DESCRIPTION OF THE CHAIRMAN'S MODIFICATION TO THE "IRAN SANCTIONS ACT OF 2008"

Scheduled for Markup
by the
Senate Committee on Finance
on June 18, 2008

I. Introduction

This document provides a description of the Chairman's modification to the provisions of the "Iran Sanctions Act of 2008," which is scheduled to be marked up by the Senate Committee on Finance on June 18, 2008.

II. Modifications to the Original Bill

A. Elimination of Certain Tax Incentives for Oil Companies Investing in Iran

Present Law

Geological and geophysical expenditures ("G&G costs") are incurred by a taxpayer for the purpose of obtaining and accumulating data that will serve as the basis for the acquisition and retention of mineral properties by taxpayers exploring for minerals. G&G costs incurred by independent producers and smaller integrated[1] oil companies in connection with oil and gas exploration in the United States may generally be amortized over two years.[2] Major integrated oil companies are required to amortize all G&G costs over seven years.[3] For these purposes, a major integrated oil company, with respect to any taxable year, is a producer of crude oil which has an average daily worldwide production of crude oil of at least 500,000 barrels for the taxable year, had gross receipts in excess of one billion dollars for its last taxable year ending during the calendar year 2005, and generally has an ownership interest in a crude oil refiner of 15 percent or more.[4] In the case of abandoned property, any remaining basis may not be recovered in the year of abandonment as all basis is recovered over the applicable amortization period.

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[1] Generally, an integrated oil company is a producer of crude oil that engages in the refining or retail sale of petroleum products in excess of certain threshold amounts.

[2] Sec. 167(h)(1).

[3] Sec. 167(h)(5).

[4] Id.

Description of Proposal

For taxpayers on whom certain economic sanctions for investing in Iran are imposed, or on whose affiliates such sanctions would have been imposed if such affiliates were U.S. persons, G&G costs paid or incurred in connection with the exploration for, or development of, oil or gas within the United States must be amortized over 10 years. For this purpose, the economic sanctions requiring the extended G&G amortization consist of (1) sanctions under section 5(a) of the Iran Sanction Act of 1996 and (2) sanctions described in Executive Orders 12959[5] or 13059,[6] or under any other prohibition on transactions with respect to Iran imposed under the authority of the International Emergency Economic Power Act.[7] For purposes of this proposal, an affiliate is defined as a member of an affiliated group under section 1504(a) determined using a 50 percent (instead of 80 percent) voting and value test and including insurance companies, foreign corporations, and corporations with respect to which an election under section 936 is in effect.

If the sanctions with respect to the taxpayer are lifted (either because the taxpayer comes into compliance or because the sanctions regime terminates), the taxpayer may elect to treat any remaining unamortized G&G costs incurred prior to or during the sanction period as incurred on the date the sanctions are lifted and amortize them over the period described in section 167(h)(1) or (h)(5), as the case may be. Taxpayers not making an election must continue to amortize those expenses over the ten year period. The proposal terminates five years after the date of enactment.

Example 1

Taxpayer A, a domestic corporation with a foreign parent, FP, incurs $5 million of G&G costs in Year 1 and begins amortizing the costs over seven years under section 167(h)(5). In Year 2, FP invests in Iran and sanctions under section 5(a) of the Iran Sanctions Act of 1996 would be imposed if Foreign Parent were a domestic company. As a result, Taxpayer A must amortize any remaining unamortized G&G costs that were incurred in Year 1 over a 10 year period beginning in Year 2 (applying the half-year convention rule of section 167(h)(2)).

In Year 4, FP abandons its investment in Iran and is no longer subject to sanctions. Taxpayer A may either continue to amortize the costs over the remaining 10 years or treat the remaining costs as incurred in Year 4 and recover the costs over seven years under section 167(h)(5).

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[5] 60 Fed. Reg. 24,757 (May 9, 1995).

[6] 62 Fed. Reg. 44,531 (Aug. 21, 1997).

[7] 50 U.S.C. sec. 1701 et seq.

Example 2

Assume the same facts as Example 1, except that instead of FP abandoning its investment in Iran, the sanctions are no longer in effect in Year 6 due to the termination of the Iran Counter-Proliferation Act of 2008. In this case, Taxpayer A may either continue to amortize the costs over the remaining 10 years or treat the costs as incurred in Year 6 and recover the costs over seven years under section 167(h)(5).

Example 3

Taxpayer B, a domestic corporation, and Taxpayer C, a foreign corporation, have a common foreign parent. In Year 1, Taxpayer C invests in Iran and sanctions under section 5(a) of the Iran Sanctions Act of 1996 would be imposed if Taxpayer C were a domestic company. In Year 3, Taxpayer B incurs $5 million of G&G costs and absent this proposal would amortize the costs over two years under section 167(h)(1). Under the proposal, Taxpayer B must amortize the G&G costs over a 10 year period beginning in Year 3 (applying the half-year convention rule of section 167(h)(2)).
In Year 4, Taxpayer C abandons its investment in Iran and is no longer subject to sanctions. Taxpayer B may either continue to amortize the costs over the remaining 10 years or treat the remaining costs as incurred in Year 4 and recover the costs over two years under section 167(h)(1).

Effective Date

The proposal is effective for G&G costs paid or incurred on or after January 1, 2009.

B. Sense of Congress

1. Provision expressing the sense of Congress regarding exports or imports of petroleum products to and from Iran

Present Law

Current law does not discourage foreign governments or entities from exporting or importing refined petroleum products to or from Iran. But current law requires the President to impose sanctions on domestic and foreign state-owned and private entities that invest more than $20 million in one year in Iran’s petroleum or natural gas sectors.

Description of Proposal

The modification includes a provision expressing the sense of Congress that foreign governments should encourage their state-owned and private entities to cease (1) exports to and imports from Iran of refined petroleum products, and (2) investments in Iran's energy sector.

2. Two provisions expressing the sense of Congress regarding United Nations (U.N.) Security Council Resolutions relating to Iran

Present Law

Since 2006, the United States has supported several U.N. Security Council Resolutions, including Resolutions 1737, 1747, and 1803, which sanction Iran for its failure to suspend uranium enrichment-related and reprocessing activities.

Description of Proposal

The modification introduces two provisions expressing the sense of Congress regarding U.N. Security Council Resolutions relating to Iran. The first provision states that it is the sense of Congress that Iran should comply fully with its obligations under U.N. Security Council Resolutions 1737, 1747, 1803, and any subsequent Security Council Resolutions. The second provision states that it is the sense of Congress that the U.N. Security Council should take measures beyond Resolutions 1737, 1747, and 1803 to tighten sanctions on Iran until such time that Iran halts its nuclear enrichment program.

3. Provision expressing the sense of Congress regarding Iran's ability to conduct international transactions

Present Law

Under current law, U.S. banks may handle "U-turn" transactions with certain Iranian state-owned banks. U-turn transactions are those transactions where U.S. banks cover payments involving Iran that are by order of a third country bank for payment to another third country bank. While existing U.S. law prohibits U.S. depository institutions from servicing accounts of the Government of Iran or persons in Iran, it does not prohibit foreign banks that operate in U.S. currency from engaging in dollar transactions with Iranian institutions.

Description of Proposal

The modification adds a provision expressing the sense of Congress that the United States should pursue measures to (1) restrict Iran's ability to conduct international transactions, including by prohibiting banks in the United States from handling indirect transactions with Iranian state-owned banks; and (2) prohibit institutions that operate in U.S. currency from engaging in dollar transactions with Iranian institutions.

4. Provision expressing the sense of Congress regarding divestment of federal and state pension plans

Present Law

Under current law, federal and state pension plans are not required to divest assets or holdings in entities that invest in Iran's energy sector.

Description of Proposal

The modification adds a provision expressing the sense of Congress that Federal and State pension plans should divest assets and holdings in entities that have invested or invest in the future in Iran's energy sector.