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2d Session

HOUSE OF REPRESENTATIVES

{ REPORT  
115-958

PROTECTING FAMILY AND SMALL BUSINESS  
TAX CUTS ACT OF 2018

---

R E P O R T

OF THE

COMMITTEE ON WAYS AND MEANS  
HOUSE OF REPRESENTATIVES

ON

H.R. 6760

together with

DISSENTING VIEWS

[Including cost estimate of the Congressional Budget Office]



SEPTEMBER 24, 2018.—Committed to the Committee of the Whole House  
on the State of the Union and ordered to be printed

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PROTECTING FAMILY AND SMALL BUSINESS TAX CUTS  
ACT OF 2018

SEPTEMBER 24, 2018.—Committed to the Committee of the Whole House on the  
State of the Union and ordered to be printed

Mr. BRADY of Texas, from the Committee on Ways and Means,  
submitted the following

R E P O R T

together with

DISSENTING VIEWS

[To accompany H.R. 6760]

[Including cost estimate of the Congressional Budget Office]

The Committee on Ways and Means, to whom was referred the bill (H.R. 6760) to amend the Internal Revenue Code of 1986 to make permanent certain provisions of the Tax Cuts and Jobs Act affecting individuals, families, and small businesses, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Strike all after the enacting clause and insert the following:

**SECTION 1. SHORT TITLE, ETC.**

(a) **SHORT TITLE.**—This Act may be cited as the “Protecting Family and Small Business Tax Cuts Act of 2018”.

(b) **AMENDMENT OF 1986 CODE.**—Except as otherwise expressly provided, whenever in this Act 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) **REFERENCES TO THE TAX CUTS AND JOBS ACT.**—Title I of Public Law 115-97 may be cited as the “Tax Cuts and Jobs Act”.

(d) **TABLE OF CONTENTS.**—The table of contents of this Act is as follows:

Sec. 1. Short title, etc.

TITLE I—INDIVIDUAL REFORM MADE PERMANENT

Subtitle A—Rate Reform

Sec. 101. Modification of rates.

Subtitle B—Deduction for Qualified Business Income of Pass-thru Entities

- Sec. 111. Deduction for qualified business income.  
 Sec. 112. Limitation on losses for taxpayers other than corporations.

Subtitle C—Tax Benefits for Families and Individuals

- Sec. 121. Increase in standard deduction.  
 Sec. 122. Increase in and modification of child tax credit.  
 Sec. 123. Increased limitation for certain charitable contributions.  
 Sec. 124. Increased contributions to ABLE accounts.  
 Sec. 125. Rollovers to ABLE programs from 529 programs.  
 Sec. 126. Treatment of certain individuals performing services in the Sinai Peninsula of Egypt.  
 Sec. 127. Extension of reduction in threshold for medical expense deduction.

Subtitle D—Education

- Sec. 131. Treatment of student loans discharged on account of death or disability.

Subtitle E—Deductions and Exclusions

- Sec. 141. Repeal of deduction for personal exemptions.  
 Sec. 142. Limitation on deduction for State and local, etc. taxes.  
 Sec. 143. Limitation on deduction for qualified residence interest.  
 Sec. 144. Modification of deduction for personal casualty losses.  
 Sec. 145. Termination of miscellaneous itemized deductions.  
 Sec. 146. Repeal of overall limitation on itemized deductions.  
 Sec. 147. Termination of exclusion for qualified bicycle commuting reimbursement.  
 Sec. 148. Qualified moving expense reimbursement exclusion limited to members of Armed Forces.  
 Sec. 149. Deduction for moving expenses limited to members of Armed Forces.  
 Sec. 150. Limitation on wagering losses.

Subtitle F—Increase in Estate and Gift Tax Exemption

- Sec. 151. Increase in estate and gift tax exemption.

TITLE II—INCREASED EXEMPTION FOR ALTERNATIVE MINIMUM TAX MADE PERMANENT

- Sec. 201. Increased exemption for individuals.

## TITLE I—INDIVIDUAL REFORM MADE PERMANENT

### Subtitle A—Rate Reform

**SEC. 101. MODIFICATION OF RATES.**

(a) **MARRIED INDIVIDUALS FILING JOINT RETURNS AND SURVIVING SPOUSES.**—Section 1(a) is amended by striking the table contained therein and inserting the following:

| "If taxable income is:                      | The tax is:  |
|---|--|
| Not over \$19,050 .....                     | 10% of taxable income.                             |
| Over \$19,050 but not over \$77,400 .....   | \$1,905, plus 12% of the excess over \$19,050.     |
| Over \$77,400 but not over \$165,000 .....  | \$8,907, plus 22% of the excess over \$77,400.     |
| Over \$165,000 but not over \$315,000 ..... | \$28,179, plus 24% of the excess over \$165,000.   |
| Over \$315,000 but not over \$400,000 ..... | \$64,179, plus 32% of the excess over \$315,000.   |
| Over \$400,000 but not over \$600,000 ..... | \$91,379, plus 35% of the excess over \$400,000.   |
| Over \$600,000 .....                        | \$161,379, plus 37% of the excess over \$600,000." |

(b) **HEAD OF HOUSEHOLDS.**—Section 1(b) is amended by striking the table contained therein and inserting the following:

| "If taxable income is:                      | The tax is:  |
|---|--|
| Not over \$13,600 .....                     | 10% of taxable income.                             |
| Over \$13,600 but not over \$51,800 .....   | \$1,360, plus 12% of the excess over \$13,600.     |
| Over \$51,800 but not over \$82,500 .....   | \$5,944, plus 22% of the excess over \$51,800.     |
| Over \$82,500 but not over \$157,500 .....  | \$12,698, plus 24% of the excess over \$82,500.    |
| Over \$157,500 but not over \$200,000 ..... | \$30,698, plus 32% of the excess over \$157,500.   |
| Over \$200,000 but not over \$500,000 ..... | \$44,298, plus 35% of the excess over \$200,000.   |
| Over \$500,000 .....                        | \$149,298, plus 37% of the excess over \$500,000." |

(c) **UNMARRIED INDIVIDUALS OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLD.**—Section 1(c) is amended by striking the table contained therein and inserting the following:

| "If taxable income is:                      | The tax is:   |
|---|---|
| Not over \$9,525 .....                      | 10% of taxable income.                                |
| Over \$9,525 but not over \$38,700 .....    | \$952.50, plus 12% of the excess over \$9,525.        |
| Over \$38,700 but not over \$82,500 .....   | \$4,453.50, plus 22% of the excess over \$38,700.     |
| Over \$82,500 but not over \$157,500 .....  | \$14,089.50, plus 24% of the excess over \$82,500.    |
| Over \$157,500 but not over \$200,000 ..... | \$32,089.50, plus 32% of the excess over \$157,500.   |
| Over \$200,000 but not over \$500,000 ..... | \$45,689.50, plus 35% of the excess over \$200,000.   |
| Over \$500,000 .....                        | \$150,689.50, plus 37% of the excess over \$500,000." |

(d) **MARRIED INDIVIDUALS FILING SEPARATE RETURNS.**—Section 1(d) is amended by striking the table contained therein and inserting the following:

| "If taxable income is:                      | The tax is:  |
|---|--|
| Not over \$9,525 .....                      | 10% of taxable income.                               |
| Over \$9,525 but not over \$38,700 .....    | \$952.50, plus 12% of the excess over \$9,525.       |
| Over \$38,700 but not over \$82,500 .....   | \$4,453.50, plus 22% of the excess over \$38,700.    |
| Over \$82,500 but not over \$157,500 .....  | \$14,089.50, plus 24% of the excess over \$82,500.   |
| Over \$157,500 but not over \$200,000 ..... | \$32,089.50, plus 32% of the excess over \$157,500.  |
| Over \$200,000 but not over \$300,000 ..... | \$45,689.50, plus 35% of the excess over \$200,000.  |
| Over \$300,000 .....                        | \$80,689.50, plus 37% of the excess over \$300,000." |

(e) **ESTATES AND TRUSTS.**—Section 1(e) is amended by striking the table contained therein and inserting the following:

| "If taxable income is:                   | The tax is:  |
|--|--|
| Not over \$2,550 .....                   | 10% of taxable income.                             |
| Over \$2,550 but not over \$9,150 .....  | \$255, plus 24% of the excess over \$2,550.        |
| Over \$9,150 but not over \$12,500 ..... | \$1,839, plus 35% of the excess over \$9,150.      |
| Over \$12,500 .....                      | \$3,011.50, plus 37% of the excess over \$12,500." |

(f) **INFLATION ADJUSTMENTS.**—Section 1(f) is amended—

(1) by striking "1993" in paragraph (1) and inserting "2018",

(2) by amending paragraph (2)(A) to read as follows:

"(A) by increasing the minimum and maximum dollar amounts for each bracket for which a tax is imposed under such table by the cost-of-living adjustment for such calendar year, determined under this subsection for such calendar year by substituting '2017' for '2016' in paragraph (3)(A)(ii),"

(3) in paragraph (7)(B), by striking all that precedes "(other than with respect to" and inserting the following:

"(B) **SPECIAL RULE.**—In the case of a table prescribed in lieu of the table contained in subsection (b), (c), or (d), subparagraph (A)",

(4) by striking paragraph (8), and

(5) in the heading, by striking "PHASEOUT OF MARRIAGE PENALTY IN 15-PERCENT BRACKET; ADJUSTMENTS" and inserting "ADJUSTMENTS".

(g) **SPECIAL RULES FOR CERTAIN CHILDREN WITH UNEARNED INCOME.**—

(1) **IN GENERAL.**—Section 1(g) is amended by striking all that precedes paragraph (2) and inserting the following:

"(g) **SPECIAL RULES FOR CERTAIN CHILDREN WITH UNEARNED INCOME.**—

"(1) **IN GENERAL.**—In the case of any child to whom this subsection applies—

"(A) **MODIFICATIONS TO APPLICABLE RATE BRACKETS.**—In determining the amount of tax imposed by this section for the taxable year on such child, the income tax table otherwise applicable under this section to such child shall be applied with the following modifications:

"(i) **24-PERCENT BRACKET.**—The maximum taxable income which is taxed at a rate below 24 percent shall not be more than the sum of—

"(I) the earned taxable income of such child, plus

"(II) the minimum taxable income for the 24-percent bracket in the table under subsection (e) (as adjusted under subsection (f) for the taxable year.

"(ii) **35-PERCENT BRACKET.**—The maximum taxable income which is taxed at a rate below 35 percent shall not be more than the sum of—

"(I) the earned taxable income of such child, plus

"(II) the minimum taxable income for the 35-percent bracket in the table under subsection (e) (as adjusted under subsection (f) for the taxable year.

- “(iii) 37-PERCENT BRACKET.—The maximum taxable income which is taxed at a rate below 37 percent shall not be more than the sum of—
- “(I) the earned taxable income of such child, plus
- “(II) the minimum taxable income for the 37-percent bracket in the table under subsection (e) (as adjusted under subsection (f)) for the taxable year.
- “(B) COORDINATION WITH CAPITAL GAINS RATES.—For purposes of applying section 1(h)—
- “(i) the maximum zero rate amount shall not be more than the sum of—
- “(I) the earned taxable income of such child, plus
- “(II) the amount in effect under subsection (h)(13) for the taxable year, and
- “(ii) the maximum 15-percent rate amount shall not be more than the sum of—
- “(I) the earned taxable income of such child, plus
- “(II) the amount in effect under subsection (h)(12)(D) for the taxable year.”.
- (2) EARNED TAXABLE INCOME.—Section 1(g)(3) is amended to read as follows:
- “(3) EARNED TAXABLE INCOME.—For purposes of this subsection, the term ‘earned taxable income’ means, with respect to any child for any taxable year, the taxable income of such child reduced (but not below zero) by the net unearned income of such child.”.
- (3) CONFORMING AMENDMENT.—So much of paragraph (5) of section 1(g) as precedes subparagraph (A) thereof is amended to read as follows:
- “(5) SPECIAL RULES FOR DETERMINING PARENT ELIGIBLE TO MAKE ELECTION.—For purposes of paragraph (7), the parent referred to in subparagraph (A)(iv) thereof is—”.
- (h) APPLICATION OF INCOME TAX BRACKETS TO CAPITAL GAINS BRACKETS.—Section 1(h) is amended—
- (1) in paragraph (1)(B)(i), by striking “25 percent” and inserting “22 percent”,
- (2) in paragraph (1)(C)(ii)(I), by striking “which would (without regard to this paragraph) be taxed at a rate below 39.6 percent” and inserting “below the maximum 15-percent rate amount”, and
- (3) by adding at the end the following new paragraphs:
- “(12) MAXIMUM 15-PERCENT RATE AMOUNT DEFINED.—For purposes of this subsection, the maximum 15-percent rate amount shall be—
- “(A) in the case of a joint return or surviving spouse (as defined in section 2(a)), \$479,000 (½ such amount in the case of a married individual filing a separate return),
- “(B) in the case of an individual who is the head of a household (as defined in section 2(b)), \$452,400,
- “(C) in the case of any other individual (other than an estate or trust), \$425,800, and
- “(D) in the case of an estate or trust, \$12,700.
- “(13) DETERMINATION OF 0 PERCENT RATE BRACKET FOR ESTATES AND TRUSTS.—In the case of any estate or trust, paragraph (1)(B) shall be applied by treating the amount determined in clause (i) thereof as being equal to \$2,600.
- “(14) INFLATION ADJUSTMENT.—
- “(A) IN GENERAL.—In the case of any taxable year beginning after 2018, each of the dollar amounts in paragraphs (12) and (13) shall be increased by an amount equal to—
- “(i) such dollar amount, multiplied by
- “(ii) the cost-of-living adjustment determined under subsection (f)(3) for the calendar year in which the taxable year begins, determined by substituting ‘calendar year 2017’ for ‘calendar year 2016’ in subparagraph (A)(ii) thereof.
- “(B) ROUNDING.—If any increase under subparagraph (A) is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.”.
- (i) APPLICATION OF SECTION 15.—
- (1) IN GENERAL.—Subsection (a) of section 15 is amended by striking “If any rate of tax” and inserting “In the case of a corporation, if any rate of tax”.
- (2) CONFORMING AMENDMENTS.—
- (A) Section 15 is amended by striking subsections (d), (e), and (f).
- (B) Section 6013(c) is amended by striking “sections 15, 443, and 7851(a)(1)(A)” and inserting “section 443”.



(C) The heading of section 15 is amended by inserting “ON CORPORATIONS” after “EFFECT OF CHANGES”.

(D) The table of sections for part III of subchapter A of chapter 1 is amended by striking the item relating to section 15 and inserting the following new item:

“Sec. 15. Effect of changes on corporations.”.

(j) CONFORMING AMENDMENTS.—

(1) Section 1 is amended by striking subsections (i) and (j).

(2) Section 3402(q)(1) is amended by striking “third lowest” and inserting “fourth lowest”.

(k) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

(2) APPLICATION OF SECTION 15.—Section 15 of the Internal Revenue Code of 1986 shall not apply to any change in a rate of tax by reason of—

(A) section 1(j) of such Code (as in effect before its repeal by this section),

or

(B) any amendment made by this Act.

## **Subtitle B—Deduction for Qualified Business Income of Pass-thru Entities**

### **SEC. 111. DEDUCTION FOR QUALIFIED BUSINESS INCOME.**

(a) IN GENERAL.—Section 199A is amended by striking subsection (i).

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

### **SEC. 112. LIMITATION ON LOSSES FOR TAXPAYERS OTHER THAN CORPORATIONS.**

(a) IN GENERAL.—Section 461 is amended—

(1) by amending subsection (l)(1) to read as follows:

“(1) LIMITATION.—In the case of a taxpayer other than a corporation, any excess business loss of the taxpayer for the taxable year shall not be allowed,” and

(2) by striking subsection (j) and redesignating subsections (k) and (l) (as amended) as subsections (j) and (k), respectively.

(b) CONFORMING AMENDMENTS.—

(1) Section 58(a)(2)(A) is amended by striking “461(k)” and inserting “461(j)”.

(2) Section 461(i)(4) is amended by striking “subsection (k)” and inserting “subsection (j)”.

(3) Section 464(d)(2)(B)(iii) is amended by striking “section 461(k)(2)(E)” and inserting “section 461(j)(2)(E)”.

(4) Subparagraphs (B) and (C) of section 1256(e)(3) are each amended by striking “section 461(k)(4)” and inserting “section 461(j)(4)”.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

## **Subtitle C—Tax Benefits for Families and Individuals**

### **SEC. 121. INCREASE IN STANDARD DEDUCTION.**

(a) IN GENERAL.—Section 63(c)(2) is amended—

(1) by striking “\$4,400” in subparagraph (B) and inserting “\$18,000”, and

(2) by striking “\$3,000” in subparagraph (C) and inserting “\$12,000”.

(b) INFLATION ADJUSTMENT.—Section 63(c)(4) is amended to read as follows:

“(4) ADJUSTMENTS FOR INFLATION.—

“(A) IN GENERAL.—In the case of a taxable year beginning after 2018, each dollar amount in paragraph (2)(B), (2)(C), or (5) or subsection (f) shall be increased by an amount equal to—

“(i) such dollar amount, multiplied by

“(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting for ‘2016’ in subparagraph (A)(ii) thereof—

“(1) in the case of the dollar amounts contained in paragraph (2)(B) or (2)(C), ‘2017’,

“(II) in the case of the dollar amounts contained in paragraph (5)(A) or subsection (f), ‘1987’, and

“(III) in the case of the dollar amount contained in paragraph (5)(B), ‘1997’.

“(B) ROUNDING.—If any increase under subparagraph (A) is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.”

(c) CONFORMING AMENDMENTS.—

(1) Section 1(f)(7)(A) is amended by striking “section 63(c)(4),”.

(2) Section 1(f)(7)(B) is amended by striking “sections 63(c)(4) and” and inserting “section”.

(3) Section 63(c) is amended by striking paragraph (7).

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 122. INCREASE IN AND MODIFICATION OF CHILD TAX CREDIT.**

(a) IN GENERAL.—Section 24 is amended by striking subsections (a), (b), and (c) and inserting the following new subsections:

“(a) ALLOWANCE OF CREDIT.—There shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to the sum of—

“(1) \$2,000 for each qualifying child of the taxpayer, and

“(2) \$500 for each qualifying dependent (other than a qualifying child) of the taxpayer.

“(b) LIMITATION BASED ON ADJUSTED GROSS INCOME.—The amount of the credit allowable under subsection (a) shall be reduced (but not below zero) by \$50 for each \$1,000 (or fraction thereof) by which the taxpayer’s modified adjusted gross income exceeds \$400,000 in the case of a joint return (\$200,000 in any other case). For purposes of the preceding sentence, the term “modified adjusted gross income” means adjusted gross income increased by any amount excluded from gross income under section 911, 931, or 933.

“(c) QUALIFYING CHILD; QUALIFYING DEPENDENT.—For purposes of this section—

“(1) QUALIFYING CHILD.—The term ‘qualifying child’ means any qualifying dependent of the taxpayer—

“(A) who is a qualifying child (as defined in section 7706(c)) of the taxpayer,

“(B) who has not attained age 17 at the close of the calendar year in which the taxable year of the taxpayer begins, and

“(C) whose name and social security number are included on the taxpayer’s return of tax for the taxable year.

“(2) QUALIFYING DEPENDENT.—The term ‘qualifying dependent’ means any dependent of the taxpayer (as defined in section 7706 without regard to all that follows ‘resident of the United States’ in section 7706(b)(3)(A)) whose name and TIN are included on the taxpayer’s return of tax for the taxable year.

“(3) SOCIAL SECURITY NUMBER DEFINED.—For purposes of this subsection, the term ‘social security number’ means, with respect to a return of tax, a social security number issued to an individual by the Social Security Administration, but only if the social security number is issued—

“(A) to a citizen of the United States or pursuant to subclause (I) (or that portion of subclause (III) that relates to subclause (I)) of section 205(c)(2)(B)(i) of the Social Security Act, and

“(B) on or before the due date of filing such return.”

(b) PORTION OF CREDIT REFUNDABLE.—

(1) IN GENERAL.—Section 24(d)(1)(A) is amended to read as follows:

“(A) the credit which would be allowed under this section determined—

“(i) by substituting ‘\$1,400’ for ‘\$2,000’ in subsection (a)(1),

“(ii) without regard to subsection (a)(2), and

“(iii) without regard to this subsection and the limitation under section 26(a), or”.

(2) MODIFICATION OF LIMITATION BASED ON EARNED INCOME.—Section 24(d)(1)(B)(i) is amended by striking “\$3,000” and inserting “\$2,500”.

(3) INFLATION ADJUSTMENT.—Section 24(d) is amended by inserting after paragraph (3) the following new paragraph:

“(4) ADJUSTMENT FOR INFLATION.—

“(A) IN GENERAL.—In the case of a taxable year beginning after 2018, the \$1,400 amount in paragraph (1)(A)(i) shall be increased by an amount equal to—

“(i) such dollar amount, multiplied by

“(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting ‘2017’ for ‘2016’ in subparagraph (A)(ii) thereof.

“(B) ROUNDING.—If any increase under subparagraph (A) is not a multiple of \$100, such increase shall be rounded to the next lowest multiple of \$100.

“(C) LIMITATION.—The amount of any increase under subparagraph (A) (after the application of subparagraph (B)) shall not exceed \$600.”.

(4) CONFORMING AMENDMENTS.—

(A) Section 24(e) is amended to read as follows:

“(e) TAXPAYER IDENTIFICATION REQUIREMENT.—No credit shall be allowed under this section if the identifying number of the taxpayer was issued after the due date for filing the return of tax for the taxable year.”.

(B) Section 24 is amended by striking subsection (h).

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 123. INCREASED LIMITATION FOR CERTAIN CHARITABLE CONTRIBUTIONS.**

(a) IN GENERAL.—Section 170(b)(1)(G) is amended to read as follows:

“(G) CASH CONTRIBUTIONS.—

“(i) IN GENERAL.—Any contribution of cash to an organization described in subparagraph (A) shall be allowed to the extent that the aggregate of such contributions does not exceed 60 percent of the taxpayer’s contribution base for the taxable year, reduced by the aggregate amount of contributions allowable under subparagraph (A) for such taxpayer for such year.

“(ii) CARRYOVER.—If the aggregate amount of contributions described in clause (i) exceeds the limitation of clause (i), such excess shall be treated (in a manner consistent with the rules of subsection (d)(1)) as a charitable contribution to which clause (i) applies in each of the 5 succeeding years in order of time.”.

(b) COORDINATION WITH LIMITATIONS ON OTHER CONTRIBUTIONS.—

(1) COORDINATION WITH 50 PERCENT LIMITATION.—Section 170(b)(1)(A) is amended by striking “Any charitable contribution” and inserting “Any charitable contribution other than a contribution described in subparagraph (G)”.

(2) COORDINATION WITH 30 PERCENT LIMITATION.—Section 170(b)(1)(B) is amended—

(A) in the matter preceding clause (i), by striking “to which subparagraph (A) applies” and inserting “to which subparagraph (A) or (G) applies”,

(B) by amending clause (ii) to read as follows:

“(ii) the excess of—

“(I) the sum of 50 percent of the taxpayer’s contribution base for the taxable year, plus so much of the amount of charitable contributions allowable under subparagraph (G) as does not exceed 10 percent of such contribution base, over

“(II) the amount of charitable contributions allowable under subparagraphs (A) and (G) (determined without regard to subparagraph (C)).”, and

(C) in the matter following clause (ii), by striking “(to which subparagraph (A) does not apply)” and inserting “(to which neither subparagraph (A) nor (G) applies)”.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to contributions made in taxable years beginning after December 31, 2017.

**SEC. 124. INCREASED CONTRIBUTIONS TO ABLE ACCOUNTS.**

(a) INCREASE IN LIMITATION FOR CONTRIBUTIONS FROM COMPENSATION OF INDIVIDUALS WITH DISABILITIES.—Section 529A(b)(2)(B)(ii) is amended by striking “before January 1, 2026”.

(b) ALLOWANCE OF SAVER’S CREDIT FOR ABLE CONTRIBUTIONS BY ACCOUNT HOLDER.—Section 25B(d)(1)(D) is amended by striking “made before January 1, 2026”.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 125. ROLLOVERS TO ABLE PROGRAMS FROM 529 PROGRAMS.**

(a) IN GENERAL.—Section 529(c)(3)(C)(i)(III) is amended by striking “before January 1, 2026”.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to distributions after December 31, 2017.

**SEC. 126. TREATMENT OF CERTAIN INDIVIDUALS PERFORMING SERVICES IN THE SINAI PENINSULA OF EGYPT.**

- (a) **IN GENERAL.**—Section 112(c)(2) is amended—
- (1) by striking “means any area” and inserting “means—  
“**(A)** any area”, and
  - (2) by striking the period at the end and inserting “, and  
“**(B)** the Sinai Peninsula of Egypt.”.
- (b) **PERIOD OF TREATMENT.**—Section 112(c)(3) is amended—
- (1) by striking “only if performed” and inserting “only if—  
“**(A)** in the case of an area described in paragraph (2)(A), such service is performed”, and
  - (2) by striking the period at the end and inserting “, and  
“**(B)** in the case of the area described in paragraph (2)(B), such service is performed during any period with respect to which one or more members of the Armed Forces of the United States are entitled to special pay under section 310 of title 37, United States Code (relating to special pay; duty subject to hostile fire or imminent danger), for service performed in such area.”.
- (c) **CONFORMING AMENDMENT.**—The Tax Cuts and Jobs Act is amended by striking section 11026.
- (d) **EFFECTIVE DATE.**—The amendments made by this section shall apply with respect to services performed on or after the date of the enactment of this Act.

**SEC. 127. EXTENSION OF REDUCTION IN THRESHOLD FOR MEDICAL EXPENSE DEDUCTION.**

- (a) **IN GENERAL.**—Section 213(a) is amended by inserting “(7.5 percent in the case of any taxable year beginning after December 31, 2018, and ending before January 1, 2021)” after “10 percent”.
- (b) **CONFORMING AMENDMENTS.**—
- (1) Section 56(b)(1) is amended by striking subparagraph (B) and by redesignating subparagraphs (C) through (F) as subparagraphs (B) through (E), respectively.
  - (2) Section 213 is amended by striking subsection (f).
- (c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 2018.

## Subtitle D—Education

**SEC. 131. TREATMENT OF STUDENT LOANS DISCHARGED ON ACCOUNT OF DEATH OR DISABILITY.**

- (a) **IN GENERAL.**—Section 108(f)(5) is amended by striking “after December 31, 2017, and before January 1, 2026”.
- (b) **EFFECTIVE DATE.**—The amendment made by this section shall apply to discharges of indebtedness after December 31, 2017.

## Subtitle E—Deductions and Exclusions

**SEC. 141. REPEAL OF DEDUCTION FOR PERSONAL EXEMPTIONS.**

- (a) **IN GENERAL.**—Part V of subchapter B of chapter 1 is hereby repealed.
- (b) **DEFINITION OF DEPENDENT RETAINED.**—Section 152, prior to the repeal made by subsection (a), is hereby redesignated as section 7706 and moved to the end of chapter 79.
- (c) **APPLICATION TO TRUSTS AND ESTATES.**—Section 642(b) is amended—
- (1) in paragraph (2)(C)—
    - (A) in clause (i), by striking “the exemption amount under section 151(d)” and all that follows through the period at the end and inserting “the dollar amount in effect under section 7706(d)(1)(B).”, and
    - (B) by striking clause (iii),
  - (2) by striking paragraph (3), and
  - (3) by striking “DEDUCTION FOR PERSONAL EXEMPTION” in the heading thereof and inserting “BASIC DEDUCTION”.
- (d) **APPLICATION TO NONRESIDENT ALIENS.**—Section 873(b) is amended by striking paragraph (3).
- (e) **MODIFICATION OF RETURN REQUIREMENT.**—
- (1) **IN GENERAL.**—Section 6012(a)(1) is amended to read as follows:
    - (1) Every individual who has gross income for the taxable year, except that a return shall not be required of—

“(A) an individual who is not married (determined by applying section 7703) and who has gross income for the taxable year which does not exceed the standard deduction applicable to such individual for such taxable year under section 63, or

“(B) an individual entitled to make a joint return if—

“(i) the gross income of such individual, when combined with the gross income of such individual’s spouse, for the taxable year does not exceed the standard deduction which would be applicable for such taxable year under section 63 if such individual and such individual’s spouse made a joint return,

“(ii) such individual’s spouse does not make a separate return, and

“(iii) neither such individual nor such individual’s spouse is an individual described in section 63(c)(4) who has income (other than earned income) in excess of the amount in effect under section 63(c)(4)(A).”

(2) BANKRUPTCY ESTATES.—Section 6012(a)(8) is amended by striking “the sum of the exemption amount plus”.

(3) CONFORMING AMENDMENT.—Section 6012 is amended by striking subsection (f).

(f) CONFORMING AMENDMENTS.—

(1) Section 1(f)(7), as amended by section 121, is amended—

(A) by striking “, section 68(b)(2) or section 151(d)(4)” in subparagraph (A) and inserting “or section 68(b)(2)”, and

(B) by striking “(other than with respect to section 151(d)(4)(A))” in subparagraph (B).

(2) Section 1(g)(5)(A) is amended by striking “section 152(e)” and inserting “section 7706(e)”.

(3) Section 2(a)(1)(B) is amended—

(A) by striking “section 152” and inserting “section 7706”, and

(B) by striking “with respect to whom the taxpayer is entitled to a deduction for the taxable year under section 151” and inserting “whose TIN is included on the taxpayer’s return of tax for the taxable year”.

(4) Section 2(b)(1)(A)(i) is amended—

(A) in the matter preceding subclause (I)—

(i) by striking “section 152(c)” and inserting “section 7706(c)”, and

(ii) by striking “section 152(e)” and inserting “section 7706(e)”, and

(B) in subclause (II), by striking “section 152(b)(2) or 152(b)(3)” and inserting “section 7706(b)(2) or 7706(b)(3)”.

(5) Section 2(b)(1)(A)(ii) is amended by striking “if the taxpayer is entitled to a deduction for the taxable year for such person under section 151” and inserting “if the taxpayer included such person’s TIN on the return of tax for the taxable year”.

(6) Section 2(b)(1)(B) is amended by striking “if the taxpayer is entitled to a deduction for the taxable year for such father or mother under section 151” and inserting “if such father or mother is a dependent of the taxpayer and the taxpayer included such father or mother’s TIN on the return of tax for the taxable year”.

(7) Section 2(b)(3)(B) is amended—

(A) by striking “section 152(d)(2)” in clause (i) and inserting “section 7706(d)(2)”, and

(B) by striking “section 152(d)” in clause (ii) and inserting “section 7706(d)”.

(8) Section 21(b)(1)(A) is amended by striking “section 152(a)(1)” and inserting “section 7706(a)(1)”.

(9) Section 21(b)(1)(B) is amended by striking “section 152” and inserting “section 7706”.

(10) Section 21(e)(5)(A) is amended by striking “section 152(e)” and inserting “section 7706(e)”.

(11) Section 21(e)(5) is amended by striking “section 152(e)(4)(A)” in the matter following subparagraph (B) and inserting “section 7706(e)(4)(A)”.

(12) Section 21(e)(6)(A) is amended to read as follows:

“(A) who is a dependent of either the taxpayer or the taxpayer’s spouse for the taxable year, or”.

(13) Section 21(e)(6)(B) is amended by striking “section 152(f)(1)” and inserting “section 7706(f)(1)”.

(14) Section 25A(f)(1)(A)(iii) is amended by striking “with respect to whom the taxpayer is allowed a deduction under section 151”.

(15) Section 25A(g)(3) is amended by striking “If a deduction under section 151 with respect to an individual is allowed to another taxpayer” and inserting “If an individual is a dependent of another taxpayer”.

(16) Section 25B(c)(2)(A) is amended by striking “any individual with respect to whom a deduction under section 151 is allowed to another taxpayer” and inserting “any individual who is a dependent of another taxpayer”.

(17) Section 25B(c)(2)(B) is amended by striking “section 152(f)(2)” and inserting “section 7706(f)(2)”.

(18) Section 32(c)(1)(A)(ii)(III) is amended by striking “a dependent for whom a deduction is allowable under section 151 to another taxpayer” and inserting “a dependent of another taxpayer”.

(19) Section 32(c)(3) is amended—

(A) in subparagraph (A)—

(i) by striking “section 152(c)” and inserting “section 7706(c)”, and

(ii) by striking “section 152(e)” and inserting “section 7706(e)”,

(B) in subparagraph (B), by striking “unless the taxpayer is entitled to a deduction under section 151 for such taxable year with respect to such individual (or would be so entitled but for section 152(e))” and inserting “if such individual is not treated as a dependent of such taxpayer for such taxable year by reason of section 7706(b)(2) (determined without regard to section 7706(e))”, and

(C) in subparagraph (C), by striking “section 152(c)(1)(B)” and inserting “section 7706(c)(1)(B)”.

(20) Section 35(d)(1)(B) is amended by striking “with respect to whom the taxpayer is entitled to a deduction under section 151(c)” and inserting “if the taxpayer included such person’s TIN on the return of tax for the taxable year”.

(21) Section 35(d)(2) is amended—

(A) by striking “section 152(e)” and inserting “section 7706(e)”, and

(B) by striking “section 152(e)(4)(A)” and inserting “section 7706(e)(4)(A)”.

(22) Section 36B(b)(2)(A) is amended by striking “section 152” and inserting “section 7706”.

(23) Section 36B(b)(3)(B) is amended by striking “unless a deduction is allowed under section 151 for the taxable year with respect to a dependent” in the flush matter at the end and inserting “unless the taxpayer has a dependent for the taxable year (and the taxpayer included such dependent’s TIN on the return of tax for the taxable year)”.

(24) Section 36B(c)(1)(D) is amended by striking “with respect to whom a deduction under section 151 is allowable to another taxpayer” and inserting “who is a dependent of another taxpayer”.

(25) Section 36B(d)(1) is amended by striking “equal to the number of individuals for whom the taxpayer is allowed a deduction under section 151 (relating to allowance of deduction for personal exemptions) for the taxable year” and inserting “the sum of 1 (2 in the case of a joint return) plus the number of individuals who are dependents of the taxpayer for the taxable year”.

(26) Section 36B(e)(1) is amended by striking “1 or more individuals for whom a taxpayer is allowed a deduction under section 151 (relating to allowance of deduction for personal exemptions) for the taxable year (including the taxpayer or his spouse)” and inserting “1 or more of the taxpayer, the taxpayer’s spouse, or any dependent of the taxpayer”.

(27) Section 42(i)(3)(D)(ii)(I) is amended by striking “section 152” and inserting “section 7706”.

(28) Section 45R(e)(1)(A)(iv) is amended—

(A) by striking “section 152(d)(2)” and inserting “section 7706(d)(2)”, and

(B) by striking “section 152(d)(2)(H)” and inserting “section 7706(d)(2)(H)”.

(29) Section 51(i)(1) is amended—

(A) by striking “section 152(d)(2)” in subparagraphs (A) and (B) and inserting “section 7706(d)(2)”, and

(B) by striking “section 152(d)(2)(H)” in subparagraph (C) and inserting “section 7706(d)(2)(H)”.

(30) Section 56(b)(1)(D), as amended by the preceding provisions of this Act, is amended—

(A) by striking “, the deduction for personal exemptions under section 151”, and

(B) by striking “AND DEDUCTION FOR PERSONAL EXEMPTIONS” in the heading thereof.

(31) Section 63(b) is amended by adding “and” at the end of paragraph (1), by striking paragraph (2), and by redesignating paragraph (3) as paragraph (2).

(32)(A) Section 63(c), as amended by section 121, is amended by striking paragraph (3) and redesignating paragraphs (4), (5), and (6) as paragraphs (3), (4), and (5), respectively.

(B) Section 1(g)(4)(A)(ii)(I) is amended by striking “section 63(c)(5)(A)” and inserting “section 63(c)(4)(A)”.

(33) Section 63(c)(4), as redesignated, is amended—

(A) by striking “with respect to whom a deduction under section 151 is allowable to” and inserting “who is a dependent of”, and

(B) by striking “CERTAIN” in the heading thereof.

(34) Section 63(d) is amended by adding “and” at the end of paragraph (1), by striking paragraph (2), and by redesignating paragraph (3) as paragraph (2).

(35) Section 63(f) is amended by striking all that precedes paragraph (3) and inserting the following:

“(f) ADDITIONAL STANDARD DEDUCTION FOR THE AGED AND BLIND.—

“(1) IN GENERAL.—For purposes of subsection (c)(1), the additional standard deduction is, with respect to a taxpayer for a taxable year, the sum of—

“(A) \$600 if the taxpayer has attained age 65 before the close of such taxable year, and

“(B) \$600 if the taxpayer is blind as of the close of such taxable year.

“(2) APPLICATION TO MARRIED INDIVIDUALS.—

“(A) JOINT RETURNS.—In the case of a joint return, paragraph (1) shall be applied separately with respect to each spouse.

“(B) CERTAIN MARRIED INDIVIDUALS FILING SEPARATELY.—In the case of a married individual filing a separate return, if—

“(i) the spouse of such individual has no gross income for the calendar year in which the taxable year of such individual begins,

“(ii) such spouse is not the dependent of another taxpayer for a taxable year beginning in the calendar year in which such individual’s taxable year begins, and

“(iii) the TIN of such spouse is included on such individual’s return of tax for the taxable year,

the additional standard deduction shall be determined in the same manner as if such individual and such individual’s spouse filed a joint return.”

(36) Section 63(f)(3) is amended by striking “paragraphs (1) and (2)” and inserting “subparagraphs (A) and (B) of paragraph (1)”.

(37) Section 72(t)(2)(D)(i)(III) is amended by striking “section 152” and inserting “section 7706”.

(38) Section 72(t)(7)(A)(iii) is amended by striking “section 152(f)(1)” and inserting “section 7706(f)(1)”.

(39) Section 105(b) is amended—

(A) by striking “as defined in section 152” and inserting “as defined in section 7706”,

(B) by striking “section 152(f)(1)” and inserting “section 7706(f)(1)” and

(C) by striking “section 152(e)” and inserting “section 7706(e)”.

(40) Section 105(c)(1) is amended by striking “section 152” and inserting “section 7706”.

(41) Section 125(e)(1)(D) is amended by striking “section 152” and inserting “section 7706”.

(42) Section 129(c)(1) is amended to read as follows:

“(1) who is a dependent of such employee or of such employee’s spouse, or”.

(43) Section 129(c)(2) is amended by striking “section 152(f)(1)” and inserting “section 7706(f)(1)”.

(44) Section 132(h)(2)(B) is amended—

(A) by striking “section 152(f)(1)” and inserting “section 7706(f)(1)”, and

(B) by striking “section 152(e)” and inserting “section 7706(e)”.

(45) Section 139D(c)(5) is amended by striking “section 152” and inserting “section 7706”.

(46) Section 139E(c)(2) is amended by striking “section 152” and inserting “section 7706”.

(47) Section 162(l)(1)(D) is amended by striking “section 152(f)(1)” and inserting “section 7706(f)(1)”.

(48) Section 170(g)(1) is amended by striking “section 152” and inserting “section 7706”.

(49) Section 170(g)(3) is amended by striking “section 152(d)(2)” and inserting “section 7706(d)(2)”.

(50) Section 172(d) is amended by striking paragraph (3).

(51) Section 213(a) is amended by striking “section 152” and inserting “section 7706”.

(52) Section 213(d)(5) is amended by striking “section 152(e)” and inserting “section 7706(e)”.

(53) Section 213(d)(11) is amended by striking “section 152(d)(2)” in the matter following subparagraph (B) and inserting “section 7706(d)(2)”.

- (54) Section 220(b)(6) is amended by striking “with respect to whom a deduction under section 151 is allowable to” and inserting “who is a dependent of”.
- (55) Section 220(d)(2)(A) is amended by striking “section 152” and inserting “section 7706”.
- (56) Section 221(d)(4) is amended by striking “section 152” and inserting “section 7706”.
- (57) Section 222(c)(3) is amended by striking “with respect to whom a deduction under section 151 is allowable to” and inserting “who is a dependent of”.
- (58) Section 223(b)(6) is amended by striking “with respect to whom a deduction under section 151 is allowable to” and inserting “who is a dependent of”.
- (59) Section 223(d)(2)(A) is amended by striking “section 152” and inserting “section 7706”.
- (60) Section 401(h) is amended by striking “section 152(f)(1)” in the last sentence and inserting “section 7706(f)(1)”.
- (61) Section 402(l)(4)(D) is amended by striking “section 152” and inserting “section 7706”.
- (62) Section 409A(a)(2)(B)(ii)(I) is amended by striking “section 152(a)” and inserting “section 7706(a)”.
- (63) Section 441(f)(2)(B)(iii) is amended by striking “, but only the adjusted amount of the deductions for personal exemptions as described in section 443(c)”.
- (64) Section 443 is amended—
- (A) in subsection (b)—
    - (i) by striking paragraph (3), and
    - (ii) by striking “modified taxable income” and inserting “taxable income” each place such term appears,
  - (B) by striking subsection (c), and
  - (C) by redesignating subsections (d) and (e) as subsections (c) and (d), respectively.
- (65) Section 501(c)(9) is amended by striking “section 152(f)(1)” and inserting “section 7706(f)(1)”.
- (66) Section 529(e)(2)(B) is amended by striking “section 152(d)(2)” and inserting “section 7706(d)(2)”.
- (67) Section 529A(e)(4) is amended—
- (A) by striking “section 152(d)(2)(B)” and inserting “section 7706(d)(2)(B)”, and
  - (B) by striking “section 152(f)(1)(B)” and inserting “section 7706(f)(1)(B)”.
- (68) Section 643(a)(2) is amended—
- (A) by striking “(relating to deduction for personal exemptions)” and inserting “(relating to basic deduction)”, and
  - (B) by striking “DEDUCTION FOR PERSONAL EXEMPTION” in the heading thereof and inserting “BASIC DEDUCTION”.
- (69) Section 703(a)(2) is amended by striking subparagraph (A) and by redesignating subparagraphs (B) through (F) as subparagraphs (A) through (E), respectively.
- (70) Section 874 is amended by striking subsection (b) and by redesignating subsection (c) as subsection (b).
- (71) Section 891 is amended by striking “under section 151 and”.
- (72) Section 904(b)(1) is amended to read as follows:
- “(1) DEDUCTION FOR ESTATES AND TRUSTS.—For purposes of subsection (a), the taxable income of an estate or trust shall be computed without any deduction under section 642(b).”.
- (73) Section 931(b)(1) is amended to read as follows:
- “(1) any deduction from gross income, or”.
- (74) Section 933 is amended—
- (A) by striking “as a deduction from his gross income any deductions (other than the deduction under section 151, relating to personal exemptions)” in paragraph (1) and inserting “any deduction from gross income”, and
  - (B) by striking “as a deduction from his gross income any deductions (other than the deduction for personal exemptions under section 151)” in paragraph (2) and inserting “any deduction from gross income”.
- (75) Section 1212(b)(2)(B)(ii) is amended to read as follows:
- “(ii) in the case of an estate or trust, the deduction allowed for such year under section 642(b).”.
- (76) Section 1361(c)(1)(C) is amended by striking “section 152(f)(1)(C)” and inserting “section 7706(f)(1)(C)”.
- (77) Section 1402(a) is amended by striking paragraph (7).



(78) Section 2032A(c)(7)(D) is amended by striking “section 152(f)(2)” and inserting “section 7706(f)(2)”.

(79) Section 3402(m)(1) is amended by striking “other than the deductions referred to in section 151 and”.

(80) Section 3402(r)(2) is amended by striking “the sum of—” and all that follows and inserting “the basic standard deduction (as defined in section 63(c)) for an individual to whom section 63(c)(2)(C) applies.”.

(81) Section 5000A(b)(3)(A) is amended by striking “section 152” and inserting “section 7706”.

(82) Section 5000A(c)(4)(A) is amended by striking “the number of individuals for whom the taxpayer is allowed a deduction under section 151 (relating to allowance of deduction for personal exemptions) for the taxable year” and inserting “the sum of 1 (2 in the case of a joint return) plus the number of the taxpayer’s dependents for the taxable year”.

(83) Section 6013(b)(3)(A) is amended—

(A) by striking “had less than the exemption amount of gross income” in clause (ii) and inserting “had no gross income”,

(B) by striking “had gross income of the exemption amount or more” in clause (iii) and inserting “had any gross income”, and

(C) by striking the flush language following clause (iii).

(84) Section 6014(a) is amended by striking “section 6012(a)(1)(C)(i)” and inserting “section 6012(a)(1)(B)(iii)”.

(85) Section 6014(b)(4) is amended by striking “63(c)(5)” and inserting “63(c)(4)”.

(86) Section 6103(l)(21)(A)(iii) is amended to read as follows:

“(iii) the number of the taxpayer’s dependents.”.

(87) Section 6213(g)(2)(H) is amended by striking “section 21 (relating to expenses for household and dependent care services necessary for gainful employment) or section 151 (relating to allowance of deductions for personal exemptions)” and inserting “subsection (a)(1)(B), (b)(1)(A)(ii), or (b)(1)(B) of section 2 or section 21, 35(d)(1)(B), 36B(b)(3)(B), or 63(f)(2)(B)”.

(88) Section 6334(d) is amended—

(A) by amending paragraph (2) to read as follows:

“(2) EXEMPT AMOUNT.—

“(A) IN GENERAL.—For purposes of paragraph (1), the term ‘exempt amount’ means an amount equal to—

“(i) the sum of the amount determined under subparagraph (B) and the standard deduction, divided by

“(ii) 52.

“(B) AMOUNT DETERMINED.—For purposes of subparagraph (A), the amount determined under this subparagraph is—

“(i) the dollar amount in effect under section 7706(d)(1)(B), multiplied

by

“(ii) the number of the taxpayer’s dependents for the taxable year in which the levy occurs.

“(C) VERIFIED STATEMENT.—Unless the taxpayer submits to the Secretary a written and properly verified statement specifying the facts necessary to determine the proper amount under subparagraph (A), subparagraph (A) shall be applied as if the taxpayer were a married individual filing a separate return with no dependents.”, and

(B) by striking paragraph (4).

(89) Section 7702B(f)(2)(C)(iii) is amended by striking “section 152(d)(2)” and inserting “section 7706(d)(2)”.

(90) Section 7703(a) is amended by striking “part V of subchapter B of chapter 1 and”.

(91) Section 7703(b)(1) is amended by striking “section 152(f)(1)” and all that follows and inserting “section 7706(f)(1) who is a dependent of such individual for the taxable year (or would be but for section 7706(e))”.

(92) Section 7706(a), as redesignated by this section, is amended by striking “this subtitle” and inserting “subtitle A”.

(93)(A) Section 7706(d)(1)(B), as redesignated by this section, is amended by striking “the exemption amount (as defined in section 151(d))” and inserting “\$4,150”.

(B) Section 7706(d), as redesignated by this section, is amended by adding at the end the following new paragraph:

“(6) INFLATION ADJUSTMENT.—In the case of any taxable year beginning in a calendar year beginning after 2018, the \$4,150 amount in paragraph (1)(B) shall be increased by an amount equal to—

“(A) such dollar amount, multiplied by

“(B) the cost-of-living adjustment determined under section 1(c)(2)(A) for the calendar year in which such taxable year begins, determined by substituting ‘calendar year 2017’ for ‘calendar year 2016’ in clause (ii) thereof. If any increase determined under the preceding sentence is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.”

(94) Section 7706(e)(3), as redesignated by this section, is amended by inserting “(as in effect before its repeal)” after “section 151”.

(95) Section 7706(f)(6)(B), as redesignated by this section, is amended by striking clause (i) and designating clauses (ii), (iii), and (iv) as clauses (i), (ii), and (iii), respectively.

(96) The table of parts for subchapter B of chapter 1 is amended by striking the item relating to part V.

(97) The table of sections for chapter 79 is amended by adding at the end the following new item:

“Sec. 7706. Dependent defined.”.

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 142. LIMITATION ON DEDUCTION FOR STATE AND LOCAL, ETC. TAXES.**

(a) IN GENERAL.—Section 164(b)(6) is amended by striking all that precedes “The preceding sentence” and inserting the following:

“(6) LIMITATION ON INDIVIDUAL DEDUCTIONS.—In the case of an individual—

“(A) no deduction shall be allowed under this chapter for foreign real property taxes paid or accrued during the taxable year, and

“(B) the aggregate amount of the deduction allowed under this chapter for taxes described in paragraphs (1), (2), and (3) of subsection (a) and paragraph (5) of this subsection paid or accrued by the taxpayer during the taxable year shall not exceed \$10,000 (\$5,000 in the case of a married individual filing a separate return).”.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 143. LIMITATION ON DEDUCTION FOR QUALIFIED RESIDENCE INTEREST.**

(a) INTEREST ON HOME EQUITY INDEBTEDNESS.—Section 163(h)(3)(A) is amended by striking “during the taxable year on” and all that follows through “residence of the taxpayer.” and inserting “during the taxable year on acquisition indebtedness with respect to any qualified residence of the taxpayer.”.

(b) LIMITATION ON ACQUISITION INDEBTEDNESS.—Section 163(h)(3)(B)(ii) is amended to read as follows:

“(ii) LIMITATION.—The aggregate amount treated as acquisition indebtedness for any period shall not exceed the excess (if any) of—

“(I) \$750,000 (\$375,000, in the case of a married individual filing a separate return), over

“(II) the sum of the aggregate outstanding pre-October 13, 1987, indebtedness (as defined in subparagraph (D)) plus the aggregate outstanding pre-December 15, 2017, indebtedness (as defined in subparagraph (C)).”.

(c) TREATMENT OF INDEBTEDNESS INCURRED ON OR BEFORE DECEMBER 15, 2017.—Section 163(h)(3)(C) is amended to read as follows:

“(C) TREATMENT OF INDEBTEDNESS INCURRED ON OR BEFORE DECEMBER 15, 2017.—

“(i) IN GENERAL.—In the case of any pre-December 15, 2017, indebtedness, subparagraph (B)(ii) shall not apply and the aggregate amount of such indebtedness treated as acquisition indebtedness for any period shall not exceed the excess (if any) of—

“(I) \$1,000,000 (\$500,000, in the case of a married individual filing a separate return), over

“(II) the aggregate outstanding pre-October 13, 1987, indebtedness (as defined in subparagraph (D)).

“(ii) PRE-DECEMBER 15, 2017, INDEBTEDNESS.—For purposes of this subparagraph—

“(I) IN GENERAL.—The term ‘pre-December 15, 2017, indebtedness’ means indebtedness (other than pre-October 13, 1987, indebtedness) incurred on or before December 15, 2017.

“(II) BINDING WRITTEN CONTRACT EXCEPTION.—In the case of a taxpayer who enters into a written binding contract before December 15, 2017, to close on the purchase of a principal residence before January 1, 2018, and who purchases such residence before

April 1, 2018, the term ‘pre-December 15, 2017, indebtedness’ shall include indebtedness secured by such residence.

“(iii) REFINANCING INDEBTEDNESS.—

“(I) IN GENERAL.—In the case of any indebtedness which is incurred to refinance indebtedness, such refinanced indebtedness shall be treated for purposes of this subparagraph as incurred on the date that the original indebtedness was incurred to the extent the amount of the indebtedness resulting from such refinancing does not exceed the amount of the refinanced indebtedness.

“(II) LIMITATION ON PERIOD OF REFINANCING.—Subclause (I) shall not apply to any indebtedness after the expiration of the term of the original indebtedness or, if the principal of such original indebtedness is not amortized over its term, the expiration of the term of the 1st refinancing of such indebtedness (or if earlier, the date which is 30 years after the date of such 1st refinancing).”.

(d) COORDINATION WITH TREATMENT OF INDEBTEDNESS INCURRED ON OR BEFORE OCTOBER 13, 1987.—Section 163(h)(3)(D) is amended—

(1) by striking clause (ii) and redesignating clauses (iii) and (iv) as clauses (ii) and (iii), respectively, and

(2) in clause (iii) (as so redesignated)—

(A) by striking “clause (ii)” in the matter preceding subclause (I) and inserting “clause (ii)”, and

(B) by striking “clause (iii)(I)” in subclauses (I) and (II) and inserting “clause (ii)(I)”.

(e) COORDINATION WITH EXCLUSION OF INCOME FROM DISCHARGE OF INDEBTEDNESS.—Section 108(h)(2) is amended by striking “\$1,000,000 (\$500,000)” and inserting “\$750,000 (\$375,000)”.

(f) CONFORMING AMENDMENT.—Section 163(h)(3) is amended by striking subparagraph (F).

(g) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 144. MODIFICATION OF DEDUCTION FOR PERSONAL CASUALTY LOSSES.**

(a) IN GENERAL.—Section 165(h)(5)(A) is amended by striking “in a taxable year beginning after December 31, 2017, and before January 1, 2026,”.

(b) CONFORMING AMENDMENTS.—

(1) Section 165(h)(5)(B) is amended by striking “for any taxable year to which subparagraph (A) applies”.

(2) Section 165(h)(5) is amended by striking “FOR TAXABLE YEARS 2018 THROUGH 2025” in the heading thereof and inserting “TO LOSSES ATTRIBUTABLE TO FEDERALLY DECLARED DISASTERS”.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to losses sustained in taxable years beginning after December 31, 2017.

**SEC. 145. TERMINATION OF MISCELLANEOUS ITEMIZED DEDUCTIONS.**

(a) IN GENERAL.—Section 67 is amended—

(1) by amending subsection (a) to read as follows:

“(a) IN GENERAL.—In the case of an individual, miscellaneous itemized deductions shall not be allowed.”, and

(2) by striking subsection (g).

(b) MOVEMENT OF DEFINITION OF ADJUSTED GROSS INCOME FOR ESTATES AND TRUSTS.—

(1) Section 67 is amended by striking subsection (e).

(2) Section 641 is amended by adding at the end the following new subsection:

“(d) COMPUTATION OF ADJUSTED GROSS INCOME.—For purposes of this title, the adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual, except that—

“(1) the deductions for costs which are paid or incurred in connection with the administration of the estate or trust and which would not have been incurred if the property were not held in such trust or estate, and

“(2) the deductions allowable under sections 642(b), 651, and 661,

shall be treated as allowable in arriving at adjusted gross income.”.

(c) CONFORMING AMENDMENTS.—

(1) Section 56(b)(1)(A) is amended to read as follows:

“(A) CERTAIN TAXES.—No deduction (other than a deduction allowable in computing adjusted gross income) shall be allowed for any taxes described in paragraph (1), (2), or (3) of section 164(a) or clause (ii) of section 164(b)(5)(A).”.

(2) Section 56(b)(1)(C), as amended by the preceding provisions of this Act, is amended by striking “subparagraph (A)(ii)” and inserting “subparagraph (A)”.

(3) Section 62(a) is amended by striking “subtitle” in the matter preceding paragraph (1) and inserting “title”.

(4) Section 641(c)(2)(E) is amended to read as follows:

“(E) Section 642(c) shall not apply.”.

(5) Section 1411(a)(2) is amended by striking “(as defined in section 67(e))”.

(6) Section 6654(d)(1)(C) is amended by striking clause (iii).

(7) Section 67 is amended in the heading, by striking “**2-PERCENT FLOOR ON**” and inserting “**DENIAL OF**”.

(8) The table of sections for part 1 of subchapter B of chapter 1 is amended by striking the item relating to section 67 and inserting the following new item:

“Sec. 67. Denial of miscellaneous itemized deductions.”.

(d) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 146. REPEAL OF OVERALL LIMITATION ON ITEMIZED DEDUCTIONS.**

(a) **IN GENERAL.**—Part 1 of subchapter B of chapter 1 is amended by striking section 68 (and the item relating to such section in the table of sections for such part).

(b) **CONFORMING AMENDMENTS.**—

(1) Section 1(f)(7)(A), as amended by sections 121 and 141, is amended by striking “or section 68(b)(2)”.

(2) Section 56(b)(1), as amended by the preceding provisions of this Act, is amended by striking subparagraph (E).

(3) Section 164(b)(5)(H)(ii)(III) is amended by striking “(as determined under section 68(b))”.

(4) Section 164(b)(5)(H) is amended by adding at the end the following new clause:

“(iii) **APPLICABLE AMOUNT DEFINED.**—For purposes of clause (ii), the term ‘applicable amount’ means—

“(I) \$300,000 in the case of a joint return or a surviving spouse,

“(II) \$275,000 in the case of a head of household,

“(III) \$250,000 in the case of an individual who is not married and who is not a surviving spouse or head of household, and

“(IV)  $\frac{1}{2}$  the amount applicable under subclause (I) in the case of a married individual filing a separate return.

For purposes of this paragraph, marital status shall be determined under section 7703. In the case of any taxable year beginning in calendar years after 2017, each of the dollar amounts in this clause shall be increased by an amount equal to such dollar amount, multiplied by the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting ‘2012’ for ‘2016’ in subparagraph (A)(ii) thereof. If any amount after adjustment under the preceding sentence is not a multiple of \$50, such amount shall be rounded to the next lowest multiple of \$50.”.

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 147. TERMINATION OF EXCLUSION FOR QUALIFIED BICYCLE COMMUTING REIMBURSEMENT.**

(a) **IN GENERAL.**—Section 132(f)(1) is amended by striking subparagraph (D).

(b) **CONFORMING AMENDMENTS.**—

(1) Section 132(f)(2) is amended by adding “and” at the end of subparagraph (A), striking “, and” at the end of subparagraph (B) and inserting a period, and striking subparagraph (C).

(2) Section 132(f)(4) is amended by striking “(other than a qualified bicycle commuting reimbursement)”.

(3) Section 132(f) is amended by striking paragraph (8).

(4) Section 274(l)(2) is amended by striking “after December 31, 2017, and before January 1, 2026”.

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 148. QUALIFIED MOVING EXPENSE REIMBURSEMENT EXCLUSION LIMITED TO MEMBERS OF ARMED FORCES.**

(a) **IN GENERAL.**—Section 132(g) is amended—

(1) by striking “by an individual” in paragraph (1) and inserting “by a qualified military individual”, and

(2) by striking paragraph (2) and inserting the following new paragraph:

“(2) **QUALIFIED MILITARY INDIVIDUAL.**—For purposes of this subsection, the term ‘qualified military individual’ means a member of the Armed Forces of the

United States on active duty who moves pursuant to a military order and incident to a permanent change of station.”.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 149. DEDUCTION FOR MOVING EXPENSES LIMITED TO MEMBERS OF ARMED FORCES.**

(a) IN GENERAL.—Section 217 is amended—

(1) by amending subsection (a) to read as follows:

“(a) DEDUCTION ALLOWED.—There shall be allowed as a deduction moving expenses paid or incurred during the taxable year by a member of the Armed Forces of the United States on active duty who moves pursuant to a military order and incident to a permanent change of station.”.

(2) by striking subsections (c), (d), (f), and (g) and redesignating subsections (h), (i), (j), and (k) as subsections (c), (d), (f) and (g), respectively, and

(3) by inserting after subsection (d), as so redesignated, the following new subsection:

“(e) EXPENSES FURNISHED IN KIND.—Any moving and storage expenses which are furnished in kind (or for which reimbursement or an allowance is provided, but only to the extent of the expenses paid or incurred)—

“(1) to such member, his spouse, or his dependents, shall not be includible in gross income, and no reporting with respect to such expenses shall be required by the Secretary of Defense or the Secretary of Transportation, as the case may be, and

“(2) to such member’s spouse and his dependents with regard to moving to a location other than the one to which such member moves (or from a location other than the one from which such member moves), this section shall apply with respect to the moving expenses of his spouse and dependents as if his spouse commenced work as an employee at a new principal place of work at such location.”.

(b) CONFORMING AMENDMENTS.—

(1) Subsections (d)(3)(C) and (e) of section 23 are each amended by striking “section 217(h)(3)” and inserting “section 217(c)(3)”.

(2) Section 7872(f) is amended by striking paragraph (11).

(3) Section 217 is amended in the heading by striking “MOVING EXPENSES” and inserting “CERTAIN MOVING EXPENSES OF MEMBERS OF ARMED FORCES”.

(4) The table of sections for part VII of subchapter B of chapter 1 is amended by striking the item relating to section 217 and inserting the following new item:

“Sec. 217. Certain moving expenses of members of Armed Forces.”.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

**SEC. 150. LIMITATION ON WAGERING LOSSES.**

(a) IN GENERAL.—Section 165(d) is amended by striking “in the case of taxable years beginning after December 31, 2017, and before January 1, 2026.”.

(b) EFFECTIVE DATE.—The amendment made by this section shall apply to taxable years beginning after December 31, 2017.

## **Subtitle F—Increase in Estate and Gift Tax Exemption**

**SEC. 151. INCREASE IN ESTATE AND GIFT TAX EXEMPTION.**

(a) IN GENERAL.—Section 2010(c)(3) is amended in subparagraph (A), by striking “\$5,000,000” and inserting “\$10,000,000”.

(b) CONFORMING AMENDMENTS.—

(1) Section 2001(g) is amended to read as follows:

“(g) MODIFICATIONS TO GIFT TAX PAYABLE TO REFLECT DIFFERENT TAX RATES.—For purposes of applying subsection (b)(2) with respect to 1 or more gifts, the rates of tax under subsection (c) in effect at the decedent’s death shall, in lieu of the rates of tax in effect at the time of such gifts, be used both to compute—

“(1) the tax imposed by chapter 12 with respect to such gifts, and

“(2) the credit allowed against such tax under section 2505, including in computing—

“(A) the applicable credit amount under section 2505(a)(1), and

“(B) the sum of the amounts allowed as a credit for all preceding periods under section 2505(a)(2).”.

(2) Section 2010(c)(3) is amended by striking subparagraph (C).

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to estates of decedents dying and gifts made after December 31, 2017.

## TITLE II—INCREASED EXEMPTION FOR ALTERNATIVE MINIMUM TAX MADE PERMANENT

### SEC. 201. INCREASED EXEMPTION FOR INDIVIDUALS.

- (a) IN GENERAL.—Section 55(d)(1) is amended—
- (1) by striking “\$78,750” in subparagraph (A) and inserting “\$109,400”, and
  - (2) by striking “\$50,600” in subparagraph (B) and inserting “\$70,300”.
- (b) PHASE-OUT OF EXEMPTION AMOUNT.—Section 55(d)(2) is amended—
- (1) by striking “\$150,000” in subparagraph (A) and inserting “\$1,000,000”, and
  - (2) by striking subparagraphs (B) and (C) and by inserting the following new subparagraphs:
    - “(B) 50 percent of the dollar amount applicable under subparagraph (A) in the case of a taxpayer described in paragraph (1)(B) or (1)(C), and
    - “(C) \$75,000 in the case of a taxpayer described in paragraph (1)(D).”
- (c) INFLATION ADJUSTMENT.—Section 55(d)(3) is amended to read as follows:
- “(3) INFLATION ADJUSTMENT.—In the case of any taxable year beginning in a calendar year after 2018, each dollar amount described in clause (i) or (ii) of subparagraph (B) shall be increased by an amount equal to—
- “(A) such dollar amount, multiplied by
  - “(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting—
    - “(i) in the case of a dollar amount contained in paragraph (1)(D) or (2)(C) or in subsection (b)(1)(A), ‘calendar year 2011’ for ‘calendar year 2016’ in subparagraph (A)(ii) thereof, and
    - “(ii) in the case of a dollar amount contained in paragraph (1)(A), (1)(B), or (2)(A), ‘calendar year 2017’ for ‘calendar year 2016’ in subparagraph (A)(ii) thereof.
- Any increased amount determined under this paragraph shall be rounded to the nearest multiple of \$100 (\$50 in the case of the dollar amount contained in paragraph (2)(C)).”
- (d) CONFORMING AMENDMENT.—Section 55(d) is amended by striking paragraph (4).
- (e) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 2017.

## I. SUMMARY AND BACKGROUND

### A. PURPOSE AND SUMMARY

H.R. 6760, as reported by the Committee on Ways and Means, makes permanent the comprehensive reforms to the Internal Revenue Code of 1986 to provide tax relief and simplification to American families, individuals, and small businesses that were enacted on a temporary basis by subtitles A and B of the Tax Cuts and Jobs Act (Public Law 115–97).

### B. BACKGROUND AND NEED FOR LEGISLATION

H.R. 6760 furthers the goals of the Tax Cuts and Jobs Act (Public Law 115–97) in comprehensively reforming the tax code to reduce tax burdens and encourage growth and job creation. Making permanent these important reforms that lower the tax burden on the middle class and create a healthier economy will promote stability, certainty, and growth.

## C. LEGISLATIVE HISTORY

*Background*

H.R. 6760 was introduced on September 10, 2018, and was referred to the Committee on Ways and Means.

*Committee action*

The Ways and Means Committee and the Subcommittee on Tax Policy have held extensive hearings over many years focused on the benefits of tax reform and permanent tax policy, including hearings during the 115th Congress that addressed the particular aspects of tax reform that are made permanent by H.R. 6760:

- Tax Reform and Small Business: Growing Our Economy and Creating Jobs (May 23, 2018)
- Growing Our Economy and Creating Jobs (May 16, 2018)
- How Tax Reform Will Help America’s Small Businesses Grow and Create New Jobs (July 13, 2017)
- How Tax Reform Will Simplify Our Broken Tax Code and Help Individuals and Families (July 19, 2017)
- How Tax Reform Will Grow our Economy and Create Jobs (May 18, 2017)
- The President’s Fiscal Year 2018 Budget Proposals (May 24, 2017)

**II. EXPLANATION OF THE BILL**

## PRESENT LAW

On December 22, 2017, Public Law 115–97<sup>1</sup> (referred to herein as the Tax Cuts and Jobs Act or the TCJA) was enacted into law. The TCJA made numerous changes to the income tax system, many of which expire for taxable years beginning after December 31, 2025. These temporary provisions include the following:

1. The TCJA modifies the tax rates and tax bracket breakpoints in order to provide tax relief to individuals and pass-through businesses.<sup>2</sup> For taxable years beginning after December 31, 2025, the tax rates and brackets revert to their inflation-adjusted levels based on the law as in existence in 2017.<sup>3</sup>
2. The TCJA modifies the tax on unearned income of a minor child (known as the “kiddie tax”) such that the tax is generally imposed using the tax brackets applicable to trusts and estates, rather than with reference to the child’s parents’ tax situation.<sup>4</sup>

<sup>1</sup> 31 Stat. 2054.

<sup>2</sup> Sec. 11001 of the TCJA and sec. 1 of the Internal Revenue code of 1986, as amended (the “Code”).

<sup>3</sup> Because the TCJA modified the method used to index dollar amounts in the Code, switching the measurement of inflation from the Consumer Price Index (“CPI”) to the Chained Consumer Price Index (“C–CPI–U”) the C–CPI–U, and because this switch does not expire, the actual tax bracket breakpoints are projected to be lower in 2026 than they would have been had the TCJA not been enacted.

<sup>4</sup> Sec. 11001 of the TCJA and sec. 1 of the Code.

3. The TCJA creates a deduction for qualified business income, generally equaling up to 20-percent of non-wage income for qualified individuals.<sup>5</sup>

4. The TCJA limits the deduction for business losses to \$500,000 for joint filers and \$250,000 for other individuals.<sup>6</sup>

5. The TCJA increases the standard deduction to \$24,000 for married taxpayers filing jointly and surviving spouses, \$18,000 for heads of household, and \$12,000 for all other taxpayers.<sup>7</sup> These amounts are indexed for inflation. For taxable years beginning after December 31, 2025, the standard deduction reverts to its inflation-adjusted 2017 levels.

6. The TCJA increases the child tax credit from \$1,000 to \$2,000, and increases the phaseout thresholds to \$400,000 for married couples filing a joint return (\$200,000 for all other taxpayers).<sup>8</sup> Additionally, the TCJA provides for a \$500 non-refundable credit for non-child dependents. The refundable child tax credit is modified by lowering the earned income threshold from \$3,000 to \$2,500, and increasing the maximum value of the refundable credit to \$1,400 (indexed). Finally, the TCJA modifies the identification requirements applicable to a child on whose behalf the credit is claimed, requiring that the child's taxpayer identification number be a Social Security number issued by the due date of the return in order to qualify for the \$2,000 credit.

7. The TCJA increases the charitable contribution percentage limit from 50 percent to 60 percent of the contribution base (generally, adjusted gross income) for contributions of cash to organizations described in section 170(b)(1)(A) (generally, public charities and certain private foundations that are not non-operating private foundations).<sup>9</sup>

8. The TCJA allows ABLE account owners to make contributions of earned income, but not in excess of the Federal poverty line, to their ABLE accounts, in addition to the limitations imposed on other contributions made to such accounts.<sup>10</sup> Additionally the TCJA allows individuals who make such contributions to be eligible for the saver's credit. These modifications do not apply for contributions made to ABLE accounts after December 31, 2025.

9. The TCJA allows amounts in qualified tuition programs (known as 529 accounts) to be rolled over into ABLE accounts, subject to the overall contribution limits on ABLE accounts.<sup>11</sup> This provision does not apply to rollovers made after December 31, 2025.

<sup>5</sup>Sec. 11011 of the TCJA and new sec. 199A of the Code. Note that the treatment of income relating to cooperatives under section 199A (as originally enacted on December 22, 2017) was modified by the Consolidated Appropriations Act, 2018, Pub. L. No. 115-141, enacted on March 23, 2018. For a description of the modification, see Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions of the House Amendment to the Senate Amendment to H.R. 1625 (Rules Committee Print 115-66)*, JCX-6-18, March 22, 2018, pp. 5-27.

<sup>6</sup>Sec. 11012 of the TCJA and sec. 461 of the Code.

<sup>7</sup>Sec. 11021 of the TCJA and sec. 63 of the Code.

<sup>8</sup>Sec. 11022 of the TCJA and sec. 24 of the Code.

<sup>9</sup>Sec. 11023 of the TCJA and sec. 170(b)(1)(G) of the Code.

<sup>10</sup>Sec. 11024 of the TCJA and sec. 529A of the Code.

<sup>11</sup>Sec. 11025 of the TCJA and secs. 529 and 529A of the Code.



10. The TCJA grants combat zone tax benefits to those members of the Armed Forces serving in the Sinai Peninsula of Egypt.<sup>12</sup>

11. The TCJA reduces the threshold above which unreimbursed medical expenses may be deducted from 10 percent to 7.5 percent of adjusted gross income (“AGI”) for taxable years beginning after December 31, 2016 and ending before January 1, 2019.<sup>13</sup>

12. The TCJA provides that certain student loans that are discharged on account of the death or disability of the borrower are excluded from gross income.<sup>14</sup> This exclusion does not apply for student loans discharged after December 31, 2025.

13. The TCJA reduces the amount of the personal exemption deduction to zero.<sup>15</sup> For taxable years beginning after December 31, 2025, the personal exemption deduction reverts to its inflation-adjusted 2017 level.

14. The TCJA limits the itemized deduction for State and local property taxes (other than paid or accrued in carrying on a trade or business, or an activity described in section 212) and State and local income, war profits, and excess profits taxes (or sales taxes in lieu of income taxes) to \$10,000 for all taxpayers other than married taxpayers filing separate returns, for whom the limit is \$5,000.<sup>16</sup> The TCJA also repeals the deduction for foreign real property taxes (other than paid or accrued in carrying on a trade or business, or an activity described in section 212).

15. The TCJA reduces the \$1 million limitation of acquisition indebtedness with respect to which interest is deductible to \$750,000 (\$375,000 in the case of married taxpayers filing a separate return) in the case of acquisition indebtedness incurred on or after December 15, 2017.<sup>17</sup> Additionally, under the TCJA, home equity interest is not deductible.

16. The TCJA suspends the deduction for a personal casualty loss, or for theft, unless such casualty loss or theft is attributable to a disaster declared by the President under section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act.<sup>18</sup>

17. The TCJA suspends the deduction for miscellaneous itemized deductions.<sup>19</sup>

18. The TCJA suspends the overall limitation on itemized deductions (commonly referred to as the “Pease limitation”).<sup>20</sup>

19. The TCJA suspends the exclusion from gross income and wages for qualified bicycle commuting reimbursements.<sup>21</sup>

20. The TCJA suspends the exclusion from gross income and wages for qualified moving expense reimbursements for all taxpayers other than members of the Armed Forces of the United

<sup>12</sup> Sec. 11026 of the TCJA, affecting various Code sections.

<sup>13</sup> Sec. 11027 of the TCJA and sec. 213 of the Code.

<sup>14</sup> Sec. 11031 of the TCJA and sec. 108 of the Code.

<sup>15</sup> Sec. 11041 of the TCJA and sec. 151 of the Code.

<sup>16</sup> Sec. 11042 of the TCJA and sec. 164 of the Code.

<sup>17</sup> Sec. 11043 of the TCJA and sec. 163 of the Code.

<sup>18</sup> Sec. 11044 of the TCJA and sec. 165 of the Code.

<sup>19</sup> Sec. 11045 of the TCJA and sec. 67 of the Code.

<sup>20</sup> Sec. 11046 of the TCJA and sec. 68 of the Code.

<sup>21</sup> Sec. 11047 of the TCJA and sec. 132(f) of the Code.

States on active duty who move pursuant to a military order and incident to a permanent change of station.<sup>22</sup>

21. The TCJA suspends the above-the-line deduction for moving expenses incurred in connection with the relocation of a taxpayer for a new principal place of work for all taxpayers other than members of the Armed Forces of the United States on active duty who move pursuant to a military order and incident to a permanent change of station.<sup>23</sup>

22. The TCJA provides that wagering losses, and the limitations applicable to those losses, include expenses incurred in connection with the conduct of such individual's gambling activity (and not only the actual costs of the wagers incurred by such individual).<sup>24</sup>

23. The TCJA doubles the estate and gift tax exemption amounts, such that for 2018 the exemption amount is \$11.2 million per individual.<sup>25</sup> For estates of decedents dying and gifts made after December 31, 2025, the exemption amount reverts to its inflation-adjusted 2017 amount.

24. The TCJA increases the alternative minimum tax exemption amount to \$109,400 for joint returns and surviving spouses (half this amount for married taxpayers filing a separate return) and \$70,300 for all other taxpayers (other than trusts and estates). Additionally the phaseout thresholds for the exemption amount are increased to \$1,000,000 for married taxpayers filing a joint return and \$500,000 for all other taxpayers (other than trusts and estates).<sup>26</sup>

#### REASONS FOR CHANGE

The Committee believes that the tax relief provided by the Tax Cuts and Jobs Act has spurred economic growth and created jobs. The Committee believes it is appropriate to permanently extend the individual and pass-through business provisions that were temporary in the TCJA, in order to provide certainty to individuals, families, and small businesses and continue to drive economic growth and job creation.

#### EXPLANATION OF PROVISION

For the above-described provisions that expire after December 31, 2025, the provision repeals the expiration date, thereby fully and permanently integrating the policy enacted by the Tax Cuts and Jobs Act into the tax code.

The provision extends the reduction of the threshold above which unreimbursed medical expenses may be deducted, so that this reduction in the threshold from 10 percent to 7.5 percent of AGI applies to taxable years beginning after December 31, 2016 and ending before January 1, 2021.

#### *Other modifications contained in the provision*

The provision makes other modifications to certain provisions relating to the TCJA.

<sup>22</sup> Sec. 11048 of the TCJA and sec. 132(g) of the Code.

<sup>23</sup> Sec. 11049 of the TCJA and sec. 217 of the Code.

<sup>24</sup> Sec. 11050 of the TCJA and sec. 165(d) of the Code.

<sup>25</sup> Sec. 11061 of the TCJA and sec. 2010 of the Code.

<sup>26</sup> Sec. 12001 of the TCJA and sec. 55 of the Code.

*Modification to capital gains bracket breakpoints*

The provision modifies the breakpoints between the zero and 15-percent rate on long-term capital gains and qualified dividends, conforming the breakpoints to the maximum ordinary income amounts taxed at rates below the 22-percent bracket breakpoint on ordinary income. This modification assures that taxpayers cannot have long-term capital gains income taxed at a higher rate of tax than ordinary income would be taxed. The capital gains breakpoints applicable to trusts and estates are not modified under this provision.

*Modification of return requirement*

The provision modifies the tax filing requirement so that a married taxpayer does not need to file an income tax return if the combined gross income of the taxpayer (individual and spouse) is less than the applicable standard deduction, even if the individual and spouse do not have the same household as their home at the close of the taxable year.<sup>27</sup>

*Modification to section 15*

Section 15 provides a rule for the computation of tax in the event of a tax rate change (or a repeal of a tax) for a taxable year beginning on a date other than the first date of a taxpayer's taxable year. This provision does not apply to changes due to individual inflation adjustments or to changes in the individual tax rates made by the various tax Acts enacted in recent years. The provision modifies section 15 to apply only to changes in corporate tax rates.

*Technical and clerical modifications contained in the provision**Modification of rules related to rounding of income tax brackets*

The provision modifies the rounding rule applicable to the income tax brackets applicable to heads of household, so as to conform those rules to those that apply to the tax brackets applicable to unmarried individuals (other than heads of household or surviving spouses). Under the provision the income tax brackets for heads of household, unmarried individuals, and married individuals filing separately all round to the next lowest multiple of \$25.

*ITIN requirement for non-child dependents*

The provision clarifies that a taxpayer identification number is necessary with respect to any non-child dependent for whom the \$500 non-refundable credit is claimed. The taxpayer identification number may be either a Social Security number or an individual taxpayer identification number.

*Gross income requirement for non-child dependent*

The provision makes a technical change to provide that, as under 2017 law, an individual other than a child may qualify as a dependent of another taxpayer if such individual has gross income not in excess of \$4,150. This amount is indexed for inflation.

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<sup>27</sup> Sec. 6012(a)(1)(A)(iv) of the Code.

*Increased limitation for certain charitable contributions*

The provision provides that the 60-percent limit for cash contributions is applied after (and reduced by) the amount of noncash contributions to organizations described in section 170(b)(1)(A). For example, assume an individual with a contribution base of \$100,000 for the taxable year makes a contribution of unappreciated property with a fair market value of \$50,000 and a contribution of \$10,000 cash to a qualified public charity. Under the provision, the cash contribution limit is determined after accounting for noncash contributions. Thus, in the above example, the \$50,000 contribution of unappreciated property is accounted for first, using up the entire 50-percent contribution limit described in section 170(b)(1)(A), but leaving \$10,000 in allowable cash contributions under the 60-percent limit.

*Limitation on deduction for State and local, etc. taxes*

The provision makes a technical change to clarify that the \$10,000 limitation on the itemized deduction for State and local property taxes (other than paid or accrued in carrying on a trade or business, or an activity described in section 212) and State and local income, war profits and excess profits taxes (or sales taxes in lieu of income taxes) applies with respect to all such State and local taxes otherwise deductible under chapter 1 of the Internal Revenue Code.

## EFFECTIVE DATE

The provision is generally effective for taxable years beginning after December 31, 2017.

**III. VOTES OF THE COMMITTEE**

In compliance with the Rules of the House of Representatives, the following statement is made concerning the vote of the Committee on Ways and Means during the markup consideration of H.R. 6760, "Protecting Family and Small Business Tax Cuts Act of 2018" on September 13, 2018.

The vote on the amendment offered by Mr. Pascrell to the amendment in the nature of a substitute to H.R. 6760, which would expand the itemized deduction for state and local taxes and increase the corporate tax rate, was not agreed to by a roll call vote of 15 yeas to 21 nays (with a quorum being present). The vote was as follows:

| Representative       | Yea | Nay | Present | Representative       | Yea | Nay   | Present |
|----------------------|-----|-----|---------|----------------------|-----|-------|---------|
| Mr. Brady .....      |     | X   | .....   | Mr. Neal .....       | X   | ..... | .....   |
| Mr. Johnson .....    |     | X   | .....   | Mr. Levin .....      | X   | ..... | .....   |
| Mr. Nunes .....      |     | X   | .....   | Mr. Lewis .....      | X   | ..... | .....   |
| Mr. Reichert .....   |     | X   | .....   | Mr. Doggett .....    | X   | ..... | .....   |
| Mr. Roskam .....     |     | X   | .....   | Mr. Thompson .....   | X   | ..... | .....   |
| Mr. Buchanan .....   |     | X   | .....   | Mr. Larson .....     | X   | ..... | .....   |
| Mr. Smith (NE) ..... |     | X   | .....   | Mr. Blumenauer ..... | X   | ..... | .....   |
| Ms. Jenkins .....    |     | X   | .....   | Mr. Kind .....       | X   | ..... | .....   |
| Mr. Paulsen .....    |     | X   | .....   | Mr. Pascrell .....   | X   | ..... | .....   |
| Mr. Marchant .....   |     | X   | .....   | Mr. Crowley .....    | X   | ..... | .....   |
| Ms. Black .....      |     | X   | .....   | Mr. Davis .....      | X   | ..... | .....   |
| Mr. Reed .....       |     | X   | .....   | Ms. Sanchez .....    | X   | ..... | .....   |
| Mr. Kelly .....      |     | X   | .....   | Mr. Higgins .....    |     | ..... | .....   |
| Mr. Renacci .....    |     |     | .....   | Ms. Sewell .....     | X   | ..... | .....   |

| Representative       | Yea | Nay | Present | Representative    | Yea | Nay   | Present |
|----------------------|-----|-----|---------|-------------------|-----|-------|---------|
| Ms. Noem .....       |     | X   | .....   | Ms. DelBene ..... | X   | ..... | .....   |
| Mr. Holding .....    |     |     | .....   | Ms. Chu .....     | X   | ..... | .....   |
| Mr. Smith (MO) ..... |     | X   | .....   |                   |     |       |         |
| Mr. Rice .....       |     |     | .....   |                   |     |       |         |
| Mr. Schweikert ..... |     | X   | .....   |                   |     |       |         |
| Ms. Walorski .....   |     | X   | .....   |                   |     |       |         |
| Mr. Curbelo .....    |     | X   | .....   |                   |     |       |         |
| Mr. Bishop .....     |     | X   | .....   |                   |     |       |         |
| Mr. LaHood .....     |     | X   | .....   |                   |     |       |         |
| Mr. Wenstrup .....   |     | X   | .....   |                   |     |       |         |

In compliance with the Rules of the House of Representatives, the following statement is made concerning the vote of the Committee on Ways and Means during the markup consideration of H.R. 6760, “Protecting Family and Small Business Tax Cuts Act of 2018” on September 13, 2018.

The vote on the amendment offered by Mr. Neal to the amendment in the nature of a substitute to H.R. 6760, which would expand several individual tax credits and increase the top individual tax rate, was not agreed to by a roll call vote of 15 yeas to 21 nays (with a quorum being present). The vote was as follows:

| Representative       | Yea | Nay | Present | Representative       | Yea | Nay   | Present |
|----------------------|-----|-----|---------|----------------------|-----|-------|---------|
| Mr. Brady .....      |     | X   | .....   | Mr. Neal .....       | X   | ..... | .....   |
| Mr. Johnson .....    |     | X   | .....   | Mr. Levin .....      | X   | ..... | .....   |
| Mr. Nunes .....      |     | X   | .....   | Mr. Lewis .....      | X   | ..... | .....   |
| Mr. Reichert .....   |     | X   | .....   | Mr. Doggett .....    | X   | ..... | .....   |
| Mr. Roskam .....     |     | X   | .....   | Mr. Thompson .....   | X   | ..... | .....   |
| Mr. Buchanan .....   |     | X   | .....   | Mr. Larson .....     | X   | ..... | .....   |
| Mr. Smith (NE) ..... |     | X   | .....   | Mr. Blumenauer ..... | X   | ..... | .....   |
| Ms. Jenkins .....    |     | X   | .....   | Mr. Kind .....       | X   | ..... | .....   |
| Mr. Paulsen .....    |     | X   | .....   | Mr. Pascrell .....   | X   | ..... | .....   |
| Mr. Marchant .....   |     | X   | .....   | Mr. Crowley .....    | X   | ..... | .....   |
| Ms. Black .....      |     | X   | .....   | Mr. Davis .....      | X   | ..... | .....   |
| Mr. Reed .....       |     | X   | .....   | Ms. Sanchez .....    | X   | ..... | .....   |
| Mr. Kelly .....      |     | X   | .....   | Mr. Higgins .....    | X   | ..... | .....   |
| Mr. Renacci .....    |     |     | .....   | Ms. Sewell .....     |     | ..... | .....   |
| Ms. Noem .....       |     | X   | .....   | Ms. DelBene .....    | X   | ..... | .....   |
| Mr. Holding .....    |     |     | .....   | Ms. Chu .....        | X   | ..... | .....   |
| Mr. Smith (MO) ..... |     | X   | .....   |                      |     |       |         |
| Mr. Rice .....       |     |     | .....   |                      |     |       |         |
| Mr. Schweikert ..... |     | X   | .....   |                      |     |       |         |
| Ms. Walorski .....   |     | X   | .....   |                      |     |       |         |
| Mr. Curbelo .....    |     | X   | .....   |                      |     |       |         |
| Mr. Bishop .....     |     | X   | .....   |                      |     |       |         |
| Mr. LaHood .....     |     | X   | .....   |                      |     |       |         |
| Mr. Wenstrup .....   |     | X   | .....   |                      |     |       |         |

In compliance with the Rules of the House of Representatives, the following statement is made concerning the vote of the Committee on Ways and Means during the markup consideration of H.R. 6760, “Protecting Family and Small Business Tax Cuts Act of 2018” on September 13, 2018.

The vote on the amendment offered by Mr. Thompson to the amendment in the nature of a substitute to H.R. 6760, which would expand the itemized deduction for casualty losses, include permanent provisions related to federally-declared disasters, and increase the corporate tax rate, was not agreed to by a roll call vote of 15 yeas to 21 nays (with a quorum being present). The vote was as follows:

| Representative | Yea | Nay | Present | Representative | Yea | Nay | Present |
|----------------|-----|-----|---------|----------------|-----|-----|---------|
| Mr. Brady      |     | X   |         | Mr. Neal       | X   |     |         |
| Mr. Johnson    |     | X   |         | Mr. Levin      | X   |     |         |
| Mr. Nunes      |     | X   |         | Mr. Lewis      | X   |     |         |
| Mr. Reichert   |     | X   |         | Mr. Doggett    | X   |     |         |
| Mr. Roskam     |     | X   |         | Mr. Thompson   | X   |     |         |
| Mr. Buchanan   |     | X   |         | Mr. Larson     | X   |     |         |
| Mr. Smith (NE) |     | X   |         | Mr. Blumenauer | X   |     |         |
| Ms. Jenkins    |     | X   |         | Mr. Kind       | X   |     |         |
| Mr. Paulsen    |     | X   |         | Mr. Pascrell   | X   |     |         |
| Mr. Marchant   |     | X   |         | Mr. Crowley    | X   |     |         |
| Ms. Black      |     | X   |         | Mr. Davis      | X   |     |         |
| Mr. Reed       |     | X   |         | Ms. Sanchez    | X   |     |         |
| Mr. Kelly      |     | X   |         | Mr. Higgins    | X   |     |         |
| Mr. Renacci    |     |     |         | Ms. Sewell     |     |     |         |
| Ms. Noem       |     | X   |         | Ms. DelBene    | X   |     |         |
| Mr. Holding    |     |     |         | Ms. Chu        | X   |     |         |
| Mr. Smith (MO) |     | X   |         |                |     |     |         |
| Mr. Rice       |     |     |         |                |     |     |         |
| Mr. Schweikert |     | X   |         |                |     |     |         |
| Ms. Walorski   |     | X   |         |                |     |     |         |
| Mr. Curbelo    |     | X   |         |                |     |     |         |
| Mr. Bishop     |     | X   |         |                |     |     |         |
| Mr. LaHood     |     | X   |         |                |     |     |         |
| Mr. Wenstrup   |     | X   |         |                |     |     |         |

In compliance with the Rules of the House of Representatives, the following statement is made concerning the vote of the Committee on Ways and Means during the markup consideration of H.R. 6760, “Protecting Family and Small Business Tax Cuts Act of 2018” on September 13, 2018.

The vote on the amendment offered by Ms. Sánchez to the amendment in the nature of a substitute to H.R. 6760, which would make the 7.5 percent of adjusted gross income floor on the deduction for certain medical expenses permanent and increase the corporate tax rate, was not agreed to by a roll call vote of 15 yeas to 21 nays (with a quorum being present). The vote was as follows:

| Representative | Yea | Nay | Present | Representative | Yea | Nay | Present |
|----------------|-----|-----|---------|----------------|-----|-----|---------|
| Mr. Brady      |     | X   |         | Mr. Neal       | X   |     |         |
| Mr. Johnson    |     | X   |         | Mr. Levin      | X   |     |         |
| Mr. Nunes      |     | X   |         | Mr. Lewis      | X   |     |         |
| Mr. Reichert   |     | X   |         | Mr. Doggett    | X   |     |         |
| Mr. Roskam     |     | X   |         | Mr. Thompson   | X   |     |         |
| Mr. Buchanan   |     | X   |         | Mr. Larson     | X   |     |         |
| Mr. Smith (NE) |     | X   |         | Mr. Blumenauer | X   |     |         |
| Ms. Jenkins    |     | X   |         | Mr. Kind       | X   |     |         |
| Mr. Paulsen    |     | X   |         | Mr. Pascrell   | X   |     |         |
| Mr. Marchant   |     | X   |         | Mr. Crowley    | X   |     |         |
| Ms. Black      |     | X   |         | Mr. Davis      | X   |     |         |
| Mr. Reed       |     | X   |         | Ms. Sanchez    | X   |     |         |
| Mr. Kelly      |     | X   |         | Mr. Higgins    | X   |     |         |
| Mr. Renacci    |     |     |         | Ms. Sewell     |     |     |         |
| Ms. Noem       |     | X   |         | Ms. DelBene    | X   |     |         |
| Mr. Holding    |     |     |         | Ms. Chu        | X   |     |         |
| Mr. Smith (MO) |     | X   |         |                |     |     |         |
| Mr. Rice       |     |     |         |                |     |     |         |
| Mr. Schweikert |     | X   |         |                |     |     |         |
| Ms. Walorski   |     | X   |         |                |     |     |         |
| Mr. Curbelo    |     | X   |         |                |     |     |         |
| Mr. Bishop     |     | X   |         |                |     |     |         |
| Mr. LaHood     |     | X   |         |                |     |     |         |
| Mr. Wenstrup   |     | X   |         |                |     |     |         |

In compliance with the Rules of the House of Representatives, the following statement is made concerning the vote of the Committee on Ways and Means during the markup consideration of H.R. 6760, “Protecting Family and Small Business Tax Cuts Act of 2018” on September 13, 2018.

The vote on Mr. Reichert’s motion to table Mr. Doggett’s appeal of the ruling of the Chair was agreed to by a roll call vote of 21 yeas to 15 nays. The vote was as follows:

| Representative | Yea | Nay | Present | Representative | Yea | Nay | Present |
|----------------|-----|-----|---------|----------------|-----|-----|---------|
| Mr. Brady      | X   |     |         | Mr. Neal       |     | X   |         |
| Mr. Johnson    | X   |     |         | Mr. Levin      |     | X   |         |
| Mr. Nunes      | X   |     |         | Mr. Lewis      |     | X   |         |
| Mr. Reichert   | X   |     |         | Mr. Doggett    |     | X   |         |
| Mr. Roskam     | X   |     |         | Mr. Thompson   |     | X   |         |
| Mr. Buchanan   | X   |     |         | Mr. Larson     |     | X   |         |
| Mr. Smith (NE) | X   |     |         | Mr. Blumenauer |     | X   |         |
| Ms. Jenkins    | X   |     |         | Mr. Kind       |     | X   |         |
| Mr. Paulsen    | X   |     |         | Mr. Pascrell   |     | X   |         |
| Mr. Marchant   | X   |     |         | Mr. Crowley    |     | X   |         |
| Ms. Black      | X   |     |         | Mr. Davis      |     | X   |         |
| Mr. Reed       | X   |     |         | Ms. Sanchez    |     | X   |         |
| Mr. Kelly      | X   |     |         | Mr. Higgins    |     | X   |         |
| Mr. Renacci    |     |     |         | Ms. Sewell     |     |     |         |
| Ms. Noem       | X   |     |         | Ms. DelBene    |     | X   |         |
| Mr. Holding    |     |     |         | Ms. Chu        |     | X   |         |
| Mr. Smith (MO) | X   |     |         |                |     |     |         |
| Mr. Rice       |     |     |         |                |     |     |         |
| Mr. Schweikert | X   |     |         |                |     |     |         |
| Ms. Walorski   | X   |     |         |                |     |     |         |
| Mr. Curbelo    | X   |     |         |                |     |     |         |
| Mr. Bishop     | X   |     |         |                |     |     |         |
| Mr. LaHood     | X   |     |         |                |     |     |         |
| Mr. Wenstrup   | X   |     |         |                |     |     |         |

In compliance with the Rules of the House of Representatives, the following statement is made concerning the vote of the Committee on Ways and Means during the markup consideration of H.R. 6760, “Protecting Family and Small Business Tax Cuts Act of 2018” on September 13, 2018.

The vote on the amendment offered by Mr. Larson to the amendment in the nature of a substitute to H.R. 6760, which would condition the provisions of the bill on an actuarial certification regarding the Social Security and Medicare Trust Funds was not agreed to by a roll call vote of 15 yeas to 21 nays (with a quorum being present). The vote was as follows:

| Representative | Yea | Nay | Present | Representative | Yea | Nay | Present |
|----------------|-----|-----|---------|----------------|-----|-----|---------|
| Mr. Brady      |     | X   |         | Mr. Neal       | X   |     |         |
| Mr. Johnson    |     | X   |         | Mr. Levin      | X   |     |         |
| Mr. Nunes      |     | X   |         | Mr. Lewis      | X   |     |         |
| Mr. Reichert   |     | X   |         | Mr. Doggett    | X   |     |         |
| Mr. Roskam     |     | X   |         | Mr. Thompson   | X   |     |         |
| Mr. Buchanan   |     | X   |         | Mr. Larson     | X   |     |         |
| Mr. Smith (NE) |     | X   |         | Mr. Blumenauer |     |     |         |
| Ms. Jenkins    |     | X   |         | Mr. Kind       | X   |     |         |
| Mr. Paulsen    |     | X   |         | Mr. Pascrell   | X   |     |         |
| Mr. Marchant   |     | X   |         | Mr. Crowley    | X   |     |         |
| Ms. Black      |     | X   |         | Mr. Davis      | X   |     |         |
| Mr. Reed       |     | X   |         | Ms. Sanchez    | X   |     |         |
| Mr. Kelly      |     | X   |         | Mr. Higgins    | X   |     |         |
| Mr. Renacci    |     |     |         | Ms. Sewell     | X   |     |         |
| Ms. Noem       |     | X   |         | Ms. DelBene    | X   |     |         |

| Representative       | Yea   | Nay   | Present | Representative | Yea | Nay   | Present |
|----------------------|-------|-------|---------|----------------|-----|-------|---------|
| Mr. Holding .....    | ..... | ..... | .....   | Ms. Chu .....  | X   | ..... | .....   |
| Mr. Smith (MO) ..... | ..... | X     | .....   |                |     |       |         |
| Mr. Rice .....       | ..... |       | .....   |                |     |       |         |
| Mr. Schweikert ..... | ..... | X     | .....   |                |     |       |         |
| Ms. Walorski .....   | ..... | X     | .....   |                |     |       |         |
| Mr. Curbelo .....    | ..... | X     | .....   |                |     |       |         |
| Mr. Bishop .....     | ..... | X     | .....   |                |     |       |         |
| Mr. LaHood .....     | ..... | X     | .....   |                |     |       |         |
| Mr. Wenstrup .....   | ..... | X     | .....   |                |     |       |         |

In compliance with the Rules of the House of Representatives, the following statement is made concerning the vote of the Committee on Ways and Means during the markup consideration of H.R. 6760, "Protecting Family and Small Business Tax Cuts Act of 2018" on September 13, 2018.

The vote on Mr. Reichert's motion to table Mr. Doggett's appeal of the ruling of the Chair was agreed to by a roll call vote of 21 yeas to 15 nays. The vote was as follows:

| Representative       | Yea   | Nay   | Present | Representative       | Yea   | Nay | Present |
|----------------------|-------|-------|---------|----------------------|-------|-----|---------|
| Mr. Brady .....      | X     | ..... | .....   | Mr. Neal .....       | ..... | X   | .....   |
| Mr. Johnson .....    | X     | ..... | .....   | Mr. Levin .....      | ..... | X   | .....   |
| Mr. Nunes .....      | X     | ..... | .....   | Mr. Lewis .....      | ..... | X   | .....   |
| Mr. Reichert .....   | X     | ..... | .....   | Mr. Doggett .....    | ..... | X   | .....   |
| Mr. Roskam .....     | X     | ..... | .....   | Mr. Thompson .....   | ..... | X   | .....   |
| Mr. Buchanan .....   | X     | ..... | .....   | Mr. Larson .....     | ..... | X   | .....   |
| Mr. Smith (NE) ..... | X     | ..... | .....   | Mr. Blumenauer ..... | ..... |     | .....   |
| Ms. Jenkins .....    | X     | ..... | .....   | Mr. Kind .....       | ..... | X   | .....   |
| Mr. Paulsen .....    | X     | ..... | .....   | Mr. Pascrell .....   | ..... | X   | .....   |
| Mr. Marchant .....   | X     | ..... | .....   | Mr. Crowley .....    | ..... | X   | .....   |
| Ms. Black .....      | X     | ..... | .....   | Mr. Davis .....      | ..... | X   | .....   |
| Mr. Reed .....       | X     | ..... | .....   | Ms. Sanchez .....    | ..... | X   | .....   |
| Mr. Kelly .....      | X     | ..... | .....   | Mr. Higgins .....    | ..... | X   | .....   |
| Mr. Renacci .....    | ..... | ..... | .....   | Ms. Sewell .....     | ..... | X   | .....   |
| Ms. Noem .....       | X     | ..... | .....   | Ms. DelBene .....    | ..... | X   | .....   |
| Mr. Holding .....    | ..... | ..... | .....   | Ms. Chu .....        | ..... | X   | .....   |
| Mr. Smith (MO) ..... | X     | ..... | .....   |                      |       |     |         |
| Mr. Rice .....       | ..... | ..... | .....   |                      |       |     |         |
| Mr. Schweikert ..... | X     | ..... | .....   |                      |       |     |         |
| Ms. Walorski .....   | X     | ..... | .....   |                      |       |     |         |
| Mr. Curbelo .....    | X     | ..... | .....   |                      |       |     |         |
| Mr. Bishop .....     | X     | ..... | .....   |                      |       |     |         |
| Mr. LaHood .....     | X     | ..... | .....   |                      |       |     |         |
| Mr. Wenstrup .....   | X     | ..... | .....   |                      |       |     |         |

In compliance with the Rules of the House of Representatives, the following statement is made concerning the vote of the Committee on Ways and Means during the markup consideration of H.R. 6760, "Protecting Family and Small Business Tax Cuts Act of 2018" on September 13, 2018.

H.R. 6760 was ordered favorably reported to the House of Representatives as amended by an amendment in the nature of a substitute offered by Chairman Brady by a roll call vote of 21 yeas to 15 nays. The vote was as follows:

| Representative     | Yea | Nay   | Present | Representative     | Yea   | Nay | Present |
|--------------------|-----|-------|---------|--------------------|-------|-----|---------|
| Mr. Brady .....    | X   | ..... | .....   | Mr. Neal .....     | ..... | X   | .....   |
| Mr. Johnson .....  | X   | ..... | .....   | Mr. Levin .....    | ..... | X   | .....   |
| Mr. Nunes .....    | X   | ..... | .....   | Mr. Lewis .....    | ..... | X   | .....   |
| Mr. Reichert ..... | X   | ..... | .....   | Mr. Doggett .....  | ..... | X   | .....   |
| Mr. Roskam .....   | X   | ..... | .....   | Mr. Thompson ..... | ..... | X   | .....   |



| Representative       | Yea   | Nay   | Present | Representative       | Yea   | Nay   | Present |
|----------------------|-------|-------|---------|----------------------|-------|-------|---------|
| Mr. Buchanan .....   | X     | ..... | .....   | Mr. Larson .....     | ..... | X     | .....   |
| Mr. Smith (NE) ..... | X     | ..... | .....   | Mr. Blumenauer ..... | ..... | ..... | .....   |
| Ms. Jenkins .....    | X     | ..... | .....   | Mr. Kind .....       | ..... | X     | .....   |
| Mr. Paulsen .....    | X     | ..... | .....   | Mr. Pascrell .....   | ..... | X     | .....   |
| Mr. Marchant .....   | X     | ..... | .....   | Mr. Crowley .....    | ..... | X     | .....   |
| Ms. Black .....      | X     | ..... | .....   | Mr. Davis .....      | ..... | X     | .....   |
| Mr. Reed .....       | X     | ..... | .....   | Ms. Sanchez .....    | ..... | X     | .....   |
| Mr. Kelly .....      | X     | ..... | .....   | Mr. Higgins .....    | ..... | X     | .....   |
| Mr. Renacci .....    | ..... | ..... | .....   | Ms. Sewell .....     | ..... | X     | .....   |
| Ms. Noem .....       | X     | ..... | .....   | Ms. DelBene .....    | ..... | X     | .....   |
| Mr. Holding .....    | ..... | ..... | .....   | Ms. Chu .....        | ..... | X     | .....   |
| Mr. Smith (MO) ..... | X     | ..... | .....   |                      |       |       |         |
| Mr. Rice .....       | ..... | ..... | .....   |                      |       |       |         |
| Mr. Schweikert ..... | X     | ..... | .....   |                      |       |       |         |
| Ms. Walorski .....   | X     | ..... | .....   |                      |       |       |         |
| Mr. Curbelo .....    | X     | ..... | .....   |                      |       |       |         |
| Mr. Bishop .....     | X     | ..... | .....   |                      |       |       |         |
| Mr. LaHood .....     | X     | ..... | .....   |                      |       |       |         |
| Mr. Wenstrup .....   | X     | ..... | .....   |                      |       |       |         |

### III. BUDGET EFFECTS OF THE BILL

#### A. COMMITTEE ESTIMATE OF BUDGETARY EFFECTS

In compliance with clause 3(d) of rule XIII of the Rules of the House of Representatives, the following statement is made concerning the effects on the budget of the bill, H.R. 6760, as reported.

The bill, as reported, is estimated to have the following effect on Federal fiscal year budget receipts for the period 2019–2028:

ESTIMATED BUDGET EFFECTS OF H.R. 6760,  
THE "PROTECTING FAMILY AND SMALL BUSINESS TAX CUTS ACT OF 2018,"  
AS REPORTED BY THE COMMITTEE ON WAYS AND MEANS

Fiscal Years 2019 - 2028

[Millions of Dollars]

| Provision  | Effective                  | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025   | 2026    | 2027     | 2028     | 2019-23 | 2019-28  |
|--|----------------------------|------|------|------|------|------|------|--------|---------|----------|----------|---------|----------|
| <b>I. Individual Reform Made Permanent</b>   |                            |      |      |      |      |      |      |        |         |          |          |         |          |
| A. Simplification and Reform of Rates, Standard Deductions, and Exemptions   |                            |      |      |      |      |      |      |        |         |          |          |         |          |
| 1. 10%, 12%, 22%, 24%, 32%, 35%, and 37% income tax rate brackets [1][2][3]  | tyba 12/31/17              | ---  | ---  | ---  | ---  | ---  | ---  | ---    | 128,895 | -191,704 | -201,134 | ---     | -521,733 |
| 2. Modify standard deduction (\$12,000 for singles, \$24,000 for married filing jointly, \$18,000 for HoH) [2]   | tyba 12/31/17 generally    | ---  | ---  | ---  | ---  | ---  | ---  | ---    | -77,044 | -113,196 | -117,265 | ---     | -307,505 |
| 3. Repeal of deduction for personal exemptions [2]   | tyba 12/31/17              | ---  | ---  | ---  | ---  | ---  | ---  | ---    | 125,020 | 183,636  | 190,119  | ---     | 498,775  |
| B. Treatment of Business Income of Individuals, Trusts, and Estates  |                            |      |      |      |      |      |      |        |         |          |          |         |          |
| 1. Allow 20 percent deduction of qualified business income and certain dividends for individuals and for gross income of agricultural or horticultural cooperatives  | generally<br>tyba 12/31/17 | ---  | ---  | ---  | ---  | ---  | ---  | -5,698 | -38,133 | -64,337  | -70,797  | ---     | -178,965 |
| 2. Disallow active pass-through losses in excess of \$500,000 for joint filers, \$250,000 for all others   | tyba 12/31/17              | ---  | ---  | ---  | ---  | ---  | ---  | ---    | 15,859  | 27,204   | 28,504   | ---     | 71,568   |
| C. Reform of the Child Tax Credit  |                            |      |      |      |      |      |      |        |         |          |          |         |          |
| 1. Modification of child tax credit: \$2,000 not indexed; refundable up to \$1,400 indexed down to nearest \$100 base year 2018; \$2,500 refundability threshold not indexed; \$500 other dependents not indexed; phase out \$200K-\$400K not indexed [2][3] | tyba 12/31/17              | ---  | ---  | ---  | ---  | ---  | ---  | ---    | -37,220 | -84,262  | -85,816  | ---     | -207,298 |
| 2. Require valid Social Security number of each child to claim refundable and non-refundable portions of child credit, non-child dependents and any child without a valid Social Security number still receives \$500 non-refundable credit [2][3]           | tyba 12/31/17              | ---  | ---  | ---  | ---  | ---  | ---  | ---    | 568     | 3,213    | 3,485    | ---     | 7,267    |

| Provision   | Effective                          | 2019        | 2020          | 2021          | 2022       | 2023       | 2024       | 2025          | 2026            | 2027            | 2028           | 2019-23       | 2019-28         |
|---|------------------------------------|-------------|---------------|---------------|------------|------------|------------|---------------|-----------------|-----------------|----------------|---------------|-----------------|
| D. Simplification and Reform of Deductions and Exclusions   |                                    |             |               |               |            |            |            |               |                 |                 |                |               |                 |
| 1. Repeat of itemized deductions for taxes not paid or accrued in a trade or business (except for up to \$10,000 in State and local taxes), interest on mortgage debt in excess of \$750K, interest on home equity debt, non-disaster casualty losses, and certain miscellaneous expenses [2][3]..... | generally<br>tyba 12/31/17         | ---         | ---           | ---           | ---        | ---        | ---        | 73,562        | 120,841         | 123,401         | ---            | ---           | 317,804         |
| 2. Increase percentage limit for charitable contributions of cash to public charities [5].....  | em tyba 12/31/17<br>tyba 12/31/17  | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 3. Repeat of overall limitation on itemized deductions.....   | tyba 12/31/17                      | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 4. Repeat exclusion for employer-provided bicycle commuter fringe benefit.....  | tyba 12/31/17                      | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 5. Repeat exclusion for employer-provided qualified moving expense reimbursements (other than members of the Armed Forces) [4].....   | tyba 12/31/17                      | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 6. Repeat of deduction for moving expenses (other than members of the Armed Forces).....  | tyba 12/31/17                      | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 7. Limitation on wagering losses.....   | tyba 12/31/17                      | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| E. Double Estate, Gift, and GST Tax Exemption Amount.....   | tyba 12/31/17                      | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| F. Increase the Individual AMT Exemption Amounts and Phase-out Thresholds.....  | dd & gma 12/31/17<br>tyba 12/31/17 | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| G. Other Provisions   |                                    |             |               |               |            |            |            |               |                 |                 |                |               |                 |
| 1. Allow for increased contributions to ABLE accounts; allow saver's credit for ABLE contributions.....   | tyba 12/31/17                      | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 2. Allow rollovers from 529 accounts to ABLE accounts.....  | Da 12/31/17                        | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 3. Treatment of certain individuals performing services in the Sinai Peninsula of Egypt.....  | spola 12/31/17                     | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 4. Treatment of student loans discharged on account of death or disability.....   | doia 12/31/17                      | ---         | ---           | ---           | ---        | ---        | ---        | ---           | ---             | ---             | ---            | ---           | ---             |
| 5. Confirm the 0%/15% breakpoints for capital gains and qualified dividends to the 12%/22% ordinary income breakpoints for individuals.....   | tyba 12/31/17                      | -42         | -26           | -25           | -32        | -24        | -26        | -33           | -36             | -43             | -44            | -149          | -332            |
| 6. Set AGI floor on itemized medical expenses to 7.5% for two years.....  | tyba 12/31/18                      | -346        | -1,931        | -1,593        | ---        | ---        | ---        | ---           | ---             | ---             | ---            | -3,869        | -3,869          |
| <b>NET TOTAL</b> .....  |                                    | <b>-388</b> | <b>-1,957</b> | <b>-1,618</b> | <b>-32</b> | <b>-24</b> | <b>-78</b> | <b>-6,102</b> | <b>-102,369</b> | <b>-250,376</b> | <b>267,959</b> | <b>-4,018</b> | <b>-630,898</b> |
| Joint Committee on Taxation   |                                    |             |               |               |            |            |            |               |                 |                 |                |               |                 |

NOTE: Details may not add to totals due to rounding. The date of enactment is generally assumed to be October 1, 2018.

*Legend and Footnotes for the Table appear on the following page.*



Clause 8 of rule XIII of the Rules of the House of Representatives requires that an estimate provided by the Joint Committee on Taxation to the Director of the Congressional Budget Office under section 201(f) of the Congressional Budget Act of 1974 for any major legislation shall, to the extent practicable, incorporate the budgetary effects of changes in economic output, employment, capital stock, and other macroeconomic variables resulting from such legislation. Major legislation is defined as legislation having a gross budgetary effect (before incorporating macroeconomic effects) that is greater in any fiscal year than 0.25 percent of the current projected gross domestic product of the United States for that fiscal year. The bill meets this definition of major legislation.

The staff of the Joint Committee on Taxation is currently analyzing changes in economic output, employment, capital stock, and other macroeconomic variables resulting from the bill for purposes of determining these budgetary effects. However, it was not practicable to complete this analysis, which requires accounting for the effects of each provision in this bill, along with interactions between these provisions, by the filing of this report.

B. STATEMENT REGARDING NEW BUDGET AUTHORITY AND TAX  
EXPENDITURES BUDGET AUTHORITY

In compliance with clause 3(c)(2) of rule XIII of the Rules of the House of Representatives, the Committee states that the bill involves no new or increased budget authority. The Committee further states that the revenue provisions involve no new tax expenditures.

C. COST ESTIMATE PREPARED BY THE CONGRESSIONAL BUDGET  
OFFICE

In compliance with clause 3(c)(3) of rule XIII of the Rules of the House of Representatives, requiring a cost estimate prepared by the CBO, the following statement by CBO is provided.

U.S. CONGRESS,  
CONGRESSIONAL BUDGET OFFICE,  
*Washington, DC, September 21, 2018.*

Hon. KEVIN BRADY,  
*Chairman, Committee on Ways and Means,  
House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 6760, the Protecting Family and Small Business Tax Cuts Act of 2018. It contains estimates of tax provisions prepared by the staff of the Joint Committee on Taxation.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Cecilia Pastrone.

Sincerely,

KEITH HALL,  
*Director.*

Enclosure.

*H.R. 6760—Protecting Family and Small Business Tax Cuts Act of 2018*

Summary: H.R. 6760, the Protecting Family and Small Business Tax Cuts Act of 2018, would repeal the December 31, 2025 expiration date for numerous provisions of U.S. tax law that were temporarily changed by the 2017 tax act (Public Law 115–97). The bill would make permanent the individual income tax brackets and tax rates, standard deduction and child tax credit amounts, business income deduction, and exemption amounts for the Alternative Minimum Tax in effect under current law. Deductions for personal exemptions and certain itemized deductions would be permanently repealed.

The staff of the Joint Committee on Taxation (JCT) estimates that enacting the bill would reduce revenues by about \$597 billion over the 2019–2028 period, and increase outlays by \$34 billion over the same period, leading to an increase in the deficit of \$631 billion over the next 10 years. A portion of the changes in revenues would be from Social Security payroll taxes, which are off-budget. Excluding the estimated \$687 million increase in off-budget revenues over the next 10 years, JCT estimates that H.R. 6760 would increase on-budget deficits by about \$632 billion over the period from 2019 to 2028. Pay-as-you-go procedures apply because enacting the legislation would affect direct spending and revenues.

JCT estimates that enacting H.R. 6760 would increase on-budget deficits by more than \$5 billion in at least one of the four 10-year periods beginning in 2029. CBO and JCT estimate that enacting the legislation would increase net direct spending by more than \$2.5 billion in at least one of the four consecutive 10-year periods beginning in 2029.

Because of the magnitude of the estimated budgetary effects, this bill is considered to be “major legislation,” as defined in section 5107 of H. Con. Res. 71, the Concurrent Resolution on the Budget for Fiscal Year 2018. Hence, it triggers the requirement that the cost estimate, to the extent practicable, include the budgetary impact of its macroeconomic effects. The staff of the Joint Committee on Taxation is currently analyzing changes in economic output, employment, capital stock, and other macroeconomic variables resulting from the bill for purposes of determining these budgetary effects. However, JCT indicates a macroeconomic analysis incorporating the full effects of all of the provisions in the bill, including interactions between these provisions, is not available at the time of filing of the committee report.

JCT has determined that the tax provisions of the bill contain no intergovernmental or private sector mandates as defined in the Unfunded Mandates Reform Act (UMRA).

Estimated cost to the Federal Government: The estimated budgetary effect of H.R. 6760 is shown in the following table.

Basis of estimate:

*Revenues and direct spending*

The Congressional Budget Act of 1974, as amended, stipulates that revenue estimates provided by the staff of the Joint Committee on Taxation will be the official estimates for all tax legislation considered by the Congress. As such, CBO incorporates those estimates into its cost estimates of the effects of legislation. All of

the estimates for the provisions of H.R. 6760 were provided by JCT.<sup>1</sup> The date of enactment is generally assumed to be October 1, 2018.

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<sup>1</sup> For JCT's description of the bill and estimates of the provisions, which include detail beyond the summary presented below, see Joint Committee on Taxation, Description Of H.R. 6760, the "Protecting Family And Small Business Tax Cuts Act Of 2018," JCX-69-18, <https://www.jct.gov/publications.html?func=startdown&id=5134>, and Estimated Revenue Effects of H.R. 6760, the "Protecting Family And Small Business Tax Cuts Act Of 2018," JCX-71-18, <https://www.jct.gov/publications.html?func=startdown&id=5136>.

|   | By fiscal year, in billions of dollars— |      |      |      |      |      |      |      |        |        |        |           |           |
|---|---|------|------|------|------|------|------|------|--------|--------|--------|-----------|-----------|
|   | 2018                                    | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2026   | 2027   | 2028   | 2019–2023 | 2019–2028 |
| <b>CHANGES IN REVENUES</b>                              |   |      |      |      |      |      |      |      |        |        |        |           |           |
| Estimated Changes in Revenues .....                     | 0                                       | -0.4 | -2.0 | -1.6 | 0.0  | 0.0  | -0.1 | -6.1 | -102.4 | -233.4 | -250.9 | -4.0      | -596.8    |
| On-Budget .....   | 0                                       | -0.4 | -2.0 | -1.6 | 0.0  | 0.0  | -0.1 | -6.1 | -102.6 | -233.6 | -251.1 | -4.0      | -597.5    |
| Off-Budget <sup>a</sup> .....                           | 0                                       | 0    | 0    | 0    | 0    | 0    | 0    | 0    | 0.2    | 0.2    | 0.3    | 0         | 0.7       |
| <b>CHANGES IN DIRECT SPENDING</b>                       |   |      |      |      |      |      |      |      |        |        |        |           |           |
| Total Changes in Direct Spending:                       |   |      |      |      |      |      |      |      |        |        |        |           |           |
| Estimated Budget Authority .....                        | 0                                       | 0    | 0    | 0    | 0    | 0    | 0    | 0    | 0      | 17.0   | 17.1   | 0         | 34.1      |
| Estimated Outlays .....                                 | 0                                       | 0    | 0    | 0    | 0    | 0    | 0    | 0    | 0      | 17.0   | 17.1   | 0         | 34.1      |
| <b>NET INCREASE OR DECREASE (-) IN THE DEFICIT FROM</b> |   |      |      |      |      |      |      |      |        |        |        |           |           |
| <b>CHANGES IN DIRECT SPENDING AND REVENUES</b>          |   |      |      |      |      |      |      |      |        |        |        |           |           |
| Effect on Deficit .....                                 | 0                                       | 0.4  | 2.0  | 1.6  | 0.0  | 0.0  | 0.1  | 6.1  | 102.4  | 250.4  | 268.0  | 4.0       | 630.9     |
| On-Budget Deficit .....                                 | 0                                       | 0.4  | 2.0  | 1.6  | 0.0  | 0.0  | 0.1  | 6.1  | 102.6  | 250.6  | 268.2  | 4.0       | 631.6     |
| Off-Budget Deficit .....                                | 0                                       | 0    | 0    | 0    | 0    | 0    | 0    | 0    | -0.2   | -0.2   | -0.3   | 0         | -0.7      |

Source: Staff of the Joint Committee on Taxation.  
 Components may not add to totals due to rounding.  
<sup>a</sup>Off-budget revenues result from changes in Social Security payroll tax receipts.



Individual Reform Made Permanent. H.R. 6760 would make permanent numerous changes to tax law pertaining to individuals made by the 2017 tax act. Such provisions estimated to reduce revenues over the 2019 to 2028 period include the following changes made by the 2017 tax act, which would no longer expire in 2026:

- Establish seven brackets with tax rates of 10 percent, 12 percent, 22 percent, 24 percent, 32 percent, 35 percent, and 37 percent;
- Increase the standard deduction;
- Establish a deduction for qualified business income;
- Repeal the overall limit on itemized deductions (“Pease limitation”);
- Increase the child tax credit, and add a \$500 credit for non-child dependents; and
- Double the exemption amount allowed under estate and gift taxes.

Provisions estimated to increase revenues over the 2019 to 2028 period include the following changes made by the 2017 tax act, which would no longer expire in 2026:

- Repeal deductions for personal exemptions; and
- Repeal and limit certain itemized deductions, including limiting the deduction for state and local taxes to \$10,000.

The largest revenue reductions would result from the provision to permanently extend the current income tax rate and bracket structure, which JCT estimates would reduce revenues by \$520 billion over the period from 2019 to 2028 and increase outlays for refundable tax credits by \$2 billion over the same period. In addition, extending the increase in the standard deduction would reduce revenues by \$286 billion over the period from 2019 to 2028 and increase outlays for refundable tax credits by \$21 billion over the same period, according to JCT’s estimates. Making the increased exemptions to the alternative minimum tax on individuals permanent would reduce revenues by \$283 billion from 2019 to 2028.

JCT also estimates that permanently extending the deduction for qualified business income would reduce revenues by \$179 billion over the period from 2019 to 2028, and that extending the modified child tax credit would, over the same 10-year period, reduce revenues by \$155 billion and increase outlays for refundable tax credits by \$53 billion. JCT estimates that additional revenue reductions, totaling \$28 billion from 2019 to 2028, would result from making the 2017 tax act modifications to estate and gift taxes permanent.

The largest revenue increases would result from permanently repealing deductions for personal exemptions, which JCT estimates would increase revenues by \$463 billion and reduce outlays for refundable credits by \$36 billion over the 2019 to 2028 period. In addition, JCT estimates that the permanent repeal and limitation of certain itemized deductions would increase revenues by \$317 billion and reduce outlays for refundable credits by \$828 million from 2019 to 2028.

Pay-As-You-Go considerations: The Statutory Pay-As-You-Go Act of 2010 establishes budget-reporting and enforcement procedures for legislation affecting direct spending or revenues. The net changes in outlays and revenues that are subject to those pay-as-you-go procedures are shown in the following table. Only on-budget

changes to outlays or revenues are subject to pay-as-you-go procedures.

**CBO ESTIMATE OF PAY-AS-YOU-GO EFFECTS FOR H.R. 6760, AS ORDERED REPORTED BY THE HOUSE COMMITTEE ON WAYS AND MEANS ON SEPTEMBER 13, 2018**

|                                       | By fiscal year, in billions of dollars—      |      |      |      |      |      |      |      |        |        |        |           |           |
|---------------------------------------|--|------|------|------|------|------|------|------|--------|--------|--------|-----------|-----------|
|                                       | 2018   | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2026   | 2027   | 2028   | 2019–2023 | 2019–2028 |
|                                       | <b>NET INCREASE IN THE ON-BUDGET DEFICIT</b> |      |      |      |      |      |      |      |        |        |        |           |           |
| Statutory Pay-As-You-Go Effects ..... | 0  | 0.4  | 2.0  | 1.6  | 0.0  | 0.0  | 0.1  | 6.1  | 102.6  | 250.6  | 268.2  | 4.0       | 631.6     |
| Memorandum: <sup>a</sup>              |  |      |      |      |      |      |      |      |        |        |        |           |           |
| Change in Outlays .....               | 0  | 0    | 0    | 0    | 0    | 0    | 0    | 0    | 0      | 17.0   | 17.1   | 0         | 34.1      |
| Change in On-Budget Revenues .....    | 0  | -0.4 | -2.0 | -1.6 | 0.0  | 0.0  | -0.1 | -6.1 | -102.6 | -233.6 | -251.1 | -4.0      | -597.5    |

Source: Staff of the Joint Committee on Taxation.

Components may not add to totals due to rounding.

<sup>a</sup>A positive sign for outlays indicates an increase in outlays. A negative sign for revenues indicates a reduction in revenues.

Increase in long term direct spending and deficits: JCT estimates that enacting H.R. 6760 would increase on-budget deficits by more than \$5 billion in at least one of the four 10-year periods beginning in 2029. CBO and JCT estimate that enacting the legislation would increase net direct spending by more than \$2.5 billion in at least one of the four consecutive 10-year periods beginning in 2029.

Mandates: JCT has determined that H.R. 6760 contains no private-sector or intergovernmental mandates as defined by UMRA.

Estimate prepared by: Staff of the Joint Committee on Taxation and Cecilia Pastrone.

Estimate reviewed by: Joshua Shakin, Chief, Revenue Estimating Unit; John McClelland, Assistant Director for Tax Analysis.

## **V. OTHER MATTERS TO BE DISCUSSED UNDER THE RULES OF THE HOUSE**

### A. COMMITTEE OVERSIGHT FINDINGS AND RECOMMENDATIONS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the Committee advises that the findings and recommendations of the Committee, based on oversight activities under clause 2(b)(1) of rule X of the Rules of the House of Representatives, are incorporated into the description portions of this report.

### B. STATEMENT OF GENERAL PERFORMANCE GOALS AND OBJECTIVES

With respect to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee advises that the bill contains no measure that authorizes funding, so no statement of general performance goals and objectives for which any measure authorizes funding is required.

### C. INFORMATION RELATING TO UNFUNDED MANDATES

This information is provided in accordance with section 423 of the Unfunded Mandates Reform Act of 1995 (Pub. L. No. 104-4).

The Committee has determined that the bill does not contain Federal mandates on the private sector. The Committee has determined that the bill does not impose a Federal intergovernmental mandate on State, local, or tribal governments.

### D. APPLICABILITY OF HOUSE RULE XXI 5(b)

Rule XXI 5(b) of the Rules of the House of Representatives provides, in part, that “A bill or joint resolution, amendment, or conference report carrying a Federal income tax rate increase may not be considered as passed or agreed to unless so determined by a vote of not less than three-fifths of the Members voting, a quorum being present.” The Committee has carefully reviewed the bill and states that the bill does not involve any Federal income tax rate increases within the meaning of the rule.

### E. TAX COMPLEXITY ANALYSIS

Section 4022(b) of the Internal Revenue Service Restructuring and Reform Act of 1998 (“IRS Reform Act”) requires the staff of the Joint Committee on Taxation (in consultation with the Internal

Revenue Service and the Treasury Department) to provide a tax complexity analysis. The complexity analysis is required for all legislation reported by the Senate Committee on Finance, the House Committee on Ways and Means, or any committee of conference if the legislation includes a provision that directly or indirectly amends the Internal Revenue Code of 1986 and has widespread applicability to individuals or small businesses.

Pursuant to clause 3(h)(1) of rule XIII of the Rules of the House of Representatives, for each such provision identified by the staff of the Joint Committee on Taxation, a summary description of the provision is provided below along with an estimate of the number and type of affected taxpayers, and a discussion regarding the relevant complexity and administrative issues.

Following the analysis of the staff of the Joint Committee on Taxation are the comments of the IRS and Treasury regarding each provision included in the complexity analysis.

*Make permanent modification of tax rates, tax brackets, standard deduction and repeal of personal exemptions (secs. 101, 121, and 141 of the bill)*

*Summary description of the provisions*

The bill makes permanent the structure of the individual income tax as modified in Pub. L. No. 97–115. Under the permanent rate structure, the tax brackets are 10-percent, 12-percent, 22-percent, 24-percent, 32-percent, 35-percent and 37-percent. The bill makes permanent the increase in the size the standard deduction amount (for 2018 the standard deduction is \$24,000 for joint filers, \$18,000 for heads of household and \$12,000 for other filers), and makes permanent the elimination of personal exemptions.

*Number of affected taxpayers*

It is estimated that the provision will affect approximately 129 million tax returns in 2026.

*Discussion*

It is not anticipated that individuals will need to keep additional records due to these provisions. It should not result in an increase in disputes with the IRS, nor will regulatory guidance be necessary to implement this provision.

The provision will save the IRS from needing to re-adjust its wage withholding tables to reflect the expiration of these provisions for the taxable year 2026. Further, the IRS will no longer need to modify its forms and publications to reflect the expiration of these provisions for taxable year 2026.

Taxpayers who, under the provisions of Pub. L. No. 115–97, were able to claim the standard deduction rather than itemizing, will now continue to be able to do so after taxable year 2025. According to estimates by the staff of the Joint Committee on Taxation, approximately 89 percent of taxpayers will claim the standard deduction in 2026 under the bill, up from approximately 70 percent in 2017. For these taxpayers, it will not be necessary to file Schedule A to Form 1040, allowing a significant number to forgo record keeping inherent in itemizing below-the-line deductions. Moreover, by claiming the standard deduction, such taxpayers may qualify to

use simpler versions of the Form 1040 (*i.e.*, Form 1040EZ or Form 1040A) that are not available to individuals who itemize their deductions. These forms simplify the return preparation process by eliminating from the Form 1040 those items that do not apply to particular taxpayers.

This reduction in complexity and record keeping also may result in a decline in the number of individuals using a tax preparation service, or tax preparation software, or a decline in the cost of such service or software. The provision also should reduce the number of disputes between taxpayers and the IRS regarding the substantiation of itemized deductions.

*Make permanent the deduction for qualified business income (sec. 111 of the bill)*

*Summary description of the provisions*

The bill makes permanent the provision enacted in Pub. L. No. 115–97 (Code section 199A), as subsequently modified by Pub. L. No. 115–141. Under the provision, an individual taxpayer generally may deduct 20 percent of qualified business income from a partnership, S corporation, or sole proprietorship, as well as 20 percent of aggregate qualified REIT dividends and qualified publicly traded partnership income. Special rules apply to specified agricultural or horticultural cooperatives and their patrons.

A limitation based on the greater of 50 percent of W–2 wages paid, or the sum of 25 percent of W–2 wages paid plus a capital allowance, is phased in above a threshold amount of taxable income. A disallowance of the deduction with respect to specified service trades or businesses is also phased in above the same threshold amount of taxable income. The threshold amount is \$157,500 (twice that amount or \$315,000 in the case of a joint return), indexed. These limitations are fully phased in for a taxpayer with taxable income in excess of the threshold amount plus \$50,000 (\$100,000 in the case of a joint return).

Qualified business income for a taxable year generally means the net amount of domestic qualified items of income, gain, deduction, and loss with respect to the taxpayer’s qualified businesses. Qualified business income does not include any amount paid by an S corporation that is treated as reasonable compensation of the taxpayer. Similarly, qualified business income does not include any guaranteed payment for services rendered with respect to the trade or business, and to the extent provided in regulations, does not include any amount allocated or distributed by a partnership to a partner who is acting other than in his or her capacity as a partner for services. Qualified business income or loss does not include certain investment-related income, gain, deductions, or loss.

*Number of affected taxpayers*

It is estimated that the provision will affect over ten percent of small business tax returns.

*Discussion*

In the absence of making the provision permanent, the period of time with respect to which taxpayers could have to keep additional records, or might engage in disputes with the IRS regarding appli-

cation of the provision, would end. On the other hand, in the absence of making the provision permanent, the IRS would have to revise forms and promulgate revised guidance relating to the end of the period in which the provision applies. Making the provision permanent provides more time for a body of law, including regulations or other guidance, to clarify the application of the provision generally as well as in particular fact situations, potentially facilitating taxpayer compliance with, and IRS administration of, the provision as it remains in effect. Over time, increasing familiarity of the provision may result in a decline in the annual number of questions that taxpayers ask the IRS, such as how to calculate qualified business income and how to apply the phase-ins of the W-2 wage (or W-2 wage and capital) limit and of the exclusion of service business income in the case of taxpayers with taxable income exceeding the threshold amount of \$157,500 (twice that amount or \$315,000 in the case of a joint return), indexed. The possible decline in the volume of questions could improve efficiency of the IRS and permit the use of greater IRS resources for taxpayer service and administration of other aspects of the tax law. Making the provision permanent principally affects taxable years beginning after 2025, so the provision will have been in effect for several years by the end of 2025, potentially permitting tax advisors and tax software makers to improve aids for taxpayers' compliance. Consequently, making the provision permanent should not increase the tax preparation costs for most individuals.

*Increase in child tax credit made permanent (sec. 122 of the bill)*

*Summary description of the provisions*

The bill makes permanent the provision of Pub. L. No. 115-97 that increases the value of the child tax credit to \$2,000, and providing for a refundable child tax credit of up to \$1,400 per child. This \$1,400 limitation is indexed for inflation. In order to qualify for the child tax credit, a Social Security number must be provided for the qualifying child for whom such credit is claimed.

*Number of affected taxpayers*

It is estimated that the provision will affect approximately 53 million tax returns in 2026.

*Discussion*

It is not anticipated that individuals will need to keep additional records due to these provisions. It should not result in an increase in disputes with the IRS, nor will regulatory guidance be necessary to implement this provision.

The IRS will no longer need to modify its forms and publications for taxable year 2026 to reflect the expiration of this provision.

*Make permanent the limitation on deduction for State and local income taxes (sec. 142 of the bill)*

*Summary description of the provisions*

The bill makes permanent the provision contained in Pub. L. No. 115-97 which provides that, the case of an individual, as a general matter, State, local, and foreign property taxes and State and local sales taxes are allowed as a deduction only when paid or accrued

in carrying on a trade or business, or an activity described in section 212 (relating to expenses for the production of income).

The bill makes permanent the exception provided by Pub. L. No. 115-97 to the above-stated rule. Under the provision a taxpayer may claim an itemized deduction of up to \$10,000 (\$5,000 for married taxpayer filing a separate return) for the aggregate of (i) State and local property taxes not paid or accrued in carrying on a trade or business, or an activity described in section 212, and (ii) State and local income, war profits, and excess profits taxes (or sales taxes in lieu of income, etc. taxes) paid or accrued in the taxable year. Foreign real property taxes may not be deducted under this exception.

*Number of affected taxpayers*

It is estimated that the provision will affect approximately 19 million tax returns in 2026.

*Discussion*

It is not anticipated that individuals will need to keep additional records due to this provision.

To the extent the IRS would have needed to modify its forms and publications to reflect the expiration of this provision for taxable years beginning after 2025, it will no longer need to do so.





COMMISSIONER

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

September 20, 2018

Mr. Thomas A. Barthold  
Chief of Staff  
Joint Committee on Taxation  
Washington, D.C. 20515

Dear Mr. Barthold:

I am responding to your letter dated September 13, 2018, in which you requested a complexity analysis related to the Conference Report for H.R. 6760, the "Protecting Family and Small Business Tax Cuts Act of 2018."

Enclosed are the combined comments of the Internal Revenue Service (IRS) and the Treasury Department for inclusion in the complexity analysis in the Conference Report for H.R. 6760, the "Protecting Family and Small Business Tax Cuts Act of 2018."

Our analysis covers the four provisions that you preliminarily identified in your letter: make permanent modification of tax rates, tax brackets, standard deduction and repeal of personal exemptions; make permanent the deduction for qualified business income; increase in child tax credit made permanent; make permanent the limitation on deduction for State and local income taxes.

Please note that for purposes of this complexity analysis, IRS staff assumed timely enactment of this legislation. If legislation is not enacted before the end of the year, there would be complexity for IRS and for taxpayers that is not addressed in this response.

Our comments are based on the description of the provision provided in your letter. This analysis does not include the administrative cost estimates for the changes that would be required. Due to the short turnaround time, our comments are provisional and subject to change upon a more complete and in-depth analysis of the provisions.

Sincerely,

David J. Kautter  
Acting Commissioner

Enclosure

**COMPLEXITY ANALYSIS OF H.R. 6760  
PROTECTING FAMILY AND SMALL BUSINESS TAX CUTS ACT OF 2018**

**1. Make permanent modification of tax rates, tax brackets, standard deduction and repeal of personal exemptions (secs. 101, 121, and 141 of the bill)**

The bill makes permanent the structure of the individual income tax as modified in Pub. L. No. 97-115. Under the permanent rate structure, the tax brackets are 10-percent, 12-percent, 22-percent, 24-percent, 32-percent, 35-percent and 37-percent. The bill makes permanent the increase in the size of the standard deduction amount (for 2018 the standard deduction is \$24,000 for joint filers, \$18,000 for heads of household and \$12,000 for other filers), and makes permanent the elimination of personal exemptions.

**IRS and Treasury Comments:**

- Internal Revenue Manuals and employee training would need to be updated.
- Training materials for new employees would need to be updated.
- Internal communications would be shared with all employees.
- Communications would be needed for external stakeholders.
- IRS.gov updates would need to be provided.

**2. Make permanent the deduction for qualified business income (sec. 111 of the bill)**

The bill makes permanent the provision enacted in Pub. L. No. 115-97 (Code section 199A), as subsequently modified by Pub. L. No. 115-141. Under the provision, an individual taxpayer generally may deduct 20 percent of qualified business income from a partnership, S corporation, or sole proprietorship, as well as 20 percent of aggregate qualified REIT dividends and qualified publicly traded partnership income. Special rules apply to specified agricultural or horticultural cooperatives and their patrons.

A limitation based on the greater of 50 percent of W-2 wages paid, or the sum of 25 percent of W-2 wages paid plus a capital allowance, is phased in above a threshold amount of taxable income. A disallowance of the deduction with respect to specified service trades or businesses is also phased in above the same threshold amount of taxable income. The threshold amount is \$157,500 (twice that amount or \$315,000 in the case of a joint return), indexed. These limitations are fully phased in for a taxpayer with taxable income in excess of the threshold amount plus \$50,000 (\$100,000 in the case of a joint return).

Qualified business income for a taxable year generally means the net amount of domestic qualified items of income, gain, deduction, and loss with respect to the taxpayer's qualified businesses. Qualified business income does not include any amount paid by an S corporation that is treated as reasonable compensation of the taxpayer. Similarly, qualified business income does not include any guaranteed payment for services rendered with respect to the trade or business, and to the extent provided in regulations, does not include any amount allocated or distributed by a partnership to a partner who is acting other than in his or her capacity as a partner for services. Qualified business income or loss does not include certain investment-related income, gain, deductions, or loss.

**IRS and Treasury Comments:**

- Internal Revenue Manuals and employee training would need to be updated.
- Training materials for new employees would need to be updated.
- Internal communications would be shared with all employees.
- Communications would be needed for external stakeholders.
- IRS.gov updates would need to be provided.

**3. Increase in child tax credit made permanent (sec. 122 of the bill)**

The bill makes permanent the provision of Pub. L. No. 115-97 that increases the value of the child tax credit to \$2,000, and providing for a refundable child tax credit of up to \$1,400 per child. This \$1,400 limitation is indexed for inflation. In order to qualify for the child tax credit, a Social Security number must be provided for the qualifying child for whom such credit is claimed.

**IRS and Treasury Comments:**

- Internal Revenue Manuals and employee training would need to be updated.
- Training materials for new employees would need to be updated.
- Internal communications would be shared with all employees.
- Communications would be needed for external stakeholders.
- IRS.gov updates would need to be provided.

**4. Make permanent the limitation on deduction for State and local income taxes (sec. 142 of the bill)**

The bill makes permanent the provision contained in Pub. L. No. 115-97 which provides that, the case of an individual, as a general matter, State, local, and foreign property taxes and State and local sales taxes are allowed as a deduction

only when paid or accrued in carrying on a trade or business, or an activity described in section 212 (relating to expenses for the production of income).

The bill makes permanent the exception provided by Pub. L. No. 115-97 to the above-stated rule. Under the provision a taxpayer may claim an itemized deduction of up to \$10,000 (\$5,000 for married taxpayer filing a separate return) for the aggregate of (i) State and local property taxes not paid or accrued in carrying on a trade or business, or an activity described in section 212, and (ii) State and local income, war profits, and excess profits taxes (or sales taxes in lieu of income, etc. taxes) paid or accrued in the taxable year. Foreign real property taxes may not be deducted under this exception.

**IRS and Treasury Comments:**

- Internal Revenue Manuals and employee training would need to be updated.
- Training materials for new employees would need to be updated.
- Internal communications would be shared with all employees.
- Communications would be needed for external stakeholders.
- IRS.gov updates would need to be provided.

F. CONGRESSIONAL EARMARKS, LIMITED TAX BENEFITS, AND  
LIMITED TARIFF BENEFITS

With respect to clause 9 of rule XXI of the Rules of the House of Representatives, the Committee has carefully reviewed the provisions of the bill and states that the provisions of the bill do not contain any congressional earmarks, limited tax benefits, or limited tariff benefits within the meaning of the rule.

G. DUPLICATION OF FEDERAL PROGRAMS

In compliance with Sec. 3(c)(5) of rule XIII of the Rules of the House of Representatives, the Committee states that no provision of the bill establishes or reauthorizes: (1) a program of the Federal Government known to be duplicative of another Federal program, (2) a program included in any report from the Government Accountability Office to Congress pursuant to section 21 of Public Law 111–139, or (3) a program related to a program identified in the most recent Catalog of Federal Domestic Assistance, published pursuant to section 6104 of title 31, United States Code.

H. DISCLOSURE OF DIRECTED RULE MAKINGS

In compliance with Sec. 3(i) of H. Res. 5 (115th Congress), the following statement is made concerning directed rule makings: The Committee advises that the bill requires no directed rule makings within the meaning of such section.

**VI. CHANGES IN EXISTING LAW MADE BY THE BILL, AS  
REPORTED**

A. CHANGES IN EXISTING LAW PROPOSED BY THE BILL, AS REPORTED

In compliance with clause 3(e)(1)(B) of rule XIII of the Rules of the House of Representatives, changes in existing law proposed by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, and existing law in which no change is proposed is shown in roman):

**INTERNAL REVENUE CODE OF 1986**

\* \* \* \* \*

**Subtitle A—Income Taxes**

\* \* \* \* \*

**CHAPTER 1—NORMAL TAXES AND SURTAXES**

\* \* \* \* \*

**Subchapter A—Determination of Tax Liability**

\* \* \* \* \*

**PART I—TAX ON INDIVIDUALS**

\* \* \* \* \*

**SEC. 1. TAX IMPOSED.**

(a) **MARRIED INDIVIDUALS FILING JOINT RETURNS AND SURVIVING SPOUSES.**—There is hereby imposed on the taxable income of—

(1) every married individual (as defined in section 7703) who makes a single return jointly with his spouse under section 6013, and

(2) every surviving spouse (as defined in section 2(a)), a tax determined in accordance with the following table:

| If taxable income is:                 | The tax is:  |
|---------------------------------------|--|
| Not over \$36,900                     | 15% of taxable income.                                 |
| Over \$36,900 but not over \$89,150   | \$5,535, plus 28% of the excess over \$36,900.         |
| Over \$89,150 but not over \$140,000  | \$20,165, plus 31% of the excess over \$89,150.        |
| Over \$140,000 but not over \$250,000 | \$35,928.50, plus 36% of the excess over \$140,000.    |
| Over \$250,000                        | \$75,528.50, plus 39.6% of the excess over \$250,000.】 |

| If taxable income is:                              | The tax is:  |
|--|--|
| <i>Not over \$19,050 .....</i>                     | <i>10% of taxable income.</i>                            |
| <i>Over \$19,050 but not over \$77,400 .....</i>   | <i>\$1,905, plus 12% of the excess over \$19,050.</i>    |
| <i>Over \$77,400 but not over \$165,000 .....</i>  | <i>\$8,907, plus 22% of the excess over \$77,400.</i>    |
| <i>Over \$165,000 but not over \$315,000 .....</i> | <i>\$28,179, plus 24% of the excess over \$165,000.</i>  |
| <i>Over \$315,000 but not over \$400,000 .....</i> | <i>\$64,179, plus 32% of the excess over \$315,000.</i>  |
| <i>Over \$400,000 but not over \$600,000 .....</i> | <i>\$91,379, plus 35% of the excess over \$400,000.</i>  |
| <i>Over \$600,000 .....</i>                        | <i>\$161,379, plus 37% of the excess over \$600,000.</i> |

(b) **HEADS OF HOUSEHOLDS.**—There is hereby imposed on the taxable income of every head of a household (as defined in section 2(b)) a tax determined in accordance with the following table:

| If taxable income is:                | The tax is:                                     |
|--------------------------------------|---|
| Not over \$29,600                    | 15% of taxable income.                          |
| Over \$29,600 but not over \$76,400  | \$4,440, plus 28% of the excess over \$29,600.  |
| Over \$76,400 but not over \$127,500 | \$17,544, plus 31% of the excess over \$76,400. |

| If taxable income is:                 | The tax is:   |
|---------------------------------------|---|
| Over \$127,500 but not over \$250,000 | \$33,385, plus 36% of the excess over \$127,500.    |
| Over \$250,000                        | \$77,485, plus 39.6% of the excess over \$250,000.】 |

| If taxable income is:                              | The tax is:  |
|--|--|
| <i>Not over \$13,600</i> .....                     | <i>10% of taxable income.</i>                            |
| <i>Over \$13,600 but not over \$51,800</i> .....   | <i>\$1,360, plus 12% of the excess over \$13,600.</i>    |
| <i>Over \$51,800 but not over \$82,500</i> .....   | <i>\$5,944, plus 22% of the excess over \$51,800.</i>    |
| <i>Over \$82,500 but not over \$157,500</i> .....  | <i>\$12,698, plus 24% of the excess over \$82,500.</i>   |
| <i>Over \$157,500 but not over \$200,000</i> ..... | <i>\$30,698, plus 32% of the excess over \$157,500.</i>  |
| <i>Over \$200,000 but not over \$500,000</i> ..... | <i>\$44,298, plus 35% of the excess over \$200,000.</i>  |
| <i>Over \$500,000</i> .....                        | <i>\$149,298, plus 37% of the excess over \$500,000.</i> |

(c) UNMARRIED INDIVIDUALS (OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLDS).—There is hereby imposed on the taxable income of every individual (other than a surviving spouse as defined in section 2(a) or the head of a household as defined in section 2(b)) who is not a married individual (as defined in section 7703) a tax determined in accordance with the following table:

| If taxable income is:                 | The tax is:   |
|---------------------------------------|---|
| Not over \$22,100                     | 15% of taxable income.                              |
| Over \$22,100 but not over \$53,500   | \$3,315, plus 28% of the excess over \$22,100.      |
| Over \$53,500 but not over \$115,000  | \$12,107, plus 31% of the excess over \$53,500.     |
| Over \$115,000 but not over \$250,000 | \$31,172, plus 36% of the excess over \$115,000.    |
| Over \$250,000                        | \$79,772, plus 39.6% of the excess over \$250,000.】 |

| If taxable income is:                              | The tax is:   |
|--|---|
| <i>Not over \$9,525</i> .....                      | <i>10% of taxable income.</i>                               |
| <i>Over \$9,525 but not over \$38,700</i> .....    | <i>\$952.50, plus 12% of the excess over \$9,525.</i>       |
| <i>Over \$38,700 but not over \$82,500</i> .....   | <i>\$4,453.50, plus 22% of the excess over \$38,700.</i>    |
| <i>Over \$82,500 but not over \$157,500</i> .....  | <i>\$14,089.50, plus 24% of the excess over \$82,500.</i>   |
| <i>Over \$157,500 but not over \$200,000</i> ..... | <i>\$32,089.50, plus 32% of the excess over \$157,500.</i>  |
| <i>Over \$200,000 but not over \$500,000</i> ..... | <i>\$45,689.50, plus 35% of the excess over \$200,000.</i>  |
| <i>Over \$500,000</i> .....                        | <i>\$150,689.50, plus 37% of the excess over \$500,000.</i> |

(d) **MARRIED INDIVIDUALS FILING SEPARATE RETURNS.**—There is hereby imposed on the taxable income of every married individual (as defined in section 7703) who does not make a single return jointly with his spouse under section 6013, a tax determined in accordance with the following table:

| <b>¶ If taxable income is:</b>       | <b>The tax is:</b>                                     |
|--------------------------------------|--|
| Not over \$18,450                    | 15% of taxable income.                                 |
| Over \$18,450 but not over \$44,575  | \$2,767.50, plus 28% of the excess over \$18,450.      |
| Over \$44,575 but not over \$70,000  | \$10,082.50, plus 31% of the excess over \$44,575.     |
| Over \$70,000 but not over \$125,000 | \$17,964.25, plus 36% of the excess over \$70,000.     |
| Over \$125,000                       | \$37,764.25, plus 39.6% of the excess over \$125,000.¶ |

| <b>If taxable income is:</b>                       | <b>The tax is:</b>   |
|--|--|
| <i>Not over \$9,525 .....</i>                      | <i>10% of taxable income.</i>                              |
| <i>Over \$9,525 but not over \$38,700 .....</i>    | <i>\$952.50, plus 12% of the excess over \$9,525.</i>      |
| <i>Over \$38,700 but not over \$82,500 .....</i>   | <i>\$4,453.50, plus 22% of the excess over \$38,700.</i>   |
| <i>Over \$82,500 but not over \$157,500 .....</i>  | <i>\$14,089.50, plus 24% of the excess over \$82,500.</i>  |
| <i>Over \$157,500 but not over \$200,000 .....</i> | <i>\$32,089.50, plus 32% of the excess over \$157,500.</i> |
| <i>Over \$200,000 but not over \$300,000 .....</i> | <i>\$45,689.50, plus 35% of the excess over \$200,000.</i> |
| <i>Over \$300,000 .....</i>                        | <i>\$80,689.50, plus 37% of the excess over \$300,000.</i> |

(e) **ESTATES AND TRUSTS.**—There is hereby imposed on the taxable income of—

- (1) every estate, and
- (2) every trust, taxable under this subsection a tax determined in accordance with the following table:

| <b>¶ If taxable income is:</b>    | <b>The tax is:</b>                               |
|-----------------------------------|--|
| Not over \$1,500                  | 15% of taxable income.                           |
| Over \$1,500 but not over \$3,500 | \$225, plus 28% of the excess over \$1,500.      |
| Over \$3,500 but not over \$5,500 | \$785, plus 31% of the excess over \$3,500.      |
| Over \$5,500 but not over \$7,500 | \$1,405, plus 36% of the excess over \$5,500.    |
| Over \$7,500                      | \$2,125, plus 39.6% of the excess over \$7,500.¶ |

| <b>If taxable income is:</b>                    | <b>The tax is:</b>                                       |
|---|--|
| <i>Not over \$2,550 .....</i>                   | <i>10% of taxable income.</i>                            |
| <i>Over \$2,550 but not over \$9,150 .....</i>  | <i>\$255, plus 24% of the excess over \$2,550.</i>       |
| <i>Over \$9,150 but not over \$12,500 .....</i> | <i>\$1,839, plus 35% of the excess over \$9,150.</i>     |
| <i>Over \$12,500 .....</i>                      | <i>\$3,011.50, plus 37% of the excess over \$12,500.</i> |



(f) **【PHASEOUT OF MARRIAGE PENALTY IN 15-PERCENT BRACKET; ADJUSTMENTS】** *ADJUSTMENTS* IN TAX TABLES SO THAT INFLATION WILL NOT RESULT IN TAX INCREASES.—

(1) **IN GENERAL.**—Not later than December 15 of **【1993】** 2018, and each subsequent calendar year, the Secretary shall prescribe tables which shall apply in lieu of the tables contained in subsections (a), (b), (c), (d), and (e) with respect to taxable years beginning in the succeeding calendar year.

(2) **METHOD OF PRESCRIBING TABLES.**—The table which under paragraph (1) is to apply in lieu of the table contained in subsection (a), (b), (c), (d), or (e), as the case may be, with respect to taxable years beginning in any calendar year shall be prescribed—

**【(A) except as provided in paragraph (8), by increasing the minimum and maximum dollar amounts for each bracket for which a tax is imposed under such table by the cost-of-living adjustment for such calendar year, determined—**

**【(i) except as provided in clause (ii), by substituting “1992” for “2016” in paragraph (3)(A)(ii), and**

**【(ii) in the case of adjustments to the dollar amounts at which the 36 percent rate bracket begins or at which the 39.6 percent rate bracket begins, by substituting “1993” for “2016” in paragraph (3)(A)(ii),】**

*(A) by increasing the minimum and maximum dollar amounts for each bracket for which a tax is imposed under such table by the cost-of-living adjustment for such calendar year, determined under this subsection for such calendar year by substituting “2017” for “2016” in paragraph (3)(A)(ii),*

*(B) by not changing the rate applicable to any rate bracket as adjusted under subparagraph (A), and*

*(C) by adjusting the amounts setting forth the tax to the extent necessary to reflect the adjustments in the rate brackets.*

(3) **COST-OF-LIVING ADJUSTMENT.**—For purposes of this subsection—

**(A) IN GENERAL.**—The cost-of-living adjustment for any calendar year is the percentage (if any) by which—

(i) the C-CPI-U for the preceding calendar year, exceeds

(ii) the CPI for calendar year 2016, multiplied by the amount determined under subparagraph (B).

**(B) AMOUNT DETERMINED.**—The amount determined under this clause is the amount obtained by dividing—

(i) the C-CPI-U for calendar year 2016, by

(ii) the CPI for calendar year 2016.

**(C) SPECIAL RULE FOR ADJUSTMENTS WITH A BASE YEAR AFTER 2016.**—For purposes of any provision of this title which provides for the substitution of a year after 2016 for “2016” in subparagraph (A)(ii), subparagraph (A) shall be applied by substituting “the C-CPI-U for calendar year 2016” for “the CPI for calendar year 2016” and all that follows in clause (ii) thereof.

(4) **CPI FOR ANY CALENDAR YEAR.**—For purposes of paragraph (3), the CPI for any calendar year is the average of the Consumer Price Index as of the close of the 12-month period ending on August 31 of such calendar year.

(5) **CONSUMER PRICE INDEX.**—For purposes of paragraph (4), the term “Consumer Price Index” means the last Consumer Price Index for all-urban consumers published by the Department of Labor. For purposes of the preceding sentence, the revision of the Consumer Price Index which is most consistent with the Consumer Price Index for calendar year 1986 shall be used.

(6) **C-CPI-U.**—For purposes of this subsection—

(A) **IN GENERAL.**—The term “C-CPI-U” means the Chained Consumer Price Index for All Urban Consumers (as published by the Bureau of Labor Statistics of the Department of Labor). The values of the Chained Consumer Price Index for All Urban Consumers taken into account for purposes of determining the cost-of-living adjustment for any calendar year under this subsection shall be the latest values so published as of the date on which such Bureau publishes the initial value of the Chained Consumer Price Index for All Urban Consumers for the month of August for the preceding calendar year.

(B) **DETERMINATION FOR CALENDAR YEAR.**—The C-CPI-U for any calendar year is the average of the C-CPI-U as of the close of the 12-month period ending on August 31 of such calendar year.

(7) **ROUNDING.**—

(A) **IN GENERAL.**—If any increase determined under paragraph (2)(A) **[(**, section 63(c)(4), section 68(b)(2) or section 151(d)(4)**)]** is not multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.

**[(B) TABLE FOR MARRIED INDIVIDUALS FILING SEPARATELY.**—In the case of a married individual filing a separate return, subparagraph (A)**]**

(B) **SPECIAL RULE.**—*In the case of a table prescribed in lieu of the table contained in subsection (b), (c), or (d), subparagraph (A) [(other than with respect to sections 63(c)(4) and 151(d)(4)(A))]* shall be applied by substituting “\$25” for “\$50” each place it appears.

**[(8) ELIMINATION OF MARRIAGE PENALTY IN 15-PERCENT BRACKET.**—With respect to taxable years beginning after December 31, 2003, in prescribing the tables under paragraph (1)—

**[(A) the maximum taxable income in the 15-percent rate bracket in the table contained in subsection (a) (and the minimum taxable income in the next higher taxable income bracket in such table) shall be 200 percent of the maximum taxable income in the 15-percent rate bracket in the table contained in subsection (c) (after any other adjustment under this subsection), and**

**[(B) the comparable taxable income amounts in the table contained in subsection (d) shall be ½ of the amounts determined under subparagraph (A).]**

[(g) CERTAIN UNEARNED INCOME OF CHILDREN TAXED AS IF PARENT'S INCOME.—

[(1) IN GENERAL.—In the case of any child to whom this subsection applies, the tax imposed by this section shall be equal to the greater of—

[(A) the tax imposed by this section without regard to this subsection, or

[(B) the sum of—

[(i) the tax which would be imposed by this section if the taxable income of such child for the taxable year were reduced by the net unearned income of such child, plus

[(ii) such child's share of the allocable parental tax.]

(g) SPECIAL RULES FOR CERTAIN CHILDREN WITH UNEARNED INCOME.—

(1) IN GENERAL.—In the case of any child to whom this subsection applies—

(A) MODIFICATIONS TO APPLICABLE RATE BRACKETS.—In determining the amount of tax imposed by this section for the taxable year on such child, the income tax table otherwise applicable under this section to such child shall be applied with the following modifications:

(i) 24-PERCENT BRACKET.—The maximum taxable income which is taxed at a rate below 24 percent shall not be more than the sum of—

(I) the earned taxable income of such child, plus

(II) the minimum taxable income for the 24-percent bracket in the table under subsection (e) (as adjusted under subsection (f)) for the taxable year.

(ii) 35-PERCENT BRACKET.—The maximum taxable income which is taxed at a rate below 35 percent shall not be more than the sum of—

(I) the earned taxable income of such child, plus

(II) the minimum taxable income for the 35-percent bracket in the table under subsection (e) (as adjusted under subsection (f)) for the taxable year.

(iii) 37-PERCENT BRACKET.—The maximum taxable income which is taxed at a rate below 37 percent shall not be more than the sum of—

(I) the earned taxable income of such child, plus

(II) the minimum taxable income for the 37-percent bracket in the table under subsection (e) (as adjusted under subsection (f)) for the taxable year.

(B) COORDINATION WITH CAPITAL GAINS RATES.—For purposes of applying section 1(h)—

(i) the maximum zero rate amount shall not be more than the sum of—

(I) the earned taxable income of such child, plus

(II) the amount in effect under subsection (h)(13) for the taxable year, and

(ii) the maximum 15-percent rate amount shall not be more than the sum of—

(I) the earned taxable income of such child, plus

(II) the amount in effect under subsection (h)(12)(D) for the taxable year.

(2) CHILD TO WHOM SUBSECTION APPLIES.—This subsection shall apply to any child for any taxable year if—

(A) such child—

(i) has not attained age 18 before the close of the taxable year, or

(ii)(I) has attained age 18 before the close of the taxable year and meets the age requirements of section 152(c)(3) (determined without regard to subparagraph (B) thereof), and

(II) whose earned income (as defined in section 911(d)(2)) for such taxable year does not exceed one-half of the amount of the individual's support (within the meaning of section 152(c)(1)(D) after the application of section 152(f)(5) (without regard to subparagraph (A) thereof)) for such taxable year,

(B) either parent of such child is alive at the close of the taxable year, and

(C) such child does not file a joint return for the taxable year.

[(3) ALLOCABLE PARENTAL TAX.—For purposes of this subsection—

[(A) IN GENERAL.—The term “allocable parental tax” means the excess of—

[(i) the tax which would be imposed by this section on the parent's taxable income if such income included the net unearned income of all children of the parent to whom this subsection applies, over

[(ii) the tax imposed by this section on the parent without regard to this subsection.

For purposes of clause (i), net unearned income of all children of the parent shall not be taken into account in computing any exclusion, deduction, or credit of the parent.

[(B) CHILD'S SHARE.—A child's share of any allocable parental tax of a parent shall be equal to an amount which bears the same ratio to the total allocable parental tax as the child's net unearned income bears to the aggregate net unearned income of all children of such parent to whom this subsection applies.

[(C) SPECIAL RULE WHERE PARENT HAS DIFFERENT TAXABLE YEAR.—Except as provided in regulations, if the parent does not have the same taxable year as the child, the allocable parental tax shall be determined on the basis of the taxable year of the parent ending in the child's taxable year.]

(3) EARNED TAXABLE INCOME.—*For purposes of this subsection, the term “earned taxable income” means, with respect to any child for any taxable year, the taxable income of such child reduced (but not below zero) by the net unearned income of such child.*

(4) NET UNEARNED INCOME.—For purposes of this subsection—

(A) IN GENERAL.—The term “net unearned income” means the excess of—

- (i) the portion of the adjusted gross income for the taxable year which is not attributable to earned income (as defined in section 911(d)(2)), over
- (ii) the sum of—

- (I) the amount in effect for the taxable year under section 63(c)(5)(A) (relating to limitation on standard deduction in the case of certain dependents), plus

- (II) the greater of the amount described in subclause (I) or, if the child itemizes his deductions for the taxable year, the amount of the itemized deductions allowed by this chapter for the taxable year which are directly connected with the production of the portion of adjusted gross income referred to in clause (i).

(B) LIMITATION BASED ON TAXABLE INCOME.—The amount of the net unearned income for any taxable year shall not exceed the individual's taxable income for such taxable year.

(C) TREATMENT OF DISTRIBUTIONS FROM QUALIFIED DISABILITY TRUSTS.—For purposes of this subsection, in the case of any child who is a beneficiary of a qualified disability trust (as defined in section 642(b)(2)(C)(ii)), any amount included in the income of such child under sections 652 and 662 during a taxable year shall be considered earned income of such child for such taxable year.

(5) **[SPECIAL RULES FOR DETERMINING PARENT TO WHOM SUBSECTION APPLIES.—]** *SPECIAL RULES FOR DETERMINING PARENT ELIGIBLE TO MAKE ELECTION.*—**[**For purposes of this subsection, the parent whose taxable income shall be taken into account shall be—**]** *For purposes of paragraph (7), the parent referred to in subparagraph (A)(iv) thereof is—*

- (A) in the case of parents who are not married (within the meaning of section 7703), the custodial parent (within the meaning of **[**section 152(e)**]** *section 7706(e)*) of the child, and

- (B) in the case of married individuals filing separately, the individual with the greater taxable income.

(6) PROVIDING OF PARENT'S TIN.—The parent of any child to whom this subsection applies for any taxable year shall provide the TIN of such parent to such child and such child shall include such TIN on the child's return of tax imposed by this section for such taxable year.

(7) ELECTION TO CLAIM CERTAIN UNEARNED INCOME OF CHILD ON PARENT'S RETURN.—

(A) IN GENERAL.—If—

- (i) any child to whom this subsection applies has gross income for the taxable year only from interest and dividends (including Alaska Permanent Fund dividends),

- (ii) such gross income is more than the amount described in paragraph (4)(A)(ii)(I) and less than 10 times the amount so described,

- (iii) no estimated tax payments for such year are made in the name and TIN of such child, and no

amount has been deducted and withheld under section 3406, and

(iv) the parent of such child (as determined under paragraph (5)) elects the application of subparagraph (B),

such child shall be treated (other than for purposes of this paragraph) as having no gross income for such year and shall not be required to file a return under section 6012.

(B) INCOME INCLUDED ON PARENT'S RETURN.—In the case of a parent making the election under this paragraph—

(i) the gross income of each child to whom such election applies (to the extent the gross income of such child exceeds twice the amount described in paragraph (4)(A)(ii)(I)) shall be included in such parent's gross income for the taxable year,

(ii) the tax imposed by this section for such year with respect to such parent shall be the amount equal to the sum of—

(I) the amount determined under this section after the application of clause (i), plus

(II) for each such child, 10 percent of the lesser of the amount described in paragraph (4)(A)(ii)(I) or the excess of the gross income of such child over the amount so described, and

(iii) any interest which is an item of tax preference under section 57(a)(5) of the child shall be treated as an item of tax preference of such parent (and not of such child).

(C) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this paragraph.

(h) MAXIMUM CAPITAL GAINS RATE.—

(1) IN GENERAL.—If a taxpayer has a net capital gain for any taxable year, the tax imposed by this section for such taxable year shall not exceed the sum of—

(A) a tax computed at the rates and in the same manner as if this subsection had not been enacted on the greater of—

(i) taxable income reduced by the net capital gain; or

(ii) the lesser of—

(I) the amount of taxable income taxed at a rate below 25 percent; or

(II) taxable income reduced by the adjusted net capital gain;

(B) 0 percent of so much of the adjusted net capital gain (or, if less, taxable income) as does not exceed the excess (if any) of—

(i) the amount of taxable income which would (without regard to this paragraph) be taxed at a rate below **25 percent** *22 percent*, over

(ii) the taxable income reduced by the adjusted net capital gain;

(C) 15 percent of the lesser of—

- (i) so much of the adjusted net capital gain (or, if less, taxable income) as exceeds the amount on which a tax is determined under subparagraph (B), or
  - (ii) the excess of—
    - (I) the amount of taxable income [which would (without regard to this paragraph) be taxed at a rate below 39.6 percent] *below the maximum 15-percent rate amount*, over
    - (II) the sum of the amounts on which a tax is determined under subparagraphs (A) and (B),
  - (D) 20 percent of the adjusted net capital gain (or, if less, taxable income) in excess of the sum of the amounts on which tax is determined under subparagraphs (B) and (C),
  - (E) 25 percent of the excess (if any) of—
    - (i) the unrecaptured section 1250 gain (or, if less, the net capital gain (determined without regard to paragraph (11))), over
    - (ii) the excess (if any) of—
      - (I) the sum of the amount on which tax is determined under subparagraph (A) plus the net capital gain, over
      - (II) taxable income; and
  - (F) 28 percent of the amount of taxable income in excess of the sum of the amounts on which tax is determined under the preceding subparagraphs of this paragraph.
- (2) NET CAPITAL GAIN TAKEN INTO ACCOUNT AS INVESTMENT INCOME.—For purposes of this subsection, the net capital gain for any taxable year shall be reduced (but not below zero) by the amount which the taxpayer takes into account as investment income under section 163(d)(4)(B)(iii).
- (3) ADJUSTED NET CAPITAL GAIN.—For purposes of this subsection, the term “adjusted net capital gain” means the sum of—
- (A) net capital gain (determined without regard to paragraph (11)) reduced (but not below zero) by the sum of—
    - (i) unrecaptured section 1250 gain, and
    - (ii) 28-percent rate gain, plus
  - (B) qualified dividend income (as defined in paragraph (11)).
- (4) 28-PERCENT RATE GAIN.—For purposes of this subsection, the term “28-percent rate gain” means the excess (if any) of—
- (A) the sum of—
    - (i) collectibles gain; and
    - (ii) section 1202 gain, over
  - (B) the sum of—
    - (i) collectibles loss;
    - (ii) the net short-term capital loss; and
    - (iii) the amount of long-term capital loss carried under section 1212(b)(1)(B) to the taxable year.
- (5) COLLECTIBLES GAIN AND LOSS.—For purposes of this subsection—
- (A) IN GENERAL.—The terms “collectibles gain” and “collectibles loss” mean gain or loss (respectively) from the sale or exchange of a collectible (as defined in section

408(m) without regard to paragraph (3) thereof) which is a capital asset held for more than 1 year but only to the extent such gain is taken into account in computing gross income and such loss is taken into account in computing taxable income.

(B) PARTNERSHIPS, ETC.—For purposes of subparagraph (A), any gain from the sale of an interest in a partnership, S corporation, or trust which is attributable to unrealized appreciation in the value of collectibles shall be treated as gain from the sale or exchange of a collectible. Rules similar to the rules of section 751 shall apply for purposes of the preceding sentence.

(6) UNRECAPTURED SECTION 1250 GAIN.—For purposes of this subsection—

(A) IN GENERAL.—The term “unrecaptured section 1250 gain” means the excess (if any) of—

(i) the amount of long-term capital gain (not otherwise treated as ordinary income) which would be treated as ordinary income if section 1250(b)(1) included all depreciation and the applicable percentage under section 1250(a) were 100 percent, over

(ii) the excess (if any) of—

(I) the amount described in paragraph (4)(B);  
over

(II) the amount described in paragraph (4)(A).

(B) LIMITATION WITH RESPECT TO SECTION 1231 PROPERTY.—The amount described in subparagraph (A)(i) from sales, exchanges, and conversions described in section 1231(a)(3)(A) for any taxable year shall not exceed the net section 1231 gain (as defined in section 1231(c)(3)) for such year.

(7) SECTION 1202 GAIN.—For purposes of this subsection, the term “section 1202 gain” means the excess of—

(A) the gain which would be excluded from gross income under section 1202 but for the percentage limitation in section 1202(a), over

(B) the gain excluded from gross income under section 1202.

(8) COORDINATION WITH RECAPTURE OF NET ORDINARY LOSSES UNDER SECTION 1231.—If any amount is treated as ordinary income under section 1231(c), such amount shall be allocated among the separate categories of net section 1231 gain (as defined in section 1231(c)(3)) in such manner as the Secretary may by forms or regulations prescribe.

(9) REGULATIONS.—The Secretary may prescribe such regulations as are appropriate (including regulations requiring reporting) to apply this subsection in the case of sales and exchanges by pass-thru entities and of interests in such entities.

(10) PASS-THRU ENTITY DEFINED.—For purposes of this subsection, the term “pass-thru entity” means—

(A) a regulated investment company;

(B) a real estate investment trust;

(C) an S corporation;

(D) a partnership;

(E) an estate or trust;



- (F) a common trust fund; and
  - (G) a qualified electing fund (as defined in section 1295).
- (11) DIVIDENDS TAXED AS NET CAPITAL GAIN.—
- (A) IN GENERAL.—For purposes of this subsection, the term “net capital gain” means net capital gain (determined without regard to this paragraph) increased by qualified dividend income.
  - (B) QUALIFIED DIVIDEND INCOME.—For purposes of this paragraph—
    - (i) IN GENERAL.—The term “qualified dividend income” means dividends received during the taxable year from—
      - (I) domestic corporations, and
      - (II) qualified foreign corporations.
    - (ii) CERTAIN DIVIDENDS EXCLUDED.—Such term shall not include—
      - (I) any dividend from a corporation which for the taxable year of the corporation in which the distribution is made, or the preceding taxable year, is a corporation exempt from tax under section 501 or 521,
      - (II) any amount allowed as a deduction under section 591 (relating to deduction for dividends paid by mutual savings banks, etc.), and
      - (III) any dividend described in section 404(k).
    - (iii) COORDINATION WITH SECTION 246(C).—Such term shall not include any dividend on any share of stock—
      - (I) with respect to which the holding period requirements of section 246(c) are not met (determined by substituting in section 246(c) “60 days” for “45 days” each place it appears and by substituting “121- day period” for “91-day period”), or
      - (II) to the extent that the taxpayer is under an obligation (whether pursuant to a short sale or otherwise) to make related payments with respect to positions in substantially similar or related property.
  - (C) QUALIFIED FOREIGN CORPORATIONS.—
    - (i) IN GENERAL.—Except as otherwise provided in this paragraph, the term “qualified foreign corporation” means any foreign corporation if—
      - (I) such corporation is incorporated in a possession of the United States, or
      - (II) such corporation is eligible for benefits of a comprehensive income tax treaty with the United States which the Secretary determines is satisfactory for purposes of this paragraph and which includes an exchange of information program.
    - (ii) DIVIDENDS ON STOCK READILY TRADABLE ON UNITED STATES SECURITIES MARKET.—A foreign corporation not otherwise treated as a qualified foreign corporation under clause (i) shall be so treated with respect to any dividend paid by such corporation if the stock with respect to which such dividend is paid is

readily tradable on an established securities market in the United States.

(iii) EXCLUSION OF DIVIDENDS OF CERTAIN FOREIGN CORPORATIONS.—Such term shall not include—

(I) any foreign corporation which for the taxable year of the corporation in which the dividend was paid, or the preceding taxable year, is a passive foreign investment company (as defined in section 1297), and

(II) any corporation which first becomes a surrogate foreign corporation (as defined in section 7874(a)(2)(B)) after the date of the enactment of this subclause, other than a foreign corporation which is treated as a domestic corporation under section 7874(b).

(iv) COORDINATION WITH FOREIGN TAX CREDIT LIMITATION.—Rules similar to the rules of section 904(b)(2)(B) shall apply with respect to the dividend rate differential under this paragraph.

(D) SPECIAL RULES.—

(i) AMOUNTS TAKEN INTO ACCOUNT AS INVESTMENT INCOME.—Qualified dividend income shall not include any amount which the taxpayer takes into account as investment income under section 163(d)(4)(B).

(ii) EXTRAORDINARY DIVIDENDS.—If a taxpayer to whom this section applies receives, with respect to any share of stock, qualified dividend income from 1 or more dividends which are extraordinary dividends (within the meaning of section 1059(c)), any loss on the sale or exchange of such share shall, to the extent of such dividends, be treated as long-term capital loss.

(iii) TREATMENT OF DIVIDENDS FROM REGULATED INVESTMENT COMPANIES AND REAL ESTATE INVESTMENT TRUSTS.—A dividend received from a regulated investment company or a real estate investment trust shall be subject to the limitations prescribed in sections 854 and 857.

(12) MAXIMUM 15-PERCENT RATE AMOUNT DEFINED.—For purposes of this subsection, the maximum 15-percent rate amount shall be—

(A) in the case of a joint return or surviving spouse (as defined in section 2(a)), \$479,000 (1/2 such amount in the case of a married individual filing a separate return),

(B) in the case of an individual who is the head of a household (as defined in section 2(b)), \$452,400,

(C) in the case of any other individual (other than an estate or trust), \$425,800, and

(D) in the case of an estate or trust, \$12,700.

(13) DETERMINATION OF 0 PERCENT RATE BRACKET FOR ESTATES AND TRUSTS.—In the case of any estate or trust, paragraph (1)(B) shall be applied by treating the amount determined in clause (i) thereof as being equal to \$2,600.

(14) INFLATION ADJUSTMENT.—

(A) *IN GENERAL.*—In the case of any taxable year beginning after 2018, each of the dollar amounts in paragraphs (12) and (13) shall be increased by an amount equal to—

- (i) such dollar amount, multiplied by
- (ii) the cost-of-living adjustment determined under subsection (f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2017” for “calendar year 2016” in subparagraph (A)(ii) thereof.

(B) *ROUNDING.*—If any increase under subparagraph (A) is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.

**[(i) RATE REDUCTIONS AFTER 2000.—**

**[(1) 10-percent rate bracket**

**[(A) IN GENERAL.**—In the case of taxable years beginning after December 31, 2000—

**[(i)** the rate of tax under subsections (a), (b), (c), and (d) on taxable income not over the initial bracket amount shall be 10 percent, and

**[(ii)** the 15 percent rate of tax shall apply only to taxable income over the initial bracket amount but not over the maximum dollar amount for the 15-percent rate bracket.

**[(B) INITIAL BRACKET AMOUNT.**—For purposes of this paragraph, the initial bracket amount is—

**[(i)** \$14,000 in the case of subsection (a),

**[(ii)** \$10,000 in the case of subsection (b), and

**[(iii)** 1/2 the amount applicable under clause (i) (after adjustment, if any, under subparagraph (C)) in the case of subsections (c) and (d).

**[(C) INFLATION ADJUSTMENT.**—In prescribing the tables under subsection (f) which apply with respect to taxable years beginning in calendar years after 2003—

**[(i)** the cost-of-living adjustment shall be determined under subsection (f)(3) by substituting “2002” for “2016” in subparagraph (A)(ii) thereof, and

**[(ii)** the adjustments under clause (i) shall not apply to the amount referred to in subparagraph (B)(iii).

If any amount after adjustment under the preceding sentence is not a multiple of \$50, such amount shall be rounded to the next lowest multiple of \$50.

**[(2) 25-, 28-, AND 33-PERCENT RATE BRACKETS.**—The tables under subsections (a), (b), (c), (d), and (e) shall be applied—

**[(A)** by substituting “25%” for “28%” each place it appears (before the application of subparagraph (B)),

**[(B)** by substituting “28%” for “31%” each place it appears, and

**[(C)** by substituting “33%” for “36%” each place it appears.

**[(3) MODIFICATIONS TO INCOME TAX BRACKETS FOR HIGH-INCOME TAXPAYERS.—**

**[(A) 35-PERCENT RATE BRACKET.**—In the case of taxable years beginning after December 31, 2012—

**[(i)** the rate of tax under subsections (a), (b), (c), and (d) on a taxpayer’s taxable income in the highest rate

bracket shall be 35 percent to the extent such income does not exceed an amount equal to the excess of—

[(I) the applicable threshold, over

[(II) the dollar amount at which such bracket begins, and

[(ii) the 39.6 percent rate of tax under such subsections shall apply only to the taxpayer’s taxable income in such bracket in excess of the amount to which clause (i) applies.

[(B) APPLICABLE THRESHOLD.—For purposes of this paragraph, the term “applicable threshold” means—

[(i) \$450,000 in the case of subsection (a),

[(ii) \$425,000 in the case of subsection (b),

[(iii) \$400,000 in the case of subsection (c), and

[(iv) ½ the amount applicable under clause (i) (after adjustment, if any, under subparagraph (C)) in the case of subsection (d).

[(C) INFLATION ADJUSTMENT.—For purposes of this paragraph, with respect to taxable years beginning in calendar years after 2013, each of the dollar amounts under clauses (i), (ii), and (iii) of subparagraph (B) shall be adjusted in the same manner as under paragraph (1)(C)(i), except that subsection (f)(3)(A)(ii) shall be applied by substituting “2012” for “2016”.

[(4) ADJUSTMENT OF TABLES.—The Secretary shall adjust the tables prescribed under subsection (f) to carry out this subsection.

[(j) MODIFICATIONS FOR TAXABLE YEARS 2018 THROUGH 2025.—

[(1) IN GENERAL.—In the case of a taxable year beginning after December 31, 2017, and before January 1, 2026—

[(A) subsection (i) shall not apply, and

[(B) this section (other than subsection (i)) shall be applied as provided in paragraphs (2) through (6).

[(2) RATE TABLES.—

[(A) MARRIED INDIVIDUALS FILING JOINT RETURNS AND SURVIVING SPOUSES.—The following table shall be applied in lieu of the table contained in subsection (a):

| [(If taxable income is:                 | The tax is:                                       |
|---|---|
| Not over \$19,050.....                  | 10% of taxable income.                            |
| Over \$19,050 but not over \$77,400...  | \$1,905, plus 12% of the excess over \$19,050.    |
| Over \$77,400 but not over \$165,000... | \$8,907, plus 22% of the excess over \$77,400.    |
| Over \$165,000 but not over \$315,000.. | \$28,179, plus 24% of the excess over \$165,000.  |
| Over \$315,000 but not over \$400,000.. | \$64,179, plus 32% of the excess over \$315,000.  |
| Over \$400,000 but not over \$600,000.. | \$91,379, plus 35% of the excess over \$400,000.  |
| Over \$600,000.....                     | \$161,379, plus 37% of the excess over \$600,000. |

[(B) HEADS OF HOUSEHOLDS.—The following table shall be applied in lieu of the table contained in subsection (b):

| [(If taxable income is: | The tax is:            |
|-------------------------|------------------------|
| Not over \$13,600.....  | 10% of taxable income. |

| If taxable income is:                   | The tax is:                                       |
|---|---|
| Over \$13,600 but not over \$51,800.... | \$1,360, plus 12% of the excess over \$13,600.    |
| Over \$51,800 but not over \$82,500.... | \$5,944, plus 22% of the excess over \$51,800.    |
| Over \$82,500 but not over \$157,500... | \$12,698, plus 24% of the excess over \$82,500.   |
| Over \$157,500 but not over \$200,000.. | \$30,698, plus 32% of the excess over \$157,500.  |
| Over \$200,000 but not over \$500,000.. | \$44,298, plus 35% of the excess over \$200,000.  |
| Over \$500,000.....                     | \$149,298, plus 37% of the excess over \$500,000. |

**[(C) UNMARRIED INDIVIDUALS OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLDS.—**The following table shall be applied in lieu of the table contained in subsection (c):

| If taxable income is:                   | The tax is:  |
|---|--|
| Not over \$9,525.....                   | 10% of taxable income.                               |
| Over \$9,525 but not over \$38,700....  | \$952.50, plus 12% of the excess over \$9,525.       |
| Over \$38,700 but not over \$82,500.... | \$4,453.50, plus 22% of the excess over \$38,700.    |
| Over \$82,500 but not over \$157,500... | \$14,089.50, plus 24% of the excess over \$82,500.   |
| Over \$157,500 but not over \$200,000.. | \$32,089.50, plus 32% of the excess over \$157,500.  |
| Over \$200,000 but not over \$500,000.. | \$45,689.50, plus 35% of the excess over \$200,000.  |
| Over \$500,000.....                     | \$150,689.50, plus 37% of the excess over \$500,000. |

**[(D) MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—**The following table shall be applied in lieu of the table contained in subsection (d):

| If taxable income is:                   | The tax is:   |
|---|---|
| Not over \$9,525.....                   | 10% of taxable income.                              |
| Over \$9,525 but not over \$38,700....  | \$952.50, plus 12% of the excess over \$9,525.      |
| Over \$38,700 but not over \$82,500.... | \$4,453.50, plus 22% of the excess over \$38,700.   |
| Over \$82,500 but not over \$157,500... | \$14,089.50, plus 24% of the excess over \$82,500.  |
| Over \$157,500 but not over \$200,000.. | \$32,089.50, plus 32% of the excess over \$157,500. |
| Over \$200,000 but not over \$300,000.. | \$45,689.50, plus 35% of the excess over \$200,000. |
| Over \$300,000.....                     | \$80,689.50, plus 37% of the excess over \$300,000. |

**[(E) ESTATES AND TRUSTS.—**The following table shall be applied in lieu of the table contained in subsection (e):

| If taxable income is:                   | The tax is:                                       |
|---|---|
| Not over \$2,550.....                   | 10% of taxable income.                            |
| Over \$2,550 but not over \$9,150.....  | \$255, plus 24% of the excess over \$2,550.       |
| Over \$9,150 but not over \$12,500..... | \$1,839, plus 35% of the excess over \$9,150.     |
| Over \$12,500.....                      | \$3,011.50, plus 37% of the excess over \$12,500. |

**[(F) REFERENCES TO RATE TABLES.—**Any reference in this title to a rate of tax under subsection (c) shall be treated as a reference to the corresponding rate bracket under subparagraph (C) of this paragraph, except that the reference in section 3402(q)(1) to the third lowest rate of tax applicable under subsection (c) shall be treated as a

reference to the fourth lowest rate of tax under subparagraph (C).

**[(3) ADJUSTMENTS.—**

**[(A) NO ADJUSTMENT IN 2018.—**The tables contained in paragraph (2) shall apply without adjustment for taxable years beginning after December 31, 2017, and before January 1, 2019.

**[(B) SUBSEQUENT YEARS.—**For taxable years beginning after December 31, 2018, the Secretary shall prescribe tables which shall apply in lieu of the tables contained in paragraph (2) in the same manner as under paragraphs (1) and (2) of subsection (f) (applied without regard to clauses (i) and (ii) of subsection (f)(2)(A)), except that in prescribing such tables—

**[(i) subsection (f)(3) shall be applied by substituting “calendar year 2017” for “calendar year 2016” in subparagraph (A)(ii) thereof,**

**[(ii) subsection (f)(7)(B) shall apply to any unmarried individual other than a surviving spouse or head of household, and**

**[(iii) subsection (f)(8) shall not apply.**

**[(4) SPECIAL RULES FOR CERTAIN CHILDREN WITH UNEARNED INCOME.—**

**[(A) IN GENERAL.—**In the case of a child to whom subsection (g) applies for the taxable year, the rules of subparagraphs (B) and (C) shall apply in lieu of the rule under subsection (g)(1).

**[(B) MODIFICATIONS TO APPLICABLE RATE BRACKETS.—**In determining the amount of tax imposed by this section for the taxable year on a child described in subparagraph (A), the income tax table otherwise applicable under this subsection to the child shall be applied with the following modifications:

**[(i) 24-PERCENT BRACKET.—**The maximum taxable income which is taxed at a rate below 24 percent shall not be more than the sum of—

**[(I) the earned taxable income of such child, plus**

**[(II) the minimum taxable income for the 24-percent bracket in the table under paragraph (2)(E) (as adjusted under paragraph (3)) for the taxable year.**

**[(ii) 35-PERCENT BRACKET.—**The maximum taxable income which is taxed at a rate below 35 percent shall not be more than the sum of—

**[(I) the earned taxable income of such child, plus (II) the minimum taxable income for the 35-percent bracket in the table under paragraph (2)(E) (as adjusted under paragraph (3)) for the taxable year.**

**[(iii) 37-PERCENT BRACKET.—**The maximum taxable income which is taxed at a rate below 37 percent shall not be more than the sum of—

**[(I) the earned taxable income of such child, plus**

[(II) the minimum taxable income for the 37-percent bracket in the table under paragraph (2)(E) (as adjusted under paragraph (3)) for the taxable year.

[(C) COORDINATION WITH CAPITAL GAINS RATES.—For purposes of applying section 1(h) (after the modifications under paragraph (5)(A))—

[(i) the maximum zero rate amount shall not be more than the sum of—

[(I) the earned taxable income of such child, plus

[(II) the amount in effect under paragraph (5)(B)(i)(IV) for the taxable year, and

[(ii) the maximum 15-percent rate amount shall not be more than the sum of—

[(I) the earned taxable income of such child, plus

[(II) the amount in effect under paragraph (5)(B)(ii)(IV) for the taxable year.

[(D) EARNED TAXABLE INCOME.—For purposes of this paragraph, the term “earned taxable income” means, with respect to any child for any taxable year, the taxable income of such child reduced (but not below zero) by the net unearned income (as defined in subsection (g)(4)) of such child.

[(5) APPLICATION OF CURRENT INCOME TAX BRACKETS TO CAPITAL GAINS BRACKETS.—

[(A) IN GENERAL.—Section 1(h)(1) shall be applied—

[(i) by substituting “below the maximum zero rate amount” for “which would (without regard to this paragraph) be taxed at a rate below 25 percent” in subparagraph (B)(i), and

[(ii) by substituting “below the maximum 15-percent rate amount” for “which would (without regard to this paragraph) be taxed at a rate below 39.6 percent” in subparagraph (C)(ii)(I).

[(B) MAXIMUM AMOUNTS DEFINED.—For purposes of applying section 1(h) with the modifications described in subparagraph (A)—

[(i) MAXIMUM ZERO RATE AMOUNT.—The maximum zero rate amount shall be—

[(I) in the case of a joint return or surviving spouse, \$77,200,

[(II) in the case of an individual who is a head of household (as defined in section 2(b)), \$51,700,

[(III) in the case of any other individual (other than an estate or trust), an amount equal to ½ of the amount in effect for the taxable year under subclause (I), and

[(IV) in the case of an estate or trust, \$2,600.

[(ii) MAXIMUM 15-PERCENT RATE AMOUNT.—The maximum 15-percent rate amount shall be—

[(I) in the case of a joint return or surviving spouse, \$479,000 (½ such amount in the case of a married individual filing a separate return),

[(II) in the case of an individual who is the head of a household (as defined in section 2(b)), \$452,400,

[(III) in the case of any other individual (other than an estate or trust), \$425,800, and

[(IV) in the case of an estate or trust, \$12,700.

[(C) INFLATION ADJUSTMENT.—In the case of any taxable year beginning after 2018, each of the dollar amounts in clauses (i) and (ii) of subparagraph (B) shall be increased by an amount equal to—

[(i) such dollar amount, multiplied by

[(ii) the cost-of-living adjustment determined under subsection (f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2017” for “calendar year 2016” in subparagraph (A)(ii) thereof.

If any increase under this subparagraph is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.

[(6) SECTION 15 NOT TO APPLY.—Section 15 shall not apply to any change in a rate of tax by reason of this subsection.]

## SEC. 2. DEFINITIONS AND SPECIAL RULES.

(a) DEFINITION OF SURVIVING SPOUSE.—

(1) IN GENERAL.—For purposes of section 1, the term “surviving spouse” means a taxpayer—

(A) whose spouse died during either of his two taxable years immediately preceding the taxable year, and

(B) who maintains as his home a household which constitutes for the taxable year the principal place of abode (as a member of such household) of a dependent (i) who (within the meaning of [section 152] *section 7706*, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof) is a son, stepson, daughter, or stepdaughter of the taxpayer, and (ii) [with respect to whom the taxpayer is entitled to a deduction for the taxable year under section 151] *whose TIN is included on the taxpayer’s return of tax for the taxable year.*

For purposes of this paragraph, an individual shall be considered as maintaining a household only if over half of the cost of maintaining the household during the taxable year is furnished by such individual.

(2) LIMITATIONS.—Notwithstanding paragraph (1), for purposes of section 1 a taxpayer shall not be considered to be a surviving spouse—

(A) if the taxpayer has remarried at any time before the close of the taxable year, or

(B) unless, for the taxpayer’s taxable year during which his spouse died, a joint return could have been made under the provisions of section 6013 (without regard to subsection (a)(3) thereof).

(3) SPECIAL RULE WHERE DECEASED SPOUSE WAS IN MISSING STATUS.—If an individual was in a missing status (within the meaning of section 6013(f)(3)) as a result of service in a combat zone (as determined for purposes of section 112) and if such individual remains in such status until the date referred to in



subparagraph (A) or (B), then, for purposes of paragraph (1)(A), the date on which such individual died shall be treated as the earlier of the date determined under subparagraph (A) or the date determined under subparagraph (B):

(A) the date on which the determination is made under section 556 of title 37 of the United States Code or under section 5566 of title 5 of such Code (whichever is applicable) that such individual died while in such missing status, or

(B) except in the case of the combat zone designated for purposes of the Vietnam conflict, the date which is 2 years after the date designated under section 112 as the date of termination of combatant activities in that zone.

(b) DEFINITION OF HEAD OF HOUSEHOLD.—

(1) IN GENERAL.—For purposes of this subtitle, an individual shall be considered a head of a household if, and only if, such individual is not married at the close of his taxable year, is not a surviving spouse (as defined in subsection (a)), and either—

(A) maintains as his home a household which constitutes for more than one-half of such taxable year the principal place of abode, as a member of such household, of—

(i) a qualifying child of the individual (as defined in **[section 152(c)]** *section 7706(c)*, determined without regard to **[section 152(e)]** *section 7706(e)*), but not if such child—

(I) is married at the close of the taxpayer's taxable year, and

(II) is not a dependent of such individual by reason of **[section 152(b)(2) or 152(b)(3)]** *section 7706(b)(2) or 7706(b)(3)*, or both, or

(ii) any other person who is a dependent of the taxpayer, **[if the taxpayer is entitled to a deduction for the taxable year for such person under section 151]** *if the taxpayer included such person's TIN on the return of tax for the taxable year*, or

(B) maintains a household which constitutes for such taxable year the principal place of abode of the father or mother of the taxpayer, **[if the taxpayer is entitled to a deduction for the taxable year for such father or mother under section 151]** *if such father or mother is a dependent of the taxpayer and the taxpayer included such father or mother's TIN on the return of tax for the taxable year*.

For purposes of this paragraph, an individual shall be considered as maintaining a household only if over half of the cost of maintaining the household during the taxable year is furnished by such individual.

(2) DETERMINATION OF STATUS.—For purposes of this subsection—

(A) an individual who is legally separated from his spouse under a decree of divorce or of separate maintenance shall not be considered as married;

(B) a taxpayer shall be considered as not married at the close of his taxable year if at any time during the taxable year his spouse is a nonresident alien; and

- (C) a taxpayer shall be considered as married at the close of his taxable year if his spouse (other than a spouse described in subparagraph (B)) died during the taxable year.
- (3) LIMITATIONS.—Notwithstanding paragraph (1), for purposes of this subtitle a taxpayer shall not be considered to be a head of a household—
- (A) if at any time during the taxable year he is a nonresident alien; or
- (B) by reason of an individual who would not be a dependent for the taxable year but for—
- (i) subparagraph (H) of [section 152(d)(2)] *section 7706(d)(2)*, or
- (ii) paragraph (3) of [section 152(d)] *section 7706(d)*.
- (c) CERTAIN MARRIED INDIVIDUALS LIVING APART.—For purposes of this part, an individual shall be treated as not married at the close of the taxable year if such individual is so treated under the provisions of section 7703(b).
- (d) NONRESIDENT ALIENS.—In the case of a nonresident alien individual, the taxes imposed by sections 1 and 55 shall apply only as provided by section 871 or 877.
- (e) CROSS REFERENCE.—For definition of taxable income, see section 63.

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### PART III—CHANGES IN RATES DURING A TAXABLE YEAR

**[Sec. 15. Effect of changes.]**  
*Sec. 15. Effect of changes on corporations.*

**SEC. 15. EFFECT OF CHANGES ON CORPORATIONS.**

(a) GENERAL RULE.—**[If any rate of tax]** *In the case of a corporation, if any rate of tax imposed by this chapter changes, and if the taxable year includes the effective date of the change (unless that date is the first day of the taxable year), then—*

- (1) tentative taxes shall be computed by applying the rate for the period before the effective date of the change, and the rate for the period on and after such date, to the taxable income for the entire taxable year; and
- (2) the tax for such taxable year shall be the sum of that proportion of each tentative tax which the number of days in each period bears to the number of days in the entire taxable year.
- (b) REPEAL OF TAX.—For purposes of subsection (a)—
- (1) if a tax is repealed, the repeal shall be considered a change of rate; and
- (2) the rate for the period after the repeal shall be zero.
- (c) EFFECTIVE DATE OF CHANGE.—For purposes of subsections (a) and (b)—
- (1) if the rate changes for taxable years “beginning after” or “ending after” a certain date, the following day shall be considered the effective date of the change; and
- (2) if a rate changes for taxable years “beginning on or after” a certain date, that date shall be considered the effective date of the change.

[(d) SECTION NOT TO APPLY TO INFLATION ADJUSTMENTS.—This section shall not apply to any change in rates under subsection (f) of section 1 (relating to adjustments in tax tables so that inflation will not result in tax increases).

[(e) REFERENCES TO HIGHEST RATE.—If the change referred to in subsection (a) involves a change in the highest rate of tax imposed by section 1 or 11(b), any reference in this chapter to such highest rate (other than in a provision imposing a tax by reference to such rate) shall be treated as a reference to the weighted average of the highest rates before and after the change determined on the basis of the respective portions of the taxable year before the date of the change and on or after the date of the change.

[(f) RATE REDUCTIONS ENACTED BY ECONOMIC GROWTH AND TAX RELIEF RECONCILIATION ACT OF 2001.—This section shall not apply to any change in rates under subsection (i) of section 1 (relating to rate reductions after 2000).]

## PART IV—CREDITS AGAINST TAX

\* \* \* \* \*

### Subpart A—Nonrefundable Personal Credits

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#### SEC. 21. EXPENSES FOR HOUSEHOLD AND DEPENDENT CARE SERVICES NECESSARY FOR GAINFUL EMPLOYMENT.

##### (a) ALLOWANCE OF CREDIT.—

(1) IN GENERAL.—In the case of an individual for which there are 1 or more qualifying individuals (as defined in subsection (b)(1)) with respect to such individual, there shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to the applicable percentage of the employment-related expenses (as defined in subsection (b)(2)) paid by such individual during the taxable year.

(2) APPLICABLE PERCENTAGE DEFINED.—For purposes of paragraph (1), the term “applicable percentage” means 35 percent reduced (but not below 20 percent) by 1 percentage point for each \$2,000 (or fraction thereof) by which the taxpayer’s adjusted gross income for the taxable year exceeds \$15,000.

##### (b) DEFINITIONS OF QUALIFYING INDIVIDUAL AND EMPLOYMENT-RELATED EXPENSES.—For purposes of this section—

(1) QUALIFYING INDIVIDUAL.—The term “qualifying individual” means—

(A) a dependent of the taxpayer (as defined in [section 152(a)(1)] *section 7706(a)(1)*) who has not attained age 13,

(B) a dependent of the taxpayer (as defined in [section 152] *section 7706*, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B)) who is physically or mentally incapable of caring for himself or herself and who has the same principal place of abode as the taxpayer for more than one-half of such taxable year, or

(C) the spouse of the taxpayer, if the spouse is physically or mentally incapable of caring for himself or herself and who has the same principal place of abode as the taxpayer for more than one-half of such taxable year.

(2) EMPLOYMENT-RELATED EXPENSES.—

(A) IN GENERAL.—The term “employment-related expenses” means amounts paid for the following expenses, but only if such expenses are incurred to enable the taxpayer to be gainfully employed for any period for which there are 1 or more qualifying individuals with respect to the taxpayer:

- (i) expenses for household services, and
- (ii) expenses for the care of a qualifying individual.

Such term shall not include any amount paid for services outside the taxpayer’s household at a camp where the qualifying individual stays overnight.

(B) EXCEPTION.—Employment-related expenses described in subparagraph (A) which are incurred for services outside the taxpayer’s household shall be taken into account only if incurred for the care of—

- (i) a qualifying individual described in paragraph (1)(A), or
- (ii) a qualifying individual (not described in paragraph (1)(A)) who regularly spends at least 8 hours each day in the taxpayer’s household.

(C) DEPENDENT CARE CENTERS.—Employment-related expenses described in subparagraph (A) which are incurred for services provided outside the taxpayer’s household by a dependent care center (as defined in subparagraph (D)) shall be taken into account only if—

- (i) such center complies with all applicable laws and regulations of a State or unit of local government, and
- (ii) the requirements of subparagraph (B) are met.

(D) DEPENDENT CARE CENTER DEFINED.—For purposes of this paragraph, the term “dependent care center” means any facility which—

- (i) provides care for more than six individuals (other than individuals who reside at the facility), and
- (ii) receives a fee, payment, or grant for providing services for any of the individuals (regardless of whether such facility is operated for profit).

(c) DOLLAR LIMIT ON AMOUNT CREDITABLE.—The amount of the employment-related expenses incurred during any taxable year which may be taken into account under subsection (a) shall not exceed—

- (1) \$3,000 if there is 1 qualifying individual with respect to the taxpayer for such taxable year, or
- (2) \$6,000 if there are 2 or more qualifying individuals with respect to the taxpayer for such taxable year.

The amount determined under paragraph (1) or (2) (whichever is applicable) shall be reduced by the aggregate amount excludable from gross income under section 129 for the taxable year.

(d) EARNED INCOME LIMITATION.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amount of the employment-related expenses incurred during any taxable year which may be taken into account under subsection (a) shall not exceed—

(A) in the case of an individual who is not married at the close of such year, such individual’s earned income for such year, or

(B) in the case of an individual who is married at the close of such year, the lesser of such individual's earned income or the earned income of his spouse for such year.

(2) SPECIAL RULE FOR SPOUSE WHO IS A STUDENT OR INCAPABLE OF CARING FOR HIMSELF.—In the case of a spouse who is a student or a qualifying individual described in subsection (b)(1)(C), for purposes of paragraph (1), such spouse shall be deemed for each month during which such spouse is a full-time student at an educational institution, or is such a qualifying individual, to be gainfully employed and to have earned income of not less than—

(A) \$250 if subsection (c)(1) applies for the taxable year,

or

(B) \$500 if subsection (c)(2) applies for the taxable year.

In the case of any husband and wife, this paragraph shall apply with respect to only one spouse for any one month.

(e) SPECIAL RULES.—For purposes of this section—

(1) PLACE OF ABODE.—An individual shall not be treated as having the same principal place of abode of the taxpayer if at any time during the taxable year of the taxpayer the relationship between the individual and the taxpayer is in violation of local law.

(2) MARRIED COUPLES MUST FILE JOINT RETURN.—If the taxpayer is married at the close of the taxable year, the credit shall be allowed under subsection (a) only if the taxpayer and his spouse file a joint return for the taxable year.

(3) MARITAL STATUS.—An individual legally separated from his spouse under a decree of divorce or of separate maintenance shall not be considered as married.

(4) CERTAIN MARRIED INDIVIDUALS LIVING APART.—If—

(A) an individual who is married and who files a separate return—

(i) maintains as his home a household which constitutes for more than one-half of the taxable year the principal place of abode of a qualifying individual, and

(ii) furnishes over half of the cost of maintaining such household during the taxable year, and

(B) during the last 6 months of such taxable year such individual's spouse is not a member of such household, such individual shall not be considered as married.

(5) SPECIAL DEPENDENCY TEST IN CASE OF DIVORCED PARENTS, ETC.—If—

(A) **[section 152(e)] section 7706(e)** applies to any child with respect to any calendar year, and

(B) such child is under the age of 13 or is physically or mentally incapable of caring for himself,

in the case of any taxable year beginning in such calendar year, such child shall be treated as a qualifying individual described in subparagraph (A) or (B) of subsection (b)(1) (whichever is appropriate) with respect to the custodial parent (as defined in **[section 152(e)(4)(A)] section 7706(e)(4)(A)**), and shall not be treated as a qualifying individual with respect to the noncustodial parent.

(6) PAYMENTS TO RELATED INDIVIDUALS.—No credit shall be allowed under subsection (a) for any amount paid by the taxpayer to an individual—

【(A) with respect to whom, for the taxable year, a deduction under section 151(c) (relating to deduction for personal exemptions for dependents) is allowable either to the taxpayer or his spouse, or】

(A) *who is a dependent of either the taxpayer or the taxpayer's spouse for the taxable year, or*

(B) who is a child of the taxpayer (within the meaning of 【section 152(f)(1)】 *section 7706(f)(1)*) who has not attained the age of 19 at the close of the taxable year.

For purposes of this paragraph, the term “taxable year” means the taxable year of the taxpayer in which the service is performed.

(7) STUDENT.—The term “student” means an individual who during each of 5 calendar months during the taxable year is a full-time student at an educational organization.

(8) EDUCATIONAL ORGANIZATION.—The term “educational organization” means an educational organization described in section 170(b)(1)(A)(ii).

(9) IDENTIFYING INFORMATION REQUIRED WITH RESPECT TO SERVICE PROVIDER.—No credit shall be allowed under subsection (a) for any amount paid to any person unless—

(A) the name, address, and taxpayer identification number of such person are included on the return claiming the credit, or

(B) if such person is an organization described in section 501(c)(3) and exempt from tax under section 501(a), the name and address of such person are included on the return claiming the credit.

In the case of a failure to provide the information required under the preceding sentence, the preceding sentence shall not apply if it is shown that the taxpayer exercised due diligence in attempting to provide the information so required.

(10) IDENTIFYING INFORMATION REQUIRED WITH RESPECT TO QUALIFYING INDIVIDUALS.—No credit shall be allowed under this section with respect to any qualifying individual unless the TIN of such individual is included on the return claiming the credit.

(f) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this section.

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## SEC. 23. ADOPTION EXPENSES.

(a) ALLOWANCE OF CREDIT.—

(1) IN GENERAL.—In the case of an individual, there shall be allowed as a credit against the tax imposed by this chapter the amount of the qualified adoption expenses paid or incurred by the taxpayer.

(2) YEAR CREDIT ALLOWED.—The credit under paragraph (1) with respect to any expense shall be allowed—

(A) in the case of any expense paid or incurred before the taxable year in which such adoption becomes final, for

the taxable year following the taxable year during which such expense is paid or incurred, and

(B) in the case of an expense paid or incurred during or after the taxable year in which such adoption becomes final, for the taxable year in which such expense is paid or incurred.

(3) \$10,000 CREDIT FOR ADOPTION OF CHILD WITH SPECIAL NEEDS REGARDLESS OF EXPENSES.—In the case of an adoption of a child with special needs which becomes final during a taxable year, the taxpayer shall be treated as having paid during such year qualified adoption expenses with respect to such adoption in an amount equal to the excess (if any) of \$10,000 over the aggregate qualified adoption expenses actually paid or incurred by the taxpayer with respect to such adoption during such taxable year and all prior taxable years.

(b) LIMITATIONS.—

(1) DOLLAR LIMITATION.—The aggregate amount of qualified adoption expenses which may be taken into account under subsection (a) for all taxable years with respect to the adoption of a child by the taxpayer shall not exceed \$10,000.

(2) INCOME LIMITATION.—

(A) IN GENERAL.—The amount allowable as a credit under subsection (a) for any taxable year (determined without regard to subsection (c)) shall be reduced (but not below zero) by an amount which bears the same ratio to the amount so allowable (determined without regard to this paragraph but with regard to paragraph (1)) as—

- (i) the amount (if any) by which the taxpayer's adjusted gross income exceeds \$150,000, bears to
- (ii) \$40,000.

(B) DETERMINATION OF ADJUSTED GROSS INCOME.—For purposes of subparagraph (A), adjusted gross income shall be determined without regard to sections 911, 931, and 933.

(3) DENIAL OF DOUBLE BENEFIT.—

(A) IN GENERAL.—No credit shall be allowed under subsection (a) for any expense for which a deduction or credit is allowed under any other provision of this chapter.

(B) GRANTS.—No credit shall be allowed under subsection (a) for any expense to the extent that funds for such expense are received under any Federal, State, or local program.

(c) CARRYFORWARDS OF UNUSED CREDIT.—

(1) IN GENERAL.—If the credit allowable under subsection (a) for any taxable year exceeds the limitation imposed by section 26(a) for such taxable year reduced by the sum of the credits allowable under this subpart (other than this section and section 25D), such excess shall be carried to the succeeding taxable year and added to the credit allowable under subsection (a) for such taxable year.

(2) LIMITATION.—No credit may be carried forward under this subsection to any taxable year following the fifth taxable year after the taxable year in which the credit arose. For purposes of the preceding sentence, credits shall be treated as used on a first-in first-out basis.

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

(1) QUALIFIED ADOPTION EXPENSES.—The term “qualified adoption expenses” means reasonable and necessary adoption fees, court costs, attorney fees, and other expenses—

(A) which are directly related to, and the principal purpose of which is for, the legal adoption of an eligible child by the taxpayer,

(B) which are not incurred in violation of State or Federal law or in carrying out any surrogate parenting arrangement,

(C) which are not expenses in connection with the adoption by an individual of a child who is the child of such individual’s spouse, and

(D) which are not reimbursed under an employer program or otherwise.

(2) ELIGIBLE CHILD.—The term “eligible child” means any individual who—

(A) has not attained age 18, or

(B) is physically or mentally incapable of caring for himself.

(3) CHILD WITH SPECIAL NEEDS.—The term “child with special needs” means any child if—

(A) a State has determined that the child cannot or should not be returned to the home of his parents,

(B) such State has determined that there exists with respect to the child a specific factor or condition (such as his ethnic background, age, or membership in a minority or sibling group, or the presence of factors such as medical conditions or physical, mental, or emotional handicaps) because of which it is reasonable to conclude that such child cannot be placed with adoptive parents without providing adoption assistance, and

(C) such child is a citizen or resident of the United States (as defined in [section 217(h)(3)] *section 217(c)(3)*).

(e) SPECIAL RULES FOR FOREIGN ADOPTIONS.—In the case of an adoption of a child who is not a citizen or resident of the United States (as defined in [section 217(h)(3)] *section 217(c)(3)*)—

(1) subsection (a) shall not apply to any qualified adoption expense with respect to such adoption unless such adoption becomes final, and

(2) any such expense which is paid or incurred before the taxable year in which such adoption becomes final shall be taken into account under this section as if such expense were paid or incurred during such year.

(f) FILING REQUIREMENTS.—

(1) MARRIED COUPLES MUST FILE JOINT RETURNS.—Rules similar to the rules of paragraphs (2), (3), and (4) of section 21(e) shall apply for purposes of this section.

(2) TAXPAYER MUST INCLUDE TIN.—

(A) IN GENERAL.—No credit shall be allowed under this section with respect to any eligible child unless the taxpayer includes (if known) the name, age, and TIN of such child on the return of tax for the taxable year.

(B) OTHER METHODS.—The Secretary may, in lieu of the information referred to in subparagraph (A), require other



information meeting the purposes of subparagraph (A), including identification of an agent assisting with the adoption.

(g) **BASIS ADJUSTMENTS.**—For purposes of this subtitle, if a credit is allowed under this section for any expenditure with respect to any property, the increase in the basis of such property which would (but for this subsection) result from such expenditure shall be reduced by the amount of the credit so allowed.

(h) **ADJUSTMENTS FOR INFLATION.**—In the case of a taxable year beginning after December 31, 2002, each of the dollar amounts in subsection (a)(3) and paragraphs (1) and (2)(A)(i) of subsection (b) shall be increased by an amount equal to—

(1) such dollar amount, multiplied by

(2) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2001” for “calendar year 2016” in subparagraph (A)(ii) thereof.

If any amount as increased under the preceding sentence is not a multiple of \$10, such amount shall be rounded to the nearest multiple of \$10.

(i) **REGULATIONS.**—The Secretary shall prescribe such regulations as may be appropriate to carry out this section and section 137, including regulations which treat unmarried individuals who pay or incur qualified adoption expenses with respect to the same child as 1 taxpayer for purposes of applying the dollar amounts in subsections (a)(3) and (b)(1) of this section and in section 137(b)(1).

#### **SEC. 24. CHILD TAX CREDIT.**

[(a) **ALLOWANCE OF CREDIT.**—There shall be allowed as a credit against the tax imposed by this chapter for the taxable year with respect to each qualifying child of the taxpayer for which the taxpayer is allowed a deduction under section 151 an amount equal to \$1,000.

[(b) **LIMITATIONS.**—

[(1) **LIMITATION BASED ON ADJUSTED GROSS INCOME.**—The amount of the credit allowable under subsection (a) shall be reduced (but not below zero) by \$50 for each \$1,000 (or fraction thereof) by which the taxpayer’s modified adjusted gross income exceeds the threshold amount. For purposes of the preceding sentence, the term “modified adjusted gross income” means adjusted gross income increased by any amount excluded from gross income under section 911, 931, or 933.

[(2) **THRESHOLD AMOUNT.**—For purposes of paragraph (1), the term “threshold amount” means—

[(A) \$110,000 in the case of a joint return,

[(B) \$75,000 in the case of an individual who is not married, and

[(C) \$55,000 in the case of a married individual filing a separate return.

For purposes of this paragraph, marital status shall be determined under section 7703.

[(c) **QUALIFYING CHILD.**—For purposes of this section—

[(1) **IN GENERAL.**—The term “qualifying child” means a qualifying child of the taxpayer (as defined in section 152(c)) who has not attained age 17.

**[(2) EXCEPTION FOR CERTAIN NONCITIZENS.—**The term “qualifying child” shall not include any individual who would not be a dependent if subparagraph (A) of section 152(b)(3) were applied without regard to all that follows “resident of the United States”.**]**

(a) **ALLOWANCE OF CREDIT.—***There shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to the sum of—*

- (1) \$2,000 for each qualifying child of the taxpayer, and
- (2) \$500 for each qualifying dependent (other than a qualifying child) of the taxpayer.

(b) **LIMITATION BASED ON ADJUSTED GROSS INCOME.—***The amount of the credit allowable under subsection (a) shall be reduced (but not below zero) by \$50 for each \$1,000 (or fraction thereof) by which the taxpayer’s modified adjusted gross income exceeds \$400,000 in the case of a joint return (\$200,000 in any other case). For purposes of the preceding sentence, the term “modified adjusted gross income” means adjusted gross income increased by any amount excluded from gross income under section 911, 931, or 933.*

(c) **QUALIFYING CHILD; QUALIFYING DEPENDENT.—***For purposes of this section—*

(1) **QUALIFYING CHILD.—***The term “qualifying child” means any qualifying dependent of the taxpayer—*

(A) *who is a qualifying child (as defined in section 7706(c)) of the taxpayer,*

(B) *who has not attained age 17 at the close of the calendar year in which the taxable year of the taxpayer begins, and*

(C) *whose name and social security number are included on the taxpayer’s return of tax for the taxable year.*

(2) **QUALIFYING DEPENDENT.—***The term “qualifying dependent” means any dependent of the taxpayer (as defined in section 7706 without regard to all that follows “resident of the United States” in section 7706(b)(3)(A)) whose name and TIN are included on the taxpayer’s return of tax for the taxable year.*

(3) **SOCIAL SECURITY NUMBER DEFINED.—***For purposes of this subsection, the term “social security number” means, with respect to a return of tax, a social security number issued to an individual by the Social Security Administration, but only if the social security number is issued—*

(A) *to a citizen of the United States or pursuant to subclause (I) (or that portion of subclause (III) that relates to subclause (I)) of section 205(c)(2)(B)(i) of the Social Security Act, and*

(B) *on or before the due date of filing such return.*

(d) **PORTION OF CREDIT REFUNDABLE.—**

(1) **IN GENERAL.—***The aggregate credits allowed to a taxpayer under subpart C shall be increased by the lesser of—*

**[(A) the credit which would be allowed under this section without regard to this subsection and the limitation under section 26(a) or]**

*(A) the credit which would be allowed under this section determined—*

*(i) by substituting “\$1,400” for “\$2,000” in subsection (a)(1),*

(ii) without regard to subsection (a)(2), and  
 (iii) without regard to this subsection and the limitation under section 26(a), or

(B) the amount by which the aggregate amount of credits allowed by this subpart (determined without regard to this subsection) would increase if the limitation imposed by section 26(a) were increased by the greater of—

(i) 15 percent of so much of the taxpayer's earned income (within the meaning of section 32) which is taken into account in computing taxable income for the taxable year as exceeds ~~【\$3,000】~~ \$2,500, or

(ii) in the case of a taxpayer with 3 or more qualifying children, the excess (if any) of—

(I) the taxpayer's social security taxes for the taxable year, over

(II) the credit allowed under section 32 for the taxable year.

The amount of the credit allowed under this subsection shall not be treated as a credit allowed under this subpart and shall reduce the amount of credit otherwise allowable under subsection (a) without regard to section 26(a). For purposes of subparagraph (B), any amount excluded from gross income by reason of section 112 shall be treated as earned income which is taken into account in computing taxable income for the taxable year.

(2) SOCIAL SECURITY TAXES.—For purposes of paragraph (1)—

(A) IN GENERAL.—The term “social security taxes” means, with respect to any taxpayer for any taxable year—

(i) the amount of the taxes imposed by sections 3101 and 3201(a) on amounts received by the taxpayer during the calendar year in which the taxable year begins,

(ii) 50 percent of the taxes imposed by section 1401 on the self-employment income of the taxpayer for the taxable year, and

(iii) 50 percent of the taxes imposed by section 3211(a) on amounts received by the taxpayer during the calendar year in which the taxable year begins.

(B) COORDINATION WITH SPECIAL REFUND OF SOCIAL SECURITY TAXES.—The term “social security taxes” shall not include any taxes to the extent the taxpayer is entitled to a special refund of such taxes under section 6413(c).

(C) SPECIAL RULE.—Any amounts paid pursuant to an agreement under section 3121(l) (relating to agreements entered into by American employers with respect to foreign affiliates) which are equivalent to the taxes referred to in subparagraph (A)(i) shall be treated as taxes referred to in such subparagraph.

(3) EXCEPTION FOR TAXPAYERS EXCLUDING FOREIGN EARNED INCOME.—Paragraph (1) shall not apply to any taxpayer for any taxable year if such taxpayer elects to exclude any amount from gross income under section 911 for such taxable year.

(4) ADJUSTMENT FOR INFLATION.—

(A) *IN GENERAL.*—In the case of a taxable year beginning after 2018, the \$1,400 amount in paragraph (1)(A)(i) shall be increased by an amount equal to—

- (i) such dollar amount, multiplied by
- (ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “2017” for “2016” in subparagraph (A)(ii) thereof.

(B) *ROUNDING.*—If any increase under subparagraph (A) is not a multiple of \$100, such increase shall be rounded to the next lowest multiple of \$100.

(C) *LIMITATION.*—The amount of any increase under subparagraph (A) (after the application of subparagraph (B)) shall not exceed \$600.

**[(e) IDENTIFICATION REQUIREMENTS.—**

**[(1) QUALIFYING CHILD IDENTIFICATION REQUIREMENT.—**No credit shall be allowed under this section to a taxpayer with respect to any qualifying child unless the taxpayer includes the name and taxpayer identification number of such qualifying child on the return of tax for the taxable year and such taxpayer identification number was issued on or before the due date for filing such return.

**[(2) TAXPAYER IDENTIFICATION REQUIREMENT.—**No credit shall be allowed under this section if the taxpayer identification number of the taxpayer was issued after the due date for filing the return for the taxable year.]

*(e) TAXPAYER IDENTIFICATION REQUIREMENT.—*No credit shall be allowed under this section if the identifying number of the taxpayer was issued after the due date for filing the return of tax for the taxable year.

(f) *TAXABLE YEAR MUST BE FULL TAXABLE YEAR.*—Except in the case of a taxable year closed by reason of the death of the taxpayer, no credit shall be allowable under this section in the case of a taxable year covering a period of less than 12 months.

(g) *RESTRICTIONS ON TAXPAYERS WHO IMPROPERLY CLAIMED CREDIT IN PRIOR YEAR.—*

**(1) TAXPAYERS MAKING PRIOR FRAUDULENT OR RECKLESS CLAIMS.—**

(A) *IN GENERAL.*—No credit shall be allowed under this section for any taxable year in the disallowance period.

(B) *DISALLOWANCE PERIOD.*—For purposes of subparagraph (A), the disallowance period is—

- (i) the period of 10 taxable years after the most recent taxable year for which there was a final determination that the taxpayer’s claim of credit under this section was due to fraud, and
- (ii) the period of 2 taxable years after the most recent taxable year for which there was a final determination that the taxpayer’s claim of credit under this section was due to reckless or intentional disregard of rules and regulations (but not due to fraud).

**(2) TAXPAYERS MAKING IMPROPER PRIOR CLAIMS.—**In the case of a taxpayer who is denied credit under this section for any taxable year as a result of the deficiency procedures under subchapter B of chapter 63, no credit shall be allowed under this

section for any subsequent taxable year unless the taxpayer provides such information as the Secretary may require to demonstrate eligibility for such credit.

**[(h) SPECIAL RULES FOR TAXABLE YEARS 2018 THROUGH 2025.—**

**[(1) IN GENERAL.—**In the case of a taxable year beginning after December 31, 2017, and before January 1, 2026, this section shall be applied as provided in paragraphs (2) through (7).

**[(2) CREDIT AMOUNT.—**Subsection (a) shall be applied by substituting “\$2,000” for “\$1,000”.

**[(3) LIMITATION.—**In lieu of the amount determined under subsection (b)(2), the threshold amount shall be \$400,000 in the case of a joint return (\$200,000 in any other case).

**[(4) PARTIAL CREDIT ALLOWED FOR CERTAIN OTHER DEPENDENTS.—**

**[(A) IN GENERAL.—**The credit determined under subsection (a) (after the application of paragraph (2)) shall be increased by \$500 for each dependent of the taxpayer (as defined in section 152) other than a qualifying child described in subsection (c).

**[(B) EXCEPTION FOR CERTAIN NONCITIZENS.—**Subparagraph (A) shall not apply with respect to any individual who would not be a dependent if subparagraph (A) of section 152(b)(3) were applied without regard to all that follows “resident of the United States”.

**[(C) CERTAIN QUALIFYING CHILDREN.—**In the case of any qualifying child with respect to whom a credit is not allowed under this section by reason of paragraph (7), such child shall be treated as a dependent to whom subparagraph (A) applies.

**[(5) MAXIMUM AMOUNT OF REFUNDABLE CREDIT.—**

**[(A) IN GENERAL.—**The amount determined under subsection (d)(1)(A) with respect to any qualifying child shall not exceed \$1,400, and such subsection shall be applied without regard to paragraph (4) of this subsection.

**[(B) ADJUSTMENT FOR INFLATION.—**In the case of a taxable year beginning after 2018, the \$1,400 amount in subparagraph (A) shall be increased by an amount equal to—

**[(i) such dollar amount, multiplied by**

**[(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “2017” for “2016” in subparagraph (A)(ii) thereof.**

If any increase under this clause is not a multiple of \$100, such increase shall be rounded to the next lowest multiple of \$100.

**[(6) EARNED INCOME THRESHOLD FOR REFUNDABLE CREDIT.—**Subsection (d)(1)(B)(i) shall be applied by substituting “\$2,500” for “\$3,000”.

**[(7) SOCIAL SECURITY NUMBER REQUIRED.—**No credit shall be allowed under this section to a taxpayer with respect to any qualifying child unless the taxpayer includes the social security number of such child on the return of tax for the taxable year. For purposes of the preceding sentence, the term “social security number” means a social security number issued to an indi-

vidual by the Social Security Administration, but only if the social security number is issued—

【(A) to a citizen of the United States or pursuant to subclause (I) (or that portion of subclause (III) that relates to subclause (I)) of section 205(c)(2)(B)(i) of the Social Security Act, and

【(B) before the due date for such return.】

\* \* \* \* \*

**SEC. 25A. AMERICAN OPPORTUNITY AND LIFETIME LEARNING CREDITS.**

(a) ALLOWANCE OF CREDIT.—In the case of an individual, there shall be allowed as a credit against the tax imposed by this chapter for the taxable year the amount equal to the sum of—

- (1) the American Opportunity Tax Credit, plus
- (2) the Lifetime Learning Credit.

(b) AMERICAN OPPORTUNITY TAX CREDIT.—

(1) PER STUDENT CREDIT.—In the case of any eligible student for whom an election is in effect under this section for any taxable year, the American Opportunity Tax Credit is an amount equal to the sum of—

(A) 100 percent of so much of the qualified tuition and related expenses paid by the taxpayer during the taxable year (for education furnished to the eligible student during any academic period beginning in such taxable year) as does not exceed \$2,000, plus

(B) 25 percent of such expenses so paid as exceeds \$2,000 but does not exceed \$4,000.

(2) LIMITATIONS APPLICABLE TO AMERICAN OPPORTUNITY TAX CREDIT.—

(A) CREDIT ALLOWED ONLY FOR 4 TAXABLE YEARS.—An election to have this section apply with respect to any eligible student for purposes of the American Opportunity Tax Credit under subsection (a)(1) may not be made for any taxable year if such an election (by the taxpayer or any other individual) is in effect with respect to such student for any 4 prior taxable years.

(B) CREDIT ALLOWED FOR YEAR ONLY IF INDIVIDUAL IS AT LEAST 1/2 TIME STUDENT FOR PORTION OF YEAR.—The American Opportunity Tax Credit under subsection (a)(1) shall not be allowed for a taxable year with respect to the qualified tuition and related expenses of an individual unless such individual is an eligible student for at least one academic period which begins during such year.

(C) CREDIT ALLOWED ONLY FOR FIRST 4 YEARS OF POST-SECONDARY EDUCATION.—The American Opportunity Tax Credit under subsection (a)(1) shall not be allowed for a taxable year with respect to the qualified tuition and related expenses of an eligible student if the student has completed (before the beginning of such taxable year) the first 4 years of postsecondary education at an eligible educational institution.

(D) DENIAL OF CREDIT IF STUDENT CONVICTED OF A FELONY DRUG OFFENSE.—The American Opportunity Tax Credit under subsection (a)(1) shall not be allowed for

qualified tuition and related expenses for the enrollment or attendance of a student for any academic period if such student has been convicted of a Federal or State felony offense consisting of the possession or distribution of a controlled substance before the end of the taxable year with or within which such period ends.

(3) **ELIGIBLE STUDENT.**—For purposes of this subsection, the term “eligible student” means, with respect to any academic period, a student who—

(A) meets the requirements of section 484(a)(1) of the Higher Education Act of 1965 (20 U.S.C. 1091(a)(1)), as in effect on the date of the enactment of this section, and

(B) is carrying at least 1/2 the normal full-time work load for the course of study the student is pursuing.

(4) **RESTRICTIONS ON TAXPAYERS WHO IMPROPERLY CLAIMED AMERICAN OPPORTUNITY TAX CREDIT IN PRIOR YEARS.**—

(A) **TAXPAYERS MAKING PRIOR FRAUDULENT OR RECKLESS CLAIMS.**—

(i) **IN GENERAL.**—No American Opportunity Tax Credit shall be allowed under this section for any taxable year in the disallowance period.

(ii) **DISALLOWANCE PERIOD.**—For purposes of subparagraph (A), the disallowance period is—

(I) the period of 10 taxable years after the most recent taxable year for which there was a final determination that the taxpayer’s claim of the American Opportunity Tax Credit under this section was due to fraud, and

(II) the period of 2 taxable years after the most recent taxable year for which there was a final determination that the taxpayer’s claim of the American Opportunity Tax Credit under this section was due to reckless or intentional disregard of rules and regulations (but not due to fraud).

(B) **TAXPAYERS MAKING IMPROPER PRIOR CLAIMS.**—In the case of a taxpayer who is denied the American Opportunity Tax Credit under this section for any taxable year as a result of the deficiency procedures under subchapter B of chapter 63, no American Opportunity Tax Credit shall be allowed under this section for any subsequent taxable year unless the taxpayer provides such information as the Secretary may require to demonstrate eligibility for such credit.

(c) **LIFETIME LEARNING CREDIT.**—

(1) **PER TAXPAYER CREDIT.**—The Lifetime Learning Credit for any taxpayer for any taxable year is an amount equal to 20 percent of so much of the qualified tuition and related expenses paid by the taxpayer during the taxable year (for education furnished during any academic period beginning in such taxable year) as does not exceed \$10,000.

(2) **SPECIAL RULES FOR DETERMINING EXPENSES.**—

(A) **COORDINATION WITH AMERICAN OPPORTUNITY TAX CREDIT.**—The qualified tuition and related expenses with respect to an individual who is an eligible student for whom a American Opportunity Tax Credit under sub-

section (a)(1) is allowed for the taxable year shall not be taken into account under this subsection.

(B) EXPENSES ELIGIBLE FOR LIFETIME LEARNING CREDIT.—For purposes of paragraph (1), qualified tuition and related expenses shall include expenses described in subsection (f)(1) with respect to any course of instruction at an eligible educational institution to acquire or improve job skills of the individual.

(d) LIMITATIONS BASED ON MODIFIED ADJUSTED GROSS INCOME.—

(1) AMERICAN OPPORTUNITY TAX CREDIT.—The American Opportunity Tax Credit (determined without regard to this paragraph) shall be reduced (but not below zero) by the amount which bears the same ratio to such credit (as so determined) as—

(A) the excess of—

(i) the taxpayer's modified adjusted gross income for such taxable year, over

(ii) \$80,000 (\$160,000 in the case of a joint return), bears to (B) \$10,000 (\$20,000 in the case of a joint return).

(2) LIFETIME LEARNING CREDIT.—The Lifetime Learning Credit (determined without regard to this paragraph) shall be reduced (but not below zero) by the amount which bears the same ratio to such credit (as so determined) as—

(A) the excess of—

(i) the taxpayer's modified adjusted gross income for such taxable year, over

(ii) \$40,000 (\$80,000 in the case of a joint return), bears to (B) \$10,000 (\$20,000 in the case of a joint return).

(3) MODIFIED ADJUSTED GROSS INCOME.—For purposes of this subsection, the term “modified adjusted gross income” means the adjusted gross income of the taxpayer for the taxable year increased by any amount excluded from gross income under section 911, 931, or 933.

(e) ELECTION NOT TO HAVE SECTION APPLY.—A taxpayer may elect not to have this section apply with respect to the qualified tuition and related expenses of an individual for any taxable year.

(f) DEFINITIONS.—For purposes of this section—

(1) QUALIFIED TUITION AND RELATED EXPENSES.—

(A) IN GENERAL.—The term “qualified tuition and related expenses” means tuition and fees required for the enrollment or attendance of—

(i) the taxpayer,

(ii) the taxpayer's spouse, or

(iii) any dependent of the taxpayer [with respect to whom the taxpayer is allowed a deduction under section 151],

at an eligible educational institution for courses of instruction of such individual at such institution.

(B) EXCEPTION FOR EDUCATION INVOLVING SPORTS, ETC.—Such term does not include expenses with respect to any course or other education involving sports, games, or hobbies, unless such course or other education is part of the individual's degree program.



(C) EXCEPTION FOR NONACADEMIC FEES.—Such term does not include student activity fees, athletic fees, insurance expenses, or other expenses unrelated to an individual's academic course of instruction.

(D) REQUIRED COURSE MATERIALS TAKEN INTO ACCOUNT FOR AMERICAN OPPORTUNITY TAX CREDIT.—For purposes of determining the American Opportunity Tax Credit, subparagraph (A) shall be applied by substituting “tuition, fees, and course materials” for “tuition and fees”.

(2) ELIGIBLE EDUCATIONAL INSTITUTION.—The term “eligible educational institution” means an institution—

(A) which is described in section 481 of the Higher Education Act of 1965 (20 U.S.C. 1088), as in effect on the date of the enactment of this section, and

(B) which is eligible to participate in a program under title IV of such Act.

(g) SPECIAL RULES.—

(1) IDENTIFICATION REQUIREMENT.—

(A) IN GENERAL.—No credit shall be allowed under subsection (a) to a taxpayer with respect to the qualified tuition and related expenses of an individual unless the taxpayer includes the name and taxpayer identification number of such individual on the return of tax for the taxable year.

(B) ADDITIONAL IDENTIFICATION REQUIREMENTS WITH RESPECT TO AMERICAN OPPORTUNITY TAX CREDIT.—

(i) STUDENT.—The requirements of subparagraph (A) shall not be treated as met with respect to the American Opportunity Tax Credit unless the individual's taxpayer identification number was issued on or before the due date for filing the return of tax for the taxable year.

(ii) TAXPAYER.—No American Opportunity Tax Credit shall be allowed under this section if the taxpayer identification number of the taxpayer was issued after the due date for filing the return for the taxable year.

(iii) INSTITUTION.—No American Opportunity Tax Credit shall be allowed under this section unless the taxpayer includes the employer identification number of any institution to which qualified tuition and related expenses were paid with respect to the individual.

(2) ADJUSTMENT FOR CERTAIN SCHOLARSHIPS, ETC.—The amount of qualified tuition and related expenses otherwise taken into account under subsection (a) with respect to an individual for an academic period shall be reduced (before the application of subsections (b), (c), and (d)) by the sum of any amounts paid for the benefit of such individual which are allocable to such period as—

(A) a qualified scholarship which is excludable from gross income under section 117,

(B) an educational assistance allowance under chapter 30, 31, 32, 34, or 35 of title 38, United States Code, or under chapter 1606 of title 10, United States Code, and

(C) a payment (other than a gift, bequest, devise, or inheritance within the meaning of section 102(a)) for such individual's educational expenses, or attributable to such individual's enrollment at an eligible educational institution, which is excludable from gross income under any law of the United States.

(3) TREATMENT OF EXPENSES PAID BY DEPENDENT.—**[[If a deduction under section 151 with respect to an individual is allowed to another taxpayer]** *If an individual is a dependent of another taxpayer* for a taxable year beginning in the calendar year in which such individual's taxable year begins—

(A) no credit shall be allowed under subsection (a) to such individual for such individual's taxable year,

(B) qualified tuition and related expenses paid by such individual during such individual's taxable year shall be treated for purposes of this section as paid by such other taxpayer, and

(C) a statement described in paragraph (8) and received by such individual shall be treated as received by the taxpayer.

(4) TREATMENT OF CERTAIN PREPAYMENTS.—If qualified tuition and related expenses are paid by the taxpayer during a taxable year for an academic period which begins during the first 3 months following such taxable year, such academic period shall be treated for purposes of this section as beginning during such taxable year.

(5) DENIAL OF DOUBLE BENEFIT.—No credit shall be allowed under this section for any expense for which a deduction is allowed under any other provision of this chapter.

(6) NO CREDIT FOR MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—If the taxpayer is a married individual (within the meaning of section 7703), this section shall apply only if the taxpayer and the taxpayer's spouse file a joint return for the taxable year.

(7) NONRESIDENT ALIENS.—If the taxpayer is a nonresident alien individual for any portion of the taxable year, this section shall apply only if such individual is treated as a resident alien of the United States for purposes of this chapter by reason of an election under subsection (g) or (h) of section 6013.

(8) PAYEE STATEMENT REQUIREMENT.—Except as otherwise provided by the Secretary, no credit shall be allowed under this section unless the taxpayer receives a statement furnished under section 6050S(d) which contains all of the information required by paragraph (2) thereof.

(h) INFLATION ADJUSTMENT.—

(1) IN GENERAL.—In the case of a taxable year beginning after 2001, the \$40,000 and \$80,000 amounts in subsection (d)(2) shall each be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting "calendar year 2000" for "calendar year 2016" in subparagraph (A)(ii) thereof.

(2) **ROUNDING.**—If any amount as adjusted under paragraph (1) is not a multiple of \$1,000, such amount shall be rounded to the next lowest multiple of \$1,000.

(i) **PORTRION OF AMERICAN OPPORTUNITY TAX CREDIT MADE REFUNDABLE.**—Forty percent of so much of the credit allowed under subsection (a) as is attributable to the American Opportunity Tax Credit (determined after application of subsection (d) and without regard to this paragraph and section 26(a)) shall be treated as a credit allowable under subpart C (and not allowed under subsection (a)). The preceding sentence shall not apply to any taxpayer for any taxable year if such taxpayer is a child to whom subsection (g) of section 1 applies for such taxable year.

(j) **REGULATIONS.**—The Secretary may prescribe such regulations as may be necessary or appropriate to carry out this section, including regulations providing for a recapture of the credit allowed under this section in cases where there is a refund in a subsequent taxable year of any amount which was taken into account in determining the amount of such credit.

**SEC. 25B. ELECTIVE DEFERRALS AND IRA CONTRIBUTIONS BY CERTAIN INDIVIDUALS.**

(a) **ALLOWANCE OF CREDIT.**—In the case of an eligible individual, there shall be allowed as a credit against the tax imposed by this subtitle for the taxable year an amount equal to the applicable percentage of so much of the qualified retirement savings contributions of the eligible individual for the taxable year as do not exceed \$2,000.

(b) **APPLICABLE PERCENTAGE.**—For purposes of this section—

(1) **JOINT RETURNS.**—In the case of a joint return, the applicable percentage is—

(A) if the adjusted gross income of the taxpayer is not over \$30,000, 50 percent,

(B) if the adjusted gross income of the taxpayer is over \$30,000 but not over \$32,500, 20 percent,

(C) if the adjusted gross income of the taxpayer is over \$32,500 but not over \$50,000, 10 percent, and

(D) if the adjusted gross income of the taxpayer is over \$50,000, zero percent.

(2) **OTHER RETURNS.**—In the case of—

(A) a head of household, the applicable percentage shall be determined under paragraph (1) except that such paragraph shall be applied by substituting for each dollar amount therein (as adjusted under paragraph (3)) a dollar amount equal to 75 percent of such dollar amount, and

(B) any taxpayer not described in paragraph (1) or subparagraph (A), the applicable percentage shall be determined under paragraph (1) except that such paragraph shall be applied by substituting for each dollar amount therein (as adjusted under paragraph (3)) a dollar amount equal to 50 percent of such dollar amount.

(3) **INFLATION ADJUSTMENT.**—In the case of any taxable year beginning in a calendar year after 2006, each of the dollar amounts in paragraph (1) shall be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2005” for “calendar year 2016” in subparagraph (A)(ii) thereof.

Any increase determined under the preceding sentence shall be rounded to the nearest multiple of \$500.

(c) ELIGIBLE INDIVIDUAL.—For purposes of this section—

(1) IN GENERAL.—The term “eligible individual” means any individual if such individual has attained the age of 18 as of the close of the taxable year.

(2) DEPENDENTS AND FULL-TIME STUDENTS NOT ELIGIBLE.—The term “eligible individual” shall not include—

(A) [any individual with respect to whom a deduction under section 151 is allowed to another taxpayer] *any individual who is a dependent of another taxpayer* for a taxable year beginning in the calendar year in which such individual’s taxable year begins, and

(B) any individual who is a student (as defined in [section 152(f)(2)] *section 7706(f)(2)*).

(d) QUALIFIED RETIREMENT SAVINGS CONTRIBUTIONS.—For purposes of this section—

(1) IN GENERAL.—The term “qualified retirement savings contributions” means, with respect to any taxable year, the sum of—

(A) the amount of the qualified retirement contributions (as defined in section 219(e)) made by the eligible individual,

(B) the amount of—

(i) any elective deferrals (as defined in section 402(g)(3)) of such individual, and

(ii) any elective deferral of compensation by such individual under an eligible deferred compensation plan (as defined in section 457(b)) of an eligible employer described in section 457(e)(1)(A),

(C) the amount of voluntary employee contributions by such individual to any qualified retirement plan (as defined in section 4974(c)), and

(D) the amount of contributions [made before January 1, 2026,] by such individual to the ABLE account (within the meaning of section 529A) of which such individual is the designated beneficiary.

(2) REDUCTION FOR CERTAIN DISTRIBUTIONS.—

(A) IN GENERAL.—The qualified retirement savings contributions determined under paragraph (1) shall be reduced (but not below zero) by the aggregate distributions received by the individual during the testing period from any entity of a type to which contributions under paragraph (1) may be made. The preceding sentence shall not apply to the portion of any distribution which is not includible in gross income by reason of a trustee-to-trustee transfer or a rollover distribution.

(B) TESTING PERIOD.—For purposes of subparagraph (A), the testing period, with respect to a taxable year, is the period which includes—

(i) such taxable year,

- (ii) the 2 preceding taxable years, and
- (iii) the period after such taxable year and before the due date (including extensions) for filing the return of tax for such taxable year.

(C) EXCEPTED DISTRIBUTIONS.—There shall not be taken into account under subparagraph (A)—

- (i) any distribution referred to in section 72(p), 401(k)(8), 401(m)(6), 402(g)(2), 404(k), or 408(d)(4), and
- (ii) any distribution to which section 408A(d)(3) applies.

(D) TREATMENT OF DISTRIBUTIONS RECEIVED BY SPOUSE OF INDIVIDUAL.—For purposes of determining distributions received by an individual under subparagraph (A) for any taxable year, any distribution received by the spouse of such individual shall be treated as received by such individual if such individual and spouse file a joint return for such taxable year and for the taxable year during which the spouse receives the distribution.

(e) ADJUSTED GROSS INCOME.—For purposes of this section, adjusted gross income shall be determined without regard to sections 911, 931, and 933.

(f) INVESTMENT IN THE CONTRACT.—Notwithstanding any other provision of law, a qualified retirement savings contribution shall not fail to be included in determining the investment in the contract for purposes of section 72 by reason of the credit under this section.

\* \* \* \* \*

**Subpart C—Refundable Credits**

\* \* \* \* \*

**SEC. 32. EARNED INCOME.**

(a) ALLOWANCE OF CREDIT.—

(1) IN GENERAL.—In the case of an eligible individual, there shall be allowed as a credit against the tax imposed by this subtitle for the taxable year an amount equal to the credit percentage of so much of the taxpayer’s earned income for the taxable year as does not exceed the earned income amount.

(2) LIMITATION.—The amount of the credit allowable to a taxpayer under paragraph (1) for any taxable year shall not exceed the excess (if any) of—

(A) the credit percentage of the earned income amount, over

(B) the phaseout percentage of so much of the adjusted gross income (or, if greater, the earned income) of the taxpayer for the taxable year as exceeds the phaseout amount.

(b) PERCENTAGES AND AMOUNTS.—For purposes of subsection (a)—

(1) PERCENTAGES.—The credit percentage and the phaseout percentage shall be determined as follows:

| In the case of an eligible individual with: | The credit percentage is: | The phaseout percentage is: |
|---|---------------------------|-----------------------------|
| 1 qualifying child                          | 34                        | 15.98                       |
| 2 qualifying children                       | 40                        | 21.06                       |
| 3 or more qualifying children               | 45                        | 21.06                       |
| No qualifying children                      | 7.65                      | 7.65                        |

## (2) AMOUNTS.—

(A) IN GENERAL.—Subject to subparagraph (B), the earned income amount and the phaseout amount shall be determined as follows:

| In the case of an eligible individual with: | The earned income amount is: | The phaseout amount is: |
|---|------------------------------|-------------------------|
| 1 qualifying child                          | \$6,330                      | \$11,610                |
| 2 or more qualifying children               | \$8,890                      | \$11,610                |
| No qualifying children                      | \$4,220                      | \$ 5,280                |

(B) JOINT RETURNS.—In the case of a joint return filed by an eligible individual and such individual's spouse, the phaseout amount determined under subparagraph (A) shall be increased by \$5,000.

(c) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

## (1) ELIGIBLE INDIVIDUAL.—

(A) IN GENERAL.—The term “eligible individual” means—

(i) any individual who has a qualifying child for the taxable year, or

(ii) any other individual who does not have a qualifying child for the taxable year, if—

(I) such individual's principal place of abode is in the United States for more than one-half of such taxable year,

(II) such individual (or, if the individual is married, either the individual or the individual's spouse) has attained age 25 but not attained age 65 before the close of the taxable year, and

(III) such individual is not **[a dependent for whom a deduction is allowable under section 151 to another taxpayer]** *a dependent of another taxpayer* for any taxable year beginning in the same calendar year as such taxable year.

For purposes of the preceding sentence, marital status shall be determined under section 7703.

(B) QUALIFYING CHILD INELIGIBLE.—If an individual is the qualifying child of a taxpayer for any taxable year of such taxpayer beginning in a calendar year, such individual shall not be treated as an eligible individual for any taxable year of such individual beginning in such calendar year.

(C) EXCEPTION FOR INDIVIDUAL CLAIMING BENEFITS UNDER SECTION 911.—The term “eligible individual” does not include any individual who claims the benefits of sec-

tion 911 (relating to citizens or residents living abroad) for the taxable year.

(D) LIMITATION ON ELIGIBILITY OF NONRESIDENT ALIENS.—The term “eligible individual” shall not include any individual who is a nonresident alien individual for any portion of the taxable year unless such individual is treated for such taxable year as a resident of the United States for purposes of this chapter by reason of an election under subsection (g) or (h) of section 6013.

(E) IDENTIFICATION NUMBER REQUIREMENT.—No credit shall be allowed under this section to an eligible individual who does not include on the return of tax for the taxable year—

- (i) such individual’s taxpayer identification number, and
- (ii) if the individual is married (within the meaning of section 7703), the taxpayer identification number of such individual’s spouse.

(G) INDIVIDUALS WHO DO NOT INCLUDE TIN, ETC., OF ANY QUALIFYING CHILD.—No credit shall be allowed under this section to any eligible individual who has one or more qualifying children if no qualifying child of such individual is taken into account under subsection (b) by reason of paragraph (3)(D).

(2) EARNED INCOME.—

(A) The term “earned income” means—

- (i) wages, salaries, tips, and other employee compensation, but only if such amounts are includible in gross income for the taxable year, plus
- (ii) the amount of the taxpayer’s net earnings from self-employment for the taxable year (within the meaning of section 1402(a)), but such net earnings shall be determined with regard to the deduction allowed to the taxpayer by section 164(f).

(B) For purposes of subparagraph (A)—

- (i) the earned income of an individual shall be computed without regard to any community property laws,
- (ii) no amount received as a pension or annuity shall be taken into account,
- (iii) no amount to which section 871(a) applies (relating to income of nonresident alien individuals not connected with United States business) shall be taken into account,
- (iv) no amount received for services provided by an individual while the individual is an inmate at a penal institution shall be taken into account,
- (v) no amount described in subparagraph (A) received for service performed in work activities as defined in paragraph (4) or (7) of section 407(d) of the Social Security Act to which the taxpayer is assigned under any State program under part A of title IV of such Act shall be taken into account, but only to the extent such amount is subsidized under such State program, and

(vi) a taxpayer may elect to treat amounts excluded from gross income by reason of section 112 as earned income.

(3) QUALIFYING CHILD.—

(A) IN GENERAL.—The term “qualifying child” means a qualifying child of the taxpayer (as defined in [section 152(c)] *section 7706(c)*), determined without regard to paragraph (1)(D) thereof and [section 152(e)] *section 7706(e)*).

(B) MARRIED INDIVIDUAL.—The term “qualifying child” shall not include an individual who is married as of the close of the taxpayer’s taxable year [unless the taxpayer is entitled to a deduction under section 151 for such taxable year with respect to such individual (or would be so entitled but for section 152(e)] *if such individual is not treated as a dependent of such taxpayer for such taxable year by reason of section 7706(b)(2) (determined without regard to section 7706(e))*).

(C) PLACE OF ABODE.—For purposes of subparagraph (A), the requirements of [section 152(c)(1)(B)] *section 7706(c)(1)(B)* shall be met only if the principal place of abode is in the United States.

(D) IDENTIFICATION REQUIREMENTS.—

(i) IN GENERAL.—A qualifying child shall not be taken into account under subsection (b) unless the taxpayer includes the name, age, and TIN of the qualifying child on the return of tax for the taxable year.

(ii) OTHER METHODS.—The Secretary may prescribe other methods for providing the information described in clause (i).

(4) TREATMENT OF MILITARY PERSONNEL STATIONED OUTSIDE THE UNITED STATES.—For purposes of paragraphs (1)(A)(ii)(I) and (3)(C), the principal place of abode of a member of the Armed Forces of the United States shall be treated as in the United States during any period during which such member is stationed outside the United States while serving on extended active duty with the Armed Forces of the United States. For purposes of the preceding sentence, the term “extended active duty” means any period of active duty pursuant to a call or order to such duty for a period in excess of 90 days or for an indefinite period.

(d) MARRIED INDIVIDUALS.—In the case of an individual who is married (within the meaning of section 7703), this section shall apply only if a joint return is filed for the taxable year under section 6013.

(e) TAXABLE YEAR MUST BE FULL TAXABLE YEAR.—Except in the case of a taxable year closed by reason of the death of the taxpayer, no credit shall be allowable under this section in the case of a taxable year covering a period of less than 12 months.

(f) AMOUNT OF CREDIT TO BE DETERMINED UNDER TABLES.—

(1) IN GENERAL.—The amount of the credit allowed by this section shall be determined under tables prescribed by the Secretary.

(2) REQUIREMENTS FOR TABLES.—The tables prescribed under paragraph (1) shall reflect the provisions of subsections (a) and



(b) and shall have income brackets of not greater than \$50 each—

(A) for earned income between \$0 and the amount of earned income at which the credit is phased out under subsection (b), and

(B) for adjusted gross income between the dollar amount at which the phaseout begins under subsection (b) and the amount of adjusted gross income at which the credit is phased out under subsection (b).

(i) DENIAL OF CREDIT FOR INDIVIDUALS HAVING EXCESSIVE INVESTMENT INCOME.—

(1) IN GENERAL.—No credit shall be allowed under subsection (a) for the taxable year if the aggregate amount of disqualified income of the taxpayer for the taxable year exceeds \$2,200.

(2) DISQUALIFIED INCOME.—For purposes of paragraph (1), the term “disqualified income” means—

(A) interest or dividends to the extent includible in gross income for the taxable year,

(B) interest received or accrued during the taxable year which is exempt from tax imposed by this chapter,

(C) the excess (if any) of—

(i) gross income from rents or royalties not derived in the ordinary course of a trade or business, over

(ii) the sum of—

(I) the deductions (other than interest) which are clearly and directly allocable to such gross income, plus

(II) interest deductions properly allocable to such gross income,

(D) the capital gain net income (as defined in section 1222) of the taxpayer for such taxable year, and

(E) the excess (if any) of—

(i) the aggregate income from all passive activities for the taxable year (determined without regard to any amount included in earned income under subsection (c)(2) or described in a preceding subparagraph), over

(ii) the aggregate losses from all passive activities for the taxable year (as so determined).

For purposes of subparagraph (E), the term “passive activity” has the meaning given such term by section 469.

(j) INFLATION ADJUSTMENTS.—

(1) IN GENERAL.—In the case of any taxable year beginning after 2015, each of the dollar amounts in subsections (b)(2) and (i)(1) shall be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting in subparagraph (A)(ii) thereof—

(i) in the case of amounts in subsections (b)(2)(A) and (i)(1), “calendar year 1995” for “calendar year 2016, and

(ii) in the case of the \$5,000 amount in subsection (b)(2)(B), “calendar year 2008” for “calendar year 2016”.

## (2) ROUNDING.—

(A) IN GENERAL.—If any dollar amount in subsection (b)(2)(A) (after being increased under subparagraph (B) thereof), after being increased under paragraph (1), is not a multiple of \$10, such dollar amount shall be rounded to the nearest multiple of \$10.

(B) DISQUALIFIED INCOME THRESHOLD AMOUNT.—If the dollar amount in subsection (i)(1), after being increased under paragraph (1), is not a multiple of \$50, such amount shall be rounded to the next lowest multiple of \$50.

## (k) RESTRICTIONS ON TAXPAYERS WHO IMPROPERLY CLAIMED CREDIT IN PRIOR YEAR.—

## (1) TAXPAYERS MAKING PRIOR FRAUDULENT OR RECKLESS CLAIMS.—

(A) IN GENERAL.—No credit shall be allowed under this section for any taxable year in the disallowance period.

(B) DISALLOWANCE PERIOD.—For purposes of paragraph (1), the disallowance period is—

(i) the period of 10 taxable years after the most recent taxable year for which there was a final determination that the taxpayer's claim of credit under this section was due to fraud, and

(ii) the period of 2 taxable years after the most recent taxable year for which there was a final determination that the taxpayer's claim of credit under this section was due to reckless or intentional disregard of rules and regulations (but not due to fraud).

(2) TAXPAYERS MAKING IMPROPER PRIOR CLAIMS.—In the case of a taxpayer who is denied credit under this section for any taxable year as a result of the deficiency procedures under subchapter B of chapter 63, no credit shall be allowed under this section for any subsequent taxable year unless the taxpayer provides such information as the Secretary may require to demonstrate eligibility for such credit.

## (l) COORDINATION WITH CERTAIN MEANS-TESTED PROGRAMS.—For purposes of—

(1) the United States Housing Act of 1937,

(2) title V of the Housing Act of 1949,

(3) section 101 of the Housing and Urban Development Act of 1965,

(4) sections 221(d)(3), 235, and 236 of the National Housing Act, and

(5) the Food and Nutrition Act of 2008, any refund made to an individual (or the spouse of an individual) by reason of this section shall not be treated as income (and shall not be taken into account in determining resources for the month of its receipt and the following month).

(m) IDENTIFICATION NUMBERS.—Solely for purposes of subsections (c)(1)(E) and (c)(3)(D), a taxpayer identification number means a social security number issued to an individual by the Social Security Administration (other than a social security number issued pursuant to clause (II) (or that portion of clause (III) that relates to clause (II)) of section 205(c)(2)(B)(i) of the Social Security Act) on or before the due date for filing the return for the taxable year.

\* \* \* \* \*

**SEC. 35. HEALTH INSURANCE COSTS OF ELIGIBLE INDIVIDUALS.**

(a) **IN GENERAL.**—In the case of an individual, there shall be allowed as a credit against the tax imposed by subtitle A an amount equal to 72.5 percent of the amount paid by the taxpayer for coverage of the taxpayer and qualifying family members under qualified health insurance for eligible coverage months beginning in the taxable year.

(b) **ELIGIBLE COVERAGE MONTH.**—For purposes of this section—

(1) **IN GENERAL.**—The term “eligible coverage month” means any month if—

(A) as of the first day of such month, the taxpayer—

- (i) is an eligible individual,
- (ii) is covered by qualified health insurance, the premium for which is paid by the taxpayer,
- (iii) does not have other specified coverage, and
- (iv) is not imprisoned under Federal, State, or local authority, and

(B) such month begins more than 90 days after the date of the enactment of the Trade Act of 2002, and before January 1, 2020.

(2) **JOINT RETURNS.**—In the case of a joint return, the requirements of paragraph (1)(A) shall be treated as met with respect to any month if at least 1 spouse satisfies such requirements.

(c) **ELIGIBLE INDIVIDUAL.**—For purposes of this section—

(1) **IN GENERAL.**—The term “eligible individual” means—

- (A) an eligible TAA recipient,
- (B) an eligible alternative TAA recipient, and
- (C) an eligible PBGC pension recipient.

(2) **ELIGIBLE TAA RECIPIENT.**—

(A) **IN GENERAL.**—Except as provided in subparagraph (B), the term “eligible TAA recipient” means, with respect to any month, any individual who is receiving for any day of such month a trade readjustment allowance under chapter 2 of title II of the Trade Act of 1974 or who would be eligible to receive such allowance if section 231 of such Act were applied without regard to subsection (a)(3)(B) of such section. An individual shall continue to be treated as an eligible TAA recipient during the first month that such individual would otherwise cease to be an eligible TAA recipient by reason of the preceding sentence.

(B) **SPECIAL RULE.**—In the case of any eligible coverage month beginning after the date of the enactment of this paragraph, the term “eligible TAA recipient” means, with respect to any month, any individual who—

(i) is receiving for any day of such month a trade readjustment allowance under chapter 2 of title II of the Trade Act of 1974,

(ii) would be eligible to receive such allowance except that such individual is in a break in training provided under a training program approved under section 236 of such Act that exceeds the period specified in section 233(e) of such Act, but is within the period for receiving such allowances provided under section 233(a) of such Act, or

(iii) is receiving unemployment compensation (as defined in section 85(b)) for any day of such month and who would be eligible to receive such allowance for such month if section 231 of such Act were applied without regard to subsections (a)(3)(B) and (a)(5) thereof.

An individual shall continue to be treated as an eligible TAA recipient during the first month that such individual would otherwise cease to be an eligible TAA recipient by reason of the preceding sentence.

(3) ELIGIBLE ALTERNATIVE TAA RECIPIENT.—The term “eligible alternative TAA recipient” means, with respect to any month, any individual who—

(A) is a worker described in section 246(a)(3)(B) of the Trade Act of 1974 who is participating in the program established under section 246(a)(1) of such Act, and

(B) is receiving a benefit for such month under section 246(a)(2) of such Act.

An individual shall continue to be treated as an eligible alternative TAA recipient during the first month that such individual would otherwise cease to be an eligible alternative TAA recipient by reason of the preceding sentence.

(4) ELIGIBLE PBGC PENSION RECIPIENT.—The term “eligible PBGC pension recipient” means, with respect to any month, any individual who—

(A) has attained age 55 as of the first day of such month, and

(B) is receiving a benefit for such month any portion of which is paid by the Pension Benefit Guaranty Corporation under title IV of the Employee Retirement Income Security Act of 1974.

(d) QUALIFYING FAMILY MEMBER.—For purposes of this section—

(1) IN GENERAL.—The term “qualifying family member” means—

(A) the taxpayer’s spouse, and

(B) any dependent of the taxpayer [with respect to whom the taxpayer is entitled to a deduction under section 151(c)] *if the taxpayer included such person’s TIN on the return of tax for the taxable year.*

Such term does not include any individual who has other specified coverage.

(2) SPECIAL DEPENDENCY TEST IN CASE OF DIVORCED PARENTS, ETC.—If [section 152(e)] *section 7706(e)* applies to any child with respect to any calendar year, in the case of any taxable year beginning in such calendar year, such child shall be treated as described in paragraph (1)(B) with respect to the custodial parent (as defined in [section 152(e)(4)(A)] *section 7706(e)(4)(A)*) and not with respect to the noncustodial parent.

(e) QUALIFIED HEALTH INSURANCE.—For purposes of this section—

(1) IN GENERAL.—The term “qualified health insurance” means any of the following:

(A) Coverage under a COBRA continuation provision (as defined in section 9832(d)(1)).

(B) State-based continuation coverage provided by the State under a State law that requires such coverage.

(C) Coverage offered through a qualified State high risk pool (as defined in section 2744(c)(2) of the Public Health Service Act).

(D) Coverage under a health insurance program offered for State employees.

(E) Coverage under a State-based health insurance program that is comparable to the health insurance program offered for State employees.

(F) Coverage through an arrangement entered into by a State and—

(i) a group health plan (including such a plan which is a multiemployer plan as defined in section 3(37) of the Employee Retirement Income Security Act of 1974),

(ii) an issuer of health insurance coverage,

(iii) an administrator, or

(iv) an employer.

(G) Coverage offered through a State arrangement with a private sector health care coverage purchasing pool.

(H) Coverage under a State-operated health plan that does not receive any Federal financial participation.

(I) Coverage under a group health plan that is available through the employment of the eligible individual's spouse.

(J) In the case of any eligible individual and such individual's qualifying family members, coverage under individual health insurance (other than coverage enrolled in through an Exchange established under the Patient Protection and Affordable Care Act). For purposes of this subparagraph, the term "individual health insurance" means any insurance which constitutes medical care offered to individuals other than in connection with a group health plan and does not include Federal- or State-based health insurance coverage.

(K) Coverage under an employee benefit plan funded by a voluntary employees' beneficiary association (as defined in section 501(c)(9)) established pursuant to an order of a bankruptcy court, or by agreement with an authorized representative, as provided in section 1114 of title 11, United States Code.

(2) REQUIREMENTS FOR STATE-BASED COVERAGE.—

(A) IN GENERAL.—The term "qualified health insurance" does not include any coverage described in subparagraphs (B) through (H) of paragraph (1) unless the State involved has elected to have such coverage treated as qualified health insurance under this section and such coverage meets the following requirements:

(i) GUARANTEED ISSUE.—Each qualifying individual is guaranteed enrollment if the individual pays the premium for enrollment or provides a qualified health insurance costs credit eligibility certificate described in section 7527 and pays the remainder of such premium.

(ii) **NO IMPOSITION OF PREEXISTING CONDITION EXCLUSION.**—No pre-existing condition limitations are imposed with respect to any qualifying individual.

(iii) **NONDISCRIMINATORY PREMIUM.**—The total premium (as determined without regard to any subsidies) with respect to a qualifying individual may not be greater than the total premium (as so determined) for a similarly situated individual who is not a qualifying individual.

(iv) **SAME BENEFITS.**—Benefits under the coverage are the same as (or substantially similar to) the benefits provided to similarly situated individuals who are not qualifying individuals.

(B) **QUALIFYING INDIVIDUAL.**—For purposes of this paragraph, the term “qualifying individual” means—

(i) an eligible individual for whom, as of the date on which the individual seeks to enroll in the coverage described in subparagraphs (B) through (H) of paragraph (1), the aggregate of the periods of creditable coverage (as defined in section 9801(c)) is 3 months or longer and who, with respect to any month, meets the requirements of clauses (iii) and (iv) of subsection (b)(1)(A); and

(ii) the qualifying family members of such eligible individual.

(3) **EXCEPTION.**—The term “qualified health insurance” shall not include—

(A) a flexible spending or similar arrangement, and

(B) any insurance if substantially all of its coverage is of excepted benefits described in section 9832(c).

(f) **OTHER SPECIFIED COVERAGE.**—For purposes of this section, an individual has other specified coverage for any month if, as of the first day of such month—

(1) **SUBSIDIZED COVERAGE.**—

(A) **IN GENERAL.**—Such individual is covered under any insurance which constitutes medical care (except insurance substantially all of the coverage of which is of excepted benefits described in section 9832(c)) under any health plan maintained by any employer (or former employer) of the taxpayer or the taxpayer’s spouse and at least 50 percent of the cost of such coverage (determined under section 4980B) is paid or incurred by the employer.

(B) **ELIGIBLE ALTERNATIVE TAA RECIPIENTS.**—In the case of an eligible alternative TAA recipient, such individual is either—

(i) eligible for coverage under any qualified health insurance (other than insurance described in subparagraph (A), (B), or (F) of subsection (e)(1)) under which at least 50 percent of the cost of coverage (determined under section 4980B(f)(4)) is paid or incurred by an employer (or former employer) of the taxpayer or the taxpayer’s spouse, or

(ii) covered under any such qualified health insurance under which any portion of the cost of coverage (as so determined) is paid or incurred by an employer

(or former employer) of the taxpayer or the taxpayer's spouse.

(C) TREATMENT OF CAFETERIA PLANS.—For purposes of subparagraphs (A) and (B), the cost of coverage shall be treated as paid or incurred by an employer to the extent the coverage is in lieu of a right to receive cash or other qualified benefits under a cafeteria plan (as defined in section 125(d)).

(2) COVERAGE UNDER MEDICARE, MEDICAID, OR SCHIP.—Such individual—

(A) is entitled to benefits under part A of title XVIII of the Social Security Act or is enrolled under part B of such title, or

(B) is enrolled in the program under title XIX or XXI of such Act (other than under section 1928 of such Act).

(3) CERTAIN OTHER COVERAGE.—Such individual—

(A) is enrolled in a health benefits plan under chapter 89 of title 5, United States Code, or

(B) is entitled to receive benefits under chapter 55 of title 10, United States Code.

(g) SPECIAL RULES.—

(1) COORDINATION WITH ADVANCE PAYMENTS OF CREDIT.—With respect to any taxable year, the amount which would (but for this subsection) be allowed as a credit to the taxpayer under subsection (a) shall be reduced (but not below zero) by the aggregate amount paid on behalf of such taxpayer under section 7527 for months beginning in such taxable year.

(2) COORDINATION WITH OTHER DEDUCTIONS.—Amounts taken into account under subsection (a) shall not be taken into account in determining any deduction allowed under section 162(l) or 213.

(3) MEDICAL AND HEALTH SAVINGS ACCOUNTS.—Amounts distributed from an Archer MSA (as defined in section 220(d)) or from a health savings account (as defined in section 223(d)) shall not be taken into account under subsection (a).

(4) DENIAL OF CREDIT TO DEPENDENTS.—No credit shall be allowed under this section to any individual with respect to whom a deduction under section 151 is allowable to another taxpayer for a taxable year beginning in the calendar year in which such individual's taxable year begins.

(5) BOTH SPOUSES ELIGIBLE INDIVIDUALS.—The spouse of the taxpayer shall not be treated as a qualifying family member for purposes of subsection (a), if—

(A) the taxpayer is married at the close of the taxable year,

(B) the taxpayer and the taxpayer's spouse are both eligible individuals during the taxable year, and

(C) the taxpayer files a separate return for the taxable year.

(6) MARITAL STATUS; CERTAIN MARRIED INDIVIDUALS LIVING APART.—Rules similar to the rules of paragraphs (3) and (4) of section 21(e) shall apply for purposes of this section.

(7) INSURANCE WHICH COVERS OTHER INDIVIDUALS.—For purposes of this section, rules similar to the rules of section 213(d)(6) shall apply with respect to any contract for qualified

health insurance under which amounts are payable for coverage of an individual other than the taxpayer and qualifying family members.

(8) TREATMENT OF PAYMENTS.—For purposes of this section—

(A) PAYMENTS BY SECRETARY.—Payments made by the Secretary on behalf of any individual under section 7527 (relating to advance payment of credit for health insurance costs of eligible individuals) shall be treated as having been made by the taxpayer on the first day of the month for which such payment was made.

(B) PAYMENTS BY TAXPAYER.—Payments made by the taxpayer for eligible coverage months shall be treated as having been made by the taxpayer on the first day of the month for which such payment was made.

(9) COBRA PREMIUM ASSISTANCE.—In the case of an assistance eligible individual who receives premium reduction for COBRA continuation coverage under section 3001(a) of title III of division B of the American Recovery and Reinvestment Act of 2009 for any month during the taxable year, such individual shall not be treated as an eligible individual, a certified individual, or a qualifying family member for purposes of this section or section 7527 with respect to such month.

(10) CONTINUED QUALIFICATION OF FAMILY MEMBERS AFTER CERTAIN EVENTS.—

(A) MEDICARE ELIGIBILITY.—In the case of any month which would be an eligible coverage month with respect to an eligible individual but for subsection (f)(2)(A), such month shall be treated as an eligible coverage month with respect to such eligible individual solely for purposes of determining the amount of the credit under this section with respect to any qualifying family members of such individual (and any advance payment of such credit under section 7527). This subparagraph shall only apply with respect to the first 24 months after such eligible individual is first entitled to the benefits described in subsection (f)(2)(A).

(B) DIVORCE.—In the case of the finalization of a divorce between an eligible individual and such individual's spouse, such spouse shall be treated as an eligible individual for purposes of this section and section 7527 for a period of 24 months beginning with the date of such finalization, except that the only qualifying family members who may be taken into account with respect to such spouse are those individuals who were qualifying family members immediately before such finalization.

(C) DEATH.—In the case of the death of an eligible individual—

(i) any spouse of such individual (determined at the time of such death) shall be treated as an eligible individual for purposes of this section and section 7527 for a period of 24 months beginning with the date of such death, except that the only qualifying family members who may be taken into account with respect to such spouse are those individuals who were qualifying family members immediately before such death, and



(ii) any individual who was a qualifying family member of the decedent immediately before such death (or, in the case of an individual to whom paragraph (4) applies, the taxpayer to whom the deduction under section 151 is allowable) shall be treated as an eligible individual for purposes of this section and section 7527 for a period of 24 months beginning with the date of such death, except that in determining the amount of such credit only such qualifying family member may be taken into account.

(11) ELECTION.—

(A) IN GENERAL.—This section shall not apply to any taxpayer for any eligible coverage month unless such taxpayer elects the application of this section for such month.

(B) TIMING AND APPLICABILITY OF ELECTION.—Except as the Secretary may provide—

(i) an election to have this section apply for any eligible coverage month in a taxable year shall be made not later than the due date (including extensions) for the return of tax for the taxable year; and

(ii) any election for this section to apply for an eligible coverage month shall apply for all subsequent eligible coverage months in the taxable year and, once made, shall be irrevocable with respect to such months.

(12) COORDINATION WITH PREMIUM TAX CREDIT.—

(A) IN GENERAL.—An eligible coverage month to which the election under paragraph (11) applies shall not be treated as a coverage month (as defined in section 36B(c)(2)) for purposes of section 36B with respect to the taxpayer.

(B) COORDINATION WITH ADVANCE PAYMENTS OF PREMIUM TAX CREDIT.—In the case of a taxpayer who makes the election under paragraph (11) with respect to any eligible coverage month in a taxable year or on behalf of whom any advance payment is made under section 7527 with respect to any month in such taxable year—

(i) the tax imposed by this chapter for the taxable year shall be increased by the excess, if any, of—

(I) the sum of any advance payments made on behalf of the taxpayer under section 1412 of the Patient Protection and Affordable Care Act and section 7527 for months during such taxable year, over

(II) the sum of the credits allowed under this section (determined without regard to paragraph (1)) and section 36B (determined without regard to subsection (f)(1) thereof) for such taxable year; and

(ii) section 36B(f)(2) shall not apply with respect to such taxpayer for such taxable year, except that if such taxpayer received any advance payments under section 7527 for any month in such taxable year and is later allowed a credit under section 36B for such taxable year, then section 36B(f)(2)(B) shall be applied

by substituting the amount determined under clause (i) for the amount determined under section 36B(f)(2)(A).

(13) REGULATIONS.—The Secretary may prescribe such regulations and other guidance as may be necessary or appropriate to carry out this section, section 6050T, and section 7527.

\* \* \* \* \*

**SEC. 36B. REFUNDABLE CREDIT FOR COVERAGE UNDER A QUALIFIED HEALTH PLAN.**

(a) IN GENERAL.—In the case of an applicable taxpayer, there shall be allowed as a credit against the tax imposed by this subtitle for any taxable year an amount equal to the premium assistance credit amount of the taxpayer for the taxable year.

(b) PREMIUM ASSISTANCE CREDIT AMOUNT.—For purposes of this section—

(1) IN GENERAL.—The term “premium assistance credit amount” means, with respect to any taxable year, the sum of the premium assistance amounts determined under paragraph (2) with respect to all coverage months of the taxpayer occurring during the taxable year.

(2) PREMIUM ASSISTANCE AMOUNT.—The premium assistance amount determined under this subsection with respect to any coverage month is the amount equal to the lesser of—

(A) the monthly premiums for such month for 1 or more qualified health plans offered in the individual market within a State which cover the taxpayer, the taxpayer’s spouse, or any dependent (as defined in [section 152] section 7706) of the taxpayer and which were enrolled in through an Exchange established by the State under 1311 of the Patient Protection and Affordable Care Act, or

(B) the excess (if any) of—

(i) the adjusted monthly premium for such month for the applicable second lowest cost silver plan with respect to the taxpayer, over

(ii) an amount equal to 1/12 of the product of the applicable percentage and the taxpayer’s household income for the taxable year.

(3) OTHER TERMS AND RULES RELATING TO PREMIUM ASSISTANCE AMOUNTS.—For purposes of paragraph (2)—

(A) APPLICABLE PERCENTAGE.—

(i) IN GENERAL.—Except as provided in clause (ii), the applicable percentage for any taxable year shall be the percentage such that the applicable percentage for any taxpayer whose household income is within an income tier specified in the following table shall increase, on a sliding scale in a linear manner, from the initial premium percentage to the final premium percentage specified in such table for such income tier:

| In the case of household income (expressed as a percent of poverty line) within the following income tier: | The initial premium percentage is-- | The final premium percentage is-- |
|--|-------------------------------------|-----------------------------------|
| Up to 133%   | 2.0%                                | 2.0%                              |

| In the case of household income (expressed as a percent of poverty line) within the following income tier: | The initial premium percentage is-- | The final premium percentage is-- |
|--|-------------------------------------|-----------------------------------|
| 133% up to 150%  | 3.0%                                | 4.0%                              |
| 150% up to 200%  | 4.0%                                | 6.3%                              |
| 200% up to 250%  | 6.3%                                | 8.05%                             |
| 250% up to 300%  | 8.05%                               | 9.5%                              |
| 300% up to 400%  | 9.5%                                | 9.5%                              |

## (ii) INDEXING.—

(I) IN GENERAL.—Subject to subclause (II), in the case of taxable years beginning in any calendar year after 2014, the initial and final applicable percentages under clause (i) (as in effect for the preceding calendar year after application of this clause) shall be adjusted to reflect the excess of the rate of premium growth for the preceding calendar year over the rate of income growth for the preceding calendar year.

(II) ADDITIONAL ADJUSTMENT.—Except as provided in subclause (III), in the case of any calendar year after 2018, the percentages described in subclause (I) shall, in addition to the adjustment under subclause (I), be adjusted to reflect the excess (if any) of the rate of premium growth estimated under subclause (I) for the preceding calendar year over the rate of growth in the consumer price index for the preceding calendar year.

(III) FAILSAFE.—Subclause (II) shall apply for any calendar year only if the aggregate amount of premium tax credits under this section and cost-sharing reductions under section 1402 of the Patient Protection and Affordable Care Act for the preceding calendar year exceeds an amount equal to 0.504 percent of the gross domestic product for the preceding calendar year.

(B) APPLICABLE SECOND LOWEST COST SILVER PLAN.—The applicable second lowest cost silver plan with respect to any applicable taxpayer is the second lowest cost silver plan of the individual market in the rating area in which the taxpayer resides which—

(i) is offered through the same Exchange through which the qualified health plans taken into account under paragraph (2)(A) were offered, and

(ii) provides—

(I) self-only coverage in the case of an applicable taxpayer—

(aa) whose tax for the taxable year is determined under section 1(c) (relating to unmarried individuals other than surviving spouses and heads of households) and who is not allowed a deduction under section 151 for the taxable year with respect to a dependent, or

(bb) who is not described in item (aa) but who purchases only self-only coverage, and

(II) family coverage in the case of any other applicable taxpayer.

If a taxpayer files a joint return and no credit is allowed under this section with respect to 1 of the spouses by reason of subsection (e), the taxpayer shall be treated as described in clause (ii)(I) [unless a deduction is allowed under section 151 for the taxable year with respect to a dependent] *unless the taxpayer has a dependent for the taxable year (and the taxpayer included such dependent's TIN on the return of tax for the taxable year)* other than either spouse and subsection (e) does not apply to the dependent.

(C) ADJUSTED MONTHLY PREMIUM.—The adjusted monthly premium for an applicable second lowest cost silver plan is the monthly premium which would have been charged (for the rating area with respect to which the premiums under paragraph (2)(A) were determined) for the plan if each individual covered under a qualified health plan taken into account under paragraph (2)(A) were covered by such silver plan and the premium was adjusted only for the age of each such individual in the manner allowed under section 2701 of the Public Health Service Act. In the case of a State participating in the wellness discount demonstration project under section 2705(d) of the Public Health Service Act, the adjusted monthly premium shall be determined without regard to any premium discount or rebate under such project.

(D) ADDITIONAL BENEFITS.—If—

(i) a qualified health plan under section 1302(b)(5) of the Patient Protection and Affordable Care Act offers benefits in addition to the essential health benefits required to be provided by the plan, or

(ii) a State requires a qualified health plan under section 1311(d)(3)(B) of such Act to cover benefits in addition to the essential health benefits required to be provided by the plan,

the portion of the premium for the plan properly allocable (under rules prescribed by the Secretary of Health and Human Services) to such additional benefits shall not be taken into account in determining either the monthly premium or the adjusted monthly premium under paragraph (2).

(E) SPECIAL RULE FOR PEDIATRIC DENTAL COVERAGE.—For purposes of determining the amount of any monthly premium, if an individual enrolls in both a qualified health plan and a plan described in section 1311(d)(2)(B)(ii) (I) of the Patient Protection and Affordable Care Act for any plan year, the portion of the premium for the plan described in such section that (under regulations prescribed by the Secretary) is properly allocable to pediatric dental benefits which are included in the essential health benefits required to be provided by a qualified health plan under section 1302(b)(1)(J) of such Act shall be treated as a premium payable for a qualified health plan.

(c) DEFINITION AND RULES RELATING TO APPLICABLE TAXPAYERS, COVERAGE MONTHS, AND QUALIFIED HEALTH PLAN.—For purposes of this section—

(1) APPLICABLE TAXPAYER.—

(A) IN GENERAL.—The term “applicable taxpayer” means, with respect to any taxable year, a taxpayer whose household income for the taxable year equals or exceeds 100 percent but does not exceed 400 percent of an amount equal to the poverty line for a family of the size involved.

(B) SPECIAL RULE FOR CERTAIN INDIVIDUALS LAWFULLY PRESENT IN THE UNITED STATES.—If—

(i) a taxpayer has a household income which is not greater than 100 percent of an amount equal to the poverty line for a family of the size involved, and

(ii) the taxpayer is an alien lawfully present in the United States, but is not eligible for the medicaid program under title XIX of the Social Security Act by reason of such alien status,

the taxpayer shall, for purposes of the credit under this section, be treated as an applicable taxpayer with a household income which is equal to 100 percent of the poverty line for a family of the size involved.

(C) MARRIED COUPLES MUST FILE JOINT RETURN.—If the taxpayer is married (within the meaning of section 7703) at the close of the taxable year, the taxpayer shall be treated as an applicable taxpayer only if the taxpayer and the taxpayer’s spouse file a joint return for the taxable year.

(D) DENIAL OF CREDIT TO DEPENDENTS.—No credit shall be allowed under this section to any individual [with respect to whom a deduction under section 151 is allowable to another taxpayer] *who is a dependent of another taxpayer* for a taxable year beginning in the calendar year in which such individual’s taxable year begins.

(2) COVERAGE MONTH.—For purposes of this subsection—

(A) IN GENERAL.—The term “coverage month” means, with respect to an applicable taxpayer, any month if—

(i) as of the first day of such month the taxpayer, the taxpayer’s spouse, or any dependent of the taxpayer is covered by a qualified health plan described in subsection (b)(2)(A) that was enrolled in through an Exchange established by the State under section 1311 of the Patient Protection and Affordable Care Act, and

(ii) the premium for coverage under such plan for such month is paid by the taxpayer (or through advance payment of the credit under subsection (a) under section 1412 of the Patient Protection and Affordable Care Act).

(B) EXCEPTION FOR MINIMUM ESSENTIAL COVERAGE.—

(i) IN GENERAL.—The term “coverage month” shall not include any month with respect to an individual if for such month the individual is eligible for minimum essential coverage other than eligibility for coverage described in section 5000A(f)(1)(C) (relating to coverage in the individual market).

(ii) **MINIMUM ESSENTIAL COVERAGE.**—The term “minimum essential coverage” has the meaning given such term by section 5000A(f).

(C) **SPECIAL RULE FOR EMPLOYER-SPONSORED MINIMUM ESSENTIAL COVERAGE.**—For purposes of subparagraph (B)—

(i) **COVERAGE MUST BE AFFORDABLE.**—Except as provided in clause (iii), an employee shall not be treated as eligible for minimum essential coverage if such coverage—

(I) consists of an eligible employer-sponsored plan (as defined in section 5000A(f)(2)), and

(II) the employee’s required contribution (within the meaning of section 5000A(e)(1)(B)) with respect to the plan exceeds 9.5 percent of the applicable taxpayer’s household income.

This clause shall also apply to an individual who is eligible to enroll in the plan by reason of a relationship the individual bears to the employee.

(ii) **COVERAGE MUST PROVIDE MINIMUM VALUE.**—Except as provided in clause (iii), an employee shall not be treated as eligible for minimum essential coverage if such coverage consists of an eligible employer-sponsored plan (as defined in section 5000A(f)(2)) and the plan’s share of the total allowed costs of benefits provided under the plan is less than 60 percent of such costs.

(iii) **EMPLOYEE OR FAMILY MUST NOT BE COVERED UNDER EMPLOYER PLAN.**—Clauses (i) and (ii) shall not apply if the employee (or any individual described in the last sentence of clause (i)) is covered under the eligible employer-sponsored plan or the grandfathered health plan.

(iv) **INDEXING.**—In the case of plan years beginning in any calendar year after 2014, the Secretary shall adjust the 9.5 percent under clause (i)(II) in the same manner as the percentages are adjusted under subsection (b)(3)(A)(ii).

(3) **DEFINITIONS AND OTHER RULES.**—

(A) **QUALIFIED HEALTH PLAN.**—The term “qualified health plan” has the meaning given such term by section 1301(a) of the Patient Protection and Affordable Care Act, except that such term shall not include a qualified health plan which is a catastrophic plan described in section 1302(e) of such Act.

(B) **GRANDFATHERED HEALTH PLAN.**—The term “grandfathered health plan” has the meaning given such term by section 1251 of the Patient Protection and Affordable Care Act.

(4) **SPECIAL RULES FOR QUALIFIED SMALL EMPLOYER HEALTH REIMBURSEMENT ARRANGEMENTS.**—

(A) **IN GENERAL.**—The term “coverage month” shall not include any month with respect to an employee (or any spouse or dependent of such employee) if for such month the employee is provided a qualified small employer health

reimbursement arrangement which constitutes affordable coverage.

(B) DENIAL OF DOUBLE BENEFIT.—In the case of any employee who is provided a qualified small employer health reimbursement arrangement for any coverage month (determined without regard to subparagraph (A)), the credit otherwise allowable under subsection (a) to the taxpayer for such month shall be reduced (but not below zero) by the amount described in subparagraph (C)(i)(II) for such month.

(C) AFFORDABLE COVERAGE.—For purposes of subparagraph (A), a qualified small employer health reimbursement arrangement shall be treated as constituting affordable coverage for a month if—

(i) the excess of—

(I) the amount that would be paid by the employee as the premium for such month for self-only coverage under the second lowest cost silver plan offered in the relevant individual health insurance market, over

(II)  $\frac{1}{12}$  of the employee's permitted benefit (as defined in section 9831(d)(3)(C)) under such arrangement, does not exceed—

(ii)  $\frac{1}{12}$  of 9.5 percent of the employee's household income.

(D) QUALIFIED SMALL EMPLOYER HEALTH REIMBURSEMENT ARRANGEMENT.—For purposes of this paragraph, the term “qualified small employer health reimbursement arrangement” has the meaning given such term by section 9831(d)(2).

(E) COVERAGE FOR LESS THAN ENTIRE YEAR.—In the case of an employee who is provided a qualified small employer health reimbursement arrangement for less than an entire year, subparagraph (C)(i)(II) shall be applied by substituting “the number of months during the year for which such arrangement was provided” for “12”.

(F) INDEXING.—In the case of plan years beginning in any calendar year after 2014, the Secretary shall adjust the 9.5 percent amount under subparagraph (C)(ii) in the same manner as the percentages are adjusted under subsection (b)(3)(A)(ii).

(d) TERMS RELATING TO INCOME AND FAMILIES.—For purposes of this section—

(1) FAMILY SIZE.—The family size involved with respect to any taxpayer shall be [equal to the number of individuals for whom the taxpayer is allowed a deduction under section 151 (relating to allowance of deduction for personal exemptions) for the taxable year] *the sum of 1 (2 in the case of a joint return) plus the number of individuals who are dependents of the taxpayer for the taxable year.*

(2) HOUSEHOLD INCOME.—

(A) HOUSEHOLD INCOME.—The term “household income” means, with respect to any taxpayer, an amount equal to the sum of—

(i) the modified adjusted gross income of the taxpayer, plus

(ii) the aggregate modified adjusted gross incomes of all other individuals who—

(I) were taken into account in determining the taxpayer's family size under paragraph (1), and

(II) were required to file a return of tax imposed by section 1 for the taxable year.

(B) MODIFIED ADJUSTED GROSS INCOME.—The term “modified adjusted gross income” means adjusted gross income increased by—

(i) any amount excluded from gross income under section 911,

(ii) any amount of interest received or accrued by the taxpayer during the taxable year which is exempt from tax, and

(iii) an amount equal to the portion of the taxpayer's social security benefits (as defined in section 86(d)) which is not included in gross income under section 86 for the taxable year.

(3) POVERTY LINE.—

(A) IN GENERAL.—The term “poverty line” has the meaning given that term in section 2110(c)(5) of the Social Security Act (42 U.S.C. 1397jj(c)(5)).

(B) POVERTY LINE USED.—In the case of any qualified health plan offered through an Exchange for coverage during a taxable year beginning in a calendar year, the poverty line used shall be the most recently published poverty line as of the 1st day of the regular enrollment period for coverage during such calendar year.

(e) RULES FOR INDIVIDUALS NOT LAWFULLY PRESENT.—

(1) IN GENERAL.—If **1 or more individuals for whom a taxpayer is allowed a deduction under section 151 (relating to allowance of deduction for personal exemptions) for the taxable year (including the taxpayer or his spouse)** *1 or more of the taxpayer, the taxpayer's spouse, or any dependent of the taxpayer* are individuals who are not lawfully present—

(A) the aggregate amount of premiums otherwise taken into account under clauses (i) and (ii) of subsection (b)(2)(A) shall be reduced by the portion (if any) of such premiums which is attributable to such individuals, and

(B) for purposes of applying this section, the determination as to what percentage a taxpayer's household income bears to the poverty level for a family of the size involved shall be made under one of the following methods:

(i) A method under which—

(I) the taxpayer's family size is determined by not taking such individuals into account, and

(II) the taxpayer's household income is equal to the product of the taxpayer's household income (determined without regard to this subsection) and a fraction—

(aa) the numerator of which is the poverty line for the taxpayer's family size determined after application of subclause (I), and



(bb) the denominator of which is the poverty line for the taxpayer's family size determined without regard to subclause (I).

(ii) A comparable method reaching the same result as the method under clause (i).

(2) **LAWFULLY PRESENT.**—For purposes of this section, an individual shall be treated as lawfully present only if the individual is, and is reasonably expected to be for the entire period of enrollment for which the credit under this section is being claimed, a citizen or national of the United States or an alien lawfully present in the United States.

(3) **SECRETARIAL AUTHORITY.**—The Secretary of Health and Human Services, in consultation with the Secretary, shall prescribe rules setting forth the methods by which calculations of family size and household income are made for purposes of this subsection. Such rules shall be designed to ensure that the least burden is placed on individuals enrolling in qualified health plans through an Exchange and taxpayers eligible for the credit allowable under this section.

(f) **RECONCILIATION OF CREDIT AND ADVANCE CREDIT.**—

(1) **IN GENERAL.**—The amount of the credit allowed under this section for any taxable year shall be reduced (but not below zero) by the amount of any advance payment of such credit under section 1412 of the Patient Protection and Affordable Care Act.

(2) **EXCESS ADVANCE PAYMENTS.**—

(A) **IN GENERAL.**—If the advance payments to a taxpayer under section 1412 of the Patient Protection and Affordable Care Act for a taxable year exceed the credit allowed by this section (determined without regard to paragraph (1)), the tax imposed by this chapter for the taxable year shall be increased by the amount of such excess.

(B) **LIMITATION ON INCREASE.**—

(i) **IN GENERAL.**—In the case of a taxpayer whose household income is less than 400 percent of the poverty line for the size of the family involved for the taxable year, the amount of the increase under subparagraph (A) shall in no event exceed the applicable dollar amount determined in accordance with the following table (one-half of such amount in the case of a taxpayer whose tax is determined under section 1(c) for the taxable year):

| If the household income (expressed as a percent of poverty line) is: | The applicable dollar amount is: |
|--|----------------------------------|
| Less than 200%   | \$600                            |
| At least 200% but less than 300%                                     | \$1,500                          |
| At least 300% but less than 400%                                     | \$2,500                          |

(ii) **INDEXING OF AMOUNT.**—In the case of any calendar year beginning after 2014, each of the dollar amounts in the table contained under clause (i) shall be increased by an amount equal to—

(I) such dollar amount, multiplied by

(II) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year, determined by substituting “calendar year 2013” for “calendar year 2016” in subparagraph (A)(ii) thereof.

If the amount of any increase under clause (i) is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.

(3) INFORMATION REQUIREMENT.—Each Exchange (or any person carrying out 1 or more responsibilities of an Exchange under section 1311(f)(3) or 1321(c) of the Patient Protection and Affordable Care Act) shall provide the following information to the Secretary and to the taxpayer with respect to any health plan provided through the Exchange:

(A) The level of coverage described in section 1302(d) of the Patient Protection and Affordable Care Act and the period such coverage was in effect.

(B) The total premium for the coverage without regard to the credit under this section or cost-sharing reductions under section 1402 of such Act.

(C) The aggregate amount of any advance payment of such credit or reductions under section 1412 of such Act.

(D) The name, address, and TIN of the primary insured and the name and TIN of each other individual obtaining coverage under the policy.

(E) Any information provided to the Exchange, including any change of circumstances, necessary to determine eligibility for, and the amount of, such credit.

(F) Information necessary to determine whether a taxpayer has received excess advance payments.

(g) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this section, including regulations which provide for—

(1) the coordination of the credit allowed under this section with the program for advance payment of the credit under section 1412 of the Patient Protection and Affordable Care Act, and

(2) the application of subsection (f) where the filing status of the taxpayer for a taxable year is different from such status used for determining the advance payment of the credit.

\* \* \* \* \*

**Subpart D—Business Related Credits**

\* \* \* \* \*

**SEC. 42. LOW-INCOME HOUSING CREDIT.**

(a) IN GENERAL.—For purposes of section 38, the amount of the low-income housing credit determined under this section for any taxable year in the credit period shall be an amount equal to—

(1) the applicable percentage of

(2) the qualified basis of each qualified low-income building.

(b) APPLICABLE PERCENTAGE: 70 PERCENT PRESENT VALUE CREDIT FOR CERTAIN NEW BUILDINGS; 30 PERCENT PRESENT VALUE CREDIT FOR CERTAIN OTHER BUILDINGS.—

(1) DETERMINATION OF APPLICABLE PERCENTAGE.—For purposes of this section—

(A) IN GENERAL.—The term “applicable percentage” means, with respect to any building, the appropriate percentage prescribed by the Secretary for the earlier of—

(i) the month in which such building is placed in service, or

(ii) at the election of the taxpayer—

(I) the month in which the taxpayer and the housing credit agency enter into an agreement with respect to such building (which is binding on such agency, the taxpayer, and all successors in interest) as to the housing credit dollar amount to be allocated to such building, or

(II) in the case of any building to which subsection (h)(4)(B) applies, the month in which the tax-exempt obligations are issued.

A month may be elected under clause (ii) only if the election is made not later than the 5th day after the close of such month. Such an election, once made, shall be irrevocable.

(B) METHOD OF PRESCRIBING PERCENTAGES.—The percentages prescribed by the Secretary for any month shall be percentages which will yield over a 10-year period amounts of credit under subsection (a) which have a present value equal to—

(i) 70 percent of the qualified basis of a new building which is not federally subsidized for the taxable year, and

(ii) 30 percent of the qualified basis of a building not described in clause (i).

(C) METHOD OF DISCOUNTING.—The present value under subparagraph (B) shall be determined—

(i) as of the last day of the 1st year of the 10-year period referred to in subparagraph (B),

(ii) by using a discount rate equal to 72 percent of the average of the annual Federal mid-term rate and the annual Federal long-term rate applicable under section 1274(d)(1) to the month applicable under clause (i) or (ii) of subparagraph (A) and compounded annually, and

(iii) by assuming that the credit allowable under this section for any year is received on the last day of such year.

(2) MINIMUM CREDIT RATE FOR NON-FEDERALLY SUBSIDIZED NEW BUILDINGS.—In the case of any new building—

(A) which is placed in service by the taxpayer after the date of the enactment of this paragraph, and

(B) which is not federally subsidized for the taxable year,  
the applicable percentage shall not be less than 9 percent.

(3) CROSS REFERENCES.—

(A) For treatment of certain rehabilitation expenditures as separate new buildings, see subsection (e).

(B) For determination of applicable percentage for increases in qualified basis after the 1st year of the credit period, see subsection (f)(3).

(C) For authority of housing credit agency to limit applicable percentage and qualified basis which may be taken into account under this section with respect to any building, see subsection (h)(7).

(c) **QUALIFIED BASIS; QUALIFIED LOW-INCOME BUILDING.**—For purposes of this section—

(1) **QUALIFIED BASIS.**—

(A) **DETERMINATION.**—The qualified basis of any qualified low-income building for any taxable year is an amount equal to—

(i) the applicable fraction (determined as of the close of such taxable year) of

(ii) the eligible basis of such building (determined under subsection (d)(5)).

(B) **APPLICABLE FRACTION.**—For purposes of subparagraph (A), the term “applicable fraction” means the smaller of the unit fraction or the floor space fraction.

(C) **UNIT FRACTION.**—For purposes of subparagraph (B), the term “unit fraction” means the fraction—

(i) the numerator of which is the number of low-income units in the building, and

(ii) the denominator of which is the number of residential rental units (whether or not occupied) in such building.

(D) **FLOOR SPACE FRACTION.**—For purposes of subparagraph (B), the term “floor space fraction” means the fraction—

(i) the numerator of which is the total floor space of the low-income units in such building, and

(ii) the denominator of which is the total floor space of the residential rental units (whether or not occupied) in such building.

(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).

(2) **QUALIFIED LOW-INCOME BUILDING.**—The term “qualified low-income building” means any building—

(A) which is part of a qualified low-income housing project at all times during the period—

(i) beginning on the 1st day in the compliance period on which such building is part of such a project, and

(ii) ending on the last day of the compliance period with respect to such building, and

- (B) to which the amendments made by section 201(a) of the Tax Reform Act of 1986 apply.
- (d) ELIGIBLE BASIS.—For purposes of this section—
- (1) NEW BUILDINGS.—The eligible basis of a new building is its adjusted basis as of the close of the 1st taxable year of the credit period.
- (2) EXISTING BUILDINGS.—
- (A) IN GENERAL.—The eligible basis of an existing building is—
- (i) in the case of a building which meets the requirements of subparagraph (B), its adjusted basis as of the close of the 1st taxable year of the credit period, and
  - (ii) zero in any other case.
- (B) REQUIREMENTS.—A building meets the requirements of this subparagraph if—
- (i) the building is acquired by purchase (as defined in section 179(d)(2)),
  - (ii) there is a period of at least 10 years between the date of its acquisition by the taxpayer and the date the building was last placed in service,
  - (iii) the building was not previously placed in service by the taxpayer or by any person who was a related person with respect to the taxpayer as of the time previously placed in service, and
  - (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.
- (C) ADJUSTED BASIS.—For purposes of subparagraph (A), the adjusted basis of any building shall not include so much of the basis of such building as is determined by reference to the basis of other property held at any time by the person acquiring the building.
- (D) Special rules for subparagraph (B)
- (i) SPECIAL RULES FOR CERTAIN TRANSFERS.—For purposes of determining under subparagraph (B)(ii) when a building was last placed in service, there shall not be taken into account any placement in service—
    - (I) in connection with the acquisition of the building in a transaction in which the basis of the building in the hands of the person acquiring it is determined in whole or in part by reference to the adjusted basis of such building in the hands of the person from whom acquired,
    - (II) by a person whose basis in such building is determined under section 1014(a) (relating to property acquired from a decedent),
    - (III) by any governmental unit or qualified non-profit organization (as defined in subsection (h)(5)) if the requirements of subparagraph (B)(ii) are met with respect to the placement in service by such unit or organization and all the income from such property is exempt from Federal income taxation,
    - (IV) by any person who acquired such building by foreclosure (or by instrument in lieu of fore-

closure) of any purchase-money security interest held by such person if the requirements of subparagraph (B)(ii) are met with respect to the placement in service by such person and such building is resold within 12 months after the date such building is placed in service by such person after such foreclosure, or

(V) of a single-family residence by any individual who owned and used such residence for no other purpose than as his principal residence.

(ii) RELATED PERSON.—For purposes of subparagraph (B)(iii), a person (hereinafter in this subclause referred to as the “related person”) is related to any person if the related person bears a relationship to such person specified in section 267(b) or 707(b)(1), or the related person and such person are engaged in trades or businesses under common control (within the meaning of subsections (a) and (b) of section 52).

(3) ELIGIBLE BASIS REDUCED WHERE DISPROPORTIONATE STANDARDS FOR UNITS.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the eligible basis of any building shall be reduced by an amount equal to the portion of the adjusted basis of the building which is attributable to residential rental units in the building which are not low-income units and which are above the average quality standard of the low-income units in the building.

(B) EXCEPTION WHERE TAXPAYER ELECTS TO EXCLUDE EXCESS COSTS.—

(i) IN GENERAL.—Subparagraph (A) shall not apply with respect to a residential rental unit in a building which is not a low-income unit if—

(I) the excess described in clause (ii) with respect to such unit is not greater than 15 percent of the cost described in clause (ii)(II), and

(II) the taxpayer elects to exclude from the eligible basis of such building the excess described in clause (ii) with respect to such unit.

(ii) EXCESS.—The excess described in this clause with respect to any unit is the excess of—

(I) the cost of such unit, over

(II) the amount which would be the cost of such unit if the average cost per square foot of low-income units in the building were substituted for the cost per square foot of such unit.

The Secretary may by regulation provide for the determination of the excess under this clause on a basis other than square foot costs.

(4) SPECIAL RULES RELATING TO DETERMINATION OF ADJUSTED BASIS.—For purposes of this subsection—

(A) IN GENERAL.—Except as provided in subparagraphs (B) and (C), the adjusted basis of any building shall be determined without regard to the adjusted basis of any property which is not residential rental property.

(B) BASIS OF PROPERTY IN COMMON AREAS, ETC., INCLUDED.—The adjusted basis of any building shall be determined by taking into account the adjusted basis of property (of a character subject to the allowance for depreciation) used in common areas or provided as comparable amenities to all residential rental units in such building.

(C) INCLUSION OF BASIS OF PROPERTY USED TO PROVIDE SERVICES FOR CERTAIN NONTENANTS.—

(i) IN GENERAL.—The adjusted basis of any building located in a qualified census tract (as defined in paragraph (5)(B)(ii)) shall be determined by taking into account the adjusted basis of property (of a character subject to the allowance for depreciation and not otherwise taken into account) used throughout the taxable year in providing any community service facility.

(ii) LIMITATION.—The increase in the adjusted basis of any building which is taken into account by reason of clause (i) shall not exceed the sum of—

(I) 25 percent of so much of the eligible basis of the qualified low-income housing project of which it is a part as does not exceed \$15,000,000, plus

(II) 10 percent of so much of the eligible basis of such project as is not taken into account under subclause (I).

For purposes of the preceding sentence, all community service facilities which are part of the same qualified low-income housing project shall be treated as one facility.

(iii) COMMUNITY SERVICE FACILITY.—For purposes of this subparagraph, the term “community service facility” means any facility designed to serve primarily individuals whose income is 60 percent or less of area median income (within the meaning of subsection (g)(1)(B)).

(D) NO REDUCTION FOR DEPRECIATION.—The adjusted basis of any building shall be determined without regard to paragraphs (2) and (3) of section 1016(a).

(5) SPECIAL RULES FOR DETERMINING ELIGIBLE BASIS.—

(A) FEDERAL GRANTS NOT TAKEN INTO ACCOUNT IN DETERMINING ELIGIBLE BASIS.—The eligible basis of a building shall not include any costs financed with the proceeds of a federally funded grant.

(B) 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 expend-

itures determined without regard to this subparagraph.

(ii) QUALIFIED CENSUS TRACT.—

(I) IN GENERAL.—The term “qualified census tract” means any census tract which is designated by the Secretary of Housing and Urban Development and, for the most recent year for which census data are available on household income in such tract, either in which 50 percent or more of the households have an income which is less than 60 percent of the area median gross income for such year or which has a poverty rate of at least 25 percent. If the Secretary of Housing and Urban Development determines that sufficient data for any period are not available to apply this clause on the basis of census tracts, such Secretary shall apply this clause for such period on the basis of enumeration districts.

(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 non-metropolitan 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.



(v) BUILDINGS DESIGNATED BY STATE HOUSING CREDIT AGENCY.—Any building which is designated by the State housing credit agency as requiring the increase in credit under this subparagraph in order for such building to be financially feasible as part of a qualified low-income housing project shall be treated for purposes of this subparagraph as located in a difficult development area which is designated for purposes of this subparagraph. The preceding sentence shall not apply to any building if paragraph (1) of subsection (h) does not apply to any portion of the eligible basis of such building by reason of paragraph (4) of such subsection.

(6) Credit allowable for certain buildings acquired during 10-year period described in paragraph (2)(B)(ii)

(A) IN GENERAL.—Paragraph (2)(B)(ii) shall not apply to any federally- or State-assisted building.

(B) BUILDINGS ACQUIRED FROM INSURED DEPOSITORY INSTITUTIONS IN DEFAULT.—On application by the taxpayer, the Secretary may waive paragraph (2)(B)(ii) 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.

(C) FEDERALLY- OR STATE-ASSISTED BUILDING.—For purposes of this paragraph—

(i) FEDERALLY-ASSISTED BUILDING.—The term “federally-assisted building” means any building which is substantially assisted, financed, or operated under section 8 of the United States Housing Act of 1937, section 221(d)(3), 221(d)(4), or 236 of the National Housing Act, section 515 of the Housing Act of 1949, or any other housing program administered by the Department of Housing and Urban Development or by the Rural Housing Service of the Department of Agriculture.

(ii) STATE-ASSISTED BUILDING.—The term “State-assisted building” means any building which is substantially assisted, financed, or operated under any State law similar in purposes to any of the laws referred to in clause (i).

(7) ACQUISITION OF BUILDING BEFORE END OF PRIOR COMPLIANCE PERIOD.—

(A) IN GENERAL.—Under regulations prescribed by the Secretary, in the case of a building described in subparagraph (B) (or interest therein) which is acquired by the taxpayer—

(i) paragraph (2)(B) shall not apply, but

(ii) the credit allowable by reason of subsection (a) to the taxpayer for any period after such acquisition shall be equal to the amount of credit which would have been allowable under subsection (a) for such period to the prior owner referred to in subparagraph (B) had such owner not disposed of the building.

(B) DESCRIPTION OF BUILDING.—A building is described in this subparagraph if—

- (i) a credit was allowed by reason of subsection (a) to any prior owner of such building, and
- (ii) the taxpayer acquired such building before the end of the compliance period for such building with respect to such prior owner (determined without regard to any disposition by such prior owner).

(e) REHABILITATION EXPENDITURES TREATED AS SEPARATE NEW BUILDING.—

(1) IN GENERAL.—Rehabilitation expenditures paid or incurred by the taxpayer with respect to any building shall be treated for purposes of this section as a separate new building.

(2) REHABILITATION EXPENDITURES.—For purposes of paragraph (1)—

(A) IN GENERAL.—The term “rehabilitation expenditures” means amounts chargeable to capital account and incurred for property (or additions or improvements to property) of a character subject to the allowance for depreciation in connection with the rehabilitation of a building.

(B) COST OF ACQUISITION, ETC., NOT INCLUDED.—Such term does not include the cost of acquiring any building (or interest therein) or any amount not permitted to be taken into account under paragraph (3) or (4) of subsection (d).

(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 20 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 \$6,000 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).

(C) DATE OF DETERMINATION.—The determination under subparagraph (A) shall be made as of the close of the 1st taxable year in the credit period with respect to such expenditures.

(D) INFLATION ADJUSTMENT.—In the case of any expenditures which are treated under paragraph (4) as placed in

service during any calendar year after 2009, the \$6,000 amount in subparagraph (A)(ii)(II) shall be increased by an amount equal to—

- (i) such dollar amount, multiplied by
- (ii) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year by substituting “calendar year 2008” for “calendar year 2016” in subparagraph (A)(ii) thereof.

Any increase under the preceding sentence which is not a multiple of \$100 shall be rounded to the nearest multiple of \$100.

(4) SPECIAL RULES.—For purposes of applying this section with respect to expenditures which are treated as a separate building by reason of this subsection—

(A) such expenditures shall be treated as placed in service at the close of the 24-month period referred to in paragraph (3)(A), and

(B) the applicable fraction under subsection (c)(1) shall be the applicable fraction for the building (without regard to paragraph (1)) with respect to which the expenditures were incurred.

Nothing in subsection (d)(2) shall prevent a credit from being allowed by reason of this subsection.

(5) NO DOUBLE COUNTING.—Rehabilitation expenditures may, at the election of the taxpayer, be taken into account under this subsection or subsection (d)(2)(A)(i) but not under both such subsections.

(6) REGULATIONS TO APPLY SUBSECTION WITH RESPECT TO GROUP OF UNITS IN BUILDING.—The Secretary may prescribe regulations, consistent with the purposes of this subsection, treating a group of units with respect to which rehabilitation expenditures are incurred as a separate new building.

(f) DEFINITION AND SPECIAL RULES RELATING TO CREDIT PERIOD.—

(1) CREDIT PERIOD DEFINED.—For purposes of this section, the term “credit period” means, with respect to any building, the period of 10 taxable years beginning with—

(A) the taxable year in which the building is placed in service, or

(B) at the election of the taxpayer, the succeeding taxable year,

but only if the building is a qualified low-income building as of the close of the 1st year of such period. The election under subparagraph (B), once made, shall be irrevocable.

(2) SPECIAL RULE FOR 1ST YEAR OF CREDIT PERIOD.—

(A) IN GENERAL.—The credit allowable under subsection (a) with respect to any building for the 1st taxable year of the credit period shall be determined by substituting for the applicable fraction under subsection (c)(1) the fraction—

- (i) the numerator of which is the sum of the applicable fractions determined under subsection (c)(1) as of the close of each full month of such year during which such building was in service, and
- (ii) the denominator of which is 12.

(B) DISALLOWED 1ST YEAR CREDIT ALLOWED IN 11TH YEAR.—Any reduction by reason of subparagraph (A) in the credit allowable (without regard to subparagraph (A)) for the 1st taxable year of the credit period shall be allowable under subsection (a) for the 1st taxable year following the credit period.

(3) DETERMINATION OF APPLICABLE PERCENTAGE WITH RESPECT TO INCREASES IN QUALIFIED BASIS AFTER 1ST YEAR OF CREDIT PERIOD.—

(A) IN GENERAL.—In the case of any building which was a qualified low-income building as of the close of the 1st year of the credit period, if—

(i) as of the close of any taxable year in the compliance period (after the 1st year of the credit period) the qualified basis of such building exceeds

(ii) the qualified basis of such building as of the close of the 1st year of the credit period,

the applicable percentage which shall apply under subsection (a) for the taxable year to such excess shall be the percentage equal to  $\frac{2}{3}$  of the applicable percentage which (after the application of subsection (h)) would but for this paragraph apply to such basis.

(B) 1ST YEAR COMPUTATION APPLIES.—A rule similar to the rule of paragraph (2)(A) shall apply to any increase in qualified basis to which subparagraph (A) applies for the 1st year of such increase.

(4) DISPOSITIONS OF PROPERTY.—If a building (or an interest therein) is disposed of during any year for which credit is allowable under subsection (a), such credit shall be allocated between the parties on the basis of the number of days during such year the building (or interest) was held by each. In any such case, proper adjustments shall be made in the application of subsection (j).

(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)(B) 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 the dollar amount in effect under subsection (e)(3)(A)(ii)(II) were two-thirds of such amount.

(g) QUALIFIED LOW-INCOME HOUSING PROJECT.—For purposes of this section—

(1) IN GENERAL.—The term “qualified low-income housing project” means any project for residential rental property if the project meets the requirements of subparagraph (A), (B), or (C) whichever is elected by the taxpayer:

(A) 20-50 TEST.—The project meets the requirements of this subparagraph if 20 percent or more of the residential units in such project are both rent-restricted and occupied by individuals whose income is 50 percent or less of area median gross income.

(B) 40-60 TEST.—The project meets the requirements of this subparagraph if 40 percent or more of the residential units in such project are both rent-restricted and occupied by individuals whose income is 60 percent or less of area median gross income.

(C) AVERAGE INCOME TEST.—

(i) IN GENERAL.—The project meets the minimum requirements of this subparagraph if 40 percent or more (25 percent or more in the case of a project described in section 142(d)(6)) of the residential units in such project are both rent-restricted and occupied by individuals whose income does not exceed the imputed income limitation designated by the taxpayer with respect to the respective unit.

(ii) SPECIAL RULES RELATING TO INCOME LIMITATION.—For purposes of clause (i)—

(I) DESIGNATION.—The taxpayer shall designate the imputed income limitation of each unit taken into account under such clause.

(II) AVERAGE TEST.—The average of the imputed income limitations designated under subclause (I) shall not exceed 60 percent of area median gross income.

(III) 10-PERCENT INCREMENTS.—The designated imputed income limitation of any unit under subclause (I) shall be 20 percent, 30 percent, 40 percent, 50 percent, 60 percent, 70 percent, or 80 percent of area median gross income.

Any election under this paragraph, once made, shall be irrevocable. For purposes of this paragraph, any property shall not be treated as failing to be residential rental property merely because part of the building in which such property is located is used for purposes other than residential rental purposes.

(2) RENT-RESTRICTED UNITS.—

(A) IN GENERAL.—For purposes of paragraph (1), a residential unit is rent-restricted if the gross rent with respect to such unit does not exceed 30 percent of the imputed income limitation applicable to such unit. 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.

(B) GROSS RENT.—For purposes of subparagraph (A), gross rent—

(i) does not include any payment under section 8 of the United States Housing Act of 1937 or any comparable rental assistance program (with respect to such unit or occupants thereof),

(ii) includes any utility allowance determined by the Secretary after taking into account such determinations under section 8 of the United States Housing Act of 1937,

(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, and

(iv) does not include any rental payment to the owner of the unit to the extent such owner pays an equivalent amount to the Farmers' Home Administration under section 515 of the Housing Act of 1949.

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.

(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 if 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 other-

wise 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 clauses (ii), (iii), and (iv), 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 and such unit continues to be rent-restricted.

(ii) RENTAL OF NEXT AVAILABLE UNIT IN CASE OF 20-50 OR 40-60 TEST.—In the case of a project with respect to which the taxpayer elects the requirements of subparagraph (A) or (B) of paragraph (1), 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.

(iii) Rental of next available unit in case of average income test

In the case of a project with respect to which the taxpayer elects the requirements of subparagraph (C) of paragraph (1), if the income of the occupants of the unit increases above 140 percent of the greater of—

(I) 60 percent of area median gross income, or

(II) the imputed income limitation designated with respect to the unit under paragraph (1)(C)(ii)(I),

clause (i) shall cease to apply to any 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 the limitation described in clause (v).

(iv) DEEP RENT SKEWED PROJECTS.—In the case of a project described in section 142(d)(4)(B), clause (ii) or (iii), whichever is applicable, shall be applied by substituting “170 percent” for “140 percent”, and—

(I) in the case of clause (ii), by substituting “any low-income unit in the building is occupied by a new resident whose income exceeds 40 percent of area median gross income” for “any residential rental unit” and all that follows in such clause, and

(II) in the case of clause (iii), by substituting “any low-income unit in the building is occupied by a new resident whose income exceeds the lesser of 40 percent of area median gross income or the imputed income limitation designated with respect to such unit under paragraph (1)(C)(ii)(I)” for “any

residential rental unit” and all that follows in such clause.

(v) LIMITATION DESCRIBED.—For purposes of clause (iii), the limitation described in this clause with respect to any unit is—

(I) the imputed income limitation designated with respect to such unit under paragraph (1)(C)(ii)(I), in the case of a unit which was taken into account as a low-income unit prior to becoming vacant, and

(II) the imputed income limitation which would have to be designated with respect to such unit under such paragraph in order for the project to continue to meet the requirements of paragraph (1)(C)(ii)(II), in the case of any other unit.

(E) UNITS WHERE FEDERAL RENTAL ASSISTANCE IS REDUCED AS TENANT’S INCOME INCREASES.—If the gross rent with respect to a residential unit exceeds the limitation under subparagraph (A) by reason of the fact that the income of the occupants thereof exceeds the income limitation applicable under paragraph (1), such unit shall, nevertheless, be treated as a rent-restricted unit for purposes of paragraph (1) if—

(i) a Federal rental assistance payment described in subparagraph (B)(i) is made with respect to such unit or its occupants, and

(ii) the sum of such payment and the gross rent with respect to such unit does not exceed the sum of the amount of such payment which would be made and the gross rent which would be payable with respect to such unit if—

(I) the income of the occupants thereof did not exceed the income limitation applicable under paragraph (1), and

(II) such units were rent-restricted within the meaning of subparagraph (A).

The preceding sentence shall apply to any unit only if the result described in clause (ii) is required by Federal statute as of the date of the enactment of this subparagraph and as of the date the Federal rental assistance payment is made.

(3) DATE FOR MEETING REQUIREMENTS.—

(A) IN GENERAL.—Except as otherwise provided in this paragraph, a building shall be treated as a qualified low-income building only if the project (of which such building is a part) meets the requirements of paragraph (1) not later than the close of the 1st year of the credit period for such building.

(B) BUILDINGS WHICH RELY ON LATER BUILDINGS FOR QUALIFICATION.—

(i) IN GENERAL.—In determining whether a building (hereinafter in this subparagraph referred to as the “prior building”) is a qualified low-income building, the taxpayer may take into account 1 or more additional buildings placed in service during the 12-month period



described in subparagraph (A) with respect to the prior building only if the taxpayer elects to apply clause (ii) with respect to each additional building taken into account.

(ii) TREATMENT OF ELECTED BUILDINGS.—In the case of a building which the taxpayer elects to take into account under clause (i), the period under subparagraph (A) for such building shall end at the close of the 12-month period applicable to the prior building.

(iii) DATE PRIOR BUILDING IS TREATED AS PLACED IN SERVICE.—For purposes of determining the credit period and the compliance period for the prior building, the prior building shall be treated for purposes of this section as placed in service on the most recent date any additional building elected by the taxpayer (with respect to such prior building) was placed in service.

(C) SPECIAL RULE.—A building—

(i) other than the 1st building placed in service as part of a project, and

(ii) other than a building which is placed in service during the 12-month period described in subparagraph (A) with respect to a prior building which becomes a qualified low-income building,

shall in no event be treated as a qualified low-income building unless the project is a qualified low-income housing project (without regard to such building) on the date such building is placed in service.

(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.

(4) CERTAIN RULES MADE APPLICABLE.—Paragraphs (2) (other than subparagraph (A) thereof), (3), (4), (5), (6), and (7) of section 142(d), and section 6652(j), shall apply for purposes of determining whether any project is a qualified low-income housing project and whether any unit is a low-income unit; except that, in applying such provisions for such purposes, the term “gross rent” shall have the meaning given such term by paragraph (2)(B) of this subsection.

(5) ELECTION TO TREAT BUILDING AFTER COMPLIANCE PERIOD AS NOT PART OF A PROJECT.—For purposes of this section, the taxpayer may elect to treat any building as not part of a qualified low-income housing project for any period beginning after the compliance period for such building.

(6) SPECIAL RULE WHERE DE MINIMIS EQUITY CONTRIBUTION.—Property shall not be treated as failing to be residential rental property for purposes of this section merely because the occupant of a residential unit in the project pays (on a voluntary basis) to the lessor a de minimis amount to be held toward the purchase by such occupant of a residential unit in such project if—

- (A) all amounts so paid are refunded to the occupant on the cessation of his occupancy of a unit in the project, and
- (B) the purchase of the unit is not permitted until after the close of the compliance period with respect to the building in which the unit is located.

Any amount paid to the lessor as described in the preceding sentence shall be included in gross rent under paragraph (2) for purposes of determining whether the unit is rent-restricted.

(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.

(8) WAIVER OF CERTAIN DE MINIMIS ERRORS AND RECERTIFICATIONS.—On application by the taxpayer, the Secretary may waive—

- (A) any recapture under subsection (j) in the case of any de minimis error in complying with paragraph (1), or
- (B) any annual recertification of tenant income for purposes of this subsection, if the entire building is occupied by low-income tenants.

(9) CLARIFICATION OF GENERAL PUBLIC USE REQUIREMENT.—A project does not fail to meet the general public use requirement solely because of occupancy restrictions or preferences that favor tenants—

- (A) with special needs,
- (B) who are members of a specified group under a Federal program or State program or policy that supports housing for such a specified group, or
- (C) who are involved in artistic or literary activities.

(h) LIMITATION ON AGGREGATE CREDIT ALLOWABLE WITH RESPECT TO PROJECTS LOCATED IN A STATE.—

(1) CREDIT MAY NOT EXCEED CREDIT AMOUNT ALLOCATED TO BUILDING.—

(A) IN GENERAL.—The amount of the credit determined under this section for any taxable year with respect to any building shall not exceed the housing credit dollar amount allocated to such building under this subsection.

(B) TIME FOR MAKING ALLOCATION.—Except in the case of an allocation which meets the requirements of subparagraph (C), (D), (E), or (F), an allocation shall be taken into account under subparagraph (A) only if it is made not later than the close of the calendar year in which the building is placed in service.

(C) EXCEPTION WHERE BINDING COMMITMENT.—An allocation meets the requirements of this subparagraph if there is a binding commitment (not later than the close of the calendar year in which the building is placed in service) by the housing credit agency to allocate a specified housing credit dollar amount to such building beginning in a specified later taxable year.

(D) EXCEPTION WHERE INCREASE IN QUALIFIED BASIS.—

- (i) IN GENERAL.—An allocation meets the requirements of this subparagraph if such allocation is made

not later than the close of the calendar year in which ends the taxable year to which it will 1st apply but only to the extent the amount of such allocation does not exceed the limitation under clause (ii).

(ii) **LIMITATION.**—The limitation under this clause is the amount of credit allowable under this section (without regard to this subsection) for a taxable year with respect to an increase in the qualified basis of the building equal to the excess of—

(I) the qualified basis of such building as of the close of the 1st taxable year to which such allocation will apply, over

(II) the qualified basis of such building as of the close of the 1st taxable year to which the most recent prior housing credit allocation with respect to such building applied.

(iii) **HOUSING CREDIT DOLLAR AMOUNT REDUCED BY FULL ALLOCATION.**—Notwithstanding clause (i), the full amount of the allocation shall be taken into account under paragraph (2).

(E) **EXCEPTION WHERE 10 PERCENT OF COST INCURRED.**—

(i) **IN GENERAL.**—An allocation meets the requirements of this subparagraph if such allocation is made with respect to a qualified building which is placed in service not later than the close of the second calendar year following the calendar year in which the allocation is made.

(ii) **QUALIFIED BUILDING.**—For purposes of clause (i), the term “qualified building” means any building which is part of a project if the taxpayer’s basis in such project (as of the date which is 1 year after the date that the allocation was made) is more than 10 percent of the taxpayer’s reasonably expected basis in such project (as of the close of the second calendar year referred to in clause (i)). Such term does not include any existing building unless a credit is allowable under subsection (e) for rehabilitation expenditures paid or incurred by the taxpayer with respect to such building for a taxable year ending during the second calendar year referred to in clause (i) or the prior taxable year.

(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) ALLOCATED CREDIT AMOUNT TO APPLY TO ALL TAXABLE YEARS ENDING DURING OR AFTER CREDIT ALLOCATION YEAR.—Any housing credit dollar amount allocated to any building for any calendar year—

(A) shall apply to such building for all taxable years in the compliance period ending during or after such calendar year, and

(B) shall reduce the aggregate housing credit dollar amount of the allocating agency only for such calendar year.

(3) HOUSING CREDIT DOLLAR AMOUNT FOR AGENCIES.—

(A) IN GENERAL.—The aggregate housing credit dollar amount which a housing credit agency may allocate for any calendar year is the portion of the State housing credit ceiling allocated under this paragraph for such calendar year to such agency.

(B) STATE CEILING INITIALLY ALLOCATED TO STATE HOUSING CREDIT AGENCIES.—Except as provided in subparagraphs (D) and (E), the State housing credit ceiling for each calendar year shall be allocated to the housing credit agency of such State. If there is more than 1 housing credit agency of a State, all such agencies shall be treated as a single agency.

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

(ii) the greater of—

(I) \$1.75 multiplied by the State population, or

(II) \$2,000,000,

(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 (i), the unused State housing credit ceiling for any calendar year is the excess (if any) of the sum of the amounts described in clauses (ii) through (iv) 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 fails to meet the 10 percent test under paragraph (1)(E)(ii) on a date after the close of the calendar year in which the allocation was made or 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 cancelled 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—

(I) the unused State housing credit ceiling for the year preceding such year, over

(II) the aggregate housing credit dollar amount allocated for such year.

(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).

(E) SPECIAL RULE FOR STATES WITH CONSTITUTIONAL HOME RULE CITIES.—For purposes of this subsection—

(i) IN GENERAL.—The aggregate housing credit dollar amount for any constitutional home rule city for any calendar year shall be an amount which bears the same ratio to the State housing credit ceiling for such calendar year as—

(I) the population of such city, bears to

(II) the population of the entire State.

(ii) COORDINATION WITH OTHER ALLOCATIONS.—In the case of any State which contains 1 or more constitutional home rule cities, for purposes of applying this paragraph with respect to housing credit agencies in such State other than constitutional home rule cities, the State housing credit ceiling for any calendar year shall be reduced by the aggregate housing credit dollar amounts determined for such year for all constitutional home rule cities in such State.

(iii) CONSTITUTIONAL HOME RULE CITY.—For purposes of this paragraph, the term “constitutional home rule city” has the meaning given such term by section 146(d)(3)(C).

(F) STATE MAY PROVIDE FOR DIFFERENT ALLOCATION.—Rules similar to the rules of section 146(e) (other than paragraph (2)(B) thereof) shall apply for purposes of this paragraph.

(G) POPULATION.—For purposes of this paragraph, population shall be determined in accordance with section 146(j).

(H) COST-OF-LIVING ADJUSTMENT.—

(i) IN GENERAL.—In the case of a calendar year after 2002, the \$2,000,000 and \$1.75 amounts in subparagraph (C) shall each be increased by an amount equal to—

(I) such dollar amount, multiplied by

(II) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year by substituting “calendar year 2001” for “calendar year 2016” in subparagraph (A)(ii) thereof.

(ii) ROUNDING.—

(I) In the case of the \$2,000,000 amount, any increase under clause (i) which is not a multiple of \$5,000 shall be rounded to the next lowest multiple of \$5,000.

(II) In the case of the \$1.75 amount, any increase under clause (i) which is not a multiple of 5 cents shall be rounded to the next lowest multiple of 5 cents.

(I) INCREASE IN STATE HOUSING CREDIT CEILING FOR 2018, 2019, 2020, AND 2021.—In the case of calendar years 2018, 2019, 2020, and 2021, each of the dollar amounts in effect under clauses (I) and (II) of subparagraph (C)(ii) for any calendar year (after any increase under subparagraph (H)) shall be increased by multiplying such dollar amount by 1.125.

(4) CREDIT FOR BUILDINGS FINANCED BY TAX-EXEMPT BONDS SUBJECT TO VOLUME CAP NOT TAKEN INTO ACCOUNT.—

(A) IN GENERAL.—Paragraph (1) shall not apply to the portion of any credit allowable under subsection (a) which is attributable to eligible basis financed by any obligation the interest on which is exempt from tax under section 103 if—

(i) such obligation is taken into account under section 146, and

(ii) principal payments on such financing are applied within a reasonable period to redeem obligations the proceeds of which were used to provide such financing or such financing is refunded as described in section 146(i)(6).

(B) SPECIAL RULE WHERE 50 PERCENT OR MORE OF BUILDING IS FINANCED WITH TAX-EXEMPT BONDS SUBJECT TO VOLUME CAP.—For purposes of subparagraph (A), if 50 percent or more of the aggregate basis of any building and the

land on which the building is located is financed by any obligation described in subparagraph (A), paragraph (1) shall not apply to any portion of the credit allowable under subsection (a) with respect to such building.

(5) PORTION OF STATE CEILING SET-ASIDE FOR CERTAIN PROJECTS INVOLVING QUALIFIED NONPROFIT ORGANIZATIONS.—

(A) IN GENERAL.—Not more than 90 percent of the State housing credit ceiling for any State for any calendar year shall be allocated to projects other than qualified low-income housing projects described in subparagraph (B).

(B) PROJECTS INVOLVING QUALIFIED NONPROFIT ORGANIZATIONS.—For purposes of subparagraph (A), a qualified low-income housing project is described in this subparagraph if a qualified nonprofit organization is to own an interest in the project (directly or through a partnership) and materially participate (within the meaning of section 469(h)) in the development and operation of the project throughout the compliance period.

(C) QUALIFIED NONPROFIT ORGANIZATION.—For purposes of this paragraph, the term “qualified nonprofit organization” means any organization if—

(i) such organization is described in paragraph (3) or (4) of section 501(c) and is exempt from tax under section 501(a),

(ii) such organization is determined by the State housing credit agency not to be affiliated with or controlled by a for-profit organization, and

(iii) 1 of the exempt purposes of such organization includes the fostering of low-income housing.

(D) TREATMENT OF CERTAIN SUBSIDIARIES.—

(i) IN GENERAL.—For purposes of this paragraph, a qualified nonprofit organization shall be treated as satisfying the ownership and material participation test of subparagraph (B) if any qualified corporation in which such organization holds stock satisfies such test.

(ii) QUALIFIED CORPORATION.—For purposes of clause (i), the term “qualified corporation” means any corporation if 100 percent of the stock of such corporation is held by 1 or more qualified nonprofit organizations at all times during the period such corporation is in existence.

(E) STATE MAY NOT OVERRIDE SET-ASIDE.—Nothing in subparagraph (F) of paragraph (3) shall be construed to permit a State not to comply with subparagraph (A) of this 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 and which prohibits the actions described in subclauses (I) and (II) of subparagraph (E)(ii),

(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 and prohibitions of clause (i),

(iii) which prohibits the disposition to any person of any portion of the building to which such agreement applies unless all of the building to which such agreement applies is disposed of to such person,

(iv) which prohibits the refusal to lease to a holder of a voucher or certificate of eligibility under section 8 of the United States Housing Act of 1937 because of the status of the prospective tenant as such a holder,

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

(vi) 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) unless the Secretary determines that such acquisition is part of an arrangement with the taxpayer a purpose of which is to terminate such period, 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 not otherwise permitted under this section.

(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 nonlow-income portion of the building for fair market value and 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 2016” in subparagraph (A)(ii) thereof.

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 C-CPI-U for any calendar year (as defined in section 1(f)(6)) exceeds the C-CPI-U for the preceding calendar year by more than 5 percent, the C-CPI-U for the base calendar year shall be increased such that such excess shall never be taken into account under clause (i). In the case of a base calendar year before 2017, the C-CPI-U for such year shall be determined by multiplying the CPI for such year by the amount determined under section 1(f)(3)(B).

(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 person to acquire the taxpayer’s interest in the low-income portion of the building.

(J) 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.

(K) 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.

(7) SPECIAL RULES.—

(A) BUILDING MUST BE LOCATED WITHIN JURISDICTION OF CREDIT AGENCY.—A housing credit agency may allocate its aggregate housing credit dollar amount only to buildings located in the jurisdiction of the governmental unit of which such agency is a part.

(B) AGENCY ALLOCATIONS IN EXCESS OF LIMIT.—If the aggregate housing credit dollar amounts allocated by a housing credit agency for any calendar year exceed the portion of the State housing credit ceiling allocated to such agency for such calendar year, the housing credit dollar amounts so allocated shall be reduced (to the extent of such excess) for buildings in the reverse of the order in which the allocations of such amounts were made.

(C) Credit reduced if allocated credit dollar amount is less than credit which would be allowable without regard to placed in service convention, etc.

(i) IN GENERAL.—The amount of the credit determined under this section with respect to any building shall not exceed the clause (ii) percentage of the amount of the credit which would (but for this subparagraph) be determined under this section with respect to such building.

(ii) DETERMINATION OF PERCENTAGE.—For purposes of clause (i), the clause (ii) percentage with respect to any building is the percentage which—

(I) the housing credit dollar amount allocated to such building bears to

(II) the credit amount determined in accordance with clause (iii).

(iii) DETERMINATION OF CREDIT AMOUNT.—The credit amount determined in accordance with this clause is the amount of the credit which would (but for this subparagraph) be determined under this section with respect to the building if—

(I) this section were applied without regard to paragraphs (2)(A) and (3)(B) of subsection (f), and

(II) subsection (f)(3)(A) were applied without regard to “the percentage equal to 2/3 of”.

(D) HOUSING CREDIT AGENCY TO SPECIFY APPLICABLE PERCENTAGE AND MAXIMUM QUALIFIED BASIS.—In allocating a housing credit dollar amount to any building, the housing credit agency shall specify the applicable percentage and the maximum qualified basis which may be taken into account under this section with respect to such building. The applicable percentage and maximum qualified basis so specified shall not exceed the applicable percentage and qualified basis determined under this section without regard to this subsection.

(8) OTHER DEFINITIONS.—For purposes of this subsection—

(A) HOUSING CREDIT AGENCY.—The term “housing credit agency” means any agency authorized to carry out this subsection.

(B) POSSESSIONS TREATED AS STATES.—The term “State” includes a possession of the United States.

(i) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) COMPLIANCE PERIOD.—The term “compliance period” means, with respect to any building, the period of 15 taxable years beginning with the 1st taxable year of the credit period with respect thereto.

## (2) DETERMINATION OF WHETHER BUILDING IS FEDERALLY SUBSIDIZED.—

(A) IN GENERAL.—Except as otherwise provided in this paragraph, for purposes of subsection (b)(1), a new building shall be treated as federally subsidized for any taxable year if, at any time during such taxable year or any prior taxable year, there is or was outstanding any obligation the interest on which is exempt from tax under section 103 the proceeds of which are or were used (directly or indirectly) with respect to such building or the operation thereof.

(B) ELECTION TO REDUCE ELIGIBLE BASIS BY PROCEEDS OF OBLIGATIONS.—A tax-exempt obligation shall not be taken into account under subparagraph (A) if the taxpayer elects to exclude from the eligible basis of the building for purposes of subsection (d) the proceeds of such obligation.

(C) SPECIAL RULE FOR SUBSIDIZED CONSTRUCTION FINANCING.—Subparagraph (A) shall not apply to any tax-exempt obligation used to provide construction financing for any building if—

- (i) such obligation (when issued) identified the building for which the proceeds of such obligation would be used, and
- (ii) such obligation is redeemed before such building is placed in service.

## (3) LOW-INCOME UNIT.—

(A) IN GENERAL.—The term “low-income unit” means any unit in a building if—

- (i) such unit is rent-restricted (as defined in subsection (g)(2)), and
- (ii) the individuals occupying such unit meet the income limitation applicable under subsection (g)(1) to the project of which such building is a part.

## (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 McKinney-Vento 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

(h)(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.

(C) SPECIAL RULE FOR BUILDINGS HAVING 4 OR FEWER UNITS.—In the case of any building which has 4 or fewer residential rental units, no unit in such building shall be treated as a low-income unit if the units in such building are owned by—

(i) any individual who occupies a residential unit in such building, or

(ii) any person who is related (as defined in subsection (d)(2)(D)(iii)) to such individual.

(D) CERTAIN STUDENTS NOT TO DISQUALIFY UNIT.—A unit shall not fail to be treated as a low-income unit merely because it is occupied—

(i) by an individual who is—

(I) a student and receiving assistance under title IV of the Social Security Act,

(II) a student who was previously under the care and placement responsibility of the State agency responsible for administering a plan under part B or part E of title IV of the Social Security Act, or

(III) enrolled in a job training program receiving assistance under the Job Training Partnership Act or under other similar Federal, State, or local laws, or

(ii) entirely by full-time students if such students are—

(I) single parents and their children and such parents are not dependents (as defined in [section 152] section 7706, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof) of another individual and such children are not dependents (as so defined) of another individual other than a parent of such children, or

(II) married and file a joint return.

(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.

(4) NEW BUILDING.—The term “new building” means a building the original use of which begins with the taxpayer.

(5) EXISTING BUILDING.—The term “existing building” means any building which is not a new building.

(6) APPLICATION TO ESTATES AND TRUSTS.—In the case of an estate or trust, the amount of the credit determined under subsection (a) and any increase in tax under subsection (j) shall be apportioned between the estate or trust and the beneficiaries on the basis of the income of the estate or trust allocable to each.

(7) IMPACT OF TENANT’S 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 (in cooperative form or otherwise) or resident management corporation of such building or by a qualified nonprofit organization (as defined in subsection (h)(5)(C)) or government agency 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).

(8) TREATMENT OF RURAL PROJECTS.—For purposes of this section, in the case of any project for residential rental property located in a rural area (as defined in section 520 of the Housing Act of 1949), any income limitation measured by reference to area median gross income shall be measured by reference to the greater of area median gross income or national non-metropolitan median income. The preceding sentence shall not apply with respect to any building if paragraph (1) of section 42(h) does not apply by reason of paragraph (4) thereof to any portion of the credit determined under this section with respect to such building.

(9) COORDINATION WITH LOW-INCOME HOUSING GRANTS.—

(A) REDUCTION IN STATE HOUSING CREDIT CEILING FOR LOW-INCOME HOUSING GRANTS RECEIVED IN 2009.—For purposes of this section, the amounts described in clauses (i) through (iv) of subsection (h)(3)(C) with respect to any State for 2009 shall each be reduced by so much of such amount as is taken into account in determining the

amount of any grant to such State under section 1602 of the American Recovery and Reinvestment Tax Act of 2009.

(B) SPECIAL RULE FOR BASIS.—Basis of a qualified low-income building shall not be reduced by the amount of any grant described in subparagraph (A).

(j) RECAPTURE OF CREDIT.—

(1) IN GENERAL.—If—

(A) as of the close of any taxable year in the compliance period, the amount of the qualified basis of any building with respect to the taxpayer is less than

(B) the amount of such basis as of the close of the preceding taxable year,

then the taxpayer's tax under this chapter for the taxable year shall be increased by the credit recapture amount.

(2) CREDIT RECAPTURE AMOUNT.—For purposes of paragraph (1), the credit recapture amount is an amount equal to the sum of—

(A) the aggregate decrease in the credits allowed to the taxpayer under section 38 for all prior taxable years which would have resulted if the accelerated portion of the credit allowable by reason of this section were not allowed for all prior taxable years with respect to the excess of the amount described in paragraph (1)(B) over the amount described in paragraph (1)(A), plus

(B) interest at the overpayment rate established under section 6621 on the amount determined under subparagraph (A) for each prior taxable year for the period beginning on the due date for filing the return for the prior taxable year involved.

No deduction shall be allowed under this chapter for interest described in subparagraph (B).

(3) ACCELERATED PORTION OF CREDIT.—For purposes of paragraph (2), the accelerated portion of the credit for the prior taxable years with respect to any amount of basis is the excess of—

(A) the aggregate credit allowed by reason of this section (without regard to this subsection) for such years with respect to such basis, over

(B) the aggregate credit which would be allowable by reason of this section for such years with respect to such basis if the aggregate credit which would (but for this subsection) have been allowable for the entire compliance period were allowable ratably over 15 years.

(4) SPECIAL RULES.—

(A) TAX BENEFIT RULE.—The tax for the taxable year shall be increased under paragraph (1) only with respect to credits allowed by reason of this section which were used to reduce tax liability. In the case of credits not so used to reduce tax liability, the carryforwards and carrybacks under section 39 shall be appropriately adjusted.

(B) ONLY BASIS FOR WHICH CREDIT ALLOWED TAKEN INTO ACCOUNT.—Qualified basis shall be taken into account under paragraph (1)(B) only to the extent such basis was taken into account in determining the credit under sub-

section (a) for the preceding taxable year referred to in such paragraph.

(C) NO RECAPTURE OF ADDITIONAL CREDIT ALLOWABLE BY REASON OF SUBSECTION (F)(3).—Paragraph (1) shall apply to a decrease in qualified basis only to the extent such decrease exceeds the amount of qualified basis with respect to which a credit was allowable for the taxable year referred to in paragraph (1)(B) by reason of subsection (f)(3).

(D) NO CREDITS AGAINST TAX.—Any increase in tax under this subsection shall not be treated as a tax imposed by this chapter for purposes of determining the amount of any credit under this chapter.

(E) NO RECAPTURE BY REASON OF CASUALTY LOSS.—The increase in tax under this subsection shall not apply to a reduction in qualified basis by reason of a casualty loss to the extent such loss is restored by reconstruction or replacement within a reasonable period established by the Secretary.

(F) NO RECAPTURE WHERE DE MINIMIS CHANGES IN FLOOR SPACE.—The Secretary may provide that the increase in tax under this subsection shall not apply with respect to any building if—

- (i) such increase results from a de minimis change in the floor space fraction under subsection (c)(1), and
- (ii) the building is a qualified low-income building after such change.

(5) CERTAIN PARTNERSHIPS TREATED AS THE TAXPAYER.—

(A) IN GENERAL.—For purposes of applying this subsection to a partnership to which this paragraph applies—

- (i) such partnership shall be treated as the taxpayer to which the credit allowable under subsection (a) was allowed,
- (ii) the amount of such credit allowed shall be treated as the amount which would have been allowed to the partnership were such credit allowable to such partnership,
- (iii) paragraph (4)(A) shall not apply, and
- (iv) the amount of the increase in tax under this subsection for any taxable year shall be allocated among the partners of such partnership in the same manner as such partnership's taxable income for such year is allocated among such partners.

(B) PARTNERSHIPS TO WHICH PARAGRAPH APPLIES.—This paragraph shall apply to any partnership which has 35 or more partners unless the partnership elects not to have this paragraph apply.

(C) SPECIAL RULES.—

(i) HUSBAND AND WIFE TREATED AS 1 PARTNER.—For purposes of subparagraph (B)(i), a husband and wife (and their estates) shall be treated as 1 partner.

(ii) ELECTION IRREVOCABLE.—Any election under subparagraph (B), once made, shall be irrevocable.

(6) NO RECAPTURE ON DISPOSITION OF BUILDING WHICH CONTINUES IN QUALIFIED USE.—



(A) IN GENERAL.—The increase in tax under this subsection shall not apply solely by reason of the disposition of a building (or an interest therein) if it is reasonably expected that such building will continue to be operated as a qualified low-income building for the remaining compliance period with respect to such building.

(B) STATUTE OF LIMITATIONS.—If a building (or an interest therein) is disposed of during any taxable year and there is any reduction in the qualified basis of such building which results in an increase in tax under this subsection for such taxable or any subsequent taxable year, then—

(i) the statutory period for the assessment of any deficiency with respect to such increase in tax shall not expire before the expiration of 3 years from the date the Secretary is notified by the taxpayer (in such manner as the Secretary may prescribe) of such reduction in qualified basis, and

(ii) such deficiency may be assessed before the expiration of such 3-year period notwithstanding the provisions of any other law or rule of law which would otherwise prevent such assessment.

(k) APPLICATION OF AT-RISK RULES.—For purposes of this section—

(1) IN GENERAL.—Except as otherwise provided in this subsection, rules similar to the rules of section 49(a)(1) (other than subparagraphs (D)(ii)(II) and (D)(iv)(I) thereof), section 49(a)(2), and section 49(b)(1) shall apply in determining the qualified basis of any building in the same manner as such sections apply in determining the credit base of property.

(2) SPECIAL RULES FOR DETERMINING QUALIFIED PERSON.—For purposes of paragraph (1)—

(A) IN GENERAL.—If the requirements of subparagraphs (B), (C), and (D) are met with respect to any financing borrowed from a qualified nonprofit organization (as defined in subsection (h)(5)), the determination of whether such financing is qualified commercial financing with respect to any qualified low-income building shall be made without regard to whether such organization—

(i) is actively and regularly engaged in the business of lending money, or

(ii) is a person described in section 49(a)(1)(D)(iv)(II).

(B) FINANCING SECURED BY PROPERTY.—The requirements of this subparagraph are met with respect to any financing if such financing is secured by the qualified low-income building, except that this subparagraph shall not apply in the case of a federally assisted building described in subsection (d)(6)(C) if—

(i) a security interest in such building is not permitted by a Federal agency holding or insuring the mortgage secured by such building, and

(ii) the proceeds from the financing (if any) are applied to acquire or improve such building.

(C) PORTION OF BUILDING ATTRIBUTABLE TO FINANCING.—The requirements of this subparagraph are met with respect to any financing for any taxable year in the compliance period if, as of the close of such taxable year, not more than 60 percent of the eligible basis of the qualified low-income building is attributable to such financing (reduced by the principal and interest of any governmental financing which is part of a wrap-around mortgage involving such financing).

(D) REPAYMENT OF PRINCIPAL AND INTEREST.—The requirements of this subparagraph are met with respect to any financing if such financing is fully repaid on or before the earliest of—

- (i) the date on which such financing matures,
- (ii) the 90th day after the close of the compliance period with respect to the qualified low-income building,
- or
- (iii) the date of its refinancing or the sale of the building to which such financing relates.

In the case of a qualified nonprofit organization which is not described in section 49(a)(1)(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.

(3) PRESENT VALUE OF FINANCING.—If the rate of interest on any financing described in paragraph (2)(A) is less than the rate which is 1 percentage point below the applicable Federal rate as of the time such financing is incurred, then the qualified basis (to which such financing relates) of the qualified low-income building shall be the present value of the amount of such financing, using as the discount rate such applicable Federal rate. For purposes of the preceding sentence, the rate of interest on any financing shall be determined by treating interest to the extent of government subsidies as not payable.

(4) FAILURE TO FULLY REPAY.—

(A) IN GENERAL.—To the extent that the requirements of paragraph (2)(D) are not met, then the taxpayer's tax under this chapter for the taxable year in which such failure occurs shall be increased by an amount equal to the applicable portion of the credit under this section with respect to such building, increased by an amount of interest for the period—

- (i) beginning with the due date for the filing of the return of tax imposed by chapter 1 for the 1st taxable year for which such credit was allowable, and
- (ii) ending with the due date for the taxable year in which such failure occurs,

determined by using the underpayment rate and method under section 6621.

(B) APPLICABLE PORTION.—For purposes of subparagraph (A), the term “applicable portion” means the aggregate decrease in the credits allowed to a taxpayer under section 38 for all prior taxable years which would have resulted if

the eligible basis of the building were reduced by the amount of financing which does not meet requirements of paragraph (2)(D).

(C) CERTAIN RULES TO APPLY.—Rules similar to the rules of subparagraphs (A) and (D) of subsection (j)(4) shall apply for purposes of this subsection.

(l) CERTIFICATIONS AND OTHER REPORTS TO SECRETARY.—

(1) CERTIFICATION WITH RESPECT TO 1ST YEAR OF CREDIT PERIOD.—Following the close of the 1st taxable year in the credit period with respect to any qualified low-income building, the taxpayer shall certify to the Secretary (at such time and in such form and in such manner as the Secretary prescribes)—

(A) the taxable year, and calendar year, in which such building was placed in service,

(B) the adjusted basis and eligible basis of such building as of the close of the 1st year of the credit period,

(C) the maximum applicable percentage and qualified basis permitted to be taken into account by the appropriate housing credit agency under subsection (h),

(D) the election made under subsection (g) with respect to the qualified low-income housing project of which such building is a part, and

(E) such other information as the Secretary may require.

In the case of a failure to make the certification required by the preceding sentence on the date prescribed therefor, unless it is shown that such failure is due to reasonable cause and not to willful neglect, no credit shall be allowable by reason of subsection (a) with respect to such building for any taxable year ending before such certification is made.

(2) ANNUAL REPORTS TO THE SECRETARY.—The Secretary may require taxpayers to submit an information return (at such time and in such form and manner as the Secretary prescribes) for each taxable year setting forth—

(A) the qualified basis for the taxable year of each qualified low-income building of the taxpayer,

(B) the information described in paragraph (1)(C) for the taxable year, and

(C) such other information as the Secretary may require.

The penalty under section 6652(j) shall apply to any failure to submit the return required by the Secretary under the preceding sentence on the date prescribed therefor.

(3) ANNUAL REPORTS FROM HOUSING CREDIT AGENCIES.—Each agency which allocates any housing credit amount to any building for any calendar year shall submit to the Secretary (at such time and in such manner as the Secretary shall prescribe) an annual report specifying—

(A) the amount of housing credit amount allocated to each building for such year,

(B) sufficient information to identify each such building and the taxpayer with respect thereto, and

(C) such other information as the Secretary may require.

The penalty under section 6652(j) shall apply to any failure to submit the report required by the preceding sentence on the date prescribed therefor.

(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,

(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,

(iii) a comprehensive market study of the housing needs of low-income individuals in the area to be served by the project is conducted before the credit allocation is made and at the developer's expense by a disinterested party who is approved by such agency, and

(iv) a written explanation is available to the general public for any allocation of a housing credit dollar amount which is not made in accordance with established priorities and selection criteria of the housing credit agency.

(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 also gives preference in allocating housing credit dollar amounts among selected projects to—

(I) projects serving the lowest income tenants,

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

(III) projects which are located in qualified census tracts (as defined in subsection (d)(5)(B)(ii)) and the development of which contributes to a concerted community revitalization plan, and

(iii) which provides a procedure that the agency (or an agent or other private contractor of such agency) will follow in monitoring for noncompliance with the provisions of this section and in notifying the Internal Revenue Service of such noncompliance which such agency becomes aware of and in monitoring for noncompliance with habitability standards through regular site visits.

(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, including whether the project includes the use of existing housing as part of a community revitalization plan,
- (iv) sponsor characteristics,
- (v) tenant populations with special housing needs,
- (vi) public housing waiting lists,
- (vii) tenant populations of individuals with children,
- (viii) projects intended for eventual tenant ownership,
- (ix) the energy efficiency of the project, and
- (x) the historic nature of the project.

(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,
- (ii) any proceeds or receipts expected to be generated by reason of tax benefits,
- (iii) the percentage of the housing credit dollar amount used for project costs other than the cost of intermediaries, and
- (iv) the reasonableness of the developmental and operational costs of the project.

Clause (iii) shall not be applied so as to impede the development of projects in hard-to-develop areas. 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).
- (n) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations—
- (1) dealing with—
    - (A) projects which include more than 1 building or only a portion of a building,
    - (B) buildings which are placed in service in portions,
  - (2) providing for the application of this section to short taxable years,
  - (3) preventing the avoidance of the rules of this section, and
  - (4) providing the opportunity for housing credit agencies to correct administrative errors and omissions with respect to allocations and record keeping within a reasonable period after their discovery, taking into account the availability of regulations and other administrative guidance from the Secretary.

\* \* \* \* \*

**SEC. 45R. EMPLOYEE HEALTH INSURANCE EXPENSES OF SMALL EMPLOYERS.**

- (a) GENERAL RULE.—For purposes of section 38, in the case of an eligible small employer, the small employer health insurance credit determined under this section for any taxable year in the credit period is the amount determined under subsection (b).
- (b) HEALTH INSURANCE CREDIT AMOUNT.—Subject to subsection (c), the amount determined under this subsection with respect to any eligible small employer is equal to 50 percent (35 percent in the case of a tax-exempt eligible small employer) of the lesser of—
- (1) the aggregate amount of nonelective contributions the employer made on behalf of its employees during the taxable year under the arrangement described in subsection (d)(4) for premiums for qualified health plans offered by the employer to its employees through an Exchange, or
  - (2) the aggregate amount of nonelective contributions which the employer would have made during the taxable year under the arrangement if each employee taken into account under paragraph (1) had enrolled in a qualified health plan which had a premium equal to the average premium (as determined by the Secretary of Health and Human Services) for the small group market in the rating area in which the employee enrolls for coverage.
- (c) PHASEOUT OF CREDIT AMOUNT BASED ON NUMBER OF EMPLOYEES AND AVERAGE WAGES.—The amount of the credit determined under subsection (b) without regard to this subsection shall be reduced (but not below zero) by the sum of the following amounts:
- (1) Such amount multiplied by a fraction the numerator of which is the total number of full-time equivalent employees of the employer in excess of 10 and the denominator of which is 15.

- (2) Such amount multiplied by a fraction the numerator of which is the average annual wages of the employer in excess of the dollar amount in effect under subsection (d)(3)(B) and the denominator of which is such dollar amount.
- (d) ELIGIBLE SMALL EMPLOYER.—For purposes of this section—
- (1) IN GENERAL.—The term “eligible small employer” means, with respect to any taxable year, an employer—
- (A) which has no more than 25 full-time equivalent employees for the taxable year,
- (B) the average annual wages of which do not exceed an amount equal to twice the dollar amount in effect under paragraph (3)(B) for the taxable year, and
- (C) which has in effect an arrangement described in paragraph (4).
- (2) FULL-TIME EQUIVALENT EMPLOYEES.—
- (A) IN GENERAL.—The term “full-time equivalent employees” means a number of employees equal to the number determined by dividing—
- (i) the total number of hours of service for which wages were paid by the employer to employees during the taxable year, by
- (ii) 2,080.
- Such number shall be rounded to the next lowest whole number if not otherwise a whole number.
- (B) EXCESS HOURS NOT COUNTED.—If an employee works in excess of 2,080 hours of service during any taxable year, such excess shall not be taken into account under subparagraph (A).
- (C) HOURS OF SERVICE.—The Secretary, in consultation with the Secretary of Labor, shall prescribe such regulations, rules, and guidance as may be necessary to determine the hours of service of an employee, including rules for the application of this paragraph to employees who are not compensated on an hourly basis.
- (3) AVERAGE ANNUAL WAGES.—
- (A) IN GENERAL.—The average annual wages of an eligible small employer for any taxable year is the amount determined by dividing—
- (i) the aggregate amount of wages which were paid by the employer to employees during the taxable year, by
- (ii) the number of full-time equivalent employees of the employee determined under paragraph (2) for the taxable year.
- Such amount shall be rounded to the next lowest multiple of \$1,000 if not otherwise such a multiple.
- (B) DOLLAR AMOUNT.—For purposes of paragraph (1)(B) and subsection (c)(2)—
- (i) 2010, 2011, 2012, AND 2013.—The dollar amount in effect under this paragraph for taxable years beginning in 2010, 2011, 2012, or 2013 is \$25,000.
- (ii) SUBSEQUENT YEARS.—In the case of a taxable year beginning in a calendar year after 2013, the dollar amount in effect under this paragraph shall be equal to \$25,000, multiplied by the cost-of-living ad-

justment under section 1(f)(3) for the calendar year, determined by substituting “calendar year 2012” for “calendar year 2016” in subparagraph (A)(ii) thereof.

(4) CONTRIBUTION ARRANGEMENT.—An arrangement is described in this paragraph if it requires an eligible small employer to make a nonelective contribution on behalf of each employee who enrolls in a qualified health plan offered to employees by the employer through an exchange in an amount equal to a uniform percentage (not less than 50 percent) of the premium cost of the qualified health plan.

(5) SEASONAL WORKER HOURS AND WAGES NOT COUNTED.—For purposes of this subsection—

(A) IN GENERAL.—The number of hours of service worked by, and wages paid to, a seasonal worker of an employer shall not be taken into account in determining the full-time equivalent employees and average annual wages of the employer unless the worker works for the employer on more than 120 days during the taxable year.

(B) DEFINITION OF SEASONAL WORKER.—The term “seasonal worker” means a worker who performs labor or services on a seasonal basis as defined by the Secretary of Labor, including workers covered by section 500.20(s)(1) of title 29, Code of Federal Regulations and retail workers employed exclusively during holiday seasons.

(e) OTHER RULES AND DEFINITIONS.—For purposes of this section—

(1) EMPLOYEE.—

(A) CERTAIN EMPLOYEES EXCLUDED.—The term “employee” shall not include—

(i) an employee within the meaning of section 401(c)(1),

(ii) any 2-percent shareholder (as defined in section 1372(b)) of an eligible small business which is an S corporation,

(iii) any 5-percent owner (as defined in section 416(i)(1)(B)(i)) of an eligible small business, or

(iv) any individual who bears any of the relationships described in subparagraphs (A) through (G) of [section 152(d)(2)] *section 7706(d)(2)* to, or is a dependent described in [section 152(d)(2)(H)] *section 7706(d)(2)(H)* of, an individual described in clause (i), (ii), or (iii).

(B) LEASED EMPLOYEES.—The term “employee” shall include a leased employee within the meaning of section 414(n).

(2) CREDIT PERIOD.—The term “credit period” means, with respect to any eligible small employer, the 2-consecutive-taxable year period beginning with the 1st taxable year in which the employer (or any predecessor) offers 1 or more qualified health plans to its employees through an Exchange.

(3) NONELECTIVE CONTRIBUTION.—The term “nonelective contribution” means an employer contribution other than an employer contribution pursuant to a salary reduction arrangement.



(4) **WAGES.**—The term “wages” has the meaning given such term by section 3121(a) (determined without regard to any dollar limitation contained in such section).

(5) **AGGREGATION AND OTHER RULES MADE APPLICABLE.**—

(A) **AGGREGATION RULES.**—All employers treated as a single employer under subsection (b), (c), (m), or (o) of section 414 shall be treated as a single employer for purposes of this section.

(B) **OTHER RULES.**—Rules similar to the rules of subsections (c), (d), and (e) of section 52 shall apply.

(f) **CREDIT MADE AVAILABLE TO TAX-EXEMPT ELIGIBLE SMALL EMPLOYERS.**—

(1) **IN GENERAL.**—In the case of a tax-exempt eligible small employer, there shall be treated as a credit allowable under subpart C (and not allowable under this subpart) the lesser of—

(A) the amount of the credit determined under this section with respect to such employer, or

(B) the amount of the payroll taxes of the employer during the calendar year in which the taxable year begins.

(2) **TAX-EXEMPT ELIGIBLE SMALL EMPLOYER.**—For purposes of this section, the term “tax-exempt eligible small employer” means an eligible small employer which is any organization described in section 501(c) which is exempt from taxation under section 501(a).

(3) **PAYROLL TAXES.**—For purposes of this subsection—

(A) **IN GENERAL.**—The term “payroll taxes” means—

(i) amounts required to be withheld from the employees of the tax-exempt eligible small employer under section 3401(a),

(ii) amounts required to be withheld from such employees under section 3101(b), and

(iii) amounts of the taxes imposed on the tax-exempt eligible small employer under section 3111(b).

(B) **SPECIAL RULE.**—A rule similar to the rule of section 24(d)(2)(C) shall apply for purposes of subparagraph (A).

(g) **APPLICATION OF SECTION FOR CALENDAR YEARS 2010, 2011, 2012, AND 2013.**—In the case of any taxable year beginning in 2010, 2011, 2012, or 2013, the following modifications to this section shall apply in determining the amount of the credit under subsection (a):

(1) **NO CREDIT PERIOD REQUIRED.**—The credit shall be determined without regard to whether the taxable year is in a credit period and for purposes of applying this section to taxable years beginning after 2013, no credit period shall be treated as beginning with a taxable year beginning before 2014.

(2) **AMOUNT OF CREDIT.**—The amount of the credit determined under subsection (b) shall be determined—

(A) by substituting “35 percent (25 percent in the case of a tax-exempt eligible small employer)” for “50 percent (35 percent in the case of a tax-exempt eligible small employer)”,

(B) by reference to an eligible small employer’s nonelective contributions for premiums paid for health insurance

coverage (within the meaning of section 9832(b)(1)) of an employee, and

(C) by substituting for the average premium determined under subsection (b)(2) the amount the Secretary of Health and Human Services determines is the average premium for the small group market in the State in which the employer is offering health insurance coverage (or for such area within the State as is specified by the Secretary).

(3) CONTRIBUTION ARRANGEMENT.—An arrangement shall not fail to meet the requirements of subsection (d)(4) solely because it provides for the offering of insurance outside of an Exchange.

(h) INSURANCE DEFINITIONS.—Any term used in this section which is also used in the Public Health Service Act or subtitle A of title I of the Patient Protection and Affordable Care Act shall have the meaning given such term by such Act or subtitle.

(i) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this section, including regulations to prevent the avoidance of the 2-year limit on the credit period through the use of successor entities and the avoidance of the limitations under subsection (c) through the use of multiple entities.

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**Subpart F—Rules for Computing Work Opportunity Credit**

\* \* \* \* \*

**SEC. 51. AMOUNT OF CREDIT.**

(a) DETERMINATION OF AMOUNT.—For purposes of section 38, the amount of the work opportunity credit determined under this section for the taxable year shall be equal to 40 percent of the qualified first-year wages for such year.

(b) QUALIFIED WAGES DEFINED.—For purposes of this subpart—

(1) IN GENERAL.—The term “qualified wages” means the wages paid or incurred by the employer during the taxable year to individuals who are members of a targeted group.

(2) QUALIFIED FIRST-YEAR WAGES.—The term “qualified first-year wages” means, with respect to any individual, qualified wages attributable to service rendered during the 1-year period beginning with the day the individual begins work for the employer.

(3) LIMITATION ON WAGES PER YEAR TAKEN INTO ACCOUNT.—The amount of the qualified first-year wages which may be taken into account with respect to any individual shall not exceed \$6,000 per year (\$12,000 per year in the case of any individual who is a qualified veteran by reason of subsection (d)(3)(A)(ii)(I), \$14,000 per year in the case of any individual who is a qualified veteran by reason of subsection (d)(3)(A)(iv), and \$24,000 per year in the case of any individual who is a qualified veteran by reason of subsection (d)(3)(A)(ii)(II)).

(c) WAGES DEFINED.—For purposes of this subpart—

(1) IN GENERAL.—Except as otherwise provided in this subsection and subsection (h)(2), the term “wages” has the meaning given to such term by subsection (b) of section 3306 (determined without regard to any dollar limitation contained in such section).

## (2) ON-THE-JOB TRAINING AND WORK SUPPLEMENTATION PAYMENTS.—

(A) EXCLUSION FOR EMPLOYERS RECEIVING ON-THE-JOB TRAINING PAYMENTS.—The term “wages” shall not include any amounts paid or incurred by an employer for any period to any individual for whom the employer receives federally funded payments for on-the-job training of such individual for such period.

(B) REDUCTION FOR WORK SUPPLEMENTATION PAYMENTS TO EMPLOYERS.—The amount of wages which would (but for this subparagraph) be qualified wages under this section for an employer with respect to an individual for a taxable year shall be reduced by an amount equal to the amount of the payments made to such employer (however utilized by such employer) with respect to such individual for such taxable year under a program established under section 482(e) of the Social Security Act.

## (3) PAYMENTS FOR SERVICES DURING LABOR DISPUTES.—If—

(A) the principal place of employment of an individual with the employer is at a plant or facility, and

(B) there is a strike or lockout involving employees at such plant or facility,  
the term “wages” shall not include any amount paid or incurred by the employer to such individual for services which are the same as, or substantially similar to, those services performed by employees participating in, or affected by, the strike or lockout during the period of such strike or lockout.

(4) TERMINATION.—The term “wages” shall not include any amount paid or incurred to an individual who begins work for the employer after December 31, 2019.

(5) COORDINATION WITH PAYROLL TAX FORGIVENESS.—The term “wages” shall not include any amount paid or incurred to a qualified individual (as defined in section 3111(d)(3)) during the 1-year period beginning on the hiring date of such individual by a qualified employer (as defined in section 3111(d)) unless such qualified employer makes an election not to have section 3111(d) apply.

## (d) MEMBERS OF TARGETED GROUPS.—For purposes of this subpart—

(1) IN GENERAL.—An individual is a member of a targeted group if such individual is—

- (A) a qualified IV-A recipient,
- (B) a qualified veteran,
- (C) a qualified ex-felon,
- (D) a designated community resident,
- (E) a vocational rehabilitation referral,
- (F) a qualified summer youth employee,
- (G) a qualified supplemental nutrition assistance program benefits recipient,
- (H) a qualified SSI recipient,
- (I) a long-term family assistance recipient, or
- (J) a qualified long-term unemployment recipient.

## (2) QUALIFIED IV-A RECIPIENT.—

(A) IN GENERAL.—The term “qualified IV-A recipient” means any individual who is certified by the designated

local agency as being a member of a family receiving assistance under a IV-A program for any 9 months during the 18-month period ending on the hiring date.

(B) IV-A PROGRAM.—For purposes of this paragraph, the term “IV-A program” means any program providing assistance under a State program funded under part A of title IV of the Social Security Act and any successor of such program.

(3) QUALIFIED VETERAN.—

(A) IN GENERAL.—The term “qualified veteran” means any veteran who is certified by the designated local agency as—

(i) being a member of a family receiving assistance under a supplemental nutrition assistance program under the Food and Nutrition Act of 2008 for at least a 3-month period ending during the 12-month period ending on the hiring date,

(ii) entitled to compensation for a service-connected disability, and—

(I) having a hiring date which is not more than 1 year after having been discharged or released from active duty in the Armed Forces of the United States, or

(II) having aggregate periods of unemployment during the 1-year period ending on the hiring date which equal or exceed 6 months,

(iii) having aggregate periods of unemployment during the 1-year period ending on the hiring date which equal or exceed 4 weeks (but less than 6 months), or

(iv) having aggregate periods of unemployment during the 1-year period ending on the hiring date which equal or exceed 6 months.

(B) VETERAN.—For purposes of subparagraph (A), the term “veteran” means any individual who is certified by the designated local agency as—

(i)

(I) having served on active duty (other than active duty for training) in the Armed Forces of the United States for a period of more than 180 days, or

(II) having been discharged or released from active duty in the Armed Forces of the United States for a service-connected disability, and

(ii) not having any day during the 60-day period ending on the hiring date which was a day of extended active duty in the Armed Forces of the United States.

For purposes of clause (ii), the term “extended active duty” means a period of more than 90 days during which the individual was on active duty (other than active duty for training).

(C) OTHER DEFINITIONS.—For purposes of subparagraph (A), the terms “compensation” and “service-connected” have the meanings given such terms under section 101 of title 38, United States Code.

(4) **QUALIFIED EX-FELON.**—The term “qualified ex-felon” means any individual who is certified by the designated local agency—

(A) as having been convicted of a felony under any statute of the United States or any State, and

(B) as having a hiring date which is not more than 1 year after the last date on which such individual was so convicted or was released from prison.

(5) **DESIGNATED COMMUNITY RESIDENTS.**—

(A) **IN GENERAL.**—The term “designated community resident” means any individual who is certified by the designated local agency—

(i) as having attained age 18 but not age 40 on the hiring date, and

(ii) as having his principal place of abode within an empowerment zone, enterprise community, renewal community, or rural renewal county.

(B) **INDIVIDUAL MUST CONTINUE TO RESIDE IN ZONE, COMMUNITY, OR COUNTY.**—In the case of a designated community resident, the term “qualified wages” shall not include wages paid or incurred for services performed while the individual’s principal place of abode is outside an empowerment zone, enterprise community, renewal community, or rural renewal county.

(C) **RURAL RENEWAL COUNTY.**—For purposes of this paragraph, the term “rural renewal county” means any county which—

(i) is outside a metropolitan statistical area (defined as such by the Office of Management and Budget), and

(ii) during the 5-year periods 1990 through 1994 and 1995 through 1999 had a net population loss.

(6) **VOCATIONAL REHABILITATION REFERRAL.**—The term “vocational rehabilitation referral” means any individual who is certified by the designated local agency as—

(A) having a physical or mental disability which, for such individual, constitutes or results in a substantial handicap to employment, and

(B) having been referred to the employer upon completion of (or while receiving) rehabilitative services pursuant to—

(i) an individualized written plan for employment under a State plan for vocational rehabilitation services approved under the Rehabilitation Act of 1973,

(ii) a program of vocational rehabilitation carried out under chapter 31 of title 38, United States Code, or

(iii) an individual work plan developed and implemented by an employment network pursuant to subsection (g) of section 1148 of the Social Security Act with respect to which the requirements of such subsection are met.

(7) **QUALIFIED SUMMER YOUTH EMPLOYEE.**—

(A) **IN GENERAL.**—The term “qualified summer youth employee” means any individual—

(i) who performs services for the employer between May 1 and September 15,

(ii) who is certified by the designated local agency as having attained age 16 but not 18 on the hiring date (or if later, on May 1 of the calendar year involved),

(iii) who has not been an employee of the employer during any period prior to the 90-day period described in subparagraph (B)(i), and

(iv) who is certified by the designated local agency as having his principal place of abode within an empowerment zone, enterprise community, or renewal community.

(B) SPECIAL RULES FOR DETERMINING AMOUNT OF CREDIT.—For purposes of applying this subpart to wages paid or incurred to any qualified summer youth employee—

(i) subsection (b)(2) shall be applied by substituting “any 90-day period between May 1 and September 15” for “the 1-year period beginning with the day the individual begins work for the employer”, and

(ii) subsection (b)(3) shall be applied by substituting “\$3,000” for “\$6,000”.

The preceding sentence shall not apply to an individual who, with respect to the same employer, is certified as a member of another targeted group after such individual has been a qualified summer youth employee.

(C) YOUTH MUST CONTINUE TO RESIDE IN ZONE OR COMMUNITY.—Paragraph (5)(B) shall apply for purposes of subparagraph (A)(iv).

(8) QUALIFIED SUPPLEMENTAL NUTRITION ASSISTANCE PROGRAM BENEFITS RECIPIENT.—

(A) IN GENERAL.—The term “qualified supplemental nutrition assistance program benefits recipient” means any individual who is certified by the designated local agency—

(i) as having attained age 18 but not age 40 on the hiring date, and

(ii) as being a member of a family—

(I) receiving assistance under a supplemental nutrition assistance program under the Food and Nutrition Act of 2008 for the 6-month period ending on the hiring date, or

(II) receiving such assistance for at least 3 months of the 5-month period ending on the hiring date, in the case of a member of a family who ceases to be eligible for such assistance under section 6(o) of the Food and Nutrition Act of 2008.

(B) PARTICIPATION INFORMATION.—Notwithstanding any other provision of law, the Secretary of the Treasury and the Secretary of Agriculture shall enter into an agreement to provide information to designated local agencies with respect to participation in the supplemental nutrition assistance program.

(9) QUALIFIED SSI RECIPIENT.—The term “qualified SSI recipient” means any individual who is certified by the designated local agency as receiving supplemental security income benefits under title XVI of the Social Security Act (including

supplemental security income benefits of the type described in section 1616 of such Act or section 212 of Public Law 93-66) for any month ending within the 60-day period ending on the hiring date.

(10) LONG-TERM FAMILY ASSISTANCE RECIPIENT.—The term “long-term family assistance recipient” means any individual who is certified by the designated local agency—

(A) as being a member of a family receiving assistance under a IV-A program (as defined in paragraph (2)(B)) for at least the 18-month period ending on the hiring date,

(B)(i) as being a member of a family receiving such assistance for 18 months beginning after August 5, 1997, and

(ii) as having a hiring date which is not more than 2 years after the end of the earliest such 18-month period, or

(C)(i) as being a member of a family which ceased to be eligible for such assistance by reason of any limitation imposed by Federal or State law on the maximum period such assistance is payable to a family, and

(ii) as having a hiring date which is not more than 2 years after the date of such cessation.

(11) HIRING DATE.—The term “hiring date” means the day the individual is hired by the employer.

(12) DESIGNATED LOCAL AGENCY.—The term “designated local agency” means a State employment security agency established in accordance with the Act of June 6, 1933, as amended (29 U.S.C. 49-49n).

(13) SPECIAL RULES FOR CERTIFICATIONS.—

(A) IN GENERAL.—An individual shall not be treated as a member of a targeted group unless—

(i) on or before the day on which such individual begins work for the employer, the employer has received a certification from a designated local agency that such individual is a member of a targeted group, or

(ii)(I) on or before the day the individual is offered employment with the employer, a pre-screening notice is completed by the employer with respect to such individual, and

(II) not later than the 28th day after the individual begins work for the employer, the employer submits such notice, signed by the employer and the individual under penalties of perjury, to the designated local agency as part of a written request for such a certification from such agency.

For purposes of this paragraph, the term “pre-screening notice” means a document (in such form as the Secretary shall prescribe) which contains information provided by the individual on the basis of which the employer believes that the individual is a member of a targeted group.

(B) INCORRECT CERTIFICATIONS.—If—

(i) an individual has been certified by a designated local agency as a member of a targeted group, and

(ii) such certification is incorrect because it was based on false information provided by such individual, the certification shall be revoked and wages

paid by the employer after the date on which notice of revocation is received by the employer shall not be treated as qualified wages.

(C) EXPLANATION OF DENIAL OF REQUEST.—If a designated local agency denies a request for certification of membership in a targeted group, such agency shall provide to the person making such request a written explanation of the reasons for such denial.

(D) CREDIT FOR UNEMPLOYED VETERANS.—

(i) IN GENERAL.—Notwithstanding subparagraph (A), for purposes of paragraph (3)(A)—

(I) a veteran will be treated as certified by the designated local agency as having aggregate periods of unemployment meeting the requirements of clause (ii)(II) or (iv) of such paragraph (whichever is applicable) if such veteran is certified by such agency as being in receipt of unemployment compensation under State or Federal law for not less than 6 months during the 1-year period ending on the hiring date, and

(II) a veteran will be treated as certified by the designated local agency as having aggregate periods of unemployment meeting the requirements of clause (iii) of such paragraph if such veteran is certified by such agency as being in receipt of unemployment compensation under State or Federal law for not less than 4 weeks (but less than 6 months) during the 1-year period ending on the hiring date.

(ii) REGULATORY AUTHORITY.—The Secretary may provide alternative methods for certification of a veteran as a qualified veteran described in clause (ii)(II), (iii), or (iv) of paragraph (3)(A), at the Secretary's discretion.

(14) CREDIT ALLOWED FOR UNEMPLOYED VETERANS AND DISCONNECTED YOUTH HIRED IN 2009 OR 2010.—

(A) IN GENERAL.—Any unemployed veteran or disconnected youth who begins work for the employer during 2009 or 2010 shall be treated as a member of a targeted group for purposes of this subpart.

(B) DEFINITIONS.—For purposes of this paragraph—

(i) UNEMPLOYED VETERAN.—The term “unemployed veteran” means any veteran (as defined in paragraph (3)(B), determined without regard to clause (ii) thereof) who is certified by the designated local agency as—

(I) having been discharged or released from active duty in the Armed Forces at any time during the 5-year period ending on the hiring date, and

(II) being in receipt of unemployment compensation under State or Federal law for not less than 4 weeks during the 1-year period ending on the hiring date.

(ii) DISCONNECTED YOUTH.—The term “disconnected youth” means any individual who is certified by the designated local agency—



(I) as having attained age 16 but not age 25 on the hiring date,

(II) as not regularly attending any secondary, technical, or post-secondary school during the 6-month period preceding the hiring date,

(III) as not regularly employed during such 6-month period, and

(IV) as not readily employable by reason of lacking a sufficient number of basic skills.

(15) QUALIFIED LONG-TERM UNEMPLOYMENT RECIPIENT.—The term “qualified long-term unemployment recipient” means any individual who is certified by the designated local agency as being in a period of unemployment which—

(A) is not less than 27 consecutive weeks, and

(B) includes a period in which the individual was receiving unemployment compensation under State or Federal law.

(e) CREDIT FOR SECOND-YEAR WAGES FOR EMPLOYMENT OF LONG-TERM FAMILY ASSISTANCE RECIPIENTS.—

(1) IN GENERAL.—With respect to the employment of a long-term family assistance recipient—

(A) the amount of the work opportunity credit determined under this section for the taxable year shall include 50 percent of the qualified second-year wages for such year, and

(B) in lieu of applying subsection (b)(3), the amount of the qualified first-year wages, and the amount of qualified second-year wages, which may be taken into account with respect to such a recipient shall not exceed \$10,000 per year.

(2) QUALIFIED SECOND-YEAR WAGES.—For purposes of this subsection, the term “qualified second-year wages” means qualified wages—

(A) which are paid to a long-term family assistance recipient, and

(B) which are attributable to service rendered during the 1-year period beginning on the day after the last day of the 1-year period with respect to such recipient determined under subsection (b)(2).

(3) SPECIAL RULES FOR AGRICULTURAL AND RAILWAY LABOR.—If such recipient is an employee to whom subparagraph (A) or (B) of subsection (h)(1) applies, rules similar to the rules of such subparagraphs shall apply except that—

(A) such subparagraph (A) shall be applied by substituting “\$10,000” for “\$6,000”, and

(B) such subparagraph (B) shall be applied by substituting “\$833.33” for “\$500”.

(f) REMUNERATION MUST BE FOR TRADE OR BUSINESS EMPLOYMENT.—

(1) IN GENERAL.—For purposes of this subpart, remuneration paid by an employer to an employee during any taxable year shall be taken into account only if more than one-half of the remuneration so paid is for services performed in a trade or business of the employer.

(2) SPECIAL RULE FOR CERTAIN DETERMINATION.—Any determination as to whether paragraph (1), or subparagraph (A) or (B) of subsection (h)(1), applies with respect to any employee for any taxable year shall be made without regard to subsections (a) and (b) of section 52.

(g) UNITED STATES EMPLOYMENT SERVICE TO NOTIFY EMPLOYERS OF AVAILABILITY OF CREDIT.—The United States Employment Service, in consultation with the Internal Revenue Service, shall take such steps as may be necessary or appropriate to keep employers apprised of the availability of the work opportunity credit determined under this subpart.

(h) SPECIAL RULES FOR AGRICULTURAL LABOR AND RAILWAY LABOR.—For purposes of this subpart—

(1) UNEMPLOYMENT INSURANCE WAGES.—

(A) AGRICULTURAL LABOR.—If the services performed by any employee for an employer during more than one-half of any pay period (within the meaning of section 3306(d)) taken into account with respect to any year constitute agricultural labor (within the meaning of section 3306(k)), the term “unemployment insurance wages” means, with respect to the remuneration paid by the employer to such employee for such year, an amount equal to so much of such remuneration as constitutes “wages” within the meaning of section 3121(a), except that the contribution and benefit base for each calendar year shall be deemed to be \$6,000.

(B) RAILWAY LABOR.—If more than one-half of remuneration paid by an employer to an employee during any year is remuneration for service described in section 3306(c)(9), the term “unemployment insurance wages” means, with respect to such employee for such year, an amount equal to so much of the remuneration paid to such employee during such year which would be subject to contributions under section 8(a) of the Railroad Unemployment Insurance Act (45 USC Sec. 358(a)) if the maximum amount subject to such contributions were \$500 per month.

(2) WAGES.—In any case to which subparagraph (A) or (B) of paragraph (1) applies, the term “wages” means unemployment insurance wages (determined without regard to any dollar limitation).

(i) CERTAIN INDIVIDUALS INELIGIBLE.—

(1) RELATED INDIVIDUALS.—No wages shall be taken into account under subsection (a) with respect to an individual who—

(A) bears any of the relationships described in subparagraphs (A) through (G) of [section 152(d)(2)] *section 7706(d)(2)* to the taxpayer, or, if the taxpayer is a corporation, to an individual who owns, directly or indirectly, more than 50 percent in value of the outstanding stock of the corporation, or, if the taxpayer is an entity other than a corporation, to any individual who owns, directly or indirectly, more than 50 percent of the capital and profits interests in the entity (determined with the application of section 267(c)),

(B) if the taxpayer is an estate or trust, is a grantor, beneficiary, or fiduciary of the estate or trust, or is an indi-

vidual who bears any of the relationships described in subparagraphs (A) through (G) of **[section 152(d)(2)]** *section 7706(d)(2)* to a grantor, beneficiary, or fiduciary of the estate or trust, or

(C) is a dependent (described in **[section 152(d)(2)(H)]** *section 7706(d)(2)(H)*) of the taxpayer, or, if the taxpayer is a corporation, of an individual described in subparagraph (A), or, if the taxpayer is an estate or trust, of a grantor, beneficiary, or fiduciary of the estate or trust.

(2) **NONQUALIFYING REHIRES.**—No wages shall be taken into account under subsection (a) with respect to any individual if, prior to the hiring date of such individual, such individual had been employed by the employer at any time.

(3) **INDIVIDUALS NOT MEETING MINIMUM EMPLOYMENT PERIOD.**—

(A) **REDUCTION OF CREDIT FOR INDIVIDUALS PERFORMING FEWER THAN 400 HOURS OF SERVICE.**—In the case of an individual who has performed at least 120 hours, but less than 400 hours, of service for the employer, subsection (a) shall be applied by substituting “25 percent” for “40 percent”.

(B) **DENIAL OF CREDIT FOR INDIVIDUALS PERFORMING FEWER THAN 120 HOURS OF SERVICE.**—No wages shall be taken into account under subsection (a) with respect to any individual unless such individual has performed at least 120 hours of service for the employer.

(j) **ELECTION TO HAVE WORK OPPORTUNITY CREDIT NOT APPLY.**—

(1) **IN GENERAL.**—A taxpayer may elect to have this section not apply for any taxable year.

(2) **TIME FOR MAKING ELECTION.**—An election under paragraph (1) for any taxable year may be made (or revoked) at any time before the expiration of the 3-year period beginning on the last date prescribed by law for filing the return for such taxable year (determined without regard to extensions)

(3) **MANNER OF MAKING ELECTION.**—An election under paragraph (1) (or revocation thereof) shall be made in such manner as the Secretary may by regulations prescribe.

(k) **TREATMENT OF SUCCESSOR EMPLOYERS; TREATMENT OF EMPLOYEES PERFORMING SERVICES FOR OTHER PERSONS.**—

(1) **TREATMENT OF SUCCESSOR EMPLOYERS.**—Under regulations prescribed by the Secretary, in the case of a successor employer referred to in section 3306(b)(1), the determination of the amount of the credit under this section with respect to wages paid by such successor employer shall be made in the same manner as if such wages were paid by the predecessor employer referred to in such section.

(2) **TREATMENT OF EMPLOYEES PERFORMING SERVICES FOR OTHER PERSONS.**—No credit shall be determined under this section with respect to remuneration paid by an employer to an employee for services performed by such employee for another person unless the amount reasonably expected to be received by the employer for such services from such other person exceeds the remuneration paid by the employer to such employee for such services.

\* \* \* \* \*

**PART VI—ALTERNATIVE MINIMUM TAX**

\* \* \* \* \*

**SEC. 55. ALTERNATIVE MINIMUM TAX IMPOSED.**

(a) **GENERAL RULE.**—In the case of a taxpayer other than a corporation, there is hereby imposed (in addition to any other tax imposed by this subtitle) a tax equal to the excess (if any) of—

- (1) the tentative minimum tax for the taxable year, over
- (2) the regular tax for the taxable year.

(b) **TENTATIVE MINIMUM TAX.**—For purposes of this part—

(1) **AMOUNT OF TENTATIVE TAX.**—

(A) **IN GENERAL.**—The tentative minimum tax for the taxable year is the sum of—

- (i) 26 percent of so much of the taxable excess as does not exceed \$175,000, plus
- (ii) 28 percent of so much of the taxable excess as exceeds \$175,000.

The amount determined under the preceding sentence shall be reduced by the alternative minimum tax foreign tax credit for the taxable year.

(B) **TAXABLE EXCESS.**—For purposes of this subsection, the term “taxable excess” means so much of the alternative minimum taxable income for the taxable year as exceeds the exemption amount.

(C) **MARRIED INDIVIDUAL FILING SEPARATE RETURN.**—In the case of a married individual filing a separate return, subparagraph (A) shall be applied by substituting 50 percent of the dollar amount otherwise applicable under clause (i) and clause (ii) thereof. For purposes of the preceding sentence, marital status shall be determined under section 7703.

(2) **ALTERNATIVE MINIMUM TAXABLE INCOME.**—The term “alternative minimum taxable income” means the taxable income of the taxpayer for the taxable year—

(A) determined with the adjustments provided in section 56 and section 58, and

(B) increased by the amount of the items of tax preference described in section 57.

If a taxpayer is subject to the regular tax, such taxpayer shall be subject to the tax imposed by this section (and, if the regular tax is determined by reference to an amount other than taxable income, such amount shall be treated as the taxable income of such taxpayer for purposes of the preceding sentence).

(3) **MAXIMUM RATE OF TAX ON NET CAPITAL GAIN OF NONCORPORATE TAXPAYERS.**—The amount determined under the first sentence of paragraph (1)(A) shall not exceed the sum of—

(A) the amount determined under such first sentence computed at the rates and in the same manner as if this paragraph had not been enacted on the taxable excess reduced by the lesser of—

- (i) the net capital gain; or
- (ii) the sum of—

(I) the adjusted net capital gain, plus

(II) the unrecaptured section 1250 gain, plus

(B) 0 percent of so much of the adjusted net capital gain (or, if less, taxable excess) as does not exceed an amount equal to the excess described in section 1(h)(1)(B), plus

(C) 15 percent of the lesser of—

(i) so much of the adjusted net capital gain (or, if less, taxable excess) as exceeds the amount on which tax is determined under subparagraph (B), or

(ii) the excess described in section 1(h)(1)(C)(ii), plus

(D) 20 percent of the adjusted net capital gain (or, if less, taxable excess) in excess of the sum of the amounts on which tax is determined under subparagraphs (B) and (C), plus

(E) 25 percent of the amount of taxable excess in excess of the sum of the amounts on which tax is determined under the preceding subparagraphs of this paragraph.

Terms used in this paragraph which are also used in section 1(h) shall have the respective meanings given such terms by section 1(h) but computed with the adjustments under this part.

(c) REGULAR TAX.—

(1) IN GENERAL.—For purposes of this section, the term “regular tax” means the regular tax liability for the taxable year (as defined in section 26(b)) reduced by the foreign tax credit allowable under section 27(a). Such term shall not include any increase in tax under section 45(e)(11)(C), 49(b) or 50(a) or subsection (j) or (k) of section 42.

(2) COORDINATION WITH INCOME AVERAGING FOR FARMERS AND FISHERMEN.—Solely for purposes of this section, section 1301 (relating to averaging of farm and fishing income) shall not apply in computing the regular tax liability.

(3) CROSS REFERENCES.—For provisions providing that certain credits are not allowable against the tax imposed by this section, see sections 30C(d)(2) and 38(c).

(d) EXEMPTION AMOUNT.—For purposes of this section—

(1) EXEMPTION AMOUNT FOR TAXPAYERS OTHER THAN CORPORATIONS.—In the case of a taxpayer other than a corporation, the term “exemption amount” means—

(A) ~~【\$78,750】~~ *\$109,400* in the case of—

(i) a joint return, or

(ii) a surviving spouse,

(B) ~~【\$50,600】~~ *\$70,300* in the case of an individual who—

(i) is not a married individual, and

(ii) is not a surviving spouse,

(C) 50 percent of the dollar amount applicable under subparagraph (A) in the case of a married individual who files a separate return, and

(D) *\$22,500* in the case of an estate or trust.

For purposes of this paragraph, the term “surviving spouse” has the meaning given to such term by section 2(a), and marital status shall be determined under section 7703.

(2) PHASE-OUT OF EXEMPTION AMOUNT.—The exemption amount of any taxpayer shall be reduced (but not below zero) by an amount equal to 25 percent of the amount by which the alternative minimum taxable income of the taxpayer exceeds—

(A) **[\$150,000]** *\$1,000,000* in the case of a taxpayer described in paragraph (1)(A),

**[(B)** \$112,500 in the case of a taxpayer described in paragraph (1)(B), and

**[(C)** 50 percent of the dollar amount applicable under subparagraph (A) in the case of a taxpayer described in subparagraph (C) or (D) of paragraph (1).**]**

*(B) 50 percent of the dollar amount applicable under subparagraph (A) in the case of a taxpayer described in paragraph (1)(B) or (1)(C), and*

*(C) \$75,000 in the case of a taxpayer described in paragraph (1)(D).*

In the case of a taxpayer described in paragraph (1)(C), alternative minimum taxable income shall be increased by the lesser of (i) 25 percent of the excess of alternative minimum taxable income (determined without regard to this sentence) over the minimum amount of such income (as so determined) for which the exemption amount under paragraph (1)(C) is zero, or (ii) such exemption amount (determined without regard to this paragraph).

**[(3) INFLATION ADJUSTMENT.—**

**[(A) IN GENERAL.—**In the case of any taxable year beginning in a calendar year after 2012, the amounts described in subparagraph (B) shall each be increased by an amount equal to—

**[(i)** such dollar amount, multiplied by

**[(ii)** the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2011” for “calendar year 2016” in subparagraph (A)(ii) thereof.

**[(B) AMOUNTS DESCRIBED.—**The amounts described in this subparagraph are—

**[(i)** each of the dollar amounts contained in subsection (b)(1)(A),

**[(ii)** each of the dollar amounts contained in subparagraphs (A), (B), and (D) of paragraph (1), and

**[(iii)** each of the dollar amounts in subparagraphs (A) and (B) of paragraph (2).

**[(C) ROUNDING.—**Any increased amount determined under subparagraph (A) shall be rounded to the nearest multiple of \$100.

**[(4) SPECIAL RULE FOR TAXABLE YEARS BEGINNING AFTER 2017 AND BEFORE 2026.—**

**[(A) IN GENERAL.—**In the case of any taxable year beginning after December 31, 2017, and before January 1, 2026—

**[(i)** paragraph (1) shall be applied—

**[(I)** by substituting “\$109,400” for “\$78,750” in subparagraph (A), and

**[(II)** by substituting “\$70,300” for “\$50,600” in subparagraph (B), and

**[(ii)** paragraph (2) shall be applied—

**[(I)** by substituting “\$1,000,000” for “\$150,000” in subparagraph (A),

[(II) by substituting “50 percent of the dollar amount applicable under subparagraph (A)” for “\$112,500” in subparagraph (B), and

[(III) in the case of a taxpayer described in paragraph (1)(D), without regard to the substitution under subclause (I).

**[(B) INFLATION ADJUSTMENT.—**

[(i) IN GENERAL.—In the case of any taxable year beginning in a calendar year after 2018, the amounts described in clause (ii) shall each be increased by an amount equal to—

[(I) such dollar amount, multiplied by

[(II) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2017” for “calendar year 2016” in subparagraph (A)(ii) thereof.

[(ii) AMOUNTS DESCRIBED.—The amounts described in this clause are the \$109,400 amount in subparagraph (A)(i)(I), the \$70,300 amount in subparagraph (A)(i)(II), and the \$1,000,000 amount in subparagraph (A)(ii)(I).

[(iii) ROUNDING.—Any increased amount determined under clause (i) shall be rounded to the nearest multiple of \$100.

[(iv) COORDINATION WITH CURRENT ADJUSTMENTS.—In the case of any taxable year to which subparagraph (A) applies, no adjustment shall be made under paragraph (3) to any of the numbers which are substituted under subparagraph (A) and adjusted under this subparagraph.]

*(3) INFLATION ADJUSTMENT.—In the case of any taxable year beginning in a calendar year after 2018, each dollar amount described in clause (i) or (ii) of subparagraph (B) shall be increased by an amount equal to—*

*(A) such dollar amount, multiplied by*

*(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting—*

*(i) in the case of a dollar amount contained in paragraph (1)(D) or (2)(C) or in subsection (b)(1)(A), “calendar year 2011” for “calendar year 2016” in subparagraph (A)(ii) thereof, and*

*(ii) in the case of a dollar amount contained in paragraph (1)(A), (1)(B), or (2)(A), “calendar year 2017” for “calendar year 2016” in subparagraph (A)(ii) thereof.*

*Any increased amount determined under this paragraph shall be rounded to the nearest multiple of \$100 (\$50 in the case of the dollar amount contained in paragraph (2)(C)).*

**SEC. 56. ADJUSTMENTS IN COMPUTING ALTERNATIVE MINIMUM TAXABLE INCOME.**

(a) **ADJUSTMENTS APPLICABLE TO ALL TAXPAYERS.—**In determining the amount of the alternative minimum taxable income for any taxable year the following treatment shall apply (in lieu of the treatment applicable for purposes of computing the regular tax):

## (1) DEPRECIATION.—

## (A) IN GENERAL.—

(i) PROPERTY OTHER THAN CERTAIN PERSONAL PROPERTY.—Except as provided in clause (ii), the depreciation deduction allowable under section 167 with respect to any tangible property placed in service after December 31, 1986, shall be determined under the alternative system of section 168(g). In the case of property placed in service after December 31, 1998, the preceding sentence shall not apply but clause (ii) shall continue to apply.

(ii) 150-PERCENT DECLINING BALANCE METHOD FOR CERTAIN PROPERTY.—The method of depreciation used shall be—

(I) the 150 percent declining balance method,

(II) switching to the straight line method for the 1st taxable year for which using the straight line method with respect to the adjusted basis as of the beginning of the year will yield a higher allowance.

The preceding sentence shall not apply to any section 1250 property (as defined in section 1250(c)) (and the straight line method shall be used for such section 1250 property) or to any other property if the depreciation deduction determined under section 168 with respect to such other property for purposes of the regular tax is determined by using the straight line method.

(B) EXCEPTION FOR CERTAIN PROPERTY.—This paragraph shall not apply to property described in paragraph (1), (2), (3), or (4) of section 168(f), or in section 168(e)(3)(C)(iv).

## (C) COORDINATION WITH TRANSITIONAL RULES.—

(i) IN GENERAL.—This paragraph shall not apply to property placed in service after December 31, 1986, to which the amendments made by section 201 of the Tax Reform Act of 1986 do not apply by reason of section 203, 204, or 251(d) of such Act.

(ii) TREATMENT OF CERTAIN PROPERTY PLACED IN SERVICE BEFORE 1987.—This paragraph shall apply to any property to which the amendments made by section 201 of the Tax Reform Act of 1986 apply by reason of an election under section 203(a)(1)(B) of such Act without regard to the requirement of subparagraph (A) that the property be placed in service after December 31, 1986.

(D) NORMALIZATION RULES.—With respect to public utility property described in section 168(i)(10), the Secretary shall prescribe the requirements of a normalization method of accounting for this section.

## (2) MINING EXPLORATION AND DEVELOPMENT COSTS.—

(A) IN GENERAL.—With respect to each mine or other natural deposit (other than an oil, gas, or geothermal well) of the taxpayer, the amount allowable as a deduction under section 616(a) or 617(a) (determined without regard to section 291(b)) in computing the regular tax for costs



paid or incurred after December 31, 1986, shall be capitalized and amortized ratably over the 10-year period beginning with the taxable year in which the expenditures were made.

(B) LOSS ALLOWED.—If a loss is sustained with respect to any property described in subparagraph (A), a deduction shall be allowed for the expenditures described in subparagraph (A) for the taxable year in which such loss is sustained in an amount equal to the lesser of—

(i) the amount allowable under section 165(a) for the expenditures if they had remained capitalized, or

(ii) the amount of such expenditures which have not previously been amortized under subparagraph (A).

(3) TREATMENT OF CERTAIN LONG-TERM CONTRACTS.—In the case of any long-term contract entered into by the taxpayer on or after March 1, 1986, the taxable income from such contract shall be determined under the percentage of completion method of accounting (as modified by section 460(b)). For purposes of the preceding sentence, in the case of a contract described in section 460(e)(1), the percentage of the contract completed shall be determined under section 460(b)(1) by using the simplified procedures for allocation of costs prescribed under section 460(b)(3). The first sentence of this paragraph shall not apply to any home construction contract (as defined in section 460(e)(6)).

(4) ALTERNATIVE TAX NET OPERATING LOSS DEDUCTION.—The alternative tax net operating loss deduction shall be allowed in lieu of the net operating loss deduction allowed under section 172.

(5) POLLUTION CONTROL FACILITIES.—In the case of any certified pollution control facility placed in service after December 31, 1986, the deduction allowable under section 169 (without regard to section 291) shall be determined under the alternative system of section 168(g). In the case of such a facility placed in service after December 31, 1998, such deduction shall be determined under section 168 using the straight line method.

(6) ADJUSTED BASIS.—The adjusted basis of any property to which paragraph (1) or (5) applies (or with respect to which there are any expenditures to which paragraph (2) or subsection (b)(2) applies) shall be determined on the basis of the treatment prescribed in paragraph (1), (2), or (5), or subsection (b)(2), whichever applies.

(7) SECTION 87 NOT APPLICABLE.—Section 87 (relating to alcohol fuel credit) shall not apply.

(b) ADJUSTMENTS APPLICABLE TO INDIVIDUALS.—In determining the amount of the alternative minimum taxable income of any taxpayer (other than a corporation), the following treatment shall apply (in lieu of the treatment applicable for purposes of computing the regular tax):

(1) LIMITATION ON DEDUCTIONS.—

[(A) IN GENERAL.—No deduction shall be allowed—

[(i) for any miscellaneous itemized deduction (as defined in section 67(b)), or

[(ii) for any taxes described in paragraph (1), (2), or (3) of section 164(a) or clause (ii) of section 164(b)(5)(A).

Clause (ii) shall not apply to any amount allowable in computing adjusted gross income.

**[(B) MEDICAL EXPENSES.—**In determining the amount allowable as a deduction under section 213, subsection (a) of section 213 shall be applied without regard to subsection (f) of such section. This subparagraph shall not apply to taxable years beginning after December 31, 2016, and ending before January 1, 2019]

*(A) CERTAIN TAXES.—No deduction (other than a deduction allowable in computing adjusted gross income) shall be allowed for any taxes described in paragraph (1), (2), or (3) of section 164(a) or clause (ii) of section 164(b)(5)(A).*

**[(C)] (B) INTEREST.—**In determining the amount allowable as a deduction for interest, subsections (d) and (h) of section 163 shall apply, except that—

(i) in lieu of the exception under section 163(h)(2)(D), the term “personal interest” shall not include any qualified housing interest (as defined in subsection (e)),

(ii) interest on any specified private activity bond (and any amount treated as interest on a specified private activity bond under section 57(a)(5)(B)), and any deduction referred to in section 57(a)(5)(A), shall be treated as includible in gross income (or as deductible) for purposes of applying section 163(d),

(iii) in lieu of the exception under section 163(d)(3)(B)(i), the term “investment interest” shall not include any qualified housing interest (as defined in subsection (e)), and

(iv) the adjustments of this section and sections 57 and 58 shall apply in determining net investment income under section 163(d).

**[(D)] (C) TREATMENT OF CERTAIN RECOVERIES.—**No recovery of any tax to which [subparagraph (A)(ii)] *subparagraph (A)* applied shall be included in gross income for purposes of determining alternative minimum taxable income.

**[(E)] (D) STANDARD DEDUCTION [AND DEDUCTION FOR PERSONAL EXEMPTIONS] NOT ALLOWED.—**The standard deduction under section 63(c)[, the deduction for personal exemptions under section 151,] and the deduction under section 642(b) shall not be allowed.

**[(F) SECTION 68 NOT APPLICABLE.—**Section 68 shall not apply.]

**(2) CIRCULATION AND RESEARCH AND EXPERIMENTAL EXPENDITURES.—**

**(A) IN GENERAL.—**The amount allowable as a deduction under section 173 or 174(a) in computing the regular tax for amounts paid or incurred after December 31, 1986, shall be capitalized and—

(i) in the case of circulation expenditures described in section 173, shall be amortized ratably over the 3-

year period beginning with the taxable year in which the expenditures were made, or

(ii) in the case of research and experimental expenditures described in section 174(a), shall be amortized ratably over the 10-year period beginning with the taxable year in which the expenditures were made.

(B) LOSS ALLOWED.—If a loss is sustained with respect to any property described in subparagraph (A), a deduction shall be allowed for the expenditures described in subparagraph (A) for the taxable year in which such loss is sustained in an amount equal to the lesser of—

(i) the amount allowable under section 165(a) for the expenditures if they had remained capitalized, or

(ii) the amount of such expenditures which have not previously been amortized under subparagraph (A).

(C) EXCEPTION FOR CERTAIN RESEARCH AND EXPERIMENTAL EXPENDITURES.—If the taxpayer materially participates (within the meaning of section 469(h)) in an activity, this paragraph shall not apply to any amount allowable as a deduction under section 174(a) for expenditures paid or incurred in connection with such activity.

(3) TREATMENT OF INCENTIVE STOCK OPTIONS.—Section 421 shall not apply to the transfer of stock acquired pursuant to the exercise of an incentive stock option (as defined in section 422). Section 422(c)(2) shall apply in any case where the disposition and the inclusion for purposes of this part are within the same taxable year and such section shall not apply in any other case. The adjusted basis of any stock so acquired shall be determined on the basis of the treatment prescribed by this paragraph.

(d) ALTERNATIVE TAX NET OPERATING LOSS DEDUCTION DEFINED.—

(1) IN GENERAL.—For purposes of subsection (a)(4), the term “alternative tax net operating loss deduction” means the net operating loss deduction allowable for the taxable year under section 172, except that—

(A) the amount of such deduction shall not exceed the sum of—

(i) the lesser of—

(I) the amount of such deduction attributable to net operating losses (other than the deduction described in clause (ii)(I)), or

(II) 90 percent of alternative minimum taxable income determined without regard to such deduction and the deduction under section 199, plus

(ii) the lesser of—

(I) the amount of such deduction attributable to an applicable net operating loss with respect to which an election is made under section 172(b)(1)(H) (as in effect before its repeal by the Tax Increase Prevention Act of 2014), or

(II) alternative minimum taxable income determined without regard to such deduction and the deduction under section 199 reduced by the amount determined under clause (i), and

(B) in determining the amount of such deduction—

(i) the net operating loss (within the meaning of section 172(c)) for any loss year shall be adjusted as provided in paragraph (2), and

(ii) appropriate adjustments in the application of section 172(b)(2) shall be made to take into account the limitation of subparagraph (A).

(2) ADJUSTMENTS TO NET OPERATING LOSS COMPUTATION.—

(A) POST-1986 LOSS YEARS.—In the case of a loss year beginning after December 31, 1986, the net operating loss for such year under section 172(c) shall—

(i) be determined with the adjustments provided in this section and section 58, and

(ii) be reduced by the items of tax preference determined under section 57 for such year.

An item of tax preference shall be taken into account under clause (ii) only to the extent such item increased the amount of the net operating loss for the taxable year under section 172(c).

(B) PRE-1987 YEARS.—In the case of loss years beginning before January 1, 1987, the amount of the net operating loss which may be carried over to taxable years beginning after December 31, 1986, for purposes of paragraph (2), shall be equal to the amount which may be carried from the loss year to the first taxable year of the taxpayer beginning after December 31, 1986.

(e) QUALIFIED HOUSING INTEREST.—For purposes of this part—

(1) IN GENERAL.—The term “qualified housing interest” means interest which is qualified residence interest (as defined in section 163(h)(3)) and is paid or accrued during the taxable year on indebtedness which is incurred in acquiring, constructing, or substantially improving any property which—

(A) is the principal residence (within the meaning of section 121) of the taxpayer at the time such interest accrues, or

(B) is a qualified dwelling which is a qualified residence (within the meaning of section 163(h)(4)).

Such term also includes interest on any indebtedness resulting from the refinancing of indebtedness meeting the requirements of the preceding sentence; but only to the extent that the amount of the indebtedness resulting from such refinancing does not exceed the amount of the refinanced indebtedness immediately before the refinancing.

(2) QUALIFIED DWELLING.—The term “qualified dwelling” means any—

- (A) house,
- (B) apartment,
- (C) condominium, or

(D) mobile home not used on a transient basis (within the meaning of section 7701(a)(19)(C)(v)), including all structures or other property appurtenant thereto.

(3) SPECIAL RULE FOR INDEBTEDNESS INCURRED BEFORE JULY 1, 1982.—The term “qualified housing interest” includes interest which is qualified residence interest (as defined in section 163(h)(3)) and is paid or accrued on indebtedness which—

(A) was incurred by the taxpayer before July 1, 1982, and

(B) is secured by property which, at the time such indebtedness was incurred, was—

(i) the principal residence (within the meaning of section 121) of the taxpayer, or

(ii) a qualified dwelling used by the taxpayer (or any member of his family (within the meaning of section 267(c)(4))).

\* \* \* \* \*

**SEC. 58. DENIAL OF CERTAIN LOSSES.**

(a) DENIAL OF FARM LOSS.—

(1) IN GENERAL.—For purposes of computing the amount of the alternative minimum taxable income for any taxable year of a taxpayer other than a corporation—

(A) DISALLOWANCE OF FARM LOSS.—No loss of the taxpayer for such taxable year from any tax shelter farm activity shall be allowed.

(B) DEDUCTION IN SUCCEEDING TAXABLE YEAR.—Any loss from a tax shelter farm activity disallowed under subparagraph (A) shall be treated as a deduction allocable to such activity in the 1st succeeding taxable year.

(2) TAX SHELTER FARM ACTIVITY.—For purposes of this subsection, the term “tax shelter farm activity” means—

(A) any farming syndicate as defined in section [461(k)] 461(j), and

(B) any other activity consisting of farming which is a passive activity (within the meaning of section 469(c)).

(3) DETERMINATION OF LOSS.—In determining the amount of the loss from any tax shelter farm activity, the adjustments of sections 56 and 57 shall apply.

(b) DISALLOWANCE OF PASSIVE ACTIVITY LOSS.—In computing the alternative minimum taxable income of the taxpayer for any taxable year, section 469 shall apply, except that in applying section 469 -

(1) the adjustments of sections 56 and 57 shall apply, and

(2) in lieu of applying section 469(j)(7), the passive activity loss of a taxpayer shall be computed without regard to qualified housing interest (as defined in section 56(e)).

(c) SPECIAL RULES.—For purposes of this section—

(1) SPECIAL RULE FOR INSOLVENT TAXPAYERS.—

(A) IN GENERAL.—The amount of losses to which subsection (a) or (b) applies shall be reduced by the amount (if any) by which the taxpayer is insolvent as of the close of the taxable year.

(B) INSOLVENT.—For purposes of this paragraph, the term “insolvent” means the excess of liabilities over the fair market value of assets.

(2) LOSS ALLOWED FOR YEAR OF DISPOSITION OF FARM SHELTER ACTIVITY.—If the taxpayer disposes of his entire interest in any tax shelter farm activity during any taxable year, the amount of the loss attributable to such activity (determined after carryovers under subsection (a)(1)(B)) shall (to the extent otherwise allowable) be allowed for such taxable year in com-

puting alternative minimum taxable income and not treated as a loss from a tax shelter farm activity.

\* \* \* \* \*

**Subchapter B—Computation of Taxable Income**

PART I—DEFINITION OF GROSS INCOME, ADJUSTED GROSS INCOME, TAXABLE INCOME, ETC

\* \* \* \* \*

【PART V—DEDUCTIONS FOR PERSONAL EXEMPTIONS

\* \* \* \* \*

**PART I—DEFINITION OF GROSS INCOME, ADJUSTED GROSS INCOME, TAXABLE INCOME, ETC**

Sec. 61. Gross income defined.

\* \* \* \* \*

【Sec. 67. 2-percent floor on miscellaneous itemized deductions.】

*Sec. 67. Denial of miscellaneous itemized deductions.*

【Sec. 68. Overall limitation on itemized deductions.】

\* \* \* \* \*

**SEC. 62. ADJUSTED GROSS INCOME DEFINED.**

(a) GENERAL RULE.—For purposes of this [subtitle] *title*, the term “adjusted gross income” means, in the case of an individual, gross income minus the following deductions:

(1) TRADE AND BUSINESS DEDUCTIONS.—The deductions allowed by this chapter (other than by part VII of this subchapter) which are attributable to a trade or business carried on by the taxpayer, if such trade or business does not consist of the performance of services by the taxpayer as an employee.

(2) CERTAIN TRADE AND BUSINESS DEDUCTIONS OF EMPLOYEES.—

(A) REIMBURSED EXPENSES OF EMPLOYEES.—The deductions allowed by part VI (section 161 and following) which consist of expenses paid or incurred by the taxpayer, in connection with the performance by him of services as an employee, under a reimbursement or other expense allowance arrangement with his employer. The fact that the reimbursement may be provided by a third party shall not be determinative of whether or not the preceding sentence applies.

(B) CERTAIN EXPENSES OF PERFORMING ARTISTS.—The deductions allowed by section 162 which consist of expenses paid or incurred by a qualified performing artist in connection with the performances by him of services in the performing arts as an employee.

(C) CERTAIN EXPENSES OF OFFICIALS.—The deductions allowed by section 162 which consist of expenses paid or incurred with respect to services performed by an official as an employee of a State or a political subdivision thereof in a position compensated in whole or in part on a fee basis.

(D) CERTAIN EXPENSES OF ELEMENTARY AND SECONDARY SCHOOL TEACHERS.—The deductions allowed by section 162

which consist of expenses, not in excess of \$250, paid or incurred by an eligible educator—

(i) by reason of the participation of the educator in professional development courses related to the curriculum in which the educator provides instruction or to the students for which the educator provides instruction, and

(ii) in connection with books, supplies (other than nonathletic supplies for courses of instruction in health or physical education), computer equipment (including related software and services) and other equipment, and supplementary materials used by the eligible educator in the classroom.

(E) CERTAIN EXPENSES OF MEMBERS OF RESERVE COMPONENTS OF THE ARMED FORCES OF THE UNITED STATES.—The deductions allowed by section 162 which consist of expenses, determined at a rate not in excess of the rates for travel expenses (including per diem in lieu of subsistence) authorized for employees of agencies under subchapter I of chapter 57 of title 5, United States Code, paid or incurred by the taxpayer in connection with the performance of services by such taxpayer as a member of a reserve component of the Armed Forces of the United States for any period during which such individual is more than 100 miles away from home in connection with such services.

(3) LOSSES FROM SALE OR EXCHANGE OF PROPERTY.—The deductions allowed by part VI (sec. 161 and following) as losses from the sale or exchange of property.

(4) DEDUCTIONS ATTRIBUTABLE TO RENTS AND ROYALTIES.—The deductions allowed by part VI (sec. 161 and following), by section 212 (relating to expenses for production of income), and by section 611 (relating to depletion) which are attributable to property held for the production of rents or royalties.

(5) CERTAIN DEDUCTIONS OF LIFE TENANTS AND INCOME BENEFICIARIES OF PROPERTY.—In the case of a life tenant of property, or an income beneficiary of property held in trust, or an heir, legatee, or devisee of an estate, the deduction for depreciation allowed by section 167 and the deduction allowed by section 611.

(6) PENSION, PROFIT-SHARING, AND ANNUITY PLANS OF SELF-EMPLOYED INDIVIDUALS.—In the case of an individual who is an employee within the meaning of section 401(c)(1), the deduction allowed by section 404.

(7) RETIREMENT SAVINGS.—The deduction allowed by section 219 (relating to deduction of certain retirement savings).

(9) PENALTIES FORFEITED BECAUSE OF PREMATURE WITHDRAWAL OF FUNDS FROM TIME SAVINGS ACCOUNTS OR DEPOSITS.—The deductions allowed by section 165 for losses incurred in any transaction entered into for profit, though not connected with a trade or business, to the extent that such losses include amounts forfeited to a bank, mutual savings bank, savings and loan association, building and loan association, cooperative bank or homestead association as a penalty for premature withdrawal of funds from a time savings account, certificate of deposit, or similar class of deposit.

(11) REFORESTATION EXPENSES.—The deduction allowed by section 194.

(12) CERTAIN REQUIRED REPAYMENTS OF SUPPLEMENTAL UNEMPLOYMENT COMPENSATION BENEFITS.—The deduction allowed by section 165 for the repayment to a trust described in paragraph (9) or (17) of section 501(c) of supplemental unemployment compensation benefits received from such trust if such repayment is required because of the receipt of trade readjustment allowances under section 231 or 232 of the Trade Act of 1974 (19 U.S.C. Sec. 2291 and 2292).

(13) JURY DUTY PAY REMITTED TO EMPLOYER.—Any deduction allowable under this chapter by reason of an individual remitting any portion of any jury pay to such individual's employer in exchange for payment by the employer of compensation for the period such individual was performing jury duty. For purposes of the preceding sentence, the term "jury pay" means any payment received by the individual for the discharge of jury duty.

(15) MOVING EXPENSES.—The deduction allowed by section 217.

(16) ARCHER MSAS.—The deduction allowed by section 220.

(17) INTEREST ON EDUCATION LOANS.—The deduction allowed by section 221.

(18) HIGHER EDUCATION EXPENSES.—The deduction allowed by section 222.

(19) HEALTH SAVINGS ACCOUNTS.—The deduction allowed by section 223.

(20) COSTS INVOLVING DISCRIMINATION SUITS, ETC.—Any deduction allowable under this chapter for attorney fees and court costs paid by, or on behalf of, the taxpayer in connection with any action involving a claim of unlawful discrimination (as defined in subsection (e)) or a claim of a violation of subchapter III of chapter 37 of title 31, United States Code or a claim made under section 1862(b)(3)(A) of the Social Security Act (42 U.S.C. 1395y(b)(3)(A)). The preceding sentence shall not apply to any deduction in excess of the amount includible in the taxpayer's gross income for the taxable year on account of a judgment or settlement (whether by suit or agreement and whether as lump sum or periodic payments) resulting from such claim.

(21) ATTORNEYS' FEES RELATING TO AWARDS TO WHISTLEBLOWERS.—

(A) IN GENERAL.—Any deduction allowable under this chapter for attorney fees and court costs paid by, or on behalf of, the taxpayer in connection with any award under—

(i) section 7623(b), or

(ii) in the case of taxable years beginning after December 31, 2017, any action brought under—

(I) section 21F of the Securities Exchange Act of 1934 (15 U.S.C. 78u-6),

(II) a State false claims act, including a State false claims act with qui tam provisions, or

(III) section 23 of the Commodity Exchange Act (7 U.S.C. 26).



(B) MAY NOT EXCEED AWARD.—Subparagraph (A) shall not apply to any deduction in excess of the amount includible in the taxpayer's gross income for the taxable year on account of such award.

Nothing in this section shall permit the same item to be deducted more than once. Any deduction allowed by section 199A shall not be treated as a deduction described in any of the preceding paragraphs of this subsection.

(b) QUALIFIED PERFORMING ARTIST.—

(1) IN GENERAL.—For purposes of subsection (a)(2)(B), the term “qualified performing artist” means, with respect to any taxable year, any individual if—

(A) such individual performed services in the performing arts as an employee during the taxable year for at least 2 employers,

(B) the aggregate amount allowable as a deduction under section 162 in connection with the performance of such services exceeds 10 percent of such individual's gross income attributable to the performance of such services, and

(C) the adjusted gross income of such individual for the taxable year (determined without regard to subsection (a)(2)(B)) does not exceed \$16,000.

(2) NOMINAL EMPLOYER NOT TAKEN INTO ACCOUNT.—An individual shall not be treated as performing services in the performing arts as an employee for any employer during any taxable year unless the amount received by such individual from such employer for the performance of such services during the taxable year equals or exceeds \$200.

(3) SPECIAL RULES FOR MARRIED COUPLES.—

(A) IN GENERAL.—Except in the case of a husband and wife who lived apart at all times during the taxable year, if the taxpayer is married at the close of the taxable year, subsection (a)(2)(B) shall apply only if the taxpayer and his spouse file a joint return for the taxable year.

(B) APPLICATION OF PARAGRAPH (1).—In the case of a joint return—

(i) paragraph (1) (other than subparagraph (C) thereof) shall be applied separately with respect to each spouse, but

(ii) paragraph (1)(C) shall be applied with respect to their combined adjusted gross income.

(C) DETERMINATION OF MARITAL STATUS.—For purposes of this subsection, marital status shall be determined under section 7703(a).

(D) JOINT RETURN.—For purposes of this subsection, the term “joint return” means the joint return of a husband and wife made under section 6013.

(c) CERTAIN ARRANGEMENTS NOT TREATED AS REIMBURSEMENT ARRANGEMENTS.—For purposes of subsection (a)(2)(A), an arrangement shall in no event be treated as a reimbursement or other expense allowance arrangement if—

(1) such arrangement does not require the employee to substantiate the expenses covered by the arrangement to the person providing the reimbursement, or

(2) such arrangement provides the employee the right to retain any amount in excess of the substantiated expenses covered under the arrangement.

The substantiation requirements of the preceding sentence shall not apply to any expense to the extent that substantiation is not required under section 274(d) for such expense by reason of the regulations prescribed under the 2nd sentence thereof.

(d) DEFINITION; SPECIAL RULES.—

(1) ELIGIBLE EDUCATOR.—

(A) IN GENERAL.—For purposes of subsection (a)(2)(D), the term “eligible educator” means, with respect to any taxable year, an individual who is a kindergarten through grade 12 teacher, instructor, counselor, principal, or aide in a school for at least 900 hours during a school year.

(B) SCHOOL.—The term “school” means any school which provides elementary education or secondary education (kindergarten through grade 12), as determined under State law.

(2) COORDINATION WITH EXCLUSIONS.—A deduction shall be allowed under subsection (a)(2)(D) for expenses only to the extent the amount of such expenses exceeds the amount excludable under section 135, 529(c)(1), or 530(d)(2) for the taxable year.

(3) INFLATION ADJUSTMENT.—In the case of any taxable year beginning after 2015, the \$250 amount in subsection (a)(2)(D) shall be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2014” for “calendar year 2016” in subparagraph (A)(ii) thereof.

Any increase determined under the preceding sentence shall be rounded to the nearest multiple of \$50.

(e) UNLAWFUL DISCRIMINATION DEFINED.—For purposes of subsection (a)(20), the term “unlawful discrimination” means an act that is unlawful under any of the following:

(1) Section 302 of the Civil Rights Act of 1991 (42 U.S.C. 2000e-16b).

(2) Section 201, 202, 203, 204, 205, 206, or 207 of the Congressional Accountability Act of 1995 (2 U.S.C. 1311, 1312, 1313, 1314, 1315, 1316, or 1317).

(3) The National Labor Relations Act (29 U.S.C. 151 et seq.).

(4) The Fair Labor Standards Act of 1938 (29 U.S.C. 201 et seq.).

(5) Section 4 or 15 of the Age Discrimination in Employment Act of 1967 (29 U.S.C. 623 or 633a).

(6) Section 501 or 504 of the Rehabilitation Act of 1973 (29 U.S.C. 791 or 794).

(7) Section 510 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1140).

(8) Title IX of the Education Amendments of 1972 (20 U.S.C. 1681 et seq.).

(9) The Employee Polygraph Protection Act of 1988 (29 U.S.C. 2001 et seq.).

(10) The Worker Adjustment and Retraining Notification Act (29 U.S.C. 2102 et seq.).

(11) Section 105 of the Family and Medical Leave Act of 1993 (29 U.S.C. 2615).

(12) Chapter 43 of title 38, United States Code (relating to employment and reemployment rights of members of the uniformed services).

(13) Section 1977, 1979, or 1980 of the Revised Statutes (42 U.S.C. 1981, 1983, or 1985).

(14) Section 703, 704, or 717 of the Civil Rights Act of 1964 (42 U.S.C. 2000e-2, 2000e-3, or 2000e-16).

(15) Section 804, 805, 806, 808, or 818 of the Fair Housing Act (42 U.S.C. 3604, 3605, 3606, 3608, or 3617).

(16) Section 102, 202, 302, or 503 of the Americans with Disabilities Act of 1990 (42 U.S.C. 12112, 12132, 12182, or 12203).

(17) Any provision of Federal law (popularly known as whistleblower protection provisions) prohibiting the discharge of an employee, the discrimination against an employee, or any other form of retaliation or reprisal against an employee for asserting rights or taking other actions permitted under Federal law.

(18) Any provision of Federal, State, or local law, or common law claims permitted under Federal, State, or local law—

(i) providing for the enforcement of civil rights, or

(ii) regulating any aspect of the employment relationship, including claims for wages, compensation, or benefits, or prohibiting the discharge of an employee, the discrimination against an employee, or any other form of retaliation or reprisal against an employee for asserting rights or taking other actions permitted by law.

#### **SEC. 63. TAXABLE INCOME DEFINED.**

(a) **IN GENERAL.**—Except as provided in subsection (b), for purposes of this subtitle, the term “taxable income” means gross income minus the deductions allowed by this chapter (other than the standard deduction).

(b) **INDIVIDUALS WHO DO NOT ITEMIZE THEIR DEDUCTIONS.**—In the case of an individual who does not elect to itemize his deductions for the taxable year, for purposes of this subtitle, the term “taxable income” means adjusted gross income, minus—

(1) the standard deduction, *and*

[(2) the deduction for personal exemptions provided in section 151, and.

[(3)] (2) any deduction provided in section 199A.

(c) **STANDARD DEDUCTION.**—For purposes of this subtitle—

(1) **IN GENERAL.**—Except as otherwise provided in this subsection, the term “standard deduction” means the sum of—

(A) the basic standard deduction, and

(B) the additional standard deduction.

(2) **BASIC STANDARD DEDUCTION.**—For purposes of paragraph (1), the basic standard deduction is—

(A) 200 percent of the dollar amount in effect under subparagraph (C) for the taxable year in the case of—

(i) a joint return, or

(ii) a surviving spouse (as defined in section 2(a)),

(B) **[\$4,400] \$18,000** in the case of a head of household (as defined in section 2(b)), or

(C) **[\$3,000]** \$12,000 in any other case.

**[(3) ADDITIONAL STANDARD DEDUCTION FOR AGED AND BLIND.—**For purposes of paragraph (1), the additional standard deduction is the sum of each additional amount to which the taxpayer is entitled under subsection (f).

**[(4) ADJUSTMENTS FOR INFLATION.—**In the case of any taxable year beginning in a calendar year after 1988, each dollar amount contained in paragraph (2)(B), (2)(C), or (5) or subsection (f) shall be increased by an amount equal to—

**[(A) such dollar amount, multiplied by**

**[(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting for “calendar year 2016” in subparagraph (A)(ii) thereof—**

**[(i) “calendar year 1987” in the case of the dollar amounts contained in paragraph (2)(B), (2)(C), or (5)(A) or subsection (f), and**

**[(ii) “calendar year 1997” in the case of the dollar amount contained in paragraph (5)(B).]**

**(3) ADJUSTMENTS FOR INFLATION.—**

**(A) IN GENERAL.—***In the case of a taxable year beginning after 2018, each dollar amount in paragraph (2)(B), (2)(C), or (5) or subsection (f) shall be increased by an amount equal to—*

*(i) such dollar amount, multiplied by*

*(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting for “2016” in subparagraph (A)(ii) thereof—*

*(I) in the case of the dollar amounts contained in paragraph (2)(B) or (2)(C), “2017”,*

*(II) in the case of the dollar amounts contained in paragraph (5)(A) or subsection (f), “1987”, and*

*(III) in the case of the dollar amount contained in paragraph (5)(B), “1997”.*

**(B) ROUNDING.—***If any increase under subparagraph (A) is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.*

**[(5)] (4) LIMITATION ON BASIC STANDARD DEDUCTION IN THE CASE OF [CERTAIN] DEPENDENTS.—**In the case of an individual **[with respect to whom a deduction under section 151 is allowable to]** *who is a dependent of another taxpayer for a taxable year beginning in the calendar year in which the individual’s taxable year begins, the basic standard deduction applicable to such individual for such individual’s taxable year shall not exceed the greater of—*

**(A) \$500, or**

**(B) the sum of \$250 and such individual’s earned income.**

**[(6)] (5) CERTAIN INDIVIDUALS, ETC., NOT ELIGIBLE FOR STANDARD DEDUCTION.—**In the case of—

**(A) a married individual filing a separate return where either spouse itemizes deductions,**

**(B) a nonresident alien individual,**

(C) an individual making a return under section 443(a)(1) for a period of less than 12 months on account of a change in his annual accounting period, or

(D) an estate or trust, common trust fund, or partnership, the standard deduction shall be zero.

[(7) SPECIAL RULES FOR TAXABLE YEARS 2018 THROUGH 2025.—In the case of a taxable year beginning after December 31, 2017, and before January 1, 2026—

[(A) INCREASE IN STANDARD DEDUCTION.—Paragraph (2) shall be applied—

[(i) by substituting “\$18,000” for “\$4,400” in subparagraph (B), and

[(ii) by substituting “\$12,000” for “\$3,000” in subparagraph (C).

[(B) ADJUSTMENT FOR INFLATION.—

[(i) IN GENERAL.—Paragraph (4) shall not apply to the dollar amounts contained in paragraphs (2)(B) and (2)(C).

[(ii) ADJUSTMENT OF INCREASED AMOUNTS.—In the case of a taxable year beginning after 2018, the \$18,000 and \$12,000 amounts in subparagraph (A) shall each be increased by an amount equal to—

[(I) such dollar amount, multiplied by

[(II) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “2017” for “2016” in subparagraph (A)(ii) thereof.

If any increase under this clause is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.]

(d) ITEMIZED DEDUCTIONS.—For purposes of this subtitle, the term “itemized deductions” means the deductions allowable under this chapter other than—

(1) the deductions allowable in arriving at adjusted gross income, and

[(2) the deduction for personal exemptions provided by section 151, and

[(3)] (2) any deduction provided in section 199A.

(e) ELECTION TO ITEMIZE.—

(1) IN GENERAL.—Unless an individual makes an election under this subsection for the taxable year, no itemized deduction shall be allowed for the taxable year. For purposes of this subtitle, the determination of whether a deduction is allowable under this chapter shall be made without regard to the preceding sentence.

(2) TIME AND MANNER OF ELECTION.—Any election under this subsection shall be made on the taxpayer’s return, and the Secretary shall prescribe the manner of signifying such election on the return.

(3) CHANGE OF ELECTION.—Under regulations prescribed by the Secretary, a change of election with respect to itemized deductions for any taxable year may be made after the filing of the return for such year. If the spouse of the taxpayer filed a separate return for any taxable year corresponding to the tax-

able year of the taxpayer, the change shall not be allowed unless, in accordance with such regulations—

(A) the spouse makes a change of election with respect to itemized deductions, for the taxable year covered in such separate return, consistent with the change of treatment sought by the taxpayer, and

(B) the taxpayer and his spouse consent in writing to the assessment (within such period as may be agreed on with the Secretary) of any deficiency, to the extent attributable to such change of election, even though at the time of the filing of such consent the assessment of such deficiency would otherwise be prevented by the operation of any law or rule of law.

This paragraph shall not apply if the tax liability of the taxpayer's spouse for the taxable year corresponding to the taxable year of the taxpayer has been compromised under section 7122.

**[(f) AGED OR BLIND ADDITIONAL AMOUNTS.—**

**[(1) ADDITIONAL AMOUNTS FOR THE AGED.—**The taxpayer shall be entitled to an additional amount of \$600—

**[(A)** for himself if he has attained age 65 before the close of his taxable year, and

**[(B)** for the spouse of the taxpayer if the spouse has attained age 65 before the close of the taxable year and an additional exemption is allowable to the taxpayer for such spouse under section 151(b).

**[(2) ADDITIONAL AMOUNT FOR BLIND.—**The taxpayer shall be entitled to an additional amount of \$600—

**[(A)** for himself if he is blind at the close of the taxable year, and

**[(B)** for the spouse of the taxpayer if the spouse is blind as of the close of the taxable year and an additional exemption is allowable to the taxpayer for such spouse under section 151(b).

For purposes of subparagraph (B), if the spouse dies during the taxable year the determination of whether such spouse is blind shall be made as of the time of such death.】

**(f) ADDITIONAL STANDARD DEDUCTION FOR THE AGED AND BLIND.—**

**(1) IN GENERAL.—***For purposes of subsection (c)(1), the additional standard deduction is, with respect to a taxpayer for a taxable year, the sum of—*

*(A) \$600 if the taxpayer has attained age 65 before the close of such taxable year, and*

*(B) \$600 if the taxpayer is blind as of the close of such taxable year.*

**(2) APPLICATION TO MARRIED INDIVIDUALS.—**

**(A) JOINT RETURNS.—***In the case of a joint return, paragraph (1) shall be applied separately with respect to each spouse.*

**(B) CERTAIN MARRIED INDIVIDUALS FILING SEPARATELY.—***In the case of a married individual filing a separate return, if—*

(i) the spouse of such individual has no gross income for the calendar year in which the taxable year of such individual begins,

(ii) such spouse is not the dependent of another taxpayer for a taxable year beginning in the calendar year in which such individual's taxable year begins, and

(iii) the TIN of such spouse is included on such individual's return of tax for the taxable year,

the additional standard deduction shall be determined in the same manner as if such individual and such individual's spouse filed a joint return.

(3) HIGHER AMOUNT FOR CERTAIN UNMARRIED INDIVIDUALS.—In the case of an individual who is not married and is not a surviving spouse, [paragraphs (1) and (2)] subparagraphs (A) and (B) of paragraph (1) shall be applied by substituting “\$750” for “\$600”.

(4) BLINDNESS DEFINED.—For purposes of this subsection, an individual is blind only if his central visual acuity does not exceed 20/200 in the better eye with correcting lenses, or if his visual acuity is greater than 20/200 but is accompanied by a limitation in the fields of vision such that the widest diameter of the visual field subtends an angle no greater than 20 degrees.

(g) MARITAL STATUS.—For purposes of this section, marital status shall be determined under section 7703.

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**SEC. 67. [2-PERCENT FLOOR ON] DENIAL OF MISCELLANEOUS ITEMIZED DEDUCTIONS.**

[(a) GENERAL RULE.—In the case of an individual, the miscellaneous itemized deductions for any taxable year shall be allowed only to the extent that the aggregate of such deductions exceeds 2 percent of adjusted gross income.]

(a) IN GENERAL.—In the case of an individual, miscellaneous itemized deductions shall not be allowed.

(b) MISCELLANEOUS ITEMIZED DEDUCTIONS.—For purposes of this section, the term “miscellaneous itemized deductions” means the itemized deductions other than—

- (1) the deduction under section 163 (relating to interest),
- (2) the deduction under section 164 (relating to taxes),
- (3) the deduction under section 165(a) for casualty or theft losses described in paragraph (2) or (3) of section 165(c) or for losses described in section 165(d),
- (4) the deductions under section 170 (relating to charitable, etc., contributions and gifts) and section 642(c) (relating to deduction for amounts paid or permanently set aside for a charitable purpose),
- (5) the deduction under section 213 (relating to medical, dental, etc., expenses),
- (6) any deduction allowable for impairment-related work expenses,
- (7) the deduction under section 691(c) (relating to deduction for estate tax in case of income in respect of the decedent),
- (8) any deduction allowable in connection with personal property used in a short sale,

(9) the deduction under section 1341 (relating to computation of tax where taxpayer restores substantial amount held under claim of right),

(10) the deduction under section 72(b)(3) (relating to deduction where annuity payments cease before investment recovered),

(11) the deduction under section 171 (relating to deduction for amortizable bond premium), and

(12) the deduction under section 216 (relating to deductions in connection with cooperative housing corporations).

(c) DISALLOWANCE OF INDIRECT DEDUCTION THROUGH PASS-THRU ENTITY.—

(1) IN GENERAL.—The Secretary shall prescribe regulations which prohibit the indirect deduction through pass-thru entities of amounts which are not allowable as a deduction if paid or incurred directly by an individual and which contain such reporting requirements as may be necessary to carry out the purposes of this subsection.

(2) TREATMENT OF PUBLICLY OFFERED REGULATED INVESTMENT COMPANIES.—

(A) IN GENERAL.—Paragraph (1) shall not apply with respect to any publicly offered regulated investment company.

(B) PUBLICLY OFFERED REGULATED INVESTMENT COMPANIES.—For purposes of this subsection—

(i) IN GENERAL.—The term “publicly offered regulated investment company” means a regulated investment company the shares of which are—

(I) continuously offered pursuant to a public offering (within the meaning of section 4 of the Securities Act of 1933, as amended (15 U.S.C. 77a to 77aa)),

(II) regularly traded on an established securities market, or

(III) held by or for no fewer than 500 persons at all times during the taxable year.

(ii) SECRETARY MAY REDUCE 500 PERSON REQUIREMENT.—The Secretary may by regulation decrease the minimum shareholder requirement of clause (i)(III) in the case of regulated investment companies which experience a loss of shareholders through net redemptions of their shares.

(3) TREATMENT OF CERTAIN OTHER ENTITIES.—Paragraph (1) shall not apply—

(A) with respect to cooperatives and real estate investment trusts, and

(B) except as provided in regulations, with respect to estates and trusts.

(d) IMPAIRMENT-RELATED WORK EXPENSES.—For purposes of this section, the term “impairment-related work expenses” means expenses—

(1) of a handicapped individual (as defined in section 190(b)(3)) for attendant care services at the individual’s place of employment and other expenses in connection with such



place of employment which are necessary for such individual to be able to work, and

(2) with respect to which a deduction is allowable under section 162 (determined without regard to this section).

**[(e) DETERMINATION OF ADJUSTED GROSS INCOME IN CASE OF ESTATES AND TRUSTS.—**For purposes of this section, the adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual, except that—

**[(1)** the deductions for costs which are paid or incurred in connection with the administration of the estate or trust and which would not have been incurred if the property were not held in such trust or estate, and

**[(2)** the deductions allowable under sections 642(b), 651, and 661, shall be treated as

allowable in arriving at adjusted gross income. Under regulations, appropriate adjustments shall be made in the application of part I of subchapter J of this chapter to take into account the provisions of this section.]

**(f) COORDINATION WITH OTHER LIMITATION.—**This section shall be applied before the application of the dollar limitation of the second sentence of section 162(a) (relating to trade or business expenses).

**[(g) SUSPENSION FOR TAXABLE YEARS 2018 THROUGH 2025.—**Notwithstanding subsection (a), no miscellaneous itemized deduction shall be allowed for any taxable year beginning after December 31, 2017, and before January 1, 2026.]

**[SEC. 68. OVERALL LIMITATION ON ITEMIZED DEDUCTIONS.**

**[(a) GENERAL RULE.—**In the case of an individual whose adjusted gross income exceeds the applicable amount, the amount of the itemized deductions otherwise allowable for the taxable year shall be reduced by the lesser of—

**[(1)** 3 percent of the excess of adjusted gross income over the applicable amount, or

**[(2)** 80 percent of the amount of the itemized deductions otherwise allowable for such taxable year.

**[(b) APPLICABLE AMOUNT.—**

**[(1) IN GENERAL.—**For purposes of this section, the term “applicable amount” means—

**[(A)** \$300,000 in the case of a joint return or a surviving spouse (as defined in section 2(a)),

**[(B)** \$275,000 in the case of a head of household (as defined in section 2(b)),

**[(C)** \$250,000 in the case of an individual who is not married and who is not a surviving spouse or head of household, and

**[(D)** ½ the amount applicable under subparagraph (A) (after adjustment, if any, under paragraph (2)) in the case of a married individual filing a separate return.

For purposes of this paragraph, marital status shall be determined under section 7703.

**[(2) INFLATION ADJUSTMENT.—**In the case of any taxable year beginning in calendar years after 2013, each of the dollar amounts under subparagraphs (A), (B), and (C) of paragraph (1) shall be increased by an amount equal to—

**[(A)** such dollar amount, multiplied by

[(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, except that section 1(f)(3)(A)(ii) shall be applied by substituting “2012” for “2016”.

If any amount after adjustment under the preceding sentence is not a multiple of \$50, such amount shall be rounded to the next lowest multiple of \$50.

[(c) EXCEPTION FOR CERTAIN ITEMIZED DEDUCTIONS.—For purposes of this section, the term “itemized deductions” does not include—

[(1) the deduction under section 213 (relating to medical, etc. expenses),

[(2) any deduction for investment interest (as defined in section 163(d)), and

[(3) the deduction under section 165(a) for casualty or theft losses described in paragraph (2) or (3) of section 165(c) or for losses described in section 165(d).

[(d) COORDINATION WITH OTHER LIMITATIONS.—This section shall be applied after the application of any other limitation on the allowance of any itemized deduction.

[(e) EXCEPTION FOR ESTATES AND TRUSTS.—This section shall not apply to any estate or trust.

[(f) SECTION NOT TO APPLY.—This section shall not apply to any taxable year beginning after December 31, 2017, and before January 1, 2026.]

**PART II—ITEMS SPECIFICALLY INCLUDED IN GROSS INCOME**

\* \* \* \* \*

**SEC. 72. ANNUITIES; CERTAIN PROCEEDS OF ENDOWMENT AND LIFE INSURANCE CONTRACTS.**

(a) GENERAL RULES FOR ANNUITIES.—

(1) INCOME INCLUSION.—Except as otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period certain or during one or more lives) under an annuity, endowment, or life insurance contract.

(2) PARTIAL ANNUITIZATION.—If any amount is received as an annuity for a period of 10 years or more or during one or more lives under any portion of an annuity, endowment, or life insurance contract—

(A) such portion shall be treated as a separate contract for purposes of this section,

(B) for purposes of applying subsections (b), (c), and (e), the investment in the contract shall be allocated pro rata between each portion of the contract from which amounts are received as an annuity and the portion of the contract from which amounts are not received as an annuity, and

(C) a separate annuity starting date under subsection (c)(4) shall be determined with respect to each portion of the contract from which amounts are received as an annuity.

(b) EXCLUSION RATIO.—

(1) IN GENERAL.—Gross income does not include that part of any amount received as an annuity under an annuity, endowment, or life insurance contract which bears the same ratio to

such amount as the investment in the contract (as of the annuity starting date) bears to the expected return under the contract (as of such date).

(2) EXCLUSION LIMITED TO INVESTMENT.—The portion of any amount received as an annuity which is excluded from gross income under paragraph (1) shall not exceed the unrecovered investment in the contract immediately before the receipt of such amount.

(3) DEDUCTION WHERE ANNUITY PAYMENTS CEASE BEFORE ENTIRE INVESTMENT RECOVERED.—

(A) IN GENERAL.—If—

(i) after the annuity starting date, payments as an annuity under the contract cease by reason of the death of an annuitant, and

(ii) as of the date of such cessation, there is unrecovered investment in the contract,

the amount of such unrecovered investment (in excess of any amount specified in subsection (e)(5) which was not included in gross income) shall be allowed as a deduction to the annuitant for his last taxable year.

(B) PAYMENTS TO OTHER PERSONS.—In the case of any contract which provides for payments meeting the requirements of subparagraphs (B) and (C) of subsection (c)(2), the deduction under subparagraph (A) shall be allowed to the person entitled to such payments for the taxable year in which such payments are received.

(C) NET OPERATING LOSS DEDUCTIONS PROVIDED.—For purposes of section 172, a deduction allowed under this paragraph shall be treated as if it were attributable to a trade or business of the taxpayer.

(4) UNRECOVERED INVESTMENT.—For purposes of this subsection, the unrecovered investment in the contract as of any date is—

(A) the investment in the contract (determined without regard to subsection (c)(2)) as of the annuity starting date, reduced by

(B) the aggregate amount received under the contract on or after such annuity starting date and before the date as of which the determination is being made, to the extent such amount was excludable from gross income under this subtitle.

(c) DEFINITIONS.—

(1) INVESTMENT IN THE CONTRACT.—For purposes of subsection (b), the investment in the contract as of the annuity starting date is—

(A) the aggregate amount of premiums or other consideration paid for the contract, minus

(B) the aggregate amount received under the contract before such date, to the extent that such amount was excludable from gross income under this subtitle or prior income tax laws.

(2) ADJUSTMENT IN INVESTMENT WHERE THERE IS REFUND FEATURE.—If—

(A) the expected return under the contract depends in whole or in part on the life expectancy of one or more individuals;

(B) the contract provides for payments to be made to a beneficiary (or to the estate of an annuitant) on or after the death of the annuitant or annuitants; and

(C) such payments are in the nature of a refund of the consideration paid,

then the value (computed without discount for interest) of such payments on the annuity starting date shall be subtracted from the amount determined under paragraph (1). Such value shall be computed in accordance with actuarial tables prescribed by the Secretary. For purposes of this paragraph and of subsection (e)(2)(A), the term "refund of the consideration paid" includes amounts payable after the death of an annuitant by reason of a provision in the contract for a life annuity with minimum period of payments certain, but (if part of the consideration was contributed by an employer) does not include that part of any payment to a beneficiary (or to the estate of the annuitant) which is not attributable to the consideration paid by the employee for the contract as determined under paragraph (1)(A).

(3) EXPECTED RETURN.—For purposes of subsection (b), the expected return under the contract shall be determined as follows:

(A) LIFE EXPECTANCY.—If the expected return under the contract, for the period on and after the annuity starting date, depends in whole or in part on the life expectancy of one or more individuals, the expected return shall be computed with reference to actuarial tables prescribed by the Secretary.

(B) INSTALLMENT PAYMENTS.—If subparagraph (A) does not apply, the expected return is the aggregate of the amounts receivable under the contract as an annuity.

(4) ANNUITY STARTING DATE.—For purposes of this section, the annuity starting date in the case of any contract is the first day of the first period for which an amount is received as an annuity under the contract.

(d) SPECIAL RULES FOR QUALIFIED EMPLOYER RETIREMENT PLANS.—

(1) SIMPLIFIED METHOD OF TAXING ANNUITY PAYMENTS.—

(A) IN GENERAL.—In the case of any amount received as an annuity under a qualified employer retirement plan—

(i) subsection (b) shall not apply, and

(ii) the investment in the contract shall be recovered as provided in this paragraph.

(B) METHOD OF RECOVERING INVESTMENT IN CONTRACT.—

(i) IN GENERAL.—Gross income shall not include so much of any monthly annuity payment under a qualified employer retirement plan as does not exceed the amount obtained by dividing—

(I) the investment in the contract (as of the annuity starting date), by

(II) the number of anticipated payments determined under the table contained in clause (iii) (or,

in the case of a contract to which subsection (c)(3)(B) applies, the number of monthly annuity payments under such contract).

(ii) CERTAIN RULES MADE APPLICABLE.—Rules similar to the rules of paragraphs (2) and (3) of subsection (b) shall apply for purposes of this paragraph.

(iii) NUMBER OF ANTICIPATED PAYMENTS.—If the annuity is payable over the life of a single individual, the number of anticipated payments shall be determined as follows:

| If the age of the annuitant on the annuity starting date is: | The number of anticipated payments is: |
|--|--|
| Not more than 55.....  | 360                                    |
| More than 55 but not more than 60                            | 310                                    |
| More than 60 but not more than 65                            | 260                                    |
| More than 65 but not more than 70                            | 210                                    |
| More than 70.....  | 160.                                   |

(iv) NUMBER OF ANTICIPATED PAYMENTS WHERE MORE THAN ONE LIFE.—If the annuity is payable over the lives of more than 1 individual, the number of anticipated payments shall be determined as follows:

| If the combined ages of annuitants are:   | The number is: |
|---|----------------|
| Not more than 110 .....                   | 410            |
| More than 110 but not more than 120 ..... | 360            |
| More than 120 but not more than 130 ..... | 310            |
| More than 130 but not more than 140 ..... | 260            |
| More than 140 .....                       | 210.           |

(C) ADJUSTMENT FOR REFUND FEATURE NOT APPLICABLE.—For purposes of this paragraph, investment in the contract shall be determined under subsection (c)(1) without regard to subsection (c)(2).

(D) SPECIAL RULE WHERE LUMP SUM PAID IN CONNECTION WITH COMMENCEMENT OF ANNUITY PAYMENTS.—If, in connection with the commencement of annuity payments under any qualified employer retirement plan, the taxpayer receives a lump-sum payment—

- (i) such payment shall be taxable under subsection (e) as if received before the annuity starting date, and
- (ii) the investment in the contract for purposes of this paragraph shall be determined as if such payment had been so received.

(E) EXCEPTION.—This paragraph shall not apply in any case where the primary annuitant has attained age 75 on the annuity starting date unless there are fewer than 5 years of guaranteed payments under the annuity.

(F) ADJUSTMENT WHERE ANNUITY PAYMENTS NOT ON MONTHLY BASIS.—In any case where the annuity payments are not made on a monthly basis, appropriate adjustments in the application of this paragraph shall be made to take

into account the period on the basis of which such payments are made.

(G) QUALIFIED EMPLOYER RETIREMENT PLAN.—For purposes of this paragraph, the term “qualified employer retirement plan” means any plan or contract described in paragraph (1), (2), or (3) of section 4974(c).

(2) TREATMENT OF EMPLOYEE CONTRIBUTIONS UNDER DEFINED CONTRIBUTION PLANS.—For purposes of this section, employee contributions (and any income allocable thereto) under a defined contribution plan may be treated as a separate contract.

(e) AMOUNTS NOT RECEIVED AS ANNUITIES.—

(1) APPLICATION OF SUBSECTION.—

(A) IN GENERAL.—This subsection shall apply to any amount which—

(i) is received under an annuity, endowment, or life insurance contract, and

(ii) is not received as an annuity, if no provision of this subtitle (other than this subsection) applies with respect to such amount.

(B) DIVIDENDS.—For purposes of this section, any amount received which is in the nature of a dividend or similar distribution shall be treated as an amount not received as an annuity.

(2) GENERAL RULE.—Any amount to which this subsection applies—

(A) if received on or after the annuity starting date, shall be included in gross income, or

(B) if received before the annuity starting date—

(i) shall be included in gross income to the extent allocable to income on the contract, and

(ii) shall not be included in gross income to the extent allocable to the investment in the contract.

(3) ALLOCATION OF AMOUNTS TO INCOME AND INVESTMENT.—For purposes of paragraph (2)(B)—

(A) ALLOCATION TO INCOME.—Any amount to which this subsection applies shall be treated as allocable to income on the contract to the extent that such amount does not exceed the excess (if any) of—

(i) the cash value of the contract (determined without regard to any surrender charge) immediately before the amount is received, over

(ii) the investment in the contract at such time.

(B) ALLOCATION TO INVESTMENT.—Any amount to which this subsection applies shall be treated as allocable to investment in the contract to the extent that such amount is not allocated to income under subparagraph (A).

(4) SPECIAL RULES FOR APPLICATION OF PARAGRAPH (2)(B).—For purposes of paragraph (2)(B)—

(A) LOANS TREATED AS DISTRIBUTIONS.—If, during any taxable year, an individual—

(i) receives (directly or indirectly) any amount as a loan under any contract to which this subsection applies, or

(ii) assigns or pledges (or agrees to assign or pledge) any portion of the value of any such contract,

such amount or portion shall be treated as received under the contract as an amount not received as an annuity. The preceding sentence shall not apply for purposes of determining investment in the contract, except that the investment in the contract shall be increased by any amount included in gross income by reason of the amount treated as received under the preceding sentence.

(B) TREATMENT OF POLICYHOLDER DIVIDENDS.—Any amount described in paragraph (1)(B) shall not be included in gross income under paragraph (2)(B)(i) to the extent such amount is retained by the insurer as a premium or other consideration paid for the contract.

(C) TREATMENT OF TRANSFERS WITHOUT ADEQUATE CONSIDERATION.—

(i) IN GENERAL.—If an individual who holds an annuity contract transfers it without full and adequate consideration, such individual shall be treated as receiving an amount equal to the excess of—

(I) the cash surrender value of such contract at the time of transfer, over

(II) the investment in such contract at such time,

under the contract as an amount not received as an annuity.

(ii) EXCEPTION FOR CERTAIN TRANSFERS BETWEEN SPOUSES OR FORMER SPOUSES.—Clause (i) shall not apply to any transfer to which section 1041(a) (relating to transfers of property between spouses or incident to divorce) applies.

(iii) ADJUSTMENT TO INVESTMENT IN CONTRACT OF TRANSFEREE.—If under clause (i) an amount is included in the gross income of the transferor of an annuity contract, the investment in the contract of the transferee in such contract shall be increased by the amount so included.

(5) RETENTION OF EXISTING RULES IN CERTAIN CASES.—

(A) IN GENERAL.—In any case to which this paragraph applies—

(i) paragraphs (2)(B) and (4)(A) shall not apply, and

(ii) if paragraph (2)(A) does not apply, the amount shall be included in gross income, but only to the extent it exceeds the investment in the contract.

(B) EXISTING CONTRACTS.—This paragraph shall apply to contracts entered into before August 14, 1982. Any amount allocable to investment in the contract after August 13, 1982, shall be treated as from a contract entered into after such date.

(C) CERTAIN LIFE INSURANCE AND ENDOWMENT CONTRACTS.—Except as provided in paragraph (10) and except to the extent prescribed by the Secretary by regulations, this paragraph shall apply to any amount not received as an annuity which is received under a life insurance or endowment contract.

(D) **CONTRACTS UNDER QUALIFIED PLANS.**—Except as provided in paragraph (8), this paragraph shall apply to any amount received—

(i) from a trust described in section 401(a) which is exempt from tax under section 501(a),

(ii) from a contract—

(I) purchased by a trust described in clause (i),

(II) purchased as part of a plan described in section 403(a),

(III) described in section 403(b), or

(IV) provided for employees of a life insurance company under a plan described in section 818(a)(3), or

(iii) from an individual retirement account or an individual retirement annuity.

Any dividend described in section 404(k) which is received by a participant or beneficiary shall, for purposes of this subparagraph, be treated as paid under a separate contract to which clause (ii)(I) applies.

(E) **FULL REFUNDS, SURRENDERS, REDEMPTIONS, AND MATURITIES.**—This paragraph shall apply to—

(i) any amount received, whether in a single sum or otherwise, under a contract in full discharge of the obligation under the contract which is in the nature of a refund of the consideration paid for the contract, and

(ii) any amount received under a contract on its complete surrender, redemption, or maturity.

In the case of any amount to which the preceding sentence applies, the rule of paragraph (2)(A) shall not apply.

(6) **INVESTMENT IN THE CONTRACT.**—For purposes of this subsection, the investment in the contract as of any date is—

(A) the aggregate amount of premiums or other consideration paid for the contract before such date, minus

(B) the aggregate amount received under the contract before such date, to the extent that such amount was excludable from gross income under this subtitle or prior income tax laws.

(8) **Extension of paragraph (2)(b) to qualified plans**

(A) **IN GENERAL.**—Notwithstanding any other provision of this subsection, in the case of any amount received before the annuity starting date from a trust or contract described in paragraph (5)(D), paragraph (2)(B) shall apply to such amounts.

(B) **ALLOCATION OF AMOUNT RECEIVED.**—For purposes of paragraph (2)(B), the amount allocated to the investment in the contract shall be the portion of the amount described in subparagraph (A) which bears the same ratio to such amount as the investment in the contract bears to the account balance. The determination under the preceding sentence shall be made as of the time of the distribution or at such other time as the Secretary may prescribe.

(C) **TREATMENT OF FORFEITABLE RIGHTS.**—If an employee does not have a nonforfeitable right to any amount under any trust or contract to which subparagraph (A) applies,



such amount shall not be treated as part of the account balance.

(D) INVESTMENT IN THE CONTRACT BEFORE 1987.—In the case of a plan which on May 5, 1986, permitted withdrawal of any employee contributions before separation from service, subparagraph (A) shall apply only to the extent that amounts received before the annuity starting date (when increased by amounts previously received under the contract after December 31, 1986) exceed the investment in the contract as of December 31, 1986.

(9) EXTENSION OF PARAGRAPH (2)(B) TO QUALIFIED TUITION PROGRAMS AND COVERDELL EDUCATION SAVINGS ACCOUNTS.—Notwithstanding any other provision of this subsection, paragraph (2)(B) shall apply to amounts received under a qualified tuition program (as defined in section 529(b)) or under a Coverdell education savings account (as defined in section 530(b)). The rule of paragraph (8)(B) shall apply for purposes of this paragraph.

(10) TREATMENT OF MODIFIED ENDOWMENT CONTRACTS.—

(A) IN GENERAL.—Notwithstanding paragraph (5)(C), in the case of any modified endowment contract (as defined in section 7702A)—

(i) paragraphs (2)(B) and (4)(A) shall apply, and

(ii) in applying paragraph (4)(A), “any person” shall be substituted for “an individual”.

(B) TREATMENT OF CERTAIN BURIAL CONTRACTS.—Notwithstanding subparagraph (A), paragraph (4)(A) shall not apply to any assignment (or pledge) of a modified endowment contract if such assignment (or pledge) is solely to cover the payment of expenses referred to in section 7702(e)(2)(C)(iii) and if the maximum death benefit under such contract does not exceed \$25,000.

(11) SPECIAL RULES FOR CERTAIN COMBINATION CONTRACTS PROVIDING LONG-TERM CARE INSURANCE.—Notwithstanding paragraphs (2), (5)(C), and (10), in the case of any charge against the cash value of an annuity contract or the cash surrender value of a life insurance contract made as payment for coverage under a qualified long-term care insurance contract which is part of or a rider on such annuity or life insurance contract—

(A) the investment in the contract shall be reduced (but not below zero) by such charge, and

(B) such charge shall not be includible in gross income.

(12) ANTI-ABUSE RULES.—

(A) IN GENERAL.—For purposes of determining the amount includible in gross income under this subsection—

(i) all modified endowment contracts issued by the same company to the same policyholder during any calendar year shall be treated as 1 modified endowment contract, and

(ii) all annuity contracts issued by the same company to the same policyholder during any calendar year shall be treated as 1 annuity contract.

The preceding sentence shall not apply to any contract described in paragraph (5)(D).

(B) REGULATORY AUTHORITY.—The Secretary may by regulations prescribe such additional rules as may be necessary or appropriate to prevent avoidance of the purposes of this subsection through serial purchases of contracts or otherwise.

(f) SPECIAL RULES FOR COMPUTING EMPLOYEES' CONTRIBUTIONS.—In computing, for purposes of subsection (c)(1)(A), the aggregate amount of premiums or other consideration paid for the contract, and for purposes of subsection (e)(6), the aggregate premiums or other consideration paid, amounts contributed by the employer shall be included, but only to the extent that—

(1) such amounts were includible in the gross income of the employee under this subtitle or prior income tax laws; or

(2) if such amounts had been paid directly to the employee at the time they were contributed, they would not have been includible in the gross income of the employee under the law applicable at the time of such contribution.

Paragraph (2) shall not apply to amounts which were contributed by the employer after December 31, 1962, and which would not have been includible in the gross income of the employee by reason of the application of section 911 if such amounts had been paid directly to the employee at the time of contribution. The preceding sentence shall not apply to amounts which were contributed by the employer, as determined under regulations prescribed by the Secretary, to provide pension or annuity credits, to the extent such credits are attributable to services performed before January 1, 1963, and are provided pursuant to pension or annuity plan provisions in existence on March 12, 1962, and on that date applicable to such services, or to the extent such credits are attributable to services performed as a foreign missionary (within the meaning of section 403(b)(2)(D)(iii), as in effect before the enactment of the Economic Growth and Tax Relief Reconciliation Act of 2001).

(g) RULES FOR TRANSFEREE WHERE TRANSFER WAS FOR VALUE.—Where any contract (or any interest therein) is transferred (by assignment or otherwise) for a valuable consideration, to the extent that the contract (or interest therein) does not, in the hands of the transferee, have a basis which is determined by reference to the basis in the hands of the transferor, then—

(1) for purposes of this section, only the actual value of such consideration, plus the amount of the premiums and other consideration paid by the transferee after the transfer, shall be taken into account in computing the aggregate amount of the premiums or other consideration paid for the contract;

(2) for purposes of subsection (c)(1)(B), there shall be taken into account only the aggregate amount received under the contract by the transferee before the annuity starting date, to the extent that such amount was excludable from gross income under this subtitle or prior income tax laws; and

(3) the annuity starting date is the first day of the first period for which the transferee received an amount under the contract as an annuity.

For purposes of this subsection, the term “transferee” includes a beneficiary of, or the estate of, the transferee.

(h) OPTION TO RECEIVE ANNUITY IN LIEU OF LUMP SUM.—If—

(1) a contract provides for payment of a lump sum in full discharge of an obligation under the contract, subject to an option to receive an annuity in lieu of such lump sum;

(2) the option is exercised within 60 days after the day on which such lump sum first became payable; and

(3) part or all of such lump sum would (but for this subsection) be includible in gross income by reason of subsection (e)(1), then, for purposes of this subtitle, no part of such lump sum shall be considered as includible in gross income at the time such lump sum first became payable.

(j) INTEREST.—Notwithstanding any other provision of this section, if any amount is held under an agreement to pay interest thereon, the interest payments shall be included in gross income.

(l) FACE-AMOUNT CERTIFICATES.—For purposes of this section, the term “endowment contract” includes a face-amount certificate, as defined in section 2(a)(15) of the Investment Company Act of 1940 (15 U.S.C., sec. 80a-2), issued after December 31, 1954.

(m) SPECIAL RULES APPLICABLE TO EMPLOYEE ANNUITIES AND DISTRIBUTIONS UNDER EMPLOYEE PLANS.—

(2) COMPUTATION OF CONSIDERATION PAID BY THE EMPLOYEE.—In computing—

(A) the aggregate amount of premiums or other consideration paid for the contract for purposes of subsection (c)(1)(A) (relating to the investment in the contract), and

(B) the aggregate premiums or other consideration paid for purposes of subsection (e)(6) (relating to certain amounts not received as an annuity),

any amount allowed as a deduction with respect to the contract under section 404 which was paid while the employee was an employee within the meaning of section 401(c)(1) shall be treated as consideration contributed by the employer, and there shall not be taken into account any portion of the premiums or other consideration for the contract paid while the employee was an owner-employee which is properly allocable (as determined under regulations prescribed by the Secretary) to the cost of life, accident, health, or other insurance.

(3) LIFE INSURANCE CONTRACTS.—

(A) This paragraph shall apply to any life insurance contract—

(i) purchased as a part of a plan described in section 403(a), or

(ii) purchased by a trust described in section 401(a) which is exempt from tax under section 501(a) if the proceeds of such contract are payable directly or indirectly to a participant in such trust or to a beneficiary of such participant.

(B) Any contribution to a plan described in subparagraph (A)(i) or a trust described in subparagraph (A)(ii) which is allowed as a deduction under section 404, and any income of a trust described in subparagraph (A)(ii), which is determined in accordance with regulations prescribed by the Secretary to have been applied to purchase the life insurance protection under a contract described in subparagraph (A), is includible in the gross income of the participant for the taxable year when so applied.

(C) In the case of the death of an individual insured under a contract described in subparagraph (A), an amount equal to the cash surrender value of the contract immediately before the death of the insured shall be treated as a payment under such plan or a distribution by such trust, and the excess of the amount payable by reason of the death of the insured over such cash surrender value shall not be includible in gross income under this section and shall be treated as provided in section 101.

(5) Penalties applicable to certain amounts received by 5-percent owners (A) This paragraph applies to amounts which are received from a qualified trust described in section 401(a) or under a plan described in section 403(a) at any time by an individual who is, or has been, a 5-percent owner, or by a successor of such an individual, but only to the extent such amounts are determined, under regulations prescribed by the Secretary, to exceed the benefits provided for such individual under the plan formula.

(B) If a person receives an amount to which this paragraph applies, his tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 10 percent of the portion of the amount so received which is includible in his gross income for such taxable year.

(C) For purposes of this paragraph, the term "5-percent owner" means any individual who, at any time during the 5 plan years preceding the plan year ending in the taxable year in which the amount is received, is a 5-percent owner (as defined in section 416(i)(1)(B)).

(6) OWNER-EMPLOYEE DEFINED.—For purposes of this subsection, the term "owner-employee" has the meaning assigned to it by section 401(c)(3) and includes an individual for whose benefit an individual retirement account or annuity described in section 408(a) or (b) is maintained. For purposes of the preceding sentence, the term "owner-employee" shall include an employee within the meaning of section 401(c)(1).

(7) MEANING OF DISABLED.—For purposes of this section, an individual shall be considered to be disabled if he is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration. An individual shall not be considered to be disabled unless he furnishes proof of the existence thereof in such form and manner as the Secretary may require.

(10) DETERMINATION OF INVESTMENT IN THE CONTRACT IN THE CASE OF QUALIFIED DOMESTIC RELATIONS ORDERS.—Under regulations prescribed by the Secretary, in the case of a distribution or payment made to an alternate payee who is the spouse or former spouse of the participant pursuant to a qualified domestic relations order (as defined in section 414(p)), the investment in the contract as of the date prescribed in such regulations shall be allocated on a pro rata basis between the present value of such distribution or payment and the present value of all other benefits payable with respect to the participant to which such order relates.

(n) ANNUITIES UNDER RETIRED SERVICEMAN'S FAMILY PROTECTION PLAN OR SURVIVOR BENEFIT PLAN.—Subsection (b) shall not apply in the case of amounts received after December 31, 1965, as an annuity under chapter 73 of title 10 of the United States Code, but all such amounts shall be excluded from gross income until there has been so excluded (under section 122(b)(1) or this section, including amounts excluded before January 1, 1966) an amount equal to the consideration for the contract (as defined by section 122(b)(2)), plus any amount treated pursuant to section 101 (b)(2)(D) (as in effect on the day before the date of the enactment of the Small Business Job Protection Act of 1996) as additional consideration paid by the employee. Thereafter all amounts so received shall be included in gross income.

(o) SPECIAL RULES FOR DISTRIBUTIONS FROM QUALIFIED PLANS TO WHICH EMPLOYEE MADE DEDUCTIBLE CONTRIBUTIONS.—

(1) TREATMENT OF CONTRIBUTIONS.—For purposes of this section and sections 402 and 403, notwithstanding section 414(h), any deductible employee contribution made to a qualified employer plan or government plan shall be treated as an amount contributed by the employer which is not includible in the gross income of the employee.

(3) AMOUNTS CONSTRUCTIVELY RECEIVED.—

(A) IN GENERAL.—For purposes of this subsection, rules similar to the rules provided by subsection (p) (other than the exception contained in paragraph (2) thereof) shall apply.

(B) PURCHASE OF LIFE INSURANCE.—To the extent any amount of accumulated deductible employee contributions of an employee are applied to the purchase of life insurance contracts, such amount shall be treated as distributed to the employee in the year so applied.

(4) SPECIAL RULE FOR TREATMENT OF ROLLOVER AMOUNTS.—For purposes of sections 402(c), 403(a)(4), 403(b)(8), 408(d)(3), and 457(e)(16), the Secretary shall prescribe regulations providing for such allocations of amounts attributable to accumulated deductible employee contributions, and for such other rules, as may be necessary to insure that such accumulated deductible employee contributions do not become eligible for additional tax benefits (or freed from limitations) through the use of rollovers.

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

(A) DEDUCTIBLE EMPLOYEE CONTRIBUTIONS.—The term “deductible employee contributions” means any qualified voluntary employee contribution (as defined in section 219(e)(2)) made after December 31, 1981, in a taxable year beginning after such date and made for a taxable year beginning before January 1, 1987, and allowable as a deduction under section 219(a) for such taxable year.

(B) ACCUMULATED DEDUCTIBLE EMPLOYEE CONTRIBUTIONS.—The term “accumulated deductible employee contributions” means the deductible employee contributions—

(i) increased by the amount of income and gain allocable to such contributions, and

(ii) reduced by the sum of the amount of loss and expense allocable to such contributions and the amounts distributed with respect to the employee which are attributable to such contributions (or income or gain allocable to such contributions).

(C) QUALIFIED EMPLOYER PLAN.—The term “qualified employer plan” has the meaning given to such term by subsection (p)(3)(A)(i).

(D) GOVERNMENT PLAN.—The term “government plan” has the meaning given such term by subsection (p)(3)(B).

(6) ORDERING RULES.—Unless the plan specifies otherwise, any distribution from such plan shall not be treated as being made from the accumulated deductible employee contributions, until all other amounts to the credit of the employee have been distributed.

(p) LOANS TREATED AS DISTRIBUTIONS.—For purposes of this section—

(1) TREATMENT AS DISTRIBUTIONS.—

(A) LOANS.—If during any taxable year a participant or beneficiary receives (directly or indirectly) any amount as a loan from a qualified employer plan, such amount shall be treated as having been received by such individual as a distribution under such plan.

(B) ASSIGNMENTS OR PLEDGES.—If during any taxable year a participant or beneficiary assigns (or agrees to assign) or pledges (or agrees to pledge) any portion of his interest in a qualified employer plan, such portion shall be treated as having been received by such individual as a loan from such plan.

(2) EXCEPTION FOR CERTAIN LOANS.—

(A) GENERAL RULE.—Paragraph (1) shall not apply to any loan to the extent that such loan (when added to the outstanding balance of all other loans from such plan whether made on, before, or after August 13, 1982), does not exceed the lesser of—

(i) \$50,000, reduced by the excess (if any) of—

(I) the highest outstanding balance of loans from the plan during the 1-year period ending on the day before the date on which such loan was made, over

(II) the outstanding balance of loans from the plan on the date on which such loan was made, or

(ii) the greater of (I) one-half of the present value of the nonforfeitable accrued benefit of the employee under the plan, or (II) \$10,000.

For purposes of clause (ii), the present value of the nonforfeitable accrued benefit shall be determined without regard to any accumulated deductible employee contributions (as defined in subsection (o)(5)(B)).

(B) REQUIREMENT THAT LOAN BE REPAYABLE WITHIN 5 YEARS.—

(i) IN GENERAL.—Subparagraph (A) shall not apply to any loan unless such loan, by its terms, is required to be repaid within 5 years.

(ii) EXCEPTION FOR HOME LOANS.—Clause (i) shall not apply to any loan used to acquire any dwelling unit which within a reasonable time is to be used (determined at the time the loan is made) as the principal residence of the participant.

(C) REQUIREMENT OF LEVEL AMORTIZATION.—Except as provided in regulations, this paragraph shall not apply to any loan unless substantially level amortization of such loan (with payments not less frequently than quarterly) is required over the term of the loan.

(D) RELATED EMPLOYERS AND RELATED PLANS.—For purposes of this paragraph—

(i) the rules of subsections (b), (c), and (m) of section 414 shall apply, and

(ii) all plans of an employer (determined after the application of such subsections) shall be treated as 1 plan.

(3) DENIAL OF INTEREST DEDUCTIONS IN CERTAIN CASES.—

(A) IN GENERAL.—No deduction otherwise allowable under this chapter shall be allowed under this chapter for any interest paid or accrued on any loan to which paragraph (1) does not apply by reason of paragraph (2) during the period described in subparagraph (B).

(B) PERIOD TO WHICH SUBPARAGRAPH (A) APPLIES.—For purposes of subparagraph (A), the period described in this subparagraph is the period—

(i) on or after the 1st day on which the individual to whom the loan is made is a key employee (as defined in section 416(i)), or

(ii) such loan is secured by amounts attributable to elective deferrals described in subparagraph (A) or (C) of section 402(g)(3).

(4) QUALIFIED EMPLOYER PLAN, ETC.—For purposes of this subsection—

(A) QUALIFIED EMPLOYER PLAN.—

(i) IN GENERAL.—The term “qualified employer plan” means—

(I) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a),

(II) an annuity plan described in section 403(a), and

(III) a plan under which amounts are contributed by an individual’s employer for an annuity contract described in section 403(b).

(ii) SPECIAL RULE.—The term “qualified employer plan” shall include any plan which was (or was determined to be) a qualified employer plan or a government plan.

(B) GOVERNMENT PLAN.—The term “government plan” means any plan, whether or not qualified, established and maintained for its employees by the United States, by a State or political subdivision thereof, or by an agency or instrumentality of any of the foregoing.

(5) SPECIAL RULES FOR LOANS, ETC., FROM CERTAIN CONTRACTS.—For purposes of this subsection, any amount received as a loan under a contract purchased under a qualified employer plan (and any assignment or pledge with respect to such a contract) shall be treated as a loan under such employer plan.

(q) 10-PERCENT PENALTY FOR PREMATURE DISTRIBUTIONS FROM ANNUITY CONTRACTS.—

(1) IMPOSITION OF PENALTY.—If any taxpayer receives any amount under an annuity contract, the taxpayer's tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 10 percent of the portion of such amount which is includible in gross income.

(2) SUBSECTION NOT TO APPLY TO CERTAIN DISTRIBUTIONS.—Paragraph 1 shall not apply to any distribution—

(A) made on or after the date on which the taxpayer attains age 59 1/2,

(B) made on or after the death of the holder (or, where the holder is not an individual, the death of the primary annuitant (as defined in subsection (s)(6)(B))),

(C) attributable to the taxpayer's becoming disabled within the meaning of subsection (m)(7),

(D) which is a part of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the taxpayer or the joint lives (or joint life expectancies) of such taxpayer and his designated beneficiary,

(E) from a plan, contract, account, trust, or annuity described in subsection (e)(5)(D),

(F) allocable to investment in the contract before August 14, 1982, or

(G) under a qualified funding asset (within the meaning of section 130(d), but without regard to whether there is a qualified assignment),

(H) to which subsection (t) applies (without regard to paragraph (2) thereof),

(I) under an immediate annuity contract (within the meaning of section 72(u)(4)), or

(J) which is purchased by an employer upon the termination of a plan described in section 401(a) or 403(a) and which is held by the employer until such time as the employee separates from service.

(3) CHANGE IN SUBSTANTIALLY EQUAL PAYMENTS.—If—

(A) paragraph (1) does not apply to a distribution by reason of paragraph (2)(D), and

(B) the series of payments under such paragraph are subsequently modified (other than by reason of death or disability)—

(i) before the close of the 5-year period beginning on the date of the first payment and after the taxpayer attains age 59 1/2, or

(ii) before the taxpayer attains age 59 1/2, the taxpayer's tax for the 1st taxable year in which such modification occurs shall be increased by an amount, determined under regulations, equal to the tax which



(but for paragraph (2)(D)) would have been imposed, plus interest for the deferral period (within the meaning of subsection (t)(4)(B)).

(r) CERTAIN RAILROAD RETIREMENT BENEFITS TREATED AS RECEIVED UNDER EMPLOYER PLANS.—

(1) IN GENERAL.—Notwithstanding any other provision of law, any benefit provided under the Railroad Retirement Act of 1974 (other than a tier 1 railroad retirement benefit) shall be treated for purposes of this title as a benefit provided under an employer plan which meets the requirements of section 401(a).

(2) TIER 2 TAXES TREATED AS CONTRIBUTIONS.—

(A) IN GENERAL.—For purposes of paragraph (1)—

(i) the tier 2 portion of the tax imposed by section 3201 (relating to tax on employees) shall be treated as an employee contribution,

(ii) the tier 2 portion of the tax imposed by section 3211 (relating to tax on employee representatives) shall be treated as an employee contribution, and

(iii) the tier 2 portion of the tax imposed by section 3221 (relating to tax on employers) shall be treated as an employer contribution.

(B) TIER 2 PORTION.—For purposes of subparagraph (A)—

(i) AFTER 1984.—With respect to compensation paid after 1984, the tier 2 portion shall be the taxes imposed by sections 3201(b), 3211(b), and 3221(b).

(ii) AFTER SEPTEMBER 30, 1981, AND BEFORE 1985.—With respect to compensation paid before 1985 for services rendered after September 30, 1981, the tier 2 portion shall be—

(I) so much of the tax imposed by section 3201 as is determined at the 2 percent rate, and

(II) so much of the taxes imposed by sections 3211 and 3221 as is determined at the 11.75 percent rate.

With respect to compensation paid for services rendered after December 31, 1983, and before 1985, subclause (I) shall be applied by substituting “2.75 percent” for “2 percent”, and subclause (II) shall be applied by substituting “12.75 percent” for “11.75 percent”.

(iii) BEFORE OCTOBER 1, 1981.—With respect to compensation paid for services rendered during any period before October 1, 1981, the tier 2 portion shall be the excess (if any) of—

(I) the tax imposed for such period by section 3201, 3211, or 3221, as the case may be (other than any tax imposed with respect to man-hours), over

(II) the tax which would have been imposed by such section for such period had the rates of the comparable taxes imposed by chapter 21 for such period applied under such section.

(C) CONTRIBUTIONS NOT ALLOCABLE TO SUPPLEMENTAL ANNUITY OR WINDFALL BENEFITS.—For purposes of para-

graph (1), no amount treated as an employee contribution under this paragraph shall be allocated to—

- (i) any supplemental annuity paid under section 2(b) of the Railroad Retirement Act of 1974, or
- (ii) any benefit paid under section 3(h), 4(e), or 4(h) of such Act.

(3) TIER 1 RAILROAD RETIREMENT BENEFIT.—For purposes of paragraph (1), the term “tier 1 railroad retirement benefit” has the meaning given such term by section 86(d)(4).

(s) REQUIRED DISTRIBUTIONS WHERE HOLDER DIES BEFORE ENTIRE INTEREST IS DISTRIBUTED.—

(1) IN GENERAL.—A contract shall not be treated as an annuity contract for purposes of this title unless it provides that—

(A) if any holder of such contract dies on or after the annuity starting date and before the entire interest in such contract has been distributed, the remaining portion of such interest will be distributed at least as rapidly as under the method of distributions being used as of the date of his death, and

(B) if any holder of such contract dies before the annuity starting date, the entire interest in such contract will be distributed within 5 years after the death of such holder.

(2) EXCEPTION FOR CERTAIN AMOUNTS PAYABLE OVER LIFE OF BENEFICIARY.—If—

(A) any portion of the holder’s interest is payable to (or for the benefit of) a designated beneficiary,

(B) such portion will be distributed (in accordance with regulations) over the life of such designated beneficiary (or over a period not extending beyond the life expectancy of such beneficiary), and

(C) such distributions begin not later than 1 year after the date of the holder’s death or such later date as the Secretary may by regulations prescribe,

then for purposes of paragraph (1), the portion referred to in subparagraph (A) shall be treated as distributed on the day on which such distributions begin.

(3) SPECIAL RULE WHERE SURVIVING SPOUSE BENEFICIARY.—If the designated beneficiary referred to in paragraph (2)(A) is the surviving spouse of the holder of the contract, paragraphs (1) and (2) shall be applied by treating such spouse as the holder of such contract.

(4) DESIGNATED BENEFICIARY.—For purposes of this subsection, the term “designated beneficiary” means any individual designated a beneficiary by the holder of the contract.

(5) EXCEPTION FOR CERTAIN ANNUITY CONTRACTS.—This subsection shall not apply to any annuity contract—

(A) which is provided—

- (i) under a plan described in section 401(a) which includes a trust exempt from tax under section 501, or
- (ii) under a plan described in section 403(a),

(B) which is described in section 403(b),

(C) which is an individual retirement annuity or provided under an individual retirement account or annuity, or

(D) which is a qualified funding asset (as defined in section 130(d), but without regard to whether there is a qualified assignment).

(6) SPECIAL RULE WHERE HOLDER IS CORPORATION OR OTHER NON-INDIVIDUAL.—

(A) IN GENERAL.—For purposes of this subsection, if the holder of the contract is not an individual, the primary annuitant shall be treated as the holder of the contract.

(B) PRIMARY ANNUITANT.—For purposes of subparagraph (A), the term “primary annuitant” means the individual, the events in the life of whom are of primary importance in affecting the timing or amount of the payout under the contract.

(7) TREATMENT OF CHANGES IN PRIMARY ANNUITANT WHERE HOLDER OF CONTRACT IS NOT AN INDIVIDUAL.—For purposes of this subsection, in the case of a holder of an annuity contract which is not an individual, if there is a change in a primary annuitant (as defined in paragraph (6)(B)), such change shall be treated as the death of the holder.

(t) 10-PERCENT ADDITIONAL TAX ON EARLY DISTRIBUTIONS FROM QUALIFIED RETIREMENT PLANS.—

(1) IMPOSITION OF ADDITIONAL TAX.—If any taxpayer receives any amount from a qualified retirement plan (as defined in section 4974(c)), the taxpayer’s tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 10 percent of the portion of such amount which is includible in gross income.

(2) SUBSECTION NOT TO APPLY TO CERTAIN DISTRIBUTIONS.—Except as provided in paragraphs (3) and (4), paragraph (1) shall not apply to any of the following distributions:

(A) IN GENERAL.—Distributions which are—

(i) made on or after the date on which the employee attains age 59 1/2,

(ii) made to a beneficiary (or to the estate of the employee) on or after the death of the employee,

(iii) attributable to the employee’s being disabled within the meaning of subsection (m)(7),

(iv) part of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the employee or the joint lives (or joint life expectancies) of such employee and his designated beneficiary,

(v) made to an employee after separation from service after attainment of age 55,

(vi) dividends paid with respect to stock of a corporation which are described in section 404(k),

(vii) made on account of a levy under section 6331 on the qualified retirement plan, or

(viii) payments under a phased retirement annuity under section 8366a(a)(5) or 8412a(a)(5) of title 5, United States Code, or a composite retirement annuity under section 8366a(a)(1) or 8412a(a)(1) of such title.

(B) MEDICAL EXPENSES.—Distributions made to the employee (other than distributions described in subparagraph (A), (C), or (D)) to the extent such distributions do not ex-

ceed the amount allowable as a deduction under section 213 to the employee for amounts paid during the taxable year for medical care (determined without regard to whether the employee itemizes deductions for such taxable year).

(C) PAYMENTS TO ALTERNATE PAYEES PURSUANT TO QUALIFIED DOMESTIC RELATIONS ORDERS.—Any distribution to an alternate payee pursuant to a qualified domestic relations order (within the meaning of section 414(p)(1)).

(D) DISTRIBUTIONS TO UNEMPLOYED INDIVIDUALS FOR HEALTH INSURANCE PREMIUMS.—

(i) IN GENERAL.—Distributions from an individual retirement plan to an individual after separation from employment—

(I) if such individual has received unemployment compensation for 12 consecutive weeks under any Federal or State unemployment compensation law by reason of such separation,

(II) if such distributions are made during any taxable year during which such unemployment compensation is paid or the succeeding taxable year, and

(III) to the extent such distributions do not exceed the amount paid during the taxable year for insurance described in section 213(d)(1)(D) with respect to the individual and the individual's spouse and dependents (as defined in [section 152] *section 7706*, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof).

(ii) DISTRIBUTIONS AFTER REEMPLOYMENT.—Clause (i) shall not apply to any distribution made after the individual has been employed for at least 60 days after the separation from employment to which clause (i) applies.

(iii) SELF-EMPLOYED INDIVIDUALS.—To the extent provided in regulations, a self-employed individual shall be treated as meeting the requirements of clause (i)(I) if, under Federal or State law, the individual would have received unemployment compensation but for the fact the individual was self-employed.

(E) DISTRIBUTIONS FROM INDIVIDUAL RETIREMENT PLANS FOR HIGHER EDUCATION EXPENSES.—Distributions to an individual from an individual retirement plan to the extent such distributions do not exceed the qualified higher education expenses (as defined in paragraph (7)) of the taxpayer for the taxable year. Distributions shall not be taken into account under the preceding sentence if such distributions are described in subparagraph (A), (C), or (D) or to the extent paragraph (1) does not apply to such distributions by reason of subparagraph (B).

(F) DISTRIBUTIONS FROM CERTAIN PLANS FOR FIRST HOME PURCHASES.—Distributions to an individual from an individual retirement plan which are qualified first-time homebuyer distributions (as defined in paragraph (8)). Distributions shall not be taken into account under the preceding

sentence if such distributions are described in subparagraph (A), (C), (D), or (E) or to the extent paragraph (1) does not apply to such distributions by reason of subparagraph (B).

(G) DISTRIBUTIONS FROM RETIREMENT PLANS TO INDIVIDUALS CALLED TO ACTIVE DUTY.—

(i) IN GENERAL.—Any qualified reservist distribution.

(ii) AMOUNT DISTRIBUTED MAY BE REPAID.—Any individual who receives a qualified reservist distribution may, at any time during the 2-year period beginning on the day after the end of the active duty period, make one or more contributions to an individual retirement plan of such individual in an aggregate amount not to exceed the amount of such distribution. The dollar limitations otherwise applicable to contributions to individual retirement plans shall not apply to any contribution made pursuant to the preceding sentence. No deduction shall be allowed for any contribution pursuant to this clause.

(iii) QUALIFIED RESERVIST DISTRIBUTION.—For purposes of this subparagraph, the term “qualified reservist distribution” means any distribution to an individual if—

(I) such distribution is from an individual retirement plan, or from amounts attributable to employer contributions made pursuant to elective deferrals described in subparagraph (A) or (C) of section 402(g)(3) or section 501(c)(18)(D)(iii),

(II) such individual was (by reason of being a member of a reserve component (as defined in section 101 of title 37, United States Code)) ordered or called to active duty for a period in excess of 179 days or for an indefinite period, and

(III) such distribution is made during the period beginning on the date of such order or call and ending at the close of the active duty period.

(iv) APPLICATION OF SUBPARAGRAPH.—This subparagraph applies to individuals ordered or called to active duty after September 11, 2001. In no event shall the 2-year period referred to in clause (ii) end before the date which is 2 years after the date of the enactment of this subparagraph.

(3) LIMITATIONS.—

(A) CERTAIN EXCEPTIONS NOT TO APPLY TO INDIVIDUAL RETIREMENT PLANS.—Subparagraphs (A)(v) and (C) of paragraph (2) shall not apply to distributions from an individual retirement plan.

(B) PERIODIC PAYMENTS UNDER QUALIFIED PLANS MUST BEGIN AFTER SEPARATION.—Paragraph (2)(A)(iv) shall not apply to any amount paid from a trust described in section 401(a) which is exempt from tax under section 501(a) or from a contract described in section 72(e)(5)(D)(ii) unless the series of payments begins after the employee separates from service.

## (4) CHANGE IN SUBSTANTIALLY EQUAL PAYMENTS.—

## (A) IN GENERAL.—If—

(i) paragraph (1) does not apply to a distribution by reason of paragraph (2)(A)(iv), and

(ii) the series of payments under such paragraph are subsequently modified (other than by reason of death or disability or a distribution to which paragraph (10) applies)—

(I) before the close of the 5-year period beginning with the date of the first payment and after the employee attains age 59 1/2, or

(II) before the employee attains age 59 1/2, the taxpayer's tax for the 1st taxable year in which such modification occurs shall be increased by an amount, determined under regulations, equal to the tax which (but for paragraph (2)(A)(iv)) would have been imposed, plus interest for the deferral period.

(B) DEFERRAL PERIOD.—For purposes of this paragraph, the term “deferral period” means the period beginning with the taxable year in which (without regard to paragraph (2)(A)(iv)) the distribution would have been includible in gross income and ending with the taxable year in which the modification described in subparagraph (A) occurs.

(5) EMPLOYEE.—For purposes of this subsection, the term “employee” includes any participant, and in the case of an individual retirement plan, the individual for whose benefit such plan was established.

(6) SPECIAL RULES FOR SIMPLE RETIREMENT ACCOUNTS.—In the case of any amount received from a simple retirement account (within the meaning of section 408(p)) during the 2-year period beginning on the date such individual first participated in any qualified salary reduction arrangement maintained by the individual's employer under section 408(p)(2), paragraph (1) shall be applied by substituting “25 percent” for “10 percent”.

(7) QUALIFIED HIGHER EDUCATION EXPENSES.—For purposes of paragraph (2)(E)—

(A) IN GENERAL.—The term “qualified higher education expenses” means qualified higher education expenses (as defined in section 529(e)(3)) for education furnished to—

(i) the taxpayer,

(ii) the taxpayer's spouse, or

(iii) any child (as defined in [section 152(f)(1)] *section 7706(f)(1)*) or grandchild of the taxpayer or the taxpayer's spouse,

at an eligible educational institution (as defined in section 529(e)(5)).

(B) COORDINATION WITH OTHER BENEFITS.—The amount of qualified higher education expenses for any taxable year shall be reduced as provided in section 25A(g)(2).

(8) QUALIFIED FIRST-TIME HOMEBUYER DISTRIBUTIONS.—For purposes of paragraph (2)(F)—

(A) **IN GENERAL.**—The term “qualified first-time homebuyer distribution” means any payment or distribution received by an individual to the extent such payment or distribution is used by the individual before the close of the 120th day after the day on which such payment or distribution is received to pay qualified acquisition costs with respect to a principal residence of a first-time homebuyer who is such individual, the spouse of such individual, or any child, grandchild, or ancestor of such individual or the individual’s spouse.

(B) **LIFETIME DOLLAR LIMITATION.**—The aggregate amount of payments or distributions received by an individual which may be treated as qualified first-time homebuyer distributions for any taxable year shall not exceed the excess (if any) of—

(i) \$10,000, over

(ii) the aggregate amounts treated as qualified first-time homebuyer distributions with respect to such individual for all prior taxable years.

(C) **QUALIFIED ACQUISITION COSTS.**—For purposes of this paragraph, the term “qualified acquisition costs” means the costs of acquiring, constructing, or reconstructing a residence. Such term includes any usual or reasonable settlement, financing, or other closing costs.

(D) **FIRST-TIME HOMEBUYER; OTHER DEFINITIONS.**—For purposes of this paragraph—

(i) **FIRST-TIME HOMEBUYER.**—The term “first-time homebuyer” means any individual if—

(I) such individual (and if married, such individual’s spouse) had no present ownership interest in a principal residence during the 2-year period ending on the date of acquisition of the principal residence to which this paragraph applies, and

(II) subsection (h) or (k) of section 1034 (as in effect on the day before the date of the enactment of this paragraph) did not suspend the running of any period of time specified in section 1034 (as so in effect) with respect to such individual on the day before the date the distribution is applied pursuant to subparagraph (A).

(ii) **PRINCIPAL RESIDENCE.**—The term “principal residence” has the same meaning as when used in section 121.

(iii) **DATE OF ACQUISITION.**—The term “date of acquisition” means the date—

(I) on which a binding contract to acquire the principal residence to which subparagraph (A) applies is entered into, or

(II) on which construction or reconstruction of such a principal residence is commenced.

(E) **SPECIAL RULE WHERE DELAY IN ACQUISITION.**—If any distribution from any individual retirement plan fails to meet the requirements of subparagraph (A) solely by reason of a delay or cancellation of the purchase or construction of the residence, the amount of the distribution may

be contributed to an individual retirement plan as provided in section 408(d)(3)(A)(i) (determined by substituting “120th day” for “60th day” in such section), except that—

(i) section 408(d)(3)(B) shall not be applied to such contribution, and

(ii) such amount shall not be taken into account in determining whether section 408(d)(3)(B) applies to any other amount.

(9) SPECIAL RULE FOR ROLLOVERS TO SECTION 457 PLANS.—For purposes of this subsection, a distribution from an eligible deferred compensation plan (as defined in section 457(b)) of an eligible employer described in section 457(e)(1)(A) shall be treated as a distribution from a qualified retirement plan described in 4974(c)(1) to the extent that such distribution is attributable to an amount transferred to an eligible deferred compensation plan from a qualified retirement plan (as defined in section 4974(c)).

(10) DISTRIBUTIONS TO QUALIFIED PUBLIC SAFETY EMPLOYEES IN GOVERNMENTAL PLANS.—

(A) IN GENERAL.—In the case of a distribution to a qualified public safety employee from a governmental plan (within the meaning of section 414(d)), paragraph (2)(A)(v) shall be applied by substituting “age 50” for “age 55”.

(B) QUALIFIED PUBLIC SAFETY EMPLOYEE.—For purposes of this paragraph, the term “qualified public safety employee” means—

(i) any employee of a State or political subdivision of a State who provides police protection, firefighting services, or emergency medical services for any area within the jurisdiction of such State or political subdivision, or

(ii) any Federal law enforcement officer described in section 8331(20) or 8401(17) of title 5, United States Code, any Federal customs and border protection officer described in section 8331(31) or 8401(36) of such title, any Federal firefighter described in section 8331(21) or 8401(14) of such title, any air traffic controller described in 8331(30) or 8401(35) of such title, any nuclear materials courier described in section 8331(27) or 8401(33) of such title, any member of the United States Capitol Police, any member of the Supreme Court Police, or any diplomatic security special agent of the Department of State.

(u) TREATMENT OF ANNUITY CONTRACTS NOT HELD BY NATURAL PERSONS.—

(1) IN GENERAL.—If any annuity contract is held by a person who is not a natural person—

(A) such contract shall not be treated as an annuity contract for purposes of this subtitle (other than subchapter L), and

(B) the income on the contract for any taxable year of the policyholder shall be treated as ordinary income received or accrued by the owner during such taxable year.



For purposes of this paragraph, holding by a trust or other entity as an agent for a natural person shall not be taken into account.

(2) INCOME ON THE CONTRACT.—

(A) IN GENERAL.—For purposes of paragraph (1), the term “income on the contract” means, with respect to any taxable year of the policyholder, the excess of—

(i) the sum of the net surrender value of the contract as of the close of the taxable year plus all distributions under the contract received during the taxable year or any prior taxable year, reduced by

(ii) the sum of the amount of net premiums under the contract for the taxable year and prior taxable years and amounts includible in gross income for prior taxable years with respect to such contract under this subsection.

Where necessary to prevent the avoidance of this subsection, the Secretary may substitute “fair market value of the contract” for “net surrender value of the contract” each place it appears in the preceding sentence.

(B) NET PREMIUMS.—For purposes of this paragraph, the term “net premiums” means the amount of premiums paid under the contract reduced by any policyholder dividends.

(3) EXCEPTIONS.—This subsection shall not apply to any annuity contract which—

(A) is acquired by the estate of a decedent by reason of the death of the decedent,

(B) is held under a plan described in section 401(a) or 403(a), under a program described in section 403(b), or under an individual retirement plan,

(C) is a qualified funding asset (as defined in section 130(d), but without regard to whether there is a qualified assignment),

(D) is purchased by an employer upon the termination of a plan described in section 401(a) or 403(a) and is held by the employer until all amounts under such contract are distributed to the employee for whom such contract was purchased or the employee’s beneficiary, or

(E) is an immediate annuity.

(4) IMMEDIATE ANNUITY.—For purposes of this subsection, the term “immediate annuity” means an annuity—

(A) which is purchased with a single premium or annuity consideration,

(B) the annuity starting date (as defined in subsection (c)(4)) of which commences no later than 1 year from the date of the purchase of the annuity, and

(C) which provides for a series of substantially equal periodic payments (to be made not less frequently than annually) during the annuity period.

(v) 10-PERCENT ADDITIONAL TAX FOR TAXABLE DISTRIBUTIONS FROM MODIFIED ENDOWMENT CONTRACTS.—

(1) IMPOSITION OF ADDITIONAL TAX.—If any taxpayer receives any amount under a modified endowment contract (as defined in section 7702A), the taxpayer’s tax under this chapter for the taxable year in which such amount is received shall be in-

creased by an amount equal to 10 percent of the portion of such amount which is includible in gross income.

(2) SUBSECTION NOT TO APPLY TO CERTAIN DISTRIBUTIONS.— Paragraph (1) shall not apply to any distribution—

(A) made on or after the date on which the taxpayer attains age 59 1/2,

(B) which is attributable to the taxpayer's becoming disabled (within the meaning of subsection (m)(7)), or

(C) which is part of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the taxpayer or the joint lives (or joint life expectancies) of such taxpayer and his beneficiary.

(w) APPLICATION OF BASIS RULES TO NONRESIDENT ALIENS.—

(1) IN GENERAL.—Notwithstanding any other provision of this section, for purposes of determining the portion of any distribution which is includible in gross income of a distributee who is a citizen or resident of the United States, the investment in the contract shall not include any applicable nontaxable contributions or applicable nontaxable earnings.

(2) APPLICABLE NONTAXABLE CONTRIBUTION.—For purposes of this subsection, the term “applicable nontaxable contribution” means any employer or employee contribution—

(A) which was made with respect to compensation—

(i) for labor or personal services performed by an employee who, at the time the labor or services were performed, was a nonresident alien for purposes of the laws of the United States in effect at such time, and

(ii) which is treated as from sources without the United States, and

(B) which was not subject to income tax (and would have been subject to income tax if paid as cash compensation when the services were rendered) under the laws of the United States or any foreign country.

(3) APPLICABLE NONTAXABLE EARNINGS.—For purposes of this subsection, the term “applicable nontaxable earnings” means earnings—

(A) which are paid or accrued with respect to any employer or employee contribution which was made with respect to compensation for labor or personal services performed by an employee,

(B) with respect to which the employee was at the time the earnings were paid or accrued a nonresident alien for purposes of the laws of the United States, and

(C) which were not subject to income tax under the laws of the United States or any foreign country.

(4) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this subsection, including regulations treating contributions and earnings as not subject to tax under the laws of any foreign country where appropriate to carry out the purposes of this subsection.

(x) CROSS REFERENCE.—For limitation on adjustments to basis of annuity contracts sold, see section 1021.

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**PART III—ITEMS SPECIFICALLY EXCLUDED FROM  
GROSS INCOME**

\* \* \* \* \*

**SEC. 105. AMOUNTS RECEIVED UNDER ACCIDENT AND HEALTH PLANS.**

(a) **AMOUNTS ATTRIBUTABLE TO EMPLOYER CONTRIBUTIONS.**—Except as otherwise provided in this section, amounts received by an employee through accident or health insurance for personal injuries or sickness shall be included in gross income to the extent such amounts (1) are attributable to contributions by the employer which were not includible in the gross income of the employee, or (2) are paid by the employer.

(b) **AMOUNTS EXPENDED FOR MEDICAL CARE.**—Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 213 (relating to medical, etc., expenses) for any prior taxable year, gross income does not include amounts referred to in subsection (a) if such amounts are paid, directly or indirectly, to the taxpayer to reimburse the taxpayer for expenses incurred by him for the medical care (as defined in section 213(d)) of the taxpayer, his spouse, his dependents (as defined in section 152) as defined in section 7706, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof, and any child (as defined in section 152(f)(1)) section 7706(f)(1) of the taxpayer who as of the end of the taxable year has not attained age 27. Any child to whom section 152(e) section 7706(e) applies shall be treated as a dependent of both parents for purposes of this subsection.

(c) **PAYMENTS UNRELATED TO ABSENCE FROM WORK.**—Gross income does not include amounts referred to in subsection (a) to the extent such amounts—

(1) constitute payment for the permanent loss or loss of use of a member or function of the body, or the permanent disfigurement, of the taxpayer, his spouse, or a dependent (as defined in section 152) section 7706, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof, and

(2) are computed with reference to the nature of the injury without regard to the period the employee is absent from work.

(e) **ACCIDENT AND HEALTH PLANS.**—For purposes of this section and section 104—

(1) amounts received under an accident or health plan for employees, and

(2) amounts received from a sickness and disability fund for employees maintained under the law of a State or the District of Columbia,

shall be treated as amounts received through accident or health insurance.

(f) **RULES FOR APPLICATION OF SECTION 213.**—For purposes of section 213(a) (relating to medical, dental, etc., expenses) amounts excluded from gross income under subsection (c) shall not be considered as compensation (by insurance or otherwise) for expenses paid for medical care.

(g) **SELF-EMPLOYED INDIVIDUAL NOT CONSIDERED AN EMPLOYEE.**—For purposes of this section, the term “employee” does not include an individual who is an employee within the meaning of section 401(c)(1) (relating to self-employed individuals).

(h) AMOUNT PAID TO HIGHLY COMPENSATED INDIVIDUALS UNDER A DISCRIMINATORY SELF-INSURED MEDICAL EXPENSE REIMBURSEMENT PLAN.—

(1) IN GENERAL.—In the case of amounts paid to a highly compensated individual under a self-insured medical reimbursement plan which does not satisfy the requirements of paragraph (2) for a plan year, subsection (b) shall not apply to such amounts to the extent they constitute an excess reimbursement of such highly compensated individual.

(2) PROHIBITION OF DISCRIMINATION.—A self-insured medical reimbursement plan satisfies the requirements of this paragraph only if—

(A) the plan does not discriminate in favor of highly compensated individuals as to eligibility to participate; and

(B) the benefits provided under the plan do not discriminate in favor of participants who are highly compensated individuals.

(3) NONDISCRIMINATORY ELIGIBILITY CLASSIFICATIONS.—

(A) IN GENERAL.—A self-insured medical reimbursement plan does not satisfy the requirements of subparagraph (A) of paragraph (2) unless such plan benefits—

(i) 70 percent or more of all employees, or 80 percent or more of all the employees who are eligible to benefit under the plan if 70 percent or more of all employees are eligible to benefit under the plan; or

(ii) such employees as qualify under a classification set up by the employer and found by the Secretary not to be discriminatory in favor of highly compensated individuals.

(B) EXCLUSION OF CERTAIN EMPLOYEES.—For purposes of subparagraph (A), there may be excluded from consideration—

(i) employees who have not completed 3 years of service;

(ii) employees who have not attained age 25;

(iii) part-time or seasonal employees;

(iv) employees not included in the plan who are included in a unit of employees covered by an agreement between employee representatives and one or more employers which the Secretary finds to be a collective bargaining agreement, if accident and health benefits were the subject of good faith bargaining between such employee representatives and such employer or employers; and

(v) employees who are nonresident aliens and who receive no earned income (within the meaning of section 911(d)(2)) from the employer which constitutes income from sources within the United States (within the meaning of section 861(a)(3)).

(4) NONDISCRIMINATORY BENEFITS.—A self-insured medical reimbursement plan does not meet the requirements of subparagraph (B) of paragraph (2) unless all benefits provided for participants who are highly compensated individuals are provided for all other participants.

(5) **HIGHLY COMPENSATED INDIVIDUAL DEFINED.**—For purposes of this subsection, the term “highly compensated individual” means an individual who is—

(A) one of the 5 highest paid officers,

(B) a shareholder who owns (with the application of section 318) more than 10 percent in value of the stock of the employer, or

(C) among the highest paid 25 percent of all employees (other than employees described in paragraph (3)(B) who are not participants).

(6) **SELF-INSURED MEDICAL REIMBURSEMENT PLAN.**—The term “self-insured medical reimbursement plan” means a plan of an employer to reimburse employees for expenses referred to in subsection (b) for which reimbursement is not provided under a policy of accident and health insurance.

(7) **EXCESS REIMBURSEMENT OF HIGHLY COMPENSATED INDIVIDUAL.**—For purposes of this section, the excess reimbursement of a highly compensated individual which is attributable to a self-insured medical reimbursement plan is—

(A) in the case of a benefit available to highly compensated individuals but not to all other participants (or which otherwise fails to satisfy the requirements of paragraph (2)(B)), the amount reimbursed under the plan to the employee with respect to such benefit, and

(B) in the case of benefits (other than benefits described in subparagraph (A)) paid to a highly compensated individual by a plan which fails to satisfy the requirements of paragraph (2), the total amount reimbursed to the highly compensated individual for the plan year multiplied by a fraction—

(i) the numerator of which is the total amount reimbursed to all participants who are highly compensated individuals under the plan for the plan year, and

(ii) the denominator of which is the total amount reimbursed to all employees under the plan for such plan year.

In determining the fraction under subparagraph (B), there shall not be taken into account any reimbursement which is attributable to a benefit described in subparagraph (A).

(8) **CERTAIN CONTROLLED GROUPS, ETC.**—All employees who are treated as employed by a single employer under subsection (b), (c), or (m) of section 414 shall be treated as employed by a single employer for purposes of this section.

(9) **REGULATIONS.**—The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this section.

(10) **TIME OF INCLUSION.**—Any amount paid for a plan year that is included in income by reason of this subsection shall be treated as received or accrued in the taxable year of the participant in which the plan year ends.

(i) **SICK PAY UNDER RAILROAD UNEMPLOYMENT INSURANCE ACT.**—Notwithstanding any other provision of law, gross income includes benefits paid under section 2(a) of the Railroad Unemployment Insurance Act for days of sickness; except to the extent such sickness

(as determined in accordance with standards prescribed by the Railroad Retirement Board) is the result of on-the-job injury.

(j) SPECIAL RULE FOR CERTAIN GOVERNMENTAL PLANS.—

(1) IN GENERAL.—For purposes of subsection (b), amounts paid (directly or indirectly) to a qualified taxpayer from an accident or health plan described in paragraph (2) shall not fail to be excluded from gross income solely because such plan, on or before January 1, 2008, provides for reimbursements of health care expenses of a deceased employee's beneficiary (other than an individual described in paragraph (3)(B)).

(2) PLAN DESCRIBED.—An accident or health plan is described in this paragraph if such plan is funded by a medical trust that is established in connection with a public retirement system or established by or on behalf of a State or political subdivision thereof and that—

(A) has been authorized by a State legislature, or

(B) has received a favorable ruling from the Internal Revenue Service that the trust's income is not includible in gross income under section 115 or 501(c)(9).

(3) QUALIFIED TAXPAYER.—For purposes of paragraph (1), with respect to an accident or health plan described in paragraph (2), the term “qualified taxpayer” means a taxpayer who is—

(A) an employee, or

(B) the spouse, dependent (as defined for purposes of subsection (b)), or child (as defined for purposes of such subsection) of an employee.

\* \* \* \* \*

**SEC. 108. INCOME FROM DISCHARGE OF INDEBTEDNESS.**

(a) EXCLUSION FROM GROSS INCOME.—

(1) IN GENERAL.—Gross income does not include any amount which (but for this subsection) would be includible in gross income by reason of the discharge (in whole or in part) of indebtedness of the taxpayer if—

(A) the discharge occurs in a title 11 case,

(B) the discharge occurs when the taxpayer is insolvent,

(C) the indebtedness discharged is qualified farm indebtedness,

(D) in the case of a taxpayer other than a C corporation, the indebtedness discharged is qualified real property business indebtedness, or

(E) the indebtedness discharged is qualified principal residence indebtedness which is discharged—

(i) before January 1, 2018, or ii) subject to an arrangement that is entered into and evidenced in writing before January 1, 2018.

(2) COORDINATION OF EXCLUSIONS.—

(A) TITLE 11 EXCLUSION TAKES PRECEDENCE.—Subparagraphs (B), (C), (D), and (E) of paragraph (1) shall not apply to a discharge which occurs in a title 11 case.

(B) INSOLVENCY EXCLUSION TAKES PRECEDENCE OVER QUALIFIED FARM EXCLUSION AND QUALIFIED REAL PROPERTY BUSINESS EXCLUSION.—Subparagraphs (C) and (D) of para-

graph (1) shall not apply to a discharge to the extent the taxpayer is insolvent.

(C) PRINCIPAL RESIDENCE EXCLUSION TAKES PRECEDENCE OVER INSOLVENCY EXCLUSION UNLESS ELECTED OTHERWISE.—Paragraph (1)(B) shall not apply to a discharge to which paragraph (1)(E) applies unless the taxpayer elects to apply paragraph (1)(B) in lieu of paragraph (1)(E).

(3) INSOLVENCY EXCLUSION LIMITED TO AMOUNT OF INSOLVENCY.—In the case of a discharge to which paragraph (1)(B) applies, the amount excluded under paragraph (1)(B) shall not exceed the amount by which the taxpayer is insolvent.

(b) REDUCTION OF TAX ATTRIBUTES.—

(1) IN GENERAL.—The amount excluded from gross income under subparagraph (A), (B), or (C) of subsection (a)(1) shall be applied to reduce the tax attributes of the taxpayer as provided in paragraph (2).

(2) TAX ATTRIBUTES AFFECTED; ORDER OF REDUCTION.—Except as provided in paragraph (5), the reduction referred to in paragraph (1) shall be made in the following tax attributes in the following order:

(A) NOL.—Any net operating loss for the taxable year of the discharge, and any net operating loss carryover to such taxable year.

(B) GENERAL BUSINESS CREDIT.—Any carryover to or from the taxable year of a discharge of an amount for purposes for determining the amount allowable as a credit under section 38 (relating to general business credit).

(C) MINIMUM TAX CREDIT.—The amount of the minimum tax credit available under section 53(b) as of the beginning of the taxable year immediately following the taxable year of the discharge.

(D) CAPITAL LOSS CARRYOVERS.—Any net capital loss for the taxable year of the discharge, and any capital loss carryover to such taxable year under section 1212.

(E) BASIS REDUCTION.—

(i) IN GENERAL.—The basis of the property of the taxpayer.

(ii) CROSS REFERENCE.—For provisions for making the reduction described in clause (i), see section 1017.

(F) PASSIVE ACTIVITY LOSS AND CREDIT CARRYOVERS.—Any passive activity loss or credit carryover of the taxpayer under section 469(b) from the taxable year of the discharge.

(G) FOREIGN TAX CREDIT CARRYOVERS.—Any carryover to or from the taxable year of the discharge for purposes of determining the amount of the credit allowable under section 27.

(3) AMOUNT OF REDUCTION.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the reductions described in paragraph (2) shall be one dollar for each dollar excluded by subsection (a).

(B) CREDIT CARRYOVER REDUCTION.—The reductions described in subparagraphs (B), (C), and (G) shall be 33 1/3 cents for each dollar excluded by subsection (a). The reduction described in subparagraph (F) in any passive ac-

tivity credit carryover shall be 33 1/3 cents for each dollar excluded by subsection (a).

(4) ORDERING RULES.—

(A) REDUCTIONS MADE AFTER DETERMINATION OF TAX FOR YEAR.—The reductions described in paragraph (2) shall be made after the determination of the tax imposed by this chapter for the taxable year of the discharge.

(B) REDUCTIONS UNDER SUBPARAGRAPH (A) OR (D) OF PARAGRAPH (2).—The reductions described in subparagraph (A) or (D) of paragraph (2) (as the case may be) shall be made first in the loss for the taxable year of the discharge and then in the carryovers to such taxable year in the order of the taxable years from which each such carryover arose.

(C) REDUCTIONS UNDER SUBPARAGRAPHS (B) AND (G) OF PARAGRAPH (2).—The reductions described in subparagraphs (B) and (G) of paragraph (2) shall be made in the order in which carryovers are taken into account under this chapter for the taxable year of the discharge.

(5) ELECTION TO APPLY REDUCTION FIRST AGAINST DEPRECIABLE PROPERTY.—

(A) IN GENERAL.—The taxpayer may elect to apply any portion of the reduction referred to in paragraph (1) to the reduction under section 1017 of the basis of the depreciable property of the taxpayer.

(B) LIMITATION.—The amount to which an election under subparagraph (A) applies shall not exceed the aggregate adjusted bases of the depreciable property held by the taxpayer as of the beginning of the taxable year following the taxable year in which the discharge occurs.

(C) OTHER TAX ATTRIBUTES NOT REDUCED.—Paragraph (2) shall not apply to any amount to which an election under this paragraph applies.

(c) TREATMENT OF DISCHARGE OF QUALIFIED REAL PROPERTY BUSINESS INDEBTEDNESS.—

(1) BASIS REDUCTION.—

(A) IN GENERAL.—The amount excluded from gross income under subparagraph (D) of subsection (a)(1) shall be applied to reduce the basis of the depreciable real property of the taxpayer.

(B) CROSS REFERENCE.—For provisions making the reduction described in subparagraph (A), see section 1017.

(2) LIMITATIONS.—

(A) INDEBTEDNESS IN EXCESS OF VALUE.—The amount excluded under subparagraph (D) of subsection (a)(1) with respect to any qualified real property business indebtedness shall not exceed the excess (if any) of—

(i) the outstanding principal amount of such indebtedness (immediately before the discharge), over

(ii) the fair market value of the real property described in paragraph (3)(A) (as of such time), reduced by the outstanding principal amount of any other qualified real property business indebtedness secured by such property (as of such time).



(B) OVERALL LIMITATION.—The amount excluded under subparagraph (D) of subsection (a)(1) shall not exceed the aggregate adjusted bases of depreciable real property (determined after any reductions under subsections (b) and (g)) held by the taxpayer immediately before the discharge (other than depreciable real property acquired in contemplation of such discharge).

(3) QUALIFIED REAL PROPERTY BUSINESS INDEBTEDNESS.—The term “qualified real property business indebtedness” means indebtedness which—

(A) was incurred or assumed by the taxpayer in connection with real property used in a trade or business and is secured by such real property,

(B) was incurred or assumed before January 1, 1993, or if incurred or assumed on or after such date, is qualified acquisition indebtedness, and

(C) with respect to which such taxpayer makes an election to have this paragraph apply.

Such term shall not include qualified farm indebtedness. Indebtedness under subparagraph (B) shall include indebtedness resulting from the refinancing of indebtedness under subparagraph (B) (or this sentence), but only to the extent it does not exceed the amount of the indebtedness being refinanced.

(4) QUALIFIED ACQUISITION INDEBTEDNESS.—For purposes of paragraph (3)(B), the term “qualified acquisition indebtedness” means, with respect to any real property described in paragraph (3)(A), indebtedness incurred or assumed to acquire, construct, reconstruct, or substantially improve such property.

(5) REGULATIONS.—The Secretary shall issue such regulations as are necessary to carry out this subsection, including regulations preventing the abuse of this subsection through cross-collateralization or other means.

(d) MEANING OF TERMS; SPECIAL RULES RELATING TO CERTAIN PROVISIONS.—

(1) INDEBTEDNESS OF TAXPAYER.—For purposes of this section, the term “indebtedness of the taxpayer” means any indebtedness—

(A) for which the taxpayer is liable, or

(B) subject to which the taxpayer holds property.

(2) TITLE 11 CASE.—For purposes of this section, the term “title 11 case” means a case under title 11 of the United States Code (relating to bankruptcy), but only if the taxpayer is under the jurisdiction of the court in such case and the discharge of indebtedness is granted by the court or is pursuant to a plan approved by the court.

(3) INSOLVENT.—For purposes of this section, the term “insolvent” means the excess of liabilities over the fair market value of assets. With respect to any discharge, whether or not the taxpayer is insolvent, and the amount by which the taxpayer is insolvent, shall be determined on the basis of the taxpayer’s assets and liabilities immediately before the discharge.

(4) Repealed. Pub. L. 99-514, title VIII, Sec. 822(b)(3)(A), Oct. 22, 1986, 100 Stat. 2373

(5) DEPRECIABLE PROPERTY.—The term “depreciable property” has the same meaning as when used in section 1017.

(6) CERTAIN PROVISIONS TO BE APPLIED AT PARTNER LEVEL.—In the case of a partnership, subsections (a), (b), (c), and (g) shall be applied at the partner level.

(7) SPECIAL RULES FOR S CORPORATION.—

(A) CERTAIN PROVISIONS TO BE APPLIED AT CORPORATE LEVEL.—In the case of an S corporation, subsections (a), (b), (c), and (g) shall be applied at the corporate level, including by not taking into account under section 1366(a) any amount excluded under subsection (a) of this section.

(B) REDUCTION IN CARRYOVER OF DISALLOWED LOSSES AND DEDUCTIONS.—In the case of an S corporation, for purposes of subparagraph (A) of subsection (b)(2), any loss or deduction which is disallowed for the taxable year of the discharge under section 1366(d)(1) shall be treated as a net operating loss for such taxable year. The preceding sentence shall not apply to any discharge to the extent that subsection (a)(1)(D) applies to such discharge.

(C) COORDINATION WITH BASIS ADJUSTMENTS UNDER SECTION 1367(B)(2).—For purposes of subsection (e)(6), a shareholder's adjusted basis in indebtedness of an S corporation shall be determined without regard to any adjustments made under section 1367(b)(2).

(8) REDUCTIONS OF TAX ATTRIBUTES IN TITLE 11 CASES OF INDIVIDUALS TO BE MADE BY ESTATE.—In any case under chapter 7 or 11 of title 11 of the United States Code to which section 1398 applies, for purposes of paragraphs (1) and (5) of subsection (b) the estate (and not the individual) shall be treated as the taxpayer. The preceding sentence shall not apply for purposes of applying section 1017 to property transferred by the estate to the individual.

(9) TIME FOR MAKING ELECTION, ETC.—

(A) TIME.—An election under paragraph (5) of subsection (b) or under paragraph (3)(C) of subsection (c) shall be made on the taxpayer's return for the taxable year in which the discharge occurs or at such other time as may be permitted in regulations prescribed by the Secretary.

(B) REVOCATION ONLY WITH CONSENT.—An election referred to in subparagraph (A), once made, may be revoked only with the consent of the Secretary.

(C) MANNER.—An election referred to in subparagraph (A) shall be made in such manner as the Secretary may by regulations prescribe.

(10) CROSS REFERENCE.—For provision that no reduction is to be made in the basis of exempt property of an individual debtor, see section 1017(c)(1).

(e) GENERAL RULES FOR DISCHARGE OF INDEBTEDNESS (INCLUDING DISCHARGES NOT IN TITLE 11 CASES OR INSOLVENCY).—For purposes of this title—

(1) NO OTHER INSOLVENCY EXCEPTION.—Except as otherwise provided in this section, there shall be no insolvency exception from the general rule that gross income includes income from the discharge of indebtedness.

(2) INCOME NOT REALIZED TO EXTENT OF LOST DEDUCTIONS.—No income shall be realized from the discharge of indebtedness

to the extent that payment of the liability would have given rise to a deduction.

(3) ADJUSTMENTS FOR UNAMORTIZED PREMIUM AND DISCOUNT.—The amount taken into account with respect to any discharge shall be properly adjusted for unamortized premium and unamortized discount with respect to the indebtedness discharged.

(4) ACQUISITION OF INDEBTEDNESS BY PERSON RELATED TO DEBTOR.—

(A) TREATED AS ACQUISITION BY DEBTOR.—For purposes of determining income of the debtor from discharge of indebtedness, to the extent provided in regulations prescribed by the Secretary, the acquisition of outstanding indebtedness by a person bearing a relationship to the debtor specified in section 267(b) or 707(b)(1) from a person who does not bear such a relationship to the debtor shall be treated as the acquisition of such indebtedness by the debtor. Such regulations shall provide for such adjustments in the treatment of any subsequent transactions involving the indebtedness as may be appropriate by reason of the application of the preceding sentence.

(B) MEMBERS OF FAMILY.—For purposes of this paragraph, sections 267(b) and 707(b)(1) shall be applied as if section 267(c)(4) provided that the family of an individual consists of the individual's spouse, the individual's children, grandchildren, and parents, and any spouse of the individual's children or grandchildren.

(C) ENTITIES UNDER COMMON CONTROL TREATED AS RELATED.—For purposes of this paragraph, two entities which are treated as a single employer under subsection (b) or (c) of section 414 shall be treated as bearing a relationship to each other which is described in section 267(b).

(5) PURCHASE-MONEY DEBT REDUCTION FOR SOLVENT DEBTOR TREATED AS PRICE REDUCTION.—If—

(A) the debt of a purchaser of property to the seller of such property which arose out of the purchase of such property is reduced,

(B) such reduction does not occur—

(i) in a title 11 case, or

(ii) when the purchaser is insolvent, and

(C) but for this paragraph, such reduction would be treated as income to the purchaser from the discharge of indebtedness,

then such reduction shall be treated as a purchase price adjustment.

(6) INDEBTEDNESS CONTRIBUTED TO CAPITAL.—Except as provided in regulations, for purposes of determining income of the debtor from discharge of indebtedness, if a debtor corporation acquires its indebtedness from a shareholder as a contribution to capital—

(A) section 118 shall not apply, but

(B) such corporation shall be treated as having satisfied the indebtedness with an amount of money equal to the shareholder's adjusted basis in the indebtedness.

(7) RECAPTURE OF GAIN ON SUBSEQUENT SALE OF STOCK.—

(A) IN GENERAL.—If a creditor acquires stock of a debtor corporation in satisfaction of such corporation's indebtedness, for purposes of section 1245—

(i) such stock (and any other property the basis of which is determined in whole or in part by reference to the adjusted basis of such stock) shall be treated as section 1245 property,

(ii) the aggregate amount allowed to the creditor—

(I) as deductions under subsection (a) or (b) of section 166 (by reason of the worthlessness or partial worthlessness of the indebtedness), or

(II) as an ordinary loss on the exchange, shall be treated as an amount allowed as a deduction for depreciation, and

(iii) an exchange of such stock qualifying under section 354(a), 355(a), or 356(a) shall be treated as an exchange to which section 1245(b)(3) applies.

The amount determined under clause (ii) shall be reduced by the amount (if any) included in the creditor's gross income on the exchange.

(B) SPECIAL RULE FOR CASH BASIS TAXPAYERS.—In the case of any creditor who computes his taxable income under the cash receipts and disbursements method, proper adjustment shall be made in the amount taken into account under clause (ii) of subparagraph (A) for any amount which was not included in the creditor's gross income but which would have been included in such gross income if such indebtedness had been satisfied in full.

(C) STOCK OF PARENT CORPORATION.—For purposes of this paragraph, stock of a corporation in control (within the meaning of section 368(c)) of the debtor corporation shall be treated as stock of the debtor corporation.

(D) TREATMENT OF SUCCESSOR CORPORATION.—For purposes of this paragraph, the term "debtor corporation" includes a successor corporation.

(E) PARTNERSHIP RULE.—Under regulations prescribed by the Secretary, rules similar to the rules of the foregoing subparagraphs of this paragraph shall apply with respect to the indebtedness of a partnership.

(8) INDEBTEDNESS SATISFIED BY CORPORATE STOCK OR PARTNERSHIP INTEREST.—For purposes of determining income of a debtor from discharge of indebtedness, if—

(A) a debtor corporation transfers stock, or

(B) a debtor partnership transfers a capital or profits interest in such partnership,

to a creditor in satisfaction of its recourse or nonrecourse indebtedness, such corporation or partnership shall be treated as having satisfied the indebtedness with an amount of money equal to the fair market value of the stock or interest. In the case of any partnership, any discharge of indebtedness income recognized under this paragraph shall be included in the distributive shares of taxpayers which were the partners in the partnership immediately before such discharge.

(9) DISCHARGE OF INDEBTEDNESS INCOME NOT TAKEN INTO ACCOUNT IN DETERMINING WHETHER ENTITY MEETS REIT QUALI-

FICATIONS.—Any amount included in gross income by reason of the discharge of indebtedness shall not be taken into account for purposes of paragraphs (2) and (3) of section 856(c).

(10) INDEBTEDNESS SATISFIED BY ISSUANCE OF DEBT INSTRUMENT.—

(A) IN GENERAL.—For purposes of determining income of a debtor from discharge of indebtedness, if a debtor issues a debt instrument in satisfaction of indebtedness, such debtor shall be treated as having satisfied the indebtedness with an amount of money equal to the issue price of such debt instrument.

(B) ISSUE PRICE.—For purposes of subparagraph (A), the issue price of any debt instrument shall be determined under sections 1273 and 1274. For purposes of the preceding sentence, section 1273(b)(4) shall be applied by reducing the stated redemption price of any instrument by the portion of such stated redemption price which is treated as interest for purposes of this chapter.

(f) STUDENT LOANS.—

(1) IN GENERAL.—In the case of an individual, gross income does not include any amount which (but for this subsection) would be includible in gross income by reason of the discharge (in whole or in part) of any student loan if such discharge was pursuant to a provision of such loan under which all or part of the indebtedness of the individual would be discharged if the individual worked for a certain period of time in certain professions for any of a broad class of employers.

(2) STUDENT LOAN.—For purposes of this subsection, the term “student loan” means any loan to an individual to assist the individual in attending an educational organization described in section 170(b)(1)(A)(ii) made by—

(A) the United States, or an instrumentality or agency thereof,

(B) a State, territory, or possession of the United States, or the District of Columbia, or any political subdivision thereof,

(C) a public benefit corporation—

(i) which is exempt from taxation under section 501(c)(3),

(ii) which has assumed control over a State, county, or municipal hospital, and

(iii) whose employees have been deemed to be public employees under State law, or

(D) any educational organization described in section 170(b)(1)(A)(ii) if such loan is made—

(i) pursuant to an agreement with any entity described in subparagraph (A), (B), or (C) under which the funds from which the loan was made were provided to such educational organization, or

(ii) pursuant to a program of such educational organization which is designed to encourage its students to serve in occupations with unmet needs or in areas with unmet needs and under which the services provided by the students (or former students) are for or under the direction of a governmental unit or an orga-

nization described in section 501(c)(3) and exempt from tax under section 501(a).

The term “student loan” includes any loan made by an educational organization described in section 170(b)(1)(A)(ii) or by an organization exempt from tax under section 501(a) to refinance a loan to an individual to assist the individual in attending any such educational organization but only if the refinancing loan is pursuant to a program of the refinancing organization which is designed as described in subparagraph (D)(ii).

(3) EXCEPTION FOR DISCHARGES ON ACCOUNT OF SERVICES PERFORMED FOR CERTAIN LENDERS.—Paragraph (1) shall not apply to the discharge of a loan made by an organization described in paragraph (2)(D) if the discharge is on account of services performed for either such organization.

(4) PAYMENTS UNDER NATIONAL HEALTH SERVICE CORPS LOAN REPAYMENT PROGRAM AND CERTAIN STATE LOAN REPAYMENT PROGRAMS.—In the case of an individual, gross income shall not include any amount received under section 338B(g) of the Public Health Service Act, under a State program described in section 338I of such Act, or under any other State loan repayment or loan forgiveness program that is intended to provide for the increased availability of health care services in underserved or health professional shortage areas (as determined by such State).

(5) DISCHARGES ON ACCOUNT OF DEATH OR DISABILITY.—

(A) IN GENERAL.—In the case of an individual, gross income does not include any amount which (but for this subsection) would be includible in gross income for such taxable year by reasons of the discharge (in whole or in part) of any loan described in subparagraph (B) [after December 31, 2017, and before January 1, 2026], if such discharge was—

(i) pursuant to subsection (a) or (d) of section 437 of the Higher Education Act of 1965 or the parallel benefit under part D of title IV of such Act (relating to the repayment of loan liability),

(ii) pursuant to section 464(c)(1)(F) of such Act, or

(iii) otherwise discharged on account of the death or total and permanent disability of the student.

(B) LOANS DESCRIBED.—A loan is described in this subparagraph if such loan is—

(i) a student loan (as defined in paragraph (2)), or

(ii) a private education loan (as defined in section 140(7) of the Consumer Credit Protection Act (15 U.S.C. 1650(7))).

(g) SPECIAL RULES FOR DISCHARGE OF QUALIFIED FARM INDEBTEDNESS.—

(1) DISCHARGE MUST BE BY QUALIFIED PERSON.—

(A) IN GENERAL.—Subparagraph (C) of subsection (a)(1) shall apply only if the discharge is by a qualified person.

(B) QUALIFIED PERSON.—For purposes of subparagraph (A), the term “qualified person” has the meaning given to such term by section 49(a)(1)(D)(iv); except that such term

shall include any Federal, State, or local government or agency or instrumentality thereof.

(2) QUALIFIED FARM INDEBTEDNESS.—For purposes of this section, indebtedness of a taxpayer shall be treated as qualified farm indebtedness if—

(A) such indebtedness was incurred directly in connection with the operation by the taxpayer of the trade or business of farming, and

(B) 50 percent or more of the aggregate gross receipts of the taxpayer for the 3 taxable years preceding the taxable year in which the discharge of such indebtedness occurs is attributable to the trade or business of farming.

(3) AMOUNT EXCLUDED CANNOT EXCEED SUM OF TAX ATTRIBUTES AND BUSINESS AND INVESTMENT ASSETS.—

(A) IN GENERAL.—The amount excluded under subparagraph (C) of subsection (a)(1) shall not exceed the sum of—

(i) the adjusted tax attributes of the taxpayer, and

(ii) the aggregate adjusted bases of qualified property held by the taxpayer as of the beginning of the taxable year following the taxable year in which the discharge occurs.

(B) ADJUSTED TAX ATTRIBUTES.—For purposes of subparagraph (A), the term “adjusted tax attributes” means the sum of the tax attributes described in subparagraphs (A), (B), (C), (D), (F), and (G) of subsection (b)(2) determined by taking into account \$3 for each \$1 of the attributes described in subparagraphs (B), (C), and (G) of subsection (b)(2) and the attribute described in subparagraph (F) of subsection (b)(2) to the extent attributable to any passive activity credit carryover.

(C) QUALIFIED PROPERTY.—For purposes of this paragraph, the term “qualified property” means any property which is used or is held for use in a trade or business or for the production of income.

(D) COORDINATION WITH INSOLVENCY EXCLUSION.—For purposes of this paragraph, the adjusted basis of any qualified property and the amount of the adjusted tax attributes shall be determined after any reduction under subsection (b) by reason of amounts excluded from gross income under subsection (a)(1)(B).

(h) SPECIAL RULES RELATING TO QUALIFIED PRINCIPAL RESIDENCE INDEBTEDNESS.—

(1) BASIS REDUCTION.—The amount excluded from gross income by reason of subsection (a)(1)(E) shall be applied to reduce (but not below zero) the basis of the principal residence of the taxpayer.

(2) QUALIFIED PRINCIPAL RESIDENCE INDEBTEDNESS.—For purposes of this section, the term “qualified principal residence indebtedness” means acquisition indebtedness (within the meaning of section 163(h)(3)(B), applied by substituting “\$2,000,000 (\$1,000,000)” for “**[\$1,000,000 (\$500,000)] \$750,000 (\$375,000)**” in clause (ii) thereof) with respect to the principal residence of the taxpayer.

(3) EXCEPTION FOR CERTAIN DISCHARGES NOT RELATED TO TAXPAYER’S FINANCIAL CONDITION.—Subsection (a)(1)(E) shall

not apply to the discharge of a loan if the discharge is on account of services performed for the lender or any other factor not directly related to a decline in the value of the residence or to the financial condition of the taxpayer.

(4) ORDERING RULE.—If any loan is discharged, in whole or in part, and only a portion of such loan is qualified principal residence indebtedness, subsection (a)(1)(E) shall apply only to so much of the amount discharged as exceeds the amount of the loan (as determined immediately before such discharge) which is not qualified principal residence indebtedness.

(5) PRINCIPAL RESIDENCE.—For purposes of this subsection, the term “principal residence” has the same meaning as when used in section 121.

(i) DEFERRAL AND RATABLE INCLUSION OF INCOME ARISING FROM BUSINESS INDEBTEDNESS DISCHARGED BY THE REACQUISITION OF A DEBT INSTRUMENT.—

(1) IN GENERAL.—At the election of the taxpayer, income from the discharge of indebtedness in connection with the reacquisition after December 31, 2008, and before January 1, 2011, of an applicable debt instrument shall be includible in gross income ratably over the 5-taxable-year period beginning with—

(A) in the case of a reacquisition occurring in 2009, the fifth taxable year following the taxable year in which the reacquisition occurs, and

(B) in the case of a reacquisition occurring in 2010, the fourth taxable year following the taxable year in which the reacquisition occurs.

(2) DEFERRAL OF DEDUCTION FOR ORIGINAL ISSUE DISCOUNT IN DEBT FOR DEBT EXCHANGES.—

(A) IN GENERAL.—If, as part of a reacquisition to which paragraph (1) applies, any debt instrument is issued for the applicable debt instrument being reacquired (or is treated as so issued under subsection (e)(4) and the regulations thereunder) and there is any original issue discount determined under subpart A of part V of subchapter P of this chapter with respect to the debt instrument so issued—

(i) except as provided in clause (ii), no deduction otherwise allowable under this chapter shall be allowed to the issuer of such debt instrument with respect to the portion of such original issue discount which—

(I) accrues before the 1st taxable year in the 5-taxable-year period in which income from the discharge of indebtedness attributable to the reacquisition of the debt instrument is includible under paragraph (1), and

(II) does not exceed the income from the discharge of indebtedness with respect to the debt instrument being reacquired, and

(ii) the aggregate amount of deductions disallowed under clause (i) shall be allowed as a deduction ratably over the 5-taxable-year period described in clause (i)(I).

If the amount of the original issue discount accruing before such 1st taxable year exceeds the income from the dis-



charge of indebtedness with respect to the applicable debt instrument being reacquired, the deductions shall be disallowed in the order in which the original issue discount is accrued.

(B) DEEMED DEBT FOR DEBT EXCHANGES.—For purposes of subparagraph (A), if any debt instrument is issued by an issuer and the proceeds of such debt instrument are used directly or indirectly by the issuer to reacquire an applicable debt instrument of the issuer, the debt instrument so issued shall be treated as issued for the debt instrument being reacquired. If only a portion of the proceeds from a debt instrument are so used, the rules of subparagraph (A) shall apply to the portion of any original issue discount on the newly issued debt instrument which is equal to the portion of the proceeds from such instrument used to reacquire the outstanding instrument.

(3) APPLICABLE DEBT INSTRUMENT.—For purposes of this subsection—

(A) APPLICABLE DEBT INSTRUMENT.—The term “applicable debt instrument” means any debt instrument which was issued by—

- (i) a C corporation, or
- (ii) any other person in connection with the conduct of a trade or business by such person.

(B) DEBT INSTRUMENT.—The term “debt instrument” means a bond, debenture, note, certificate, or any other instrument or contractual arrangement constituting indebtedness (within the meaning of section 1275(a)(1)).

(4) REACQUISITION.—For purposes of this subsection—

(A) IN GENERAL.—The term “reacquisition” means, with respect to any applicable debt instrument, any acquisition of the debt instrument by—

- (i) the debtor which issued (or is otherwise the obligor under) the debt instrument, or
- (ii) a related person to such debtor.

(B) ACQUISITION.—The term “acquisition” shall, with respect to any applicable debt instrument, include an acquisition of the debt instrument for cash, the exchange of the debt instrument for another debt instrument (including an exchange resulting from a modification of the debt instrument), the exchange of the debt instrument for corporate stock or a partnership interest, and the contribution of the debt instrument to capital. Such term shall also include the complete forgiveness of the indebtedness by the holder of the debt instrument.

(5) OTHER DEFINITIONS AND RULES.—For purposes of this subsection—

(A) RELATED PERSON.—The determination of whether a person is related to another person shall be made in the same manner as under subsection (e)(4).

(B) ELECTION.—

- (i) IN GENERAL.—An election under this subsection with respect to any applicable debt instrument shall be made by including with the return of tax imposed by chapter 1 for the taxable year in which the reacqui-

sition of the debt instrument occurs a statement which—

(I) clearly identifies such instrument, and

(II) includes the amount of income to which paragraph (1) applies and such other information as the Secretary may prescribe.

(ii) ELECTION IRREVOCABLE.—Such election, once made, is irrevocable.

(iii) PASS-THRU ENTITIES.—In the case of a partnership, S corporation, or other pass-thru entity, the election under this subsection shall be made by the partnership, the S corporation, or other entity involved.

(C) COORDINATION WITH OTHER EXCLUSIONS.—If a taxpayer elects to have this subsection apply to an applicable debt instrument, subparagraphs (A), (B), (C), and (D) of subsection (a)(1) shall not apply to the income from the discharge of such indebtedness for the taxable year of the election or any subsequent taxable year.

(D) ACCELERATION OF DEFERRED ITEMS.—

(i) IN GENERAL.—In the case of the death of the taxpayer, the liquidation or sale of substantially all the assets of the taxpayer (including in a title 11 or similar case), the cessation of business by the taxpayer, or similar circumstances, any item of income or deduction which is deferred under this subsection (and has not previously been taken into account) shall be taken into account in the taxable year in which such event occurs (or in the case of a title 11 or similar case, the day before the petition is filed).

(ii) SPECIAL RULE FOR PASS-THRU ENTITIES.—The rule of clause (i) shall also apply in the case of the sale or exchange or redemption of an interest in a partnership, S corporation, or other pass-thru entity by a partner, shareholder, or other person holding an ownership interest in such entity.

(6) SPECIAL RULE FOR PARTNERSHIPS.—In the case of a partnership, any income deferred under this subsection shall be allocated to the partners in the partnership immediately before the discharge in the manner such amounts would have been included in the distributive shares of such partners under section 704 if such income were recognized at such time. Any decrease in a partner's share of partnership liabilities as a result of such discharge shall not be taken into account for purposes of section 752 at the time of the discharge to the extent it would cause the partner to recognize gain under section 731. Any decrease in partnership liabilities deferred under the preceding sentence shall be taken into account by such partner at the same time, and to the extent remaining in the same amount, as income deferred under this subsection is recognized.

(7) SECRETARIAL AUTHORITY.—The Secretary may prescribe such regulations, rules, or other guidance as may be necessary or appropriate for purposes of applying this subsection, including—

(A) extending the application of the rules of paragraph (5)(D) to other circumstances where appropriate,

(B) requiring reporting of the election (and such other information as the Secretary may require) on returns of tax for subsequent taxable years, and

(C) rules for the application of this subsection to partnerships, S corporations, and other pass-thru entities, including for the allocation of deferred deductions.

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**SEC. 112. CERTAIN COMBAT ZONE COMPENSATION OF MEMBERS OF THE ARMED FORCES.**

(a) **ENLISTED PERSONNEL.**—Gross income does not include compensation received for active service as a member below the grade of commissioned officer in the Armed Forces of the United States for any month during any part of which such member—

(1) served in a combat zone, or

(2) was hospitalized as a result of wounds, disease, or injury incurred while serving in a combat zone; but this paragraph shall not apply for any month beginning more than 2 years after the date of the termination of combatant activities in such zone.

With respect to service in the combat zone designated for purposes of the Vietnam conflict, paragraph (2) shall not apply to any month after January 1978.

(b) **COMMISSIONED OFFICERS.**—Gross income does not include so much of the compensation as does not exceed the maximum enlisted amount received for active service as a commissioned officer in the Armed Forces of the United States for any month during any part of which such officer—

(1) served in a combat zone, or

(2) was hospitalized as a result of wounds, disease, or injury incurred while serving in a combat zone; but this paragraph shall not apply for any month beginning more than 2 years after the date of the termination of combatant activities in such zone.

With respect to service in the combat zone designated for purposes of the Vietnam conflict, paragraph (2) shall not apply to any month after January 1978.

(c) **DEFINITIONS.**—For purposes of this section—

(1) The term “commissioned officer” does not include a commissioned warrant officer.

(2) The term “combat zone” [means any area] *means*—

(A) *any area* which the President of the United States by Executive Order designates, for purposes of this section or corresponding provisions of prior income tax laws, as an area in which Armed Forces of the United States are or have engaged in combat[.], and

(B) *the Sinai Peninsula of Egypt.*

(3) Service is performed in a combat zone [only if performed] *only if*—

(A) *in the case of an area described in paragraph (2)(A), such service is performed on or after the date designated by the President by Executive Order as the date of the commencing of combatant activities in such zone, and on*

or before the date designated by the President by Executive Order as the date of the termination of combatant activities in such zone[.], and

(B) in the case of the area described in paragraph (2)(B), such service is performed during any period with respect to which one or more members of the Armed Forces of the United States are entitled to special pay under section 310 of title 37, United States Code (relating to special pay; duty subject to hostile fire or imminent danger), for service performed in such area.

(4) The term "compensation" does not include pensions and retirement pay.

(5) The term "maximum enlisted amount" means, for any month, the sum of—

(A) the highest rate of basic pay payable for such month to any enlisted member of the Armed Forces of the United States at the highest pay grade applicable to enlisted members, and

(B) in the case of an officer entitled to special pay under section 310, or paragraph (1) or (3) of section 351(a), of title 37, United States Code, for such month, the amount of such special pay payable to such officer for such month.

(d) PRISONERS OF WAR, ETC.—

(1) MEMBERS OF THE ARMED FORCES.—Gross income does not include compensation received for active service as a member of the Armed Forces of the United States for any month during any part of which such member is in a missing status (as defined in section 551(2) of title 37, United States Code) during the Vietnam conflict as a result of such conflict, other than a period with respect to which it is officially determined under section 552(c) of such title 37 that he is officially absent from his post of duty without authority.

(2) CIVILIAN EMPLOYEES.—Gross income does not include compensation received for active service as an employee for any month during any part of which such employee is in a missing status during the Vietnam conflict as a result of such conflict. For purposes of this paragraph, the terms "active service", "employee", and "missing status" have the respective meanings given to such terms by section 5561 of title 5 of the United States Code.

(3) PERIOD OF CONFLICT.—For purposes of this subsection, the Vietnam conflict began February 28, 1961, and ends on the date designated by the President by Executive order as the date of the termination of combatant activities in Vietnam. For purposes of this subsection, an individual is in a missing status as a result of the Vietnam conflict if immediately before such status began he was performing service in Vietnam or was performing service in Southeast Asia in direct support of military operations in Vietnam.

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#### SEC. 125. CAFETERIA PLANS.

(a) GENERAL RULE.—Except as provided in subsection (b), no amount shall be included in the gross income of a participant in

a cafeteria plan solely because, under the plan, the participant may choose among the benefits of the plan.

(b) EXCEPTION FOR HIGHLY COMPENSATED PARTICIPANTS AND KEY EMPLOYEES.—

(1) HIGHLY COMPENSATED PARTICIPANTS.—In the case of a highly compensated participant, subsection (a) shall not apply to any benefit attributable to a plan year for which the plan discriminates in favor of—

(A) highly compensated individuals as to eligibility to participate, or

(B) highly compensated participants as to contributions and benefits.

(2) KEY EMPLOYEES.—In the case of a key employee (within the meaning of section 416(i)(1)), subsection (a) shall not apply to any benefit attributable to a plan for which the qualified benefits provided to key employees exceed 25 percent of the aggregate of such benefits provided for all employees under the plan. For purposes of the preceding sentence, qualified benefits shall be determined without regard to the second sentence of subsection (f).

(3) YEAR OF INCLUSION.—For purposes of determining the taxable year of inclusion, any benefit described in paragraph (1) or (2) shall be treated as received or accrued in the taxable year of the participant or key employee in which the plan year ends.

(c) DISCRIMINATION AS TO BENEFITS OR CONTRIBUTIONS.—For purposes of subparagraph (B) of subsection (b)(1), a cafeteria plan does not discriminate where qualified benefits and total benefits (or employer contributions allocable to qualified benefits and employer contributions for total benefits) do not discriminate in favor of highly compensated participants.

(d) CAFETERIA PLAN DEFINED.—For purposes of this section—

(1) IN GENERAL.—The term “cafeteria plan” means a written plan under which—

(A) all participants are employees, and

(B) the participants may choose among 2 or more benefits consisting of cash and qualified benefits.

(2) DEFERRED COMPENSATION PLANS EXCLUDED.—

(A) IN GENERAL.—The term “cafeteria plan” does not include any plan which provides for deferred compensation.

(B) EXCEPTION FOR CASH AND DEFERRED ARRANGEMENTS.—Subparagraph (A) shall not apply to a profit-sharing or stock bonus plan or rural cooperative plan (within the meaning of section 401(k)(7)) which includes a qualified cash or deferred arrangement (as defined in section 401(k)(2)) to the extent of amounts which a covered employee may elect to have the employer pay as contributions to a trust under such plan on behalf of the employee.

(C) EXCEPTION FOR CERTAIN PLANS MAINTAINED BY EDUCATIONAL INSTITUTIONS.—Subparagraph (A) shall not apply to a plan maintained by an educational organization described in section 170(b)(1)(A)(ii) to the extent of amounts which a covered employee may elect to have the employer pay as contributions for post-retirement group life insurance if—

(i) all contributions for such insurance must be made before retirement, and

(ii) such life insurance does not have a cash surrender value at any time.

For purposes of section 79, any life insurance described in the preceding sentence shall be treated as group-term life insurance.

(D) EXCEPTION FOR HEALTH SAVINGS ACCOUNTS.—Subparagraph (A) shall not apply to a plan to the extent of amounts which a covered employee may elect to have the employer pay as contributions to a health savings account established on behalf of the employee.

(e) HIGHLY COMPENSATED PARTICIPANT AND INDIVIDUAL DEFINED.—For purposes of this section—

(1) HIGHLY COMPENSATED PARTICIPANT.—The term “highly compensated participant” means a participant who is—

(A) an officer,

(B) a shareholder owning more than 5 percent of the voting power or value of all classes of stock of the employer,

(C) highly compensated, or

(D) a spouse or dependent (within the meaning of [section 152] section 7706, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof) of an individual described in subparagraph (A), (B), or (C).

(2) HIGHLY COMPENSATED INDIVIDUAL.—The term “highly compensated individual” means an individual who is described in subparagraph (A), (B), (C), or (D) of paragraph (1).

(f) QUALIFIED BENEFITS DEFINED.—For purposes of this section—

(1) IN GENERAL.—The term “qualified benefit” means any benefit which, with the application of subsection (a), is not includible in the gross income of the employee by reason of an express provision of this chapter (other than section 106(b), 117, 127, or 132). Such term includes any group term life insurance which is includible in gross income only because it exceeds the dollar limitation of section 79 and such term includes any other benefit permitted under regulations.

(2) LONG-TERM CARE INSURANCE NOT QUALIFIED.—The term “qualified benefit” shall not include any product which is advertised, marketed, or offered as long-term care insurance.

(3) CERTAIN EXCHANGE-PARTICIPATING QUALIFIED HEALTH PLANS NOT QUALIFIED.—

(A) IN GENERAL.—The term “qualified benefit” shall not include any qualified health plan (as defined in section 1301(a) of the Patient Protection and Affordable Care Act) offered through an Exchange established under section 1311 of such Act.

(B) EXCEPTION FOR EXCHANGE-ELIGIBLE EMPLOYERS.—Subparagraph (A) shall not apply with respect to any employee if such employee’s employer is a qualified employer (as defined in section 1312(f)(2) of the Patient Protection and Affordable Care Act) offering the employee the opportunity to enroll through such an Exchange in a qualified health plan in a group market.

(g) SPECIAL RULES.—

(1) COLLECTIVELY BARGAINED PLAN NOT CONSIDERED DISCRIMINATORY.—For purposes of this section, a plan shall not be treated as discriminatory if the plan is maintained under an agreement which the Secretary finds to be a collective bargaining agreement between employee representatives and one or more employers.

(2) HEALTH BENEFITS.—For purposes of subparagraph (B) of subsection (b)(1), a cafeteria plan which provides health benefits shall not be treated as discriminatory if—

(A) contributions under the plan on behalf of each participant include an amount which—

(i) equals 100 percent of the cost of the health benefit coverage under the plan of the majority of the highly compensated participants similarly situated, or

(ii) equals or exceeds 75 percent of the cost of the health benefit coverage of the participant (similarly situated) having the highest cost health benefit coverage under the plan, and

(B) contributions or benefits under the plan in excess of those described in subparagraph (A) bear a uniform relationship to compensation.

(3) CERTAIN PARTICIPATION ELIGIBILITY RULES NOT TREATED AS DISCRIMINATORY.—For purposes of subparagraph (A) of subsection (b)(1), a classification shall not be treated as discriminatory if the plan—

(A) benefits a group of employees described in section 410(b)(2)(A)(i), and

(B) meets the requirements of clauses (i) and (ii):

(i) No employee is required to complete more than 3 years of employment with the employer or employers maintaining the plan as a condition of participation in the plan, and the employment requirement for each employee is the same.

(ii) Any employee who has satisfied the employment requirement of clause (i) and who is otherwise entitled to participate in the plan commences participation no later than the first day of the first plan year beginning after the date the employment requirement was satisfied unless the employee was separated from service before the first day of that plan year.

(4) CERTAIN CONTROLLED GROUPS, ETC.—All employees who are treated as employed by a single employer under subsection (b), (c), or (m) of section 414 shall be treated as employed by a single employer for purposes of this section.

(h) SPECIAL RULE FOR UNUSED BENEFITS IN HEALTH FLEXIBLE SPENDING ARRANGEMENTS OF INDIVIDUALS CALLED TO ACTIVE DUTY.—

(1) IN GENERAL.—For purposes of this title, a plan or other arrangement shall not fail to be treated as a cafeteria plan or health flexible spending arrangement (and shall not fail to be treated as an accident or health plan) merely because such arrangement provides for qualified reservist distributions.

(2) QUALIFIED RESERVIST DISTRIBUTION.—For purposes of this subsection, the term “qualified reservist distribution” means

any distribution to an individual of all or a portion of the balance in the employee's account under such arrangement if—

(A) such individual was (by reason of being a member of a reserve component (as defined in section 101 of title 37, United States Code)) ordered or called to active duty for a period in excess of 179 days or for an indefinite period, and

(B) such distribution is made during the period beginning on the date of such order or call and ending on the last date that reimbursements could otherwise be made under such arrangement for the plan year which includes the date of such order or call.

(i) **LIMITATION ON HEALTH FLEXIBLE SPENDING ARRANGEMENTS.—**

(1) **IN GENERAL.—**For purposes of this section, if a benefit is provided under a cafeteria plan through employer contributions to a health flexible spending arrangement, such benefit shall not be treated as a qualified benefit unless the cafeteria plan provides that an employee may not elect for any taxable year to have salary reduction contributions in excess of \$2,500 made to such arrangement.

(2) **ADJUSTMENT FOR INFLATION.—**In the case of any taxable year beginning after December 31, 2013, the dollar amount in paragraph (1) shall be increased by an amount equal to—

(A) such amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which such taxable year begins by substituting “calendar year 2012” for “calendar year 2016” in subparagraph (A)(ii) thereof.

If any increase determined under this paragraph is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.

(j) **SIMPLE CAFETERIA PLANS FOR SMALL BUSINESSES.—**

(1) **IN GENERAL.—**An eligible employer maintaining a simple cafeteria plan with respect to which the requirements of this subsection are met for any year shall be treated as meeting any applicable nondiscrimination requirement during such year.

(2) **SIMPLE CAFETERIA PLAN.—**For purposes of this subsection, the term “simple cafeteria plan” means a cafeteria plan—

(A) which is established and maintained by an eligible employer, and

(B) with respect to which the contribution requirements of paragraph (3), and the eligibility and participation requirements of paragraph (4), are met.

(3) **CONTRIBUTION REQUIREMENTS.—**

(A) **IN GENERAL.—**The requirements of this paragraph are met if, under the plan the employer is required, without regard to whether a qualified employee makes any salary reduction contribution, to make a contribution to provide qualified benefits under the plan on behalf of each qualified employee in an amount equal to—

(i) a uniform percentage (not less than 2 percent) of the employee's compensation for the plan year, or

(ii) an amount which is not less than the lesser of—



(I) 6 percent of the employee's compensation for the plan year, or

(II) twice the amount of the salary reduction contributions of each qualified employee.

(B) MATCHING CONTRIBUTIONS ON BEHALF OF HIGHLY COMPENSATED AND KEY EMPLOYEES.—The requirements of subparagraph (A)(ii) shall not be treated as met if, under the plan, the rate of contributions with respect to any salary reduction contribution of a highly compensated or key employee at any rate of contribution is greater than that with respect to an employee who is not a highly compensated or key employee.

(C) ADDITIONAL CONTRIBUTIONS.—Subject to subparagraph (B), nothing in this paragraph shall be treated as prohibiting an employer from making contributions to provide qualified benefits under the plan in addition to contributions required under subparagraph (A).

(D) DEFINITIONS.—For purposes of this paragraph—

(i) SALARY REDUCTION CONTRIBUTION.—The term “salary reduction contribution” means, with respect to a cafeteria plan, any amount which is contributed to the plan at the election of the employee and which is not includible in gross income by reason of this section.

(ii) QUALIFIED EMPLOYEE.—The term “qualified employee” means, with respect to a cafeteria plan, any employee who is not a highly compensated or key employee and who is eligible to participate in the plan.

(iii) HIGHLY COMPENSATED EMPLOYEE.—The term “highly compensated employee” has the meaning given such term by section 414(q).

(iv) KEY EMPLOYEE.—The term “key employee” has the meaning given such term by section 416(i).

(4) MINIMUM ELIGIBILITY AND PARTICIPATION REQUIREMENTS.—

(A) IN GENERAL.—The requirements of this paragraph shall be treated as met with respect to any year if, under the plan—

(i) all employees who had at least 1,000 hours of service for the preceding plan year are eligible to participate, and

(ii) each employee eligible to participate in the plan may, subject to terms and conditions applicable to all participants, elect any benefit available under the plan.

(B) CERTAIN EMPLOYEES MAY BE EXCLUDED.—For purposes of subparagraph (A)(i), an employer may elect to exclude under the plan employees—

(i) who have not attained the age of 21 before the close of a plan year,

(ii) who have less than 1 year of service with the employer as of any day during the plan year,

(iii) who are covered under an agreement which the Secretary of Labor finds to be a collective bargaining agreement if there is evidence that the benefits cov-

ered under the cafeteria plan were the subject of good faith bargaining between employee representatives and the employer, or

(iv) who are described in section 410(b)(3)(C) (relating to nonresident aliens working outside the United States).

A plan may provide a shorter period of service or younger age for purposes of clause (i) or (ii).

(5) ELIGIBLE EMPLOYER.—For purposes of this subsection—

(A) IN GENERAL.—The term “eligible employer” means, with respect to any year, any employer if such employer employed an average of 100 or fewer employees on business days during either of the 2 preceding years. For purposes of this subparagraph, a year may only be taken into account if the employer was in existence throughout the year.

(B) EMPLOYERS NOT IN EXISTENCE DURING PRECEDING YEAR.—If an employer was not in existence throughout the preceding year, the determination under subparagraph (A) shall be based on the average number of employees that it is reasonably expected such employer will employ on business days in the current year.

(C) GROWING EMPLOYERS RETAIN TREATMENT AS SMALL EMPLOYER.—

(i) IN GENERAL.—If—

(I) an employer was an eligible employer for any year (a “qualified year”), and

(II) such employer establishes a simple cafeteria plan for its employees for such year,

then, notwithstanding the fact the employer fails to meet the requirements of subparagraph (A) for any subsequent year, such employer shall be treated as an eligible employer for such subsequent year with respect to employees (whether or not employees during a qualified year) of any trade or business which was covered by the plan during any qualified year.

(ii) EXCEPTION.—This subparagraph shall cease to apply if the employer employs an average of 200 or more employees on business days during any year preceding any such subsequent year.

(D) SPECIAL RULES.—

(i) PREDECESSORS.—Any reference in this paragraph to an employer shall include a reference to any predecessor of such employer.

(ii) AGGREGATION RULES.—All persons treated as a single employer under subsection (a) or (b) of section 52, or subsection (n) or (o) of section 414, shall be treated as one person.

(6) APPLICABLE NONDISCRIMINATION REQUIREMENT.—For purposes of this subsection, the term “applicable nondiscrimination requirement” means any requirement under subsection (b) of this section, section 79(d), section 105(h), or paragraph (2), (3), (4), or (8) of section 129(d).

(7) COMPENSATION.—The term “compensation” has the meaning given such term by section 414(s).

(k) CROSS REFERENCE.—For reporting and recordkeeping requirements, see section 6039D.

(l) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the provisions of this section.

\* \* \* \* \*

**SEC. 129. DEPENDENT CARE ASSISTANCE PROGRAMS.**

(a) EXCLUSION.—

(1) IN GENERAL.—Gross income of an employee does not include amounts paid or incurred by the employer for dependent care assistance provided to such employee if the assistance is furnished pursuant to a program which is described in subsection (d).

(2) LIMITATION OF EXCLUSION.—

(A) IN GENERAL.—The amount which may be excluded under paragraph (1) for dependent care assistance with respect to dependent care services provided during a taxable year shall not exceed \$5,000 (\$2,500 in the case of a separate return by a married individual).

(B) YEAR OF INCLUSION.—The amount of any excess under subparagraph (A) shall be included in gross income in the taxable year in which the dependent care services were provided (even if payment of dependent care assistance for such services occurs in a subsequent taxable year).

(C) MARITAL STATUS.—For purposes of this paragraph, marital status shall be determined under the rules of paragraphs (3) and (4) of section 21(e).

(b) EARNED INCOME LIMITATION.—

(1) IN GENERAL.—The amount excluded from the income of an employee under subsection (a) for any taxable year shall not exceed—

(A) in the case of an employee who is not married at the close of such taxable year, the earned income of such employee for such taxable year, or

(B) in the case of an employee who is married at the close of such taxable year, the lesser of—

(i) the earned income of such employee for such taxable year, or

(ii) the earned income of the spouse of such employee for such taxable year.

(2) SPECIAL RULE FOR CERTAIN SPOUSES.—For purposes of paragraph (1), the provisions of section 21(d)(2) shall apply in determining the earned income of a spouse who is a student or incapable of caring for himself.

(c) PAYMENTS TO RELATED INDIVIDUALS.—No amount paid or incurred during the taxable year of an employee by an employer in providing dependent care assistance to such employee shall be excluded under subsection (a) if such amount was paid or incurred to an individual—

【(1) with respect to whom, for such taxable year, a deduction is allowable under section 151(c) (relating to personal exemptions for dependents) to such employee or the spouse of such employee, or】

(1) *who is a dependent of such employee or of such employee's spouse, or*

(2) *who is a child of such employee (within the meaning of [section 152(f)(1)] section 7706(f)(1)) under the age of 19 at the close of such taxable year.*

(d) **DEPENDENT CARE ASSISTANCE PROGRAM.**—

(1) **IN GENERAL.**—For purposes of this section a dependent care assistance program is a separate written plan of an employer for the exclusive benefit of his employees to provide such employees with dependent care assistance which meets the requirements of paragraphs (2) through (8) of this subsection. If any plan would qualify as a dependent care assistance program but for a failure to meet the requirements of this subsection, then, notwithstanding such failure, such plan shall be treated as a dependent care assistance program in the case of employees who are not highly compensated employees.

(2) **DISCRIMINATION.**—The contributions or benefits provided under the plan shall not discriminate in favor of employees who are highly compensated employees (within the meaning of section 414(q)) or their dependents.

(3) **ELIGIBILITY.**—The program shall benefit employees who qualify under a classification set up by the employer and found by the Secretary not to be discriminatory in favor of employees described in paragraph (2), or their dependents.

(4) **PRINCIPAL SHAREHOLDERS OR OWNERS.**—Not more than 25 percent of the amounts paid or incurred by the employer for dependent care assistance during the year may be provided for the class of individuals who are shareholders or owners (or their spouses or dependents), each of whom (on any day of the year) owns more than 5 percent of the stock or of the capital or profits interest in the employer.

(5) **NO FUNDING REQUIRED.**—A program referred to in paragraph (1) is not required to be funded.

(6) **NOTIFICATION OF ELIGIBLE EMPLOYEES.**—Reasonable notification of the availability and terms of the program shall be provided to eligible employees.

(7) **STATEMENT OF EXPENSES.**—The plan shall furnish to an employee, on or before January 31, a written statement showing the amounts paid or expenses incurred by the employer in providing dependent care assistance to such employee during the previous calendar year.

(8) **BENEFITS.**—

(A) **IN GENERAL.**—A plan meets the requirements of this paragraph if the average benefits provided to employees who are not highly compensated employees under all plans of the employer is at least 55 percent of the average benefits provided to highly compensated employees under all plans of the employer.

(B) **SALARY REDUCTION AGREEMENTS.**—For purposes of subparagraph (A), in the case of any benefits provided through a salary reduction agreement, a plan may disregard any employees whose compensation is less than \$25,000. For purposes of this subparagraph, the term “compensation” has the meaning given such term by section 414(q)(4), except that, under rules prescribed by the

Secretary, an employer may elect to determine compensation on any other basis which does not discriminate in favor of highly compensated employees.

(9) EXCLUDED EMPLOYEES.—For purposes of paragraphs (3) and (8), there shall be excluded from consideration—

(A) subject to rules similar to the rules of section 410(b)(4), employees who have not attained the age of 21 and completed 1 year of service (as defined in section 410(a)(3)), and

(B) employees not included in a dependent care assistance program who are included in a unit of employees covered by an agreement which the Secretary finds to be a collective bargaining agreement between employee representatives and 1 or more employees, if there is evidence that dependent care benefits were the subject of good faith bargaining between such employee representatives and such employer or employers.

(e) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) DEPENDENT CARE ASSISTANCE.—The term “dependent care assistance” means the payment of, or provision of, those services which if paid for by the employee would be considered employment-related expenses under section 21(b)(2) (relating to expenses for household and dependent care services necessary for gainful employment).

(2) EARNED INCOME.—The term “earned income” shall have the meaning given such term in section 32(c)(2), but such term shall not include any amounts paid or incurred by an employer for dependent care assistance to an employee.

(3) EMPLOYEE.—The term “employee” includes, for any year, an individual who is an employee within the meaning of section 401(c)(1) (relating to self-employed individuals).

(4) EMPLOYER.—An individual who owns the entire interest in an unincorporated trade or business shall be treated as his own employer. A partnership shall be treated as the employer of each partner who is an employee within the meaning of paragraph (3).

(5) ATTRIBUTION RULES.—

(A) OWNERSHIP OF STOCK.—Ownership of stock in a corporation shall be determined in accordance with the rules provided under subsections (d) and (e) of section 1563 (without regard to section 1563(e)(3)(C)).

(B) INTEREST IN UNINCORPORATED TRADE OR BUSINESS.—The interest of an employee in a trade or business which is not incorporated shall be determined in accordance with regulations prescribed by the Secretary, which shall be based on principles similar to the principles which apply in the case of subparagraph (A).

(6) UTILIZATION TEST NOT APPLICABLE.—A dependent care assistance program shall not be held or considered to fail to meet any requirements of subsection (d) (other than paragraphs (4) and (8) thereof) merely because of utilization rates for the different types of assistance made available under the program.

(7) DISALLOWANCE OF EXCLUDED AMOUNTS AS CREDIT OR DEDUCTION.—No deduction or credit shall be allowed to the em-

ployee under any other section of this chapter for any amount excluded from the gross income of the employee by reason of this section.

(8) TREATMENT OF ONSITE FACILITIES.—In the case of an on-site facility maintained by an employer, except to the extent provided in regulations, the amount of dependent care assistance provided to an employee excluded with respect to any dependent shall be based on—

(A) utilization of the facility by a dependent of the employee, and

(B) the value of the services provided with respect to such dependent.

(9) IDENTIFYING INFORMATION REQUIRED WITH RESPECT TO SERVICE PROVIDER.—No amount paid or incurred by an employer for dependent care assistance provided to an employee shall be excluded from the gross income of such employee unless—

(A) the name, address, and taxpayer identification number of the person performing the services are included on the return to which the exclusion relates, or

(B) if such person is an organization described in section 501(c)(3) and exempt from tax under section 501(a), the name and address of such person are included on the return to which the exclusion relates.

In the case of a failure to provide the information required under the preceding sentence, the preceding sentence shall not apply if it is shown that the taxpayer exercised due diligence in attempting to provide the information so required.

\* \* \* \* \*

**SEC. 132. CERTAIN FRINGE BENEFITS.**

(a) EXCLUSION FROM GROSS INCOME.—Gross income shall not include any fringe benefit which qualifies as a—

- (1) no-additional-cost service,
- (2) qualified employee discount,
- (3) working condition fringe,
- (4) de minimis fringe,
- (5) qualified transportation fringe,
- (6) qualified moving expense reimbursement,
- (7) qualified retirement planning services, or
- (8) qualified military base realignment and closure fringe.

(b) NO-ADDITIONAL-COST SERVICE DEFINED.—For purposes of this section, the term “no-additional-cost service” means any service provided by an employer to an employee for use by such employee if—

- (1) such service is offered for sale to customers in the ordinary course of the line of business of the employer in which the employee is performing services, and
- (2) the employer incurs no substantial additional cost (including forgone revenue) in providing such service to the employee (determined without regard to any amount paid by the employee for such service).

(c) QUALIFIED EMPLOYEE DISCOUNT DEFINED.—For purposes of this section—

(1) **QUALIFIED EMPLOYEE DISCOUNT.**—The term “qualified employee discount” means any employee discount with respect to qualified property or services to the extent such discount does not exceed—

(A) in the case of property, the gross profit percentage of the price at which the property is being offered by the employer to customers, or

(B) in the case of services, 20 percent of the price at which the services are being offered by the employer to customers.

(2) **GROSS PROFIT PERCENTAGE.**—

(A) **IN GENERAL.**—The term “gross profit percentage” means the percent which—

(i) the excess of the aggregate sales price of property sold by the employer to customers over the aggregate cost of such property to the employer, is of

(ii) the aggregate sale price of such property.

(B) **DETERMINATION OF GROSS PROFIT PERCENTAGE.**—Gross profit percentage shall be determined on the basis of—

(i) all property offered to customers in the ordinary course of the line of business of the employer in which the employee is performing services (or a reasonable classification of property selected by the employer), and

(ii) the employer’s experience during a representative period.

(3) **EMPLOYEE DISCOUNT DEFINED.**—The term “employee discount” means the amount by which—

(A) the price at which the property or services are provided by the employer to an employee for use by such employee, is less than

(B) the price at which such property or services are being offered by the employer to customers.

(4) **QUALIFIED PROPERTY OR SERVICES.**—The term “qualified property or services” means any property (other than real property and other than personal property of a kind held for investment) or services which are offered for sale to customers in the ordinary course of the line of business of the employer in which the employee is performing services.

(d) **WORKING CONDITION FRINGE DEFINED.**—For purposes of this section, the term “working condition fringe” means any property or services provided to an employee of the employer to the extent that, if the employee paid for such property or services, such payment would be allowable as a deduction under section 162 or 167.

(e) **DE MINIMIS FRINGE DEFINED.**—For purposes of this section—

(1) **IN GENERAL.**—The term “de minimis fringe” means any property or service the value of which is (after taking into account the frequency with which similar fringes are provided by the employer to the employer’s employees) so small as to make accounting for it unreasonable or administratively impracticable.

(2) **TREATMENT OF CERTAIN EATING FACILITIES.**—The operation by an employer of any eating facility for employees shall be treated as a de minimis fringe if—

(A) such facility is located on or near the business premises of the employer, and

(B) revenue derived from such facility normally equals or exceeds the direct operating costs of such facility.

The preceding sentence shall apply with respect to any highly compensated employee only if access to the facility is available on substantially the same terms to each member of a group of employees which is defined under a reasonable classification set up by the employer which does not discriminate in favor of highly compensated employees. For purposes of subparagraph (B), an employee entitled under section 119 to exclude the value of a meal provided at such facility shall be treated as having paid an amount for such meal equal to the direct operating costs of the facility attributable to such meal.

(f) QUALIFIED TRANSPORTATION FRINGE.—

(1) IN GENERAL.—For purposes of this section, the term “qualified transportation fringe” means any of the following provided by an employer to an employee:

(A) Transportation in a commuter highway vehicle if such transportation is in connection with travel between the employee’s residence and place of employment.

(B) Any transit pass.

(C) Qualified parking.

**[(D) Any qualified bicycle commuting reimbursement.]**

(2) LIMITATION ON EXCLUSION.—The amount of the fringe benefits which are provided by an employer to any employee and which may be excluded from gross income under subsection (a)(5) shall not exceed—

(A) \$175 per month in the case of the aggregate of the benefits described in subparagraphs (A) and (B) of paragraph (1), *and*

(B) \$175 per month in the case of qualified parking**], and]**.

**[(C) the applicable annual limitation in the case of any qualified bicycle commuting reimbursement.]**

(3) CASH REIMBURSEMENTS.—For purposes of this subsection, the term “qualified transportation fringe” includes a cash reimbursement by an employer to an employee for a benefit described in paragraph (1). The preceding sentence shall apply to a cash reimbursement for any transit pass only if a voucher or similar item which may be exchanged only for a transit pass is not readily available for direct distribution by the employer to the employee.

(4) NO CONSTRUCTIVE RECEIPT.—No amount shall be included in the gross income of an employee solely because the employee may choose between any qualified transportation fringe **[(other than a qualified bicycle commuting reimbursement)]** and compensation which would otherwise be includible in gross income of such employee.

(5) DEFINITIONS.—For purposes of this subsection—

(A) TRANSIT PASS.—The term “transit pass” means any pass, token, farecard, voucher, or similar item entitling a person to transportation (or transportation at a reduced price) if such transportation is—



(i) on mass transit facilities (whether or not publicly owned), or

(ii) provided by any person in the business of transporting persons for compensation or hire if such transportation is provided in a vehicle meeting the requirements of subparagraph (B)(i).

(B) COMMUTER HIGHWAY VEHICLE.—The term “commuter highway vehicle” means any highway vehicle—

(i) the seating capacity of which is at least 6 adults (not including the driver), and

(ii) at least 80 percent of the mileage use of which can reasonably be expected to be—

(I) for purposes of transporting employees in connection with travel between their residences and their place of employment, and

(II) on trips during which the number of employees transported for such purposes is at least 1/2 of the adult seating capacity of such vehicle (not including the driver).

(C) QUALIFIED PARKING.—The term “qualified parking” means parking provided to an employee on or near the business premises of the employer or on or near a location from which the employee commutes to work by transportation described in subparagraph (A), in a commuter highway vehicle, or by carpool. Such term shall not include any parking on or near property used by the employee for residential purposes.

(D) TRANSPORTATION PROVIDED BY EMPLOYER.—Transportation referred to in paragraph (1)(A) shall be considered to be provided by an employer if such transportation is furnished in a commuter highway vehicle operated by or for the employer.

(E) EMPLOYEE.—For purposes of this subsection, the term “employee” does not include an individual who is an employee within the meaning of section 401(c)(1).

(F) DEFINITIONS RELATED TO BICYCLE COMMUTING REIMBURSEMENT.—

(i) QUALIFIED BICYCLE COMMUTING REIMBURSEMENT.—The term “qualified bicycle commuting reimbursement” means, with respect to any calendar year, any employer reimbursement during the 15-month period beginning with the first day of such calendar year for reasonable expenses incurred by the employee during such calendar year for the purchase of a bicycle and bicycle improvements, repair, and storage, if such bicycle is regularly used for travel between the employee’s residence and place of employment.

(ii) APPLICABLE ANNUAL LIMITATION.—The term “applicable annual limitation” means, with respect to any employee for any calendar year, the product of \$20 multiplied by the number of qualified bicycle commuting months during such year.

(iii) QUALIFIED BICYCLE COMMUTING MONTH.—The term “qualified bicycle commuting month” means, with

respect to any employee, any month during which such employee—

(I) regularly uses the bicycle for a substantial portion of the travel between the employee's residence and place of employment, and

(II) does not receive any benefit described in subparagraph (A), (B), or (C) of paragraph (1).

(6) INFLATION ADJUSTMENT.—

(A) IN GENERAL.—In the case of any taxable year beginning in a calendar year after 1999, the dollar amounts contained in subparagraphs (A) and (B) of paragraph (2) shall be increased by an amount equal to—

(i) such dollar amount, multiplied by

(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting “calendar year 1998” for “calendar year 2016” in subparagraph (A)(ii) thereof.

In the case of any taxable year beginning in a calendar year after 2002, clause (ii) shall be applied by substituting “calendar year 2001” for “calendar year 1998” for purposes of adjusting the dollar amount contained in paragraph (2)(A).

(B) ROUNDING.—If any increase determined under subparagraph (A) is not a multiple of \$5, such increase shall be rounded to the next lowest multiple of \$5.

(7) COORDINATION WITH OTHER PROVISIONS.—For purposes of this section, the terms “working condition fringe” and “de minimis fringe” shall not include any qualified transportation fringe (determined without regard to paragraph (2)).

[(8) SUSPENSION OF QUALIFIED BICYCLE COMMUTING REIMBURSEMENT EXCLUSION.—Paragraph (1)(D) shall not apply to any taxable year beginning after December 31, 2017, and before January 1, 2026.]

(g) QUALIFIED MOVING EXPENSE REIMBURSEMENT.—For purposes of this section—

(1) IN GENERAL.—The term “qualified moving expense reimbursement” means any amount received (directly or indirectly) **[by an individual]** *by a qualified military individual* from an employer as a payment for (or a reimbursement of) expenses which would be deductible as moving expenses under section 217 if directly paid or incurred by the individual. Such term shall not include any payment for (or reimbursement of) an expense actually deducted by the individual in a prior taxable year.

[(2) SUSPENSION FOR TAXABLE YEARS 2018 THROUGH 2025.—Except in the case of a member of the Armed Forces of the United States on active duty who moves pursuant to a military order and incident to a permanent change of station, subsection (a)(6) shall not apply to any taxable year beginning after December 31, 2017, and before January 1, 2026.]

(2) QUALIFIED MILITARY INDIVIDUAL.—*For purposes of this subsection, the term “qualified military individual” means a member of the Armed Forces of the United States on active duty*

*who moves pursuant to a military order and incident to a permanent change of station.*

(h) CERTAIN INDIVIDUALS TREATED AS EMPLOYEES FOR PURPOSES OF SUBSECTIONS (A)(1) AND (2).—For purposes of paragraphs (1) and (2) of subsection (a)—

(1) RETIRED AND DISABLED EMPLOYEES AND SURVIVING SPOUSE OF EMPLOYEE TREATED AS EMPLOYEE.—With respect to a line of business of an employer, the term “employee” includes—

(A) any individual who was formerly employed by such employer in such line of business and who separated from service with such employer in such line of business by reason of retirement or disability, and

(B) any widow or widower of any individual who died while employed by such employer in such line of business or while an employee within the meaning of subparagraph (A).

(2) SPOUSE AND DEPENDENT CHILDREN.—

(A) IN GENERAL.—Any use by the spouse or a dependent child of the employee shall be treated as use by the employee.

(B) DEPENDENT CHILD.—For purposes of subparagraph (A), the term “dependent child” means any child (as defined in [section 152(f)(1)] *section 7706(f)(1)*) of the employee—

(i) who is a dependent of the employee, or

(ii) both of whose parents are deceased and who has not attained age 25.

For purposes of the preceding sentence, any child to whom [section 152(e)] *section 7706(e)* applies shall be treated as the dependent of both parents.

(3) SPECIAL RULE FOR PARENTS IN THE CASE OF AIR TRANSPORTATION.—Any use of air transportation by a parent of an employee (determined without regard to paragraph (1)(B)) shall be treated as use by the employee.

(i) RECIPROCAL AGREEMENTS.—For purposes of paragraph (1) of subsection (a), any service provided by an employer to an employee of another employer shall be treated as provided by the employer of such employee if—

(1) such service is provided pursuant to a written agreement between such employers, and

(2) neither of such employers incurs any substantial additional costs (including foregone revenue) in providing such service or pursuant to such agreement.

(j) SPECIAL RULES.—

(1) EXCLUSIONS UNDER SUBSECTION (A)(1) AND (2) APPLY TO HIGHLY COMPENSATED EMPLOYEES ONLY IF NO DISCRIMINATION.—Paragraphs (1) and (2) of subsection (a) shall apply with respect to any fringe benefit described therein provided with respect to any highly compensated employee only if such fringe benefit is available on substantially the same terms to each member of a group of employees which is defined under a reasonable classification set up by the employer which does not discriminate in favor of highly compensated employees.

## (2) SPECIAL RULE FOR LEASED SECTIONS OF DEPARTMENT STORES.—

(A) IN GENERAL.—For purposes of paragraph (2) of subsection (a), in the case of a leased section of a department store—

(i) such section shall be treated as part of the line of business of the person operating the department store, and

(ii) employees in the leased section shall be treated as employees of the person operating the department store.

(B) LEASED SECTION OF DEPARTMENT STORE.—For purposes of subparagraph (A), a leased section of a department store is any part of a department store where over-the-counter sales of property are made under a lease or similar arrangement where it appears to the general public that individuals making such sales are employed by the person operating the department store.

## (3) AUTO SALESMEN.—

(A) IN GENERAL.—For purposes of subsection (a)(3), qualified automobile demonstration use shall be treated as a working condition fringe.

(B) QUALIFIED AUTOMOBILE DEMONSTRATION USE.—For purposes of subparagraph (A), the term “qualified automobile demonstration use” means any use of an automobile by a full-time automobile salesman in the sales area in which the automobile dealer’s sales office is located if—

(i) such use is provided primarily to facilitate the salesman’s performance of services for the employer, and

(ii) there are substantial restrictions on the personal use of such automobile by such salesman.

## (4) ON-PREMISES GYMS AND OTHER ATHLETIC FACILITIES.—

(A) IN GENERAL.—Gross income shall not include the value of any on-premises athletic facility provided by an employer to his employees.

(B) ON-PREMISES ATHLETIC FACILITY.—For purposes of this paragraph, the term “on-premises athletic facility” means any gym or other athletic facility—

(i) which is located on the premises of the employer,

(ii) which is operated by the employer, and

(iii) substantially all the use of which is by employees of the employer, their spouses, and their dependent children (within the meaning of subsection (h)).

## (5) SPECIAL RULE FOR AFFILIATES OF AIRLINES.—

(A) IN GENERAL.—If—

(i) a qualified affiliate is a member of an affiliated group another member of which operates an airline, and

(ii) employees of the qualified affiliate who are directly engaged in providing airline-related services are entitled to no-additional-cost service with respect to air transportation provided by such other member,

then, for purposes of applying paragraph (1) of subsection (a) to such no-additional-cost service provided to such employees, such qualified affiliate shall be treated as engaged in the same line of business as such other member.

(B) QUALIFIED AFFILIATE.—For purposes of this paragraph, the term “qualified affiliate” means any corporation which is predominantly engaged in airline-related services.

(C) AIRLINE-RELATED SERVICES.—For purposes of this paragraph, the term “airline-related services” means any of the following services provided in connection with air transportation:

- (i) Catering.
- (ii) Baggage handling.
- (iii) Ticketing and reservations.
- (iv) Flight planning and weather analysis.
- (v) Restaurants and gift shops located at an airport.
- (vi) Such other similar services provided to the airline as the Secretary may prescribe.

(D) AFFILIATED GROUP.—For purposes of this paragraph, the term “affiliated group” has the meaning given such term by section 1504(a).

(6) HIGHLY COMPENSATED EMPLOYEE.—For purposes of this section, the term “highly compensated employee” has the meaning given such term by section 414(q).

(7) AIR CARGO.—For purposes of subsection (b), the transportation of cargo by air and the transportation of passengers by air shall be treated as the same service.

(8) APPLICATION OF SECTION TO OTHERWISE TAXABLE EDUCATIONAL OR TRAINING BENEFITS.—Amounts paid or expenses incurred by the employer for education or training provided to the employee which are not excludable from gross income under section 127 shall be excluded from gross income under this section if (and only if) such amounts or expenses are a working condition fringe.

(k) CUSTOMERS NOT TO INCLUDE EMPLOYEES.—For purposes of this section (other than subsection (c)(2)), the term “customers” shall only include customers who are not employees.

(l) SECTION NOT TO APPLY TO FRINGE BENEFITS EXPRESSLY PROVIDED FOR ELSEWHERE.—This section (other than subsections (e) and (g)) shall not apply to any fringe benefits of a type the tax treatment of which is expressly provided for in any other section of this chapter.

(m) QUALIFIED RETIREMENT PLANNING SERVICES.—

(1) IN GENERAL.—For purposes of this section, the term “qualified retirement planning services” means any retirement planning advice or information provided to an employee and his spouse by an employer maintaining a qualified employer plan.

(2) NONDISCRIMINATION RULE.—Subsection (a)(7) shall apply in the case of highly compensated employees only if such services are available on substantially the same terms to each member of the group of employees normally provided education and information regarding the employer’s qualified employer plan.

(3) **QUALIFIED EMPLOYER PLAN.**—For purposes of this subsection, the term “qualified employer plan” means a plan, contract, pension, or account described in section 219(g)(5).

(n) **QUALIFIED MILITARY BASE REALIGNMENT AND CLOSURE FRINGE.**—For purposes of this section—

(1) **IN GENERAL.**—The term “qualified military base realignment and closure fringe” means 1 or more payments under the authority of section 1013 of the Demonstration Cities and Metropolitan Development Act of 1966 (42 U.S.C. 3374) (as in effect on the date of the enactment of the American Recovery and Reinvestment Tax Act of 2009).

(2) **LIMITATION.**—With respect to any property, such term shall not include any payment referred to in paragraph (1) to the extent that the sum of all of such payments related to such property exceeds the maximum amount described in subsection (c) of such section (as in effect on such date).

(o) **REGULATIONS.**—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.

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**SEC. 139D. INDIAN HEALTH CARE BENEFITS.**

(a) **GENERAL RULE.**—Except as otherwise provided in this section, gross income does not include the value of any qualified Indian health care benefit.

(b) **QUALIFIED INDIAN HEALTH CARE BENEFIT.**—For purposes of this section, the term “qualified Indian health care benefit” means—

(1) any health service or benefit provided or purchased, directly or indirectly, by the Indian Health Service through a grant to or a contract or compact with an Indian tribe or tribal organization, or through a third-party program funded by the Indian Health Service,

(2) medical care provided or purchased by, or amounts to reimburse for such medical care provided by, an Indian tribe or tribal organization for, or to, a member of an Indian tribe, including a spouse or dependent of such a member,

(3) coverage under accident or health insurance (or an arrangement having the effect of accident or health insurance), or an accident or health plan, provided by an Indian tribe or tribal organization for medical care to a member of an Indian tribe, include a spouse or dependent of such a member, and

(4) any other medical care provided by an Indian tribe or tribal organization that supplements, replaces, or substitutes for a program or service relating to medical care provided by the Federal government to Indian tribes or members of such a tribe.

(c) **DEFINITIONS.**—For purposes of this section—

(1) **INDIAN TRIBE.**—The term “Indian tribe” has the meaning given such term by section 45A(c)(6).

(2) **TRIBAL ORGANIZATION.**—The term “tribal organization” has the meaning given such term by section 4(1) of the Indian Self-Determination and Education Assistance Act.

(3) **MEDICAL CARE.**—The term “medical care” has the same meaning as when used in section 213.

(4) ACCIDENT OR HEALTH INSURANCE; ACCIDENT OR HEALTH PLAN.—The terms “accident or health insurance” and “accident or health plan” have the same meaning as when used in section 105.

(5) DEPENDENT.—The term “dependent” has the meaning given such term by [section 152] *section 7706*, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof.

(d) DENIAL OF DOUBLE BENEFIT.—Subsection (a) shall not apply to the amount of any qualified Indian health care benefit which is not includible in gross income of the beneficiary of such benefit under any other provision of this chapter, or to the amount of any such benefit for which a deduction is allowed to such beneficiary under any other provision of this chapter.

**SEC. 139E. INDIAN GENERAL WELFARE BENEFITS.**

(a) IN GENERAL.—Gross income does not include the value of any Indian general welfare benefit.

(b) INDIAN GENERAL WELFARE BENEFIT.—For purposes of this section, the term “Indian general welfare benefit” includes any payment made or services provided to or on behalf of a member of an Indian tribe (or any spouse or dependent of such a member) pursuant to an Indian tribal government program, but only if—

(1) the program is administered under specified guidelines and does not discriminate in favor of members of the governing body of the tribe, and

(2) the benefits provided under such program—

(A) are available to any tribal member who meets such guidelines,

(B) are for the promotion of general welfare,

(C) are not lavish or extravagant, and

(D) are not compensation for services.

(c) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) INDIAN TRIBAL GOVERNMENT.—For purposes of this section, the term “Indian tribal government” includes any agencies or instrumentalities of an Indian tribal government and any Alaska Native regional or village corporation, as defined in, or established pursuant to, the Alaska Native Claims Settlement Act (43 U.S.C. 1601 et seq.).

(2) DEPENDENT.—The term “dependent” has the meaning given such term by [section 152] *section 7706*, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B).

(3) LAVISH OR EXTRAVAGANT.—The Secretary shall, in consultation with the Tribal Advisory Committee (as established under section 3(a) of the Tribal General Welfare Exclusion Act of 2014), establish guidelines for what constitutes lavish or extravagant benefits with respect to Indian tribal government programs.

(4) ESTABLISHMENT OF TRIBAL GOVERNMENT PROGRAM.—A program shall not fail to be treated as an Indian tribal government program solely by reason of the program being established by tribal custom or government practice.

(5) CEREMONIAL ACTIVITIES.—Any items of cultural significance, reimbursement of costs, or cash honorarium for participation in cultural or ceremonial activities for the transmission

of tribal culture shall not be treated as compensation for services.

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## **[PART V—DEDUCTIONS FOR PERSONAL EXEMPTIONS**

### **[SEC. 151. ALLOWANCE OF DEDUCTIONS FOR PERSONAL EXEMPTIONS.**

**[(a) ALLOWANCE OF DEDUCTIONS.—**In the case of an individual, the exemptions provided by this section shall be allowed as deductions in computing taxable income.

**[(b) TAXPAYER AND SPOUSE.—**An exemption of the exemption amount for the taxpayer; and an additional exemption of the exemption amount for the spouse of the taxpayer if a joint return is not made by the taxpayer and his spouse, and if the spouse, for the calendar year in which the taxable year of the taxpayer begins, has no gross income and is not the dependent of another taxpayer.

**[(c) ADDITIONAL EXEMPTION FOR DEPENDENTS.—**An exemption of the exemption amount for each individual who is a dependent (as defined in section 152) of the taxpayer for the taxable year.

**[(d) EXEMPTION AMOUNT.—**For purposes of this section—

**[(1) IN GENERAL.—**Except as otherwise provided in this subsection, the term “exemption amount” means \$2,000.

**[(2) EXEMPTION AMOUNT DISALLOWED IN CASE OF CERTAIN DEPENDENTS.—**In the case of an individual with respect to whom a deduction under this section is allowable to another taxpayer for a taxable year beginning in the calendar year in which the individual’s taxable year begins, the exemption amount applicable to such individual for such individual’s taxable year shall be zero.

**[(3) PHASEOUT.—**

**[(A) IN GENERAL.—**In the case of any taxpayer whose adjusted gross income for the taxable year exceeds the applicable amount in effect under section 68(b), the exemption amount shall be reduced by the applicable percentage.

**[(B) APPLICABLE PERCENTAGE.—**For purposes of subparagraph (A), the term “applicable percentage” means 2 percentage points for each \$2,500 (or fraction thereof) by which the taxpayer’s adjusted gross income for the taxable year exceeds the applicable amount in effect under section 68(b). In the case of a married individual filing a separate return, the preceding sentence shall be applied by substituting “\$1,250” for “\$2,500”. In no event shall the applicable percentage exceed 100 percent.

**[(C) COORDINATION WITH OTHER PROVISIONS.—**The provisions of this paragraph shall not apply for purposes of determining whether a deduction under this section with respect to any individual is allowable to another taxpayer for any taxable year.

**[(4) INFLATION ADJUSTMENT.—**Except as provided in paragraph (5), in the case of any taxable year beginning in a calendar year after 1989, the dollar amount contained in paragraph (1) shall be increased by an amount equal to—

**[(A) such dollar amount, multiplied by**



[(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting “calendar year 1988” for “calendar year 2016” in subparagraph (A)(ii) thereof.]

[(5) SPECIAL RULES FOR TAXABLE YEARS 2018 THROUGH 2025.—In the case of a taxable year beginning after December 31, 2017, and before January 1, 2026—

[(A) EXEMPTION AMOUNT.—The term “exemption amount” means zero.]

[(B) REFERENCES.—For purposes of any other provision of this title, the reduction of the exemption amount to zero under subparagraph (A) shall not be taken into account in determining whether a deduction is allowed or allowable, or whether a taxpayer is entitled to a deduction, under this section.]

[(e) IDENTIFYING INFORMATION REQUIRED.—No exemption shall be allowed under this section with respect to any individual unless the TIN of such individual is included on the return claiming the exemption.]

**[SEC. 153. CROSS REFERENCES.]**

[(1) For deductions of estates and trusts, in lieu of the exemptions under section 151, see section 642(b).]

[(2) For exemptions of nonresident aliens, see section 873(b)(3).]

[(3) For determination of marital status, see section 7703.]

**PART VI—ITEMIZED DEDUCTIONS FOR INDIVIDUALS AND CORPORATIONS**

\* \* \* \* \*

**SEC. 162. TRADE OR BUSINESS EXPENSES.**

(a) IN GENERAL.—There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including—

(1) a reasonable allowance for salaries or other compensation for personal services actually rendered;

(2) traveling expenses (including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances) while away from home in the pursuit of a trade or business; and

(3) rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

For purposes of the preceding sentence, the place of residence of a Member of Congress (including any Delegate and Resident Commissioner) within the State, congressional district, or possession which he represents in Congress shall be considered his home, but amounts expended by such Members within each taxable year for living expenses shall not be deductible for income tax purposes. For purposes of paragraph (2), the taxpayer shall not be treated as being temporarily away from home during any period of employment if such period exceeds 1 year. The preceding sentence shall not apply to any Federal employee during any period for which such employee is certified by the Attorney General (or the designee thereof) as traveling on behalf of the United States in temporary

duty status to investigate or prosecute, or provide support services for the investigation or prosecution of, a Federal crime.

(b) CHARITABLE CONTRIBUTIONS AND GIFTS EXCEPTED.—No deduction shall be allowed under subsection (a) for any contribution or gift which would be allowable as a deduction under section 170 were it not for the percentage limitations, the dollar limitations, or the requirements as to the time of payment, set forth in such section.

(c) ILLEGAL BRIBES, KICKBACKS, AND OTHER PAYMENTS.—

(1) ILLEGAL PAYMENTS TO GOVERNMENT OFFICIALS OR EMPLOYEES.—No deduction shall be allowed under subsection (a) for any payment made, directly or indirectly, to an official or employee of any government, or of any agency or instrumentality of any government, if the payment constitutes an illegal bribe or kickback or, if the payment is to an official or employee of a foreign government, the payment is unlawful under the Foreign Corrupt Practices Act of 1977. The burden of proof in respect of the issue, for the purposes of this paragraph, as to whether a payment constitutes an illegal bribe or kickback (or is unlawful under the Foreign Corrupt Practices Act of 1977) shall be upon the Secretary to the same extent as he bears the burden of proof under section 7454 (concerning the burden of proof when the issue relates to fraud).

(2) OTHER ILLEGAL PAYMENTS.—No deduction shall be allowed under subsection (a) for any payment (other than a payment described in paragraph (1)) made, directly or indirectly, to any person, if the payment constitutes an illegal bribe, illegal kickback, or other illegal payment under any law of the United States, or under any law of a State (but only if such State law is generally enforced), which subjects the payor to a criminal penalty or the loss of license or privilege to engage in a trade or business. For purposes of this paragraph, a kickback includes a payment in consideration of the referral of a client, patient, or customer. The burden of proof in respect of the issue, for purposes of this paragraph, as to whether a payment constitutes an illegal bribe, illegal kickback, or other illegal payment shall be upon the Secretary to the same extent as he bears the burden of proof under section 7454 (concerning the burden of proof when the issue relates to fraud).

(3) KICKBACKS, REBATES, AND BRIBES UNDER MEDICARE AND MEDICAID.—No deduction shall be allowed under subsection (a) for any kickback, rebate, or bribe made by any provider of services, supplier, physician, or other person who furnishes items or services for which payment is or may be made under the Social Security Act, or in whole or in part out of Federal funds under a State plan approved under such Act, if such kickback, rebate, or bribe is made in connection with the furnishing of such items or services or the making or receipt of such payments. For purposes of this paragraph, a kickback includes a payment in consideration of the referral of a client, patient, or customer.

(d) CAPITAL CONTRIBUTIONS TO FEDERAL NATIONAL MORTGAGE ASSOCIATION.—For purposes of this subtitle, whenever the amount of capital contributions evidenced by a share of stock issued pursuant to section 303(c) of the Federal National Mortgage Association

Charter Act (12 U.S.C., sec. 1718) exceeds the fair market value of the stock as of the issue date of such stock, the initial holder of the stock shall treat the excess as ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business.

(e) DENIAL OF DEDUCTION FOR CERTAIN LOBBYING AND POLITICAL EXPENDITURES.—

(1) IN GENERAL.—No deduction shall be allowed under subsection (a) for any amount paid or incurred in connection with—

(A) influencing legislation,

(B) participation in, or intervention in, any political campaign on behalf of (or in opposition to) any candidate for public office,

(C) any attempt to influence the general public, or segments thereof, with respect to elections, legislative matters, or referendums, or

(D) any direct communication with a covered executive branch official in an attempt to influence the official actions or positions of such official.

(2) APPLICATION TO DUES OF TAX-EXEMPT ORGANIZATIONS.—No deduction shall be allowed under subsection (a) for the portion of dues or other similar amounts paid by the taxpayer to an organization which is exempt from tax under this subtitle which the organization notifies the taxpayer under section 6033(e)(1)(A)(ii) is allocable to expenditures to which paragraph (1) applies.

(3) INFLUENCING LEGISLATION.—For purposes of this subsection—

(A) IN GENERAL.—The term “influencing legislation” means any attempt to influence any legislation through communication with any member or employee of a legislative body, or with any government official or employee who may participate in the formulation of legislation.

(B) LEGISLATION.—The term “legislation” has the meaning given such term by section 4911(e)(2).

(4) OTHER SPECIAL RULES.—

(A) EXCEPTION FOR CERTAIN TAXPAYERS.—In the case of any taxpayer engaged in the trade or business of conducting activities described in paragraph (1), paragraph (1) shall not apply to expenditures of the taxpayer in conducting such activities directly on behalf of another person (but shall apply to payments by such other person to the taxpayer for conducting such activities).

(B) DE MINIMIS EXCEPTION.—

(i) IN GENERAL.—Paragraph (1) shall not apply to any in-house expenditures for any taxable year if such expenditures do not exceed \$2,000. In determining whether a taxpayer exceeds the \$2,000 limit under this clause, there shall not be taken into account overhead costs otherwise allocable to activities described in paragraphs (1)(A) and (D).

(ii) IN-HOUSE EXPENDITURES.—For purposes of clause (i), the term “in-house expenditures” means expendi-

tures described in paragraphs (1)(A) and (D) other than—

(I) payments by the taxpayer to a person engaged in the trade or business of conducting activities described in paragraph (1) for the conduct of such activities on behalf of the taxpayer, or

(II) dues or other similar amounts paid or incurred by the taxpayer which are allocable to activities described in paragraph (1).

(C) EXPENSES INCURRED IN CONNECTION WITH LOBBYING AND POLITICAL ACTIVITIES.—Any amount paid or incurred for research for, or preparation, planning, or coordination of, any activity described in paragraph (1) shall be treated as paid or incurred in connection with such activity.

(5) COVERED EXECUTIVE BRANCH OFFICIAL.—For purposes of this subsection, the term “covered executive branch official” means—

(A) the President,

(B) the Vice President,

(C) any officer or employee of the White House Office of the Executive Office of the President, and the 2 most senior level officers of each of the other agencies in such Executive Office, and

(D)(i) any individual serving in a position in level I of the Executive Schedule under section 5312 of title 5, United States Code, (ii) any other individual designated by the President as having Cabinet level status, and (iii) any immediate deputy of an individual described in clause (i) or (ii).

(6) CROSS REFERENCE.—For reporting requirements and alternative taxes related to this subsection, see section 6033(e).

(f) FINES, PENALTIES, AND OTHER AMOUNTS.—

(1) IN GENERAL.—Except as provided in the following paragraphs of this subsection, no deduction otherwise allowable shall be allowed under this chapter for any amount paid or incurred (whether by suit, agreement, or otherwise) to, or at the direction of, a government or governmental entity in relation to the violation of any law or the investigation or inquiry by such government or entity into the potential violation of any law.

(2) EXCEPTION FOR AMOUNTS CONSTITUTING RESTITUTION OR PAID TO COME INTO COMPLIANCE WITH LAW.—

(A) IN GENERAL.—Paragraph (1) shall not apply to any amount that—

(i) the taxpayer establishes—

(I) constitutes restitution (including remediation of property) for damage or harm which was or may be caused by the violation of any law or the potential violation of any law, or

(II) is paid to come into compliance with any law which was violated or otherwise involved in the investigation or inquiry described in paragraph (1),

(ii) is identified as restitution or as an amount paid to come into compliance with such law, as the case

may be, in the court order or settlement agreement, and

(iii) in the case of any amount of restitution for failure to pay any tax imposed under this title in the same manner as if such amount were such tax, would have been allowed as a deduction under this chapter if it had been timely paid.

The identification under clause (ii) alone shall not be sufficient to make the establishment required under clause (i).

(B) LIMITATION.—Subparagraph (A) shall not apply to any amount paid or incurred as reimbursement to the government or entity for the costs of any investigation or litigation.

(3) EXCEPTION FOR AMOUNTS PAID OR INCURRED AS THE RESULT OF CERTAIN COURT ORDERS.—Paragraph (1) shall not apply to any amount paid or incurred by reason of any order of a court in a suit in which no government or governmental entity is a party.

(4) EXCEPTION FOR TAXES DUE.—Paragraph (1) shall not apply to any amount paid or incurred as taxes due.

(5) TREATMENT OF CERTAIN NONGOVERNMENTAL REGULATORY ENTITIES.—For purposes of this subsection, the following nongovernmental entities shall be treated as governmental entities:

(A) Any nongovernmental entity which exercises self-regulatory powers (including imposing sanctions) in connection with a qualified board or exchange (as defined in section 1256(g)(7)).

(B) To the extent provided in regulations, any nongovernmental entity which exercises self-regulatory powers (including imposing sanctions) as part of performing an essential governmental function.

(g) TREBLE DAMAGE PAYMENTS UNDER THE ANTITRUST LAWS.—If in a criminal proceeding a taxpayer is convicted of a violation of the antitrust laws, or his plea of guilty or nolo contendere to an indictment or information charging such a violation is entered or accepted in such a proceeding, no deduction shall be allowed under subsection (a) for two-thirds of any amount paid or incurred—

(1) on any judgment for damages entered against the taxpayer under section 4 of the Act entitled “An Act to supplement existing laws against unlawful restraints and monopolies, and for other purposes”, approved October 15, 1914 (commonly known as the Clayton Act), on account of such violation or any related violation of the antitrust laws which occurred prior to the date of the final judgment of such conviction, or

(2) in settlement of any action brought under such section 4 on account of such violation or related violation.

(h) STATE LEGISLATORS’ TRAVEL EXPENSES AWAY FROM HOME.—

(1) IN GENERAL.—For purposes of subsection (a), in the case of any individual who is a State legislator at any time during the taxable year and who makes an election under this subsection for the taxable year—

(A) the place of residence of such individual within the legislative district which he represented shall be considered his home,

(B) he shall be deemed to have expended for living expenses (in connection with his trade or business as a legislator) an amount equal to the sum of the amounts determined by multiplying each legislative day of such individual during the taxable year by the greater of—

(i) the amount generally allowable with respect to such day to employees of the State of which he is a legislator for per diem while away from home, to the extent such amount does not exceed 110 percent of the amount described in clause (ii) with respect to such day, or

(ii) the amount generally allowable with respect to such day to employees of the executive branch of the Federal Government for per diem while away from home but serving in the United States, and

(C) he shall be deemed to be away from home in the pursuit of a trade or business on each legislative day.

(2) LEGISLATIVE DAYS.—For purposes of paragraph (1), a legislative day during any taxable year for any individual shall be any day during such year on which—

(A) the legislature was in session (including any day in which the legislature was not in session for a period of 4 consecutive days or less), or

(B) the legislature was not in session but the physical presence of the individual was formally recorded at a meeting of a committee of such legislature.

(3) ELECTION.—An election under this subsection for any taxable year shall be made at such time and in such manner as the Secretary shall by regulations prescribe.

(4) SECTION NOT TO APPLY TO LEGISLATORS WHO RESIDE NEAR CAPITOL.—This subsection shall not apply to any legislator whose place of residence within the legislative district which he represents is 50 or fewer miles from the capitol building of the State.

(j) CERTAIN FOREIGN ADVERTISING EXPENSES.—

(1) IN GENERAL.—No deduction shall be allowed under subsection (a) for any expenses of an advertisement carried by a foreign broadcast undertaking and directed primarily to a market in the United States. This paragraph shall apply only to foreign broadcast undertakings located in a country which denies a similar deduction for the cost of advertising directed primarily to a market in the foreign country when placed with a United States broadcast undertaking.

(2) BROADCAST UNDERTAKING.—For purposes of paragraph (1), the term “broadcast undertaking” includes (but is not limited to) radio and television stations.

(k) STOCK REACQUISITION EXPENSES.—

(1) IN GENERAL.—Except as provided in paragraph (2), no deduction otherwise allowable shall be allowed under this chapter for any amount paid or incurred by a corporation in connection with the reacquisition of its stock or of the stock of any related person (as defined in section 465(b)(3)(C)).

(2) EXCEPTIONS.—Paragraph (1) shall not apply to—

(A) CERTAIN SPECIFIC DEDUCTIONS.—Any—

(i) deduction allowable under section 163 (relating to interest),

(ii) deduction for amounts which are properly allocable to indebtedness and amortized over the term of such indebtedness, or

(iii) deduction for dividends paid (within the meaning of section 561).

(B) STOCK OF CERTAIN REGULATED INVESTMENT COMPANIES.—Any amount paid or incurred in connection with the redemption of any stock in a regulated investment company which issues only stock which is redeemable upon the demand of the shareholder.

(1) SPECIAL RULES FOR HEALTH INSURANCE COSTS OF SELF-EMPLOYED INDIVIDUALS.—

(1) ALLOWANCE OF DEDUCTION.—In the case of a taxpayer who is an employee within the meaning of section 401(c)(1), there shall be allowed as a deduction under this section an amount equal to the amount paid during the taxable year for insurance which constitutes medical care for—

(A) the taxpayer,

(B) the taxpayer's spouse,

(C) the taxpayer's dependents, and

(D) any child (as defined in [section 152(f)(1)] *section 7706(f)(1)*) of the taxpayer who as of the end of the taxable year has not attained age 27.

(2) LIMITATIONS.—

(A) DOLLAR AMOUNT.—No deduction shall be allowed under paragraph (1) to the extent that the amount of such deduction exceeds the taxpayer's earned income (within the meaning of section 401(c)) derived by the taxpayer from the trade or business with respect to which the plan providing the medical care coverage is established.

(B) OTHER COVERAGE.—Paragraph (1) shall not apply to any taxpayer for any calendar month for which the taxpayer is eligible to participate in any subsidized health plan maintained by any employer of the taxpayer or of the spouse of, or any dependent, or individual described in subparagraph (D) of paragraph (1) with respect to, the taxpayer. The preceding sentence shall be applied separately with respect to—

(i) plans which include coverage for qualified long-term care services (as defined in section 7702B(c)) or are qualified long-term care insurance contracts (as defined in section 7702B(b)), and

(ii) plans which do not include such coverage and are not such contracts.

(C) LONG-TERM CARE PREMIUMS.—In the case of a qualified long-term care insurance contract (as defined in section 7702B(b)), only eligible long-term care premiums (as defined in section 213(d)(10)) shall be taken into account under paragraph (1).

(3) COORDINATION WITH MEDICAL DEDUCTION.—Any amount paid by a taxpayer for insurance to which paragraph (1) applies shall not be taken into account in computing the amount allowable to the taxpayer as a deduction under section 213(a).

(4) DEDUCTION NOT ALLOWED FOR SELF-EMPLOYMENT TAX PURPOSES.—The deduction allowable by reason of this subsection shall not be taken into account in determining an individual's net earnings from self-employment (within the meaning of section 1402(a)) for purposes of chapter 2 for taxable years beginning before January 1, 2010, or after December 31, 2010.

(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.

(m) CERTAIN EXCESSIVE EMPLOYEE REMUNERATION.—

(1) IN GENERAL.—In the case of any publicly held corporation, no deduction shall be allowed under this chapter for applicable employee remuneration with respect to any covered employee to the extent that the amount of such remuneration for the taxable year with respect to such employee exceeds \$1,000,000.

(2) PUBLICLY HELD CORPORATION.—For purposes of this subsection, the term “publicly held corporation” means any corporation which is an issuer (as defined in section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78c))—

(A) the securities of which are required to be registered under section 12 of such Act (15 U.S.C. 78l), or

(B) that is required to file reports under section 15(d) of such Act (15 U.S.C. 78o(d)).

(3) COVERED EMPLOYEE.—For purposes of this subsection, the term “covered employee” means any employee of the taxpayer if—

(A) such employee is the principal executive officer or principal financial officer of the taxpayer at any time during the taxable year, or was an individual acting in such a capacity,

(B) the total compensation of such employee for the taxable year is required to be reported to shareholders under the Securities Exchange Act of 1934 by reason of such employee being among the 3 highest compensated officers for the taxable year (other than any individual described in subparagraph (A)), or

(C) was a covered employee of the taxpayer (or any predecessor) for any preceding taxable year beginning after December 31, 2016.

Such term shall include any employee who would be described in subparagraph (B) if the reporting described in such subparagraph were required as so described.

(4) APPLICABLE EMPLOYEE REMUNERATION.—For purposes of this subsection—

(A) IN GENERAL.—Except as otherwise provided in this paragraph, the term “applicable employee remuneration”



means, with respect to any covered employee for any taxable year, the aggregate amount allowable as a deduction under this chapter for such taxable year (determined without regard to this subsection) for remuneration for services performed by such employee (whether or not during the taxable year).

(B) EXCEPTION FOR EXISTING BINDING CONTRACTS.—The term “applicable employee remuneration” shall not include any remuneration payable under a written binding contract which was in effect on February 17, 1993, and which was not modified thereafter in any material respect before such remuneration is paid.

(C) REMUNERATION.—For purposes of this paragraph, the term “remuneration” includes any remuneration (including benefits) in any medium other than cash, but shall not include—

- (i) any payment referred to in so much of section 3121(a)(5) as precedes subparagraph (E) thereof, and
- (ii) any benefit provided to or on behalf of an employee if at the time such benefit is provided it is reasonable to believe that the employee will be able to exclude such benefit from gross income under this chapter.

For purposes of clause (i), section 3121(a)(5) shall be applied without regard to section 3121(v)(1).

(D) COORDINATION WITH DISALLOWED GOLDEN PARACHUTE PAYMENTS.—The dollar limitation contained in paragraph (1) shall be reduced (but not below zero) by the amount (if any) which would have been included in the applicable employee remuneration of the covered employee for the taxable year but for being disallowed under section 280G.

(E) COORDINATION WITH EXCISE TAX ON SPECIFIED STOCK COMPENSATION.—The dollar limitation contained in paragraph (1) with respect to any covered employee shall be reduced (but not below zero) by the amount of any payment (with respect to such employee) of the tax imposed by section 4985 directly or indirectly by the expatriated corporation (as defined in such section) or by any member of the expanded affiliated group (as defined in such section) which includes such corporation.

(F) SPECIAL RULE FOR REMUNERATION PAID TO BENEFICIARIES, ETC.—Remuneration shall not fail to be applicable employee remuneration merely because it is includible in the income of, or paid to, a person other than the covered employee, including after the death of the covered employee.

(5) SPECIAL RULE FOR APPLICATION TO EMPLOYERS PARTICIPATING IN THE TROUBLED ASSETS RELIEF PROGRAM.—

(A) IN GENERAL.—In the case of an applicable employer, no deduction shall be allowed under this chapter—

- (i) in the case of executive remuneration for any applicable taxable year which is attributable to services performed by a covered executive during such applica-

ble taxable year, to the extent that the amount of such remuneration exceeds \$500,000, or

(ii) in the case of deferred deduction executive remuneration for any taxable year for services performed during any applicable taxable year by a covered executive, to the extent that the amount of such remuneration exceeds \$500,000 reduced (but not below zero) by the sum of—

(I) the executive remuneration for such applicable taxable year, plus

(II) the portion of the deferred deduction executive remuneration for such services which was taken into account under this clause in a preceding taxable year.

(B) APPLICABLE EMPLOYER.—For purposes of this paragraph—

(i) IN GENERAL.—Except as provided in clause (ii), the term “applicable employer” means any employer from whom 1 or more troubled assets are acquired under a program established by the Secretary under section 101(a) of the Emergency Economic Stabilization Act of 2008 if the aggregate amount of the assets so acquired for all taxable years exceeds \$300,000,000.

(ii) DISREGARD OF CERTAIN ASSETS SOLD THROUGH DIRECT PURCHASE.—If the only sales of troubled assets by an employer under the program described in clause (i) are through 1 or more direct purchases (within the meaning of section 113(c) of the Emergency Economic Stabilization Act of 2008), such assets shall not be taken into account under clause (i) in determining whether the employer is an applicable employer for purposes of this paragraph.

(iii) AGGREGATION RULES.—Two or more persons who are treated as a single employer under subsection (b) or (c) of section 414 shall be treated as a single employer, except that in applying section 1563(a) for purposes of either such subsection, paragraphs (2) and (3) thereof shall be disregarded.

(C) APPLICABLE TAXABLE YEAR.—For purposes of this paragraph, the term “applicable taxable year” means, with respect to any employer—

(i) the first taxable year of the employer—

(I) which includes any portion of the period during which the authorities under section 101(a) of the Emergency Economic Stabilization Act of 2008 are in effect (determined under section 120 thereof), and

(II) in which the aggregate amount of troubled assets acquired from the employer during the taxable year pursuant to such authorities (other than assets to which subparagraph (B)(ii) applies), when added to the aggregate amount so acquired for all preceding taxable years, exceeds \$300,000,000, and

(ii) any subsequent taxable year which includes any portion of such period.

(D) COVERED EXECUTIVE.—For purposes of this paragraph—

(i) IN GENERAL.—The term “covered executive” means, with respect to any applicable taxable year, any employee—

(I) who, at any time during the portion of the taxable year during which the authorities under section 101(a) of the Emergency Economic Stabilization Act of 2008 are in effect (determined under section 120 thereof), is the chief executive officer of the applicable employer or the chief financial officer of the applicable employer, or an individual acting in either such capacity, or

(II) who is described in clause (ii).

(ii) HIGHEST COMPENSATED EMPLOYEES.—An employee is described in this clause if the employee is 1 of the 3 highest compensated officers of the applicable employer for the taxable year (other than an individual described in clause (i)(I)), determined—

(I) on the basis of the shareholder disclosure rules for compensation under the Securities Exchange Act of 1934 (without regard to whether those rules apply to the employer), and

(II) by only taking into account employees employed during the portion of the taxable year described in clause (i)(I).

(iii) EMPLOYEE REMAINS COVERED EXECUTIVE.—If an employee is a covered executive with respect to an applicable employer for any applicable taxable year, such employee shall be treated as a covered executive with respect to such employer for all subsequent applicable taxable years and for all subsequent taxable years in which deferred deduction executive remuneration with respect to services performed in all such applicable taxable years would (but for this paragraph) be deductible.

(E) EXECUTIVE REMUNERATION.—For purposes of this paragraph, the term “executive remuneration” means the applicable employee remuneration of the covered executive, as determined under paragraph (4) without regard to subparagraph (B) thereof. Such term shall not include any deferred deduction executive remuneration with respect to services performed in a prior applicable taxable year.

(F) DEFERRED DEDUCTION EXECUTIVE REMUNERATION.—For purposes of this paragraph, the term “deferred deduction executive remuneration” means remuneration which would be executive remuneration for services performed in an applicable taxable year but for the fact that the deduction under this chapter (determined without regard to this paragraph) for such remuneration is allowable in a subsequent taxable year.

(G) COORDINATION.—Rules similar to the rules of subparagraphs (D) and (E) of paragraph (4) shall apply for purposes of this paragraph.

(H) REGULATORY AUTHORITY.—The Secretary may prescribe such guidance, rules, or regulations as are necessary to carry out the purposes of this paragraph and the Emergency Economic Stabilization Act of 2008, including the extent to which this paragraph applies in the case of any acquisition, merger, or reorganization of an applicable employer.

(6) SPECIAL RULE FOR APPLICATION TO CERTAIN HEALTH INSURANCE PROVIDERS.—

(A) IN GENERAL.—No deduction shall be allowed under this chapter—

(i) in the case of applicable individual remuneration which is for any disqualified taxable year beginning after December 31, 2012, and which is attributable to services performed by an applicable individual during such taxable year, to the extent that the amount of such remuneration exceeds \$500,000, or

(ii) in the case of deferred deduction remuneration for any taxable year beginning after December 31, 2012, which is attributable to services performed by an applicable individual during any disqualified taxable year beginning after December 31, 2009, to the extent that the amount of such remuneration exceeds \$500,000 reduced (but not below zero) by the sum of—

(I) the applicable individual remuneration for such disqualified taxable year, plus

(II) the portion of the deferred deduction remuneration for such services which was taken into account under this clause in a preceding taxable year (or which would have been taken into account under this clause in a preceding taxable year if this clause were applied by substituting ‘December 31, 2009’ for ‘December 31, 2012’ in the matter preceding subclause (I)).

(B) DISQUALIFIED TAXABLE YEAR.—For purposes of this paragraph, the term “disqualified taxable year” means, with respect to any employer, any taxable year for which such employer is a covered health insurance provider.

(C) COVERED HEALTH INSURANCE PROVIDER.—For purposes of this paragraph—

(i) IN GENERAL.—The term “covered health insurance provider” means—

(I) with respect to taxable years beginning after December 31, 2009, and before January 1, 2013, any employer which is a health insurance issuer (as defined in section 9832(b)(2)) and which receives premiums from providing health insurance coverage (as defined in section 9832(b)(1)), and

(II) with respect to taxable years beginning after December 31, 2012, any employer which is a health insurance issuer (as defined in section 9832(b)(2)) and with respect to which not less

than 25 percent of the gross premiums received from providing health insurance coverage (as defined in section 9832(b)(1)) is from minimum essential coverage (as defined in section 5000A(f)).

(ii) AGGREGATION RULES.—Two or more persons who are treated as a single employer under subsection (b), (c), (m), or (o) of section 414 shall be treated as a single employer, except that in applying section 1563(a) for purposes of any such subsection, paragraphs (2) and (3) thereof shall be disregarded.

(D) APPLICABLE INDIVIDUAL REMUNERATION.—For purposes of this paragraph, the term “applicable individual remuneration” means, with respect to any applicable individual for any disqualified taxable year, the aggregate amount allowable as a deduction under this chapter for such taxable year (determined without regard to this subsection) for remuneration (as defined in paragraph (4) without regard to subparagraph (B) thereof) for services performed by such individual (whether or not during the taxable year). Such term shall not include any deferred deduction remuneration with respect to services performed during the disqualified taxable year.

(E) DEFERRED DEDUCTION REMUNERATION.—For purposes of this paragraph, the term “deferred deduction remuneration” means remuneration which would be applicable individual remuneration for services performed in a disqualified taxable year but for the fact that the deduction under this chapter (determined without regard to this paragraph) for such remuneration is allowable in a subsequent taxable year.

(F) APPLICABLE INDIVIDUAL.—For purposes of this paragraph, the term “applicable individual” means, with respect to any covered health insurance provider for any disqualified taxable year, any individual—

(i) who is an officer, director, or employee in such taxable year, or

(ii) who provides services for or on behalf of such covered health insurance provider during such taxable year.

(G) COORDINATION.—Rules similar to the rules of subparagraphs (D) and (E) of paragraph (4) shall apply for purposes of this paragraph.

(H) REGULATORY AUTHORITY.—The Secretary may prescribe such guidance, rules, or regulations as are necessary to carry out the purposes of this paragraph.

(n) SPECIAL RULE FOR CERTAIN GROUP HEALTH PLANS.—

(1) IN GENERAL.—No deduction shall be allowed under this chapter to an employer for any amount paid or incurred in connection with a group health plan if the plan does not reimburse for inpatient hospital care services provided in the State of New York—

(A) except as provided in subparagraphs (B) and (C), at the same rate as licensed commercial insurers are required to reimburse hospitals for such services when such reimbursement is not through such a plan,

(B) in the case of any reimbursement through a health maintenance organization, at the same rate as health maintenance organizations are required to reimburse hospitals for such services for individuals not covered by such a plan (determined without regard to any government-supported individuals exempt from such rate), or

(C) in the case of any reimbursement through any corporation organized under Article 43 of the New York State Insurance Law, at the same rate as any such corporation is required to reimburse hospitals for such services for individuals not covered by such a plan.

(2) STATE LAW EXCEPTION.—Paragraph (1) shall not apply to any group health plan which is not required under the laws of the State of New York (determined without regard to this subsection or other provisions of Federal law) to reimburse at the rates provided in paragraph (1).

(3) GROUP HEALTH PLAN.—For purposes of this subsection, the term “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 any employee, any former employee, the employer, or any other individual associated or formerly associated with the employer in a business relationship, or any member of their family.

(o) TREATMENT OF CERTAIN EXPENSES OF RURAL MAIL CARRIERS.—

(1) GENERAL RULE.—In the case of any employee of the United States Postal Service who performs services involving the collection and delivery of mail on a rural route and who receives qualified reimbursements for the expenses incurred by such employee for the use of a vehicle in performing such services—

(A) the amount allowable as a deduction under this chapter for the use of a vehicle in performing such services shall be equal to the amount of such qualified reimbursements; and

(B) such qualified reimbursements shall be treated as paid under a reimbursement or other expense allowance arrangement for purposes of section 62(a)(2)(A) (and section 62(c) shall not apply to such qualified reimbursements).

(2) SPECIAL RULE WHERE EXPENSES EXCEED REIMBURSEMENTS.—Notwithstanding paragraph (1)(A), if the expenses incurred by an employee for the use of a vehicle in performing services described in paragraph (1) exceed the qualified reimbursements for such expenses, such excess shall be taken into account in computing the miscellaneous itemized deductions of the employee under section 67.

(3) DEFINITION OF QUALIFIED REIMBURSEMENTS.—For purposes of this subsection, the term “qualified reimbursements” means the amounts paid by the United States Postal Service to employees as an equipment maintenance allowance under the 1991 collective bargaining agreement between the United States Postal Service and the National Rural Letter Carriers’ Association. Amounts paid as an equipment maintenance allowance by such Postal Service under later collective bargaining agreements that supersede the 1991 agreement shall

be considered qualified reimbursements if such amounts do not exceed the amounts that would have been paid under the 1991 agreement, adjusted by increasing any such amount under the 1991 agreement by an amount equal to—

(A) such amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting “calendar year 1990” for “calendar year 2016” in subparagraph (A)(ii) thereof.

(p) TREATMENT OF EXPENSES OF MEMBERS OF RESERVE COMPONENT OF ARMED FORCES OF THE UNITED STATES.—For purposes of subsection (a)(2), in the case of an individual who performs services as a member of a reserve component of the Armed Forces of the United States at any time during the taxable year, such individual shall be deemed to be away from home in the pursuit of a trade or business for any period during which such individual is away from home in connection with such service.

(q) PAYMENTS RELATED TO SEXUAL HARASSMENT AND SEXUAL ABUSE.—No deduction shall be allowed under this chapter for—

(1) any settlement or payment related to sexual harassment or sexual abuse if such settlement or payment is subject to a nondisclosure agreement, or

(2) attorney’s fees related to such a settlement or payment.

(r) DISALLOWANCE OF FDIC PREMIUMS PAID BY CERTAIN LARGE FINANCIAL INSTITUTIONS.—

(1) IN GENERAL.—No deduction shall be allowed for the applicable percentage of any FDIC premium paid or incurred by the taxpayer.

(2) EXCEPTION FOR SMALL INSTITUTIONS.—Paragraph (1) shall not apply to any taxpayer for any taxable year if the total consolidated assets of such taxpayer (determined as of the close of such taxable year) do not exceed \$10,000,000,000.

(3) APPLICABLE PERCENTAGE.—For purposes of this subsection, the term “applicable percentage” means, with respect to any taxpayer for any taxable year, the ratio (expressed as a percentage but not greater than 100 percent) which—

(A) the excess of—

(i) the total consolidated assets of such taxpayer (determined as of the close of such taxable year), over

(ii) \$10,000,000,000, bears to (B) \$40,000,000,000.

(4) FDIC PREMIUMS.—For purposes of this subsection, the term “FDIC premium” means any assessment imposed under section 7(b) of the Federal Deposit Insurance Act (12 U.S.C. 1817(b)).

(5) TOTAL CONSOLIDATED ASSETS.—For purposes of this subsection, the term “total consolidated assets” has the meaning given such term under section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (12 U.S.C. 5365).

(6) AGGREGATION RULE.—

(A) IN GENERAL.—Members of an expanded affiliated group shall be treated as a single taxpayer for purposes of applying this subsection.

(B) EXPANDED AFFILIATED GROUP.—

(i) **IN GENERAL.**—For purposes of this paragraph, the term “expanded affiliated group” means an affiliated group as defined in section 1504(a), determined—

(I) by substituting “more than 50 percent” for “at least 80 percent” each place it appears, and

(II) without regard to paragraphs (2) and (3) of section 1504(b).

(ii) **CONTROL OF NON-CORPORATE ENTITIES.**—A partnership or any other entity (other than a corporation) shall be treated as a member of an expanded affiliated group if such entity is controlled (within the meaning of section 954(d)(3)) by members of such group (including any entity treated as a member of such group by reason of this clause).

(s) **CROSS REFERENCE.**—

(1) For special rule relating to expenses in connection with subdividing real property for sale, see section 1237.

(2) For special rule relating to the treatment of payments by a transferee of a franchise, trademark, or trade name, see section 1253.

(3) For special rules relating to—

(A) funded welfare benefit plans, see section 419, and

(B) deferred compensation and other deferred benefits, see section 404.

**SEC. 163. INTEREST.**

(a) **GENERAL RULE.**—There shall be allowed as a deduction all interest paid or accrued within the taxable year on indebtedness.

(b) **INSTALLMENT PURCHASES WHERE INTEREST CHARGE IS NOT SEPARATELY STATED.**—

(1) **GENERAL RULE.**—If personal property or educational services are purchased under a contract—

(A) which provides that payment of part or all of the purchase price is to be made in installments, and

(B) in which carrying charges are separately stated but the interest charge cannot be ascertained,

then the payments made during the taxable year under the contract shall be treated for purposes of this section as if they included interest equal to 6 percent of the average unpaid balance under the contract during the taxable year. For purposes of the preceding sentence, the average unpaid balance is the sum of the unpaid balance outstanding on the first day of each month beginning during the taxable year, divided by 12. For purposes of this paragraph, the term “educational services” means any service (including lodging) which is purchased from an educational organization described in section 170(b)(1)(A)(ii) and which is provided for a student of such organization.

(2) **LIMITATION.**—In the case of any contract to which paragraph (1) applies, the amount treated as interest for any taxable year shall not exceed the aggregate carrying charges which are properly attributable to such taxable year.

(c) **REDEEMABLE GROUND RENTS.**—For purposes of this subtitle, any annual or periodic rental under a redeemable ground rent (excluding amounts in redemption thereof) shall be treated as interest on an indebtedness secured by a mortgage.

(d) **LIMITATION ON INVESTMENT INTEREST.**—



(1) **IN GENERAL.**—In the case of a taxpayer other than a corporation, the amount allowed as a deduction under this chapter for investment interest for any taxable year shall not exceed the net investment income of the taxpayer for the taxable year.

(2) **CARRYFORWARD OF DISALLOWED INTEREST.**—The amount not allowed as a deduction for any taxable year by reason of paragraph (1) shall be treated as investment interest paid or accrued by the taxpayer in the succeeding taxable year.

(3) **INVESTMENT INTEREST.**—For purposes of this subsection—

(A) **IN GENERAL.**—The term “investment interest” means any interest allowable as a deduction under this chapter (determined without regard to paragraph (1)) which is paid or accrued on indebtedness properly allocable to property held for investment.

(B) **EXCEPTIONS.**—The term “investment interest” shall not include—

(i) any qualified residence interest (as defined in subsection (h)(3)), or

(ii) any interest which is taken into account under section 469 in computing income or loss from a passive activity of the taxpayer.

(C) **PERSONAL PROPERTY USED IN SHORT SALE.**—For purposes of this paragraph, the term “interest” includes any amount allowable as a deduction in connection with personal property used in a short sale.

(4) **NET INVESTMENT INCOME.**—For purposes of this subsection—

(A) **IN GENERAL.**—The term “net investment income” means the excess of—

(i) investment income, over

(ii) investment expenses.

(B) **INVESTMENT INCOME.**—The term “investment income” means the sum of—

(i) gross income from property held for investment (other than any gain taken into account under clause (ii)(I)),

(ii)(I),

(ii) the excess (if any) of—

(I) the net gain attributable to the disposition of property held for investment, over

(II) the net capital gain determined by only taking into account gains and losses from dispositions of property held for investment, plus (iii) so much of the net capital gain referred to in clause (ii)(II) (or, if lesser, the net gain referred to in clause (ii)(I)) as the taxpayer elects to take into account under this clause.

Such term shall include qualified dividend income (as defined in section 1(h)(11)(B)) only to the extent the taxpayer elects to treat such income as investment income for purposes of this subsection.

(C) **INVESTMENT EXPENSES.**—The term “investment expenses” means the deductions allowed under this chapter (other than for interest) which are directly connected with the production of investment income.

- (D) INCOME AND EXPENSES FROM PASSIVE ACTIVITIES.—Investment income and investment expenses shall not include any income or expenses taken into account under section 469 in computing income or loss from a passive activity.
- (5) PROPERTY HELD FOR INVESTMENT.—For purposes of this subsection—
- (A) IN GENERAL.—The term “property held for investment” shall include—
- (i) any property which produces income of a type described in section 469(e)(1), and
  - (ii) any interest held by a taxpayer in an activity involving the conduct of a trade or business—
    - (I) which is not a passive activity, and
    - (II) with respect to which the taxpayer does not materially participate.
- (B) INVESTMENT EXPENSES.—In the case of property described in subparagraph (A)(i), expenses shall be allocated to such property in the same manner as under section 469.
- (C) TERMS.—For purposes of this paragraph, the terms “activity”, “passive activity”, and “materially participate” have the meanings given such terms by section 469.
- (e) ORIGINAL ISSUE DISCOUNT.—
- (1) IN GENERAL.—The portion of the original issue discount with respect to any debt instrument which is allowable as a deduction to the issuer for any taxable year shall be equal to the aggregate daily portions of the original issue discount for days during such taxable year.
- (2) DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—
- (A) DEBT INSTRUMENT.—The term “debt instrument” has the meaning given such term by section 1275(a)(1).
- (B) DAILY PORTIONS.—The daily portion of the original issue discount for any day shall be determined under section 1272(a) (without regard to paragraph (7) thereof and without regard to section 1273(a)(3)).
- (C) SHORT-TERM OBLIGATIONS.—In the case of an obligor of a short-term obligation (as defined in section 1283(a)(1)(A)) who uses the cash receipts and disbursements method of accounting, the original issue discount (and any other interest payable) on such obligation shall be deductible only when paid.
- (3) SPECIAL RULE FOR ORIGINAL ISSUE DISCOUNT ON OBLIGATION HELD BY RELATED FOREIGN PERSON.—
- (A) IN GENERAL.—If any debt instrument having original issue discount is held by a related foreign person, any portion of such original issue discount shall not be allowable as a deduction to the issuer until paid. The preceding sentence shall not apply to the extent that the original issue discount is effectively connected with the conduct by such foreign related person of a trade or business within the United States unless such original issue discount is exempt from taxation (or is subject to a reduced rate of tax) pursuant to a treaty obligation of the United States.
- (B) SPECIAL RULE FOR CERTAIN FOREIGN ENTITIES.—

(i) **IN GENERAL.**—In the case of any debt instrument having original issue discount which is held by a related foreign person which is a controlled foreign corporation (as defined in section 957) or a passive foreign investment company (as defined in section 1297), a deduction shall be allowable to the issuer with respect to such original issue discount for any taxable year before the taxable year in which paid only to the extent such original issue discount is includible (determined without regard to properly allocable deductions and qualified deficits under section 952(c)(1)(B)) during such prior taxable year in the gross income of a United States person who owns (within the meaning of section 958(a)) stock in such corporation.

(ii) **SECRETARIAL AUTHORITY.**—The Secretary may by regulation exempt transactions from the application of clause (i), including any transaction which is entered into by a payor in the ordinary course of a trade or business in which the payor is predominantly engaged.

(C) **RELATED FOREIGN PERSON.**—For purposes of subparagraph (A), the term “related foreign person” means any person—

- (i) who is not a United States person, and
- (ii) who is related (within the meaning of section 267(b)) to the issuer.

(4) **EXCEPTION.**—This subsection shall not apply to any debt instrument described in section 1272(a)(2)(D) (relating to loans between natural persons).

(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 this paragraph, rules similar to the rules of subsection (i)(3)(B) shall apply in determining the amount of the original issue discount and 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 in 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) SUSPENSION OF APPLICATION OF PARAGRAPH.—

(i) TEMPORARY SUSPENSION.—This paragraph shall not apply to any applicable high yield discount obligation issued during the period beginning on September 1, 2008, and ending on December 31, 2009, in exchange (including an exchange resulting from a modification of the debt instrument) for an obligation which is not an applicable high yield discount obligation and the issuer (or obligor) of which is the same as the issuer (or obligor) of such applicable high yield discount obligation. The preceding sentence shall not apply to any obligation the interest on which is interest described in section 871(h)(4) (without regard to subparagraph (D) thereof) or to any obligation issued to a related person (within the meaning of section 108(e)(4)).

(ii) **SUCCESSIVE APPLICATION.**—Any obligation to which clause (i) applies shall not be treated as an applicable high yield discount obligation for purposes of applying this subparagraph to any other obligation issued in exchange for such obligation.

(iii) **SECRETARIAL AUTHORITY TO SUSPEND APPLICATION.**—The Secretary may apply this paragraph with respect to debt instruments issued in periods following the period described in clause (i) if the Secretary determines that such application is appropriate in light of distressed conditions in the debt capital markets.

(G) **CROSS REFERENCE.**—For definition of applicable high yield discount obligation, see subsection (i).

(6) **CROSS REFERENCES FOR PROVISION RELATING TO DEDUCTION OF ORIGINAL ISSUE.**—discount on tax-exempt obligation, see section 1288.

For special rules in the case of the borrower under certain loans for personal use, see section 1275(b).

(f) **DENIAL OF DEDUCTION FOR INTEREST ON CERTAIN OBLIGATIONS NOT IN REGISTERED FORM.**—

(1) **IN GENERAL.**—Nothing in subsection (a) or in any other provision of law shall be construed to provide a deduction for interest on any registration-required obligation unless such obligation is in registered form.

(2) **REGISTRATION-REQUIRED OBLIGATION.**—For purposes of this section—

(A) **IN GENERAL.**—The term “registration-required obligation” means any obligation (including any obligation issued by a governmental entity) other than an obligation which—

- (i) is issued by a natural person,
- (ii) is not of a type offered to the public, or
- (iii) has a maturity (at issue) of not more than 1 year.

(B) **AUTHORITY TO INCLUDE OTHER OBLIGATIONS.**—Clauses (ii) and (iii) of subparagraph (A) shall not apply to any obligation if—

- (i) such obligation is of a type which the Secretary has determined by regulations to be used frequently in avoiding Federal taxes, and
- (ii) such obligation is issued after the date on which the regulations referred to in clause (i) take effect.

(3) **BOOK ENTRIES PERMITTED, ETC.**—For purposes of this subsection, rules similar to the rules of section 149(a)(3) shall apply, except that a dematerialized book entry system or other book entry system specified by the Secretary shall be treated as a book entry system described in such section.

(g) **REDUCTION OF DEDUCTION WHERE SECTION 25 CREDIT TAKEN.**—The amount of the deduction under this section for interest paid or accrued during any taxable year on indebtedness with respect to which a mortgage credit certificate has been issued under section 25 shall be reduced by the amount of the credit allowable with respect to such interest under section 25 (determined without regard to section 26).

(h) **DISALLOWANCE OF DEDUCTION FOR PERSONAL INTEREST.**—

(1) **IN GENERAL.**—In the case of a taxpayer other than a corporation, no deduction shall be allowed under this chapter for personal interest paid or accrued during the taxable year.

(2) **PERSONAL INTEREST.**—For purposes of this subsection, the term “personal interest” means any interest allowable as a deduction under this chapter other than—

(A) interest paid or accrued on indebtedness properly allocable to a trade or business (other than the trade or business of performing services as an employee),

(B) any investment interest (within the meaning of subsection (d)),

(C) any interest which is taken into account under section 469 in computing income or loss from a passive activity of the taxpayer,

(D) any qualified residence interest (within the meaning of paragraph (3)),

(E) any interest payable under section 6601 on any unpaid portion of the tax imposed by section 2001 for the period during which an extension of time for payment of such tax is in effect under section 6163, and

(F) any interest allowable as a deduction under section 221 (relating to interest on educational loans).

(3) **QUALIFIED RESIDENCE INTEREST.**—For purposes of this subsection—

(A) **IN GENERAL.**—The term “qualified residence interest” means any interest which is paid or accrued **[during the taxable year on—]**

**[(i) acquisition indebtedness with respect to any qualified residence of the taxpayer, or**

**[(ii) [home equity indebtedness with respect to any qualified residence of the taxpayer.] *during the taxable year on acquisition indebtedness with respect to any qualified residence of the taxpayer.***

For purposes of the preceding sentence, the determination of whether any property is a qualified residence of the taxpayer shall be made as of the time the interest is accrued.

(B) **ACQUISITION INDEBTEDNESS.**—

(i) **IN GENERAL.**—The term “acquisition indebtedness” means any indebtedness which—

(I) is incurred in acquiring, constructing, or substantially improving any qualified residence of the taxpayer, and

(II) is secured by such residence.

Such term also includes any indebtedness secured by such residence resulting from the refinancing of indebtedness meeting the requirements of the preceding sentence (or this sentence); but only to the extent the amount of the indebtedness resulting from such refinancing does not exceed the amount of the refinanced indebtedness.

**[(ii) \$1,000,000 LIMITATION.**—The aggregate amount treated as acquisition indebtedness for any period shall not exceed \$1,000,000 (\$500,000 in the case of a married individual filing a separate return).**]**

(ii) *LIMITATION.*—The aggregate amount treated as acquisition indebtedness for any period shall not exceed the excess (if any) of—

(I) \$750,000 (\$375,000, in the case of a married individual filing a separate return), over

(II) the sum of the aggregate outstanding pre-October 13, 1987, indebtedness (as defined in subparagraph (D)) plus the aggregate outstanding pre-December 15, 2017, indebtedness (as defined in subparagraph (C)).

**[(C) HOME EQUITY INDEBTEDNESS.—**

**[(i) IN GENERAL.—**The term “home equity indebtedness” means any indebtedness (other than acquisition indebtedness) secured by a qualified residence to the extent the aggregate amount of such indebtedness does not exceed—

**[(I) the fair market value of such qualified residence, reduced by**

**[(II) the amount of acquisition indebtedness with respect to such residence.**

**[(ii) LIMITATION.—**The aggregate amount treated as home equity indebtedness for any period shall not exceed \$100,000 (\$50,000 in the case of a separate return by a married individual).**]**

**(C) TREATMENT OF INDEBTEDNESS INCURRED ON OR BEFORE DECEMBER 15, 2017.—**

(i) *IN GENERAL.*—In the case of any pre-December 15, 2017, indebtedness, subparagraph (B)(ii) shall not apply and the aggregate amount of such indebtedness treated as acquisition indebtedness for any period shall not exceed the excess (if any) of—

(I) \$1,000,000 (\$500,000, in the case of a married individual filing a separate return), over

(II) the aggregate outstanding pre-October 13, 1987, indebtedness (as defined in subparagraph (D)).

(ii) *PRE-DECEMBER 15, 2017, INDEBTEDNESS.*—For purposes of this subparagraph—

(I) *IN GENERAL.*—The term “pre-December 15, 2017, indebtedness” means indebtedness (other than pre-October 13, 1987, indebtedness) incurred on or before December 15, 2017.

(II) *BINDING WRITTEN CONTRACT EXCEPTION.*—In the case of a taxpayer who enters into a written binding contract before December 15, 2017, to close on the purchase of a principal residence before January 1, 2018, and who purchases such residence before April 1, 2018, the term “pre-December 15, 2017, indebtedness” shall include indebtedness secured by such residence.

(iii) *REFINANCING INDEBTEDNESS.*—

(I) *IN GENERAL.*—In the case of any indebtedness which is incurred to refinance indebtedness, such refinanced indebtedness shall be treated for purposes of this subparagraph as incurred on the date

that the original indebtedness was incurred to the extent the amount of the indebtedness resulting from such refinancing does not exceed the amount of the refinanced indebtedness.

(II) *LIMITATION ON PERIOD OF REFINANCING.*—Subclause (I) shall not apply to any indebtedness after the expiration of the term of the original indebtedness or, if the principal of such original indebtedness is not amortized over its term, the expiration of the term of the 1st refinancing of such indebtedness (or if earlier, the date which is 30 years after the date of such 1st refinancing).

(D) *TREATMENT OF INDEBTEDNESS INCURRED ON OR BEFORE OCTOBER 13, 1987.*—

(i) *IN GENERAL.*—In the case of any pre-October 13, 1987, indebtedness—

(I) such indebtedness shall be treated as acquisition indebtedness, and

(II) the limitation of subparagraph (B)(ii) shall not apply.

[(ii) *REDUCTION IN \$1,000,000 LIMITATION.*—The limitation of subparagraph (B)(ii) shall be reduced (but not below zero) by the aggregate amount of outstanding pre-October 13, 1987, indebtedness.

[(iii) *(ii) PRE-OCTOBER 13, 1987, INDEBTEDNESS.*—The term “pre-October 13, 1987, indebtedness” means—

(I) any indebtedness which was incurred on or before October 13, 1987, and which was secured by a qualified residence on October 13, 1987, and at all times thereafter before the interest is paid or accrued, or

(II) any indebtedness which is secured by the qualified residence and was incurred after October 13, 1987, to refinance indebtedness described in subclause (I) (or refinanced indebtedness meeting the requirements of this subclause) to the extent (immediately after the refinancing) the principal amount of the indebtedness resulting from the refinancing does not exceed the principal amount of the refinanced indebtedness (immediately before the refinancing).

[(iv) *(iii) LIMITATION ON PERIOD OF REFINANCING.*—Subclause (II) of [clause (iii)] *clause (ii)* shall not apply to any indebtedness after—

(I) the expiration of the term of the indebtedness described in [clause (iii)(I)] *clause (ii)(I)*, or

(II) if the principal of the indebtedness described in [clause (iii)(I)] *clause (ii)(I)* is not amortized over its term, the expiration of the term of the 1st refinancing of such indebtedness (or if earlier, the date which is 30 years after the date of such 1st refinancing).

(E) *MORTGAGE INSURANCE PREMIUMS TREATED AS INTEREST.*—



(i) **IN GENERAL.**—Premiums paid or accrued for qualified mortgage insurance by a taxpayer during the taxable year in connection with acquisition indebtedness with respect to a qualified residence of the taxpayer shall be treated for purposes of this section as interest which is qualified residence interest.

(ii) **PHASEOUT.**—The amount otherwise treated as interest under clause (i) shall be reduced (but not below zero) by 10 percent of such amount for each \$1,000 (\$500 in the case of a married individual filing a separate return) (or fraction thereof) that the taxpayer's adjusted gross income for the taxable year exceeds \$100,000 (\$50,000 in the case of a married individual filing a separate return).

(iii) **LIMITATION.**—Clause (i) shall not apply with respect to any mortgage insurance contracts issued before January 1, 2007.

(iv) **TERMINATION.**—Clause (i) shall not apply to amounts—

(I) paid or accrued after December 31, 2017, or

(II) properly allocable to any period after such date.

**[(F) SPECIAL RULES FOR TAXABLE YEARS 2018 THROUGH 2025.—**

**[(i) IN GENERAL.—**In the case of taxable years beginning after December 31, 2017, and before January 1, 2026—

**[(I) DISALLOWANCE OF HOME EQUITY INDEBTEDNESS INTEREST.—**Subparagraph (A)(ii) shall not apply.

**[(II) LIMITATION ON ACQUISITION INDEBTEDNESS.—**Subparagraph (B)(ii) shall be applied by substituting “\$750,000 (\$375,000” for “\$1,000,000 (\$500,000”.

**[(III) Treatment of indebtedness incurred on or before December 15, 2017—**Subclause (II) shall not apply to any indebtedness incurred on or before December 15, 2017, and, in applying such subclause to any indebtedness incurred after such date, the limitation under such subclause shall be reduced (but not below zero) by the amount of any indebtedness incurred on or before December 15, 2017, which is treated as acquisition indebtedness for purposes of this subsection for the taxable year.

**[(IV) BINDING CONTRACT EXCEPTION.—**In the case of a taxpayer who enters into a written binding contract before December 15, 2017, to close on the purchase of a principal residence before January 1, 2018, and who purchases such residence before April 1, 2018, subclause (III) shall be applied by substituting “April 1, 2018” for “December 15, 2017”.

**[(ii) TREATMENT OF LIMITATION IN TAXABLE YEARS AFTER DECEMBER 31, 2025.—**In the case of taxable

years beginning after December 31, 2025, the limitation under subparagraph (B)(ii) shall be applied to the aggregate amount of indebtedness of the taxpayer described in subparagraph (B)(i) without regard to the taxable year in which the indebtedness was incurred.

[(iii) TREATMENT OF REFINANCINGS OF INDEBTEDNESS.—

[(I) IN GENERAL.—In the case of any indebtedness which is incurred to refinance indebtedness, such refinanced indebtedness shall be treated for purposes of clause (i)(III) as incurred on the date that the original indebtedness was incurred to the extent the amount of the indebtedness resulting from such refinancing does not exceed the amount of the refinanced indebtedness.

[(II) LIMITATION ON PERIOD OF REFINANCING.—Subclause (I) shall not apply to any indebtedness after the expiration of the term of the original indebtedness or, if the principal of such original indebtedness is not amortized over its term, the expiration of the term of the 1st refinancing of such indebtedness (or if earlier, the date which is 30 years after the date of such 1st refinancing).

[(iv) COORDINATION WITH EXCLUSION OF INCOME FROM DISCHARGE OF INDEBTEDNESS.—Section 108(h)(2) shall be applied without regard to this subparagraph.】

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

(A) QUALIFIED RESIDENCE.—

(i) IN GENERAL.—The term “qualified residence” means—

(I) the principal residence (within the meaning of section 121) of the taxpayer, and

(II) 1 other residence of the taxpayer which is selected by the taxpayer for purposes of this subsection for the taxable year and which is used by the taxpayer as a residence (within the meaning of section 280A(d)(1)).

(ii) MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—If a married couple does not file a joint return for the taxable year—

(I) such couple shall be treated as 1 taxpayer for purposes of clause (i), and

(II) each individual shall be entitled to take into account 1 residence unless both individuals consent in writing to 1 individual taking into account the principal residence and 1 other residence.

(iii) RESIDENCE NOT RENTED.—For purposes of clause (i)(II), notwithstanding section 280A(d)(1), if the taxpayer does not rent a dwelling unit at any time during a taxable year, such unit may be treated as a residence for such taxable year.

(B) SPECIAL RULE FOR COOPERATIVE HOUSING CORPORATIONS.—Any indebtedness secured by stock held by the taxpayer as a tenant-stockholder (as defined in section

216) in a cooperative housing corporation (as so defined) shall be treated as secured by the house or apartment which the taxpayer is entitled to occupy as such a tenant-stockholder. If stock described in the preceding sentence may not be used to secure indebtedness, indebtedness shall be treated as so secured if the taxpayer establishes to the satisfaction of the Secretary that such indebtedness was incurred to acquire such stock.

(C) UNENFORCEABLE SECURITY INTERESTS.—Indebtedness shall not fail to be treated as secured by any property solely because, under any applicable State or local homestead or other debtor protection law in effect on August 16, 1986, the security interest is ineffective or the enforceability of the security interest is restricted.

(D) SPECIAL RULES FOR ESTATES AND TRUSTS.—For purposes of determining whether any interest paid or accrued by an estate or trust is qualified residence interest, any residence held by such estate or trust shall be treated as a qualified residence of such estate or trust if such estate or trust establishes that such residence is a qualified residence of a beneficiary who has a present interest in such estate or trust or an interest in the residuary of such estate or trust.

(E) QUALIFIED MORTGAGE INSURANCE.—The term “qualified mortgage insurance” means—

(i) mortgage insurance provided by the Department of Veterans Affairs, the Federal Housing Administration, or the Rural Housing Service, and

(ii) private mortgage insurance (as defined by section 2 of the Homeowners Protection Act of 1998 (12 U.S.C. 4901), as in effect on the date of the enactment of this subparagraph).

(F) SPECIAL RULES FOR PREPAID QUALIFIED MORTGAGE INSURANCE.—Any amount paid by the taxpayer for qualified mortgage insurance that is properly allocable to any mortgage the payment of which extends to periods that are after the close of the taxable year in which such amount is paid shall be chargeable to capital account and shall be treated as paid in such periods to which so allocated. No deduction shall be allowed for the unamortized balance of such account if such mortgage is satisfied before the end of its term. The preceding sentences shall not apply to amounts paid for qualified mortgage insurance provided by the Department of Veterans Affairs or the Rural Housing Service.

(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 (i) 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, or (ii) permit, on a temporary basis, a rate to be used with respect to any debt instrument which is higher than the applicable Federal rate if the Secretary determines that such rate is appropriate in light of distressed conditions in the debt capital markets.

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

Except for purposes of paragraph (1)(B), any reference to an obligation in subparagraph (B) of this paragraph shall be treated as including a reference to 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 instru-

ments, 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.

(j) LIMITATION ON BUSINESS INTEREST.—

(1) IN GENERAL.—The amount allowed as a deduction under this chapter for any taxable year for business interest shall not exceed the sum of—

(A) the business interest income of such taxpayer for such taxable year,

(B) 30 percent of the adjusted taxable income of such taxpayer for such taxable year, plus

(C) the floor plan financing interest of such taxpayer for such taxable year.

The amount determined under subparagraph (B) shall not be less than zero.

(2) CARRYFORWARD OF DISALLOWED BUSINESS INTEREST.—The amount of any business interest not allowed as a deduction for any taxable year by reason of paragraph (1) shall be treated as business interest paid or accrued in the succeeding taxable year.

(3) EXEMPTION FOR CERTAIN SMALL BUSINESSES.—In the case of any taxpayer (other than a tax shelter prohibited from using the cash receipts and disbursements method of accounting under section 448(a)(3)) which meets the gross receipts test of section 448(c) for any taxable year, paragraph (1) shall not apply to such taxpayer for such taxable year. In the case of any taxpayer which is not a corporation or a partnership, the gross receipts test of section 448(c) shall be applied in the same manner as if such taxpayer were a corporation or partnership.

(4) APPLICATION TO PARTNERSHIPS, ETC.—

(A) IN GENERAL.—In the case of any partnership—

(i) this subsection shall be applied at the partnership level and any deduction for business interest shall be taken into account in determining the nonseparately stated taxable income or loss of the partnership, and

(ii) the adjusted taxable income of each partner of such partnership—

(I) shall be determined without regard to such partner's distributive share of any items of income, gain, deduction, or loss of such partnership, and

(II) shall be increased by such partner's distributive share of such partnership's excess taxable income.

For purposes of clause (ii)(II), a partner's distributive share of partnership excess taxable income shall be determined in the same manner as the partner's distributive share of nonseparately stated taxable income or loss of the partnership.

## (B) SPECIAL RULES FOR CARRYFORWARDS.—

(i) IN GENERAL.—The amount of any business interest not allowed as a deduction to a partnership for any taxable year by reason of paragraph (1) for any taxable year—

(I) shall not be treated under paragraph (2) as business interest paid or accrued by the partnership in the succeeding taxable year, and

(II) shall, subject to clause (ii), be treated as excess business interest which is allocated to each partner in the same manner as the non-separately stated taxable income or loss of the partnership.

(ii) TREATMENT OF EXCESS BUSINESS INTEREST ALLOCATED TO PARTNERS.—If a partner is allocated any excess business interest from a partnership under clause (i) for any taxable year—

(I) such excess business interest shall be treated as business interest paid or accrued by the partner in the next succeeding taxable year in which the partner is allocated excess taxable income from such partnership, but only to the extent of such excess taxable income, and

(II) any portion of such excess business interest remaining after the application of subclause (I) shall, subject to the limitations of subclause (I), be treated as business interest paid or accrued in succeeding taxable years.

For purposes of applying this paragraph, excess taxable income allocated to a partner from a partnership for any taxable year shall not be taken into account under paragraph (1)(A) with respect to any business interest other than excess business interest from the partnership until all such excess business interest for such taxable year and all preceding taxable years has been treated as paid or accrued under clause (ii).

(iii) BASIS ADJUSTMENTS.—

(I) IN GENERAL.—The adjusted basis of a partner in a partnership interest shall be reduced (but not below zero) by the amount of excess business interest allocated to the partner under clause (i)(II).

(II) SPECIAL RULE FOR DISPOSITIONS.—If a partner disposes of a partnership interest, the adjusted basis of the partner in the partnership interest shall be increased immediately before the disposition by the amount of the excess (if any) of the amount of the basis reduction under subclause (I) over the portion of any excess business interest allocated to the partner under clause (i)(II) which has previously been treated under clause (ii) as business interest paid or accrued by the partner. The preceding sentence shall also apply to transfers of the partnership interest (including by reason of death) in a transaction in which gain is not recognized in whole or in part. No deduction shall

be allowed to the transferor or transferee under this chapter for any excess business interest resulting in a basis increase under this subclause.

(C) EXCESS TAXABLE INCOME.—The term “excess taxable income” means, with respect to any partnership, the amount which bears the same ratio to the partnership’s adjusted taxable income as—

(i) the excess (if any) of—

(I) the amount determined for the partnership under paragraph (1)(B), over

(II) the amount (if any) by which the business interest of the partnership, reduced by the floor plan financing interest, exceeds the business interest income of the partnership, bears to

(ii) the amount determined for the partnership under paragraph (1)(B).

(D) APPLICATION TO S CORPORATIONS.—Rules similar to the rules of subparagraphs (A) and (C) shall apply with respect to any S corporation and its shareholders.

(5) BUSINESS INTEREST.—For purposes of this subsection, the term “business interest” means any interest paid or accrued on indebtedness properly allocable to a trade or business. Such term shall not include investment interest (within the meaning of subsection (d)).

(6) BUSINESS INTEREST INCOME.—For purposes of this subsection, the term “business interest income” means the amount of interest includible in the gross income of the taxpayer for the taxable year which is properly allocable to a trade or business. Such term shall not include investment income (within the meaning of subsection (d)).

(7) TRADE OR BUSINESS.—For purposes of this subsection—

(A) IN GENERAL.—The term “trade or business” shall not include—

(i) the trade or business of performing services as an employee,

(ii) any electing real property trade or business,

(iii) any electing farming business, or

(iv) the trade or business of the furnishing or sale of—

(I) electrical energy, water, or sewage disposal services,

(II) gas or steam through a local distribution system, or

(III) transportation of gas or steam by pipeline, if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, by a public service or public utility commission or other similar body of any State or political subdivision thereof, or by the governing or ratemaking body of an electric cooperative.

(B) ELECTING REAL PROPERTY TRADE OR BUSINESS.—For purposes of this paragraph, the term “electing real property trade or business” means any trade or business which

is described in section 469(c)(7)(C) and which makes an election under this subparagraph. Any such election shall be made at such time and in such manner as the Secretary shall prescribe, and, once made, shall be irrevocable.

(C) ELECTING FARMING BUSINESS.—For purposes of this paragraph, the term “electing farming business” means—

(i) a farming business (as defined in section 263A(e)(4)) which makes an election under this subparagraph, or

(ii) any trade or business of a specified agricultural or horticultural cooperative (as defined in section 199A(g)(2)) with respect to which the cooperative makes an election under this subparagraph.

Any such election shall be made at such time and in such manner as the Secretary shall prescribe, and, once made, shall be irrevocable.

(8) ADJUSTED TAXABLE INCOME.—For purposes of this subsection, the term “adjusted taxable income” means the taxable income of the taxpayer—

(A) computed without regard to—

(i) any item of income, gain, deduction, or loss which is not properly allocable to a trade or business,

(ii) any business interest or business interest income,

(iii) the amount of any net operating loss deduction under section 172,

(iv) the amount of any deduction allowed under section 199A, and

(v) in the case of taxable years beginning before January 1, 2022, any deduction allowable for depreciation, amortization, or depletion, and

(B) computed with such other adjustments as provided by the Secretary.

(9) FLOOR PLAN FINANCING INTEREST DEFINED.—For purposes of this subsection—

(A) IN GENERAL.—The term “floor plan financing interest” means interest paid or accrued on floor plan financing indebtedness.

(B) FLOOR PLAN FINANCING INDEBTEDNESS.—The term “floor plan financing indebtedness” means indebtedness—

(i) used to finance the acquisition of motor vehicles held for sale or lease, and

(ii) secured by the inventory so acquired.

(C) MOTOR VEHICLE.—The term “motor vehicle” means a motor vehicle that is any of the following:

(i) Any self-propelled vehicle designed for transporting persons or property on a public street, highway, or road.

(ii) A boat.

(iii) Farm machinery or equipment.

(10) CROSS REFERENCES.—

(A) For requirement that an electing real property trade or business use the alternative depreciation system, see section 168(g)(1)(F).



(B) For requirement that an electing farming business use the alternative depreciation system, see section 168(g)(1)(G).

(k) SECTION 6166 INTEREST.—No deduction shall be allowed under this section for any interest payable under section 6601 on any unpaid portion of the tax imposed by section 2001 for the period during which an extension of time for payment of such tax is in effect under section 6166.

(l) DISALLOWANCE OF DEDUCTION ON CERTAIN DEBT INSTRUMENTS OF CORPORATIONS.—

(1) IN GENERAL.—No deduction shall be allowed under this chapter for any interest paid or accrued on a disqualified debt instrument.

(2) DISQUALIFIED DEBT INSTRUMENT.—For purposes of this subsection, the term “disqualified debt instrument” means any indebtedness of a corporation which is payable in equity of the issuer or a related party or equity held by the issuer (or any related party) in any other person.

(3) SPECIAL RULES FOR AMOUNTS PAYABLE IN EQUITY.—For purposes of paragraph (2), indebtedness shall be treated as payable in equity of the issuer or any other person only if—

(A) a substantial amount of the principal or interest is required to be paid or converted, or at the option of the issuer or a related party is payable in, or convertible into, such equity,

(B) a substantial amount of the principal or interest is required to be determined, or at the option of the issuer or a related party is determined, by reference to the value of such equity, or

(C) the indebtedness is part of an arrangement which is reasonably expected to result in a transaction described in subparagraph (A) or (B).

For purposes of this paragraph, principal or interest shall be treated as required to be so paid, converted, or determined if it may be required at the option of the holder or a related party and there is a substantial certainty the option will be exercised.

(4) CAPITALIZATION ALLOWED WITH RESPECT TO EQUITY OF PERSONS OTHER THAN ISSUER AND RELATED PARTIES.—If the disqualified debt instrument of a corporation is payable in equity held by the issuer (or any related party) in any other person (other than a related party), the basis of such equity shall be increased by the amount not allowed as a deduction by reason of paragraph (1) with respect to the instrument.

(5) EXCEPTION FOR CERTAIN INSTRUMENTS ISSUED BY DEALERS IN SECURITIES.—For purposes of this subsection, the term “disqualified debt instrument” does not include indebtedness issued by a dealer in securities (or a related party) which is payable in, or by reference to, equity (other than equity of the issuer or a related party) held by such dealer in its capacity as a dealer in securities. For purposes of this paragraph, the term “dealer in securities” has the meaning given such term by section 475.

(6) RELATED PARTY.—For purposes of this subsection, a person is a related party with respect to another person if such

person bears a relationship to such other person described in section 267(b) or 707(b).

(7) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subsection, including regulations preventing avoidance of this subsection through the use of an issuer other than a corporation.

(m) INTEREST ON UNPAID TAXES ATTRIBUTABLE TO NONDISCLOSED REPORTABLE TRANSACTIONS.—No deduction shall be allowed under this chapter for any interest paid or accrued under section 6601 on any underpayment of tax which is attributable to the portion of any reportable transaction understatement (as defined in section 6662A(b)) with respect to which the requirement of section 6664(d)(2)(A) is not met.

(n) CROSS REFERENCES.—

(1) For disallowance of certain amounts paid in connection with insurance, endowment, or annuity contracts, see section 264.

(2) For disallowance of deduction for interest relating to tax-exempt income, see section 265(a)(2).

(3) For disallowance of deduction for carrying charges chargeable to capital account, see section 266.

(4) For disallowance of interest with respect to transactions between related taxpayers, see section 267.

(5) For treatment of redeemable ground rents and real property held subject to liabilities under redeemable ground rents, see section 1055.

#### **SEC. 164. TAXES.**

(a) GENERAL RULE.—Except as otherwise provided in this section, the following taxes shall be allowed as a deduction for the taxable year within which paid or accrued:

(1) State and local, and foreign, real property taxes.

(2) State and local personal property taxes.

(3) State and local, and foreign, income, war profits, and excess profits taxes.

(4) The GST tax imposed on income distributions.

In addition, there shall be allowed as a deduction State and local, and foreign, taxes not described in the preceding sentence which are paid or accrued within the taxable year in carrying on a trade or business or an activity described in section 212 (relating to expenses for production of income). Notwithstanding the preceding sentence, any tax (not described in the first sentence of this subsection) which is paid or accrued by the taxpayer in connection with an acquisition or disposition of property shall be treated as part of the cost of the acquired property or, in the case of a disposition, as a reduction in the amount realized on the disposition.

(b) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) PERSONAL PROPERTY TAXES.—The term “personal property tax” means an ad valorem tax which is imposed on an annual basis in respect of personal property.

(2) STATE OR LOCAL TAXES.—A State or local tax includes only a tax imposed by a State, a possession of the United States, or a political subdivision of any of the foregoing, or by the District of Columbia.

(3) FOREIGN TAXES.—A foreign tax includes only a tax imposed by the authority of a foreign country.

(4) SPECIAL RULES FOR GST TAX.—

(A) IN GENERAL.—The GST tax imposed on income distributions is—

(i) the tax imposed by section 2601, and

(ii) any State tax described in section 2604 (as in effect before its repeal),

but only to the extent such tax is imposed on a transfer which is included in the gross income of the distributee and to which section 666 does not apply.

(B) SPECIAL RULE FOR TAX PAID BEFORE DUE DATE.—Any tax referred to in subparagraph (A) imposed with respect to a transfer occurring during the taxable year of the distributee (or, in the case of a taxable termination, the trust) which is paid not later than the time prescribed by law (including extensions) for filing the return with respect to such transfer shall be treated as having been paid on the last day of the taxable year in which the transfer was made.

(5) GENERAL SALES TAXES.—For purposes of subsection (a)—

(A) ELECTION TO DEDUCT STATE AND LOCAL SALES TAXES IN LIEU OF STATE AND LOCAL INCOME TAXES.—At the election of the taxpayer for the taxable year, subsection (a) shall be applied—

(i) without regard to the reference to State and local income taxes, and

(ii) as if State and local general sales taxes were referred to in a paragraph thereof.

(B) DEFINITION OF GENERAL SALES TAX.—The term “general sales tax” means a tax imposed at one rate with respect to the sale at retail of a broad range of classes of items.

(C) SPECIAL RULES FOR FOOD, ETC.—In the case of items of food, clothing, medical supplies, and motor vehicles—

(i) the fact that the tax does not apply with respect to some or all of such items shall not be taken into account in determining whether the tax applies with respect to a broad range of classes of items, and

(ii) the fact that the rate of tax applicable with respect to some or all of such items is lower than the general rate of tax shall not be taken into account in determining whether the tax is imposed at one rate.

(D) ITEMS TAXED AT DIFFERENT RATES.—Except in the case of a lower rate of tax applicable with respect to an item described in subparagraph (C), no deduction shall be allowed under this paragraph for any general sales tax imposed with respect to an item at a rate other than the general rate of tax.

(E) COMPENSATING USE TAXES.—A compensating use tax with respect to an item shall be treated as a general sales tax. For purposes of the preceding sentence, the term “compensating use tax” means, with respect to any item, a tax which—

(i) is imposed on the use, storage, or consumption of such item, and

(ii) is complementary to a general sales tax, but only if a deduction is allowable under this paragraph with respect to items sold at retail in the taxing jurisdiction which are similar to such item.

(F) SPECIAL RULE FOR MOTOR VEHICLES.—In the case of motor vehicles, if the rate of tax exceeds the general rate, such excess shall be disregarded and the general rate shall be treated as the rate of tax.

(G) SEPARATELY STATED GENERAL SALES TAXES.—If the amount of any general sales tax is separately stated, then, to the extent that the amount so stated is paid by the consumer (other than in connection with the consumer's trade or business) to the seller, such amount shall be treated as a tax imposed on, and paid by, such consumer.

(H) AMOUNT OF DEDUCTION MAY BE DETERMINED UNDER TABLES.—

(i) IN GENERAL.—At the election of the taxpayer for the taxable year, the amount of the deduction allowed under this paragraph for such year shall be—

(I) the amount determined under this paragraph (without regard to this subparagraph) with respect to motor vehicles, boats, and other items specified by the Secretary, and

(II) the amount determined under tables prescribed by the Secretary with respect to items to which subclause (I) does not apply.

(ii) REQUIREMENTS FOR TABLES.—The tables prescribed under clause (i)—

(I) shall reflect the provisions of this paragraph,

(II) shall be based on the average consumption by taxpayers on a State-by-State basis (as determined by the Secretary) of items to which clause (i)(I) does not apply, taking into account filing status, number of dependents, adjusted gross income, and rates of State and local general sales taxation, and

(III) need only be determined with respect to adjusted gross incomes up to the applicable amount **[(as determined under section 68(b))]**.

(iii) APPLICABLE AMOUNT DEFINED.—For purposes of clause (ii), the term “applicable amount” means—

(I) \$300,000 in the case of a joint return or a surviving spouse,

(II) \$275,000 in the case of a head of household,

(III) \$250,000 in the case of an individual who is not married and who is not a surviving spouse or head of household, and

(IV) 1/2 the amount applicable under subclause (I) in the case of a married individual filing a separate return.

For purposes of this paragraph, marital status shall be determined under section 7703. In the case of any taxable year beginning in calendar years after 2017, each

*of the dollar amounts in this clause shall be increased by an amount equal to such dollar amount, multiplied by the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “2012” for “2016” in subparagraph (A)(ii) thereof. If any amount after adjustment under the preceding sentence is not a multiple of \$50, such amount shall be rounded to the next lowest multiple of \$50.*

**[(6) LIMITATION ON INDIVIDUAL DEDUCTIONS FOR TAXABLE YEARS 2018 THROUGH 2025.—**In the case of an individual and a taxable year beginning after December 31, 2017, and before January 1, 2026—

**[(A) foreign real property taxes shall not be taken into account under subsection (a)(1), and**

**[(B) the aggregate amount of taxes taken into account under paragraphs (1), (2), and (3) of subsection (a) and paragraph (5) of this subsection for any taxable year shall not exceed \$10,000 (\$5,000 in the case of a married individual filing a separate return).]**

**(6) LIMITATION ON INDIVIDUAL DEDUCTIONS.—***In the case of an individual—*

*(A) no deduction shall be allowed under this chapter for foreign real property taxes paid or accrued during the taxable year, and*

*(B) the aggregate amount of the deduction allowed under this chapter for taxes described in paragraphs (1), (2), and (3) of subsection (a) and paragraph (5) of this subsection paid or accrued by the taxpayer during the taxable year shall not exceed \$10,000 (\$5,000 in the case of a married individual filing a separate return).*

The preceding sentence shall not apply to any foreign taxes described in subsection (a)(3) or to any taxes described in paragraph (1) and (2) of subsection (a) which are paid or accrued in carrying on a trade or business or an activity described in section 212. For purposes of subparagraph (B), an amount paid in a taxable year beginning before January 1, 2018, with respect to a State or local income tax imposed for a taxable year beginning after December 31, 2017, shall be treated as paid on the last day of the taxable year for which such tax is so imposed.

**(c) DEDUCTION DENIED IN CASE OF CERTAIN TAXES.—**No deduction shall be allowed for the following taxes:

(1) Taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not prevent the deduction of so much of such taxes as is properly allocable to maintenance or interest charges.

(2) Taxes on real property, to the extent that subsection (d) requires such taxes to be treated as imposed on another taxpayer.

**(d) APPORTIONMENT OF TAXES ON REAL PROPERTY BETWEEN SELLER AND PURCHASER.—**

(1) **GENERAL RULE.—**For purposes of subsection (a), if real property is sold during any real property tax year, then—

(A) so much of the real property tax as is properly allocable to that part of such year which ends on the day before the date of the sale shall be treated as a tax imposed on the seller, and

(B) so much of such tax as is properly allocable to that part of such year which begins on the date of the sale shall be treated as a tax imposed on the purchaser.

(2) SPECIAL RULES.—

(A) in the case of any sale of real property, if—

(i) a taxpayer may not, by reason of his method of accounting, deduct any amount for taxes unless paid, and

(ii) the other party to the sale is (under the law imposing the real property tax) liable for the real property tax for the real property tax year,

then for purposes of subsection (a) the taxpayer shall be treated as having paid, on the date of the sale, so much of such tax as, under paragraph (1) of this subsection, is treated as imposed on the taxpayer. For purposes of the preceding sentence, if neither party is liable for the tax, then the party holding the property at the time the tax becomes a lien on the property shall be considered liable for the real property tax for the real property tax year.

(B) In the case of any sale of real property, if the taxpayer's taxable income for the taxable year during which the sale occurs is computed under an accrual method of accounting, and if no election under section 461(c) (relating to the accrual of real property taxes) applies, then, for purposes of subsection (a), that portion of such tax which—

(i) is treated, under paragraph (1) of this subsection, as imposed on the taxpayer, and

(ii) may not, by reason of the taxpayer's method of accounting, be deducted by the taxpayer for any taxable year,

shall be treated as having accrued on the date of the sale.

(e) TAXES OF SHAREHOLDER PAID BY CORPORATION.—Where a corporation pays a tax imposed on a shareholder on his interest as a shareholder, and where the shareholder does not reimburse the corporation, then—

(1) the deduction allowed by subsection (a) shall be allowed to the corporation; and

(2) no deduction shall be allowed the shareholder for such tax.

(f) DEDUCTION FOR ONE-HALF OF SELF-EMPLOYMENT TAXES.—

(1) IN GENERAL.—In the case of an individual, in addition to the taxes described in subsection (a), there shall be allowed as a deduction for the taxable year an amount equal to one-half of the taxes imposed by section 1401 (other than the taxes imposed by section 1401(b)(2)) for such taxable year.

(2) DEDUCTION TREATED AS ATTRIBUTABLE TO TRADE OR BUSINESS.—For purposes of this chapter, the deduction allowed by paragraph (1) shall be treated as attributable to a trade or business carried on by the taxpayer which does not consist of the performance of services by the taxpayer as an employee.

(g) CROSS REFERENCES.—

(1) For provisions disallowing any deduction for certain taxes, see section 275.

(2) For treatment of taxes imposed by Indian tribal governments (or their subdivisions), see section 7871.

**SEC. 165. LOSSES.**

(a) **GENERAL RULE.**—There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.

(b) **AMOUNT OF DEDUCTION.**—For purposes of subsection (a), the basis for determining the amount of the deduction for any loss shall be the adjusted basis provided in section 1011 for determining the loss from the sale or other disposition of property.

(c) **LIMITATION ON LOSSES OF INDIVIDUALS.**—In the case of an individual, the deduction under subsection (a) shall be limited to—

(1) losses incurred in a trade or business;

(2) losses incurred in any transaction entered into for profit, though not connected with a trade or business; and

(3) except as provided in subsection (h), losses of property not connected with a trade or business or a transaction entered into for profit, if such losses arise from fire, storm, shipwreck, or other casualty, or from theft.

(d) **WAGERING LOSSES.**—Losses from wagering transactions shall be allowed only to the extent of the gains from such transactions. For purposes of the preceding sentence, [in the case of taxable years beginning after December 31, 2017, and before January 1, 2026,] the term “losses from wagering transactions” includes any deduction otherwise allowable under this chapter incurred in carrying on any wagering transaction.

(e) **THEFT LOSSES.**—For purposes of subsection (a), any loss arising from theft shall be treated as sustained during the taxable year in which the taxpayer discovers such loss.

(f) **CAPITAL LOSSES.**—Losses from sales or exchanges of capital assets shall be allowed only to the extent allowed in sections 1211 and 1212.

(g) **WORTHLESS SECURITIES.**—

(1) **GENERAL RULE.**—If any security which is a capital asset becomes worthless during the taxable year, the loss resulting therefrom shall, for purposes of this subtitle, be treated as a loss from the sale or exchange, on the last day of the taxable year, of a capital asset.

(2) **SECURITY DEFINED.**—For purposes of this subsection, the term “security” means—

(A) a share of stock in a corporation;

(B) a right to subscribe for, or to receive, a share of stock in a corporation; or

(C) a bond, debenture, note, or certificate, or other evidence of indebtedness, issued by a corporation or by a government or political subdivision thereof, with interest coupons or in registered form.

(3) **SECURITIES IN AFFILIATED CORPORATION.**—For purposes of paragraph (1), any security in a corporation affiliated with a taxpayer which is a domestic corporation shall not be treated as a capital asset. For purposes of the preceding sentence, a corporation shall be treated as affiliated with the taxpayer only if—

(A) the taxpayer owns directly stock in such corporation meeting the requirements of section 1504(a)(2), and

(B) more than 90 percent of the aggregate of its gross receipts for all taxable years has been from sources other than royalties, rents (except rents derived from rental of properties to employees of the corporation in the ordinary course of its operating business), dividends, interest (except interest received on deferred purchase price of operating assets sold), annuities, and gains from sales or exchanges of stocks and securities.

In computing gross receipts for purposes of the preceding sentence, gross receipts from sales or exchanges of stocks and securities shall be taken into account only to the extent of gains therefrom.

(h) TREATMENT OF CASUALTY GAINS AND LOSSES.—

(1) DOLLAR LIMITATION PER CASUALTY.—Any loss of an individual described in subsection (c)(3) shall be allowed only to the extent that the amount of the loss to such individual arising from each casualty, or from each theft, exceeds \$500 (\$100 for taxable years beginning after December 31, 2009).

(2) NET CASUALTY LOSS ALLOWED ONLY TO THE EXTENT IT EXCEEDS 10 PERCENT OF ADJUSTED GROSS INCOME.—

(A) IN GENERAL.—If the personal casualty losses for any taxable year exceed the personal casualty gains for such taxable year, such losses shall be allowed for the taxable year only to the extent of the sum of—

(i) the amount of the personal casualty gains for the taxable year, plus

(ii) so much of such excess as exceeds 10 percent of the adjusted gross income of the individual.

(B) SPECIAL RULE WHERE PERSONAL CASUALTY GAINS EXCEED PERSONAL CASUALTY LOSSES.—If the personal casualty gains for any taxable year exceed the personal casualty losses for such taxable year—

(i) all such gains shall be treated as gains from sales or exchanges of capital assets, and

(ii) all such losses shall be treated as losses from sales or exchanges of capital assets.

(3) DEFINITIONS OF PERSONAL CASUALTY GAIN AND PERSONAL CASUALTY LOSS.—For purposes of this subsection—

(A) PERSONAL CASUALTY GAIN.—The term “personal casualty gain” means the recognized gain from any involuntary conversion of property which is described in subsection (c)(3) arising from fire, storm, shipwreck, or other casualty, or from theft.

(B) PERSONAL CASUALTY LOSS.—The term “personal casualty loss” means any loss described in subsection (c)(3). For purposes of paragraph (2), the amount of any personal casualty loss shall be determined after the application of paragraph (1).

(4) SPECIAL RULES.—

(A) PERSONAL CASUALTY LOSSES ALLOWABLE IN COMPUTING ADJUSTED GROSS INCOME TO THE EXTENT OF PERSONAL CASUALTY GAINS.—In any case to which paragraph (2)(A) applies, the deduction for personal casualty losses



for any taxable year shall be treated as a deduction allowable in computing adjusted gross income to the extent such losses do not exceed the personal casualty gains for the taxable year.

(B) JOINT RETURNS.—For purposes of this subsection, a husband and wife making a joint return for the taxable year shall be treated as 1 individual.

(C) DETERMINATION OF ADJUSTED GROSS INCOME IN CASE OF ESTATES AND TRUSTS.—For purposes of paragraph (2), the adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual, except that the deductions for costs paid or incurred in connection with the administration of the estate or trust shall be treated as allowable in arriving at adjusted gross income.

(D) COORDINATION WITH ESTATE TAX.—No loss described in subsection (c)(3) shall be allowed if, at the time of filing the return, such loss has been claimed for estate tax purposes in the estate tax return.

(E) CLAIM REQUIRED TO BE FILED IN CERTAIN CASES.—Any loss of an individual described in subsection (c)(3) to the extent covered by insurance shall be taken into account under this section only if the individual files a timely insurance claim with respect to such loss.

**(5) LIMITATION [FOR TAXABLE YEARS 2018 THROUGH 2025] TO LOSSES ATTRIBUTABLE TO FEDERALLY DECLARED DISASTERS.—**

(A) IN GENERAL.—In the case of an individual, except as provided in subparagraph (B), any personal casualty loss which (but for this paragraph) would be deductible [in a taxable year beginning after December 31, 2017, and before January 1, 2026,] shall be allowed as a deduction under subsection (a) only to the extent it is attributable to a Federally declared disaster (as defined in subsection (i)(5)).

(B) EXCEPTION RELATED TO PERSONAL CASUALTY GAINS.—If a taxpayer has personal casualty gains [for any taxable year to which subparagraph (A) applies]—

(i) subparagraph (A) shall not apply to the portion of the personal casualty loss not attributable to a Federally declared disaster (as so defined) to the extent such loss does not exceed such gains, and

(ii) in applying paragraph (2) for purposes of subparagraph (A) to the portion of personal casualty loss which is so attributable to such a disaster, the amount of personal casualty gains taken into account under paragraph (2)(A) shall be reduced by the portion of such gains taken into account under clause (i).

**(i) DISASTER LOSSES.—**

(1) ELECTION TO TAKE DEDUCTION FOR PRECEDING YEAR.—Notwithstanding the provisions of subsection (a), any loss occurring in a disaster area and attributable to a federally declared disaster may, at the election of the taxpayer, be taken into account for the taxable year immediately preceding the taxable year in which the disaster occurred.

(2) YEAR OF LOSS.—If an election is made under this subsection, the casualty resulting in the loss shall be treated for purposes of this title as having occurred in the taxable year for which the deduction is claimed.

(3) AMOUNT OF LOSS.—The amount of the loss taken into account in the preceding taxable year by reason of paragraph (1) shall not exceed the uncompensated amount determined on the basis of the facts existing at the date the taxpayer claims the loss.

(4) USE OF DISASTER LOAN APPRAISALS TO ESTABLISH AMOUNT OF LOSS.—Nothing in this title shall be construed to prohibit the Secretary from prescribing regulations or other guidance under which an appraisal for the purpose of obtaining a loan of Federal funds or a loan guarantee from the Federal Government as a result of a federally declared disaster may be used to establish the amount of any loss described in paragraph (1) or (2).

(5) FEDERALLY DECLARED DISASTERS.—For purposes of this subsection—

(A) IN GENERAL.—The term “Federally declared disaster” means any disaster subsequently determined by the President of the United States to warrant assistance by the Federal Government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act.

(B) DISASTER AREA.—The term “disaster area” means the area so determined to warrant such assistance.

(j) DENIAL OF DEDUCTION FOR LOSSES ON CERTAIN OBLIGATIONS NOT IN REGISTERED FORM.—

(1) IN GENERAL.—Nothing in subsection (a) or in any other provision of law shall be construed to provide a deduction for any loss sustained on any registration-required obligation unless such obligation is in registered form (or the issuance of such obligation was subject to tax under section 4701).

(2) DEFINITIONS.—For purposes of this subsection—

(A) REGISTRATION-REQUIRED OBLIGATION.—The term “registration-required obligation” has the meaning given to such term by section 163(f)(2).

(B) REGISTERED FORM.—The term “registered form” has the same meaning as when used in section 163(f).

(3) EXCEPTIONS.—The Secretary may, by regulations, provide that this subsection and section 1287 shall not apply with respect to obligations held by any person if—

(A) such person holds such obligations in connection with a trade or business outside the United States,

(B) such person holds such obligations as a broker dealer (registered under Federal or State law) for sale to customers in the ordinary course of his trade or business,

(C) such person complies with reporting requirements with respect to ownership, transfers, and payments as the Secretary may require, or

(D) such person promptly surrenders the obligation to the issuer for the issuance of a new obligation in registered form,

but only if such obligations are held under arrangements provided in regulations or otherwise which are designed to assure

that such obligations are not delivered to any United States person other than a person described in subparagraph (A), (B), or (C).

(k) TREATMENT AS DISASTER LOSS WHERE TAXPAYER ORDERED TO DEMOLISH OR RELOCATE RESIDENCE IN DISASTER AREA BECAUSE OF DISASTER.—In the case of a taxpayer whose residence is located in an area which has been determined by the President of the United States to warrant assistance by the Federal Government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act, if—

(1) not later than the 120th day after the date of such determination, the taxpayer is ordered, by the government of the State or any political subdivision thereof in which such residence is located, to demolish or relocate such residence, and

(2) the residence has been rendered unsafe for use as a residence by reason of the disaster,  
any loss attributable to such disaster shall be treated as a loss which arises from a casualty and which is described in subsection (i).

(l) TREATMENT OF CERTAIN LOSSES IN INSOLVENT FINANCIAL INSTITUTIONS.—

(1) IN GENERAL.—If—

(A) as of the close of the taxable year, it can reasonably be estimated that there is a loss on a qualified individual's deposit in a qualified financial institution, and

(B) such loss is on account of the bankruptcy or insolvency of such institution,

then the taxpayer may elect to treat the amount so estimated as a loss described in subsection (c)(3) incurred during the taxable year.

(2) QUALIFIED INDIVIDUAL DEFINED.—For purposes of this subsection, the term “qualified individual” means any individual, except an individual—

(A) who owns at least 1 percent in value of the outstanding stock of the qualified financial institution,

(B) who is an officer of the qualified financial institution,

(C) who is a sibling (whether by the whole or half blood), spouse, aunt, uncle, nephew, niece, ancestor, or lineal descendant of an individual described in subparagraph (A) or (B), or

(D) who otherwise is a related person (as defined in section 267(b)) with respect to an individual described in subparagraph (A) or (B).

(3) QUALIFIED FINANCIAL INSTITUTION.—For purposes of this subsection, the term “qualified financial institution” means—

(A) any bank (as defined in section 581),

(B) any institution described in section 591,

(C) any credit union the deposits or accounts in which are insured under Federal or State law or are protected or guaranteed under State law, or

(D) any similar institution chartered and supervised under Federal or State law.

(4) DEPOSIT.—For purposes of this subsection, the term “deposit” means any deposit, withdrawable account, or withdrawable or repurchasable share.

## (5) ELECTION TO TREAT AS ORDINARY LOSS.—

(A) IN GENERAL.—In lieu of any election under paragraph (1), the taxpayer may elect to treat the amount referred to in paragraph (1) for the taxable year as an ordinary loss described in subsection (c)(2) incurred during the taxable year.

## (B) LIMITATIONS.—

(i) DEPOSIT MAY NOT BE FEDERALLY INSURED.—No election may be made under subparagraph (A) with respect to any loss on a deposit in a qualified financial institution if part or all of such deposit is insured under Federal law.

(ii) DOLLAR LIMITATION.—With respect to each financial institution, the aggregate amount of losses attributable to deposits in such financial institution to which an election under subparagraph (A) may be made by the taxpayer for any taxable year shall not exceed \$20,000 (\$10,000 in the case of a separate return by a married individual). The limitation of the preceding sentence shall be reduced by the amount of any insurance proceeds under any State law which can reasonably be expected to be received with respect to losses on deposits in such institution.

## (6) ELECTION.—Any election by the taxpayer under this subsection for any taxable year—

(A) shall apply to all losses for such taxable year of the taxpayer on deposits in the institution with respect to which such election was made, and

(B) may be revoked only with the consent of the Secretary.

## (7) COORDINATION WITH SECTION 166.—Section 166 shall not apply to any loss to which an election under this subsection applies.

## (m) CROSS REFERENCES.—

(1) For special rule for banks with respect to worthless securities, see section 582.

(2) For disallowance of deduction for worthlessness of securities to which subsection (g)(2)(C) applies, if issued by a political party or similar organization, see section 271.

(3) For special rule for losses on stock in a small business investment company, see section 1242.

(4) For special rule for losses of a small business investment company, see section 1243.

(5) For special rule for losses on small business stock, see section 1244.

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**SEC. 170. CHARITABLE, ETC., CONTRIBUTIONS AND GIFTS.**

## (a) ALLOWANCE OF DEDUCTION.—

(1) GENERAL RULE.—There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year. A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary.

(2) CORPORATIONS ON ACCRUAL BASIS.—In the case of a corporation reporting its taxable income on the accrual basis, if—

(A) the board of directors authorizes a charitable contribution during any taxable year, and

(B) payment of such contribution is made after the close of such taxable year and on or before the 15th day of the fourth month following the close of such taxable year, then the taxpayer may elect to treat such contribution as paid during such taxable year. The election may be made only at the time of the filing of the return for such taxable year, and shall be signified in such manner as the Secretary shall by regulations prescribe.

(3) FUTURE INTERESTS IN TANGIBLE PERSONAL PROPERTY.—For purposes of this section, payment of a charitable contribution which consists of a future interest in tangible personal property shall be treated as made only when all intervening interests in, and rights to the actual possession or enjoyment of, the property have expired or are held by persons other than the taxpayer or those standing in a relationship to the taxpayer described in section 267(b) or 707(b). For purposes of the preceding sentence, a fixture which is intended to be severed from the real property shall be treated as tangible personal property.

(b) PERCENTAGE LIMITATIONS.—

(1) INDIVIDUALS.—In the case of an individual, the deduction provided in subsection (a) shall be limited as provided in the succeeding subparagraphs.

(A) GENERAL RULE.—**[Any charitable contribution]** *Any charitable contribution other than a contribution described in subparagraph (G) to—*

(i) a church or a convention or association of churches,

(ii) an educational organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on,

(iii) an organization the principal purpose or functions of which are the providing of medical or hospital care or medical education or medical research, if the organization is a hospital, or if the organization is a medical research organization directly engaged in the continuous active conduct of medical research in conjunction with a hospital, and during the calendar year in which the contribution is made such organization is committed to spend such contributions for such research before January 1 of the fifth calendar year which begins after the date such contribution is made,

(iv) an organization which normally receives a substantial part of its support (exclusive of income received in the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501(a)) from the United States or any State or political subdivision thereof or from direct or

indirect contributions from the general public, and which is organized and operated exclusively to receive, hold, invest, and administer property and to make expenditures to or for the benefit of a college or university which is an organization referred to in clause (ii) of this subparagraph and which is an agency or instrumentality of a State or political subdivision thereof, or which is owned or operated by a State or political subdivision thereof or by an agency or instrumentality of one or more States or political subdivisions,

(v) a governmental unit referred to in subsection (c)(1),

(vi) an organization referred to in subsection (c)(2) which normally receives a substantial part of its support (exclusive of income received in the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501(a)) from a governmental unit referred to in subsection (c)(1) or from direct or indirect contributions from the general public,

(vii) a private foundation described in subparagraph (F),

(viii) an organization described in section 509(a)(2) or (3), or

(ix) an agricultural research organization directly engaged in the continuous active conduct of agricultural research (as defined in section 1404 of the National Agricultural Research, Extension, and Teaching Policy Act of 1977) in conjunction with a land-grant college or university (as defined in such section) or a non-land grant college of agriculture (as defined in such section), and during the calendar year in which the contribution is made such organization is committed to spend such contribution for such research before January 1 of the fifth calendar year which begins after the date such contribution is made,

shall be allowed to the extent that the aggregate of such contributions does not exceed 50 percent of the taxpayer's contribution base for the taxable year.

(B) OTHER CONTRIBUTIONS.—Any charitable contribution other than a charitable contribution [to which subparagraph (A) applies] *to which subparagraph (A) or (G) applies* shall be allowed to the extent that the aggregate of such contributions does not exceed the lesser of—

(i) 30 percent of the taxpayer's contribution base for the taxable year, or

[(ii) the excess of 50 percent of the taxpayer's contribution base for the taxable year over the amount of charitable contributions allowable under subparagraph (A) (determined without regard to subparagraph (C)).]

(ii) *the excess of—*

*(I) the sum of 50 percent of the taxpayer's contribution base for the taxable year, plus so much of the amount of charitable contributions allowable*

*under subparagraph (G) as does not exceed 10 percent of such contribution base, over*

*(II) the amount of charitable contributions allowable under subparagraphs (A) and (G) (determined without regard to subparagraph (C)).*

If the aggregate of such contributions exceeds the limitation of the preceding sentence, such excess shall be treated (in a manner consistent with the rules of subsection (d)(1)) as a charitable contribution [(to which subparagraph (A) does not apply)] *(to which neither subparagraph (A) nor (G) applies)* in each of the 5 succeeding taxable years in order of time.

(C) Special limitation with respect to contributions described in subparagraph (A) of certain capital gain property (i) In the case of charitable contributions described in subparagraph (A) of capital gain property to which subsection (e)(1)(B) does not apply, the total amount of contributions of such property which may be taken into account under subsection (a) for any taxable year shall not exceed 30 percent of the taxpayer's contribution base for such year. For purposes of this subsection, contributions of capital gain property to which this subparagraph applies shall be taken into account after all other charitable contributions (other than charitable contributions to which subparagraph (D) applies).

(ii) If charitable contributions described in subparagraph (A) of capital gain property to which clause (i) applies exceeds 30 percent of the taxpayer's contribution base for any taxable year, such excess shall be treated, in a manner consistent with the rules of subsection (d)(1), as a charitable contribution of capital gain property to which clause (i) applies in each of the 5 succeeding taxable years in order of time.

(iii) At the election of the taxpayer (made at such time and in such manner as the Secretary prescribes by regulations), subsection (e)(1) shall apply to all contributions of capital gain property (to which subsection (e)(1)(B) does not otherwise apply) made by the taxpayer during the taxable year. If such an election is made, clauses (i) and (ii) shall not apply to contributions of capital gain property made during the taxable year, and, in applying subsection (d)(1) for such taxable year with respect to contributions of capital gain property made in any prior contribution year for which an election was not made under this clause, such contributions shall be reduced as if subsection (e)(1) had applied to such contributions in the year in which made.

(iv) For purposes of this paragraph, the term "capital gain property" means, with respect to any contribution, any capital asset the sale of which at its fair market value at the time of the contribution would have resulted in gain which would have been long-term capital gain. For purposes of the preceding sentence, any property which is property used in the

trade or business (as defined in section 1231(b)) shall be treated as a capital asset.

(D) Special limitation with respect to contributions of capital gain property to organizations not described in subparagraph (A)

(i) IN GENERAL.—In the case of charitable contributions (other than charitable contributions to which subparagraph (A) applies) of capital gain property, the total amount of such contributions of such property taken into account under subsection (a) for any taxable year shall not exceed the lesser of—

(I) 20 percent of the taxpayer's contribution base for the taxable year, or

(II) the excess of 30 percent of the taxpayer's contribution base for the taxable year over the amount of the contributions of capital gain property to which subparagraph (C) applies.

For purposes of this subsection, contributions of capital gain property to which this subparagraph applies shall be taken into account after all other charitable contributions.

(ii) CARRYOVER.—If the aggregate amount of contributions described in clause (i) exceeds the limitation of clause (i), such excess shall be treated (in a manner consistent with the rules of subsection (d)(1)) as a charitable contribution of capital gain property to which clause (i) applies in each of the 5 succeeding taxable years in order of time.

(E) CONTRIBUTIONS OF QUALIFIED CONSERVATION CONTRIBUTIONS.—

(i) IN GENERAL.—Any qualified conservation contribution (as defined in subsection (h)(1)) shall be allowed to the extent the aggregate of such contributions does not exceed the excess of 50 percent of the taxpayer's contribution base over the amount of all other charitable contributions allowable under this paragraph.

(ii) CARRYOVER.—If the aggregate amount of contributions described in clause (i) exceeds the limitation of clause (i), such excess shall be treated (in a manner consistent with the rules of subsection (d)(1)) as a charitable contribution to which clause (i) applies in each of the 15 succeeding years in order of time.

(iii) COORDINATION WITH OTHER SUBPARAGRAPHS.—For purposes of applying this subsection and subsection (d)(1), contributions described in clause (i) shall not be treated as described in subparagraph (A), (B), (C), or (D) and such subparagraphs shall apply without regard to such contributions.

(iv) SPECIAL RULE FOR CONTRIBUTION OF PROPERTY USED IN AGRICULTURE OR LIVESTOCK PRODUCTION.—

(I) IN GENERAL.—If the individual is a qualified farmer or rancher for the taxable year for which the contribution is made, clause (i) shall be ap-



plied by substituting “100 percent” for “50 percent”.

(II) EXCEPTION.—Subclause (I) shall not apply to any contribution of property made after the date of the enactment of this subparagraph which is used in agriculture or livestock production (or available for such production) unless such contribution is subject to a restriction that such property remain available for such production. This subparagraph shall be applied separately with respect to property to which subclause (I) does not apply by reason of the preceding sentence prior to its application to property to which subclause (I) does apply.

(v) DEFINITION.—For purposes of clause (iv), the term “qualified farmer or rancher” means a taxpayer whose gross income from the trade or business of farming (within the meaning of section 2032A(e)(5)) is greater than 50 percent of the taxpayer’s gross income for the taxable year.

(F) CERTAIN PRIVATE FOUNDATIONS.—The private foundations referred to in subparagraph (A)(vii) and subsection (e)(1)(B) are—

(i) a private operating foundation (as defined in section 4942(j)(3)),

(ii) any other private foundation (as defined in section 509(a)) which, not later than the 15th day of the third month after the close of the foundation’s taxable year in which contributions are received, makes qualifying distributions (as defined in section 4942(g), without regard to paragraph (3) thereof), which are treated, after the application of section 4942(g)(3), as distributions out of corpus (in accordance with section 4942(h)) in an amount equal to 100 percent of such contributions, and with respect to which the taxpayer obtains adequate records or other sufficient evidence from the foundation showing that the foundation made such qualifying distributions, and

(iii) a private foundation all of the contributions to which are pooled in a common fund and which would be described in section 509(a)(3) but for the right of any substantial contributor (hereafter in this clause called “donor”) or his spouse to designate annually the recipients, from among organizations described in paragraph (1) of section 509(a), of the income attributable to the donor’s contribution to the fund and to direct (by deed or by will) the payment, to an organization described in such paragraph (1), of the corpus in the common fund attributable to the donor’s contribution; but this clause shall apply only if all of the income of the common fund is required to be (and is) distributed to one or more organizations described in such paragraph (1) not later than the 15th day of the third month after the close of the taxable year in which the income is realized by the fund and only if

all of the corpus attributable to any donor's contribution to the fund is required to be (and is) distributed to one or more of such organizations not later than one year after his death or after the death of his surviving spouse if she has the right to designate the recipients of such corpus.

**[(G) INCREASED LIMITATION FOR CASH CONTRIBUTIONS.—**

**[(i) IN GENERAL.—**In the case of any contribution of cash to an organization described in subparagraph (A), the total amount of such contributions which may be taken into account under subsection (a) for any taxable year beginning after December 31, 2017, and before January 1, 2026, shall not exceed 60 percent of the taxpayer's contribution base for such year.

**[(ii) CARRYOVER.—**If the aggregate amount of contributions described in clause (i) exceeds the applicable limitation under clause (i) for any taxable year described in such clause, such excess shall be treated (in a manner consistent with the rules of subsection (d)(1)) as a charitable contribution to which clause (i) applies in each of the 5 succeeding years in order of time.

**[(iii) Coordination with subparagraphs (A) and (B)**

**[(I) IN GENERAL.—**Contributions taken into account under this subparagraph shall not be taken into account under subparagraph (A).

**[(II) LIMITATION REDUCTION.—**For each taxable year described in clause (i), and each taxable year to which any contribution under this subparagraph is carried over under clause (ii), subparagraph (A) shall be applied by reducing (but not below zero) the contribution limitation allowed for the taxable year under such subparagraph by the aggregate contributions allowed under this subparagraph for such taxable year, and subparagraph (B) shall be applied by treating any reference to subparagraph (A) as a reference to both subparagraph (A) and this subparagraph.]

**(G) CASH CONTRIBUTIONS.—**

*(i) IN GENERAL.—Any contribution of cash to an organization described in subparagraph (A) shall be allowed to the extent that the aggregate of such contributions does not exceed 60 percent of the taxpayer's contribution base for the taxable year, reduced by the aggregate amount of contributions allowable under subparagraph (A) for such taxpayer for such year.*

*(ii) CARRYOVER.—If the aggregate amount of contributions described in clause (i) exceeds the limitation of clause (i), such excess shall be treated (in a manner consistent with the rules of subsection (d)(1)) as a charitable contribution to which clause (i) applies in each of the 5 succeeding years in order of time.*

**(H) CONTRIBUTION BASE DEFINED.—**For purposes of this section, the term "contribution base" means adjusted gross

income (computed without regard to any net operating loss carryback to the taxable year under section 172).

(2) CORPORATIONS.—In the case of a corporation—

(A) IN GENERAL.—The total deductions under subsection (a) for any taxable year (other than for contributions to which subparagraph (B) or (C) applies) shall not exceed 10 percent of the taxpayer's taxable income.

(B) QUALIFIED CONSERVATION CONTRIBUTIONS BY CERTAIN CORPORATE FARMERS AND RANCHERS.—

(i) IN GENERAL.—Any qualified conservation contribution (as defined in subsection (h)(1))—

(I) which is made by a corporation which, for the taxable year during which the contribution is made, is a qualified farmer or rancher (as defined in paragraph (1)(E)(v)) and the stock of which is not readily tradable on an established securities market at any time during such year, and

(II) which, in the case of contributions made after the date of the enactment of this subparagraph, is a contribution of property which is used in agriculture or livestock production (or available for such production) and which is subject to a restriction that such property remain available for such production,

shall be allowed to the extent the aggregate of such contributions does not exceed the excess of the taxpayer's taxable income over the amount of charitable contributions allowable under subparagraph (A).

(ii) CARRYOVER.—If the aggregate amount of contributions described in clause (i) exceeds the limitation of clause (i), such excess shall be treated (in a manner consistent with the rules of subsection (d)(2)) as a charitable contribution to which clause (i) applies in each of the 15 succeeding taxable years in order of time.

(C) QUALIFIED CONSERVATION CONTRIBUTIONS BY CERTAIN NATIVE CORPORATIONS.—

(i) IN GENERAL.—Any qualified conservation contribution (as defined in subsection (h)(1)) which—

(I) is made by a Native Corporation, and

(II) is a contribution of property which was land conveyed under the Alaska Native Claims Settlement Act,

shall be allowed to the extent that the aggregate amount of such contributions does not exceed the excess of the taxpayer's taxable income over the amount of charitable contributions allowable under subparagraph (A).

(ii) CARRYOVER.—If the aggregate amount of contributions described in clause (i) exceeds the limitation of clause (i), such excess shall be treated (in a manner consistent with the rules of subsection (d)(2)) as a charitable contribution to which clause (i) applies in each of the 15 succeeding taxable years in order of time.

(iii) NATIVE CORPORATION.—For purposes of this subparagraph, the term “Native Corporation” has the meaning given such term by section 3(m) of the Alaska Native Claims Settlement Act.

(D) TAXABLE INCOME.—For purposes of this paragraph, taxable income shall be computed without regard to—

- (i) this section,
- (ii) part VIII (except section 248),
- (iii) any net operating loss carryback to the taxable year under section 172,
- (iv) any capital loss carryback to the taxable year under section 1212(a)(1)
- (v) section 199A(g).

(c) CHARITABLE CONTRIBUTION DEFINED.—For purposes of this section, the term “charitable contribution” means a contribution or gift to or for the use of—

(1) A State, a possession of the United States, or any political subdivision of any of the foregoing, or the United States or the District of Columbia, but only if the contribution or gift is made for exclusively public purposes.

(2) A corporation, trust, or community chest, fund, or foundation—

(A) created or organized in the United States or in any possession thereof, or under the law of the United States, any State, the District of Columbia, or any possession of the United States;

(B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals;

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and

(D) which is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

A contribution or gift by a corporation to a trust, chest, fund, or foundation shall be deductible by reason of this paragraph only if it is to be used within the United States or any of its possessions exclusively for purposes specified in subparagraph (B). Rules similar to the rules of section 501(j) shall apply for purposes of this paragraph.

(3) A post or organization of war veterans, or an auxiliary unit or society of, or trust or foundation for, any such post or organization—

(A) organized in the United States or any of its possessions, and

(B) no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(4) In the case of a contribution or gift by an individual, a domestic fraternal society, order, or association, operating

under the lodge system, but only if such contribution or gift is to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals.

(5) A cemetery company owned and operated exclusively for the benefit of its members, or any corporation chartered solely for burial purposes as a cemetery corporation and not permitted by its charter to engage in any business not necessarily incident to that purpose, if such company or corporation is not operated for profit and no part of the net earnings of such company or corporation inures to the benefit of any private shareholder or individual.

For purposes of this section, the term "charitable contribution" also means an amount treated under subsection (g) as paid for the use of an organization described in paragraph (2), (3), or (4).

(d) CARRYOVERS OF EXCESS CONTRIBUTIONS.—

(1) INDIVIDUALS.—

(A) IN GENERAL.—In the case of an individual, if the amount of charitable contributions described in subsection (b)(1)(A) payment of which is made within a taxable year (hereinafter in this paragraph referred to as the "contribution year") exceeds 50 percent of the taxpayer's contribution base for such year, such excess shall be treated as a charitable contribution described in subsection (b)(1)(A) paid in each of the 5 succeeding taxable years in order of time, but, with respect to any such succeeding taxable year, only to the extent of the lesser of the two following amounts:

(i) the amount by which 50 percent of the taxpayer's contribution base for such succeeding taxable year exceeds the sum of the charitable contributions described in subsection (b)(1)(A) payment of which is made by the taxpayer within such succeeding taxable year (determined without regard to this subparagraph) and the charitable contributions described in subsection (b)(1)(A) payment of which was made in taxable years before the contribution year which are treated under this subparagraph as having been paid in such succeeding taxable year; or

(ii) in the case of the first succeeding taxable year, the amount of such excess, and in the case of the second, third, fourth, or fifth succeeding taxable year, the portion of such excess not treated under this subparagraph as a charitable contribution described in subsection (b)(1)(A) paid in any taxable year intervening between the contribution year and such succeeding taxable year.

(B) SPECIAL RULE FOR NET OPERATING LOSS CARRYOVERS.—In applying subparagraph (A), the excess determined under subparagraph (A) for the contribution year shall be reduced to the extent that such excess reduces taxable income (as computed for purposes of the second sentence of section 172(b)(2)) and increases the net operating loss deduction for a taxable year succeeding the contribution year.

## (2) CORPORATIONS.—

(A) IN GENERAL.—Any contribution made by a corporation in a taxable year (hereinafter in this paragraph referred to as the “contribution year”) in excess of the amount deductible for such year under subsection (b)(2)(A) shall be deductible for each of the 5 succeeding taxable years in order of time, but only to the extent of the lesser of the two following amounts: (i) the excess of the maximum amount deductible for such succeeding taxable year under subsection (b)(2)(A) over the sum of the contributions made in such year plus the aggregate of the excess contributions which were made in taxable years before the contribution year and which are deductible under this subparagraph for such succeeding taxable year; or (ii) in the case of the first succeeding taxable year, the amount of such excess contribution, and in the case of the second, third, fourth, or fifth succeeding taxable year, the portion of such excess contribution not deductible under this subparagraph for any taxable year intervening between the contribution year and such succeeding taxable year.

(B) SPECIAL RULE FOR NET OPERATING LOSS CARRYOVERS.—For purposes of subparagraph (A), the excess of—

(i) the contributions made by a corporation in a taxable year to which this section applies, over

(ii) the amount deductible in such year under the limitation in subsection (b)(2)(A),

shall be reduced to the extent that such excess reduces taxable income (as computed for purposes of the second sentence of section 172(b)(2)) and increases a net operating loss carryover under section 172 to a succeeding taxable year.

## (e) CERTAIN CONTRIBUTIONS OF ORDINARY INCOME AND CAPITAL GAIN PROPERTY.—

(1) GENERAL RULE.—The amount of any charitable contribution of property otherwise taken into account under this section shall be reduced by the sum of—

(A) the amount of gain which would not have been long-term capital gain (determined without regard to section 1221(b)(3)) if the property contributed had been sold by the taxpayer at its fair market value (determined at the time of such contribution), and

(B) in the case of a charitable contribution—

(i) of tangible personal property—

(I) if the use by the donee is unrelated to the purpose or function constituting the basis for its exemption under section 501 (or, in the case of a governmental unit, to any purpose or function described in subsection (c)), or

(II) which is applicable property (as defined in paragraph (7)(C), but without regard to clause (ii) thereof) which is sold, exchanged, or otherwise disposed of by the donee before the last day of the taxable year in which the contribution was made and with respect to which the donee has not made

a certification in accordance with paragraph (7)(D),

(ii) to or for the use of a private foundation (as defined in section 509(a)), other than a private foundation described in subsection (b)(1)(F),

(iii) of any patent, copyright (other than a copyright described in section 1221(a)(3) or 1231(b)(1)(C)), trademark, trade name, trade secret, know-how, software (other than software described in section 197(e)(3)(A)(i)), or similar property, or applications or registrations of such property, or

(iv) of any taxidermy property which is contributed by the person who prepared, stuffed, or mounted the property or by any person who paid or incurred the cost of such preparation, stuffing, or mounting,

the amount of gain which would have been long-term capital gain if the property contributed had been sold by the taxpayer at its fair market value (determined at the time of such contribution).

For purposes of applying this paragraph (other than in the case of gain to which section 617(d)(1), 1245(a), 1250(a), 1252(a), or 1254(a) applies), property which is property used in the trade or business (as defined in section 1231(b)) shall be treated as a capital asset. For purposes of applying this paragraph in the case of a charitable contribution of stock in an S corporation, rules similar to the rules of section 751 shall apply in determining whether gain on such stock would have been long-term capital gain if such stock were sold by the taxpayer.

(2) ALLOCATION OF BASIS.—For purposes of paragraph (1), in the case of a charitable contribution of less than the taxpayer's entire interest in the property contributed, the taxpayer's adjusted basis in such property shall be allocated between the interest contributed and any interest not contributed in accordance with regulations prescribed by the Secretary.

(3) SPECIAL RULE FOR CERTAIN CONTRIBUTIONS OF INVENTORY AND OTHER PROPERTY.—

(A) QUALIFIED CONTRIBUTIONS.—For purposes of this paragraph, a qualified contribution shall mean a charitable contribution of property described in paragraph (1) or (2) of section 1221(a), by a corporation (other than a corporation which is an S corporation) to an organization which is described in section 501(c)(3) and is exempt under section 501(a) (other than a private foundation, as defined in section 509(a), which is not an operating foundation, as defined in section 4942(j)(3)), but only if—

(i) the use of the property by the donee is related to the purpose or function constituting the basis for its exemption under section 501 and the property is to be used by the donee solely for the care of the ill, the needy, or infants;

(ii) the property is not transferred by the donee in exchange for money, other property, or services;

(iii) the taxpayer receives from the donee a written statement representing that its use and disposition of

the property will be in accordance with the provisions of clauses (i) and (ii); and

(iv) in the case where the property is subject to regulation under the Federal Food, Drug, and Cosmetic Act, as amended, such property must fully satisfy the applicable requirements of such Act and regulations promulgated thereunder on the date of transfer and for one hundred and eighty days prior thereto.

(B) AMOUNT OF REDUCTION.—The reduction under paragraph (1)(A) for any qualified contribution (as defined in subparagraph (A)) shall be no greater than the sum of—

(i) one-half of the amount computed under paragraph (1)(A) (computed without regard to this paragraph), and

(ii) the amount (if any) by which the charitable contribution deduction under this section for any qualified contribution (computed by taking into account the amount determined in clause (i), but without regard to this clause) exceeds twice the basis of such property.

(C) SPECIAL RULE FOR CONTRIBUTIONS OF FOOD INVENTORY.—

(i) GENERAL RULE.—In the case of a charitable contribution of food from any trade or business of the taxpayer, this paragraph shall be applied—

(I) without regard to whether the contribution is made by a C corporation, and

(II) only to food that is apparently wholesome food.

(ii) LIMITATION.—The aggregate amount of such contributions for any taxable year which may be taken into account under this section shall not exceed—

(I) in the case of any taxpayer other than a C corporation, 15 percent of the taxpayer's aggregate net income for such taxable year from all trades or businesses from which such contributions were made for such year, computed without regard to this section, and

(II) in the case of a C corporation, 15 percent of taxable income (as defined in subsection (b)(2)(D)).

(iii) RULES RELATED TO LIMITATION.—

(I) CARRYOVER.—If such aggregate amount exceeds the limitation imposed under clause (ii), such excess shall be treated (in a manner consistent with the rules of subsection (d)) as a charitable contribution described in clause (i) in each of the 5 succeeding taxable years in order of time.

(II) COORDINATION WITH OVERALL CORPORATE LIMITATION.—In the case of any charitable contribution which is allowable after the application of clause (ii)(II), subsection (b)(2)(A) shall not apply to such contribution, but the limitation imposed by such subsection shall be reduced (but not below zero) by the aggregate amount of such contributions. For purposes of subsection (b)(2)(B),



such contributions shall be treated as allowable under subsection (b)(2)(A).

(iv) DETERMINATION OF BASIS FOR CERTAIN TAXPAYERS.—If a taxpayer—

(I) does not account for inventories under section 471, and

(II) is not required to capitalize indirect costs under section 263A,

the taxpayer may elect, solely for purposes of subparagraph (B), to treat the basis of any apparently wholesome food as being equal to 25 percent of the fair market value of such food.

(v) DETERMINATION OF FAIR MARKET VALUE.—In the case of any such contribution of apparently wholesome food which cannot or will not be sold solely by reason of internal standards of the taxpayer, lack of market, or similar circumstances, or by reason of being produced by the taxpayer exclusively for the purposes of transferring the food to an organization described in subparagraph (A), the fair market value of such contribution shall be determined—

(I) without regard to such internal standards, such lack of market, such circumstances, or such exclusive purpose, and

(II) by taking into account the price at which the same or substantially the same food items (as to both type and quality) are sold by the taxpayer at the time of the contribution (or, if not so sold at such time, in the recent past).

(vi) APPARENTLY WHOLESOME FOOD.—For purposes of this subparagraph, the term “apparently wholesome food” has the meaning given to such term by section 22(b)(2) of the Bill Emerson Good Samaritan Food Donation Act (42 U.S.C. 1791(b)(2)), as in effect on the date of the enactment of this subparagraph.

(D) This paragraph shall not apply to so much of the amount of the gain described in paragraph (1)(A) which would be long-term capital gain but for the application of sections 617, 1245, 1250, or 1252.

(4) SPECIAL RULE FOR CONTRIBUTIONS OF SCIENTIFIC PROPERTY USED FOR RESEARCH.—

(A) LIMIT ON REDUCTION.—In the case of a qualified research contribution, the reduction under paragraph (1)(A) shall be no greater than the amount determined under paragraph (3)(B).

(B) QUALIFIED RESEARCH CONTRIBUTIONS.—For purposes of this paragraph, the term “qualified research contribution” means a charitable contribution by a corporation of tangible personal property described in paragraph (1) of section 1221(a), but only if—

(i) the contribution is to an organization described in subparagraph (A) or subparagraph (B) of section 41(e)(6),

(ii) the property is constructed or assembled by the taxpayer,

(iii) the contribution is made not later than 2 years after the date the construction or assembly of the property is substantially completed,

(iv) the original use of the property is by the donee,

(v) the property is scientific equipment or apparatus substantially all of the use of which by the donee is for research or experimentation (within the meaning of section 174), or for research training, in the United States in physical or biological sciences,

(vi) the property is not transferred by the donee in exchange for money, other property, or services, and

(vii) the taxpayer receives from the donee a written statement representing that its use and disposition of the property will be in accordance with the provisions of clauses (v) and (vi).

(C) CONSTRUCTION OF PROPERTY BY TAXPAYER.—For purposes of this paragraph, property shall be treated as constructed by the taxpayer only if the cost of the parts used in the construction of such property (other than parts manufactured by the taxpayer or a related person) do not exceed 50 percent of the taxpayer's basis in such property.

(D) CORPORATION.—For purposes of this paragraph, the term "corporation" shall not include—

(i) an S corporation,

(ii) a personal holding company (as defined in section 542), and

(iii) a service organization (as defined in section 414(m)(3)).

(5) SPECIAL RULE FOR CONTRIBUTIONS OF STOCK FOR WHICH MARKET QUOTATIONS ARE READILY AVAILABLE.—

(A) IN GENERAL.—Subparagraph (B)(ii) of paragraph (1) shall not apply to any contribution of qualified appreciated stock.

(B) QUALIFIED APPRECIATED STOCK.—Except as provided in subparagraph (C), for purposes of this paragraph, the term "qualified appreciated stock" means any stock of a corporation—

(i) for which (as of the date of the contribution) market quotations are readily available on an established securities market, and

(ii) which is capital gain property (as defined in subsection (b)(1)(C)(iv)).

(C) DONOR MAY NOT CONTRIBUTE MORE THAN 10 PERCENT OF STOCK OF CORPORATION.—

(i) IN GENERAL.—In the case of any donor, the term "qualified appreciated stock" shall not include any stock of a corporation contributed by the donor in a contribution to which paragraph (1)(B)(ii) applies (determined without regard to this paragraph) to the extent that the amount of the stock so contributed (when increased by the aggregate amount of all prior such contributions by the donor of stock in such corporation) exceeds 10 percent (in value) of all of the outstanding stock of such corporation.

(ii) SPECIAL RULE.—For purposes of clause (i), an individual shall be treated as making all contributions made by any member of his family (as defined in section 267(c)(4)).

(7) RECAPTURE OF DEDUCTION ON CERTAIN DISPOSITIONS OF EXEMPT USE PROPERTY.—

(A) IN GENERAL.—In the case of an applicable disposition of applicable property, there shall be included in the income of the donor of such property for the taxable year of such donor in which the applicable disposition occurs an amount equal to the excess (if any) of—

- (i) the amount of the deduction allowed to the donor under this section with respect to such property, over
- (ii) the donor's basis in such property at the time such property was contributed.

(B) APPLICABLE DISPOSITION.—For purposes of this paragraph, the term “applicable disposition” means any sale, exchange, or other disposition by the donee of applicable property—

- (i) after the last day of the taxable year of the donor in which such property was contributed, and
- (ii) before the last day of the 3-year period beginning on the date of the contribution of such property, unless the donee makes a certification in accordance with subparagraph (D).

(C) APPLICABLE PROPERTY.—For purposes of this paragraph, the term “applicable property” means charitable deduction property (as defined in section 6050L(a)(2)(A))—

- (i) which is tangible personal property the use of which is identified by the donee as related to the purpose or function constituting the basis of the donee's exemption under section 501, and
- (ii) for which a deduction in excess of the donor's basis is allowed.

(D) CERTIFICATION.—A certification meets the requirements of this subparagraph if it is a written statement which is signed under penalty of perjury by an officer of the donee organization and—

- (i) which—

(I) certifies that the use of the property by the donee was substantial and related to the purpose or function constituting the basis for the donee's exemption under section 501, and

(II) describes how the property was used and how such use furthered such purpose or function, or

- (ii) which—

(I) states the intended use of the property by the donee at the time of the contribution, and

(II) certifies that such intended use has become impossible or infeasible to implement.

(f) DISALLOWANCE OF DEDUCTION IN CERTAIN CASES AND SPECIAL RULES.—

(1) IN GENERAL.—No deduction shall be allowed under this section for a contribution to or for the use of an organization

or trust described in section 508(d) or 4948(c)(4) subject to the conditions specified in such sections.

(2) CONTRIBUTIONS OF PROPERTY PLACED IN TRUST.—

(A) REMAINDER INTEREST.—In the case of property transferred in trust, no deduction shall be allowed under this section for the value of a contribution of a remainder interest unless the trust is a charitable remainder annuity trust or a charitable remainder unitrust (described in section 664), or a pooled income fund (described in section 642(c)(5)).

(B) INCOME INTERESTS, ETC.—No deduction shall be allowed under this section for the value of any interest in property (other than a remainder interest) transferred in trust unless the interest is in the form of a guaranteed annuity or the trust instrument specifies that the interest is a fixed percentage distributed yearly of the fair market value of the trust property (to be determined yearly) and the grantor is treated as the owner of such interest for purposes of applying section 671. If the donor ceases to be treated as the owner of such an interest for purposes of applying section 671, at the time the donor ceases to be so treated, the donor shall for purposes of this chapter be considered as having received an amount of income equal to the amount of any deduction he received under this section for the contribution reduced by the discounted value of all amounts of income earned by the trust and taxable to him before the time at which he ceases to be treated as the owner of the interest. Such amounts of income shall be discounted to the date of the contribution. The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subparagraph.

(C) DENIAL OF DEDUCTION IN CASE OF PAYMENTS BY CERTAIN TRUSTS.—In any case in which a deduction is allowed under this section for the value of an interest in property described in subparagraph (B), transferred in trust, no deduction shall be allowed under this section to the grantor or any other person for the amount of any contribution made by the trust with respect to such interest.

(D) EXCEPTION.—This paragraph shall not apply in a case in which the value of all interests in property transferred in trust are deductible under subsection (a).

(3) DENIAL OF DEDUCTION IN CASE OF CERTAIN CONTRIBUTIONS OF PARTIAL INTERESTS IN PROPERTY.—

(A) IN GENERAL.—In the case of a contribution (not made by a transfer in trust) of an interest in property which consists of less than the taxpayer's entire interest in such property, a deduction shall be allowed under this section only to the extent that the value of the interest contributed would be allowable as a deduction under this section if such interest had been transferred in trust. For purposes of this subparagraph, a contribution by a taxpayer of the right to use property shall be treated as a contribution of less than the taxpayer's entire interest in such property.

(B) EXCEPTIONS.—Subparagraph (A) shall not apply to—

- (i) a contribution of a remainder interest in a personal residence or farm,
- (ii) a contribution of an undivided portion of the taxpayer's entire interest in property, and
- (iii) a qualified conservation contribution.

(4) VALUATION OF REMAINDER INTEREST IN REAL PROPERTY.—For purposes of this section, in determining the value of a remainder interest in real property, depreciation (computed on the straight line method) and depletion of such property shall be taken into account, and such value shall be discounted at a rate of 6 percent per annum, except that the Secretary may prescribe a different rate.

(5) REDUCTION FOR CERTAIN INTEREST.—If, in connection with any charitable contribution, a liability is assumed by the recipient or by any other person, or if a charitable contribution is of property which is subject to a liability, then, to the extent necessary to avoid the duplication of amounts, the amount taken into account for purposes of this section as the amount of the charitable contribution—

(A) shall be reduced for interest (i) which has been paid (or is to be paid) by the taxpayer, (ii) which is attributable to the liability, and (iii) which is attributable to any period after the making of the contribution, and

(B) in the case of a bond, shall be further reduced for interest (i) which has been paid (or is to be paid) by the taxpayer on indebtedness incurred or continued to purchase or carry such bond, and (ii) which is attributable to any period before the making of the contribution.

The reduction pursuant to subparagraph (B) shall not exceed the interest (including interest equivalent) on the bond which is attributable to any period before the making of the contribution and which is not (under the taxpayer's method of accounting) includible in the gross income of the taxpayer for any taxable year. For purposes of this paragraph, the term "bond" means any bond, debenture, note, or certificate or other evidence of indebtedness.

(6) DEDUCTIONS FOR OUT-OF-POCKET EXPENDITURES.—No deduction shall be allowed under this section for an out-of-pocket expenditure made by any person on behalf of an organization described in subsection (c) (other than an organization described in section 501(h)(5) (relating to churches, etc.)) if the expenditure is made for the purpose of influencing legislation (within the meaning of section 501(c)(3)).

(7) Reformation to comply with paragraph (2)

(A) IN GENERAL.—A deduction shall be allowed under subsection (a) in respect of any qualified reformation (within the meaning of section 2055(e)(3)(B)).

(B) RULES SIMILAR TO SECTION 2055(E)(3) TO APPLY.—For purposes of this paragraph, rules similar to the rules of section 2055(e)(3) shall apply.

(8) SUBSTANTIATION REQUIREMENT FOR CERTAIN CONTRIBUTIONS.—

(A) GENERAL RULE.—No deduction shall be allowed under subsection (a) for any contribution of \$250 or more unless the taxpayer substantiates the contribution by a

contemporaneous written acknowledgment of the contribution by the donee organization that meets the requirements of subparagraph (B).

(B) CONTENT OF ACKNOWLEDGEMENT.—An acknowledgment meets the requirements of this subparagraph if it includes the following information:

(i) The amount of cash and a description (but not value) of any property other than cash contributed.

(ii) Whether the donee organization provided any goods or services in consideration, in whole or in part, for any property described in clause (i).

(iii) A description and good faith estimate of the value of any goods or services referred to in clause (ii) or, if such goods or services consist solely of intangible religious benefits, a statement to that effect.

For purposes of this subparagraph, the term “intangible religious benefit” means any intangible religious benefit which is provided by an organization organized exclusively for religious purposes and which generally is not sold in a commercial transaction outside the donative context.

(C) CONTEMPORANEOUS.—For purposes of subparagraph (A), an acknowledgment shall be considered to be contemporaneous if the taxpayer obtains the acknowledgment on or before the earlier of—

(i) the date on which the taxpayer files a return for the taxable year in which the contribution was made, or

(ii) the due date (including extensions) for filing such return.

(D) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this paragraph, including regulations that may provide that some or all of the requirements of this paragraph do not apply in appropriate cases.

(9) DENIAL OF DEDUCTION WHERE CONTRIBUTION FOR LOBBYING ACTIVITIES.—No deduction shall be allowed under this section for a contribution to an organization which conducts activities to which section 162(e)(1) applies on matters of direct financial interest to the donor’s trade or business, if a principal purpose of the contribution was to avoid Federal income tax by securing a deduction for such activities under this section which would be disallowed by reason of section 162(e) if the donor had conducted such activities directly. No deduction shall be allowed under section 162(a) for any amount for which a deduction is disallowed under the preceding sentence.

(10) SPLIT-DOLLAR LIFE INSURANCE, ANNUITY, AND ENDOWMENT CONTRACTS.—

(A) IN GENERAL.—Nothing in this section or in section 545(b)(2), 642(c), 2055, 2106(a)(2), or 2522 shall be construed to allow a deduction, and no deduction shall be allowed, for any transfer to or for the use of an organization described in subsection (c) if in connection with such transfer—

(i) the organization directly or indirectly pays, or has previously paid, any premium on any personal benefit contract with respect to the transferor, or

(ii) there is an understanding or expectation that any person will directly or indirectly pay any premium on any personal benefit contract with respect to the transferor.

(B) **PERSONAL BENEFIT CONTRACT.**—For purposes of subparagraph (A), the term “personal benefit contract” means, with respect to the transferor, any life insurance, annuity, or endowment contract if any direct or indirect beneficiary under such contract is the transferor, any member of the transferor’s family, or any other person (other than an organization described in subsection (c)) designated by the transferor.

(C) **APPLICATION TO CHARITABLE REMAINDER TRUSTS.**—In the case of a transfer to a trust referred to in subparagraph (E), references in subparagraphs (A) and (F) to an organization described in subsection (c) shall be treated as a reference to such trust.

(D) **EXCEPTION FOR CERTAIN ANNUITY CONTRACTS.**—If, in connection with a transfer to or for the use of an organization described in subsection (c), such organization incurs an obligation to pay a charitable gift annuity (as defined in section 501(m)) and such organization purchases any annuity contract to fund such obligation, persons receiving payments under the charitable gift annuity shall not be treated for purposes of subparagraph (B) as indirect beneficiaries under such contract if—

(i) such organization possesses all of the incidents of ownership under such contract,

(ii) such organization is entitled to all the payments under such contract, and

(iii) the timing and amount of payments under such contract are substantially the same as the timing and amount of payments to each such person under such obligation (as such obligation is in effect at the time of such transfer).

(E) **EXCEPTION FOR CERTAIN CONTRACTS HELD BY CHARITABLE REMAINDER TRUSTS.**—A person shall not be treated for purposes of subparagraph (B) as an indirect beneficiary under any life insurance, annuity, or endowment contract held by a charitable remainder annuity trust or a charitable remainder unitrust (as defined in section 664(d)) solely by reason of being entitled to any payment referred to in paragraph (1)(A) or (2)(A) of section 664(d) if—

(i) such trust possesses all of the incidents of ownership under such contract, and

(ii) such trust is entitled to all the payments under such contract.

(F) **EXCISE TAX ON PREMIUMS PAID.**—

(i) **IN GENERAL.**—There is hereby imposed on any organization described in subsection (c) an excise tax equal to the premiums paid by such organization on any life insurance, annuity, or endowment contract if

the payment of premiums on such contract is in connection with a transfer for which a deduction is not allowable under subparagraph (A), determined without regard to when such transfer is made.

(ii) PAYMENTS BY OTHER PERSONS.—For purposes of clause (i), payments made by any other person pursuant to an understanding or expectation referred to in subparagraph (A) shall be treated as made by the organization.

(iii) REPORTING.—Any organization on which tax is imposed by clause (i) with respect to any premium shall file an annual return which includes—

(I) the amount of such premiums paid during the year and the name and TIN of each beneficiary under the contract to which the premium relates, and

(II) such other information as the Secretary may require.

The penalties applicable to returns required under section 6033 shall apply to returns required under this clause. Returns required under this clause shall be furnished at such time and in such manner as the Secretary shall by forms or regulations require.

(iv) CERTAIN RULES TO APPLY.—The tax imposed by this subparagraph shall be treated as imposed by chapter 42 for purposes of this title other than subchapter B of chapter 42.

(G) SPECIAL RULE WHERE STATE REQUIRES SPECIFICATION OF CHARITABLE GIFT ANNUITANT IN CONTRACT.—In the case of an obligation to pay a charitable gift annuity referred to in subparagraph (D) which is entered into under the laws of a State which requires, in order for the charitable gift annuity to be exempt from insurance regulation by such State, that each beneficiary under the charitable gift annuity be named as a beneficiary under an annuity contract issued by an insurance company authorized to transact business in such State, the requirements of clauses (i) and (ii) of subparagraph (D) shall be treated as met if—

(i) such State law requirement was in effect on February 8, 1999,

(ii) each such beneficiary under the charitable gift annuity is a bona fide resident of such State at the time the obligation to pay a charitable gift annuity is entered into, and

(iii) the only persons entitled to payments under such contract are persons entitled to payments as beneficiaries under such obligation on the date such obligation is entered into.

(H) MEMBER OF FAMILY.—For purposes of this paragraph, an individual's family consists of the individual's grandparents, the grandparents of such individual's spouse, the lineal descendants of such grandparents, and any spouse of such a lineal descendant.

(I) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry



out the purposes of this paragraph, including regulations to prevent the avoidance of such purposes.

(11) QUALIFIED APPRAISAL AND OTHER DOCUMENTATION FOR CERTAIN CONTRIBUTIONS.—

(A) IN GENERAL.—

(i) DENIAL OF DEDUCTION.—In the case of an individual, partnership, or corporation, no deduction shall be allowed under subsection (a) for any contribution of property for which a deduction of more than \$500 is claimed unless such person meets the requirements of subparagraphs (B), (C), and (D), as the case may be, with respect to such contribution.

(ii) EXCEPTIONS.—

(I) READILY VALUED PROPERTY.—Subparagraphs (C) and (D) shall not apply to cash, property described in subsection (e)(1)(B)(iii) or section 1221(a)(1), publicly traded securities (as defined in section 6050L(a)(2)(B)), and any qualified vehicle described in paragraph (12)(A)(ii) for which an acknowledgement under paragraph (12)(B)(iii) is provided.

(II) REASONABLE CAUSE.—Clause (i) shall not apply if it is shown that the failure to meet such requirements is due to reasonable cause and not to willful neglect.

(B) PROPERTY DESCRIPTION FOR CONTRIBUTIONS OF MORE THAN \$500.—In the case of contributions of property for which a deduction of more than \$500 is claimed, the requirements of this subparagraph are met if the individual, partnership or corporation includes with the return for the taxable year in which the contribution is made a description of such property and such other information as the Secretary may require. The requirements of this subparagraph shall not apply to a C corporation which is not a personal service corporation or a closely held C corporation.

(C) QUALIFIED APPRAISAL FOR CONTRIBUTIONS OF MORE THAN \$5,000.—In the case of contributions of property for which a deduction of more than \$5,000 is claimed, the requirements of this subparagraph are met if the individual, partnership, or corporation obtains a qualified appraisal of such property and attaches to the return for the taxable year in which such contribution is made such information regarding such property and such appraisal as the Secretary may require.

(D) SUBSTANTIATION FOR CONTRIBUTIONS OF MORE THAN \$500,000.—In the case of contributions of property for which a deduction of more than \$500,000 is claimed, the requirements of this subparagraph are met if the individual, partnership, or corporation attaches to the return for the taxable year a qualified appraisal of such property.

(E) QUALIFIED APPRAISAL AND APPRAISER.—For purposes of this paragraph—

(i) **QUALIFIED APPRAISAL.**—The term “qualified appraisal” means, with respect to any property, an appraisal of such property which—

(I) is treated for purposes of this paragraph as a qualified appraisal under regulations or other guidance prescribed by the Secretary, and

(II) is conducted by a qualified appraiser in accordance with generally accepted appraisal standards and any regulations or other guidance prescribed under subclause (I).

(ii) **QUALIFIED APPRAISER.**—Except as provided in clause (iii), the term “qualified appraiser” means an individual who—

(I) has earned an appraisal designation from a recognized professional appraiser organization or has otherwise met minimum education and experience requirements set forth in regulations prescribed by the Secretary,

(II) regularly performs appraisals for which the individual receives compensation, and

(III) meets such other requirements as may be prescribed by the Secretary in regulations or other guidance.

(iii) **SPECIFIC APPRAISALS.**—An individual shall not be treated as a qualified appraiser with respect to any specific appraisal unless—

(I) the individual demonstrates verifiable education and experience in valuing the type of property subject to the appraisal, and

(II) the individual has not been prohibited from practicing before the Internal Revenue Service by the Secretary under section 330(c) of title 31, United States Code, at any time during the 3-year period ending on the date of the appraisal.

(F) **AGGREGATION OF SIMILAR ITEMS OF PROPERTY.**—For purposes of determining thresholds under this paragraph, property and all similar items of property donated to 1 or more donees shall be treated as 1 property.

(G) **SPECIAL RULE FOR PASS-THRU ENTITIES.**—In the case of a partnership or S corporation, this paragraph shall be applied at the entity level, except that the deduction shall be denied at the partner or shareholder level.

(H) **REGULATIONS.**—The Secretary may prescribe such regulations as may be necessary or appropriate to carry out the purposes of this paragraph, including regulations that may provide that some or all of the requirements of this paragraph do not apply in appropriate cases.

(12) **CONTRIBUTIONS OF USED MOTOR VEHICLES, BOATS, AND AIRPLANES.**—

(A) **IN GENERAL.**—In the case of a contribution of a qualified vehicle the claimed value of which exceeds \$500—

(i) paragraph (8) shall not apply and no deduction shall be allowed under subsection (a) for such contribution unless the taxpayer substantiates the contribution by a contemporaneous written acknowledge-

ment of the contribution by the donee organization that meets the requirements of subparagraph (B) and includes the acknowledgement with the taxpayer's return of tax which includes the deduction, and

(ii) if the organization sells the vehicle without any significant intervening use or material improvement of such vehicle by the organization, the amount of the deduction allowed under subsection (a) shall not exceed the gross proceeds received from such sale.

(B) **CONTENT OF ACKNOWLEDGEMENT.**—An acknowledgement meets the requirements of this subparagraph if it includes the following information:

(i) The name and taxpayer identification number of the donor.

(ii) The vehicle identification number or similar number.

(iii) In the case of a qualified vehicle to which subparagraph (A)(ii) applies—

(I) a certification that the vehicle was sold in an arm's length transaction between unrelated parties,

(II) the gross proceeds from the sale, and

(III) a statement that the deductible amount may not exceed the amount of such gross proceeds.

(iv) In the case of a qualified vehicle to which subparagraph (A)(ii) does not apply—

(I) a certification of the intended use or material improvement of the vehicle and the intended duration of such use, and

(II) a certification that the vehicle would not be transferred in exchange for money, other property, or services before completion of such use or improvement.

(v) Whether the donee organization provided any goods or services in consideration, in whole or in part, for the qualified vehicle.

(vi) A description and good faith estimate of the value of any goods or services referred to in clause (v) or, if such goods or services consist solely of intangible religious benefits (as defined in paragraph (8)(B)), a statement to that effect.

(C) **CONTEMPORANEOUS.**—For purposes of subparagraph (A), an acknowledgement shall be considered to be contemporaneous if the donee organization provides it within 30 days of—

(i) the sale of the qualified vehicle, or

(ii) in the case of an acknowledgement including a certification described in subparagraph (B)(iv), the contribution of the qualified vehicle.

(D) **INFORMATION TO SECRETARY.**—A donee organization required to provide an acknowledgement under this paragraph shall provide to the Secretary the information contained in the acknowledgement. Such information shall be

provided at such time and in such manner as the Secretary may prescribe.

(E) QUALIFIED VEHICLE.—For purposes of this paragraph, the term “qualified vehicle” means any—

- (i) motor vehicle manufactured primarily for use on public streets, roads, and highways,
- (ii) boat, or
- (iii) airplane.

Such term shall not include any property which is described in section 1221(a)(1).

(F) REGULATIONS OR OTHER GUIDANCE.—The Secretary shall prescribe such regulations or other guidance as may be necessary to carry out the purposes of this paragraph. The Secretary may prescribe regulations or other guidance which exempts sales by the donee organization which are in direct furtherance of such organization’s charitable purpose from the requirements of subparagraphs (A)(ii) and (B)(iv)(II).

(13) CONTRIBUTIONS OF CERTAIN INTERESTS IN BUILDINGS LOCATED IN REGISTERED HISTORIC DISTRICTS.—

(A) IN GENERAL.—No deduction shall be allowed with respect to any contribution described in subparagraph (B) unless the taxpayer includes with the return for the taxable year of the contribution a \$500 filing fee.

(B) CONTRIBUTION DESCRIBED.—A contribution is described in this subparagraph if such contribution is a qualified conservation contribution (as defined in subsection (h)) which is a restriction with respect to the exterior of a building described in subsection (h)(4)(C)(ii) and for which a deduction is claimed in excess of \$10,000.

(C) DEDICATION OF FEE.—Any fee collected under this paragraph shall be used for the enforcement of the provisions of subsection (h).

(14) REDUCTION FOR AMOUNTS ATTRIBUTABLE TO REHABILITATION CREDIT.—In the case of any qualified conservation contribution (as defined in subsection (h)), the amount of the deduction allowed under this section shall be reduced by an amount which bears the same ratio to the fair market value of the contribution as—

(A) the sum of the credits allowed to the taxpayer under section 47 for the 5 preceding taxable years with respect to any building which is a part of such contribution, bears to

(B) the fair market value of the building on the date of the contribution.

(15) SPECIAL RULE FOR TAXIDERMY PROPERTY.—

(A) BASIS.—For purposes of this section and notwithstanding section 1012, in the case of a charitable contribution of taxidermy property which is made by the person who prepared, stuffed, or mounted the property or by any person who paid or incurred the cost of such preparation, stuffing, or mounting, only the cost of the preparing, stuffing, or mounting shall be included in the basis of such property.

(B) TAXIDERMY PROPERTY.—For purposes of this section, the term “taxidermy property” means any work of art which—

(i) is the reproduction or preservation of an animal, in whole or in part,

(ii) is prepared, stuffed, or mounted for purposes of recreating one or more characteristics of such animal, and

(iii) contains a part of the body of the dead animal.

(16) CONTRIBUTIONS OF CLOTHING AND HOUSEHOLD ITEMS.—

(A) IN GENERAL.—In the case of an individual, partnership, or corporation, no deduction shall be allowed under subsection (a) for any contribution of clothing or a household item unless such clothing or household item is in good used condition or better.

(B) ITEMS OF MINIMAL VALUE.—Notwithstanding subparagraph (A), the Secretary may by regulation deny a deduction under subsection (a) for any contribution of clothing or a household item which has minimal monetary value.

(C) EXCEPTION FOR CERTAIN PROPERTY.—Subparagraphs (A) and (B) shall not apply to any contribution of a single item of clothing or a household item for which a deduction of more than \$500 is claimed if the taxpayer includes with the taxpayer’s return a qualified appraisal with respect to the property.

(D) HOUSEHOLD ITEMS.—For purposes of this paragraph—

(i) IN GENERAL.—The term “household items” includes furniture, furnishings, electronics, appliances, linens, and other similar items.

(ii) EXCLUDED ITEMS.—Such term does not include—

(I) food,

(II) paintings, antiques, and other objects of art,

(III) jewelry and gems, and

(IV) collections.

(E) SPECIAL RULE FOR PASS-THRU ENTITIES.—In the case of a partnership or S corporation, this paragraph shall be applied at the entity level, except that the deduction shall be denied at the partner or shareholder level.

(17) RECORDKEEPING.—No deduction shall be allowed under subsection (a) for any contribution of a cash, check, or other monetary gift unless the donor maintains as a record of such contribution a bank record or a written communication from the donee showing the name of the donee organization, the date of the contribution, and the amount of the contribution.

(18) CONTRIBUTIONS TO DONOR ADVISED FUNDS.—A deduction otherwise allowed under subsection (a) for any contribution to a donor advised fund (as defined in section 4966(d)(2)) shall only be allowed if—

(A) the sponsoring organization (as defined in section 4966(d)(1)) with respect to such donor advised fund is not—

(i) described in paragraph (3), (4), or (5) of subsection (c), or

(ii) a type III supporting organization (as defined in section 4943(f)(5)(A)) which is not a functionally integrated type III supporting organization (as defined in section 4943(f)(5)(B)), and

(B) the taxpayer obtains a contemporaneous written acknowledgment (determined under rules similar to the rules of paragraph (8)(C)) from the sponsoring organization (as so defined) of such donor advised fund that such organization has exclusive legal control over the assets contributed.

(g) AMOUNTS PAID TO MAINTAIN CERTAIN STUDENTS AS MEMBERS OF TAXPAYER'S HOUSEHOLD.—

(1) IN GENERAL.—Subject to the limitations provided by paragraph (2), amounts paid by the taxpayer to maintain an individual (other than a dependent, as defined in [section 152] section 7706 (determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof), or a relative of the taxpayer) as a member of his household during the period that such individual is—

(A) a member of the taxpayer's household under a written agreement between the taxpayer and an organization described in paragraph (2), (3), or (4) of subsection (c) to implement a program of the organization to provide educational opportunities for pupils or students in private homes, and

(B) a full-time pupil or student in the twelfth or any lower grade at an educational organization described in section 170(b)(1)(A)(ii) located in the United States, shall be treated as amounts paid for the use of the organization.

(2) LIMITATIONS.—

(A) AMOUNT.—Paragraph (1) shall apply to amounts paid within the taxable year only to the extent that such amounts do not exceed \$50 multiplied by the number of full calendar months during the taxable year which fall within the period described in paragraph (1). For purposes of the preceding sentence, if 15 or more days of a calendar month fall within such period such month shall be considered as a full calendar month.

(B) COMPENSATION OR REIMBURSEMENT.—Paragraph (1) shall not apply to any amount paid by the taxpayer within the taxable year if the taxpayer receives any money or other property as compensation or reimbursement for maintaining the individual in his household during the period described in paragraph (1).

(3) RELATIVE DEFINED.—For purposes of paragraph (1), the term "relative of the taxpayer" means an individual who, with respect to the taxpayer, bears any of the relationships described in subparagraphs (A) through (G) of [section 152(d)(2)] section 7706(d)(2).

(4) NO OTHER AMOUNT ALLOWED AS DEDUCTION.—No deduction shall be allowed under subsection (a) for any amount paid by a taxpayer to maintain an individual as a member of his household under a program described in paragraph (1)(A) except as provided in this subsection.

(h) QUALIFIED CONSERVATION CONTRIBUTION.—

(1) **IN GENERAL.**—For purposes of subsection (f)(3)(B)(iii), the term “qualified conservation contribution” means a contribution—

- (A) of a qualified real property interest,
- (B) to a qualified organization,
- (C) exclusively for conservation purposes.

(2) **QUALIFIED REAL PROPERTY INTEREST.**—For purposes of this subsection, the term “qualified real property interest” means any of the following interests in real property:

- (A) the entire interest of the donor other than a qualified mineral interest,
- (B) a remainder interest, and
- (C) a restriction (granted in perpetuity) on the use which may be made of the real property.

(3) **QUALIFIED ORGANIZATION.**—For purposes of paragraph (1), the term “qualified organization” means an organization which—

- (A) is described in clause (v) or (vi) of subsection (b)(1)(A), or
- (B) is described in section 501(c)(3) and—
  - (i) meets the requirements of section 509(a)(2), or
  - (ii) meets the requirements of section 509(a)(3) and is controlled by an organization described in subparagraph (A) or in clause (i) of this subparagraph.

(4) **CONSERVATION PURPOSE DEFINED.**—

(A) **IN GENERAL.**—For purposes of this subsection, the term “conservation purpose” means—

- (i) the preservation of land areas for outdoor recreation by, or the education of, the general public,
- (ii) the protection of a relatively natural habitat of fish, wildlife, or plants, or similar ecosystem,
- (iii) the preservation of open space (including farmland and forest land) where such preservation is—

- (I) for the scenic enjoyment of the general public, or
- (II) pursuant to a clearly delineated Federal, State, or local governmental conservation policy, and will yield a significant public benefit, or
- (iv) the preservation of an historically important land area or a certified historic structure.

(B) **SPECIAL RULES WITH RESPECT TO BUILDINGS IN REGISTERED HISTORIC DISTRICTS.**—In the case of any contribution of a qualified real property interest which is a restriction with respect to the exterior of a building described in subparagraph (C)(ii), such contribution shall not be considered to be exclusively for conservation purposes unless—

- (i) such interest—
  - (I) includes a restriction which preserves the entire exterior of the building (including the front, sides, rear, and height of the building), and
  - (II) prohibits any change in the exterior of the building which is inconsistent with the historical character of such exterior,

(ii) the donor and donee enter into a written agreement certifying, under penalty of perjury, that the donee—

(I) is a qualified organization (as defined in paragraph (3)) with a purpose of environmental protection, land conservation, open space preservation, or historic preservation, and

(II) has the resources to manage and enforce the restriction and a commitment to do so, and

(iii) in the case of any contribution made in a taxable year beginning after the date of the enactment of this subparagraph, the taxpayer includes with the taxpayer's return for the taxable year of the contribution—

(I) a qualified appraisal (within the meaning of subsection (f)(11)(E)) of the qualified property interest,

(II) photographs of the entire exterior of the building, and

(III) a description of all restrictions on the development of the building.

(C) CERTIFIED HISTORIC STRUCTURE.—For purposes of subparagraph (A)(iv), the term “certified historic structure” means—

(i) any building, structure, or land area which is listed in the National Register, or

(ii) any building which is located in a registered historic district (as defined in section 47(c)(3)(B)) and is certified by the Secretary of the Interior to the Secretary as being of historic significance to the district.

A building, structure, or land area satisfies the preceding sentence if it satisfies such sentence either at the time of the transfer or on the due date (including extensions) for filing the transferor's return under this chapter for the taxable year in which the transfer is made.

(5) EXCLUSIVELY FOR CONSERVATION PURPOSES.—For purposes of this subsection—

(A) CONSERVATION PURPOSE MUST BE PROTECTED.—A contribution shall not be treated as exclusively for conservation purposes unless the conservation purpose is protected in perpetuity.

(B) NO SURFACE MINING PERMITTED.—

(i) IN GENERAL.—Except as provided in clause (ii), in the case of a contribution of any interest where there is a retention of a qualified mineral interest, subparagraph (A) shall not be treated as met if at any time there may be extraction or removal of minerals by any surface mining method.

(ii) SPECIAL RULE.—With respect to any contribution of property in which the ownership of the surface estate and mineral interests has been and remains separated, subparagraph (A) shall be treated as met if the probability of surface mining occurring on such property is so remote as to be negligible.



(6) QUALIFIED MINERAL INTEREST.—For purposes of this subsection, the term “qualified mineral interest” means—

- (A) subsurface oil, gas, or other minerals, and
- (B) the right to access to such minerals.

(i) STANDARD MILEAGE RATE FOR USE OF PASSENGER AUTOMOBILE.—For purposes of computing the deduction under this section for use of a passenger automobile, the standard mileage rate shall be 14 cents per mile.

(j) DENIAL OF DEDUCTION FOR CERTAIN TRAVEL EXPENSES.—No deduction shall be allowed under this section for traveling expenses (including amounts expended for meals and lodging) while away from home, whether paid directly or by reimbursement, unless there is no significant element of personal pleasure, recreation, or vacation in such travel.

(l) TREATMENT OF CERTAIN AMOUNTS PAID TO OR FOR THE BENEFIT OF INSTITUTIONS OF HIGHER EDUCATION.—

(1) IN GENERAL.—No deduction shall be allowed under this section for any amount described in paragraph (2).

(2) AMOUNT DESCRIBED.—For purposes of paragraph (1), an amount is described in this paragraph if—

(A) the amount is paid by the taxpayer to or for the benefit of an educational organization—

- (i) which is described in subsection (b)(1)(A)(ii), and
- (ii) which is an institution of higher education (as defined in section 3304(f)), and

(B) the taxpayer receives (directly or indirectly) as a result of paying such amount the right to purchase tickets for seating at an athletic event in an athletic stadium of such institution.

If any portion of a payment is for the purchase of such tickets, such portion and the remaining portion (if any) of such payment shall be treated as separate amounts for purposes of this subsection.

(m) CERTAIN DONEE INCOME FROM INTELLECTUAL PROPERTY TREATED AS AN ADDITIONAL CHARITABLE CONTRIBUTION.—

(1) TREATMENT AS ADDITIONAL CONTRIBUTION.—In the case of a taxpayer who makes a qualified intellectual property contribution, the deduction allowed under subsection (a) for each taxable year of the taxpayer ending on or after the date of such contribution shall be increased (subject to the limitations under subsection (b)) by the applicable percentage of qualified donee income with respect to such contribution which is properly allocable to such year under this subsection.

(2) REDUCTION IN ADDITIONAL DEDUCTIONS TO EXTENT OF INITIAL DEDUCTION.—With respect to any qualified intellectual property contribution, the deduction allowed under subsection (a) shall be increased under paragraph (1) only to the extent that the aggregate amount of such increases with respect to such contribution exceed the amount allowed as a deduction under subsection (a) with respect to such contribution determined without regard to this subsection.

(3) QUALIFIED DONEE INCOME.—For purposes of this subsection, the term “qualified donee income” means any net income received by or accrued to the donee which is properly allocable to the qualified intellectual property.

(4) **ALLOCATION OF QUALIFIED DONEE INCOME TO TAXABLE YEARS OF DONOR.**—For purposes of this subsection, qualified donee income shall be treated as properly allocable to a taxable year of the donor if such income is received by or accrued to the donee for the taxable year of the donee which ends within or with such taxable year of the donor.

(5) **10-YEAR LIMITATION.**—Income shall not be treated as properly allocable to qualified intellectual property for purposes of this subsection if such income is received by or accrued to the donee after the 10-year period beginning on the date of the contribution of such property.

(6) **BENEFIT LIMITED TO LIFE OF INTELLECTUAL PROPERTY.**—Income shall not be treated as properly allocable to qualified intellectual property for purposes of this subsection if such income is received by or accrued to the donee after the expiration of the legal life of such property.

(7) **APPLICABLE PERCENTAGE.**—For purposes of this subsection, the term “applicable percentage” means the percentage determined under the following table which corresponds to a taxable year of the donor ending on or after the date of the qualified intellectual property contribution:

| Taxable Year of Donor Ending on or After Date of Contribution: | Applicable Percentage: |
|--|------------------------|
| 1st.....   | 100                    |
| 2nd.....   | 100                    |
| 3rd.....   | 90                     |
| 4th.....   | 80                     |
| 5th.....   | 70                     |
| 6th.....   | 60                     |
| 7th.....   | 50                     |
| 8th.....   | 40                     |
| 9th.....   | 30                     |
| 10th.....  | 20                     |
| 11th.....  | 10                     |
| 12th.....  | 10                     |

(8) **QUALIFIED INTELLECTUAL PROPERTY CONTRIBUTION.**—For purposes of this subsection, the term “qualified intellectual property contribution” means any charitable contribution of qualified intellectual property—

(A) the amount of which taken into account under this section is reduced by reason of subsection (e)(1), and

(B) with respect to which the donor informs the donee at the time of such contribution that the donor intends to treat such contribution as a qualified intellectual property contribution for purposes of this subsection and section 6050L.

(9) **QUALIFIED INTELLECTUAL PROPERTY.**—For purposes of this subsection, the term “qualified intellectual property” means property described in subsection (e)(1)(B)(iii) (other than property contributed to or for the use of an organization described in subsection (e)(1)(B)(ii)).

(10) **OTHER SPECIAL RULES.**—

(A) **APPLICATION OF LIMITATIONS ON CHARITABLE CONTRIBUTIONS.**—Any increase under this subsection of the de-

duction provided under subsection (a) shall be treated for purposes of subsection (b) as a deduction which is attributable to a charitable contribution to the donee to which such increase relates.

(B) NET INCOME DETERMINED BY DONEE.—The net income taken into account under paragraph (3) shall not exceed the amount of such income reported under section 6050L(b)(1).

(C) DEDUCTION LIMITED TO 12 TAXABLE YEARS.—Except as may be provided under subparagraph (D)(i), this subsection shall not apply with respect to any qualified intellectual property contribution for any taxable year of the donor after the 12th taxable year of the donor which ends on or after the date of such contribution.

(D) REGULATIONS.—The Secretary may issue regulations or other guidance to carry out the purposes of this subsection, including regulations or guidance—

(i) modifying the application of this subsection in the case of a donor or donee with a short taxable year, and

(ii) providing for the determination of an amount to be treated as net income of the donee which is properly allocable to qualified intellectual property in the case of a donee who uses such property to further a purpose or function constituting the basis of the donee's exemption under section 501 (or, in the case of a governmental unit, any purpose described in section 170(c)) and does not possess a right to receive any payment from a third party with respect to such property.

(n) EXPENSES PAID BY CERTAIN WHALING CAPTAINS IN SUPPORT OF NATIVE ALASKAN SUBSISTENCE WHALING.—

(1) IN GENERAL.—In the case of an individual who is recognized by the Alaska Eskimo Whaling Commission as a whaling captain charged with the responsibility of maintaining and carrying out sanctioned whaling activities and who engages in such activities during the taxable year, the amount described in paragraph (2) (to the extent such amount does not exceed \$10,000 for the taxable year) shall be treated for purposes of this section as a charitable contribution.

(2) AMOUNT DESCRIBED.—

(A) IN GENERAL.—The amount described in this paragraph is the aggregate of the reasonable and necessary whaling expenses paid by the taxpayer during the taxable year in carrying out sanctioned whaling activities.

(B) WHALING EXPENSES.—For purposes of subparagraph (A), the term “whaling expenses” includes expenses for—

(i) the acquisition and maintenance of whaling boats, weapons, and gear used in sanctioned whaling activities,

(ii) the supplying of food for the crew and other provisions for carrying out such activities, and

(iii) storage and distribution of the catch from such activities.

(3) SANCTIONED WHALING ACTIVITIES.—For purposes of this subsection, the term “sanctioned whaling activities” means subsistence bowhead whale hunting activities conducted pursu-

ant to the management plan of the Alaska Eskimo Whaling Commission.

(4) SUBSTANTIATION OF EXPENSES.—The Secretary shall issue guidance requiring that the taxpayer substantiate the whaling expenses for which a deduction is claimed under this subsection, including by maintaining appropriate written records with respect to the time, place, date, amount, and nature of the expense, as well as the taxpayer's eligibility for such deduction, and that (to the extent provided by the Secretary) such substantiation be provided as part of the taxpayer's return of tax.

(o) SPECIAL RULES FOR FRACTIONAL GIFTS.—

(1) DENIAL OF DEDUCTION IN CERTAIN CASES.—

(A) IN GENERAL.—No deduction shall be allowed for a contribution of an undivided portion of a taxpayer's entire interest in tangible personal property unless all interests in the property are held immediately before such contribution by—

- (i) the taxpayer, or
- (ii) the taxpayer and the donee.

(B) EXCEPTIONS.—The Secretary may, by regulation, provide for exceptions to subparagraph (A) in cases where all persons who hold an interest in the property make proportional contributions of an undivided portion of the entire interest held by such persons.

(2) VALUATION OF SUBSEQUENT GIFTS.—In the case of any additional contribution, the fair market value of such contribution shall be determined by using the lesser of—

- (A) the fair market value of the property at the time of the initial fractional contribution, or
- (B) the fair market value of the property at the time of the additional contribution.

(3) RECAPTURE OF DEDUCTION IN CERTAIN CASES; ADDITION TO TAX.—

(A) RECAPTURE.—The Secretary shall provide for the recapture of the amount of any deduction allowed under this section (plus interest) with respect to any contribution of an undivided portion of a taxpayer's entire interest in tangible personal property—

- (i) in any case in which the donor does not contribute all of the remaining interests in such property to the donee (or, if such donee is no longer in existence, to any person described in section 170(c)) on or before the earlier of—

(I) the date that is 10 years after the date of the initial fractional contribution, or

(II) the date of the death of the donor, and (ii) in any case in which the donee has not, during the period beginning on the date of the initial fractional contribution and ending on the date described in clause (i)—

(I) had substantial physical possession of the property, and

(II) used the property in a use which is related to a purpose or function constituting the basis for the organizations' exemption under section 501.

(B) ADDITION TO TAX.—The tax imposed under this chapter for any taxable year for which there is a recapture under subparagraph (A) shall be increased by 10 percent of the amount so recaptured.

(4) DEFINITIONS.—For purposes of this subsection—

(A) ADDITIONAL CONTRIBUTION.—The term “additional contribution” means any charitable contribution by the taxpayer of any interest in property with respect to which the taxpayer has previously made an initial fractional contribution.

(B) INITIAL FRACTIONAL CONTRIBUTION.—The term “initial fractional contribution” means, with respect to any taxpayer, the first charitable contribution of an undivided portion of the taxpayer’s entire interest in any tangible personal property.

(p) OTHER CROSS REFERENCES.—

(1) For treatment of certain organizations providing child care, see section 501(k).

(2) For charitable contributions of estates and trusts, see section 642(c).

(3) For nondeductibility of contributions by common trust funds, see section 584.

(4) For charitable contributions of partners, see section 702.

(5) For charitable contributions of nonresident aliens, see section 873.

(6) For treatment of gifts for benefit of or use in connection with the Naval Academy as gifts to or for use of the United States, see section 6973 of title 10, United States Code.

(7) For treatment of gifts accepted by the Secretary of State, the Director of the International Communication Agency, or the Director of the United States International Development Cooperation Agency, as gifts to or for the use of the United States, see section 25 of the State Department Basic Authorities Act of 1956.

(8) For treatment of gifts of money accepted by the Attorney General for credit to the “Commissary Funds Federal Prisons” as gifts to or for the use of the United States, see section 4043 of title 18, United States Code.

(9) For charitable contributions to or for the use of Indian tribal governments (or their subdivisions), see section 7871.

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#### SEC. 172. NET OPERATING LOSS DEDUCTION.

(a) DEDUCTION ALLOWED.—There shall be allowed as a deduction for the taxable year an amount equal to the lesser of—

(1) the aggregate of the net operating loss carryovers to such year, plus the net operating loss carrybacks to such year, or

(2) 80 percent of taxable income computed without regard to the deduction allowable under this section.

For purposes of this subtitle, the term “net operating loss deduction” means the deduction allowed by this subsection.

(b) NET OPERATING LOSS CARRYBACKS AND CARRYOVERS.—

(1) YEARS TO WHICH LOSS MAY BE CARRIED.—

(A) GENERAL RULE.—Except as otherwise provided in this paragraph, a net operating loss for any taxable year—

(i) except as otherwise provided in this paragraph, shall not be a net operating loss carryback to any taxable year preceding the taxable year of such loss, and  
 (ii) shall be a net operating loss carryover to each taxable year following the taxable year of the loss.

(B) FARMING LOSSES.—

(i) IN GENERAL.—In the case of any portion of a net operating loss for the taxable year which is a farming loss with respect to the taxpayer, such loss shall be a net operating loss carryback to each of the 2 taxable years preceding the taxable year of such loss.

(ii) FARMING LOSS.—For purposes of this section, the term “farming loss” means the lesser of—

(I) the amount which would be the net operating loss for the taxable year if only income and deductions attributable to farming businesses (as defined in section 263A(e)(4)) are taken into account, or

(II) the amount of the net operating loss for such taxable year.

(iii) COORDINATION WITH PARAGRAPH (2).—For purposes of applying paragraph (2), a farming loss for any taxable year shall be treated as a separate net operating loss for such taxable year to be taken into account after the remaining portion of the net operating loss for such taxable year.

(iv) ELECTION.—Any taxpayer entitled to a 2-year carryback under clause (i) from any loss year may elect not to have such clause apply to such loss year. Such election shall be made in such manner as prescribed by the Secretary and shall be made by the due date (including extensions of time) for filing the taxpayer’s return for the taxable year of the net operating loss. Such election, once made for any taxable year, shall be irrevocable for such taxable year.

(C) INSURANCE COMPANIES.—In the case of an insurance company (as defined in section 816(a)) other than a life insurance company, the net operating loss for any taxable year—

(i) shall be a net operating loss carryback to each of the 2 taxable years preceding the taxable year of such loss, and

(ii) shall be a net operating loss carryover to each of the 20 taxable years following the taxable year of the loss.

(2) AMOUNT OF CARRYBACKS AND CARRYOVERS.—The entire amount of the net operating loss for any taxable year (hereinafter in this section referred to as the “loss year”) shall be carried to the earliest of the taxable years to which (by reason of paragraph (1)) such loss may be carried. The portion of such loss which shall be carried to each of the other taxable years shall be the excess, if any, of the amount of such loss over the sum of the taxable income for each of the prior taxable years to which such loss may be carried. For purposes of the pre-

ceding sentence, the taxable income for any such prior taxable year shall—

(A) be computed with the modifications specified in subsection (d) other than paragraphs (1), (4), and (5) thereof, and by determining the amount of the net operating loss deduction without regard to the net operating loss for the loss year or for any taxable year thereafter,

(B) not be considered to be less than zero, and

(C) not exceed the amount determined under subsection (a)(2) for such prior taxable year.

(3) ELECTION TO WAIVE CARRYBACK.—Any taxpayer entitled to a carryback period under paragraph (1) may elect to relinquish the entire carryback period with respect to a net operating loss for any taxable year. Such election shall be made in such manner as may be prescribed by the Secretary, and shall be made by the due date (including extensions of time) for filing the taxpayer's return for the taxable year of the net operating loss for which the election is to be in effect. Such election, once made for any taxable year, shall be irrevocable for such taxable year.

(c) NET OPERATING LOSS DEFINED.—For purposes of this section, the term “net operating loss” means the excess of the deductions allowed by this chapter over the gross income. Such excess shall be computed with the modifications specified in subsection (d).

(d) MODIFICATIONS.—The modifications referred to in this section are as follows:

(1) NET OPERATING LOSS DEDUCTION.—No net operating loss deduction shall be allowed.

(2) CAPITAL GAINS AND LOSSES OF TAXPAYERS OTHER THAN CORPORATIONS.—In the case of a taxpayer other than a corporation—

(A) the amount deductible on account of losses from sales or exchanges of capital assets shall not exceed the amount includable on account of gains from sales or exchanges of capital assets; and

(B) the exclusion provided by section 1202 shall not be allowed.

[(3) DEDUCTION FOR PERSONAL EXEMPTIONS.—No deduction shall be allowed under section 151 (relating to personal exemptions). No deduction in lieu of any such deduction shall be allowed.]

(4) NONBUSINESS DEDUCTIONS OF TAXPAYERS OTHER THAN CORPORATIONS.—In the case of a taxpayer other than a corporation, the deductions allowable by this chapter which are not attributable to a taxpayer's trade or business shall be allowed only to the extent of the amount of the gross income not derived from such trade or business. For purposes of the preceding sentence—

(A) any gain or loss from the sale or other disposition of—

(i) property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 167, or

(ii) real property used in the trade or business, shall be treated as attributable to the trade or business;

(B) the modifications specified in paragraphs (1), (2)(B), and (3) shall be taken into account;

(C) any deduction for casualty or theft losses allowable under paragraph (2) or (3) of section 165(c) shall be treated as attributable to the trade or business; and

(D) any deduction allowed under section 404 to the extent attributable to contributions which are made on behalf of an individual who is an employee within the meaning of section 401(c)(1) shall not be treated as attributable to the trade or business of such individual.

(5) COMPUTATION OF DEDUCTION FOR DIVIDENDS RECEIVED.—The deductions allowed by sections 243 (relating to dividends received by corporations) and 245 (relating to dividends received from certain foreign corporations) shall be computed without regard to section 246(b) (relating to limitation on aggregate amount of deductions).

(6) MODIFICATIONS RELATED TO REAL ESTATE INVESTMENT TRUSTS.—In the case of any taxable year for which part II of subchapter M (relating to real estate investment trusts) applies to the taxpayer—

(A) the net operating loss for such taxable year shall be computed by taking into account the adjustments described in section 857(b)(2) (other than the deduction for dividends paid described in section 857(b)(2)(B));

(B) where such taxable year is a “prior taxable year” referred to in paragraph (2) of subsection (b), the term “taxable income” in such paragraph shall mean “real estate investment trust taxable income” (as defined in section 857(b)(2)); and

(C) subsection (a)(2) shall be applied by substituting “real estate investment trust taxable income (as defined in section 857(b)(2) but without regard to the deduction for dividends paid (as defined in section 561))” for “taxable income”.

(8) QUALIFIED BUSINESS INCOME DEDUCTION.—Any deduction under section 199A shall not be allowed.

(9) DEDUCTION FOR FOREIGN-DERIVED INTANGIBLE INCOME.—The deduction under section 250 shall not be allowed.

(e) LAW APPLICABLE TO COMPUTATIONS.—In determining the amount of any net operating loss carryback or carryover to any taxable year, the necessary computations involving any other taxable year shall be made under the law applicable to such other taxable year.

(f) SPECIAL RULE FOR INSURANCE COMPANIES.—In the case of an insurance company (as defined in section 816(a)) other than a life insurance company—

(1) the amount of the deduction allowed under subsection (a) shall be the aggregate of the net operating loss carryovers to such year, plus the net operating loss carrybacks to such year, and

(2) subparagraph (C) of subsection (b)(2) shall not apply.

(g) CROSS REFERENCES.—

(1) For treatment of net operating loss carryovers in certain corporate acquisitions, see section 381.



(2) For special limitation on net operating loss carryovers in case of a corporate change of ownership, see section 382.

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## Subchapter B—Computation of Taxable Income

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### PART VI—ITEMIZED DEDUCTIONS FOR INDIVIDUALS AND CORPORATIONS

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#### SEC. 199A. QUALIFIED BUSINESS INCOME.

(a) ALLOWANCE OF DEDUCTION.—In the case of a taxpayer other than a corporation, there shall be allowed as a deduction for any taxable year an amount equal to the lesser of—

(1) the combined qualified business income amount of the taxpayer, or

(2) an amount equal to 20 percent of the excess (if any) of—

(A) the taxable income of the taxpayer for the taxable year, over

(B) the net capital gain (as defined in section 1(h)) of the taxpayer for such taxable year.

(b) COMBINED QUALIFIED BUSINESS INCOME AMOUNT.—For purposes of this section—

(1) IN GENERAL.—The term “combined qualified business income amount” means, with respect to any taxable year, an amount equal to—

(A) the sum of the amounts determined under paragraph (2) for each qualified trade or business carried on by the taxpayer, plus

(B) 20 percent of the aggregate amount of the qualified REIT dividends and qualified publicly traded partnership income of the taxpayer for the taxable year.

(2) DETERMINATION OF DEDUCTIBLE AMOUNT FOR EACH TRADE OR BUSINESS.—The amount determined under this paragraph with respect to any qualified trade or business is the lesser of—

(A) 20 percent of the taxpayer’s qualified business income with respect to the qualified trade or business, or

(B) the greater of—

(i) 50 percent of the W-2 wages with respect to the qualified trade or business, or

(ii) the sum of 25 percent of the W-2 wages with respect to the qualified trade or business, plus 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property.

(3) MODIFICATIONS TO LIMIT BASED ON TAXABLE INCOME.—

(A) EXCEPTION FROM LIMIT.—In the case of any taxpayer whose taxable income for the taxable year does not exceed the threshold amount, paragraph (2) shall be applied without regard to subparagraph (B).

(B) PHASE-IN OF LIMIT FOR CERTAIN TAXPAYERS.—

(i) IN GENERAL.—If—

(I) the taxable income of a taxpayer for any taxable year exceeds the threshold amount, but does not exceed the sum of the threshold amount plus \$50,000 (\$100,000 in the case of a joint return), and

(II) the amount determined under paragraph (2)(B) (determined without regard to this subparagraph) with respect to any qualified trade or business carried on by the taxpayer is less than the amount determined under paragraph (2)(A) with respect to such trade or business, then paragraph (2) shall be applied with respect to such trade or business without regard to subparagraph (B) thereof and by reducing the amount determined under subparagraph (A) thereof by the amount determined under clause (ii).

(ii) AMOUNT OF REDUCTION.—The amount determined under this subparagraph is the amount which bears the same ratio to the excess amount as—

(I) the amount by which the taxpayer's taxable income for the taxable year exceeds the threshold amount, bears to

(II) \$50,000 (\$100,000 in the case of a joint return).

(iii) EXCESS AMOUNT.—For purposes of clause (ii), the excess amount is the excess of—

(I) the amount determined under paragraph (2)(A) (determined without regard to this paragraph), over

(II) the amount determined under paragraph (2)(B) (determined without regard to this paragraph).

(4) Wages, etc.

(A) IN GENERAL.—The term “W-2 wages” means, with respect to any person for any taxable year of such person, the amounts described in paragraphs (3) and (8) of section 6051(a) paid by such person with respect to employment of employees by such person during the calendar year ending during such taxable year.

(B) LIMITATION TO WAGES ATTRIBUTABLE TO QUALIFIED BUSINESS INCOME.—Such term shall not include any amount which is not properly allocable to qualified business income for purposes of subsection (c)(1).

(C) RETURN REQUIREMENT.—Such term shall not include any amount which is not properly included in a return filed with the Social Security Administration on or before the 60th day after the due date (including extensions) for such return.

(5) ACQUISITIONS, DISPOSITIONS, AND SHORT TAXABLE YEARS.—The Secretary shall provide for the application of this subsection in cases of a short taxable year or where the taxpayer acquires, or disposes of, the major portion of a trade or business or the major portion of a separate unit of a trade or business during the taxable year.

(6) QUALIFIED PROPERTY.—For purposes of this section:

(A) IN GENERAL.—The term “qualified property” means, with respect to any qualified trade or business for a taxable year, tangible property of a character subject to the allowance for depreciation under section 167—

(i) which is held by, and available for use in, the qualified trade or business at the close of the taxable year,

(ii) which is used at any point during the taxable year in the production of qualified business income, and

(iii) the depreciable period for which has not ended before the close of the taxable year.

(B) DEPRECIABLE PERIOD.—The term “depreciable period” means, with respect to qualified property of a taxpayer, the period beginning on the date the property was first placed in service by the taxpayer and ending on the later of—

(i) the date that is 10 years after such date, or

(ii) the last day of the last full year in the applicable recovery period that would apply to the property under section 168 (determined without regard to subsection (g) thereof).

(7) SPECIAL RULE WITH RESPECT TO INCOME RECEIVED FROM COOPERATIVES.—In the case of any qualified trade or business of a patron of a specified agricultural or horticultural cooperative, the amount determined under paragraph (2) with respect to such trade or business shall be reduced by the lesser of—

(A) 9 percent of so much of the qualified business income with respect to such trade or business as is properly allocable to qualified payments received from such cooperative, or

(B) 50 percent of so much of the W-2 wages with respect to such trade or business as are so allocable.

(c) QUALIFIED BUSINESS INCOME.—For purposes of this section—

(1) IN GENERAL.—The term “qualified business income” means, for any taxable year, the net amount of qualified items of income, gain, deduction, and loss with respect to any qualified trade or business of the taxpayer. Such term shall not include any qualified REIT dividends, or qualified publicly traded partnership income.

(2) CARRYOVER OF LOSSES.—If the net amount of qualified income, gain, deduction, and loss with respect to qualified trades or businesses of the taxpayer for any taxable year is less than zero, such amount shall be treated as a loss from a qualified trade or business in the succeeding taxable year.

(3) QUALIFIED ITEMS OF INCOME, GAIN, DEDUCTION, AND LOSS.—For purposes of this subsection—

(A) IN GENERAL.—The term “qualified items of income, gain, deduction, and loss” means items of income, gain, deduction, and loss to the extent such items are—

(i) effectively connected with the conduct of a trade or business within the United States (within the meaning of section 864(c), determined by substituting “qualified trade or business (within the meaning of section 199A)” for “nonresident alien individual or a

foreign corporation” or for “a foreign corporation” each place it appears), and

(ii) included or allowed in determining taxable income for the taxable year.

(B) EXCEPTIONS.—The following items shall not be taken into account as a qualified item of income, gain, deduction, or loss:

(i) Any item of short-term capital gain, short-term capital loss, long-term capital gain, or long-term capital loss.

(ii) Any dividend, income equivalent to a dividend, or payment in lieu of dividends described in section 954(c)(1)(G). Any amount described in section 1385(a)(1) shall not be treated as described in this clause.

(iii) Any interest income other than interest income which is properly allocable to a trade or business.

(iv) Any item of gain or loss described in subparagraph (C) or (D) of section 954(c)(1) (applied by substituting “qualified trade or business” for “controlled foreign corporation”).

(v) Any item of income, gain, deduction, or loss taken into account under section 954(c)(1)(F) (determined without regard to clause (ii) thereof and other than items attributable to notional principal contracts entered into in transactions qualifying under section 1221(a)(7)).

(vi) Any amount received from an annuity which is not received in connection with the trade or business.

(vii) Any item of deduction or loss properly allocable to an amount described in any of the preceding clauses.

(4) TREATMENT OF REASONABLE COMPENSATION AND GUARANTEED PAYMENTS.—Qualified business income shall not include—

(A) reasonable compensation paid to the taxpayer by any qualified trade or business of the taxpayer for services rendered with respect to the trade or business,

(B) any guaranteed payment described in section 707(c) paid to a partner for services rendered with respect to the trade or business, and

(C) to the extent provided in regulations, any payment described in section 707(a) to a partner for services rendered with respect to the trade or business.

(d) QUALIFIED TRADE OR BUSINESS.—For purposes of this section—

(1) IN GENERAL.—The term “qualified trade or business” means any trade or business other than—

(A) a specified service trade or business, or

(B) the trade or business of performing services as an employee.

(2) SPECIFIED SERVICE TRADE OR BUSINESS.—The term “specified service trade or business” means any trade or business—

(A) which is described in section 1202(e)(3)(A) (applied without regard to the words “engineering, architecture,”)

or which would be so described if the term “employees or owners” were substituted for “employees” therein, or

(B) which involves the performance of services that consist of investing and investment management, trading, or dealing in securities (as defined in section 475(c)(2)), partnership interests, or commodities (as defined in section 475(e)(2)).

(3) EXCEPTION FOR SPECIFIED SERVICE BUSINESSES BASED ON TAXPAYER’S INCOME.—

(A) IN GENERAL.—If, for any taxable year, the taxable income of any taxpayer is less than the sum of the threshold amount plus \$50,000 (\$100,000 in the case of a joint return), then—

(i) any specified service trade or business of the taxpayer shall not fail to be treated as a qualified trade or business due to paragraph (1)(A), but

(ii) only the applicable percentage of qualified items of income, gain, deduction, or loss, and the W-2 wages and the unadjusted basis immediately after acquisition of qualified property, of the taxpayer allocable to such specified service trade or business shall be taken into account in computing the qualified business income, W-2 wages, and the unadjusted basis immediately after acquisition of qualified property of the taxpayer for the taxable year for purposes of applying this section.

(B) APPLICABLE PERCENTAGE.—For purposes of subparagraph (A), the term “applicable percentage” means, with respect to any taxable year, 100 percent reduced (not below zero) by the percentage equal to the ratio of—

(i) the taxable income of the taxpayer for the taxable year in excess of the threshold amount, bears to

(ii) \$50,000 (\$100,000 in the case of a joint return).

(e) OTHER DEFINITIONS.—For purposes of this section—

(1) TAXABLE INCOME.—Except as otherwise provided in subsection (g)(2)(B), taxable income shall be computed without regard to any deduction allowable under this section.

(2) THRESHOLD AMOUNT.—

(A) IN GENERAL.—The term “threshold amount” means \$157,500 (200 percent of such amount in the case of a joint return).

(B) INFLATION ADJUSTMENT.—In the case of any taxable year beginning after 2018, the dollar amount in subparagraph (A) shall be increased by an amount equal to—

(i) such dollar amount, multiplied by

(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2017” for “calendar year 2016” in subparagraph (A)(ii) thereof.

The amount of any increase under the preceding sentence shall be rounded as provided in section 1(f)(7).

(3) QUALIFIED REIT DIVIDEND.—The term “qualified REIT dividend” means any dividend from a real estate investment trust received during the taxable year which—

(A) is not a capital gain dividend, as defined in section 857(b)(3), and

(B) is not qualified dividend income, as defined in section 1(h)(11).

(4) QUALIFIED PUBLICLY TRADED PARTNERSHIP INCOME.—The term “qualified publicly traded partnership income” means, with respect to any qualified trade or business of a taxpayer, the sum of—

(A) the net amount of such taxpayer’s allocable share of each qualified item of income, gain, deduction, and loss (as defined in subsection (c)(3) and determined after the application of subsection (c)(4)) from a publicly traded partnership (as defined in section 7704(a)) which is not treated as a corporation under section 7704(c), plus

(B) any gain recognized by such taxpayer upon disposition of its interest in such partnership to the extent such gain is treated as an amount realized from the sale or exchange of property other than a capital asset under section 751(a).

(f) SPECIAL RULES.—

(1) APPLICATION TO PARTNERSHIPS AND S CORPORATIONS.—

(A) IN GENERAL.—In the case of a partnership or S corporation—

(i) this section shall be applied at the partner or shareholder level,

(ii) each partner or shareholder shall take into account such person’s allocable share of each qualified item of income, gain, deduction, and loss, and

(iii) each partner or shareholder shall be treated for purposes of subsection (b) as having W-2 wages and unadjusted basis immediately after acquisition of qualified property for the taxable year in an amount equal to such person’s allocable share of the W-2 wages and the unadjusted basis immediately after acquisition of qualified property of the partnership or S corporation for the taxable year (as determined under regulations prescribed by the Secretary).

For purposes of clause (iii), a partner’s or shareholder’s allocable share of W-2 wages shall be determined in the same manner as the partner’s or shareholder’s allocable share of wage expenses. For purposes of such clause, partner’s or shareholder’s allocable share of the unadjusted basis immediately after acquisition of qualified property shall be determined in the same manner as the partner’s or shareholder’s allocable share of depreciation. For purposes of this subparagraph, in the case of an S corporation, an allocable share shall be the shareholder’s pro rata share of an item.

(B) APPLICATION TO TRUSTS AND ESTATES.—Rules similar to the rules under section 199(d)(1)(B)(i) (as in effect on December 1, 2017) for the apportionment of W-2 wages shall apply to the apportionment of W-2 wages and the apportionment of unadjusted basis immediately after acquisition of qualified property under this section.

## (C) TREATMENT OF TRADES OR BUSINESS IN PUERTO RICO.—

(i) IN GENERAL.—In the case of any taxpayer with qualified business income from sources within the commonwealth of Puerto Rico, if all such income is taxable under section 1 for such taxable year, then for purposes of determining the qualified business income of such taxpayer for such taxable year, the term “United States” shall include the Commonwealth of Puerto Rico.

(ii) SPECIAL RULE FOR APPLYING LIMIT.—In the case of any taxpayer described in clause (i), the determination of W-2 wages of such taxpayer with respect to any qualified trade or business conducted in Puerto Rico shall be made without regard to any exclusion under section 3401(a)(8) for remuneration paid for services in Puerto Rico.

(2) COORDINATION WITH MINIMUM TAX.—For purposes of determining alternative minimum taxable income under section 55, qualified business income shall be determined without regard to any adjustments under sections 56 through 59.

(3) DEDUCTION LIMITED TO INCOME TAXES.—The deduction under subsection (a) shall only be allowed for purposes of this chapter.

(4) REGULATIONS.—The Secretary shall prescribe such regulations as are necessary to carry out the purposes of this section, including regulations—

(A) for requiring or restricting the allocation of items and wages under this section and such reporting requirements as the Secretary determines appropriate, and

(B) for the application of this section in the case of tiered entities.

(g) DEDUCTION FOR INCOME ATTRIBUTABLE TO DOMESTIC PRODUCTION ACTIVITIES OF SPECIFIED AGRICULTURAL OR HORTICULTURAL COOPERATIVES.—

(1) ALLOWANCE OF DEDUCTION.—

(A) IN GENERAL.—In the case of a taxpayer which is a specified agricultural or horticultural cooperative, there shall be allowed as a deduction an amount equal to 9 percent of the lesser of—

(i) the qualified production activities income of the taxpayer for the taxable year, or

(ii) the taxable income of the taxpayer for the taxable year.

(B) LIMITATION.—

(i) IN GENERAL.—The deduction allowable under subparagraph (A) for any taxable year shall not exceed 50 percent of the W-2 wages of the taxpayer for the taxable year.

(ii) W-2 WAGES.—For purposes of this subparagraph, the W-2 wages of the taxpayer shall be determined in the same manner as under subsection (b)(4) (without regard to subparagraph (B) thereof and after application of subsection (b)(5)), except that such wages shall not include any amount which is not properly allocable

to domestic production gross receipts for purposes of paragraph (3)(A).

(C) TAXABLE INCOME OF COOPERATIVES DETERMINED WITHOUT REGARD TO CERTAIN DEDUCTIONS.—For purposes of this subsection, the taxable income of a specified agricultural or horticultural cooperative shall be computed without regard to any deduction allowable under subsection (b) or (c) of section 1382 (relating to patronage dividends, per-unit retain allocations, and nonpatronage distributions).

(2) DEDUCTION ALLOWED TO PATRONS.—

(A) IN GENERAL.—In the case of any eligible taxpayer who receives a qualified payment from a specified agricultural or horticultural cooperative, there shall be allowed as a deduction for the taxable year in which such payment is received an amount equal to the portion of the deduction allowed under paragraph (1) to such cooperative which is—

(i) allowed with respect to the portion of the qualified production activities income to which such payment is attributable, and

(ii) identified by such cooperative in a written notice mailed to such taxpayer during the payment period described in section 1382(d).

(B) LIMITATION BASED ON TAXABLE INCOME.—The deduction allowed to any taxpayer under this paragraph shall not exceed the taxable income of the taxpayer determined without regard to the deduction allowed under this paragraph and after taking into account any deduction allowed to the taxpayer under subsection (a) for the taxable year.

(C) COOPERATIVE DENIED DEDUCTION FOR PORTION OF QUALIFIED PAYMENTS.—The taxable income of a specified agricultural or horticultural cooperative shall not be reduced under section 1382 by reason of that portion of any qualified payment as does not exceed the deduction allowable under subparagraph (A) with respect to such payment.

(D) ELIGIBLE TAXPAYER.—For purposes of this paragraph, the term “eligible taxpayer” means—

(i) a taxpayer other than a corporation, or

(ii) a specified agricultural or horticultural cooperative.

(E) QUALIFIED PAYMENT.—For purposes of this section, the term “qualified payment” means, with respect to any eligible taxpayer, any amount which—

(i) is described in paragraph (1) or (3) of section 1385(a),

(ii) is received by such taxpayer from a specified agricultural or horticultural cooperative, and

(iii) is attributable to qualified production activities income with respect to which a deduction is allowed to such cooperative under paragraph (1).

(3) QUALIFIED PRODUCTION ACTIVITIES INCOME.—For purposes of this subsection—



(A) IN GENERAL.—The term “qualified production activities income” for any taxable year means an amount equal to the excess (if any) of—

(i) the taxpayer’s domestic production gross receipts for such taxable year, over

(ii) the sum of—

(I) the cost of goods sold that are allocable to such receipts, and

(II) other expenses, losses, or deductions (other than the deduction allowed under this subsection), which are properly allocable to such receipts.

(B) ALLOCATION METHOD.—The Secretary shall prescribe rules for the proper allocation of items described in subparagraph (A) for purposes of determining qualified production activities income. Such rules shall provide for the proper allocation of items whether or not such items are directly allocable to domestic production gross receipts.

(C) SPECIAL RULES FOR DETERMINING COSTS.—

(i) IN GENERAL.—For purposes of determining costs under subclause (I) of subparagraph (A)(ii), any item or service brought into the United States shall be treated as acquired by purchase, and its cost shall be treated as not less than its value immediately after it entered the United States. A similar rule shall apply in determining the adjusted basis of leased or rented property where the lease or rental gives rise to domestic production gross receipts.

(ii) EXPORTS FOR FURTHER MANUFACTURE.—In the case of any property described in clause (i) that had been exported by the taxpayer for further manufacture, the increase in cost or adjusted basis under clause (i) shall not exceed the difference between the value of the property when exported and the value of the property when brought back into the United States after the further manufacture.

(D) DOMESTIC PRODUCTION GROSS RECEIPTS.—

(i) IN GENERAL.—The term “domestic production gross receipts” means the gross receipts of the taxpayer which are derived from any lease, rental, license, sale, exchange, or other disposition of any agricultural or horticultural product which was manufactured, produced, grown, or extracted by the taxpayer (determined after the application of paragraph (4)(B)) in whole or significant part within the United States. Such term shall not include gross receipts of the taxpayer which are derived from the lease, rental, license, sale, exchange, or other disposition of land.

(ii) RELATED PERSONS.—

(I) IN GENERAL.—The term “domestic production gross receipts” shall not include any gross receipts of the taxpayer derived from property leased, licensed, or rented by the taxpayer for use by any related person.

(II) RELATED PERSON.—For purposes of subclause (I), a person shall be treated as related to

another person if such persons are treated as a single employer under subsection (a) or (b) of section 52 or subsection (m) or (o) of section 414, except that determinations under subsections (a) and (b) of section 52 shall be made without regard to section 1563(b).

(4) SPECIFIED AGRICULTURAL OR HORTICULTURAL COOPERATIVE.—For purposes of this section—

(A) IN GENERAL.—The term “specified agricultural or horticultural cooperative” means an organization to which part I of subchapter T applies which is engaged—

(i) in the manufacturing, production, growth, or extraction in whole or significant part of any agricultural or horticultural product, or

(ii) in the marketing of agricultural or horticultural products.

(B) APPLICATION TO MARKETING COOPERATIVES.—A specified agricultural or horticultural cooperative described in subparagraph (A)(ii) shall be treated as having manufactured, produced, grown, or extracted in whole or significant part any agricultural or horticultural product marketed by the specified agricultural or horticultural cooperative which its patrons have so manufactured, produced, grown, or extracted.

(5) DEFINITIONS AND SPECIAL RULES.—

(A) SPECIAL RULE FOR AFFILIATED GROUPS.—

(i) IN GENERAL.—All members of an expanded affiliated group shall be treated as a single corporation for purposes of this subsection.

(ii) PARTNERSHIPS OWNED BY EXPANDED AFFILIATED GROUPS.—For purposes of paragraph (3)(D), if all of the interests in the capital and profits of a partnership are owned by members of a single expanded affiliated group at all times during the taxable year of such partnership, the partnership and all members of such group shall be treated as a single taxpayer during such period.

(iii) EXPANDED AFFILIATED GROUP.—For purposes of this subsection, the term “expanded affiliated group” means an affiliated group as defined in section 1504(a), determined—

(I) by substituting “more than 50 percent” for “at least 80 percent” each place it appears, and

(II) without regard to paragraphs (2) and (4) of section 1504(b).

(iv) ALLOCATION OF DEDUCTION.—Except as provided in regulations, the deduction under paragraph (1) shall be allocated among the members of the expanded affiliated group in proportion to each member’s respective amount (if any) of qualified production activities income.

(B) SPECIAL RULE FOR COOPERATIVE PARTNERS.—In the case of a specified agricultural or horticultural cooperative which is a partner in a partnership, rules similar to the

rules of subsection (f)(1) shall apply for purposes of this subsection.

(C) **TRADE OR BUSINESS REQUIREMENT.**—This subsection shall be applied by only taking into account items which are attributable to the actual conduct of a trade or business.

(D) **UNRELATED BUSINESS TAXABLE INCOME.**—For purposes of determining the tax imposed by section 511, this section shall be applied by substituting “unrelated business taxable income” for “taxable income” each place it appears in this section (other than this subparagraph).

(E) **SPECIAL RULE FOR COOPERATIVE WITH OIL RELATED QUALIFIED PRODUCTION ACTIVITIES INCOME.**—

(i) **IN GENERAL.**—If a specified agricultural or horticultural cooperative has oil related qualified production activities income for any taxable year, the amount otherwise allowable as a deduction under paragraph (1) shall be reduced by 3 percent of the least of—

(I) the oil related qualified production activities income of the cooperative for the taxable year,

(II) the qualified production activities income of the cooperative for the taxable year, or

(III) taxable income.

(ii) **OIL RELATED QUALIFIED PRODUCTION ACTIVITIES INCOME.**—For purposes of this subparagraph, the term “oil related qualified production activities income” means for any taxable year the qualified production activities income which is attributable to the production, refining, processing, transportation, or distribution of oil, gas, or any primary product thereof (within the meaning of section 927(a)(2)(C), as in effect before its repeal) during such taxable year.

(6) **REGULATIONS.**—The Secretary shall prescribe such regulations as are necessary to carry out the purposes of this subsection, including regulations which prevent more than 1 taxpayer from being allowed a deduction under this subsection with respect to any activity described in paragraph (3)(D)(i). Such regulations shall be based on the regulations applicable to cooperatives and their patrons under section 199 (as in effect before its repeal).

(h) **ANTI-ABUSE RULES.**—The Secretary shall—

(1) apply rules similar to the rules under section 179(d)(2) in order to prevent the manipulation of the depreciable period of qualified property using transactions between related parties, and

(2) prescribe rules for determining the unadjusted basis immediately after acquisition of qualified property acquired in like-kind exchanges or involuntary conversions.

[(i) **TERMINATION.**—This section shall not apply to taxable years beginning after December 31, 2025.]

**PART VII—ADDITIONAL ITEMIZED DEDUCTIONS FOR  
INDIVIDUALS**

Sec. 211. Allowance of deductions.

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**【Sec. 217. Moving expenses.】**

*Sec. 217. Certain moving expenses of members of Armed Forces.*

\* \* \* \* \*

**SEC. 213. MEDICAL, DENTAL, ETC., EXPENSES.**

(a) **ALLOWANCE OF DEDUCTION.**—There shall be allowed as a deduction the expenses paid during the taxable year, not compensated for by insurance or otherwise, for medical care of the taxpayer, his spouse, or a dependent (as defined in **【section 152】** *section 7706*, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof), to the extent that such expenses exceed 10 percent (7.5 percent in the case of any taxable year beginning after December 31, 2018, and ending before January 1, 2021) of adjusted gross income.

(b) **LIMITATION WITH RESPECT TO MEDICINE AND DRUGS.**—An amount paid during the taxable year for medicine or a drug shall be taken into account under subsection (a) only if such medicine or drug is a prescribed drug or is insulin.

(c) **SPECIAL RULE FOR DECEDENTS.**—

(1) **TREATMENT OF EXPENSES PAID AFTER DEATH.**—For purposes of subsection (a), expenses for the medical care of the taxpayer which are paid out of his estate during the 1-year period beginning with the day after the date of his death shall be treated as paid by the taxpayer at the time incurred.

(2) **LIMITATION.**—Paragraph (1) shall not apply if the amount paid is allowable under section 2053 as a deduction in computing the taxable estate of the decedent, but this paragraph shall not apply if (within the time and in the manner and form prescribed by the Secretary) there is filed—

(A) a statement that such amount has not been allowed as a deduction under section 2053, and

(B) a waiver of the right to have such amount allowed at any time as a deduction under section 2053.

(d) **DEFINITIONS.**—For purposes of this section—

(1) The term “medical care” means amounts paid—

(A) for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body,

(B) for transportation primarily for and essential to medical care referred to in subparagraph (A),

(C) for qualified long-term care services (as defined in section 7702B(c)), or

(D) for insurance (including amounts paid as premiums under part B of title XVIII of the Social Security Act, relating to supplementary medical insurance for the aged) covering medical care referred to in subparagraphs (A) and (B) or for any qualified long-term care insurance contract (as defined in section 7702B(b)).

In the case of a qualified long-term care insurance contract (as defined in section 7702B(b)), only eligible long-term care pre-

miums (as defined in paragraph (10)) shall be taken into account under subparagraph (D).

(2) Amounts paid for certain lodging away from home treated as paid for medical care

Amounts paid for lodging (not lavish or extravagant under the circumstances) while away from home primarily for and essential to medical care referred to in paragraph (1)(A) shall be treated as amounts paid for medical care if—

(A) the medical care referred to in paragraph (1)(A) is provided by a physician in a licensed hospital (or in a medical care facility which is related to, or the equivalent of, a licensed hospital), and

(B) there is no significant element of personal pleasure, recreation, or vacation in the travel away from home.

The amount taken into account under the preceding sentence shall not exceed \$50 for each night for each individual.

(3) Prescribed drug

The term “prescribed drug” means a drug or biological which requires a prescription of a physician for its use by an individual.

(4) Physician

The term “physician” has the meaning given to such term by section 1861(r) of the Social Security Act (42 U.S.C. 1395x(r)).

(5) Special rule in the case of child of divorced parents, etc.

Any child to whom [section 152(e)] *section 7706(e)* applies shall be treated as a dependent of both parents for purposes of this section.

(6) In the case of an insurance contract under which amounts are payable for other than medical care referred to in subparagraphs (A), (B), and (C) of paragraph (1)—

(A) no amount shall be treated as paid for insurance to which paragraph (1)(D) applies unless the charge for such insurance is either separately stated in the contract, or furnished to the policyholder by the insurance company in a separate statement,

(B) the amount taken into account as the amount paid for such insurance shall not exceed such charge, and

(C) no amount shall be treated as paid for such insurance if the amount specified in the contract (or furnished to the policyholder by the insurance company in a separate statement) as the charge for such insurance is unreasonably large in relation to the total charges under the contract.

(7) Subject to the limitations of paragraph (6), premiums paid during the taxable year by a taxpayer before he attains the age of 65 for insurance covering medical care (within the meaning of subparagraphs (A), (B), and (C) of paragraph (1)) for the taxpayer, his spouse, or a dependent after the taxpayer attains the age of 65 shall be treated as expenses paid during the taxable year for insurance which constitutes medical care if premiums for such insurance are payable (on a level payment basis) under the contract for a period of 10 years or more or until the year in which the taxpayer attains the age of 65 (but in no case for a period of less than 5 years).

(8) The determination of whether an individual is married at any time during the taxable year shall be made in accordance with the provisions of section 6013(d) (relating to determination of status as husband and wife).

(9) COSMETIC SURGERY.—

(A) IN GENERAL.—The term “medical care” does not include cosmetic surgery or other similar procedures, unless the surgery or procedure is necessary to ameliorate a deformity arising from, or directly related to, a congenital abnormality, a personal injury resulting from an accident or trauma, or disfiguring disease.

(B) COSMETIC SURGERY DEFINED.—For purposes of this paragraph, the term “cosmetic surgery” means any procedure which is directed at improving the patient’s appearance and does not meaningfully promote the proper function of the body or prevent or treat illness or disease.

(10) ELIGIBLE LONG-TERM CARE PREMIUMS.—

(A) IN GENERAL.—For purposes of this section, the term “eligible long-term care Premiums” means the amount paid during a taxable year for any qualified long-term care insurance contract (as defined in section 7702B(b)) covering an individual, to the extent such amount does not exceed the limitation determined under the following table:

| In the case of an individual with an attained age before the close of the taxable year of: | The limitation is: |
|--|--------------------|
| 40 or less   | \$200              |
| More than 40 but not more than 50  | 375                |
| More than 50 but not more than 60  | 750                |
| More than 60 but not more than 70  | 2,000              |
| More than 70   | 2,500.             |

(B) INDEXING.—

(i) IN GENERAL.—In the case of any taxable year beginning in a calendar year after 1997, each dollar amount contained in subparagraph (A) shall be increased by the medical care cost adjustment of such amount for such calendar year. If any increase determined under the preceding sentence is not a multiple of \$10, such increase shall be rounded to the nearest multiple of \$10.

(ii) MEDICAL CARE COST ADJUSTMENT.—For purposes of clause (i), the medical care cost adjustment for any calendar year is the percentage (if any) by which—

(I) the medical care component of the C-CPI-U (as defined in section 1(f)(6)) for August of the preceding calendar year, exceeds

(II) such component of the CPI (as defined in section 1(f)(4)) for August of 1996, multiplied by the amount determined under section 1(f)(3)(B).

The Secretary shall, in consultation with the Secretary of Health and Human Services, prescribe an adjustment which the Secretary determines is more appropriate for purposes of this paragraph than the adjust-

ment described in the preceding sentence, and the adjustment so prescribed shall apply in lieu of the adjustment described in the preceding sentence.

(11) Certain payments to relatives treated as not paid for medical care --An amount paid for a qualified long-term care service (as defined in section 7702B(c)) provided to an individual shall be treated as not paid for medical care if such service is provided—

(A) by the spouse of the individual or by a relative (directly or through a partnership, corporation, or other entity) unless the service is provided by a licensed professional with respect to such service, or

(B) by a corporation or partnership which is related (within the meaning of section 267(b) or 707(b)) to the individual.

For purposes of this paragraph, the term “relative” means an individual bearing a relationship to the individual which is described in any of subparagraphs (A) through (G) of [section 152(d)(2)] *section 7706(d)(2)*. This paragraph shall not apply for purposes of section 105(b) with respect to reimbursements through insurance.

(e) EXCLUSION OF AMOUNTS ALLOWED FOR CARE OF CERTAIN DEPENDENTS.—Any expense allowed as a credit under section 21 shall not be treated as an expense paid for medical care.

[(f) SPECIAL RULES FOR 2013 THROUGH 2018.—In the case of any taxable year—

[(1) beginning after December 31, 2012, and ending before January 1, 2017, in the case of a taxpayer if such taxpayer or such taxpayer’s spouse has attained age 65 before the close of such taxable year, and

[(2) beginning after December 31, 2016, and ending before January 1, 2019, in the case of any taxpayer,

subsection (a) shall be applied with respect to a taxpayer by substituting “7.5 percent” for “10 percent”.]

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**SEC. 217. [MOVING EXPENSES] CERTAIN MOVING EXPENSES OF MEMBERS OF ARMED FORCES.**

[(a) DEDUCTION ALLOWED.—There shall be allowed as a deduction moving expenses paid or incurred during the taxable year in connection with the commencement of work by the taxpayer as an employee or as a self-employed individual at a new principal place of work.]

(a) *DEDUCTION ALLOWED.—There shall be allowed as a deduction moving expenses paid or incurred during the taxable year by a member of the Armed Forces of the United States on active duty who moves pursuant to a military order and incident to a permanent change of station.*

(b) DEFINITION OF MOVING EXPENSES.—

(1) IN GENERAL.—For purposes of this section, the term “moving expenses” means only the reasonable expenses—

(A) of moving household goods and personal effects from the former residence to the new residence, and

(B) of traveling (including lodging) from the former residence to the new place of residence.

Such term shall not include any expenses for meals.

(2) INDIVIDUALS OTHER THAN TAXPAYER.—In the case of any individual other than the taxpayer, expenses referred to in paragraph (1) shall be taken into account only if such individual has both the former residence and the new residence as his principal place of abode and is a member of the taxpayer's household.

[(c) CONDITIONS FOR ALLOWANCE.—No deduction shall be allowed under this section unless—

[(1) the taxpayer's new principal place of work—

[(A) is at least 50 miles farther from his former residence than was his former principal place of work, or

[(B) if he had no former principal place of work, is at least 50 miles from his former residence, and

[(2) either—

[(A) during the 12-month period immediately following his arrival in the general location of his new principal place of work, the taxpayer is a full-time employee, in such general location, during at least 39 weeks, or

[(B) during the 24-month period immediately following his arrival in the general location of his new principal place of work, the taxpayer is a full-time employee or performs services as a self-employed individual on a full-time basis, in such general location, during at least 78 weeks, of which not less than 39 weeks are during the 12-month period referred to in subparagraph (A).

For purposes of paragraph (1), the distance between two points shall be the shortest of the more commonly traveled routes between such two points.

[(d) RULES FOR APPLICATION OF SUBSECTION (C)(2).—

[(1) The condition of subsection (c)(2) shall not apply if the taxpayer is unable to satisfy such condition by reason of—

[(A) death or disability, or

[(B) involuntary separation (other than for willful misconduct) from the service of, or transfer for the benefit of, an employer after obtaining full-time employment in which the taxpayer could reasonably have been expected to satisfy such condition.

[(2) If a taxpayer has not satisfied the condition of subsection (c)(2) before the time prescribed by law (including extensions thereof) for filing the return for the taxable year during which he paid or incurred moving expenses which would otherwise be deductible under this section, but may still satisfy such condition, then such expenses may (at the election of the taxpayer) be deducted for such taxable year notwithstanding subsection (c)(2).

[(3) If—

[(A) for any taxable year moving expenses have been deducted in accordance with the rule provided in paragraph (2), and

[(B) the condition of subsection (c)(2) cannot be satisfied at the close of a subsequent taxable year, then an amount equal to the expenses which were so deducted shall be included in gross income for the first such subsequent taxable year.



[(f) SELF-EMPLOYED INDIVIDUAL.—For purposes of this section, the term “self-employed individual” means an individual who performs personal services—

[(1) as the owner of the entire interest in an unincorporated trade or business, or

[(2) as a partner in a partnership carrying on a trade or business.

[(g) RULES FOR MEMBERS OF THE ARMED FORCES OF THE UNITED STATES.—In the case of a member of the Armed Forces of the United States on active duty who moves pursuant to a military order and incident to a permanent change of station—

[(1) the limitations under subsection (c) shall not apply;

[(2) any moving and storage expenses which are furnished in kind (or for which reimbursement or an allowance is provided, but only to the extent of the expenses paid or incurred) to such member, his spouse, or his dependents, shall not be includible in gross income, and no reporting with respect to such expenses shall be required by the Secretary of Defense or the Secretary of Transportation, as the case may be; and

[(3) if moving and storage expenses are furnished in kind (or if reimbursement or an allowance for such expenses is provided) to such member’s spouse and his dependents with regard to moving to a location other than the one to which such member moves (or from a location other than the one from which such member moves), this section shall apply with respect to the moving expenses of his spouse and dependents—

[(A) as if his spouse commenced work as an employee at a new principal place of work at such location; and

[(B) without regard to the limitations under subsection (c).]

[(h)] (c) SPECIAL RULES FOR FOREIGN MOVES.—

(1) ALLOWANCE OF CERTAIN STORAGE FEES.—In the case of a foreign move, for purposes of this section, the moving expenses described in subsection (b)(1)(A) include the reasonable expenses—

(A) of moving household goods and personal effects to and from storage, and

(B) of storing such goods and effects for part or all of the period during which the new place of work continues to be the taxpayer’s principal place of work.

(2) FOREIGN MOVE.—For purposes of this subsection, the term “foreign move” means the commencement of work by the taxpayer at a new principal place of work located outside the United States.

(3) UNITED STATES DEFINED.—For purposes of this subsection and subsection (i), the term “United States” includes the possessions of the United States.

[(i)] (d) ALLOWANCE OF DEDUCTIONS IN CASE OF RETIREES OR DECEDENTS WHO WERE WORKING ABROAD.—

(1) IN GENERAL.—In the case of any qualified retiree moving expenses or qualified survivor moving expenses—

(A) this section (other than subsection (h)) shall be applied with respect to such expenses as if they were incurred in connection with the commencement of work by

the taxpayer as an employee at a new principal place of work located within the United States, and

(B) the limitations of subsection (c)(2) shall not apply.

(2) **QUALIFIED RETIREE MOVING EXPENSES.**—For purposes of paragraph (1), the term “qualified retiree moving expenses” means any moving expenses—

(A) which are incurred by an individual whose former principal place of work and former residence were outside the United States, and

(B) which are incurred for a move to a new residence in the United States in connection with the bona fide retirement of the individual.

(3) **QUALIFIED SURVIVOR MOVING EXPENSES.**—For purposes of paragraph (1), the term “qualified survivor moving expenses” means moving expenses—

(A) which are paid or incurred by the spouse or any dependent of any decedent who (as of the time of his death) had a principal place of work outside the United States, and

(B) which are incurred for a move which begins within 6 months after the death of such decedent and which is to a residence in the United States from a former residence outside the United States which (as of the time of the decedent’s death) was the residence of such decedent and the individual paying or incurring the expense.

(e) *EXPENSES FURNISHED IN KIND.*—*Any moving and storage expenses which are furnished in kind (or for which reimbursement or an allowance is provided, but only to the extent of the expenses paid or incurred)—*

(1) *to such member, his spouse, or his dependents, shall not be includible in gross income, and no reporting with respect to such expenses shall be required by the Secretary of Defense or the Secretary of Transportation, as the case may be, and*

(2) *to such member’s spouse and his dependents with regard to moving to a location other than the one to which such member moves (or from a location other than the one from which such member moves), this section shall apply with respect to the moving expenses of his spouse and dependents as if his spouse commenced work as an employee at a new principal place of work at such location.*

[(j)] (f) **REGULATIONS.**—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this section.

[(k)] (g) **SUSPENSION OF DEDUCTION FOR TAXABLE YEARS 2018 THROUGH 2025.**—Except in the case of an individual to whom subsection (g) applies, this section shall not apply to any taxable year beginning after December 31, 2017, and before January 1, 2026.

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**SEC. 220. ARCHER MSAS.**

(a) **DEDUCTION ALLOWED.**—In the case of an individual who is an eligible individual for any month during the taxable year, there shall be allowed as a deduction for the taxable year an amount equal to the aggregate amount paid in cash during such taxable year by such individual to an Archer MSA of such individual.

## (b) LIMITATIONS.—

(1) IN GENERAL.—The amount allowable as a deduction under subsection (a) to an individual for the taxable year shall not exceed the sum of the monthly limitations for months during such taxable year that the individual is an eligible individual.

(2) MONTHLY LIMITATION.—The monthly limitation for any month is the amount equal to 1/12 of—

(A) in the case of an individual who has self-only coverage under the high deductible health plan as of the first day of such month, 65 percent of the annual deductible under such coverage, and

(B) in the case of an individual who has family coverage under the high deductible health plan as of the first day of such month, 75 percent of the annual deductible under such coverage.

(3) SPECIAL RULE FOR MARRIED INDIVIDUALS.—In the case of individuals who are married to each other, if either spouse has family coverage—

(A) both spouses shall be treated as having only such family coverage (and if such spouses each have family coverage under different plans, as having the family coverage with the lowest annual deductible), and

(B) the limitation under paragraph (1) (after the application of subparagraph (A) of this paragraph) shall be divided equally between them unless they agree on a different division.

(4) DEDUCTION NOT TO EXCEED COMPENSATION.—

(A) EMPLOYEES.—The deduction allowed under subsection (a) for contributions as an eligible individual described in subclause (I) of subsection (c)(1)(A)(iii) shall not exceed such individual's wages, salaries, tips, and other employee compensation which are attributable to such individual's employment by the employer referred to in such subclause.

(B) SELF-EMPLOYED INDIVIDUALS.—The deduction allowed under subsection (a) for contributions as an eligible individual described in subclause (II) of subsection (c)(1)(A)(iii) shall not exceed such individual's earned income (as defined in section 401(c)(1)) derived by the taxpayer from the trade or business with respect to which the high deductible health plan is established.

(C) COMMUNITY PROPERTY LAWS NOT TO APPLY.—The limitations under this paragraph shall be determined without regard to community property laws.

(5) COORDINATION WITH EXCLUSION FOR EMPLOYER CONTRIBUTIONS.—No deduction shall be allowed under this section for any amount paid for any taxable year to an Archer MSA of an individual if—

(A) any amount is contributed to any Archer MSA of such individual for such year which is excludable from gross income under section 106(b), or

(B) if such individual's spouse is covered under the high deductible health plan covering such individual, any

amount is contributed for such year to any Archer MSA of such spouse which is so excludable.

(6) DENIAL OF DEDUCTION TO DEPENDENTS.—No deduction shall be allowed under this section to any individual [with respect to whom a deduction under section 151 is allowable to] *who is a dependent of* another taxpayer for a taxable year beginning in the calendar year in which such individual's taxable year begins.

(7) MEDICARE ELIGIBLE INDIVIDUALS.—The limitation under this subsection for any month with respect to an individual shall be zero for the first month such individual is entitled to benefits under title XVIII of the Social Security Act and for each month thereafter.

(c) DEFINITIONS.—For purposes of this section—

(1) ELIGIBLE INDIVIDUAL.—

(A) IN GENERAL.—The term “eligible individual” means, with respect to any month, any individual if—

(i) such individual is covered under a high deductible health plan as of the 1st day of such month,

(ii) such individual is not, while covered under a high deductible health plan, covered under any health plan—

(I) which is not a high deductible health plan, and

(II) which provides coverage for any benefit which is covered under the high deductible health plan, and

(iii)(I) the high deductible health plan covering such individual is established and maintained by the employer of such individual or of the spouse of such individual and such employer is a small employer, or

(II) such individual is an employee (within the meaning of section 401(c)(1)) or the spouse of such an employee and the high deductible health plan covering such individual is not established or maintained by any employer of such individual or spouse.

(B) CERTAIN COVERAGE DISREGARDED.—Subparagraph (A)(ii) shall be applied without regard to—

(i) coverage for any benefit provided by permitted insurance, and

(ii) coverage (whether through insurance or otherwise) for accidents, disability, dental care, vision care, or long-term care.

(C) CONTINUED ELIGIBILITY OF EMPLOYEE AND SPOUSE ESTABLISHING ARCHER MSAS.—If, while an employer is a small employer—

(i) any amount is contributed to an Archer MSA of an individual who is an employee of such employer or the spouse of such an employee, and

(ii) such amount is excludable from gross income under section 106(b) or allowable as a deduction under this section,

such individual shall not cease to meet the requirement of subparagraph (A)(iii)(I) by reason of such employer ceasing

to be a small employer so long as such employee continues to be an employee of such employer.

(D) LIMITATIONS ON ELIGIBILITY.—For limitations on number of taxpayers who are eligible to have Archer MSAs, see subsection (i).

(2) HIGH DEDUCTIBLE HEALTH PLAN.—

(A) IN GENERAL.—The term “high deductible health plan” means a health plan—

(i) in the case of self-only coverage, which has an annual deductible which is not less than \$1,500 and not more than \$2,250,

(ii) in the case of family coverage, which has an annual deductible which is not less than \$3,000 and not more than \$4,500, and

(iii) the annual out-of-pocket expenses required to be paid under the plan (other than for premiums) for covered benefits does not exceed—

(I) \$3,000 for self-only coverage, and

(II) \$5,500 for family coverage.

(B) SPECIAL RULES.—

(i) EXCLUSION OF CERTAIN PLANS.—Such term does not include a health plan if substantially all of its coverage is coverage described in paragraph (1)(B).

(ii) SAFE HARBOR FOR ABSENCE OF PREVENTIVE CARE DEDUCTIBLE.—A plan shall not fail to be treated as a high deductible health plan by reason of failing to have a deductible for preventive care if the absence of a deductible for such care is required by State law.

(3) PERMITTED INSURANCE.—The term “permitted insurance” means—

(A) insurance if substantially all of the coverage provided under such insurance relates to—

(i) liabilities incurred under workers’ compensation laws,

(ii) tort liabilities,

(iii) liabilities relating to ownership or use of property, or

(iv) such other similar liabilities as the Secretary may specify by regulations,

(B) insurance for a specified disease or illness, and

(C) insurance paying a fixed amount per day (or other period) of hospitalization.

(4) SMALL EMPLOYER.—

(A) IN GENERAL.—The term “small employer” means, with respect to any calendar year, any employer if such employer employed an average of 50 or fewer employees on business days during either of the 2 preceding calendar years. For purposes of the preceding sentence, a preceding calendar year may be taken into account only if the employer was in existence throughout such year.

(B) EMPLOYERS NOT IN EXISTENCE IN PRECEDING YEAR.—In the case of an employer which was not in existence throughout the 1st preceding calendar year, the determination under subparagraph (A) shall be based on the average number of employees that it is reasonably expected

such employer will employ on business days in the current calendar year.

(C) CERTAIN GROWING EMPLOYERS RETAIN TREATMENT AS SMALL EMPLOYER.—The term “small employer” includes, with respect to any calendar year, any employer if—

(i) such employer met the requirement of subparagraph (A) (determined without regard to subparagraph (B)) for any preceding calendar year after 1996,

(ii) any amount was contributed to the Archer MSA of any employee of such employer with respect to coverage of such employee under a high deductible health plan of such employer during such preceding calendar year and such amount was excludable from gross income under section 106(b) or allowable as a deduction under this section, and

(iii) such employer employed an average of 200 or fewer employees on business days during each preceding calendar year after 1996.

(D) SPECIAL RULES.—

(i) CONTROLLED GROUPS.—For purposes of this paragraph, all persons treated as a single employer under subsection (b), (c), (m), or (o) of section 414 shall be treated as 1 employer.

(ii) PREDECESSORS.—Any reference in this paragraph to an employer shall include a reference to any predecessor of such employer.

(5) FAMILY COVERAGE.—The term “family coverage” means any coverage other than self-only coverage.

(d) ARCHER MSA.—For purposes of this section—

(1) ARCHER MSA.—The term “Archer MSA” means a trust created or organized in the United States as a medical savings account exclusively for the purpose of paying the qualified medical expenses of the account holder, but only if the written governing instrument creating the trust meets the following requirements:

(A) Except in the case of a rollover contribution described in subsection (f)(5), no contribution will be accepted—

(i) unless it is in cash, or

(ii) to the extent such contribution, when added to previous contributions to the trust for the calendar year, exceeds 75 percent of the highest annual limit deductible permitted under subsection (c)(2)(A)(ii) for such calendar year.

(B) The trustee is a bank (as defined in section 408(n)), an insurance company (as defined in section 816), or another person who demonstrates to the satisfaction of the Secretary that the manner in which such person will administer the trust will be consistent with the requirements of this section.

(C) No part of the trust assets will be invested in life insurance contracts.

(D) The assets of the trust will not be commingled with other property except in a common trust fund or common investment fund.

(E) The interest of an individual in the balance in his account is nonforfeitable.

(2) QUALIFIED MEDICAL EXPENSES.—

(A) IN GENERAL.—The term “qualified medical expenses” means, with respect to an account holder, amounts paid by such holder for medical care (as defined in section 213(d)) for such individual, the spouse of such individual, and any dependent (as defined in [section 152] *section 7706*, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof) of such individual, but only to the extent such amounts are not compensated for by insurance or otherwise. Such term shall include an amount paid for medicine or a drug only if such medicine or drug is a prescribed drug (determined without regard to whether such drug is available without a prescription) or is insulin.

(B) HEALTH INSURANCE MAY NOT BE PURCHASED FROM ACCOUNT.—

(i) IN GENERAL.—Subparagraph (A) shall not apply to any payment for insurance.

(ii) EXCEPTIONS.—Clause (i) shall not apply to any expense for coverage under—

(I) a health plan during any period of continuation coverage required under any Federal law,

(II) a qualified long-term care insurance contract (as defined in section 7702B(b)), or

(III) a health plan during a period in which the individual is receiving unemployment compensation under any Federal or State law.

(C) MEDICAL EXPENSES OF INDIVIDUALS WHO ARE NOT ELIGIBLE INDIVIDUALS.—Subparagraph (A) shall apply to an amount paid by an account holder for medical care of an individual who is not described in clauses (i) and (ii) of subsection (c)(1)(A) for the month in which the expense for such care is incurred only if no amount is contributed (other than a rollover contribution) to any Archer MSA of such account holder for the taxable year which includes such month. This subparagraph shall not apply to any expense for coverage described in subclause (I) or (III) of subparagraph (B)(ii).

(3) ACCOUNT HOLDER.—The term “account holder” means the individual on whose behalf the Archer MSA was established.

(4) CERTAIN RULES TO APPLY.—Rules similar to the following rules shall apply for purposes of this section:

(A) Section 219(d)(2) (relating to no deduction for rollovers).

(B) Section 219(f)(3) (relating to time when contributions deemed made).

(C) Except as provided in section 106(b), section 219(f)(5) (relating to employer payments).

(D) Section 408(g) (relating to community property laws).

(E) Section 408(h) (relating to custodial accounts).

(e) TAX TREATMENT OF ACCOUNTS.—

(1) IN GENERAL.—An Archer MSA is exempt from taxation under this subtitle unless such account has ceased to be an Archer MSA. Notwithstanding the preceding sentence, any such

account is subject to the taxes imposed by section 511 (relating to imposition of tax on unrelated business income of charitable, etc. organizations).

(2) ACCOUNT TERMINATIONS.—Rules similar to the rules of paragraphs (2) and (4) of section 408(e) shall apply to Archer MSAs, and any amount treated as distributed under such rules shall be treated as not used to pay qualified medical expenses.

(f) TAX TREATMENT OF DISTRIBUTIONS.—

(1) AMOUNTS USED FOR QUALIFIED MEDICAL EXPENSES.—Any amount paid or distributed out of an Archer MSA which is used exclusively to pay qualified medical expenses of any account holder shall not be includible in gross income.

(2) INCLUSION OF AMOUNTS NOT USED FOR QUALIFIED MEDICAL EXPENSES.—Any amount paid or distributed out of an Archer MSA which is not used exclusively to pay the qualified medical expenses of the account holder shall be included in the gross income of such holder.

(3) EXCESS CONTRIBUTIONS RETURNED BEFORE DUE DATE OF RETURN.—

(A) IN GENERAL.—If any excess contribution is contributed for a taxable year to any Archer MSA of an individual, paragraph (2) shall not apply to distributions from the Archer MSAs of such individual (to the extent such distributions do not exceed the aggregate excess contributions to all such accounts of such individual for such year) if—

(i) such distribution is received by the individual on or before the last day prescribed by law (including extensions of time) for filing such individual's return for such taxable year, and

(ii) such distribution is accompanied by the amount of net income attributable to such excess contribution.

Any net income described in clause (ii) shall be included in the gross income of the individual for the taxable year in which it is received.

(B) EXCESS CONTRIBUTION.—For purposes of subparagraph (A), the term “excess contribution” means any contribution (other than a rollover contribution) which is neither excludable from gross income under section 106(b) nor deductible under this section.

(4) ADDITIONAL TAX ON DISTRIBUTIONS NOT USED FOR QUALIFIED MEDICAL EXPENSES.—

(A) IN GENERAL.—The tax imposed by this chapter on the account holder for any taxable year in which there is a payment or distribution from an Archer MSA of such holder which is includible in gross income under paragraph (2) shall be increased by 20 percent of the amount which is so includible.

(B) EXCEPTION FOR DISABILITY OR DEATH.—Subparagraph (A) shall not apply if the payment or distribution is made after the account holder becomes disabled within the meaning of section 72(m)(7) or dies.

(C) EXCEPTION FOR DISTRIBUTIONS AFTER MEDICARE ELIGIBILITY.—Subparagraph (A) shall not apply to any payment or distribution after the date on which the account



holder attains the age specified in section 1811 of the Social Security Act.

(5) ROLLOVER CONTRIBUTION.—An amount is described in this paragraph as a rollover contribution if it meets the requirements of subparagraphs (A) and (B).

(A) IN GENERAL.—Paragraph (2) shall not apply to any amount paid or distributed from an Archer MSA to the account holder to the extent the amount received is paid into an Archer MSA or a health savings account (as defined in section 223(d)) for the benefit of such holder not later than the 60th day after the day on which the holder receives the payment or distribution.

(B) LIMITATION.—This paragraph shall not apply to any amount described in subparagraph (A) received by an individual from an Archer MSA if, at any time during the 1-year period ending on the day of such receipt, such individual received any other amount described in subparagraph (A) from an Archer MSA which was not includible in the individual's gross income because of the application of this paragraph.

(6) COORDINATION WITH MEDICAL EXPENSE DEDUCTION.—For purposes of determining the amount of the deduction under section 213, any payment or distribution out of an Archer MSA for qualified medical expenses shall not be treated as an expense paid for medical care.

(7) TRANSFER OF ACCOUNT INCIDENT TO DIVORCE.—The transfer of an individual's interest in an Archer MSA to an individual's spouse or former spouse under a divorce or separation instrument described in clause (i) of section 121(d)(3)(C) shall not be considered a taxable transfer made by such individual notwithstanding any other provision of this subtitle, and such interest shall, after such transfer, be treated as an Archer MSA with respect to which such spouse is the account holder.

(8) TREATMENT AFTER DEATH OF ACCOUNT HOLDER.—

(A) TREATMENT IF DESIGNATED BENEFICIARY IS SPOUSE.—If the account holder's surviving spouse acquires such holder's interest in an Archer MSA by reason of being the designated beneficiary of such account at the death of the account holder, such Archer MSA shall be treated as if the spouse were the account holder.

(B) OTHER CASES.—

(i) IN GENERAL.—If, by reason of the death of the account holder, any person acquires the account holder's interest in an Archer MSA in a case to which subparagraph (A) does not apply—

(I) such account shall cease to be an Archer MSA as of the date of death, and

(II) an amount equal to the fair market value of the assets in such account on such date shall be includible if such person is not the estate of such holder, in such person's gross income for the taxable year which includes such date, or if such person is the estate of such holder, in such holder's gross income for the last taxable year of such holder.

## (ii) SPECIAL RULES.—

(I) REDUCTION OF INCLUSION FOR PRE-DEATH EXPENSES.—The amount includible in gross income under clause (i) by any person (other than the estate) shall be reduced by the amount of qualified medical expenses which were incurred by the decedent before the date of the decedent's death and paid by such person within 1 year after such date.

(II) DEDUCTION FOR ESTATE TAXES.—An appropriate deduction shall be allowed under section 691(c) to any person (other than the decedent or the decedent's spouse) with respect to amounts included in gross income under clause (i) by such person.

(g) COST-OF-LIVING ADJUSTMENT.—In the case of any taxable year beginning in a calendar year after 1998, each dollar amount in subsection (c)(2) shall be increased by an amount equal to—

(1) such dollar amount, multiplied by

(2) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which such taxable year begins by substituting “calendar year 1997” for “calendar year 2016” in subparagraph (A)(ii) thereof.

If any increase under the preceding sentence is not a multiple of \$50, such increase shall be rounded to the nearest multiple of \$50.

(h) REPORTS.—The Secretary may require the trustee of an Archer MSA to make such reports regarding such account to the Secretary and to the account holder with respect to contributions, distributions, and such other matters as the Secretary determines appropriate. The reports required by this subsection shall be filed at such time and in such manner and furnished to such individuals at such time and in such manner as may be required by the Secretary.

(i) LIMITATION ON NUMBER OF TAXPAYERS HAVING ARCHER MSAs.—

(1) IN GENERAL.—Except as provided in paragraph (5), no individual shall be treated as an eligible individual for any taxable year beginning after the cut-off year unless—

(A) such individual was an active MSA participant for any taxable year ending on or before the close of the cut-off year, or

(B) such individual first became an active MSA participant for a taxable year ending after the cut-off year by reason of coverage under a high deductible health plan of an MSA-participating employer.

(2) CUT-OFF YEAR.—For purposes of paragraph (1), the term “cut-off year” means the earlier of—

(A) calendar year 2007, or

(B) the first calendar year before 2007 for which the Secretary determines under subsection (j) that the numerical limitation for such year has been exceeded.

(3) ACTIVE MSA PARTICIPANT.—For purposes of this subsection—

(A) IN GENERAL.—The term “active MSA participant” means, with respect to any taxable year, any individual who is the account holder of any Archer MSA into which

any contribution was made which was excludable from gross income under section 106(b), or allowable as a deduction under this section, for such taxable year.

(B) SPECIAL RULE FOR CUT-OFF YEARS BEFORE 2007.—In the case of a cut-off year before 2007—

(i) an individual shall not be treated as an eligible individual for any month of such year or an active MSA participant under paragraph (1)(A) unless such individual is, on or before the cut-off date, covered under a high deductible health plan, and

(ii) an employer shall not be treated as an MSA-participating employer unless the employer, on or before the cut-off date, offered coverage under a high deductible health plan to any employee.

(C) CUT-OFF DATE.—For purposes of subparagraph (B)—

(i) IN GENERAL.—Except as otherwise provided in this subparagraph, the cut-off date is October 1 of the cut-off year.

(ii) EMPLOYEES WITH ENROLLMENT PERIODS AFTER OCTOBER 1.—In the case of an individual described in subclause (I) of subsection (c)(1)(A)(iii), if the regularly scheduled enrollment period for health plans of the individual's employer occurs during the last 3 months of the cut-off year, the cut-off date is December 31 of the cut-off year.

(iii) SELF-EMPLOYED INDIVIDUALS.—In the case of an individual described in subclause (II) of subsection (c)(1)(A)(iii), the cut-off date is November 1 of the cut-off year.

(iv) SPECIAL RULES FOR 1997.—If 1997 is a cut-off year by reason of subsection (j)(1)(A)—

(I) each of the cut-off dates under clauses (i) and (iii) shall be 1 month earlier than the date determined without regard to this clause, and

(II) clause (ii) shall be applied by substituting “4 months” for “3 months”.

(4) MSA-PARTICIPATING EMPLOYER.—For purposes of this subsection, the term “MSA-participating employer” means any small employer if—

(A) such employer made any contribution to the Archer MSA of any employee during the cut-off year or any preceding calendar year which was excludable from gross income under section 106(b), or

(B) at least 20 percent of the employees of such employer who are eligible individuals for any month of the cut-off year by reason of coverage under a high deductible health plan of such employer each made a contribution of at least \$100 to their Archer MSAs for any taxable year ending with or within the cut-off year which was allowable as a deduction under this section.

(5) ADDITIONAL ELIGIBILITY AFTER CUT-OFF YEAR.—If the Secretary determines under subsection (j)(2)(A) that the numerical limit for the calendar year following a cut-off year described in paragraph (2)(B) has not been exceeded—

(A) this subsection shall not apply to any otherwise eligible individual who is covered under a high deductible health plan during the first 6 months of the second calendar year following the cut-off year (and such individual shall be treated as an active MSA participant for purposes of this subsection if a contribution is made to any Archer MSA with respect to such coverage), and

(B) any employer who offers coverage under a high deductible health plan to any employee during such 6-month period shall be treated as an MSA-participating employer for purposes of this subsection if the requirements of paragraph (4) are met with respect to such coverage.

For purposes of this paragraph, subsection (j)(2)(A) shall be applied for 1998 by substituting "750,000" for "600,000".

(j) DETERMINATION OF WHETHER NUMERICAL LIMITS ARE EXCEEDED.—

(1) DETERMINATION OF WHETHER LIMIT EXCEEDED FOR 1997.—The numerical limitation for 1997 is exceeded if, based on the reports required under paragraph (4), the number of Archer MSAs established as of—

- (A) April 30, 1997, exceeds 375,000, or
- (B) June 30, 1997, exceeds 525,000.

(2) DETERMINATION OF WHETHER LIMIT EXCEEDED FOR 1998, 1999, 2001, 2002, 2004, 2005, OR 2006.—

(A) IN GENERAL.—The numerical limitation for 1998, 1999, 2001, 2002, 2004, 2005, or 2006 is exceeded if the sum of—

(i) the number of MSA returns filed on or before April 15 of such calendar year for taxable years ending with or within the preceding calendar year, plus

(ii) the Secretary's estimate (determined on the basis of the returns described in clause (i)) of the number of MSA returns for such taxable years which will be filed after such date,

exceeds 750,000 (600,000 in the case of 1998). For purposes of the preceding sentence, the term "MSA return" means any return on which any exclusion is claimed under section 106(b) or any deduction is claimed under this section.

(B) ALTERNATIVE COMPUTATION OF LIMITATION.—The numerical limitation for 1998, 1999, 2001, 2002, 2004, 2005, or 2006 is also exceeded if the sum of—

(i) 90 percent of the sum determined under subparagraph (A) for such calendar year, plus

(ii) the product of 2.5 and the number of Archer MSAs established during the portion of such year preceding July 1 (based on the reports required under paragraph (4)) for taxable years beginning in such year,

exceeds 750,000.

(C) NO LIMITATION FOR 2000 OR 2003.—The numerical limitation shall not apply for 2000 or 2003.

(3) PREVIOUSLY UNINSURED INDIVIDUALS NOT INCLUDED IN DETERMINATION.—

(A) **IN GENERAL.**—The determination of whether any calendar year is a cut-off year shall be made by not counting the Archer MSA of any previously uninsured individual.

(B) **PREVIOUSLY UNINSURED INDIVIDUAL.**—For purposes of this subsection, the term “previously uninsured individual” means, with respect to any Archer MSA, any individual who had no health plan coverage (other than coverage referred to in subsection (c)(1)(B)) at any time during the 6-month period before the date such individual’s coverage under the high deductible health plan commences.

(4) **REPORTING BY MSA TRUSTEES.**—

(A) **IN GENERAL.**—Not later than August 1 of 1997, 1998, 1999, 2001, 2002, 2004, 2005, and 2006, each person who is the trustee of an Archer MSA established before July 1 of such calendar year shall make a report to the Secretary (in such form and manner as the Secretary shall specify) which specifies—

(i) the number of Archer MSAs established before such July 1 (for taxable years beginning in such calendar year) of which such person is the trustee,

(ii) the name and TIN of the account holder of each such account, and

(iii) the number of such accounts which are accounts of previously uninsured individuals.

(B) **ADDITIONAL REPORT FOR 1997.**—Not later than June 1, 1997, each person who is the trustee of an Archer MSA established before May 1, 1997, shall make an additional report described in subparagraph (A) but only with respect to accounts established before May 1, 1997.

(C) **PENALTY FOR FAILURE TO FILE REPORT.**—The penalty provided in section 6693(a) shall apply to any report required by this paragraph, except that—

(i) such section shall be applied by substituting “\$25” for “\$50”, and

(ii) the maximum penalty imposed on any trustee shall not exceed \$5,000.

(D) **AGGREGATION OF ACCOUNTS.**—To the extent practicable, in determining the number of Archer MSAs on the basis of the reports under this paragraph, all Archer MSAs of an individual shall be treated as 1 account and all accounts of individuals who are married to each other shall be treated as 1 account.

(5) **DATE OF MAKING DETERMINATIONS.**—Any determination under this subsection that a calendar year is a cut-off year shall be made by the Secretary and shall be published not later than October 1 of such year.

**SEC. 221. INTEREST ON EDUCATION LOANS.**

(a) **ALLOWANCE OF DEDUCTION.**—In the case of an individual, there shall be allowed as a deduction for the taxable year an amount equal to the interest paid by the taxpayer during the taxable year on any qualified education loan.

(b) **MAXIMUM DEDUCTION.**—

(1) **IN GENERAL.**—Except as provided in paragraph (2), the deduction allowed by subsection (a) for the taxable year shall not exceed \$2,500.

## (2) LIMITATION BASED ON MODIFIED ADJUSTED GROSS INCOME.—

(A) IN GENERAL.—The amount which would (but for this paragraph) be allowable as a deduction under this section shall be reduced (but not below zero) by the amount determined under subparagraph (B).

(B) AMOUNT OF REDUCTION.—The amount determined under this subparagraph is the amount which bears the same ratio to the amount which would be so taken into account as—

(i) the excess of—

(I) the taxpayer's modified adjusted gross income for such taxable year, over

(II) \$50,000 (\$100,000 in the case of a joint return), bears to (ii) \$15,000 (\$30,000 in the case of a joint return).

(C) MODIFIED ADJUSTED GROSS INCOME.—The term "modified adjusted gross income" means adjusted gross income determined—

(i) without regard to this section and sections 222, 911, 931, and 933, and

(ii) AFTER APPLICATION OF SECTIONS 86, 135, 137, 219, AND 469 (C) DEPENDENTS NOT ELIGIBLE FOR DEDUCTION.—No deduction shall be allowed by this section to an individual for the taxable year if a deduction under section 151 with respect to such individual is allowed to another taxpayer for the taxable year beginning in the calendar year in which such individual's taxable year begins.

## (d) DEFINITIONS.—For purposes of this section—

(1) QUALIFIED EDUCATION LOAN.—The term "qualified education loan" means any indebtedness incurred by the taxpayer solely to pay qualified higher education expenses—

(A) which are incurred on behalf of the taxpayer, the taxpayer's spouse, or any dependent of the taxpayer as of the time the indebtedness was incurred,

(B) which are paid or incurred within a reasonable period of time before or after the indebtedness is incurred, and

(C) which are attributable to education furnished during a period during which the recipient was an eligible student.

Such term includes indebtedness used to refinance indebtedness which qualifies as a qualified education loan. The term "qualified education loan" shall not include any indebtedness owed to a person who is related (within the meaning of section 267(b) or 707(b)(1)) to the taxpayer or to any person by reason of a loan under any qualified employer plan (as defined in section 72(p)(4)) or under any contract referred to in section 72(p)(5).

(2) QUALIFIED HIGHER EDUCATION EXPENSES.—The term "qualified higher education expenses" means the cost of attendance (as defined in section 472 of the Higher Education Act of 1965, 20 U.S.C. 1087ll, as in effect on the day before the date

of the enactment of the Taxpayer Relief Act of 1997) at an eligible educational institution, reduced by the sum of—

(A) the amount excluded from gross income under section 127, 135, 529, or 530 by reason of such expenses, and

(B) the amount of any scholarship, allowance, or payment described in section 25A(g)(2).

For purposes of the preceding sentence, the term “eligible educational institution” has the same meaning given such term by section 25A(f)(2), except that such term shall also include an institution conducting an internship or residency program leading to a degree or certificate awarded by an institution of higher education, a hospital, or a health care facility which offers postgraduate training.

(3) ELIGIBLE STUDENT.—The term “eligible student” has the meaning given such term by section 25A(b)(3).

(4) DEPENDENT.—The term “dependent” has the meaning given such term by [section 152] *section 7706* (determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof).

(e) SPECIAL RULES.—

(1) DENIAL OF DOUBLE BENEFIT.—No deduction shall be allowed under this section for any amount for which a deduction is allowable under any other provision of this chapter.

(2) MARRIED COUPLES MUST FILE JOINT RETURN.—If the taxpayer is married at the close of the taxable year, the deduction shall be allowed under subsection (a) only if the taxpayer and the taxpayer’s spouse file a joint return for the taxable year.

(3) MARITAL STATUS.—Marital status shall be determined in accordance with section 7703.

(f) INFLATION ADJUSTMENTS.—

(1) IN GENERAL.—In the case of a taxable year beginning after 2002, the \$50,000 and \$100,000 amounts in subsection (b)(2) shall each be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “calendar year 2001” for “calendar year 2016” in subparagraph (A)(ii) thereof.

(2) ROUNDING.—If any amount as adjusted under paragraph (1) is not a multiple of \$5,000, such amount shall be rounded to the next lowest multiple of \$5,000.

**SEC. 222. QUALIFIED TUITION AND RELATED EXPENSES.**

(a) ALLOWANCE OF DEDUCTION.—In the case of an individual, there shall be allowed as a deduction an amount equal to the qualified tuition and related expenses paid by the taxpayer during the taxable year.

(b) DOLLAR LIMITATIONS.—

(1) IN GENERAL.—The amount allowed as a deduction under subsection (a) with respect to the taxpayer for any taxable year shall not exceed the applicable dollar limit.

(2) APPLICABLE DOLLAR LIMIT.—

(A) 2002 AND 2003.—In the case of a taxable year beginning in 2002 or 2003, the applicable dollar limit shall be equal to—

(i) in the case of a taxpayer whose adjusted gross income for the taxable year does not exceed \$65,000 (\$130,000 in the case of a joint return), \$3,000, and—  
 (ii) in the case of any other taxpayer, zero.

(B) AFTER 2003.—In the case of any taxable year beginning after 2003, the applicable dollar amount shall be equal to—

(i) in the case of a taxpayer whose adjusted gross income for the taxable year does not exceed \$65,000 (\$130,000 in the case of a joint return), \$4,000,

(ii) in the case of a taxpayer not described in clause (i) whose adjusted gross income for the taxable year does not exceed \$80,000 (\$160,000 in the case of a joint return), \$2,000, and

(iii) in the case of any other taxpayer, zero.

(C) ADJUSTED GROSS INCOME.—For purposes of this paragraph, adjusted gross income shall be determined—

(i) without regard to this section and sections 911, 931, and 933, and

(ii) after application of sections 86, 135, 137, 219, 221, and 469.

(c) NO DOUBLE BENEFIT.—

(1) IN GENERAL.—No deduction shall be allowed under subsection (a) for any expense for which a deduction is allowed to the taxpayer under any other provision of this chapter.

(2) COORDINATION WITH OTHER EDUCATION INCENTIVES.—

(A) DENIAL OF DEDUCTION IF CREDIT ELECTED.—No deduction shall be allowed under subsection (a) for a taxable year with respect to the qualified tuition and related expenses with respect to an individual if the taxpayer or any other person elects to have section 25A apply with respect to such individual for such year.

(B) COORDINATION WITH EXCLUSIONS.—The total amount of qualified tuition and related expenses shall be reduced by the amount of such expenses taken into account in determining any amount excluded under section 135, 529(c)(1), or 530(d)(2). For purposes of the preceding sentence, the amount taken into account in determining the amount excluded under section 529(c)(1) shall not include that portion of the distribution which represents a return of any contributions to the plan.

(3) DEPENDENTS.—No deduction shall be allowed under subsection (a) to any individual [with respect to whom a deduction under section 151 is allowable to] *who is a dependent of* another taxpayer for a taxable year beginning in the calendar year in which such individual's taxable year begins.

(d) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) QUALIFIED TUITION AND RELATED EXPENSES.—The term “qualified tuition and related expenses” has the meaning given such term by section 25A(f). Such expenses shall be reduced in the same manner as under section 25A(g)(2).

(2) IDENTIFICATION REQUIREMENT.—No deduction shall be allowed under subsection (a) to a taxpayer with respect to the qualified tuition and related expenses of an individual unless



the taxpayer includes the name and taxpayer identification number of the individual on the return of tax for the taxable year.

(3) **LIMITATION ON TAXABLE YEAR OF DEDUCTION.**—

(A) **IN GENERAL.**—A deduction shall be allowed under subsection (a) for qualified tuition and related expenses for any taxable year only to the extent such expenses are in connection with enrollment at an institution of higher education during the taxable year.

(B) **CERTAIN PREPAYMENTS ALLOWED.**—Subparagraph (A) shall not apply to qualified tuition and related expenses paid during a taxable year if such expenses are in connection with an academic term beginning during such taxable year or during the first 3 months of the next taxable year.

(4) **NO DEDUCTION FOR MARRIED INDIVIDUALS FILING SEPARATE RETURNS.**—If the taxpayer is a married individual (within the meaning of section 7703), this section shall apply only if the taxpayer and the taxpayer's spouse file a joint return for the taxable year.

(5) **NONRESIDENT ALIENS.**—If the taxpayer is a nonresident alien individual for any portion of the taxable year, this section shall apply only if such individual is treated as a resident alien of the United States for purposes of this chapter by reason of an election under subsection (g) or (h) of section 6013.

(6) **PAYEE STATEMENT REQUIREMENT.**—

(A) **IN GENERAL.**—Except as otherwise provided by the Secretary, no deduction shall be allowed under subsection (a) unless the taxpayer receives a statement furnished under section 6050S(d) which contains all of the information required by paragraph (2) thereof.

(B) **STATEMENT RECEIVED BY DEPENDENT.**—The receipt of the statement referred to in subparagraph (A) by an individual described in subsection (c)(3) shall be treated for purposes of subparagraph (A) as received by the taxpayer.

(7) **REGULATIONS.**—The Secretary may prescribe such regulations as may be necessary or appropriate to carry out this section, including regulations requiring recordkeeping and information reporting.

(e) **TERMINATION.**—This section shall not apply to taxable years beginning after December 31, 2017.

**SEC. 223. HEALTH SAVINGS ACCOUNTS.**

(a) **DEDUCTION ALLOWED.**—In the case of an individual who is an eligible individual for any month during the taxable year, there shall be allowed as a deduction for the taxable year an amount equal to the aggregate amount paid in cash during such taxable year by or on behalf of such individual to a health savings account of such individual.

(b) **LIMITATIONS.**—

(1) **IN GENERAL.**—The amount allowable as a deduction under subsection (a) to an individual for the taxable year shall not exceed the sum of the monthly limitations for months during such taxable year that the individual is an eligible individual.

(2) **MONTHLY LIMITATION.**—The monthly limitation for any month is  $\frac{1}{12}$  of—

(A) in the case of an eligible individual who has self-only coverage under a high deductible health plan as of the first day of such month, \$2,250.

(B) in the case of an eligible individual who has family coverage under a high deductible health plan as of the first day of such month, \$4,500.

(3) ADDITIONAL CONTRIBUTIONS FOR INDIVIDUALS 55 OR OLDER.—

(A) IN GENERAL.—In the case of an individual who has attained age 55 before the close of the taxable year, the applicable limitation under subparagraphs (A) and (B) of paragraph (2) shall be increased by the additional contribution amount.

(B) ADDITIONAL CONTRIBUTION AMOUNT.—For purposes of this section, the additional contribution amount is the amount determined in accordance with the following table:

| For taxable years beginning in: | The additional contribution amount is: |
|---------------------------------|--|
| 2004                            | \$500                                  |
| 2005                            | \$600                                  |
| 2006                            | \$700                                  |
| 2007                            | \$800                                  |
| 2008                            | \$900                                  |
| 2009 and thereafter             | \$1,000.                               |

(4) COORDINATION WITH OTHER CONTRIBUTIONS.—The limitation which would (but for this paragraph) apply under this subsection to an individual for any taxable year shall be reduced (but not below zero) by the sum of—

(A) the aggregate amount paid for such taxable year to Archer MSAs of such individual,

(B) the aggregate amount contributed to health savings accounts of such individual which is excludable from the taxpayer's gross income for such taxable year under section 106(d) (and such amount shall not be allowed as a deduction under subsection (a)), and

(C) the aggregate amount contributed to health savings accounts of such individual for such taxable year under section 408(d)(9) (and such amount shall not be allowed as a deduction under subsection (a)).

Subparagraph (A) shall not apply with respect to any individual to whom paragraph (5) applies.

(5) SPECIAL RULE FOR MARRIED INDIVIDUALS.—In the case of individuals who are married to each other, if either spouse has family coverage—

(A) both spouses shall be treated as having only such family coverage (and if such spouses each have family coverage under different plans, as having the family coverage with the lowest annual deductible), and

(B) the limitation under paragraph (1) (after the application of subparagraph (A) and without regard to any additional contribution amount under paragraph (3))—

(i) shall be reduced by the aggregate amount paid to Archer MSAs of such spouses for the taxable year, and

(ii) after such reduction, shall be divided equally between them unless they agree on a different division.

(6) DENIAL OF DEDUCTION TO DEPENDENTS.—No deduction shall be allowed under this section to any individual [with respect to whom a deduction under section 151 is allowable to] *who is a dependent of* another taxpayer for a taxable year beginning in the calendar year in which such individual's taxable year begins.

(7) MEDICARE ELIGIBLE INDIVIDUALS.—The limitation under this subsection for any month with respect to an individual shall be zero for the first month such individual is entitled to benefits under title XVIII of the Social Security Act and for each month thereafter.

(8) INCREASE IN LIMIT FOR INDIVIDUALS BECOMING ELIGIBLE INDIVIDUALS AFTER THE BEGINNING OF THE YEAR.—

(A) IN GENERAL.—For purposes of computing the limitation under paragraph (1) for any taxable year, an individual who is an eligible individual during the last month of such taxable year shall be treated—

(i) as having been an eligible individual during each of the months in such taxable year, and

(ii) as having been enrolled, during each of the months such individual is treated as an eligible individual solely by reason of clause (i), in the same high deductible health plan in which the individual was enrolled for the last month of such taxable year.

(B) FAILURE TO MAINTAIN HIGH DEDUCTIBLE HEALTH PLAN COVERAGE.—

(i) IN GENERAL.—If, at any time during the testing period, the individual is not an eligible individual, then—

(I) gross income of the individual for the taxable year in which occurs the first month in the testing period for which such individual is not an eligible individual is increased by the aggregate amount of all contributions to the health savings account of the individual which could not have been made but for subparagraph (A), and

(II) the tax imposed by this chapter for any taxable year on the individual shall be increased by 10 percent of the amount of such increase.

(ii) EXCEPTION FOR DISABILITY OR DEATH.—Subclauses (I) and (II) of clause (i) shall not apply if the individual ceased to be an eligible individual by reason of the death of the individual or the individual becoming disabled (within the meaning of section 72(m)(7)).

(iii) TESTING PERIOD.—The term "testing period" means the period beginning with the last month of the taxable year referred to in subparagraph (A) and ending on the last day of the 12th month following such month.

(c) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) ELIGIBLE INDIVIDUAL.—

- (A) IN GENERAL.—The term “eligible individual” means, with respect to any month, any individual if—
- (i) such individual is covered under a high deductible health plan as of the 1st day of such month, and
  - (ii) such individual is not, while covered under a high deductible health plan, covered under any health plan—
    - (I) which is not a high deductible health plan, and
    - (II) which provides coverage for any benefit which is covered under the high deductible health plan.
- (B) CERTAIN COVERAGE DISREGARDED.—Subparagraph (A)(ii) shall be applied without regard to—
- (i) coverage for any benefit provided by permitted insurance,
  - (ii) coverage (whether through insurance or otherwise) for accidents, disability, dental care, vision care, or long-term care, and
  - (iii) for taxable years beginning after December 31, 2006, coverage under a health flexible spending arrangement during any period immediately following the end of a plan year of such arrangement during which unused benefits or contributions remaining at the end of such plan year may be paid or reimbursed to plan participants for qualified benefit expenses incurred during such period if—
    - (I) the balance in such arrangement at the end of such plan year is zero, or
    - (II) the individual is making a qualified HSA distribution (as defined in section 106(e)) in an amount equal to the remaining balance in such arrangement as of the end of such plan year, in accordance with rules prescribed by the Secretary.
- (C) SPECIAL RULE FOR INDIVIDUALS ELIGIBLE FOR CERTAIN VETERANS BENEFITS.—An individual shall not fail to be treated as an eligible individual for any period merely because the individual receives hospital care or medical services under any law administered by the Secretary of Veterans Affairs for a service-connected disability (within the meaning of section 101(16) of title 38, United States Code).
- (2) HIGH DEDUCTIBLE HEALTH PLAN.—
- (A) IN GENERAL.—The term “high deductible health plan” means a health plan—
- (i) which has an annual deductible which is not less than—
    - (I) \$1,000 for self-only coverage, and
    - (II) twice the dollar amount in subclause (I) for family coverage, and
  - (ii) the sum of the annual deductible and the other annual out-of-pocket expenses required to be paid under the plan (other than for premiums) for covered benefits does not exceed—
    - (I) \$5,000 for self-only coverage, and

(II) twice the dollar amount in subclause (I) for family coverage.

(B) EXCLUSION OF CERTAIN PLANS.—Such term does not include a health plan if substantially all of its coverage is coverage described in paragraph (1)(B).

(C) SAFE HARBOR FOR ABSENCE OF PREVENTIVE CARE DEDUCTIBLE.—A plan shall not fail to be treated as a high deductible health plan by reason of failing to have a deductible for preventive care (within the meaning of section 1861 of the Social Security Act, except as otherwise provided by the Secretary).

(D) SPECIAL RULES FOR NETWORK PLANS.—In the case of a plan using a network of providers—

(i) ANNUAL OUT-OF-POCKET LIMITATION.—Such plan shall not fail to be treated as a high deductible health plan by reason of having an out-of-pocket limitation for services provided outside of such network which exceeds the applicable limitation under subparagraph (A)(ii).

(ii) ANNUAL DEDUCTIBLE.—Such plan's annual deductible for services provided outside of such network shall not be taken into account for purposes of subsection (b)(2).

(3) PERMITTED INSURANCE.—The term “permitted insurance” means—

(A) insurance if substantially all of the coverage provided under such insurance relates to—

(i) liabilities incurred under workers' compensation laws,

(ii) tort liabilities,

(iii) liabilities relating to ownership or use of property, or

(iv) such other similar liabilities as the Secretary may specify by regulations,

(B) insurance for a specified disease or illness, and

(C) insurance paying a fixed amount per day (or other period) of hospitalization.

(4) FAMILY COVERAGE.—The term “family coverage” means any coverage other than self-only coverage.

(5) ARCHER MSA.—The term “Archer MSA” has the meaning given such term in section 220(d).

(d) HEALTH SAVINGS ACCOUNT.—For purposes of this section—

(1) IN GENERAL.—The term “health savings account” means a trust created or organized in the United States as a health savings account exclusively for the purpose of paying the qualified medical expenses of the account beneficiary, but only if the written governing instrument creating the trust meets the following requirements:

(A) Except in the case of a rollover contribution described in subsection (f)(5) or section 220(f)(5), no contribution will be accepted—

(i) unless it is in cash, or

(ii) to the extent such contribution, when added to previous contributions to the trust for the calendar year, exceeds the sum of—

(I) the dollar amount in effect under subsection (b)(2)(B), and

(II) the dollar amount in effect under subsection (b)(3)(B).

(B) The trustee is a bank (as defined in section 408(n)), an insurance company (as defined in section 816), or another person who demonstrates to the satisfaction of the Secretary that the manner in which such person will administer the trust will be consistent with the requirements of this section.

(C) No part of the trust assets will be invested in life insurance contracts.

(D) The assets of the trust will not be commingled with other property except in a common trust fund or common investment fund.

(E) The interest of an individual in the balance in his account is nonforfeitable.

(2) QUALIFIED MEDICAL EXPENSES.—

(A) IN GENERAL.—The term “qualified medical expenses” means, with respect to an account beneficiary, amounts paid by such beneficiary for medical care (as defined in section 213(d)) for such individual, the spouse of such individual, and any dependent (as defined in [section 152] *section 7706*, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof) of such individual, but only to the extent such amounts are not compensated for by insurance or otherwise. Such term shall include an amount paid for medicine or a drug only if such medicine or drug is a prescribed drug (determined without regard to whether such drug is available without a prescription) or is insulin.

(B) HEALTH INSURANCE MAY NOT BE PURCHASED FROM ACCOUNT.—Subparagraph (A) shall not apply to any payment for insurance.

(C) EXCEPTIONS.—Subparagraph (B) shall not apply to any expense for coverage under—

(i) a health plan during any period of continuation coverage required under any Federal law,

(ii) a qualified long-term care insurance contract (as defined in section 7702B(b)),

(iii) a health plan during a period in which the individual is receiving unemployment compensation under any Federal or State law, or

(iv) in the case of an account beneficiary who has attained the age specified in section 1811 of the Social Security Act, any health insurance other than a medicare supplemental policy (as defined in section 1882 of the Social Security Act).

(3) ACCOUNT BENEFICIARY.—The term “account beneficiary” means the individual on whose behalf the health savings account was established.

(4) CERTAIN RULES TO APPLY.—Rules similar to the following rules shall apply for purposes of this section:

(A) Section 219(d)(2) (relating to no deduction for rollovers).

(B) Section 219(f)(3) (relating to time when contributions deemed made).

(C) Except as provided in section 106(d), section 219(f)(5) (relating to employer payments).

(D) Section 408(g) (relating to community property laws).

(E) Section 408(h) (relating to custodial accounts).

(e) TAX TREATMENT OF ACCOUNTS.—

(1) IN GENERAL.—A health savings account is exempt from taxation under this subtitle unless such account has ceased to be a health savings account. Notwithstanding the preceding sentence, any such account is subject to the taxes imposed by section 511 (relating to imposition of tax on unrelated business income of charitable, etc. organizations).

(2) ACCOUNT TERMINATIONS.—Rules similar to the rules of paragraphs (2) and (4) of section 408(e) shall apply to health savings accounts, and any amount treated as distributed under such rules shall be treated as not used to pay qualified medical expenses.

(f) TAX TREATMENT OF DISTRIBUTIONS.—

(1) AMOUNTS USED FOR QUALIFIED MEDICAL EXPENSES.—Any amount paid or distributed out of a health savings account which is used exclusively to pay qualified medical expenses of any account beneficiary shall not be includible in gross income.

(2) INCLUSION OF AMOUNTS NOT USED FOR QUALIFIED MEDICAL EXPENSES.—Any amount paid or distributed out of a health savings account which is not used exclusively to pay the qualified medical expenses of the account beneficiary shall be included in the gross income of such beneficiary.

(3) EXCESS CONTRIBUTIONS RETURNED BEFORE DUE DATE OF RETURN.—

(A) IN GENERAL.—If any excess contribution is contributed for a taxable year to any health savings account of an individual, paragraph (2) shall not apply to distributions from the health savings accounts of such individual (to the extent such distributions do not exceed the aggregate excess contributions to all such accounts of such individual for such year) if—

(i) such distribution is received by the individual on or before the last day prescribed by law (including extensions of time) for filing such individual's return for such taxable year, and

(ii) such distribution is accompanied by the amount of net income attributable to such excess contribution.

Any net income described in clause (ii) shall be included in the gross income of the individual for the taxable year in which it is received.

(B) EXCESS CONTRIBUTION.—For purposes of subparagraph (A), the term “excess contribution” means any contribution (other than a rollover contribution described in paragraph (5) or section 220(f)(5)) which is neither excludable from gross income under section 106(d) nor deductible under this section.

(4) ADDITIONAL TAX ON DISTRIBUTIONS NOT USED FOR QUALIFIED MEDICAL EXPENSES.—

(A) IN GENERAL.—The tax imposed by this chapter on the account beneficiary for any taxable year in which there is a payment or distribution from a health savings account of such beneficiary which is includible in gross income under paragraph (2) shall be increased by 20 percent of the amount which is so includible.

(B) EXCEPTION FOR DISABILITY OR DEATH.—Subparagraph (A) shall not apply if the payment or distribution is made after the account beneficiary becomes disabled within the meaning of section 72(m)(7) or dies.

(C) EXCEPTION FOR DISTRIBUTIONS AFTER MEDICARE ELIGIBILITY.—Subparagraph (A) shall not apply to any payment or distribution after the date on which the account beneficiary attains the age specified in section 1811 of the Social Security Act.

(5) ROLLOVER CONTRIBUTION.—An amount is described in this paragraph as a rollover contribution if it meets the requirements of subparagraphs (A) and (B).

(A) IN GENERAL.—Paragraph (2) shall not apply to any amount paid or distributed from a health savings account to the account beneficiary to the extent the amount received is paid into a health savings account for the benefit of such beneficiary not later than the 60th day after the day on which the beneficiary receives the payment or distribution.

(B) LIMITATION.—This paragraph shall not apply to any amount described in subparagraph (A) received by an individual from a health savings account if, at any time during the 1-year period ending on the day of such receipt, such individual received any other amount described in subparagraph (A) from a health savings account which was not includible in the individual's gross income because of the application of this paragraph.

(6) COORDINATION WITH MEDICAL EXPENSE DEDUCTION.—For purposes of determining the amount of the deduction under section 213, any payment or distribution out of a health savings account for qualified medical expenses shall not be treated as an expense paid for medical care.

(7) TRANSFER OF ACCOUNT INCIDENT TO DIVORCE.—The transfer of an individual's interest in a health savings account to an individual's spouse or former spouse under a divorce or separation instrument described in clause (i) of section 121(d)(3)(C) shall not be considered a taxable transfer made by such individual notwithstanding any other provision of this subtitle, and such interest shall, after such transfer, be treated as a health savings account with respect to which such spouse is the account beneficiary.

(8) TREATMENT AFTER DEATH OF ACCOUNT BENEFICIARY.—

(A) TREATMENT IF DESIGNATED BENEFICIARY IS SPOUSE.—If the account beneficiary's surviving spouse acquires such beneficiary's interest in a health savings account by reason of being the designated beneficiary of such account at the death of the account beneficiary, such health savings account shall be treated as if the spouse were the account beneficiary.



## (B) OTHER CASES.—

(i) IN GENERAL.—If, by reason of the death of the account beneficiary, any person acquires the account beneficiary's interest in a health savings account in a case to which subparagraph (A) does not apply—

(I) such account shall cease to be a health savings account as of the date of death, and

(II) an amount equal to the fair market value of the assets in such account on such date shall be includible if such person is not the estate of such beneficiary, in such person's gross income for the taxable year which includes such date, or if such person is the estate of such beneficiary, in such beneficiary's gross income for the last taxable year of such beneficiary.

## (ii) SPECIAL RULES.—

(I) REDUCTION OF INCLUSION FOR PREDEATH EXPENSES.—The amount includible in gross income under clause (i) by any person (other than the estate) shall be reduced by the amount of qualified medical expenses which were incurred by the decedent before the date of the decedent's death and paid by such person within 1 year after such date.

(II) DEDUCTION FOR ESTATE TAXES.—An appropriate deduction shall be allowed under section 691(c) to any person (other than the decedent or the decedent's spouse) with respect to amounts included in gross income under clause (i) by such person.

## (g) COST-OF-LIVING ADJUSTMENT.—

(1) IN GENERAL.—Each dollar amount in subsections (b)(2) and (c)(2)(A) shall be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which such taxable year begins determined by substituting for "calendar year 2016" in subparagraph (A)(ii) thereof—

(i) except as provided in clause (ii), "calendar year 1997", and

(ii) in the case of each dollar amount in subsection (c)(2)(A), "calendar year 2003".

In the case of adjustments made for any taxable year beginning after 2007, section 1(f)(4) shall be applied for purposes of this paragraph by substituting "March 31" for "August 31", and the Secretary shall publish the adjusted amounts under subsections (b)(2) and (c)(2)(A) for taxable years beginning in any calendar year no later than June 1 of the preceding calendar year.

(2) ROUNDING.—If any increase under paragraph (1) is not a multiple of \$50, such increase shall be rounded to the nearest multiple of \$50.

## (h) REPORTS.—The Secretary may require—

(1) the trustee of a health savings account to make such reports regarding such account to the Secretary and to the account beneficiary with respect to contributions, distributions,

the return of excess contributions, and such other matters as the Secretary determines appropriate, and

(2) any person who provides an individual with a high deductible health plan to make such reports to the Secretary and to the account beneficiary with respect to such plan as the Secretary determines appropriate.

The reports required by this subsection shall be filed at such time and in such manner and furnished to such individuals at such time and in such manner as may be required by the Secretary.

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## PART VIII—SPECIAL DEDUCTIONS FOR CORPORATIONS

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## PART IX—ITEMS NOT DEDUCTIBLE

\* \* \* \* \*

### SEC. 274. DISALLOWANCE OF CERTAIN ENTERTAINMENT, ETC., EXPENSES.

(a) ENTERTAINMENT, AMUSEMENT, RECREATION, OR QUALIFIED TRANSPORTATION FRINGES.—

(1) IN GENERAL.—No deduction otherwise allowable under this chapter shall be allowed for any item—

(A) ACTIVITY.—With respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, or

(B) FACILITY.—With respect to a facility used in connection with an activity referred to in subparagraph (A).

(2) SPECIAL RULES.—For purposes of applying paragraph (1)—

(A) Dues or fees to any social, athletic, or sporting club or organization shall be treated as items with respect to facilities.

(B) An activity described in section 212 shall be treated as a trade or business.

(3) DENIAL OF DEDUCTION FOR CLUB DUES.—Notwithstanding the preceding provisions of this subsection, no deduction shall be allowed under this chapter for amounts paid or incurred for membership in any club organized for business, pleasure, recreation, or other social purpose.

(4) QUALIFIED TRANSPORTATION FRINGES.—No deduction shall be allowed under this chapter for the expense of any qualified transportation fringe (as defined in section 132(f)) provided to an employee of the taxpayer.

(b) GIFTS.—

(1) LIMITATION.—No deduction shall be allowed under section 162 or section 212 for any expense for gifts made directly or indirectly to any individual to the extent that such expense, when added to prior expenses of the taxpayer for gifts made to such individual during the same taxable year, exceeds \$25. For purposes of this section, the term “gift” means any item excludable from gross income of the recipient under section 102 which is not excludable from his gross income under any other provision of this chapter, but such term does not include—

(A) an item having a cost to the taxpayer not in excess of \$4.00 on which the name of the taxpayer is clearly and permanently imprinted and which is one of a number of identical items distributed generally by the taxpayer, or

(B) a sign, display rack, or other promotional material to be used on the business premises of the recipient.

(2) SPECIAL RULES.—

(A) In the case of a gift by a partnership, the limitation contained in paragraph (1) shall apply to the partnership as well as to each member thereof.

(B) For purposes of paragraph (1), a husband and wife shall be treated as one taxpayer.

(c) CERTAIN FOREIGN TRAVEL.—

(1) IN GENERAL.—In the case of any individual who travels outside the United States away from home in pursuit of a trade or business or in pursuit of an activity described in section 212, no deduction shall be allowed under section 162, or section 212 for that portion of the expenses of such travel otherwise allowable under such section which, under regulations prescribed by the Secretary, is not allocable to such trade or business or to such activity.

(2) EXCEPTION.—Paragraph (1) shall not apply to the expenses of any travel outside the United States away from home if—

(A) such travel does not exceed one week, or

(B) the portion of the time of travel outside the United States away from home which is not attributable to the pursuit of the taxpayer's trade or business or an activity described in section 212 is less than 25 percent of the total time on such travel.

(3) DOMESTIC TRAVEL EXCLUDED.—For purposes of this subsection, travel outside the United States does not include any travel from one point in the United States to another point in the United States.

(d) SUBSTANTIATION REQUIRED.—No deduction or credit shall be allowed—

(1) under section 162 or 212 for any traveling expense (including meals and lodging while away from home),

(2) for any expense for gifts, or

(3) with respect to any listed property (as defined in section 280F(d)(4)),

unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating the taxpayer's own statement (A) the amount of such expense or other item, (B) the time and place of the travel or the date and description of the gift, (C) the business purpose of the expense or other item, and (D) the business relationship to the taxpayer of the person receiving the benefit. The Secretary may by regulations provide that some or all of the requirements of the preceding sentence shall not apply in the case of an expense which does not exceed an amount prescribed pursuant to such regulations. This subsection shall not apply to any qualified nonpersonal use vehicle (as defined in subsection (i)).

(e) SPECIFIC EXCEPTIONS TO APPLICATION OF SUBSECTION (A).—Subsection (a) shall not apply to—

(1) **FOOD AND BEVERAGES FOR EMPLOYEES.**—Expenses for food and beverages (and facilities used in connection therewith) furnished on the business premises of the taxpayer primarily for his employees.

(2) **EXPENSES TREATED AS COMPENSATION.**—

(A) **IN GENERAL.**—Except as provided in subparagraph (B), expenses for goods, services, and facilities, to the extent that the expenses are treated by the taxpayer, with respect to the recipient of the entertainment, amusement, or recreation, as compensation to an employee on the taxpayer's return of tax under this chapter and as wages to such employee for purposes of chapter 24 (relating to withholding of income tax at source on wages).

(B) **SPECIFIED INDIVIDUALS.**—

(i) **IN GENERAL.**—In the case of a recipient who is a specified individual, subparagraph (A) and paragraph (9) shall each be applied by substituting “to the extent that the expenses do not exceed the amount of the expenses which” for “to the extent that the expenses”.

(ii) **SPECIFIED INDIVIDUAL.**—For purposes of clause (i), the term “specified individual” means any individual who—

(I) is subject to the requirements of section 16(a) of the Securities Exchange Act of 1934 with respect to the taxpayer or a related party to the taxpayer, or

(II) would be subject to such requirements if the taxpayer (or such related party) were an issuer of equity securities referred to in such section.

For purposes of this clause, a person is a related party with respect to another person if such person bears a relationship to such other person described in section 267(b) or 707(b).

(3) **REIMBURSED EXPENSES.**—Expenses paid or incurred by the taxpayer, in connection with the performance by him of services for another person (whether or not such other person is his employer), under a reimbursement or other expense allowance arrangement with such other person, but this paragraph shall apply—

(A) where the services are performed for an employer, only if the employer has not treated such expenses in the manner provided in paragraph (2), or

(B) where the services are performed for a person other than an employer, only if the taxpayer accounts (to the extent provided by subsection (d)) to such person.

(4) **RECREATIONAL, ETC., EXPENSES FOR EMPLOYEES.**—Expenses for recreational, social, or similar activities (including facilities therefor) primarily for the benefit of employees (other than employees who are highly compensated employees (within the meaning of section 414(q))). For purposes of this paragraph, an individual owning less than a 10-percent interest in the taxpayer's trade or business shall not be considered a shareholder or other owner, and for such purposes an individual shall be treated as owning any interest owned by a member of his family (within the meaning of section 267(c)(4)).

This paragraph shall not apply for purposes of subsection (a)(3).

(5) EMPLOYEES, STOCKHOLDER, ETC., BUSINESS MEETINGS.—Expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors.

(6) MEETINGS OF BUSINESS LEAGUES, ETC.—Expenses directly related and necessary to attendance at a business meeting or convention of any organization described in section 501(c)(6) (relating to business leagues, chambers of commerce, real estate boards, and boards of trade) and exempt from taxation under section 501(a).

(7) ITEMS AVAILABLE TO PUBLIC.—Expenses for goods, services, and facilities made available by the taxpayer to the general public.

(8) ENTERTAINMENT SOLD TO CUSTOMERS.—Expenses for goods or services (including the use of facilities) which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth.

(9) EXPENSES INCLUDIBLE IN INCOME OF PERSONS WHO ARE NOT EMPLOYEES.—Expenses paid or incurred by the taxpayer for goods, services, and facilities to the extent that the expenses are includible in the gross income of a recipient of the entertainment, amusement, or recreation who is not an employee of the taxpayer as compensation for services rendered or as a prize or award under section 74. The preceding sentence shall not apply to any amount paid or incurred by the taxpayer if such amount is required to be included (or would be so required except that the amount is less than \$600) in any information return filed by such taxpayer under part III of subchapter A of chapter 61 and is not so included.

For purposes of this subsection, any item referred to in subsection (a) shall be treated as an expense.

(f) INTEREST, TAXES, CASUALTY LOSSES, ETC.—This section shall not apply to any deduction allowable to the taxpayer without regard to its connection with his trade or business (or with his income-producing activity). In the case of a taxpayer which is not an individual, the preceding sentence shall be applied as if it were an individual.

(g) TREATMENT OF ENTERTAINMENT, ETC., TYPE FACILITY.—For purposes of this chapter, if deductions are disallowed under subsection (a) with respect to any portion of a facility, such portion shall be treated as an asset which is used for personal, living, and family purposes (and not as an asset used in the trade or business).

(h) ATTENDANCE AT CONVENTIONS, ETC.—

(1) IN GENERAL.—In the case of any individual who attends a convention, seminar, or similar meeting which is held outside the North American area, no deduction shall be allowed under section 162 for expenses allocable to such meeting unless the taxpayer establishes that the meeting is directly related to the active conduct of his trade or business and that, after taking into account in the manner provided by regulations prescribed by the Secretary—

(A) the purpose of such meeting and the activities taking place at such meeting,

(B) the purposes and activities of the sponsoring organizations or groups,

(C) the residences of the active members of the sponsoring organization and the places at which other meetings of the sponsoring organization or groups have been held or will be held, and

(D) such other relevant factors as the taxpayer may present, it is as reasonable for the meeting to be held outside the North American area as within the North American area.

(2) CONVENTIONS ON CRUISE SHIPS.—In the case of any individual who attends a convention, seminar, or other meeting which is held on any cruise ship, no deduction shall be allowed under section 162 for expenses allocable to such meeting, unless the taxpayer meets the requirements of paragraph (5) and establishes that the meeting is directly related to the active conduct of his trade or business and that—

(A) the cruise ship is a vessel registered in the United States; and

(B) all ports of call of such cruise ship are located in the United States or in possessions of the United States.

With respect to cruises beginning in any calendar year, not more than \$2,000 of the expenses attributable to an individual attending one or more meetings may be taken into account under section 162 by reason of the preceding sentence.

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

(A) NORTH AMERICAN AREA.—The term “North American area” means the United States, its possessions, and the Trust Territory of the Pacific Islands, and Canada and Mexico.

(B) CRUISE SHIP.—The term “cruise ship” means any vessel sailing within or without the territorial waters of the United States.

(4) SUBSECTION TO APPLY TO EMPLOYER AS WELL AS TO TRAVELER.—

(A) Except as provided in subparagraph (B), this subsection shall apply to deductions otherwise allowable under section 162 to any person, whether or not such person is the individual attending the convention, seminar, or similar meeting.

(B) This subsection shall not deny a deduction to any person other than the individual attending the convention, seminar, or similar meeting with respect to any amount paid by such person to or on behalf of such individual if includible in the gross income of such individual. The preceding sentence shall not apply if the amount is required to be included in any information return filed by such person under part III of subchapter A of chapter 61 and is not so included.

(5) REPORTING REQUIREMENTS.—No deduction shall be allowed under section 162 for expenses allocable to attendance at a convention, seminar, or similar meeting on any cruise ship unless the taxpayer claiming the deduction attaches to the return of tax on which the deduction is claimed—

(A) a written statement signed by the individual attending the meeting which includes—

(i) information with respect to the total days of the trip, excluding the days of transportation to and from the cruise ship port, and the number of hours of each day of the trip which such individual devoted to scheduled business activities,

(ii) a program of the scheduled business activities of the meeting, and

(iii) such other information as may be required in regulations prescribed by the Secretary; and

(B) a written statement signed by an officer of the organization or group sponsoring the meeting which includes—

(i) a schedule of the business activities of each day of the meeting,

(ii) the number of hours which the individual attending the meeting attended such scheduled business activities, and

(iii) such other information as may be required in regulations prescribed by the Secretary.

(6) TREATMENT OF CONVENTIONS IN CERTAIN CARIBBEAN COUNTRIES.—

(A) IN GENERAL.—For purposes of this subsection, the term “North American area” includes, with respect to any convention, seminar, or similar meeting, any beneficiary country if (as of the time such meeting begins)—

(i) there is in effect a bilateral or multilateral agreement described in subparagraph (C) between such country and the United States providing for the exchange of information between the United States and such country, and

(ii) there is not in effect a finding by the Secretary that the tax laws of such country discriminate against conventions held in the United States.

(B) BENEFICIARY COUNTRY.—For purposes of this paragraph, the term “beneficiary country” has the meaning given to such term by section 212(a)(1)(A) of the Caribbean Basin Economic Recovery Act; except that such term shall include Bermuda.

(C) AUTHORITY TO CONCLUDE EXCHANGE OF INFORMATION AGREEMENTS.—

(i) IN GENERAL.—The Secretary is authorized to negotiate and conclude an agreement for the exchange of information with any beneficiary country. Except as provided in clause (ii), an exchange of information agreement shall provide for the exchange of such information (not limited to information concerning nationals or residents of the United States or the beneficiary country) as may be necessary or appropriate to carry out and enforce the tax laws of the United States and the beneficiary country (whether criminal or civil proceedings), including information which may otherwise be subject to nondisclosure provisions of the local law of the beneficiary country such as provisions respecting bank secrecy and bearer shares. The ex-

change of information agreement shall be terminable by either country on reasonable notice and shall provide that information received by either country will be disclosed only to persons or authorities (including courts and administrative bodies) involved in the administration or oversight of, or in the determination of appeals in respect of, taxes of the United States or the beneficiary country and will be used by such persons or authorities only for such purposes.

(ii) NONDISCLOSURE OF QUALIFIED CONFIDENTIAL INFORMATION SOUGHT FOR CIVIL TAX PURPOSES.—An exchange of information agreement need not provide for the exchange of qualified confidential information which is sought only for civil tax purposes if—

(I) the Secretary of the Treasury, after making all reasonable efforts to negotiate an agreement which includes the exchange of such information, determines that such an agreement cannot be negotiated but that the agreement which was negotiated will significantly assist in the administration and enforcement of the tax laws of the United States, and

(II) the President determines that the agreement as negotiated is in the national security interest of the United States.

(iii) QUALIFIED CONFIDENTIAL INFORMATION DEFINED.—For purposes of this subparagraph, the term “qualified confidential information” means information which is subject to the nondisclosure provisions of any local law of the beneficiary country regarding bank secrecy or ownership of bearer shares.

(iv) CIVIL TAX PURPOSES.—For purposes of this subparagraph, the determination of whether information is sought only for civil tax purposes shall be made by the requesting party.

(D) COORDINATION WITH OTHER PROVISIONS.—Any exchange of information agreement negotiated under subparagraph (C) shall be treated as an income tax convention for purposes of section 6103(k)(4). The Secretary may exercise his authority under subchapter A of chapter 78 to carry out any obligation of the United States under an agreement referred to in subparagraph (C).

(E) DETERMINATIONS PUBLISHED IN THE FEDERAL REGISTER.—The following shall be published in the Federal Register—

(i) any determination by the President under subparagraph (C)(ii) (including the reasons for such determination),

(ii) any determination by the Secretary under subparagraph (C)(ii) (including the reasons for such determination), and

(iii) any finding by the Secretary under subparagraph (A)(ii) (and any termination thereof).



(7) SEMINARS, ETC. FOR SECTION 212 PURPOSES.—No deduction shall be allowed under section 212 for expenses allocable to a convention, seminar, or similar meeting.

(i) QUALIFIED NONPERSONAL USE VEHICLE.—For purposes of subsection (d), the term “qualified nonpersonal use vehicle” means any vehicle which, by reason of its nature, is not likely to be used more than a de minimis amount for personal purposes.

(j) EMPLOYEE ACHIEVEMENT AWARDS.—

(1) GENERAL RULE.—No deduction shall be allowed under section 162 or section 212 for the cost of an employee achievement award except to the extent that such cost does not exceed the deduction limitations of paragraph (2).

(2) DEDUCTION LIMITATIONS.—The deduction for the cost of an employee achievement award made by an employer to an employee—

(A) which is not a qualified plan award, when added to the cost to the employer for all other employee achievement awards made to such employee during the taxable year which are not qualified plan awards, shall not exceed \$400, and

(B) which is a qualified plan award, when added to the cost to the employer for all other employee achievement awards made to such employee during the taxable year (including employee achievement awards which are not qualified plan awards), shall not exceed \$1,600.

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

(A) EMPLOYEE ACHIEVEMENT AWARD.—

(i) IN GENERAL.—The term “employee achievement award” means an item of tangible personal property which is—

(I) transferred by an employer to an employee for length of service achievement or safety achievement,

(II) awarded as part of a meaningful presentation, and

(III) awarded under conditions and circumstances that do not create a significant likelihood of the payment of disguised compensation.

(ii) TANGIBLE PERSONAL PROPERTY.—For purposes of clause (i), the term “tangible personal property” shall not include—

(I) cash, cash equivalents, gift cards, gift coupons, or gift certificates (other than arrangements conferring only the right to select and receive tangible personal property from a limited array of such items pre-selected or pre-approved by the employer), or

(II) vacations, meals, lodging, tickets to theater or sporting events, stocks, bonds, other securities, and other similar items.

(B) QUALIFIED PLAN AWARD.—

(i) IN GENERAL.—The term “qualified plan award” means an employee achievement award awarded as part of an established written plan or program of the taxpayer which does not discriminate in favor of high-

ly compensated employees (within the meaning of section 414(q)) as to eligibility or benefits.

(ii) **LIMITATION.**—An employee achievement award shall not be treated as a qualified plan award for any taxable year if the average cost of all employee achievement awards which are provided by the employer during the year, and which would be qualified plan awards but for this subparagraph, exceeds \$400. For purposes of the preceding sentence, average cost shall be determined by including the entire cost of qualified plan awards, without taking into account employee achievement awards of nominal value.

(4) **SPECIAL RULES.**—For purposes of this subsection—

(A) **PARTNERSHIPS.**—In the case of an employee achievement award made by a partnership, the deduction limitations contained in paragraph (2) shall apply to the partnership as well as to each member thereof.

(B) **LENGTH OF SERVICE AWARDS.**—An item shall not be treated as having been provided for length of service achievement if the item is received during the recipient's 1st 5 years of employment or if the recipient received a length of service achievement award (other than an award excludable under section 132(e)(1)) during that year or any of the prior 4 years.

(C) **SAFETY ACHIEVEMENT AWARDS.**—An item provided by an employer to an employee shall not be treated as having been provided for safety achievement if—

(i) during the taxable year, employee achievement awards (other than awards excludable under section 132(e)(1)) for safety achievement have previously been awarded by the employer to more than 10 percent of the employees of the employer (excluding employees described in clause (ii)), or

(ii) such item is awarded to a manager, administrator, clerical employee, or other professional employee.

(k) **BUSINESS MEALS.**—

(1) **IN GENERAL.**—No deduction shall be allowed under this chapter for the expense of any food or beverages unless—

(A) such expense is not lavish or extravagant under the circumstances, and

(B) the taxpayer (or an employee of the taxpayer) is present at the furnishing of such food or beverages.

(2) **EXCEPTIONS.**—Paragraph (1) shall not apply to—

(A) any expense described in paragraph (2), (3), (4), (7), (8), or (9) of subsection (e), and

(B) any other expense to the extent provided in regulations.

(l) **TRANSPORTATION AND COMMUTING BENEFITS.**—

(1) **IN GENERAL.**—No deduction shall be allowed under this chapter for any expense incurred for providing any transportation, or any payment or reimbursement, to an employee of the taxpayer in connection with travel between the employee's residence and place of employment, except as necessary for ensuring the safety of the employee.

(2) EXCEPTION.—In the case of any qualified bicycle commuting reimbursement (as described in section 132(f)(5)(F)), this subsection shall not apply for any amounts paid or incurred [after December 31, 2017, and before January 1, 2026].

(m) ADDITIONAL LIMITATIONS ON TRAVEL EXPENSES.—

(1) LUXURY WATER TRANSPORTATION.—

(A) IN GENERAL.—No deduction shall be allowed under this chapter for expenses incurred for transportation by water to the extent such expenses exceed twice the aggregate per diem amounts for days of such transportation. For purposes of the preceding sentence, the term “per diem amounts” means the highest amount generally allowable with respect to a day to employees of the executive branch of the Federal Government for per diem while away from home but serving in the United States.

(B) EXCEPTIONS.—Subparagraph (A) shall not apply to—

- (i) any expense allocable to a convention, seminar, or other meeting which is held on any cruise ship, and
- (ii) any expense described in paragraph (2), (3), (4), (7), (8), or (9) of subsection (e).

(2) TRAVEL AS FORM OF EDUCATION.—No deduction shall be allowed under this chapter for expenses for travel as a form of education.

(3) TRAVEL EXPENSES OF SPOUSE, DEPENDENT, OR OTHERS.—No deduction shall be allowed under this chapter (other than section 217) for travel expenses paid or incurred with respect to a spouse, dependent, or other individual accompanying the taxpayer (or an officer or employee of the taxpayer) on business travel, unless—

(A) the spouse, dependent, or other individual is an employee of the taxpayer,

(B) the travel of the spouse, dependent, or other individual is for a bona fide business purpose, and

(C) such expenses would otherwise be deductible by the spouse, dependent, or other individual.

(n) ONLY 50 PERCENT OF MEAL EXPENSES ALLOWED AS DEDUCTION.—

(1) IN GENERAL.—The amount allowable as a deduction under this chapter for any expense for food or beverages shall not exceed 50 percent of the amount of such expense which would (but for this paragraph) be allowable as a deduction under this chapter.

(2) EXCEPTIONS.—Paragraph (1) shall not apply to any expense if—

(A) such expense is described in paragraph (2), (3), (4), (7), (8), or (9) of subsection (e),

(B) in the case of an employer who pays or reimburses moving expenses of an employee, such expenses are includible in the income of the employee under section 82, or

(C) such expense is for food or beverages—

(i) required by any Federal law to be provided to crew members of a commercial vessel,

(ii) provided to crew members of a commercial vessel—

(I) which is operating on the Great Lakes, the Saint Lawrence Seaway, or any inland waterway of the United States, and

(II) which is of a kind which would be required by Federal law to provide food and beverages to crew members if it were operated at sea,

(iii) provided on an oil or gas platform or drilling rig if the platform or rig is located offshore, or

(iv) provided on an oil or gas platform or drilling rig, or at a support camp which is in proximity and integral to such platform or rig, if the platform or rig is located in the United States north of 54 degrees north latitude.

Clauses (i) and (ii) of subparagraph (C) shall not apply to vessels primarily engaged in providing luxury water transportation (determined under the principles of subsection (m)). In the case of the employee, the exception of subparagraph (A) shall not apply to expenses described in subparagraph (B).

(3) SPECIAL RULE FOR INDIVIDUALS SUBJECT TO FEDERAL HOURS OF SERVICE.—In the case of any expenses for food or beverages consumed while away from home (within the meaning of section 162(a)(2)) by an individual during, or incident to, the period of duty subject to the hours of service limitations of the Department of Transportation, paragraph (1) shall be applied by substituting “80 percent” for “50 percent”.

(o) MEALS PROVIDED AT CONVENIENCE OF EMPLOYER.—No deduction shall be allowed under this chapter for—

(1) any expense for the operation of a facility described in section 132(e)(2), and any expense for food or beverages, including under section 132(e)(1), associated with such facility, or

(2) any expense for meals described in section 119(a).

(p) REGULATORY AUTHORITY.—The Secretary shall prescribe such regulations as he may deem necessary to carry out the purposes of this section, including regulations prescribing whether subsection (a) or subsection (b) applies in cases where both such subsections would otherwise apply.

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**Subchapter D—Deferred Compensation, Etc**

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**PART I—PENSION, PROFIT-SHARING, STOCK BONUS PLANS, ETC**

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**Subpart A—General Rule**

\* \* \* \* \*

**SEC. 401. QUALIFIED PENSION, PROFIT-SHARING, AND STOCK BONUS PLANS.**

(a) REQUIREMENTS FOR QUALIFICATION.—A trust created or organized in the United States and forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit

of his employees or their beneficiaries shall constitute a qualified trust under this section—

(1) if contributions are made to the trust by such employer, or employees, or both, or by another employer who is entitled to deduct his contributions under section 404(a)(3)(B) (relating to deduction for contributions to profit-sharing and stock bonus plans), or by a charitable remainder trust pursuant to a qualified gratuitous transfer (as defined in section 664(g)(1)), for the purpose of distributing to such employees or their beneficiaries the corpus and income of the fund accumulated by the trust in accordance with such plan;

(2) if under the trust instrument it is impossible, at any time prior to the satisfaction of all liabilities with respect to employees and their beneficiaries under the trust, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, purposes other than for the exclusive benefit of his employees or their beneficiaries (but this paragraph shall not be construed, in the case of a multiemployer plan, to prohibit the return of a contribution within 6 months after the plan administrator determines that the contribution was made by a mistake of fact or law (other than a mistake relating to whether the plan is described in section 401(a) or the trust which is part of such plan is exempt from taxation under section 501(a), or the return of any withdrawal liability payment determined to be an overpayment within 6 months of such determination));

(3) if the plan of which such trust is a part satisfies the requirements of section 410 (relating to minimum participation standards); and

(4) if the contributions or benefits provided under the plan do not discriminate in favor of highly compensated employees (within the meaning of section 414(q)). For purposes of this paragraph, there shall be excluded from consideration employees described in section 410(b)(3)(A) and (C).

(5) SPECIAL RULES RELATING TO NONDISCRIMINATION REQUIREMENTS.—

(A) SALARIED OR CLERICAL EMPLOYEES.—A classification shall not be considered discriminatory within the meaning of paragraph (4) or section 410(b)(2)(A)(i) merely because it is limited to salaried or clerical employees.

(B) CONTRIBUTIONS AND BENEFITS MAY BEAR UNIFORM RELATIONSHIP TO COMPENSATION.—A plan shall not be considered discriminatory within the meaning of paragraph (4) merely because the contributions or benefits of, or on behalf of, the employees under the plan bear a uniform relationship to the compensation (within the meaning of section 414(s)) of such employees.

(C) CERTAIN DISPARITY PERMITTED.—A plan shall not be considered discriminatory within the meaning of paragraph (4) merely because the contributions or benefits of, or on behalf of, the employees under the plan favor highly compensated employees (as defined in section 414(q)) in the manner permitted under subsection (1).

(D) INTEGRATED DEFINED BENEFIT PLAN.—

(i) IN GENERAL.—A defined benefit plan shall not be considered discriminatory within the meaning of paragraph (4) merely because the plan provides that the employer-derived accrued retirement benefit for any participant under the plan may not exceed the excess (if any) of—

(I) the participant's final pay with the employer, over

(II) the employer-derived retirement benefit created under Federal law attributable to service by the participant with the employer.

For purposes of this clause, the employer-derived retirement benefit created under Federal law shall be treated as accruing ratably over 35 years.

(ii) FINAL PAY.—For purposes of this subparagraph, the participant's final pay is the compensation (as defined in section 414(q)(4)) paid to the participant by the employer for any year—

(I) which ends during the 5-year period ending with the year in which the participant separated from service for the employer, and

(II) for which the participant's total compensation from the employer was highest.

(E) 2 OR MORE PLANS TREATED AS SINGLE PLAN.—For purposes of determining whether 2 or more plans of an employer satisfy the requirements of paragraph (4) when considered as a single plan—

(i) CONTRIBUTIONS.—If the amount of contributions on behalf of the employees allowed as a deduction under section 404 for the taxable year with respect to such plans, taken together, bears a uniform relationship to the compensation (within the meaning of section 414(s)) of such employees, the plans shall not be considered discriminatory merely because the rights of employees to, or derived from, the employer contributions under the separate plans do not become nonforfeitable at the same rate.

(ii) BENEFITS.—If the employees' rights to benefits under the separate plans do not become nonforfeitable at the same rate, but the levels of benefits provided by the separate plans satisfy the requirements of regulations prescribed by the Secretary to take account of the differences in such rates, the plans shall not be considered discriminatory merely because of the difference in such rates.

(F) SOCIAL SECURITY RETIREMENT AGE.—For purposes of testing for discrimination under paragraph (4)—

(i) the social security retirement age (as defined in section 415(b)(8)) shall be treated as a uniform retirement age, and

(ii) subsidized early retirement benefits and joint and survivor annuities shall not be treated as being unavailable to employees on the same terms merely because such benefits or annuities are based in whole

or in part on an employee's social security retirement age (as so defined).

(G) GOVERNMENTAL PLANS.—Paragraphs (3) and (4) shall not apply to a governmental plan (within the meaning of section 414(d)).

(6) A plan shall be considered as meeting the requirements of paragraph (3) during the whole of any taxable year of the plan if on one day in each quarter it satisfied such requirements.

(7) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part satisfies the requirements of section 411 (relating to minimum vesting standards).

(8) A trust forming part of a defined benefit plan shall not constitute a qualified trust under this section unless the plan provides that forfeitures must not be applied to increase the benefits any employee would otherwise receive under the plan.

(9) REQUIRED DISTRIBUTIONS.—

(A) IN GENERAL.—A trust shall not constitute a qualified trust under this subsection unless the plan provides that the entire interest of each employee—

(i) will be distributed to such employee not later than the required beginning date, or

(ii) will be distributed, beginning not later than the required beginning date, in accordance with regulations, over the life of such employee or over the lives of such employee and a designated beneficiary (or over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and a designated beneficiary).

(B) REQUIRED DISTRIBUTION WHERE EMPLOYEE DIES BEFORE ENTIRE INTEREST IS DISTRIBUTED.—

(i) WHERE DISTRIBUTIONS HAVE BEGUN UNDER SUBPARAGRAPH (A)(II).—A trust shall not constitute a qualified trust under this section unless the plan provides that if—

(I) the distribution of the employee's interest has begun in accordance with subparagraph (A)(ii), and

(II) the employee dies before his entire interest has been distributed to him,

the remaining portion of such interest will be distributed at least as rapidly as under the method of distributions being used under subparagraph (A)(ii) as of the date of his death.

(ii) 5-YEAR RULE FOR OTHER CASES.—A trust shall not constitute a qualified trust under this section unless the plan provides that, if an employee dies before the distribution of the employee's interest has begun in accordance with subparagraph (A)(ii), the entire interest of the employee will be distributed within 5 years after the death of such employee.

(iii) EXCEPTION TO 5-YEAR RULE FOR CERTAIN AMOUNTS PAYABLE OVER LIFE OF BENEFICIARY.—If—

(I) any portion of the employee's interest is payable to (or for the benefit of) a designated beneficiary,

(II) such portion will be distributed (in accordance with regulations) over the life of such designated beneficiary (or over a period not extending beyond the life expectancy of such beneficiary), and

(III) such distributions begin not later than 1 year after the date of the employee's death or such later date as the Secretary may by regulations prescribe,

for purposes of clause (ii), the portion referred to in subclause (I) shall be treated as distributed on the date on which such distributions begin.

(iv) SPECIAL RULE FOR SURVIVING SPOUSE OF EMPLOYEE.—If the designated beneficiary referred to in clause (iii)(I) is the surviving spouse of the employee—

(I) the date on which the distributions are required to begin under clause (iii)(III) shall not be earlier than the date on which the employee would have attained age 70 1/2, and

(II) if the surviving spouse dies before the distributions to such spouse begin, this subparagraph shall be applied as if the surviving spouse were the employee.

(C) REQUIRED BEGINNING DATE.—For purposes of this paragraph—

(i) IN GENERAL.—The term “required beginning date” means April 1 of the calendar year following the later of—

(I) the calendar year in which the employee attains age 70 1/2, or

(II) the calendar year in which the employee retires.

(ii) EXCEPTION.—Subclause (II) of clause (i) shall not apply—

(I) except as provided in section 409(d), in the case of an employee who is a 5-percent owner (as defined in section 416) with respect to the plan year ending in the calendar year in which the employee attains age 70 1/2, or

(II) for purposes of section 408(a)(6) or (b)(3).

(iii) ACTUARIAL ADJUSTMENT.—In the case of an employee to whom clause (i)(II) applies who retires in a calendar year after the calendar year in which the employee attains age 70 1/2, the employee's accrued benefit shall be actuarially increased to take into account the period after age 70 1/2 in which the employee was not receiving any benefits under the plan.

(iv) EXCEPTION FOR GOVERNMENTAL AND CHURCH PLANS.—Clauses (ii) and (iii) shall not apply in the case of a governmental plan or church plan. For purposes of this clause, the term “church plan” means a plan maintained by a church for church employees,



and the term “church” means any church (as defined in section 3121(w)(3)(A)) or qualified church-controlled organization (as defined in section 3121(w)(3)(B)).

(D) LIFE EXPECTANCY.—For purposes of this paragraph, the life expectancy of an employee and the employee’s spouse (other than in the case of a life annuity) may be re-determined but not more frequently than annually.

(E) DESIGNATED BENEFICIARY.—For purposes of this paragraph, the term “designated beneficiary” means any individual designated as a beneficiary by the employee.

(F) TREATMENT OF PAYMENTS TO CHILDREN.—Under regulations prescribed by the Secretary, for purposes of this paragraph, any amount paid to a child shall be treated as if it had been paid to the surviving spouse if such amount will become payable to the surviving spouse upon such child reaching majority (or other designated event permitted under regulations).

(G) TREATMENT OF INCIDENTAL DEATH BENEFIT DISTRIBUTIONS.—For purposes of this title, any distribution required under the incidental death benefit requirements of this subsection shall be treated as a distribution required under this paragraph.

(10) OTHER REQUIREMENTS.—

(A) PLANS BENEFITING OWNER-EMPLOYEES.—In the case of any plan which provides contributions or benefits for employees some or all of whom are owner-employees (as defined in subsection (c)(3)), a trust forming part of such plan shall constitute a qualified trust under this section only if the requirements of subsection (d) are also met.

(B) TOP-HEAVY PLANS.—

(i) IN GENERAL.—In the case of any top-heavy plan, a trust forming part of such plan shall constitute a qualified trust under this section only if the requirements of section 416 are met.

(ii) PLANS WHICH MAY BECOME TOP-HEAVY.—Except to the extent provided in regulations, a trust forming part of a plan (whether or not a top-heavy plan) shall constitute a qualified trust under this section only if such plan contains provisions—

(I) which will take effect if such plan becomes a top-heavy plan, and

(II) which meet the requirements of section 416.

(iii) EXEMPTION FOR GOVERNMENTAL PLANS.—This subparagraph shall not apply to any governmental plan.

(11) REQUIREMENT OF JOINT AND SURVIVOR ANNUITY AND PRERETIREMENT SURVIVOR ANNUITY.—

(A) IN GENERAL.—In the case of any plan to which this paragraph applies, except as provided in section 417, a trust forming part of such plan shall not constitute a qualified trust under this section unless—

(i) in the case of a vested participant who does not die before the annuity starting date, the accrued benefit payable to such participant is provided in the form of a qualified joint and survivor annuity, and

(ii) in the case of a vested participant who dies before the annuity starting date and who has a surviving spouse, a qualified preretirement survivor annuity is provided to the surviving spouse of such participant.

(B) PLANS TO WHICH PARAGRAPH APPLIES.—This paragraph shall apply to—

- (i) any defined benefit plan,
- (ii) any defined contribution plan which is subject to the funding standards of section 412, and
- (iii) any participant under any other defined contribution plan unless—

(I) such plan provides that the participant's nonforfeitable accrued benefit (reduced by any security interest held by the plan by reason of a loan outstanding to such participant) is payable in full, on the death of the participant, to the participant's surviving spouse (or, if there is no surviving spouse or the surviving spouse consents in the manner required under section 417(a)(2), to a designated beneficiary),

(II) such participant does not elect a payment of benefits in the form of a life annuity, and

(III) with respect to such participant, such plan is not a direct or indirect transferee (in a transfer after December 31, 1984) of a plan which is described in clause (i) or (ii) or to which this clause applied with respect to the participant.

Clause (iii)(III) shall apply only with respect to the transferred assets (and income therefrom) if the plan separately accounts for such assets and any income therefrom.

(C) EXCEPTION FOR CERTAIN ESOP BENEFITS.—

(i) IN GENERAL.—In the case of—

(I) a tax credit employee stock ownership plan (as defined in section 409(a)), or

(II) an employee stock ownership plan (as defined in section 4975(e)(7)),

subparagraph (A) shall not apply to that portion of the employee's accrued benefit to which the requirements of section 409(h) apply.

(ii) NONFORFEITABLE BENEFIT MUST BE PAID IN FULL, ETC.—In the case of any participant, clause (i) shall apply only if the requirements of subclauses (I), (II), and (III) of subparagraph (B)(iii) are met with respect to such participant.

(D) SPECIAL RULE WHERE PARTICIPANT AND SPOUSE MARRIED LESS THAN 1 YEAR.—A plan shall not be treated as failing to meet the requirements of subparagraphs (B)(iii) or (C) merely because the plan provides that benefits will not be payable to the surviving spouse of the participant unless the participant and such spouse had been married throughout the 1-year period ending on the earlier of the participant's annuity starting date or the date of the participant's death.

(E) EXCEPTION FOR PLANS DESCRIBED IN SECTION 404(C).—This paragraph shall not apply to a plan which the Sec-

retary has determined is a plan described in section 404(c) (or a continuation thereof) in which participation is substantially limited to individuals who, before January 1, 1976, ceased employment covered by the plan.

(F) CROSS REFERENCE.—For—

- (i) provisions under which participants may elect to waive the requirements of this paragraph, and
- (ii) other definitions and special rules for purposes of this paragraph,

see section 417.

(12) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that in the case of any merger or consolidation with, or transfer of assets or liabilities to, any other plan after September 2, 1974, each participant in the plan would (if the plan then terminated) receive a benefit immediately after the merger, consolidation, or transfer which is equal to or greater than the benefit he would have been entitled to receive immediately before the merger, consolidation, or transfer (if the plan had then terminated). The preceding sentence does not apply to any multiemployer plan with respect to any transaction to the extent that participants either before or after the transaction are covered under a multiemployer plan to which title IV of the Employee Retirement Income Security Act of 1974 applies.

(13) ASSIGNMENT AND ALIENATION.—

(A) IN GENERAL.—A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that benefits provided under the plan may not be assigned or alienated. For purposes of the preceding sentence, there shall not be taken into account any voluntary and revocable assignment of not to exceed 10 percent of any benefit payment made by any participant who is receiving benefits under the plan unless the assignment or alienation is made for purposes of defraying plan administration costs. For purposes of this paragraph a loan made to a participant or beneficiary shall not be treated as an assignment or alienation if such loan is secured by the participant's accrued nonforfeitable benefit and is exempt from the tax imposed by section 4975 (relating to tax on prohibited transactions) by reason of section 4975(d)(1). This paragraph shall take effect on January 1, 1976 and shall not apply to assignments which were irrevocable on September 2, 1974.

(B) SPECIAL RULES FOR DOMESTIC RELATIONS ORDERS.—Subparagraph (A) shall apply to the creation, assignment, or recognition of a right to any benefit payable with respect to a participant pursuant to a domestic relations order, except that subparagraph (A) shall not apply if the order is determined to be a qualified domestic relations order.

(C) SPECIAL RULE FOR CERTAIN JUDGMENTS AND SETTLEMENTS.—Subparagraph (A) shall not apply to any offset of a participant's benefits provided under a plan against an amount that the participant is ordered or required to pay to the plan if—

(i) the order or requirement to pay arises—

(I) under a judgment of conviction for a crime involving such plan,

(II) under a civil judgment (including a consent order or decree) entered by a court in an action brought in connection with a violation (or alleged violation) of part 4 of subtitle B of title I of the Employee Retirement Income Security Act of 1974, or

(III) pursuant to a settlement agreement between the Secretary of Labor and the participant, or a settlement agreement between the Pension Benefit Guaranty Corporation and the participant, in connection with a violation (or alleged violation) of part 4 of such subtitle by a fiduciary or any other person,

(ii) the judgment, order, decree, or settlement agreement expressly provides for the offset of all or part of the amount ordered or required to be paid to the plan against the participant's benefits provided under the plan, and

(iii) in a case in which the survivor annuity requirements of section 401(a)(11) apply with respect to distributions from the plan to the participant, if the participant has a spouse at the time at which the offset is to be made—

(I) either such spouse has consented in writing to such offset and such consent is witnessed by a notary public or representative of the plan (or it is established to the satisfaction of a plan representative that such consent may not be obtained by reason of circumstances described in section 417(a)(2)(B)), or an election to waive the right of the spouse to either a qualified joint and survivor annuity or a qualified preretirement survivor annuity is in effect in accordance with the requirements of section 417(a),

(II) such spouse is ordered or required in such judgment, order, decree, or settlement to pay an amount to the plan in connection with a violation of part 4 of such subtitle, or

(III) in such judgment, order, decree, or settlement, such spouse retains the right to receive the survivor annuity under a qualified joint and survivor annuity provided pursuant to section 401(a)(11)(A)(i) and under a qualified preretirement survivor annuity provided pursuant to section 401(a)(11)(A)(ii), determined in accordance with subparagraph (D).

A plan shall not be treated as failing to meet the requirements of this subsection, subsection (k), section 403(b), or section 409(d) solely by reason of an offset described in this subparagraph.

(D) SURVIVOR ANNUITY.—

(i) IN GENERAL.—The survivor annuity described in subparagraph (C)(iii)(III) shall be determined as if—

(I) the participant terminated employment on the date of the offset,

(II) there was no offset,

(III) the plan permitted commencement of benefits only on or after normal retirement age,

(IV) the plan provided only the minimum-required qualified joint and survivor annuity, and

(V) the amount of the qualified preretirement survivor annuity under the plan is equal to the amount of the survivor annuity payable under the minimum-required qualified joint and survivor annuity.

(ii) DEFINITION.—For purposes of this subparagraph, the term “minimum-required qualified joint and survivor annuity” means the qualified joint and survivor annuity which is the actuarial equivalent of the participant’s accrued benefit (within the meaning of section 411(a)(7)) and under which the survivor annuity is 50 percent of the amount of the annuity which is payable during the joint lives of the participant and the spouse.

(14) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that, unless the participant otherwise elects, the payment of benefits under the plan to the participant will begin not later than the 60th day after the latest of the close of the plan year in which—

(A) the date on which the participant attains the earlier of age 65 or the normal retirement age specified under the plan,

(B) occurs the 10th anniversary of the year in which the participant commenced participation in the plan, or

(C) the participant terminates his service with the employer.

In the case of a plan which provides for the payment of an early retirement benefit, a trust forming a part of such plan shall not constitute a qualified trust under this section unless a participant who satisfied the service requirements for such early retirement benefit, but separated from the service (with any nonforfeitable right to an accrued benefit) before satisfying the age requirement for such early retirement benefit, is entitled upon satisfaction of such age requirement to receive a benefit not less than the benefit to which he would be entitled at the normal retirement age, actuarially, reduced under regulations prescribed by the Secretary.

(15) A trust shall not constitute a qualified trust under this section unless under the plan of which such trust is a part—

(A) in the case of a participant or beneficiary who is receiving benefits under such plan, or

(B) in the case of a participant who is separated from the service and who has nonforfeitable rights to benefits, such benefits are not decreased by reason of any increase in the benefit levels payable under title II of the Social Security

Act or any increase in the wage base under such title II, if such increase takes place after September 2, 1974, or (if later) the earlier of the date of first receipt of such benefits or the date of such separation, as the case may be.

(16) A trust shall not constitute a qualified trust under this section if the plan of which such trust is a part provides for benefits or contributions which exceed the limitations of section 415.

(17) COMPENSATION LIMIT.—

(A) IN GENERAL.—A trust shall not constitute a qualified trust under this section unless, under the plan of which such trust is a part, the annual compensation of each employee taken into account under the plan for any year does not exceed \$200,000.

(B) COST-OF-LIVING ADJUSTMENT.—The Secretary shall adjust annually the \$200,000 amount in subparagraph (A) for increases in the cost-of-living at the same time and in the same manner as adjustments under section 415(d); except that the base period shall be the calendar quarter beginning July 1, 2001, and any increase which is not a multiple of \$5,000 shall be rounded to the next lowest multiple of \$5,000.

(19) A trust shall not constitute a qualified trust under this section if under the plan of which such trust is a part any part of a participant's accrued benefit derived from employer contributions (whether or not otherwise nonforfeitable), is forfeitable solely because of withdrawal by such participant of any amount attributable to the benefit derived from contributions made by such participant. The preceding sentence shall not apply to the accrued benefit of any participant unless, at the time of such withdrawal, such participant has a nonforfeitable right to at least 50 percent of such accrued benefit (as determined under section 411). The first sentence of this paragraph shall not apply to the extent that an accrued benefit is permitted to be forfeited in accordance with section 411(a)(3)(D)(iii) (relating to proportional forfeitures of benefits accrued before September 2, 1974, in the event of withdrawal of certain mandatory contributions).

(20) A trust forming part of a pension plan shall not be treated as failing to constitute a qualified trust under this section merely because the pension plan of which such trust is a part makes 1 or more distributions within 1 taxable year to a distributee on account of a termination of the plan of which the trust is a part, or in the case of a profit-sharing or stock bonus plan, a complete discontinuance of contributions under such plan. This paragraph shall not apply to a defined benefit plan unless the employer maintaining such plan files a notice with the Pension Benefit Guaranty Corporation (at the time and in the manner prescribed by the Pension Benefit Guaranty Corporation) notifying the Corporation of such payment or distribution and the Corporation has approved such payment or distribution or, within 90 days after the date on which such notice was filed, has failed to disapprove such payment or distribution. For purposes of this paragraph, rules similar to the rules of section 402(a)(6)(B) (as in effect before its repeal by

section 521 of the Unemployment Compensation Amendments of 1992) shall apply.

(22) If a defined contribution plan (other than a profit-sharing plan)—

(A) is established by an employer whose stock is not readily tradable on an established market, and

(B) after acquiring securities of the employer, more than 10 percent of the total assets of the plan are securities of the employer,

any trust forming part of such plan shall not constitute a qualified trust under this section unless the plan meets the requirements of subsection (e) of section 409. The requirements of subsection (e) of section 409 shall not apply to any employees of an employer who are participants in any defined contribution plan established and maintained by such employer if the stock of such employer is not readily tradable on an established market and the trade or business of such employer consists of publishing on a regular basis a newspaper for general circulation. For purposes of the preceding sentence, subsections (b), (c), (m), and (o) of section 414 shall not apply except for determining whether stock of the employer is not readily tradable on an established market.

(23) A stock bonus plan shall not be treated as meeting the requirements of this section unless such plan meets the requirements of subsections (h) and (o) of section 409, except that in applying section 409(h) for purposes of this paragraph, the term “employer securities” shall include any securities of the employer held by the plan.

(24) Any group trust which otherwise meets the requirements of this section shall not be treated as not meeting such requirements on account of the participation or inclusion in such trust of the moneys of any plan or governmental unit described in section 818(a)(6).

(25) REQUIREMENT THAT ACTUARIAL ASSUMPTIONS BE SPECIFIED.—A defined benefit plan shall not be treated as providing definitely determinable benefits unless, whenever the amount of any benefit is to be determined on the basis of actuarial assumptions, such assumptions are specified in the plan in a way which precludes employer discretion.

(26) ADDITIONAL PARTICIPATION REQUIREMENTS.—

(A) IN GENERAL.—In the case of a trust which is a part of a defined benefit plan, such trust shall not constitute a qualified trust under this subsection unless on each day of the plan year such trust benefits at least the lesser of—

(i) 50 employees of the employer, or

(ii) the greater of—

(I) 40 percent of all employees of the employer,

or

(II) 2 employees (or if there is only 1 employee, such employee).

(B) TREATMENT OF EXCLUDABLE EMPLOYEES.—

(i) IN GENERAL.—A plan may exclude from consideration under this paragraph employees described in paragraphs (3) and (4)(A) of section 410(b).

(ii) SEPARATE APPLICATION FOR CERTAIN EXCLUDABLE EMPLOYEES.—If employees described in section 410(b)(4)(B) are covered under a plan which meets the requirements of subparagraph (A) separately with respect to such employees, such employees may be excluded from consideration in determining whether any plan of the employer meets such requirements if—

(I) the benefits for such employees are provided under the same plan as benefits for other employees,

(II) the benefits provided to such employees are not greater than comparable benefits provided to other employees under the plan, and

(III) no highly compensated employee (within the meaning of section 414(q)) is included in the group of such employees for more than 1 year.

(C) SPECIAL RULE FOR COLLECTIVE BARGAINING UNITS.—Except to the extent provided in regulations, a plan covering only employees described in section 410(b)(3)(A) may exclude from consideration any employees who are not included in the unit or units in which the covered employees are included.

(D) PARAGRAPH NOT TO APPLY TO MULTIEMPLOYER PLANS.—Except to the extent provided in regulations, this paragraph shall not apply to employees in a multiemployer plan (within the meaning of section 414(f)) who are covered by collective bargaining agreements.

(E) SPECIAL RULE FOR CERTAIN DISPOSITIONS OR ACQUISITIONS.—Rules similar to the rules of section 410(b)(6)(C) shall apply for purposes of this paragraph.

(F) SEPARATE LINES OF BUSINESS.—At the election of the employer and with the consent of the Secretary, this paragraph may be applied separately with respect to each separate line of business of the employer. For purposes of this paragraph, the term “separate line of business” has the meaning given such term by section 414(r) (without regard to paragraph (2)(A) or (7) thereof).

(G) EXCEPTION FOR GOVERNMENTAL PLANS.—This paragraph shall not apply to a governmental plan (within the meaning of section 414(d)).

(H) REGULATIONS.—The Secretary may by regulation provide that any separate benefit structure, any separate trust, or any other separate arrangement is to be treated as a separate plan for purposes of applying this paragraph.

(27) DETERMINATIONS AS TO PROFIT-SHARING PLANS.—

(A) CONTRIBUTIONS NEED NOT BE BASED ON PROFITS.—The determination of whether the plan under which any contributions are made is a profit-sharing plan shall be made without regard to current or accumulated profits of the employer and without regard to whether the employer is a tax-exempt organization.

(B) PLAN MUST DESIGNATE TYPE.—In the case of a plan which is intended to be a money purchase pension plan or a profit-sharing plan, a trust forming part of such plan shall not constitute a qualified trust under this subsection



unless the plan designates such intent at such time and in such manner as the Secretary may prescribe.

(28) ADDITIONAL REQUIREMENTS RELATING TO EMPLOYEE STOCK OWNERSHIP PLANS.—

(A) IN GENERAL.—In the case of a trust which is part of an employee stock ownership plan (within the meaning of section 4975(e)(7)) or a plan which meets the requirements of section 409(a), such trust shall not constitute a qualified trust under this section unless such plan meets the requirements of subparagraphs (B) and (C).

(B) DIVERSIFICATION OF INVESTMENTS.—

(i) IN GENERAL.—A plan meets the requirements of this subparagraph if each qualified participant in the plan may elect within 90 days after the close of each plan year in the qualified election period to direct the plan as to the investment of at least 25 percent of the participant's account in the plan (to the extent such portion exceeds the amount to which a prior election under this subparagraph applies). In the case of the election year in which the participant can make his last election, the preceding sentence shall be applied by substituting "50 percent" for "25 percent".

(ii) METHOD OF MEETING REQUIREMENTS.—A plan shall be treated as meeting the requirements of clause (i) if—

(I) the portion of the participant's account covered by the election under clause (i) is distributed within 90 days after the period during which the election may be made, or

(II) the plan offers at least 3 investment options (not inconsistent with regulations prescribed by the Secretary) to each participant making an election under clause (i) and within 90 days after the period during which the election may be made, the plan invests the portion of the participant's account covered by the election in accordance with such election.

(iii) QUALIFIED PARTICIPANT.—For purposes of this subparagraph, the term "qualified participant" means any employee who has completed at least 10 years of participation under the plan and has attained age 55.

(iv) QUALIFIED ELECTION PERIOD.—For purposes of this subparagraph, the term "qualified election period" means the 6-plan-year period beginning with the later of—

(I) the 1st plan year in which the individual first became a qualified participant, or

(II) the 1st plan year beginning after December 31, 1986.

For purposes of the preceding sentence, an employer may elect to treat an individual first becoming a qualified participant in the 1st plan year beginning in 1987 as having become a participant in the 1st plan year beginning in 1988.

(v) EXCEPTION.—This subparagraph shall not apply to an applicable defined contribution plan (as defined in paragraph (35)(E)).

(C) USE OF INDEPENDENT APPRAISER.—A plan meets the requirements of this subparagraph if all valuations of employer securities which are not readily tradable on an established securities market with respect to activities carried on by the plan are by an independent appraiser. For purposes of the preceding sentence, the term “independent appraiser” means any appraiser meeting requirements similar to the requirements of the regulations prescribed under section 170(a)(1).

(29) BENEFIT LIMITATIONS.—In the case of a defined benefit plan (other than a multiemployer plan or a CSEC plan) to which the requirements of section 412 apply, the trust of which the plan is a part shall not constitute a qualified trust under this subsection unless the plan meets the requirements of section 436.

(30) LIMITATIONS ON ELECTIVE DEFERRALS.—In the case of a trust which is part of a plan under which elective deferrals (within the meaning of section 402(g)(3)) may be made with respect to any individual during a calendar year, such trust shall not constitute a qualified trust under this subsection unless the plan provides that the amount of such deferrals under such plan and all other plans, contracts, or arrangements of an employer maintaining such plan may not exceed the amount of the limitation in effect under section 402(g)(1)(A) for taxable years beginning in such calendar year.

(31) DIRECT TRANSFER OF ELIGIBLE ROLLOVER DISTRIBUTIONS.—

(A) IN GENERAL.—A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that if the distributee of any eligible rollover distribution—

(i) elects to have such distribution paid directly to an eligible retirement plan, and

(ii) specifies the eligible retirement plan to which such distribution is to be paid (in such form and at such time as the plan administrator may prescribe),

such distribution shall be made in the form of a direct trustee-to-trustee transfer to the eligible retirement plan so specified.

(B) CERTAIN MANDATORY DISTRIBUTIONS.—

(i) IN GENERAL.—In case of a trust which is part of an eligible plan, such trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that if—

(I) a distribution described in clause (ii) in excess of \$1,000 is made, and

(II) the distributee does not make an election under subparagraph (A) and does not elect to receive the distribution directly,

the plan administrator shall make such transfer to an individual retirement plan of a designated trustee or issuer and shall notify the distributee in writing (ei-

ther separately or as part of the notice under section 402(f) that the distribution may be transferred to another individual retirement plan.

(ii) **ELIGIBLE PLAN.**—For purposes of clause (i), the term “eligible plan” means a plan which provides that any nonforfeitable accrued benefit for which the present value (as determined under section 411(a)(11)) does not exceed \$5,000 shall be immediately distributed to the participant.

(C) **LIMITATION.**—Subparagraphs (A) and (B) shall apply only to the extent that the eligible rollover distribution would be includible in gross income if not transferred as provided in subparagraph (A) (determined without regard to sections 402(c), 403(a)(4), 403(b)(8), and 457(e)(16)). The preceding sentence shall not apply to such distribution if the plan to which such distribution is transferred—

(i) is a qualified trust which is part of a plan which is a defined contribution plan and agrees to separately account for amounts so transferred, including separately accounting for the portion of such distribution which is includible in gross income and the portion of such distribution which is not so includible, or

(ii) is an eligible retirement plan described in clause (i) or (ii) of section 402(c)(8)(B).

(D) **ELIGIBLE ROLLOVER DISTRIBUTION.**—For purposes of this paragraph, the term “eligible rollover distribution” has the meaning given such term by section 402(f)(2)(A).

(E) **ELIGIBLE RETIREMENT PLAN.**—For purposes of this paragraph, the term “eligible retirement plan” has the meaning given such term by section 402(c)(8)(B), except that a qualified trust shall be considered an eligible retirement plan only if it is a defined contribution plan, the terms of which permit the acceptance of rollover distributions.

(32) **TREATMENT OF FAILURE TO MAKE CERTAIN PAYMENTS IF PLAN HAS LIQUIDITY SHORTFALL.**—

(A) **IN GENERAL.**—A trust forming part of a pension plan to which section 430(j)(4) or 433(f)(5) applies shall not be treated as failing to constitute a qualified trust under this section merely because such plan ceases to make any payment described in subparagraph (B) during any period that such plan has a liquidity shortfall (as defined in section 430(j)(4) or 433(f)(5)).

(B) **PAYMENTS DESCRIBED.**—A payment is described in this subparagraph if such payment is—

(i) any payment, in excess of the monthly amount paid under a single life annuity (plus any social security supplements described in the last sentence of section 411(a)(9)), to a participant or beneficiary whose annuity starting date (as defined in section 417(f)(2)) occurs during the period referred to in subparagraph (A),

(ii) any payment for the purchase of an irrevocable commitment from an insurer to pay benefits, and

(iii) any other payment specified by the Secretary by regulations.

(C) PERIOD OF SHORTFALL.—For purposes of this paragraph, a plan has a liquidity shortfall during the period that there is an underpayment of an installment under section 430(j)(3) or 433(f) by reason of section 430(j)(4)(A) or 433(f)(5), respectively.

(33) PROHIBITION ON BENEFIT INCREASES WHILE SPONSOR IS IN BANKRUPTCY.—

(A) IN GENERAL.—A trust which is part of a plan to which this paragraph applies shall not constitute a qualified trust under this section if an amendment to such plan is adopted while the employer is a debtor in a case under title 11, United States Code, or similar Federal or State law, if such amendment increases liabilities of the plan by reason of

- (i) any increase in benefits,
- (ii) any change in the accrual of benefits, or
- (iii) any change in the rate at which benefits become nonforfeitable under the plan,

with respect to employees of the debtor, and such amendment is effective prior to the effective date of such employer's plan of reorganization.

(B) EXCEPTIONS.—This paragraph shall not apply to any plan amendment if—

- (i) the plan, were such amendment to take effect, would have a funding target attainment percentage (as defined in section 430(d)(2)) of 100 percent or more,
- (ii) the Secretary determines that such amendment is reasonable and provides for only de minimis increases in the liabilities of the plan with respect to employees of the debtor,
- (iii) such amendment only repeals an amendment described in section 412(d)(2), or
- (iv) such amendment is required as a condition of qualification under this part.

(C) PLANS TO WHICH THIS PARAGRAPH APPLIES.—This paragraph shall apply only to plans (other than multiemployer plans or CSEC plans) covered under section 4021 of the Employee Retirement Income Security Act of 1974.

(D) EMPLOYER.—For purposes of this paragraph, the term “employer” means the employer referred to in section 412(b)(1), without regard to section 412(b)(2).

(34) BENEFITS OF MISSING PARTICIPANTS ON PLAN TERMINATION.—In the case of a plan covered by title IV of the Employee Retirement Income Security Act of 1974, a trust forming part of such plan shall not be treated as failing to constitute a qualified trust under this section merely because the pension plan of which such trust is a part, upon its termination, transfers benefits of missing participants to the Pension Benefit Guaranty Corporation in accordance with section 4050 of such Act.

(35) DIVERSIFICATION REQUIREMENTS FOR CERTAIN DEFINED CONTRIBUTION PLANS.—

(A) IN GENERAL.—A trust which is part of an applicable defined contribution plan shall not be treated as a qualified trust unless the plan meets the diversification requirements of subparagraphs (B), (C), and (D).

(B) EMPLOYEE CONTRIBUTIONS AND ELECTIVE DEFERRALS INVESTED IN EMPLOYER SECURITIES.—In the case of the portion of an applicable individual's account attributable to employee contributions and elective deferrals which is invested in employer securities, a plan meets the requirements of this subparagraph if the applicable individual may elect to direct the plan to divest any such securities and to reinvest an equivalent amount in other investment options meeting the requirements of subparagraph (D).

(C) EMPLOYER CONTRIBUTIONS INVESTED IN EMPLOYER SECURITIES.—In the case of the portion of the account attributable to employer contributions other than elective deferrals which is invested in employer securities, a plan meets the requirements of this subparagraph if each applicable individual who—

(i) is a participant who has completed at least 3 years of service, or

(ii) is a beneficiary of a participant described in clause (i) or of a deceased participant,

may elect to direct the plan to divest any such securities and to reinvest an equivalent amount in other investment options meeting the requirements of subparagraph (D).

(D) INVESTMENT OPTIONS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if the plan offers not less than 3 investment options, other than employer securities, to which an applicable individual may direct the proceeds from the divestment of employer securities pursuant to this paragraph, each of which is diversified and has materially different risk and return characteristics.

(ii) TREATMENT OF CERTAIN RESTRICTIONS AND CONDITIONS.—

(I) TIME FOR MAKING INVESTMENT CHOICES.—A plan shall not be treated as failing to meet the requirements of this subparagraph merely because the plan limits the time for divestment and reinvestment to periodic, reasonable opportunities occurring no less frequently than quarterly.

(II) CERTAIN RESTRICTIONS AND CONDITIONS NOT ALLOWED.—Except as provided in regulations, a plan shall not meet the requirements of this subparagraph if the plan imposes restrictions or conditions with respect to the investment of employer securities which are not imposed on the investment of other assets of the plan. This subclause shall not apply to any restrictions or conditions imposed by reason of the application of securities laws.

(E) APPLICABLE DEFINED CONTRIBUTION PLAN.—For purposes of this paragraph—

(i) IN GENERAL.—The term “applicable defined contribution plan” means any defined contribution plan which holds any publicly traded employer securities.

(ii) EXCEPTION FOR CERTAIN ESOPS.—Such term does not include an employee stock ownership plan if—

(I) there are no contributions to such plan (or earnings thereunder) which are held within such plan and are subject to subsection (k) or (m), and

(II) such plan is a separate plan for purposes of section 414(l) with respect to any other defined benefit plan or defined contribution plan maintained by the same employer or employers.

(iii) EXCEPTION FOR ONE PARTICIPANT PLANS.—Such term does not include a one-participant retirement plan.

(iv) ONE-PARTICIPANT RETIREMENT PLAN.—For purposes of clause (iii), the term “one-participant retirement plan” means a retirement plan that on the first day of the plan year—

(I) covered only one individual (or the individual and the individual’s spouse) and the individual (or the individual and the individual’s spouse) owned 100 percent of the plan sponsor (whether or not incorporated), or

(II) covered only one or more partners (or partners and their spouses) in the plan sponsor.

(F) CERTAIN PLANS TREATED AS HOLDING PUBLICLY TRADED EMPLOYER SECURITIES.—

(i) IN GENERAL.—Except as provided in regulations or in clause (ii), a plan holding employer securities which are not publicly traded employer securities shall be treated as holding publicly traded employer securities if any employer corporation, or any member of a controlled group of corporations which includes such employer corporation, has issued a class of stock which is a publicly traded employer security.

(ii) EXCEPTION FOR CERTAIN CONTROLLED GROUPS WITH PUBLICLY TRADED SECURITIES.—Clause (i) shall not apply to a plan if—

(I) no employer corporation, or parent corporation of an employer corporation, has issued any publicly traded employer security, and

(II) no employer corporation, or parent corporation of an employer corporation, has issued any special class of stock which grants particular rights to, or bears particular risks for, the holder or issuer with respect to any corporation described in clause (i) which has issued any publicly traded employer security.

(iii) DEFINITIONS.—For purposes of this subparagraph, the term—

(I) “controlled group of corporations” has the meaning given such term by section 1563(a), ex-

cept that “50 percent” shall be substituted for “80 percent” each place it appears,

(II) “employer corporation” means a corporation which is an employer maintaining the plan, and

(III) “parent corporation” has the meaning given such term by section 424(e).

(G) OTHER DEFINITIONS.—For purposes of this paragraph—

(i) APPLICABLE INDIVIDUAL.—The term “applicable individual” means—

(I) any participant in the plan, and

(II) any beneficiary who has an account under the plan with respect to which the beneficiary is entitled to exercise the rights of a participant.

(ii) ELECTIVE DEFERRAL.—The term “elective deferral” means an employer contribution described in section 402(g)(3)(A).

(iii) EMPLOYER SECURITY.—The term “employer security” has the meaning given such term by section 407(d)(1) of the Employee Retirement Income Security Act of 1974.

(iv) EMPLOYEE STOCK OWNERSHIP PLAN.—The term “employee stock ownership plan” has the meaning given such term by section 4975(e)(7).

(v) PUBLICLY TRADED EMPLOYER SECURITIES.—The term “publicly traded employer securities” means employer securities which are readily tradable on an established securities market.

(vi) YEAR OF SERVICE.—The term “year of service” has the meaning given such term by section 411(a)(5).

(H) TRANSITION RULE FOR SECURITIES ATTRIBUTABLE TO EMPLOYER CONTRIBUTIONS.—

(i) RULES PHASED IN OVER 3 YEARS.—

(I) IN GENERAL.—In the case of the portion of an account to which subparagraph (C) applies and which consists of employer securities acquired in a plan year beginning before January 1, 2007, subparagraph (C) shall only apply to the applicable percentage of such securities. This subparagraph shall be applied separately with respect to each class of securities.

(II) EXCEPTION FOR CERTAIN PARTICIPANTS AGED 55 OR OVER.—Subclause (I) shall not apply to an applicable individual who is a participant who has attained age 55 and completed at least 3 years of service before the first plan year beginning after December 31, 2005.

(ii) APPLICABLE PERCENTAGE.—For purposes of clause (i), the applicable percentage shall be determined as follows:

| Plan year to which subparagraph (C) applies: | The applicable percentage is: |
|--|-------------------------------|
| 1st.....                                     | 33                            |

| Plan year to which subparagraph (C) applies: | The applicable percentage is: |
|--|-------------------------------|
| 2d.....                                      | 66                            |
| 3d and following.....                        | 100.                          |

(36) DISTRIBUTIONS DURING WORKING RETIREMENT.—A trust forming part of a pension plan shall not be treated as failing to constitute a qualified trust under this section solely because the plan provides that a distribution may be made from such trust to an employee who has attained age 62 and who is not separated from employment at the time of such distribution.

(37) DEATH BENEFITS UNDER USERRA-QUALIFIED ACTIVE MILITARY SERVICE.—A trust shall not constitute a qualified trust unless the plan provides that, in the case of a participant who dies while performing qualified military service (as defined in section 414(u)), the survivors of the participant are entitled to any additional benefits (other than benefit accruals relating to the period of qualified military service) provided under the plan had the participant resumed and then terminated employment on account of death.

Paragraphs (11), (12), (13), (14), (15), (19), and (20) shall apply only in the case of a plan to which section 411 (relating to minimum vesting standards) applies without regard to subsection (e)(2) of such section.

(b) CERTAIN RETROACTIVE CHANGES IN PLAN.—A stock bonus, pension, profit-sharing, or annuity plan shall be considered as satisfying the requirements of subsection (a) for the period beginning with the date on which it was put into effect, or for the period beginning with the earlier of the date on which there was adopted or put into effect any amendment which caused the plan to fail to satisfy such requirements, and ending with the time prescribed by law for filing the return of the employer for his taxable year in which such plan or amendment was adopted (including extensions thereof) or such later time as the Secretary may designate, if all provisions of the plan which are necessary to satisfy such requirements are in effect by the end of such period and have been made effective for all purposes for the whole of such period.

(c) DEFINITIONS AND RULES RELATING TO SELF-EMPLOYED INDIVIDUALS AND OWNER-EMPLOYEES.—For purposes of this section—

(1) SELF-EMPLOYED INDIVIDUAL TREATED AS EMPLOYEE.—

(A) IN GENERAL.—The term “employee” includes, for any taxable year, an individual who is a self-employed individual for such taxable year.

(B) SELF-EMPLOYED INDIVIDUAL.—The term “self-employed individual” means, with respect to any taxable year, an individual who has earned income (as defined in paragraph (2)) for such taxable year. To the extent provided in regulations prescribed by the Secretary, such term also includes, for any taxable year—

(i) an individual who would be a self-employed individual within the meaning of the preceding sentence but for the fact that the trade or business carried on by such individual did not have net profits for the taxable year, and



(ii) an individual who has been a self-employed individual within the meaning of the preceding sentence for any prior taxable year.

(2) EARNED INCOME.—

(A) IN GENERAL.—The term “earned income” means the net earnings from self-employment (as defined in section 1402(a)), but such net earnings shall be determined—

(i) only with respect to a trade or business in which personal services of the taxpayer are a material income-producing factor,

(ii) without regard to paragraphs (4) and (5) of section 1402(c),

(iii) in the case of any individual who is treated as an employee under subparagraph (A), (C), or (D) of section 3121(d)(3), without regard to section 1402(c)(2)

(iv) without regard to items which are not included in gross income for purposes of this chapter, and the deductions properly allocable to or chargeable against such items,

(v) with regard to the deductions allowed by section 404 to the taxpayer, and

(vi) with regard to the deduction allowed to the taxpayer by section 164(f).

For purposes of this subparagraph, section 1402, as in effect for a taxable year ending on December 31, 1962, shall be treated as having been in effect for all taxable years ending before such date. For purposes of this part only (other than sections 419 and 419A), this subparagraph shall be applied as if the term “trade or business” for purposes of section 1402 included service described in section 1402(c)(6).

(B) Repealed

(C) INCOME FROM DISPOSITION OF CERTAIN PROPERTY.—

For purposes of this section, the term “earned income” includes gains (other than any gain which is treated under any provision of this chapter as gain from the sale or exchange of a capital asset) and net earnings derived from the sale or other disposition of, the transfer of any interest in, or the licensing of the use of property (other than good will) by an individual whose personal efforts created such property.

(3) OWNER-EMPLOYEE.—The term “owner-employee” means an employee who—

(A) owns the entire interest in an unincorporated trade or business, or

(B) in the case of a partnership, is a partner who owns more than 10 percent of either the capital interest or the profits interest in such partnership.

To the extent provided in regulations prescribed by the Secretary, such term also means an individual who has been an owner-employee within the meaning of the preceding sentence.

(4) EMPLOYER.—An individual who owns the entire interest in an unincorporated trade or business shall be treated as his own employer. A partnership shall be treated as the employer

of each partner who is an employee within the meaning of paragraph (1).

(5) CONTRIBUTIONS ON BEHALF OF OWNER-EMPLOYEES.—The term “contribution on behalf of an owner-employee” includes, except as the context otherwise requires, a contribution under a plan—

- (A) by the employer for an owner-employee, and
- (B) by an owner-employee as an employee.

(6) SPECIAL RULE FOR CERTAIN FISHERMEN.—For purposes of this subsection, the term “self-employed individual” includes an individual described in section 3121(b)(20) (relating to certain fishermen).

(d) CONTRIBUTION LIMIT ON OWNER-EMPLOYEES.—A trust forming part of a pension or profit-sharing plan which provides contributions or benefits for employees some or all of whom are owner-employees shall constitute a qualified trust under this section only if, in addition to meeting the requirements of subsection (a), the plan provides that contributions on behalf of any owner-employee may be made only with respect to the earned income of such owner-employee which is derived from the trade or business with respect to which such plan is established.

(f) CERTAIN CUSTODIAL ACCOUNTS AND CONTRACTS.—For purposes of this title, a custodial account, an annuity contract, or a contract (other than a life, health or accident, property, casualty, or liability insurance contract) issued by an insurance company qualified to do business in a State shall be treated as a qualified trust under this section if—

(1) the custodial account or contract would, except for the fact that it is not a trust, constitute a qualified trust under this section, and

(2) in the case of a custodial account the assets thereof are held by a bank (as defined in section 408(n)) or another person who demonstrates, to the satisfaction of the Secretary, that the manner in which he will hold the assets will be consistent with the requirements of this section.

For purposes of this title, in the case of a custodial account or contract treated as a qualified trust under this section by reason of this subsection, the person holding the assets of such account or holding such contract shall be treated as the trustee thereof.

(g) ANNUITY DEFINED.—For purposes of this section and sections 402, 403, and 404, the term “annuity” includes a face-amount certificate, as defined in section 2(a)(15) of the Investment Company Act of 1940 (15 U.S.C., sec. 80a-2); but does not include any contract or certificate issued after December 31, 1962, which is transferable, if any person other than the trustee of a trust described in section 401(a) which is exempt from tax under section 501(a) is the owner of such contract or certificate.

(h) MEDICAL, ETC., BENEFITS FOR RETIRED EMPLOYEES AND THEIR SPOUSES AND DEPENDENTS.—Under regulations prescribed by the Secretary, and subject to the provisions of section 420, a pension or annuity plan may provide for the payment of benefits for sickness, accident, hospitalization, and medical expenses of retired employees, their spouses and their dependents, but only if—

(1) such benefits are subordinate to the retirement benefits provided by the plan,

(2) a separate account is established and maintained for such benefits,

(3) the employer's contributions to such separate account are reasonable and ascertainable,

(4) it is impossible, at any time prior to the satisfaction of all liabilities under the plan to provide such benefits, for any part of the corpus or income of such separate account to be (within the taxable year or thereafter) used for, or diverted to, any purpose other than the providing of such benefits,

(5) notwithstanding the provisions of subsection (a)(2), upon the satisfaction of all liabilities under the plan to provide such benefits, any amount remaining in such separate account must, under the terms of the plan, be returned to the employer, and

(6) in the case of an employee who is a key employee, a separate account is established and maintained for such benefits payable to such employee (and his spouse and dependents) and such benefits (to the extent attributable to plan years beginning after March 31, 1984, for which the employee is a key employee) are only payable to such employee (and his spouse and dependents) from such separate account.

For purposes of paragraph (6), the term "key employee" means any employee, who at any time during the plan year or any preceding plan year during which contributions were made on behalf of such employee, is or was a key employee as defined in section 416(i). 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. For purposes of this subsection, the term "dependent" shall include any individual who is a child (as defined in [section 152(f)(1)] *section 7706(f)(1)*) of a retired employee who as of the end of the calendar year has not attained age 27.

(i) CERTAIN UNION-NEGOTIATED PENSION PLANS.—In the case of a trust forming part of a pension plan which has been determined by the Secretary to constitute a qualified trust under subsection (a) and to be exempt from taxation under section 501(a) for a period beginning after contributions were first made to or for such trust, if it is shown to the satisfaction of the Secretary that—

(1) such trust was created pursuant to a collective bargaining agreement between employee representatives and one or more employers,

(2) any disbursements of contributions, made to or for such trust before the time as of which the Secretary or his delegate determined that the trust constituted a qualified trust, substantially complied with the terms of the trust, and the plan of which the trust is a part, as subsequently qualified, and

(3) before the time as of which the Secretary determined that the trust constitutes a qualified trust, the contributions to or for such trust were not used in a manner which would jeopardize the interests of its beneficiaries,

then such trust shall be considered as having constituted a qualified trust under subsection (a) and as having been exempt from

taxation under section 501(a) for the period beginning on the date on which contributions were first made to or for such trust and ending on the date such trust first constituted (without regard to this subsection) a qualified trust under subsection (a).

(k) CASH OR DEFERRED ARRANGEMENTS.—

(1) GENERAL RULE.—A profit-sharing or stock bonus plan, a pre-ERISA money purchase plan, or a rural cooperative plan shall not be considered as not satisfying the requirements of subsection (a) merely because the plan includes a qualified cash or deferred arrangement.

(2) QUALIFIED CASH OR DEFERRED ARRANGEMENT.—A qualified cash or deferred arrangement is any arrangement which is part of a profit-sharing or stock bonus plan, a pre-ERISA money purchase plan, or a rural cooperative plan which meets the requirements of subsection (a)—

(A) under which a covered employee may elect to have the employer make payments as contributions to a trust under the plan on behalf of the employee, or to the employee directly in cash;

(B) under which amounts held by the trust which are attributable to employer contributions made pursuant to the employee's election—

(i) may not be distributable to participants or other beneficiaries earlier than—

(I) severance from employment, death, or disability,

(II) an event described in paragraph (10),

(III) in the case of a profit-sharing or stock bonus plan, the attainment of age 59 1/2,

(IV) subject to the provisions of paragraph (14), upon hardship of the employee, or

(V) in the case of a qualified reservist distribution (as defined in section 72(t)(2)(G)(iii)), the date on which a period referred to in subclause (III) of such section begins, and

(ii) will not be distributable merely by reason of the completion of a stated period of participation or the lapse of a fixed number of years;

(C) which provides that an employee's right to his accrued benefit derived from employer contributions made to the trust pursuant to his election is nonforfeitable, and

(D) which does not require, as a condition of participation in the arrangement, that an employee complete a period of service with the employer (or employers) maintaining the plan extending beyond the period permitted under section 410(a)(1) (determined without regard to subparagraph (B)(i) thereof).

(3) APPLICATION OF PARTICIPATION AND DISCRIMINATION STANDARDS.—

(A) A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement unless—

(i) those employees eligible to benefit under the arrangement satisfy the provisions of section 410(b)(1), and

(ii) the actual deferral percentage for eligible highly compensated employees (as defined in paragraph (5)) for the plan year bears a relationship to the actual deferral percentage for all other eligible employees for the preceding plan year which meets either of the following tests:

(I) The actual deferral percentage for the group of eligible highly compensated employees is not more than the actual deferral percentage of all other eligible employees multiplied by 1.25.

(II) The excess of the actual deferral percentage for the group of eligible highly compensated employees over that of all other eligible employees is not more than 2 percentage points, and the actual deferral percentage for the group of eligible highly compensated employees is not more than the actual deferral percentage of all other eligible employees multiplied by 2.

If 2 or more plans which include cash or deferred arrangements are considered as 1 plan for purposes of section 401(a)(4) or 410(b), the cash or deferred arrangements included in such plans shall be treated as 1 arrangement for purposes of this subparagraph.

If any highly compensated employee is a participant under 2 or more cash or deferred arrangements of the employer, for purposes of determining the deferral percentage with respect to such employee, all such cash or deferred arrangements shall be treated as 1 cash or deferred arrangement. An arrangement may apply clause (ii) by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary.

(B) For purposes of subparagraph (A), the actual deferral percentage for a specified group of employees for a plan year shall be the average of the ratios (calculated separately for each employee in such group) of—

(i) the amount of employer contributions actually paid over to the trust on behalf of each such employee for such plan year, to

(ii) the employee's compensation for such plan year.

(C) A cash or deferred arrangement shall be treated as meeting the requirements of subsection (a)(4) with respect to contributions if the requirements of subparagraph (A)(ii) are met.

(D) For purposes of subparagraph (B), the employer contributions on behalf of any employee—

(i) shall include any employer contributions made pursuant to the employee's election under paragraph (2), and

(ii) under such rules as the Secretary may prescribe, may, at the election of the employer, include—

(I) matching contributions (as defined in 401(m)(4)(A)) which meet the requirements of paragraph (2)(B) and (C), and

(II) qualified nonelective contributions (within the meaning of section 401(m)(4)(C)).

(E) For purposes of this paragraph, in the case of the first plan year of any plan (other than a successor plan), the amount taken into account as the actual deferral percentage of nonhighly compensated employees for the preceding plan year shall be—

(i) 3 percent, or

(ii) if the employer makes an election under this subclause, the actual deferral percentage of nonhighly compensated employees determined for such first plan year.

(F) SPECIAL RULE FOR EARLY PARTICIPATION.—If an employer elects to apply section 410(b)(4)(B) in determining whether a cash or deferred arrangement meets the requirements of subparagraph (A)(i), the employer may, in determining whether the arrangement meets the requirements of subparagraph (A)(ii), exclude from consideration all eligible employees (other than highly compensated employees) who have not met the minimum age and service requirements of section 410(a)(1)(A).

(G) GOVERNMENTAL PLAN.—A governmental plan (within the meaning of section 414(d)) shall be treated as meeting the requirements of this paragraph.

(4) OTHER REQUIREMENTS.—

(A) BENEFITS (OTHER THAN MATCHING CONTRIBUTIONS) MUST NOT BE CONTINGENT ON ELECTION TO DEFER.—A cash or deferred arrangement of any employer shall not be treated as a qualified cash or deferred arrangement if any other benefit is conditioned (directly or indirectly) on the employee electing to have the employer make or not make contributions under the arrangement in lieu of receiving cash. The preceding sentence shall not apply to any matching contribution (as defined in section 401(m)) made by reason of such an election.

(B) ELIGIBILITY OF STATE AND LOCAL GOVERNMENTS AND TAX-EXEMPT ORGANIZATIONS.—

(i) TAX-EXEMPTS ELIGIBLE.—Except as provided in clause (ii), any organization exempt from tax under this subtitle may include a qualified cash or deferred arrangement as part of a plan maintained by it.

(ii) GOVERNMENTS INELIGIBLE.—A cash or deferred arrangement shall not be treated as a qualified cash or deferred arrangement if it is part of a plan maintained by a State or local government or political subdivision thereof, or any agency or instrumentality thereof. This clause shall not apply to a rural cooperative plan or to a plan of an employer described in clause (iii).

(iii) TREATMENT OF INDIAN TRIBAL GOVERNMENTS.—An employer which is an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), an agency or instrumentality of an Indian tribal government or subdivision thereof, or

a corporation chartered under Federal, State, or tribal law which is owned in whole or in part by any of the foregoing may include a qualified cash or deferred arrangement as part of a plan maintained by the employer.

(C) COORDINATION WITH OTHER PLANS.—Except as provided in section 401(m), any employer contribution made pursuant to an employee's election under a qualified cash or deferred arrangement shall not be taken into account for purposes of determining whether any other plan meets the requirements of section 401(a) or 410(b). This subparagraph shall not apply for purposes of determining whether a plan meets the average benefit requirement of section 410(b)(2)(A)(ii).

(5) HIGHLY COMPENSATED EMPLOYEE.—For purposes of this subsection, the term “highly compensated employee” has the meaning given such term by section 414(q).

(6) PRE-ERISA MONEY PURCHASE PLAN.—For purposes of this subsection, the term “pre-ERISA money purchase plan” means a pension plan—

(A) which is a defined contribution plan (as defined in section 414(i)),

(B) which was in existence on June 27, 1974, and which, on such date, included a salary reduction arrangement, and

(C) under which neither the employee contributions nor the employer contributions may exceed the levels provided for by the contribution formula in effect under the plan on such date.

(7) RURAL COOPERATIVE PLAN.—For purposes of this subsection—

(A) IN GENERAL.—The term “rural cooperative plan” means any pension plan—

(i) which is a defined contribution plan (as defined in section 414(i)), and

(ii) which is established and maintained by a rural cooperative.

(B) RURAL COOPERATIVE DEFINED.—For purposes of subparagraph (A), the term “rural cooperative” means—

(i) any organization which—

(I) is engaged primarily in providing electric service on a mutual or cooperative basis, or

(II) is engaged primarily in providing electric service to the public in its area of service and which is exempt from tax under this subtitle or which is a State or local government (or an agency or instrumentality thereof), other than a municipality (or an agency or instrumentality thereof),

(ii) any organization described in paragraph (4) or (6) of section 501(c) and at least 80 percent of the members of which are organizations described in clause (i),

(iii) a cooperative telephone company described in section 501(c)(12),

(iv) any organization which—

(I) is a mutual irrigation or ditch company described in section 501(c)(12) (without regard to the 85 percent requirement thereof), or

(II) is a district organized under the laws of a State as a municipal corporation for the purpose of irrigation, water conservation, or drainage, and

(v) an organization which is a national association of organizations described in clause (i), (ii), (iii), or (iv).

(C) SPECIAL RULE FOR CERTAIN DISTRIBUTIONS.—A rural cooperative plan which includes a qualified cash or deferred arrangement shall not be treated as violating the requirements of section 401(a) or of paragraph (2) merely by reason of a hardship distribution or a distribution to a participant after attainment of age 59 1/2. For purposes of this section, the term “hardship distribution” means a distribution described in paragraph (2)(B)(i)(IV) (without regard to the limitation of its application to profit-sharing or stock bonus plans).

(8) ARRANGEMENT NOT DISQUALIFIED IF EXCESS CONTRIBUTIONS DISTRIBUTED.—

(A) IN GENERAL.—A cash or deferred arrangement shall not be treated as failing to meet the requirements of clause (ii) of paragraph (3)(A) for any plan year if, before the close of the following plan year—

(i) the amount of the excess contributions for such plan year (and any income allocable to such contributions through the end of such year) is distributed, or

(ii) to the extent provided in regulations, the employee elects to treat the amount of the excess contributions as an amount distributed to the employee and then contributed by the employee to the plan.

Any distribution of excess contributions (and income) may be made without regard to any other provision of law.

(B) EXCESS CONTRIBUTIONS.—For purposes of subparagraph (A), the term “excess contributions” means, with respect to any plan year, the excess of—

(i) the aggregate amount of employer contributions actually paid over to the trust on behalf of highly compensated employees for such plan year, over

(ii) the maximum amount of such contributions permitted under the limitations of clause (ii) of paragraph (3)(A) (determined by reducing contributions made on behalf of highly compensated employees in order of the actual deferral percentages beginning with the highest of such percentages).

(C) METHOD OF DISTRIBUTING EXCESS CONTRIBUTIONS.—Any distribution of the excess contributions for any plan year shall be made to highly compensated employees on the basis of the amount of contributions by, or on behalf of, each of such employees.

(D) ADDITIONAL TAX UNDER SECTION 72(T) NOT TO APPLY.—No tax shall be imposed under section 72(t) on any amount required to be distributed under this paragraph.



(E) TREATMENT OF MATCHING CONTRIBUTIONS FORFEITED BY REASON OF EXCESS DEFERRAL OR CONTRIBUTION OR PERMISSIBLE WITHDRAWAL.—For purposes of paragraph (2)(C), a matching contribution (within the meaning of subsection (m)) shall not be treated as forfeitable merely because such contribution is forfeitable if the contribution to which the matching contribution relates is treated as an excess contribution under subparagraph (B), an excess deferral under section 402(g)(2)(A), a permissible withdrawal under section 414(w), or an excess aggregate contribution under section 401(m)(6)(B).

(F) CROSS REFERENCE.—For excise tax on certain excess contributions, see section 4979.

(9) COMPENSATION.—For purposes of this subsection, the term “compensation” has the meaning given such term by section 414(s).

(10) DISTRIBUTIONS UPON TERMINATION OF PLAN.—

(A) IN GENERAL.—An event described in this subparagraph is the termination of the plan without establishment or maintenance of another defined contribution plan (other than an employee stock ownership plan as defined in section 4975(e)(7)).

(B) DISTRIBUTIONS MUST BE LUMP SUM DISTRIBUTIONS.—

(i) IN GENERAL.—A termination shall not be treated as described in subparagraph (A) with respect to any employee unless the employee receives a lump sum distribution by reason of the termination.

(ii) LUMP-SUM DISTRIBUTION.—For purposes of this subparagraph, the term “lump-sum distribution” has the meaning given such term by section 402(e)(4)(D) (without regard to subclauses (I), (II), (III), and (IV) of clause (i) thereof). Such term includes a distribution of an annuity contract from—

(I) a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501(a), or

(II) an annuity plan described in section 403(a).

(11) ADOPTION OF SIMPLE PLAN TO MEET NONDISCRIMINATION TESTS.—

(A) IN GENERAL.—A cash or deferred arrangement maintained by an eligible employer shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement meets—

(i) the contribution requirements of subparagraph

(B),

(ii) the exclusive plan requirements of subparagraph (C), and

(iii) the vesting requirements of section 408(p)(3).

(B) CONTRIBUTION REQUIREMENTS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement—

(I) an employee may elect to have the employer make elective contributions for the year on behalf of the employee to a trust under the plan in an amount which is expressed as a percentage of

compensation of the employee but which in no event exceeds the amount in effect under section 408(p)(2)(A)(ii),

(II) the employer is required to make a matching contribution to the trust for the year in an amount equal to so much of the amount the employee elects under subclause (I) as does not exceed 3 percent of compensation for the year, and

(III) no other contributions may be made other than contributions described in subclause (I) or (II).

(ii) EMPLOYER MAY ELECT 2-PERCENT NONELECTIVE CONTRIBUTION.—An employer shall be treated as meeting the requirements of clause (i)(II) for any year if, in lieu of the contributions described in such clause, the employer elects (pursuant to the terms of the arrangement) to make nonelective contributions of 2 percent of compensation for each employee who is eligible to participate in the arrangement and who has at least \$5,000 of compensation from the employer for the year. If an employer makes an election under this subparagraph for any year, the employer shall notify employees of such election within a reasonable period of time before the 60th day before the beginning of such year.

(iii) ADMINISTRATIVE REQUIREMENTS.—

(I) IN GENERAL.—Rules similar to the rules of subparagraphs (B) and (C) of section 408(p)(5) shall apply for purposes of this subparagraph.

(II) NOTICE OF ELECTION PERIOD.—The requirements of this subparagraph shall not be treated as met with respect to any year unless the employer notifies each employee eligible to participate, within a reasonable period of time before the 60th day before the beginning of such year (and, for the first year the employee is so eligible, the 60th day before the first day such employee is so eligible), of the rules similar to the rules of section 408(p)(5)(C) which apply by reason of subclause (I).

(C) EXCLUSIVE PLAN REQUIREMENT.—The requirements of this subparagraph are met for any year to which this paragraph applies if no contributions were made, or benefits were accrued, for services during such year under any qualified plan of the employer on behalf of any employee eligible to participate in the cash or deferred arrangement, other than contributions described in subparagraph (B).

(D) DEFINITIONS AND SPECIAL RULE.—

(i) DEFINITIONS.—For purposes of this paragraph, any term used in this paragraph which is also used in section 408(p) shall have the meaning given such term by such section.

(ii) COORDINATION WITH TOP-HEAVY RULES.—A plan meeting the requirements of this paragraph for any year shall not be treated as a top-heavy plan under

section 416 for such year if such plan allows only contributions required under this paragraph.

(12) ALTERNATIVE METHODS OF MEETING NONDISCRIMINATION REQUIREMENTS.—

(A) IN GENERAL.—A cash or deferred arrangement shall be treated as meeting the requirements of paragraph (3)(A)(ii) if such arrangement—

- (i) meets the contribution requirements of subparagraph (B) or (C), and
- (ii) meets the notice requirements of subparagraph (D).

(B) MATCHING CONTRIBUTIONS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement, the employer makes matching contributions on behalf of each employee who is not a highly compensated employee in an amount equal to—

(I) 100 percent of the elective contributions of the employee to the extent such elective contributions do not exceed 3 percent of the employee's compensation, and

(II) 50 percent of the elective contributions of the employee to the extent that such elective contributions exceed 3 percent but do not exceed 5 percent of the employee's compensation.

(ii) RATE FOR HIGHLY COMPENSATED EMPLOYEES.—The requirements of this subparagraph are not met if, under the arrangement, the rate of matching contribution with respect to any elective contribution of a highly compensated employee at any rate of elective contribution is greater than that with respect to an employee who is not a highly compensated employee.

(iii) ALTERNATIVE PLAN DESIGNS.—If the rate of any matching contribution with respect to any rate of elective contribution is not equal to the percentage required under clause (i), an arrangement shall not be treated as failing to meet the requirements of clause (i) if—

(I) the rate of an employer's matching contribution does not increase as an employee's rate of elective contributions increase, and

(II) the aggregate amount of matching contributions at such rate of elective contribution is at least equal to the aggregate amount of matching contributions which would be made if matching contributions were made on the basis of the percentages described in clause (i).

(C) NONELECTIVE CONTRIBUTIONS.—The requirements of this subparagraph are met if, under the arrangement, the employer is required, without regard to whether the employer makes an elective contribution or employee contribution, to make a contribution to a defined contribution plan on behalf of each employee who is not a highly compensated employee and who is eligible to participate in the

arrangement in an amount equal to at least 3 percent of the employee's compensation.

(D) NOTICE REQUIREMENT.—An arrangement meets the requirements of this paragraph if, under the arrangement, each employee eligible to participate is, within a reasonable period before any year, given written notice of the employee's rights and obligations under the arrangement which—

- (i) is sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and
- (ii) is written in a manner calculated to be understood by the average employee eligible to participate.

(E) OTHER REQUIREMENTS.—

(i) WITHDRAWAL AND VESTING RESTRICTIONS.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) of this paragraph unless the requirements of subparagraphs (B) and (C) of paragraph (2) are met with respect to all employer contributions (including matching contributions) taken into account in determining whether the requirements of subparagraphs (B) and (C) of this paragraph are met.

(ii) SOCIAL SECURITY AND SIMILAR CONTRIBUTIONS NOT TAKEN INTO ACCOUNT.—An arrangement shall not be treated as meeting the requirements of subparagraph (B) or (C) unless such requirements are met without regard to subsection (l), and, for purposes of subsection (l), employer contributions under subparagraph (B) or (C) shall not be taken into account.

(F) OTHER PLANS.—An arrangement shall be treated as meeting the requirements under subparagraph (A)(i) if any other plan maintained by the employer meets such requirements with respect to employees eligible under the arrangement.

(13) ALTERNATIVE METHOD FOR AUTOMATIC CONTRIBUTION ARRANGEMENTS TO MEET NONDISCRIMINATION REQUIREMENTS.—

(A) IN GENERAL.—A qualified automatic contribution arrangement shall be treated as meeting the requirements of paragraph (3)(A)(ii).

(B) QUALIFIED AUTOMATIC CONTRIBUTION ARRANGEMENT.—For purposes of this paragraph, the term “qualified automatic contribution arrangement” means any cash or deferred arrangement which meets the requirements of subparagraphs (C) through (E).

(C) AUTOMATIC DEFERRAL.—

(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement, each employee eligible to participate in the arrangement is treated as having elected to have the employer make elective contributions in an amount equal to a qualified percentage of compensation.

(ii) ELECTION OUT.—The election treated as having been made under clause (i) shall cease to apply with respect to any employee if such employee makes an affirmative election—

(I) to not have such contributions made, or

(II) to make elective contributions at a level specified in such affirmative election.

(iii) QUALIFIED PERCENTAGE.—For purposes of this subparagraph, the term “qualified percentage” means, with respect to any employee, any percentage determined under the arrangement if such percentage is applied uniformly, does not exceed 10 percent, and is at least—

(I) 3 percent during the period ending on the last day of the first plan year which begins after the date on which the first elective contribution described in clause (i) is made with respect to such employee,

(II) 4 percent during the first plan year following the plan year described in subclause (I),

(III) 5 percent during the second plan year following the plan year described in subclause (I), and

(IV) 6 percent during any subsequent plan year.

(iv) AUTOMATIC DEFERRAL FOR CURRENT EMPLOYEES NOT REQUIRED.—Clause (i) may be applied without taking into account any employee who—

(I) was eligible to participate in the arrangement (or a predecessor arrangement) immediately before the date on which such arrangement becomes a qualified automatic contribution arrangement (determined after application of this clause), and

(II) had an election in effect on such date either to participate in the arrangement or to not participate in the arrangement.

(D) MATCHING OR NONELECTIVE CONTRIBUTIONS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if, under the arrangement, the employer—

(I) makes matching contributions on behalf of each employee who is not a highly compensated employee in an amount equal to the sum of 100 percent of the elective contributions of the employee to the extent that such contributions do not exceed 1 percent of compensation plus 50 percent of so much of such contributions as exceed 1 percent but do not exceed 6 percent of compensation, or

(II) is required, without regard to whether the employee makes an elective contribution or employee contribution, to make a contribution to a defined contribution plan on behalf of each employee who is not a highly compensated employee and who is eligible to participate in the arrangement in an amount equal to at least 3 percent of the employee’s compensation.

(ii) APPLICATION OF RULES FOR MATCHING CONTRIBUTIONS.—The rules of clauses (ii) and (iii) of paragraph (12)(B) shall apply for purposes of clause (i)(I).

(iii) WITHDRAWAL AND VESTING RESTRICTIONS.—An arrangement shall not be treated as meeting the requirements of clause (i) unless, with respect to employer contributions (including matching contributions) taken into account in determining whether the requirements of clause (i) are met—

(I) any employee who has completed at least 2 years of service (within the meaning of section 411(a)) has a nonforfeitable right to 100 percent of the employee's accrued benefit derived from such employer contributions, and

(II) the requirements of subparagraph (B) of paragraph (2) are met with respect to all such employer contributions.

(iv) APPLICATION OF CERTAIN OTHER RULES.—The rules of subparagraphs (E)(ii) and (F) of paragraph (12) shall apply for purposes of subclauses (I) and (II) of clause (i).

(E) NOTICE REQUIREMENTS.—

(i) IN GENERAL.—The requirements of this subparagraph are met if, within a reasonable period before each plan year, each employee eligible to participate in the arrangement for such year receives written notice of the employee's rights and obligations under the arrangement which—

(I) is sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and

(II) is written in a manner calculated to be understood by the average employee to whom the arrangement applies.

(ii) TIMING AND CONTENT REQUIREMENTS.—A notice shall not be treated as meeting the requirements of clause (i) with respect to an employee unless—

(I) the notice explains the employee's right under the arrangement to elect not to have elective contributions made on the employee's behalf (or to elect to have such contributions made at a different percentage),

(II) in the case of an arrangement under which the employee may elect among 2 or more investment options, the notice explains how contributions made under the arrangement will be invested in the absence of any investment election by the employee, and

(III) the employee has a reasonable period of time after receipt of the notice described in subclauses (I) and (II) and before the first elective contribution is made to make either such election.

(14) SPECIAL RULES RELATING TO HARDSHIP WITHDRAWALS.—For purposes of paragraph (2)(B)(i)(IV)—

- (A) AMOUNTS WHICH MAY BE WITHDRAWN.—The following amounts may be distributed upon hardship of the employee:
- (i) Contributions to a profit-sharing or stock bonus plan to which section 402(e)(3) applies.
  - (ii) Qualified nonelective contributions (as defined in subsection (m)(4)(C)).
  - (iii) Qualified matching contributions described in paragraph (3)(D)(ii)(I).
  - (iv) Earnings on any contributions described in clause (i), (ii), or (iii).
- (B) NO REQUIREMENT TO TAKE AVAILABLE LOAN.—A distribution shall not be treated as failing to be made upon the hardship of an employee solely because the employee does not take any available loan under the plan.
- (1) PERMITTED DISPARITY IN PLAN CONTRIBUTIONS OR BENEFITS.—
- (1) IN GENERAL.—The requirements of this subsection are met with respect to a plan if—
    - (A) in the case of a defined contribution plan, the requirements of paragraph (2) are met, and
    - (B) in the case of a defined benefit plan, the requirements of paragraph (3) are met.
  - (2) DEFINED CONTRIBUTION PLAN.—
    - (A) IN GENERAL.—A defined contribution plan meets the requirements of this paragraph if the excess contribution percentage does not exceed the base contribution percentage by more than the lesser of—
      - (i) the base contribution percentage, or
      - (ii) the greater of—
        - (I) 5.7 percentage points, or
        - (II) the percentage equal to the portion of the rate of tax under section 3111(a) (in effect as of the beginning of the year) which is attributable to old-age insurance.
    - (B) CONTRIBUTION PERCENTAGES.—For purposes of this paragraph—
      - (i) EXCESS CONTRIBUTION PERCENTAGE.—The term “excess contribution percentage” means the percentage of compensation which is contributed by the employer under the plan with respect to that portion of each participant’s compensation in excess of the integration level.
      - (ii) BASE CONTRIBUTION PERCENTAGE.—The term “base contribution percentage” means the percentage of compensation contributed by the employer under the plan with respect to that portion of each participant’s compensation not in excess of the integration level.
  - (3) DEFINED BENEFIT PLAN.—A defined benefit plan meets the requirements of this paragraph if—
    - (A) EXCESS PLANS.—
      - (i) IN GENERAL.—In the case of a plan other than an offset plan—

(I) the excess benefit percentage does not exceed the base benefit percentage by more than the maximum excess allowance,

(II) any optional form of benefit, preretirement benefit, actuarial factor, or other benefit or feature provided with respect to compensation in excess of the integration level is provided with respect to compensation not in excess of such level, and

(III) benefits are based on average annual compensation.

(ii) **BENEFIT PERCENTAGES.**—For purposes of this subparagraph, the excess and base benefit percentages shall be computed in the same manner as the excess and base contribution percentages under paragraph (2)(B), except that such determination shall be made on the basis of benefits attributable to employer contributions rather than contributions.

(B) **OFFSET PLANS.**—In the case of an offset plan, the plan provides that—

(i) a participant's accrued benefit attributable to employer contributions (within the meaning of section 411(c)(1)) may not be reduced (by reason of the offset) by more than the maximum offset allowance, and

(ii) benefits are based on average annual compensation.

(4) **DEFINITIONS RELATING TO PARAGRAPH (3).**—For purposes of paragraph (3)—

(A) **MAXIMUM EXCESS ALLOWANCE.**—The maximum excess allowance is equal to—

(i) in the case of benefits attributable to any year of service with the employer taken into account under the plan,  $\frac{3}{4}$  of a percentage point, and

(ii) in the case of total benefits,  $\frac{3}{4}$  of a percentage point, multiplied by the participant's years of service (not in excess of 35) with the employer taken into account under the plan.

In no event shall the maximum excess allowance exceed the base benefit percentage.

(B) **MAXIMUM OFFSET ALLOWANCE.**—The maximum offset allowance is equal to—

(i) in the case of benefits attributable to any year of service with the employer taken into account under the plan,  $\frac{3}{4}$  percent of the participant's final average compensation, and

(ii) in the case of total benefits,  $\frac{3}{4}$  percent of the participant's final average compensation, multiplied by the participant's years of service (not in excess of 35) with the employer taken into account under the plan.

In no event shall the maximum offset allowance exceed 50 percent of the benefit which would have accrued without regard to the offset reduction.

(C) **REDUCTIONS.**—

(i) **IN GENERAL.**—The Secretary shall prescribe regulations requiring the reduction of the  $\frac{3}{4}$  percentage factor under subparagraph (A) or (B)—



(I) in the case of a plan other than an offset plan which has an integration level in excess of covered compensation, or

(II) with respect to any participant in an offset plan who has final average compensation in excess of covered compensation.

(ii) BASIS OF REDUCTIONS.—Any reductions under clause (i) shall be based on the percentages of compensation replaced by the employer-derived portions of primary insurance amounts under the Social Security Act for participants with compensation in excess of covered compensation.

(D) OFFSET PLAN.—The term “offset plan” means any plan with respect to which the benefit attributable to employer contributions for each participant is reduced by an amount specified in the plan.

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

(A) INTEGRATION LEVEL.—

(i) IN GENERAL.—The term “integration level” means the amount of compensation specified under the plan (by dollar amount or formula) at or below which the rate at which contributions or benefits are provided (expressed as a percentage) is less than such rate above such amount.

(ii) LIMITATION.—The integration level for any year may not exceed the contribution and benefit base in effect under section 230 of the Social Security Act for such year.

(iii) LEVEL TO APPLY TO ALL PARTICIPANTS.—A plan’s integration level shall apply with respect to all participants in the plan.

(iv) MULTIPLE INTEGRATION LEVELS.—Under rules prescribed by the Secretary, a defined benefit plan may specify multiple integration levels.

(B) COMPENSATION.—The term “compensation” has the meaning given such term by section 414(s).

(C) AVERAGE ANNUAL COMPENSATION.—The term “average annual compensation” means the participant’s highest average annual compensation for—

- (i) any period of at least 3 consecutive years, or
- (ii) if shorter, the participant’s full period of service.

(D) FINAL AVERAGE COMPENSATION.—

(i) IN GENERAL.—The term “final average compensation” means the participant’s average annual compensation for—

(I) the 3-consecutive year period ending with the current year, or

(II) if shorter, the participant’s full period of service.

(ii) LIMITATION.—A participant’s final average compensation shall be determined by not taking into account in any year compensation in excess of the contribution and benefit base in effect under section 230 of the Social Security Act for such year.

## (E) COVERED COMPENSATION.—

(i) IN GENERAL.—The term “covered compensation” means, with respect to an employee, the average of the contribution and benefit bases in effect under section 230 of the Social Security Act for each year in the 35-year period ending with the year in which the employee attains the social security retirement age.

(ii) COMPUTATION FOR ANY YEAR.—For purposes of clause (i), the determination for any year preceding the year in which the employee attains the social security retirement age shall be made by assuming that there is no increase in the bases described in clause (i) after the determination year and before the employee attains the social security retirement age.

(iii) SOCIAL SECURITY RETIREMENT AGE.—For purposes of this subparagraph, the term “social security retirement age” has the meaning given such term by section 415(b)(8).

(F) REGULATIONS.—The Secretary shall prescribe such regulations as are necessary or appropriate to carry out the purposes of this subsection, including—

(i) in the case of a defined benefit plan which provides for unreduced benefits commencing before the social security retirement age (as defined in section 415(b)(8)), rules providing for the reduction of the maximum excess allowance and the maximum offset allowance, and

(ii) in the case of an employee covered by 2 or more plans of the employer which fail to meet the requirements of subsection (a)(4) (without regard to this subsection), rules preventing the multiple use of the disparity permitted under this subsection with respect to any employee.

For purposes of clause (i), unreduced benefits shall not include benefits for disability (within the meaning of section 223(d) of the Social Security Act).

(6) SPECIAL RULE FOR PLAN MAINTAINED BY RAILROADS.—In determining whether a plan which includes employees of a railroad employer who are entitled to benefits under the Railroad Retirement Act of 1974 meets the requirements of this subsection, rules similar to the rules set forth in this subsection shall apply. Such rules shall take into account the employer-derived portion of the employees’ tier 2 railroad retirement benefits and any supplemental annuity under the Railroad Retirement Act of 1974.

(m) NONDISCRIMINATION TEST FOR MATCHING CONTRIBUTIONS AND EMPLOYEE CONTRIBUTIONS.—

(1) IN GENERAL.—A defined contribution plan shall be treated as meeting the requirements of subsection (a)(4) with respect to the amount of any matching contribution or employee contribution for any plan year only if the contribution percentage requirement of paragraph (2) of this subsection is met for such plan year.

(2) REQUIREMENTS.—

(A) CONTRIBUTION PERCENTAGE REQUIREMENT.—A plan meets the contribution percentage requirement of this paragraph for any plan year only if the contribution percentage for eligible highly compensated employees for such plan year does not exceed the greater of—

- (i) 125 percent of such percentage for all other eligible employees for the preceding plan year, or
- (ii) the lesser of 200 percent of such percentage for all other eligible employees for the preceding plan year, or such percentage for all other eligible employees for the preceding plan year plus 2 percentage points.

This subparagraph may be applied by using the plan year rather than the preceding plan year if the employer so elects, except that if such an election is made, it may not be changed except as provided by the Secretary.

(B) MULTIPLE PLANS TREATED AS A SINGLE PLAN.—If two or more plans of an employer to which matching contributions, employee contributions, or elective deferrals are made are treated as one plan for purposes of section 410(b), such plans shall be treated as one plan for purposes of this subsection. If a highly compensated employee participates in two or more plans of an employer to which contributions to which this subsection applies are made, all such contributions shall be aggregated for purposes of this subsection.

(3) CONTRIBUTION PERCENTAGE.—For purposes of paragraph (2), the contribution percentage for a specified group of employees for a plan year shall be the average of the ratios (calculated separately for each employee in such group) of—

- (A) the sum of the matching contributions and employee contributions paid under the plan on behalf of each such employee for such plan year, to
- (B) the employee's compensation (within the meaning of section 414(s)) for such plan year.

Under regulations, an employer may elect to take into account (in computing the contribution percentage) elective deferrals and qualified nonelective contributions under the plan or any other plan of the employer. If matching contributions are taken into account for purposes of subsection (k)(3)(A)(ii) for any plan year, such contributions shall not be taken into account under subparagraph (A) for such year. Rules similar to the rules of subsection (k)(3)(E) shall apply for purposes of this subsection.

(4) DEFINITIONS.—For purposes of this subsection—

(A) MATCHING CONTRIBUTION.—The term “matching contribution” means—

- (i) any employer contribution made to a defined contribution plan on behalf of an employee on account of an employee contribution made by such employee, and
- (ii) any employer contribution made to a defined contribution plan on behalf of an employee on account of an employee's elective deferral.

(B) ELECTIVE DEFERRAL.—The term “elective deferral” means any employer contribution described in section 402(g)(3).

(C) QUALIFIED NONELECTIVE CONTRIBUTIONS.—The term “qualified nonelective contribution” means any employer contribution (other than a matching contribution) with respect to which—

(i) the employee may not elect to have the contribution paid to the employee in cash instead of being contributed to the plan, and

(ii) the requirements of subparagraphs (B) and (C) of subsection (k)(2) are met.

(5) EMPLOYEES TAKEN INTO CONSIDERATION.—

(A) IN GENERAL.—Any employee who is eligible to make an employee contribution (or, if the employer takes elective contributions into account, elective contributions) or to receive a matching contribution under the plan being tested under paragraph (1) shall be considered an eligible employee for purposes of this subsection.

(B) CERTAIN NONPARTICIPANTS.—If an employee contribution is required as a condition of participation in the plan, any employee who would be a participant in the plan if such employee made such a contribution shall be treated as an eligible employee on behalf of whom no employer contributions are made.

(C) SPECIAL RULE FOR EARLY PARTICIPATION.—If an employer elects to apply section 410(b)(4)(B) in determining whether a plan meets the requirements of section 410(b), the employer may, in determining whether the plan meets the requirements of paragraph (2), exclude from consideration all eligible employees (other than highly compensated employees) who have not met the minimum age and service requirements of section 410(a)(1)(A).

(6) PLAN NOT DISQUALIFIED IF EXCESS AGGREGATE CONTRIBUTIONS DISTRIBUTED BEFORE END OF FOLLOWING PLAN YEAR.—

(A) IN GENERAL.—A plan shall not be treated as failing to meet the requirements of paragraph (1) for any plan year if, before the close of the following plan year, the amount of the excess aggregate contributions for such plan year (and any income allocable to such contributions through the end of such year) is distributed (or, if forfeitable, is forfeited). Such contributions (and such income) may be distributed without regard to any other provision of law.

(B) EXCESS AGGREGATE CONTRIBUTIONS.—For purposes of subparagraph (A), the term “excess aggregate contributions” means, with respect to any plan year, the excess of—

(i) the aggregate amount of the matching contributions and employee contributions (and any qualified nonelective contribution or elective contribution taken into account in computing the contribution percentage) actually made on behalf of highly compensated employees for such plan year, over

(ii) the maximum amount of such contributions permitted under the limitations of paragraph (2)(A) (determined by reducing contributions made on behalf of highly compensated employees in order of their con-

tribution percentages beginning with the highest of such percentages).

(C) METHOD OF DISTRIBUTING EXCESS AGGREGATE CONTRIBUTIONS.—Any distribution of the excess aggregate contributions for any plan year shall be made to highly compensated employees on the basis of the amount of contributions on behalf of, or by, each such employee. Forfeitures of excess aggregate contributions may not be allocated to participants whose contributions are reduced under this paragraph.

(D) COORDINATION WITH SUBSECTION (K) AND 402(G).—The determination of the amount of excess aggregate contributions with respect to a plan shall be made after—

- (i) first determining the excess deferrals (within the meaning of section 402(g)), and
- (ii) then determining the excess contributions under subsection (k).

(7) TREATMENT OF DISTRIBUTIONS.—

(A) ADDITIONAL TAX OF SECTION 72(T) NOT APPLICABLE.—No tax shall be imposed under section 72(t) on any amount required to be distributed under paragraph (6).

(B) EXCLUSION OF EMPLOYEE CONTRIBUTIONS.—Any distribution attributable to employee contributions shall not be included in gross income except to the extent attributable to income on such contributions.

(8) HIGHLY COMPENSATED EMPLOYEE.—For purposes of this subsection, the term “highly compensated employee” has the meaning given to such term by section 414(q).

(9) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subsection and subsection (k), including regulations permitting appropriate aggregation of plans and contributions.

(10) ALTERNATIVE METHOD OF SATISFYING TESTS.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

(A) meets the contribution requirements of subparagraph (B) of subsection (k)(11),

(B) meets the exclusive plan requirements of subsection (k)(11)(C), and

(C) meets the vesting requirements of section 408(p)(3).

(11) ADDITIONAL ALTERNATIVE METHOD OF SATISFYING TESTS.—

(A) IN GENERAL.—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

(i) meets the contribution requirements of subparagraph (B) or (C) of subsection (k)(12),

(ii) meets the notice requirements of subsection (k)(12)(D), and

(iii) meets the requirements of subparagraph (B).

(B) LIMITATION ON MATCHING CONTRIBUTIONS.—The requirements of this subparagraph are met if—

(i) matching contributions on behalf of any employee may not be made with respect to an employee’s con-

tributions or elective deferrals in excess of 6 percent of the employee's compensation,

(ii) the rate of an employer's matching contribution does not increase as the rate of an employee's contributions or elective deferrals increase, and

(iii) the matching contribution with respect to any highly compensated employee at any rate of an employee contribution or rate of elective deferral is not greater than that with respect to an employee who is not a highly compensated employee.

(12) **ALTERNATIVE METHOD FOR AUTOMATIC CONTRIBUTION ARRANGEMENTS.**—A defined contribution plan shall be treated as meeting the requirements of paragraph (2) with respect to matching contributions if the plan—

(A) is a qualified automatic contribution arrangement (as defined in subsection (k)(13)), and

(B) meets the requirements of paragraph (11)(B).

(13) **CROSS REFERENCE.**—For excise tax on certain excess contributions, see section 4979.

(n) **COORDINATION WITH QUALIFIED DOMESTIC RELATIONS ORDERS.**—The Secretary shall prescribe such rules or regulations as may be necessary to coordinate the requirements of subsection (a)(13)(B) and section 414(p) (and the regulations issued by the Secretary of Labor thereunder) with the other provisions of this chapter.

(o) **CROSS REFERENCE.**—For exemption from tax of a trust qualified under this section, see section 501(a).

**SEC. 402. TAXABILITY OF BENEFICIARY OF EMPLOYEES' TRUST.**

(a) **TAXABILITY OF BENEFICIARY OF EXEMPT TRUST.**—Except as otherwise provided in this section, any amount actually distributed to any distributee by any employees' trust described in section 401(a) which is exempt from tax under section 501(a) shall be taxable to the distributee, in the taxable year of the distributee in which distributed, under section 72 (relating to annuities).

(b) **TAXABILITY OF BENEFICIARY OF NONEXEMPT TRUST.**—

(1) **CONTRIBUTIONS.**—Contributions to an employees' trust made by an employer during a taxable year of the employer which ends with or within a taxable year of the trust for which the trust is not exempt from tax under section 501(a) shall be included in the gross income of the employee in accordance with section 83 (relating to property transferred in connection with performance of services), except that the value of the employee's interest in the trust shall be substituted for the fair market value of the property for purposes of applying such section.

(2) **DISTRIBUTIONS.**—The amount actually distributed or made available to any distributee by any trust described in paragraph (1) shall be taxable to the distributee, in the taxable year in which so distributed or made available, under section 72 (relating to annuities), except that distributions of income of such trust before the annuity starting date (as defined in section 72(c)(4)) shall be included in the gross income of the employee without regard to section 72(e)(5) (relating to amounts not received as annuities).

(3) GRANTOR TRUSTS.—A beneficiary of any trust described in paragraph (1) shall not be considered the owner of any portion of such trust under subpart E of part I of subchapter J (relating to grantors and others treated as substantial owners).

(4) Failure to meet requirements of section 410(b)

(A) HIGHLY COMPENSATED EMPLOYEES.—If 1 of the reasons a trust is not exempt from tax under section 501(a) is the failure of the plan of which it is a part to meet the requirements of section 401(a)(26) or 410(b), then a highly compensated employee shall, in lieu of the amount determined under paragraph (1) or (2) include in gross income for the taxable year with or within which the taxable year of the trust ends an amount equal to the vested accrued benefit of such employee (other than the employee's investment in the contract) as of the close of such taxable year of the trust.

(B) FAILURE TO MEET COVERAGE TESTS.—If a trust is not exempt from tax under section 501(a) for any taxable year solely because such trust is part of a plan which fails to meet the requirements of section 401(a)(26) or 410(b), paragraphs (1) and (2) shall not apply by reason of such failure to any employee who was not a highly compensated employee during—

(i) such taxable year, or

(ii) any preceding period for which service was creditable to such employee under the plan.

(C) HIGHLY COMPENSATED EMPLOYEE.—For purposes of this paragraph, the term “highly compensated employee” has the meaning given such term by section 414(q).

(c) RULES APPLICABLE TO ROLLOVERS FROM EXEMPT TRUSTS.—

(1) EXCLUSION FROM INCOME.—If—

(A) any portion of the balance to the credit of an employee in a qualified trust is paid to the employee in an eligible rollover distribution,

(B) the distributee transfers any portion of the property received in such distribution to an eligible retirement plan, and

(C) in the case of a distribution of property other than money, the amount so transferred consists of the property distributed,

then such distribution (to the extent so transferred) shall not be includible in gross income for the taxable year in which paid.

(2) MAXIMUM AMOUNT WHICH MAY BE ROLLED OVER.—In the case of any eligible rollover distribution, the maximum amount transferred to which paragraph (1) applies shall not exceed the portion of such distribution which is includible in gross income (determined without regard to paragraph (1)). The preceding sentence shall not apply to such distribution to the extent—

(A) such portion is transferred in a direct trustee-to-trustee transfer to a qualified trust or to an annuity contract described in section 403(b) and such trust or contract provides for separate accounting for amounts so transferred (and earnings thereon), including separately accounting for the portion of such distribution which is in-

cludible in gross income and the portion of such distribution which is not so includible, or

(B) such portion is transferred to an eligible retirement plan described in clause (i) or (ii) of paragraph (8)(B). In the case of a transfer described in subparagraph (A) or (B), the amount transferred shall be treated as consisting first of the portion of such distribution that is includible in gross income (determined without regard to paragraph (1)).

(3) TIME LIMIT ON TRANSFERS.—

(A) IN GENERAL.—Except as provided in subparagraphs (B) and (C), paragraph (1) shall not apply to any transfer of a distribution made after the 60th day following the day on which the distributee received the property distributed.

(B) HARDSHIP EXCEPTION.—The Secretary may waive the 60-day requirement under subparagraph (A) where the failure to waive such requirement would be against equity or good conscience, including casualty, disaster, or other events beyond the reasonable control of the individual subject to such requirement.

(C) ROLLOVER OF CERTAIN PLAN LOAN OFFSET AMOUNTS.—

(i) IN GENERAL.—In the case of a qualified plan loan offset amount, paragraph (1) shall not apply to any transfer of such amount made after the due date (including extensions) for filing the return of tax for the taxable year in which such amount is treated as distributed from a qualified employer plan.

(ii) QUALIFIED PLAN LOAN OFFSET AMOUNT.—For purposes of this subparagraph, the term “qualified plan loan offset amount” means a plan loan offset amount which is treated as distributed from a qualified employer plan to a participant or beneficiary solely by reason of—

(I) the termination of the qualified employer plan, or

(II) the failure to meet the repayment terms of the loan from such plan because of the severance from employment of the participant.

(iii) PLAN LOAN OFFSET AMOUNT.—For purposes of clause (ii), the term “plan loan offset amount” means the amount by which the participant’s accrued benefit under the plan is reduced in order to repay a loan from the plan.

(iv) LIMITATION.—This subparagraph shall not apply to any plan loan offset amount unless such plan loan offset amount relates to a loan to which section 72(p)(1) does not apply by reason of section 72(p)(2).

(v) QUALIFIED EMPLOYER PLAN.—For purposes of this subsection, the term “qualified employer plan” has the meaning given such term by section 72(p)(4).

(4) ELIGIBLE ROLLOVER DISTRIBUTION.—For purposes of this subsection, the term “eligible rollover distribution” means any distribution to an employee of all or any portion of the balance to the credit of the employee in a qualified trust; except that such term shall not include—



(A) any distribution which is one of a series of substantially equal periodic payments (not less frequently than annually) made—

(i) for the life (or life expectancy) of the employee or the joint lives (or joint life expectancies) of the employee and the employee's designated beneficiary, or

(ii) for a specified period of 10 years or more,

(B) any distribution to the extent such distribution is required under section 401(a)(9), and

(C) any distribution which is made upon hardship of the employee.

If all or any portion of a distribution during 2009 is treated as an eligible rollover distribution but would not be so treated if the minimum distribution requirements under section 401(a)(9) had applied during 2009, such distribution shall not be treated as an eligible rollover distribution for purposes of section 401(a)(31) or 3405(c) or subsection (f) of this section.

(5) TRANSFER TREATED AS ROLLOVER CONTRIBUTION UNDER SECTION 408.—For purposes of this title, a transfer to an eligible retirement plan described in clause (i) or (ii) of paragraph (8)(B) resulting in any portion of a distribution being excluded from gross income under paragraph (1) shall be treated as a rollover contribution described in section 408(d)(3).

(6) SALES OF DISTRIBUTED PROPERTY.—For purposes of this subsection—

(A) TRANSFER OF PROCEEDS FROM SALE OF DISTRIBUTED PROPERTY TREATED AS TRANSFER OF DISTRIBUTED PROPERTY.—The transfer of an amount equal to any portion of the proceeds from the sale of property received in the distribution shall be treated as the transfer of property received in the distribution.

(B) PROCEEDS ATTRIBUTABLE TO INCREASE IN VALUE.—The excess of fair market value of property on sale over its fair market value on distribution shall be treated as property received in the distribution.

(C) DESIGNATION WHERE AMOUNT OF DISTRIBUTION EXCEEDS ROLLOVER CONTRIBUTION.—In any case where part or all of the distribution consists of property other than money—

(i) the portion of the money or other property which is to be treated as attributable to amounts not included in gross income, and

(ii) the portion of the money or other property which is to be treated as included in the rollover contribution,

shall be determined on a ratable basis unless the taxpayer designates otherwise. Any designation under this subparagraph for a taxable year shall be made not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof). Any such designation, once made, shall be irrevocable.

(D) NONRECOGNITION OF GAIN OR LOSS.—No gain or loss shall be recognized on any sale described in subparagraph (A) to the extent that an amount equal to the proceeds is transferred pursuant to paragraph (1).

## (7) SPECIAL RULE FOR FROZEN DEPOSITS.—

(A) IN GENERAL.—The 60-day period described in paragraph (3) shall not—

- (i) include any period during which the amount transferred to the employee is a frozen deposit, or
- (ii) end earlier than 10 days after such amount ceases to be a frozen deposit.

(B) FROZEN DEPOSITS.—For purposes of this subparagraph, the term “frozen deposit” means any deposit which may not be withdrawn because of—

- (i) the bankruptcy or insolvency of any financial institution, or
- (ii) any requirement imposed by the State in which such institution is located by reason of the bankruptcy or insolvency (or threat thereof) of 1 or more financial institutions in such State.

A deposit shall not be treated as a frozen deposit unless on at least 1 day during the 60-day period described in paragraph (3) (without regard to this paragraph) such deposit is described in the preceding sentence.

## (8) DEFINITIONS.—For purposes of this subsection—

(A) QUALIFIED TRUST.—The term “qualified trust” means an employees’ trust described in section 401(a) which is exempt from tax under section 501(a).

(B) ELIGIBLE RETIREMENT PLAN.—The term “eligible retirement plan” means—

- (i) an individual retirement account described in section 408(a),
- (ii) an individual retirement annuity described in section 408(b) (other than an endowment contract),
- (iii) a qualified trust,
- (iv) an annuity plan described in section 403(a),
- (v) an eligible deferred compensation plan described in section 457(b) which is maintained by an eligible employer described in section 457(e)(1)(A), and
- (vi) an annuity contract described in section 403(b).

If any portion of an eligible rollover distribution is attributable to payments or distributions from a designated Roth account (as defined in section 402A), an eligible retirement plan with respect to such portion shall include only another designated Roth account and a Roth IRA.

(9) ROLLOVER WHERE SPOUSE RECEIVES DISTRIBUTION AFTER DEATH OF EMPLOYEE.—If any distribution attributable to an employee is paid to the spouse of the employee after the employee’s death, the preceding provisions of this subsection shall apply to such distribution in the same manner as if the spouse were the employee.

(10) SEPARATE ACCOUNTING.—Unless a plan described in clause (v) of paragraph (8)(B) agrees to separately account for amounts rolled into such plan from eligible retirement plans not described in such clause, the plan described in such clause may not accept transfers or rollovers from such retirement plans.

(11) DISTRIBUTIONS TO INHERITED INDIVIDUAL RETIREMENT PLAN OF NONSPOUSE BENEFICIARY.—

(A) IN GENERAL.—If, with respect to any portion of a distribution from an eligible retirement plan described in paragraph (8)(B)(iii) of a deceased employee, a direct trustee-to-trustee transfer is made to an individual retirement plan described in clause (i) or (ii) of paragraph (8)(B) established for the purposes of receiving the distribution on behalf of an individual who is a designated beneficiary (as defined by section 401(a)(9)(E)) of the employee and who is not the surviving spouse of the employee—

(i) the transfer shall be treated as an eligible rollover distribution,

(ii) the individual retirement plan shall be treated as an inherited individual retirement account or individual retirement annuity (within the meaning of section 408(d)(3)(C)) for purposes of this title, and

(iii) section 401(a)(9)(B) (other than clause (iv) thereof) shall apply to such plan.

(B) CERTAIN TRUSTS TREATED AS BENEFICIARIES.—For purposes of this paragraph, to the extent provided in rules prescribed by the Secretary, a trust maintained for the benefit of one or more designated beneficiaries shall be treated in the same manner as a designated beneficiary.

(d) TAXABILITY OF BENEFICIARY OF CERTAIN FOREIGN SITUS TRUSTS.—For purposes of subsections (a), (b), and (c), a stock bonus, pension, or profit-sharing trust which would qualify for exemption from tax under section 501(a) except for the fact that it is a trust created or organized outside the United States shall be treated as if it were a trust exempt from tax under section 501(a).

(e) OTHER RULES APPLICABLE TO EXEMPT TRUSTS.—

(1) ALTERNATE PAYEES.—

(A) ALTERNATE PAYEE TREATED AS DISTRIBUTE.—For purposes of subsection (a) and section 72, an alternate payee who is the spouse or former spouse of the participant shall be treated as the distributee of any distribution or payment made to the alternate payee under a qualified domestic relations order (as defined in section 414(p)).

(B) ROLLOVERS.—If any amount is paid or distributed to an alternate payee who is the spouse or former spouse of the participant by reason of any qualified domestic relations order (within the meaning of section 414(p)), subsection (c) shall apply to such distribution in the same manner as if such alternate payee were the employee.

(2) DISTRIBUTIONS BY UNITED STATES TO NONRESIDENT ALIENS.—The amount includible under subsection (a) in the gross income of a nonresident alien with respect to a distribution made by the United States in respect of services performed by an employee of the United States shall not exceed an amount which bears the same ratio to the amount includible in gross income without regard to this paragraph as—

(A) the aggregate basic pay paid by the United States to such employee for such services, reduced by the amount of such basic pay which was not includible in gross income by reason of being from sources without the United States, bears to

(B) the aggregate basic pay paid by the United States to such employee for such services.

In the case of distributions under the civil service retirement laws, the term "basic pay" shall have the meaning provided in section 8331(3) of title 5, United States Code.

(3) CASH OR DEFERRED ARRANGEMENTS.—For purposes of this title, contributions made by an employer on behalf of an employee to a trust which is a part of a qualified cash or deferred arrangement (as defined in section 401(k)(2)) or which is part of a salary reduction agreement under section 403(b) shall not be treated as distributed or made available to the employee nor as contributions made to the trust by the employee merely because the arrangement includes provisions under which the employee has an election whether the contribution will be made to the trust or received by the employee in cash.

(4) NET UNREALIZED APPRECIATION.—

(A) AMOUNTS ATTRIBUTABLE TO EMPLOYEE CONTRIBUTIONS.—For purposes of subsection (a) and section 72, in the case of a distribution other than a lump sum distribution, the amount actually distributed to any distributee from a trust described in subsection (a) shall not include any net unrealized appreciation in securities of the employer corporation attributable to amounts contributed by the employee (other than deductible employee contributions within the meaning of section 72(o)(5)). This subparagraph shall not apply to a distribution to which subsection (c) applies.

(B) AMOUNTS ATTRIBUTABLE TO EMPLOYER CONTRIBUTIONS.—For purposes of subsection (a) and section 72, in the case of any lump sum distribution which includes securities of the employer corporation, there shall be excluded from gross income the net unrealized appreciation attributable to that part of the distribution which consists of securities of the employer corporation. In accordance with rules prescribed by the Secretary, a taxpayer may elect, on the return of tax on which a lump sum distribution is required to be included, not to have this subparagraph apply to such distribution.

(C) DETERMINATION OF AMOUNTS AND ADJUSTMENTS.—For purposes of subparagraphs (A) and (B), net unrealized appreciation and the resulting adjustments to basis shall be determined in accordance with regulations prescribed by the Secretary.

(D) LUMP-SUM DISTRIBUTION.—For purposes of this paragraph—

(i) IN GENERAL.—The term "lump-sum distribution" means the distribution or payment within one taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient—

- (I) on account of the employee's death,
- (II) after the employee attains age 59 1/2,
- (III) on account of the employee's separation from service, or
- (IV) after the employee has become disabled (within the meaning of section 72(m)(7)),

from a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501 or from a plan described in section 403(a). Subclause (III) of this clause shall be applied only with respect to an individual who is an employee without regard to section 401(c)(1), and subclause (IV) shall be applied only with respect to an employee within the meaning of section 401(c)(1). For purposes of this clause, a distribution to two or more trusts shall be treated as a distribution to one recipient. For purposes of this paragraph, the balance to the credit of the employee does not include the accumulated deductible employee contributions under the plan (within the meaning of section 72(o)(5)).

(ii) **AGGREGATION OF CERTAIN TRUSTS AND PLANS.**—For purposes of determining the balance to the credit of an employee under clause (i)—

(I) all trusts which are part of a plan shall be treated as a single trust, all pension plans maintained by the employer shall be treated as a single plan, all profit-sharing plans maintained by the employer shall be treated as a single plan, and all stock bonus plans maintained by the employer shall be treated as a single plan, and

(II) trusts which are not qualified trusts under section 401(a) and annuity contracts which do not satisfy the requirements of section 404(a)(2) shall not be taken into account.

(iii) **COMMUNITY PROPERTY LAWS.**—The provisions of this paragraph shall be applied without regard to community property laws.

(iv) **AMOUNTS SUBJECT TO PENALTY.**—This paragraph shall not apply to amounts described in subparagraph (A) of section 72(m)(5) to the extent that section 72(m)(5) applies to such amounts.

(v) **BALANCE TO CREDIT OF EMPLOYEE NOT TO INCLUDE AMOUNTS PAYABLE UNDER QUALIFIED DOMESTIC RELATIONS ORDER.**—For purposes of this paragraph, the balance to the credit of an employee shall not include any amount payable to an alternate payee under a qualified domestic relations order (within the meaning of section 414(p)).

(vi) **TRANSFERS TO COST-OF-LIVING ARRANGEMENT NOT TREATED AS DISTRIBUTION.**—For purposes of this paragraph, the balance to the credit of an employee under a defined contribution plan shall not include any amount transferred from such defined contribution plan to a qualified cost-of-living arrangement (within the meaning of section 415(k)(2)) under a defined benefit plan.

(vii) **LUMP-SUM DISTRIBUTIONS OF ALTERNATE PAYEES.**—If any distribution or payment of the balance to the credit of an employee would be treated as a lump-sum distribution, then, for purposes of this paragraph, the payment under a qualified domestic relations order (within the meaning of section 414(p)) of the bal-

ance to the credit of an alternate payee who is the spouse or former spouse of the employee shall be treated as a lump-sum distribution. For purposes of this clause, the balance to the credit of the alternate payee shall not include any amount payable to the employee.

(E) DEFINITIONS RELATING TO SECURITIES.—For purposes of this paragraph—

(i) SECURITIES.—The term “securities” means only shares of stock and bonds or debentures issued by a corporation with interest coupons or in registered form.

(ii) SECURITIES OF THE EMPLOYER.—The term “securities of the employer corporation” includes securities of a parent or subsidiary corporation (as defined in subsections (e) and (f) of section 424) of the employer corporation.

(6) DIRECT TRUSTEE-TO-TRUSTEE TRANSFERS.—Any amount transferred in a direct trustee-to-trustee transfer in accordance with section 401(a)(31) shall not be includible in gross income for the taxable year of such transfer.

(f) WRITTEN EXPLANATION TO RECIPIENTS OF DISTRIBUTIONS ELIGIBLE FOR ROLLOVER TREATMENT.—

(1) IN GENERAL.—The plan administrator of any plan shall, within a reasonable period of time before making an eligible rollover distribution, provide a written explanation to the recipient—

(A) of the provisions under which the recipient may have the distribution directly transferred to an eligible retirement plan and that the automatic distribution by direct transfer applies to certain distributions in accordance with section 401(a)(31)(B),

(B) of the provision which requires the withholding of tax on the distribution if it is not directly transferred to an eligible retirement plan,

(C) of the provisions under which the distribution will not be subject to tax if transferred to an eligible retirement plan within 60 days after the date on which the recipient received the distribution,

(D) if applicable, of the provisions of subsections (d) and (e) of this section, and

(E) of the provisions under which distributions from the eligible retirement plan receiving the distribution may be subject to restrictions and tax consequences which are different from those applicable to distributions from the plan making such distribution.

(2) DEFINITIONS.—For purposes of this subsection—

(A) ELIGIBLE ROLLOVER DISTRIBUTION.—The term “eligible rollover distribution” has the same meaning as when used in subsection (c) of this section, paragraph (4) of section 403(a), subparagraph (A) of section 403(b)(8), or subparagraph (A) of section 457(e)(16). Such term shall include any distribution to a designated beneficiary which would be treated as an eligible rollover distribution by reason of subsection (c)(11), or section 403(a)(4)(B),

403(b)(8)(B), or 457(e)(16)(B), if the requirements of subsection (c)(11) were satisfied.

(B) ELIGIBLE RETIREMENT PLAN.—The term “eligible retirement plan” has the meaning given such term by subsection (c)(8)(B).

(g) LIMITATION ON EXCLUSION FOR ELECTIVE DEFERRALS.—

(1) IN GENERAL.—

(A) LIMITATION.—Notwithstanding subsections (e)(3) and (h)(1)(B), the elective deferrals of any individual for any taxable year shall be included in such individual’s gross income to the extent the amount of such deferrals for the taxable year exceeds the applicable dollar amount. The preceding sentence shall not apply to the portion of such excess as does not exceed the designated Roth contributions of the individual for the taxable year.

(B) APPLICABLE DOLLAR AMOUNT.—For purposes of subparagraph (A), the applicable dollar amount is \$15,000.

(C) CATCH-UP CONTRIBUTIONS.—In addition to subparagraph (A), in the case of an eligible participant (as defined in section 414(v)), gross income shall not include elective deferrals in excess of the applicable dollar amount under subparagraph (B) to the extent that the amount of such elective deferrals does not exceed the applicable dollar amount under section 414(v)(2)(B)(i) for the taxable year (without regard to the treatment of the elective deferrals by an applicable employer plan under section 414(v)).

(2) DISTRIBUTION OF EXCESS DEFERRALS.—

(A) IN GENERAL.—If any amount (hereinafter in this paragraph referred to as “excess deferrals”) is included in the gross income of an individual under paragraph (1) (or would be included but for the last sentence thereof) for any taxable year—

(i) not later than the 1st March 1 following the close of the taxable year, the individual may allocate the amount of such excess deferrals among the plans under which the deferrals were made and may notify each such plan of the portion allocated to it, and

(ii) not later than the 1st April 15 following the close of the taxable year, each such plan may distribute to the individual the amount allocated to it under clause (i) (and any income allocable to such amount through the end of such taxable year).

The distribution described in clause (ii) may be made notwithstanding any other provision of law.

(B) TREATMENT OF DISTRIBUTION UNDER SECTION 401(K).—Except to the extent provided under rules prescribed by the Secretary, notwithstanding the distribution of any portion of an excess deferral from a plan under subparagraph (A)(ii), such portion shall, for purposes of applying section 401(k)(3)(A)(ii), be treated as an employer contribution.

(C) TAXATION OF DISTRIBUTION.—In the case of a distribution to which subparagraph (A) applies—

(i) except as provided in clause (ii), such distribution shall not be included in gross income, and

(ii) any income on the excess deferral shall, for purposes of this chapter, be treated as earned and received in the taxable year in which such income is distributed.

No tax shall be imposed under section 72(t) on any distribution described in the preceding sentence.

(D) PARTIAL DISTRIBUTIONS.—If a plan distributes only a portion of any excess deferral and income allocable thereto, such portion shall be treated as having been distributed ratably from the excess deferral and the income.

(3) ELECTIVE DEFERRALS.—For purposes of this subsection, the term “elective deferrals” means, with respect to any taxable year, the sum of—

(A) any employer contribution under a qualified cash or deferred arrangement (as defined in section 401(k)) to the extent not includible in gross income for the taxable year under subsection (e)(3) (determined without regard to this subsection),

(B) any employer contribution to the extent not includible in gross income for the taxable year under subsection (h)(1)(B) (determined without regard to this subsection),

(C) any employer contribution to purchase an annuity contract under section 403(b) under a salary reduction agreement (within the meaning of section 3121(a)(5)(D)), and

(D) any elective employer contribution under section 408(p)(2)(A)(i).

An employer contribution shall not be treated as an elective deferral described in subparagraph (C) if under the salary reduction agreement such contribution is made pursuant to a one-time irrevocable election made by the employee at the time of initial eligibility to participate in the agreement or is made pursuant to a similar arrangement involving a one-time irrevocable election specified in regulations.

(4) COST-OF-LIVING ADJUSTMENT.—In the case of taxable years beginning after December 31, 2006, the Secretary shall adjust the \$15,000 amount under paragraph (1)(B) at the same time and in the same manner as under section 415(d), except that the base period shall be the calendar quarter beginning July 1, 2005, and any increase under this paragraph which is not a multiple of \$500 shall be rounded to the next lowest multiple of \$500.

(5) DISREGARD OF COMMUNITY PROPERTY LAWS.—This subsection shall be applied without regard to community property laws.

(6) COORDINATION WITH SECTION 72.—For purposes of applying section 72, any amount includible in gross income for any taxable year under this subsection but which is not distributed from the plan during such taxable year shall not be treated as investment in the contract.

(7) SPECIAL RULE FOR CERTAIN ORGANIZATIONS.—

(A) IN GENERAL.—In the case of a qualified employee of a qualified organization, with respect to employer contributions described in paragraph (3)(C) made by such organization, the limitation of paragraph (1) for any taxable year



shall be increased by whichever of the following is the least:

(i) \$3,000,

(ii) \$15,000 reduced by the sum of—

(I) the amounts not included in gross income for prior taxable years by reason of this paragraph, plus

(II) the aggregate amount of designated Roth contributions (as defined in section 402A(c)) permitted for prior taxable years by reason of this paragraph, or

(iii) the excess of \$5,000 multiplied by the number of years of service of the employee with the qualified organization over the employer contributions described in paragraph (3) made by the organization on behalf of such employee for prior taxable years (determined in the manner prescribed by the Secretary).

(B) QUALIFIED ORGANIZATION.—For purposes of this paragraph, the term “qualified organization” means any educational organization, hospital, home health service agency, health and welfare service agency, church, or convention or association of churches. Such term includes any organization described in section 414(e)(3)(B)(ii). Terms used in this subparagraph shall have the same meaning as when used in section 415(c)(4) (as in effect before the enactment of the Economic Growth and Tax Relief Reconciliation Act of 2001).

(C) QUALIFIED EMPLOYEE.—For purposes of this paragraph, the term “qualified employee” means any employee who has completed 15 years of service with the qualified organization.

(D) YEARS OF SERVICE.—For purposes of this paragraph, the term “years of service” has the meaning given such term by section 403(b).

(8) MATCHING CONTRIBUTIONS ON BEHALF OF SELF-EMPLOYED INDIVIDUALS NOT TREATED AS ELECTIVE EMPLOYER CONTRIBUTIONS.—Except as provided in section 401(k)(3)(D)(ii), any matching contribution described in section 401(m)(4)(A) which is made on behalf of a self-employed individual (as defined in section 401(c)) shall not be treated as an elective employer contribution under a qualified cash or deferred arrangement (as defined in section 401(k)) for purposes of this title.

(h) SPECIAL RULES FOR SIMPLIFIED EMPLOYEE PENSIONS.—For purposes of this chapter—

(1) IN GENERAL.—Except as provided in paragraph (2), contributions made by an employer on behalf of an employee to an individual retirement plan pursuant to a simplified employee pension (as defined in section 408(k))—

(A) shall not be treated as distributed or made available to the employee or as contributions made by the employee, and

(B) if such contributions are made pursuant to an arrangement under section 408(k)(6) under which an employee may elect to have the employer make contributions to the simplified employee pension on behalf of the em-

ployee, shall not be treated as distributed or made available or as contributions made by the employee merely because the simplified employee pension includes provisions for such election.

(2) LIMITATIONS ON EMPLOYER CONTRIBUTIONS.—Contributions made by an employer to a simplified employee pension with respect to an employee for any year shall be treated as distributed or made available to such employee and as contributions made by the employee to the extent such contributions exceed the lesser of—

(A) 25 percent of the compensation (within the meaning of section 414(s)) from such employer includible in the employee's gross income for the year (determined without regard to the employer contributions to the simplified employee pension), or

(B) the limitation in effect under section 415(c)(1)(A), reduced in the case of any highly compensated employee (within the meaning of section 414(q)) by the amount taken into account with respect to such employee under section 408(k)(3)(D).

(3) DISTRIBUTIONS.—Any amount paid or distributed out of an individual retirement plan pursuant to a simplified employee pension shall be included in gross income by the payee or distributee, as the case may be, in accordance with the provisions of section 408(d).

(i) TREATMENT OF SELF-EMPLOYED INDIVIDUALS.—For purposes of this section, except as otherwise provided in subsection (e)(4)(D)(i), the term “employee” includes a self-employed individual (as defined in section 401(c)(1)(B)) and the employer of such individual shall be the person treated as his employer under section 401(c)(4).

(j) EFFECT OF DISPOSITION OF STOCK BY PLAN ON NET UNREALIZED APPRECIATION.—

(1) IN GENERAL.—For purposes of subsection (e)(4), in the case of any transaction to which this subsection applies, the determination of net unrealized appreciation shall be made without regard to such transaction.

(2) TRANSACTION TO WHICH SUBSECTION APPLIES.—This subsection shall apply to any transaction in which—

(A) the plan trustee exchanges the plan's securities of the employer corporation for other such securities, or

(B) the plan trustee disposes of securities of the employer corporation and uses the proceeds of such disposition to acquire securities of the employer corporation within 90 days (or such longer period as the Secretary may prescribe), except that this subparagraph shall not apply to any employee with respect to whom a distribution of money was made during the period after such disposition and before such acquisition.

(k) TREATMENT OF SIMPLE RETIREMENT ACCOUNTS.—Rules similar to the rules of paragraphs (1) and (3) of subsection (h) shall apply to contributions and distributions with respect to a simple retirement account under section 408(p).

(l) DISTRIBUTIONS FROM GOVERNMENTAL PLANS FOR HEALTH AND LONG-TERM CARE INSURANCE.—

(1) **IN GENERAL.**—In the case of an employee who is an eligible retired public safety officer who makes the election described in paragraph (6) with respect to any taxable year of such employee, gross income of such employee for such taxable year does not include any distribution from an eligible retirement plan maintained by the employer described in paragraph (4)(B) to the extent that the aggregate amount of such distributions does not exceed the amount paid by such employee for qualified health insurance premiums for such taxable year.

(2) **LIMITATION.**—The amount which may be excluded from gross income for the taxable year by reason of paragraph (1) shall not exceed \$3,000.

(3) **DISTRIBUTIONS MUST OTHERWISE BE INCLUDIBLE.**—

(A) **IN GENERAL.**—An amount shall be treated as a distribution for purposes of paragraph (1) only to the extent that such amount would be includible in gross income without regard to paragraph (1).

(B) **APPLICATION OF SECTION 72.**—Notwithstanding section 72, in determining the extent to which an amount is treated as a distribution for purposes of subparagraph (A), the aggregate amounts distributed from an eligible retirement plan in a taxable year (up to the amount excluded under paragraph (1)) shall be treated as includible in gross income (without regard to subparagraph (A)) to the extent that such amount does not exceed the aggregate amount which would have been so includible if all amounts to the credit of the eligible public safety officer in all eligible retirement plans maintained by the employer described in paragraph (4)(B) were distributed during such taxable year and all such plans were treated as 1 contract for purposes of determining under section 72 the aggregate amount which would have been so includible. Proper adjustments shall be made in applying section 72 to other distributions in such taxable year and subsequent taxable years.

(4) **DEFINITIONS.**—For purposes of this subsection—

(A) **ELIGIBLE RETIREMENT PLAN.**—For purposes of paragraph (1), the term “eligible retirement plan” means a governmental plan (within the meaning of section 414(d)) which is described in clause (iii), (iv), (v), or (vi) of subsection (c)(8)(B).

(B) **ELIGIBLE RETIRED PUBLIC SAFETY OFFICER.**—The term “eligible retired public safety officer” means an individual who, by reason of disability or attainment of normal retirement age, is separated from service as a public safety officer with the employer who maintains the eligible retirement plan from which distributions subject to paragraph (1) are made.

(C) **PUBLIC SAFETY OFFICER.**—The term “public safety officer” shall have the same meaning given such term by section 1204(9)(A) of the Omnibus Crime Control and Safe Streets Act of 1968 (42 U.S.C. 3796b(9)(A)), as in effect immediately before the enactment of the National Defense Authorization Act for Fiscal Year 2013.

(D) **QUALIFIED HEALTH INSURANCE PREMIUMS.**—The term “qualified health insurance premiums” means premiums

for coverage for the eligible retired public safety officer, his spouse, and dependents (as defined in [section 152] *section 7706*), by an accident or health plan or qualified long-term care insurance contract (as defined in section 7702B(b)).

(5) SPECIAL RULES.—For purposes of this subsection—

(A) DIRECT PAYMENT TO INSURER REQUIRED.—Paragraph (1) shall only apply to a distribution if payment of the premiums is made directly to the provider of the accident or health plan or qualified long-term care insurance contract by deduction from a distribution from the eligible retirement plan.

(B) RELATED PLANS TREATED AS 1.—All eligible retirement plans of an employer shall be treated as a single plan.

(6) ELECTION DESCRIBED.—

(A) IN GENERAL.—For purposes of paragraph (1), an election is described in this paragraph if the election is made by an employee after separation from service with respect to amounts not distributed from an eligible retirement plan to have amounts from such plan distributed in order to pay for qualified health insurance premiums.

(B) SPECIAL RULE.—A plan shall not be treated as violating the requirements of section 401, or as engaging in a prohibited transaction for purposes of section 503(b), merely because it provides for an election with respect to amounts that are otherwise distributable under the plan or merely because of a distribution made pursuant to an election described in subparagraph (A).

(7) COORDINATION WITH MEDICAL EXPENSE DEDUCTION.—The amounts excluded from gross income under paragraph (1) shall not be taken into account under section 213.

(8) COORDINATION WITH DEDUCTION FOR HEALTH INSURANCE COSTS OF SELF-EMPLOYED INDIVIDUALS.—The amounts excluded from gross income under paragraph (1) shall not be taken into account under section 162(l).

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**SEC. 409A. INCLUSION IN GROSS INCOME OF DEFERRED COMPENSATION UNDER NONQUALIFIED DEFERRED COMPENSATION PLANS.**

(a) RULES RELATING TO CONSTRUCTIVE RECEIPT.—

(1) PLAN FAILURES.—

(A) GROSS INCOME INCLUSION.—

(i) IN GENERAL.—If at any time during a taxable year a nonqualified deferred compensation plan—

(I) fails to meet the requirements of paragraphs (2), (3), and (4), or

(II) is not operated in accordance with such requirements, all compensation deferred under the plan for the taxable year and all preceding taxable years shall be includible in gross income for the taxable year to the extent not subject to a substantial risk of forfeiture and not previously included in gross income.

(ii) APPLICATION ONLY TO AFFECTED PARTICIPANTS.— Clause (i) shall only apply with respect to all compensation deferred under the plan for participants with respect to whom the failure relates.

(B) INTEREST AND ADDITIONAL TAX PAYABLE WITH RESPECT TO PREVIOUSLY DEFERRED COMPENSATION.—

(i) IN GENERAL.—If compensation is required to be included in gross income under subparagraph (A) for a taxable year, the tax imposed by this chapter for the taxable year shall be increased by the sum of—

(I) the amount of interest determined under clause (ii), and

(II) an amount equal to 20 percent of the compensation which is required to be included in gross income.

(ii) INTEREST.—For purposes of clause (i), the interest determined under this clause for any taxable year is the amount of interest at the underpayment rate plus 1 percentage point on the underpayments that would have occurred had the deferred compensation been includible in gross income for the taxable year in which first deferred or, if later, the first taxable year in which such deferred compensation is not subject to a substantial risk of forfeiture.

(2) DISTRIBUTIONS.—

(A) IN GENERAL.—The requirements of this paragraph are met if the plan provides that compensation deferred under the plan may not be distributed earlier than—

(i) separation from service as determined by the Secretary (except as provided in subparagraph (B)(i)),

(ii) the date the participant becomes disabled (within the meaning of subparagraph (C)),

(iii) death,

(iv) a specified time (or pursuant to a fixed schedule) specified under the plan at the date of the deferral of such compensation,

(v) to the extent provided by the Secretary, a change in the ownership or effective control of the corporation, or in the ownership of a substantial portion of the assets of the corporation, or

(vi) the occurrence of an unforeseeable emergency.

(B) SPECIAL RULES.—

(i) SPECIFIED EMPLOYEES.—In the case of any specified employee, the requirement of subparagraph (A)(i) is met only if distributions may not be made before the date which is 6 months after the date of separation from service (or, if earlier, the date of death of the employee). For purposes of the preceding sentence, a specified employee is a key employee (as defined in section 416(i) without regard to paragraph (5) thereof) of a corporation any stock in which is publicly traded on an established securities market or otherwise.

(ii) UNFORESEEABLE EMERGENCY.—For purposes of subparagraph (A)(vi)—

(I) IN GENERAL.—The term “unforeseeable emergency” means a severe financial hardship to the participant resulting from an illness or accident of the participant, the participant’s spouse, or a dependent (as defined in [section 152(a)] *section 7706(a)*) of the participant, loss of the participant’s property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the participant.

(II) LIMITATION ON DISTRIBUTIONS.—The requirement of subparagraph (A)(vi) is met only if, as determined under regulations of the Secretary, the amounts distributed with respect to an emergency do not exceed the amounts necessary to satisfy such emergency plus amounts necessary to pay taxes reasonably anticipated as a result of the distribution, after taking into account the extent to which such hardship is or may be relieved through reimbursement or compensation by insurance or otherwise or by liquidation of the participant’s assets (to the extent the liquidation of such assets would not itself cause severe financial hardship).

(C) DISABLED.—For purposes of subparagraph (A)(ii), a participant shall be considered disabled if the participant—

(i) is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, or

(ii) is, by reason of any medically determinable physical or mental impairment which can be expected to result in death or can be expected to last for a continuous period of not less than 12 months, receiving income replacement benefits for a period of not less than 3 months under an accident and health plan covering employees of the participant’s employer.

(3) ACCELERATION OF BENEFITS.—The requirements of this paragraph are met if the plan does not permit the acceleration of the time or schedule of any payment under the plan, except as provided in regulations by the Secretary.

(4) ELECTIONS.—

(A) IN GENERAL.—The requirements of this paragraph are met if the requirements of subparagraphs (B) and (C) are met.

(B) INITIAL DEFERRAL DECISION.—

(i) IN GENERAL.—The requirements of this subparagraph are met if the plan provides that compensation for services performed during a taxable year may be deferred at the participant’s election only if the election to defer such compensation is made not later than the close of the preceding taxable year or at such other time as provided in regulations.

(ii) **FIRST YEAR OF ELIGIBILITY.**—In the case of the first year in which a participant becomes eligible to participate in the plan, such election may be made with respect to services to be performed subsequent to the election within 30 days after the date the participant becomes eligible to participate in such plan.

(iii) **PERFORMANCE-BASED COMPENSATION.**—In the case of any performance-based compensation based on services performed over a period of at least 12 months, such election may be made no later than 6 months before the end of the period.

(C) **CHANGES IN TIME AND FORM OF DISTRIBUTION.**—The requirements of this subparagraph are met if, in the case of a plan which permits under a subsequent election a delay in a payment or a change in the form of payment—

(i) the plan requires that such election may not take effect until at least 12 months after the date on which the election is made,

(ii) in the case of an election related to a payment not described in clause (ii), (iii), or (vi) of paragraph (2)(A), the plan requires that the payment with respect to which such election is made be deferred for a period of not less than 5 years from the date such payment would otherwise have been made, and

(iii) the plan requires that any election related to a payment described in paragraph (2)(A)(iv) may not be made less than 12 months prior to the date of the first scheduled payment under such paragraph.

(b) **RULES RELATING TO FUNDING.**—

(1) **OFFSHORE PROPERTY IN A TRUST.**—In the case of assets set aside (directly or indirectly) in a trust (or other arrangement determined by the Secretary) for purposes of paying deferred compensation under a nonqualified deferred compensation plan, for purposes of section 83 such assets shall be treated as property transferred in connection with the performance of services whether or not such assets are available to satisfy claims of general creditors—

(A) at the time set aside if such assets (or such trust or other arrangement) are located outside of the United States, or

(B) at the time transferred if such assets (or such trust or other arrangement) are subsequently transferred outside of the United States.

This paragraph shall not apply to assets located in a foreign jurisdiction if substantially all of the services to which the nonqualified deferred compensation relates are performed in such jurisdiction.

(2) **EMPLOYER'S FINANCIAL HEALTH.**—In the case of compensation deferred under a nonqualified deferred compensation plan, there is a transfer of property within the meaning of section 83 with respect to such compensation as of the earlier of—

(A) the date on which the plan first provides that assets will become restricted to the provision of benefits under the plan in connection with a change in the employer's financial health, or

(B) the date on which assets are so restricted, whether or not such assets are available to satisfy claims of general creditors.

(3) TREATMENT OF EMPLOYER'S DEFINED BENEFIT PLAN DURING RESTRICTED PERIOD.—

(A) IN GENERAL.—If—

(i) during any restricted period with respect to a single-employer defined benefit plan, assets are set aside or reserved (directly or indirectly) in a trust (or other arrangement as determined by the Secretary) or transferred to such a trust or other arrangement for purposes of paying deferred compensation of an applicable covered employee under a nonqualified deferred compensation plan of the plan sponsor or member of a controlled group which includes the plan sponsor, or

(ii) a nonqualified deferred compensation plan of the plan sponsor or member of a controlled group which includes the plan sponsor provides that assets will become restricted to the provision of benefits under the plan to an applicable covered employee in connection with such restricted period (or other similar financial measure determined by the Secretary) with respect to the defined benefit plan, or assets are so restricted,

such assets shall, for purposes of section 83, be treated as property transferred in connection with the performance of services whether or not such assets are available to satisfy claims of general creditors. Clause (i) shall not apply with respect to any assets which are so set aside before the restricted period with respect to the defined benefit plan.

(B) RESTRICTED PERIOD.—For purposes of this section, the term “restricted period” means, with respect to any plan described in subparagraph (A)—

(i) any period during which the plan is in at-risk status (as defined in section 430(i)),

(ii) any period the plan sponsor is a debtor in a case under title 11, United States Code, or similar Federal or State law, and

(iii) the 12-month period beginning on the date which is 6 months before the termination date of the plan if, as of the termination date, the plan is not sufficient for benefit liabilities (within the meaning of section 4041 of the Employee Retirement Income Security Act of 1974).

(C) SPECIAL RULE FOR PAYMENT OF TAXES ON DEFERRED COMPENSATION INCLUDED IN INCOME.—If an employer provides directly or indirectly for the payment of any Federal, State, or local income taxes with respect to any compensation required to be included in gross income by reason of this paragraph—

(i) interest shall be imposed under subsection (a)(1)(B)(i)(I) on the amount of such payment in the same manner as if such payment was part of the deferred compensation to which it relates,

(ii) such payment shall be taken into account in determining the amount of the additional tax under sub-



section (a)(1)(B)(i)(II) in the same manner as if such payment was part of the deferred compensation to which it relates, and

(iii) no deduction shall be allowed under this title with respect to such payment.

(D) OTHER DEFINITIONS.—For purposes of this section—

(i) APPLICABLE COVERED EMPLOYEE.—The term “applicable covered employee” means any—

(I) covered employee of a plan sponsor,

(II) covered employee of a member of a controlled group which includes the plan sponsor, and

(III) former employee who was a covered employee at the time of termination of employment with the plan sponsor or a member of a controlled group which includes the plan sponsor.

(ii) COVERED EMPLOYEE.—The term “covered employee” means an individual described in section 162(m)(3) or an individual subject to the requirements of section 16(a) of the Securities Exchange Act of 1934.

(4) INCOME INCLUSION FOR OFFSHORE TRUSTS AND EMPLOYER’S FINANCIAL HEALTH.—For each taxable year that assets treated as transferred under this subsection remain set aside in a trust or other arrangement subject to paragraph (1), (2), or (3), any increase in value in, or earnings with respect to, such assets shall be treated as an additional transfer of property under this subsection (to the extent not previously included in income).

(5) INTEREST ON TAX LIABILITY PAYABLE WITH RESPECT TO TRANSFERRED PROPERTY.—

(A) IN GENERAL.—If amounts are required to be included in gross income by reason of paragraph (1), (2), or (3) for a taxable year, the tax imposed by this chapter for such taxable year shall be increased by the sum of—

(i) the amount of interest determined under subparagraph (B), and

(ii) an amount equal to 20 percent of the amounts required to be included in gross income.

(B) INTEREST.—For purposes of subparagraph (A), the interest determined under this subparagraph for any taxable year is the amount of interest at the underpayment rate plus 1 percentage point on the underpayments that would have occurred had the amounts so required to be included in gross income by paragraph (1), (2), or (3) been includible in gross income for the taxable year in which first deferred or, if later, the first taxable year in which such amounts are not subject to a substantial risk of forfeiture.

(c) NO INFERENCE ON EARLIER INCOME INCLUSION OR REQUIREMENT OF LATER INCLUSION.—Nothing in this section shall be construed to prevent the inclusion of amounts in gross income under any other provision of this chapter or any other rule of law earlier than the time provided in this section. Any amount included in gross income under this section shall not be required to be included in gross income under any other provision of this chapter or any other rule of law later than the time provided in this section.

(d) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section:

(1) NONQUALIFIED DEFERRED COMPENSATION PLAN.—The term “nonqualified deferred compensation plan” means any plan that provides for the deferral of compensation, other than—

(A) a qualified employer plan, and

(B) any bona fide vacation leave, sick leave, compensatory time, disability pay, or death benefit plan.

(2) QUALIFIED EMPLOYER PLAN.—The term “qualified employer plan” means—

(A) any plan, contract, pension, account, or trust described in subparagraph (A) or (B) of section 219(g)(5) (without regard to subparagraph (A)(iii)),

(B) any eligible deferred compensation plan (within the meaning of section 457(b)), and

(C) any plan described in section 415(m).

(3) PLAN INCLUDES ARRANGEMENTS, ETC.—The term “plan” includes any agreement or arrangement, including an agreement or arrangement that includes one person.

(4) SUBSTANTIAL RISK OF FORFEITURE.—The rights of a person to compensation are subject to a substantial risk of forfeiture if such person’s rights to such compensation are conditioned upon the future performance of substantial services by any individual.

(5) TREATMENT OF EARNINGS.—References to deferred compensation shall be treated as including references to income (whether actual or notional) attributable to such compensation or such income.

(6) AGGREGATION RULES.—Except as provided by the Secretary, rules similar to the rules of subsections (b) and (c) of section 414 shall apply.

(7) TREATMENT OF QUALIFIED STOCK.—An arrangement under which an employee may receive qualified stock (as defined in section 83(i)(2)) shall not be treated as a nonqualified deferred compensation plan with respect to such employee solely because of such employee’s election, or ability to make an election, to defer recognition of income under section 83(i).

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

(1) providing for the determination of amounts of deferral in the case of a nonqualified deferred compensation plan which is a defined benefit plan,

(2) relating to changes in the ownership and control of a corporation or assets of a corporation for purposes of subsection (a)(2)(A)(v),

(3) exempting arrangements from the application of subsection (b) if such arrangements will not result in an improper deferral of United States tax and will not result in assets being effectively beyond the reach of creditors,

(4) defining financial health for purposes of subsection (b)(2), and

(5) disregarding a substantial risk of forfeiture in cases where necessary to carry out the purposes of this section.

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## Subchapter E—Accounting Periods and Methods of Accounting

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### PART I—ACCOUNTING PERIODS

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#### SEC. 441. PERIOD FOR COMPUTATION OF TAXABLE INCOME.

(a) COMPUTATION OF TAXABLE INCOME.—Taxable income shall be computed on the basis of the taxpayer's taxable year.

(b) TAXABLE YEAR.—For purposes of this subtitle, the term “taxable year” means—

(1) the taxpayer's annual accounting period, if it is a calendar year or a fiscal year;

(2) the calendar year, if subsection (g) applies;

(3) the period for which the return is made, if a return is made for a period of less than 12 months; or

(4) in the case of a DISC filing a return for a period of at least 12 months, the period determined under subsection (h).

(c) ANNUAL ACCOUNTING PERIOD.—For purposes of this subtitle, the term “annual accounting period” means the annual period on the basis of which the taxpayer regularly computes his income in keeping his books.

(d) CALENDAR YEAR.—For purposes of this subtitle, the term “calendar year” means a period of 12 months ending on December 31.

(e) FISCAL YEAR.—For purposes of this subtitle, the term “fiscal year” means a period of 12 months ending on the last day of any month other than December. In the case of any taxpayer who has made the election provided by subsection (f) the term means the annual period (varying from 52 to 53 weeks) so elected.

(f) ELECTION OF YEAR CONSISTING OF 52-53 WEEKS.—

(1) GENERAL RULE.—A taxpayer who, in keeping his books, regularly computes his income on the basis of an annual period which varies from 52 to 53 weeks and ends always on the same day of the week and ends always—

(A) on whatever date such same day of the week last occurs in a calendar month, or

(B) on whatever date such same day of the week falls which is nearest to the last day of a calendar month,

may (in accordance with the regulations prescribed under paragraph (3)) elect to compute his taxable income for purposes of this subtitle on the basis of such annual period. This paragraph shall apply to taxable years ending after the date of the enactment of this title.

(2) SPECIAL RULES FOR 52-53-WEEK YEAR.—

(A) EFFECTIVE DATES.—In any case in which the effective date or the applicability of any provision of this title is expressed in terms of taxable years beginning, including, or ending with reference to a specified date which is

the first or last day of a month, a taxable year described in paragraph (1) shall (except for purposes of the computation under section 15) be treated—

(i) as beginning with the first day of the calendar month beginning nearest to the first day of such taxable year, or

(ii) as ending with the last day of the calendar month ending nearest to the last day of such taxable year,

as the case may be.

(B) CHANGE IN ACCOUNTING PERIOD.—In the case of a change from or to a taxable year described in paragraph (1)—

(i) if such change results in a short period (within the meaning of section 443) of 359 days or more, or of less than 7 days, section 443(b) (relating to alternative tax computation) shall not apply;

(ii) if such change results in a short period of less than 7 days, such short period shall, for purposes of this subtitle, be added to and deemed a part of the following taxable year; and

(iii) if such change results in a short period to which subsection (b) of section 443 applies, the taxable income for such short period shall be placed on an annual basis for purposes of such subsection by multiplying the gross income for such short period (minus the deductions allowed by this chapter for the short period, but only the adjusted amount of the deductions for personal exemptions as described in section 443(c)) by 365, by dividing the result by the number of days in the short period, and the tax shall be the same part of the tax computed on the annual basis as the number of days in the short period is of 365 days.

(3) SPECIAL RULE FOR PARTNERSHIPS, S CORPORATIONS, AND PERSONAL SERVICE CORPORATIONS.—The Secretary may by regulation provide terms and conditions for the application of this subsection to a partnership, S corporation, or personal service corporation (within the meaning of section 441(i)(2)).

(4) REGULATIONS.—The Secretary shall prescribe such regulations as he deems necessary for the application of this subsection.

(g) NO BOOKS KEPT; NO ACCOUNTING PERIOD.—Except as provided in section 443 (relating to returns for periods of less than 12 months), the taxpayer's taxable year shall be the calendar year if—

(1) the taxpayer keeps no books;

(2) the taxpayer does not have an annual accounting period;

or

(3) the taxpayer has an annual accounting period, but such period does not qualify as a fiscal year.

(h) TAXABLE YEAR OF DISC'S.—

(1) IN GENERAL.—For purposes of this subtitle, the taxable year of any DISC shall be the taxable year of that shareholder (or group of shareholders with the same 12-month taxable year) who has the highest percentage of voting power.

(2) SPECIAL RULE WHERE MORE THAN ONE SHAREHOLDER (OR GROUP) HAS HIGHEST PERCENTAGE.—If 2 or more shareholders (or groups) have the highest percentage of voting power under paragraph (1), the taxable year of the DISC shall be the same 12-month period as that of any such shareholder (or group).

(3) SUBSEQUENT CHANGES OF OWNERSHIP.—The Secretary shall prescribe regulations under which paragraphs (1) and (2) shall apply to a change of ownership of a corporation after the taxable year of the corporation has been determined under paragraph (1) or (2) only if such change is a substantial change of ownership.

(4) VOTING POWER DETERMINED.—For purposes of this subsection, voting power shall be determined on the basis of total combined voting power of all classes of stock of the corporation entitled to vote.

(i) TAXABLE YEAR OF PERSONAL SERVICE CORPORATIONS.—

(1) IN GENERAL.—For purposes of this subtitle, the taxable year of any personal service corporation shall be the calendar year unless the corporation establishes, to the satisfaction of the Secretary, a business purpose for having a different period for its taxable year. For purposes of this paragraph, any deferral of income to shareholders shall not be treated as a business purpose.

(2) PERSONAL SERVICE CORPORATION.—For purposes of this subsection, the term “personal service corporation” has the meaning given such term by section 269A(b)(1), except that section 269A(b)(2) shall be applied—

(A) by substituting “any” for “more than 10 percent”, and

(B) by substituting “any” for “50 percent or more in value” in section 318(a)(2)(C).

A corporation shall not be treated as a personal service corporation unless more than 10 percent of the stock (by value) in such corporation is held by employee-owners (within the meaning of section 269A(b)(2), as modified by the preceding sentence). If a corporation is a member of an affiliated group filing a consolidated return, all members of such group shall be taken into account in determining whether such corporation is a personal service corporation.

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**SEC. 443. RETURNS FOR A PERIOD OF LESS THAN 12 MONTHS.**

(a) RETURNS FOR SHORT PERIOD.—A return for a period of less than 12 months (referred to in this section as “short period”) shall be made under any of the following circumstances:

(1) CHANGE OF ANNUAL ACCOUNTING PERIOD.—When the taxpayer, with the approval of the Secretary, changes his annual accounting period. In such a case, the return shall be made for the short period beginning on the day after the close of the former taxable year and ending at the close of the day before the day designated as the first day of the new taxable year.

(2) TAXPAYER NOT IN EXISTENCE FOR ENTIRE TAXABLE YEAR.—When the taxpayer is in existence during only part of what would otherwise be his taxable year.

(b) COMPUTATION OF TAX ON CHANGE OF ANNUAL ACCOUNTING PERIOD.—

(1) GENERAL RULE.—If a return is made under paragraph (1) of subsection (a), the taxable income for the short period shall be placed on an annual basis by multiplying the [modified taxable income] *taxable income* for such short period by 12, dividing the result by the number of months in the short period. The tax shall be the same part of the tax computed on the annual basis as the number of months in the short period is of 12 months.

(2) EXCEPTION.—

(A) COMPUTATION BASED ON 12-MONTH PERIOD.—If the taxpayer applies for the benefits of this paragraph and establishes the amount of this taxable income for the 12-month period described in subparagraph (B), computed as if that period were a taxable year and under the law applicable to that year, then the tax for the short period, computed under paragraph (1), shall be reduced to the greater of the following:

(i) an amount which bears the same ratio to the tax computed on the taxable income for the 12-month period as the [modified taxable income] *taxable income* computed on the basis of the short period bears to the [modified taxable income] *taxable income* for the 12-month period; or

(ii) the tax computed on the [modified taxable income] *taxable income* for the short period.

The taxpayer (other than a taxpayer to whom subparagraph (B)(ii) applies) shall compute the tax and file his return without the application of this paragraph.

(B) 12-MONTH PERIOD.—The 12-month period referred to in subparagraph (A) shall be—

(i) the period of 12 months beginning on the first day of the short period, or

(ii) the period of 12 months ending at the close of the last day of the short period, if at the end of the 12 months referred to in clause (i) the taxpayer is not in existence or (if a corporation) has theretofore disposed of substantially all of its assets.

(C) APPLICATION FOR BENEFITS.—Application for the benefits of this paragraph shall be made in such manner and at such time as the regulations prescribed under subparagraph (D) may require; except that the time so prescribed shall not be later than the time (including extensions) for filing the return for the first taxable year which ends on or after the day which is 12 months after the first day of the short period. Such application, in case the return was filed without regard to this paragraph, shall be considered a claim for credit or refund with respect to the amount by which the tax is reduced under this paragraph.

(D) REGULATIONS.—The Secretary shall prescribe such regulations as he deems necessary for the application of this paragraph.

(3) MODIFIED TAXABLE INCOME DEFINED.—For purposes of this subsection the term modified taxable income means, with respect to any period, the gross income for such period minus the deductions allowed by this chapter for such period (but, in

the case of a short period, only the adjusted amount of the deductions for personal exemptions).】

【(c) ADJUSTMENT IN DEDUCTION FOR PERSONAL EXEMPTION.—In the case of a taxpayer other than a corporation, if a return is made for a short period by reason of subsection (a)(1) and if the tax is not computed under subsection (b)(2), then the exemptions allowed as a deduction under section 151 (and any deduction in lieu thereof) shall be reduced to amounts which bear the same ratio to the full exemptions as the number of months in the short period bears to 12.】

【(d) (c) ADJUSTMENT IN COMPUTING MINIMUM TAX AND TAX PREFERENCES.—If a return is made for a short period by reason of subsection (a)—

(1) the alternative minimum taxable income for the short period shall be placed on an annual basis by multiplying such amount by 12 and dividing the result by the number of months in the short period, and

(2) the amount computed under paragraph (1) of section 55(a) shall bear the same relation to the tax computed on the annual basis as the number of months in the short period bears to 12.

【(e) (d) CROSS REFERENCES.—For inapplicability of subsection (b) in computing—

(1) Accumulated earnings tax, see section 536.

(2) Personal holding company tax, see section 546.

(3) The taxable income of a regulated investment company, see section 852(b)(2)(E).

(4) The taxable income of a real estate investment trust, see section 857(b)(2)(C).

For returns for a period of less than 12 months in the case of a debtor's election to terminate a taxable year, see section 1398(d)(2)(E).

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## PART II—METHODS OF ACCOUNTING

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### Subpart C—Taxable Year for Which Deductions Taken

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#### SEC. 461. GENERAL RULE FOR TAXABLE YEAR OF DEDUCTION.

(a) GENERAL RULE.—The amount of any deduction or credit allowed by this subtitle shall be taken for the taxable year which is the proper taxable year under the method of accounting used in computing taxable income.

(b) SPECIAL RULE IN CASE OF DEATH.—In the case of the death of a taxpayer whose taxable income is computed under an accrual method of accounting, any amount accrued as a deduction or credit only by reason of the death of the taxpayer shall not be allowed in computing taxable income for the period in which falls the date of the taxpayer's death.

(c) ACCRUAL OF REAL PROPERTY TAXES.—

(1) IN GENERAL.—If the taxable income is computed under an accrual method of accounting, then, at the election of the tax-

payer, any real property tax which is related to a definite period of time shall be accrued ratably over that period.

(2) WHEN ELECTION MAY BE MADE.—

(A) WITHOUT CONSENT.—A taxpayer may, without the consent of the Secretary, make an election under this subsection for his first taxable year in which he incurs real property taxes. Such an election shall be made not later than the time prescribed by law for filing the return for such year (including extensions thereof).

(B) WITH CONSENT.—A taxpayer may, with the consent of the Secretary, make an election under this subsection at any time.

(d) LIMITATION ON ACCELERATION OF ACCRUAL OF TAXES.—

(1) GENERAL RULE.—In the case of a taxpayer whose taxable income is computed under an accrual method of accounting, to the extent that the time for accruing taxes is earlier than it would be but for any action of any taxing jurisdiction taken after December 31, 1960, then, under regulations prescribed by the Secretary, such taxes shall be treated as accruing at the time they would have accrued but for such action by such taxing jurisdiction.

(2) LIMITATION.—Under regulations prescribed by the Secretary, paragraph (1) shall be inapplicable to any item of tax to the extent that its application would (but for this paragraph) prevent all persons (including successors in interest) from ever taking such item into account.

(e) DIVIDENDS OR INTEREST PAID ON CERTAIN DEPOSITS OR WITHDRAWABLE ACCOUNTS.—Except as provided in regulations prescribed by the Secretary, amounts paid to, or credited to the accounts of, depositors or holders of accounts as dividends or interest on their deposits or withdrawable accounts (if such amounts paid or credited are withdrawable on demand subject only to customary notice to withdraw) by a mutual savings bank not having capital stock represented by shares, a domestic building and loan association, or a cooperative bank shall not be allowed as a deduction for the taxable year to the extent such amounts are paid or credited for periods representing more than 12 months. Any such amount not allowed as a deduction as the result of the application of the preceding sentence shall be allowed as a deduction for such other taxable year as the Secretary determines to be consistent with the preceding sentence.

(f) CONTESTED LIABILITIES.—If—

- (1) the taxpayer contests an asserted liability,
- (2) the taxpayer transfers money or other property to provide for the satisfaction of the asserted liability,
- (3) the contest with respect to the asserted liability exists after the time of the transfer, and
- (4) but for the fact that the asserted liability is contested, a deduction would be allowed for the taxable year of the transfer (or for an earlier taxable year) determined after application of subsection (h),

then the deduction shall be allowed for the taxable year of the transfer. This subsection shall not apply in respect of the deduction for income, war profits, and excess profits taxes imposed by the authority of any foreign country or possession of the United States.



## (g) PREPAID INTEREST.—

(1) IN GENERAL.—If the taxable income of the taxpayer is computed under the cash receipts and disbursements method of accounting, interest paid by the taxpayer which, under regulations prescribed by the Secretary, is properly allocable to any period—

(A) with respect to which the interest represents a charge for the use or forbearance of money, and

(B) which is after the close of the taxable year in which paid,  
shall be charged to capital account and shall be treated as paid in the period to which so allocable.

(2) EXCEPTION.—This subsection shall not apply to points paid in respect of any indebtedness incurred in connection with the purchase or improvement of, and secured by, the principal residence of the taxpayer to the extent that, under regulations prescribed by the Secretary, such payment of points is an established business practice in the area in which such indebtedness is incurred, and the amount of such payment does not exceed the amount generally charged in such area.

## (h) CERTAIN LIABILITIES NOT INCURRED BEFORE ECONOMIC PERFORMANCE.—

(1) IN GENERAL.—For purposes of this title, in determining whether an amount has been incurred with respect to any item during any taxable year, the all events test shall not be treated as met any earlier than when economic performance with respect to such item occurs.

(2) TIME WHEN ECONOMIC PERFORMANCE OCCURS.—Except as provided in regulations prescribed by the Secretary, the time when economic performance occurs shall be determined under the following principles:

(A) SERVICES AND PROPERTY PROVIDED TO THE TAXPAYER.—If the liability of the taxpayer arises out of—

(i) the providing of services to the taxpayer by another person, economic performance occurs as such person provides such services,

(ii) the providing of property to the taxpayer by another person, economic performance occurs as the person provides such property, or

(iii) the use of property by the taxpayer, economic performance occurs as the taxpayer uses such property.

(B) SERVICES AND PROPERTY PROVIDED BY THE TAXPAYER.—If the liability of the taxpayer requires the taxpayer to provide property or services, economic performance occurs as the taxpayer provides such property or services.

(C) WORKERS COMPENSATION AND TORT LIABILITIES OF THE TAXPAYER.—If the liability of the taxpayer requires a payment to another person and—

(i) arises under any workers compensation act, or

(ii) arises out of any tort, economic performance occurs as the payments to such person are made. Subparagraphs (A) and (B) shall not apply to any liability described in the preceding sentence.

(D) OTHER ITEMS.—In the case of any other liability of the taxpayer, economic performance occurs at the time determined under regulations prescribed by the Secretary.

(3) EXCEPTION FOR CERTAIN RECURRING ITEMS.—

(A) IN GENERAL.—Notwithstanding paragraph (1) an item shall be treated as incurred during any taxable year if—

(i) the all events test with respect to such item is met during such taxable year (determined without regard to paragraph (1)),

(ii) economic performance with respect to such item occurs within the shorter of—

(I) a reasonable period after the close of such taxable year, or

(II) 8 1/2 months after the close of such taxable year,

(iii) such item is recurring in nature and the taxpayer consistently treats items of such kind as incurred in the taxable year in which the requirements of clause (i) are met, and

(iv) either—

(I) such item is not a material item, or

(II) the accrual of such item in the taxable year in which the requirements of clause (i) are met results in a more proper match against income than accruing such item in the taxable year in which economic performance occurs.

(B) FINANCIAL STATEMENTS CONSIDERED UNDER SUBPARAGRAPH (A)(IV).—In making a determination under subparagraph (A)(iv), the treatment of such item on financial statements shall be taken into account.

(C) PARAGRAPH NOT TO APPLY TO WORKERS COMPENSATION AND TORT LIABILITIES.—This paragraph shall not apply to any item described in subparagraph (C) of paragraph (2).

(4) ALL EVENTS TEST.—For purposes of this subsection, the all events test is met with respect to any item if all events have occurred which determine the fact of liability and the amount of such liability can be determined with reasonable accuracy.

(5) SUBSECTION NOT TO APPLY TO CERTAIN ITEMS.—This subsection shall not apply to any item for which a deduction is allowable under a provision of this title which specifically provides for a deduction for a reserve for estimated expenses.

(i) SPECIAL RULES FOR TAX SHELTERS.—

(1) RECURRING ITEM EXCEPTION NOT TO APPLY.—In the case of a tax shelter, economic performance shall be determined without regard to paragraph (3) of subsection (h).

(2) SPECIAL RULE FOR SPUDDING OF OIL OR GAS WELLS.—

(A) IN GENERAL.—In the case of a tax shelter, economic performance with respect to amounts paid during the taxable year for drilling an oil or gas well shall be treated as having occurred within a taxable year if drilling of the well commences before the close of the 90th day after the close of the taxable year.

**(B) DEDUCTION LIMITED TO CASH BASIS.—**

(i) **TAX SHELTER PARTNERSHIPS.**—In the case of a tax shelter which is a partnership, in applying section 704(d) to a deduction or loss for any taxable year attributable to an item which is deductible by reason of subparagraph (A), the term “cash basis” shall be substituted for the term “adjusted basis”.

(ii) **OTHER TAX SHELTERS.**—Under regulations prescribed by the Secretary, in the case of a tax shelter other than a partnership, the aggregate amount of the deductions allowable by reason of subparagraph (A) for any taxable year shall be limited in a manner similar to the limitation under clause (i).

**(C) CASH BASIS DEFINED.**—For purposes of subparagraph (B), a partner’s cash basis in a partnership shall be equal to the adjusted basis of such partner’s interest in the partnership, determined without regard to—

- (i) any liability of the partnership, and
- (ii) any amount borrowed by the partner with respect to such partnership which—

(I) was arranged by the partnership or by any person who participated in the organization, sale, or management of the partnership (or any person related to such person within the meaning of section 465(b)(3)(C)), or

(II) was secured by any asset of the partnership.

**(3) TAX SHELTER DEFINED.**—For purposes of this subsection, the term “tax shelter” means—

(A) any enterprise (other than a C corporation) if at any time interests in such enterprise have been offered for sale in any offering required to be registered with any Federal or State agency having the authority to regulate the offering of securities for sale,

(B) any syndicate (within the meaning of section 1256(e)(3)(B)), and

(C) any tax shelter (as defined in section 6662(d)(2)(C)(ii)).

**(4) SPECIAL RULES FOR FARMING.**—In the case of the trade or business of farming (as defined in section 464(e)), in determining whether an entity is a tax shelter, the definition of farming syndicate in **subsection (k)** *subsection (j)* shall be substituted for subparagraphs (A) and (B) of paragraph (3).

**(5) ECONOMIC PERFORMANCE.**—For purposes of this subsection, the term “economic performance” has the meaning given such term by subsection (h).

**[(j) LIMITATION ON EXCESS FARM LOSSES OF CERTAIN TAXPAYERS.—**

**[(1) LIMITATION.**—If a taxpayer other than a C corporation receives any applicable subsidy for any taxable year, any excess farm loss of the taxpayer for the taxable year shall not be allowed.

**[(2) DISALLOWED LOSS CARRIED TO NEXT TAXABLE YEAR.—**Any loss which is disallowed under paragraph (1) shall be treated as a deduction of the taxpayer attributable to farming businesses in the next taxable year.

[(3) APPLICABLE SUBSIDY.—For purposes of this subsection, the term “applicable subsidy” means—

[(A) any direct or counter-cyclical payment under title I of the Food, Conservation, and Energy Act of 2008, or any payment elected to be received in lieu of any such payment, or

[(B) any Commodity Credit Corporation loan.

[(4) EXCESS FARM LOSS.—For purposes of this subsection—

[(A) IN GENERAL.—The term “excess farm loss” means the excess of—

[(i) the aggregate deductions of the taxpayer for the taxable year which are attributable to farming businesses of such taxpayer (determined without regard to whether or not such deductions are disallowed for such taxable year under paragraph (1)), over

[(ii) the sum of—

[(I) the aggregate gross income or gain of such taxpayer for the taxable year which is attributable to such farming businesses, plus

[(II) the threshold amount for the taxable year.

[(B) THRESHOLD AMOUNT.—

[(i) IN GENERAL.—The term “threshold amount” means, with respect to any taxable year, the greater of—

[(I) \$300,000 (\$150,000 in the case of married individuals filing separately), or

[(II) the excess (if any) of the aggregate amounts described in subparagraph (A)(ii)(I) for the 5-consecutive taxable year period preceding the taxable year over the aggregate amounts described in subparagraph (A)(i) for such period.

[(ii) SPECIAL RULES FOR DETERMINING AGGREGATE AMOUNTS.—For purposes of clause (i)(II)—

[(I) notwithstanding the disregard in subparagraph (A)(i) of any disallowance under paragraph (1), in the case of any loss which is carried forward under paragraph (2) from any taxable year, such loss (or any portion thereof) shall be taken into account for the first taxable year in which a deduction for such loss (or portion) is not disallowed by reason of this subsection, and

[(II) the Secretary shall prescribe rules for the computation of the aggregate amounts described in such clause in cases where the filing status of the taxpayer is not the same for the taxable year and each of the taxable years in the period described in such clause.

[(C) FARMING BUSINESS.—

[(i) IN GENERAL.—The term “farming business” has the meaning given such term in section 263A(e)(4).

[(ii) CERTAIN TRADES AND BUSINESSES INCLUDED.—If, without regard to this clause, a taxpayer is engaged in a farming business with respect to any agricultural or horticultural commodity—

[(I) the term “farming business” shall include any trade or business of the taxpayer of the processing of such commodity (without regard to whether the processing is incidental to the growing, raising, or harvesting of such commodity), and

[(II) if the taxpayer is a member of a cooperative to which subchapter T applies, any trade or business of the cooperative described in subclause (I) shall be treated as the trade or business of the taxpayer.

[(D) CERTAIN LOSSES DISREGARDED.—For purposes of subparagraph (A)(i), there shall not be taken into account any deduction for any loss arising by reason of fire, storm, or other casualty, or by reason of disease or drought, involving any farming business.

[(5) APPLICATION OF SUBSECTION IN CASE OF PARTNERSHIPS AND S CORPORATIONS.—In the case of a partnership or S corporation—

[(A) this subsection shall be applied at the partner or shareholder level, and

[(B) each partner’s or shareholder’s proportionate share of the items of income, gain, or deduction of the partnership or S corporation for any taxable year from farming businesses attributable to the partnership or S corporation, and of any applicable subsidies received by the partnership or S corporation during the taxable year, shall be taken into account by the partner or shareholder in applying this subsection to the taxable year of such partner or shareholder with or within which the taxable year of the partnership or S corporation ends.

The Secretary may provide rules for the application of this paragraph to any other pass-thru entity to the extent necessary to carry out the provisions of this subsection.

[(6) ADDITIONAL REPORTING.—The Secretary may prescribe such additional reporting requirements as the Secretary determines appropriate to carry out the purposes of this subsection.

[(7) COORDINATION WITH SECTION 469.—This subsection shall be applied before the application of section 469.]

[(k)] (j) FARMING SYNDICATE DEFINED.—

(1) IN GENERAL.—For purposes of subsection (i)(4), the term “farming syndicate” means—

(A) a partnership or any other enterprise other than a corporation which is not an S corporation engaged in the trade or business of farming, if at any time interests in such partnership or enterprise have been offered for sale in any offering required to be registered with any Federal or State agency having authority to regulate the offering of securities for sale, or

(B) a partnership or any other enterprise other than a corporation which is not an S corporation engaged in the trade or business of farming, if more than 35 percent of the losses during any period are allocable to limited partners or limited entrepreneurs.

(2) **HOLDINGS ATTRIBUTABLE TO ACTIVE MANAGEMENT.**—For purposes of paragraph (1)(B), the following shall be treated as an interest which is not held by a limited partner or a limited entrepreneur:

(A) in the case of any individual who has actively participated (for a period of not less than 5 years) in the management of any trade or business of farming, any interest in a partnership or other enterprise which is attributable to such active participation,

(B) in the case of any individual whose principal residence is on a farm, any partnership or other enterprise engaged in the trade or business of farming such farm,

(C) in the case of any individual who is actively participating in the management of any trade or business of farming or who is an individual who is described in subparagraph (A) or (B), any participation in the further processing of livestock which was raised in such trade or business (or in the trade or business referred to in subparagraph (A) or (B)),

(D) in the case of an individual whose principal business activity involves active participation in the management of a trade or business of farming, any interest in any other trade or business of farming, and,

(E) any interest held by a member of the family (or a spouse of any such member) of a grandparent of an individual described in subparagraph (A), (B), (C), or (D) if the interest in the partnership or the enterprise is attributable to the active participation of the individual described in subparagraph (A), (B), (C), or (D).

For purposes of subparagraph (A), where one farm is substituted for or added to another farm, both farms shall be treated as one farm. For purposes of subparagraph (E), the term “family” has the meaning given to such term by section 267(c)(4).

(3) **FARMING.**—For purposes of this subsection, the term “farming” has the meaning given to such term by section 464(e).

(4) **LIMITED ENTREPRENEUR.**—For purposes of this subsection, the term “limited entrepreneur” means a person who—

(A) has an interest in an enterprise other than as a limited partner, and

(B) does not actively participate in the management of such enterprise.

**[(1)] (k) LIMITATION ON EXCESS BUSINESS LOSSES OF NONCORPORATE TAXPAYERS.**—

**[(1) LIMITATION.**—

**[(A) subsection (j) (relating to limitation on excess farm losses of certain taxpayers) shall not apply, and**

**[(B) any excess business loss of the taxpayer for the taxable year shall not be allowed.]]**

*(1) LIMITATION.—In the case of a taxpayer other than a corporation, any excess business loss of the taxpayer for the taxable year shall not be allowed.*

(2) **DISALLOWED LOSS CARRYOVER.**—Any loss which is disallowed under paragraph (1) shall be treated as a net oper-

ating loss carryover to the following taxable year under section 172.

(3) EXCESS BUSINESS LOSS.—For purposes of this subsection—

(A) IN GENERAL.—The term “excess business loss” means the excess (if any) of—

(i) the aggregate deductions of the taxpayer for the taxable year which are attributable to trades or businesses of such taxpayer (determined without regard to whether or not such deductions are disallowed for such taxable year under paragraph (1)), over

(ii) the sum of—

(I) the aggregate gross income or gain of such taxpayer for the taxable year which is attributable to such trades or businesses, plus

(II) \$250,000 (200 percent of such amount in the case of a joint return).

(B) ADJUSTMENT FOR INFLATION.—In the case of any taxable year beginning after December 31, 2018, the \$250,000 amount in subparagraph (A)(ii)(II) shall be increased by an amount equal to—

(i) such dollar amount, multiplied by

(ii) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “2017” for “2016” in subparagraph (A)(ii) thereof.

If any amount as increased under the preceding sentence is not a multiple of \$1,000, such amount shall be rounded to the nearest multiple of \$1,000.

(4) APPLICATION OF SUBSECTION IN CASE OF PARTNERSHIPS AND S CORPORATIONS.—In the case of a partnership or S corporation—

(A) this subsection shall be applied at the partner or shareholder level, and

(B) each partner’s or shareholder’s allocable share of the items of income, gain, deduction, or loss of the partnership or S corporation for any taxable year from trades or businesses attributable to the partnership or S corporation shall be taken into account by the partner or shareholder in applying this subsection to the taxable year of such partner or shareholder with or within which the taxable year of the partnership or S corporation ends.

For purposes of this paragraph, in the case of an S corporation, an allocable share shall be the shareholder’s pro rata share of an item.

(5) ADDITIONAL REPORTING.—The Secretary shall prescribe such additional reporting requirements as the Secretary determines necessary to carry out the purposes of this subsection.

(6) COORDINATION WITH SECTION 469.—This subsection shall be applied after the application of section 469.

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**SEC. 464. LIMITATIONS ON DEDUCTIONS FOR CERTAIN FARMING EXPENSES.**

(a) **GENERAL RULE.**—In the case of any taxpayer to whom subsection (d) applies, a deduction (otherwise allowable under this chapter) for amounts paid for feed, seed, fertilizer, or other similar farm supplies shall only be allowed for the taxable year in which such feed, seed, fertilizer, or other supplies are actually used or consumed, or, if later, for the taxable year for which allowable as a deduction (determined without regard to this section).

(b) **CERTAIN POULTRY EXPENSES.**—In the case of any taxpayer to whom subsection (d) applies—

(1) the cost of poultry (including egg-laying hens and baby chicks) purchased for use in a trade or business (or both for use in a trade or business and for sale) shall be capitalized and deducted ratably over the lesser of 12 months or their useful life in the trade or business, and

(2) the cost of poultry purchased for sale shall be deducted for the taxable year in which the poultry is sold or otherwise disposed of.

(c) **EXCEPTION.**—Subsection (a) shall not apply to any amount paid for supplies which are on hand at the close of the taxable year on account of fire, storm, or other casualty, or on account of disease or drought.

(d) **CERTAIN PERSONS PREPAYING 50 PERCENT OR MORE OF CERTAIN FARMING EXPENSES.**—

(1) **TAXPAYER TO WHOM SUBSECTION APPLIES.**—This subsection applies to any taxpayer for any taxable year if such taxpayer—

(A) does not use an accrual method of accounting,

(B) has excess prepaid farm supplies for the taxable year, and

(C) is not a qualified farm-related taxpayer.

(2) **QUALIFIED FARM-RELATED TAXPAYER.**—

(A) **IN GENERAL.**—For purposes of this subsection, the term “qualified farm-related taxpayer” means any farm-related taxpayer if—

(i)(I) the aggregate prepaid farm supplies for the 3 taxable years preceding the taxable year are less than 50 percent of,

(II) the aggregate deductible farming expenses (other than prepaid farm supplies) for such 3 taxable years, or

(ii) the taxpayer has excess prepaid farm supplies for the taxable year by reason of any change in business operation directly attributable to extraordinary circumstances.

(B) **FARM-RELATED TAXPAYER.**—For purposes of this paragraph, the term “farm-related taxpayer” means any taxpayer—

(i) whose principal residence (within the meaning of section 121) is on a farm,

(ii) who has a principal occupation of farming, or

(iii) who is a member of the family (within the meaning of [section 461(k)(2)(E)] *section 461(j)(2)(E)*) of a taxpayer described in clause (i) or (ii).



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

(A) EXCESS PREPAID FARM SUPPLIES.—The term “excess prepaid farm supplies” means the prepaid farm supplies for the taxable year to the extent the amount of such supplies exceeds 50 percent of the deductible farming expenses for the taxable year (other than prepaid farm supplies).

(B) PREPAID FARM SUPPLIES.—The term “prepaid farm supplies” means any amounts which are described in subsection (a) or (b) and would be allowable for a subsequent taxable year under the rules of subsections (a) and (b).

(C) DEDUCTIBLE FARMING EXPENSES.—The term “deductible farming expenses” means any amount allowable as a deduction under this chapter (including any amount allowable as a deduction for depreciation or amortization) which is properly allocable to the trade or business of farming.

(e) FARMING.—For purposes of this section, the term “farming” means the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity including the raising, shearing, feeding, caring for, training, and management of animals. For purposes of the preceding sentence, trees (other than trees bearing fruit or nuts) shall not be treated as an agricultural or horticultural commodity.

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**Subchapter F—Exempt Organizations**

\* \* \* \* \*

**PART I—GENERAL RULE**

\* \* \* \* \*

**SEC. 501. EXEMPTION FROM TAX ON CORPORATIONS, CERTAIN TRUSTS, ETC.**

(a) EXEMPTION FROM TAXATION.—An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503.

(b) TAX ON UNRELATED BUSINESS INCOME AND CERTAIN OTHER ACTIVITIES.—An organization exempt from taxation under subsection (a) shall be subject to tax to the extent provided in parts II, III, and VI of this subchapter, but (notwithstanding parts II, III, and VI of this subchapter) shall be considered an organization exempt from income taxes for the purpose of any law which refers to organizations exempt from income taxes.

(c) LIST OF EXEMPT ORGANIZATIONS.—The following organizations are referred to in subsection (a):

(1) Any corporation organized under Act of Congress which is an instrumentality of the United States but only if such corporation—

(A) is exempt from Federal income taxes—

(i) under such Act as amended and supplemented before July 18, 1984, or

(ii) under this title without regard to any provision of law which is not contained in this title and which is not contained in a revenue Act, or

(B) is described in subsection (1).

(2) Corporations organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempt under this section. Rules similar to the rules of subparagraph (G) of paragraph (25) shall apply for purposes of this paragraph.

(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

(4)(A) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

(B) Subparagraph (A) shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.

(5) Labor, agricultural, or horticultural organizations.

(6) Business leagues, chambers of commerce, real-estate boards, boards of trade, or professional football leagues (whether or not administering a pension fund for football players), not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(7) Clubs organized for pleasure, recreation, and other non-profitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder.

(8) Fraternal beneficiary societies, orders, or associations—

(A) operating under the lodge system or for the exclusive benefit of the members of a fraternity itself operating under the lodge system, and

(B) providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents.

(9) Voluntary employees' beneficiary associations providing for the payment of life, sick, accident, or other benefits to the members of such association or their dependents or designated

beneficiaries, if no part of the net earnings of such association inures (other than through such payments) to the benefit of any private shareholder or individual. For purposes of providing for the payment of sick and accident benefits to members of such an association and their dependents, the term “dependent” shall include any individual who is a child (as defined in [section 152(f)(1)] *section 7706(f)(1)*) of a member who as of the end of the calendar year has not attained age 27.

(10) Domestic fraternal societies, orders, or associations, operating under the lodge system—

(A) the net earnings of which are devoted exclusively to religious, charitable, scientific, literary, educational, and fraternal purposes, and

(B) which do not provide for the payment of life, sick, accident, or other benefits.

(11) Teachers’ retirement fund associations of a purely local character, if—

(A) no part of their net earnings inures (other than through payment of retirement benefits) to the benefit of any private shareholder or individual, and

(B) the income consists solely of amounts received from public taxation, amounts received from assessments on the teaching salaries of members, and income in respect of investments.

(12)(A) Benevolent life insurance associations of a purely local character, mutual ditch or irrigation companies, mutual or cooperative telephone companies, or like organizations; but only if 85 percent or more of the income consists of amounts collected from members for the sole purpose of meeting losses and expenses.

(B) In the case of a mutual or cooperative telephone company, subparagraph (A) shall be applied without taking into account any income received or accrued—

(i) from a nonmember telephone company for the performance of communication services which involve members of the mutual or cooperative telephone company,

(ii) from qualified pole rentals,

(iii) from the sale of display listings in a directory furnished to the members of the mutual or cooperative telephone company, or

(iv) from the prepayment of a loan under section 306A, 306B, or 311 of the Rural Electrification Act of 1936 (as in effect on January 1, 1987).

(C) In the case of a mutual or cooperative electric company, subparagraph (A) shall be applied without taking into account any income received or accrued—

(i) from qualified pole rentals, or

(ii) from any provision or sale of electric energy transmission services or ancillary services if such services are provided on a nondiscriminatory open access basis under an open access transmission tariff approved or accepted by FERC or under an independent transmission provider agreement approved or accepted

by FERC (other than income received or accrued directly or indirectly from a member),

(iii) from the provision or sale of electric energy distribution services or ancillary services if such services are provided on a nondiscriminatory open access basis to distribute electric energy not owned by the mutual or electric cooperative company—

(I) to end-users who are served by distribution facilities not owned by such company or any of its members (other than income received or accrued directly or indirectly from a member), or

(II) generated by a generation facility not owned or leased by such company or any of its members and which is directly connected to distribution facilities owned by such company or any of its members (other than income received or accrued directly or indirectly from a member),

(iv) from any nuclear decommissioning transaction,

or

(v) from any asset exchange or conversion transaction.

(D) For purposes of this paragraph, the term “qualified pole rental” means any rental of a pole (or other structure used to support wires) if such pole (or other structure)—

(i) is used by the telephone or electric company to support one or more wires which are used by such company in providing telephone or electric services to its members, and

(ii) is used pursuant to the rental to support one or more wires (in addition to the wires described in clause (i)) for use in connection with the transmission by wire of electricity or of telephone or other communications.

For purposes of the preceding sentence, the term “rental” includes any sale of the right to use the pole (or other structure).

(E) For purposes of subparagraph (C)(ii), the term “FERC” means—

(i) the Federal Energy Regulatory Commission, or

(ii) in the case of any utility with respect to which all of the electricity generated, transmitted, or distributed by such utility is generated, transmitted, distributed, and consumed in the same State, the State agency of such State with the authority to regulate electric utilities.

(F) For purposes of subparagraph (C)(iv), the term “nuclear decommissioning transaction” means—

(i) any transfer into a trust, fund, or instrument established to pay any nuclear decommissioning costs if the transfer is in connection with the transfer of the mutual or cooperative electric company’s interest in a nuclear power plant or nuclear power plant unit,

(ii) any distribution from any trust, fund, or instrument established to pay any nuclear decommissioning costs, or

(iii) any earnings from any trust, fund, or instrument established to pay any nuclear decommissioning costs.

(G) For purposes of subparagraph (C)(v), the term “asset exchange or conversion transaction” means any voluntary exchange or involuntary conversion of any property related to generating, transmitting, distributing, or selling electric energy by a mutual or cooperative electric company, the gain from which qualifies for deferred recognition under section 1031 or 1033, but only if the replacement property acquired by such company pursuant to such section constitutes property which is used, or to be used, for—

(i) generating, transmitting, distributing, or selling electric energy, or

(ii) producing, transmitting, distributing, or selling natural gas.

(H)(i) In the case of a mutual or cooperative electric company described in this paragraph or an organization described in section 1381(a)(2)(C), income received or accrued from a load loss transaction shall be treated as an amount collected from members for the sole purpose of meeting losses and expenses.

(ii) For purposes of clause (i), the term “load loss transaction” means any wholesale or retail sale of electric energy (other than to members) to the extent that the aggregate sales during the recovery period do not exceed the load loss mitigation sales limit for such period.

(iii) For purposes of clause (ii), the load loss mitigation sales limit for the recovery period is the sum of the annual load losses for each year of such period.

(iv) For purposes of clause (iii), a mutual or cooperative electric company’s annual load loss for each year of the recovery period is the amount (if any) by which—

(I) the megawatt hours of electric energy sold during such year to members of such electric company are less than

(II) the megawatt hours of electric energy sold during the base year to such members.

(v) For purposes of clause (iv)(II), the term “base year” means—

(I) the calendar year preceding the start-up year, or

(II) at the election of the mutual or cooperative electric company, the second or third calendar years preceding the start-up year.

(vi) For purposes of this subparagraph, the recovery period is the 7-year period beginning with the start-up year.

(vii) For purposes of this subparagraph, the start-up year is the first year that the mutual or cooperative electric company offers nondiscriminatory open access or the calendar year which includes the date of the en-

actment of this subparagraph, if later, at the election of such company.

(viii) A company shall not fail to be treated as a mutual or cooperative electric company for purposes of this paragraph or as a corporation operating on a cooperative basis for purposes of section 1381(a)(2)(C) by reason of the treatment under clause (i).

(ix) For purposes of subparagraph (A), in the case of a mutual or cooperative electric company, income received, or accrued, indirectly from a member shall be treated as an amount collected from members for the sole purpose of meeting losses and expenses.

(I) In the case of a mutual or cooperative electric company described in this paragraph or an organization described in section 1381(a)(2), income received or accrued in connection with an election under section 45J(e)(1) shall be treated as an amount collected from members for the sole purpose of meeting losses and expenses.

(13) Cemetery companies owned and operated exclusively for the benefit of their members or which are not operated for profit; and any corporation chartered solely for the purpose of the disposal of bodies by burial or cremation which is not permitted by its charter to engage in any business not necessarily incident to that purpose and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(14)(A) Credit unions without capital stock organized and operated for mutual purposes and without profit.

(B) Corporations or associations without capital stock organized before September 1, 1957, and operated for mutual purposes and without profit for the purpose of providing reserve funds for, and insurance of shares or deposits in—

(i) domestic building and loan associations,

(ii) cooperative banks without capital stock organized and operated for mutual purposes and without profit,

(iii) mutual savings banks not having capital stock represented by shares, or

(iv) mutual savings banks described in section 591(b). (C) Corporations or associations organized before September 1, 1957, and operated for mutual purposes and without profit for the purpose of providing reserve funds for associations or banks described in clause (i), (ii), or (iii) of subparagraph (B); but only if 85 percent or more of the income is attributable to providing such reserve funds and to investments. This subparagraph shall not apply to any corporation or association entitled to exemption under subparagraph (B).

(15)(A) Insurance companies (as defined in section 816(a)) other than life (including interinsurers and reciprocal underwriters) if—

(i)(I) the gross receipts for the taxable year do not exceed \$600,000, and

- (II) more than 50 percent of such gross receipts consist of premiums, or
- (ii) in the case of a mutual insurance company—
  - (I) the gross receipts of which for the taxable year do not exceed \$150,000, and
  - (II) more than 35 percent of such gross receipts consist of premiums.

Clause (ii) shall not apply to a company if any employee of the company, or a member of the employee's family (as defined in section 2032A(e)(2)), is an employee of another company exempt from taxation by reason of this paragraph (or would be so exempt but for this sentence).

(B) For purposes of subparagraph (A), in determining whether any company or association is described in subparagraph (A), such company or association shall be treated as receiving during the taxable year amounts described in subparagraph (A) which are received during such year by all other companies or associations which are members of the same controlled group as the insurance company or association for which the determination is being made.

(C) For purposes of subparagraph (B), the term "controlled group" has the meaning given such term by section 831(b)(2)(B)(ii), except that in applying section 831(b)(2)(B)(ii) for purposes of this subparagraph, subparagraphs (B) and (C) of section 1563(b)(2) shall be disregarded.

(16) Corporations organized by an association subject to part IV of this subchapter or members thereof, for the purpose of financing the ordinary crop operations of such members or other producers, and operated in conjunction with such association. Exemption shall not be denied any such corporation because it has capital stock, if the dividend rate of such stock is fixed at not to exceed the legal rate of interest in the State of incorporation or 8 percent per annum, whichever is greater, on the value of the consideration for which the stock was issued, and if substantially all such stock (other than nonvoting preferred stock, the owners of which are not entitled or permitted to participate, directly or indirectly, in the profits of the corporation, on dissolution or otherwise, beyond the fixed dividends) is owned by such association, or members thereof; nor shall exemption be denied any such corporation because there is accumulated and maintained by it a reserve required by State law or a reasonable reserve for any necessary purpose.

(17)(A) A trust or trusts forming part of a plan providing for the payment of supplemental unemployment compensation benefits, if—

- (i) under the plan, it is impossible, at any time prior to the satisfaction of all liabilities, with respect to employees under the plan, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, any purpose other than the providing of supplemental unemployment compensation benefits,

- (ii) such benefits are payable to employees under a classification which is set forth in the plan and which

is found by the Secretary not to be discriminatory in favor of employees who are highly compensated employees (within the meaning of section 414(q)), and

(iii) such benefits do not discriminate in favor of employees who are highly compensated employees (within the meaning of section 414(q)). A plan shall not be considered discriminatory within the meaning of this clause merely because the benefits received under the plan bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of the employees covered by the plan.

(B) In determining whether a plan meets the requirements of subparagraph (A), any benefits provided under any other plan shall not be taken into consideration, except that a plan shall not be considered discriminatory—

(i) merely because the benefits under the plan which are first determined in a nondiscriminatory manner within the meaning of subparagraph (A) are then reduced by any sick, accident, or unemployment compensation benefits received under State or Federal law (or reduced by a portion of such benefits if determined in a nondiscriminatory manner), or

(ii) merely because the plan provides only for employees who are not eligible to receive sick, accident, or unemployment compensation benefits under State or Federal law the same benefits (or a portion of such benefits if determined in a nondiscriminatory manner) which such employees would receive under such laws if such employees were eligible for such benefits, or

(iii) merely because the plan provides only for employees who are not eligible under another plan (which meets the requirements of subparagraph (A)) of supplemental unemployment compensation benefits provided wholly by the employer the same benefits (or a portion of such benefits if determined in a nondiscriminatory manner) which such employees would receive under such other plan if such employees were eligible under such other plan, but only if the employees eligible under both plans would make a classification which would be nondiscriminatory within the meaning of subparagraph (A).

(C) A plan shall be considered to meet the requirements of subparagraph (A) during the whole of any year of the plan if on one day in each quarter it satisfies such requirements.

(D) The term “supplemental unemployment compensation benefits” means only—

(i) benefits which are paid to an employee because of his involuntary separation from the employment of the employer (whether or not such separation is temporary) resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions, and

(ii) sick and accident benefits subordinate to the benefits described in clause (i).



(E) Exemption shall not be denied under subsection (a) to any organization entitled to such exemption as an association described in paragraph (9) of this subsection merely because such organization provides for the payment of supplemental unemployment benefits (as defined in subparagraph (D)(i)).

(18) A trust or trusts created before June 25, 1959, forming part of a plan providing for the payment of benefits under a pension plan funded only by contributions of employees, if—

(A) under the plan, it is impossible, at any time prior to the satisfaction of all liabilities with respect to employees under the plan, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, any purpose other than the providing of benefits under the plan,

(B) such benefits are payable to employees under a classification which is set forth in the plan and which is found by the Secretary not to be discriminatory in favor of employees who are highly compensated employees (within the meaning of section 414(q)),

(C) such benefits do not discriminate in favor of employees who are highly compensated employees (within the meaning of section 414(q)). A plan shall not be considered discriminatory within the meaning of this subparagraph merely because the benefits received under the plan bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of the employees covered by the plan, and

(D) in the case of a plan under which an employee may designate certain contributions as deductible—

(i) such contributions do not exceed the amount with respect to which a deduction is allowable under section 219(b)(3),

(ii) requirements similar to the requirements of section 401(k)(3)(A)(ii) are met with respect to such elective contributions,

(iii) such contributions are treated as elective deferrals for purposes of section 402(g), and

(iv) the requirements of section 401(a)(30) are met.

For purposes of subparagraph (D)(ii), rules similar to the rules of section 401(k)(8) shall apply. For purposes of section 4979, any excess contribution under clause (ii) shall be treated as an excess contribution under a cash or deferred arrangement.

(19) A post or organization of past or present members of the Armed Forces of the United States, or an auxiliary unit or society of, or a trust or foundation for, any such post or organization—

(A) organized in the United States or any of its possessions,

(B) at least 75 percent of the members of which are past or present members of the Armed Forces of the United States and substantially all of the other members of which are individuals who are cadets or are spouses, widows, widowers, ancestors, or lineal descendants of past or

present members of the Armed Forces of the United States or of cadets, and

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(21)(A) A trust or trusts established in writing, created or organized in the United States, and contributed to by any person (except an insurance company) if—

(i) the purpose of such trust or trusts is exclusively—

(I) to satisfy, in whole or in part, the liability of such person for, or with respect to, claims for compensation for disability or death due to pneumoconiosis under Black Lung Acts,

(II) to pay premiums for insurance exclusively covering such liability,

(III) to pay administrative and other incidental expenses of such trust in connection with the operation of the trust and the processing of claims against such person under Black Lung Acts, and

(IV) to pay accident or health benefits for retired miners and their spouses and dependents (including administrative and other incidental expenses of such trust in connection therewith) or premiums for insurance exclusively covering such benefits; and

(ii) no part of the assets of the trust may be used for, or diverted to, any purpose other than—

(I) the purposes described in clause (i),

(II) investment (but only to the extent that the trustee determines that a portion of the assets is not currently needed for the purposes described in clause (i)) in qualified investments, or

(III) payment into the Black Lung Disability Trust Fund established under section 9501, or into the general fund of the United States Treasury (other than in satisfaction of any tax or other civil or criminal liability of the person who established or contributed to the trust).

(B) No deduction shall be allowed under this chapter for any payment described in subparagraph (A)(i)(IV) from such trust.

(C) Payments described in subparagraph (A)(i)(IV) may be made from such trust during a taxable year only to the extent that the aggregate amount of such payments during such taxable year does not exceed the excess (if any), as of the close of the preceding taxable year, of—

(i) the fair market value of the assets of the trust, over

(ii) 110 percent of the present value of the liability described in subparagraph (A)(i)(I) of such person.

The determinations under the preceding sentence shall be made by an independent actuary using actuarial methods and assumptions (not inconsistent with the regulations prescribed under section 192(c)(1)(A)) each of which is reasonable and which are reasonable in the aggregate.

(D) For purposes of this paragraph:

(i) The term “Black Lung Acts” means part C of title IV of the Federal Mine Safety and Health Act of 1977, and any State law providing compensation for disability or death due to that pneumoconiosis.

(ii) The term “qualified investments” means—

(I) public debt securities of the United States,

(II) obligations of a State or local government which are not in default as to principal or interest, and

(III) time or demand deposits in a bank (as defined in section 581) or an insured credit union (within the meaning of section 101(7) of the Federal Credit Union Act, 12 U.S.C. 1752(7)) located in the United States.

(iii) The term “miner” has the same meaning as such term has when used in section 402(d) of the Black Lung Benefits Act (30 U.S.C. 902(d)).

(iv) The term “incidental expenses” includes legal, accounting, actuarial, and trustee expenses.

(22) A trust created or organized in the United States and established in writing by the plan sponsors of multiemployer plans if—

(A) the purpose of such trust is exclusively—

(i) to pay any amount described in section 4223(c) or (h) of the Employee Retirement Income Security Act of 1974, and

(ii) to pay reasonable and necessary administrative expenses in connection with the establishment and operation of the trust and the processing of claims against the trust,

(B) no part of the assets of the trust may be used for, or diverted to, any purpose other than—

(i) the purposes described in subparagraph (A), or

(ii) the investment in securities, obligations, or time or demand deposits described in clause (ii) of paragraph (21)(D),

(C) such trust meets the requirements of paragraphs (2), (3), and (4) of section 4223(b), 4223(h), or, if applicable, section 4223(c) of the Employee Retirement Income Security Act of 1974, and

(D) the trust instrument provides that, on dissolution of the trust, assets of the trust may not be paid other than to plans which have participated in the plan or, in the case of a trust established under section 4223(h) of such Act, to plans with respect to which employers have participated in the fund.

(23) Any association organized before 1880 more than 75 percent of the members of which are present or past members of the Armed Forces and a principal purpose of which is to provide insurance and other benefits to veterans or their dependents.

(24) A trust described in section 4049 of the Employee Retirement Income Security Act of 1974 (as in effect on the date

of the enactment of the Single-Employer Pension Plan Amendments Act of 1986).

- (25)(A) Any corporation or trust which—
- (i) has no more than 35 shareholders or beneficiaries,
  - (ii) has only 1 class of stock or beneficial interest, and
  - (iii) is organized for the exclusive purposes of—
    - (I) acquiring real property and holding title to, and collecting income from, such property, and
    - (II) remitting the entire amount of income from such property (less expenses) to 1 or more organizations described in subparagraph (C) which are shareholders of such corporation or beneficiaries of such trust.

For purposes of clause (iii), the term “real property” shall not include any interest as a tenant in common (or similar interest) and shall not include any indirect interest.

(B) A corporation or trust shall be described in subparagraph (A) without regard to whether the corporation or trust is organized by 1 or more organizations described in subparagraph (C).

(C) An organization is described in this subparagraph if such organization is—

- (i) a qualified pension, profit sharing, or stock bonus plan that meets the requirements of section 401(a),
- (ii) a governmental plan (within the meaning of section 414(d)),
- (iii) the United States, any State or political subdivision thereof, or any agency or instrumentality of any of the foregoing, or
- (iv) any organization described in paragraph (3).

(D) A corporation or trust shall in no event be treated as described in subparagraph (A) unless such corporation or trust permits its shareholders or beneficiaries—

- (i) to dismiss the corporation’s or trust’s investment adviser, following reasonable notice, upon a vote of the shareholders or beneficiaries holding a majority of interest in the corporation or trust, and
- (ii) to terminate their interest in the corporation or trust by either, or both, of the following alternatives, as determined by the corporation or trust:

(I) by selling or exchanging their stock in the corporation or interest in the trust (subject to any Federal or State securities law) to any organization described in subparagraph (C) so long as the sale or exchange does not increase the number of shareholders or beneficiaries in such corporation or trust above 35, or

(II) by having their stock or interest redeemed by the corporation or trust after the shareholder or beneficiary has provided 90 days notice to such corporation or trust.

(E)(i) For purposes of this title—

(I) a corporation which is a qualified subsidiary shall not be treated as a separate corporation, and

(II) all assets, liabilities, and items of income, deduction, and credit of a qualified subsidiary shall be treated as assets, liabilities, and such items (as the case may be) of the corporation or trust described in subparagraph (A).

(ii) For purposes of this subparagraph, the term “qualified subsidiary” means any corporation if, at all times during the period such corporation was in existence, 100 percent of the stock of such corporation is held by the corporation or trust described in subparagraph (A).

(iii) For purposes of this subtitle, if any corporation which was a qualified subsidiary ceases to meet the requirements of clause (ii), such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the corporation or trust described in subparagraph (A) in exchange for its stock.

(F) For purposes of subparagraph (A), the term “real property” includes any personal property which is leased under, or in connection with, a lease of real property, but only if the rent attributable to such personal property (determined under the rules of section 856(d)(1)) for the taxable year does not exceed 15 percent of the total rent for the taxable year attributable to both the real and personal property leased under, or in connection with, such lease.

(G)(i) An organization shall not be treated as failing to be described in this paragraph merely by reason of the receipt of any otherwise disqualifying income which is incidentally derived from the holding of real property.

(ii) Clause (i) shall not apply if the amount of gross income described in such clause exceeds 10 percent of the organization’s gross income for the taxable year unless the organization establishes to the satisfaction of the Secretary that the receipt of gross income described in clause (i) in excess of such limitation was inadvertent and reasonable steps are being taken to correct the circumstances giving rise to such income.

(26) Any membership organization if—

(A) such organization is established by a State exclusively to provide coverage for medical care (as defined in section 213(d)) on a not-for-profit basis to individuals described in subparagraph (B) through—

(i) insurance issued by the organization, or

(ii) a health maintenance organization under an arrangement with the organization,

(B) the only individuals receiving such coverage through the organization are individuals—

(i) who are residents of such State, and

(ii) who, by reason of the existence or history of a medical condition—

(I) are unable to acquire medical care coverage for such condition through insurance or from a health maintenance organization, or

(II) are able to acquire such coverage only at a rate which is substantially in excess of the rate for such coverage through the membership organization,

(C) the composition of the membership in such organization is specified by such State, and

(D) no part of the net earnings of the organization inures to the benefit of any private shareholder or individual.

A spouse and any qualifying child (as defined in section 24(c)) of an individual described in subparagraph (B) (without regard to this sentence) shall be treated as described in subparagraph (B).

(27)(A) Any membership organization if—

(i) such organization is established before June 1, 1996, by a State exclusively to reimburse its members for losses arising under workmen's compensation acts,

(ii) such State requires that the membership of such organization consist of—

(I) all persons who issue insurance covering workmen's compensation losses in such State, and

(II) all persons and governmental entities who self-insure against such losses, and

(iii) such organization operates as a non-profit organization by—

(I) returning surplus income to its members or workmen's compensation policyholders on a periodic basis, and

(II) reducing initial premiums in anticipation of investment income.

(B) Any organization (including a mutual insurance company) if—

(i) such organization is created by State law and is organized and operated under State law exclusively to—

(I) provide workmen's compensation insurance which is required by State law or with respect to which State law provides significant disincentives if such insurance is not purchased by an employer, and

(II) provide related coverage which is incidental to workmen's compensation insurance,

(ii) such organization must provide workmen's compensation insurance to any employer in the State (for employees in the State or temporarily assigned out-of-State) which seeks such insurance and meets other reasonable requirements relating thereto,

(iii)(I) the State makes a financial commitment with respect to such organization either by extending the full faith and credit of the State to the initial debt of such organization or by providing the initial operating capital of such organization, and (II) in the case of periods after the date of enactment of this subparagraph,

the assets of such organization revert to the State upon dissolution or State law does not permit the dissolution of such organization, and

(iv) the majority of the board of directors or oversight body of such organization are appointed by the chief executive officer or other executive branch official of the State, by the State legislature, or by both.

(28) The National Railroad Retirement Investment Trust established under section 15(j) of the Railroad Retirement Act of 1974.

(29) CO-OP HEALTH INSURANCE ISSUERS.—

(A) IN GENERAL.—A qualified nonprofit health insurance issuer (within the meaning of section 1322 of the Patient Protection and Affordable Care Act) which has received a loan or grant under the CO-OP program under such section, but only with respect to periods for which the issuer is in compliance with the requirements of such section and any agreement with respect to the loan or grant.

(B) CONDITIONS FOR EXEMPTION.—Subparagraph (A) shall apply to an organization only if—

(i) the organization has given notice to the Secretary, in such manner as the Secretary may by regulations prescribe, that it is applying for recognition of its status under this paragraph,

(ii) except as provided in section 1322(c)(4) of the Patient Protection and Affordable Care Act, no part of the net earnings of which inures to the benefit of any private shareholder or individual,

(iii) no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and

(iv) the organization does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

(d) RELIGIOUS AND APOSTOLIC ORGANIZATIONS.—The following organizations are referred to in subsection (a): Religious or apostolic associations or corporations, if such associations or corporations have a common treasury or community treasury, even if such associations or corporations engage in business for the common benefit of the members, but only if the members thereof include (at the time of filing their returns) in their gross income their entire pro rata shares, whether distributed or not, of the taxable income of the association or corporation for such year. Any amount so included in the gross income of a member shall be treated as a dividend received.

(e) COOPERATIVE HOSPITAL SERVICE ORGANIZATIONS.—For purposes of this title, an organization shall be treated as an organization organized and operated exclusively for charitable purposes, if—

(1) such organization is organized and operated solely—

(A) to perform, on a centralized basis, one or more of the following services which, if performed on its own behalf by a hospital which is an organization described in subsection (c)(3) and exempt from taxation under subsection (a),

would constitute activities in exercising or performing the purpose or function constituting the basis for its exemption: data processing, purchasing (including the purchasing of insurance on a group basis), warehousing, billing and collection (including the purchase of patron accounts receivable on a recourse basis), food, clinical, industrial engineering, laboratory, printing, communications, record center, and personnel (including selection, testing, training, and education of personnel) services; and

(B) to perform such services solely for two or more hospitals each of which is—

(i) an organization described in subsection (c)(3) which is exempt from taxation under subsection (a),

(ii) a constituent part of an organization described in subsection (c)(3) which is exempt from taxation under subsection (a) and which, if organized and operated as a separate entity, would constitute an organization described in subsection (c)(3), or

(iii) owned and operated by the United States, a State, the District of Columbia, or a possession of the United States, or a political subdivision or an agency or instrumentality of any of the foregoing;

(2) such organization is organized and operated on a cooperative basis and allocates or pays, within 8 1/2 months after the close of its taxable year, all net earnings to patrons on the basis of services performed for them; and

(3) if such organization has capital stock, all of such stock outstanding is owned by its patrons.

For purposes of this title, any organization which, by reason of the preceding sentence, is an organization described in subsection (c)(3) and exempt from taxation under subsection (a), shall be treated as a hospital and as an organization referred to in section 170(b)(1)(A)(iii).

(f) COOPERATIVE SERVICE ORGANIZATIONS OF OPERATING EDUCATIONAL ORGANIZATIONS.—For purposes of this title, if an organization is—

(1) organized and operated solely to hold, commingle, and collectively invest and reinvest (including arranging for and supervising the performance by independent contractors of investment services related thereto) in stocks and securities, the moneys contributed thereto by each of the members of such organization, and to collect income therefrom and turn over the entire amount thereof, less expenses, to such members,

(2) organized and controlled by one or more such members, and

(3) comprised solely of members that are organizations described in clause (ii) or (iv) of section 170(b)(1)(A)—

(A) which are exempt from taxation under subsection (a),

or

(B) the income of which is excluded from taxation under section 115,

then such organization shall be treated as an organization organized and operated exclusively for charitable purposes.

(g) DEFINITION OF AGRICULTURAL.—For purposes of subsection (c)(5), the term “agricultural” includes the art or science of culti-



vating land, harvesting crops or aquatic resources, or raising livestock.

(h) EXPENDITURES BY PUBLIC CHARITIES TO INFLUENCE LEGISLATION.—

(1) GENERAL RULE.—In the case of an organization to which this subsection applies, exemption from taxation under subsection (a) shall be denied because a substantial part of the activities of such organization consists of carrying on propaganda, or otherwise attempting, to influence legislation, but only if such organization normally—

(A) makes lobbying expenditures in excess of the lobbying ceiling amount for such organization for each taxable year, or

(B) makes grass roots expenditures in excess of the grass roots ceiling amount for such organization for each taxable year.

(2) DEFINITIONS.—For purposes of this subsection—

(A) LOBBYING EXPENDITURES.—The term “lobbying expenditures” means expenditures for the purpose of influencing legislation (as defined in section 4911(d)).

(B) LOBBYING CEILING AMOUNT.—The lobbying ceiling amount for any organization for any taxable year is 150 percent of the lobbying nontaxable amount for such organization for such taxable year, determined under section 4911.

(C) GRASS ROOTS EXPENDITURES.—The term “grass roots expenditures” means expenditures for the purpose of influencing legislation (as defined in section 4911(d) without regard to paragraph (1)(B) thereof).

(D) GRASS ROOTS CEILING AMOUNT.—The grass roots ceiling amount for any organization for any taxable year is 150 percent of the grass roots nontaxable amount for such organization for such taxable year, determined under section 4911.

(3) ORGANIZATIONS TO WHICH THIS SUBSECTION APPLIES.—This subsection shall apply to any organization which has elected (in such manner and at such time as the Secretary may prescribe) to have the provisions of this subsection apply to such organization and which, for the taxable year which includes the date the election is made, is described in subsection (c)(3) and—

(A) is described in paragraph (4), and

(B) is not a disqualified organization under paragraph (5).

(4) ORGANIZATIONS PERMITTED TO ELECT TO HAVE THIS SUBSECTION APPLY.—An organization is described in this paragraph if it is described in—

(A) section 170(b)(1)(A)(ii) (relating to educational institutions),

(B) section 170(b)(1)(A)(iii) (relating to hospitals and medical research organizations),

(C) section 170(b)(1)(A)(iv) (relating to organizations supporting government schools),

(D) section 170(b)(1)(A)(vi) (relating to organizations publicly supported by charitable contributions),

(E) section 170(b)(1)(A)(ix) (relating to agricultural research organizations),

(F) section 509(a)(2) (relating to organizations publicly supported by admissions, sales, etc.), or

(G) section 509(a)(3) (relating to organizations supporting certain types of public charities) except that for purposes of this subparagraph, section 509(a)(3) shall be applied without regard to the last sentence of section 509(a).

(5) DISQUALIFIED ORGANIZATIONS.—For purposes of paragraph (3) an organization is a disqualified organization if it is—

(A) described in section 170(b)(1)(A)(i) (relating to churches),

(B) an integrated auxiliary of a church or of a convention or association of churches, or

(C) a member of an affiliated group of organizations (within the meaning of section 4911(f)(2)) if one or more members of such group is described in subparagraph (A) or (B).

(6) YEARS FOR WHICH ELECTION IS EFFECTIVE.—An election by an organization under this subsection shall be effective for all taxable years of such organization which—

(A) end after the date the election is made, and

(B) begin before the date the election is revoked by such organization (under regulations prescribed by the Secretary).

(7) NO EFFECT ON CERTAIN ORGANIZATIONS.—With respect to any organization for a taxable year for which—

(A) such organization is a disqualified organization (within the meaning of paragraph (5)), or

(B) an election under this subsection is not in effect for such organization,

nothing in this subsection or in section 4911 shall be construed to affect the interpretation of the phrase, “no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation,” under subsection (c)(3).

(8) Affiliated organizations For rules regarding affiliated organizations, see section 4911(f).

(i) PROHIBITION OF DISCRIMINATION BY CERTAIN SOCIAL CLUBS.—Notwithstanding subsection (a), an organization which is described in subsection (c)(7) shall not be exempt from taxation under subsection (a) for any taxable year if, at any time during such taxable year, the charter, bylaws, or other governing instrument, of such organization or any written policy statement of such organization contains a provision which provides for discrimination against any person on the basis of race, color, or religion. The preceding sentence to the extent it relates to discrimination on the basis of religion shall not apply to—

(1) an auxiliary of a fraternal beneficiary society if such society—

(A) is described in subsection (c)(8) and exempt from tax under subsection (a), and

- (B) limits its membership to the members of a particular religion, or
- (2) a club which in good faith limits its membership to the members of a particular religion in order to further the teachings or principles of that religion, and not to exclude individuals of a particular race or color.
- (j) SPECIAL RULES FOR CERTAIN AMATEUR SPORTS ORGANIZATIONS.—
- (1) IN GENERAL.—In the case of a qualified amateur sports organization—
- (A) the requirement of subsection (c)(3) that no part of its activities involve the provision of athletic facilities or equipment shall not apply, and
- (B) such organization shall not fail to meet the requirements of subsection (c)(3) merely because its membership is local or regional in nature.
- (2) QUALIFIED AMATEUR SPORTS ORGANIZATION DEFINED.—For purposes of this subsection, the term “qualified amateur sports organization” means any organization organized and operated exclusively to foster national or international amateur sports competition if such organization is also organized and operated primarily to conduct national or international competition in sports or to support and develop amateur athletes for national or international competition in sports.
- (k) TREATMENT OF CERTAIN ORGANIZATIONS PROVIDING CHILD CARE.—For purposes of subsection (c)(3) of this section and sections 170(c)(2), 2055(a)(2), and 2522(a)(2), the term “educational purposes” includes the providing of care of children away from their homes if—
- (1) substantially all of the care provided by the organization is for purposes of enabling individuals to be gainfully employed, and
- (2) the services provided by the organization are available to the general public.
- (l) GOVERNMENT CORPORATIONS EXEMPT UNDER SUBSECTION (C)(1).—For purposes of subsection (c)(1), the following organizations are described in this subsection:
- (1) The Central Liquidity Facility established under title III of the Federal Credit Union Act (12 U.S.C. 1795 et seq.).
- (2) The Resolution Trust Corporation established under section 21A of the Federal Home Loan Bank Act.
- (3) The Resolution Funding Corporation established under section 21B of the Federal Home Loan Bank Act.
- (4) The Patient-Centered Outcomes Research Institute established under section 1181(b) of the Social Security Act.
- (m) CERTAIN ORGANIZATIONS PROVIDING COMMERCIAL-TYPE INSURANCE NOT EXEMPT FROM TAX.—
- (1) DENIAL OF TAX EXEMPTION WHERE PROVIDING COMMERCIAL-TYPE INSURANCE IS SUBSTANTIAL PART OF ACTIVITIES.—An organization described in paragraph (3) or (4) of subsection (c) shall be exempt from tax under subsection (a) only if no substantial part of its activities consists of providing commercial-type insurance.
- (2) OTHER ORGANIZATIONS TAXED AS INSURANCE COMPANIES ON INSURANCE BUSINESS.—In the case of an organization de-

scribed in paragraph (3) or (4) of subsection (c) which is exempt from tax under subsection (a) after the application of paragraph (1) of this subsection—

(A) the activity of providing commercial-type insurance shall be treated as an unrelated trade or business (as defined in section 513), and

(B) in lieu of the tax imposed by section 511 with respect to such activity, such organization shall be treated as an insurance company for purposes of applying subchapter L with respect to such activity.

(3) COMMERCIAL-TYPE INSURANCE.—For purposes of this subsection, the term “commercial-type insurance” shall not include—

(A) insurance provided at substantially below cost to a class of charitable recipients,

(B) incidental health insurance provided by a health maintenance organization of a kind customarily provided by such organizations,

(C) property or casualty insurance provided (directly or through an organization described in section 414(e)(3)(B)(ii)) by a church or convention or association of churches for such church or convention or association of churches,

(D) providing retirement or welfare benefits (or both) by a church or a convention or association of churches (directly or through an organization described in section 414(e)(3)(A) or 414(e)(3)(B)(ii)) for the employees (including employees described in section 414(e)(3)(B)) of such church or convention or association of churches or the beneficiaries of such employees, and

(E) charitable gift annuities.

(4) INSURANCE INCLUDES ANNUITIES.—For purposes of this subsection, the issuance of annuity contracts shall be treated as providing insurance.

(5) CHARITABLE GIFT ANNUITY.—For purposes of paragraph (3)(E), the term “charitable gift annuity” means an annuity if—

(A) a portion of the amount paid in connection with the issuance of the annuity is allowable as a deduction under section 170 or 2055, and

(B) the annuity is described in section 514(c)(5) (determined as if any amount paid in cash in connection with such issuance were property).

(n) CHARITABLE RISK POOLS.—

(1) IN GENERAL.—For purposes of this title—

(A) a qualified charitable risk pool shall be treated as an organization organized and operated exclusively for charitable purposes, and

(B) subsection (m) shall not apply to a qualified charitable risk pool.

(2) QUALIFIED CHARITABLE RISK POOL.—For purposes of this subsection, the term “qualified charitable risk pool” means any organization—

(A) which is organized and operated solely to pool insurable risks of its members (other than risks related to med-

ical malpractice) and to provide information to its members with respect to loss control and risk management,

(B) which is comprised solely of members that are organizations described in subsection (c)(3) and exempt from tax under subsection (a), and

(C) which meets the organizational requirements of paragraph (3).

(3) ORGANIZATIONAL REQUIREMENTS.—An organization (hereinafter in this subsection referred to as the “risk pool”) meets the organizational requirements of this paragraph if—

(A) such risk pool is organized as a nonprofit organization under State law provisions authorizing risk pooling arrangements for charitable organizations,

(B) such risk pool is exempt from any income tax imposed by the State (or will be so exempt after such pool qualifies as an organization exempt from tax under this title),

(C) such risk pool has obtained at least \$1,000,000 in startup capital from nonmember charitable organizations,

(D) such risk pool is controlled by a board of directors elected by its members, and

(E) the organizational documents of such risk pool require that—

(i) each member of such pool shall at all times be an organization described in subsection (c)(3) and exempt from tax under subsection (a),

(ii) any member which receives a final determination that it no longer qualifies as an organization described in subsection (c)(3) shall immediately notify the pool of such determination and the effective date of such determination, and

(iii) each policy of insurance issued by the risk pool shall provide that such policy will not cover the insured with respect to events occurring after the date such final determination was issued to the insured.

An organization shall not cease to qualify as a qualified charitable risk pool solely by reason of the failure of any of its members to continue to be an organization described in subsection (c)(3) if, within a reasonable period of time after such pool is notified as required under subparagraph (E)(ii), such pool takes such action as may be reasonably necessary to remove such member from such pool.

(4) OTHER DEFINITIONS.—For purposes of this subsection—

(A) STARTUP CAPITAL.—The term “startup capital” means any capital contributed to, and any program-related investments (within the meaning of section 4944(c)) made in, the risk pool before such pool commences operations.

(B) NONMEMBER CHARITABLE ORGANIZATION.—The term “nonmember charitable organization” means any organization which is described in subsection (c)(3) and exempt from tax under subsection (a) and which is not a member of the risk pool and does not benefit (directly or indirectly) from the insurance coverage provided by the pool to its members.

(o) **TREATMENT OF HOSPITALS PARTICIPATING IN PROVIDER-SPONSORED ORGANIZATIONS.**—An organization shall not fail to be treated as organized and operated exclusively for a charitable purpose for purposes of subsection (c)(3) solely because a hospital which is owned and operated by such organization participates in a provider-sponsored organization (as defined in section 1855(d) of the Social Security Act), whether or not the provider-sponsored organization is exempt from tax. For purposes of subsection (c)(3), any person with a material financial interest in such a provider-sponsored organization shall be treated as a private shareholder or individual with respect to the hospital.

(p) **SUSPENSION OF TAX-EXEMPT STATUS OF TERRORIST ORGANIZATIONS.**—

(1) **IN GENERAL.**—The exemption from tax under subsection (a) with respect to any organization described in paragraph (2), and the eligibility of any organization described in paragraph (2) to apply for recognition of exemption under subsection (a), shall be suspended during the period described in paragraph (3).

(2) **TERRORIST ORGANIZATIONS.**—An organization is described in this paragraph if such organization is designated or otherwise individually identified—

(A) under section 212(a)(3)(B)(vi)(II) or 219 of the Immigration and Nationality Act as a terrorist organization or foreign terrorist organization,

(B) in or pursuant to an Executive order which is related to terrorism and issued under the authority of the International Emergency Economic Powers Act or section 5 of the United Nations Participation Act of 1945 for the purpose of imposing on such organization an economic or other sanction, or

(C) in or pursuant to an Executive order issued under the authority of any Federal law if—

(i) the organization is designated or otherwise individually identified in or pursuant to such Executive order as supporting or engaging in terrorist activity (as defined in section 212(a)(3)(B) of the Immigration and Nationality Act) or supporting terrorism (as defined in section 140(d)(2) of the Foreign Relations Authorization Act, Fiscal Years 1988 and 1989); and

(ii) such Executive order refers to this subsection.

(3) **PERIOD OF SUSPENSION.**—With respect to any organization described in paragraph (2), the period of suspension—

(A) begins on the later of—

(i) the date of the first publication of a designation or identification described in paragraph (2) with respect to such organization, or

(ii) the date of the enactment of this subsection, and  
(B) ends on the first date that all designations and identifications described in paragraph (2) with respect to such organization are rescinded pursuant to the law or Executive order under which such designation or identification was made.

(4) **DENIAL OF DEDUCTION.**—No deduction shall be allowed under any provision of this title, including sections 170,

545(b)(2), 642(c), 2055, 2106(a)(2), and 2522, with respect to any contribution to an organization described in paragraph (2) during the period described in paragraph (3).

(5) DENIAL OF ADMINISTRATIVE OR JUDICIAL CHALLENGE OF SUSPENSION OR DENIAL OF DEDUCTION.—Notwithstanding section 7428 or any other provision of law, no organization or other person may challenge a suspension under paragraph (1), a designation or identification described in paragraph (2), the period of suspension described in paragraph (3), or a denial of a deduction under paragraph (4) in any administrative or judicial proceeding relating to the Federal tax liability of such organization or other person.

(6) ERRONEOUS DESIGNATION.—

(A) IN GENERAL.—If—

(i) the tax exemption of any organization described in paragraph (2) is suspended under paragraph (1),

(ii) each designation and identification described in paragraph (2) which has been made with respect to such organization is determined to be erroneous pursuant to the law or Executive order under which such designation or identification was made, and

(iii) the erroneous designations and identifications result in an overpayment of income tax for any taxable year by such organization,

credit or refund (with interest) with respect to such overpayment shall be made.

(B) WAIVER OF LIMITATIONS.—If the credit or refund of any overpayment of tax described in subparagraph (A)(iii) is prevented at any time by the operation of any law or rule of law (including *res judicata*), such credit or refund may nevertheless be allowed or made if the claim therefor is filed before the close of the 1-year period beginning on the date of the last determination described in subparagraph (A)(ii).

(7) NOTICE OF SUSPENSIONS.—If the tax exemption of any organization is suspended under this subsection, the Internal Revenue Service shall update the listings of tax-exempt organizations and shall publish appropriate notice to taxpayers of such suspension and of the fact that contributions to such organization are not deductible during the period of such suspension.

(q) SPECIAL RULES FOR CREDIT COUNSELING ORGANIZATIONS.—

(1) IN GENERAL.—An organization with respect to which the provision of credit counseling services is a substantial purpose shall not be exempt from tax under subsection (a) unless such organization is described in paragraph (3) or (4) of subsection (c) and such organization is organized and operated in accordance with the following requirements:

(A) The organization—

(i) provides credit counseling services tailored to the specific needs and circumstances of consumers,

(ii) makes no loans to debtors (other than loans with no fees or interest) and does not negotiate the making of loans on behalf of debtors,

(iii) provides services for the purpose of improving a consumer's credit record, credit history, or credit rating only to the extent that such services are incidental to providing credit counseling services, and

(iv) does not charge any separately stated fee for services for the purpose of improving any consumer's credit record, credit history, or credit rating.

(B) The organization does not refuse to provide credit counseling services to a consumer due to the inability of the consumer to pay, the ineligibility of the consumer for debt management plan enrollment, or the unwillingness of the consumer to enroll in a debt management plan.

(C) The organization establishes and implements a fee policy which—

(i) requires that any fees charged to a consumer for services are reasonable,

(ii) allows for the waiver of fees if the consumer is unable to pay, and

(iii) except to the extent allowed by State law, prohibits charging any fee based in whole or in part on a percentage of the consumer's debt, the consumer's payments to be made pursuant to a debt management plan, or the projected or actual savings to the consumer resulting from enrolling in a debt management plan.

(D) At all times the organization has a board of directors or other governing body—

(i) which is controlled by persons who represent the broad interests of the public, such as public officials acting in their capacities as such, persons having special knowledge or expertise in credit or financial education, and community leaders,

(ii) not more than 20 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities (other than through the receipt of reasonable directors' fees or the repayment of consumer debt to creditors other than the credit counseling organization or its affiliates), and

(iii) not more than 49 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities (other than through the receipt of reasonable directors' fees).

(E) The organization does not own more than 35 percent of—

(i) the total combined voting power of any corporation (other than a corporation which is an organization described in subsection (c)(3) and exempt from tax under subsection (a)) which is in the trade or business of lending money, repairing credit, or providing debt management plan services, payment processing, or similar services,



(ii) the profits interest of any partnership (other than a partnership which is an organization described in subsection (c)(3) and exempt from tax under subsection (a)) which is in the trade or business of lending money, repairing credit, or providing debt management plan services, payment processing, or similar services, and

(iii) the beneficial interest of any trust or estate (other than a trust which is an organization described in subsection (c)(3) and exempt from tax under subsection (a)) which is in the trade or business of lending money, repairing credit, or providing debt management plan services, payment processing, or similar services.

(F) The organization receives no amount for providing referrals to others for debt management plan services, and pays no amount to others for obtaining referrals of consumers.

(2) Additional requirements for organizations described in subsection (c)(3)

(A) IN GENERAL.—In addition to the requirements under paragraph (1), an organization with respect to which the provision of credit counseling services is a substantial purpose and which is described in paragraph (3) of subsection (c) shall not be exempt from tax under subsection (a) unless such organization is organized and operated in accordance with the following requirements:

(i) The organization does not solicit contributions from consumers during the initial counseling process or while the consumer is receiving services from the organization.

(ii) The aggregate revenues of the organization which are from payments of creditors of consumers of the organization and which are attributable to debt management plan services do not exceed the applicable percentage of the total revenues of the organization.

(B) APPLICABLE PERCENTAGE.—

(i) IN GENERAL.—For purposes of subparagraph (A)(ii), the applicable percentage is 50 percent.

(ii) TRANSITION RULE.—Notwithstanding clause (i), in the case of an organization with respect to which the provision of credit counseling services is a substantial purpose and which is described in paragraph (3) of subsection (c) and exempt from tax under subsection (a) on the date of the enactment of this subsection, the applicable percentage is—

(I) 80 percent for the first taxable year of such organization beginning after the date which is 1 year after the date of the enactment of this subsection, and

(II) 70 percent for the second such taxable year beginning after such date, and

(III) 60 percent for the third such taxable year beginning after such date.

(3) ADDITIONAL REQUIREMENT FOR ORGANIZATIONS DESCRIBED IN SUBSECTION (C)(4).—In addition to the requirements under paragraph (1), an organization with respect to which the provision of credit counseling services is a substantial purpose and which is described in paragraph (4) of subsection (c) shall not be exempt from tax under subsection (a) unless such organization notifies the Secretary, in such manner as the Secretary may by regulations prescribe, that it is applying for recognition as a credit counseling organization.

(4) CREDIT COUNSELING SERVICES; DEBT MANAGEMENT PLAN SERVICES.—For purposes of this subsection—

(A) CREDIT COUNSELING SERVICES.—The term “credit counseling services” means—

(i) the providing of educational information to the general public on budgeting, personal finance, financial literacy, saving and spending practices, and the sound use of consumer credit,

(ii) the assisting of individuals and families with financial problems by providing them with counseling, or

(iii) a combination of the activities described in clauses (i) and (ii).

(B) DEBT MANAGEMENT PLAN SERVICES.—The term “debt management plan services” means services related to the repayment, consolidation, or restructuring of a consumer’s debt, and includes the negotiation with creditors of lower interest rates, the waiver or reduction of fees, and the marketing and processing of debt management plans.

(r) ADDITIONAL REQUIREMENTS FOR CERTAIN HOSPITALS.—

(1) IN GENERAL.—A hospital organization to which this subsection applies shall not be treated as described in subsection (c)(3) unless the organization—

(A) meets the community health needs assessment requirements described in paragraph (3),

(B) meets the financial assistance policy requirements described in paragraph (4),

(C) meets the requirements on charges described in paragraph (5), and

(D) meets the billing and collection requirement described in paragraph (6).

(2) HOSPITAL ORGANIZATIONS TO WHICH SUBSECTION APPLIES.—

(A) IN GENERAL.—This subsection shall apply to—

(i) an organization which operates a facility which is required by a State to be licensed, registered, or similarly recognized as a hospital, and

(ii) any other organization which the Secretary determines has the provision of hospital care as its principal function or purpose constituting the basis for its exemption under subsection (c)(3) (determined without regard to this subsection).

(B) ORGANIZATIONS WITH MORE THAN 1 HOSPITAL FACILITY.—If a hospital organization operates more than 1 hospital facility—

(i) the organization shall meet the requirements of this subsection separately with respect to each such facility, and

(ii) the organization shall not be treated as described in subsection (c)(3) with respect to any such facility for which such requirements are not separately met.

(3) COMMUNITY HEALTH NEEDS ASSESSMENTS.—

(A) IN GENERAL.—An organization meets the requirements of this paragraph with respect to any taxable year only if the organization—

(i) has conducted a community health needs assessment which meets the requirements of subparagraph (B) in such taxable year or in either of the 2 taxable years immediately preceding such taxable year, and

(ii) has adopted an implementation strategy to meet the community health needs identified through such assessment.

(B) COMMUNITY HEALTH NEEDS ASSESSMENT.—A community health needs assessment meets the requirements of this paragraph if such community health needs assessment—

(i) takes into account input from persons who represent the broad interests of the community served by the hospital facility, including those with special knowledge of or expertise in public health, and

(ii) is made widely available to the public.

(4) FINANCIAL ASSISTANCE POLICY.—An organization meets the requirements of this paragraph if the organization establishes the following policies:

(A) FINANCIAL ASSISTANCE POLICY.—A written financial assistance policy which includes—

(i) eligibility criteria for financial assistance, and whether such assistance includes free or discounted care,

(ii) the basis for calculating amounts charged to patients,

(iii) the method for applying for financial assistance,

(iv) in the case of an organization which does not have a separate billing and collections policy, the actions the organization may take in the event of non-payment, including collections action and reporting to credit agencies, and

(v) measures to widely publicize the policy within the community to be served by the organization.

(B) POLICY RELATING TO EMERGENCY MEDICAL CARE.—A written policy requiring the organization to provide, without discrimination, care for emergency medical conditions (within the meaning of section 1867 of the Social Security Act (42 U.S.C. 1395dd)) to individuals regardless of their eligibility under the financial assistance policy described in subparagraph (A).

(5) LIMITATION ON CHARGES.—An organization meets the requirements of this paragraph if the organization—

(A) limits amounts charged for emergency or other medically necessary care provided to individuals eligible for assistance under the financial assistance policy described in paragraph (4)(A) to not more than the amounts generally billed to individuals who have insurance covering such care, and

(B) prohibits the use of gross charges.

(6) BILLING AND COLLECTION REQUIREMENTS.—An organization meets the requirement of this paragraph only if the organization does not engage in extraordinary collection actions before the organization has made reasonable efforts to determine whether the individual is eligible for assistance under the financial assistance policy described in paragraph (4)(A).

(7) REGULATORY AUTHORITY.—The Secretary shall issue such regulations and guidance as may be necessary to carry out the provisions of this subsection, including guidance relating to what constitutes reasonable efforts to determine the eligibility of a patient under a financial assistance policy for purposes of paragraph (6).

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**PART VIII—CERTAIN SAVINGS ENTITIES**

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**SEC. 529. QUALIFIED TUITION PROGRAMS.**

(a) GENERAL RULE.—A qualified tuition program shall be exempt from taxation under this subtitle. Notwithstanding the preceding sentence, such program shall be subject to the taxes imposed by section 511 (relating to imposition of tax on unrelated business income of charitable organizations).

(b) QUALIFIED TUITION PROGRAM.—For purposes of this section—

(1) IN GENERAL.—The term “qualified tuition program” means a program established and maintained by a State or agency or instrumentality thereof or by 1 or more eligible educational institutions—

(A) under which a person—

(i) may purchase tuition credits or certificates on behalf of a designated beneficiary which entitle the beneficiary to the waiver or payment of qualified higher education expenses of the beneficiary, or

(ii) in the case of a program established and maintained by a State or agency or instrumentality thereof, may make contributions to an account which is established for the purpose of meeting the qualified higher education expenses of the designated beneficiary of the account, and

(B) which meets the other requirements of this subsection.

Except to the extent provided in regulations, a program established and maintained by 1 or more eligible educational institutions shall not be treated as a qualified tuition program unless such program provides that amounts are held in a qualified trust and such program has received a ruling or determination that such program meets the applicable requirements for a qualified tuition program. For purposes of the preceding

sentence, the term “qualified trust” means a trust which is created or organized in the United States for the exclusive benefit of designated beneficiaries and with respect to which the requirements of paragraphs (2) and (5) of section 408(a) are met.

(2) CASH CONTRIBUTIONS.—A program shall not be treated as a qualified tuition program unless it provides that purchases or contributions may only be made in cash.

(3) SEPARATE ACCOUNTING.—A program shall not be treated as a qualified tuition program unless it provides separate accounting for each designated beneficiary.

(4) LIMITED INVESTMENT DIRECTION.—A program shall not be treated as a qualified tuition program unless it provides that any contributor to, or designated beneficiary under, such program may, directly or indirectly, direct the investment of any contributions to the program (or any earnings thereon) no more than 2 times in any calendar year.

(5) NO PLEDGING OF INTEREST AS SECURITY.—A program shall not be treated as a qualified tuition program if it allows any interest in the program or any portion thereof to be used as security for a loan.

(6) PROHIBITION ON EXCESS CONTRIBUTIONS.—A program shall not be treated as a qualified tuition program unless it provides adequate safeguards to prevent contributions on behalf of a designated beneficiary in excess of those necessary to provide for the qualified higher education expenses of the beneficiary.

(c) TAX TREATMENT OF DESIGNATED BENEFICIARIES AND CONTRIBUTORS.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, no amount shall be includible in gross income of—

(A) a designated beneficiary under a qualified tuition program, or

(B) a contributor to such program on behalf of a designated beneficiary, with respect to any distribution or earnings under such program.

(2) GIFT TAX TREATMENT OF CONTRIBUTIONS.—For purposes of chapters 12 and 13—

(A) IN GENERAL.—Any contribution to a qualified tuition program on behalf of any designated beneficiary—

(i) shall be treated as a completed gift to such beneficiary which is not a future interest in property, and

(ii) shall not be treated as a qualified transfer under section 2503(e).

(B) TREATMENT OF EXCESS CONTRIBUTIONS.—If the aggregate amount of contributions described in subparagraph (A) during the calendar year by a donor exceeds the limitation for such year under section 2503(b), such aggregate amount shall, at the election of the donor, be taken into account for purposes of such section ratably over the 5-year period beginning with such calendar year.

(3) DISTRIBUTIONS.—

(A) IN GENERAL.—Any distribution under a qualified tuition program shall be includible in the gross income of the distributee in the manner as provided under section 72 to

the extent not excluded from gross income under any other provision of this chapter.

(B) DISTRIBUTIONS FOR QUALIFIED HIGHER EDUCATION EXPENSES.—For purposes of this paragraph—

(i) IN-KIND DISTRIBUTIONS.—No amount shall be includible in gross income under subparagraph (A) by reason of a distribution which consists of providing a benefit to the distributee which, if paid for by the distributee, would constitute payment of a qualified higher education expense.

(ii) CASH DISTRIBUTIONS.—In the case of distributions not described in clause (i), if—

(I) such distributions do not exceed the qualified higher education expenses (reduced by expenses described in clause (i)), no amount shall be includible in gross income, and

(II) in any other case, the amount otherwise includible in gross income shall be reduced by an amount which bears the same ratio to such amount as such expenses bear to such distributions.

(iii) EXCEPTION FOR INSTITUTIONAL PROGRAMS.—In the case of any taxable year beginning before January 1, 2004, clauses (i) and (ii) shall not apply with respect to any distribution during such taxable year under a qualified tuition program established and maintained by 1 or more eligible educational institutions.

(iv) TREATMENT AS DISTRIBUTIONS.—Any benefit furnished to a designated beneficiary under a qualified tuition program shall be treated as a distribution to the beneficiary for purposes of this paragraph.

(v) COORDINATION WITH AMERICAN OPPORTUNITY AND LIFETIME LEARNING CREDITS.—The total amount of qualified higher education expenses with respect to an individual for the taxable year shall be reduced—

(I) as provided in section 25A(g)(2), and

(II) by the amount of such expenses which were taken into account in determining the credit allowed to the taxpayer or any other person under section 25A.

(vi) COORDINATION WITH COVERDELL EDUCATION SAVINGS ACCOUNTS.—If, with respect to an individual for any taxable year—

(I) the aggregate distributions to which clauses (i) and (ii) and section 530(d)(2)(A) apply, exceed

(II) the total amount of qualified higher education expenses otherwise taken into account under clauses (i) and (ii) (after the application of clause (v)) for such year,

the taxpayer shall allocate such expenses among such distributions for purposes of determining the amount of the exclusion under clauses (i) and (ii) and section 530(d)(2)(A).

(C) CHANGE IN BENEFICIARIES OR PROGRAMS.—

(i) ROLLOVERS.—Subparagraph (A) shall not apply to that portion of any distribution which, within 60 days of such distribution, is transferred—

(I) to another qualified tuition program for the benefit of the designated beneficiary,

(II) to the credit of another designated beneficiary under a qualified tuition program who is a member of the family of the designated beneficiary with respect to which the distribution was made, or

(III) **【before January 1, 2026,】** to an ABLE account (as defined in section 529A(e)(6)) of the designated beneficiary or a member of the family of the designated beneficiary.

Subclause (III) shall not apply to so much of a distribution which, when added to all other contributions made to the ABLE account for the taxable year, exceeds the limitation under section 529A(b)(2)(B)(i).

(ii) CHANGE IN DESIGNATED BENEFICIARIES.—Any change in the designated beneficiary of an interest in a qualified tuition program shall not be treated as a distribution for purposes of subparagraph (A) if the new beneficiary is a member of the family of the old beneficiary.

(iii) LIMITATION ON CERTAIN ROLLOVERS.—Clause (i)(I) shall not apply to any transfer if such transfer occurs within 12 months from the date of a previous transfer to any qualified tuition program for the benefit of the designated beneficiary.

(D) SPECIAL RULE FOR CONTRIBUTIONS OF REFUNDED AMOUNTS.—In the case of a beneficiary who receives a refund of any qualified higher education expenses from an eligible educational institution, subparagraph (A) shall not apply to that portion of any distribution for the taxable year which is recontributed to a qualified tuition program of which such individual is a beneficiary, but only to the extent such recontribution is made not later than 60 days after the date of such refund and does not exceed the refunded amount.

(4) ESTATE TAX TREATMENT.—

(A) IN GENERAL.—No amount shall be includible in the gross estate of any individual for purposes of chapter 11 by reason of an interest in a qualified tuition program.

(B) AMOUNTS INCLUDIBLE IN ESTATE OF DESIGNATED BENEFICIARY IN CERTAIN CASES.—Subparagraph (A) shall not apply to amounts distributed on account of the death of a beneficiary.

(C) AMOUNTS INCLUDIBLE IN ESTATE OF DONOR MAKING EXCESS CONTRIBUTIONS.—In the case of a donor who makes the election described in paragraph (2)(B) and who dies before the close of the 5-year period referred to in such paragraph, notwithstanding subparagraph (A), the gross estate of the donor shall include the portion of such contributions properly allocable to periods after the date of death of the donor.

(5) OTHER GIFT TAX RULES.—For purposes of chapters 12 and 13—

(A) TREATMENT OF DISTRIBUTIONS.—Except as provided in subparagraph (B), in no event shall a distribution from a qualified tuition program be treated as a taxable gift.

(B) TREATMENT OF DESIGNATION OF NEW BENEFICIARY.—The taxes imposed by chapters 12 and 13 shall apply to a transfer by reason of a change in the designated beneficiary under the program (or a rollover to the account of a new beneficiary) unless the new beneficiary is—

(i) assigned to the same generation as (or a higher generation than) the old beneficiary (determined in accordance with section 2651), and

(ii) a member of the family of the old beneficiary.

(6) ADDITIONAL TAX.—The tax imposed by section 530(d)(4) shall apply to any payment or distribution from a qualified tuition program in the same manner as such tax applies to a payment or distribution from a Coverdell education savings account. This paragraph shall not apply to any payment or distribution in any taxable year beginning before January 1, 2004, which is includible in gross income but used for qualified higher education expenses of the designated beneficiary.

(7) TREATMENT OF ELEMENTARY AND SECONDARY TUITION.—Any reference in this subsection to the term “qualified higher education expense” shall include a reference to expenses for tuition in connection with enrollment or attendance at an elementary or secondary public, private, or religious school.

(d) REPORTS.—Each officer or employee having control of the qualified tuition program or their designee shall make such reports regarding such program to the Secretary and to designated beneficiaries with respect to contributions, distributions, and such other matters as the Secretary may require. The reports required by this subsection shall be filed at such time and in such manner and furnished to such individuals at such time and in such manner as may be required by the Secretary.

(e) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) DESIGNATED BENEFICIARY.—The term “designated beneficiary” means—

(A) the individual designated at the commencement of participation in the qualified tuition program as the beneficiary of amounts paid (or to be paid) to the program,

(B) in the case of a change in beneficiaries described in subsection (c)(3)(C), the individual who is the new beneficiary, and

(C) in the case of an interest in a qualified tuition program purchased by a State or local government (or agency or instrumentality thereof) or an organization described in section 501(c)(3) and exempt from taxation under section 501(a) as part of a scholarship program operated by such government or organization, the individual receiving such interest as a scholarship.

(2) MEMBER OF FAMILY.—The term “member of the family” means, with respect to any designated beneficiary—

(A) the spouse of such beneficiary;



- (B) an individual who bears a relationship to such beneficiary which is described in subparagraphs (A) through (G) of ~~section 152(d)(2)~~ *section 7706(d)(2)*;
- (C) the spouse of any individual described in subparagraph (B); and
- (D) any first cousin of such beneficiary.

(3) QUALIFIED HIGHER EDUCATION EXPENSES.—

(A) IN GENERAL.—The term “qualified higher education expenses” means—

(i) tuition, fees, books, supplies, and equipment required for the enrollment or attendance of a designated beneficiary at an eligible educational institution,

(ii) expenses for special needs services in the case of a special needs beneficiary which are incurred in connection with such enrollment or attendance, and

(iii) expenses for the purchase of computer or peripheral equipment (as defined in section 168(i)(2)(B)), computer software (as defined in section 197(e)(3)(B)), or Internet access and related services, if such equipment, software, or services are to be used primarily by the beneficiary during any of the years the beneficiary is enrolled at an eligible educational institution.

Clause (iii) shall not include expenses for computer software designed for sports, games, or hobbies unless the software is predominantly educational in nature. The amount of cash distributions from all qualified tuition programs described in subsection (b)(1)(A)(ii) with respect to a beneficiary during any taxable year shall, in the aggregate, include not more than \$10,000 in expenses described in subsection (c)(7) incurred during the taxable year.

(B) ROOM AND BOARD INCLUDED FOR STUDENTS WHO ARE AT LEAST HALF-TIME.—

(i) IN GENERAL.—In the case of an individual who is an eligible student (as defined in section 25A(b)(3)) for any academic period, such term shall also include reasonable costs for such period (as determined under the qualified tuition program) incurred by the designated beneficiary for room and board while attending such institution. For purposes of subsection (b)(6), a designated beneficiary shall be treated as meeting the requirements of this clause.

(ii) LIMITATION.—The amount treated as qualified higher education expenses by reason of clause (i) shall not exceed—

(I) the allowance (applicable to the student) for room and board included in the cost of attendance (as defined in section 472 of the Higher Education Act of 1965 (20 U.S.C. 1087ll), as in effect on the date of the enactment of the Economic Growth and Tax Relief Reconciliation Act of 2001) as determined by the eligible educational institution for such period, or

(II) if greater, the actual invoice amount the student residing in housing owned or operated by

the eligible educational institution is charged by such institution for room and board costs for such period.

(4) APPLICATION OF SECTION 514.—An interest in a qualified tuition program shall not be treated as debt for purposes of section 514.

(5) ELIGIBLE EDUCATIONAL INSTITUTION.—The term “eligible educational institution” means an institution—

(A) which is described in section 481 of the Higher Education Act of 1965 (20 U.S.C. 1088), as in effect on the date of the enactment of this paragraph, and

(B) which is eligible to participate in a program under title IV of such Act.

(f) REGULATIONS.—Notwithstanding any other provision of this section, the Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section and to prevent abuse of such purposes, including regulations under chapters 11, 12, and 13 of this title.

**SEC. 529A. QUALIFIED ABLE PROGRAMS.**

(a) GENERAL RULE.—A qualified ABLE program shall be exempt from taxation under this subtitle. Notwithstanding the preceding sentence, such program shall be subject to the taxes imposed by section 511 (relating to imposition of tax on unrelated business income of charitable organizations).

(b) QUALIFIED ABLE PROGRAM.—For purposes of this section—

(1) IN GENERAL.—The term “qualified ABLE program” means a program established and maintained by a State, or agency or instrumentality thereof—

(A) under which a person may make contributions for a taxable year, for the benefit of an individual who is an eligible individual for such taxable year, to an ABLE account which is established for the purpose of meeting the qualified disability expenses of the designated beneficiary of the account,

(B) which limits a designated beneficiary to 1 ABLE account for purposes of this section, and

(C) which meets the other requirements of this section.

(2) CASH CONTRIBUTIONS.—A program shall not be treated as a qualified ABLE program unless it provides that no contribution will be accepted—

(A) unless it is in cash, or

(B) except in the case of contributions under subsection (c)(1)(C), if such contribution to an ABLE account would result in aggregate contributions from all contributors to the ABLE account for the taxable year exceeding the sum of—

(i) the amount in effect under section 2503(b) for the calendar year in which the taxable year begins, plus

(ii) in the case of any contribution by a designated beneficiary described in paragraph (7) [before January 1, 2026], the lesser of—

(I) compensation (as defined by section 219(f)(1)) includible in the designated beneficiary’s gross income for the taxable year, or

(II) an amount equal to the poverty line for a one-person household, as determined for the calendar year preceding the calendar year in which the taxable year begins.

For purposes of this paragraph, rules similar to the rules of section 408(d)(4) (determined without regard to subparagraph (B) thereof) shall apply. A designated beneficiary (or a person acting on behalf of such beneficiary) shall maintain adequate records for purposes of ensuring, and shall be responsible for ensuring, that the requirements of subparagraph (B)(ii) are met.

(3) SEPARATE ACCOUNTING.—A program shall not be treated as a qualified ABLE program unless it provides separate accounting for each designated beneficiary.

(4) LIMITED INVESTMENT DIRECTION.—A program shall not be treated as a qualified ABLE program unless it provides that any designated beneficiary under such program may, directly or indirectly, direct the investment of any contributions to the program (or any earnings thereon) no more than 2 times in any calendar year.

(5) NO PLEDGING OF INTEREST AS SECURITY.—A program shall not be treated as a qualified ABLE program if it allows any interest in the program or any portion thereof to be used as security for a loan.

(6) PROHIBITION ON EXCESS CONTRIBUTIONS.—A program shall not be treated as a qualified ABLE program unless it provides adequate safeguards to prevent aggregate contributions on behalf of a designated beneficiary in excess of the limit established by the State under section 529(b)(6). For purposes of the preceding sentence, aggregate contributions include contributions under any prior qualified ABLE program of any State or agency or instrumentality thereof.

(7) SPECIAL RULES RELATED TO CONTRIBUTION LIMIT.—For purposes of paragraph (2)(B)(ii)—

(A) DESIGNATED BENEFICIARY.—A designated beneficiary described in this paragraph is an employee (including an employee within the meaning of section 401(c)) with respect to whom—

(i) no contribution is made for the taxable year to a defined contribution plan (within the meaning of section 414(i)) with respect to which the requirements of section 401(a) or 403(a) are met,

(ii) no contribution is made for the taxable year to an annuity contract described in section 403(b), and

(iii) no contribution is made for the taxable year to an eligible deferred compensation plan described in section 457(b).

(B) POVERTY LINE.—The term “poverty line” has the meaning given such term by section 673 of the Community Services Block Grant Act (42 U.S.C. 9902).

(c) TAX TREATMENT.—

(1) DISTRIBUTIONS.—

(A) IN GENERAL.—Any distribution under a qualified ABLE program shall be includible in the gross income of the distributee in the manner as provided under section 72

to the extent not excluded from gross income under any other provision of this chapter.

(B) DISTRIBUTIONS FOR QUALIFIED DISABILITY EXPENSES.—For purposes of this paragraph, if distributions from a qualified ABLE program—

(i) do not exceed the qualified disability expenses of the designated beneficiary, no amount shall be includible in gross income, and

(ii) in any other case, the amount otherwise includible in gross income shall be reduced by an amount which bears the same ratio to such amount as such expenses bear to such distributions.

(C) CHANGE IN DESIGNATED BENEFICIARIES OR PROGRAMS.—

(i) ROLLOVERS FROM ABLE ACCOUNTS.—Subparagraph (A) shall not apply to any amount paid or distributed from an ABLE account to the extent that the amount received is paid, not later than the 60th day after the date of such payment or distribution, into another ABLE account for the benefit of the same designated beneficiary or an eligible individual who is a member of the family of the designated beneficiary.

(ii) CHANGE IN DESIGNATED BENEFICIARIES.—Any change in the designated beneficiary of an interest in a qualified ABLE program during a taxable year shall not be treated as a distribution for purposes of subparagraph (A) if the new beneficiary is an eligible individual for such taxable year and a member of the family of the former beneficiary.

(iii) LIMITATION ON CERTAIN ROLLOVERS.—Clause (i) shall not apply to any transfer if such transfer occurs within 12 months from the date of a previous transfer to any qualified ABLE program for the benefit of the designated beneficiary.

(2) GIFT TAX RULES.—For purposes of chapters 12 and 13—

(A) CONTRIBUTIONS.—Any contribution to a qualified ABLE program on behalf of any designated beneficiary—

(i) shall be treated as a completed gift to such designated beneficiary which is not a future interest in property, and

(ii) shall not be treated as a qualified transfer under section 2503(e).

(B) TREATMENT OF DISTRIBUTIONS.—In no event shall a distribution from an ABLE account to such account's designated beneficiary be treated as a taxable gift.

(C) TREATMENT OF TRANSFER TO NEW DESIGNATED BENEFICIARY.—The taxes imposed by chapters 12 and 13 shall not apply to a transfer by reason of a change in the designated beneficiary under subsection (c)(1)(C).

(3) ADDITIONAL TAX FOR DISTRIBUTIONS NOT USED FOR DISABILITY EXPENSES.—

(A) IN GENERAL.—The tax imposed by this chapter for any taxable year on any taxpayer who receives a distribution from a qualified ABLE program which is includible in

gross income shall be increased by 10 percent of the amount which is so includible.

(B) EXCEPTION.—Subparagraph (A) shall not apply if the payment or distribution is made to a beneficiary (or to the estate of the designated beneficiary) on or after the death of the designated beneficiary.

(C) CONTRIBUTIONS RETURNED BEFORE CERTAIN DATE.—Subparagraph (A) shall not apply to the distribution of any contribution made during a taxable year on behalf of the designated beneficiary if—

(i) such distribution is received on or before the day prescribed by law (including extensions of time) for filing such designated beneficiary's return for such taxable year, and

(ii) such distribution is accompanied by the amount of net income attributable to such excess contribution.

Any net income described in clause (ii) shall be included in gross income for the taxable year in which such excess contribution was made.

(4) LOSS OF ABLE ACCOUNT TREATMENT.—If an ABLE account is established for a designated beneficiary, no account subsequently established for such beneficiary shall be treated as an ABLE account. The preceding sentence shall not apply in the case of an account established for purposes of a rollover described in paragraph (1)(C)(i) of this section if the transferor account is closed as of the end of the 60th day referred to in paragraph (1)(C)(i).

(d) REPORTS.—

(1) IN GENERAL.—Each officer or employee having control of the qualified ABLE program or their designee shall make such reports regarding such program to the Secretary and to designated beneficiaries with respect to contributions, distributions, the return of excess contributions, and such other matters as the Secretary may require.

(2) CERTAIN AGGREGATED INFORMATION.—For research purposes, the Secretary shall make available to the public reports containing aggregate information, by diagnosis and other relevant characteristics, on contributions and distributions from the qualified ABLE program. In carrying out the preceding sentence an item may not be made available to the public if such item can be associated with, or otherwise identify, directly or indirectly, a particular individual.

(3) NOTICE OF ESTABLISHMENT OF ABLE ACCOUNT.—A qualified ABLE program shall submit a notice to the Secretary upon the establishment of an ABLE account. Such notice shall contain the name of the designated beneficiary and such other information as the Secretary may require.

(4) ELECTRONIC DISTRIBUTION STATEMENTS.—For purposes of section 103 of the Stephen Beck, Jr., ABLE Act of 2014, States shall submit electronically on a monthly basis to the Commissioner of Social Security, in the manner specified by the Commissioner, statements on relevant distributions and account balances from all ABLE accounts.

(5) REQUIREMENTS.—The reports and notices required by paragraphs (1), (2), and (3) shall be filed at such time and in

such manner and furnished to such individuals at such time and in such manner as may be required by the Secretary.

(e) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

(1) ELIGIBLE INDIVIDUAL.—An individual is an eligible individual for a taxable year if during such taxable year—

(A) the individual is entitled to benefits based on blindness or disability under title II or XVI of the Social Security Act, and such blindness or disability occurred before the date on which the individual attained age 26, or

(B) a disability certification with respect to such individual is filed with the Secretary for such taxable year.

(2) DISABILITY CERTIFICATION.—

(A) IN GENERAL.—The term “disability certification” means, with respect to an individual, a certification to the satisfaction of the Secretary by the individual or the parent or guardian of the individual that—

(i) certifies that—

(I) the individual has a medically determinable physical or mental impairment, which results in marked and severe functional limitations, and which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months, or is blind (within the meaning of section 1614(a)(2) of the Social Security Act), and

(II) such blindness or disability occurred before the date on which the individual attained age 26, and

(ii) includes a copy of the individual’s diagnosis relating to the individual’s relevant impairment or impairments, signed by a physician meeting the criteria of section 1861(r)(1) of the Social Security Act.

(B) RESTRICTION ON USE OF CERTIFICATION.—No inference may be drawn from a disability certification for purposes of establishing eligibility for benefits under title II, XVI, or XIX of the Social Security Act.

(3) DESIGNATED BENEFICIARY.—The term “designated beneficiary” in connection with an ABLE account established under a qualified ABLE program means the eligible individual who established an ABLE account and is the owner of such account.

(4) MEMBER OF FAMILY.—The term “member of the family” means, with respect to any designated beneficiary, an individual who bears a relationship to such beneficiary which is described in **[section 152(d)(2)(B)]** *section 7706(d)(2)(B)*. For purposes of the preceding sentence, a rule similar to the rule of **[section 152(f)(1)(B)]** *section 7706(f)(1)(B)* shall apply.

(5) QUALIFIED DISABILITY EXPENSES.—The term “qualified disability expenses” means any expenses related to the eligible individual’s blindness or disability which are made for the benefit of an eligible individual who is the designated beneficiary, including the following expenses: education, housing, transportation, employment training and support, assistive technology and personal support services, health, prevention and wellness, financial management and administrative services, legal fees,

expenses for oversight and monitoring, funeral and burial expenses, and other expenses, which are approved by the Secretary under regulations and consistent with the purposes of this section.

(6) **ABLE ACCOUNT.**—The term “ABLE account” means an account established by an eligible individual, owned by such eligible individual, and maintained under a qualified ABLE program.

(f) **TRANSFER TO STATE.**—Subject to any outstanding payments due for qualified disability expenses, upon the death of the designated beneficiary, all amounts remaining in the qualified ABLE account not in excess of the amount equal to the total medical assistance paid for the designated beneficiary after the establishment of the account, net of any premiums paid from the account or paid by or on behalf of the beneficiary to a Medicaid Buy-In program under any State Medicaid plan established under title XIX of the Social Security Act, shall be distributed to such State upon filing of a claim for payment by such State. For purposes of this paragraph, the State shall be a creditor of an ABLE account and not a beneficiary. Subsection (c)(3) shall not apply to a distribution under the preceding sentence.

(g) **REGULATIONS.**—The Secretary shall prescribe such regulations or other guidance as the Secretary determines necessary or appropriate to carry out the purposes of this section, including regulations—

- (1) to enforce the 1 ABLE account per eligible individual limit,
- (2) providing for the information required to be presented to open an ABLE account,
- (3) to generally define qualified disability expenses,
- (4) developed in consultation with the Commissioner of Social Security, relating to disability certifications and determinations of disability, including those conditions deemed to meet the requirements of subsection (e)(1)(B),
- (5) to prevent fraud and abuse with respect to amounts claimed as qualified disability expenses,
- (6) under chapters 11, 12, and 13 of this title, and
- (7) to allow for transfers from one ABLE account to another ABLE account.

**Subchapter J—Estates, Trusts, Beneficiaries, and Decedents**

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**PART I—ESTATES, TRUSTS, AND BENEFICIARIES**

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**Subpart A—General Rules for Taxation of Estates and Trusts**

\* \* \* \* \*

**SEC. 641. IMPOSITION OF TAX.**

(a) **APPLICATION OF TAX.**—The tax imposed by section 1(e) shall apply to the taxable income of estates or of any kind of property held in trust, including—

(1) income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) **COMPUTATION AND PAYMENT.**—The taxable income of an estate or trust shall be computed in the same manner as in the case of an individual, except as otherwise provided in this part. The tax shall be computed on such taxable income and shall be paid by the fiduciary. For purposes of this subsection, a foreign trust or foreign estate shall be treated as a nonresident alien individual who is not present in the United States at any time.

(c) **SPECIAL RULES FOR TAXATION OF ELECTING SMALL BUSINESS TRUSTS.**—

(1) **IN GENERAL.**—For purposes of this chapter—

(A) the portion of any electing small business trust which consists of stock in 1 or more S corporations shall be treated as a separate trust, and

(B) the amount of the tax imposed by this chapter on such separate trust shall be determined with the modifications of paragraph (2).

(2) **MODIFICATIONS.**—For purposes of paragraph (1), the modifications of this paragraph are the following:

(A) Except as provided in section 1(h), the amount of the tax imposed by section 1(e) shall be determined by using the highest rate of tax set forth in section 1(e).

(B) The exemption amount under section 55(d) shall be zero.

(C) The only items of income, loss, deduction, or credit to be taken into account are the following:

(i) The items required to be taken into account under section 1366.

(ii) Any gain or loss from the disposition of stock in an S corporation.

(iii) To the extent provided in regulations, State or local income taxes or administrative expenses to the extent allocable to items described in clauses (i) and (ii).

(iv) Any interest expense paid or accrued on indebtedness incurred to acquire stock in an S corporation. No deduction or credit shall be allowed for any amount not described in this paragraph, and no item described in this paragraph shall be apportioned to any beneficiary.



(D) No amount shall be allowed under paragraph (1) or (2) of section 1211(b).

[(E)(i) Section 642(c) shall not apply.]

[(ii) For purposes of section 170(b)(1)(G), adjusted gross income shall be computed in the same manner as in the case of an individual, except that the deductions for costs which are paid or incurred in connection with the administration of the trust and which would not have been incurred if the property were not held in such trust shall be treated as allowable in arriving at adjusted gross income.]

*(E) Section 642(c) shall not apply.*

(3) TREATMENT OF REMAINDER OF TRUST AND DISTRIBUTIONS.—For purposes of determining—

(A) the amount of the tax imposed by this chapter on the portion of any electing small business trust not treated as a separate trust under paragraph (1), and

(B) the distributable net income of the entire trust, the items referred to in paragraph (2)(C) shall be excluded. Except as provided in the preceding sentence, this subsection shall not affect the taxation of any distribution from the trust.

(4) TREATMENT OF UNUSED DEDUCTIONS WHERE TERMINATION OF SEPARATE TRUST.—If a portion of an electing small business trust ceases to be treated as a separate trust under paragraph (1), any carryover or excess deduction of the separate trust which is referred to in section 642(h) shall be taken into account by the entire trust.

(5) ELECTING SMALL BUSINESS TRUST.—For purposes of this subsection, the term “electing small business trust” has the meaning given such term by section 1361(e)(1).

*(d) COMPUTATION OF ADJUSTED GROSS INCOME.—For purposes of this title, the adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual, except that—*

*(1) the deductions for costs which are paid or incurred in connection with the administration of the estate or trust and which would not have been incurred if the property were not held in such trust or estate, and*

*(2) the deductions allowable under sections 642(b), 651, and 661,*

*shall be treated as allowable in arriving at adjusted gross income.*

#### **SEC. 642. SPECIAL RULES FOR CREDITS AND DEDUCTIONS.**

(a) FOREIGN TAX CREDIT ALLOWED.—An estate or trust shall be allowed the credit against tax for taxes imposed by foreign countries and possessions of the United States, to the extent allowed by section 901, only in respect of so much of the taxes described in such section as is not properly allocable under such section to the beneficiaries.

(b) [DEDUCTION FOR PERSONAL EXEMPTION] *BASIC DEDUCTION.*—

(1) ESTATES.—An estate shall be allowed a deduction of \$600.

(2) TRUSTS.—

(A) IN GENERAL.—Except as otherwise provided in this paragraph, a trust shall be allowed a deduction of \$100.

(B) TRUSTS DISTRIBUTING INCOME CURRENTLY.—A trust which, under its governing instrument, is required to distribute all of its income currently shall be allowed a deduction of \$300.

(C) DISABILITY TRUSTS.—

(i) IN GENERAL.—A qualified disability trust shall be allowed a deduction equal to **the exemption amount under section 151(d), determined—** *the dollar amount in effect under section 7706(d)(1)(B).*

**[(I) by treating such trust as an individual described in section**

**[(II) by applying section 67(e) (without the reference to section 642(b)) for purposes of determining the adjusted gross income of the trust.]**

(ii) QUALIFIED DISABILITY TRUST.—For purposes of clause (i), the term “qualified disability trust” means any trust if—

(I) such trust is a disability trust described in subsection (c)(2)(B)(iv) of section 1917 of the Social Security Act (42 U.S.C. 1396p), and

(II) all of the beneficiaries of the trust as of the close of the taxable year are determined by the Commissioner of Social Security to have been disabled (within the meaning of section 1614(a)(3) of the Social Security Act, 42 U.S.C. 1382c(a)(3)) for some portion of such year.

A trust shall not fail to meet the requirements of subclause (II) merely because the corpus of the trust may revert to a person who is not so disabled after the trust ceases to have any beneficiary who is so disabled.

**[(iii) YEARS WHEN PERSONAL EXEMPTION AMOUNT IS ZERO.—**

**[(I) IN GENERAL.—In the case of any taxable year in which the exemption amount under section 151(d) is zero, clause (i) shall be applied by substituting “\$4,150” for “the exemption amount under section 151(d)”.**

**[(II) INFLATION ADJUSTMENT.—In the case of any taxable year beginning in a calendar year after 2018, the \$4,150 amount in subparagraph (A) shall be increased in the same manner as provided in section 6334(d)(4)(C).]**

**[(3) DEDUCTIONS IN LIEU OF PERSONAL EXEMPTION.—The deductions allowed by this subsection shall be in lieu of the deductions allowed under section 151 (relating to deduction for personal exemption).]**

(c) DEDUCTION FOR AMOUNTS PAID OR PERMANENTLY SET ASIDE FOR A CHARITABLE PURPOSE.—

(1) GENERAL RULE.—In the case of an estate or trust (other than a trust meeting the specifications of subpart B), there shall be allowed as a deduction in computing its taxable income (in lieu of the deduction allowed by section 170(a), relating to deduction for charitable, etc., contributions and gifts) any amount of the gross income, without limitation, which pur-

suant to the terms of the governing instrument is, during the taxable year, paid for a purpose specified in section 170(c) (determined without regard to section 170(c)(2)(A)). If a charitable contribution is paid after the close of such taxable year and on or before the last day of the year following the close of such taxable year, then the trustee or administrator may elect to treat such contribution as paid during such taxable year. The election shall be made at such time and in such manner as the Secretary prescribes by regulations.

(2) AMOUNTS PERMANENTLY SET ASIDE.—In the case of an estate, and in the case of a trust (other than a trust meeting the specifications of subpart B) required by the terms of its governing instrument to set aside amounts which was—

(A) created on or before October 9, 1969, if—

(i) an irrevocable remainder interest is transferred to or for the use of an organization described in section 170(c), or

(ii) the grantor is at all times after October 9, 1969, under a mental disability to change the terms of the trust; or

(B) established by a will executed on or before October 9, 1969, if—

(i) the testator dies before October 9, 1972, without having republished the will after October 9, 1969, by codicil or otherwise,

(ii) the testator at no time after October 9, 1969, had the right to change the portions of the will which pertain to the trust, or

(iii) the will is not republished by codicil or otherwise before October 9, 1972, and the testator is on such date and at all times thereafter under a mental disability to republish the will by codicil or otherwise,

there shall also be allowed as a deduction in computing its taxable income any amount of the gross income, without limitation, which pursuant to the terms of the governing instrument is, during the taxable year, permanently set aside for a purpose specified in section 170(c), or is to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, or for the establishment, acquisition, maintenance, or operation of a public cemetery not operated for profit. In the case of a trust, the preceding sentence shall apply only to gross income earned with respect to amounts transferred to the trust before October 9, 1969, or transferred under a will to which subparagraph (B) applies.

(3) POOLED INCOME FUNDS.—In the case of a pooled income fund (as defined in paragraph (5)), there shall also be allowed as a deduction in computing its taxable income any amount of the gross income attributable to gain from the sale of a capital asset held for more than 1 year, without limitation, which pursuant to the terms of the governing instrument is, during the taxable year, permanently set aside for a purpose specified in section 170(c).

(4) ADJUSTMENTS.—To the extent that the amount otherwise allowable as a deduction under this subsection consists of gain

described in section 1202(a), proper adjustment shall be made for any exclusion allowable to the estate or trust under section 1202. In the case of a trust, the deduction allowed by this subsection shall be subject to section 681 (relating to unrelated business income).

(5) DEFINITION OF POOLED INCOME FUND.—For purposes of paragraph (3), a pooled income fund is a trust—

(A) to which each donor transfers property, contributing an irrevocable remainder interest in such property to or for the use of an organization described in section 170(b)(1)(A) (other than in clauses (vii) or (viii)), and retaining an income interest for the life of one or more beneficiaries (living at the time of such transfer),

(B) in which the property transferred by each donor is commingled with property transferred by other donors who have made or make similar transfers,

(C) which cannot have investments in securities which are exempt from the taxes imposed by this subtitle,

(D) which includes only amounts received from transfers which meet the requirements of this paragraph,

(E) which is maintained by the organization to which the remainder interest is contributed and of which no donor or beneficiary of an income interest is a trustee, and

(F) from which each beneficiary of an income interest receives income, for each year for which he is entitled to receive the income interest referred to in subparagraph (A), determined by the rate of return earned by the trust for such year.

For purposes of determining the amount of any charitable contribution allowable by reason of a transfer of property to a pooled fund, the value of the income interest shall be determined on the basis of the highest rate of return earned by the fund for any of the 3 taxable years immediately preceding the taxable year of the fund in which the transfer is made. In the case of funds in existence less than 3 taxable years preceding the taxable year of the fund in which a transfer is made the rate of return shall be deemed to be 6 percent per annum, except that the Secretary may prescribe a different rate of return.

(6) TAXABLE PRIVATE FOUNDATIONS.—In the case of a private foundation which is not exempt from taxation under section 501(a) for the taxable year, the provisions of this subsection shall not apply and the provisions of section 170 shall apply.

(d) NET OPERATING LOSS DEDUCTION.—The benefit of the deduction for net operating losses provided by section 172 shall be allowed to estates and trusts under regulations prescribed by the Secretary.

(e) DEDUCTION FOR DEPRECIATION AND DEPLETION.—An estate or trust shall be allowed the deduction for depreciation and depletion only to the extent not allowable to beneficiaries under section 167(d) and 611(b).

(f) AMORTIZATION DEDUCTIONS.—The benefit of the deductions for amortization provided by sections 169 and 197 shall be allowed to estates and trusts in the same manner as in the case of an individual. The allowable deduction shall be apportioned between the

income beneficiaries and the fiduciary under regulations prescribed by the Secretary.

(g) **DISALLOWANCE OF DOUBLE DEDUCTIONS.**—Amounts allowable under section 2053 or 2054 as a deduction in computing the taxable estate of a decedent shall not be allowed as a deduction (or as an offset against the sales price of property in determining gain or loss) in computing the taxable income of the estate or of any other person, unless there is filed, within the time and in the manner and form prescribed by the Secretary, a statement that the amounts have not been allowed as deductions under section 2053 or 2054 and a waiver of the right to have such amounts allowed at any time as deductions under section 2053 or 2054. Rules similar to the rules of the preceding sentence shall apply to amounts which may be taken into account under section 2621(a)(2) or 2622(b). This subsection shall not apply with respect to deductions allowed under part II (relating to income in respect of decedents).

(h) **UNUSED LOSS CARRYOVERS AND EXCESS DEDUCTIONS ON TERMINATION AVAILABLE TO BENEFICIARIES.**—If on the termination of an estate or trust, the estate or trust has—

(1) a net operating loss carryover under section 172 or a capital loss carryover under section 1212, or

(2) for the last taxable year of the estate or trust deductions (other than the deductions allowed under subsections (b) or (c)) in excess of gross income for such year,

then such carryover or such excess shall be allowed as a deduction, in accordance with regulations prescribed by the Secretary, to the beneficiaries succeeding to the property of the estate or trust.

(i) **CERTAIN DISTRIBUTIONS BY CEMETERY PERPETUAL CARE FUNDS.**—In the case of a cemetery perpetual care fund which—

(1) was created pursuant to local law by a taxable cemetery corporation for the care and maintenance of cemetery property, and

(2) is treated for the taxable year as a trust for purposes of this subchapter,

any amount distributed by such fund for the care and maintenance of gravesites which have been purchased from the cemetery corporation before the beginning of the taxable year of the trust and with respect to which there is an obligation to furnish care and maintenance shall be considered to be a distribution solely for purposes of sections 651 and 661, but only to the extent that the aggregate amount so distributed during the taxable year does not exceed \$5 multiplied by the aggregate number of such gravesites.

**SEC. 643. DEFINITIONS APPLICABLE TO SUBPARTS A, B, C, AND D.**

(a) **DISTRIBUTABLE NET INCOME.**—For purposes of this part, the term “distributable net income” means, with respect to any taxable year, the taxable income of the estate or trust computed with the following modifications—

(1) **DEDUCTION FOR DISTRIBUTIONS.**—No deduction shall be taken under sections 651 and 661 (relating to additional deductions).

(2) **【DEDUCTION FOR PERSONAL EXEMPTION】** *BASIC DEDUCTION.*—No deduction shall be taken under section 642(b) **【(relating to deduction for personal exemptions)】** (*relating to basic deduction*).

(3) CAPITAL GAINS AND LOSSES.—Gains from the sale or exchange of capital assets shall be excluded to the extent that such gains are allocated to corpus and are not (A) paid, credited, or required to be distributed to any beneficiary during the taxable year, or (B) paid, permanently set aside, or to be used for the purposes specified in section 642(c). Losses from the sale or exchange of capital assets shall be excluded, except to the extent such losses are taken into account in determining the amount of gains from the sale or exchange of capital assets which are paid, credited, or required to be distributed to any beneficiary during the taxable year. The exclusion under section 1202 shall not be taken into account.

(4) EXTRAORDINARY DIVIDENDS AND TAXABLE STOCK DIVIDENDS.—For purposes only of subpart B (relating to trusts which distribute current income only), there shall be excluded those items of gross income constituting extraordinary dividends or taxable stock dividends which the fiduciary, acting in good faith, does not pay or credit to any beneficiary by reason of his determination that such dividends are allocable to corpus under the terms of the governing instrument and applicable local law.

(5) TAX-EXEMPT INTEREST.—There shall be included any tax-exempt interest to which section 103 applies, reduced by any amounts which would be deductible in respect of disbursements allocable to such interest but for the provisions of section 265 (relating to disallowance of certain deductions).

(6) INCOME OF FOREIGN TRUST.—In the case of a foreign trust—

(A) There shall be included the amounts of gross income from sources without the United States, reduced by any amounts which would be deductible in respect of disbursements allocable to such income but for the provisions of section 265(a)(1) (relating to disallowance of certain deductions).

(B) Gross income from sources within the United States shall be determined without regard to section 894 (relating to income exempt under treaty).

(C) Paragraph (3) shall not apply to a foreign trust. In the case of such a trust, there shall be included gains from the sale or exchange of capital assets, reduced by losses from such sales or exchanges to the extent such losses do not exceed gains from such sales or exchanges.

(7) ABUSIVE TRANSACTIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this part, including regulations to prevent avoidance of such purposes.

If the estate or trust is allowed a deduction under section 642(c), the amount of the modifications specified in paragraphs (5) and (6) shall be reduced to the extent that the amount of income which is paid, permanently set aside, or to be used for the purposes specified in section 642(c) is deemed to consist of items specified in those paragraphs. For this purpose, such amount shall (in the absence of specific provisions in the governing instrument) be deemed to consist of the same proportion of each class of items of income of the

estate or trust as the total of each class bears to the total of all classes.

(b) **INCOME.**—For purposes of this subpart and subparts B, C, and D, the term “income”, when not preceded by the words “taxable”, “distributable net”, “undistributed net”, or “gross”, means the amount of income of the estate or trust for the taxable year determined under the terms of the governing instrument and applicable local law. Items of gross income constituting extraordinary dividends or taxable stock dividends which the fiduciary, acting in good faith, determines to be allocable to corpus under the terms of the governing instrument and applicable local law shall not be considered income.

(c) **BENEFICIARY.**—For purposes of this part, the term “beneficiary” includes heir, legatee, devisee.

(d) **COORDINATION WITH BACK-UP WITHHOLDING.**—Except to the extent otherwise provided in regulations, this subchapter shall be applied with respect to payments subject to withholding under section 3406—

(1) by allocating between the estate or trust and its beneficiaries any credit allowable under section 31(c) (on the basis of their respective shares of any such payment taken into account under this subchapter),

(2) by treating each beneficiary to whom such credit is allocated as if an amount equal to such credit has been paid to him by the estate or trust, and

(3) by allowing the estate or trust a deduction in an amount equal to the credit so allocated to beneficiaries.

(e) **TREATMENT OF PROPERTY DISTRIBUTED IN KIND.**—

(1) **BASIS OF BENEFICIARY.**—The basis of any property received by a beneficiary in a distribution from an estate or trust shall be—

(A) the adjusted basis of such property in the hands of the estate or trust immediately before the distribution, adjusted for

(B) any gain or loss recognized to the estate or trust on the distribution.

(2) **AMOUNT OF DISTRIBUTION.**—In the case of any distribution of property (other than cash), the amount taken into account under sections 661(a)(2) and 662(a)(2) shall be the lesser of—

(A) the basis of such property in the hands of the beneficiary (as determined under paragraph (1)), or

(B) the fair market value of such property.

(3) **ELECTION TO RECOGNIZE GAIN.**—

(A) **IN GENERAL.**—In the case of any distribution of property (other than cash) to which an election under this paragraph applies—

(i) paragraph (2) shall not apply,

(ii) gain or loss shall be recognized by the estate or trust in the same manner as if such property had been sold to the distributee at its fair market value, and

(iii) the amount taken into account under sections 661(a)(2) and 662(a)(2) shall be the fair market value of such property.

(B) ELECTION.—Any election under this paragraph shall apply to all distributions made by the estate or trust during a taxable year and shall be made on the return of such estate or trust for such taxable year.

Any such election, once made, may be revoked only with the consent of the Secretary.

(4) EXCEPTION FOR DISTRIBUTIONS DESCRIBED IN SECTION 663(A).—This subsection shall not apply to any distribution described in section 663(a).

(f) TREATMENT OF MULTIPLE TRUSTS.—For purposes of this subchapter, under regulations prescribed by the Secretary, 2 or more trusts shall be treated as 1 trust if—

(1) such trusts have substantially the same grantor or grantors and substantially the same primary beneficiary or beneficiaries, and

(2) a principal purpose of such trusts is the avoidance of the tax imposed by this chapter.

For purposes of the preceding sentence, a husband and wife shall be treated as 1 person.

(g) CERTAIN PAYMENTS OF ESTIMATED TAX TREATED AS PAID BY BENEFICIARY.—

(1) IN GENERAL.—In the case of a trust—

(A) the trustee may elect to treat any portion of a payment of estimated tax made by such trust for any taxable year of the trust as a payment made by a beneficiary of such trust,

(B) any amount so treated shall be treated as paid or credited to the beneficiary on the last day of such taxable year, and

(C) for purposes of subtitle F, the amount so treated—

(i) shall not be treated as a payment of estimated tax made by the trust, but

(ii) shall be treated as a payment of estimated tax made by such beneficiary on January 15 following the taxable year.

(2) TIME FOR MAKING ELECTION.—An election under paragraph (1) shall be made on or before the 65th day after the close of the taxable year of the trust and in such manner as the Secretary may prescribe.

(3) EXTENSION TO LAST YEAR OF ESTATE.—In the case of a taxable year reasonably expected to be the last taxable year of an estate—

(A) any reference in this subsection to a trust shall be treated as including a reference to an estate, and

(B) the fiduciary of the estate shall be treated as the trustee.

(h) DISTRIBUTIONS BY CERTAIN FOREIGN TRUSTS THROUGH NOMINEES.—For purposes of this part, any amount paid to a United States person which is derived directly or indirectly from a foreign trust of which the payor is not the grantor shall be deemed in the year of payment to have been directly paid by the foreign trust to such United States person.

(i) LOANS FROM FOREIGN TRUSTS.—For purposes of subparts B, C, and D—



(1) GENERAL RULE.—Except as provided in regulations, if a foreign trust makes a loan of cash or marketable securities (or permits the use of any other trust property) directly or indirectly to or by—

- (A) any grantor or beneficiary of such trust who is a United States person, or
  - (B) any United States person not described in subparagraph (A) who is related to such grantor or beneficiary,
- the amount of such loan (or the fair market value of the use of such property) shall be treated as a distribution by such trust to such grantor or beneficiary (as the case may be).

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

(A) CASH.—The term “cash” includes foreign currencies and cash equivalents.

(B) RELATED PERSON.—

(i) IN GENERAL.—A person is related to another person if the relationship between such persons would result in a disallowance of losses under section 267 or 707(b). In applying section 267 for purposes of the preceding sentence, section 267(c)(4) shall be applied as if the family of an individual includes the spouses of the members of the family.

(ii) ALLOCATION.—If any person described in paragraph (1)(B) is related to more than one person, the grantor or beneficiary to whom the treatment under this subsection applies shall be determined under regulations prescribed by the Secretary.

(C) EXCLUSION OF TAX-EXEMPTS.—The term “United States person” does not include any entity exempt from tax under this chapter.

(D) TRUST NOT TREATED AS SIMPLE TRUST.—Any trust which is treated under this subsection as making a distribution shall be treated as not described in section 651.

(E) EXCEPTION FOR COMPENSATED USE OF PROPERTY.—In the case of the use of any trust property other than a loan of cash or marketable securities, paragraph (1) shall not apply to the extent that the trust is paid the fair market value of such use within a reasonable period of time of such use.

(3) SUBSEQUENT TRANSACTIONS.—If any loan (or use of property) is taken into account under paragraph (1), any subsequent transaction between the trust and the original borrower regarding the principal of the loan (by way of complete or partial repayment, satisfaction, cancellation, discharge, or otherwise) or the return of such property shall be disregarded for purposes of this title.

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### **Subchapter K—Partners and Partnerships**

\* \* \* \* \*

**PART I—DETERMINATION OF TAX LIABILITY**

\* \* \* \* \*

**SEC. 703. PARTNERSHIP COMPUTATIONS.**

(a) **INCOME AND DEDUCTIONS.**—The taxable income of a partnership shall be computed in the same manner as in the case of an individual except that—

(1) the items described in section 702(a) shall be separately stated, and

(2) the following deductions shall not be allowed to the partnership:

[(A) the deductions for personal exemptions provided in section 151,]

[(B) (A) the deduction for taxes provided in section 164(a) with respect to taxes, described in section 901, paid or accrued to foreign countries and to possessions of the United States,

[(C) (B) the deduction for charitable contributions provided in section 170,

[(D) (C) the net operating loss deduction provided in section 172,

[(E) (D) the additional itemized deductions for individuals provided in part VII of subchapter B (sec. 211 and following), and

[(F) (E) the deduction for depletion under section 611 with respect to oil and gas wells.

(b) **ELECTIONS OF THE PARTNERSHIP.**—Any election affecting the computation of taxable income derived from a partnership shall be made by the partnership, except that any election under—

(1) subsection (b)(5) or (c)(3) of section 108 (relating to income from discharge of indebtedness),

(2) section 617 (relating to deduction and recapture of certain mining exploration expenditures), or

(3) section 901 (relating to taxes of foreign countries and possessions of the United States),

shall be made by each partner separately.

**Subchapter N—Tax Based on Income From Sources Within or Without the United States**

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**PART II—NONRESIDENT ALIENS AND FOREIGN CORPORATIONS**

\* \* \* \* \*

**Subpart A—Nonresident Alien Individuals**

\* \* \* \* \*

**SEC. 873. DEDUCTIONS.**

(a) **GENERAL RULE.**—In the case of a nonresident alien individual, the deductions shall be allowed only for purposes of section 871(b) and (except as provided by subsection (b)) only if and to the extent that they are connected with income which is effectively connected with the conduct of a trade or business within the United States;

and the proper apportionment and allocation of the deductions for this purpose shall be determined as provided in regulations prescribed by the Secretary.

(b) **EXCEPTIONS.**—The following deductions shall be allowed whether or not they are connected with income which is effectively connected with the conduct of a trade or business within the United States:

(1) **LOSSES.**—The deduction allowed by section 165 for casualty or theft losses described in paragraph (2) or (3) of section 165(c), but only if the loss is of property located within the United States.

(2) **CHARITABLE CONTRIBUTIONS.**—The deduction for charitable contributions and gifts allowed by section 170.

[(3) **PERSONAL EXEMPTION.**—The deduction for personal exemptions allowed by section 151, except that only one exemption shall be allowed under section 151 unless the taxpayer is a resident of a contiguous country or is a national of the United States.]

(c) **CROSS REFERENCE.**—For rule that certain foreign taxes are not to be taken into account in determining deduction or credit, see section 906(b)(1).

**SEC. 874. ALLOWANCE OF DEDUCTIONS AND CREDITS.**

(a) **RETURN PREREQUISITE TO ALLOWANCE.**—A nonresident alien individual shall receive the benefit of the deductions and credits allowed to him in this subtitle only by filing or causing to be filed with the Secretary a true and accurate return, in the manner prescribed in subtitle F (sec. 6001 and following, relating to procedure and administration), including therein all the information which the Secretary may deem necessary for the calculation of such deductions and credits. This subsection shall not be construed to deny the credits provided by sections 31 and 33 for tax withheld at source or the credit provided by section 34 for certain uses of gasoline and special fuels.

[(b) **TAX WITHHELD AT SOURCE.**—The benefit of the deduction for exemptions under section 151 may, in the discretion of the Secretary, and under regulations prescribed by the Secretary, be received by a non-resident alien individual entitled thereto, by filing a claim therefor with the withholding agent.]

[(c) (b) **FOREIGN TAX CREDIT.**—Except as provided in section 906, a nonresident alien individual shall not be allowed the credits against the tax for taxes of foreign countries and possessions of the United States allowed by section 901.

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**Subpart D—Miscellaneous Provisions**

\* \* \* \* \*

**SEC. 891. DOUBLING OF RATES OF TAX ON CITIZENS AND CORPORATIONS OF CERTAIN FOREIGN COUNTRIES.**

Whenever the President finds that, under the laws of any foreign country, citizens or corporations of the United States are being subjected to discriminatory or extraterritorial taxes, the President shall so proclaim and the rates of tax imposed by sections 1, 3, 11, 801, 831, 852, 871, and 881 shall, for the taxable year during which such proclamation is made and for each taxable year thereafter, be

doubled in the case of each citizen and corporation of such foreign country; but the tax at such doubled rate shall be considered as imposed by such sections as the case may be. In no case shall this section operate to increase the taxes imposed by such sections (computed without regard to this section) to an amount in excess of 80 percent of the taxable income of the taxpayer (computed without regard to the deductions allowable [under section 151 and] under part VIII of subchapter B). Whenever the President finds that the laws of any foreign country with respect to which the President has made a proclamation under the preceding provisions of this section have been modified so that discriminatory and extraterritorial taxes applicable to citizens and corporations of the United States have been removed, he shall so proclaim, and the provisions of this section providing for doubled rates of tax shall not apply to any citizen or corporation of such foreign country with respect to any taxable year beginning after such proclamation is made.

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### PART III—INCOME FROM SOURCES WITHOUT THE UNITED STATES

\* \* \* \* \*

#### Subpart A—Foreign Tax Credit

\* \* \* \* \*

#### SEC. 904. LIMITATION ON CREDIT.

(a) **LIMITATION.**—The total amount of the credit taken under section 901(a) shall not exceed the same proportion of the tax against which such credit is taken which the taxpayer's taxable income from sources without the United States (but not in excess of the taxpayer's entire taxable income) bears to his entire taxable income for the same taxable year.

(b) **TAXABLE INCOME FOR PURPOSE OF COMPUTING LIMITATION.**—

**[(1) PERSONAL EXEMPTIONS.**—For purposes of subsection (a), the taxable income in the case of an individual, estate, or trust shall be computed without any deduction for personal exemptions under section 151 or 642(b).]

*(1) DEDUCTION FOR ESTATES AND TRUSTS.*—For purposes of subsection (a), the taxable income of an estate or trust shall be computed without any deduction under section 642(b).

(2) **CAPITAL GAINS.**—For purposes of this section—

(A) **IN GENERAL.**—Taxable income from sources outside the United States shall include gain from the sale or exchange of capital assets only to the extent of foreign source capital gain net income.

(B) **SPECIAL RULES WHERE CAPITAL GAIN RATE DIFFERENTIAL.**—In the case of any taxable year for which there is a capital gain rate differential—

(i) in lieu of applying subparagraph (A), the taxable income from sources outside the United States shall include gain from the sale or exchange of capital assets only in an amount equal to foreign source capital

gain net income reduced by the rate differential portion of foreign source net capital gain,

(ii) the entire taxable income shall include gain from the sale or exchange of capital assets only in an amount equal to capital gain net income reduced by the rate differential portion of net capital gain, and

(iii) for purposes of determining taxable income from sources outside the United States, any net capital loss (and any amount which is a short-term capital loss under section 1212(a)) from sources outside the United States to the extent taken into account in determining capital gain net income for the taxable year shall be reduced by an amount equal to the rate differential portion of the excess of net capital gain from sources within the United States over net capital gain.

(C) COORDINATION WITH CAPITAL GAINS RATES.—The Secretary may by regulations modify the application of this paragraph and paragraph (3) to the extent necessary to properly reflect any capital gain rate differential under section 1(h) and the computation of net capital gain.

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

(A) FOREIGN SOURCE CAPITAL GAIN NET INCOME.—The term “foreign source capital gain net income” means the lesser of—

(i) capital gain net income from sources without the United States, or

(ii) capital gain net income.

(B) FOREIGN SOURCE NET CAPITAL GAIN.—The term “foreign source net capital gain” means the lesser of—

(i) net capital gain from sources without the United States, or

(ii) net capital gain.

(C) SECTION 1231 GAINS.—The term “gain from the sale or exchange of capital assets” includes any gain so treated under section 1231.

(D) CAPITAL GAIN RATE DIFFERENTIAL.—There is a capital gain rate differential for any year if subsection (h) of section 1 applies to such taxable year.

(E) RATE DIFFERENTIAL PORTION.—The rate differential portion of foreign source net capital gain, net capital gain, or the excess of net capital gain from sources within the United States over net capital gain, as the case may be, is the same proportion of such amount as—

(i) the excess of—

(I) the highest rate of tax set forth in subsection (a), (b), (c), (d), or (e) of section 1 (whichever applies), over

(II) the alternative rate of tax determined under section 1(h), bears to

(ii) that rate referred to in subclause (I).

(4) TREATMENT OF DIVIDENDS FOR WHICH DEDUCTION IS ALLOWED UNDER SECTION 245A.—For purposes of subsection (a), in the case of a domestic corporation which is a United States shareholder with respect to a specified 10-percent owned foreign corporation, such shareholder’s taxable income from

sources without the United States (and entire taxable income) shall be determined without regard to—

- (A) the foreign-source portion of any dividend received from such foreign corporation, and
- (B) any deductions properly allocable or apportioned to—
  - (i) income (other than amounts includible under section 951(a)(1) or 951A(a)) with respect to stock of such specified 10-percent owned foreign corporation, or
  - (ii) such stock to the extent income with respect to such stock is other than amounts includible under section 951(a)(1) or 951A(a).

Any term which is used in section 245A and in this paragraph shall have the same meaning for purposes of this paragraph as when used in such section.

(c) CARRYBACK AND CARRYOVER OF EXCESS TAX PAID.—Any amount by which all taxes paid or accrued to foreign countries or possessions of the United States for any taxable year for which the taxpayer chooses to have the benefits of this subpart exceed the limitation under subsection (a) shall be deemed taxes paid or accrued to foreign countries or possessions of the United States in the first preceding taxable year and in any of the first 10 succeeding taxable years, in that order and to the extent not deemed taxes paid or accrued in a prior taxable year, in the amount by which the limitation under subsection (a) for such preceding or succeeding taxable year exceeds the sum of the taxes paid or accrued to foreign countries or possessions of the United States for such preceding or succeeding taxable year and the amount of the taxes for any taxable year earlier than the current taxable year which shall be deemed to have been paid or accrued in such preceding or subsequent taxable year (whether or not the taxpayer chooses to have the benefits of this subpart with respect to such earlier taxable year). Such amount deemed paid or accrued in any year may be availed of only as a tax credit and not as a deduction and only if the taxpayer for such year chooses to have the benefits of this subpart as to taxes paid or accrued for that year to foreign countries or possessions of the United States. This subsection shall not apply to taxes paid or accrued with respect to amounts described in subsection (d)(1)(A).

(d) SEPARATE APPLICATION OF SECTION WITH RESPECT TO CERTAIN CATEGORIES OF INCOME.—

(1) IN GENERAL.—The provisions of subsections (a), (b), and (c) and sections 902, 907, and 960 shall be applied separately with respect to—

- (A) any amount includible in gross income under section 951A (other than passive category income),
- (B) foreign branch income,
- (C) passive category income, and
- (D) general category income.

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

(A) CATEGORIES.—

- (i) PASSIVE CATEGORY INCOME.—The term “passive category income” means passive income and specified passive category income.

(ii) GENERAL CATEGORY INCOME.—The term “general category income” means income other than income described in paragraph (1)(A), foreign branch income, and passive category income.

(B) PASSIVE INCOME.—

(i) IN GENERAL.—Except as otherwise provided in this subparagraph, the term “passive income” means any income received or accrued by any person which is of a kind which would be foreign personal holding company income (as defined in section 954(c)).

(ii) CERTAIN AMOUNTS INCLUDED.—Except as provided in clause (iii), subparagraph (E)(ii), or paragraph (3)(H), the term “passive income” includes any amount includible in gross income under section 1293 (relating to certain passive foreign investment companies).

(iii) EXCEPTIONS.—The term “passive income” shall not include—

- (I) any export financing interest, and
- (II) any high-taxed income.

(iv) CLARIFICATION OF APPLICATION OF SECTION 864(D)(6).—In determining whether any income is of a kind which would be foreign personal holding company income, the rules of section 864(d)(6) shall apply only in the case of income of a controlled foreign corporation.

(v) SPECIFIED PASSIVE CATEGORY INCOME.—The term “specified passive category income” means—

(I) dividends from a DISC or former DISC (as defined in section 992(a)) to the extent such dividends are treated as income from sources without the United States, and

(II) distributions from a former FSC (as defined in section 922) out of earnings and profits attributable to foreign trade income (within the meaning of section 923(b)) or interest or carrying charges (as defined in section 927(d)(1)) derived from a transaction which results in foreign trade income (as defined in section 923(b)).

Any reference in subclause (II) to section 922, 923, or 927 shall be treated as a reference to such section as in effect before its repeal by the FSC Repeal and Extraterritorial Income Exclusion Act of 2000.

(C) TREATMENT OF FINANCIAL SERVICES INCOME AND COMPANIES.—

(i) IN GENERAL.—Financial services income shall be treated as general category income in the case of—

- (I) a member of a financial services group, and
- (II) any other person if such person is predominantly engaged in the active conduct of a banking, insurance, financing, or similar business.

(ii) FINANCIAL SERVICES GROUP.—The term “financial services group” means any affiliated group (as defined in section 1504(a) without regard to paragraphs (2) and (3) of section 1504(b)) which is predominantly engaged in the active conduct of a banking, insurance,

financing, or similar business. In determining whether such a group is so engaged, there shall be taken into account only the income of members of the group that are—

- (I) United States corporations, or
- (II) controlled foreign corporations in which such United States corporations own, directly or indirectly, at least 80 percent of the total voting power and value of the stock.

(iii) PASS-THRU ENTITIES.—The Secretary shall by regulation specify for purposes of this subparagraph the treatment of financial services income received or accrued by partnerships and by other pass-thru entities which are not members of a financial services group.

(D) FINANCIAL SERVICES INCOME.—

(i) IN GENERAL.—Except as otherwise provided in this subparagraph, the term “financial services income” means any income which is received or accrued by any person predominantly engaged in the active conduct of a banking, insurance, financing, or similar business, and which is—

- (I) described in clause (ii), or
- (II) passive income (determined without regard to subparagraph (B)(iii)(II)).

(ii) GENERAL DESCRIPTION OF FINANCIAL SERVICES INCOME.—Income is described in this clause if such income is—

- (I) derived in the active conduct of a banking, financing, or similar business,
- (II) derived from the investment by an insurance company of its unearned premiums or reserves ordinary and necessary for the proper conduct of its insurance business, or
- (III) of a kind which would be insurance income as defined in section 953(a) determined without regard to those provisions of paragraph (1)(A) of such section which limit insurance income to income from countries other than the country in which the corporation was created or organized.

(E) NONCONTROLLED SECTION 902 CORPORATION.—

(i) NONCONTROLLED 10-PERCENT OWNED FOREIGN CORPORATION.—The term “noncontrolled 10-percent owned foreign corporation” means any foreign corporation which is—

- (I) a specified 10-percent owned foreign corporation (as defined in section 245A(b)), or
- (II) a passive foreign investment company (as defined in section 1297(a)) with respect to which the taxpayer meets the stock ownership requirements of section 902(a) (or, for purposes of applying paragraphs (3) and (4), the requirements of section 902(b)).

A controlled foreign corporation shall not be treated as a noncontrolled 10-percent owned foreign corporation



with respect to any distribution out of its earnings and profits for periods during which it was a controlled foreign corporation. Any reference to section 902 in this clause shall be treated as a reference to such section as in effect before its repeal.

(ii) TREATMENT OF INCLUSIONS UNDER SECTION 1293.—If any foreign corporation is a noncontrolled 10-percent owned foreign corporation with respect to the taxpayer, any inclusion under section 1293 with respect to such corporation shall be treated as a dividend from such corporation.

(F) HIGH-TAXED INCOME.—The term “high-taxed income” means any income which (but for this subparagraph) would be passive income if the sum of—

(i) the foreign income taxes paid or accrued by the taxpayer with respect to such income, and

(ii) the foreign income taxes deemed paid by the taxpayer with respect to such income under section 902 or 960,

exceeds the highest rate of tax specified in section 1 or 11 (whichever applies) multiplied by the amount of such income (determined with regard to section 78). For purposes of the preceding sentence, the term “foreign income taxes” means any income, war profits, or excess profits tax imposed by any foreign country or possession of the United States.

(G) EXPORT FINANCING INTEREST.—For purposes of this paragraph, the term “export financing interest” means any interest derived from financing the sale (or other disposition) for use or consumption outside the United States of any property—

(i) which is manufactured, produced, grown, or extracted in the United States by the taxpayer or a related person, and

(ii) not more than 50 percent of the fair market value of which is attributable to products imported into the United States.

For purposes of clause (ii), the fair market value of any property imported into the United States shall be its appraised value, as determined by the Secretary under section 402 of the Tariff Act of 1930 (19 U.S.C. 1401a) in connection with its importation.

(H) TREATMENT OF INCOME TAX BASE DIFFERENCES.—

(i) IN GENERAL.—In the case of taxable years beginning after December 31, 2006, tax imposed under the law of a foreign country or possession of the United States on an amount which does not constitute income under United States tax principles shall be treated as imposed on income described in paragraph (1)(B).

(ii) SPECIAL RULE FOR YEARS BEFORE 2007.—

(I) IN GENERAL.—In the case of taxes paid or accrued in taxable years beginning after December 31, 2004, and before January 1, 2007, a taxpayer may elect to treat tax imposed under the law of a foreign country or possession of the United States

on an amount which does not constitute income under United States tax principles as tax imposed on income described in subparagraph (C) or (I) of paragraph (1).

(II) ELECTION IRREVOCABLE.—Any such election shall apply to the taxable year for which made and all subsequent taxable years described in subclause (I) unless revoked with the consent of the Secretary.

(I) RELATED PERSON.—For purposes of this paragraph, the term “related person” has the meaning given such term by section 954(d)(3), except that such section shall be applied by substituting “the person with respect to whom the determination is being made” for “controlled foreign corporation” each place it appears.

(J) FOREIGN BRANCH INCOME.—

(i) IN GENERAL.—The term “foreign branch income” means the business profits of such United States person which are attributable to 1 or more qualified business units (as defined in section 989(a)) in 1 or more foreign countries. For purposes of the preceding sentence, the amount of business profits attributable to a qualified business unit shall be determined under rules established by the Secretary.

(ii) EXCEPTION.—Such term shall not include any income which is passive category income.

(K) TRANSITIONAL RULES FOR 2007 CHANGES.—For purposes of paragraph (1)—

(i) taxes carried from any taxable year beginning before January 1, 2007, to any taxable year beginning on or after such date, with respect to any item of income, shall be treated as described in the subparagraph of paragraph (1) in which such income would be described were such taxes paid or accrued in a taxable year beginning on or after such date, and

(ii) the Secretary may by regulations provide for the allocation of any carryback of taxes with respect to income from a taxable year beginning on or after January 1, 2007, to a taxable year beginning before such date for purposes of allocating such income among the separate categories in effect for the taxable year to which carried.

(3) LOOK-THRU IN CASE OF CONTROLLED FOREIGN CORPORATIONS.—

(A) IN GENERAL.—Except as otherwise provided in this paragraph, dividends, interest, rents, and royalties received or accrued by the taxpayer from a controlled foreign corporation in which the taxpayer is a United States shareholder shall not be treated as passive category income.

(B) SUBPART F INCLUSIONS.—Any amount included in gross income under section 951(a)(1)(A) shall be treated as passive category income to the extent the amount so included is attributable to passive category income.

(C) INTEREST, RENTS, AND ROYALTIES.—Any interest, rent, or royalty which is received or accrued from a controlled foreign corporation in which the taxpayer is a United States shareholder shall be treated as passive category income to the extent it is properly allocable (under regulations prescribed by the Secretary) to passive category income of the controlled foreign corporation.

(D) DIVIDENDS.—Any dividend paid out of the earnings and profits of any controlled foreign corporation in which the taxpayer is a United States shareholder shall be treated as passive category income in proportion to the ratio of—

- (i) the portion of the earnings and profits attributable to passive category income, to
- (ii) the total amount of earnings and profits.

(E) LOOK-THRU APPLIES ONLY WHERE SUBPART F APPLIES.—If a controlled foreign corporation meets the requirements of section 954(b)(3)(A) (relating to de minimis rule) for any taxable year, for purposes of this paragraph, none of its foreign base company income (as defined in section 954(a) without regard to section 954(b)(5)) and none of its gross insurance income (as defined in section 954(b)(3)(C)) for such taxable year shall be treated as passive category income, except that this sentence shall not apply to any income which (without regard to this sentence) would be treated as financial services income. Solely for purposes of applying subparagraph (D), passive income of a controlled foreign corporation shall not be treated as passive category income if the requirements of section 954(b)(4) are met with respect to such income.

(F) COORDINATION WITH HIGH-TAXED INCOME PROVISIONS.—

- (i) In determining whether any income of a controlled foreign corporation is passive category income, subclause (II) of paragraph (2)(B)(iii) shall not apply.
- (ii) Any income of the taxpayer which is treated as passive category income under this paragraph shall be so treated notwithstanding any provision of paragraph (2); except that the determination of whether any amount is high-taxed income shall be made after the application of this paragraph.

(G) DIVIDEND.—For purposes of this paragraph, the term “dividend” includes any amount included in gross income in section 951(a)(1)(B). Any amount included in gross income under section 78 to the extent attributable to amounts included in gross income in section 951(a)(1)(A) shall not be treated as a dividend but shall be treated as included in gross income under section 951(a)(1)(A).

(H) LOOK-THRU APPLIES TO PASSIVE FOREIGN INVESTMENT COMPANY INCLUSION.—If—

- (i) a passive foreign investment company is a controlled foreign corporation, and
- (ii) the taxpayer is a United States shareholder in such controlled foreign corporation,

any amount included in gross income under section 1293 shall be treated as income in a separate category to the extent such amount is attributable to income in such category.

(4) LOOK-THRU APPLIES TO DIVIDENDS FROM NONCONTROLLED 10-PERCENT OWNED FOREIGN CORPORATIONS.—

(A) IN GENERAL.—For purposes of this subsection, any dividend from a noncontrolled 10-percent owned foreign corporation with respect to the taxpayer shall be treated as income described in a subparagraph of paragraph (1) in proportion to the ratio of—

- (i) the portion of earnings and profits attributable to income described in such subparagraph, to
- (ii) the total amount of earnings and profits.

(B) EARNINGS AND PROFITS OF CONTROLLED FOREIGN CORPORATIONS.—In the case of any distribution from a controlled foreign corporation to a United States shareholder, rules similar to the rules of subparagraph (A) shall apply in determining the extent to which earnings and profits of the controlled foreign corporation which are attributable to dividends received from a noncontrolled 10-percent owned foreign corporation may be treated as income in a separate category.

(C) SPECIAL RULES.—For purposes of this paragraph—

(i) EARNINGS AND PROFITS.—

(I) IN GENERAL.—The rules of section 316 shall apply.

(II) REGULATIONS.—The Secretary may prescribe regulations regarding the treatment of distributions out of earnings and profits for periods before the taxpayer's acquisition of the stock to which the distributions relate.

(ii) INADEQUATE SUBSTANTIATION.—If the Secretary determines that the proper subparagraph of paragraph (1) in which a dividend is described has not been substantiated, such dividend shall be treated as income described in paragraph (1)(A).

(iii) COORDINATION WITH HIGH-TAXED INCOME PROVISIONS.—Rules similar to the rules of paragraph (3)(F) shall apply for purposes of this paragraph.

(iv) LOOK-THRU WITH RESPECT TO CARRYOVER OF CREDIT.—Rules similar to subparagraph (A) also shall apply to any carryforward under subsection (c) from a taxable year beginning before January 1, 2003, of tax allocable to a dividend from a noncontrolled 10-percent owned foreign corporation with respect to the taxpayer. The Secretary may by regulations provide for the allocation of any carryback of tax allocable to a dividend from a noncontrolled 10-percent owned foreign corporation from a taxable year beginning on or after January 1, 2003, to a taxable year beginning before such date for purposes of allocating such dividend among the separate categories in effect for the taxable year to which carried.

(5) CONTROLLED FOREIGN CORPORATION; UNITED STATES SHAREHOLDER.—For purposes of this subsection—

(A) CONTROLLED FOREIGN CORPORATION.—The term “controlled foreign corporation” has the meaning given such term by section 957 (taking into account section 953(c)).

(B) UNITED STATES SHAREHOLDER.—The term “United States shareholder” has the meaning given such term by section 951(b) (taking into account section 953(c)).

(6) SEPARATE APPLICATION TO ITEMS RESOURCED UNDER TREATIES.—

(A) IN GENERAL.—If—

(i) without regard to any treaty obligation of the United States, any item of income would be treated as derived from sources within the United States,

(ii) under a treaty obligation of the United States, such item would be treated as arising from sources outside the United States, and

(iii) the taxpayer chooses the benefits of such treaty obligation,

subsections (a), (b), and (c) of this section and sections 907 and 960 shall be applied separately with respect to each such item.

(B) COORDINATION WITH OTHER PROVISIONS.—This paragraph shall not apply to any item of income to which subsection (h)(10) or section 865(h) applies.

(C) REGULATIONS.—The Secretary may issue such regulations or other guidance as is necessary or appropriate to carry out the purposes of this paragraph, including regulations or other guidance which provides that related items of income may be aggregated for purposes of this paragraph.

(7) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate for the purposes of this subsection, including regulations—

(A) for the application of paragraph (3) and subsection (f)(5) in the case of income paid (or loans made) through 1 or more entities or between 2 or more chains of entities,

(B) preventing the manipulation of the character of income the effect of which is to avoid the purposes of this subsection, and

(C) providing that rules similar to the rules of paragraph (3)(C) shall apply to interest, rents, and royalties received or accrued from entities which would be controlled foreign corporations if they were foreign corporations.

(f) RECAPTURE OF OVERALL FOREIGN LOSS.—

(1) GENERAL RULE.—For purposes of this subpart, in the case of any taxpayer who sustains an overall foreign loss for any taxable year, that portion of the taxpayer’s taxable income from sources without the United States for each succeeding taxable year which is equal to the lesser of—

(A) the amount of such loss (to the extent not used under this paragraph in prior taxable years), or

(B) 50 percent (or such larger percent as the taxpayer may choose) of the taxpayer’s taxable income from sources

without the United States for such succeeding taxable year, shall be treated as income from sources within the United States (and not as income from sources without the United States).

(2) OVERALL FOREIGN LOSS DEFINED.—For purposes of this subsection, the term “overall foreign loss” means the amount by which the gross income for the taxable year from sources without the United States (whether or not the taxpayer chooses the benefits of this subpart for such taxable year) for such year is exceeded by the sum of the deductions properly apportioned or allocated thereto, except that there shall not be taken into account—

(A) any net operating loss deduction allowable for such year under section 172(a), and

(B) any—

(i) foreign expropriation loss for such year, as defined in section 172(h) (as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990), or

(ii) loss for such year which arises from fire, storm, shipwreck, or other casualty, or from theft,

to the extent such loss is not compensated for by insurance or otherwise.

(3) DISPOSITIONS.—

(A) IN GENERAL.—For purposes of this chapter, if property which has been used predominantly without the United States in a trade or business is disposed of during any taxable year—

(i) the taxpayer, notwithstanding any other provision of this chapter (other than paragraph (1)), shall be deemed to have received and recognized taxable income from sources without the United States in the taxable year of the disposition, by reason of such disposition, in an amount equal to the lesser of the excess of the fair market value of such property over the taxpayer’s adjusted basis in such property or the remaining amount of the overall foreign losses which were not used under paragraph (1) for such taxable year or any prior taxable year, and

(ii) paragraph (1) shall be applied with respect to such income by substituting “100 percent” for “50 percent”.

In determining for purposes of this subparagraph whether the predominant use of any property has been without the United States, there shall be taken into account use during the 3-year period ending on the date of the disposition (or, if shorter, the period during which the property has been used in the trade or business).

(B) DISPOSITION DEFINED AND SPECIAL RULES.—

(i) For purposes of this subsection, the term “disposition” includes a sale, exchange, distribution, or gift of property whether or not gain or loss is recognized on the transfer.

(ii) Any taxable income recognized solely by reason of subparagraph (A) shall have the same characterization it would have had if the taxpayer had sold or exchanged the property.

(iii) The Secretary shall prescribe such regulations as he may deem necessary to provide for adjustments to the basis of property to reflect taxable income recognized solely by reason of subparagraph (A).

(C) EXCEPTIONS.—Notwithstanding subparagraph (B), the term “disposition” does not include—

(i) a disposition of property which is not a material factor in the realization of income by the taxpayer, or

(ii) a disposition of property to a domestic corporation in a distribution or transfer described in section 381(a).

(D) APPLICATION TO CERTAIN DISPOSITIONS OF STOCK IN CONTROLLED FOREIGN CORPORATION.—

(i) IN GENERAL.—This paragraph shall apply to an applicable disposition in the same manner as if it were a disposition of property described in subparagraph (A), except that the exception contained in subparagraph (C)(i) shall not apply.

(ii) APPLICABLE DISPOSITION.—For purposes of clause (i), the term “applicable disposition” means any disposition of any share of stock in a controlled foreign corporation in a transaction or series of transactions if, immediately before such transaction or series of transactions, the taxpayer owned more than 50 percent (by vote or value) of the stock of the controlled foreign corporation. Such term shall not include a disposition described in clause (iii) or (iv), except that clause (i) shall apply to any gain recognized on any such disposition.

(iii) EXCEPTION FOR CERTAIN EXCHANGES WHERE OWNERSHIP PERCENTAGE RETAINED.—A disposition shall not be treated as an applicable disposition under clause (ii) if it is part of a transaction or series of transactions—

(I) to which section 351 or 721 applies, or under which the transferor receives stock in a foreign corporation in exchange for the stock in the controlled foreign corporation and the stock received is exchanged basis property (as defined in section 7701(a)(44)), and

(II) immediately after which, the transferor owns (by vote or value) at least the same percentage of stock in the controlled foreign corporation (or, if the controlled foreign corporation is not in existence after such transaction or series of transactions, in another foreign corporation stock in which was received by the transferor in exchange for stock in the controlled foreign corporation) as the percentage of stock in the controlled foreign corporation which the taxpayer owned imme-

diately before such transaction or series of transactions.

(iv) EXCEPTION FOR CERTAIN ASSET ACQUISITIONS.—A disposition shall not be treated as an applicable disposition under clause (ii) if it is part of a transaction or series of transactions in which the taxpayer (or any member of an affiliated group of corporations filing a consolidated return under section 1501 which includes the taxpayer) acquires the assets of a controlled foreign corporation in exchange for the shares of the controlled foreign corporation in a liquidation described in section 332 or a reorganization described in section 368(a)(1).

(v) CONTROLLED FOREIGN CORPORATION.—For purposes of this subparagraph, the term “controlled foreign corporation” has the meaning given such term by section 957.

(vi) STOCK OWNERSHIP.—For purposes of this subparagraph, ownership of stock shall be determined under the rules of subsections (a) and (b) of section 958.

(4) ACCUMULATION DISTRIBUTIONS OF FOREIGN TRUST.—For purposes of this chapter, in the case of amounts of income from sources without the United States which are treated under section 666 (without regard to subsections (b) and (c) thereof if the taxpayer chose to take a deduction with respect to the amounts described in such subsections under section 667(d)(1)(B)) as having been distributed by a foreign trust in a preceding taxable year, that portion of such amounts equal to the amount of any overall foreign loss sustained by the beneficiary in a year prior to the taxable year of the beneficiary in which such distribution is received from the trust shall be treated as income from sources within the United States (and not income from sources without the United States) to the extent that such loss was not used under this subsection in prior taxable years, or in the current taxable year, against other income of the beneficiary.

(5) TREATMENT OF SEPARATE LIMITATION LOSSES.—

(A) IN GENERAL.—The amount of the separate limitation losses for any taxable year shall reduce income from sources within the United States for such taxable year only to the extent the aggregate amount of such losses exceeds the aggregate amount of the separate limitation incomes for such taxable year.

(B) ALLOCATION OF LOSSES.—The separate limitation losses for any taxable year (to the extent such losses do not exceed the separate limitation incomes for such year) shall be allocated among (and operate to reduce) such incomes on a proportionate basis.

(C) RECHARACTERIZATION OF SUBSEQUENT INCOME.—If—

(i) a separate limitation loss from any income category (hereinafter in this subparagraph referred to as “the loss category”) was allocated to income from any other category under subparagraph (B), and



(ii) the loss category has income for a subsequent taxable year,

such income (to the extent it does not exceed the aggregate separate limitation losses from the loss category not previously recharacterized under this subparagraph) shall be recharacterized as income from such other category in proportion to the prior reductions under subparagraph (B) in such other category not previously taken into account under this subparagraph. Nothing in the preceding sentence shall be construed as recharacterizing any tax.

(D) SPECIAL RULES FOR LOSSES FROM SOURCES IN THE UNITED STATES.—Any loss from sources in the United States for any taxable year (to the extent such loss does not exceed the separate limitation incomes from such year) shall be allocated among (and operate to reduce) such incomes on a proportionate basis. This subparagraph shall be applied after subparagraph (B).

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

(i) INCOME CATEGORY.—The term “income category” means each separate category of income described in subsection (d)(1).

(ii) SEPARATE LIMITATION INCOME.—The term “separate limitation income” means, with respect to any income category, the taxable income from sources outside the United States, separately computed for such category.

(iii) SEPARATE LIMITATION LOSS.—The term “separate limitation loss” means, with respect to any income category, the loss from such category determined under the principles of section 907(c)(4)(B).

(F) DISPOSITIONS.—If any separate limitation loss for any taxable year is allocated against any separate limitation income for such taxable year, except to the extent provided in regulations, rules similar to the rules of paragraph (3) shall apply to any disposition of property if gain from such disposition would be in the income category with respect to which there was such separate limitation loss.

(g) RECHARACTERIZATION OF OVERALL DOMESTIC LOSS.—

(1) GENERAL RULE.—For purposes of this subpart and section 936, in the case of any taxpayer who sustains an overall domestic loss for any taxable year beginning after December 31, 2006, that portion of the taxpayer’s taxable income from sources within the United States for each succeeding taxable year which is equal to the lesser of—

(A) the amount of such loss (to the extent not used under this paragraph in prior taxable years), or

(B) 50 percent of the taxpayer’s taxable income from sources within the United States for such succeeding taxable year,

shall be treated as income from sources without the United States (and not as income from sources within the United States).

(2) OVERALL DOMESTIC LOSS.—For purposes of this subsection—

(A) IN GENERAL.—The term “overall domestic loss” means—

(i) with respect to any qualified taxable year, the domestic loss for such taxable year to the extent such loss offsets taxable income from sources without the United States for the taxable year or for any preceding qualified taxable year by reason of a carryback, and

(ii) with respect to any other taxable year, the domestic loss for such taxable year to the extent such loss offsets taxable income from sources without the United States for any preceding qualified taxable year by reason of a carryback.

(B) DOMESTIC LOSS.—For purposes of subparagraph (A), the term “domestic loss” means the amount by which the gross income for the taxable year from sources within the United States is exceeded by the sum of the deductions properly apportioned or allocated thereto (determined without regard to any carryback from a subsequent taxable year).

(C) QUALIFIED TAXABLE YEAR.—For purposes of subparagraph (A), the term “qualified taxable year” means any taxable year for which the taxpayer chose the benefits of this subpart.

(3) CHARACTERIZATION OF SUBSEQUENT INCOME.—

(A) IN GENERAL.—Any income from sources within the United States that is treated as income from sources without the United States under paragraph (1) shall be allocated among and increase the income categories in proportion to the loss from sources within the United States previously allocated to those income categories.

(B) INCOME CATEGORY.—For purposes of this paragraph, the term “income category” has the meaning given such term by subsection (f)(5)(E)(i).

(4) COORDINATION WITH SUBSECTION (F).—The Secretary shall prescribe such regulations as may be necessary to coordinate the provisions of this subsection with the provisions of subsection (f).

(5) ELECTION TO INCREASE PERCENTAGE OF TAXABLE INCOME TREATED AS FOREIGN SOURCE.—

(A) IN GENERAL.—If any pre-2018 unused overall domestic loss is taken into account under paragraph (1) for any applicable taxable year, the taxpayer may elect to have such paragraph applied to such loss by substituting a percentage greater than 50 percent (but not greater than 100 percent) for 50 percent in subparagraph (B) thereof.

(B) PRE-2018 UNUSED OVERALL DOMESTIC LOSS.—For purposes of this paragraph, the term “pre-2018 unused overall domestic loss” means any overall domestic loss which—

(i) arises in a qualified taxable year beginning before January 1, 2018, and

(ii) has not been used under paragraph (1) for any taxable year beginning before such date.

(C) APPLICABLE TAXABLE YEAR.—For purposes of this paragraph, the term “applicable taxable year” means any

taxable year of the taxpayer beginning after December 31, 2017, and before January 1, 2028.

(h) SOURCE RULES IN CASE OF UNITED STATES-OWNED FOREIGN CORPORATIONS.—

(1) IN GENERAL.—The following amounts which are derived from a United States-owned foreign corporation and which would be treated as derived from sources outside the United States without regard to this subsection shall, for purposes of this section, be treated as derived from sources within the United States to the extent provided in this subsection:

(A) Any amount included in gross income under—

- (i) section 951(a) (relating to amounts included in gross income of United States shareholders), or
- (ii) section 1293 (relating to current taxation of income from qualified funds).

(B) Interest.

(C) Dividends.

(2) SUBPART F AND PASSIVE FOREIGN INVESTMENT COMPANY INCLUSIONS.—Any amount described in subparagraph (A) of paragraph (1) shall be treated as derived from sources within the United States to the extent such amount is attributable to income of the United States-owned foreign corporation from sources within the United States.

(3) CERTAIN INTEREST ALLOCABLE TO UNITED STATES SOURCE INCOME.—Any interest which—

(A) is paid or accrued by a United States-owned foreign corporation during any taxable year,

(B) is paid or accrued to a United States shareholder (as defined in section 951(b)) or a related person (within the meaning of section 267(b)) to such a shareholder, and

(C) is properly allocable (under regulations prescribed by the Secretary) to income of such foreign corporation for the taxable year from sources within the United States, shall be treated as derived from sources within the United States.

(4) DIVIDENDS.—

(A) IN GENERAL.—The United States source ratio of any dividend paid or accrued by a United States-owned foreign corporation shall be treated as derived from sources within the United States.

(B) UNITED STATES SOURCE RATIO.—For purposes of subparagraph (A), the term “United States source ratio” means, with respect to any dividend paid out of the earnings and profits for any taxable year, a fraction—

(i) the numerator of which is the portion of the earnings and profits for such taxable year from sources within the United States, and

(ii) the denominator of which is the total amount of earnings and profits for such taxable year.

(5) EXCEPTION WHERE UNITED STATES-OWNED FOREIGN CORPORATION HAS SMALL AMOUNT OF UNITED STATES SOURCE INCOME.—Paragraph (3) shall not apply to interest paid or accrued during any taxable year (and paragraph (4) shall not apply to any dividends paid out of the earnings and profits for such taxable year) if—

(A) the United States-owned foreign corporation has earnings and profits for such taxable year, and

(B) less than 10 percent of such earnings and profits is attributable to sources within the United States.

For purposes of the preceding sentence, earnings and profits shall be determined without any reduction for interest described in paragraph (3) (determined without regard to subparagraph (C) thereof).

(6) UNITED STATES-OWNED FOREIGN CORPORATION.—For purposes of this subsection, the term “United States-owned foreign corporation” means any foreign corporation if 50 percent or more of—

(A) the total combined voting power of all classes of stock of such corporation entitled to vote, or

(B) the total value of the stock of such corporation, is held directly (or indirectly through applying paragraphs (2) and (3) of section 958(a) and paragraph (4) of section 318(a)) by United States persons (as defined in section 7701(a)(30)).

(7) DIVIDEND.—For purposes of this subsection, the term “dividend” includes any gain treated as a dividend under section 1248.

(8) COORDINATION WITH SUBSECTION (F).—This subsection shall be applied before subsection (f).

(9) TREATMENT OF CERTAIN DOMESTIC CORPORATIONS.—In the case of any dividend treated as not from sources within the United States under section 861(a)(2)(A), the corporation paying such dividend shall be treated for purposes of this subsection as a United States-owned foreign corporation.

(10) COORDINATION WITH TREATIES.—

(A) IN GENERAL.—If—

(i) any amount derived from a United States-owned foreign corporation would be treated as derived from sources within the United States under this subsection by reason of an item of income of such United States-owned foreign corporation,

(ii) under a treaty obligation of the United States (applied without regard to this subsection and by treating any amount included in gross income under section 951(a)(1) as a dividend), such amount would be treated as arising from sources outside the United States, and

(iii) the taxpayer chooses the benefits of this paragraph, this subsection shall not apply to such amount to the extent attributable to such item of income (but subsections (a), (b), and (c) of this section and sections 907 and 960 shall be applied separately with respect to such amount to the extent so attributable).

(B) SPECIAL RULE.—Amounts included in gross income under section 951(a)(1) shall be treated as a dividend under subparagraph (A)(ii) only if dividends paid by each corporation (the stock in which is taken into account in determining whether the shareholder is a United States shareholder in the United States-owned foreign corporation), if paid to the United States shareholder, would be

treated under a treaty obligation of the United States as arising from sources outside the United States (applied without regard to this subsection).

(11) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate for purposes of this subsection, including—

(A) regulations for the application of this subsection in the case of interest or dividend payments through 1 or more entities, and

(B) regulations providing that this subsection shall apply to interest paid or accrued to any person (whether or not a United States shareholder).

(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.

(j) CERTAIN INDIVIDUALS EXEMPT.—

(1) IN GENERAL.—In the case of an individual to whom this subsection applies for any taxable year—

(A) the limitation of subsection (a) shall not apply,

(B) no taxes paid or accrued by the individual during such taxable year may be deemed paid or accrued under subsection (c) in any other taxable year, and

(C) no taxes paid or accrued by the individual during any other taxable year may be deemed paid or accrued under subsection (c) in such taxable year.

(2) INDIVIDUALS TO WHOM SUBSECTION APPLIES.—This subsection shall apply to an individual for any taxable year if—

(A) the entire amount of such individual's gross income for the taxable year from sources without the United States consists of qualified passive income,

(B) the amount of the creditable foreign taxes paid or accrued by the individual during the taxable year does not exceed \$300 (\$600 in the case of a joint return), and

(C) such individual elects to have this subsection apply for the taxable year.

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

(A) QUALIFIED PASSIVE INCOME.—The term “qualified passive income” means any item of gross income if—

(i) such item of income is passive income (as defined in subsection (d)(2)(B) without regard to clause (iii) thereof), and

(ii) such item of income is shown on a payee statement furnished to the individual.

(B) CREDITABLE FOREIGN TAXES.—The term “creditable foreign taxes” means any taxes for which a credit is allowable under section 901; except that such term shall not in-

clude any tax unless such tax is shown on a payee statement furnished to such individual.

(C) PAYEE STATEMENT.—The term “payee statement” has the meaning given to such term by section 6724(d)(2).

(D) ESTATES AND TRUSTS NOT ELIGIBLE.—This subsection shall not apply to any estate or trust.

(k) CROSS REFERENCES.—For increase of limitation under subsection (a) for taxes paid with respect to amounts received which were included in the gross income of the taxpayer for a prior taxable year as a United States shareholder with respect to a controlled foreign corporation, see section 960(c).

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**Subpart D—Possessions of the United States**

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**SEC. 931. INCOME FROM SOURCES WITHIN GUAM, AMERICAN SAMOA, OR THE NORTHERN MARIANA ISLANDS.**

(a) GENERAL RULE.—In the case of an individual who is a bona fide resident of a specified possession during the entire taxable year, gross income shall not include—

(1) income derived from sources within any specified possession, and

(2) income effectively connected with the conduct of a trade or business by such individual within any specified possession.

(b) DEDUCTIONS, ETC. ALLOCABLE TO EXCLUDED AMOUNTS NOT ALLOWABLE.—An individual shall not be allowed—

[(1) as a deduction from gross income any deductions (other than the deduction under section 151, relating to personal exemptions), or]

(1) *any deduction from gross income, or*

(2) any credit, properly allocable or chargeable against amounts excluded from gross income under this section.

(c) SPECIFIED POSSESSION.—For purposes of this section, the term “specified possession” means Guam, American Samoa, and the Northern Mariana Islands.

(d) EMPLOYEES OF THE UNITED STATES.—Amounts paid for services performed as an employee of the United States (or any agency thereof) shall be treated as not described in paragraph (1) or (2) of subsection (a).

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**SEC. 933. INCOME FROM SOURCES WITHIN PUERTO RICO.**

The following items shall not be included in gross income and shall be exempt from taxation under this subtitle:

(1) RESIDENT OF PUERTO RICO FOR ENTIRE TAXABLE YEAR.—

In the case of an individual who is a bona fide resident of Puerto Rico during the entire taxable year, income derived from sources within Puerto Rico (except amounts received for services performed as an employee of the United States or any agency thereof); but such individual shall not be allowed [as a deduction from his gross income any deductions (other than the deduction under section 151, relating to personal exemptions)] *any deduction from gross income, or any credit, prop-*

erly allocable to or chargeable against amounts excluded from gross income under this paragraph.

(2) TAXABLE YEAR OF CHANGE OF RESIDENCE FROM PUERTO RICO.—In the case of an individual citizen of the United States who has been a bona fide resident of Puerto Rico for a period of at least 2 years before the date on which he changes his residence from Puerto Rico, income derived from sources therein (except amounts received for services performed as an employee of the United States or any agency thereof) which is attributable to that part of such period of Puerto Rican residence before such date; but such individual shall not be allowed [as a deduction from his gross income any deductions (other than the deduction for personal exemptions under section 151)] *any deduction from gross income*, or any credit, properly allocable to or chargeable against amounts excluded from gross income under this paragraph.

## Subchapter P—Capital Gains and Losses

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### PART II—TREATMENT OF CAPITAL LOSSES

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#### SEC. 1212. CAPITAL LOSS CARRYBACKS AND CARRYOVERS.

##### (a) CORPORATIONS.—

(1) IN GENERAL.—If a corporation has a net capital loss for any taxable year (hereinafter in this paragraph referred to as the “loss year”), the amount thereof shall be—

(A) a capital loss carryback to each of the 3 taxable years preceding the loss year, but only to the extent—

(i) such loss is not attributable to a foreign expropriation capital loss, and

(ii) the carryback of such loss does not increase or produce a net operating loss (as defined in section 172(c)) for the taxable year to which it is being carried back;

(B) except as provided in subparagraph (C), a capital loss carryover to each of the 5 taxable years succeeding the loss year; and

(C) a capital loss carryover to each of the 10 taxable years succeeding the loss year, but only to the extent such loss is attributable to a foreign expropriation loss, and shall be treated as a short-term capital loss in each such taxable year. The entire amount of the net capital loss for any taxable year shall be carried to the earliest of the taxable years to which such loss may be carried, and the portion of such loss which shall be carried to each of the other taxable years to which such loss may be carried shall be the excess, if any, of such loss over the total of the capital gain net income for each of the prior taxable years to which such loss may be carried. For purposes of the preceding sentence, the capital gain net income for any such prior taxable year shall be computed without regard to the net capital loss for the loss year or for any taxable year thereafter. In the case of any net capital loss

which cannot be carried back in full to a preceding taxable year by reason of clause (ii) of subparagraph (A), the capital gain net income for such prior taxable year shall in no case be treated as greater than the amount of such loss which can be carried back to such preceding taxable year upon the application of such clause (ii).

(2) DEFINITIONS AND SPECIAL RULES.—

(A) FOREIGN EXPROPRIATION CAPITAL LOSS DEFINED.—For purposes of this subsection, the term “foreign expropriation capital loss” means, for any taxable year, the sum of the losses taken into account in computing the net capital loss for such year which are—

(i) losses sustained directly by reason of the expropriation, intervention, seizure, or similar taking of property by the government of any foreign country, any political subdivision thereof, or any agency or instrumentality of the foregoing, or

(ii) losses (treated under section 165(g)(1) as losses from the sale or exchange of capital assets) from securities which become worthless by reason of the expropriation, intervention, seizure, or similar taking of property by the government of any foreign country, any political subdivision thereof, or any agency or instrumentality of the foregoing.

(B) PORTION OF LOSS ATTRIBUTABLE TO FOREIGN EXPROPRIATION CAPITAL LOSS.—For purposes of paragraph (1), the portion of any net capital loss for any taxable year attributable to a foreign expropriation capital loss is the amount of the foreign expropriation capital loss for such year (but not in excess of the net capital loss for such year).

(C) PRIORITY OF APPLICATION.—For purposes of paragraph (1), if a portion of a net capital loss for any taxable year is attributable to a foreign expropriation capital loss, such portion shall be considered to be a separate net capital loss for such year to be applied after the other portion of such net capital loss.

(3) REGULATED INVESTMENT COMPANIES.—

(A) IN GENERAL.—If a regulated investment company has a net capital loss for any taxable year—

(i) paragraph (1) shall not apply to such loss,

(ii) the excess of the net short-term capital loss over the net long-term capital gain for such year shall be a short-term capital loss arising on the first day of the next taxable year, and

(iii) the excess of the net long-term capital loss over the net short-term capital gain for such year shall be a long-term capital loss arising on the first day of the next taxable year.

(B) COORDINATION WITH GENERAL RULE.—If a net capital loss to which paragraph (1) applies is carried over to a taxable year of a regulated investment company—

(i) LOSSES TO WHICH THIS PARAGRAPH APPLIES.—

Clauses (ii) and (iii) of subparagraph (A) shall be ap-



plied without regard to any amount treated as a short-term capital loss under paragraph (1).

(ii) LOSSES TO WHICH GENERAL RULE APPLIES.—Paragraph (1) shall be applied by substituting “net capital loss for the loss year or any taxable year thereafter (other than a net capital loss to which paragraph (3)(A) applies)” for “net capital loss for the loss year or any taxable year thereafter”.

(4) SPECIAL RULES ON CARRYBACKS.—A net capital loss of a corporation shall not be carried back under paragraph (1)(A) to a taxable year—

(A) for which it is a regulated investment company (as defined in section 851), or

(B) for which it is a real estate investment trust (as defined in section 856).

(b) OTHER TAXPAYERS.—

(1) IN GENERAL.—If a taxpayer other than a corporation has a net capital loss for any taxable year—

(A) the excess of the net short-term capital loss over the net long-term capital gain for such year shall be a short-term capital loss in the succeeding taxable year, and

(B) the excess of the net long-term capital loss over the net short-term capital gain for such year shall be a long-term capital loss in the succeeding taxable year.

(2) Treatment of amounts allowed under section 1211(b)(1) or (2)

(A) IN GENERAL.—For purposes of determining the excess referred to in subparagraph (A) or (B) of paragraph (1), there shall be treated as a short-term capital gain in the taxable year an amount equal to the lesser of—

(i) the amount allowed for the taxable year under paragraph (1) or (2) of section 1211(b), or

(ii) the adjusted taxable income for such taxable year.

(B) ADJUSTED TAXABLE INCOME.—For purposes of subparagraph (A), the term “adjusted taxable income” means taxable income increased by the sum of—

(i) the amount allowed for the taxable year under paragraph (1) or (2) of section 1211(b), and

[(ii) the deduction allowed for such year under section 151 or any deduction in lieu thereof.]

(ii) *in the case of an estate or trust, the deduction allowed for such year under section 642(b).*

For purposes of the preceding sentence, any excess of the deductions allowed for the taxable year over the gross income for such year shall be taken into account as negative taxable income.

(c) CARRYBACK OF LOSSES FROM SECTION 1256 CONTRACTS TO OFFSET PRIOR GAINS FROM SUCH CONTRACTS.—

(1) IN GENERAL.—If a taxpayer (other than a corporation) has a net section 1256 contracts loss for the taxable year and elects to have this subsection apply to such taxable year, the amount of such net section 1256 contracts loss—

(A) shall be a carryback to each of the 3 taxable years preceding the loss year, and

(B) to the extent that, after the application of paragraphs (2) and (3), such loss is allowed as a carryback to any such preceding taxable year—

(i) 40 percent of the amount so allowed shall be treated as a short-term capital loss from section 1256 contracts, and

(ii) 60 percent of the amount so allowed shall be treated as a long-term capital loss from section 1256 contracts.

(2) AMOUNT CARRIED TO EACH TAXABLE YEAR.—The entire amount of the net section 1256 contracts loss for any taxable year shall be carried to the earliest of the taxable years to which such loss may be carried back under paragraph (1). The portion of such loss which shall be carried to each of the 2 other taxable years to which such loss may be carried back shall be the excess (if any) of such loss over the portion of such loss which, after the application of paragraph (3), was allowed as a carryback for any prior taxable year.

(3) AMOUNT WHICH MAY BE USED IN ANY PRIOR TAXABLE YEAR.—An amount shall be allowed as a carryback under paragraph (1) to any prior taxable year only to the extent—

(A) such amount does not exceed the net section 1256 contract gain for such year, and

(B) the allowance of such carryback does not increase or produce a net operating loss (as defined in section 172(c)) for such year.

(4) NET SECTION 1256 CONTRACTS LOSS.—For purposes of paragraph (1), the term “net section 1256 contracts loss” means the lesser of—

(A) the net capital loss for the taxable year determined by taking into account only gains and losses from section 1256 contracts, or

(B) the sum of the amounts which, but for paragraph (6)(A), would be treated as capital losses in the succeeding taxable year under subparagraphs (A) and (B) of subsection (b)(1).

(5) NET SECTION 1256 CONTRACT GAIN.—For purposes of paragraph (1)—

(A) IN GENERAL.—The term “net section 1256 contract gain” means the lesser of—

(i) the capital gain net income for the taxable year determined by taking into account only gains and losses from section 1256 contracts, or

(ii) the capital gain net income for the taxable year.

(B) SPECIAL RULE.—The net section 1256 contract gain for any taxable year before the loss year shall be computed without regard to the net section 1256 contracts loss for the loss year or for any taxable year thereafter.

(6) Coordination with carryforward provisions of subsection (b)(1)

(A) CARRYFORWARD AMOUNT REDUCED BY AMOUNT USED AS CARRYBACK.—For purposes of applying subsection (b)(1), if any portion of the net section 1256 contracts loss for any taxable year is allowed as a carryback under paragraph (1) to any preceding taxable year—

(i) 40 percent of the amount allowed as a carryback shall be treated as a short-term capital gain for the loss year, and

(ii) 60 percent of the amount allowed as a carryback shall be treated as a long-term capital gain for the loss year.

(B) CARRYOVER LOSS RETAINS CHARACTER AS ATTRIBUTABLE TO SECTION 1256 CONTRACT.—Any amount carried forward as a short-term or long-term capital loss to any taxable year under subsection (b)(1) (after the application of subparagraph (A)) shall, to the extent attributable to losses from section 1256 contracts, be treated as loss from section 1256 contracts for such taxable year.

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

(A) SECTION 1256 CONTRACT.—The term “section 1256 contract” means any section 1256 contract (as defined in section 1256(b)) to which section 1256 applies.

(B) EXCLUSION FOR ESTATES AND TRUSTS.—This subsection shall not apply to any estate or trust.

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#### PART IV—SPECIAL RULES FOR DETERMINING CAPITAL GAINS AND LOSSES

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##### SEC. 1256. SECTION 1256 CONTRACTS MARKED TO MARKET.

(a) GENERAL RULE.—For purposes of this subtitle—

(1) each section 1256 contract held by the taxpayer at the close of the taxable year shall be treated as sold for its fair market value on the last business day of such taxable year (and any gain or loss shall be taken into account for the taxable year),

(2) proper adjustment shall be made in the amount of any gain or loss subsequently realized for gain or loss taken into account by reason of paragraph (1),

(3) any gain or loss with respect to a section 1256 contract shall be treated as—

(A) short-term capital gain or loss, to the extent of 40 percent of such gain or loss, and

(B) long-term capital gain or loss, to the extent of 60 percent of such gain or loss, and

(4) if all the offsetting positions making up any straddle consist of section 1256 contracts to which this section applies (and such straddle is not part of a larger straddle), sections 1092 and 263(g) shall not apply with respect to such straddle.

(b) SECTION 1256 CONTRACT DEFINED.—

(1) IN GENERAL.—For purposes of this section, the term “section 1256 contract” means—

(A) any regulated futures contract,

(B) any foreign currency contract,

(C) any nonequity option,

(D) any dealer equity option, and

(E) any dealer securities futures contract.

(2) EXCEPTIONS.—The term “section 1256 contract” shall not include—

(A) any securities futures contract or option on such a contract unless such contract or option is a dealer securities futures contract, or

(B) any interest rate swap, currency swap, basis swap, interest rate cap, interest rate floor, commodity swap, equity swap, equity index swap, credit default swap, or similar agreement.

(c) TERMINATIONS, ETC.—

(1) IN GENERAL.—The rules of paragraphs (1), (2), and (3) of subsection (a) shall also apply to the termination (or transfer) during the taxable year of the taxpayer’s obligation (or rights) with respect to a section 1256 contract by offsetting, by taking or making delivery, by exercise or being exercised, by assignment or being assigned, by lapse, or otherwise.

(2) SPECIAL RULE WHERE TAXPAYER TAKES DELIVERY ON OR EXERCISES PART OF STRADDLE.—If—

(A) 2 or more section 1256 contracts are part of a straddle (as defined in section 1092(c)), and

(B) the taxpayer takes delivery under or exercises any of such contracts,

then, for purposes of this section, each of the other such contracts shall be treated as terminated on the day on which the taxpayer took delivery.

(3) FAIR MARKET VALUE TAKEN INTO ACCOUNT.—For purposes of this subsection, fair market value at the time of the termination (or transfer) shall be taken into account.

(d) ELECTIONS WITH RESPECT TO MIXED STRADDLES.—

(1) ELECTION.—The taxpayer may elect to have this section not to apply to all section 1256 contracts which are part of a mixed straddle.

(2) TIME AND MANNER.—An election under paragraph (1) shall be made at such time and in such manner as the Secretary may by regulations prescribe.

(3) ELECTION REVOCABLE ONLY WITH CONSENT.—An election under paragraph (1) shall apply to the taxpayer’s taxable year for which made and to all subsequent taxable years, unless the Secretary consents to a revocation of such election.

(4) MIXED STRADDLE.—For purposes of this subsection, the term “mixed straddle” means any straddle (as defined in section 1092(c))—

(A) at least 1 (but not all) of the positions of which are section 1256 contracts, and

(B) with respect to which each position forming part of such straddle is clearly identified, before the close of the day on which the first section 1256 contract forming part of the straddle is acquired (or such earlier time as the Secretary may prescribe by regulations), as being part of such straddle.

(e) MARK TO MARKET NOT TO APPLY TO HEDGING TRANSACTIONS.—

(1) SECTION NOT TO APPLY.—Subsection (a) shall not apply in the case of a hedging transaction.

(2) DEFINITION OF HEDGING TRANSACTION.—For purposes of this subsection, the term “hedging transaction” means any

hedging transaction (as defined in section 1221(b)(2)(A)) if, before the close of the day on which such transaction was entered into (or such earlier time as the Secretary may prescribe by regulations), the taxpayer clearly identifies such transaction as being a hedging transaction.

(3) SPECIAL RULE FOR SYNDICATES.—

(A) IN GENERAL.—Notwithstanding paragraph (2), the term “hedging transaction” shall not include any transaction entered into by or for a syndicate.

(B) SYNDICATE DEFINED.—For purposes of subparagraph (A), the term “syndicate” means any partnership or other entity (other than a corporation which is not an S corporation) if more than 35 percent of the losses of such entity during the taxable year are allocable to limited partners or limited entrepreneurs (within the meaning of [section 461(k)(4)] *section 461(j)(4)*).

(C) HOLDINGS ATTRIBUTABLE TO ACTIVE MANAGEMENT.—For purposes of subparagraph (B), an interest in an entity shall not be treated as held by a limited partner or a limited entrepreneur (within the meaning of [section 461(k)(4)] *section 461(j)(4)*)—

(i) for any period if during such period such interest is held by an individual who actively participates at all times during such period in the management of such entity,

(ii) for any period if during such period such interest is held by the spouse, children, grandchildren, and parents of an individual who actively participates at all times during such period in the management of such entity,

(iii) if such interest is held by an individual who actively participated in the management of such entity for a period of not less than 5 years,

(iv) if such interest is held by the estate of an individual who actively participated in the management of such entity or is held by the estate of an individual if with respect to such individual such interest was at any time described in clause (ii), or

(v) if the Secretary determines (by regulations or otherwise) that such interest should be treated as held by an individual who actively participates in the management of such entity, and that such entity and such interest are not used (or to be used) for tax-avoidance purposes.

For purposes of this subparagraph, a legally adopted child of an individual shall be treated as a child of such individual by blood.

(4) LIMITATION ON LOSSES FROM HEDGING TRANSACTIONS.—

(A) IN GENERAL.—

(i) LIMITATION.—Any hedging loss for a taxable year which is allocable to any limited partner or limited entrepreneur (within the meaning of paragraph (3)) shall be allowed only to the extent of the taxable income of such limited partner or entrepreneur for such taxable year attributable to the trade or business in which the

hedging transactions were entered into. For purposes of the preceding sentence, taxable income shall be determined by not taking into account items attributable to hedging transactions.

(ii) CARRYOVER OF DISALLOWED LOSS.—Any hedging loss disallowed under clause (i) shall be treated as a deduction attributable to a hedging transaction allowable in the first succeeding taxable year.

(B) EXCEPTION WHERE ECONOMIC LOSS.—Subparagraph (A)(i) shall not apply to any hedging loss to the extent that such loss exceeds the aggregate unrecognized gains from hedging transactions as of the close of the taxable year attributable to the trade or business in which the hedging transactions were entered into.

(C) EXCEPTION FOR CERTAIN HEDGING TRANSACTIONS.—In the case of any hedging transaction relating to property other than stock or securities, this paragraph shall apply only in the case of a taxpayer described in section 465(a)(1).

(D) HEDGING LOSS.—The term “hedging loss” means the excess of—

(i) the deductions allowable under this chapter for the taxable year attributable to hedging transactions (determined without regard to subparagraph (A)(i)), over

(ii) income received or accrued by the taxpayer during such taxable year from such transactions.

(E) UNRECOGNIZED GAIN.—The term “unrecognized gain” has the meaning given to such term by section 1092(a)(3).

(f) SPECIAL RULES.—

(1) DENIAL OF CAPITAL GAINS TREATMENT FOR PROPERTY IDENTIFIED AS PART OF A HEDGING TRANSACTION.—For purposes of this title, gain from any property shall in no event be considered as gain from the sale or exchange of a capital asset if such property was at any time personal property (as defined in section 1092(d)(1)) identified under subsection (e)(2) by the taxpayer as being part of a hedging transaction.

(2) SUBSECTION (A)(3) NOT TO APPLY TO ORDINARY INCOME PROPERTY.—Paragraph (3) of subsection (a) shall not apply to any gain or loss which, but for such paragraph, would be ordinary income or loss.

(3) CAPITAL GAIN TREATMENT FOR TRADERS IN SECTION 1256 CONTRACTS.—

(A) IN GENERAL.—For purposes of this title, gain or loss from trading of section 1256 contracts shall be treated as gain or loss from the sale or exchange of a capital asset.

(B) EXCEPTION FOR CERTAIN HEDGING TRANSACTIONS.—Subparagraph (A) shall not apply to any section 1256 contract to the extent such contract is held for purposes of hedging property if any loss with respect to such property in the hands of the taxpayer would be ordinary loss.

(C) TREATMENT OF UNDERLYING PROPERTY.—For purposes of determining whether gain or loss with respect to any property is ordinary income or loss, the fact that the taxpayer is actively engaged in dealing in or trading sec-

tion 1256 contracts related to such property shall not be taken into account.

(4) SPECIAL RULE FOR DEALER EQUITY OPTIONS AND DEALER SECURITIES FUTURES CONTRACTS OF LIMITED PARTNERS OR LIMITED ENTREPRENEURS.—In the case of any gain or loss with respect to dealer equity options, or dealer securities futures contracts, which are allocable to limited partners or limited entrepreneurs (within the meaning of subsection (e)(3))—

(A) paragraph (3) of subsection (a) shall not apply to any such gain or loss, and

(B) all such gains or losses shall be treated as short-term capital gains or losses, as the case may be.

(5) SPECIAL RULE RELATED TO LOSSES.—Section 1091 (relating to loss from wash sales of stock or securities) shall not apply to any loss taken into account by reason of paragraph (1) of subsection (a).

(g) DEFINITIONS.—For purposes of this section—

(1) REGULATED FUTURES CONTRACTS DEFINED.—The term “regulated futures contract” means a contract—

(A) with respect to which the amount required to be deposited and the amount which may be withdrawn depends on a system of marking to market, and

(B) which is traded on or subject to the rules of a qualified board or exchange.

(2) FOREIGN CURRENCY CONTRACT DEFINED.—

(A) FOREIGN CURRENCY CONTRACT.—The term “foreign currency contract” means a contract—

(i) which requires delivery of, or the settlement of which depends on the value of, a foreign currency which is a currency in which positions are also traded through regulated futures contracts,

(ii) which is traded in the interbank market, and

(iii) which is entered into at arm’s length at a price determined by reference to the price in the interbank market.

(B) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of subparagraph (A), including regulations excluding from the application of subparagraph (A) any contract (or type of contract) if its application thereto would be inconsistent with such purposes.

(3) NONEQUITY OPTION.—The term “nonequity option” means any listed option which is not an equity option.

(4) DEALER EQUITY OPTION.—The term “dealer equity option” means, with respect to an options dealer, any listed option which—

(A) is an equity option,

(B) is purchased or granted by such options dealer in the normal course of his activity of dealing in options, and

(C) is listed on the qualified board or exchange on which such options dealer is registered.

(5) LISTED OPTION.—The term “listed option” means any option (other than a right to acquire stock from the issuer) which is traded on (or subject to the rules of) a qualified board or exchange.

(6) EQUITY OPTION.—The term “equity option” means any option—

(A) to buy or sell stock, or

(B) the value of which is determined directly or indirectly by reference to any stock or any narrow-based security index (as defined in section 3(a)(55) of the Securities Exchange Act of 1934, as in effect on the date of the enactment of this paragraph).

The term “equity option” includes such an option on a group of stocks only if such group meets the requirements for a narrow-based security index (as so defined). The Secretary may prescribe regulations regarding the status of options the values of which are determined directly or indirectly by reference to any index which becomes (or ceases to be) a narrow-based security index (as so defined).

(7) QUALIFIED BOARD OR EXCHANGE.—The term “qualified board or exchange” means—

(A) a national securities exchange which is registered with the Securities and Exchange Commission,

(B) a domestic board of trade designated as a contract market by the Commodity Futures Trading Commission, or

(C) any other exchange, board of trade, or other market which the Secretary determines has rules adequate to carry out the purposes of this section.

(8) OPTIONS DEALER.—

(A) IN GENERAL.—The term “options dealer” means any person registered with an appropriate national securities exchange as a market maker or specialist in listed options.

(B) PERSONS TRADING IN OTHER MARKETS.—In any case in which the Secretary makes a determination under subparagraph (C) of paragraph (7), the term “options dealer” also includes any person whom the Secretary determines performs functions similar to the persons described in subparagraph (A). Such determinations shall be made to the extent appropriate to carry out the purposes of this section.

(9) DEALER SECURITIES FUTURES CONTRACT.—

(A) IN GENERAL.—The term “dealer securities futures contract” means, with respect to any dealer, any securities futures contract, and any option on such a contract, which—

(i) is entered into by such dealer (or, in the case of an option, is purchased or granted by such dealer) in the normal course of his activity of dealing in such contracts or options, as the case may be, and

(ii) is traded on a qualified board or exchange.

(B) DEALER.—For purposes of subparagraph (A), a person shall be treated as a dealer in securities futures contracts or options on such contracts if the Secretary determines that such person performs, with respect to such contracts or options, as the case may be, functions similar to the functions performed by persons described in paragraph (8)(A). Such determination shall be made to the extent appropriate to carry out the purposes of this section.



(C) SECURITIES FUTURES CONTRACT.—The term “securities futures contract” has the meaning given to such term by section 1234B.

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## Subchapter S—Tax Treatment of S Corporations and Their Shareholders

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### PART I—IN GENERAL

\* \* \* \* \*

#### SEC. 1361. S CORPORATION DEFINED.

(a) S CORPORATION DEFINED.—

(1) IN GENERAL.—For purposes of this title, the term “S corporation” means, with respect to any taxable year, a small business corporation for which an election under section 1362(a) is in effect for such year.

(2) C CORPORATION.—For purposes of this title, the term “C corporation” means, with respect to any taxable year, a corporation which is not an S corporation for such year.

(b) SMALL BUSINESS CORPORATION.—

(1) IN GENERAL.—For purposes of this subchapter, the term “small business corporation” means a domestic corporation which is not an ineligible corporation and which does not—

(A) have more than 100 shareholders,

(B) have as a shareholder a person (other than an estate, a trust described in subsection (c)(2), or an organization described in subsection (c)(6)) who is not an individual,

(C) have a nonresident alien as a shareholder, and

(D) have more than 1 class of stock.

(2) INELIGIBLE CORPORATION DEFINED.—For purposes of paragraph (1), the term “ineligible corporation” means any corporation which is—

(A) a financial institution which uses the reserve method of accounting for bad debts described in section 585,

(B) an insurance company subject to tax under subchapter L, or

(C) a DISC or former DISC.

(3) TREATMENT OF CERTAIN WHOLLY OWNED SUBSIDIARIES.—

(A) IN GENERAL.—Except as provided in regulations prescribed by the Secretary, for purposes of this title—

(i) a corporation which is a qualified subchapter S subsidiary shall not be treated as a separate corporation, and

(ii) all assets, liabilities, and items of income, deduction, and credit of a qualified subchapter S subsidiary shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

(B) QUALIFIED SUBCHAPTER S SUBSIDIARY.—For purposes of this paragraph, the term “qualified subchapter S sub-

sidiary” means any domestic corporation which is not an ineligible corporation (as defined in paragraph (2)), if—

- (i) 100 percent of the stock of such corporation is held by the S corporation, and
- (ii) the S corporation elects to treat such corporation as a qualified subchapter S subsidiary.

(C) TREATMENT OF TERMINATIONS OF QUALIFIED SUBCHAPTER S SUBSIDIARY STATUS.—

(i) IN GENERAL.—For purposes of this title, if any corporation which was a qualified subchapter S subsidiary ceases to meet the requirements of subparagraph (B), such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the S corporation in exchange for its stock.

(ii) TERMINATION BY REASON OF SALE OF STOCK.—If the failure to meet the requirements of subparagraph (B) is by reason of the sale of stock of a corporation which is a qualified subchapter S subsidiary, the sale of such stock shall be treated as if—

(I) the sale were a sale of an undivided interest in the assets of such corporation (based on the percentage of the corporation’s stock sold), and

(II) the sale were followed by an acquisition by such corporation of all of its assets (and the assumption by such corporation of all of its liabilities) in a transaction to which section 351 applies.

(D) ELECTION AFTER TERMINATION.—If a corporation’s status as a qualified subchapter S subsidiary terminates, such corporation (and any successor corporation) shall not be eligible to make—

- (i) an election under subparagraph (B)(ii) to be treated as a qualified subchapter S subsidiary, or
- (ii) an election under section 1362(a) to be treated as an S corporation,

before its 5th taxable year which begins after the 1st taxable year for which such termination was effective, unless the Secretary consents to such election.

(E) INFORMATION RETURNS.—Except to the extent provided by the Secretary, this paragraph shall not apply to part III of subchapter A of chapter 61 (relating to information returns).

(c) SPECIAL RULES FOR APPLYING SUBSECTION (B).—

(1) MEMBERS OF A FAMILY TREATED AS 1 SHAREHOLDER.—

(A) IN GENERAL.—For purposes of subsection (b)(1)(A), there shall be treated as one shareholder—

- (i) a husband and wife (and their estates), and
- (ii) all members of a family (and their estates).

(B) MEMBERS OF A FAMILY.—For purposes of this paragraph—

- (i) IN GENERAL.—The term “members of a family” means a common ancestor, any lineal descendant of such common ancestor, and any spouse or former

spouse of such common ancestor or any such lineal descendant.

(ii) COMMON ANCESTOR.—An individual shall not be considered to be a common ancestor if, on the applicable date, the individual is more than 6 generations removed from the youngest generation of shareholders who would (but for this subparagraph) be members of the family. For purposes of the preceding sentence, a spouse (or former spouse) shall be treated as being of the same generation as the individual to whom such spouse is (or was) married.

(iii) APPLICABLE DATE.—The term “applicable date” means the latest of—

(I) the date the election under section 1362(a) is made,

(II) the earliest date that an individual described in clause (i) holds stock in the S corporation, or

(III) October 22, 2004.

(C) EFFECT OF ADOPTION, ETC.—Any legally adopted child of an individual, any child who is lawfully placed with an individual for legal adoption by the individual, and any eligible foster child of an individual (within the meaning of [section 152(f)(1)(C)] *section 7706(f)(1)(C)*), shall be treated as a child of such individual by blood.

(2) CERTAIN TRUSTS PERMITTED AS SHAREHOLDERS.—

(A) IN GENERAL.—For purposes of subsection (b)(1)(B), the following trusts may be shareholders:

(i) A trust all of which is treated (under subpart E of part I of subchapter J of this chapter) as owned by an individual who is a citizen or resident of the United States.

(ii) A trust which was described in clause (i) immediately before the death of the deemed owner and which continues in existence after such death, but only for the 2-year period beginning on the day of the deemed owner’s death.

(iii) A trust with respect to stock transferred to it pursuant to the terms of a will, but only for the 2-year period beginning on the day on which such stock is transferred to it.

(iv) A trust created primarily to exercise the voting power of stock transferred to it.

(v) An electing small business trust.

(vi) In the case of a corporation which is a bank (as defined in section 581) or a depository institution holding company (as defined in section 3(w)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1813(w)(1)), a trust which constitutes an individual retirement account under section 408(a), including one designated as a Roth IRA under section 408A, but only to the extent of the stock held by such trust in such bank or company as of the date of the enactment of this clause.

This subparagraph shall not apply to any foreign trust.

(B) TREATMENT AS SHAREHOLDERS.—For purposes of subsection (b)(1)—

(i) In the case of a trust described in clause (i) of subparagraph (A), the deemed owner shall be treated as the shareholder.

(ii) In the case of a trust described in clause (ii) of subparagraph (A), the estate of the deemed owner shall be treated as the shareholder.

(iii) In the case of a trust described in clause (iii) of subparagraph (A), the estate of the testator shall be treated as the shareholder.

(iv) In the case of a trust described in clause (iv) of subparagraph (A), each beneficiary of the trust shall be treated as a shareholder.

(v) In the case of a trust described in clause (v) of subparagraph (A), each potential current beneficiary of such trust shall be treated as a shareholder; except that, if for any period there is no potential current beneficiary of such trust, such trust shall be treated as the shareholder during such period. This clause shall not apply for purposes of subsection (b)(1)(C).

(vi) In the case of a trust described in clause (vi) of subparagraph (A), the individual for whose benefit the trust was created shall be treated as the shareholder.

(3) ESTATE OF INDIVIDUAL IN BANKRUPTCY MAY BE SHAREHOLDER.—For purposes of subsection (b)(1)(B), the term “estate” includes the estate of an individual in a case under title 11 of the United States Code.

(4) DIFFERENCES IN COMMON STOCK VOTING RIGHTS DISREGARDED.—For purposes of subsection (b)(1)(D), a corporation shall not be treated as having more than 1 class of stock solely because there are differences in voting rights among the shares of common stock.

(5) STRAIGHT DEBT SAFE HARBOR.—

(A) IN GENERAL.—For purposes of subsection (b)(1)(D), straight debt shall not be treated as a second class of stock.

(B) STRAIGHT DEBT DEFINED.—For purposes of this paragraph, the term “straight debt” means any written unconditional promise to pay on demand or on a specified date a sum certain in money if—

(i) the interest rate (and interest payment dates) are not contingent on profits, the borrower’s discretion, or similar factors,

(ii) there is no convertibility (directly or indirectly) into stock, and

(iii) the creditor is an individual (other than a non-resident alien), an estate, a trust described in paragraph (2), or a person which is actively and regularly engaged in the business of lending money.

(C) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to provide for the proper treatment of straight debt under this subchapter and for the coordination of such treatment with other provisions of this title.

(6) CERTAIN EXEMPT ORGANIZATIONS PERMITTED AS SHAREHOLDERS.—For purposes of subsection (b)(1)(B), an organization which is—

- (A) described in section 401(a) or 501(c)(3), and
- (B) exempt from taxation under section 501(a), may be a shareholder in an S corporation.

(d) SPECIAL RULE FOR QUALIFIED SUBCHAPTER S TRUST.—

(1) IN GENERAL.—In the case of a qualified subchapter S trust with respect to which a beneficiary makes an election under paragraph (2)—

(A) such trust shall be treated as a trust described in subsection (c)(2)(A)(i),

(B) for purposes of section 678(a), the beneficiary of such trust shall be treated as the owner of that portion of the trust which consists of stock in an S corporation with respect to which the election under paragraph (2) is made, and

(C) for purposes of applying sections 465 and 469 to the beneficiary of the trust, the disposition of the S corporation stock by the trust shall be treated as a disposition by such beneficiary.

(2) ELECTION.—

(A) IN GENERAL.—A beneficiary of a qualified subchapter S trust (or his legal representative) may elect to have this subsection apply.

(B) MANNER AND TIME OF ELECTION.—

(i) SEPARATE ELECTION WITH RESPECT TO EACH CORPORATION.—An election under this paragraph shall be made separately with respect to each corporation the stock of which is held by the trust.

(ii) ELECTIONS WITH RESPECT TO SUCCESSIVE INCOME BENEFICIARIES.—If there is an election under this paragraph with respect to any beneficiary, an election under this paragraph shall be treated as made by each successive beneficiary unless such beneficiary affirmatively refuses to consent to such election.

(iii) TIME, MANNER, AND FORM OF ELECTION.—Any election, or refusal, under this paragraph shall be made in such manner and form, and at such time, as the Secretary may prescribe.

(C) ELECTION IRREVOCABLE.—An election under this paragraph, once made, may be revoked only with the consent of the Secretary.

(D) GRACE PERIOD.—An election under this paragraph shall be effective up to 15 days and 2 months before the date of the election.

(3) QUALIFIED SUBCHAPTER S TRUST.—For purposes of this subsection, the term “qualified subchapter S trust” means a trust—

(A) the terms of which require that—

(i) during the life of the current income beneficiary, there shall be only 1 income beneficiary of the trust,

(ii) any corpus distributed during the life of the current income beneficiary may be distributed only to such beneficiary,

(iii) the income interest of the current income beneficiary in the trust shall terminate on the earlier of such beneficiary's death or the termination of the trust, and

(iv) upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to such beneficiary, and

(B) all of the income (within the meaning of section 643(b)) of which is distributed (or required to be distributed) currently to 1 individual who is a citizen or resident of the United States.

A substantially separate and independent share of a trust within the meaning of section 663(c) shall be treated as a separate trust for purposes of this subsection and subsection (c).

(4) TRUST CEASING TO BE QUALIFIED.—

(A) FAILURE TO MEET REQUIREMENTS OF PARAGRAPH (3)(A).—If a qualified subchapter S trust ceases to meet any requirement of paragraph (3)(A), the provisions of this subsection shall not apply to such trust as of the date it ceases to meet such requirement.

(B) FAILURE TO MEET REQUIREMENTS OF PARAGRAPH (3)(B).—If any qualified subchapter S trust ceases to meet any requirement of paragraph (3)(B) but continues to meet the requirements of paragraph (3)(A), the provisions of this subsection shall not apply to such trust as of the first day of the first taxable year beginning after the first taxable year for which it failed to meet the requirements of paragraph (3)(B).

(e) ELECTING SMALL BUSINESS TRUST DEFINED.—

(1) ELECTING SMALL BUSINESS TRUST.—For purposes of this section—

(A) IN GENERAL.—Except as provided in subparagraph (B), the term “electing small business trust” means any trust if—

(i) such trust does not have as a beneficiary any person other than (I) an individual, (II) an estate, (III) an organization described in paragraph (2), (3), (4), or (5) of section 170(c), or (IV) an organization described in section 170(c)(1) which holds a contingent interest in such trust and is not a potential current beneficiary,

(ii) no interest in such trust was acquired by purchase, and

(iii) an election under this subsection applies to such trust.

(B) CERTAIN TRUSTS NOT ELIGIBLE.—The term “electing small business trust” shall not include—

(i) any qualified subchapter S trust (as defined in subsection (d)(3)) if an election under subsection (d)(2) applies to any corporation the stock of which is held by such trust,

(ii) any trust exempt from tax under this subtitle, and

(iii) any charitable remainder annuity trust or charitable remainder unitrust (as defined in section 664(d)).

(C) PURCHASE.—For purposes of subparagraph (A), the term “purchase” means any acquisition if the basis of the property acquired is determined under section 1012.

(2) POTENTIAL CURRENT BENEFICIARY.—For purposes of this section, the term “potential current beneficiary” means, with respect to any period, any person who at any time during such period is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust (determined without regard to any power of appointment to the extent such power remains unexercised at the end of such period). If a trust disposes of all of the stock which it holds in an S corporation, then, with respect to such corporation, the term “potential current beneficiary” does not include any person who first met the requirements of the preceding sentence during the 1-year period ending on the date of such disposition.

(3) ELECTION.—An election under this subsection shall be made by the trustee. Any such election shall apply to the taxable year of the trust for which made and all subsequent taxable years of such trust unless revoked with the consent of the Secretary.

(4) CROSS REFERENCE.—For special treatment of electing small business trusts, see section 641(c).

(f) RESTRICTED BANK DIRECTOR STOCK.—

(1) IN GENERAL.—Restricted bank director stock shall not be taken into account as outstanding stock of the S corporation in applying this subchapter (other than section 1368(f)).

(2) RESTRICTED BANK DIRECTOR STOCK.—For purposes of this subsection, the term “restricted bank director stock” means stock in a bank (as defined in section 581) or a depository institution holding company (as defined in section 3(w)(1) of the Federal Deposit Insurance Act (12 U.S.C. 1813(w)(1))), if such stock—

(A) is required to be held by an individual under applicable Federal or State law in order to permit such individual to serve as a director, and

(B) is subject to an agreement with such bank or company (or a corporation which controls (within the meaning of section 368(c)) such bank or company) pursuant to which the holder is required to sell back such stock (at the same price as the individual acquired such stock) upon ceasing to hold the office of director.

(3) CROSS REFERENCE.—For treatment of certain distributions with respect to restricted bank director stock, see section 1368(f).

(g) SPECIAL RULE FOR BANK REQUIRED TO CHANGE FROM THE RESERVE METHOD OF ACCOUNTING ON BECOMING S CORPORATION.—In the case of a bank which changes from the reserve method of accounting for bad debts described in section 585 or 593 for its first taxable year for which an election under section 1362(a) is in effect, the bank may elect to take into account any adjustments under section 481 by reason of such change for the taxable year immediately preceding such first taxable year.

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## CHAPTER 2—TAX ON SELF-EMPLOYMENT INCOME

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### SEC. 1402. DEFINITIONS.

(a) **NET EARNINGS FROM SELF-EMPLOYMENT.**—The term “net earnings from self-employment” means the gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed by this subtitle which are attributable to such trade or business, plus his distributive share (whether or not distributed) of income or loss described in section 702(a)(8) from any trade or business carried on by a partnership of which he is a member; except that in computing such gross income and deductions and such distributive share of partnership ordinary income or loss—

(1) there shall be excluded rentals from real estate and from personal property leased with the real estate (including such rentals paid in crop shares, and including payments under section 1233(a)(2) of the Food Security Act of 1985 (16 U.S.C. 3833(a)(2)) to individuals receiving benefits under section 202 or 223 of the Social Security Act) together with the deductions attributable thereto, unless such rentals are received in the course of a trade or business as a real estate dealer; except that the preceding provisions of this paragraph shall not apply to any income derived by the owner or tenant of land if (A) such income is derived under an arrangement, between the owner or tenant and another individual, which provides that such other individual shall produce agricultural or horticultural commodities (including livestock, bees, poultry, and fur-bearing animals and wildlife) on such land, and that there shall be material participation by the owner or tenant (as determined without regard to any activities of an agent of such owner or tenant) in the production or the management of the production of such agricultural or horticultural commodities, and (B) there is material participation by the owner or tenant (as determined without regard to any activities of an agent of such owner or tenant) with respect to any such agricultural or horticultural commodity;

(2) there shall be excluded dividends on any share of stock, and interest on any bond, debenture, note, or certificate, or other evidence of indebtedness, issued with interest coupons or in registered form by any corporation (including one issued by a government or political subdivision thereof), unless such dividends and interest are received in the course of a trade or business as a dealer in stocks or securities;

(3) there shall be excluded any gain or loss—

(A) which is considered as gain or loss from the sale or exchange of a capital asset,

(B) from the cutting of timber, or the disposal of timber, coal, or iron ore, if section 631 applies to such gain or loss, or

(C) from the sale, exchange, involuntary conversion, or other disposition of property if such property is neither—



- (i) stock in trade or other property of a kind which would properly be includible in inventory if on hand at the close of the taxable year, nor
  - (ii) property held primarily for sale to customers in the ordinary course of the trade or business;
- (4) the deduction for net operating losses provided in section 172 shall not be allowed;
- (5) if—
  - (A) any of the income derived from a trade or business (other than a trade or business carried on by a partnership) is community income under community property laws applicable to such income, the gross income and deductions attributable to such trade or business shall be treated as the gross income and deductions of the spouse carrying on such trade or business or, if such trade or business is jointly operated, treated as the gross income and deductions of each spouse on the basis of their respective distributive share of the gross income and deductions; and
  - (B) any portion of a partner's distributive share of the ordinary income or loss from a trade or business carried on by a partnership is community income or loss under the community property laws applicable to such share, all of such distributive share shall be included in computing the net earnings from self-employment of such partner, and no part of such share shall be taken into account in computing the net earnings from self-employment of the spouse of such partner;
- (6) a resident of Puerto Rico shall compute his net earnings from self-employment in the same manner as a citizen of the United States but without regard to section 933;
- [(7) the deduction for personal exemptions provided in section 151 shall not be allowed;]
- (8) an individual who is a duly ordained, commissioned, or licensed minister of a church or a member of a religious order shall compute his net earnings from self-employment derived from the performance of service described in subsection (c)(4) without regard to section 107 (relating to rental value of parsonages), section 119 (relating to meals and lodging furnished for the convenience of the employer), and section 911 (relating to citizens or residents of the United States living abroad), but shall not include in such net earnings from self-employment the rental value of any parsonage or any parsonage allowance (whether or not excludable under section 107) provided after the individual retires, or any other retirement benefit received by such individual from a church plan (as defined in section 414(e)) after the individual retires;
- (9) the exclusion from gross income provided by section 931 shall not apply;
- (10) there shall be excluded amounts received by a partner pursuant to a written plan of the partnership, which meets such requirements as are prescribed by the Secretary, and which provides for payments on account of retirement, on a periodic basis, to partners generally or to a class or classes of

partners, such payments to continue at least until such partner's death, if—

(A) such partner rendered no services with respect to any trade or business carried on by such partnership (or its successors) during the taxable year of such partnership (or its successors), ending within or with his taxable year, in which such amounts were received, and

(B) no obligation exists (as of the close of the partnership's taxable year referred to in subparagraph (A)) from the other partners to such partner except with respect to retirement payments under such plan, and

(C) such partner's share, if any, of the capital of the partnership has been paid to him in full before the close of the partnership's taxable year referred to in subparagraph (A);

(11) the exclusion from gross income provided by section 911(a)(1) shall not apply;

(12) in lieu of the deduction provided by section 164(f) (relating to deduction for one-half of self-employment taxes), there shall be allowed a deduction equal to the product of—

(A) the taxpayer's net earnings from self-employment for the taxable year (determined without regard to this paragraph), and

(B) one-half of the sum of the rates imposed by subsections (a) and (b) of section 1401 for such year (determined without regard to the rate imposed under paragraph (2) of section 1401(b));

(13) there shall be excluded the distributive share of any item of income or loss of a limited partner, as such, other than guaranteed payments described in section 707(c) to that partner for services actually rendered to or on behalf of the partnership to the extent that those payments are established to be in the nature of remuneration for those services;

(14) in the case of church employee income, the special rules of subsection (j)(1) shall apply;

(15) in the case of a member of an Indian tribe, the special rules of section 7873 (relating to income derived by Indians from exercise of fishing rights) shall apply;

(16) the deduction provided by section 199 shall not be allowed; and

(17) notwithstanding the preceding provisions of this subsection, each spouse's share of income or loss from a qualified joint venture shall be taken into account as provided in section 761(f) in determining net earnings from self-employment of such spouse.

If the taxable year of a partner is different from that of the partnership, the distributive share which he is required to include in computing his net earnings from self-employment shall be based on the ordinary income or loss of the partnership for any taxable year of the partnership ending within or with his taxable year. In the case of any trade or business which is carried on by an individual or by a partnership and in which, if such trade or business were carried on exclusively by employees, the major portion of the services would constitute agricultural labor as defined in section 3121(g)—

(i) in the case of an individual, if the gross income derived by him from such trade or business is not more than the upper limit, the net earnings from self-employment derived by him from such trade or business may, at his option, be deemed to be  $66 \frac{2}{3}$  percent of such gross income; or

(ii) in the case of an individual, if the gross income derived by him from such trade or business is more than the upper limit and the net earnings from self-employment derived by him from such trade or business (computed under this subsection without regard to this sentence) are less than the lower limit, the net earnings from self-employment derived by him from such trade or business may, at his option, be deemed to be the lower limit; and

(iii) in the case of a member of a partnership, if his distributive share of the gross income of the partnership derived from such trade or business (after such gross income has been reduced by the sum of all payments to which section 707(c) applies) is not more than the upper limit, his distributive share of income described in section 702(a)(8) derived from such trade or business may, at his option, be deemed to be an amount equal to  $66 \frac{2}{3}$  percent of his distributive share of such gross income (after such gross income has been so reduced); or

(iv) in the case of a member of a partnership, if his distributive share of the gross income of the partnership derived from such trade or business (after such gross income has been reduced by the sum of all payments to which section 707(c) applies) is more than the upper limit and his distributive share (whether or not distributed) of income described in section 702(a)(8) derived from such trade or business (computed under this subsection without regard to this sentence) is less than the lower limit, his distributive share of income described in section 702(a)(8) derived from such trade or business may, at his option, be deemed to be the lower limit.

For purposes of the preceding sentence, gross income means—

(v) in the case of any such trade or business in which the income is computed under a cash receipts and disbursements method, the gross receipts from such trade or business reduced by the cost or other basis of property which was purchased and sold in carrying on such trade or business, adjusted (after such reduction) in accordance with the provisions of paragraphs (1) through (7) and paragraph (9) of this subsection; and

(vi) in the case of any such trade or business in which the income is computed under an accrual method, the gross income from such trade or business, ad-

justed in accordance with the provisions of paragraphs (1) through (7) and paragraph (9) of this subsection; and, for purposes of such sentence, if an individual (including a member of a partnership) derives gross income from more than one such trade or business, such gross income (including his distributive share of the gross income of any partnership derived from any such trade or business) shall be deemed to have been derived from one trade or business.

The preceding sentence and clauses (i) through (iv) of the second preceding sentence shall also apply in the case of any trade or business (other than a trade or business specified in such second preceding sentence) which is carried on by an individual who is self-employed on a regular basis as defined in subsection (h), or by a partnership of which an individual is a member on a regular basis as defined in subsection (h), but only if such individual's net earnings from self-employment as determined without regard to this sentence in the taxable year are less than the lower limit and less than  $66 \frac{2}{3}$  percent of the sum (in such taxable year) of such individual's gross income derived from all trades or businesses carried on by him and his distributive share of the income or loss from all trades or businesses carried on by all the partnerships of which he is a member; except that this sentence shall not apply to more than 5 taxable years in the case of any individual, and in no case in which an individual elects to determine the amount of his net earnings from self-employment for a taxable year under the provisions of the two preceding sentences with respect to a trade or business to which the second preceding sentence applies and with respect to a trade or business to which this sentence applies shall such net earnings for such year exceed the lower limit.

(b) **SELF-EMPLOYMENT INCOME.**—The term “self-employment income” means the net earnings from self-employment derived by an individual (other than a nonresident alien individual, except as provided by an agreement under section 233 of the Social Security Act) during any taxable year; except that such term shall not include—

(1) in the case of the tax imposed by section 1401(a), that part of the net earnings from self-employment which is in excess of (i) an amount equal to the contribution and benefit base (as determined under section 230 of the Social Security Act) which is effective for the calendar year in which such taxable year begins, minus (ii) the amount of the wages paid to such individual during such taxable years; or

(2) the net earnings from self-employment, if such net earnings for the taxable year are less than \$400.

For purposes of paragraph (1), the term “wages” (A) includes such remuneration paid to an employee for services included under an agreement entered into pursuant to the provisions of section 3121(l) (relating to coverage of citizens of the United States who are employees of foreign affiliates of American employers), as would be wages under section 3121(a) if such services constituted employment under section 3121(b), and (B) includes compensation which is subject to the tax imposed by section 3201 or 3211. An individual who is not a citizen of the United States but who is a resident of the Commonwealth of Puerto Rico, the Virgin Islands, Guam, or American Samoa shall not, for purposes of this chapter

be considered to be a nonresident alien individual. In the case of church employee income, the special rules of subsection (j)(2) shall apply for purposes of paragraph (2).

(c) TRADE OR BUSINESS.—The term “trade or business”, when used with reference to self-employment income or net earnings from self-employment, shall have the same meaning as when used in section 162 (relating to trade or business expenses), except that such term shall not include—

(1) the performance of the functions of a public office, other than the functions of a public office of a State or a political subdivision thereof with respect to fees received in any period in which the functions are performed in a position compensated solely on a fee basis and in which such functions are not covered under an agreement entered into by such State and the Commissioner of Social Security pursuant to section 218 of the Social Security Act;

(2) the performance of service by an individual as an employee, other than—

(A) service described in section 3121(b)(14)(B) performed by an individual who has attained the age of 18,

(B) service described in section 3121(b)(16),

(C) service described in section 3121(b)(11), (12), or (15) performed in the United States (as defined in section 3121(e)(2)) by a citizen of the United States, except service which constitutes “employment” under section 3121(y),

(D) service described in paragraph (4) of this subsection,

(E) service performed by an individual as an employee of a State or a political subdivision thereof in a position compensated solely on a fee basis with respect to fees received in any period in which such service is not covered under an agreement entered into by such State and the Commissioner of Social Security pursuant to section 218 of the Social Security Act,

(F) service described in section 3121(b) (20), and

(G) service described in section 3121(b)(8)(B);

(3) the performance of service by an individual as an employee or employee representative as defined in section 3231;

(4) the performance of service by a duly ordained, commissioned, or licensed minister of a church in the exercise of his ministry or by a member of a religious order in the exercise of duties required by such order;

(5) the performance of service by an individual in the exercise of his profession as a Christian Science practitioner; or

(6) the performance of service by an individual during the period for which an exemption under subsection (g) is effective with respect to him.

The provisions of paragraph (4) or (5) shall not apply to service (other than service performed by a member of a religious order who has taken a vow of poverty as a member of such order) performed by an individual unless an exemption under subsection (e) is effective with respect to him.

(d) EMPLOYEE AND WAGES.—The term “employee” and the term “wages” shall have the same meaning as when used in chapter 21 (sec. 3101 and following, relating to Federal Insurance Contributions Act).

## (e) MINISTERS, MEMBERS OF RELIGIOUS ORDERS, AND CHRISTIAN SCIENCE PRACTITIONERS.—

(1) EXEMPTION.—Subject to paragraph (2), any individual who is (A) a duly ordained, commissioned, or licensed minister of a church or a member of a religious order (other than a member of a religious order who has taken a vow of poverty as a member of such order) or (B) a Christian Science practitioner, upon filing an application (in such form and manner, and with such official, as may be prescribed by regulations made under this chapter) together with a statement that either he is conscientiously opposed to, or because of religious principles he is opposed to, the acceptance (with respect to services performed by him as such minister, member, or practitioner) of any public insurance which makes payments in the event of death, disability, old age, or retirement or makes payments toward the cost of, or provides services for, medical care (including the benefits of any insurance system established by the Social Security Act) and, in the case of an individual described in subparagraph (A), that he has informed the ordaining, commissioning, or licensing body of the church or order that he is opposed to such insurance, shall receive an exemption from the tax imposed by this chapter with respect to services performed by him as such minister, member, or practitioner. Notwithstanding the preceding sentence, an exemption may not be granted to an individual under this subsection if he had filed an effective waiver certificate under this section as it was in effect before its amendment in 1967.

(2) VERIFICATION OF APPLICATION.—The Secretary may approve an application for an exemption filed pursuant to paragraph (1) only if the Secretary has verified that the individual applying for the exemption is aware of the grounds on which the individual may receive an exemption pursuant to this subsection and that the individual seeks exemption on such grounds. The Secretary (or the Commissioner of Social Security under an agreement with the Secretary) shall make such verification by such means as prescribed in regulations.

(3) TIME FOR FILING APPLICATION.—Any individual who desires to file an application pursuant to paragraph (1) must file such application on or before the due date of the return (including any extension thereof) for the second taxable year for which he has net earnings from self-employment (computed without regard to subsections (c)(4) and (c)(5)) of \$400 or more, any part of which was derived from the performance of service described in subsection (c)(4) or (c)(5).

(4) EFFECTIVE DATE OF EXEMPTION.—An exemption received by an individual pursuant to this subsection shall be effective for the first taxable year for which he has net earnings from self-employment (computed without regard to subsections (c)(4) and (c)(5)) of \$400 or more, any part of which was derived from the performance of service described in subsection (c)(4) or (c)(5), and for all succeeding taxable years. An exemption received pursuant to this subsection shall be irrevocable.

(f) PARTNER'S TAXABLE YEAR ENDING AS THE RESULT OF DEATH.—In computing a partner's net earnings from self-employment for his taxable year which ends as a result of his death (but only if such

taxable year ends within, and not with, the taxable year of the partnership), there shall be included so much of the deceased partner's distributive share of the partnership's ordinary income or loss for the partnership taxable year as is not attributable to an interest in the partnership during any period beginning on or after the first day of the first calendar month following the month in which such partner died. For purposes of this subsection—

(1) in determining the portion of the distributive share which is attributable to any period specified in the preceding sentence, the ordinary income or loss of the partnership shall be treated as having been realized or sustained ratably over the partnership taxable year; and

(2) the term "deceased partner's distributive share" includes the share of his estate or of any other person succeeding, by reason of his death, to rights with respect to his partnership interest.

(g) MEMBERS OF CERTAIN RELIGIOUS FAITHS.—

(1) EXEMPTION.—Any individual may file an application (in such form and manner, and with such official, as may be prescribed by regulations under this chapter) for an exemption from the tax imposed by this chapter if he is a member of a recognized religious sect or division thereof and is an adherent of established tenets or teachings of such sect or division by reason of which he is conscientiously opposed to acceptance of the benefits of any private or public insurance which makes payments in the event of death, disability, old-age, or retirement or makes payments toward the cost of, or provides services for, medical care (including the benefits of any insurance system established by the Social Security Act). Such exemption may be granted only if the application contains or is accompanied by—

(A) such evidence of such individual's membership in, and adherence to the tenets or teachings of, the sect or division thereof as the Secretary may require for purposes of determining such individual's compliance with the preceding sentence, and

(B) his waiver of all benefits and other payments under titles II and XVIII of the Social Security Act on the basis of his wages and self-employment income as well as all such benefits and other payments to him on the basis of the wages and self-employment income of any other person,

and only if the Commissioner of Social Security finds that—

(C) such sect or division thereof has the established tenets or teachings referred to in the preceding sentence,

(D) it is the practice, and has been for a period of time which he deems to be substantial, for members of such sect or division thereof to make provision for their dependent members which in his judgment is reasonable in view of their general level of living, and

(E) such sect or division thereof has been in existence at all times since December 31, 1950.

An exemption may not be granted to any individual if any benefit or other payment referred to in subparagraph (B) became payable (or, but for section 203 or 222(b) of the Social Security

Act, would have become payable) at or before the time of the filing of such waiver.

(2) PERIOD FOR WHICH EXEMPTION EFFECTIVE.—An exemption granted to any individual pursuant to this subsection shall apply with respect to all taxable years beginning after December 31, 1950, except that such exemption shall not apply for any taxable year—

(A) beginning (i) before the taxable year in which such individual first met the requirements of the first sentence of paragraph (1), or (ii) before the time as of which the Commissioner of Social Security finds that the sect or division thereof of which such individual is a member met the requirements of subparagraphs (C) and (D), or

(B) ending (i) after the time such individual ceases to meet the requirements of the first sentence of paragraph (1), or (ii) after the time as of which the Commissioner of Social Security finds that the sect or division thereof of which he is a member ceases to meet the requirements of subparagraph (C) or (D).

(3) SUBSECTION TO APPLY TO CERTAIN CHURCH EMPLOYEES.—

This subsection shall apply with respect to services which are described in subparagraph (B) of section 3121(b)(8) (and are not described in subparagraph (A) of such section).

(h) REGULAR BASIS.—An individual shall be deemed to be self-employed on a regular basis in a taxable year, or to be a member of a partnership on a regular basis in such year, if he had net earnings from self-employment, as defined in the first sentence of subsection (a), of not less than \$400 in at least two of the three consecutive taxable years immediately preceding such taxable year from trades or businesses carried on by such individual or such partnership.

(i) SPECIAL RULES FOR OPTIONS AND COMMODITIES DEALERS.—

(1) IN GENERAL.—Notwithstanding subsection (a)(3)(A), in determining the net earnings from self-employment of any options dealer or commodities dealer, there shall not be excluded any gain or loss (in the normal course of the taxpayer's activity of dealing in or trading section 1256 contracts) from section 1256 contracts or property related to such contracts.

(2) DEFINITIONS.—For purposes of this subsection—

(A) OPTIONS DEALER.—The term “options dealer” has the meaning given such term by section 1256(g)(8).

(B) COMMODITIES DEALER.—The term “commodities dealer” means a person who is actively engaged in trading section 1256 contracts and is registered with a domestic board of trade which is designated as a contract market by the Commodities Futures Trading Commission.

(C) SECTION 1256 CONTRACTS.—The term “section 1256 contract” has the meaning given to such term by section 1256(b).

(j) SPECIAL RULES FOR CERTAIN CHURCH EMPLOYEE INCOME.—

(1) COMPUTATION OF NET EARNINGS.—In applying subsection

(a)—

(A) church employee income shall not be reduced by any deduction;



(B) church employee income and deductions attributable to such income shall not be taken into account in determining the amount of other net earnings from self-employment.

(2) COMPUTATION OF SELF-EMPLOYMENT INCOME.—

(A) SEPARATE APPLICATION OF SUBSECTION (B)(2).—Paragraph (2) of subsection (b) shall be applied separately—

- (i) to church employee income, and
- (ii) to other net earnings from self-employment.

(B) \$100 FLOOR.—In applying paragraph (2) of subsection (b) to church employee income, “\$100” shall be substituted for “\$400”.

(3) COORDINATION WITH SUBSECTION (A)(12).—Paragraph (1) shall not apply to any amount allowable as a deduction under subsection (a)(12), and paragraph (1) shall be applied before determining the amount so allowable.

(4) CHURCH EMPLOYEE INCOME DEFINED.—For purposes of this section, the term “church employee income” means gross income for services which are described in section 3121(b)(8)(B) (and are not described in section 3121(b)(8)(A)).

(k) CODIFICATION OF TREATMENT OF CERTAIN TERMINATION PAYMENTS RECEIVED BY FORMER INSURANCE SALESMEN.—Nothing in subsection (a) shall be construed as including in the net earnings from self-employment of an individual any amount received during the taxable year from an insurance company on account of services performed by such individual as an insurance salesman for such company if—

(1) such amount is received after termination of such individual’s agreement to perform such services for such company,

(2) such individual performs no services for such company after such termination and before the close of such taxable year,

(3) such individual enters into a covenant not to compete against such company which applies to at least the 1-year period beginning on the date of such termination, and

(4) the amount of such payment—

(A) depends primarily on policies sold by or credited to the account of such individual during the last year of such agreement or the extent to which such policies remain in force for some period after such termination, or both, and

(B) does not depend to any extent on length of service or overall earnings from services performed for such company (without regard to whether eligibility for payment depends on length of service).

(l) UPPER AND LOWER LIMITS.—For purposes of subsection (a)—

(1) LOWER LIMIT.—The lower limit for any taxable year is the sum of the amounts required under section 213(d) of the Social Security Act for a quarter of coverage in effect with respect to each calendar quarter ending with or within such taxable year.

(2) UPPER LIMIT.—The upper limit for any taxable year is the amount equal to 150 percent of the lower limit for such taxable year.

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## CHAPTER 2A—UNEARNED INCOME MEDICARE CONTRIBUTION

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### SEC. 1411. IMPOSITION OF TAX.

(a) **IN GENERAL.**—Except as provided in subsection (e)—

(1) **APPLICATION TO INDIVIDUALS.**—In the case of an individual, there is hereby imposed (in addition to any other tax imposed by this subtitle) for each taxable year a tax equal to 3.8 percent of the lesser of—

(A) net investment income for such taxable year, or

(B) the excess (if any) of—

(i) the modified adjusted gross income for such taxable year, over

(ii) the threshold amount.

(2) **APPLICATION TO ESTATES AND TRUSTS.**—In the case of an estate or trust, there is hereby imposed (in addition to any other tax imposed by this subtitle) for each taxable year a tax of 3.8 percent of the lesser of—

(A) the undistributed net investment income for such taxable year, or

(B) the excess (if any) of—

(i) the adjusted gross income [(as defined in section 67(e))] for such taxable year, over

(ii) the dollar amount at which the highest tax bracket in section 1(e) begins for such taxable year.

(b) **THRESHOLD AMOUNT.**—For purposes of this chapter, the term “threshold amount” means—

(1) in the case of a taxpayer making a joint return under section 6013 or a surviving spouse (as defined in section 2(a)), \$250,000,

(2) in the case of a married taxpayer (as defined in section 7703) filing a separate return, ½ of the dollar amount determined under paragraph (1), and

(3) in any other case, \$200,000.

(c) **NET INVESTMENT INCOME.**—For purposes of this chapter—

(1) **IN GENERAL.**—The term “net investment income” means the excess (if any) of—

(A) the sum of—

(i) gross income from interest, dividends, annuities, royalties, and rents, other than such income which is derived in the ordinary course of a trade or business not described in paragraph (2),

(ii) other gross income derived from a trade or business described in paragraph (2), and

(iii) net gain (to the extent taken into account in computing taxable income) attributable to the disposition of property other than property held in a trade or business not described in paragraph (2), over (B) the deductions allowed by this subtitle which are properly allocable to such gross income or net gain.

(2) **TRADES AND BUSINESSES TO WHICH TAX APPLIES.**—A trade or business is described in this paragraph if such trade or business is—

- (A) a passive activity (within the meaning of section 469) with respect to the taxpayer, or
- (B) a trade or business of trading in financial instruments or commodities (as defined in section 475(e)(2)).
- (3) INCOME ON INVESTMENT OF WORKING CAPITAL SUBJECT TO TAX.—A rule similar to the rule of section 469(e)(1)(B) shall apply for purposes of this subsection.
- (4) EXCEPTION FOR CERTAIN ACTIVE INTERESTS IN PARTNERSHIPS AND S CORPORATIONS.—In the case of a disposition of an interest in a partnership or S corporation—
  - (A) gain from such disposition shall be taken into account under clause (iii) of paragraph (1)(A) only to the extent of the net gain which would be so taken into account by the transferor if all property of the partnership or S corporation were sold for fair market value immediately before the disposition of such interest, and
  - (B) a rule similar to the rule of subparagraph (A) shall apply to a loss from such disposition.
- (5) EXCEPTION FOR DISTRIBUTIONS FROM QUALIFIED PLANS.—The term “net investment income” shall not include any distribution from a plan or arrangement described in section 401(a), 403(a), 403(b), 408, 408A, or 457(b).
- (6) SPECIAL RULE.—Net investment income shall not include any item taken into account in determining self-employment income for such taxable year on which a tax is imposed by section 1401(b).
- (d) MODIFIED ADJUSTED GROSS INCOME.—For purposes of this chapter, the term “modified adjusted gross income” means adjusted gross income increased by the excess of—
  - (1) the amount excluded from gross income under section 911(a)(1), over
  - (2) the amount of any deductions (taken into account in computing adjusted gross income) or exclusions disallowed under section 911(d)(6) with respect to the amounts described in paragraph (1).
- (e) NONAPPLICATION OF SECTION.—This section shall not apply to—
  - (1) a nonresident alien, or
  - (2) a trust all of the unexpired interests in which are devoted to one or more of the purposes described in section 170(c)(2)(B).

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## Subtitle B—Estate and Gift Taxes

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### CHAPTER 11—ESTATE TAX

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#### Subchapter A—Estates of Citizens or Residents

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## PART I—TAX IMPOSED

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**SEC. 2001. IMPOSITION AND RATE OF TAX.**

(a) IMPOSITION.—A tax is hereby imposed on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

(b) COMPUTATION OF TAX.—The tax imposed by this section shall be the amount equal to the excess (if any) of—

(1) a tentative tax computed under subsection (c) on the sum of—

(A) the amount of the taxable estate, and

(B) the amount of the adjusted taxable gifts, over

(2) the aggregate amount of tax which would have been payable under chapter 12 with respect to gifts made by the decedent after December 31, 1976, if the modifications described in subsection (g) had been applicable at the time of such gifts.

For purposes of paragraph (1)(B), the term “adjusted taxable gifts” means the total amount of the taxable gifts (within the meaning of section 2503) made by the decedent after December 31, 1976, other than gifts which are includible in the gross estate of the decedent.

(c) Rate schedule

| If the amount with respect to which the tentative tax to be computed is: | The tentative tax is:   |
|--|---|
| Not over \$10,000  | 18 percent of such amount.  |
| Over \$10,000 but not over \$20,000                                      | \$1,800, plus 20 percent of the excess of such amount over \$10,000.      |
| Over \$20,000 but not over \$40,000                                      | \$3,800, plus 22 percent of the excess of such amount over \$20,000.      |
| Over \$40,000 but not over \$60,000                                      | \$8,200 plus 24 percent of the excess of such amount over \$40,000.       |
| Over \$60,000 but not over \$80,000                                      | \$13,000, plus 26 percent of the excess of such amount over \$60,000.     |
| Over \$80,000 but not over \$100,000                                     | \$18,200, plus 28 percent of the excess of such amount over \$80,000.     |
| Over \$100,000 but not over \$150,000                                    | \$23,800, plus 30 percent of the excess of such amount over \$100,000.    |
| Over \$150,000 but not over \$250,000                                    | \$38,800, plus 32 percent of the excess of such amount over \$150,000.    |
| Over \$250,000 but not over \$500,000                                    | \$70,800, plus 34 percent of the excess of such amount over \$250,000.    |
| Over \$500,000 but not over \$750,000                                    | \$155,800, plus 37 percent of the excess of such amount over \$500,000.   |
| Over \$750,000 but not over \$1,000,000                                  | \$248,300, plus 39 percent of the excess of such amount over \$750,000.   |
| Over \$1,000,000   | \$345,800, plus 40 percent of the excess of such amount over \$1,000,000. |

(d) ADJUSTMENT FOR GIFT TAX PAID BY SPOUSE.—For purposes of subsection (b)(2), if—

(1) the decedent was the donor of any gift one-half of which was considered under section 2513 as made by the decedent's spouse, and

(2) the amount of such gift is includible in the gross estate of the decedent,

any tax payable by the spouse under chapter 12 on such gift (as determined under section 2012(d)) shall be treated as a tax payable with respect to a gift made by the decedent.

(e) COORDINATION OF SECTIONS 2513 AND 2035.—If—

(1) the decedent's spouse was the donor of any gift one-half of which was considered under section 2513 as made by the decedent, and

(2) the amount of such gift is includible in the gross estate of the decedent's spouse by reason of section 2035, such gift shall not be included in the adjusted taxable gifts of the decedent for purposes of subsection (b)(1)(B), and the aggregate amount determined under subsection (b)(2) shall be reduced by the amount (if any) determined under subsection (d) which was treated as a tax payable by the decedent's spouse with respect to such gift.

(f) VALUATION OF GIFTS.—

(1) IN GENERAL.—If the time has expired under section 6501 within which a tax may be assessed under chapter 12 (or under corresponding provisions of prior laws) on—

(A) the transfer of property by gift made during a preceding calendar period (as defined in section 2502(b)); or

(B) an increase in taxable gifts required under section 2701(d),

the value thereof shall, for purposes of computing the tax under this chapter, be the value as finally determined for purposes of chapter 12.

(2) FINAL DETERMINATION.—For purposes of paragraph (1), a value shall be treated as finally determined for purposes of chapter 12 if—

(A) the value is shown on a return under such chapter and such value is not contested by the Secretary before the expiration of the time referred to in paragraph (1) with respect to such return;

(B) in a case not described in subparagraph (A), the value is specified by the Secretary and such value is not timely contested by the taxpayer; or

(C) the value is determined by a court or pursuant to a settlement agreement with the Secretary.

For purposes of subparagraph (A), the value of an item shall be treated as shown on a return if the item is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature of such item.

[(g) MODIFICATIONS TO TAX PAYABLE.—

[(1) MODIFICATIONS TO GIFT TAX PAYABLE TO REFLECT DIFFERENT TAX RATES.—For purposes of applying subsection (b)(2) with respect to 1 or more gifts, the rates of tax under subsection (c) in effect at the decedent's death shall, in lieu of the rates of tax in effect at the time of such gifts, be used both to compute—

[(A) the tax imposed by chapter 12 with respect to such gifts, and

[(B) the credit allowed against such tax under section 2505, including in computing—

[(i) the applicable credit amount under section 2505(a)(1), and

[(ii) the sum of the amounts allowed as a credit for all preceding periods under section 2505(a)(2).

[(2) MODIFICATIONS TO ESTATE TAX PAYABLE TO REFLECT DIFFERENT BASIC EXCLUSION AMOUNTS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out this section with respect to any difference between—

[(A) the basic exclusion amount under section 2010(c)(3) applicable at the time of the decedent’s death, and

[(B) the basic exclusion amount under such section applicable with respect to any gifts made by the decedent.]

(g) MODIFICATIONS TO GIFT TAX PAYABLE TO REFLECT DIFFERENT TAX RATES.—For purposes of applying subsection (b)(2) with respect to 1 or more gifts, the rates of tax under subsection (c) in effect at the decedent’s death shall, in lieu of the rates of tax in effect at the time of such gifts, be used both to compute—

(1) the tax imposed by chapter 12 with respect to such gifts, and

(2) the credit allowed against such tax under section 2505, including in computing—

(A) the applicable credit amount under section 2505(a)(1), and

(B) the sum of the amounts allowed as a credit for all preceding periods under section 2505(a)(2).

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**PART II—CREDITS AGAINST TAX**

\* \* \* \* \*

**SEC. 2010. UNIFIED CREDIT AGAINST ESTATE TAX.**

(a) GENERAL RULE.—A credit of the applicable credit amount shall be allowed to the estate of every decedent against the tax imposed by section 2001.

(b) ADJUSTMENT TO CREDIT FOR CERTAIN GIFTS MADE BEFORE 1977.—The amount of the credit allowable under subsection (a) shall be reduced by an amount equal to 20 percent of the aggregate amount allowed as a specific exemption under section 2521 (as in effect before its repeal by the Tax Reform Act of 1976) with respect to gifts made by the decedent after September 8, 1976.

(c) APPLICABLE CREDIT AMOUNT.—

(1) IN GENERAL.—For purposes of this section, the applicable credit amount is the amount of the tentative tax which would be determined under section 2001(c) if the amount with respect to which such tentative tax is to be computed were equal to the applicable exclusion amount.

(2) APPLICABLE EXCLUSION AMOUNT.—For purposes of this subsection, the applicable exclusion amount is the sum of—

(A) the basic exclusion amount, and

(B) in the case of a surviving spouse, the deceased spousal unused exclusion amount.

(3) BASIC EXCLUSION AMOUNT.—

(A) IN GENERAL.—For purposes of this subsection, the basic exclusion amount is **[\$5,000,000] \$10,000,000**.

(B) INFLATION ADJUSTMENT.—In the case of any decedent dying in a calendar year after 2011, the dollar amount in

subparagraph (A) shall be increased by an amount equal to—

- (i) such dollar amount, multiplied by
- (ii) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year by substituting “calendar year 2010” for “calendar year 2016” in subparagraph (A)(ii) thereof.

If any amount as adjusted under the preceding sentence is not a multiple of \$10,000, such amount shall be rounded to the nearest multiple of \$10,000.

[(C) INCREASE IN BASIC EXCLUSION AMOUNT.—In the case of estates of decedents dying or gifts made after December 31, 2017, and before January 1, 2026, subparagraph (A) shall be applied by substituting “\$10,000,000” for “\$5,000,000”.]

(4) DECEASED SPOUSAL UNUSED EXCLUSION AMOUNT.—For purposes of this subsection, with respect to a surviving spouse of a deceased spouse dying after December 31, 2010, the term “deceased spousal unused exclusion amount” means the lesser of—

- (A) the basic exclusion amount, or
- (B) the excess of—
  - (i) the applicable exclusion amount of the last such deceased spouse of such surviving spouse, over
  - (ii) the amount with respect to which the tentative tax is determined under section 2001(b)(1) on the estate of such deceased spouse.

(5) SPECIAL RULES.—

(A) ELECTION REQUIRED.—A deceased spousal unused exclusion amount may not be taken into account by a surviving spouse under paragraph (2) unless the executor of the estate of the deceased spouse files an estate tax return on which such amount is computed and makes an election on such return that such amount may be so taken into account. Such election, once made, shall be irrevocable. No election may be made under this subparagraph if such return is filed after the time prescribed by law (including extensions) for filing such return.

(B) EXAMINATION OF PRIOR RETURNS AFTER EXPIRATION OF PERIOD OF LIMITATIONS WITH RESPECT TO DECEASED SPOUSAL UNUSED EXCLUSION AMOUNT.—Notwithstanding any period of limitation in section 6501, after the time has expired under section 6501 within which a tax may be assessed under chapter 11 or 12 with respect to a deceased spousal unused exclusion amount, the Secretary may examine a return of the deceased spouse to make determinations with respect to such amount for purposes of carrying out this subsection.

(6) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out this subsection.

(d) LIMITATION BASED ON AMOUNT OF TAX.—The amount of the credit allowed by subsection (a) shall not exceed the amount of the tax imposed by section 2001.

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**PART III—GROSS ESTATE**

\* \* \* \* \*

**SEC. 2032A. VALUATION OF CERTAIN FARM, ETC., REAL PROPERTY.**

(a) VALUE BASED ON USE UNDER WHICH PROPERTY QUALIFIES.—

(1) GENERAL RULE.—If—

(A) the decedent was (at the time of his death) a citizen or resident of the United States, and

(B) the executor elects the application of this section and files the agreement referred to in subsection (d)(2), then, for purposes of this chapter, the value of qualified real property shall be its value for the use under which it qualifies, under subsection (b), as qualified real property.

(2) LIMITATION ON AGGREGATE REDUCTION IN FAIR MARKET VALUE.—The aggregate decrease in the value of qualified real property taken into account for purposes of this chapter which results from the application of paragraph (1) with respect to any decedent shall not exceed \$750,000.

(3) INFLATION ADJUSTMENT.—In the case of estates of decedents dying in a calendar year after 1998, the \$750,000 amount contained in paragraph (2) shall be increased by an amount equal to—

(A) \$750,000, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year by substituting “calendar year 1997” for “calendar year 2016” in subparagraph (A)(ii) thereof.

If any amount as adjusted under the preceding sentence is not a multiple of \$10,000, such amount shall be rounded to the next lowest multiple of \$10,000.

(b) QUALIFIED REAL PROPERTY.—

(1) IN GENERAL.—For purposes of this section, the term “qualified real property” means real property located in the United States which was acquired from or passed from the decedent to a qualified heir of the decedent and which, on the date of the decedent’s death, was being used for a qualified use by the decedent or a member of the decedent’s family, but only if—

(A) 50 percent or more of the adjusted value of the gross estate consists of the adjusted value of real or personal property which—

(i) on the date of the decedent’s death, was being used for a qualified use by the decedent or a member of the decedent’s family, and

(ii) was acquired from or passed from the decedent to a qualified heir of the decedent.

(B) 25 percent or more of the adjusted value of the gross estate consists of the adjusted value of real property which meets the requirements of subparagraphs (A)(ii) and (C),

(C) during the 8-year period ending on the date of the decedent’s death there have been periods aggregating 5 years or more during which—

(i) such real property was owned by the decedent or a member of the decedent’s family and used for a



qualified use by the decedent or a member of the decedent's family, and

(ii) there was material participation by the decedent or a member of the decedent's family in the operation of the farm or other business, and

(D) such real property is designated in the agreement referred to in subsection (d)(2).

(2) QUALIFIED USE.—For purposes of this section, the term “qualified use” means the devotion of the property to any of the following:

(A) use as a farm for farming purposes, or

(B) use in a trade or business other than the trade or business of farming.

(3) ADJUSTED VALUE.—For purposes of paragraph (1), the term “adjusted value” means—

(A) in the case of the gross estate, the value of the gross estate for purposes of this chapter (determined without regard to this section), reduced by any amounts allowable as a deduction under paragraph (4) of section 2053(a), or

(B) in the case of any real or personal property, the value of such property for purposes of this chapter (determined without regard to this section), reduced by any amounts allowable as a deduction in respect of such property under paragraph (4) of section 2053(a).

(4) DECEDENTS WHO ARE RETIRED OR DISABLED.—

(A) IN GENERAL.—If, on the date of the decedent's death, the requirements of paragraph (1)(C)(ii) with respect to the decedent for any property are not met, and the decedent—

(i) was receiving old-age benefits under title II of the Social Security Act for a continuous period ending on such date, or

(ii) was disabled for a continuous period ending on such date,

then paragraph (1)(C)(ii) shall be applied with respect to such property by substituting “the date on which the longer of such continuous periods began” for “the date of the decedent's death” in paragraph (1)(C).

(B) DISABLED DEFINED.—For purposes of subparagraph (A), an individual shall be disabled if such individual has a mental or physical impairment which renders him unable to materially participate in the operation of the farm or other business.

(C) COORDINATION WITH RECAPTURE.—For purposes of subsection (c)(6)(B)(i), if the requirements of paragraph (1)(C)(ii) are met with respect to any decedent by reason of subparagraph (A), the period ending on the date on which the continuous period taken into account under subparagraph (A) began shall be treated as the period immediately before the decedent's death.

(5) SPECIAL RULES FOR SURVIVING SPOUSES.—

(A) IN GENERAL.—If property is qualified real property with respect to a decedent (hereinafter in this paragraph referred to as the “first decedent”) and such property was acquired from or passed from the first decedent to the surviving spouse of the first decedent, for purposes of apply-

ing this subsection and subsection (c) in the case of the estate of such surviving spouse, active management of the farm or other business by the surviving spouse shall be treated as material participation by such surviving spouse in the operation of such farm or business.

(B) SPECIAL RULE.—For the purposes of subparagraph (A), the determination of whether property is qualified real property with respect to the first decedent shall be made without regard to subparagraph (D) of paragraph (1) and without regard to whether an election under this section was made.

(C) COORDINATION WITH PARAGRAPH (4).—In any case in which to do so will enable the requirements of paragraph (1)(C)(ii) to be met with respect to the surviving spouse, this subsection and subsection (c) shall be applied by taking into account any application of paragraph (4).

(c) TAX TREATMENT OF DISPOSITIONS AND FAILURES TO USE FOR QUALIFIED USE.—

(1) IMPOSITION OF ADDITIONAL ESTATE TAX.—If, within 10 years after the decedent's death and before the death of the qualified heir—

(A) the qualified heir disposes of any interest in qualified real property (other than by a disposition to a member of his family), or

(B) the qualified heir ceases to use for the qualified use the qualified real property which was acquired (or passed) from the decedent,

then, there is hereby imposed an additional estate tax.

(2) AMOUNT OF ADDITIONAL TAX.—

(A) IN GENERAL.—The amount of the additional tax imposed by paragraph (1) with respect to any interest shall be the amount equal to the lesser of—

(i) the adjusted tax difference attributable to such interest, or

(ii) the excess of the amount realized with respect to the interest (or, in any case other than a sale or exchange at arm's length, the fair market value of the interest) over the value of the interest determined under subsection (a).

(B) ADJUSTED TAX DIFFERENCE ATTRIBUTABLE TO INTEREST.—For purposes of subparagraph (A), the adjusted tax difference attributable to an interest is the amount which bears the same ratio to the adjusted tax difference with respect to the estate (determined under subparagraph (C)) as—

(i) the excess of the value of such interest for purposes of this chapter (determined without regard to subsection (a)) over the value of such interest determined under subsection (a), bears to

(ii) a similar excess determined for all qualified real property.

(C) ADJUSTED TAX DIFFERENCE WITH RESPECT TO THE ESTATE.—For purposes of subparagraph (B), the term "adjusted tax difference with respect to the estate" means the excess of what would have been the estate tax liability but

for subsection (a) over the estate tax liability. For purposes of this subparagraph, the term “estate tax liability” means the tax imposed by section 2001 reduced by the credits allowable against such tax.

(D) PARTIAL DISPOSITIONS.—For purposes of this paragraph, where the qualified heir disposes of a portion of the interest acquired by (or passing to) such heir (or a predecessor qualified heir) or there is a cessation of use of such a portion—

(i) the value determined under subsection (a) taken into account under subparagraph (A)(ii) with respect to such portion shall be its pro rata share of such value of such interest, and

(ii) the adjusted tax difference attributable to the interest taken into account with respect to the transaction involving the second or any succeeding portion shall be reduced by the amount of the tax imposed by this subsection with respect to all prior transactions involving portions of such interest.

(E) SPECIAL RULE FOR DISPOSITION OF TIMBER.—In the case of qualified woodland to which an election under subsection (e)(13)(A) applies, if the qualified heir disposes of (or severs) any standing timber on such qualified woodland—

(i) such disposition (or severance) shall be treated as a disposition of a portion of the interest of the qualified heir in such property, and

(ii) the amount of the additional tax imposed by paragraph (1) with respect to such disposition shall be an amount equal to the lesser of—

(I) the amount realized on such disposition (or, in any case other than a sale or exchange at arm’s length, the fair market value of the portion of the interest disposed or severed), or

(II) the amount of additional tax determined under this paragraph (without regard to this subparagraph) if the entire interest of the qualified heir in the qualified woodland had been disposed of, less the sum of the amount of the additional tax imposed with respect to all prior transactions involving such woodland to which this subparagraph applied.

For purposes of the preceding sentence, the disposition of a right to sever shall be treated as the disposition of the standing timber. The amount of additional tax imposed under paragraph (1) in any case in which a qualified heir disposes of his entire interest in the qualified woodland shall be reduced by any amount determined under this subparagraph with respect to such woodland.

(3) ONLY 1 ADDITIONAL TAX IMPOSED WITH RESPECT TO ANY 1 PORTION.—In the case of an interest acquired from (or passing from) any decedent, if subparagraph (A) or (B) of paragraph (1) applies to any portion of an interest, subparagraph (B) or (A), as the case may be, of paragraph (1) shall not apply with respect to the same portion of such interest.

(4) DUE DATE.—The additional tax imposed by this subsection shall become due and payable on the day which is 6 months after the date of the disposition or cessation referred to in paragraph (1).

(5) LIABILITY FOR TAX; FURNISHING OF BOND.—The qualified heir shall be personally liable for the additional tax imposed by this subsection with respect to his interest unless the heir has furnished bond which meets the requirements of subsection (e)(11).

(6) CESSATION OF QUALIFIED USE.—For purposes of paragraph (1)(B), real property shall cease to be used for the qualified use if—

(A) such property ceases to be used for the qualified use set forth in subparagraph (A) or (B) of subsection (b)(2) under which the property qualified under subsection (b), or

(B) during any period of 8 years ending after the date of the decedent's death and before the date of the death of the qualified heir, there had been periods aggregating more than 3 years during which—

(i) in the case of periods during which the property was held by the decedent, there was no material participation by the decedent or any member of his family in the operation of the farm or other business, and

(ii) in the case of periods during which the property was held by any qualified heir, there was no material participation by such qualified heir or any member of his family in the operation of the farm or other business.

(7) SPECIAL RULES.—

(A) NO TAX IF USE BEGINS WITHIN 2 YEARS.—If the date on which the qualified heir begins to use the qualified real property (hereinafter in this subparagraph referred to as the commencement date) is before the date 2 years after the decedent's death—

(i) no tax shall be imposed under paragraph (1) by reason of the failure by the qualified heir to so use such property before the commencement date, and

(ii) the 10-year period under paragraph (1) shall be extended by the period after the decedent's death and before the commencement date.

(B) ACTIVE MANAGEMENT BY ELIGIBLE QUALIFIED HEIR TREATED AS MATERIAL PARTICIPATION.—For purposes of paragraph (6)(B)(ii), the active management of a farm or other business by—

(i) an eligible qualified heir, or

(ii) a fiduciary of an eligible qualified heir described in clause (ii) or (iii) of subparagraph (C),

shall be treated as material participation by such eligible qualified heir in the operation of such farm or business. In the case of an eligible qualified heir described in clause (ii), (iii), or (iv) of subparagraph (C), the preceding sentence shall apply only during periods during which such heir meets the requirements of such clause.

(C) ELIGIBLE QUALIFIED HEIR.—For purposes of this paragraph, the term “eligible qualified heir” means a qualified heir who—

- (i) is the surviving spouse of the decedent,
- (ii) has not attained the age of 21,
- (iii) is disabled (within the meaning of subsection (b)(4)(B)), or
- (iv) is a student.

(D) STUDENT.—For purposes of subparagraph (C), an individual shall be treated as a student with respect to periods during any calendar year if (and only if) such individual is a student (within the meaning of [section 152(f)(2)] *section 7706(f)(2)*) for such calendar year.

(E) CERTAIN RENTS TREATED AS QUALIFIED USE.—For purposes of this subsection, a surviving spouse or lineal descendant of the decedent shall not be treated as failing to use qualified real property in a qualified use solely because such spouse or descendant rents such property to a member of the family of such spouse or descendant on a net cash basis. For purposes of the preceding sentence, a legally adopted child of an individual shall be treated as the child of such individual by blood.

(8) QUALIFIED CONSERVATION CONTRIBUTION IS NOT A DISPOSITION.—A qualified conservation contribution (as defined in section 170(h)) by gift or otherwise shall not be deemed a disposition under subsection (c)(1)(A).

(d) ELECTION; AGREEMENT.—

(1) ELECTION.—The election under this section shall be made on the return of the tax imposed by section 2001. Such election shall be made in such manner as the Secretary shall by regulations prescribe. Such an election, once made, shall be irrevocable.

(2) AGREEMENT.—The agreement referred to in this paragraph is a written agreement signed by each person in being who has an interest (whether or not in possession) in any property designated in such agreement consenting to the application of subsection (c) with respect to such property.

(3) MODIFICATION OF ELECTION AND AGREEMENT TO BE PERMITTED.—The Secretary shall prescribe procedures which provide that in any case in which the executor makes an election under paragraph (1) (and submits the agreement referred to in paragraph (2)) within the time prescribed therefor, but—

(A) the notice of election, as filed, does not contain all required information, or

(B) signatures of 1 or more persons required to enter into the agreement described in paragraph (2) are not included on the agreement as filed, or the agreement does not contain all required information,

the executor will have a reasonable period of time (not exceeding 90 days) after notification of such failures to provide such information or signatures.

(e) DEFINITIONS; SPECIAL RULES.—For purposes of this section—

(1) QUALIFIED HEIR.—The term “qualified heir” means, with respect to any property, a member of the decedent’s family who acquired such property (or to whom such property passed) from

the decedent. If a qualified heir disposes of any interest in qualified real property to any member of his family, such member shall thereafter be treated as the qualified heir with respect to such interest.

(2) MEMBER OF FAMILY.—The term “member of the family” means, with respect to any individual, only—

- (A) an ancestor of such individual,
- (B) the spouse of such individual,
- (C) a lineal descendant of such individual, of such individual’s spouse, or of a parent of such individual, or
- (D) the spouse of any lineal descendant described in subparagraph (C).

For purposes of the preceding sentence, a legally adopted child of an individual shall be treated as the child of such individual by blood.

(3) CERTAIN REAL PROPERTY INCLUDED.—In the case of real property which meets the requirements of subparagraph (C) of subsection (b)(1), residential buildings and related improvements on such real property occupied on a regular basis by the owner or lessee of such real property or by persons employed by such owner or lessee for the purpose of operating or maintaining such real property, and roads, buildings, and other structures and improvements functionally related to the qualified use shall be treated as real property devoted to the qualified use.

(4) FARM.—The term “farm” includes stock, dairy, poultry, fruit, furbearing animal, and truck farms, plantations, ranches, nurseries, ranges, greenhouses or other similar structures used primarily for the raising of agricultural or horticultural commodities, and orchards and woodlands.

(5) FARMING PURPOSES.—The term “farming purposes” means—

- (A) cultivating the soil or raising or harvesting any agricultural or horticultural commodity (including the raising, shearing, feeding, caring for, training, and management of animals) on a farm;
- (B) handling, drying, packing, grading, or storing on a farm any agricultural or horticultural commodity in its unmanufactured state, but only if the owner, tenant, or operator of the farm regularly produces more than one-half of the commodity so treated; and
- (C)
  - (i) the planting, cultivating, caring for, or cutting of trees, or
  - (ii) the preparation (other than milling) of trees for market.

(6) MATERIAL PARTICIPATION.—Material participation shall be determined in a manner similar to the manner used for purposes of paragraph (1) of section 1402(a) (relating to net earnings from self-employment).

(7) METHOD OF VALUING FARMS.—

- (A) IN GENERAL.—Except as provided in subparagraph (B), the value of a farm for farming purposes shall be determined by dividing—

(i) the excess of the average annual gross cash rental for comparable land used for farming purposes and located in the locality of such farm over the average annual State and local real estate taxes for such comparable land, by

(ii) the average annual effective interest rate for all new Federal Land Bank loans.

For purposes of the preceding sentence, each average annual computation shall be made on the basis of the 5 most recent calendar years ending before the date of the decedent's death.

(B) VALUE BASED ON NET SHARE RENTAL IN CERTAIN CASES.—

(i) IN GENERAL.—If there is no comparable land from which the average annual gross cash rental may be determined but there is comparable land from which the average net share rental may be determined, subparagraph (A)(i) shall be applied by substituting “average annual net share rental” for “average annual gross cash rental”.

(ii) NET SHARE RENTAL.—For purposes of this paragraph, the term “net share rental” means the excess of—

(I) the value of the produce received by the lessor of the land on which such produce is grown, over

(II) the cash operating expenses of growing such produce which, under the lease, are paid by the lessor.

(C) EXCEPTION.—The formula provided by subparagraph (A) shall not be used—

(i) where it is established that there is no comparable land from which the average annual gross cash rental may be determined, or

(ii) where the executor elects to have the value of the farm for farming purposes determined and that there is no comparable land from which the average net share rental may be determined under paragraph (8).

(8) METHOD OF VALUING CLOSELY HELD BUSINESS INTERESTS, ETC.—In any case to which paragraph (7)(A) does not apply, the following factors shall apply in determining the value of any qualified real property:

(A) The capitalization of income which the property can be expected to yield for farming or closely held business purposes over a reasonable period of time under prudent management using traditional cropping patterns for the area, taking into account soil capacity, terrain configuration, and similar factors,

(B) The capitalization of the fair rental value of the land for farm land or closely held business purposes,

(C) Assessed land values in a State which provides a differential or use value assessment law for farmland or closely held business,

(D) Comparable sales of other farm or closely held business land in the same geographical area far enough removed from a metropolitan or resort area so that non-agricultural use is not a significant factor in the sales price, and

(E) Any other factor which fairly values the farm or closely held business value of the property.

(9) PROPERTY ACQUIRED FROM DECEDENT.—Property shall be considered to have been acquired from or to have passed from the decedent if—

(A) such property is so considered under section 1014(b) (relating to basis of property acquired from a decedent),

(B) such property is acquired by any person from the estate, or

(C) such property is acquired by any person from a trust (to the extent such property is includible in the gross estate of the decedent).

(10) COMMUNITY PROPERTY.—If the decedent and his surviving spouse at any time held qualified real property as community property, the interest of the surviving spouse in such property shall be taken into account under this section to the extent necessary to provide a result under this section with respect to such property which is consistent with the result which would have obtained under this section if such property had not been community property.

(11) BOND IN LIEU OF PERSONAL LIABILITY.—If the qualified heir makes written application to the Secretary for determination of the maximum amount of the additional tax which may be imposed by subsection (c) with respect to the qualified heir's interest, the Secretary (as soon as possible, and in any event within 1 year after the making of such application) shall notify the heir of such maximum amount. The qualified heir, on furnishing a bond in such amount and for such period as may be required, shall be discharged from personal liability for any additional tax imposed by subsection (c) and shall be entitled to a receipt or writing showing such discharge.

(12) ACTIVE MANAGEMENT.—The term “active management” means the making of the management decisions of a business (other than the daily operating decisions).

(13) SPECIAL RULES FOR WOODLANDS.—

(A) IN GENERAL.—In the case of any qualified woodland with respect to which the executor elects to have this subparagraph apply, trees growing on such woodland shall not be treated as a crop.

(B) QUALIFIED WOODLAND.—The term “qualified woodland” means any real property which—

(i) is used in timber operations, and

(ii) is an identifiable area of land such as an acre or other area for which records are normally maintained in conducting timber operations.

(C) TIMBER OPERATIONS.—The term “timber operations” means—

(i) the planting, cultivating, caring for, or cutting of trees, or



(ii) the preparation (other than milling) of trees for market.

(D) ELECTION.—An election under subparagraph (A) shall be made on the return of the tax imposed by section 2001. Such election shall be made in such manner as the Secretary shall by regulations prescribe. Such an election, once made, shall be irrevocable.

(14) TREATMENT OF REPLACEMENT PROPERTY ACQUIRED IN SECTION 1031 OR 1033 TRANSACTIONS.—

(A) IN GENERAL.—In the case of any qualified replacement property, any period during which there was ownership, qualified use, or material participation with respect to the replaced property by the decedent or any member of his family shall be treated as a period during which there was such ownership, use, or material participation (as the case may be) with respect to the qualified replacement property.

(B) LIMITATION.—Subparagraph (A) shall not apply to the extent that the fair market value of the qualified replacement property (as of the date of its acquisition) exceeds the fair market value of the replaced property (as of the date of its disposition).

(C) DEFINITIONS.—For purposes of this paragraph—

(i) QUALIFIED REPLACEMENT PROPERTY.—The term “qualified replacement property” means any real property which is—

(I) acquired in an exchange which qualifies under section 1031, or

(II) the acquisition of which results in the non-recognition of gain under section 1033.

Such term shall only include property which is used for the same qualified use as the replaced property was being used before the exchange.

(ii) REPLACED PROPERTY.—The term “replaced property” means—

(I) the property transferred in the exchange which qualifies under section 1031, or

(II) the property compulsorily or involuntarily converted (within the meaning of section 1033).

(f) STATUTE OF LIMITATIONS.—If qualified real property is disposed of or ceases to be used for a qualified use, then—

(1) the statutory period for the assessment of any additional tax under subsection (c) attributable to such disposition or cessation shall not expire before the expiration of 3 years from the date the Secretary is notified (in such manner as the Secretary may by regulations prescribe) of such disposition or cessation (or if later in the case of an involuntary conversion or exchange to which subsection (h) or (i) applies, 3 years from the date the Secretary is notified of the replacement of the converted property or of an intention not to replace or of the exchange of property), and

(2) such additional tax may be assessed before the expiration of such 3-year period notwithstanding the provisions of any other law or rule of law which would otherwise prevent such assessment.

(g) APPLICATION OF THIS SECTION AND SECTION 6324B TO INTERESTS IN PARTNERSHIPS, CORPORATIONS, AND TRUSTS.—The Secretary shall prescribe regulations setting forth the application of this section and section 6324B in the case of an interest in a partnership, corporation, or trust which, with respect to the decedent, is an interest in a closely held business (within the meaning of paragraph (1) of section 6166(b)). For purposes of the preceding sentence, an interest in a discretionary trust all the beneficiaries of which are qualified heirs shall be treated as a present interest.

(h) SPECIAL RULES FOR INVOLUNTARY CONVERSIONS OF QUALIFIED REAL PROPERTY.—

(1) TREATMENT OF CONVERTED PROPERTY.—

(A) IN GENERAL.—If there is an involuntary conversion of an interest in qualified real property—

(i) no tax shall be imposed by subsection (c) on such conversion if the cost of the qualified replacement property equals or exceeds the amount realized on such conversion, or

(ii) if clause (i) does not apply, the amount of the tax imposed by subsection (c) on such conversion shall be the amount determined under subparagraph (B).

(B) AMOUNT OF TAX WHERE THERE IS NOT COMPLETE REINVESTMENT.—The amount determined under this subparagraph with respect to any involuntary conversion is the amount of the tax which (but for this subsection) would have been imposed on such conversion reduced by an amount which—

(i) bears the same ratio to such tax, as

(ii) the cost of the qualified replacement property bears to the amount realized on the conversion.

(2) TREATMENT OF REPLACEMENT PROPERTY.—For purposes of subsection (c)—

(A) any qualified replacement property shall be treated in the same manner as if it were a portion of the interest in qualified real property which was involuntarily converted; except that with respect to such qualified replacement property the 10-year period under paragraph (1) of subsection (c) shall be extended by any period, beyond the 2-year period referred to in section 1033(a)(2)(B)(i), during which the qualified heir was allowed to replace the qualified real property,

(B) any tax imposed by subsection (c) on the involuntary conversion shall be treated as a tax imposed on a partial disposition, and

(C) paragraph (6) of subsection (c) shall be applied—

(i) by not taking into account periods after the involuntary conversion and before the acquisition of the qualified replacement property, and

(ii) by treating material participation with respect to the converted property as material participation with respect to the qualified replacement property.

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

(A) INVOLUNTARY CONVERSION.—The term “involuntary conversion” means a compulsory or involuntary conversion within the meaning of section 1033.

(B) QUALIFIED REPLACEMENT PROPERTY.—The term “qualified replacement property” means—

(i) in the case of an involuntary conversion described in section 1033(a)(1), any real property into which the qualified real property is converted, or

(ii) in the case of an involuntary conversion described in section 1033(a)(2), any real property purchased by the qualified heir during the period specified in section 1033(a)(2)(B) for purposes of replacing the qualified real property.

Such term only includes property which is to be used for the qualified use set forth in subparagraph (A) or (B) of subsection (b)(2) under which the qualified real property qualified under subsection (a).

(4) CERTAIN RULES MADE APPLICABLE.—The rules of the last sentence of section 1033(a)(2)(A) shall apply for purposes of paragraph (3)(B)(ii).

(i) EXCHANGES OF QUALIFIED REAL PROPERTY.—

(1) TREATMENT OF PROPERTY EXCHANGED.—

(A) EXCHANGES SOLELY FOR QUALIFIED EXCHANGE PROPERTY.—If an interest in qualified real property is exchanged solely for an interest in qualified exchange property in a transaction which qualifies under section 1031, no tax shall be imposed by subsection (c) by reason of such exchange.

(B) EXCHANGES WHERE OTHER PROPERTY RECEIVED.—If an interest in qualified real property is exchanged for an interest in qualified exchange property and other property in a transaction which qualifies under section 1031, the amount of the tax imposed by subsection (c) by reason of such exchange shall be the amount of tax which (but for this subparagraph) would have been imposed on such exchange under subsection (c)(1), reduced by an amount which—

(i) bears the same ratio to such tax, as

(ii) the fair market value of the qualified exchange property bears to the fair market value of the qualified real property exchanged.

For purposes of clause (ii) of the preceding sentence, fair market value shall be determined as of the time of the exchange.

(2) TREATMENT OF QUALIFIED EXCHANGE PROPERTY.—For purposes of subsection (c)—

(A) any interest in qualified exchange property shall be treated in the same manner as if it were a portion of the interest in qualified real property which was exchanged,

(B) any tax imposed by subsection (c) by reason of the exchange shall be treated as a tax imposed on a partial disposition, and

(C) paragraph (6) of subsection (c) shall be applied by treating material participation with respect to the ex-

changed property as material participation with respect to the qualified exchange property.

(3) **QUALIFIED EXCHANGE PROPERTY.**—For purposes of this subsection, the term “qualified exchange property” means real property which is to be used for the qualified use set forth in subparagraph (A) or (B) of subsection (b)(2) under which the real property exchanged therefor originally qualified under subsection (a).

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## Subtitle C—Employment Taxes

\* \* \* \* \*

### CHAPTER 24—COLLECTION OF INCOME TAX AT SOURCE ON WAGES

\* \* \* \* \*

#### SEC. 3402. INCOME TAX COLLECTED AT SOURCE.

##### (a) REQUIREMENT OF WITHHOLDING.—

(1) **IN GENERAL.**—Except as otherwise provided in this section, every employer making payment of wages shall deduct and withhold upon such wages a tax determined in accordance with tables or computational procedures prescribed by the Secretary. Any tables or procedures prescribed under this paragraph shall—

(A) apply with respect to the amount of wages paid during such periods as the Secretary may prescribe, and

(B) be in such form, and provide for such amounts to be deducted and withheld, as the Secretary determines to be most appropriate to carry out the purposes of this chapter and to reflect the provisions of chapter 1 applicable to such periods.

(2) **AMOUNT OF WAGES.**—For purposes of applying tables or procedures prescribed under paragraph (1), the term “the amount of wages” means the amount by which the wages exceed the taxpayer’s withholding allowance, prorated to the payroll period.

##### (b) PERCENTAGE METHOD OF WITHHOLDING.—

(1) If wages are paid with respect to a period which is not a payroll period, the withholding allowance allowable with respect to each payment of such wages shall be the allowance allowed for a miscellaneous payroll period containing a number of days (including Sundays and holidays) equal to the number of days in the period with respect to which such wages are paid.

(2) In any case in which wages are paid by an employer without regard to any payroll period or other period, the withholding allowance allowable with respect to each payment of such wages shall be the allowance allowed for a miscellaneous payroll period containing a number of days equal to the number of days (including Sundays and holidays) which have elapsed since the date of the last payment of such wages by

such employer during the calendar year, or the date of commencement of employment with such employer during such year, or January 1 of such year, whichever is the later.

(3) In any case in which the period, or the time described in paragraph (2), in respect of any wages is less than one week, the Secretary, under regulations prescribed by him, may authorize an employer to compute the tax to be deducted and withheld as if the aggregate of the wages paid to the employee during the calendar week were paid for a weekly payroll period.

(4) In determining the amount to be deducted and withheld under this subsection, the wages may, at the election of the employer, be computed to the nearest dollar.

(c) WAGE BRACKET WITHHOLDING.—

(1) At the election of the employer with respect to any employee, the employer shall deduct and withhold upon the wages paid to such employee a tax (in lieu of the tax required to be deducted and withheld under subsection (a)) determined in accordance with tables prescribed by the Secretary in accordance with paragraph (6).

(2) If wages are paid with respect to a period which is not a payroll period, the amount to be deducted and withheld shall be that applicable in the case of a miscellaneous payroll period containing a number of days (including Sundays and holidays) equal to the number of days in the period with respect to which such wages are paid.

(3) In any case in which wages are paid by an employer without regard to any payroll period or other period, the amount to be deducted and withheld shall be that applicable in the case of a miscellaneous payroll period containing a number of days equal to the number of days (including Sundays and holidays) which have elapsed since the date of the last payment of such wages by such employer during the calendar year, or the date of commencement of employment with such employer during such year, or January 1 of such year, whichever is the later.

(4) In any case in which the period, or the time described in paragraph (3), in respect of any wages is less than one week, the Secretary, under regulations prescribed by him, may authorize an employer to determine the amount to be deducted and withheld under the tables applicable in the case of a weekly payroll period, in which case the aggregate of the wages paid to the employee during the calendar week shall be considered the weekly wages.

(5) If the wages exceed the highest wage bracket, in determining the amount to be deducted and withheld under this subsection, the wages may, at the election of the employer, be computed to the nearest dollar.

(6) In the case of wages paid after December 31, 1969, the amount deducted and withheld under paragraph (1) shall be determined in accordance with tables prescribed by the Secretary. In the tables so prescribed, the amounts set forth as amounts of wages and amounts of income tax to be deducted and withheld shall be computed on the basis of the table for an annual payroll period prescribed pursuant to subsection (a).

(d) **TAX PAID BY RECIPIENT.**—If the employer, in violation of the provisions of this chapter, fails to deduct and withhold the tax under this chapter, and thereafter the tax against which such tax may be credited is paid, the tax so required to be deducted and withheld shall not be collected from the employer; but this subsection shall in no case relieve the employer from liability for any penalties or additions to the tax otherwise applicable in respect of such failure to deduct and withhold.

(e) **INCLUDED AND EXCLUDED WAGES.**—If the remuneration paid by an employer to an employee for services performed during one-half or more of any payroll period of not more than 31 consecutive days constitutes wages, all the remuneration paid by such employer to such employee for such period shall be deemed to be wages; but if the remuneration paid by an employer to an employee for services performed during more than one-half of any such payroll period does not constitute wages, then none of the remuneration paid by such employer to such employee for such period shall be deemed to be wages.

(f) **WITHHOLDING ALLOWANCE.**—

(1) **IN GENERAL.**—Under rules determined by the Secretary, an employee receiving wages shall on any day be entitled to a withholding allowance determined based on—

(A) whether the employee is an individual for whom a deduction is allowable with respect to another taxpayer under section 151;

(B) if the employee is married, whether the employee's spouse is entitled to an allowance, or would be so entitled if such spouse were an employee receiving wages, under subparagraph (A) or (D), but only if such spouse does not have in effect a withholding allowance certificate claiming such allowance;

(C) the number of individuals with respect to whom, on the basis of facts existing at the beginning of such day, there may reasonably be expected to be allowable a credit under section 24(a) for the taxable year under subtitle A in respect of which amounts deducted and withheld under this chapter in the calendar year in which such day falls are allowed as a credit;

(D) any additional amounts to which the employee elects to take into account under subsection (m), but only if the employee's spouse does not have in effect a withholding allowance certificate making such an election;

(E) the standard deduction allowable to such employee (one-half of such standard deduction in the case of an employee who is married (as determined under section 7703) and whose spouse is an employee receiving wages subject to withholding); and

(F) whether the employee has withholding allowance certificates in effect with respect to more than 1 employer.

(2) **ALLOWANCE CERTIFICATES.**—

(A) **ON COMMENCEMENT OF EMPLOYMENT.**—On or before the date of the commencement of employment with an employer, the employee shall furnish the employer with a signed withholding allowance certificate relating to the withholding allowance claimed by the employee, which

shall in no event exceed the amount to which the employee is entitled.

(B) CHANGE OF STATUS.—If, on any day during the calendar year, an employee's withholding allowance is in excess of the withholding allowance to which the employee would be entitled had the employee submitted a true and accurate withholding allowance certificate to the employer on that day, the employee shall within 10 days thereafter furnish the employer with a new withholding allowance certificate. If, on any day during the calendar year, an employee's withholding allowance is greater than the withholding allowance claimed, the employee may furnish the employer with a new withholding allowance certificate relating to the withholding allowance to which the employee is so entitled, which shall in no event exceed the amount to which the employee is entitled on such day.

(C) CHANGE OF STATUS WHICH AFFECTS NEXT CALENDAR YEAR.—If on any day during the calendar year the withholding allowance to which the employee will be, or may reasonably be expected to be, entitled at the beginning of the employee's next taxable year under subtitle A is different from the allowance to which the employee is entitled on such day, the employee shall, in such cases and at such times as the Secretary shall by regulations prescribe, furnish the employer with a withholding allowance certificate relating to the withholding allowance which the employee claims with respect to such next taxable year, which shall in no event exceed the withholding allowance to which the employee will be, or may reasonably be expected to be, so entitled.

(3) WHEN CERTIFICATE TAKES EFFECT.—

(A) FIRST CERTIFICATE FURNISHED.—A withholding allowance certificate furnished the employer in cases in which no previous such certificate is in effect shall take effect as of the beginning of the first payroll period ending, or the first payment of wages made without regard to a payroll period, on or after the date on which such certificate is so furnished.

(B) FURNISHED TO TAKE PLACE OF EXISTING CERTIFICATE.—

(i) IN GENERAL.—Except as provided in clauses (ii) and (iii), a withholding allowance certificate furnished to the employer in cases in which a previous such certificate is in effect shall take effect as of the beginning of the 1st payroll period ending (or the 1st payment of wages made without regard to a payroll period) on or after the 30th day after the day on which such certificate is so furnished.

(ii) EMPLOYER MAY ELECT EARLIER EFFECTIVE DATE.—At the election of the employer, a certificate described in clause (i) may be made effective beginning with any payment of wages made on or after the day on which the certificate is so furnished and before the 30th day referred to in clause (i).

(iii) CHANGE OF STATUS WHICH AFFECTS NEXT YEAR.—Any certificate furnished pursuant to paragraph (2)(C) shall not take effect, and may not be made effective, with respect to any payment of wages made in the calendar year in which the certificate is furnished.

(4) PERIOD DURING WHICH CERTIFICATE REMAINS IN EFFECT.—A withholding allowance certificate which takes effect under this subsection, or which on December 31, 1954, was in effect under the corresponding subsection of prior law, shall continue in effect with respect to the employer until another such certificate takes effect under this subsection.

(5) FORM AND CONTENTS OF CERTIFICATE.—Withholding allowance certificates shall be in such form and contain such information as the Secretary may by regulations prescribe.

(6) EXEMPTION OF CERTAIN NONRESIDENT ALIENS.—Notwithstanding the provisions of paragraph (1), a nonresident alien individual (other than an individual described in section 3401(a)(6)(A) or (B)) shall be entitled to only one withholding exemption.

(7) ALLOWANCE WHERE CERTIFICATE WITH ANOTHER EMPLOYER IS IN EFFECT.—If a withholding allowance certificate is in effect with respect to one employer, an employee shall not be entitled under a certificate in effect with any other employer to any withholding allowance which he has claimed under such first certificate.

(g) OVERLAPPING PAY PERIODS, AND PAYMENT BY AGENT OR FIDUCIARY.—If a payment of wages is made to an employee by an employer—

(1) with respect to a payroll period or other period, any part of which is included in a payroll period or other period with respect to which wages are also paid to such employee by such employer, or

(2) without regard to any payroll period or other period, but on or prior to the expiration of a payroll period or other period with respect to which wages are also paid to such employee by such employer, or

(3) with respect to a period beginning in one and ending in another calendar year, or

(4) through an agent, fiduciary, or other person who also has the control, receipt, custody, or disposal of, or pays, the wages payable by another employer to such employee,

the manner of withholding and the amount to be deducted and withheld under this chapter shall be determined in accordance with regulations prescribed by the Secretary under which the withholding allowance allowed to the employee in any calendar year shall approximate the withholding allowance allowable with respect to an annual payroll period.

(h) ALTERNATIVE METHODS OF COMPUTING AMOUNT TO BE WITHHELD.—The Secretary may, under regulations prescribed by him, authorize—

(1) WITHHOLDING ON BASIS OF AVERAGE WAGES.—An employer—

(A) to estimate the wages which will be paid to any employee in any quarter of the calendar year,



(B) to determine the amount to be deducted and withheld upon each payment of wages to such employee during such quarter as if the appropriate average of the wages so estimated constituted the actual wages paid, and

(C) to deduct and withhold upon any payment of wages to such employee during such quarter (and, in the case of tips referred to in subsection (k), within 30 days thereafter) such amount as may be necessary to adjust the amount actually deducted and withheld upon the wages of such employee during such quarter to the amount required to be deducted and withheld during such quarter without regard to this subsection.

(2) WITHHOLDING ON BASIS OF ANNUALIZED WAGES.—An employer to determine the amount of tax to be deducted and withheld upon a payment of wages to an employee for a payroll period by—

(A) multiplying the amount of an employee's wages for a payroll period by the number of such payroll periods in the calendar year,

(B) determining the amount of tax which would be required to be deducted and withheld upon the amount determined under subparagraph (A) if such amount constituted the actual wages for the calendar year and the payroll period of the employee were an annual payroll period, and

(C) dividing the amount of tax determined under subparagraph (B) by the number of payroll periods (described in subparagraph (A)) in the calendar year.

(3) WITHHOLDING ON BASIS OF CUMULATIVE WAGES.—An employer, in the case of any employee who requests to have the amount of tax to be withheld from his wages computed on the basis of his cumulative wages, to—

(A) add the amount of the wages to be paid to the employee for the payroll period to the total amount of wages paid by the employer to the employee during the calendar year,

(B) divide the aggregate amount of wages computed under subparagraph (A) by the number of payroll periods to which such aggregate amount of wages relates,

(C) compute the total amount of tax that would have been required to be deducted and withheld under subsection (a) if the average amount of wages (as computed under subparagraph (B)) had been paid to the employee for the number of payroll periods to which the aggregate amount of wages (computed under subparagraph (A)) relates,

(D) determine the excess, if any, of the amount of tax computed under subparagraph (C) over the total amount of tax deducted and withheld by the employer from wages paid to the employee during the calendar year, and

(E) deduct and withhold upon the payment of wages (referred to in subparagraph (A)) to the employee an amount equal to the excess (if any) computed under subparagraph (D).

(4) OTHER METHODS.—An employer to determine the amount of tax to be deducted and withheld upon the wages paid to an employee by any other method which will require the employer to deduct and withhold upon such wages substantially the same amount as would be required to be deducted and withheld by applying subsection (a) or (c), either with respect to a payroll period or with respect to the entire taxable year.

(i) CHANGES IN WITHHOLDING.—

(1) IN GENERAL.—The Secretary may by regulations provide for increases in the amount of withholding otherwise required under this section in cases where the employee requests such changes.

(2) TREATMENT AS TAX.—Any increased withholding under paragraph (1) shall for all purposes be considered tax required to be deducted and withheld under this chapter.

(j) NONCASH REMUNERATION TO RETAIL COMMISSION SALESMAN.—In the case of remuneration paid in any medium other than cash for services performed by an individual as a retail salesman for a person, where the service performed by such individual for such person is ordinarily performed for remuneration solely by way of cash commission an employer shall not be required to deduct or withhold any tax under this subchapter with respect to such remuneration, provided that such employer files with the Secretary such information with respect to such remuneration as the Secretary may by regulation prescribe.

(k) TIPS.—In the case of tips which constitute wages, subsection (a) shall be applicable only to such tips as are included in a written statement furnished to the employer pursuant to section 6053(a), and only to the extent that the tax can be deducted and withheld by the employer, at or after the time such statement is so furnished and before the close of the calendar year in which such statement is furnished, from such wages of the employee (excluding tips, but including funds turned over by the employee to the employer for the purpose of such deduction and withholding) as are under the control of the employer; and an employer who is furnished by an employee a written statement of tips (received in a calendar month) pursuant to section 6053(a) to which paragraph (16)(B) of section 3401(a) is applicable may deduct and withhold the tax with respect to such tips from any wages of the employee (excluding tips) under his control, even though at the time such statement is furnished the total amount of the tips included in statements furnished to the employer as having been received by the employee in such calendar month in the course of his employment by such employer is less than \$20. Such tax shall not at any time be deducted and withheld in an amount which exceeds the aggregate of such wages and funds (including funds turned over under section 3102(c)(2) or section 3202(c)(2)) minus any tax required by section 3102(a) or section 3202(a) to be collected from such wages and funds.

(l) DETERMINATION AND DISCLOSURE OF MARITAL STATUS.—

(1) DETERMINATION OF STATUS BY EMPLOYER.—For purposes of applying the tables in subsections (a) and (c) to a payment of wages, the employer shall treat the employee as a single person unless there is in effect with respect to such payment of wages a withholding allowance certificate furnished to the

employer by the employee after the date of the enactment of this subsection indicating that the employee is married.

(2) **DISCLOSURE OF STATUS BY EMPLOYEE.**—An employee shall be entitled to furnish the employer with a withholding allowance certificate indicating he is married only if, on the day of such furnishing, he is married (determined with the application of the rules in paragraph (3)). An employee whose marital status changes from married to single shall, at such time as the Secretary may by regulations prescribe, furnish the employer with a new withholding allowance certificate.

(3) **DETERMINATION OF MARITAL STATUS.**—For purposes of paragraph (2), an employee shall on any day be considered—

(A) as not married, if (i) he is legally separated from his spouse under a decree of divorce or separate maintenance, or (ii) either he or his spouse is, or on any preceding day within the calendar year was, a nonresident alien; or

(B) as married, if (i) his spouse (other than a spouse referred to in subparagraph (A)) died within the portion of his taxable year which precedes such day, or (ii) his spouse died during one of the two taxable years immediately preceding the current taxable year and, on the basis of facts existing at the beginning of such day, the employee reasonably expects, at the close of his taxable year, to be a surviving spouse (as defined in section 2(a)).

(m) **WITHHOLDING ALLOWANCES.**—Under regulations prescribed by the Secretary, an employee shall be entitled to an additional withholding allowance or additional reductions in withholding under this subsection. In determining the additional withholding allowance or the amount of additional reductions in withholding under this subsection, the employee may take into account (to the extent and in the manner provided by such regulations)—

(1) estimated itemized deductions allowable under chapter 1 and the estimated deduction allowed under section 199A (other than the deductions referred to in section 151 and) other than the deductions required to be taken into account in determining adjusted gross income under section 62(a),

(2) estimated tax credits allowable under chapter 1, and

(3) such additional deductions (including the additional standard deduction under section 63(c)(3) for the aged and blind) and other items as may be specified by the Secretary in regulations.

(n) **EMPLOYEES INCURRING NO INCOME TAX LIABILITY.**—Notwithstanding any other provision of this section, an employer shall not be required to deduct and withhold any tax under this chapter upon a payment of wages to an employee if there is in effect with respect to such payment a withholding allowance certificate (in such form and containing such other information as the Secretary may prescribe) furnished to the employer by the employee certifying that the employee—

(1) incurred no liability for income tax imposed under subtitle A for his preceding taxable year, and

(2) anticipates that he will incur no liability for income tax imposed under subtitle A for his current taxable year.

The Secretary shall by regulations provide for the coordination of the provisions of this subsection with the provisions of subsection (f).

(o) EXTENSION OF WITHHOLDING TO CERTAIN PAYMENTS OTHER THAN WAGES.—

(1) GENERAL RULE.—For purposes of this chapter (and so much of subtitle F as relates to this chapter)—

(A) any supplemental unemployment compensation benefit paid to an individual,

(B) any payment of an annuity to an individual, if at the time the payment is made a request that such annuity be subject to withholding under this chapter is in effect, and

(C) any payment to an individual of sick pay which does not constitute wages (determined without regard to this subsection), if at the time the payment is made a request that such sick pay be subject to withholding under this chapter is in effect,

shall be treated as if it were a payment of wages by an employer to an employee for a payroll period.

(2) DEFINITIONS.—

(A) SUPPLEMENTAL UNEMPLOYMENT COMPENSATION BENEFITS.—For purposes of paragraph (1), the term “supplemental unemployment compensation benefits” means amounts which are paid to an employee, pursuant to a plan to which the employer is a party, because of an employee’s involuntary separation from employment (whether or not such separation is temporary), resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions, but only to the extent such benefits are includible in the employee’s gross income.

(B) ANNUITY.—For purposes of this subsection, the term “annuity” means any amount paid to an individual as a pension or annuity.

(C) SICK PAY.—For purposes of this subsection, the term “sick pay” means any amount which—

(i) is paid to an employee pursuant to a plan to which the employer is a party, and

(ii) constitutes remuneration or a payment in lieu of remuneration for any period during which the employee is temporarily absent from work on account of sickness or personal injuries.

(3) AMOUNT WITHHELD FROM ANNUITY PAYMENTS OR SICK PAY.—If a payee makes a request that an annuity or any sick pay be subject to withholding under this chapter, the amount to be deducted and withheld under this chapter from any payment to which such request applies shall be an amount (not less than a minimum amount determined under regulations prescribed by the Secretary) specified by the payee in such request. The amount deducted and withheld with respect to a payment which is greater or less than a full payment shall bear the same relation to the specified amount as such payment bears to a full payment.

(4) REQUEST FOR WITHHOLDING.—A request that an annuity or any sick pay be subject to withholding under this chapter—

(A) shall be made by the payee in writing to the person making the payments and shall contain the social security number of the payee,

(B) shall specify the amount to be deducted and withheld from each full payment, and

(C) shall take effect—

(i) in the case of sick pay, with respect to payments made more than 7 days after the date on which such request is furnished to the payor, or

(ii) in the case of an annuity, at such time (after the date on which such request is furnished to the payor) as the Secretary shall by regulations prescribe.

Such a request may be changed or terminated by furnishing to the person making the payments a written statement of change or termination which shall take effect in the same manner as provided in subparagraph (C). At the election of the payor, any such request (or statement of change or revocation) may take effect earlier than as provided in subparagraph (C).

(5) SPECIAL RULE FOR SICK PAY PAID PURSUANT TO CERTAIN COLLECTIVE-BARGAINING AGREEMENTS.—In the case of any sick pay paid pursuant to a collective-bargaining agreement between employee representatives and one or more employers which contains a provision specifying that this paragraph is to apply to sick pay paid pursuant to such agreement and contains a provision for determining the amount to be deducted and withheld from each payment of such sick pay—

(A) the requirement of paragraph (1)(C) that a request for withholding be in effect shall not apply, and

(B) except as provided in subsection (n), the amounts to be deducted and withheld under this chapter shall be determined in accordance with such agreement.

The preceding sentence shall not apply with respect to sick pay paid pursuant to any agreement to any individual unless the social security number of such individual is furnished to the payor and the payor is furnished with such information as is necessary to determine whether the payment is pursuant to the agreement and to determine the amount to be deducted and withheld.

(6) COORDINATION WITH WITHHOLDING ON DESIGNATED DISTRIBUTIONS UNDER SECTION 3405.—This subsection shall not apply to any amount which is a designated distribution (within the meaning of section 3405(e)(1)).

(p) VOLUNTARY WITHHOLDING AGREEMENTS.—

(1) CERTAIN FEDERAL PAYMENTS.—

(A) IN GENERAL.—If, at the time a specified Federal payment is made to any person, a request by such person is in effect that such payment be subject to withholding under this chapter, then for purposes of this chapter and so much of subtitle F as relates to this chapter, such payment shall be treated as if it were a payment of wages by an employer to an employee.

(B) AMOUNT WITHHELD.—The amount to be deducted and withheld under this chapter from any payment to which any request under subparagraph (A) applies shall be an amount equal to the percentage of such payment speci-

fied in such request. Such a request shall apply to any payment only if the percentage specified is 7 percent, any percentage applicable to any of the 3 lowest income brackets in the table under section 1(c), or such other percentage as is permitted under regulations prescribed by the Secretary.

(C) SPECIFIED FEDERAL PAYMENTS.—For purposes of this paragraph, the term “specified Federal payment” means—

(i) any payment of a social security benefit (as defined in section 86(d)),

(ii) any payment referred to in the second sentence of section 451(d) which is treated as insurance proceeds,

(iii) any amount which is includible in gross income under section 77(a), and

(iv) any other payment made pursuant to Federal law which is specified by the Secretary for purposes of this paragraph.

(D) REQUESTS FOR WITHHOLDING.—Rules similar to the rules that apply to annuities under subsection (o)(4) shall apply to requests under this paragraph and paragraph (2).

(2) VOLUNTARY WITHHOLDING ON UNEMPLOYMENT BENEFITS.—If, at the time a payment of unemployment compensation (as defined in section 85(b)) is made to any person, a request by such person is in effect that such payment be subject to withholding under this chapter, then for purposes of this chapter and so much of subtitle F as relates to this chapter, such payment shall be treated as if it were a payment of wages by an employer to an employee. The amount to be deducted and withheld under this chapter from any payment to which any request under this paragraph applies shall be an amount equal to 10 percent of such payment.

(3) AUTHORITY FOR OTHER VOLUNTARY WITHHOLDING.—The Secretary is authorized by regulations to provide for withholding—

(A) from remuneration for services performed by an employee for the employee’s employer which (without regard to this paragraph) does not constitute wages, and

(B) from any other type of payment with respect to which the Secretary finds that withholding would be appropriate under the provisions of this chapter,

if the employer and employee, or the person making and the person receiving such other type of payment, agree to such withholding. Such agreement shall be in such form and manner as the Secretary may by regulations prescribe. For purposes of this chapter (and so much of subtitle F as relates to this chapter), remuneration or other payments with respect to which such agreement is made shall be treated as if they were wages paid by an employer to an employee to the extent that such remuneration is paid or other payments are made during the period for which the agreement is in effect.

(q) EXTENSION OF WITHHOLDING TO CERTAIN GAMBLING WINNINGS.—

(1) GENERAL RULE.—Every person, including the Government of the United States, a State, or a political subdivision thereof,

or any instrumentalities of the foregoing, making any payment of winnings which are subject to withholding shall deduct and withhold from such payment a tax in an amount equal to the product of the ~~【third lowest】~~ *fourth lowest* rate of tax applicable under section 1(c) and such payment.

(2) EXEMPTION WHERE TAX OTHERWISE WITHHELD.—In the case of any payment of winnings which are subject to withholding made to a nonresident alien individual or a foreign corporation, the tax imposed under paragraph (1) shall not apply to any such payment subject to tax under section 1441(a) (relating to withholding on nonresident aliens) or tax under section 1442(a) (relating to withholding on foreign corporations).

(3) WINNINGS WHICH ARE SUBJECT TO WITHHOLDING.—For purposes of this subsection, the term “winnings which are subject to withholding” means proceeds from a wager determined in accordance with the following:

(A) IN GENERAL.—Except as provided in subparagraphs (B) and (C), proceeds of more than \$5,000 from a wagering transaction, if the amount of such proceeds is at least 300 times as large as the amount wagered.

(B) STATE-CONDUCTED LOTTERIES.—Proceeds of more than \$5,000 from a wager placed in a lottery conducted by an agency of a State acting under authority of State law, but only if such wager is placed with the State agency conducting such lottery, or with its authorized employees or agents.

(C) SWEEPSTAKES, WAGERING POOLS, CERTAIN PARIMUTUEL POOLS, JAI ALAI, AND LOTTERIES.—Proceeds of more than \$5,000 from—

(i) a wager placed in a sweepstakes, wagering pool, or lottery (other than a wager described in subparagraph (B)), or

(ii) a wagering transaction in a parimutuel pool with respect to horse races, dog races, or jai alai if the amount of such proceeds is at least 300 times as large as the amount wagered.

(4) RULES FOR DETERMINING PROCEEDS FROM A WAGER.—For purposes of this subsection—

(A) proceeds from a wager shall be determined by reducing the amount received by the amount of the wager, and

(B) proceeds which are not money shall be taken into account at their fair market value.

(5) EXCEPTION FOR BINGO, KENO, AND SLOT MACHINES.—The tax imposed under paragraph (1) shall not apply to winnings from a slot machine, keno, and bingo.

(6) STATEMENT BY RECIPIENT.—Every person who is to receive a payment of winnings which are subject to withholding shall furnish the person making such payment a statement, made under the penalties of perjury, containing the name, address, and taxpayer identification number of the person receiving the payment and of each person entitled to any portion of such payment.

(7) COORDINATION WITH OTHER SECTIONS.—For purposes of sections 3403 and 3404 and for purposes of so much of subtitle F (except section 7205) as relates to this chapter, payments to

any person of winnings which are subject to withholding shall be treated as if they were wages paid by an employer to an employee.

(r) EXTENSION OF WITHHOLDING TO CERTAIN TAXABLE PAYMENTS OF INDIAN CASINO PROFITS.—

(1) IN GENERAL.—Every person, including an Indian tribe, making a payment to a member of an Indian tribe from the net revenues of any class II or class III gaming activity conducted or licensed by such tribe shall deduct and withhold from such payment a tax in an amount equal to such payment's proportionate share of the annualized tax.

(2) EXCEPTION.—The tax imposed by paragraph (1) shall not apply to any payment to the extent that the payment, when annualized, does not exceed an amount equal to [the sum of—

[(A) the basic standard deduction (as defined in section 63(c) for an individual to whom section 63(c)(2)(C) applies, and

[(B) the exemption amount (as defined in section 151(d)).] *the basic standard deduction (as defined in section 63(c) for an individual to whom section 63(c)(2)(C) applies.*

(3) ANNUALIZED TAX.—For purposes of paragraph (1), the term “annualized tax” means, with respect to any payment, the amount of tax which would be imposed by section 1(c) (determined without regard to any rate of tax in excess of the fourth lowest rate of tax applicable under section 1(c)) on an amount of taxable income equal to the excess of—

(A) the annualized amount of such payment, over

(B) the amount determined under paragraph (2).

(4) CLASSES OF GAMING ACTIVITIES, ETC.—For purposes of this subsection, terms used in paragraph (1) which are defined in section 4 of the Indian Gaming Regulatory Act (25 U.S.C. 2701 et seq.), as in effect on the date of the enactment of this subsection, shall have the respective meanings given such terms by such section.

(5) ANNUALIZATION.—Payments shall be placed on an annualized basis under regulations prescribed by the Secretary.

(6) ALTERNATE WITHHOLDING PROCEDURES.—At the election of an Indian tribe, the tax imposed by this subsection on any payment made by such tribe shall be determined in accordance with such tables or computational procedures as may be specified in regulations prescribed by the Secretary (in lieu of in accordance with paragraphs (2) and (3)).

(7) COORDINATION WITH OTHER SECTIONS.—For purposes of this chapter and so much of subtitle F as relates to this chapter, payments to any person which are subject to withholding under this subsection shall be treated as if they were wages paid by an employer to an employee.

(s) EXEMPTION FROM WITHHOLDING FOR ANY VEHICLE FRINGE BENEFIT.—

(1) EMPLOYER ELECTION NOT TO WITHHOLD.—The employer may elect not to deduct and withhold any tax under this chapter with respect to any vehicle fringe benefit provided to any employee if such employee is notified by the employer of such



election (at such time and in such manner as the Secretary shall by regulations prescribe). The preceding sentence shall not apply to any vehicle fringe benefit unless the amount of such benefit is included by the employer on a statement timely furnished under section 6051.

(2) **EMPLOYER MUST FURNISH W-2.**—Any vehicle fringe benefit shall be treated as wages from which amounts are required to be deducted and withheld under this chapter for purposes of section 6051.

(3) **VEHICLE FRINGE BENEFIT.**—For purposes of this subsection, the term “vehicle fringe benefit” means any fringe benefit—

(A) which constitutes wages (as defined in section 3401), and

(B) which consists of providing a highway motor vehicle for the use of the employee.

(t) **RATE OF WITHHOLDING FOR CERTAIN STOCK.**—In the case of any qualified stock (as defined in section 83(i)(2)) with respect to which an election is made under section 83(i)—

(1) the rate of tax under subsection (a) shall not be less than the maximum rate of tax in effect under section 1, and

(2) such stock shall be treated for purposes of section 3501(b) in the same manner as a non-cash fringe benefit.

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## **Subtitle D—Miscellaneous Excise Taxes**

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### **CHAPTER 48—MAINTENANCE OF MINIMUM ESSENTIAL COVERAGE**

Sec. 5000A. Requirement to maintain minimum essential coverage.

#### **SEC. 5000A. REQUIREMENT TO MAINTAIN MINIMUM ESSENTIAL COVERAGE.**

(a) **REQUIREMENT TO MAINTAIN MINIMUM ESSENTIAL COVERAGE.**—An applicable individual shall for each month beginning after 2013 ensure that the individual, and any dependent of the individual who is an applicable individual, is covered under minimum essential coverage for such month.

(b) **SHARED RESPONSIBILITY PAYMENT.**—

(1) **IN GENERAL.**—If a taxpayer who is an applicable individual, or an applicable individual for whom the taxpayer is liable under paragraph (3), fails to meet the requirement of subsection (a) for 1 or more months, then, except as provided in subsection (e), there is hereby imposed on the taxpayer a penalty with respect to such failures in the amount determined under subsection (c).

(2) **INCLUSION WITH RETURN.**—Any penalty imposed by this section with respect to any month shall be included with a taxpayer’s return under chapter 1 for the taxable year which includes such month.

(3) PAYMENT OF PENALTY.—If an individual with respect to whom a penalty is imposed by this section for any month—

(A) is a dependent (as defined in [section 152] *section 7706*) of another taxpayer for the other taxpayer's taxable year including such month, such other taxpayer shall be liable for such penalty, or

(B) files a joint return for the taxable year including such month, such individual and the spouse of such individual shall be jointly liable for such penalty.

(c) AMOUNT OF PENALTY.—

(1) IN GENERAL.—The amount of the penalty imposed by this section on any taxpayer for any taxable year with respect to failures described in subsection (b)(1) shall be equal to the lesser of—

(A) the sum of the monthly penalty amounts determined under paragraph (2) for months in the taxable year during which 1 or more such failures occurred, or

(B) an amount equal to the national average premium for qualified health plans which have a bronze level of coverage, provide coverage for the applicable family size involved, and are offered through Exchanges for plan years beginning in the calendar year with or within which the taxable year ends.

(2) MONTHLY PENALTY AMOUNTS.—For purposes of paragraph (1)(A), the monthly penalty amount with respect to any taxpayer for any month during which any failure described in subsection (b)(1) occurred is an amount equal to  $\frac{1}{12}$  of the greater of the following amounts:

(A) FLAT DOLLAR AMOUNT.—An amount equal to the lesser of—

(i) the sum of the applicable dollar amounts for all individuals with respect to whom such failure occurred during such month, or

(ii) 300 percent of the applicable dollar amount (determined without regard to paragraph (3)(C)) for the calendar year with or within which the taxable year ends.

(B) PERCENTAGE OF INCOME.—An amount equal to the following percentage of the excess of the taxpayer's household income for the taxable year over the amount of gross income specified in section 6012(a)(1) with respect to the taxpayer for the taxable year:

(i) 1.0 percent for taxable years beginning in 2014.

(ii) 2.0 percent for taxable years beginning in 2015.

(iii) Zero percent for taxable years beginning after 2015.

(3) APPLICABLE DOLLAR AMOUNT.—For purposes of paragraph (1)—

(A) IN GENERAL.—Except as provided in subparagraphs (B) and (C), the applicable dollar amount is \$0.

(B) PHASE IN.—The applicable dollar amount is \$95 for 2014 and \$325 for 2015.

(C) SPECIAL RULE FOR INDIVIDUALS UNDER AGE 18.—If an applicable individual has not attained the age of 18 as of the beginning of a month, the applicable dollar amount

with respect to such individual for the month shall be equal to one-half of the applicable dollar amount for the calendar year in which the month occurs.

(4) TERMS RELATING TO INCOME AND FAMILIES.—For purposes of this section—

(A) FAMILY SIZE.—The family size involved with respect to any taxpayer shall be equal to [the number of individuals for whom the taxpayer is allowed a deduction under section 151 (relating to allowance of deduction for personal exemptions) for the taxable year] *the sum of 1 (2 in the case of a joint return) plus the number of the taxpayer's dependents for the taxable year.*

(B) HOUSEHOLD INCOME.—The term “household income” means, with respect to any taxpayer for any taxable year, an amount equal to the sum of—

(i) the modified adjusted gross income of the taxpayer, plus

(ii) the aggregate modified adjusted gross incomes of all other individuals who—

(I) were taken into account in determining the taxpayer's family size under paragraph (1), and

(II) were required to file a return of tax imposed by section 1 for the taxable year.

(C) MODIFIED ADJUSTED GROSS INCOME.—The term “modified adjusted gross income” means adjusted gross income increased by—

(i) any amount excluded from gross income under section 911, and

(ii) any amount of interest received or accrued by the taxpayer during the taxable year which is exempt from tax.

(d) APPLICABLE INDIVIDUAL.—For purposes of this section—

(1) IN GENERAL.—The term “applicable individual” means, with respect to any month, an individual other than an individual described in paragraph (2), (3), or (4).

(2) RELIGIOUS EXEMPTIONS.—

(A) RELIGIOUS CONSCIENCE EXEMPTION.—Such term shall not include any individual for any month if such individual has in effect an exemption under section 1311(d)(4)(H) of the Patient Protection and Affordable Care Act which certifies that such individual is—

(i) a member of a recognized religious sect or division thereof which is described in section 1402(g)(1), and

(ii) an adherent of established tenets or teachings of such sect or division as described in such section.

(B) HEALTH CARE SHARING MINISTRY.—

(i) IN GENERAL.—Such term shall not include any individual for any month if such individual is a member of a health care sharing ministry for the month.

(ii) HEALTH CARE SHARING MINISTRY.—The term “health care sharing ministry” means an organization—

(I) which is described in section 501(c)(3) and is exempt from taxation under section 501(a),

(II) members of which share a common set of ethical or religious beliefs and share medical expenses among members in accordance with those beliefs and without regard to the State in which a member resides or is employed,

(III) members of which retain membership even after they develop a medical condition,

(IV) which (or a predecessor of which) has been in existence at all times since December 31, 1999, and medical expenses of its members have been shared continuously and without interruption since at least December 31, 1999, and

(V) which conducts an annual audit which is performed by an independent certified public accounting firm in accordance with generally accepted accounting principles and which is made available to the public upon request.

(3) **INDIVIDUALS NOT LAWFULLY PRESENT.**—Such term shall not include an individual for any month if for the month the individual is not a citizen or national of the United States or an alien lawfully present in the United States.

(4) **INCARCERATED INDIVIDUALS.**—Such term shall not include an individual for any month if for the month the individual is incarcerated, other than incarceration pending the disposition of charges.

(e) **EXEMPTIONS.**—No penalty shall be imposed under subsection (a) with respect to—

(1) **INDIVIDUALS WHO CANNOT AFFORD COVERAGE.**—

(A) **IN GENERAL.**—Any applicable individual for any month if the applicable individual's required contribution (determined on an annual basis) for coverage for the month exceeds 8 percent of such individual's household income for the taxable year described in section 1412(b)(1)(B) of the Patient Protection and Affordable Care Act. For purposes of applying this subparagraph, the taxpayer's household income shall be increased by any exclusion from gross income for any portion of the required contribution made through a salary reduction arrangement.

(B) **REQUIRED CONTRIBUTION.**—For purposes of this paragraph, the term "required contribution" means—

(i) in the case of an individual eligible to purchase minimum essential coverage consisting of coverage through an eligible-employer-sponsored plan, the portion of the annual premium which would be paid by the individual (without regard to whether paid through salary reduction or otherwise) for self-only coverage, or

(ii) in the case of an individual eligible only to purchase minimum essential coverage described in subsection (f)(1)(C), the annual premium for the lowest cost bronze plan available in the individual market through the Exchange in the State in the rating area in which the individual resides (without regard to whether the individual purchased a qualified health plan through the Exchange), reduced by the amount of

the credit allowable under section 36B for the taxable year (determined as if the individual was covered by a qualified health plan offered through the Exchange for the entire taxable year).

(C) SPECIAL RULES FOR INDIVIDUALS RELATED TO EMPLOYEES.—For purposes of subparagraph (B)(i), if an applicable individual is eligible for minimum essential coverage through an employer by reason of a relationship to an employee, the determination under subparagraph (A) shall be made by reference to required contribution of the employee.

(D) INDEXING.—In the case of plan years beginning in any calendar year after 2014, subparagraph (A) shall be applied by substituting for “8 percent” the percentage the Secretary of Health and Human Services determines reflects the excess of the rate of premium growth between the preceding calendar year and 2013 over the rate of income growth for such period.

(2) TAXPAYERS WITH INCOME BELOW FILING THRESHOLD.—Any applicable individual for any month during a calendar year if the individual’s household income for the taxable year described in section 1412(b)(1)(B) of the Patient Protection and Affordable Care Act is the amount of gross income specified in section 6012(a)(1) with respect to the taxpayer.

(3) MEMBERS OF INDIAN TRIBES.—Any applicable individual for any month during which the individual is a member of an Indian tribe (as defined in section 45A(c)(6)).

(4) MONTHS DURING SHORT COVERAGE GAPS.—

(A) IN GENERAL.—Any month the last day of which occurred during a period in which the applicable individual was not covered by minimum essential coverage for a continuous period of less than 3 months.

(B) SPECIAL RULES.—For purposes of applying this paragraph—

(i) the length of a continuous period shall be determined without regard to the calendar years in which months in such period occur,

(ii) if a continuous period is greater than the period allowed under subparagraph (A), no exception shall be provided under this paragraph for any month in the period, and

(iii) if there is more than 1 continuous period described in subparagraph (A) covering months in a calendar year, the exception provided by this paragraph shall only apply to months in the first of such periods.

The Secretary shall prescribe rules for the collection of the penalty imposed by this section in cases where continuous periods include months in more than 1 taxable year.

(5) HARDSHIPS.—Any applicable individual who for any month is determined by the Secretary of Health and Human Services under section 1311(d)(4)(H) to have suffered a hardship with respect to the capability to obtain coverage under a qualified health plan.

(f) MINIMUM ESSENTIAL COVERAGE.—For purposes of this section—

(1) IN GENERAL.—The term “minimum essential coverage” means any of the following:

(A) GOVERNMENT SPONSORED PROGRAMS.—Coverage under—

(i) the Medicare program under part A of title XVIII of the Social Security Act,

(ii) the Medicaid program under title XIX of the Social Security Act,

(iii) the CHIP program under title XXI of the Social Security Act or under a qualified CHIP look-alike program (as defined in section 2107(g) of the Social Security Act),

(iv) medical coverage under chapter 55 of title 10, United States Code, including coverage under the TRICARE program;

(v) a health care program under chapter 17 or 18 of title 38, United States Code, as determined by the Secretary of Veterans Affairs, in coordination with the Secretary of Health and Human Services and the Secretary,

(vi) a health plan under section 2504(e) of title 22, United States Code (relating to Peace Corps volunteers); or

(vii) the Nonappropriated Fund Health Benefits Program of the Department of Defense, established under section 349 of the National Defense Authorization Act for Fiscal Year 1995 (Public Law 103-337; 10 U.S.C. 1587 note).

(B) EMPLOYER-SPONSORED PLAN.—Coverage under an eligible employer-sponsored plan.

(C) PLANS IN THE INDIVIDUAL MARKET.—Coverage under a health plan offered in the individual market within a State.

(D) GRANDFATHERED HEALTH PLAN.—Coverage under a grandfathered health plan.

(E) OTHER COVERAGE.—Such other health benefits coverage, such as a State health benefits risk pool, as the Secretary of Health and Human Services, in coordination with the Secretary, recognizes for purposes of this subsection.

(2) ELIGIBLE EMPLOYER-SPONSORED PLAN.—The term “eligible employer-sponsored plan” means, with respect to any employee, a group health plan or group health insurance coverage offered by an employer to the employee which is—

(A) a governmental plan (within the meaning of section 2791(d)(8) of the Public Health Service Act), or

(B) any other plan or coverage offered in the small or large group market within a State.

Such term shall include a grandfathered health plan described in paragraph (1)(D) offered in a group market.

(3) EXCEPTED BENEFITS NOT TREATED AS MINIMUM ESSENTIAL COVERAGE.—The term “minimum essential coverage” shall not include health insurance coverage which consists of coverage of excepted benefits—

(A) described in paragraph (1) of subsection (c) of section 2791 of the Public Health Service Act; or

(B) described in paragraph (2), (3), or (4) of such subsection if the benefits are provided under a separate policy, certificate, or contract of insurance.

(4) INDIVIDUALS RESIDING OUTSIDE UNITED STATES OR RESIDENTS OF TERRITORIES.—Any applicable individual shall be treated as having minimum essential coverage for any month—

(A) if such month occurs during any period described in subparagraph (A) or (B) of section 911(d)(1) which is applicable to the individual, or

(B) if such individual is a bona fide resident of any possession of the United States (as determined under section 937(a)) for such month.

(5) INSURANCE-RELATED TERMS.—Any term used in this section which is also used in title I of the Patient Protection and Affordable Care Act shall have the same meaning as when used in such title.

(g) ADMINISTRATION AND PROCEDURE.—

(1) IN GENERAL.—The penalty provided by this section shall be paid upon notice and demand by the Secretary, and except as provided in paragraph (2), shall be assessed and collected in the same manner as an assessable penalty under subchapter B of chapter 68.

(2) SPECIAL RULES.—Notwithstanding any other provision of law—

(A) WAIVER OF CRIMINAL PENALTIES.—In the case of any failure by a taxpayer to timely pay any penalty imposed by this section, such taxpayer shall not be subject to any criminal prosecution or penalty with respect to such failure.

(B) LIMITATIONS ON LIENS AND LEVIES.—The Secretary shall not—

(i) file notice of lien with respect to any property of a taxpayer by reason of any failure to pay the penalty imposed by this section, or

(ii) levy on any such property with respect to such failure.

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**Subtitle F—Procedure and Administration**

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**CHAPTER 61—INFORMATION AND RETURNS**

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**Subchapter A—Returns and Records**

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**PART II—TAX RETURNS OR STATEMENTS**

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### Subpart B—Income Tax Returns

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#### SEC. 6012. PERSONS REQUIRED TO MAKE RETURNS OF INCOME.

(a) GENERAL RULE.—Returns with respect to income taxes under subtitle A shall be made by the following:

[(1)(A) Every individual having for the taxable year gross income which equals or exceeds the exemption amount, except that a return shall not be required of an individual—

[(i) who is not married (determined by applying section 7703), is not a surviving spouse (as defined in section 2(a)), is not a head of a household (as defined in section 2(b)), and for the taxable year has gross income of less than the sum of the exemption amount plus the basic standard deduction applicable to such an individual,

[(ii) who is a head of a household (as so defined) and for the taxable year has gross income of less than the sum of the exemption amount plus the basic standard deduction applicable to such an individual,

[(iii) who is a surviving spouse (as so defined) and for the taxable year has gross income of less than the sum of the exemption amount plus the basic standard deduction applicable to such an individual, or

[(iv) who is entitled to make a joint return and whose gross income, when combined with the gross income of his spouse, is, for the taxable year, less than the sum of twice the exemption amount plus the basic standard deduction applicable to a joint return, but only if such individual and his spouse, at the close of the taxable year, had the same household as their home.

Clause (iv) shall not apply if for the taxable year such spouse makes a separate return or any other taxpayer is entitled to an exemption for such spouse under section 151(c).

[(B) The amount specified in clause (i), (ii), or (iii) of subparagraph (A) shall be increased by the amount of 1 additional standard deduction (within the meaning of section 63(c)(3)) in the case of an individual entitled to such deduction by reason of section 63(f)(1)(A) (relating to individuals age 65 or more), and the amount specified in clause (iv) of subparagraph (A) shall be increased by the amount of the additional standard deduction for each additional standard deduction to which the individual or his spouse is entitled by reason of section 63(f)(1).

[(C) The exception under subparagraph (A) shall not apply to any individual—

[(i) who is described in section 63(c)(5) and who has—

[(I) income (other than earned income) in excess of the sum of the amount in effect under section 63(c)(5)(A) plus the additional standard deduction (if any) to which the individual is entitled, or

[(II) total gross income in excess of the standard deduction, or



[(ii) for whom the standard deduction is zero under section 63(c)(6).

[(D) For purposes of this subsection—

[(i) The terms “standard deduction”, “basic standard deduction” and “additional standard deduction” have the respective meanings given such terms by section 63(c).

[(ii) The term “exemption amount” has the meaning given such term by section 151(d). In the case of an individual described in section 151(d)(2), the exemption amount shall be zero.]

(1) *Every individual who has gross income for the taxable year, except that a return shall not be required of—*

(A) *an individual who is not married (determined by applying section 7703) and who has gross income for the taxable year which does not exceed the standard deduction applicable to such individual for such taxable year under section 63, or*

(B) *an individual entitled to make a joint return if—*

(i) *the gross income of such individual, when combined with the gross income of such individual’s spouse, for the taxable year does not exceed the standard deduction which would be applicable for such taxable year under section 63 if such individual and such individual’s spouse made a joint return,*

(ii) *such individual’s spouse does not make a separate return, and*

(iii) *neither such individual nor such individual’s spouse is an individual described in section 63(c)(4) who has income (other than earned income) in excess of the amount in effect under section 63(c)(4)(A).*

(2) Every corporation subject to taxation under subtitle A;

(3) Every estate the gross income of which for the taxable year is \$600 or more;

(4) Every trust having for the taxable year any taxable income, or having gross income of \$600 or over, regardless of the amount of taxable income;

(5) Every estate or trust of which any beneficiary is a non-resident alien;

(6) Every political organization (within the meaning of section 527(e)(1)), and every fund treated under section 527(g) as if it constituted a political organization, which has political organization taxable income (within the meaning of section 527(c)(1)) for the taxable year;

(7) Every homeowners association (within the meaning of section 528(c)(1)) which has homeowners association taxable income (within the meaning of section 528(d)) for the taxable year; and

(8) Every estate of an individual under chapter 7 or 11 of title 11 of the United States Code (relating to bankruptcy) the gross income of which for the taxable year is not less than [(the sum of the exemption amount plus the basic standard deduction under section 63(c)(2)(C))] *the standard deduction in effect under section 63(c)(1)(B)*;

except that subject to such conditions, limitations, and exceptions and under such regulations as may be prescribed by the Secretary, nonresident alien individuals subject to the tax imposed by section 871 and foreign corporations subject to the tax imposed by section 881 may be exempted from the requirement of making returns under this section.

(b) RETURNS MADE BY FIDUCIARIES AND RECEIVERS.—

(1) RETURNS OF DECEDENTS.—If an individual is deceased, the return of such individual required under subsection (a) shall be made by his executor, administrator, or other person charged with the property of such decedent.

(2) PERSONS UNDER A DISABILITY.—If an individual is unable to make a return required under subsection (a), the return of such individual shall be made by a duly authorized agent, his committee, guardian, fiduciary or other person charged with the care of the person or property of such individual. The preceding sentence shall not apply in the case of a receiver appointed by authority of law in possession of only a part of the property of an individual.

(3) RECEIVERS, TRUSTEES AND ASSIGNEES FOR CORPORATIONS.—In a case where a receiver, trustee in a case under title 11 of the United States Code, or assignee, by order of a court of competent jurisdiction, by operation of law or otherwise, has possession of or holds title to all or substantially all the property or business of a corporation, whether or not such property or business is being operated, such receiver, trustee, or assignee shall make the return of income for such corporation in the same manner and form as corporations are required to make such returns.

(4) RETURNS OF ESTATES AND TRUSTS.—Returns of an estate, a trust, or an estate of an individual under chapter 7 or 11 of title 11 of the United States Code shall be made by the fiduciary thereof.

(5) JOINT FIDUCIARIES.—Under such regulations as the Secretary may prescribe, a return made by one of two or more joint fiduciaries shall be sufficient compliance with the requirements of this section. A return made pursuant to this paragraph shall contain a statement that the fiduciary has sufficient knowledge of the affairs of the person for whom the return is made to enable him to make the return, and that the return is, to the best of his knowledge and belief, true and correct.

(6) IRA SHARE OF PARTNERSHIP INCOME.—In the case of a trust which is exempt from taxation under section 408(e), for purposes of this section, the trust's distributive share of items of gross income and gain of any partnership to which subchapter C or D of chapter 63 applies shall be treated as equal to the trust's distributive share of the taxable income of such partnership.

(c) CERTAIN INCOME EARNED ABROAD OR FROM SALE OF RESIDENCE.—For purposes of this section, gross income shall be computed without regard to the exclusion provided for in section 121 (relating to gain from sale of principal residence) and without regard to the exclusion provided for in section 911 (relating to citizens or residents of the United States living abroad).

(d) **TAX-EXEMPT INTEREST REQUIRED TO BE SHOWN ON RETURN.**—Every person required to file a return under this section for the taxable year shall include on such return the amount of interest received or accrued during the taxable year which is exempt from the tax imposed by chapter 1.

(e) **CONSOLIDATED RETURNS.**—For provisions relating to consolidated returns by affiliated corporations, see chapter 6.

[(f) **SPECIAL RULE FOR TAXABLE YEARS 2018 THROUGH 2025.**—In the case of a taxable year beginning after December 31, 2017, and before January 1, 2026, subsection (a)(1) shall not apply, and every individual who has gross income for the taxable year shall be required to make returns with respect to income taxes under subtitle A, except that a return shall not be required of—

[(1) an individual who is not married (determined by applying section 7703) and who has gross income for the taxable year which does not exceed the standard deduction applicable to such individual for such taxable year under section 63, or

[(2) an individual entitled to make a joint return if—

[(A) the gross income of such individual, when combined with the gross income of such individual's spouse, for the taxable year does not exceed the standard deduction which would be applicable to the taxpayer for such taxable year under section 63 if such individual and such individual's spouse made a joint return,

[(B) such individual and such individual's spouse have the same household as their home at the close of the taxable year,

[(C) such individual's spouse does not make a separate return, and

[(D) neither such individual nor such individual's spouse is an individual described in section 63(c)(5) who has income (other than earned income) in excess of the amount in effect under section 63(c)(5)(A).]

**SEC. 6013. JOINT RETURNS OF INCOME TAX BY HUSBAND AND WIFE.**

(a) **JOINT RETURNS.**—A husband and wife may make a single return jointly of income taxes under subtitle A, even though one of the spouses has neither gross income nor deductions, except as provided below:

(1) no joint return shall be made if either the husband or wife at any time during the taxable year is a nonresident alien;

(2) no joint return shall be made if the husband and wife have different taxable years; except that if such taxable years begin on the same day and end on different days because of the death of either or both, then the joint return may be made with respect to the taxable year of each. The above exception shall not apply if the surviving spouse remarries before the close of his taxable year, nor if the taxable year of either spouse is a fractional part of a year under section 443(a)(1);

(3) in the case of death of one spouse or both spouses the joint return with respect to the decedent may be made only by his executor or administrator; except that in the case of the death of one spouse the joint return may be made by the surviving spouse with respect to both himself and the decedent if no return for the taxable year has been made by the decedent, no executor or administrator has been appointed, and no ex-

ecutor or administrator is appointed before the last day prescribed by law for filing the return of the surviving spouse. If an executor or administrator of the decedent is appointed after the making of the joint return by the surviving spouse, the executor or administrator may disaffirm such joint return by making, within 1 year after the last day prescribed by law for filing the return of the surviving spouse, a separate return for the taxable year of the decedent with respect to which the joint return was made, in which case the return made by the survivor shall constitute his separate return.

(b) JOINT RETURN AFTER FILING SEPARATE RETURN.—

(1) IN GENERAL.—Except as provided in paragraph (2), if an individual has filed a separate return for a taxable year for which a joint return could have been made by him and his spouse under subsection (a) and the time prescribed by law for filing the return for such taxable year has expired, such individual and his spouse may nevertheless make a joint return for such taxable year. A joint return filed by the husband and wife under this subsection shall constitute the return of the husband and wife for such taxable year, and all payments, credits, refunds, or other repayments made or allowed with respect to the separate return of either spouse for such taxable year shall be taken into account in determining the extent to which the tax based upon the joint return has been paid. If a joint return is made under this subsection, any election (other than the election to file a separate return) made by either spouse in his separate return for such taxable year with respect to the treatment of any income, deduction, or credit of such spouse shall not be changed in the making of the joint return where such election would have been irrevocable if the joint return had not been made. If a joint return is made under this subsection after the death of either spouse, such return with respect to the decedent can be made only by his executor or administrator.

(2) LIMITATIONS FOR MAKING OF ELECTION.—The election provided for in paragraph (1) may not be made—

(A) after the expiration of 3 years from the last date prescribed by law for filing the return for such taxable year (determined without regard to any extension of time granted to either spouse); or

(B) after there has been mailed to either spouse, with respect to such taxable year, a notice of deficiency under section 6212, if the spouse, as to such notice, files a petition with the Tax Court within the time prescribed in section 6213; or

(C) after either spouse has commenced a suit in any court for the recovery of any part of the tax for such taxable year; or

(D) after either spouse has entered into a closing agreement under section 7121 with respect to such taxable year, or after any civil or criminal case arising against either spouse with respect to such taxable year has been compromised under section 7122.

(3) WHEN RETURN DEEMED FILED.—

(A) ASSESSMENT AND COLLECTION.—For purposes of section 6501 (relating to periods of limitations on assessment and collection), and for purposes of section 6651 (relating to delinquent returns), a joint return made under this subsection shall be deemed to have been filed—

(i) Where both spouses filed separate returns prior to making the joint return - on the date the last separate return was filed (but not earlier than the last date prescribed by law for filing the return of either spouse);

(ii) Where only one spouse filed a separate return prior to the making of the joint return, and the other spouse [had less than the exemption amount of gross income] *had no gross income* for such taxable year - on the date of the filing of such separate return (but not earlier than the last date prescribed by law for the filing of such separate return); or

(iii) Where only one spouse filed a separate return prior to the making of the joint return, and the other spouse [had gross income of the exemption amount or more] *had any gross income* for such taxable year - on the date of the filing of such joint return.

[For purposes of this subparagraph, the term “exemption amount” has the meaning given to such term by section 151(d). For purposes of clauses (ii) and (iii), if the spouse whose gross income is being compared to the exemption amount is 65 or over, such clauses shall be applied by substituting “the sum of the exemption amount and the additional standard deduction under section 63(c)(2) by reason of section 63(f)(1)(A)” for “the exemption amount”.]

(B) CREDIT OR REFUND.—For purposes of section 6511, a joint return made under this subsection shall be deemed to have been filed on the last date prescribed by law for filing the return for such taxable year (determined without regard to any extension of time granted to either spouse).

(4) ADDITIONAL TIME FOR ASSESSMENT.—If a joint return is made under this subsection, the periods of limitations provided in sections 6501 and 6502 on the making of assessments and the beginning of levy or a proceeding in court for collection shall with respect to such return include one year immediately after the date of the filing of such joint return (computed without regard to the provisions of paragraph (3)).

(5) ADDITIONS TO THE TAX AND PENALTIES.—

(A) COORDINATION WITH PART II OF SUBCHAPTER A OF CHAPTER 68.—For purposes of part II of subchapter A of chapter 68, where the sum of the amounts shown as tax on the separate returns of each spouse is less than the amount shown as tax on the joint return made under this subsection—

(i) such sum shall be treated as the amount shown on the joint return,

(ii) any negligence (or disregard of rules or regulations) on either separate return shall be treated as negligence (or such disregard) on the joint return, and

(iii) any fraud on either separate return shall be treated as fraud on the joint return.

(B) CRIMINAL PENALTY.—For purposes of section 7206(1) and (2) and section 7207 (relating to criminal penalties in the case of fraudulent returns) the term “return” includes a separate return filed by a spouse with respect to a taxable year for which a joint return is made under this subsection after the filing of such separate return.

(c) TREATMENT OF JOINT RETURN AFTER DEATH OF EITHER SPOUSE.—For purposes of [sections 15, 443, and 7851(a)(1)(A)] *section 443*, where the husband and wife have different taxable years because of the death of either spouse, the joint return shall be treated as if the taxable years of both spouses ended on the date of the closing of the surviving spouse’s taxable year.

(d) SPECIAL RULES.—For purposes of this section—

(1) the status as husband and wife of two individuals having taxable years beginning on the same day shall be determined—

(A) if both have the same taxable year - as of the close of such year; or

(B) if one dies before the close of the taxable year of the other - as of the time of such death;

(2) an individual who is legally separated from his spouse under a decree of divorce or of separate maintenance shall not be considered as married; and

(3) if a joint return is made, the tax shall be computed on the aggregate income and the liability with respect to the tax shall be joint and several.

(f) JOINT RETURN WHERE INDIVIDUAL IS IN MISSING STATUS.—For purposes of this section and subtitle A—

(1) ELECTION BY SPOUSE.—If—

(A) an individual is in a missing status (within the meaning of paragraph (3)) as a result of service in a combat zone (as determined for purposes of section 112), and

(B) the spouse of such individual is otherwise entitled to file a joint return for any taxable year which begins on or before the day which is 2 years after the date designated under section 112 as the date of termination of combatant activities in such zone,

then such spouse may elect under subsection (a) to file a joint return for such taxable year. With respect to service in the combat zone designated for purposes of the Vietnam conflict, such election may be made for any taxable year while an individual is in missing status.

(2) EFFECT OF ELECTION.—If the spouse of an individual described in paragraph (1)(A) elects to file a joint return under subsection (a) for a taxable year, then, until such election is revoked—

(A) such election shall be valid even if such individual died before the beginning of such year, and

(B) except for purposes of section 692 (relating to income taxes of members of the Armed Forces, astronauts, and victims of certain terrorist attacks on death), the income tax liability of such individual, his spouse, and his estate shall be determined as if he were alive throughout the taxable year.

## (3) MISSING STATUS.—For purposes of this subsection—

(A) UNIFORMED SERVICES.—A member of a uniformed service (within the meaning of section 101(3) of title 37 of the United States Code) is in a missing status for any period for which he is entitled to pay and allowances under section 552 of such title 37.

(B) CIVILIAN EMPLOYEES.—An employee (within the meaning of section 5561(2) of title 5 of the United States Code) is in a missing status for any period for which he is entitled to pay and allowances under section 5562 of such title 5.

(4) MAKING OF ELECTION; REVOCATION.—An election described in this subsection with respect to any taxable year may be made by filing a joint return in accordance with subsection (a) and under such regulations as may be prescribed by the Secretary. Such an election may be revoked by either spouse on or before the due date (including extensions) for such taxable year, and, in the case of an executor or administrator, may be revoked by disaffirming as provided in the last sentence of subsection (a)(3).

## (g) ELECTION TO TREAT NONRESIDENT ALIEN INDIVIDUAL AS RESIDENT OF THE UNITED STATES.—

(1) IN GENERAL.—A nonresident alien individual with respect to whom this subsection is in effect for the taxable year shall be treated as a resident of the United States—

(A) for purposes of chapter 1 for all of such taxable year, and

(B) for purposes of chapter 24 (relating to wage withholding) for payments of wages made during such taxable year.

(2) INDIVIDUALS WITH RESPECT TO WHOM THIS SUBSECTION IS IN EFFECT.—This subsection shall be in effect with respect to any individual who, at the close of the taxable year for which an election under this subsection was made, was a nonresident alien individual married to a citizen or resident of the United States, if both of them made such election to have the benefits of this subsection apply to them.

(3) DURATION OF ELECTION.—An election under this subsection shall apply to the taxable year for which made and to all subsequent taxable years until terminated under paragraph (4) or (5); except that any such election shall not apply for any taxable year if neither spouse is a citizen or resident of the United States at any time during such year.

(4) TERMINATION OF ELECTION.—An election under this subsection shall terminate at the earliest of the following times:

(A) REVOCATION BY TAXPAYERS.—If either taxpayer revokes the election, as of the first taxable year for which the last day prescribed by law for filing the return of tax under chapter 1 has not yet occurred.

(B) DEATH.—In the case of the death of either spouse, as of the beginning of the first taxable year of the spouse who survives following the taxable year in which such death occurred; except that if the spouse who survives is a citizen or resident of the United States who is a surviving spouse entitled to the benefits of section 2, the time provided by

this subparagraph shall be as of the close of the last taxable year for which such individual is entitled to the benefits of section 2.

(C) LEGAL SEPARATION.—In the case of the legal separation of the couple under a decree of divorce or of separate maintenance, as of the beginning of the taxable year in which such legal separation occurs.

(D) TERMINATION BY SECRETARY.—At the time provided in paragraph (5).

(5) TERMINATION BY SECRETARY.—The Secretary may terminate any election under this subsection for any taxable year if he determines that either spouse has failed—

(A) to keep such books and records,

(B) to grant such access to such books and records, or

(C) to supply such other information, as may be reasonably necessary to ascertain the amount of liability for taxes under chapter 1 of either spouse for such taxable year.

(6) ONLY ONE ELECTION.—If any election under this subsection for any two individuals is terminated under paragraph (4) or (5) for any taxable year, such two individuals shall be ineligible to make an election under this subsection for any subsequent taxable year.

(h) JOINT RETURN, ETC., FOR YEAR IN WHICH NONRESIDENT ALIEN BECOMES RESIDENT OF UNITED STATES.—

(1) IN GENERAL.—If—

(A) any individual is a nonresident alien individual at the beginning of any taxable year but is a resident of the United States at the close of such taxable year,

(B) at the close of such taxable year, such individual is married to a citizen or resident of the United States, and

(C) both individuals elect the benefits of this subsection at the time and in the manner prescribed by the Secretary by regulation,

then the individual referred to in subparagraph (A) shall be treated as a resident of the United States for purposes of chapter 1 for all of such taxable year, and for purposes of chapter 24 (relating to wage withholding) for payments of wages made during such taxable year.

(2) ONLY ONE ELECTION.—If any election under this subsection applies for any 2 individuals for any taxable year, such 2 individuals shall be ineligible to make an election under this subsection for any subsequent taxable year.

**SEC. 6014. INCOME TAX RETURN - TAX NOT COMPUTED BY TAXPAYER.**

(a) ELECTION BY TAXPAYER.—An individual who does not itemize his deductions and who is not described in [section 6012(a)(1)(C)(i)] *section 6012(a)(1)(B)(iii)*, whose gross income is less than \$10,000 and includes no income other than remuneration for services performed by him as an employee, dividends or interest, and whose gross income other than wages, as defined in section 3401(a), does not exceed \$100, shall at his election not be required to show on the return the tax imposed by section 1. Such election shall be made by using the form prescribed for purposes of this section. In such case the tax shall be computed by the Sec-



retary who shall mail to the taxpayer a notice stating the amount determined as payable.

(b) REGULATIONS.—The Secretary shall prescribe regulations for carrying out this section, and such regulations may provide for the application of the rules of this section—

(1) to cases where the gross income includes items other than those enumerated by subsection (a),

(2) to cases where the gross income from sources other than wages on which the tax has been withheld at the source is more than \$100,

(3) to cases where the gross income is \$10,000 or more, or

(4) to cases where the taxpayer itemizes his deductions or where the taxpayer claims a reduced standard deduction by reason of section ~~63(c)(5)~~ 63(c)(4).

Such regulations shall provide for the application of this section in the case of husband and wife, including provisions determining when a joint return under this section may be permitted or required, whether the liability shall be joint and several, and whether one spouse may make return under this section and the other without regard to this section.

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## Subchapter B—Miscellaneous Provisions

\* \* \* \* \*

### SEC. 6103. CONFIDENTIALITY AND DISCLOSURE OF RETURNS AND RETURN INFORMATION.

(a) GENERAL RULE.—Returns and return information shall be confidential, and except as authorized by this title—

(1) no officer or employee of the United States,

(2) no officer or employee of any State, any local law enforcement agency receiving information under subsection (i)(1)(C) or (7)(A), any local child support enforcement agency, or any local agency administering a program listed in subsection (l)(7)(D) who has or had access to returns or return information under this section or section 6104(c), and

(3) no other person (or officer or employee thereof) who has or had access to returns or return information under subsection (e)(1)(D)(iii), subsection (k)(10), paragraph (6), (10), (12), (16), (19), (20), or (21) of subsection (l), paragraph (2) or (4)(B) of subsection (m), or subsection (n),

shall disclose any return or return information obtained by him in any manner in connection with his service as such an officer or an employee or otherwise or under the provisions of this section. For purposes of this subsection, the term “officer or employee” includes a former officer or employee.

(b) DEFINITIONS.—For purposes of this section—

(1) RETURN.—The term “return” means any tax or information return, declaration of estimated tax, or claim for refund required by, or provided for or permitted under, the provisions of this title which is filed with the Secretary by, on behalf of, or with respect to any person, and any amendment or supplement thereto, including supporting schedules, attachments, or lists which are supplemental to, or part of, the return so filed.

(2) RETURN INFORMATION.—The term “return information” means—

(A) a taxpayer’s identity, the nature, source, or amount of his income, payments, receipts, deductions, exemptions, credits, assets, liabilities, net worth, tax liability, tax withheld, deficiencies, overassessments, or tax payments, whether the taxpayer’s return was, is being, or will be examined or subject to other investigation or processing, or any other data, received by, recorded by, prepared by, furnished to, or collected by the Secretary with respect to a return or with respect to the determination of the existence, or possible existence, of liability (or the amount thereof) of any person under this title for any tax, penalty, interest, fine, forfeiture, or other imposition, or offense,

(B) any part of any written determination or any background file document relating to such written determination (as such terms are defined in section 6110(b)) which is not open to public inspection under section 6110,

(C) any advance pricing agreement entered into by a taxpayer and the Secretary and any background information related to such agreement or any application for an advance pricing agreement, and

(D) any agreement under section 7121, and any similar agreement, and any background information related to such an agreement or request for such an agreement,

but such term does not include data in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer. Nothing in the preceding sentence, or in any other provision of law, shall be construed to require the disclosure of standards used or to be used for the selection of returns for examination, or data used or to be used for determining such standards, if the Secretary determines that such disclosure will seriously impair assessment, collection, or enforcement under the internal revenue laws.

(3) TAXPAYER RETURN INFORMATION.—The term “taxpayer return information” means return information as defined in paragraph (2) which is filed with, or furnished to, the Secretary by or on behalf of the taxpayer to whom such return information relates.

(4) TAX ADMINISTRATION.—The term “tax administration”—

(A) means—

(i) the administration, management, conduct, direction, and supervision of the execution and application of the internal revenue laws or related statutes (or equivalent laws and statutes of a State) and tax conventions to which the United States is a party, and

(ii) the development and formulation of Federal tax policy relating to existing or proposed internal revenue laws, related statutes, and tax conventions, and

(B) includes assessment, collection, enforcement, litigation, publication, and statistical gathering functions under such laws, statutes, or conventions.

(5) STATE.—

(A) IN GENERAL.—The term “State” means—

(i) any of the 50 States, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands,

(ii) for purposes of subsections (a)(2), (b)(4), (d)(1), (h)(4), and (p), any municipality—

(I) with a population in excess of 250,000 (as determined under the most recent decennial United States census data available),

(II) which imposes a tax on income or wages, and

(III) with which the Secretary (in his sole discretion) has entered into an agreement regarding disclosure, and

(iii) for purposes of subsections (a)(2), (b)(4), (d)(1), (h)(4), and (p), any governmental entity—

(I) which is formed and operated by a qualified group of municipalities, and

(II) with which the Secretary (in his sole discretion) has entered into an agreement regarding disclosure.

(B) REGIONAL INCOME TAX AGENCIES.—For purposes of subparagraph (A)(iii)—

(i) QUALIFIED GROUP OF MUNICIPALITIES.—The term “qualified group of municipalities” means, with respect to any governmental entity, 2 or more municipalities—

(I) each of which imposes a tax on income or wages,

(II) each of which, under the authority of a State statute, administers the laws relating to the imposition of such taxes through such entity, and

(III) which collectively have a population in excess of 250,000 (as determined under the most recent decennial United States census data available).

(ii) REFERENCES TO STATE LAW, ETC.—For purposes of applying subparagraph (A)(iii) to the subsections referred to in such subparagraph, any reference in such subsections to State law, proceedings, or tax returns shall be treated as references to the law, proceedings, or tax returns, as the case may be, of the municipalities which form and operate the governmental entity referred to in such subparagraph.

(iii) DISCLOSURE TO CONTRACTORS AND OTHER AGENTS.—Notwithstanding any other provision of this section, no return or return information shall be disclosed to any contractor or other agent of a governmental entity referred to in subparagraph (A)(iii) unless such entity, to the satisfaction of the Secretary—

(I) has requirements in effect which require each such contractor or other agent which would have access to returns or return information to provide safeguards (within the meaning of subsection (p)(4)) to protect the confidentiality of such returns or return information,

(II) agrees to conduct an on-site review every 3 years (or a mid-point review in the case of contracts or agreements of less than 3 years in duration) of each contractor or other agent to determine compliance with such requirements,

(III) submits the findings of the most recent review conducted under subclause (II) to the Secretary as part of the report required by subsection (p)(4)(E), and

(IV) certifies to the Secretary for the most recent annual period that such contractor or other agent is in compliance with all such requirements.

The certification required by subclause (IV) shall include the name and address of each contractor and other agent, a description of the contract or agreement with such contractor or other agent, and the duration of such contract or agreement. The requirements of this clause shall not apply to disclosures pursuant to subsection (n) for purposes of Federal tax administration and a rule similar to the rule of subsection (p)(8)(B) shall apply for purposes of this clause.

(6) **TAXPAYER IDENTITY.**—The term “taxpayer identity” means the name of a person with respect to whom a return is filed, his mailing address, his taxpayer identifying number (as described in section 6109), or a combination thereof.

(7) **INSPECTION.**—The terms “inspected” and “inspection” mean any examination of a return or return information.

(8) **DISCLOSURE.**—The term “disclosure” means the making known to any person in any manner whatever a return or return information.

(9) **FEDERAL AGENCY.**—The term “Federal agency” means an agency within the meaning of section 551(1) of title 5, United States Code.

(10) **CHIEF EXECUTIVE OFFICER.**—The term “chief executive officer” means, with respect to any municipality, any elected official and the chief official (even if not elected) of such municipality.

(11) **TERRORIST INCIDENT, THREAT, OR ACTIVITY.**—The term “terrorist incident, threat, or activity” means an incident, threat, or activity involving an act of domestic terrorism (as defined in section 2331(5) of title 18, United States Code) or international terrorism (as defined in section 2331(1) of such title).

(c) **DISCLOSURE OF RETURNS AND RETURN INFORMATION TO DESIGNEE OF TAXPAYER.**—The Secretary may, subject to such requirements and conditions as he may prescribe by regulations, disclose the return of any taxpayer, or return information with respect to such taxpayer, to such person or persons as the taxpayer may designate in a request for or consent to such disclosure, or to any other person at the taxpayer’s request to the extent necessary to comply with a request for information or assistance made by the taxpayer to such other person. However, return information shall not be disclosed to such person or persons if the Secretary determines that such disclosure would seriously impair Federal tax administration.

## (d) DISCLOSURE TO STATE TAX OFFICIALS AND STATE AND LOCAL LAW ENFORCEMENT AGENCIES.—

(1) IN GENERAL.—Returns and return information with respect to taxes imposed by chapters 1, 2, 6, 11, 12, 21, 23, 24, 31, 32, 44, 51, and 52 and subchapter D of chapter 36 shall be open to inspection by, or disclosure to, any State agency, body, or commission, or its legal representative, which is charged under the laws of such State with responsibility for the administration of State tax laws for the purpose of, and only to the extent necessary in, the administration of such laws, including any procedures with respect to locating any person who may be entitled to a refund. Such inspection shall be permitted, or such disclosure made, only upon written request by the head of such agency, body, or commission, and only to the representatives of such agency, body, or commission designated in such written request as the individuals who are to inspect or to receive the returns or return information on behalf of such agency, body, or commission. Such representatives shall not include any individual who is the chief executive officer of such State or who is neither an employee or legal representative of such agency, body, or commission nor a person described in subsection (n). However, such return information shall not be disclosed to the extent that the Secretary determines that such disclosure would identify a confidential informant or seriously impair any civil or criminal tax investigation.

## (2) DISCLOSURE TO STATE AUDIT AGENCIES.—

(A) IN GENERAL.—Any returns or return information obtained under paragraph (1) by any State agency, body, or commission may be open to inspection by, or disclosure to, officers and employees of the State audit agency for the purpose of, and only to the extent necessary in, making an audit of the State agency, body, or commission referred to in paragraph (1).

(B) STATE AUDIT AGENCY.—For purposes of subparagraph (A), the term “State audit agency” means any State agency, body, or commission which is charged under the laws of the State with the responsibility of auditing State revenues and programs.

(3) EXCEPTION FOR REIMBURSEMENT UNDER SECTION 7624.—Nothing in this section shall be construed to prevent the Secretary from disclosing to any State or local law enforcement agency which may receive a payment under section 7624 the amount of the recovered taxes with respect to which such a payment may be made.

## (4) AVAILABILITY AND USE OF DEATH INFORMATION.—

(A) IN GENERAL.—No returns or return information may be disclosed under paragraph (1) to any agency, body, or commission of any State (or any legal representative thereof) during any period during which a contract meeting the requirements of subparagraph (B) is not in effect between such State and the Secretary of Health and Human Services.

(B) CONTRACTUAL REQUIREMENTS.—A contract meets the requirements of this subparagraph if—

(i) such contract requires the State to furnish the Secretary of Health and Human Services information concerning individuals with respect to whom death certificates (or equivalent documents maintained by the State or any subdivision thereof) have been officially filed with it, and

(ii) such contract does not include any restriction on the use of information obtained by such Secretary pursuant to such contract, except that such contract may provide that such information is only to be used by the Secretary (or any other Federal agency) for purposes of ensuring that Federal benefits or other payments are not erroneously paid to deceased individuals.

Any information obtained by the Secretary of Health and Human Services under such a contract shall be exempt from disclosure under section 552 of title 5, United States Code, and from the requirements of section 552a of such title 5.

(C) SPECIAL EXCEPTION.—The provisions of subparagraph (A) shall not apply to any State which on July 1, 1993, was not, pursuant to a contract, furnishing the Secretary of Health and Human Services information concerning individuals with respect to whom death certificates (or equivalent documents maintained by the State or any subdivision thereof) have been officially filed with it.

(5) DISCLOSURE FOR COMBINED EMPLOYMENT TAX REPORTING.—

(A) IN GENERAL.—The Secretary may disclose taxpayer identity information and signatures to any agency, body, or commission of any State for the purpose of carrying out with such agency, body, or commission a combined Federal and State employment tax reporting program approved by the Secretary. Subsections (a)(2) and (p)(4) and sections 7213 and 7213A shall not apply with respect to disclosures or inspections made pursuant to this paragraph.

(B) TERMINATION.—The Secretary may not make any disclosure under this paragraph after December 31, 2007.

(6) LIMITATION ON DISCLOSURE REGARDING REGIONAL INCOME TAX AGENCIES TREATED AS STATES.—For purposes of paragraph (1), inspection by or disclosure to an entity described in subsection (b)(5)(A)(iii) shall be for the purpose of, and only to the extent necessary in, the administration of the laws of the member municipalities in such entity relating to the imposition of a tax on income or wages. Such entity may not redisclose any return or return information received pursuant to paragraph (1) to any such member municipality.

(e) DISCLOSURE TO PERSONS HAVING MATERIAL INTEREST.—

(1) IN GENERAL.—The return of a person shall, upon written request, be open to inspection by or disclosure to—

(A) in the case of the return of an individual—

(i) that individual,

(ii) the spouse of that individual if the individual and such spouse have signified their consent to consider a gift reported on such return as made one-half

by him and one-half by the spouse pursuant to the provisions of section 2513; or

(iii) the child of that individual (or such child's legal representative) to the extent necessary to comply with the provisions of section 1(g);

(B) in the case of an income tax return filed jointly, either of the individuals with respect to whom the return is filed;

(C) in the case of the return of a partnership, any person who was a member of such partnership during any part of the period covered by the return;

(D) in the case of the return of a corporation or a subsidiary thereof—

(i) any person designated by resolution of its board of directors or other similar governing body,

(ii) any officer or employee of such corporation upon written request signed by any principal officer and attested to by the secretary or other officer,

(iii) any bona fide shareholder of record owning 1 percent or more of the outstanding stock of such corporation,

(iv) if the corporation was an S corporation, any person who was a shareholder during any part of the period covered by such return during which an election under section 1362(a) was in effect, or

(v) if the corporation has been dissolved, any person authorized by applicable State law to act for the corporation or any person who the Secretary finds to have a material interest which will be affected by information contained therein;

(E) in the case of the return of an estate—

(i) the administrator, executor, or trustee of such estate, and

(ii) any heir at law, next of kin, or beneficiary under the will, of the decedent, but only if the Secretary finds that such heir at law, next of kin, or beneficiary has a material interest which will be affected by information contained therein; and

(F) in the case of the return of a trust—

(i) the trustee or trustees, jointly or separately, and

(ii) any beneficiary of such trust, but only if the Secretary finds that such beneficiary has a material interest which will be affected by information contained therein.

(2) INCOMPETENCY.—If an individual described in paragraph (1) is legally incompetent, the applicable return shall, upon written request, be open to inspection by or disclosure to the committee, trustee, or guardian of his estate.

(3) DECEASED INDIVIDUALS.—The return of a decedent shall, upon written request, be open to inspection by or disclosure to—

(A) the administrator, executor, or trustee of his estate, and

(B) any heir at law, next of kin, or beneficiary under the will, of such decedent, or a donee of property, but only if

the Secretary finds that such heir at law, next of kin, beneficiary, or donee has a material interest which will be affected by information contained therein.

(4) TITLE 11 CASES AND RECEIVERSHIP PROCEEDINGS.—If—

(A) there is a trustee in a title 11 case in which the debtor is the person with respect to whom the return is filed, or

(B) substantially all of the property of the person with respect to whom the return is filed is in the hands of a receiver,

such return or returns for prior years of such person shall, upon written request, be open to inspection by or disclosure to such trustee or receiver, but only if the Secretary finds that such trustee or receiver, in his fiduciary capacity, has a material interest which will be affected by information contained therein.

(5) INDIVIDUAL'S TITLE 11 CASE.—

(A) IN GENERAL.—In any case to which section 1398 applies (determined without regard to section 1398(b)(1)), any return of the debtor for the taxable year in which the case commenced or any preceding taxable year shall, upon written request, be open to inspection by or disclosure to the trustee in such case.

(B) RETURN OF ESTATE AVAILABLE TO DEBTOR.—Any return of an estate in a case to which section 1398 applies shall, upon written request, be open to inspection by or disclosure to the debtor in such case.

(C) SPECIAL RULE FOR INVOLUNTARY CASES.—In an involuntary case, no disclosure shall be made under subparagraph (A) until the order for relief has been entered by the court having jurisdiction of such case unless such court finds that such disclosure is appropriate for purposes of determining whether an order for relief should be entered.

(6) ATTORNEY IN FACT.—Any return to which this subsection applies shall, upon written request, also be open to inspection by or disclosure to the attorney in fact duly authorized in writing by any of the persons described in paragraph (1), (2), (3), (4), (5), (8), or (9) to inspect the return or receive the information on his behalf, subject to the conditions provided in such paragraphs.

(7) RETURN INFORMATION.—Return information with respect to any taxpayer may be open to inspection by or disclosure to any person authorized by this subsection to inspect any return of such taxpayer if the Secretary determines that such disclosure would not seriously impair Federal tax administration.

(8) DISCLOSURE OF COLLECTION ACTIVITIES WITH RESPECT TO JOINT RETURN.—If any deficiency of tax with respect to a joint return is assessed and the individuals filing such return are no longer married or no longer reside in the same household, upon request in writing by either of such individuals, the Secretary shall disclose in writing to the individual making the request whether the Secretary has attempted to collect such deficiency from such other individual, the general nature of such collection activities, and the amount collected. The preceding sen-



tence shall not apply to any deficiency which may not be collected by reason of section 6502.

(9) DISCLOSURE OF CERTAIN INFORMATION WHERE MORE THAN 1 PERSON SUBJECT TO PENALTY UNDER SECTION 6672.—If the Secretary determines that a person is liable for a penalty under section 6672(a) with respect to any failure, upon request in writing of such person, the Secretary shall disclose in writing to such person—

(A) the name of any other person whom the Secretary has determined to be liable for such penalty with respect to such failure, and

(B) whether the Secretary has attempted to collect such penalty from such other person, the general nature of such collection activities, and the amount collected.

(10) LIMITATION ON CERTAIN DISCLOSURES UNDER THIS SUBSECTION.—In the case of an inspection or disclosure under this subsection relating to the return of a partnership, S corporation, trust, or an estate, the information inspected or disclosed shall not include any supporting schedule, attachment, or list which includes the taxpayer identity information of a person other than the entity making the return or the person conducting the inspection or to whom the disclosure is made.

(11) DISCLOSURE OF INFORMATION REGARDING STATUS OF INVESTIGATION OF VIOLATION OF THIS SECTION.—In the case of a person who provides to the Secretary information indicating a violation of section 7213, 7213A, or 7214 with respect to any return or return information of such person, the Secretary may disclose to such person (or such person's designee)—

(A) whether an investigation based on the person's provision of such information has been initiated and whether it is open or closed,

(B) whether any such investigation substantiated such a violation by any individual, and

(C) whether any action has been taken with respect to such individual (including whether a referral has been made for prosecution of such individual).

(f) DISCLOSURE TO COMMITTEES OF CONGRESS.—

(1) COMMITTEE ON WAYS AND MEANS, COMMITTEE ON FINANCE, AND JOINT COMMITTEE ON TAXATION.—Upon written request from the chairman of the Committee on Ways and Means of the House of Representatives, the chairman of the Committee on Finance of the Senate, or the chairman of the Joint Committee on Taxation, the Secretary shall furnish such committee with any return or return information specified in such request, except that any return or return information which can be associated with, or otherwise identify, directly or indirectly, a particular taxpayer shall be furnished to such committee only when sitting in closed executive session unless such taxpayer otherwise consents in writing to such disclosure.

(2) CHIEF OF STAFF OF JOINT COMMITTEE ON TAXATION.—Upon written request by the Chief of Staff of the Joint Committee on Taxation, the Secretary shall furnish him with any return or return information specified in such request. Such Chief of Staff may submit such return or return information to any committee described in paragraph (1), except that any re-

turn or return information which can be associated with, or otherwise identify, directly or indirectly, a particular taxpayer shall be furnished to such committee only when sitting in closed executive session unless such taxpayer otherwise consents in writing to such disclosure.

(3) OTHER COMMITTEES.—Pursuant to an action by, and upon written request by the chairman of, a committee of the Senate or the House of Representatives (other than a committee specified in paragraph (1)) specially authorized to inspect any return or return information by a resolution of the Senate or the House of Representatives or, in the case of a joint committee (other than the joint committee specified in paragraph (1)) by concurrent resolution, the Secretary shall furnish such committee, or a duly authorized and designated subcommittee thereof, sitting in closed executive session, with any return or return information which such resolution authorizes the committee or subcommittee to inspect. Any resolution described in this paragraph shall specify the purpose for which the return or return information is to be furnished and that such information cannot reasonably be obtained from any other source.

(4) AGENTS OF COMMITTEES AND SUBMISSION OF INFORMATION TO SENATE OR HOUSE OF REPRESENTATIVES.—

(A) COMMITTEES DESCRIBED IN PARAGRAPH (1).—Any committee described in paragraph (1) or the Chief of Staff of the Joint Committee on Taxation shall have the authority, acting directly, or by or through such examiners or agents as the chairman of such committee or such chief of staff may designate or appoint, to inspect returns and return information at such time and in such manner as may be determined by such chairman or chief of staff. Any return or return information obtained by or on behalf of such committee pursuant to the provisions of this subsection may be submitted by the committee to the Senate or the House of Representatives, or to both. The Joint Committee on Taxation may also submit such return or return information to any other committee described in paragraph (1), except that any return or return information which can be associated with, or otherwise identify, directly or indirectly, a particular taxpayer shall be furnished to such committee only when sitting in closed executive session unless such taxpayer otherwise consents in writing to such disclosure.

(B) OTHER COMMITTEES.—Any committee or subcommittee described in paragraph (3) shall have the right, acting directly, or by or through no more than four examiners or agents, designated or appointed in writing in equal numbers by the chairman and ranking minority member of such committee or subcommittee, to inspect returns and return information at such time and in such manner as may be determined by such chairman and ranking minority member. Any return or return information obtained by or on behalf of such committee or subcommittee pursuant to the provisions of this subsection may be submitted by the committee to the Senate or the House of Representatives, or to both, except that any re-

turn or return information which can be associated with, or otherwise identify, directly or indirectly, a particular taxpayer, shall be furnished to the Senate or the House of Representatives only when sitting in closed executive session unless such taxpayer otherwise consents in writing to such disclosure.

(5) DISCLOSURE BY WHISTLEBLOWER.—Any person who otherwise has or had access to any return or return information under this section may disclose such return or return information to a committee referred to in paragraph (1) or any individual authorized to receive or inspect information under paragraph (4)(A) if such person believes such return or return information may relate to possible misconduct, maladministration, or taxpayer abuse.

(g) DISCLOSURE TO PRESIDENT AND CERTAIN OTHER PERSONS.—

(1) IN GENERAL.—Upon written request by the President, signed by him personally, the Secretary shall furnish to the President, or to such employee or employees of the White House Office as the President may designate by name in such request, a return or return information with respect to any taxpayer named in such request. Any such request shall state—

(A) the name and address of the taxpayer whose return or return information is to be disclosed,

(B) the kind of return or return information which is to be disclosed,

(C) the taxable period or periods covered by such return or return information, and

(D) the specific reason why the inspection or disclosure is requested.

(2) DISCLOSURE OF RETURN INFORMATION AS TO PRESIDENTIAL APPOINTEES AND CERTAIN OTHER FEDERAL GOVERNMENT APPOINTEES.—The Secretary may disclose to a duly authorized representative of the Executive Office of the President or to the head of any Federal agency, upon written request by the President or head of such agency, or to the Federal Bureau of Investigation on behalf of and upon written request by the President or such head, return information with respect to an individual who is designated as being under consideration for appointment to a position in the executive or judicial branch of the Federal Government. Such return information shall be limited to whether such individual—

(A) has filed returns with respect to the taxes imposed under chapter 1 for not more than the immediately preceding 3 years;

(B) has failed to pay any tax within 10 days after notice and demand, or has been assessed any penalty under this title for negligence, in the current year or immediately preceding 3 years;

(C) has been or is under investigation for possible criminal offenses under the internal revenue laws and the results of any such investigation; or

(D) has been assessed any civil penalty under this title for fraud.

Within 3 days of the receipt of any request for any return information with respect to any individual under this paragraph, the Secretary shall notify such individual in writing that such information has been requested under the provisions of this paragraph.

(3) RESTRICTION ON DISCLOSURE.—The employees to whom returns and return information are disclosed under this subsection shall not disclose such returns and return information to any other person except the President or the head of such agency without the personal written direction of the President or the head of such agency.

(4) RESTRICTION ON DISCLOSURE TO CERTAIN EMPLOYEES.—Disclosure of returns and return information under this subsection shall not be made to any employee whose annual rate of basic pay is less than the annual rate of basic pay specified for positions subject to section 5316 of title 5, United States Code.

(5) REPORTING REQUIREMENTS.—Within 30 days after the close of each calendar quarter, the President and the head of any agency requesting returns and return information under this subsection shall each file a report with the Joint Committee on Taxation setting forth the taxpayers with respect to whom such requests were made during such quarter under this subsection, the returns or return information involved, and the reasons for such requests. The President shall not be required to report on any request for returns and return information pertaining to an individual who was an officer or employee of the executive branch of the Federal Government at the time such request was made. Reports filed pursuant to this paragraph shall not be disclosed unless the Joint Committee on Taxation determines that disclosure thereof (including identifying details) would be in the national interest. Such reports shall be maintained by the Joint Committee on Taxation for a period not exceeding 2 years unless, within such period, the Joint Committee on Taxation determines that a disclosure to the Congress is necessary.

(h) DISCLOSURE TO CERTAIN FEDERAL OFFICERS AND EMPLOYEES FOR PURPOSES OF TAX ADMINISTRATION, ETC.—

(1) DEPARTMENT OF THE TREASURY.—Returns and return information shall, without written request, be open to inspection by or disclosure to officers and employees of the Department of the Treasury whose official duties require such inspection or disclosure for tax administration purposes.

(2) DEPARTMENT OF JUSTICE.—In a matter involving tax administration, a return or return information shall be open to inspection by or disclosure to officers and employees of the Department of Justice (including United States attorneys) personally and directly engaged in, and solely for their use in, any proceeding before a Federal grand jury or preparation for any proceeding (or investigation which may result in such a proceeding) before a Federal grand jury or any Federal or State court, but only if—

(A) the taxpayer is or may be a party to the proceeding, or the proceeding arose out of, or in connection with, determining the taxpayer's civil or criminal liability, or the col-

lection of such civil liability in respect of any tax imposed under this title;

(B) the treatment of an item reflected on such return is or may be related to the resolution of an issue in the proceeding or investigation; or

(C) such return or return information relates or may relate to a transactional relationship between a person who is or may be a party to the proceeding and the taxpayer which affects, or may affect, the resolution of an issue in such proceeding or investigation.

(3) FORM OF REQUEST.—In any case in which the Secretary is authorized to disclose a return or return information to the Department of Justice pursuant to the provisions of this subsection—

(A) if the Secretary has referred the case to the Department of Justice, or if the proceeding is authorized by subchapter B of chapter 76, the Secretary may make such disclosure on his own motion, or

(B) if the Secretary receives a written request from the Attorney General, the Deputy Attorney General, or an Assistant Attorney General for a return of, or return information relating to, a person named in such request and setting forth the need for the disclosure, the Secretary shall disclose return or return the information so requested.

(4) DISCLOSURE IN JUDICIAL AND ADMINISTRATIVE TAX PROCEEDINGS.—A return or return information may be disclosed in a Federal or State judicial or administrative proceeding pertaining to tax administration, but only—

(A) if the taxpayer is a party to the proceeding, or the proceeding arose out of, or in connection with, determining the taxpayer's civil or criminal liability, or the collection of such civil liability, in respect of any tax imposed under this title;

(B) if the treatment of an item reflected on such return is directly related to the resolution of an issue in the proceeding;

(C) if such return or return information directly relates to a transactional relationship between a person who is a party to the proceeding and the taxpayer which directly affects the resolution of an issue in the proceeding; or

(D) to the extent required by order of a court pursuant to section 3500 of title 18, United States Code, or rule 16 of the Federal Rules of Criminal Procedure, such court being authorized in the issuance of such order to give due consideration to congressional policy favoring the confidentiality of returns and return information as set forth in this title.

However, such return or return information shall not be disclosed as provided in subparagraph (A), (B), or (C) if the Secretary determines that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

(5) WITHHOLDING OF TAX FROM SOCIAL SECURITY BENEFITS.—Upon written request of the payor agency, the Secretary may

disclose available return information from the master files of the Internal Revenue Service with respect to the address and status of an individual as a nonresident alien or as a citizen or resident of the United States to the Social Security Administration or the Railroad Retirement Board (whichever is appropriate) for purposes of carrying out its responsibilities for withholding tax under section 1441 from social security benefits (as defined in section 86(d)).

(6) INTERNAL REVENUE SERVICE OVERSIGHT BOARD.—

(A) IN GENERAL.—Notwithstanding paragraph (1), and except as provided in subparagraph (B), no return or return information may be disclosed to any member of the Oversight Board described in subparagraph (A) or (D) of section 7802(b)(1) or to any employee or detailee of such Board by reason of their service with the Board. Any request for information not permitted to be disclosed under the preceding sentence, and any contact relating to a specific taxpayer, made by any such individual to an officer or employee of the Internal Revenue Service shall be reported by such officer or employee to the Secretary, the Treasury Inspector General for Tax Administration, and the Joint Committee on Taxation.

(B) EXCEPTION FOR REPORTS TO THE BOARD.—If—

(i) the Commissioner or the Treasury Inspector General for Tax Administration prepares any report or other matter for the Oversight Board in order to assist the Board in carrying out its duties; and

(ii) the Commissioner or such Inspector General determines it is necessary to include any return or return information in such report or other matter to enable the Board to carry out such duties, such return or return information (other than information regarding taxpayer identity) may be disclosed to members, employees, or detailees of the Board solely for the purpose of carrying out such duties.

(i) DISCLOSURE TO FEDERAL OFFICERS OR EMPLOYEES FOR ADMINISTRATION OF FEDERAL LAWS NOT RELATING TO TAX ADMINISTRATION.—

(1) DISCLOSURE OF RETURNS AND RETURN INFORMATION FOR USE IN CRIMINAL INVESTIGATIONS.—

(A) IN GENERAL.—Except as provided in paragraph (6), any return or return information with respect to any specified taxable period or periods shall, pursuant to and upon the grant of an ex parte order by a Federal district court judge or magistrate judge under subparagraph (B), be open (but only to the extent necessary as provided in such order) to inspection by, or disclosure to, officers and employees of any Federal agency who are personally and directly engaged in—

(i) preparation for any judicial or administrative proceeding pertaining to the enforcement of a specifically designated Federal criminal statute (not involving tax administration) to which the United States or such agency is or may be a party, or pertaining to the case of a missing or exploited child,

(ii) any investigation which may result in such a proceeding, or

(iii) any Federal grand jury proceeding pertaining to enforcement of such a criminal statute to which the United States or such agency is or may be a party, or to such a case of a missing or exploited child, solely for the use of such officers and employees in such preparation, investigation, or grand jury proceeding.

(B) APPLICATION FOR ORDER.—The Attorney General, the Deputy Attorney General, the Associate Attorney General, any Assistant Attorney General, any United States attorney, any special prosecutor appointed under section 593 of title 28, United States Code, or any attorney in charge of a criminal division organized crime strike force established pursuant to section 510 of title 28, United States Code, may authorize an application to a Federal district court judge or magistrate judge for the order referred to in subparagraph (A). Upon such application, such judge or magistrate judge may grant such order if he determines on the basis of the facts submitted by the applicant that—

(i) there is reasonable cause to believe, based upon information believed to be reliable, that a specific criminal act has been committed,

(ii) there is reasonable cause to believe that the return or return information is or may be relevant to a matter relating to the commission of such act, and

(iii) the return or return information is sought exclusively for use in a Federal criminal investigation or proceeding concerning such act (or any criminal investigation or proceeding, in the case of a matter relating to a missing or exploited child), and the information sought to be disclosed cannot reasonably be obtained, under the circumstances, from another source.

(C) DISCLOSURE TO STATE AND LOCAL LAW ENFORCEMENT AGENCIES IN THE CASE OF MATTERS PERTAINING TO A MISSING OR EXPLOITED CHILD.—

(i) IN GENERAL.—In the case of an investigation pertaining to a missing or exploited child, the head of any Federal agency, or his designee, may disclose any return or return information obtained under subparagraph (A) to officers and employees of any State or local law enforcement agency, but only if—

(I) such State or local law enforcement agency is part of a team with the Federal agency in such investigation, and

(II) such information is disclosed only to such officers and employees who are personally and directly engaged in such investigation.

(ii) LIMITATION ON USE OF INFORMATION.—Information disclosed under this subparagraph shall be solely for the use of such officers and employees in locating the missing child, in a grand jury proceeding, or in any preparation for, or investigation which may result in, a judicial or administrative proceeding.

(iii) MISSING CHILD.—For purposes of this subparagraph, the term “missing child” shall have the meaning given such term by section 403 of the Missing Children’s Assistance Act (42 U.S.C. 5772).

(iv) EXPLOITED CHILD.—For purposes of this subparagraph, the term “exploited child” means a minor with respect to whom there is reason to believe that a specified offense against a minor (as defined by section 111(7) of the Sex Offender Registration and Notification Act (42 U.S.C. 16911(7))) has or is occurring.

(2) DISCLOSURE OF RETURN INFORMATION OTHER THAN TAXPAYER RETURN INFORMATION FOR USE IN CRIMINAL INVESTIGATIONS.—

(A) IN GENERAL.—Except as provided in paragraph (6), upon receipt by the Secretary of a request which meets the requirements of subparagraph (B) from the head of any Federal agency or the Inspector General thereof, or, in the case of the Department of Justice, the Attorney General, the Deputy Attorney General, the Associate Attorney General, any Assistant Attorney General, the Director of the Federal Bureau of Investigation, the Administrator of the Drug Enforcement Administration, any United States attorney, any special prosecutor appointed under section 593 of title 28, United States Code, or any attorney in charge of a criminal division organized crime strike force established pursuant to section 510 of title 28, United States Code, the Secretary shall disclose return information (other than taxpayer return information) to officers and employees of such agency who are personally and directly engaged in—

(i) preparation for any judicial or administrative proceeding described in paragraph (1)(A)(i),

(ii) any investigation which may result in such a proceeding, or

(iii) any grand jury proceeding described in paragraph (1)(A)(iii),

solely for the use of such officers and employees in such preparation, investigation, or grand jury proceeding.

(B) REQUIREMENTS.—A request meets the requirements of this subparagraph if the request is in writing and sets forth—

(i) the name and address of the taxpayer with respect to whom the requested return information relates;

(ii) the taxable period or periods to which such return information relates;

(iii) the statutory authority under which the proceeding or investigation described in subparagraph (A) is being conducted; and

(iv) the specific reason or reasons why such disclosure is, or may be, relevant to such proceeding or investigation.

(C) TAXPAYER IDENTITY.—For purposes of this paragraph, a taxpayer’s identity shall not be treated as taxpayer return information.



(3) DISCLOSURE OF RETURN INFORMATION TO APPRISE APPROPRIATE OFFICIALS OF CRIMINAL OR TERRORIST ACTIVITIES OR EMERGENCY CIRCUMSTANCES.—

(A) POSSIBLE VIOLATIONS OF FEDERAL CRIMINAL LAW.—

(i) IN GENERAL.—Except as provided in paragraph (6), the Secretary may disclose in writing return information (other than taxpayer return information) which may constitute evidence of a violation of any Federal criminal law (not involving tax administration) to the extent necessary to apprise the head of the appropriate Federal agency charged with the responsibility of enforcing such law. The head of such agency may disclose such return information to officers and employees of such agency to the extent necessary to enforce such law.

(ii) TAXPAYER IDENTITY.—If there is return information (other than taxpayer return information) which may constitute evidence of a violation by any taxpayer of any Federal criminal law (not involving tax administration), such taxpayer's identity may also be disclosed under clause (i).

(B) EMERGENCY CIRCUMSTANCES.—

(i) DANGER OF DEATH OR PHYSICAL INJURY.—Under circumstances involving an imminent danger of death or physical injury to any individual, the Secretary may disclose return information to the extent necessary to apprise appropriate officers or employees of any Federal or State law enforcement agency of such circumstances.

(ii) FLIGHT FROM FEDERAL PROSECUTION.—Under circumstances involving the imminent flight of any individual from Federal prosecution, the Secretary may disclose return information to the extent necessary to apprise appropriate officers or employees of any Federal law enforcement agency of such circumstances.

(C) TERRORIST ACTIVITIES, ETC.—

(i) IN GENERAL.—Except as provided in paragraph (6), the Secretary may disclose in writing return information (other than taxpayer return information) that may be related to a terrorist incident, threat, or activity to the extent necessary to apprise the head of the appropriate Federal law enforcement agency responsible for investigating or responding to such terrorist incident, threat, or activity. The head of the agency may disclose such return information to officers and employees of such agency to the extent necessary to investigate or respond to such terrorist incident, threat, or activity.

(ii) DISCLOSURE TO THE DEPARTMENT OF JUSTICE.—Returns and taxpayer return information may also be disclosed to the Attorney General under clause (i) to the extent necessary for, and solely for use in preparing, an application under paragraph (7)(D).

(iii) TAXPAYER IDENTITY.—For purposes of this subparagraph, a taxpayer's identity shall not be treated as taxpayer return information.

(4) USE OF CERTAIN DISCLOSED RETURNS AND RETURN INFORMATION IN JUDICIAL OR ADMINISTRATIVE PROCEEDINGS.—

(A) RETURNS AND TAXPAYER RETURN INFORMATION.—Except as provided in subparagraph (C), any return or taxpayer return information obtained under paragraph (1) or (7)(C) may be disclosed in any judicial or administrative proceeding pertaining to enforcement of a specifically designated Federal criminal statute or related civil forfeiture (not involving tax administration) to which the United States or a Federal agency is a party—

(i) if the court finds that such return or taxpayer return information is probative of a matter in issue relevant in establishing the commission of a crime or the guilt or liability of a party, or

(ii) to the extent required by order of the court pursuant to section 3500 of title 18, United States Code, or rule 16 of the Federal Rules of Criminal Procedure.

(B) RETURN INFORMATION (OTHER THAN TAXPAYER RETURN INFORMATION).—Except as provided in subparagraph (C), any return information (other than taxpayer return information) obtained under paragraph (1), (2), (3)(A) or (C), or (7) may be disclosed in any judicial or administrative proceeding pertaining to enforcement of a specifically designated Federal criminal statute or related civil forfeiture (not involving tax administration) to which the United States or a Federal agency is a party.

(C) CONFIDENTIAL INFORMANT; IMPAIRMENT OF INVESTIGATIONS.—No return or return information shall be admitted into evidence under subparagraph (A)(i) or (B) if the Secretary determines and notifies the Attorney General or his delegate or the head of the Federal agency that such admission would identify a confidential informant or seriously impair a civil or criminal tax investigation.

(D) CONSIDERATION OF CONFIDENTIALITY POLICY.—In ruling upon the admissibility of returns or return information, and in the issuance of an order under subparagraph (A)(ii), the court shall give due consideration to congressional policy favoring the confidentiality of returns and return information as set forth in this title.

(E) REVERSIBLE ERROR.—The admission into evidence of any return or return information contrary to the provisions of this paragraph shall not, as such, constitute reversible error upon appeal of a judgment in the proceeding.

(5) DISCLOSURE TO LOCATE FUGITIVES FROM JUSTICE.—

(A) IN GENERAL.—Except as provided in paragraph (6), the return of an individual or return information with respect to such individual shall, pursuant to and upon the grant of an ex parte order by a Federal district court judge or magistrate judge under subparagraph (B), be open (but only to the extent necessary as provided in such order) to inspection by, or disclosure to, officers and employees of

any Federal agency exclusively for use in locating such individual.

(B) APPLICATION FOR ORDER.—Any person described in paragraph (1)(B) may authorize an application to a Federal district court judge or magistrate judge for an order referred to in subparagraph (A). Upon such application, such judge or magistrate judge may grant such order if he determines on the basis of the facts submitted by the applicant that—

(i) a Federal arrest warrant relating to the commission of a Federal felony offense has been issued for an individual who is a fugitive from justice,

(ii) the return of such individual or return information with respect to such individual is sought exclusively for use in locating such individual, and

(iii) there is reasonable cause to believe that such return or return information may be relevant in determining the location of such individual.

(6) CONFIDENTIAL INFORMANTS; IMPAIRMENT OF INVESTIGATIONS.—The Secretary shall not disclose any return or return information under paragraph (1), (2), (3)(A) or (C), (5), (7), or (8) if the Secretary determines (and, in the case of a request for disclosure pursuant to a court order described in paragraph (1)(B) or (5)(B), certifies to the court) that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

(7) DISCLOSURE UPON REQUEST OF INFORMATION RELATING TO TERRORIST ACTIVITIES, ETC.—

(A) DISCLOSURE TO LAW ENFORCEMENT AGENCIES.—

(i) IN GENERAL.—Except as provided in paragraph (6), upon receipt by the Secretary of a written request which meets the requirements of clause (iii), the Secretary may disclose return information (other than taxpayer return information) to officers and employees of any Federal law enforcement agency who are personally and directly engaged in the response to or investigation of any terrorist incident, threat, or activity.

(ii) DISCLOSURE TO STATE AND LOCAL LAW ENFORCEMENT AGENCIES.—The head of any Federal law enforcement agency may disclose return information obtained under clause (i) to officers and employees of any State or local law enforcement agency but only if such agency is part of a team with the Federal law enforcement agency in such response or investigation and such information is disclosed only to officers and employees who are personally and directly engaged in such response or investigation.

(iii) REQUIREMENTS.—A request meets the requirements of this clause if—

(I) the request is made by the head of any Federal law enforcement agency (or his delegate) involved in the response to or investigation of any terrorist incident, threat, or activity, and

(II) the request sets forth the specific reason or reasons why such disclosure may be relevant to a terrorist incident, threat, or activity.

(iv) LIMITATION ON USE OF INFORMATION.—Information disclosed under this subparagraph shall be solely for the use of the officers and employees to whom such information is disclosed in such response or investigation.

(v) TAXPAYER IDENTITY.—For purposes of this subparagraph, a taxpayer's identity shall not be treated as taxpayer return information.

(B) DISCLOSURE TO INTELLIGENCE AGENCIES.—

(i) IN GENERAL.—Except as provided in paragraph (6), upon receipt by the Secretary of a written request which meets the requirements of clause (ii), the Secretary may disclose return information (other than taxpayer return information) to those officers and employees of the Department of Justice, the Department of the Treasury, and other Federal intelligence agencies who are personally and directly engaged in the collection or analysis of intelligence and counterintelligence information or investigation concerning any terrorist incident, threat, or activity. For purposes of the preceding sentence, the information disclosed under the preceding sentence shall be solely for the use of such officers and employees in such investigation, collection, or analysis.

(ii) REQUIREMENTS.—A request meets the requirements of this subparagraph if the request—

(I) is made by an individual described in clause (iii), and

(II) sets forth the specific reason or reasons why such disclosure may be relevant to a terrorist incident, threat, or activity.

(iii) REQUESTING INDIVIDUALS.—An individual described in this subparagraph is an individual—

(I) who is an officer or employee of the Department of Justice or the Department of the Treasury who is appointed by the President with the advice and consent of the Senate or who is the Director of the United States Secret Service, and

(II) who is responsible for the collection and analysis of intelligence and counterintelligence information concerning any terrorist incident, threat, or activity.

(iv) TAXPAYER IDENTITY.—For purposes of this subparagraph, a taxpayer's identity shall not be treated as taxpayer return information.

(C) DISCLOSURE UNDER EX PARTE ORDERS.—

(i) IN GENERAL.—Except as provided in paragraph (6), any return or return information with respect to any specified taxable period or periods shall, pursuant to and upon the grant of an ex parte order by a Federal district court judge or magistrate judge under clause (ii), be open (but only to the extent necessary

as provided in such order) to inspection by, or disclosure to, officers and employees of any Federal law enforcement agency or Federal intelligence agency who are personally and directly engaged in any investigation, response to, or analysis of intelligence and counterintelligence information concerning any terrorist incident, threat, or activity. Return or return information opened to inspection or disclosure pursuant to the preceding sentence shall be solely for the use of such officers and employees in the investigation, response, or analysis, and in any judicial, administrative, or grand jury proceedings, pertaining to such terrorist incident, threat, or activity.

(ii) APPLICATION FOR ORDER.—The Attorney General, the Deputy Attorney General, the Associate Attorney General, any Assistant Attorney General, or any United States attorney may authorize an application to a Federal district court judge or magistrate judge for the order referred to in clause (i). Upon such application, such judge or magistrate judge may grant such order if he determines on the basis of the facts submitted by the applicant that—

(I) there is reasonable cause to believe, based upon information believed to be reliable, that the return or return information may be relevant to a matter relating to such terrorist incident, threat, or activity, and

(II) the return or return information is sought exclusively for use in a Federal investigation, analysis, or proceeding concerning any terrorist incident, threat, or activity.

(D) SPECIAL RULE FOR EX PARTE DISCLOSURE BY THE IRS.—

(i) IN GENERAL.—Except as provided in paragraph (6), the Secretary may authorize an application to a Federal district court judge or magistrate judge for the order referred to in subparagraph (C)(i). Upon such application, such judge or magistrate judge may grant such order if he determines on the basis of the facts submitted by the applicant that the requirements of subparagraph (C)(ii)(I) are met.

(ii) LIMITATION ON USE OF INFORMATION.—Information disclosed under clause (i)—

(I) may be disclosed only to the extent necessary to apprise the head of the appropriate Federal law enforcement agency responsible for investigating or responding to a terrorist incident, threat, or activity, and

(II) shall be solely for use in a Federal investigation, analysis, or proceeding concerning any terrorist incident, threat, or activity.

The head of such Federal agency may disclose such information to officers and employees of such agency to the extent necessary to investigate or respond to such terrorist incident, threat, or activity.

## (8) COMPTROLLER GENERAL.—

(A) RETURNS AVAILABLE FOR INSPECTION.—Except as provided in subparagraph (C), upon written request by the Comptroller General of the United States, returns and return information shall be open to inspection by, or disclosure to, officers and employees of the Government Accountability Office for the purpose of, and to the extent necessary in, making—

(i) an audit of the Internal Revenue Service, the Bureau of Alcohol, Tobacco, Firearms, and Explosives, Department of Justice, or the Tax and Trade Bureau, Department of the Treasury, which may be required by section 713 of title 31, United States Code, or

(ii) any audit authorized by subsection (p)(6),

except that no such officer or employee shall, except to the extent authorized by subsection (f) or (p)(6), disclose to any person, other than another officer or employee of such office whose official duties require such disclosure, any return or return information described in section 4424(a) in a form which can be associated with, or otherwise identify, directly or indirectly, a particular taxpayer, nor shall such officer or employee disclose any other return or return information, except as otherwise expressly provided by law, to any person other than such other officer or employee of such office in a form which can be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.

## (B) AUDITS OF OTHER AGENCIES.—

(i) IN GENERAL.—Nothing in this section shall prohibit any return or return information obtained under this title by any Federal agency (other than an agency referred to in subparagraph (A)) or by a Trustee as defined in the District of Columbia Retirement Protection Act of 1997, for use in any program or activity from being open to inspection by, or disclosure to, officers and employees of the Government Accountability Office if such inspection or disclosure is—

(I) for purposes of, and to the extent necessary in, making an audit authorized by law of such program or activity, and

(II) pursuant to a written request by the Comptroller General of the United States to the head of such Federal agency.

(ii) INFORMATION FROM SECRETARY.—If the Comptroller General of the United States determines that the returns or return information available under clause (i) are not sufficient for purposes of making an audit of any program or activity of a Federal agency (other than an agency referred to in subparagraph (A)), upon written request by the Comptroller General to the Secretary, returns and return information (of the type authorized by subsection (l) or (m) to be made available to the Federal agency for use in such program or activity) shall be open to inspection by, or disclosure to, officers and employees of the Government

Accountability Office for the purpose of, and to the extent necessary in, making such audit.

(iii) REQUIREMENT OF NOTIFICATION UPON COMPLETION OF AUDIT.—Within 90 days after the completion of an audit with respect to which returns or return information were opened to inspection or disclosed under clause (i) or (ii), the Comptroller General of the United States shall notify in writing the Joint Committee on Taxation of such completion. Such notice shall include—

(I) a description of the use of the returns and return information by the Federal agency involved,

(II) such recommendations with respect to the use of returns and return information by such Federal agency as the Comptroller General deems appropriate, and

(III) a statement on the impact of any such recommendations on confidentiality of returns and return information and the administration of this title.

(iv) CERTAIN RESTRICTIONS MADE APPLICABLE.—The restrictions contained in subparagraph (A) on the disclosure of any returns or return information open to inspection or disclosed under such subparagraph shall also apply to returns and return information open to inspection or disclosed under this subparagraph.

(C) DISAPPROVAL BY JOINT COMMITTEE ON TAXATION.—Returns and return information shall not be open to inspection or disclosed under subparagraph (A) or (B) with respect to an audit—

(i) unless the Comptroller General of the United States notifies in writing the Joint Committee on Taxation of such audit, and

(ii) if the Joint Committee on Taxation disapproves such audit by a vote of at least two-thirds of its members within the 30-day period beginning on the day the Joint Committee on Taxation receives such notice.

(j) STATISTICAL USE.—

(1) DEPARTMENT OF COMMERCE.—Upon request in writing by the Secretary of Commerce, the Secretary shall furnish—

(A) such returns, or return information reflected thereon, to officers and employees of the Bureau of the Census, and

(B) such return information reflected on returns of corporations to officers and employees of the Bureau of Economic Analysis,

as the Secretary may prescribe by regulation for the purpose of, but only to the extent necessary in, the structuring of censuses and national economic accounts and conducting related statistical activities authorized by law.

(2) FEDERAL TRADE COMMISSION.—Upon request in writing by the Chairman of the Federal Trade Commission, the Secretary shall furnish such return information reflected on any return of a corporation with respect to the tax imposed by chapter 1 to officers and employees of the Division of Financial Statistics of the Bureau of Economics of such commission as

the Secretary may prescribe by regulation for the purpose of, but only to the extent necessary in, administration by such division of legally authorized economic surveys of corporations.

(3) DEPARTMENT OF TREASURY.—Returns and return information shall be open to inspection by or disclosure to officers and employees of the Department of the Treasury whose official duties require such inspection or disclosure for the purpose of, but only to the extent necessary in, preparing economic or financial forecasts, projections, analyses, and statistical studies and conducting related activities. Such inspection or disclosure shall be permitted only upon written request which sets forth the specific reason or reasons why such inspection or disclosure is necessary and which is signed by the head of the bureau or office of the Department of the Treasury requesting the inspection or disclosure.

(4) ANONYMOUS FORM.—No person who receives a return or return information under this subsection shall disclose such return or return information to any person other than the taxpayer to whom it relates except in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.

(5) DEPARTMENT OF AGRICULTURE.—Upon request in writing by the Secretary of Agriculture, the Secretary shall furnish such returns, or return information reflected thereon, as the Secretary may prescribe by regulation to officers and employees of the Department of Agriculture whose official duties require access to such returns or information for the purpose of, but only to the extent necessary in, structuring, preparing, and conducting the census of agriculture pursuant to the Census of Agriculture Act of 1997 (Public Law 105-113).

(6) CONGRESSIONAL BUDGET OFFICE.—Upon written request by the Director of the Congressional Budget Office, the Secretary shall furnish to officers and employees of the Congressional Budget Office return information for the purpose of, but only to the extent necessary for, long-term models of the social security and medicare programs.

(k) DISCLOSURE OF CERTAIN RETURNS AND RETURN INFORMATION FOR TAX ADMINISTRATION PURPOSES.—

(1) DISCLOSURE OF ACCEPTED OFFERS-IN-COMPROMISE.—Return information shall be disclosed to members of the general public to the extent necessary to permit inspection of any accepted offer-in-compromise under section 7122 relating to the liability for a tax imposed by this title.

(2) DISCLOSURE OF AMOUNT OF OUTSTANDING LIEN.—If a notice of lien has been filed pursuant to section 6323(f), the amount of the outstanding obligation secured by such lien may be disclosed to any person who furnishes satisfactory written evidence that he has a right in the property subject to such lien or intends to obtain a right in such property.

(3) DISCLOSURE OF RETURN INFORMATION TO CORRECT MISSTATEMENTS OF FACT.—The Secretary may, but only following approval by the Joint Committee on Taxation, disclose such return information or any other information with respect to any specific taxpayer to the extent necessary for tax administration purposes to correct a misstatement of fact published



or disclosed with respect to such taxpayer's return or any transaction of the taxpayer with the Internal Revenue Service.

(4) DISCLOSURE OF COMPETENT AUTHORITY UNDER INCOME TAX CONVENTION.—A return or return information may be disclosed to a competent authority of a foreign government which has an income tax or gift and estate tax convention, or other convention or bilateral agreement relating to the exchange of tax information, with the United States but only to the extent provided in, and subject to the terms and conditions of, such convention or bilateral agreement.

(5) STATE AGENCIES REGULATING TAX RETURN PREPARERS.—Taxpayer identity information with respect to any tax return preparer, and information as to whether or not any penalty has been assessed against such tax return preparer under section 6694, 6695, or 7216, may be furnished to any agency, body, or commission lawfully charged under any State or local law with the licensing, registration, or regulation of tax return preparers. Such information may be furnished only upon written request by the head of such agency, body, or commission designating the officers or employees to whom such information is to be furnished. Information may be furnished and used under this paragraph only for purposes of the licensing, registration, or regulation of tax return preparers.

(6) DISCLOSURE BY CERTAIN OFFICERS AND EMPLOYEES FOR INVESTIGATIVE PURPOSES.—An internal revenue officer or employee and an officer or employee of the Office of Treasury Inspector General for Tax Administration may, in connection with his official duties relating to any audit, collection activity, or civil or criminal tax investigation or any other offense under the internal revenue laws, disclose return information to the extent that such disclosure is necessary in obtaining information, which is not otherwise reasonably available, with respect to the correct determination of tax, liability for tax, or the amount to be collected or with respect to the enforcement of any other provision of this title. Such disclosures shall be made only in such situations and under such conditions as the Secretary may prescribe by regulation.

(7) DISCLOSURE OF EXCISE TAX REGISTRATION INFORMATION.—To the extent the Secretary determines that disclosure is necessary to permit the effective administration of subtitle D, the Secretary may disclose—

(A) the name, address, and registration number of each person who is registered under any provision of subtitle D (and, in the case of a registered terminal operator, the address of each terminal operated by such operator), and

(B) the registration status of any person.

(8) LEVIES ON CERTAIN GOVERNMENT PAYMENTS.—

(A) DISCLOSURE OF RETURN INFORMATION IN LEVIES ON FINANCIAL MANAGEMENT SERVICE.—In serving a notice of levy, or release of such levy, with respect to any applicable government payment, the Secretary may disclose to officers and employees of the Financial Management Service—

(i) return information, including taxpayer identity information,

(ii) the amount of any unpaid liability under this title (including penalties and interest), and

(iii) the type of tax and tax period to which such unpaid liability relates.

(B) RESTRICTION ON USE OF DISCLOSED INFORMATION.—

Return information disclosed under subparagraph (A) may be used by officers and employees of the Financial Management Service only for the purpose of, and to the extent necessary in, transferring levied funds in satisfaction of the levy, maintaining appropriate agency records in regard to such levy or the release thereof, notifying the taxpayer and the agency certifying such payment that the levy has been honored, or in the defense of any litigation ensuing from the honor of such levy.

(C) APPLICABLE GOVERNMENT PAYMENT.—For purposes of this paragraph, the term “applicable government payment” means—

(i) any Federal payment (other than a payment for which eligibility is based on the income or assets (or both) of a payee) certified to the Financial Management Service for disbursement, and

(ii) any other payment which is certified to the Financial Management Service for disbursement and which the Secretary designates by published notice.

(9) DISCLOSURE OF INFORMATION TO ADMINISTER SECTION 6311.—The Secretary may disclose returns or return information to financial institutions and others to the extent the Secretary deems necessary for the administration of section 6311. Disclosures of information for purposes other than to accept payments by checks or money orders shall be made only to the extent authorized by written procedures promulgated by the Secretary.

(10) DISCLOSURE OF CERTAIN RETURNS AND RETURN INFORMATION TO CERTAIN PRISON OFFICIALS.—

(A) IN GENERAL.—Under such procedures as the Secretary may prescribe, the Secretary may disclose to officers and employees of the Federal Bureau of Prisons and of any State agency charged with the responsibility for administration of prisons any returns or return information with respect to individuals incarcerated in Federal or State prison systems whom the Secretary has determined may have filed or facilitated the filing of a false or fraudulent return to the extent that the Secretary determines that such disclosure is necessary to permit effective Federal tax administration.

(B) DISCLOSURE TO CONTRACTOR-RUN PRISONS.—Under such procedures as the Secretary may prescribe, the disclosures authorized by subparagraph (A) may be made to contractors responsible for the operation of a Federal or State prison on behalf of such Bureau or agency.

(C) RESTRICTIONS ON USE OF DISCLOSED INFORMATION.—Any return or return information received under this paragraph shall be used only for the purposes of and to the extent necessary in taking administrative action to prevent the filing of false and fraudulent returns, including admin-

istrative actions to address possible violations of administrative rules and regulations of the prison facility and in administrative and judicial proceedings arising from such administrative actions.

(D) RESTRICTIONS ON REDISCLOSURE AND DISCLOSURE TO LEGAL REPRESENTATIVES.—Notwithstanding subsection (h)—

(i) RESTRICTIONS ON REDISCLOSURE.—Except as provided in clause (ii), any officer, employee, or contractor of the Federal Bureau of Prisons or of any State agency charged with the responsibility for administration of prisons shall not disclose any information obtained under this paragraph to any person other than an officer or employee or contractor of such Bureau or agency personally and directly engaged in the administration of prison facilities on behalf of such Bureau or agency.

(ii) DISCLOSURE TO LEGAL REPRESENTATIVES.—The returns and return information disclosed under this paragraph may be disclosed to the duly authorized legal representative of the Federal Bureau of Prisons, State agency, or contractor charged with the responsibility for administration of prisons, or of the incarcerated individual accused of filing the false or fraudulent return who is a party to an action or proceeding described in subparagraph (C), solely in preparation for, or for use in, such action or proceeding.

(11) DISCLOSURE OF RETURN INFORMATION TO DEPARTMENT OF STATE FOR PURPOSES OF PASSPORT REVOCATION UNDER SECTION 7345.—

(A) IN GENERAL.—The Secretary shall, upon receiving a certification described in section 7345, disclose to the Secretary of State return information with respect to a taxpayer who has a seriously delinquent tax debt described in such section. Such return information shall be limited to—

(i) the taxpayer identity information with respect to such taxpayer, and

(ii) the amount of such seriously delinquent tax debt.

(B) RESTRICTION ON DISCLOSURE.—Return information disclosed under subparagraph (A) may be used by officers and employees of the Department of State for the purposes of, and to the extent necessary in, carrying out the requirements of section 32101 of the FAST Act.

(12) QUALIFIED TAX COLLECTION CONTRACTORS.—Persons providing services pursuant to a qualified tax collection contract under section 6306 may, if speaking to a person who has identified himself or herself as having the name of the taxpayer to which a tax receivable (within the meaning of such section) relates, identify themselves as contractors of the Internal Revenue Service and disclose the business name of the contractor, and the nature, subject, and reason for the contact. Disclosures under this paragraph shall be made only in such situations and under such conditions as have been approved by the Secretary.

(1) DISCLOSURE OF RETURNS AND RETURN INFORMATION FOR PURPOSES OTHER THAN TAX ADMINISTRATION.—

(1) DISCLOSURE OF CERTAIN RETURNS AND RETURN INFORMATION TO SOCIAL SECURITY ADMINISTRATION AND RAILROAD RETIREMENT BOARD.—The Secretary may, upon written request, disclose returns and return information with respect to—

(A) taxes imposed by chapters 2, 21, and 24, to the Social Security Administration for purposes of its administration of the Social Security Act;

(B) a plan to which part I of subchapter D of chapter 1 applies, to the Social Security Administration for purposes of carrying out its responsibility under section 1131 of the Social Security Act, limited, however to return information described in section 6057(d); and

(C) taxes imposed by chapter 22, to the Railroad Retirement Board for purposes of its administration of the Railroad Retirement Act.

(2) DISCLOSURE OF RETURNS AND RETURN INFORMATION TO THE DEPARTMENT OF LABOR AND PENSION BENEFIT GUARANTY CORPORATION.—The Secretary may, upon written request, furnish returns and return information to the proper officers and employees of the Department of Labor and the Pension Benefit Guaranty Corporation for purposes of, but only to the extent necessary in, the administration of titles I and IV of the Employee Retirement Income Security Act of 1974.

(3) DISCLOSURE THAT APPLICANT FOR FEDERAL LOAN HAS TAX DELINQUENT ACCOUNT.—

(A) IN GENERAL.—Upon written request, the Secretary may disclose to the head of the Federal agency administering any included Federal loan program whether or not an applicant for a loan under such program has a tax delinquent account.

(B) RESTRICTION ON DISCLOSURE.—Any disclosure under subparagraph (A) shall be made only for the purpose of, and to the extent necessary in, determining the creditworthiness of the applicant for the loan in question.

(C) INCLUDED FEDERAL LOAN PROGRAM DEFINED.—For purposes of this paragraph, the term “included Federal loan program” means any program under which the United States or a Federal agency makes, guarantees, or insures loans.

(4) DISCLOSURE OF RETURNS AND RETURN INFORMATION FOR USE IN PERSONNEL OR CLAIMANT REPRESENTATIVE MATTERS.—The Secretary may disclose returns and return information—

(A) upon written request—

(i) to an employee or former employee of the Department of the Treasury, or to the duly authorized legal representative of such employee or former employee, who is or may be a party to any administrative action or proceeding affecting the personnel rights of such employee or former employee; or

(ii) to any person, or to the duly authorized legal representative of such person, whose rights are or may be affected by an administrative action or proceeding under section 330 of title 31, United States Code,

solely for use in the action or proceeding, or in preparation for the action or proceeding, but only to the extent that the Secretary determines that such returns or return information is or may be relevant and material to the action or proceeding; or

(B) to officers and employees of the Department of the Treasury for use in any action or proceeding described in subparagraph (A), or in preparation for such action or proceeding, to the extent necessary to advance or protect the interests of the United States.

(5) SOCIAL SECURITY ADMINISTRATION.—Upon written request by the Commissioner of Social Security, the Secretary may disclose information returns filed pursuant to part III of subchapter A of chapter 61 of this subtitle for the purpose of—

(A) carrying out, in accordance with an agreement entered into pursuant to section 232 of the Social Security Act, an effective return processing program; or

(B) providing information regarding the mortality status of individuals for epidemiological and similar research in accordance with section 1106(d) of the Social Security Act.

(6) DISCLOSURE OF RETURN INFORMATION TO FEDERAL, STATE, AND LOCAL CHILD SUPPORT ENFORCEMENT AGENCIES.—

(A) RETURN INFORMATION FROM INTERNAL REVENUE SERVICE.—The Secretary may, upon written request, disclose to the appropriate Federal, State, or local child support enforcement agency—

(i) available return information from the master files of the Internal Revenue Service relating to the social security account number (or numbers, if the individual involved has more than one such number), address, filing status, amounts and nature of income, and the number of dependents reported on any return filed by, or with respect to, any individual with respect to whom child support obligations are sought to be established or enforced pursuant to the provisions of part D of title IV of the Social Security Act and with respect to any individual to whom such support obligations are owing, and

(ii) available return information reflected on any return filed by, or with respect to, any individual described in clause (i) relating to the amount of such individual's gross income (as defined in section 61) or consisting of the names and addresses of payors of such income and the names of any dependents reported on such return, but only if such return information is not reasonably available from any other source.

(B) DISCLOSURE TO CERTAIN AGENTS.—The following information disclosed to any child support enforcement agency under subparagraph (A) with respect to any individual with respect to whom child support obligations are sought to be established or enforced may be disclosed by such agency to any agent of such agency which is under contract with such agency to carry out the purposes described in subparagraph (C):

(i) The address and social security account number (or numbers) of such individual.

(ii) The amount of any reduction under section 6402(c) (relating to offset of past-due support against overpayments) in any overpayment otherwise payable to such individual.

(C) RESTRICTION ON DISCLOSURE.—Information may be disclosed under this paragraph only for purposes of, and to the extent necessary in, establishing and collecting child support obligations from, and locating, individuals owing such obligations.

(7) DISCLOSURE OF RETURN INFORMATION TO FEDERAL, STATE, AND LOCAL AGENCIES ADMINISTERING CERTAIN PROGRAMS UNDER THE SOCIAL SECURITY ACT, THE FOOD AND NUTRITION ACT OF 2008 OR TITLE 38, UNITED STATES CODE, OR CERTAIN HOUSING ASSISTANCE PROGRAMS.—

(A) RETURN INFORMATION FROM SOCIAL SECURITY ADMINISTRATION.—The Commissioner of Social Security shall, upon written request, disclose return information from returns with respect to net earnings from self-employment (as defined in section 1402), wages (as defined in section 3121(a) or 3401(a)), and payments of retirement income, which have been disclosed to the Social Security Administration as provided by paragraph (1) or (5) of this subsection, to any Federal, State, or local agency administering a program listed in subparagraph (D).

(B) RETURN INFORMATION FROM INTERNAL REVENUE SERVICE.—The Secretary shall, upon written request, disclose current return information from returns with respect to unearned income from the Internal Revenue Service files to any Federal, State, or local agency administering a program listed in subparagraph (D).

(C) RESTRICTION ON DISCLOSURE.—The Commissioner of Social Security and the Secretary shall disclose return information under subparagraphs (A) and (B) only for purposes of, and to the extent necessary in, determining eligibility for, or the correct amount of, benefits under a program listed in subparagraph (D).

(D) PROGRAMS TO WHICH RULE APPLIES.—The programs to which this paragraph applies are:

(i) a State program funded under part A of title IV of the Social Security Act;

(ii) medical assistance provided under a State plan approved under title XIX of the Social Security Act or subsidies provided under section 1860D-14 of such Act;

(iii) supplemental security income benefits provided under title XVI of the Social Security Act, and federally administered supplementary payments of the type described in section 1616(a) of such Act (including payments pursuant to an agreement entered into under section 212(a) of Public Law 93-66);

(iv) any benefits provided under a State plan approved under title I, X, XIV, or XVI of the Social Security Act (as those titles apply to Puerto Rico, Guam, and the Virgin Islands);

(v) unemployment compensation provided under a State law described in section 3304 of this title;

(vi) assistance provided under the Food and Nutrition Act of 2008;

(vii) State-administered supplementary payments of the type described in section 1616(a) of the Social Security Act (including payments pursuant to an agreement entered into under section 212(a) of Public Law 93-66);

(viii)(I) any needs-based pension provided under chapter 15 of title 38, United States Code, or under any other law administered by the Secretary of Veterans Affairs;

(II) parents' dependency and indemnity compensation provided under section 1315 of title 38, United States Code;

(III) health-care services furnished under sections 1710(a)(2)(G), 1710(a)(3), and 1710(b) of such title; and

(IV) compensation paid under chapter 11 of title 38, United States Code, at the 100 percent rate based solely on unemployability and without regard to the fact that the disability or disabilities are not rated as 100 percent disabling under the rating schedule; and

(ix) any housing assistance program administered by the Department of Housing and Urban Development that involves initial and periodic review of an applicant's or participant's income, except that return information may be disclosed under this clause only on written request by the Secretary of Housing and Urban Development and only for use by officers and employees of the Department of Housing and Urban Development with respect to applicants for and participants in such programs.

Only return information from returns with respect to net earnings from self-employment and wages may be disclosed under this paragraph for use with respect to any program described in clause (viii)(IV).

**(8) DISCLOSURE OF CERTAIN RETURN INFORMATION BY SOCIAL SECURITY ADMINISTRATION TO FEDERAL, STATE, AND LOCAL CHILD SUPPORT ENFORCEMENT AGENCIES.—**

**(A) IN GENERAL.—**Upon written request, the Commissioner of Social Security shall disclose directly to officers and employees of a Federal or State or local child support enforcement agency return information from returns with respect to social security account numbers, net earnings from self-employment (as defined in section 1402), wages (as defined in section 3121(a) or 3401(a)), and payments of retirement income which have been disclosed to the Social Security Administration as provided by paragraph (1) or (5) of this subsection.

**(B) RESTRICTION ON DISCLOSURE.—**The Commissioner of Social Security shall disclose return information under subparagraph (A) only for purposes of, and to the extent

necessary in, establishing and collecting child support obligations from, and locating, individuals owing such obligations. For purposes of the preceding sentence, the term “child support obligations” only includes obligations which are being enforced pursuant to a plan described in section 454 of the Social Security Act which has been approved by the Secretary of Health and Human Services under part D of title IV of such Act.

(C) STATE OR LOCAL CHILD SUPPORT ENFORCEMENT AGENCY.—For purposes of this paragraph, the term “State or local child support enforcement agency” means any agency of a State or political subdivision thereof operating pursuant to a plan described in subparagraph (B).

(9) DISCLOSURE OF ALCOHOL FUEL PRODUCERS TO ADMINISTRATORS OF STATE ALCOHOL LAWS.—Notwithstanding any other provision of this section, the Secretary may disclose—

(A) the name and address of any person who is qualified to produce alcohol for fuel use under section 5181, and

(B) the location of any premises to be used by such person in producing alcohol for fuel, to any State agency, body, or commission, or its legal representative, which is charged under the laws of such State with responsibility for administration of State alcohol laws solely for use in the administration of such laws.

(10) DISCLOSURE OF CERTAIN INFORMATION TO AGENCIES REQUESTING A REDUCTION UNDER SUBSECTION (C), (D), (E), OR (F) OF SECTION 6402.—

(A) RETURN INFORMATION FROM INTERNAL REVENUE SERVICE.—The Secretary may, upon receiving a written request, disclose to officers and employees of any agency seeking a reduction under subsection (c), (d), (e), or (f) of section 6402, to officers and employees of the Department of Labor for purposes of facilitating the exchange of data in connection with a notice submitted under subsection (f)(5)(C) of section 6402, and to officers and employees of the Department of the Treasury in connection with such reduction—

(i) taxpayer identity information with respect to the taxpayer against whom such a reduction was made or not made and with respect to any other person filing a joint return with such taxpayer,

(ii) the fact that a reduction has been made or has not been made under such subsection with respect to such taxpayer,

(iii) the amount of such reduction,

(iv) whether such taxpayer filed a joint return, and

(v) the fact that a payment was made (and the amount of the payment) to the spouse of the taxpayer on the basis of a joint return.

(B) RESTRICTION ON USE OF DISCLOSED INFORMATION.—

(i) Any officers and employees of an agency receiving return information under subparagraph (A) shall use such information only for the purposes of, and to the extent necessary in, establishing appropriate agency records, locating any person with respect to whom a



reduction under subsection (c), (d), (e), or (f) of section 6402 is sought for purposes of collecting the debt with respect to which the reduction is sought, or in the defense of any litigation or administrative procedure ensuing from a reduction made under subsection (c), (d), (e), or (f) of section 6402 and to officers and employees of the Department of the Treasury in connection with such reduction.

(ii) Notwithstanding clause (i), return information disclosed to officers and employees of the Department of Labor may be accessed by agents who maintain and provide technological support to the Department of Labor's Interstate Connection Network (ICON) solely for the purpose of providing such maintenance and support.

(11) DISCLOSURE OF RETURN INFORMATION TO CARRY OUT FEDERAL EMPLOYEES' RETIREMENT SYSTEM.—

(A) IN GENERAL.—The Commissioner of Social Security shall, on written request, disclose to the Office of Personnel Management return information from returns with respect to net earnings from self-employment (as defined in section 1402), wages (as defined in section 3121(a) or 3401(a)), and payments of retirement income, which have been disclosed to the Social Security Administration as provided by paragraph (1) or (5).

(B) RESTRICTION ON DISCLOSURE.—The Commissioner of Social Security shall disclose return information under subparagraph (A) only for purposes of, and to the extent necessary in, the administration of chapters 83 and 84 of title 5, United States Code.

(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 Centers for Medicare & Medicaid Services, 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)), above an amount (if any) specified by the Secretary of Health and Human Services, 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, above an amount (if any) specified by the Secretary of Health and Human Services, 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 CENTERS FOR MEDICARE & MEDICAID SERVICES.—With respect to the information disclosed under subparagraph (B), the Administrator of the Centers for Medicare & Medicaid Services 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 any group health plan (as defined in section 5000(b)(1)).

(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.

(13) DISCLOSURE OF RETURN INFORMATION TO CARRY OUT INCOME CONTINGENT REPAYMENT OF STUDENT LOANS.—

(A) IN GENERAL.—The Secretary may, upon written request from the Secretary of Education, disclose to officers and employees of the Department of Education return information with respect to a taxpayer who has received an applicable student loan and whose loan repayment amounts are based in whole or in part on the taxpayer’s income. Such return information shall be limited to—

(i) taxpayer identity information with respect to such taxpayer,

(ii) the filing status of such taxpayer, and

(iii) the adjusted gross income of such taxpayer.

(B) RESTRICTION ON USE OF DISCLOSED INFORMATION.—Return information disclosed under subparagraph (A) may be used by officers and employees of the Department of Education only for the purposes of, and to the extent necessary in, establishing the appropriate income contingent repayment amount for an applicable student loan.

(C) APPLICABLE STUDENT LOAN.—For purposes of this paragraph, the term “applicable student loan” means—

(i) any loan made under the program authorized under part D of title IV of the Higher Education Act of 1965, and

(ii) any loan made under part B or E of title IV of the Higher Education Act of 1965 which is in default and has been assigned to the Department of Education.

(D) TERMINATION.—This paragraph shall not apply to any request made after December 31, 2007.

(14) DISCLOSURE OF RETURN INFORMATION TO UNITED STATES CUSTOMS SERVICE.—The Secretary may, upon written request from the Commissioner of the United States Customs Service, disclose to officers and employees of the Department of the Treasury such return information with respect to taxes imposed by chapters 1 and 6 as the Secretary may prescribe by regulations, solely for the purpose of, and only to the extent necessary in—

(A) ascertaining the correctness of any entry in audits as provided for in section 509 of the Tariff Act of 1930 (19 U.S.C. 1509), or

(B) other actions to recover any loss of revenue, or to collect duties, taxes, and fees, determined to be due and owing pursuant to such audits.

(15) DISCLOSURE OF RETURNS FILED UNDER SECTION 6050I.—The Secretary may, upon written request, disclose to officers and employees of—

(A) any Federal agency,

(B) any agency of a State or local government, or

(C) any agency of the government of a foreign country, information contained on returns filed under section 6050I. Any such disclosure shall be made on the same basis, and subject to the same conditions, as apply to disclosures of information on reports filed under section 5313 of title 31, United States Code; except that no disclosure under this paragraph shall be made for purposes of the administration of any tax law.

(16) DISCLOSURE OF RETURN INFORMATION FOR PURPOSES OF ADMINISTERING THE DISTRICT OF COLUMBIA RETIREMENT PROTECTION ACT OF 1997.—

(A) IN GENERAL.—Upon written request available return information (including such information disclosed to the Social Security Administration under paragraph (1) or (5) of this subsection), relating to the amount of wage income (as defined in section 3121(a) or 3401(a)), the name, address, and identifying number assigned under section 6109, of payors of wage income, taxpayer identity (as defined in section 6103 (b)(6)), and the occupational status reflected on any return filed by, or with respect to, any individual with respect to whom eligibility for, or the correct amount of, benefits under the District of Columbia Retirement Protection Act of 1997, is sought to be determined, shall be disclosed by the Commissioner of Social Security, or to the extent not available from the Social Security Administration, by the Secretary, to any duly authorized officer or employee of the Department of the Treasury, or a Trustee or any designated officer or employee of a Trustee (as defined in the District of Columbia Retirement Protection Act of 1997), or any actuary engaged by a Trustee under the terms of the District of Columbia Retirement Protection Act of 1997, whose official duties require such disclosure, solely for the purpose of, and to the extent necessary in, determining an individual's eligibility for, or the correct amount of, benefits under the District of Columbia Retirement Protection Act of 1997.

(B) DISCLOSURE FOR USE IN JUDICIAL OR ADMINISTRATIVE PROCEEDINGS.—Return information disclosed to any person under this paragraph may be disclosed in a judicial or administrative proceeding relating to the determination of an individual's eligibility for, or the correct amount of, benefits under the District of Columbia Retirement Protection Act of 1997.

(17) DISCLOSURE TO NATIONAL ARCHIVES AND RECORDS ADMINISTRATION.—The Secretary shall, upon written request from the Archivist of the United States, disclose or authorize the disclosure of returns and return information to officers and employees of the National Archives and Records Administration for purposes of, and only to the extent necessary in, the appraisal of records for destruction or retention. No such officer or employee shall, except to the extent authorized by subsection (f), (i)(8), or (p), disclose any return or return information disclosed under the preceding sentence to any person other than to the Secretary, or to another officer or employee of the National Archives and Records Administration whose official duties require such disclosure for purposes of such appraisal.

(18) DISCLOSURE OF RETURN INFORMATION FOR PURPOSES OF CARRYING OUT A PROGRAM FOR ADVANCE PAYMENT OF CREDIT FOR HEALTH INSURANCE COSTS OF ELIGIBLE INDIVIDUALS.—The Secretary may disclose to providers of health insurance for any certified individual (as defined in section 7527(c)) return information with respect to such certified individual only to the extent necessary to carry out the program established by section 7527 (relating to advance payment of credit for health insurance costs of eligible individuals).

(19) DISCLOSURE OF RETURN INFORMATION FOR PURPOSES OF PROVIDING TRANSITIONAL ASSISTANCE UNDER MEDICARE DISCOUNT CARD PROGRAM.—

(A) IN GENERAL.—The Secretary, upon written request from the Secretary of Health and Human Services pursuant to carrying out section 1860D-31 of the Social Security Act, shall disclose to officers, employees, and contractors of the Department of Health and Human Services with respect to a taxpayer for the applicable year—

(i)(I) whether the adjusted gross income, as modified in accordance with specifications of the Secretary of Health and Human Services for purposes of carrying out such section, of such taxpayer and, if applicable, such taxpayer's spouse, for the applicable year, exceeds the amounts specified by the Secretary of Health and Human Services in order to apply the 100 and 135 percent of the poverty lines under such section, (II) whether the return was a joint return, and (III) the applicable year, or

(ii) if applicable, the fact that there is no return filed for such taxpayer for the applicable year.

(B) DEFINITION OF APPLICABLE YEAR.—For the purposes of this subsection, the term “applicable year” means the most recent taxable year for which information is available in the Internal Revenue Service's taxpayer data information systems, or, if there is no return filed for such taxpayer for such year, the prior taxable year.

(C) RESTRICTION ON USE OF DISCLOSED INFORMATION.—Return information disclosed under this paragraph may be used only for the purposes of determining eligibility for and administering transitional assistance under section 1860D-31 of the Social Security Act.

(20) DISCLOSURE OF RETURN INFORMATION TO CARRY OUT MEDICARE PART B PREMIUM SUBSIDY ADJUSTMENT AND PART D BASE BENEFICIARY PREMIUM INCREASE.—

(A) IN GENERAL.—The Secretary shall, upon written request from the Commissioner of Social Security, disclose to officers, employees, and contractors of the Social Security Administration return information of a taxpayer whose premium (according to the records of the Secretary) may be subject to adjustment under section 1839(i) or increase under section 1860D-13(a)(7) of the Social Security Act. Such return information shall be limited to—

(i) taxpayer identity information with respect to such taxpayer,

(ii) the filing status of such taxpayer,

(iii) the adjusted gross income of such taxpayer,

(iv) the amounts excluded from such taxpayer's gross income under sections 135 and 911 to the extent such information is available,

(v) the interest received or accrued during the taxable year which is exempt from the tax imposed by chapter 1 to the extent such information is available,

(vi) the amounts excluded from such taxpayer's gross income by sections 931 and 933 to the extent such information is available,

(vii) such other information relating to the liability of the taxpayer as is prescribed by the Secretary by regulation as might indicate in the case of a taxpayer who is an individual described in subsection (i)(4)(B)(iii) of section 1839 of the Social Security Act that the amount of the premium of the taxpayer under such section may be subject to adjustment under subsection (i) of such section or increase under section 1860D-13(a)(7) of such Act and the amount of such adjustment, and

(viii) the taxable year with respect to which the preceding information relates.

(B) RESTRICTION ON USE OF DISCLOSED INFORMATION.—

(i) IN GENERAL.—Return information disclosed under subparagraph (A) may be used by officers, employees, and contractors of the Social Security Administration only for the purposes of, and to the extent necessary in, establishing the appropriate amount of any premium adjustment under such section 1839(i) or increase under such section 1860D-13(a)(7) or for the purpose of resolving taxpayer appeals with respect to any such premium adjustment or increase.

(ii) DISCLOSURE TO OTHER AGENCIES.—Officers, employees, and contractors of the Social Security Administration may disclose—

(I) the taxpayer identity information and the amount of the premium subsidy adjustment or premium increase with respect to a taxpayer described in subparagraph (A) to officers, employees, and contractors of the Centers for Medicare and Medicaid Services, to the extent that such disclo-

sure is necessary for the collection of the premium subsidy amount or the increased premium amount,

(II) the taxpayer identity information and the amount of the premium subsidy adjustment or the increased premium amount with respect to a taxpayer described in subparagraph (A) to officers and employees of the Office of Personnel Management and the Railroad Retirement Board, to the extent that such disclosure is necessary for the collection of the premium subsidy amount or the increased premium amount,

(III) return information with respect to a taxpayer described in subparagraph (A) to officers and employees of the Department of Health and Human Services to the extent necessary to resolve administrative appeals of such premium subsidy adjustment or increased premium, and

(IV) return information with respect to a taxpayer described in subparagraph (A) to officers and employees of the Department of Justice for use in judicial proceedings to the extent necessary to carry out the purposes described in clause (i).

(21) DISCLOSURE OF RETURN INFORMATION TO CARRY OUT ELIGIBILITY REQUIREMENTS FOR CERTAIN PROGRAMS.—

(A) IN GENERAL.—The Secretary, upon written request from the Secretary of Health and Human Services, shall disclose to officers, employees, and contractors of the Department of Health and Human Services return information of any taxpayer whose income is relevant in determining any premium tax credit under section 36B or any cost-sharing reduction under section 1402 of the Patient Protection and Affordable Care Act or eligibility for participation in a State medicaid program under title XIX of the Social Security Act, a State's children's health insurance program under title XXI of the Social Security Act, or a basic health program under section 1331 of Patient Protection and Affordable Care Act. Such return information shall be limited to—

(i) taxpayer identity information with respect to such taxpayer,

(ii) the filing status of such taxpayer,

[(iii) the number of individuals for whom a deduction is allowed under section 151 with respect to the taxpayer (including the taxpayer and the taxpayer's spouse),]

(iii) *the number of the taxpayer's dependents,*

(iv) the modified adjusted gross income (as defined in section 36B) of such taxpayer and each of the other individuals included under clause (iii) who are required to file a return of tax imposed by chapter 1 for the taxable year,

(v) such other information as is prescribed by the Secretary by regulation as might indicate whether the

taxpayer is eligible for such credit or reduction (and the amount thereof), and

(vi) the taxable year with respect to which the preceding information relates or, if applicable, the fact that such information is not available.

(B) INFORMATION TO EXCHANGE AND STATE AGENCIES.—

The Secretary of Health and Human Services may disclose to an Exchange established under the Patient Protection and Affordable Care Act or its contractors, or to a State agency administering a State program described in subparagraph (A) or its contractors, any inconsistency between the information provided by the Exchange or State agency to the Secretary and the information provided to the Secretary under subparagraph (A).

(C) RESTRICTION ON USE OF DISCLOSED INFORMATION.—

Return information disclosed under subparagraph (A) or (B) may be used by officers, employees, and contractors of the Department of Health and Human Services, an Exchange, or a State agency only for the purposes of, and to the extent necessary in—

(i) establishing eligibility for participation in the Exchange, and verifying the appropriate amount of, any credit or reduction described in subparagraph (A),

(ii) determining eligibility for participation in the State programs described in subparagraph (A).

(22) DISCLOSURE OF RETURN INFORMATION TO DEPARTMENT OF HEALTH AND HUMAN SERVICES FOR PURPOSES OF ENHANCING MEDICARE PROGRAM INTEGRITY.—

(A) IN GENERAL.—The Secretary shall, upon written request from the Secretary of Health and Human Services, disclose to officers and employees of the Department of Health and Human Services return information with respect to a taxpayer who has applied to enroll, or reenroll, as a provider of services or supplier under the Medicare program under title XVIII of the Social Security Act. Such return information shall be limited to—

(i) the taxpayer identity information with respect to such taxpayer;

(ii) the amount of the delinquent tax debt owed by that taxpayer; and

(iii) the taxable year to which the delinquent tax debt pertains.

(B) RESTRICTION ON DISCLOSURE.—Return information disclosed under subparagraph (A) may be used by officers and employees of the Department of Health and Human Services for the purposes of, and to the extent necessary in, establishing the taxpayer's eligibility for enrollment or reenrollment in the Medicare program, or in any administrative or judicial proceeding relating to, or arising from, a denial of such enrollment or reenrollment, or in determining the level of enhanced oversight to be applied with respect to such taxpayer pursuant to section 1866(j)(3) of the Social Security Act.

(C) DELINQUENT TAX DEBT.—For purposes of this paragraph, the term “delinquent tax debt” means an out-



standing debt under this title for which a notice of lien has been filed pursuant to section 6323, but the term does not include a debt that is being paid in a timely manner pursuant to an agreement under section 6159 or 7122, or a debt with respect to which a collection due process hearing under section 6330 is requested, pending, or completed and no payment is required.

(m) DISCLOSURE OF TAXPAYER IDENTITY INFORMATION.—

(1) TAX REFUNDS.—The Secretary may disclose taxpayer identity information to the press and other media for purposes of notifying persons entitled to tax refunds when the Secretary, after reasonable effort and lapse of time, has been unable to locate such persons.

(2) FEDERAL CLAIMS.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the Secretary may, upon written request, disclose the mailing address of a taxpayer for use by officers, employees, or agents of a Federal agency for purposes of locating such taxpayer to collect or compromise a Federal claim against the taxpayer in accordance with sections 3711, 3717, and 3718 of title 31.

(B) SPECIAL RULE FOR CONSUMER REPORTING AGENCY.—In the case of an agent of a Federal agency which is a consumer reporting agency (within the meaning of section 603(f) of the Fair Credit Reporting Act (15 U.S.C. 1681a(f))), the mailing address of a taxpayer may be disclosed to such agent under subparagraph (A) only for the purpose of allowing such agent to prepare a commercial credit report on the taxpayer for use by such Federal agency in accordance with sections 3711, 3717, and 3718 of title 31.

(3) NATIONAL INSTITUTE FOR OCCUPATIONAL SAFETY AND HEALTH.—Upon written request, the Secretary may disclose the mailing address of taxpayers to officers and employees of the National Institute for Occupational Safety and Health solely for the purpose of locating individuals who are, or may have been, exposed to occupational hazards in order to determine the status of their health or to inform them of the possible need for medical care and treatment.

(4) INDIVIDUALS WHO OWE AN OVERPAYMENT OF FEDERAL PELL GRANTS OR WHO HAVE DEFAULTED ON STUDENT LOANS ADMINISTERED BY THE DEPARTMENT OF EDUCATION.—

(A) IN GENERAL.—Upon written request by the Secretary of Education, the Secretary may disclose the mailing address of any taxpayer—

(i) who owes an overpayment of a grant awarded to such taxpayer under subpart 1 of part A of title IV of the Higher Education Act of 1965, or

(ii) who has defaulted on a loan—

(I) made under part B, D, or E of title IV of the Higher Education Act of 1965, or

(II) made pursuant to section 3(a)(1) of the Migration and Refugee Assistance Act of 1962 to a student at an institution of higher education,

for use only by officers, employees, or agents of the Department of Education for purposes of locating such taxpayer for purposes of collecting such overpayment or loan.

(B) DISCLOSURE TO EDUCATIONAL INSTITUTIONS, ETC.—Any mailing address disclosed under subparagraph (A)(i) may be disclosed by the Secretary of Education to—

(i) any lender, or any State or nonprofit guarantee agency, which is participating under part B or D of title IV of the Higher Education Act of 1965, or

(ii) any educational institution with which the Secretary of Education has an agreement under subpart 1 of part A, or part D or E, of title IV of such Act,

for use only by officers, employees, or agents of such lender, guarantee agency, or institution whose duties relate to the collection of student loans for purposes of locating individuals who have defaulted on student loans made under such loan programs for purposes of collecting such loans.

(5) INDIVIDUALS WHO HAVE DEFAULTED ON STUDENT LOANS ADMINISTERED BY THE DEPARTMENT OF HEALTH AND HUMAN SERVICES.—

(A) IN GENERAL.—Upon written request by the Secretary of Health and Human Services, the Secretary may disclose the mailing address of any taxpayer who has defaulted on a loan made under part C of title VII of the Public Health Service Act or under subpart II of part B of title VIII of such Act, for use only by officers, employees, or agents of the Department of Health and Human Services for purposes of locating such taxpayer for purposes of collecting such loan.

(B) DISCLOSURE TO SCHOOLS AND ELIGIBLE LENDERS.—Any mailing address disclosed under subparagraph (A) may be disclosed by the Secretary of Health and Human Services to—

(i) any school with which the Secretary of Health and Human Services has an agreement under subpart II of part C of title VII of the Public Health Service Act or subpart II of part B of title VIII of such Act, or

(ii) any eligible lender (within the meaning of section 737(4) of such Act) participating under subpart I of part C of title VII of such Act,

for use only by officers, employees, or agents of such school or eligible lender whose duties relate to the collection of student loans for purposes of locating individuals who have defaulted on student loans made under such subparts for the purposes of collecting such loans.

(6) BLOOD DONOR LOCATOR SERVICE.—

(A) IN GENERAL.—Upon written request pursuant to section 1141 of the Social Security Act, the Secretary shall disclose the mailing address of taxpayers to officers and employees of the Blood Donor Locator Service in the Department of Health and Human Services.

(B) RESTRICTION ON DISCLOSURE.—The Secretary shall disclose return information under subparagraph (A) only for purposes of, and to the extent necessary in, assisting

under the Blood Donor Locator Service authorized persons (as defined in section 1141(h)(1) of the Social Security Act) in locating blood donors who, as indicated by donated blood or products derived therefrom or by the history of the subsequent use of such blood or blood products, have or may have the virus for acquired immune deficiency syndrome, in order to inform such donors of the possible need for medical care and treatment.

(C) SAFEGUARDS.—The Secretary shall destroy all related blood donor records (as defined in section 1141(h)(2) of the Social Security Act) in the possession of the Department of the Treasury upon completion of their use in making the disclosure required under subparagraph (A), so as to make such records undisclosable.

(7) SOCIAL SECURITY ACCOUNT STATEMENT FURNISHED BY SOCIAL SECURITY ADMINISTRATION.—Upon written request by the Commissioner of Social Security, the Secretary may disclose the mailing address of any taxpayer who is entitled to receive a social security account statement pursuant to section 1143(c) of the Social Security Act, for use only by officers, employees or agents of the Social Security Administration for purposes of mailing such statement to such taxpayer.

(n) CERTAIN OTHER PERSONS.—Pursuant to regulations prescribed by the Secretary, returns and return information may be disclosed to any person, including any person described in section 7513(a), to the extent necessary in connection with the processing, storage, transmission, and reproduction of such returns and return information, the programming, maintenance, repair, testing, and procurement of equipment, and the providing of other services, for purposes of tax administration.

(o) DISCLOSURE OF RETURNS AND RETURN INFORMATION WITH RESPECT TO CERTAIN TAXES.—

(1) TAXES IMPOSED BY SUBTITLE E.—

(A) IN GENERAL.—Returns and return information with respect to taxes imposed by subtitle E (relating to taxes on alcohol, tobacco, and firearms) shall be open to inspection by or disclosure to officers and employees of a Federal agency whose official duties require such inspection or disclosure.

(B) USE IN CERTAIN PROCEEDINGS.—Returns and return information disclosed to a Federal agency under subparagraph (A) may be used in an action or proceeding (or in preparation for such action or proceeding) brought under section 625 of the American Jobs Creation Act of 2004 for the collection of any unpaid assessment or penalty arising under such Act.

(2) TAXES IMPOSED BY CHAPTER 35.—Returns and return information with respect to taxes imposed by chapter 35 (relating to taxes on wagering) shall, notwithstanding any other provision of this section, be open to inspection by or disclosure only to such person or persons and for such purpose or purposes as are prescribed by section 4424.

(p) PROCEDURE AND RECORDKEEPING.—

(1) MANNER, TIME, AND PLACE OF INSPECTIONS.—Requests for the inspection or disclosure of a return or return information

and such inspection or disclosure shall be made in such manner and at such time and place as shall be prescribed by the Secretary.

(2) PROCEDURE.—

(A) REPRODUCTION OF RETURNS.—A reproduction or certified reproduction of a return shall, upon written request, be furnished to any person to whom disclosure or inspection of such return is authorized under this section. A reasonable fee may be prescribed for furnishing such reproduction or certified reproduction.

(B) DISCLOSURE OF RETURN INFORMATION.—Return information disclosed to any person under the provisions of this title may be provided in the form of written documents, reproductions of such documents, films or photoimpressions, or electronically produced tapes, disks, or records, or by any other mode or means which the Secretary determines necessary or appropriate. A reasonable fee may be prescribed for furnishing such return information.

(C) USE OF REPRODUCTIONS.—Any reproduction of any return, document, or other matter made in accordance with this paragraph shall have the same legal status as the original, and any such reproduction shall, if properly authenticated, be admissible in evidence in any judicial or administrative proceeding as if it were the original, whether or not the original is in existence.

(3) RECORDS OF INSPECTION AND DISCLOSURE.—

(A) SYSTEM OF RECORDKEEPING.—Except as otherwise provided by this paragraph, the Secretary shall maintain a permanent system of standardized records or accountings of all requests for inspection or disclosure of returns and return information (including the reasons for and dates of such requests) and of returns and return information inspected or disclosed under this section and section 6104(c). Notwithstanding the provisions of section 552a(c) of title 5, United States Code, the Secretary shall not be required to maintain a record or accounting of requests for inspection or disclosure of returns and return information, or of returns and return information inspected or disclosed, under the authority of subsection (c), (e), (f)(5), (h)(1), (3)(A), or (4), (i)(4), or (8)(A)(ii),(k)(1), (2), (6), (8), or (9), (1)(1), (4)(B), (5), (7), (8), (9), (10), (11), (12), (13), (14), (15), (16), (17), or (18), (m), or (n). The records or accountings required to be maintained under this paragraph shall be available for examination by the Joint Committee on Taxation or the Chief of Staff of such joint committee. Such record or accounting shall also be available for examination by such person or persons as may be, but only to the extent, authorized to make such examination under section 552a(c)(3) of title 5, United States Code.

(B) REPORT BY THE SECRETARY.—The Secretary shall, within 90 days after the close of each calendar year, furnish to the Joint Committee on Taxation a report with respect to, or summary of, the records or accountings described in subparagraph (A) in such form and containing such information as such joint committee or the Chief of

Staff of such joint committee may designate. Such report or summary shall not, however, include a record or accounting of any request by the President under subsection (g) for, or the disclosure in response to such request of, any return or return information with respect to any individual who, at the time of such request, was an officer or employee of the executive branch of the Federal Government. Such report or summary, or any part thereof, may be disclosed by such joint committee to such persons and for such purposes as the joint committee may, by record vote of a majority of the members of the joint committee, determine.

(C) PUBLIC REPORT ON DISCLOSURES.—The Secretary shall, within 90 days after the close of each calendar year, furnish to the Joint Committee on Taxation for disclosure to the public a report with respect to the records or accountings described in subparagraph (A) which—

(i) provides with respect to each Federal agency, each agency, body, or commission described in subsection (d), (i)(3)(B)(i) or (7)(A)(ii), or (1)(6), and the Government Accountability Office the number of—

(I) requests for disclosure of returns and return information,

(II) instances in which returns and return information were disclosed pursuant to such requests or otherwise,

(III) taxpayers whose returns, or return information with respect to whom, were disclosed pursuant to such requests, and

(ii) describes the general purposes for which such requests were made.

(4) SAFEGUARDS.—Any Federal agency described in subsection (h)(2), (h)(5), (i)(1), (2), (3), (5), or (7), (j)(1), (2), or (5), (k)(8), (10), or (11), (l)(1), (2), (3), (5), (10), (11), (13), (14), (17), or (22) or (o)(1)(A), the Government Accountability Office, the Congressional Budget Office, or any agency, body, or commission described in subsection (d), (i)(1)(C), (3)(B)(i), or (7)(A)(ii), or (k)(10), (1)(6), (7), (8), (9), (12), (15), or (16), any appropriate State officer (as defined in section 6104(c)), or any other person described in subsection (k)(10), subsection (l)(10), (16), (18), (19), or (20), or any entity described in subsection (l)(21), shall, as a condition for receiving returns or return information—

(A) establish and maintain, to the satisfaction of the Secretary, a permanent system of standardized records with respect to any request, the reason for such request, and the date of such request made by or of it and any disclosure of return or return information made by or to it;

(B) establish and maintain, to the satisfaction of the Secretary, a secure area or place in which such returns or return information shall be stored;

(C) restrict, to the satisfaction of the Secretary, access to the returns or return information only to persons whose duties or responsibilities require access and to whom disclosure may be made under the provisions of this title;

(D) provide such other safeguards which the Secretary determines (and which he prescribes in regulations) to be necessary or appropriate to protect the confidentiality of the returns or return information;

(E) furnish a report to the Secretary, at such time and containing such information as the Secretary may prescribe, which describes the procedures established and utilized by such agency, body, or commission, the Government Accountability Office, or the Congressional Budget Office for ensuring the confidentiality of returns and return information required by this paragraph; and

(F) upon completion of use of such returns or return information—

(i) in the case of an agency, body, or commission described in subsection (d), (i)(3)(B)(i), (k)(10), or (l)(6), (7), (8), (9), or (16), any appropriate State officer (as defined in section 6104(c)), or any other person described in subsection (k)(10) or subsection (l)(10), (16), (18), (19), or (20) return to the Secretary such returns or return information (along with any copies made therefrom) or make such returns or return information undisclosable in any manner and furnish a written report to the Secretary describing such manner,

(ii) in the case of an agency described in subsection (h)(2), (h)(5), (i)(1), (2), (3), (5) or (7), (j)(1), (2), or (5), (k)(8), (10), or (11), (l)(1), (2), (3), (5), (10), (11), (12), (13), (14), (15), (17), or (22), or (o)(1)(A) or any entity described in subsection (l)(21), the Government Accountability Office, or the Congressional Budget Office, either—

(I) return to the Secretary such returns or return information (along with any copies made therefrom),

(II) otherwise make such returns or return information undisclosable, or

(III) to the extent not so returned or made undisclosable, ensure that the conditions of subparagraphs (A), (B), (C), (D), and (E) of this paragraph continue to be met with respect to such returns or return information, and

(iii) in the case of the Department of Health and Human Services for purposes of subsection (m)(6), destroy all such return information upon completion of its use in providing the notification for which the information was obtained, so as to make such information undisclosable;

except that the conditions of subparagraphs (A), (B), (C), (D), and (E) shall cease to apply with respect to any return or return information if, and to the extent that, such return or return information is disclosed in the course of any judicial or administrative proceeding and made a part of the public record thereof. If the Secretary determines that any such agency, body, or commission, including an agency, an appropriate State officer (as defined in section 6104(c)), or any other person described in subsection (k)(10) or subsection (l)(10), (16), (18),

(19), or (20) or any entity described in subsection (l)(21), or the Government Accountability Office or the Congressional Budget Office, has failed to, or does not, meet the requirements of this paragraph, he may, after any proceedings for review established under paragraph (7), take such actions as are necessary to ensure such requirements are met, including refusing to disclose returns or return information to such agency, body, or commission, including an agency, an appropriate State officer (as defined in section 6104(c)), or any other person described in subsection (k)(10) or subsection (l)(10), (16), (18), (19), or (20) or any entity described in subsection (l)(21), or the Government Accountability Office or the Congressional Budget Office, until he determines that such requirements have been or will be met. In the case of any agency which receives any mailing address under paragraph (2), (4), (6), or (7) of subsection (m) and which discloses any such mailing address to any agent or which receives any information under paragraph (6)(A), (10), (12)(B), or (16) of subsection (l) and which discloses any such information to any agent, or any person including an agent described in subsection (l)(10) or (16), this paragraph shall apply to such agency and each such agent or other person (except that, in the case of an agent, or any person including an agent described in subsection (l)(10) or (16), any report to the Secretary or other action with respect to the Secretary shall be made or taken through such agency). For purposes of applying this paragraph in any case to which subsection (m)(6) applies, the term "return information" includes related blood donor records (as defined in section 1141(h)(2) of the Social Security Act).

(5) REPORT ON PROCEDURES AND SAFEGUARDS.—After the close of each calendar year, the Secretary shall furnish to each committee described in subsection (f)(1) a report which describes the procedures and safeguards established and utilized by such agencies, bodies, or commissions, the Government Accountability Office, and the Congressional Budget Office for ensuring the confidentiality of returns and return information as required by this subsection. Such report shall also describe instances of deficiencies in, and failure to establish or utilize, such procedures.

(6) AUDIT OF PROCEDURES AND SAFEGUARDS.—

(A) AUDIT BY COMPTROLLER GENERAL.—The Comptroller General may audit the procedures and safeguards established by such agencies, bodies, or commissions and the Congressional Budget Office pursuant to this subsection to determine whether such safeguards and procedures meet the requirements of this subsection and ensure the confidentiality of returns and return information. The Comptroller General shall notify the Secretary before any such audit is conducted.

(B) RECORDS OF INSPECTION AND REPORTS BY THE COMPTROLLER GENERAL.—The Comptroller General shall—

(i) maintain a permanent system of standardized records and accountings of returns and return information inspected by officers and employees of the Government Accountability Office under subsection

(i)(8)(A)(ii) and shall, within 90 days after the close of each calendar year, furnish to the Secretary a report with respect to, or summary of, such records or accountings in such form and containing such information as the Secretary may prescribe, and

(ii) furnish an annual report to each committee described in subsection (f) and to the Secretary setting forth his findings with respect to any audit conducted pursuant to subparagraph (A).

The Secretary may disclose to the Joint Committee any report furnished to him under clause (i).

(7) ADMINISTRATIVE REVIEW.—The Secretary shall by regulations prescribe procedures which provide for administrative review of any determination under paragraph (4) that any agency, body, or commission described in subsection (d) has failed to meet the requirements of such paragraph.

(8) STATE LAW REQUIREMENTS.—

(A) SAFEGUARDS.—Notwithstanding any other provision of this section, no return or return information shall be disclosed after December 31, 1978, to any officer or employee of any State which requires a taxpayer to attach to, or include in, any State tax return a copy of any portion of his Federal return, or information reflected on such Federal return, unless such State adopts provisions of law which protect the confidentiality of the copy of the Federal return (or portion thereof) attached to, or the Federal return information reflected on, such State tax return.

(B) DISCLOSURE OF RETURNS OR RETURN INFORMATION IN STATE RETURNS.—Nothing in subparagraph (A) shall be construed to prohibit the disclosure by an officer or employee of any State of any copy of any portion of a Federal return or any information on a Federal return which is required to be attached or included in a State return to another officer or employee of such State (or political subdivision of such State) if such disclosure is specifically authorized by State law.

(q) REGULATIONS.—The Secretary is authorized to prescribe such other regulations as are necessary to carry out the provisions of this section.

\* \* \* \* \*

## CHAPTER 63—ASSESSMENT

\* \* \* \* \*

### Subchapter B—Deficiency Procedures in the Case of Income, Estate, Gift, and Certain Excise Taxes

\* \* \* \* \*

#### SEC. 6213. RESTRICTIONS APPLICABLE TO DEFICIENCIES; PETITION TO TAX COURT.

(a) TIME FOR FILING PETITION AND RESTRICTION ON ASSESSMENT.—Within 90 days, or 150 days if the notice is addressed to a person outside the United States, after the notice of deficiency



authorized in section 6212 is mailed (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the last day), the taxpayer may file a petition with the Tax Court for a redetermination of the deficiency. Except as otherwise provided in section 6851, 6852, or 6861 no assessment of a deficiency in respect of any tax imposed by subtitle A, or B, chapter 41, 42, 43, or 44 and no levy or proceeding in court for its collection shall be made, begun, or prosecuted until such notice has been mailed to the taxpayer, nor until the expiration of such 90-day or 150-day period, as the case may be, nor, if a petition has been filed with the Tax Court, until the decision of the Tax Court has become final. Notwithstanding the provisions of section 7421(a), the making of such assessment or the beginning of such proceeding or levy during the time such prohibition is in force may be enjoined by a proceeding in the proper court, including the Tax Court, and a refund may be ordered by such court of any amount collected within the period during which the Secretary is prohibited from collecting by levy or through a proceeding in court under the provisions of this subsection. The Tax Court shall have no jurisdiction to enjoin any action or proceeding or order any refund under this subsection unless a timely petition for a redetermination of the deficiency has been filed and then only in respect of the deficiency that is the subject of such petition. Any petition filed with the Tax Court on or before the last date specified for filing such petition by the Secretary in the notice of deficiency shall be treated as timely filed.

(b) EXCEPTIONS TO RESTRICTIONS ON ASSESSMENT.—

(1) ASSESSMENTS ARISING OUT OF MATHEMATICAL OR CLERICAL ERRORS.—If the taxpayer is notified that, on account of a mathematical or clerical error appearing on the return, an amount of tax in excess of that shown on the return is due, and that an assessment of the tax has been or will be made on the basis of what would have been the correct amount of tax but for the mathematical or clerical error, such notice shall not be considered as a notice of deficiency for the purposes of subsection (a) (prohibiting assessment and collection until notice of the deficiency has been mailed), or of section 6212(c)(1) (restricting further deficiency letters), or of section 6512(a) (prohibiting credits or refunds after petition to the Tax Court), and the taxpayer shall have no right to file a petition with the Tax Court based on such notice, nor shall such assessment or collection be prohibited by the provisions of subsection (a) of this section. Each notice under this paragraph shall set forth the error alleged and an explanation thereof.

(2) ABATEMENT OF ASSESSMENT OF MATHEMATICAL OR CLERICAL ERRORS.—

(A) REQUEST FOR ABATEMENT.—Notwithstanding section 6404(b), a taxpayer may file with the Secretary within 60 days after notice is sent under paragraph (1) a request for an abatement of any assessment specified in such notice, and upon receipt of such request, the Secretary shall abate the assessment. Any reassessment of the tax with respect to which an abatement is made under this subparagraph shall be subject to the deficiency procedures prescribed by this subchapter.

(B) STAY OF COLLECTION.—In the case of any assessment referred to in paragraph (1), notwithstanding paragraph (1), no levy or proceeding in court for the collection of such assessment shall be made, begun, or prosecuted during the period in which such assessment may be abated under this paragraph.

(3) ASSESSMENTS ARISING OUT OF TENTATIVE CARRYBACK OR REFUND ADJUSTMENTS.—If the Secretary determines that the amount applied, credited, or refunded under section 6411 is in excess of the overassessment attributable to the carryback or the amount described in section 1341(b)(1) with respect to which such amount was applied, credited, or refunded, he may assess without regard to the provisions of paragraph (2) the amount of the excess as a deficiency as if it were due to a mathematical or clerical error appearing on the return.

(4) ASSESSMENT OF AMOUNT PAID.—Any amount paid as a tax or in respect of a tax may be assessed upon the receipt of such payment notwithstanding the provisions of subsection (a). In any case where such amount is paid after the mailing of a notice of deficiency under section 6212, such payment shall not deprive the Tax Court of jurisdiction over such deficiency determined under section 6211 without regard to such assessment.

(5) CERTAIN ORDERS OF CRIMINAL RESTITUTION.—If the taxpayer is notified that an assessment has been or will be made pursuant to section 6201(a)(4)—

(A) such notice shall not be considered as a notice of deficiency for the purposes of subsection (a) (prohibiting assessment and collection until notice of the deficiency has been mailed), section 6212(c)(1) (restricting further deficiency letters), or section 6512(a) (prohibiting credits or refunds after petition to the Tax Court), and

(B) subsection (a) shall not apply with respect to the amount of such assessment.

(c) FAILURE TO FILE PETITION.—If the taxpayer does not file a petition with the Tax Court within the time prescribed in subsection (a), the deficiency, notice of which has been mailed to the taxpayer, shall be assessed, and shall be paid upon notice and demand from the Secretary.

(d) WAIVER OF RESTRICTIONS.—The taxpayer shall at any time (whether or not a notice of deficiency has been issued) have the right, by a signed notice in writing filed with the Secretary, to waive the restrictions provided in subsection (a) on the assessment and collection of the whole or any part of the deficiency.

(e) SUSPENSION OF FILING PERIOD FOR CERTAIN EXCISE TAXES.—The running of the time prescribed by subsection (a) for filing a petition in the Tax Court with respect to the taxes imposed by section 4941 (relating to taxes on self-dealing), 4942 (relating to taxes on failure to distribute income), 4943 (relating to taxes on excess business holdings), 4944 (relating to investments which jeopardize charitable purpose), 4945 (relating to taxes on taxable expenditures), 4951 (relating to taxes on self-dealing), or 4952 (relating to taxes on taxable expenditures), 4955 (relating to taxes on political expenditures), 4958 (relating to private excess benefit), 4971 (relating to excise taxes on failure to meet minimum funding standard),

4975 (relating to excise taxes on prohibited transactions) shall be suspended for any period during which the Secretary has extended the time allowed for making correction under section 4963(e).

(f) COORDINATION WITH TITLE 11.—

(1) SUSPENSION OF RUNNING OF PERIOD FOR FILING PETITION IN TITLE 11 CASES.—In any case under title 11 of the United States Code, the running of the time prescribed by subsection (a) for filing a petition in the Tax Court with respect to any deficiency shall be suspended for the period during which the debtor is prohibited by reason of such case from filing a petition in the Tax Court with respect to such deficiency, and for 60 days thereafter.

(2) CERTAIN ACTION NOT TAKEN INTO ACCOUNT.—For purposes of the second and third sentences of subsection (a), the filing of a proof of claim or request for payment (or the taking of any other action) in a case under title 11 of the United States Code shall not be treated as action prohibited by such second sentence.

(g) DEFINITIONS.—For purposes of this section—

(1) RETURN.—The term “return” includes any return, statement, schedule, or list, and any amendment or supplement thereto, filed with respect to any tax imposed by subtitle A or B, or chapter 41, 42, 43, or 44.

(2) MATHEMATICAL OR CLERICAL ERROR.—The term “mathematical or clerical error” means—

(A) an error in addition, subtraction, multiplication, or division shown on any return,

(B) an incorrect use of any table provided by the Internal Revenue Service with respect to any return if such incorrect use is apparent from the existence of other information on the return,

(C) an entry on a return of an item which is inconsistent with another entry of the same or another item on such return,

(D) an omission of information which is required to be supplied on the return to substantiate an entry on the return,

(E) an entry on a return of a deduction or credit in an amount which exceeds a statutory limit imposed by subtitle A or B, or chapter 41, 42, 43, or 44, if such limit is expressed—

(i) as a specified monetary amount, or

(ii) as a percentage, ratio, or fraction, and if the items entering into the application of such limit appear on such return,

(F) an omission of a correct taxpayer identification number required under section 32 (relating to the earned income credit) to be included on a return,

(G) an entry on a return claiming the credit under section 32 with respect to net earnings from self-employment described in section 32(c)(2)(A) to the extent the tax imposed by section 1401 (relating to self-employment tax) on such net earnings has not been paid,

(H) an omission of a correct TIN required under [section 21 (relating to expenses for household and dependent care

services necessary for gainful employment) or section 151 (relating to allowance of deductions for personal exemptions)] subsection (a)(1)(B), (b)(1)(A)(ii), or (b)(1)(B) of section 2 or section 21, 35(d)(1)(B), 36B(b)(3)(B), or 63(f)(2)(B),

(I) an omission of a correct TIN required under section 24(e) (relating to child tax credit) to be included on a return,

(J) an omission of a correct TIN required under section 5A(g)(1) (relating to higher education tuition and related expenses) to be included on a return,

(K) an omission of information required by section 32(k)(2) (relating to taxpayers making improper prior claims of earned income credit) or an entry on the return claiming the credit under section 32 for a taxable year for which the credit is disallowed under subsection (k)(1) thereof,

(L) the inclusion on a return of a TIN required to be included on the return under section 21, 24, or 32 if—

(i) such TIN is of an individual whose age affects the amount of the credit under such section, and

(ii) the computation of the credit on the return reflects the treatment of such individual as being of an age different from the individual's age based on such TIN,

(M) the entry on the return claiming the credit under section 32 with respect to a child if, according to the Federal Case Registry of Child Support Orders established under section 453(h) of the Social Security Act, the taxpayer is a noncustodial parent of such child,

(N) an omission of any increase required under section 36(f) with respect to the recapture of a credit allowed under section 36;

(O) the inclusion on a return of an individual taxpayer identification number issued under section 6109(i) which has expired, been revoked by the Secretary, or is otherwise invalid,

(P) an omission of information required by section 24(g)(2) or an entry on the return claiming the credit under section 24 for a taxable year for which the credit is disallowed under subsection (g)(1) thereof, and

(Q) an omission of information required by section 25A(b)(4)(B) or an entry on the return claiming the American Opportunity Tax Credit for a taxable year for which such credit is disallowed under section 25A(b)(4)(A).

A taxpayer shall be treated as having omitted a correct TIN for purposes of the preceding sentence if information provided by the taxpayer on the return with respect to the individual whose TIN was provided differs from the information the Secretary obtains from the person issuing the TIN.

(h) CROSS REFERENCES.—

(1) For assessment as if a mathematical error on the return, in the case of erroneous claims for income tax prepayment credits, see section 6201(a)(3).

(2) For assessments without regard to restrictions imposed by this section in the case of—

- (A) Recovery of foreign income taxes, see section 905(c).
- (B) Recovery of foreign estate tax, see section 2016.
- (3) For provisions relating to application of this subchapter in the case of certain partnership items, etc., see section 6230(a).

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**CHAPTER 64—COLLECTION**

\* \* \* \* \*

**Subchapter D—Seizure of Property for Collection of Taxes**

\* \* \* \* \*

**PART II—LEVY**

\* \* \* \* \*

**SEC. 6334. PROPERTY EXEMPT FROM LEVY.**

- (a) **ENUMERATION.**—There shall be exempt from levy—
  - (1) **WEARING APPAREL AND SCHOOL BOOKS.**—Such items of wearing apparel and such school books as are necessary for the taxpayer or for members of his family;
  - (2) **FUEL, PROVISIONS, FURNITURE, AND PERSONAL EFFECTS.**—So much of the fuel, provisions, furniture, and personal effects in the taxpayer’s household, and of the arms for personal use, livestock, and poultry of the taxpayer, as does not exceed \$6,250 in value;
  - (3) **BOOKS AND TOOLS OF A TRADE, BUSINESS, OR PROFESSION.**—So many of the books and tools necessary for the trade, business, or profession of the taxpayer as do not exceed in the aggregate \$3,125 in value.
  - (4) **UNEMPLOYMENT BENEFITS.**—Any amount payable to an individual with respect to his unemployment (including any portion thereof payable with respect to dependents) under an unemployment compensation law of the United States, of any State, or of the District of Columbia or of the Commonwealth of Puerto Rico.
  - (5) **UNDELIVERED MAIL.**—Mail, addressed to any person, which has not been delivered to the addressee.
  - (6) **CERTAIN ANNUITY AND PENSION PAYMENTS.**—Annuity or pension payments under the Railroad Retirement Act, benefits under the Railroad Unemployment Insurance Act, special pension payments received by a person whose name has been entered on the Army, Navy, Air Force, and Coast Guard Medal of Honor roll (38 U.S.C. 1562), and annuities based on retired or retainer pay under chapter 73 of title 10 of the United States Code.
  - (7) **WORKMEN’S COMPENSATION.**—Any amount payable to an individual as workmen’s compensation (including any portion thereof payable with respect to dependents) under a workmen’s compensation law of the United States, any State, the District of Columbia, or the Commonwealth of Puerto Rico.

(8) JUDGMENTS FOR SUPPORT OF MINOR CHILDREN.—If the taxpayer is required by judgment of a court of competent jurisdiction, entered prior to the date of levy, to contribute to the support of his minor children, so much of his salary, wages, or other income as is necessary to comply with such judgment.

(9) MINIMUM EXEMPTION FOR WAGES, SALARY, AND OTHER INCOME.—Any amount payable to or received by an individual as wages or salary for personal services, or as income derived from other sources, during any period, to the extent that the total of such amounts payable to or received by him during such period does not exceed the applicable exempt amount determined under subsection (d).

(10) CERTAIN SERVICE-CONNECTED DISABILITY PAYMENTS.—Any amount payable to an individual as a service-connected (within the meaning of section 101(16) of title 38, United States Code) disability benefit under—

(A) subchapter II, III, IV, V, or VI of chapter 11 of such title 38, or

(B) chapter 13, 21, 23, 31, 32, 34, 35, 37, or 39 of such title 38.

(11) CERTAIN PUBLIC ASSISTANCE PAYMENTS.—Any amount payable to an individual as a recipient of public assistance under—

(A) title IV or title XVI (relating to supplemental security income for the aged, blind, and disabled) of the Social Security Act, or

(B) State or local government public assistance or public welfare programs for which eligibility is determined by a needs or income test.

(12) ASSISTANCE UNDER JOB TRAINING PARTNERSHIP ACT.—Any amount payable to a participant under the Job Training Partnership Act (29 U.S.C. 1501 et seq.) from funds appropriated pursuant to such Act.

(13) RESIDENCES EXEMPT IN SMALL DEFICIENCY CASES AND PRINCIPAL RESIDENCES AND CERTAIN BUSINESS ASSETS EXEMPT IN ABSENCE OF CERTAIN APPROVAL OR JEOPARDY.—

(A) RESIDENCES IN SMALL DEFICIENCY CASES.—If the amount of the levy does not exceed \$5,000—

(i) any real property used as a residence by the taxpayer; or

(ii) any real property of the taxpayer (other than real property which is rented) used by any other individual as a residence.

(B) PRINCIPAL RESIDENCES AND CERTAIN BUSINESS ASSETS.—Except to the extent provided in subsection (e)—

(i) the principal residence of the taxpayer (within the meaning of section 121); and

(ii) tangible personal property or real property (other than real property which is rented) used in the trade or business of an individual taxpayer.

(b) APPRAISAL.—The officer seizing property of the type described in subsection (a) shall appraise and set aside to the owner the amount of such property declared to be exempt. If the taxpayer objects at the time of the seizure to the valuation fixed by the officer

making the seizure, the Secretary shall summon three disinterested individuals who shall make the valuation.

(c) **NO OTHER PROPERTY EXEMPT.**—Notwithstanding any other law of the United States (including section 207 of the Social Security Act), no property or rights to property shall be exempt from levy other than the property specifically made exempt by subsection (a).

(d) **EXEMPT AMOUNT OF WAGES, SALARY, OR OTHER INCOME.**—

(1) **INDIVIDUALS ON WEEKLY BASIS.**—In the case of an individual who is paid or receives all of his wages, salary, and other income on a weekly basis, the amount of the wages, salary, and other income payable to or received by him during any week which is exempt from levy under subsection (a)(9) shall be the exempt amount.

[(2) **EXEMPT AMOUNT.**—For purposes of paragraph (1), the term “exempt amount” means an amount equal to—

[(A) the sum of—

[(i) the standard deduction, and

[(ii) the aggregate amount of the deductions for personal exemptions allowed the taxpayer under section 151 in the taxable year in which such levy occurs, divided by (B) 52.

Unless the taxpayer submits to the Secretary a written and properly verified statement specifying the facts necessary to determine the proper amount under subparagraph (A), subparagraph (A) shall be applied as if the taxpayer were a married individual filing a separate return with only 1 personal exemption.]

(2) **EXEMPT AMOUNT.**—

(A) **IN GENERAL.**—For purposes of paragraph (1), the term “exempt amount” means an amount equal to—

(i) the sum of the amount determined under subparagraph (B) and the standard deduction, divided by

(ii) 52.

(B) **AMOUNT DETERMINED.**—For purposes of subparagraph (A), the amount determined under this subparagraph is—

(i) the dollar amount in effect under section 7706(d)(1)(B), multiplied by

(ii) the number of the taxpayer’s dependents for the taxable year in which the levy occurs.

(C) **VERIFIED STATEMENT.**—Unless the taxpayer submits to the Secretary a written and properly verified statement specifying the facts necessary to determine the proper amount under subparagraph (A), subparagraph (A) shall be applied as if the taxpayer were a married individual filing a separate return with no dependents.

(3) **INDIVIDUALS ON BASIS OTHER THAN WEEKLY.**—In the case of any individual not described in paragraph (1), the amount of the wages, salary, and other income payable to or received by him during any applicable pay period or other fiscal period (as determined under regulations prescribed by the Secretary) which is exempt from levy under subsection (a)(9) shall be an amount (determined under such regulations) which as nearly as possible will result in the same total exemption from levy

for such individual over a period of time as he would have under paragraph (1) if (during such period of time) he were paid or received such wages, salary, and other income on a regular weekly basis.

**[(4) YEARS WHEN PERSONAL EXEMPTION AMOUNT IS ZERO.—**

**[(A) IN GENERAL.—**In the case of any taxable year in which the exemption amount under section 151(d) is zero, paragraph (2) shall not apply and for purposes of paragraph (1) the term “exempt amount” means an amount equal to—

**[(i)** the sum of the amount determined under subparagraph (B) and the standard deduction, divided by

**[(ii)** 52.

**[(B) AMOUNT DETERMINED.—**For purposes of subparagraph (A), the amount determined under this subparagraph is \$4,150 multiplied by the number of the taxpayer’s dependents for the taxable year in which the levy occurs.

**[(C) INFLATION ADJUSTMENT.—**In the case of any taxable year beginning in a calendar year after 2018, the \$4,150 amount in subparagraph (B) shall be increased by an amount equal to—

**[(i)** such dollar amount, multiplied by

**[(ii)** the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, determined by substituting “2017” for “2016” in subparagraph (A)(ii) thereof.

If any increase determined under the preceding sentence is not a multiple of \$100, such increase shall be rounded to the next lowest multiple of \$100.

**[(D) VERIFIED STATEMENT.—**Unless the taxpayer submits to the Secretary a written and properly verified statement specifying the facts necessary to determine the proper amount under subparagraph (A), subparagraph (A) shall be applied as if the taxpayer were a married individual filing a separate return with no dependents.]

**(e) LEVY ALLOWED ON PRINCIPAL RESIDENCES AND CERTAIN BUSINESS ASSETS IN CERTAIN CIRCUMSTANCES.—**

**(1) PRINCIPAL RESIDENCES.—**

**(A) APPROVAL REQUIRED.—**A principal residence shall not be exempt from levy if a judge or magistrate of a district court of the United States approves (in writing) the levy of such residence.

**(B) JURISDICTION.—**The district courts of the United States shall have exclusive jurisdiction to approve a levy under subparagraph (A).

**(2) CERTAIN BUSINESS ASSETS.—**Property (other than a principal residence) described in subsection (a)(13)(B) shall not be exempt from levy if—

**(A)** a district director or assistant district director of the Internal Revenue Service personally approves (in writing) the levy of such property; or

**(B)** the Secretary finds that the collection of tax is in jeopardy.

An official may not approve a levy under subparagraph (A) unless the official determines that the taxpayer’s other assets



subject to collection are insufficient to pay the amount due, together with expenses of the proceedings.

(f) LEVY ALLOWED ON CERTAIN SPECIFIED PAYMENTS.—Any payment described in subparagraph (B) or (C) of section 6331(h)(2) shall not be exempt from levy if the Secretary approves the levy thereon under section 6331(h).

(g) INFLATION ADJUSTMENT.—

(1) IN GENERAL.—In the case of any calendar year beginning after 1999, each dollar amount referred to in paragraphs (2) and (3) of subsection (a) shall be increased by an amount equal to—

(A) such dollar amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for such calendar year, by substituting “calendar year 1998” for “calendar year 2016” in subparagraph (A)(ii) thereof.

(2) ROUNDING.—If any dollar amount after being increased under paragraph (1) is not a multiple of \$10, such dollar amount shall be rounded to the nearest multiple of \$10.

\* \* \* \* \*

**CHAPTER 68—ADDITIONS TO THE TAX, ADDITIONAL AMOUNTS, AND ASSESSABLE PENALTIES**

\* \* \* \* \*

**Subchapter A—Additions to the Tax and Additional Amounts**

\* \* \* \* \*

**PART I—GENERAL PROVISIONS**

\* \* \* \* \*

**SEC. 6654. FAILURE BY INDIVIDUAL TO PAY ESTIMATED INCOME TAX.**

(a) ADDITION TO THE TAX.—Except as otherwise provided in this section, in the case of any underpayment of estimated tax by an individual, there shall be added to the tax under chapter 1, the tax under chapter 2, and the tax under chapter 2A for the taxable year an amount determined by applying—

- (1) the underpayment rate established under section 6621,
- (2) to the amount of the underpayment,
- (3) for the period of the underpayment.

(b) AMOUNT OF UNDERPAYMENT; PERIOD OF UNDERPAYMENT.—For purposes of subsection (a)—

(1) AMOUNT.—The amount of the underpayment shall be the excess of—

- (A) the required installment, over
- (B) the amount (if any) of the installment paid on or before the due date for the installment.

(2) PERIOD OF UNDERPAYMENT.—The period of the underpayment shall run from the due date for the installment to whichever of the following dates is the earlier—

- (A) the 15th day of the 4th month following the close of the taxable year, or
- (B) with respect to any portion of the underpayment, the date on which such portion is paid.
- (3) ORDER OF CREDITING PAYMENTS.—For purposes of paragraph (2)(B), a payment of estimated tax shall be credited against unpaid required installments in the order in which such installments are required to be paid.
- (c) NUMBER OF REQUIRED INSTALLMENTS; DUE DATES.—For purposes of this section—
- (1) PAYABLE IN 4 INSTALLMENTS.—There shall be 4 required installments for each taxable year.
- (2) Time for payment of installments

| In the case of the following required installments: | The due date is:                          |
|---|---|
| 1st   | April 15                                  |
| 2nd   | June 15                                   |
| 3rd   | September 15                              |
| 4th   | January 15 of the following taxable year. |

- (d) AMOUNT OF REQUIRED INSTALLMENTS.—For purposes of this section—
- (1) AMOUNT.—
- (A) IN GENERAL.—Except as provided in paragraph (2), the amount of any required installment shall be 25 percent of the required annual payment.
- (B) REQUIRED ANNUAL PAYMENT.—For purposes of subparagraph (A), the term “required annual payment” means the lesser of—
- (i) 90 percent of the tax shown on the return for the taxable year (or, if no return is filed, 90 percent of the tax for such year), or
- (ii) 100 percent of the tax shown on the return of the individual for the preceding taxable year.
- Clause (ii) shall not apply if the preceding taxable year was not a taxable year of 12 months or if the individual did not file a return for such preceding taxable year.
- (C) LIMITATION ON USE OF PRECEDING YEAR’S TAX.—
- (i) IN GENERAL.—If the adjusted gross income shown on the return of the individual for the preceding taxable year beginning in any calendar year exceeds \$150,000, clause (ii) of subparagraph (B) shall be applied by substituting “110 percent” for “100 percent”.
- (ii) SEPARATE RETURNS.—In the case of a married individual (within the meaning of section 7703) who files a separate return for the taxable year for which the amount of the installment is being determined, clause (i) shall be applied by substituting “\$75,000” for “\$150,000”.
- [(iii) SPECIAL RULE.—In the case of an estate or trust, adjusted gross income shall be determined as provided in section 67(e).]
- (2) Lower required installment where annualized income installment is less than amount determined under paragraph (1)

(A) **IN GENERAL.**—In the case of any required installment, if the individual establishes that the annualized income installment is less than the amount determined under paragraph (1)—

(i) the amount of such required installment shall be the annualized income installment, and

(ii) any reduction in a required installment resulting from the application of this subparagraph shall be recaptured by increasing the amount of the next required installment determined under paragraph (1) by the amount of such reduction (and by increasing subsequent required installments to the extent that the reduction has not previously been recaptured under this clause).

(B) **DETERMINATION OF ANNUALIZED INCOME INSTALLMENT.**—In the case of any required installment, the annualized income installment is the excess (if any) of—

(i) an amount equal to the applicable percentage of the tax for the taxable year computed by placing on an annualized basis the taxable income, alternative minimum taxable income, and adjusted self-employment income for months in the taxable year ending before the due date for the installment, over

(ii) the aggregate amount of any prior required installments for the taxable year.

(C) **SPECIAL RULES.**—For purposes of this paragraph—

(i) **ANNUALIZATION.**—The taxable income, alternative minimum taxable income, and adjusted self-employment income shall be placed on an annualized basis under regulations prescribed by the Secretary.

(ii) **APPLICABLE PERCENTAGE.**—

| In the case of the following required installments: | The applicable percentage is: |
|---|-------------------------------|
| 1st   | 22.5                          |
| 2nd   | 45                            |
| 3rd   | 67.5                          |
| 4th   | 90.                           |

(iii) **ADJUSTED SELF-EMPLOYMENT INCOME.**—The term “adjusted self-employment income” means self-employment income (as defined in section 1402(b)); except that section 1402(b) shall be applied by placing wages (within the meaning of section 1402(b)) for months in the taxable year ending before the due date for the installment on an annualized basis consistent with clause (i).

(D) **TREATMENT OF SUBPART F INCOME.**—

(i) **IN GENERAL.**—Any amounts required to be included in gross income under section 951(a) (and credits properly allocable thereto) shall be taken into account in computing any annualized income installment under subparagraph (B) in a manner similar to the manner under which partnership income inclusions

(and credits properly allocable thereto) are taken into account.

(ii) PRIOR YEAR SAFE HARBOR.—If a taxpayer elects to have this clause apply to any taxable year—

(I) clause (i) shall not apply, and

(II) for purposes of computing any annualized income installment for such taxable year, the taxpayer shall be treated as having received ratably during such taxable year items of income and credit described in clause (i) in an amount equal to the amount of such items shown on the return of the taxpayer for the preceding taxable year (the second preceding taxable year in the case of the first and second required installments for such taxable year).

(e) EXCEPTIONS.—

(1) WHERE TAX IS SMALL AMOUNT.—No addition to tax shall be imposed under subsection (a) for any taxable year if the tax shown on the return for such taxable year (or, if no return is filed, the tax), reduced by the credit allowable under section 31, is less than \$1,000.

(2) WHERE NO TAX LIABILITY FOR PRECEDING TAXABLE YEAR.—No addition to tax shall be imposed under subsection (a) for any taxable year if—

(A) the preceding taxable year was a taxable year of 12 months,

(B) the individual did not have any liability for tax for the preceding taxable year, and

(C) the individual was a citizen or resident of the United States throughout the preceding taxable year.

(3) WAIVER IN CERTAIN CASES.—

(A) IN GENERAL.—No addition to tax shall be imposed under subsection (a) with respect to any underpayment to the extent the Secretary determines that by reason of casualty, disaster, or other unusual circumstances the imposition of such addition to tax would be against equity and good conscience.

(B) NEWLY RETIRED OR DISABLED INDIVIDUALS.—No addition to tax shall be imposed under subsection (a) with respect to any underpayment if the Secretary determines that—

(i) the taxpayer—

(I) retired after having attained age 62, or

(II) became disabled,

in the taxable year for which estimated payments were required to be made or in the taxable year preceding such taxable year, and

(ii) such underpayment was due to reasonable cause and not to willful neglect.

(f) TAX COMPUTED AFTER APPLICATION OF CREDITS AGAINST TAX.—For purposes of this section, the term “tax” means—

(1) the tax imposed by chapter 1 (other than any increase in such tax by reason of section 143(m)), plus

(2) the tax imposed by chapter 2, plus

(3) the tax imposed by chapter 2A, minus

## (g) APPLICATION OF SECTION IN CASE OF TAX WITHHELD ON WAGES.—

(1) IN GENERAL.—For purposes of applying this section, the amount of the credit allowed under section 31 for the taxable year shall be deemed a payment of estimated tax, and an equal part of such amount shall be deemed paid on each due date for such taxable year, unless the taxpayer establishes the dates on which all amounts were actually withheld, in which case the amounts so withheld shall be deemed payments of estimated tax on the dates on which such amounts were actually withheld.

(2) SEPARATE APPLICATION.—The taxpayer may apply paragraph (1) separately with respect to—

(A) wage withholding, and

(B) all other amounts withheld for which credit is allowed under section 31.

(h) SPECIAL RULE WHERE RETURN FILED ON OR BEFORE JANUARY 31.—If, on or before January 31 of the following taxable year, the taxpayer files a return for the taxable year and pays in full the amount computed on the return as payable, then no addition to tax shall be imposed under subsection (a) with respect to any underpayment of the 4th required installment for the taxable year.

(i) SPECIAL RULES FOR FARMERS AND FISHERMEN.—For purposes of this section—

(1) IN GENERAL.—If an individual is a farmer or fisherman for any taxable year—

(A) there shall be only 1 required installment for the taxable year,

(B) the due date for such installment shall be January 15 of the following taxable year,

(C) the amount of such installment shall be equal to the required annual payment determined under subsection (d)(1)(B) by substituting “66 2/3 percent” for “90 percent” and without regard to subparagraph (C) of subsection (d)(1), and

(D) subsection (h) shall be applied—

(i) by substituting “March 1” for “January 31”, and

(ii) by treating the required installment described in subparagraph (A) of this paragraph as the 4th required installment.

(2) FARMER OR FISHERMAN DEFINED.—An individual is a farmer or fisherman for any taxable year if—

(A) the individual’s gross income from farming or fishing (including oyster farming) for the taxable year is at least 66 2/3 percent of the total gross income from all sources for the taxable year, or

(B) such individual’s gross income from farming or fishing (including oyster farming) shown on the return of the individual for the preceding taxable year is at least 66 2/3 percent of the total gross income from all sources shown on such return.

(j) SPECIAL RULES FOR NONRESIDENT ALIENS.—In the case of a nonresident alien described in section 6072(c):

(1) PAYABLE IN 3 INSTALLMENTS.—There shall be 3 required installments for the taxable year.

(2) **TIME FOR PAYMENT OF INSTALLMENTS.**—The due dates for required installments under this subsection shall be determined under the following table:

| In the case of the following required installments: | The due date is:                          |
|---|---|
| 1st   | June 15                                   |
| 2nd   | September 15                              |
| 3rd   | January 15 of the following taxable year. |

(3) **AMOUNT OF REQUIRED INSTALLMENTS.**—

(A) **FIRST REQUIRED INSTALLMENT.**—In the case of the first required installment, subsection (d) shall be applied by substituting “50 percent” for “25 percent” in subsection (d)(1)(A).

(B) **DETERMINATION OF APPLICABLE PERCENTAGE.**—The applicable percentage for purposes of subsection (d)(2) shall be determined under the following table:

| In the case of the following required installments: | The applicable percentage is: |
|---|-------------------------------|
| 1st   | 45                            |
| 2nd   | 67.5                          |
| 3rd   | 90.                           |

(k) **FISCAL YEARS AND SHORT YEARS.**—

(1) **FISCAL YEARS.**—In applying this section to a taxable year beginning on any date other than January 1, there shall be substituted, for the months specified in this section, the months which correspond thereto.

(2) **SHORT TAXABLE YEAR.**—This section shall be applied to taxable years of less than 12 months in accordance with regulations prescribed by the Secretary.

(l) **ESTATES AND TRUSTS.**—

(1) **IN GENERAL.**—Except as otherwise provided in this subsection, this section shall apply to any estate or trust.

(2) **EXCEPTION FOR ESTATES AND CERTAIN TRUSTS.**—With respect to any taxable year ending before the date 2 years after the date of the decedent’s death, this section shall not apply to—

(A) the estate of such decedent, or

(B) any trust—

(i) all of which was treated (under subpart E of part I of subchapter J of chapter 1) as owned by the decedent, and

(ii) to which the residue of the decedent’s estate will pass under his will (or, if no will is admitted to probate, which is the trust primarily responsible for paying debts, taxes, and expenses of administration).

(3) **EXCEPTION FOR CHARITABLE TRUSTS AND PRIVATE FOUNDATIONS.**—This section shall not apply to any trust which is subject to the tax imposed by section 511 or which is a private foundation.

(4) SPECIAL RULE FOR ANNUALIZATIONS.—In the case of any estate or trust to which this section applies, subsection (d)(2)(B)(i) shall be applied by substituting “ending before the date 1 month before the due date for the installment” for “ending before the due date for the installment”.

(m) SPECIAL RULE FOR MEDICARE TAX.—For purposes of this section, the tax imposed under section 3101(b)(2) (to the extent not withheld) shall be treated as a tax imposed under chapter 2.

(n) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this section.

\* \* \* \* \*

## CHAPTER 79—DEFINITIONS

Sec. 7701. Definitions.

\* \* \* \* \*

Sec. 7706. *Dependent defined.*

\* \* \* \* \*

### SEC. 7702B. TREATMENT OF QUALIFIED LONG-TERM CARE INSURANCE.

(a) IN GENERAL.—For purposes of this title—

(1) a qualified long-term care insurance contract shall be treated as an accident and health insurance contract,

(2) amounts (other than policyholder dividends, as defined in section 808, or premium refunds) received under a qualified long-term care insurance contract shall be treated as amounts received for personal injuries and sickness and shall be treated as reimbursement for expenses actually incurred for medical care (as defined in section 213(d)),

(3) any plan of an employer providing coverage under a qualified long-term care insurance contract shall be treated as an accident and health plan with respect to such coverage,

(4) except as provided in subsection (e)(3), amounts paid for a qualified long-term care insurance contract providing the benefits described in subsection (b)(2)(A) shall be treated as payments made for insurance for purposes of section 213(d)(1)(D), and

(5) a qualified long-term care insurance contract shall be treated as a guaranteed renewable contract subject to the rules of section 816(e).

(b) QUALIFIED LONG-TERM CARE INSURANCE CONTRACT.—For purposes of this title—

(1) IN GENERAL.—The term “qualified long-term care insurance contract” means any insurance contract if—

(A) the only insurance protection provided under such contract is coverage of qualified long-term care services,

(B) such contract does not pay or reimburse expenses incurred for services or items to the extent that such expenses are reimbursable under title XVIII of the Social Security Act or would be so reimbursable but for the application of a deductible or coinsurance amount,

(C) such contract is guaranteed renewable,

(D) such contract does not provide for a cash surrender value or other money that can be—

- (i) paid, assigned, or pledged as collateral for a loan, or
- (ii) borrowed, other than as provided in subparagraph (E) or paragraph (2)(C),

(E) all refunds of premiums, and all policyholder dividends or similar amounts, under such contract are to be applied as a reduction in future premiums or to increase future benefits, and

(F) such contract meets the requirements of subsection (g).

(2) SPECIAL RULES.—

(A) PER DIEM, ETC. PAYMENTS PERMITTED.—A contract shall not fail to be described in subparagraph (A) or (B) of paragraph (1) by reason of payments being made on a per diem or other periodic basis without regard to the expenses incurred during the period to which the payments relate.

(B) SPECIAL RULES RELATING TO MEDICARE.—

(i) Paragraph (1)(B) shall not apply to expenses which are reimbursable under title XVIII of the Social Security Act only as a secondary payor.

(ii) No provision of law shall be construed or applied so as to prohibit the offering of a qualified long-term care insurance contract on the basis that the contract coordinates its benefits with those provided under such title.

(C) REFUNDS OF PREMIUMS.—Paragraph (1)(E) shall not apply to any refund on the death of the insured, or on a complete surrender or cancellation of the contract, which cannot exceed the aggregate premiums paid under the contract. Any refund on a complete surrender or cancellation of the contract shall be includible in gross income to the extent that any deduction or exclusion was allowable with respect to the premiums.

(c) QUALIFIED LONG-TERM CARE SERVICES.—For purposes of this section—

(1) IN GENERAL.—The term “qualified long-term care services” means necessary diagnostic, preventive, therapeutic, curing, treating, mitigating, and rehabilitative services, and maintenance or personal care services, which—

(A) are required by a chronically ill individual, and

(B) are provided pursuant to a plan of care prescribed by a licensed health care practitioner.

(2) CHRONICALLY ILL INDIVIDUAL.—

(A) IN GENERAL.—The term “chronically ill individual” means any individual who has been certified by a licensed health care practitioner as—

(i) being unable to perform (without substantial assistance from another individual) at least 2 activities of daily living for a period of at least 90 days due to a loss of functional capacity,

(ii) having a level of disability similar (as determined under regulations prescribed by the Secretary



in consultation with the Secretary of Health and Human Services) to the level of disability described in clause (i), or

(iii) requiring substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment.

Such term shall not include any individual otherwise meeting the requirements of the preceding sentence unless within the preceding 12-month period a licensed health care practitioner has certified that such individual meets such requirements.

(B) ACTIVITIES OF DAILY LIVING.—For purposes of subparagraph (A), each of the following is an activity of daily living:

- (i) Eating.
- (ii) Toileting.
- (iii) Transferring.
- (iv) Bathing.
- (v) Dressing.
- (vi) Continence.

A contract shall not be treated as a qualified long-term care insurance contract unless the determination of whether an individual is a chronically ill individual described in subparagraph (A)(i) takes into account at least 5 of such activities.

(3) MAINTENANCE OR PERSONAL CARE SERVICES.—The term “maintenance or personal care services” means any care the primary purpose of which is the provision of needed assistance with any of the disabilities as a result of which the individual is a chronically ill individual (including the protection from threats to health and safety due to severe cognitive impairment).

(4) LICENSED HEALTH CARE PRACTITIONER.—The term “licensed health care practitioner” means any physician (as defined in section 1861(r)(1) of the Social Security Act) and any registered professional nurse, licensed social worker, or other individual who meets such requirements as may be prescribed by the Secretary.

(d) AGGREGATE PAYMENTS IN EXCESS OF LIMITS.—

(1) IN GENERAL.—If the aggregate of—

(A) the periodic payments received for any period under all qualified long-term care insurance contracts which are treated as made for qualified long-term care services for an insured, and

(B) the periodic payments received for such period which are treated under section 101(g) as paid by reason of the death of such insured,

exceeds the per diem limitation for such period, such excess shall be includible in gross income without regard to section 72. A payment shall not be taken into account under subparagraph (B) if the insured is a terminally ill individual (as defined in section 101(g)) at the time the payment is received.

(2) PER DIEM LIMITATION.—For purposes of paragraph (1), the per diem limitation for any period is an amount equal to the excess (if any) of—

- (A) the greater of—
- (i) the dollar amount in effect for such period under paragraph (4), or
  - (ii) the costs incurred for qualified long-term care services provided for the insured for such period, over
- (B) the aggregate payments received as reimbursements (through insurance or otherwise) for qualified long-term care services provided for the insured during such period.
- (3) AGGREGATION RULES.—For purposes of this subsection—
- (A) all persons receiving periodic payments described in paragraph (1) with respect to the same insured shall be treated as 1 person, and
  - (B) the per diem limitation determined under paragraph (2) shall be allocated first to the insured and any remaining limitation shall be allocated among the other such persons in such manner as the Secretary shall prescribe.
- (4) DOLLAR AMOUNT.—The dollar amount in effect under this subsection shall be \$175 per day (or the equivalent amount in the case of payments on another periodic basis).
- (5) INFLATION ADJUSTMENT.—In the case of a calendar year after 1997, the dollar amount contained in paragraph (4) shall be increased at the same time and in the same manner as amounts are increased pursuant to section 213(d)(10).
- (6) PERIODIC PAYMENTS.—For purposes of this subsection, the term “periodic payment” means any payment (whether on a periodic basis or otherwise) made without regard to the extent of the costs incurred by the payee for qualified long-term care services.
- (e) TREATMENT OF COVERAGE PROVIDED AS PART OF A LIFE INSURANCE OR ANNUITY CONTRACT.—Except as otherwise provided in regulations prescribed by the Secretary, in the case of any long-term care insurance coverage (whether or not qualified) provided by a rider on or as part of a life insurance contract or an annuity contract—
- (1) IN GENERAL.—This title shall apply as if the portion of the contract providing such coverage is a separate contract.
  - (2) DENIAL OF DEDUCTION UNDER SECTION 213.—No deduction shall be allowed under section 213(a) for any payment made for coverage under a qualified long-term care insurance contract if such payment is made as a charge against the cash surrender value of a life insurance contract or the cash value of an annuity contract.
  - (3) PORTION DEFINED.—For purposes of this subsection, the term “portion” means only the terms and benefits under a life insurance contract or annuity contract that are in addition to the terms and benefits under the contract without regard to long-term care insurance coverage.
  - (4) ANNUITY CONTRACTS TO WHICH PARAGRAPH (1) DOES NOT APPLY.—For purposes of this subsection, none of the following shall be treated as an annuity contract:
    - (A) A trust described in section 401(a) which is exempt from tax under section 501(a).
    - (B) A contract—

- (i) purchased by a trust described in subparagraph (A),
- (ii) purchased as part of a plan described in section 403(a),
- (iii) described in section 403(b),
- (iv) provided for employees of a life insurance company under a plan described in section 818(a)(3), or
- (v) from an individual retirement account or an individual retirement annuity.

(C) A contract purchased by an employer for the benefit of the employee (or the employee's spouse). Any dividend described in section 404(k) which is received by a participant or beneficiary shall, for purposes of this paragraph, be treated as paid under a separate contract to which subparagraph (B)(i) applies.

(f) TREATMENT OF CERTAIN STATE-MAINTAINED PLANS.—

(1) IN GENERAL.—If—

- (A) an individual receives coverage for qualified long-term care services under a State long-term care plan, and
  - (B) the terms of such plan would satisfy the requirements of subsection (b) were such plan an insurance contract,
- such plan shall be treated as a qualified long-term care insurance contract for purposes of this title.

(2) STATE LONG-TERM CARE PLAN.—For purposes of paragraph (1), the term “State long-term care plan” means any plan—

- (A) which is established and maintained by a State or an instrumentality of a State,
- (B) which provides coverage only for qualified long-term care services, and
- (C) under which such coverage is provided only to—
  - (i) employees and former employees of a State (or any political subdivision or instrumentality of a State),
  - (ii) the spouses of such employees, and
  - (iii) individuals bearing a relationship to such employees or spouses which is described in any of subparagraphs (A) through (G) of [section 152(d)(2)] *section 7706(d)(2)*.

(g) CONSUMER PROTECTION PROVISIONS.—

(1) IN GENERAL.—The requirements of this subsection are met with respect to any contract if the contract meets—

- (A) the requirements of the model regulation and model Act described in paragraph (2),
- (B) the disclosure requirement of paragraph (3), and
- (C) the requirements relating to nonforfeitability under paragraph (4).

(2) REQUIREMENTS OF MODEL REGULATION AND ACT.—

(A) IN GENERAL.—The requirements of this paragraph are met with respect to any contract if such contract meets—

- (i) MODEL REGULATION.—The following requirements of the model regulation:
  - (I) Section 7A (relating to guaranteed renewal or noncancellability), and the requirements of sec-

tion 6B of the model Act relating to such section 7A.

(II) Section 7B (relating to prohibitions on limitations and exclusions).

(III) Section 7C (relating to extension of benefits).

(IV) Section 7D (relating to continuation or conversion of coverage).

(V) Section 7E (relating to discontinuance and replacement of policies).

(VI) Section 8 (relating to unintentional lapse).

(VII) Section 9 (relating to disclosure), other than section 9F thereof.

(VIII) Section 10 (relating to prohibitions against post-claims underwriting).

(IX) Section 11 (relating to minimum standards).

(X) Section 12 (relating to requirement to offer inflation protection), except that any requirement for a signature on a rejection of inflation protection shall permit the signature to be on an application or on a separate form.

(XI) Section 23 (relating to prohibition against preexisting conditions and probationary periods in replacement policies or certificates).

(ii) MODEL ACT.—The following requirements of the model Act:

(I) Section 6C (relating to preexisting conditions).

(II) Section 6D (relating to prior hospitalization).

(B) DEFINITIONS.—For purposes of this paragraph—

(i) MODEL PROVISIONS.—The terms “model regulation” and “model Act” mean the long-term care insurance model regulation, and the long-term care insurance model Act, respectively, promulgated by the National Association of Insurance Commissioners (as adopted as of January 1993).

(ii) COORDINATION.—Any provision of the model regulation or model Act listed under clause (i) or (ii) of subparagraph (A) shall be treated as including any other provision of such regulation or Act necessary to implement the provision.

(iii) DETERMINATION.—For purposes of this section and section 4980C, the determination of whether any requirement of a model regulation or the model Act has been met shall be made by the Secretary.

(3) DISCLOSURE REQUIREMENT.—The requirement of this paragraph is met with respect to any contract if such contract meets the requirements of section 4980C(d).

(4) NONFORFEITURE REQUIREMENTS.—

(A) IN GENERAL.—The requirements of this paragraph are met with respect to any level premium contract, if the issuer of such contract offers to the policyholder, including

any group policyholder, a nonforfeiture provision meeting the requirements of subparagraph (B).

(B) REQUIREMENTS OF PROVISION.—The nonforfeiture provision required under subparagraph (A) shall meet the following requirements:

(i) The nonforfeiture provision shall be appropriately captioned.

(ii) The nonforfeiture provision shall provide for a benefit available in the event of a default in the payment of any premiums and the mount of the benefit may be adjusted subsequent to being initially granted only as necessary to reflect changes in claims, persistency, and interest as reflected in changes in rates for premium paying contracts approved by the appropriate State regulatory agency for the same contract form.

(iii) The nonforfeiture provision shall provide at least one of the following:

(I) Reduced paid-up insurance.

(II) Extended term insurance.

(III) Shortened benefit period.

(IV) Other similar offerings approved by the appropriate State regulatory agency.

(5) CROSS REFERENCE.—For coordination of the requirements of this subsection with State requirements, see section 4980C(f).

**SEC. 7703. DETERMINATION OF MARITAL STATUS.**

(a) GENERAL RULE.—For purposes of [part V of subchapter B of chapter 1 and] those provisions of this title which refer to this subsection—

(1) the determination of whether an individual is married shall be made as of the close of his taxable year; except that if his spouse dies during his taxable year such determination shall be made as of the time of such death; and

(2) an individual legally separated from his spouse under a decree of divorce or of separate maintenance shall not be considered as married.

(b) CERTAIN MARRIED INDIVIDUALS LIVING APART.—For purposes of those provisions of this title which refer to this subsection, if—

(1) an individual who is married (within the meaning of subsection (a)) and who files a separate return maintains as his home a household which constitutes for more than one-half of the taxable year the principal place of abode of a child (within the meaning of [section 152(f)(1)] with respect to whom such individual is entitled to a deduction for the taxable year under section 151 (or would be so entitled but for section 152(e)),] *section 7706(f)(1) who is a dependent of such individual for the taxable year (or would be but for section 7706(e))*,

(2) such individual furnishes over one-half of the cost of maintaining such household during the taxable year, and

(3) during the last 6 months of the taxable year, such individual's spouse is not a member of such household, such individual shall not be considered as married.

\* \* \* \* \*

**SEC. [152.] 7706. DEPENDENT DEFINED.**

(a) **IN GENERAL.**—For purposes of [this subtitle] *subtitle A*, the term “dependent” means—

- (1) a qualifying child, or
- (2) a qualifying relative.

(b) **EXCEPTIONS.**—For purposes of this section—

(1) **DEPENDENTS INELIGIBLE.**—If an individual is a dependent of a taxpayer for any taxable year of such taxpayer beginning in a calendar year, such individual shall be treated as having no dependents for any taxable year of such individual beginning in such calendar year.

(2) **MARRIED DEPENDENTS.**—An individual shall not be treated as a dependent of a taxpayer under subsection (a) if such individual has made a joint return with the individual’s spouse under section 6013 for the taxable year beginning in the calendar year in which the taxable year of the taxpayer begins.

(3) **CITIZENS OR NATIONALS OF OTHER COUNTRIES.**—

(A) **IN GENERAL.**—The term “dependent” does not include an individual who is not a citizen or national of the United States unless such individual is a resident of the United States or a country contiguous to the United States.

(B) **EXCEPTION FOR ADOPTED CHILD.**—Subparagraph (A) shall not exclude any child of a taxpayer (within the meaning of subsection (f)(1)(B)) from the definition of “dependent” if—

- (i) for the taxable year of the taxpayer, the child has the same principal place of abode as the taxpayer and is a member of the taxpayer’s household, and
- (ii) the taxpayer is a citizen or national of the United States.

(c) **QUALIFYING CHILD.**—For purposes of this section—

(1) **IN GENERAL.**—The term “qualifying child” means, with respect to any taxpayer for any taxable year, an individual—

(A) who bears a relationship to the taxpayer described in paragraph (2),

(B) who has the same principal place of abode as the taxpayer for more than one-half of such taxable year,

(C) who meets the age requirements of paragraph (3),

(D) who has not provided over one-half of such individual’s own support for the calendar year in which the taxable year of the taxpayer begins, and

(E) who has not filed a joint return (other than only for a claim of refund) with the individual’s spouse under section 6013 for the taxable year beginning in the calendar year in which the taxable year of the taxpayer begins.

(2) **RELATIONSHIP.**—For purposes of paragraph (1)(A), an individual bears a relationship to the taxpayer described in this paragraph if such individual is—

(A) a child of the taxpayer or a descendant of such a child, or

(B) a brother, sister, stepbrother, or stepsister of the taxpayer or a descendant of any such relative.

(3) **AGE REQUIREMENTS.**—

(A) **IN GENERAL.**—For purposes of paragraph (1)(C), an individual meets the requirements of this paragraph if

such individual is younger than the taxpayer claiming such individual as a qualifying child and—

(i) has not attained the age of 19 as of the close of the calendar year in which the taxable year of the taxpayer begins, or

(ii) is a student who has not attained the age of 24 as of the close of such calendar year.

(B) SPECIAL RULE FOR DISABLED.—In the case of an individual who is permanently and totally disabled (as defined in section 22(e)(3)) at any time during such calendar year, the requirements of subparagraph (A) shall be treated as met with respect to such individual.

(4) SPECIAL RULE RELATING TO 2 OR MORE WHO CAN CLAIM THE SAME QUALIFYING CHILD.—

(A) IN GENERAL.—Except as provided in subparagraphs (B) and (C), if (but for this paragraph) an individual may be claimed as a qualifying child by 2 or more taxpayers for a taxable year beginning in the same calendar year, such individual shall be treated as the qualifying child of the taxpayer who is—

(i) a parent of the individual, or

(ii) if clause (i) does not apply, the taxpayer with the highest adjusted gross income for such taxable year.

(B) MORE THAN 1 PARENT CLAIMING QUALIFYING CHILD.—If the parents claiming any qualifying child do not file a joint return together, such child shall be treated as the qualifying child of—

(i) the parent with whom the child resided for the longest period of time during the taxable year, or

(ii) if the child resides with both parents for the same amount of time during such taxable year, the parent with the highest adjusted gross income.

(C) NO PARENT CLAIMING QUALIFYING CHILD.—If the parents of an individual may claim such individual as a qualifying child but no parent so claims the individual, such individual may be claimed as the qualifying child of another taxpayer but only if the adjusted gross income of such taxpayer is higher than the highest adjusted gross income of any parent of the individual.

(d) QUALIFYING RELATIVE.—For purposes of this section—

(1) IN GENERAL.—The term “qualifying relative” means, with respect to any taxpayer for any taxable year, an individual—

(A) who bears a relationship to the taxpayer described in paragraph (2),

(B) whose gross income for the calendar year in which such taxable year begins is less than [the exemption amount (as defined in section 151(d))] \$4,150,

(C) with respect to whom the taxpayer provides over one-half of the individual’s support for the calendar year in which such taxable year begins, and

(D) who is not a qualifying child of such taxpayer or of any other taxpayer for any taxable year beginning in the calendar year in which such taxable year begins.

(2) RELATIONSHIP.—For purposes of paragraph (1)(A), an individual bears a relationship to the taxpayer described in this

paragraph if the individual is any of the following with respect to the taxpayer:

- (A) A child or a descendant of a child.
- (B) A brother, sister, stepbrother, or stepsister.
- (C) The father or mother, or an ancestor of either.
- (D) A stepfather or stepmother.
- (E) A son or daughter of a brother or sister of the taxpayer.
- (F) A brother or sister of the father or mother of the taxpayer.
- (G) A son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law.

(H) An individual (other than an individual who at any time during the taxable year was the spouse, determined without regard to section 7703, of the taxpayer) who, for the taxable year of the taxpayer, has the same principal place of abode as the taxpayer and is a member of the taxpayer's household.

(3) SPECIAL RULE RELATING TO MULTIPLE SUPPORT AGREEMENTS.—For purposes of paragraph (1)(C), over one-half of the support of an individual for a calendar year shall be treated as received from the taxpayer if—

- (A) no one person contributed over one-half of such support,
- (B) over one-half of such support was received from 2 or more persons each of whom, but for the fact that any such person alone did not contribute over one-half of such support, would have been entitled to claim such individual as a dependent for a taxable year beginning in such calendar year,
- (C) the taxpayer contributed over 10 percent of such support, and
- (D) each person described in subparagraph (B) (other than the taxpayer) who contributed over 10 percent of such support files a written declaration (in such manner and form as the Secretary may by regulations prescribe) that such person will not claim such individual as a dependent for any taxable year beginning in such calendar year.

(4) SPECIAL RULE RELATING TO INCOME OF HANDICAPPED DEPENDENTS.—

(A) IN GENERAL.—For purposes of paragraph (1)(B), the gross income of an individual who is permanently and totally disabled (as defined in section 22(e)(3)) at any time during the taxable year shall not include income attributable to services performed by the individual at a sheltered workshop if—

- (i) the availability of medical care at such workshop is the principal reason for the individual's presence there, and
- (ii) the income arises solely from activities at such workshop which are incident to such medical care.

(B) SHELTERED WORKSHOP DEFINED.—For purposes of subparagraph (A), the term “sheltered workshop” means a school—



- (i) which provides special instruction or training designed to alleviate the disability of the individual, and
- (ii) which is operated by an organization described in section 501(c)(3) and exempt from tax under section 501(a), or by a State, a possession of the United States, any political subdivision of any of the foregoing, the United States, or the District of Columbia.

(5) SPECIAL RULES FOR SUPPORT.—

(A) IN GENERAL.—For purposes of this subsection—

- (i) payments to a spouse of alimony or separate maintenance payments shall not be treated as a payment by the payor spouse for the support of any dependent, and

- (ii) in the case of the remarriage of a parent, support of a child received from the parent's spouse shall be treated as received from the parent.

(B) ALIMONY OR SEPARATE MAINTENANCE PAYMENT.—For purposes of subparagraph (A), the term “alimony or separate maintenance payment” means any payment in cash if—

- (i) such payment is received by (or on behalf of) a spouse under a divorce or separation instrument (as defined in section 121(d)(3)(C)),

- (ii) in the case of an individual legally separated from the individual's spouse under a decree of divorce or of separate maintenance, the payee spouse and the payor spouse are not members of the same household at the time such payment is made, and

- (iii) there is no liability to make any such payment for any period after the death of the payee spouse and there is no liability to make any payment (in cash or property) as a substitute for such payments after the death of the payee spouse.

(6) INFLATION ADJUSTMENT.—*In the case of any taxable year beginning in a calendar year beginning after 2018, the \$4,150 amount in paragraph (1)(B) shall be increased by an amount equal to—*

*(A) such dollar amount, multiplied by*

*(B) the cost-of-living adjustment determined under section 1(c)(2)(A) for the calendar year in which such taxable year begins, determined by substituting “calendar year 2017” for “calendar year 2016” in clause (ii) thereof.*

*If any increase determined under the preceding sentence is not a multiple of \$50, such increase shall be rounded to the next lowest multiple of \$50.*

(e) SPECIAL RULE FOR DIVORCED PARENTS, ETC.—

(1) IN GENERAL.—Notwithstanding subsection (c)(1)(B), (c)(4), or (d)(1)(C), if—

(A) a child receives over one-half of the child's support during the calendar year from the child's parents—

- (i) who are divorced or legally separated under a decree of divorce or separate maintenance,

- (ii) who are separated under a written separation agreement, or

(iii) who live apart at all times during the last 6 months of the calendar year, and—

(B) such child is in the custody of 1 or both of the child's parents for more than one-half of the calendar year, such child shall be treated as being the qualifying child or qualifying relative of the noncustodial parent for a calendar year if the requirements described in paragraph (2) or (3) are met.

(2) EXCEPTION WHERE CUSTODIAL PARENT RELEASES CLAIM TO EXEMPTION FOR THE YEAR.—For purposes of paragraph (1), the requirements described in this paragraph are met with respect to any calendar year if—

(A) the custodial parent signs a written declaration (in such manner and form as the Secretary may by regulations prescribe) that such custodial parent will not claim such child as a dependent for any taxable year beginning in such calendar year, and

(B) the noncustodial parent attaches such written declaration to the noncustodial parent's return for the taxable year beginning during such calendar year.

(3) EXCEPTION FOR CERTAIN PRE-1985 INSTRUMENTS.—

(A) IN GENERAL.—For purposes of paragraph (1), the requirements described in this paragraph are met with respect to any calendar year if—

(i) a qualified pre-1985 instrument between the parents applicable to the taxable year beginning in such calendar year provides that the noncustodial parent shall be entitled to any deduction allowable under section 151 (*as in effect before its repeal*) for such child, and

(ii) the noncustodial parent provides at least \$600 for the support of such child during such calendar year.

For purposes of this subparagraph, amounts expended for the support of a child or children shall be treated as received from the noncustodial parent to the extent that such parent provided amounts for such support.

(B) QUALIFIED PRE-1985 INSTRUMENT.—For purposes of this paragraph, the term “qualified pre-1985 instrument” means any decree of divorce or separate maintenance or written agreement—

(i) which is executed before January 1, 1985,

(ii) which on such date contains the provision described in subparagraph (A)(i), and

(iii) which is not modified on or after such date in a modification which expressly provides that this paragraph shall not apply to such decree or agreement.

(4) CUSTODIAL PARENT AND NONCUSTODIAL PARENT.—For purposes of this subsection—

(A) CUSTODIAL PARENT.—The term “custodial parent” means the parent having custody for the greater portion of the calendar year.

(B) NONCUSTODIAL PARENT.—The term “noncustodial parent” means the parent who is not the custodial parent.

(5) EXCEPTION FOR MULTIPLE-SUPPORT AGREEMENT.—This subsection shall not apply in any case where over one-half of the support of the child is treated as having been received from a taxpayer under the provision of subsection (d)(3).

(6) SPECIAL RULE FOR SUPPORT RECEIVED FROM NEW SPOUSE OF PARENT.—For purposes of this subsection, in the case of the remarriage of a parent, support of a child received from the parent's spouse shall be treated as received from the parent.

(f) OTHER DEFINITIONS AND RULES.—For purposes of this section—

(1) CHILD DEFINED.—

(A) IN GENERAL.—The term “child” means an individual who is—

(i) a son, daughter, stepson, or stepdaughter of the taxpayer, or

(ii) an eligible foster child of the taxpayer.

(B) ADOPTED CHILD.—In determining whether any of the relationships specified in subparagraph (A)(i) or paragraph (4) exists, a legally adopted individual of the taxpayer, or an individual who is lawfully placed with the taxpayer for legal adoption by the taxpayer, shall be treated as a child of such individual by blood.

(C) ELIGIBLE FOSTER CHILD.—For purposes of subparagraph (A)(ii), the term “eligible foster child” means an individual who is placed with the taxpayer by an authorized placement agency or by judgment, decree, or other order of any court of competent jurisdiction.

(2) STUDENT DEFINED.—The term “student” means an individual who during each of 5 calendar months during the calendar year in which the taxable year of the taxpayer begins—

(A) is a full-time student at an educational organization described in section 170(b)(1)(A)(ii), or

(B) is pursuing a full-time course of institutional on-farm training under the supervision of an accredited agent of an educational organization described in section 170(b)(1)(A)(ii) or of a State or political subdivision of a State.

(3) DETERMINATION OF HOUSEHOLD STATUS.—An individual shall not be treated as a member of the taxpayer's household if at any time during the taxable year of the taxpayer the relationship between such individual and the taxpayer is in violation of local law.

(4) BROTHER AND SISTER.—The terms “brother” and “sister” include a brother or sister by the half blood.

(5) SPECIAL SUPPORT TEST IN CASE OF STUDENTS.—For purposes of subsections (c)(1)(D) and (d)(1)(C), in the case of an individual who is—

(A) a child of the taxpayer, and

(B) a student, amounts received as scholarships for study at an educational organization described in section 170(b)(1)(A)(ii) shall not be taken into account.

(6) TREATMENT OF MISSING CHILDREN.—

(A) IN GENERAL.—Solely for the purposes referred to in subparagraph (B), a child of the taxpayer—

(i) who is presumed by law enforcement authorities to have been kidnapped by someone who is not a member of the family of such child or the taxpayer, and

(ii) who had, for the taxable year in which the kidnapping occurred, the same principal place of abode as the taxpayer for more than one-half of the portion of such year before the date of the kidnapping, shall be treated as meeting the requirement of subsection (c)(1)(B) with respect to a taxpayer for all taxable years ending during the period that the child is kidnapped.

(B) PURPOSES.—Subparagraph (A) shall apply solely for purposes of determining—

[(i) the deduction under section 151(c),]

[(ii) (i) the credit under section 24 (relating to child tax credit),

[(iii) (ii) whether an individual is a surviving spouse or a head of a household (as such terms are defined in section 2), and

[(iv) (iii) the earned income credit under section 32.

(C) COMPARABLE TREATMENT OF CERTAIN QUALIFYING RELATIVES.—For purposes of this section, a child of the taxpayer—

(i) who is presumed by law enforcement authorities to have been kidnapped by someone who is not a member of the family of such child or the taxpayer, and

(ii) who was (without regard to this paragraph) a qualifying relative of the taxpayer for the portion of the taxable year before the date of the kidnapping, shall be treated as a qualifying relative of the taxpayer for all taxable years ending during the period that the child is kidnapped.

(D) TERMINATION OF TREATMENT.—Subparagraphs (A) and (C) shall cease to apply as of the first taxable year of the taxpayer beginning after the calendar year in which there is a determination that the child is dead (or, if earlier, in which the child would have attained age 18).

(7) CROSS REFERENCES.—For provision treating child as dependent of both parents for purposes of certain provisions, see sections 105(b), 132(h)(2)(B), and 213(d)(5).

## CHAPTER 80—GENERAL RULES

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### Subchapter C—Provisions Affecting More Than One Subtitle

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#### SEC. 7872. TREATMENT OF LOANS WITH BELOW-MARKET INTEREST RATES.

(a) TREATMENT OF GIFT LOANS AND DEMAND LOANS.—

(1) IN GENERAL.—For purposes of this title, in the case of any below-market loan to which this section applies and which is a gift loan or a demand loan, the forgone interest shall be treated as—

(A) transferred from the lender to the borrower, and

(B) retransferred by the borrower to the lender as interest.

(2) TIME WHEN TRANSFERS MADE.—Except as otherwise provided in regulations prescribed by the Secretary, any forgone interest attributable to periods during any calendar year shall be treated as transferred (and retransferred) under paragraph (1) on the last day of such calendar year.

(b) TREATMENT OF OTHER BELOW-MARKET LOANS.—

(1) IN GENERAL.—For purposes of this title, in the case of any below-market loan to which this section applies and to which subsection (a)(1) does not apply, the lender shall be treated as having transferred on the date the loan was made (or, if later, on the first day on which this section applies to such loan), and the borrower shall be treated as having received on such date, cash in an amount equal to the excess of—

(A) the amount loaned, over

(B) the present value of all payments which are required to be made under the terms of the loan.

(2) OBLIGATION TREATED AS HAVING ORIGINAL ISSUE DISCOUNT.—For purposes of this title—

(A) IN GENERAL.—Any below-market loan to which paragraph (1) applies shall be treated as having original issue discount in an amount equal to the excess described in paragraph (1).

(B) AMOUNT IN ADDITION TO OTHER ORIGINAL ISSUE DISCOUNT.—Any original issue discount which a loan is treated as having by reason of subparagraph (A) shall be in addition to any other original issue discount on such loan (determined without regard to subparagraph (A)).

(c) BELOW-MARKET LOANS TO WHICH SECTION APPLIES.—

(1) IN GENERAL.—Except as otherwise provided in this subsection and subsection (g), this section shall apply to—

(A) GIFTS.—Any below-market loan which is a gift loan.

(B) COMPENSATION-RELATED LOANS.—Any below-market loan directly or indirectly between—

(i) an employer and an employee, or

(ii) an independent contractor and a person for whom such independent contractor provides services.

(C) CORPORATION-SHAREHOLDER LOANS.—Any below-market loan directly or indirectly between a corporation and any shareholder of such corporation.

(D) TAX AVOIDANCE LOANS.—Any below-market loan 1 of the principal purposes of the interest arrangements of which is the avoidance of any Federal tax.

(E) OTHER BELOW-MARKET LOANS.—To the extent provided in regulations, any below-market loan which is not described in subparagraph (A), (B), (C), or (F) if the interest arrangements of such loan have a significant effect on any Federal tax liability of the lender or the borrower.

(F) LOANS TO QUALIFIED CONTINUING CARE FACILITIES.— Any loan to any qualified continuing care facility pursuant to a continuing care contract.

(2) \$10,000 DE MINIMIS EXCEPTION FOR GIFT LOANS BETWEEN INDIVIDUALS.—

(A) IN GENERAL.—In the case of any gift loan directly between individuals, this section shall not apply to any day on which the aggregate outstanding amount of loans between such individuals does not exceed \$10,000.

(B) DE MINIMIS EXCEPTION NOT TO APPLY TO LOANS ATTRIBUTABLE TO ACQUISITION OF INCOME-PRODUCING ASSETS.—Subparagraph (A) shall not apply to any gift loan directly attributable to the purchase or carrying of income-producing assets.

(C) CROSS REFERENCE.—For limitation on amount treated as interest where loans do not exceed \$100,000, see subsection (d)(1).

(3) \$10,000 DE MINIMIS EXCEPTION FOR COMPENSATION-RELATED AND CORPORATE-SHAREHOLDER LOANS.—

(A) IN GENERAL.—In the case of any loan described in subparagraph (B) or (C) of paragraph (1), this section shall not apply to any day on which the aggregate outstanding amount of loans between the borrower and lender does not exceed \$10,000.

(B) EXCEPTION NOT TO APPLY WHERE 1 OF PRINCIPAL PURPOSES IS TAX AVOIDANCE.—Subparagraph (A) shall not apply to any loan the interest arrangements of which have as 1 of their principal purposes the avoidance of any Federal tax.

(d) SPECIAL RULES FOR GIFT LOANS.—

(1) LIMITATION ON INTEREST ACCRUAL FOR PURPOSES OF INCOME TAXES WHERE LOANS DO NOT EXCEED \$100,000.—

(A) IN GENERAL.—For purposes of subtitle A, in the case of a gift loan directly between individuals, the amount treated as retransferred by the borrower to the lender as of the close of any year shall not exceed the borrower's net investment income for such year.

(B) LIMITATION NOT TO APPLY WHERE 1 OF PRINCIPAL PURPOSES IS TAX AVOIDANCE.—Subparagraph (A) shall not apply to any loan the interest arrangements of which have as 1 of their principal purposes the avoidance of any Federal tax.

(C) SPECIAL RULE WHERE MORE THAN 1 GIFT LOAN OUTSTANDING.—For purposes of subparagraph (A), in any case in which a borrower has outstanding more than 1 gift loan, the net investment income of such borrower shall be allocated among such loans in proportion to the respective amounts which would be treated as retransferred by the borrower without regard to this paragraph.

(D) LIMITATION NOT TO APPLY WHERE AGGREGATE AMOUNT OF LOANS EXCEED \$100,000.—This paragraph shall not apply to any loan made by a lender to a borrower for any day on which the aggregate outstanding amount of loans between the borrower and lender exceeds \$100,000.

- (E) NET INVESTMENT INCOME.—For purposes of this paragraph—
- (i) IN GENERAL.—The term “net investment income” has the meaning given such term by section 163(d)(4).
  - (ii) DE MINIMIS RULE.—If the net investment income of any borrower for any year does not exceed \$1,000, the net investment income of such borrower for such year shall be treated as zero.
  - (iii) ADDITIONAL AMOUNTS TREATED AS INTEREST.—In determining the net investment income of a person for any year, any amount which would be included in the gross income of such person for such year by reason of section 1272 if such section applied to all deferred payment obligations shall be treated as interest received by such person for such year.
  - (iv) DEFERRED PAYMENT OBLIGATIONS.—The term “deferred payment obligation” includes any market discount bond, short-term obligation, United States savings bond, annuity, or similar obligation.
- (2) SPECIAL RULE FOR GIFT TAX.—In the case of any gift loan which is a term loan, subsection (b)(1) (and not subsection (a)) shall apply for purposes of chapter 12.
- (e) DEFINITIONS OF BELOW-MARKET LOAN AND FORGONE INTEREST.—For purposes of this section—
- (1) BELOW-MARKET LOAN.—The term “below-market loan” means any loan if—
    - (A) in the case of a demand loan, interest is payable on the loan at a rate less than the applicable Federal rate, or
    - (B) in the case of a term loan, the amount loaned exceeds the present value of all payments due under the loan.
  - (2) FORGONE INTEREST.—The term “forgone interest” means, with respect to any period during which the loan is outstanding, the excess of—
    - (A) the amount of interest which would have been payable on the loan for the period if interest accrued on the loan at the applicable Federal rate and were payable annually on the day referred to in subsection (a)(2), over
    - (B) any interest payable on the loan properly allocable to such period.
- (f) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this section—
- (1) PRESENT VALUE.—The present value of any payment shall be determined in the manner provided by regulations prescribed by the Secretary—
    - (A) as of the date of the loan, and
    - (B) by using a discount rate equal to the applicable Federal rate.
  - (2) APPLICABLE FEDERAL RATE.—
    - (A) TERM LOANS.—In the case of any term loan, the applicable Federal rate shall be the applicable Federal rate in effect under section 1274(d) (as of the day on which the loan was made), compounded semiannually.
    - (B) DEMAND LOANS.—In the case of a demand loan, the applicable Federal rate shall be the Federal short-term

rate in effect under section 1274(d) for the period for which the amount of forgone interest is being determined, compounded semiannually.

(3) GIFT LOAN.—The term “gift loan” means any below-market loan where the forgoing of interest is in the nature of a gift.

(4) AMOUNT LOANED.—The term “amount loaned” means the amount received by the borrower.

(5) DEMAND LOAN.—The term “demand loan” means any loan which is payable in full at any time on the demand of the lender. Such term also includes (for purposes other than determining the applicable Federal rate under paragraph (2)) any loan if the benefits of the interest arrangements of such loan are not transferable and are conditioned on the future performance of substantial services by an individual. To the extent provided in regulations, such term also includes any loan with an indefinite maturity.

(6) TERM LOAN.—The term “term loan” means any loan which is not a demand loan.

(7) HUSBAND AND WIFE TREATED AS 1 PERSON.—A husband and wife shall be treated as 1 person.

(8) LOANS TO WHICH SECTION 483, 643(D), OR 1274 APPLIES.—This section shall not apply to any loan to which section 483, 643(i), or 1274 applies.

(9) NO WITHHOLDING.—No amount shall be withheld under chapter 24 with respect to—

(A) any amount treated as transferred or retransferred under subsection (a), and

(B) any amount treated as received under subsection (b).

(10) SPECIAL RULE FOR TERM LOANS.—If this section applies to any term loan on any day, this section shall continue to apply to such loan notwithstanding paragraphs (2) and (3) of subsection (c). In the case of a gift loan, the preceding sentence shall only apply for purposes of chapter 12.

[(11) TIME FOR DETERMINING RATE APPLICABLE TO EMPLOYEE RELOCATION LOANS.—

[(A) IN GENERAL.—In the case of any term loan made by an employer to an employee the proceeds of which are used by the employee to purchase a principal residence (within the meaning of section 121), the determination of the applicable Federal rate shall be made as of the date the written contract to purchase such residence was entered into.

[(B) PARAGRAPH ONLY TO APPLY TO CASES TO WHICH SECTION 217 APPLIES.—Subparagraph (A) shall only apply to the purchase of a principal residence in connection with the commencement of work by an employee or a change in the principal place of work of an employee to which section 217 applies.]

(g) EXCEPTION FOR CERTAIN LOANS TO QUALIFIED CONTINUING CARE FACILITIES.—

(1) IN GENERAL.—This section shall not apply for any calendar year to any below-market loan made by a lender to a qualified continuing care facility pursuant to a continuing care



contract if the lender (or the lender's spouse) attains age 65 before the close of such year.

(2) **\$90,000 LIMIT.**—Paragraph (1) shall apply only to the extent that the aggregate outstanding amount of any loan to which such paragraph applies (determined without regard to this paragraph), when added to the aggregate outstanding amount of all other previous loans between the lender (or the lender's spouse) and any qualified continuing care facility to which paragraph (1) applies, does not exceed \$90,000.

(3) **CONTINUING CARE CONTRACT.**—For purposes of this section, the term “continuing care contract” means a written contract between an individual and a qualified continuing care facility under which—

(A) the individual or individual's spouse may use a qualified continuing care facility for their life or lives,

(B) the individual or individual's spouse—

(i) will first—

(I) reside in a separate, independent living unit with additional facilities outside such unit for the providing of meals and other personal care, and

(II) not require long-term nursing care, and (ii) then will be provided long-term and skilled nursing care as the health of such individual or individual's spouse requires, and (C) no additional substantial payment is required if such individual or individual's spouse requires increased personal care services or long-term and skilled nursing care.

(4) **QUALIFIED CONTINUING CARE FACILITY.**—

(A) **IN GENERAL.**—For purposes of this section, the term “qualified continuing care facility” means 1 or more facilities—

(i) which are designed to provide services under continuing care contracts, and

(ii) substantially all of the residents of which are covered by continuing care contracts.

(B) **SUBSTANTIALLY ALL FACILITIES MUST BE OWNED OR OPERATED BY BORROWER.**—A facility shall not be treated as a qualified continuing care facility unless substantially all facilities which are used to provide services which are required to be provided under a continuing care contract are owned or operated by the borrower.

(C) **NURSING HOMES EXCLUDED.**—The term “qualified continuing care facility” shall not include any facility which is of a type which is traditionally considered a nursing home.

(5) **ADJUSTMENT OF LIMIT FOR INFLATION.**—In the case of any loan made during any calendar year after 1986, the dollar amount in paragraph (2) shall be increased by an amount equal to—

(A) such amount, multiplied by

(B) the cost-of-living adjustment determined under section 1(f)(3) for the calendar year in which the taxable year begins, by substituting “calendar year 1985” for “calendar year 2016” in subparagraph (A)(ii) thereof.

Any increase under the preceding sentence shall be rounded to the nearest multiple of \$100 (or, if such increase is a multiple of \$50, such increase shall be increased to the nearest multiple of \$100).

(6) SUSPENSION OF APPLICATION.—Paragraph (1) shall not apply for any calendar year to which subsection (h) applies.

(h) EXCEPTION FOR LOANS TO QUALIFIED CONTINUING CARE FACILITIES.—

(1) IN GENERAL.—This section shall not apply for any calendar year to any below-market loan owed by a facility which on the last day of such year is a qualified continuing care facility, if such loan was made pursuant to a continuing care contract and if the lender (or the lender's spouse) attains age 62 before the close of such year.

(2) CONTINUING CARE CONTRACT.—For purposes of this section, the term “continuing care contract” means a written contract between an individual and a qualified continuing care facility under which—

(A) the individual or individual's spouse may use a qualified continuing care facility for their life or lives,

(B) the individual or individual's spouse will be provided with housing, as appropriate for the health of such individual or individual's spouse—

(i) in an independent living unit (which has additional available facilities outside such unit for the provision of meals and other personal care), and

(ii) in an assisted living facility or a nursing facility, as is available in the continuing care facility, and

(C) the individual or individual's spouse will be provided assisted living or nursing care as the health of such individual or individual's spouse requires, and as is available in the continuing care facility.

The Secretary shall issue guidance which limits such term to contracts which provide only facilities, care, and services described in this paragraph.

(3) QUALIFIED CONTINUING CARE FACILITY.—

(A) IN GENERAL.—For purposes of this section, the term “qualified continuing care facility” means 1 or more facilities—

(i) which are designed to provide services under continuing care contracts,

(ii) which include an independent living unit, plus an assisted living or nursing facility, or both, and

(iii) substantially all of the independent living unit residents of which are covered by continuing care contracts.

(B) NURSING HOMES EXCLUDED.—The term “qualified continuing care facility” shall not include any facility which is of a type which is traditionally considered a nursing home.

(i) REGULATIONS.—

(1) IN GENERAL.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including—

(A) regulations providing that where, by reason of varying rates of interest, conditional interest payments, waivers of interest, disposition of the lender's or borrower's interest in the loan, or other circumstances, the provisions of this section do not carry out the purposes of this section, adjustments to the provisions of this section will be made to the extent necessary to carry out the purposes of this section,

(B) regulations for the purpose of assuring that the positions of the borrower and lender are consistent as to the application (or nonapplication) of this section, and

(C) regulations exempting from the application of this section any class of transactions the interest arrangements of which have no significant effect on any Federal tax liability of the lender or the borrower.

(2) ESTATE TAX COORDINATION.—Under regulations prescribed by the Secretary, any loan which is made with donative intent and which is a term loan shall be taken into account for purposes of chapter 11 in a manner consistent with the provisions of subsection (b).

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## PUBLIC LAW 115-97

### TITLE I

\* \* \* \* \*

#### Subtitle A—Individual Tax Reform

\* \* \* \* \*

#### PART III—TAX BENEFITS FOR FAMILIES AND INDIVIDUALS

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##### **[(SEC. 11026. TREATMENT OF CERTAIN INDIVIDUALS PERFORMING SERVICES IN THE SINAI PENINSULA OF EGYPT.]**

**[(a) IN GENERAL.—**For purposes of the following provisions of the Internal Revenue Code of 1986, with respect to the applicable period, a qualified hazardous duty area shall be treated in the same manner as if it were a combat zone (as determined under section 112 of such Code):

**[(1)** Section 2(a)(3) (relating to special rule where deceased spouse was in missing status).

**[(2)** Section 112 (relating to the exclusion of certain combat pay of members of the Armed Forces).

**[(3)** Section 692 (relating to income taxes of members of Armed Forces on death).

**[(4)** Section 2201 (relating to members of the Armed Forces dying in combat zone or by reason of combat-zone-incurred wounds, etc.).

[(5) Section 3401(a)(1) (defining wages relating to combat pay for members of the Armed Forces).

[(6) Section 4253(d) (relating to the taxation of phone service originating from a combat zone from members of the Armed Forces).

[(7) Section 6013(f)(1) (relating to joint return where individual is in missing status).

[(8) Section 7508 (relating to time for performing certain acts postponed by reason of service in combat zone).

[(b) QUALIFIED HAZARDOUS DUTY AREA.—For purposes of this section, the term “qualified hazardous duty area” means the Sinai Peninsula of Egypt, if as of the date of the enactment of this section any member of the Armed Forces of the United States is entitled to special pay under section 310 of title 37, United States Code (relating to special pay; duty subject to hostile fire or imminent danger), for services performed in such location. Such term includes such location only during the period such entitlement is in effect.

[(c) APPLICABLE PERIOD.—

[(1) IN GENERAL.—Except as provided in paragraph (2), the applicable period is—

[(A) the portion of the first taxable year ending after June 9, 2015, which begins on such date, and

[(B) any subsequent taxable year beginning before January 1, 2026.

[(2) WITHHOLDING.—In the case of subsection (a)(5), the applicable period is—

[(A) the portion of the first taxable year ending after the date of the enactment of this Act which begins on such date, and

[(B) any subsequent taxable year beginning before January 1, 2026.

[(d) EFFECTIVE DATE.—

[(1) IN GENERAL.—Except as provided in paragraph (2), the provisions of this section shall take effect on June 9, 2015.

[(2) WITHHOLDING.—Subsection (a)(5) shall apply to remuneration paid after the date of the enactment of this Act.]

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## VII. DISSENTING VIEWS

It has been eight months since the Republicans enacted their massive, unpaid-for tax cut law (Public Law 115–97) without a single Democratic vote or a single hearing. At the time, Democrats and independent experts warned that a so-called tax reform plan that was not paid for and that was so heavily skewed to the wealthy and big corporations would harm our economy and damage important programs like Medicare and Social Security. Eight months later, we are beginning to see what many of us feared is coming true. Health insurance companies in state after state are announcing higher premiums for next year, while health coverage for those living with pre-existing conditions is on the chopping block. To make matters worse, the Medicare Trustees cut three years off the life of the Medicare Trust Fund because of the Republican tax bill.

Despite all of this, Republicans are doubling down and moving forward with another round of tax cuts for the well-off and well-connected with this Tax Scam 2.0, the “Protecting Family and Small Business Tax Cuts Act of 2018” (H.R. 6760).

After Republicans showered corporations with trillions of dollars in tax cuts and promised that it would lead to more jobs and higher wages, we are seeing that corporations across the country are instead pocketing their money, laying off workers, and shipping operations to other countries. In one particularly egregious case, an executive at a well-known company stated that the savings the company received from the Republican tax law allowed them to restructure and lay off hundreds of workers.

H.R. 6760 extended the section 199A pass-through deduction, which Republicans claimed would benefit small business and spur economic growth. Instead, section 199A is a massive giveaway to millionaires. In fact, 58 percent of the benefit of the Republicans’ so-called small business tax benefit goes to millionaires.

At the same time, the Republicans have doubled down on their attack on the middle class by attempting to make permanent the limits to the State and Local Tax deduction, the mortgage interest deduction, and casualty loss deductions. And by eliminating personal exemptions alone, 290 million individuals will no longer be able to claim \$1.14 trillion in tax savings. Tax Scam 2.0 targets these and many other tax incentives that help middle class families get ahead, while lavishing benefits on the wealthy and well-connected corporations.

The Republicans call themselves fiscal conservatives but nothing could be further from the truth. History doesn’t lie and now we’re seeing it again with the addition of more than \$3 trillion to the nation’s debt.

Tax Scam 2.0, like Tax Scam 1.0 before it, was jammed through the Committee with no hearings and no input from stakeholders.

The rushed and lopsided process late last year resulted in the disastrous tax law. Unsurprisingly, the Democratic staff has identified over 100 mistakes and other problems with the Republicans' tax law. Instead of seeking expert opinions, high-quality data, and a reasoned review of the performance to date of last year's law, Republicans repeated the careless, partisan process of last year and again aimed at partisan priorities instead of evidence-based reforms. Furthermore, there was no reason for them to abandon regular order, given that these bills are guaranteed to be dead-on-arrival in the Senate.

Democrats on the Committee gave Republicans the opportunity to demonstrate their priorities, offering seven fiscally-responsible amendments that truly help middle-class families and protect seniors from tax hikes and cuts to Social Security and Medicare without adding to the deficit. In a manner consistent with their habit of putting the wealthy and corporations ahead of working Americans, Republicans rejected every amendment.

Republicans rejected an amendment I offered to curb one of the worst excesses of last year's tax scam, which is made permanent in H.R. 6760. My amendment would have restored the top marginal income tax rate to pre-Public Law 115-97 levels and used the proceeds to support three key priorities that actually help hard-working Americans: expanding the Earned Income Tax Credit (EITC) to offer support to low-income workers without children, making the Adoption Tax Credit refundable, and enhancing the child and dependent care credit. Instead of offering support to ordinary families, H.R. 6760 makes permanent a reduction to the pre-Public Law 115-97 top marginal income tax rate, which was already cut in half compared to the Reagan era. A top marginal rate of 39.6 has previously won the support not only of Presidents Obama and Clinton, but also John Boehner and Mitch McConnell. That top rate is not too high—a broad bipartisan group of lawmakers and presidents were all willing to support it. There is no compelling reason why it should be lowered. My amendment offered Republicans an opportunity to change H.R. 6760 to provide meaningful support to low-wage workers, adoptive parents, and those with dependents in need of care, just by asking some of the most affluent people in our society to give up a small part of their tax cut—an opportunity Republicans resoundingly rejected.

Republicans also rejected an amendment offered by Rep. Pascrell that would have removed the cap on the deduction for state and local taxes ("SALT"), a provision that prevents individual taxpayers from owing federal taxes on the income they pay in taxes to state and local governments. Ironically, Tax Scam 1.0 allowed corporations to continue deducting state and local taxes, while eliminating much of the benefit for individuals and families. State and local tax payments are not disposable income, and it is unfair to treat them as such. Currently, more than 100 million Americans in 45 million households claim the SALT deduction. Almost 40 percent of taxpayers earning between \$50,000 and \$75,000 claim SALT, and over 70 percent of taxpayers making \$100,000 to \$200,000 use it. Over one-half the value of the deduction went to households with incomes below \$200,000. In 2016, the most recent year for which data are available, the average SALT deduction nationwide was al-

ready above \$12,500, and inflation will cause a growing number of households to experience double taxation. In fact, in 2016, the average SALT deduction was over \$10,000 in 23 states and the District of Columbia: Michigan, Missouri, Kentucky, Hawaii, Iowa, New Hampshire, Ohio, Nebraska, Pennsylvania, Maine, Virginia, Wisconsin, Illinois, Rhode Island, Vermont, Oregon, Maryland, Minnesota, Massachusetts, DC, New Jersey, California, Connecticut, and New York. With average SALT deductions exceeding \$9,000, ten more states won't be far behind: South Carolina, Arkansas, Georgia, Idaho, West Virginia, Colorado, Montana, Delaware, Kansas, and North Carolina.

People living in every congressional district in every state in the country use the SALT deduction, and it benefits taxpayers of all income levels, directly or indirectly. State and local government tax revenues support essential public services and investments, like schools, local law enforcement, fire fighters, road construction and maintenance, and health care. Nearly everyone who itemizes claims the SALT deduction; therefore, repealing SALT would raise the cost of state and local services on a wide swath of taxpayers. Because this provision effectively raises the cost of state and local taxes, state and local governments would be pressured to reduce revenues and cut crucial public investments. Republicans rejected the opportunity to restore fairness in our tax system for more taxpayers that are now facing double taxation as a result of Republican tax policy choices.

Republicans rejected an amendment offered by Rep. Thompson that would have provided fairness and certainty to taxpayers that are victims of natural disasters. The amendment would have repealed the limitations in Public Law 115-97 that restricted eligibility for itemized deductions related to casualty losses to taxpayers in certain disaster areas, and extended a suite of provisions to help victims of natural disasters nationwide, including: penalty-free access to retirement funds, an employer wage tax credit in core disaster areas, a suspension of the limitations on deduction for charitable contributions associated with disasters, a relaxation of rules associated with the deduction for personal casualty losses, a special rule for income calculations with respect to the EITC and Child Tax Credit, and special rules for application of disaster tax relief for possessions of the United States. This is nothing more than the same relief the Chairman provided to his constituents that were victims of Hurricane Harvey last year. It is unconscionable for Republicans to support the notion that only those taxpayers that are fortunate enough to reside in the district of the Chairman are entitled to tax relief following such a tragedy. Republicans rejected the opportunity to provide fairness and certainty to all taxpayers facing tragedy.

Republicans rejected an amendment offered by Rep. Sánchez that would have made permanent the reduction of the adjusted gross income threshold for deductibility of certain medical expenses. The deduction for medical expenses is an important backstop for individuals with expensive health care needs. H.R. 6760 only extended this important tax relief for two years, while making permanent all of the other individual provisions, including billions in tax relief for millionaires. Republicans have done nothing to lower prescription

drug costs for seniors, address long-term care needs, or stabilize the individual market to stem the skyrocketing premiums caused by Republican sabotage. Republicans rejected the opportunity to make permanent tax relief for millions of Americans facing significant health costs, choosing to shower the wealthy in tax benefits over middle-class Americans struggling with high out-of-pocket health care costs.

Republicans rejected an amendment offered by Rep. Doggett that would have compelled the Chairman of the Ways and Means Committee to submit a written request to the Secretary of the Treasury for federal tax returns filed by or on behalf of the President for the last ten years. There are few matters the Ways and Means Committee could consider more important than the integrity of our tax code, and the faith that the American people have in our democracy. The amendment would have contained a list of Congressional findings that raised questions about the Trump Administration and would have demanded Congressional oversight by the Committee on Ways and Means.

Republicans rejected an amendment offered by Rep. Larson that would have suspended the Republicans' misguided tax policy until it was certified that their billions of dollars in tax cuts for the wealthy would not do harm to the Social Security and Medicare trust funds. When looking at the ballooning deficit, Republicans shift blame away from the \$3 trillion their policies have added and, instead, blame programs that people have worked their entire lives for and have planned for in retirement—Medicare and Social Security. These programs are the cornerstone of the American middle class, and yet the Republicans continue to attack them. Republican actions threaten health care for 58 million seniors and individuals with disabilities. Since the Republican Tax Scam 1.0 was signed into law, the Medicare Trust Fund's solvency has been slashed by three years. The Republican's health care repeal bill would have cut three years from Medicare's Trust Fund. In contrast, the Affordable Care Act added 12 years to the Medicare Trust Fund. It is clear that enactment of these tax cut giveaways are part of the two-step Republican strategy to cut Social Security and Medicare: First, the Republicans explode the deficit by cutting taxes for the rich. Second, the Republicans use the deficits created by their tax cuts as an excuse to cut Social Security and Medicare benefits. Republicans rejected the opportunity to demonstrate to their constituents a real commitment to ensuring that benefits earned by hard-working Americans would not be cut at the expense of tax cuts for the wealthy.

Republicans rejected an amendment offered by Rep. Doggett that would have put the American worker first—ahead of billions in tax relief for multinational corporations. The amendment would have suspended the preferential tax rates on money that multinational corporations stashed offshore until the Joint Committee on Taxation certified that Americans' average household income had increased by \$4,000, a promise made by President Trump and Congressional Republicans. It is clear that, consistent with their record of offering lip service to the middle class while lavishing corporations and wealthy individuals with tax relief, Republicans were



never going to keep that promise to American workers. Republicans rejected this opportunity to put the American worker first.

I said it when Republicans rammed through their first deficit-busting tax cuts, and I'll say it again: American families should not be forced to watch as the rich get richer, and they fall further and further behind. H.R. 6760 would do just that.

RICHARD E. NEAL,  
*Ranking Member.*

