with respect to the building.

“(D) APPLICATION TO BOND FINANCED PROJECTS. —Subsection (h)(4) shall not apply to any project unless the governmental unit which issued the bonds (or on behalf of which the bonds were issued) makes a determination under rules similar to the rules of subparagraphs (A) and (B).”

(o) APPLICATION OF AT-RISK RULES WITH RESPECT TO CERTAIN FINANCING PROVIDED BY QUALIFIED NONPROFIT ORGANIZATIONS. —Subparagraph (D) of section 42(k)(2) (relating to application of at-risk rules) is amended by adding at the end thereof the following new flush sentence.

“In the case of a qualified nonprofit organization which is not described in section 46(c)(8)(D)(iv)(II) with respect to a building, clause (ii) of this subparagraph shall be applied as if the date described therein were the 90th day after the earlier of the date the building ceases to be a qualified low-income building or the date which is 15 years after the close of a compliance period with respect thereto.”

(p) TIME FOR CERTIFICATION. —Section 42(l)(1) (relating to certification with respect to 1st year of credit period) is amended —

(1) by striking “Not later than the 90th day following” and inserting “Following”, and

(2) by inserting “at such time and” before “in such form”.

(q) IMPACT OF TENANT'S RIGHT OF 1ST REFUSAL TO ACQUIRE PROPERTY. —Subsection (i) of section 42 is amended by adding at the end thereof the following new paragraph:

“(8) IMPACT OF TENANTS RIGHT OF 1ST REFUSAL TO ACQUIRE PROPERTY. —

“(A) IN GENERAL. —No Federal income tax benefit shall fail to be allowable to the taxpayer with respect to any qualified low-income building merely by reason of a right of 1st refusal held by the tenants of such building to purchase the property after the close of the compliance period for a price which is not less than the minimum purchase price determined under subparagraph (B).

“(B) MINIMUM PURCHASE PRICE. —For purposes of subparagraph (A), the minimum purchase price under this subparagraph is an amount equal to the sum of —

“(i) the principal amount of outstanding indebtedness secured by the building (other than indebtedness incurred within the 5-year period ending on the date of the sale to the tenants), and

“(ii) all Federal, State, and local taxes attributable to such sale.

Except in the case of Federal income taxes, there shall not be taken into account under clause (ii) any additional tax attributable to the application of clause (ii).”

(r) EFFECTIVE DATES. —

(1) IN GENERAL. —Except as otherwise provided in this subsection, the amendments made by this section shall apply to determinations under section 42 of the Internal Revenue Code of 1986 with respect to housing credit dollar amounts allocated from State housing credit ceilings for calendar years after 1989.

(2) BUILDINGS NOT SUBJECT TO ALLOCATION LIMITS. —Except as otherwise provided in this subsection, to the extent paragraph (1) of section 42(h) of such Code does not apply to any building by reason of paragraph (4) thereof, the amendments made by this section shall apply to buildings placed in service after December 31, 1989.

(3) ONE-YEAR CARRYOVER OF UNUSED CREDIT AUTHORITY, ETC. —The amendments made by subsection (b) shall apply to calendar years after 1989, but clauses (ii), (iii), and (iv) of section 42(h)(3)(C) of such Code (as added by this section) shall be applied without regard to allocations for 1989 or any preceding year.

(4) ADDITIONAL BUILDINGS ELIGIBLE FOR WAIVER OF 10-YEAR RULE. —The amendments made by subsection (f) shall take effect on the date of the enactment of this Act.

(5) CERTIFICATION WITH RESPECT TO 1ST YEAR OF CREDIT PERIOD. —The amendment made by subsection (p) shall apply to taxable years ending on or after December 31, 1989.

(6) CERTAIN RULES WHICH APPLY TO BONDS. —Paragraphs (1)(D) and (2)(D) of section 42(m) of such Code, as added by this section, shall apply to obligations issued December 31, 1989.

(7) CLARIFICATIONS. —The amendments made by the following provisions of this section shall apply as if included in the amendments made by section 252 of the Tax Reform Act of 1986:

(A) Paragraph (1) of subsection (h) (relating to units rented on a monthly basis).

(B) Subsection (1) (relating to eligible basis for new buildings to include expenditures before close of 1st year of credit period).

(8) GUIDANCE ON DIFFICULT DEVELOPMENT AREAS AND POSTING OF BOND TO AVOID RECAPTURE. —Not later than 180 days after the date of the enactment of this Act —

(A) the Secretary of Housing and Urban Development shall publish initial guidance on the designation of difficult development areas under section 42(d)(5)(C) of such Code, as added by this section, and

(B) the Secretary of the Treasury shall publish initial guidance under section 42(j)(6) of such Code (relating to no recapture on disposition of building (or interest therein) where bond posted).

SEC. 7109. LOW-INCOME HOUSING CREDIT EXEMPT FROM INCOME PHASE-OUT OF \$25,000 EXEMPTION FROM PASSIVE LOSS RULES.

(a) IN GENERAL. —Paragraph (3) of section 469(i) (relating to phaseout of exemption) is amended by redesignating subparagraph (D) as subparagraph (E) and by striking subparagraphs (B) and (C) and inserting the following new subparagraphs:

“(B) SPECIAL PHASE-OUT REHABILITATION CREDIT. —In the case of any portion of the passive activity credit for any taxable year which is attributable to the rehabilitation investment credit (within the meaning of section 48(o)), subparagraph (A) shall be applied by substituting ‘\$200,000’ for ‘\$100,000’.

“(C) EXCEPTION FOR LOW-INCOME HOUSING CREDIT. —Subparagraph (A) shall not apply to any portion of the passive activity credit for any taxable year which is attributable to any credit determined under section 42.

“(D) ORDERING RULES TO REFLECT EXCEPTION AND SEPARATE PHASE-OUT. —If subparagraph (B) or (C) applies for any taxable year, paragraph (1) shall be applied —

“(i) first to the passive activity loss,

“(ii) second to the portion of the passive activity credit to which subparagraph (B) or (C) does not apply,

“(iii) third to the portion of such credit to which subparagraph (B) applies, and

“(iv) then to the portion of such credit to which subparagraph (C) applies.”

(b) EFFECTIVE DATE. —

(1) IN GENERAL. —Except as provided in paragraph (2), the amendments made by this section shall apply to property placed in service after December 31, 1989, in taxable years ending after such date.

(2) SPECIAL RULE WHERE INTEREST HELD IN PASS-THRU ENTITY. —In the case of a taxpayer who holds an indirect interest in property described in paragraph (1), the amendments made by this section shall apply only if such interest is acquired after December 31, 1989.

SEC. 7110. EXTENSION AND MODIFICATION OF RESEARCH CREDIT.

(a) EXTENSION. —

(1) IN GENERAL. —Subsection (h) of section 41 (relating to termination), as redesignated by subtitle H, is amended —

(A) by striking “December 31, 1989” each place it appears and inserting “December 31, 1990”, and

(B) by striking “January 1, 1990” each place it appears and inserting “January 1, 1991”.

(2) SPECIAL RULES. —

(A) In the case of any taxable year which begins before October 1, 1990, and ends after September 30, 1990, the amount treated as the qualified research expenses for such taxable year for purposes of section 41 of the Internal Revenue Code of 1986 shall be the amount which bears the same ratio to the amount which would have been determined for such taxable year without regard to this subparagraph as the number of days in such taxable year before October 1, 1990, bears to the total number of days in such taxable year before January 1, 1991.

(B) In the case of a taxable year described in subparagraph (A), paragraph (2) of section 41(h) of such Code, as so redesignated, shall be applied by substituting “October 1, 1990” for “January 1, 1991” each place it appears and by substituting “September 30, 1990” for “December 31, 1990”.

(3) CONFORMING AMENDMENT. —Subparagraph (D) of section 28(b)(1) is amended by striking “December 31, 1989” and inserting “December 31, 1990”.

(b) CHANGES IN COMPUTATION OF INCREMENTAL CREDIT. —

(1) IN GENERAL. —Subsection (c) of section 41 is amended to read as follows:

“(c) BASE AMOUNT —

“(1) IN GENERAL. —The term ‘base amount’ means the product of —

“(A) the fixed-base percentage, and

“(B) the average annual gross receipts of the taxpayer for the 4 taxable years preceding the taxable year for which the credit is being determined (hereinafter in this subsection referred to as the ‘credit year’).

“(2) MINIMUM BASE AMOUNT. —In no event shall the base amount be less than 50 percent of the qualified research expenses for the credit year.

“(3) FIXED-BASE PERCENTAGE. —

“(A) IN GENERAL. —Except as otherwise provided in this paragraph, the fixed-base percentage is the percentage which the aggregate qualified research expenses of the taxpayer for taxable years beginning after December 31, 1983, and before January 1, 1989, is of the aggregate gross receipts of the taxpayer for such taxable years.

“(B) START-UP COMPANIES. —

“(i) TAXPAYERS TO WHICH SUBPARAGRAPH APPLIES. —The fixed-base percentage shall be determined under this subparagraph if there are fewer than 3 taxable years beginning after December 31, 1983, and before January 1, 1989, in which the taxpayer had both gross receipts and qualified research expenses.

“(ii) FIXED-BASE PERCENTAGE —In a case to which this subparagraph applies, the fixed-base percentage is 3 percent.

“(iii) TREATMENT OF DE MINIMIS AMOUNTS OF GROSS RECEIPTS AND QUALIFIED RESEARCH EXPENSES. —The Secretary may prescribe regulations providing that de minimis amounts of gross receipts and qualified research expenses shall be disregarded under clause (i).

“(C) MAXIMUM FIXED-BASE PERCENTAGE. —In no event shall the fixed-base percentage exceed 16 percent.

“(D) ROUNDING —The percentages determined under subparagraph (A) shall be rounded to the nearest 1/100th of 1 percent.

“(4) CONSISTENT TREATMENT OF EXPENSES REQUIRED. —

“(A) IN GENERAL. —Notwithstanding whether the period for filing a claim for credit or refund has expired for any taxable year taken into account in determining the fixed-base percentage, the qualified research expenses taken into account in computing such percentage shall be determined on a basis consistent with the determination of qualified research expenses for the credit year.

“(B) PREVENTION OF DISTORTIONS. —The Secretary may prescribe regulations to prevent distortions in calculating a taxpayer's qualified research expenses or gross receipts caused by a change in accounting methods used by such taxpayer between the current year and a year taken into account in computing such taxpayer's fixed-base percentage.

“(5) GROSS RECEIPTS. —For purposes of this subsection, gross receipts for any taxable year shall be reduced by returns and allowances made during the taxable year. In the case of a foreign corporation, there shall be taken into account only gross receipts which are effectively connected with the conduct of a trade or business within the United States.”

(2) CONFORMING AMENDMENTS. —

(A) Subparagraph (B) of section 41(a)(1) is amended to read as follows:

“(B) the base amount, and”.

(B) Clause (ii) of section 41(e)(7)(C) is amended by striking “base period research expenses” and inserting “base amount”.

(C) Paragraph (1) of section 41(f) (relating to aggregation of expenditures) is amended by striking “proportionate share of the increase in qualified research expenses” each place it appears and inserting “proportionate shares of the qualified research expenses and basic research payments”.

(D) Subparagraph (A) of section 41(f)(3) is amended —

(i) by striking “June 30, 1980” and inserting “December 31, 1983”, and

(ii) by inserting before the period “, and the gross receipts of the taxpayer for such periods shall be increased by so much of the gross receipts of such predecessor with respect to the acquired trade or business as is attributable to such portion”.

(E) Subparagraph (B) of section 41(f)(3) is amended —

(i) by striking “June 30, 1980” and inserting “December 31, 1983”, and

(ii) by inserting before the period “, and the gross receipts of the taxpayer for such periods shall be decreased by so much of the gross receipts as is attributable to such portion”.

(F)(i) Subparagraph (C) of section 41(f)(3) is amended by striking “for the base period” and all that follows and inserting “for the taxable years taken into account in computing the fixed-base percentage shall be increased by the lesser of —

“(i) the amount of the decrease under subparagraph (B) which is allocable to taxable years so taken into account, or

“(ii) the product of the number of taxable years so taken into account, multiplied by the amount of the reimbursement described in this subparagraph.”

(ii) The heading for such subparagraph (C) is amended to read as follows:

“(C) CERTAIN REIMBURSEMENTS TAKEN INTO ACCOUNT IN DETERMINING FIXED-BASE PERCENTAGE. —”.

(G) Paragraph (4) of section 41(f) is amended by inserting “and gross receipts” after “qualified research expenses”.

(H) Paragraph (2) of section 41(h), as redesignated by subtitle H, is amended —

(i) by striking “BASE PERIOD EXPENSES” in the heading and inserting “BASE AMOUNT”, and

(ii) by striking “any amount for any base period” and all that follows through “such base period” and inserting “the base amount with respect to such taxable year shall be the amount which bears the same ratio to the base amount for such year (determined without regard to this paragraph)”.

(b) TRADE OR BUSINESS REQUIREMENT DISREGARD FOR IN-HOUSE RESEARCH EXPENSES OF CERTAIN STARTUP VENTURES. —Subsection (b) of section 41 (defining qualified research expenses) is amended by adding at the end thereof the following new paragraph:

“(4) TRADE OR BUSINESS REQUIREMENT DISREGARDED FOR IN-HOUSE RESEARCH EXPENSES OF CERTAIN STARTUP VENTURES. —In the case of in-house research expenses, a taxpayer shall be treated as meeting the trade or business requirement of paragraph (1) if, at the time such in-house research expenses are paid or incurred, the principal purpose of the taxpayer in making such expenditures is to use the results of the research in the active conduct of a future trade or business —

“(A) of the taxpayer, or

“(B) of 1 or more other persons who with the taxpayer are treated as a single taxpayer under subsection (f)(1).”

(c) FULL DISALLOWANCE OF DEDUCTION FOR QUALIFIED RESEARCH EXPENSES. —

(1) Subsection (c) of section 280C, as amended by subtitle H, is further amended by striking “50 percent of” each place it appears.

(2) Paragraph (2) of section 196(d) is amended by inserting before the period “for a taxable year beginning before January 1, 1990”.

(d) **ONLY REASONABLE RESEARCH EXPENDITURES ELIGIBLE FOR SECTION 174.** —Section 174 is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

“(e) **ONLY REASONABLE RESEARCH EXPENDITURES ELIGIBLE.** —This section shall apply to a research or experimental expenditure only to the extent that the amount thereof is reasonable under the circumstances.”

(e) **EFFECTIVE DATE.** —The amendments made by this section (other than subsection (a)) shall apply to taxable years beginning after December 31, 1989.

SEC. 7111. ALLOCATION OF RESEARCH AND EXPERIMENTAL EXPENDITURES.

Section 864 (relating to definitions and special rule) is amended by adding at the end thereof the following new subsection:

“(f) **ALLOCATION OF RESEARCH AND EXPERIMENTAL EXPENDITURES.** —

“(1) **IN GENERAL.** —For purposes of section 861(b), 862(b), and 863(b), qualified research and experimental expenditures shall be allocated and apportioned as follows:

“(A) Any qualified research and experimental expenditures expended solely to meet legal requirements imposed by a political entity with respect to the improvement or marketing of specific products or processes for purposes not reasonably expected to generate gross income (beyond de minimis amounts) outside the jurisdiction of the political entity shall be allocated only to gross income from sources within such jurisdiction.

“(B) In the case of any qualified research and experimental expenditures (not allocated under subparagraph (A)) to the extent —

“(i) that such expenditures are attributable to activities conducted in the United States, 64 percent of such expenditures shall be allocated and apportioned to income from sources within the United States and deducted from such income in determining the amount of taxable income from sources within the United States, and

“(ii) that such expenditures are attributable to activities conducted outside the United States, 64 percent of such expenditures shall be allocated and apportioned to income from sources outside the United States and deducted from such income in determining the amount of taxable income from sources outside the United States.

“(C) The remaining portion of qualified research and experimental expenditures (not allocated under subparagraphs (A) and (B)) shall be apportioned, at the annual election of the taxpayer, on the basis of gross sales or gross income, except that, if the taxpayer elects to apportion on the basis of gross income, the amount apportioned to income from sources outside the United States shall at least be 30 percent of the amount which would be so apportioned on the basis of gross sales.

“(2) **QUALIFIED RESEARCH AND EXPERIMENTAL EXPENDITURES.** —For purposes of this

section, the term `qualified research and experimental expenditures' means amounts which are research and experimental expenditures within the meaning of section 174. For purposes of this paragraph, rules similar to the rules of subsection (c) of section 174 shall apply. Any qualified research and experimental expenditures treated as deferred expenses under subsection (b) of section 174 shall be taken into account under this subsection for the taxable year for which such expenditures are allowed as a deduction under such subsection.

“(3) SPECIAL RULES FOR EXPENDITURES ATTRIBUTABLE TO ACTIVITIES CONDUCTED IN SPACE, ETC. —

“(A) IN GENERAL. —Any qualified research and experimental expenditures described in subparagraph (B) —

“(i) if incurred by a United States person, shall be allocated and apportioned under this section in the same manner as if they were attributable to activities conducted in the United States, and

“(ii) if incurred by a person other than a United States person, shall be allocated and apportioned under this section in the same manner as if they were attributable to activities conducted outside the United States.

“(B) DESCRIPTION OF EXPENDITURES. —For purposes of subparagraph (A), qualified research and experimental expenditures are described in this subparagraph if such expenditures are attributable to activities conducted —

“(i) in space,

“(ii) on or under water not within the jurisdiction (as recognized by the United States) of a foreign country, possession of the United States, or the United States, or

“(iii) in Antarctica.

“(4) AFFILIATED GROUP. —

“(A) Except as provided in subparagraph (B), the allocation and apportionment required by paragraph (1) shall be determined as if all members of the affiliated group (as defined in subsection (e)(5)) were a single corporation.

“(B) For purposes of the allocation and apportionment required by paragraph (1) —

“(i) sales and gross income from products produced in whole or in part in a possession by an electing corporation (within the meaning of section 936(h)(5)(E)), and

“(ii) dividends from an electing corporation, shall not be taken into account, except that this subparagraph shall not apply to sales of (and gross income and dividends attributable to sales of) products with respect to which an election under section 936(h)(5)(F) is not in effect.

“(C) The qualified research and experimental expenditures taken into account for purposes of paragraph (1) shall be adjusted to reflect the amount of such expenditures included in computing the cost-sharing amount (determined under section 936(h)(5)(C)(i)(I).

“(D) The Secretary may prescribe such regulations as may be necessary to carry out the purposes of this paragraph, including regulations providing for the source of gross income and the allocation and apportionment of deductions to take into account the adjustments required by subparagraph (C).

“(E) Paragraph (6) of subsection (e) shall not apply to qualified research and experimental expenditures.

“(5) YEAR TO WHICH RULE APPLIES. —

“(A) IN GENERAL. —Except as provided in this paragraph, this subsection shall apply to the taxpayer's first taxable year beginning after August 1, 1989, and before August 2, 1990.

“(B) REDUCTION. —Notwithstanding subparagraph (A) this subsection shall only apply to that portion of the qualified research and experimental expenditures for the taxable year referred to in subparagraph (A) which bears the same ratio to the total amount of such expenditures as —

“(i) the lesser of 9 months or the number of months in the taxable year, bears to

“(ii) the number of months in the taxable year.”

Subtitle B —Corporate Provisions

SEC. 7201. LIMITATION ON USE OF GROUP LOSSES TO OFFSET INCOME OF SUBSIDIARY PAYING PREFERRED DIVIDENDS.

(a) GENERAL RULE. —Section 1503 (relating to computation and payment of tax) is amended by adding at the end thereof the following new subsection:

“(f) LIMITATION ON USE OF GROUP LOSSES TO OFFSET INCOME OF SUBSIDIARY PAYING PREFERRED DIVIDENDS. —

“(1) IN GENERAL. —In the case of any subsidiary distributing during any taxable year dividends on any applicable preferred stock —

“(A) no group loss item shall be allowed to reduce the disqualified separately computed income of such subsidiary for such taxable year, and

“(B) no group credit item shall be allowed against the tax imposed by this chapter on such disqualified separately computed income.

“(2) GROUP ITEMS. —For purposes of this subsection —

“(A) GROUP LOSS ITEM. —The term ‘group loss item’ means any of the following items of any other member of the affiliated group which includes the subsidiary:

“(i) Any net operating loss and any net operating loss carryover or carryback under section 172.

“(ii) Any loss from the sale or exchange of any capital asset and any capital loss carryover or carryback under section 1212.

“(B) GROUP CREDIT ITEM. —The term ‘group credit item’ means any credit allowable under part IV of subchapter A of chapter 1 (other than section 34) to any other member of the affiliated group which includes the subsidiary and any carryover or carryback of any such credit.

“(3) OTHER DEFINITIONS. —For purposes of this subsection —

“(A) DISQUALIFIED SEPARATELY COMPUTED INCOME. —The term ‘disqualified separately computed income’ means the portion of the separately computed taxable income of the subsidiary which does not exceed the dividends distributed by the subsidiary during the taxable year on applicable preferred stock.

“(B) SEPARATELY COMPUTED TAXABLE INCOME. —The term ‘separately computed taxable income’ means the separate taxable income of the subsidiary for the taxable year determined —

“(i) by taking into account gains and losses from the sale or exchange of a capital asset and section 1231 gains and losses,

“(ii) without regard to any net operating loss or capital loss carryover or carryback, and

“(iii) with such adjustments as the Secretary may prescribe.

“(C) SUBSIDIARY. —The term ‘subsidiary’ means any corporation which is a member of an affiliated group filing a consolidated return other than the common parent.

“(D) APPLICABLE PREFERRED STOCK. —The term ‘applicable preferred stock’ means stock described in section 1504(a)(4) in the subsidiary which is —

“(i) issued after November 17, 1989, and

“(ii) held by a person other than a member of the same affiliated group as the subsidiary.

“(4) REGULATIONS. —The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the provisions of this subsection, including regulations —

“(A) to prevent the avoidance of this subsection through the transfer of built-in losses to the subsidiary.

“(B) to provide rules for cases in which the subsidiary owns (directly or indirectly) stock in another member of the affiliated group, and

“(C) to provide for the application of this subsection where dividends are not paid currently, where the redemption and liquidation rights of the applicable preferred stock exceed the issue price for such stock, or where the stock is otherwise structured to avoid the purposes of this subsection.”

(b) EFFECTIVE DATES. —

(1) IN GENERAL. —The amendment made by this section shall apply to taxable years ending after November 17, 1989.

(2) BINDING CONTRACT EXCEPTION. —For purposes of section 1503(f)(3)(D) of the Internal Revenue Code of 1986, stock issued after November 17, 1989, pursuant to a written binding contract in effect on November 17, 1989, and at all times thereafter before such issuance, shall be treated as issued on November 17, 1989.

(3) SPECIAL RULE WHEN SUBSIDIARY LEAVES GROUP. —If, by reason of a transaction after November 17, 1989, a corporation ceases to be, or becomes, a member of an affiliated group, the stock of

such corporation shall be treated, for purposes of section 1503(f)(3)(D) of such Code, as issued on the date of such cessation or commencement, unless such transaction is of a kind which would not result in the recognition of any deferred intercompany gain under the consolidated return regulations by reason of the acquisition of the entire group.

(4) RETIRED STOCK. —

(A) Except as provided in subparagraph (B), if stock issued before November 18, 1989, (or described in paragraph (2)), is retired or acquired after November 17, 1989, by the corporation or another member of the same affiliated group, such stock shall be treated, for purposes of section 1503(f)(3)(D) of such Code, as issued on the date of such retirement or acquisition.

(B) Subparagraph (A) shall not apply to any retirement or acquisition pursuant to an obligation to reissue under a binding written contract in effect on November 17, 1989, and at all times thereafter before such retirement or acquisition.

(5) AUCTION RATE PREFERRED. —For purposes of section 1503(f)(3)(D) of such Code, auction rate preferred stock shall be treated as issued when the contract requiring the auction became binding.

(6) SPECIAL RULE FOR CERTAIN AUCTION RATE PREFERRED. —For purposes of section 1503(F)(3)(D) of the Internal Revenue Code of 1986, any auction rate preferred stock shall be treated as issued before November 18, 1989, if —

(A) a subsidiary was incorporated before July 10, 1989, for the special purpose of issuing such stock.

(B) a rating agency was retained before July 10, 1989, and

(C) such stock is issued before the date 30 days after the date of the enactment of this Act.

SEC. 7202. TREATMENT OF CERTAIN HIGH YIELD ORIGINAL ISSUE DISCOUNT OBLIGATIONS.

(a) GENERAL RULE. —Subsection (e) of section 163 (relating to interest deductions on original issue discount obligations) is amended by redesignating paragraph (5) as paragraph (6) and by inserting after paragraph (4) the following new paragraph:

“(5) SPECIAL RULES FOR ORIGINAL ISSUE DISCOUNT ON CERTAIN HIGH YIELD OBLIGATIONS —

“(A) IN GENERAL. —In the case of an applicable high yield discount obligation issued by a corporation

—

“(i) no deduction shall be allowed under this chapter for the disqualified portion of the original issue discount on such obligation, and

“(ii) the remainder of such original issue discount shall not be allowable as a deduction until paid.

For purposes of clause (ii), rules similar to the rules of subsection (i)(3)(B) shall apply in determining the time when the original issue discount is paid.

“(B) DISQUALIFIED PORTION TREATED AS STOCK DISTRIBUTION FOR PURPOSES OF DIVIDEND RECEIVED DEDUCTION. —

“(i) IN GENERAL. —Solely for purposes of sections 243, 245, 246, and 246A, the dividend equivalent portion of any amount includible in gross income of a corporation under section 1272(a) in respect of an applicable high yield discount obligation shall be treated as a dividend received by such corporation from the corporation issuing such obligation.

“(ii) DIVIDEND EQUIVALENT PORTION. —For purposes of clause (i), the dividend equivalent portion of any amount includible in gross income under section 1272(a) in respect of an applicable high yield discount obligation is the portion of the amount so includible —

“(I) which is attributable to the disqualified portion of the original issue discount on such obligation, and

“(II) which would have been treated as a dividend if it had been a distribution made by the issuing corporation with respect to stock in such corporation.

“(C) DISQUALIFIED PORTION. —

“(i) IN GENERAL. —For purposes of this paragraph, the disqualified portion of the original issue discount on any applicable high yield discount obligation is the lesser of —

“(I) the amount of such original issue discount, or

“(II) the portion of the total return on such obligation which bears the same ratio to such total return as the disqualified yield on such obligation bears to the yield to maturity on such obligation.

“(ii) DEFINITIONS. —For purposes of clause (i), the term ‘disqualified yield’ means the excess of the yield to maturity on the obligation over the sum referred to subsection (i)(1)(B), plus 1 percentage point, and the term ‘total return’ is the amount which would have been the original issue discount on the obligation if interest described in the parenthetical in section 1273(a)(2) were included in the stated redemption price at maturity.

“(D) EXCEPTION FOR S CORPORATIONS. —This paragraph shall not apply to any obligation issued by any corporation for any period for which such corporation is an S corporation.

“(E) EFFECT ON EARNINGS AND PROFITS. —This paragraph shall not apply for purposes of determining earnings and profits; except that, for purposes of determining the dividend equivalent portion of any amount includible in gross income under section 1272(a) in respect of an applicable high yield discount obligation, no reduction shall be made for any amount attributable to the disqualified portion of any original issue discount on such obligation.

“(F) CROSS REFERENCE. —

“For definition of applicable high yield discount obligation, see subsection (i).”

(b) APPLICABLE HIGH YIELD DISCOUNT OBLIGATION. —Section 163 is amended by redesignating subsection (i) as subsection (j) and by inserting after subsection (h) the following new subsection:

“(i) APPLICABLE HIGH YIELD DISCOUNT OBLIGATION. —

“(1) IN GENERAL. —For purposes of this section, the term ‘applicable high yield discount obligation’ means any debt instrument if —

“(A) the maturity date of such instrument is more than 5 years from the date of issue,

“(B) the yield to maturity on such instrument equals or exceeds the sum of —

“(i) the applicable Federal rate in effect under section 1274(d) for the calendar month in which the obligation is issued, plus

“(ii) 5 percentage points, and

“(C) such instrument has significant original issue discount.

For purposes of subparagraph (B)(i), the Secretary may by regulation permit a rate to be used with respect to any debt instrument which is higher than the applicable Federal rate if the taxpayer establishes to the satisfaction of the Secretary that such higher rate is based on the same principles as the applicable Federal rate and is appropriate for the term of the instrument.

“(2) SIGNIFICANT ORIGINAL ISSUE DISCOUNT. —For purposes of paragraph (1)(C), a debt instrument shall be treated as having significant original issue discount if —

“(A) the aggregate amount which would be includible in gross income with respect to such instrument for periods before the close of any accrual period (as defined in section 1272(a)(5)) ending after the date 5 years after the date of issue, exceeds —

“(B) the sum of —

“(i) the aggregate amount of interest to be paid under the instrument before the close of such accrual period, and

“(ii) the product of the issue price of such instrument (as defined in sections 1273(b) and 1274(a)) and its yield to maturity.

“(3) SPECIAL RULES. —For purposes of determining whether a debt instrument is an applicable high yield discount obligation —

“(A) any payment under the instrument shall be assumed to be made on the last day permitted under the instrument, and

“(B) any payment to be made in the form of another obligation (or stock) of the issuer (or a related person within the meaning of section 453(f)(1)) shall be assumed to be made when such obligation (or stock) is required to be paid in cash or in property other than such obligation (or stock).

“(4) DEBT INSTRUMENT. —For purposes of this subsection, the term ‘debt instrument’ means any instrument which is a debt instrument as defined in section 1275(a).

“(5) REGULATIONS. —The Secretary shall prescribe such regulations as may be appropriate to carry out the purposes of this subsection and subsection (e)(5), including —

“(A) regulations providing for modifications to the provisions of this subsection and subsection (e)(5) in the case of varying rates of interest, put or call options, indefinite maturities, contingent payments, assumptions of debt instruments, conversion rights, or other circumstances where such modifications are appropriate to carry out the purposes of this subsection and subsection (e)(5), and

“(B) regulations to prevent avoidance of the purposes of this subsection and subsection (e)(5) through the use of issuers other than C corporations, agreements to borrow amounts due under the debt instrument, or other arrangements.”

(c)EFFECTIVE DATE. —

(1) IN GENERAL. —Except as provided in paragraph (2), the amendments made by this section shall apply to instruments issued after July 10, 1989.

(2)EXCEPTIONS. —

(A) The amendments made by this section shall not apply to any instrument if —

(i) such instrument is issued in connection with an acquisition —

(I) which is made on or before July 10, 1989,

(II) for which there was a written binding contract in effect on July 10, 1989, and at all times thereafter before such acquisitions, or

(III) for which a tender offer was filed with the Securities and Exchange Commission on or before July 10, 1989.

(ii) the term of such instrument is not greater than —

(I) the term specified in the written documents described in clause (iii), or

(II) if no term is determined under subclause (I), 10 years, and

(iii) the use of such instrument in connection with such acquisition (and the maximum amount of proceeds from such instrument) was determined on or before July 10, 1989, and such determination is evidenced by written documents —

(I) which were transmitted on or before July 10, 1989, between the issuer and any governmental regulatory bodies or prospective parties to the issuance or acquisition, and

(II) which are customarily used for the type of acquisition or financing involved.

(B) The amendments made by this section shall not apply to any instrument issued pursuant to the terms of a debt instrument issued on or before July 10, 1989, or described in subparagraph (A) or (D).

(C) The amendments made by this section shall not apply to any instrument issued to refinance an original issue discount debt instrument to which the amendments made by this section do not apply if —

(i) the maturity date of the refinancing instrument is not later than the maturity date of the refinanced instrument,

(ii) the issue price of the refinancing instrument does not exceed the adjusted issue price of the refinanced instrument,

(iii) the stated redemption price at maturity of the refinancing instrument is not greater than the stated

redemption price at maturity of the refinanced instrument, and

(iv) the interest payments required under the refinancing instrument before maturity are not less than (and are paid not later than) the interest payments required under the refinanced instrument.

(D) The amendments made by this section shall not apply to instruments issued after July 10, 1989, pursuant to a reorganization plan in a title 11 or similar case (as defined in section 368(a)(3) of the Internal Revenue Code of 1986) if the amount of proceeds of such instruments, and the maturities of such instruments, do not exceed the amount or maturities specified in the last reorganization plan filed in such case on or before July 10, 1989.

SEC. 7203. SECURITIES TREATED AS BOOT UNDER SECTION 351.

(a) GENERAL RULE. —Section 351(a) (relating to nonrecognition in cases of transfer to corporations controlled by transferor) is amended by striking “or securities”.

(b) CONFORMING AMENDMENTS. —

(1) Subsections (b), (d), and (e)(2) of section 351 are each amended by striking “or securities”.

(2) Paragraph (2) of section 351(g) is amended by striking “stock, securities, or property” and inserting “stock or property”.

(c) EFFECTIVE DATE. —

(1) IN GENERAL. —Except as provided in this subsection, the amendments made by this section shall apply to transfers after October 2, 1989, in taxable years ending after such date.

(2) BINDING CONTRACT. —The amendments made by this section shall not apply to any transfer pursuant to a written binding contract in effect on October 2, 1989, and at all times thereafter before such transfer.

(3) CORPORATE TRANSFERS. —In the case of property transferred (directly or indirectly through a partnership or otherwise) by a C corporation, paragraphs (1) and (2) shall be applied by substituting “July 11, 1989” for “October 2, 1989”. The preceding sentence shall not apply where the corporation meets the requirements of section 1504(a)(2) of the Internal Revenue Code of 1986 with respect to the transferee corporation (and where the transfer is not part of a plan pursuant to which the transferor subsequently fails to meet such requirements).

SEC. 7204. PROVISIONS RELATED TO REGULATED INVESTMENT COMPANIES.

(a) REQUIREMENT TO DISTRIBUTE 98 PERCENT OF ORDINARY INCOME. —

(1) IN GENERAL. —Subparagraph (A) of section 4982(b)(1) (defining required distribution) is amended by striking “97 percent” and inserting “98 percent”.

(2) EFFECTIVE DATE. —The amendment made by paragraph (1) shall apply to calendar years ending after July 10, 1989.

(b) TREATMENT OF CERTAIN MUTUAL FUND LOAD CHARGES. —

(1) IN GENERAL. —Section 852 (relating to taxation of regulated investment companies and their shareholders) is amended by adding at the end thereof the following new subsection:

“(f) TREATMENT OF CERTAIN LOAD CHARGES. —

“(1) IN GENERAL. —If —

“(A) the taxpayer incurs a load charge in acquiring stock in a regulated investment company and, by reason of incurring such charge or making such acquisition, the taxpayer acquires a reinvestment right,

“(B) such stock is disposed of before the 91st day after the date on which such stock was acquired, and

“(C) the taxpayer subsequently acquires stock in such regulated investment company or in another regulated investment company and the otherwise applicable load charge is reduced by reason of the reinvestment right,

the load charge referred to in subparagraph (A) (to the extent it does not exceed the reduction referred to in subparagraph (C)) shall not be taken into account for purposes of determining the amount of gain or loss on the disposition referred to in subparagraph (B). To the extent such charge is not taken into account in determining the amount of such gain or loss, such charge shall be treated as incurred in connection with the acquisition referred to in subparagraph (C) (including for purposes of reapplying this paragraph).

“(2) DEFINITIONS AND SPECIAL RULES. —For purposes of this subsection —

“(A) LOAD CHARGE. —The term ‘load charge’ means any sales or similar charge incurred by a person in acquiring stock of a regulated investment company. Such term does not include any charge incurred by reason of the reinvestment of a dividend.

“(B) REINVESTMENT RIGHT. —The term ‘reinvestment right’ means any right to acquire stock of 1 or more regulated investment companies without the payment of a load charge or with the payment of a reduced charge.

“(C) NONRECOGNITION TRANSACTIONS. —If the taxpayer acquires stock in a regulated investment company from another person in a transaction in which gain or loss is not recognized, the taxpayer shall succeed to the treatment of such other person under this subsection.”

(2) EFFECTIVE DATE. —The amendment made by paragraph (1) shall apply to charges incurred after October 3, 1989, in taxable years ending after such date.

(c) REGULATED INVESTMENT COMPANIES REQUIRED TO ACCRUE DIVIDENDS ON THE EX-DIVIDEND DATE. —

(1) IN GENERAL. —Subsection (b) of section 852 (relating to treatment of companies and shareholders) is amended by adding at the end thereof the following new paragraph:

“(9) DIVIDENDS TREATED AS RECEIVED BY COMPANY ON EX-DIVIDEND DATE. —For purposes of this title, if a regulated investment company is the holder of record of any share of stock on the record date for any dividend payable with respect to such stock, such dividend shall be included in gross income by such company as of the later of —

“(A) the date such share became ex-dividend with respect to such dividend, or

“(B) the date such company acquired such share.”

(2) EFFECTIVE DATE. —The amendment made by paragraph (1) shall apply to dividends in cases where the stock becomes ex-dividend after the date of the enactment of this Act.

SEC. 7205. LIMITATION ON THRESHOLD REQUIREMENT UNDER SECTION 382 BUILT-IN GAIN AND LOSS PROVISIONS.

(a) GENERAL RULE. —Clause (i) of section 382(h)(3)(B) (relating to threshold requirement) is amended to read as follows:

“(i) IN GENERAL. —If the amount of the net unrealized built-in gain or net unrealized built-in loss (determined without regard to this subparagraph) of any old loss corporation is not greater than the lesser of —

“(I) 15 percent of the amount determined for purposes of subparagraph (A)(i)(I), or

“(II) \$10,000,000,

the net unrealized built-in gain or net unrealized built-in loss shall be zero.”

(b) CONFORMING AMENDMENT TO ADJUSTED CURRENT EARNINGS PREFERENCE. — Subparagraph (H) of section 56(g)(4) (relating to treatment of certain ownership changes) is amended by striking clause (ii) and all that follows and inserting the following:

“(ii) there is a net unrealized built-in loss (within the meaning of section 382(h)) with respect to such corporation,

then the adjusted basis of each asset of such corporation (immediately after the ownership change) shall be its proportionate share (determined on the basis of respective fair market values) of the fair market value of the assets of such corporation (determined under section 382(h)) immediately before the ownership change.”

(c) EFFECTIVE DATE. —

(1) IN GENERAL. —Except as otherwise provided in this subsection, the amendments made by this section shall apply to ownership changes and acquisitions after October 2, 1989, in taxable years ending after such date.

(2) BINDING CONTRACT. —The amendments made by this section shall not apply to any ownership change or acquisition pursuant to a written binding contract in effect on October 2, 1989, and at times thereafter before such change or acquisition.

(3) BANKRUPTCY PROCEEDINGS. —In the case of a reorganization described in section 368(a)(1)(G) of the Internal Revenue Code of 1986, or an exchange of debt for stock in a title 11 or similar case (as defined in section 368(a)(3) of such Code), the amendments made by this section shall not apply to any ownership change resulting from such a reorganization or proceeding if a petition in such case was filed

with the court before October 3, 1989.

(4) **SUBSIDIARIES OF BANKRUPT PARENT.** —The amendments made by this section shall not apply to any built-in loss of a corporation which is a member (on October 2, 1989) of an affiliated group the common parent of which (on such date) was subject to title 11 or similar case (as defined in section 368(a)(3) of such Code). The preceding sentence shall apply only if the ownership change or acquisition is pursuant to the plan approved in such proceeding and is before the date 2 years after the date on which the petition which commenced such proceeding was filed.

SEC. 7206. DISTRIBUTIONS ON CERTAIN PREFERRED STOCK TREATED AS EXTRAORDINARY DIVIDENDS.

(a) **GENERAL RULE.** —Section 1059 (relating to corporate shareholder's basis in stock reduced by nontaxed portion of extraordinary dividends) is amended by striking subsection (f) and inserting the following:

“(f) **TREATMENT OF DIVIDENDS ON CERTAIN PREFERRED STOCK.** —

“(1) **IN GENERAL.** —Any dividend with respect to disqualified preferred stock shall be treated as an extraordinary dividend to which paragraphs (1) and (2) of subsection (a) apply without regard to the period the taxpayer held the stock.

“(2) **DISQUALIFIED PREFERRED STOCK.** —For purposes of this subsection, the term ‘disqualified preferred stock’ means any stock which is preferred as to dividends if —

“(A) when issued, such stock has a dividend rate which declines (or can reasonably be expected to decline) in the future,

“(B) the issue price of such stock exceeds its liquidation rights or its stated redemption price, or

“(C) such stock is otherwise structured —

“(i) to avoid the other provisions of this section, and

“(ii) to enable corporate shareholders to reduce tax through a combination of dividend received deductions and loss on the disposition of the stock.

“(g) **REGULATIONS.** —The Secretary shall prescribe such regulations as may be appropriate to carry out the purposes of this section, including regulations —

“(1) providing for the application of this section in the case of stock dividends, stock splits, reorganizations, and other similar transactions and in the case of stock held by pass-thru entities, and

“(2) providing that the rules of subsection (f) shall apply in the case of stock which is not preferred as to dividends in cases where stock is structured to avoid the purposes of this section.”

(b) **EFFECTIVE DATE.** —

(1) **IN GENERAL.** —Except as provided in paragraph (2), the amendment made by subsection (a) shall apply to stock issued after July 10, 1989, in taxable years ending after such date.

(2) **BINDING CONTRACT.** —The amendment made by subsection (a) shall not apply to any stock issued pursuant to a written binding contract in effect on July 10, 1989, and at all times thereafter before the stock is issued.

SEC 7207. REPEAL OF ELECTION TO REDUCE EXCESS LOSS ACCOUNT RECAPTURE BY REDUCING BASIS OF INDEBTEDNESS.

(a) **GENERAL RULE.** —Subsection (e) of section 1503 (relating to special rule for determining adjustment to basis) is amended by adding at the end thereof the following new paragraph:

“(4) **ELIMINATION OF ELECTION TO REDUCE BASIS OF INDEBTEDNESS.** —Nothing in the regulations prescribed under section 1502 shall permit any reduction in the amount otherwise included in gross income by reason of an excess loss account if such reduction is on account of a reduction in the basis of indebtedness.”

(b) **EFFECTIVE DATE.** —

(1) **IN GENERAL.** —Except as provided in paragraph (2), the amendment made by subsection (a) shall apply to dispositions after July 10, 1989, in taxable years ending after such date.

(2) **BINDING CONTRACT.** —The amendment made by subsection (a) shall not apply to any disposition pursuant to a written binding contract in effect on July 10, 1989, and at all times thereafter before such disposition.

SEC. 7208. OTHER PROVISIONS RELATING TO TREATMENT OF STOCK AND DEBT; ETC.

(a) **CLARIFICATION OF REGULATORY AUTHORITY UNDER SECTION 385.** —

(1) **IN GENERAL.** —Subsection (a) of section 385 (relating to treatment of certain interests in corporations as stock or indebtedness) is amended by inserting “(or as in part stock and in part indebtedness)” before the period at the end thereof.

(2) **REGULATIONS NOT TO BE APPLIED RETROACTIVELY.** —Any regulations issued pursuant to the authority granted by the amendment made by paragraph (1) shall only apply with respect to instruments issued after the date on which the Secretary of the Treasury or his delegate provides public guidance as to the characterization of such instruments whether by regulation, ruling, or otherwise.

(b) **REPORTING OF CERTAIN ACQUISITIONS OR RECAPITALIZATIONS.** —

(1) **IN GENERAL.** —Section 6043 is amended by striking subsection (c) and inserting the following new subsections:

“(c) **CHANGES IN CONTROL AND RECAPITALIZATIONS.** —If —

“(1) control (as defined in section 304(c)(1)) a corporation is acquired by any person (or group of persons) in a transaction (or series of related transactions), or

“(2) there is a recapitalization of a corporation or other substantial change in the capital structure of a corporation,

when required by the Secretary, such corporation shall make a return (at such time and in such manner as the Secretary may prescribe) setting forth the identity of the parties to the transaction, the fees involved, the changes in the capital structure involved, and such other information as the Secretary may require with respect to such transaction.

“(d) CROSS REFERENCES. —For provisions relating to penalties for failure to file —

“(1) a return under subsection (b), see section 6652(c), or

“(2) a return under subsection (c), see section 6652(1).”

(2) PENALTY. —Section 6652 is amended by redesignating subsection (1) as subsection (m) and by inserting after subsection (k) the following new subsection:

“(1) FAILURE TO FILE RETURN WITH RESPECT TO CERTAIN CORPORATE TRANSACTIONS. —In the case of any failure to make a return required under section 6043(c) containing the information required by such section on the date prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause, there shall be paid (on notice and demand by the Secretary and in the same manner as tax) by the person failing to file such return, an amount equal to \$500 for each day during which such failure continues, but the total amount imposed under this subsection with respect to any return shall not exceed \$100,000.”

(3) CONFORMING AMENDMENTS. —

(A) The subsection heading for subsection (a) of section 6043 s amended by striking “CORPORATIONS” and inserting “CORPORATE LIQUIDATING, ETC., TRANSACTIONS”.

(B) The section heading for section 6043 is amended to read as follows:

“SEC. 6043. LIQUIDATING; ETC., TRANSACTIONS.”

(C) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by striking the item relating to section 6043 and inserting the following:

“Sec. 6043. Liquidating; etc., transactions.”

(4) EFFECTIVE DATE. —The amendments made by this subsection shall apply to transactions after March 31, 1990.

SEC. 7209. ESTIMATED TAX PAYMENTS REQUIRED FOR S CORPORATIONS.

(a) IN GENERAL. —Subsection (g) of section 6655 (relating to failure by corporation to pay estimated income tax) is amended by adding at the end thereof the following new paragraph:

“(4) APPLICATION OF SECTION TO CERTAIN TAXES IMPOSED ON S CORPORATIONS. —In the case of an S corporation, for purposes of this section —

“(A) The following taxes shall be treated as imposed by section 11:

“(i) The tax imposed by section 1374(a) (or the corresponding provisions of prior law).

“(ii) The tax imposed by section 1375(a).

“(iii) Any tax for which the S corporation is liable by reason of section 1371(d)(2).

“(B) Paragraph (2) of subsection (d) shall not apply.

“(C) Clause (ii) of subsection (d)(1)(B) shall be applied as if it read as follows:

“(ii) the sum of —

“(I) the amount determined under clause (i) by only taking into account the taxes referred to in clauses (i) and (iii) of subsection (g)(4)(A), and

“(II) 100 percent of the tax imposed by section 1375(a) which was shown on the return of the corporation for the preceding taxable year.’

“(D) The requirement in the last sentence of subsection (d)(1)(B) that the return for the preceding taxable year show a liability for tax shall not apply.

“(E) Any reference in subsection (e) to taxable income shall be treated as including a reference to the net recognized built-in gain or the excess passive income (as the case may be).”

(b) EFFECTIVE DATE. —The amendment made by this subsection (a) shall apply to taxable years beginning after December 31, 1989.

SEC. 7210. LIMITATION ON DEDUCTION FOR CERTAIN INTEREST PAID TO RELATED PERSON.

(a) GENERAL RULE. —Section 163 (as amended by section 7202) is amended by redesignating subsection j) as subsection (k) and by inserting after subsection (i) the following new subsection:

“(j) LIMITATION ON DEDUCTION FOR CERTAIN INTEREST PAID BY CORPORATION TO RELATED PERSON. —

“(1) LIMITATION. —

“(A) IN GENERAL. —If this subsection applies to any corporation for any taxable year, no deduction shall be allowed under this chapter for disqualified interest paid or accrued by such corporation during such taxable year. The amount disallowed under the preceding sentence shall not exceed the corporation's excess interest expense for the taxable year.

“(B) DISALLOWED AMOUNT CARRIED TO SUCCEEDING TAXABLE YEAR. —Any amount disallowed under subparagraph (A) for any taxable year shall be treated as disqualified interest paid or accrued in the succeeding taxable year.

“(2) CORPORATIONS TO WHICH SUBSECTION APPLIES. —

“(A) IN GENERAL. —This subsection shall apply to any corporation for any taxable year if —

“(i) such corporation has excess interest expense for such taxable year, and

“(ii) the ratio of debt to equity of such corporation as of the close of such taxable year (and on such other days during the taxable year as the Secretary may by regulations prescribe) exceeds 1.5 to 1.

“(B) EXCESS INTEREST EXPENSE. —

“(i) IN GENERAL. —For purposes of this subsection, the term `excess interest expense' means the excess (if any) of —

“(I) the corporation's net interest expense, over

“(II) the sum of 50 percent of the adjusted taxable income of the corporation plus any excess limitation carryforward under clause (ii).

“(ii) EXCESS LIMITATION CARRYFORWARD. —If a corporation has an excess limitation for any taxable year, the amount of such excess limitation shall be an excess limitation carryforward to the 1st succeeding taxable year and to the 2nd and 3rd succeeding taxable years to the extent not previously taken into account under this clause. The amount of such a carryforward taken into account for any such succeeding taxable year shall not exceed the excess interest expense for such succeeding taxable year (determined without regard to the carryforward from the taxable year of such excess limitation).

“(iii) EXCESS LIMITATION. —For purposes of clause (i), the term `excess limitation' means the excess (if any) of —

“(I) 50 percent of the adjusted taxable income of the corporation over

“(II) the corporation's net interest expense.

“(C) RATIO OF DEBT TO EQUITY. —For purposes of this paragraph, the term `ratio of debt to equity' means the ratio which the total indebtedness of the corporation bears to the sum of its money and all other assets less such total indebtedness. For purposes of the preceding sentence —

“(i) the amount taken into account with respect to any asset shall be the adjusted basis thereof for purposes of determining gain,

“(ii) the amount taken into account with respect to any indebtedness with original issue discount shall be its issue price plus the portion of the original issue discount previously accrued as determined under the rules of section 1272 (determined without regard to subsection (a)(7) or (b)(4) thereof), and

“(iii) there shall be such other adjustments as the Secretary may by regulations prescribe.

“(3) DISQUALIFIED INTEREST. —For purposes of this subsection —

“(A) IN GENERAL. —Except as provided in subparagraph (B), the term `disqualified interest' means any interest paid or accrued by the taxpayer (directly or indirectly) to a related person if no tax is imposed by this subtitle with respect to such interest.

“(B) EXCEPTION FOR CERTAIN EXISTING INDEBTEDNESS. —The term `disqualified interest' does

not include any interest paid or accrued under indebtedness with a fixed term —

“(i) which was issued on or before July 10, 1989, or

“(ii) which was issued after such date pursuant to a written binding contract in effect on such date and all times thereafter before such indebtedness was issued.

“(4) RELATED PERSON. —For purposes of this subsection —

“(A) IN GENERAL. —Except as provided in subparagraph (B), the term ‘related person’ means any person who is related (within the meaning of section 267(b) or 707(b)(1)) to the taxpayer.

“(B) SPECIAL RULE FOR CERTAIN PARTNERSHIPS. —

“(i) IN GENERAL. —Any interest paid or accrued to a partnership which (without regard to this subparagraph) is a related person shall not be treated as paid or accrued to a related person if less than 10 percent of the profits and capital interests in such partnership are held by persons with respect to whom no tax is imposed by this subtitle on such interest. The preceding sentence shall not apply to any interest allocable to any partner in such partnership who is a related person to the taxpayer.

“(ii) SPECIAL RULE WHERE TREATY REDUCTION. —If any treaty between the United States and any foreign country reduces the rate of tax imposed by this subtitle on a partner share of any interest paid or accrued to a partnership, such partner’s interests in such partnership shall, for purposes of clause (i), be treated as held in part by a tax-exempt person and in part by a taxable person under rules similar to the rules of paragraph (5)(B).

“(5) SPECIAL RULES FOR DETERMINING WHETHER INTEREST IS SUBJECT TO TAX. —

“(A) TREATMENT OF PASS-THRU ENTITIES. —In the case of any interest paid or accrued to a partnership, the determination of whether any tax is imposed by this subtitle on such interest shall be made at the partner level. Rules similar to the rules of the preceding sentence shall apply in the case of any pass-thru entity other than a partnership and in the case of tiered partnerships and other entities.

“(B) INTEREST TREATED AS TAX-EXEMPT TO EXTENT OF TREATY REDUCTION. —If any treaty between the United States and any foreign country reduces the rate of tax imposed by this subtitle on any interest paid or accrued by the taxpayer to a related person, such interest shall be treated as interest on which no tax is imposed by this subtitle to the extent of the same proportion of such interest as —

“(i) the rate of tax imposed without regard to such treaty, reduced by the rate of tax imposed under the treaty, bears to

“(ii) the rate of tax imposed without regard to the treaty.

“(6) OTHER DEFINITIONS AND SPECIAL RULES. —For purposes of this subsection —

“(A) ADJUSTED TAXABLE INCOME. —The term ‘adjusted taxable income’ means the taxable income of the taxpayer —

“(i) computed without regard to —

“(I) any deduction allowable under this chapter for the net interest expense,

“(II) the amount of any net operating loss deduction under section 172, and

“(III) any deduction allowable for depreciation, amortization, or depletion, and

“(ii) computed with such other adjustments as the Secretary may by regulations prescribe.

“(B) NET INTEREST EXPENSE. —The term ‘net interest expense’ means the excess (if any) of —

“(i) the interest paid or accrued by the taxpayer during the taxable year, over

“(ii) the amount of interest includible in the gross income of such taxpayer for such taxable year.

The Secretary may by regulations provide for adjustments in determining the amount of net interest expense.

“(C) TREATMENT OF AFFILIATED GROUP. —All members of the same affiliated group (within the meaning of section 1504(a)) shall be treated as 1 taxpayer.

“(7) REGULATIONS. —The Secretary shall prescribe such regulations as may be appropriate to carry out the purposes of this subsection, including —

“(A) such regulations as may be appropriate to prevent the avoidance of the purposes of this subsection,

“(B) regulations providing such adjustments in the case of corporations which are members of an affiliated group as may be appropriate to carry out the purposes of this subsection, and

“(C) regulations for the coordination of this subsection with section 884.”

(b) EFFECTIVE DATE. —

(1) IN GENERAL. —The amendment made by this section shall apply to interest paid or accrued in taxable years beginning after July 10, 1989.

(2) SPECIAL RULE FOR DEMAND LOANS, ETC. —In the case of any demand loan (or other loan without a fixed term) which was outstanding on July 10, 1989, interest on such loan to the extent attributable to periods before September 1, 1989, shall not be treated as disqualified interest for purposes of section 163(j) of the Internal Revenue Code of 1986 (as added by subsection (a)).

SEC. 7211. LIMITATIONS ON REFUNDS DUE TO NET OPERATING LOSS CARRYBACKS OR EXCESS INTEREST ALLOCABLE TO CORPORATE EQUITY REDUCTION TRANSACTIONS.

(a) IN GENERAL. —Paragraph (1) of section 172(b) (relating to years to which loss may be carried) is amended by adding at the end thereof the following new subparagraph:

“(M) EXCESS INTEREST LOSS. —

“(i) IN GENERAL. —If —

“(I) there is a corporate equity reduction transaction, and

“(II) an applicable corporation has a corporate equity reduction interest loss for any loss limitation year ending after August 2, 1989,

then the corporate equity reduction interest loss shall be a net operating loss carryback and carryover to the taxable years described in subparagraphs (A) and (B), except that such loss shall not be carried back to a taxable year preceding the taxable year in which the corporate equity reduction transaction occurs.

“(ii) LOSS LIMITATION YEAR. —For purposes of clause (i) and subsection (m), the term ‘loss limitation year’ means, with respect to any corporate equity reduction transaction, the taxable year in which such transaction occurs and each of the 2 succeeding taxable years.

“(iii) APPLICABLE CORPORATION. —For purposes of clause (i), the term ‘applicable corporation’ means a C corporation —

“(I) which acquires stock, or the stock of which is acquired, in a major stock acquisition, “(II) a corporation making distributions with respect to, or redeeming, its stock in connection with an excess distribution, or

“(III) any successor corporation of a corporation described in subclause (I) or (II).

“(iv) OTHER DEFINITIONS. —For “definitions of terms used in this subparagraph, see subsection (m).”

(b) CORPORATE EQUITY REDUCTION INTEREST LOANS AND CORPORATE EQUITY REDUCTION TRANSACTION DEFINED. —Section 172 is amended by redesignating subsection (m) as subsection (n) and by inserting after subsection (I) the following new subsection:

“(m) CORPORATE EQUITY REDUCTION INTEREST LOSSES. —For purposes of this section —

“(1) IN GENERAL. —The term ‘corporate equity reduction interest loss’ means, with respect to any loss limitation year, the excess (if any) of —

“(A) the net operating loss for such taxable year, over

“(B) the net operating loss for such taxable year determined without regard to any allocable interest deductions otherwise taken into account in computing such loss.

“(2) ALLOCABLE INTEREST DEDUCTIONS. —

“(A) IN GENERAL. —The term ‘allocable interest deductions’ means deductions allowed under this chapter for interest on the portion of any indebtedness allocable to a corporate equity reduction transaction.

“(B) METHOD OF ALLOCATION. —Except as provided in regulations and subparagraph (E), indebtedness shall be allocated to a corporate equity reduction transaction in the manner prescribed under clause (ii) of section 263A(f)(2)(A) (without regard to clause (i) thereof).

“(C) ALLOCABLE DEDUCTIONS NOT TO EXCEED INTEREST INCREASES. —Allocable interest deductions for any loss limitation year shall not exceed the excess (if any) of —

“(i) the amount allowable as a deduction for interest paid or accrued by the taxpayer during the loss limitation year, over

“(ii) the average of such amounts for the 3 taxable years preceding the taxable year in which the corporate

equity reduction transaction occurred.

“(D) DE MINIMIS RULE. —A taxpayer shall be treated as having no allocable interest deductions for any taxable year if the amount of such deductions (without regard to this subparagraph) is less than \$1,000,000.

“(E) SPECIAL RULE FOR CERTAIN UNFORESEEABLE EVENTS. —If an unforeseeable extraordinary adverse event occurs during a loss limitation year but after the corporate equity reduction transaction —

“(i) indebtedness shall be allocated in the manner described in subparagraph (B) to unreimbursed costs paid or incurred in connection with such event before being allocated to the corporate equity reduction transaction, and

“(ii) the amount determined under subparagraph (C)(i) shall be reduced by the amount of interest on indebtedness described in clause (i).

“(F) TRANSITION RULE. —If any of the 3 taxable years described in subparagraph (C)(ii) end on or before August 2, 1989, the taxpayer may substitute for the amount determined under such subparagraph an amount equal to the interest paid or accrued (determined on an annualized basis) during the taxpayer's taxable year which includes August 3, 1989, on indebtedness of the taxpayer outstanding on August 2, 1989.

“(3) CORPORATE EQUITY REDUCTION TRANSACTION. —

“(A) IN GENERAL. —The term `corporate equity reduction transaction' means —

“(i) a major stock acquisition, or

“(ii) an excess distribution.

“(B) MAJOR STOCK ACQUISITION. —

“(i) IN GENERAL. —The term `major stock acquisition' means the acquisition by a corporation pursuant to a plan of such corporation (or any group of persons acting in concert with such corporation) of stock in another corporation representing 50 percent or more (by vote or value) of the stock in such other corporation,

“(ii) EXCEPTIONS. —The term `major stock acquisition' shall not include —

“(I) a qualified stock purchase (within the meaning of section 338) to which an election under section 338 applies, or

“(II) except as provided in regulations, an acquisition in which a corporation acquires stock of another corporation which, immediately before the acquisition, was a member of an affiliated group (within the meaning of section 1504(a)) other than the common parent of such group.

“(C) EXCESS DISTRIBUTION. —The term `excess distribution' means the excess (if any) of —

“(i) the aggregate distributions (including redemptions) made during a taxable year by a corporation with respect to its stock, over

“(ii) the greater of —

“(I) 150 percent of the average of such distributions during the 3 taxable years immediately preceding such taxable year, or

“(II) 10 percent of the fair market value of the stock of such corporation as of the beginning of such taxable year.

“(D) RULES FOR APPLYING SUBPARAGRAPH (B). —For purposes of subparagraph (B) —

“(i) PLANS TO ACQUIRE STOCK. —All plans referred to in subparagraph (B) by any corporation (or group of persons acting in concert with such corporation) with respect to another corporation shall be treated as 1 plan.

“(ii) ACQUISITIONS DURING 24-MONTH PERIOD. —All acquisitions during any 24-month period shall be treated as pursuant to 1 plan.

“(E) RULES FOR APPLYING SUBPARAGRAPH (C). —For purposes of subparagraph (C) —

“(i) CERTAIN PREFERRED STOCK DISREGARDED. —Stock described in section 1504(a)(4), and distributions (including redemptions) with respect to such stock, shall be disregarded.

“(ii) ISSUANCE OF STOCK. —The amounts determined under clauses (i) and (ii)(I) of subparagraph (C) shall be reduced by the aggregate amount of stock issued by the corporation during the applicable period in exchange for money or property other than stock in the corporation.

“(4) OTHER RULES. —

“(A) ORDERING RULE. —For purposes of paragraph (1), in determining the allocable interest deductions taken into account in computing the net operating loss for any taxable year, taxable income for such taxable year shall be treated as having been computed by taking allocable interest deductions into account after all other deductions.

“(B) COORDINATION WITH SUBSECTION (B)(2). —In applying paragraph (2) of subsection (b), the corporate equity reduction interest loss shall be treated in a manner similar to the manner in which a foreign expropriation loss is treated.

“(C) MEMBERS OF AFFILIATED GROUPS. —Except as provided by regulations, all members of an affiliated group filing a consolidated return under section 1501 shall be treated as 1 taxpayer for purposes of this subsection and subsection (b)(1)(M).

“(5) REGULATIONS. —The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subsection, including regulations —

“(A) for applying this subsection to successor corporations and in cases where a taxpayer becomes, or ceases to be, a member of an affiliated group filing a consolidated return under section 1501,

“(B) to prevent the avoidance of this subsection through related parties, pass-through entities, and intermediaries, and

“(C) for applying this subsection where more than 1 corporation is involved in a corporate equity reduction transaction.

(c) EFFECTIVE DATE. —

(1) IN GENERAL. —Except as provided in this subsection, the amendments made by this section shall apply to corporate equity reduction transactions occurring after August 2, 1989, in taxable years ending after August 2, 1989.

(2) EXCEPTIONS. —In determining whether a corporate equity reduction transaction has occurred after August 2, 1989, there shall not be taken into account —

(A) acquisitions or redemptions of stock, or distributions with respect to stock, occurring on or before August 2, 1989,

(B) acquisitions or redemptions of stock after August 2, 1989, pursuant to a binding written contract (or tender offer filed with the Securities and Exchange Commission) in effect on August 2, 1989, and at all times thereafter before such acquisition or redemption, or

(C) any distribution with respect to stock after August 2, 1989, which was declared on or before August 2, 1989.

Any distribution to which the preceding sentence applies shall be taken into account under section 172(m)(3)(C)(ii)(I) of the Internal Revenue Code of 1986 (relating to base period for distributions).

Subtitle C —Employee Benefit Provisions

PART I —EMPLOYEE STOCK OWNERSHIP PLANS

SEC. 7301. LIMITATIONS ON PARTIAL EXCLUSION OF INTEREST ON LOANS USED TO ACQUIRE EMPLOYER SECURITIES.

(a) EXCLUSION AVAILABLE ONLY WHERE EMPLOYEES RECEIVE SIGNIFICANT OWNERSHIP INTEREST. —Subsection (b) of section 133 (defining securities acquisition loans) is amended by adding at the end thereof the following new paragraph:

“(6) PLAN MUST HOLD MORE THAN 50 PERCENT OF STOCK AFTER ACQUISITION OR TRANSFER. —

“(A) IN GENERAL. —A loan shall not be treated as a securities acquisition loan for purposes of this section unless, immediately after the acquisition or transfer referred to in subparagraph (A) or (B) of paragraph (1), respectively, the employee stock ownership plan owns more than 50 percent of —

“(i) each class of outstanding stock of the corporation issuing the employer securities, or

“(ii) the total value of all outstanding stock of the corporation.

“(B) FAILURE TO RETAIN MINIMUM STOCK INTEREST. —

“(i) IN GENERAL. —Subsection (a) shall not apply to any interest received with respect to a securities acquisition loan which is allowable to any period during which the employee stock ownership plan does not own stock meeting the requirements of subparagraph (A).

“(ii) EXCEPTION. —To the extent provided by the Secretary, clause (i) shall not apply to any period if, within 90 days of the first date on which the failure occurred (or such longer period not in excess of 180 days as the Secretary may prescribe), the plan acquires stock which results in its meeting the requirements of subparagraph (A).

“(C) STOCK. —For purposes of subparagraph (A) —

“(i) IN GENERAL. —The term ‘stock’ means stock other than stock described in section 1504(a)(4).

“(ii) TREATMENT OF CERTAIN RIGHTS. —The Secretary may provide that warrants, options, contracts to acquire stock, convertible debt interests and other similar interests be treated as stock for 1 or more purposes under subparagraph (A).

“(D) AGGREGATION RULE. —For purposes of determining whether the requirements of subparagraph (A) are met, an employee stock ownership plan shall be treated as owning stock in the corporation issuing the employer securities which is held by any other employee stock ownership plan which is maintained by —

“(i) the employer maintaining the plan, or

“(ii) any member of a controlled group of corporations (within the meaning of section 409(1)(4)) of which the employer described in clause (i) is a member.”

(b) TERM OF LOAN MAY EXCEED 15 YEARS. —Paragraph (1) of section 133(b) is amended by adding at the end thereof the following new sentence: “The term ‘securities acquisition loan’ shall not include a loan with a term greater than 15 years.”

(c) VOTING RIGHTS. —Subsection (b) of section 133, as amended by subsection (a), is amended by adding at the end thereof the following new paragraph:

“(7) VOTING RIGHTS OF EMPLOYER SECURITIES. —A loan shall not be treated as a securities acquisition loan for purposes of this section unless —

“(A) the employee stock ownership plan meets the requirements of section 409(e)(2) with respect to all employer securities acquired by, or transferred to, the plan in connection with such loan (without regard to whether or not the employer has a registration-type class of securities), and

“(B) no stock described in section 409(1)(3) is acquired by, or transferred to, the plan in connection with such loan unless —

“(i) such stock has voting rights equivalent to the stock to which it may be converted, and

“(ii) the requirements of subparagraph (A) are met with respect to such voting rights”.

(d) TAX ON DISPOSITION OF SECURITIES BY EMPLOYEE STOCK OWNERSHIP PLANS. —

(1) IN GENERAL. —Chapter 43 is amended by inserting after section 4978A the following new section:

“SEC. 4978B. TAX ON DISPOSITION OF EMPLOYER SECURITIES TO WHICH SECTION 133 APPLIED.

“(a) IMPOSITION OF TAX. —In the case of an employee stock ownership plan which has acquired section 133 securities, there is hereby imposed a tax on each taxable event in an amount equal to the amount determined under subsection (b).

“(b) AMOUNT OF TAX. —

“(1) IN GENERAL. —The amount of the tax imposed by subsection (a) shall be equal to 10 percent of the amount realized on the disposition to the extent allocable to section 133 securities under section 4978(b)(2).

“(2) DISPOSITIONS OTHER THAN SALES OR EXCHANGES. —For purposes of paragraph (1), in the case of a disposition of employer securities which is not a sale or exchange, the amount realized on such disposition shall be the fair market value of such securities at the time of disposition.

“(c) TAXABLE EVENT. —For purposes of this section, the term ‘taxable event’ means any of the following dispositions:

“(1) DISPOSITIONS WITHIN 3 YEARS. —Any disposition of any employer securities by an employee stock ownership plan within 3 years after such plan acquired section 133 securities if —

“(A) the total number of employer securities held by such plan after such disposition is less than the total number of employer securities held after such acquisition, or

“(B) except to the extent provided in regulations, the value of employer securities held by such plan after the disposition is 50 percent or less of the total value of all employer securities as of the time of the disposition.

For purposes of subparagraph (B), the aggregation rule of section 133(b)(6)(D) shall apply.

“(2) STOCK DISPOSED OF BEFORE ALLOCATION. —Any disposition of section 133 securities to which paragraph (1) does not apply if —

“(A) such disposition occurs before such securities are allocated to accounts of participants or their beneficiaries, and

“(B) the proceeds from such disposition are not so allocated.

“(d) SECTION NOT TO APPLY TO CERTAIN DISPOSITIONS. —

“(1) IN GENERAL. —This section shall not apply to any disposition described in paragraph (1), (3), or (4) of section 4978(d).

“(2) CERTAIN REORGANIZATIONS. —For purposes of this section, any exchange of section 133 securities for employer securities of another corporation in any reorganization described in section 368(a)(1) shall not be treated as a disposition, but the employer securities received shall be treated as section 133 securities and as having been held by the plan during the period the securities which were exchanged were held.

“(3) FORCED DISPOSITION OCCURRING BY OPERATION OF STATE LAW. —Any forced disposition of section 133 securities by an employee stock ownership plan occurring by operation of a State law shall not be treated as a disposition. This paragraph shall only apply to securities which, at the time the securities were acquired by the plan, were regularly traded on an established securities market.

“(e) DEFINITIONS AND SPECIAL RULES. —For purposes of this section —

“(1) LIABILITY FOR PAYMENT OF TAXES. —The tax imposed by this section shall be paid by the employer.

“(2) SECTION 133 SECURITIES. —The term ‘section 133 securities’ means employer securities acquired by an employee stock ownership plan in a transaction to which section 133 applied, except that such term shall not include —

“(A) qualified securities (as defined in section 4978(e)(2)), or

“(B) qualified employer securities (as defined in section 4978A(f)(2), as in effect on the day before the date of the enactment of this section).

“(3) DISPOSITION. —The term ‘disposition’ includes any distribution.

“(4) ORDERING RULES. —For ordering rules for dispositions of employer securities, see section 4978(b)(2).”

(2) CONFORMING AMENDMENT. —The table of sections for chapter 43 is amended by inserting after the item relating to section 4978A the following new item:

“Sec. 4978B. Tax on disposition of employer securities to which section 133 applied.”

(e) REPORTING REQUIREMENTS. —Section 6047 (relating to information reports relating to certain trusts or annuity plans) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

“(e) EMPLOYEE STOCK OWNERSHIP PLANS. —The Secretary shall require —

“(1) any employer maintaining, or the plan administrator (within the meaning of section 414(g)) of, an employee stock ownership plan —

“(A) which acquired stock in a transaction to which section 133 applies, or

“(B) which holds stock with respect to which section 404(k) applies to dividends paid on such stock,

“(2) any person making or holding a loan to which section 133 applies, or

“(3) both such employer or plan administrator and such person, to make returns and reports regarding such plan, transaction, or loan to the Secretary and to such other persons as the Secretary may prescribe. Such returns and reports shall be made in such form, shall be made at such time, and shall contain such information as the Secretary may prescribe.”

(f) EFFECTIVE DATES. —

(1) IN GENERAL. —Except as provided in this subsection, the amendments made by this section shall

apply to loans made after July 10, 1989.

(2) BINDING COMMITMENT EXCEPTIONS. —

(A) The amendments made by this section shall not apply to any loan —

(i) which is made pursuant to a binding written commitment in effect on June 6, 1989, and at all times thereafter before such loan is made, or

(ii) to the extent that the proceeds of such loan are used to acquire employer securities pursuant to a written binding contract (or tender offer registered with the Securities and Exchange Commission) in effect on June 6, 1989, and at all times thereafter before such securities are acquired.

(B) The amendments made by this section shall not apply to any loan to which subparagraph (A) does not apply which is made pursuant to a binding written commitment in effect on July 10, 1989, and at all times thereafter before such loan is made. The preceding sentence shall only apply to the extent that the proceeds of such loan are used to acquire employer securities pursuant to a written binding contract (or tender offer registered with the Securities and Exchange Commission) in effect on July 10, 1989, and at all times thereafter before such securities are acquired.

(C) The amendments made by this section shall not apply to any loan made on or before July 10, 1992, pursuant to a written agreement entered into on or before July 10, 1989, if such agreement evidences the intent of the borrower on a periodic basis to enter into securities acquisition loans described in section 133(b)(1)(B) of the Internal Revenue Code of 1986 (as in effect on the day before the date of the enactment of this Act). The preceding sentence shall apply only if one or more securities acquisition loans were made to the borrower on or before July 10, 1989.

(3) REFINANCINGS. —The amendments made by this section shall not apply to loans made after July 10, 1989, to refinance securities acquisition loans (determined without regard to section 133(b)(2) of the Internal Revenue Code of 1986) made on or before such date or to refinance loans described in this paragraph or paragraph (2), (4), or (5) if —

(A) such refinancing loans meet the requirements of such section 133 of such Code (as in effect before such amendments) applicable to such loans,

(B) immediately after the refinancing the principal amount of the loan resulting from the refinancing does not exceed the principal amount of the refinanced loan (immediately before the refinancing), and

(C) the term of such refinancing loan does not extend beyond the later of —

(i) the last day of the term of the original securities acquisition loan, or

(ii) the last day of the 7-year period beginning on the date the original securities acquisition loan was made.

For purposes of this paragraph, the term “securities acquisition loan” shall include a loan from a corporation to an employee stock ownership plan described in section 133(b)(3) of such Code.

(4) COLLECTIVE BARGAINING AGREEMENTS. —The amendments made by this section shall not apply to any loan to the extent such loan is used to acquire employer securities for an employee stock ownership plan pursuant to a collective bargaining agreement which sets forth the material terms of such employee stock ownership plan and which was agreed to on or before June 6, 1989, by one or more employers and employee representatives (and ratified on or before such date or within a reasonable period thereafter).

(5) **FILINGS WITH UNITED STATES.** —The amendments made by this section shall not apply to any loan the aggregate principal amount of which was specified in a filing with an agency of the United States on or before June 6, 1989, if —

(A) such filing specifies such loan is to be a securities acquisition loan for purposes of section 133 of the Internal Revenue Code of 1986 and such filing is for the registration required to permit the offering of such loan, or

(B) such filing is for the approval required in order for the employee stock ownership plan to acquire more than a certain percentage of the stock of the employer.

(6) **30-PERCENT TEST SUBSTITUTED FOR 50-PERCENT TEST IN CASE OF CERTAIN LOANS.** — In the case of a loan to which the amendments made by this section apply —

(A) which is made before November 18, 1989, or

(B) with respect to which such amendments would not apply if paragraph (2)(A) were applied by substituting “November 17, 1989” for “June 6, 1989” each place it appears,

section 133(b)(6)(A) of the Internal Revenue Code of 1986 (as added by subsection (a)) shall be applied by substituting “at least 30 percent” for “more than 50 percent” and section 4978B(c)(1)(B) of such Code (as added by subsection d)) shall be applied by substituting “less than 30 percent” for “50 percent or less”. The preceding sentence shall apply to any loan which is used to refinance a loan described in such sentence if the requirements of subparagraphs (A), (B), and (C) of paragraph (3) are met with respect to the refinancing loan.

SEC. 7302. LIMITATIONS ON DEDUCTIONS FOR DIVIDENDS PAID ON EMPLOYER SECURITIES.

(a) **IN GENERAL.** —Subsection (k) of section 404 is amended to read as follows:

“(k) **DEDUCTION FOR DIVIDENDS PAID ON CERTAIN EMPLOYER SECURITIES.** —

“(1) **GENERAL RULE.** —In the case of a corporation, there shall be allowed as a deduction for a taxable year the amount of any applicable dividend paid in cash by such corporation during the taxable year with respect to applicable employer securities. Such deduction shall be in addition to the deductions allowed under subsection (a).

“(2) **APPLICABLE DIVIDEND.** —For purposes of this subsection —

“(A) **IN GENERAL.** —The term ‘applicable dividend’ means any dividend which, in accordance with the plan provisions —

“(i) is paid in cash to the participants in the plan or their beneficiaries,

“(ii) is paid to the plan and is distributed in cash to participants in the plan or their beneficiaries not later than 90 days after the close of the plan year in which paid, or

“(iii) is used to make payments on a loan described in subsection (a)(9) the proceeds of which were used to

acquire the employer securities (whether or not allocated to participants) with respect to which the dividend is paid.

“(B) LIMITATION ON CERTAIN DIVIDENDS. —A dividend described in subparagraph (A)(iii) which is paid with respect to any employer security which is allocated to a participant shall not be treated as an applicable dividend unless the plan provides that employer securities with a fair market value of not less than the amount of such dividend are allocated to such participant for the year which (but for subparagraph (A)) such dividend would have been allocated to such participant.

“(3) APPLICABLE EMPLOYER SECURITIES. —For purposes of this subsection, the term ‘applicable employer securities’ means, with respect to any dividend, employer securities which are held on the record date for such dividend by an employee stock ownership plan which is maintained by —

“(A) the corporation paying such dividend, or

“(B) any other corporation which is a member of a controlled group of corporations (within the meaning of section 409(1)(4)) which includes such corporation.

“(4) TIME FOR DEDUCTION. —

“(A) IN GENERAL. —The deduction under paragraph (1) shall be allowable in the taxable year of the corporation in which the dividend is paid or distributed to a participant or his beneficiary.

“(B) REPAYMENT OF LOANS. —In the case of an applicable dividend described in clause (iii) of paragraph (2)(A), the deduction under paragraph (1) shall be allowable in the taxable year of the corporation in which such dividend is used to repay the loan described in such clause.

“(5) OTHER RULES. —For purposes of this subsection —

“(A) DISALLOWANCE OF DEDUCTION —The Secretary may disallow the deduction under paragraph (1) for any dividend if the Secretary determines that such dividend constitutes, in substance, an evasion of taxation.

“(B) PLAN QUALIFICATION. —A plan shall not be treated as violating the requirements of section 401, 409, or 4975(e)(7), or as engaging in a prohibited transaction for purposes of section 4975(d)(3), merely by reason of any payment or distribution described in paragraph (2)(A).

“(6) DEFINITIONS. —For purposes of this subsection —

“(A) EMPLOYER SECURITIES. —The term ‘employer securities’ has the meaning given such term by section 409(1).

“(B) EMPLOYEE STOCK OWNERSHIP PLAN. —The term ‘employee stock ownership plan’ has the meaning given such term by section 4975(e)(7). Such term includes a tax credit employee stock ownership plan (as defined in section 409).”

(b) EFFECTIVE DATE. —

(1) IN GENERAL. —The amendment made by this section shall apply to employer securities acquired after August 4, 1989.

(2) SECURITIES ACQUIRED WITH CERTAIN LOANS. —The amendment made by this section shall not apply to employer securities acquired after August 4, 1989, which are acquired —

(A) with the proceeds of any loan which was made pursuant to a binding written commitment in effect on August 4, 1989, and at all times thereafter before such loan is made, and

(B) pursuant to a written binding contract (or tender offer registered with the Securities and Exchange Commission) in effect on August 4, 1989, and at all times thereafter before such securities are acquired.

SEC. 7303. 3-YEAR HOLDING PERIOD REQUIRED BEFORE SECTION 1042 SALE.

(a) IN GENERAL. —Section 1042(b) (relating to requirements to qualify for nonrecognition) is amended by adding at the end thereof the following new paragraph:

“(4) 3-YEAR HOLDING PERIOD. —The taxpayer's holding period with respect to the qualified securities is at least 3 years (determined as of the time of the sale).”

(b) EFFECTIVE DATE. —The amendment made by this section shall apply to sales after July 10, 1989.

SEC. 7304. REPEAL OF CERTAIN PROVISIONS RELATING TO EMPLOYEE STOCK OWNERSHIP PLANS.

(a) ESTATE TAX DEDUCTION. —

(1) IN GENERAL. —Section 2057 (relating to sales of employer securities to employee stock ownership plans or worker-owned corporations) is hereby repealed.

(2) CONFORMING AMENDMENTS. —

(A) Paragraph (1) of section 409(n) is amended —

(i) by striking “or section 2057” each place it appears.

(ii) by striking “or any decedent if the executor of the estate of such decedent makes a qualified sale to which section 2057 applies” in subparagraph (A)(i) thereof, and

(iii) by striking “or the decedent” in subparagraph (A)(ii) thereof.

(B) Paragraphs (2)(C)(i) and (3)(A)(ii) of section 409(n) are each amended by striking “or section 2057”.

(C)(i) Section 4978A is hereby repealed.

(ii) Section 4978(b)(2) is amended by striking “(determined as if such securities were disposed of in the order described in section 4978A(e)).” and inserting “determined as if such securities were disposed of —

“(A) first, from section 133 securities (as defined in section 4978B(e)(2)) acquired during the 3-year period ending on the date of such disposition, beginning with the securities first so acquired.

“(B) second, from section 133 securities (as so defined) acquired before such 3-year period unless such

securities (or proceeds from the disposition) have been allocated to accounts of participants or beneficiaries.”

“(C) third, from qualified securities to which section 1042 applied acquired during the 3-year period ending on the date of the disposition, beginning with the securities first so acquired, and

“(D) then from any other employer securities.

If subsection (d) or section 4978B(d) applies to a disposition, the disposition shall be treated as made from employer securities in the opposite order of the preceding sentence.”

(iii) The table of sections for chapter 43 is amended by striking the item relating to section 4978A.

(D) Section 4979A is amended —

(i) by striking “or section 2057” in subsection (b)(1), and

(ii) by striking “or section 2057(d)” in subsection (c)(2).

(E) The table of sections for part IV of subchapter A of chapter 11 is amended by striking the item relating to section 2057.

(3) EFFECTIVE DATE. —The amendments made by this subsection shall apply to the estates of decedents dying after the date of the enactment of this Act.

(b) LIABILITY FOR PAYMENT OF ESTATE TAX. —

(1) IN GENERAL. —Section 2210 (relating to liability for payment in case of transfer of employer securities) is hereby repealed.

(2) CONFORMING AMENDMENTS. —

(A) Section 2002 is amended by striking “Except as provided in section 2210, the” and inserting “The”.

(B) Section 6018 is amended by striking subsection (c).

(C) The table of sections for subchapter C of chapter 11 is amended by striking the item relating to section 2210.

(3) EFFECTIVE DATE. —The amendments made by this subsection shall apply to estates of decedents dying after July 12, 1989.

(c) LIMITATIONS ON DEFINED CONTRIBUTION PLANS. —

(1) IN GENERAL. —Paragraph (6) of section 415(c) is amended to read as follows:

“(6) SPECIAL RULE FOR EMPLOYEE STOCK OWNERSHIP PLANS. —If no more than one-third of the employer contributions to an employee stock ownership plan (as described in section 4975(e)(7)) for a year which are deductible under paragraph (9) of section 404(a) are allocated to highly compensated employees (within the meaning of section 414(q)), the limitations imposed by this section shall not apply to —

“(A) forfeitures of employer securities (within the meaning of section 409) under such an employee stock ownership plan if such securities were acquired with the proceeds of a loan (as described in section 404(a)(9)(A)), or

(B) employer contributions to such an employee stock ownership plan which are deductible under section 404(a)(9)(B) and charged against the participant's account.”

(2) EFFECTIVE DATE. —The amendment made by this subsection shall apply to years beginning after July 12, 1989.

(d) SPECIAL RULES RELATING TO NET OPERATING LOSSES. —

(1) IN GENERAL. —Section 382(1)(3) is amended by striking subparagraph (C) and by redesignating subparagraph (D) as subparagraph (C).

(2) EFFECTIVE DATE. —The amendments made by this subsection shall apply to acquisitions of employer securities after July 12, 1989, except that such amendments shall not apply to acquisitions after July 12, 1989, pursuant to a written binding contract in effect on July 12, 1989, and at all times thereafter before such acquisition.

PART II —SECTION 401(H) ACCOUNTS

SEC. 7311. LIMITATION ON CONTRIBUTIONS TO SECTION 401(h) ACCOUNTS.

(a) IN GENERAL. —Section 401(h) is amended by adding at the end thereof the following new sentence: “In no event shall the requirements of paragraph (1) be treated as met if the aggregate actual contributions for medical benefits, when added to actual contributions for life insurance protection under the plan, exceed 25 percent of the total actual contributions to the plan (other than contributions to fund past service credits) after the date on which the account is established.”

(b) EFFECTIVE DATE. —

(1) IN GENERAL. —The amendment made by this section shall apply to contributions after October 3, 1989.

(2) TRANSITION. —The amendment made by this section shall not apply to contributions made before January 1, 1990, if —

(A) the employer requested before October 3, 1989, a private letter ruling or determination letter with respect to the qualification of the plan maintaining the account under section 401(h) of the Internal Revenue Code of 1986,

(B) the request sets forth a method under which the amount of contributions to the account are to be determined on the basis of cost,

(C) such method is permissible under section 401(h) of such Code under the provisions of General Counsel Memorandum 39785, and

(D) the Internal Revenue Service issued before October 4, 1989, a private letter ruling, determination letter, or other letter providing that the specific plan involved qualifies under section 401(a) of such Code when such method is used, that contributions to the account are deductible, or acknowledging that the account would not adversely affect the qualified status of the plan (contingent on all phases of the particular plan being approved).

Subtitle D —Foreign Provisions

SEC. 7401. TAXABLE YEAR OF CERTAIN FOREIGN CORPORATIONS.

(a) GENERAL RULE. —Subpart D of part II of subchapter N of chapter 1 (relating to miscellaneous provisions) is amended by adding at the end thereof the following new section:

“SEC. 898. TAXABLE YEAR OF CERTAIN FOREIGN CORPORATIONS.

“(a) GENERAL RULE. —For purposes of this title, the taxable year of any specified foreign corporation shall be the required year determined under subsection (c).

“(b) SPECIFIED FOREIGN CORPORATION. —For purposes of this section —

“(1) IN GENERAL. —The term ‘specified foreign corporation’ means any foreign corporation —

“(A) which is —

“(i) treated as a controlled foreign corporation for any purpose under subpart F of part III of this subchapter, or

“(ii) a foreign personal holding company (as defined in section 552), and

“(B) with respect to which the ownership requirements of paragraph (2) are met.

“(2) OWNERSHIP REQUIREMENTS. —

“(A) IN GENERAL. —The ownership requirements of this paragraph are met with respect to any foreign corporation if a United States shareholder owns, on each testing day, more than 50 percent of —

“(i) the total voting power of all classes of stock of such corporation entitled to vote, or

“(ii) the total value of all classes of stock of such corporation.

“(B) OWNERSHIP. —For purposes of subparagraph (A), the rules of subsections (a) and (b) of section 958 and sections 551(f) and 554, whichever are applicable, shall apply in determining ownership.

“(3) UNITED STATES SHAREHOLDER. —

“(A) IN GENERAL. —The term ‘United States shareholder’ has the meaning given to such term by section 951(b), except that, in the case of a foreign corporation having related person insurance income (as defined in section 953(c)(2)), the Secretary may treat any person as a United States shareholder for purposes of this section if such person is treated as a United States shareholder under section 953(c)(l).

“(B) FOREIGN PERSONAL HOLDING COMPANIES. —In the case of any foreign personal holding company (as defined in section 552) which is not a specified foreign corporation by reason of paragraph (1)(A)(i), the term ‘United States shareholder’ means any person who is treated as a United States shareholder under section 551.

“(c) DETERMINATION OF REQUIRED YEAR. —

“(1) CONTROLLED FOREIGN CORPORATIONS. —

“(A) IN GENERAL. —In the case of a specified foreign corporation described in subsection (b)(1)(A)(i), the required year is —

“(i) the majority U.S. shareholder year, or

“(ii) if there is no majority U.S. shareholder year, the taxable year prescribed under regulations.

“(B) 1-MONTH DEFERRAL ALLOWED. —A specified foreign corporation may elect, in lieu of the taxable year under subparagraph (A)(i), a taxable year beginning 1 month earlier than the majority U.S. shareholder year.

“(C) MAJORITY U.S. SHAREHOLDER YEAR. —

“(i) IN GENERAL. —For purposes of this subsection, the term ‘majority U.S. shareholder year’ means the taxable year (if any) which, on each testing day, constituted the taxable year of —

“(I) each United States shareholder described in subsection (b)(2)(A), and

“(II) each United States shareholder not described in subclause (I) whose stock was treated as owned under subsection (b)(2)(B) by any shareholder described in each subclause.

“(ii) TESTING DAY. —The testing days shall be —

“(I) the first day of the corporation's taxable year (determined without regard to this section), or

“(II) the days during such representative period as the Secretary may prescribe.

“(2) FOREIGN PERSONAL HOLDING COMPANIES. —In the case of a foreign personal holding company described in subsection (b)(3)(B), the required year shall be determined under paragraph (1), except that subparagraph (B) of paragraph (1) shall not apply.”

(b) TREATMENT OF DIVIDENDS PAID AFTER CLOSE OF TAXABLE YEAR. —

(1) IN GENERAL. —Section 563 is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

“(c) FOREIGN PERSONAL HOLDING COMPANY TAX. —

“(1) IN GENERAL. —In the determination of the dividends paid deduction for purposes of part III, a dividend paid after the close of any taxable year and on or before the 15th day of the 3rd month following the close of such taxable year shall, to the extent the company designates such dividend as being taken into account under this subsection, be considered as paid during such taxable year. The amount allowed as a deduction by reason of the application of this subsection with respect to any taxable year shall not exceed the undistributed foreign personal holding company income of the corporation for the taxable year computed without regard to this subsection.

“(2) SPECIAL RULES. —In the case of any distribution referred to in paragraph (1) —

“(A) paragraph (1) shall apply only if such distribution is to the person who was the shareholder of record (as of the last day of the taxable year of the foreign personal holding company) with respect to the stock for which such distribution is made,

“(B) the determination of the person required to include such distribution in gross income shall be made under the principles of section 551(f), and

“(C) any person required to include such distribution in gross or distributable net income shall include such distribution in income for such person's taxable year in which the taxable year, of the foreign personal holding company ends.”

(2) CONFORMING AMENDMENT. —Subsection (d) of section 563 (as redesignated by paragraph (1)) is amended by striking “subsection (a) or (b)” and inserting “subsection (a), (b), or (c)”.

(c) CLERICAL AMENDMENT. —The table of sections for subpart D of part II of subchapter N of chapter 1 is amended by adding at the end thereof the following new item:

“Sec. 898. Taxable year of certain foreign corporations.”

(d) EFFECTIVE DATE. —

(1) IN GENERAL. —The amendments made by this section shall apply to taxable years of foreign corporations beginning after July 10, 1989.

(2) SPECIAL RULES. —If any foreign corporation is required by the amendments made by this section to change its taxable year for its first taxable year beginning after July 10, 1989 —

(A) such change shall be treated as initiated by the taxpayer.

(B) such change shall be treated as having been made with the consent of the Secretary of the Treasury or his delegate, and

(C) if, by reason of such change, any United States person is required to include in gross income for 1 taxable year amounts attributable to 2 taxable years of such foreign corporation, the amount which would otherwise be required to be included in gross income for such 1 taxable year by reason of the short taxable year of the foreign corporation resulting from such change shall be included in gross income ratably over the 4-taxable-year period beginning with such 1 taxable year.

SEC. 7402. LIMITATION ON THE USE OF DECONSOLIDATION TO AVOID FOREIGN TAX CREDIT LIMITATIONS.

(a) GENERAL RULE. —Section 904 (relating to limitations on foreign tax credit) is amended by redesignating subsection (i) as subsection (j) and by inserting after subsection (h) the following new subsection:

“(i) LIMITATION ON USE OF DECONSOLIDATION TO AVOID FOREIGN TAX CREDIT LIMITATIONS. —If 2 or more domestic corporations would be members of the same affiliated group if —

“(1) section 1504(b) were applied without regard to the exceptions contained therein, and

“(2) the constructive ownership rules of section 1563(e) applied for purposes of section 1504(a),

the Secretary may by regulations provide for resourcing the income of any of such corporations or for modifications to the consolidated return regulations to the extent that such resourcing or modifications are necessary to prevent the avoidance of the provisions of this subpart.”

(b) EFFECTIVE DATE. —The amendment made by subsection (a) shall apply to taxable years beginning after July 10, 1989.

SEC. 7403. INFORMATION WITH RESPECT TO CERTAIN FOREIGN-OWNED CORPORATIONS.

(a) 25-PERCENT FOREIGN-OWNED CORPORATIONS REQUIRED TO REPORT. —

(1) Paragraph (2) of section 6038A(a) is amended to read as follows:

“(2) is 25-percent foreign owned.”

(2) Subsection (c) of section 6038A is amended to read as follows:

“(c) DEFINITIONS. —For purposes of this section —

“(1) 25-PERCENT FOREIGN-OWNED. —A corporation is 25 percent foreign-owned if at least 25 percent of —

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

“(B) the total value of all classes of stock of such corporation,

is owned at any time during the taxable year by 1 foreign person (hereinafter in this section referred to as a “25-percent foreign shareholder”).

“(2) RELATED PARTY. —The term ‘related party’ means —

“(A) any 25-percent foreign shareholder of the reporting corporation,

“(B) any person who is related (within the meaning of section 267(b) or 707(b)(1)) to the reporting corporation or to a 25-percent foreign shareholder of the reporting corporation, and

“(C) any other person who is related (within the meaning of section 482) to the reporting corporation.

“(4) FOREIGN PERSON. —The term ‘foreign person’ means any person who is not a United States person. For purposes of the preceding sentence, the term ‘United States person’ has the meaning given to such term by section 7701(a)(30), except that any individual who is a citizen of any possession of the United States (but not otherwise a citizen of the United States) and who is not a resident of the United States shall not be treated as a United States person.

“(5) RECORDS. —The term ‘records’ includes any books, papers, or other data.

“(6) SECTION 318 TO APPLY. —Section 318 shall apply for purposes of paragraphs (1) and (2), except that —

“(A) ‘10 percent’ shall be substituted for ‘50 percent’ in section 318(a)(2)(C), and

“(B) subparagraphs (A), (B), and (C) of section 318(a)(3) shall not be applied so as to consider a United States person as owning stock which is owned by a person who is not a United States person.”

(b) U.S. RECORDKEEPING REQUIREMENTS. —Subsection (a) of section 6038A is amended by inserting before the period at the end thereof the following: “and such corporation shall maintain (in the location, in the manner, and to the extent prescribed in regulations) such records as may be appropriate to determine the correct treatment of transactions with related parties as the Secretary shall by regulations prescribe (or shall cause another person to so maintain such records)”.

(c) INCREASE IN PENALTY. —Subsection (d) of section 6038A is amended to read as follows:

“(d) PENALTY FOR FAILURE TO FURNISH INFORMATION OR MAINTAIN RECORDS. —

“(1) IN GENERAL. —If a reporting corporation —

“(A) fails to furnish (within the time prescribed by regulations) any information described in subsection (b), or

“(B) fails to maintain (or cause another to maintain) records as required by subsection (a),

such corporation shall pay a penalty of \$10,000 for each taxable year with respect to which such failure occurs.

“(2) INCREASE IN PENALTY WHERE FAILURE CONTINUES AFTER NOTIFICATION. —If any failure described in paragraph (1) continues for more than 90 days after the day on which the Secretary mails notice of such failure to the reporting corporation, such corporation shall pay a penalty (in addition to the amount required under paragraph (1)) of \$10,000 for each 30-day period (or fraction thereof) during which such failure continues after the expiration of such 90-day period.

“(3) REASONABLE CAUSE. —For purposes of this subsection, the time prescribed by regulations to furnish information or maintain records (and the beginning of the 90-day period after notice by the Secretary) shall be treated as not earlier than the last day on which (as shown to the satisfaction of the Secretary) reasonable cause existed for failure to furnish the information or maintain the records.”

(d) ENFORCEMENT OF INFORMATION REQUESTS. —Section 6038A is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

“(e) ENFORCEMENT OF REQUESTS FOR CERTAIN RECORDS. —

“(1) AGREEMENT TO TREAT CORPORATION AS AGENT. —The rules of paragraph (3) shall apply to any transaction between the reporting corporation and any related party who is a foreign person unless such related party agrees (in such manner and at such time as the Secretary shall prescribe) to authorize the reporting corporation to act as such related party's limited agent solely for purposes of applying sections 7602, 7603, and 7604 with respect to any request by the Secretary to examine records or produce testimony related to any such transaction or with respect to any summons by the Secretary for such records or testimony. The appearance of persons or production of records by reason of the reporting corporation being such an agent shall not subject such persons or records to legal process for any purpose other than determining the correct treatment under this title of any transaction between the reporting corporation and such related party.

“(2) RULES WHERE INFORMATION NOT FURNISHED. —If —

“(A) for purposes of determining the correct treatment under this title of any transaction between the reporting corporation and a related party who is a foreign person, the Secretary issues a summons to such corporation to produce (either directly or as agent for such related party) any records or testimony.

“(B) such summons is not quashed in a proceeding begun under paragraph (4) and is not determined to be invalid in a proceeding begun under section 7604(b) to enforce such summons and,

“(C) the reporting corporation does not substantially comply in a timely manner with such summons and the Secretary has sent by certified or registered mail a notice to such reporting corporation that such reporting corporation has not so substantially complied,

the Secretary may apply the rules of paragraph (3) with respect to such transaction (whether or not the Secretary begins a proceeding to enforce such summons). If the reporting corporation fails to maintain (or cause another to maintain) records as required by subsection (a), and by reason of that failure, the summons is quashed in a proceeding described in subparagraph (B) or the reporting corporation is not able to provide the records requested in the summons, the Secretary may apply the rules of paragraph (3) with respect to any transaction to which the records relate.

“(3) APPLICABLE RULES IN CASES OF NONCOMPLIANCE. —If the rules of this paragraph apply to any transaction —

“(A) the amount of the deduction allowed under subtitle A for any amount paid or incurred by the reporting corporation to the related party in connection with such transaction, and

“(B) the cost to the reporting corporation of any property acquired in such transaction from the related party (or transferred by such corporation in such transaction to the related party),

shall be the amount determined by the Secretary in the Secretary's sole discretion from the Secretary's own knowledge or from such information as the Secretary may obtain through testimony or otherwise.

“(4) JUDICIAL PROCEEDINGS. —

“(A) PROCEEDINGS TO QUASH. —Notwithstanding any law or rule of law, any reporting corporation to which the Secretary issues a summons referred to in paragraph (2)(A) shall have the right to begin a proceeding to quash such summons not later than the 90th day after such summons was issued. In any such proceeding, the Secretary may seek to compel compliance with such summons.

“(B) REVIEW OF SECRETARIAL DETERMINATION OF NONCOMPLIANCE. —Notwithstanding any law or rule of law, any reporting corporation which has been notified by the Secretary that the

Secretary has determined that such corporation has not substantially complied with a summons referred to in paragraph (2) shall have the right to begin a proceeding to review such determination not later than the 90th day after the day on which the notice referred to in paragraph (2)(C) was mailed. If such a proceeding is not begun on or before such 90th day, such determination by the Secretary shall be binding and shall not be reviewed by any court.

“(C) JURISDICTION. —The United States district court for the district in which the person (to whom the summons is issued) resides or is found shall have jurisdiction to hear any proceeding brought under subparagraph (A) or (B). Any order or other determination in such a proceeding shall be treated as a final order which may be appealed.

“(D) SUSPENSION OF STATUTE OF LIMITATIONS. —If the reporting corporation brings an action under subparagraph (A) or (B), the running of any period of limitations under section 6501 (relating to assessment and collection of tax) or under section 6531 (relating to criminal prosecutions) with respect to any transaction to which the summons relates shall be suspended for the period during which such proceeding, and appeals therein, are pending. In no event shall any such period expire before the 90th day after the day on which there is a final determination in such proceeding.”

(e) EFFECTIVE DATE. —The amendments made by this section shall apply to taxable years beginning after July 10, 1989.

SEC. 7404. REPEAL OF SPECIAL TREATMENT OF INTEREST ON CERTAIN FOREIGN LOANS.

(a) GENERAL RULE. —Paragraph (2) of section 1201(e) of the Tax Reform Act of 1986 is hereby repealed.

(b) EFFECTIVE DATE. —The repeal made by subsection (a) shall apply to taxable years beginning after December 31, 1989.

(c) EXCEPTION FOR CERTAIN TAXPAYERS WITH SUBSTANTIAL LOAN LOSS RESERVES. —

(1) IN GENERAL. —The repeal made by subsection (a) shall not apply to any taxpayer if, on any financial statement filed by such taxpayer for regulatory purposes with respect to any quarter ending during the period beginning on March 31, 1989, and ending on December 31, 1989, such taxpayer showed loss reserves against its qualified loans equal to at least 25 percent of the amount of such loans.

(2) DEFINITIONS AND SPECIAL RULES. —For purposes of this subsection —

(A) QUALIFIED LOAN. —The term “qualified loan” has the meaning given such term by section 1201(e)(2)(H) of the Tax Reform Act of 1986 (as in effect before its repeal by subsection (a)).

(B) PARENT-SUBSIDIARY CONTROLLED GROUPS. —In the case of any taxpayer which is a member of a parent-subsidiary controlled group (as defined in section 585(c)(5)(A)), this subsection shall be applied by treating all members of such group as 1 taxpayer.

Subtitle E —Excise Tax Provisions

SEC. 7501. 1-YEAR SUSPENSION OF AUTOMATIC REDUCTION IN AVIATION-RELATED TAXES.

(a) **IN GENERAL.** —Subsection (a) of section 4283 (relating to reduction in aviation-related taxes in certain cases) is amended by striking “1990” and inserting “1991”.

(b) **CONFORMING AMENDMENTS.** —

(1) Clause (i) of section 4283(b)(1)(A) is amended by striking “1988 and 1989” and inserting “1989 and 1990”.

(2) Paragraph (3) of section 4283(b) is amended —

(A) by striking “1990” and inserting “1991”, and

(B) by striking “1989” and inserting “1990”.

(3) Subsection (q) of section 6427 is amended by striking “1990” each place it appears and inserting “1991”.

You have reached the end of Part 01. To reach other parts, please use NEXT.